

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

In the Matter of Missouri-American Water	)	
Company's Request for Authority to Implement	)	Case No. WR-2015-0301
General Rate Increase for Water and Sewer	)	Case No. SR-2015-0302
Service Provided in Missouri Service Areas.	)	

**MAWC’S STATEMENTS OF POSITION**

COMES NOW Missouri-American Water Company (MAWC or Company), and for its Statements of Position, states the following to the Missouri Public Service Commission (Commission) concerning the issues contained in the *List of Issues, List and Order of Witnesses, Order of Opening Statements, and Order of Cross-Examination*, filed on March 9, 2016:

**1. Regulatory Policy**

**MAWC Position:** The best way to ensure that appropriate levels of capital investment are consistently and appropriately funded is through predictable and timely recovery of investments, meaningful recognition of revenue trends, and the return on the capital devoted to serving customers' needs. Most of a water utility's costs are fixed, recovering investments in pipes, treatment plants and other equipment, while most water revenue is variable, collected through volumetric rates charged on a per-gallon basis.

Today, with static or declining per customer consumption and revenue declining due to conservation largely driven by nationwide efficiency standards, the economic and environmental policy landscape is driving the need for adjustments to traditional regulation that was developed in a growth environment. People still buy new appliances and fixtures, but due to federal mandates, those new appliances now use less energy and water than those they replace.

Today, we see increasing investment amid falling revenue. While a historic test year relying on volumetric sales might have been appropriate when the growth in usage and customers counter-balanced the growth in investment, this situation no longer exists.

Norton for Kartmann (MAWC) <sup>1</sup> (Kartmann Cor. Dir., p. 14-26)

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<sup>1</sup> Mr. Kartmann's testimony will be adopted by Ms. Cheryl Norton. She will stand cross-examination on all of Mr. Kartmann's issues at this time, except the Union issues, for which she will return.

Watkins (MAWC) (Watkins Sur., All)  
Haye for Petry (MAWC)<sup>2</sup>

## 2. Cost of Capital and Capital Structure

A. What Capital Structure should be used in this case?

**MAWC Position:** The appropriate capital structure for calculating MAWC's weighted average cost of capital is its stand-alone capital structure as of January 31, 2016, which represents the actual capital financing its jurisdictional rate base to which the overall rate of return set in this proceeding will be applied. As of January 31, 2016, MAWC's actual stand-alone capital structure was comprised of 48.3% long-term debt, 1.54% short term debt, 0.12 % preferred stock and 50.05% common equity.

MAWC's stand-alone capital structure is reasonable for ratemaking purposes because it is consistent with the capital structure ratios maintained, on average, by other investor-owned water companies. The Commission should not use American Water's consolidated capital structure because MAWC is a separate corporate entity, evidenced by the fact that it issues its own debt, with the amount based on capital expenditures and MAWC's independent assessment of its operating risks. Therefore, the facts show that MAWC independently maintains a capital structure that is appropriate for its operations.

Rungren (MAWC) (Dir., all; Reb., all; Sur., all; and to be reflected in true-up testimony and schedules)  
Morin (MAWC) (Sur., p 4-6)

B. What Return on Equity ("ROE") should be allowed?

**MAWC Position:** Based upon the common equity cost rates resulting from the use of multiple cost of common equity models – the Capital Asset Pricing Model ("CAPM"), the Empirical CAPM, the Historical Risk Premium model, the Allowed Risk Premium model, the Discounted Cash Flow ("DCF") Water Utilities Value Line Growth model, and the DCF Water Utilities Analyst Growth model – the proper return on common equity for MAWC, taking into account its business and financial risks, should be set in the upper portion of Dr. Morin's recommended range of 9.2% to 10.7%, that is, at between 10.0% and 10.7%.

Taking into account the cost rates for long-term debt (5.43%), short-term debt (0.73%), preferred stock (9.46%) and common equity (10.70%), the appropriate *pro forma* weighted cost of capital, or fair rate of return, for MAWC applicable to its jurisdictional water and wastewater utility rate base is 8.00% as of January 31, 2016.

Morin (MAWC) (Dir., all; Reb., all; Sur., all)

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<sup>2</sup> Mr. Petry's testimony will be adopted by Mr. Ed Haye.

Rungren (MAWC) true-up testimony (to be filed).

C. What reduction to ROE should be imposed, if any, if the Revenue Stabilization Mechanism proposed by MAWC is adopted?

**MAWC Position:** No adjustment to ROE should be imposed if the RSM proposed by MAWC is adopted because the water companies in Dr. Morin's proxy group already employ a variety of mechanisms like the one proposed by MAWC. Consequently, the market-derived cost of common equity already incorporates the impact of these mechanisms. Thus, while the RSM may reduce earnings risk on an absolute basis, it does not reduce risk on a relative basis.

Morin (MAWC)<sup>3</sup> (Dir., p. 62-65)  
Rungren (MAWC) (Supp., all)

### 3. Revenue Stabilization Mechanism Proposal

Should the Commission adopt the Revenue Stabilization Mechanism proposed by MAWC?

**MAWC Position:** Yes. MAWC's proposed Revenue Stabilization Mechanism (RSM) is an alternative regulatory mechanism that will advance the Commission's goals and moderate future rate increases on customers. Implementation of this alternative regulatory mechanism will remove a disincentive to promote water efficiency and will support earnings that permit continued water efficiency investments. As a ratemaking tool, MAWC's proposed RSM will effectively reduce, or even eliminate, the contentious issue of determining the projected pro-forma water volumes to set water rates and will help ensure that the Company will receive the authorized revenue, no more and no less, and customers will pay the appropriate price for water service in their bills. The RSM compares the rate case authorized amount of metered revenue and actual metered revenues by customer class and defers/accrues the difference, less the applicable change in production expenses. The class of customers to be included in the RSM are residential, commercial, Other Public Authority (OPA), and Sale for Resale. Production expenses would include purchase water, power, chemicals, and waste disposal. The Company is proposing that a reconciliation occur on an annual basis. The first credit or surcharge would occur in the second year, which will true-up any over- or under-collection in revenues, less production costs from the first year. Alternatively, the Commission could require the reconciliation of the regulatory asset/liability to be deferred and addressed in the next general rate case if it had any concerns about the lawfulness of crediting or surcharging customer bills between rate cases.

Watkins (MAWC) (Sur., all)  
Tinsley (MAWC) (Dir., p. 16-32)

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<sup>3</sup> Mr. Morin will appear on Thursday, March 17, 2016.

#### 4. District Allocations

Should a cap of \$20 per customer be imposed on allocations of Corporate A&G expenses and Service Company expenses to small districts?

**MAWC Position:** In its initial filing, MAWC proposed a cap of \$20 per customer on all corporate and joint and common costs allocated to small districts (defined as those with less than 3,000 customers). Since smaller districts do not require the same level of service as the larger districts, the Company was trying to mitigate the allocation of these joint and common costs to the smaller districts, which in turn would mitigate the rates for those smaller districts. Staff opposes any cap on the allocation of these costs to the smaller districts and, for purposes of this case, the Company does not object to Staff's proposal to allocate a full share of the joint and common costs to the smaller districts.

Tinsley (MAWC) (Dir., p. 14; Reb., p. 26-27)

#### 5. Faulty Metering Issue

How should the Commission address the faulty metering issue?

**MAWC Position:** This issue was raised in Staff's surrebuttal testimony, so MAWC has no responsive prefiled testimony. MAWC will provide Cheryl Norton and Greg Roach for any questions that may arise. However, MAWC does not object to the opening of a workshop docket for the purpose of examining this issue.

#### 6. Environmental Cost Adjustment Mechanism ("ECAM") Proposal

Should an ECAM be approved in this case as proposed by MAWC and, if so, what conditions, if any, should be implemented?

**MAWC Position:** The ECAM is a mechanism that will allow periodic rate adjustments that reflect net increases or decreases in qualified environmental costs. It has been proposed by MAWC in accordance with Section 386.260, RSMo, and Commission Rule 4 CSR 240-50.050. The ECAM should be approved with the additional conditions suggested by the Staff witnesses Gateley and Oligschlaeger.

Dunn (MAWC) (Dir., p. 22-23; Sur., p. 5-9)

#### 7. Business Transformation Program

Has American Water Works allocated an appropriate share of the costs of this program to Missouri?

**MAWC Position:** Yes. The Business Transformation Program was designed to serve the needs of the American Water Works (AWW) regulated utility subsidiaries. In certain, limited circumstances, the unregulated subsidiaries of AWW have been

permitted to use some Business Transformation applications. Where this has been permitted, the unregulated affiliates are charged the full cost of using the technology. Accordingly, the costs of the Business Transformation program are appropriately allocated to MAWC and the other regulated subsidiaries of AWW.

Haye for Petry (MAWC) (Petry Reb., p. 14-22; Sur., p. 5-7)

Haye for VerDouw (MAWC)<sup>4</sup> (VerDouw Dir., p. 12-22)

Haye for Wood (MAWC)<sup>5</sup> (Wood Dir., p. 17-22)

## 8. Service Company Costs

Are the costs charged to MAWC by the Service Company for the various services it provides reasonable and appropriate?

**MAWC Position:** Yes. The costs charged to MAWC by the Service Company are reasonable and appropriate. The Service Company provides a variety of professional services to the Company including, but not limited to, billing, customer service, engineering, accounting, finance, legal, rates and regulation, human resources and environmental. These services are provided by the Service Company at its cost with no mark-up for profit. In response to questions raised by Staff and Public Counsel regarding the appropriateness and/or reasonableness of the Service Company costs, the Company retained the services of Mr. Patrick Baryenbruch, President of Baryenbruch and Company, LLC. Mr. Baryenbruch is a management consultant, Certified Public Accountant and Certified Information Technology Professional. Based upon on Mr. Baryenbruch's analysis, he was able to conclude that:

1. MAWC was charged the lower of cost or market for managerial and professional services;
2. On average, the hourly rates for outside service providers are 70% higher than the Service Company's hourly rates;
3. The managerial and professional services provided by the Service Company are vital and could not be procured externally by MAWC, without careful supervision of MAWC; and
4. If all the managerial professional services provided by the Service Company had been outsourced during 2014, MAWC and its ratepayers would have incurred more than \$22 million in additional expenses.

It is clear from Mr. Baryenbruch's analysis that the Service Company's charges to MAWC are both appropriate and reasonable.

Haye for Petry (MAWC) (Reb., p. 2-3)

Baryenbruch (MAWC)<sup>6</sup> (Reb., all)

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<sup>4</sup> Mr. VerDouw's testimony will be adopted by Mr. Ed Haye.

<sup>5</sup> Mr. Wood's testimony on this issue will be adopted Mr. by Ed Haye.

<sup>6</sup> Mr. Baryenbruch will stand cross-examination on all of his issues at this time.

## 9. Income Taxes

A. Should the Commission adopt the adjustment for the *Domestic Production Activities Deduction* (“DPAD”) proposed by OPC?

**MAWC Position:** No. MAWC participates in a consolidated income tax return filed by its parent, American Water Works Corporation. AWW was not able to take advantage of the DPAD because of prior year losses (i.e., net loss operating carry-forward). MAWC contributed to the generation of the consolidated returns’ net operating loss carry-forward; therefore, it would not have been entitled to take a DPAD on its own tax return, if it were to file a stand-alone tax return.

B. What is the appropriate amount of Deferred Income Tax expense to include in the cost of service calculation?

**MAWC Position:** The appropriate amount of deferred income tax expense to include in MAWC’s cost of service is the deferred income tax expense calculated by the Company. Initially, there appeared to be a difference between the Company and Staff’s calculation of deferred income tax; however, it is the Company’s understanding that Staff has corrected its deferred income tax calculation and this is no longer is an issue between the Company and Staff.

Meyers (MAWC) (Dir., all; Reb., all; Sur., all)

## 10. Energy Efficiency

A. Should the Commission adopt the capital deferral mechanism and collaborative proposed by MoDOE to incentivize MAWC to increase supply-side energy efficiency and water loss reduction investment?

B. Should the Commission adopt the demand-side water efficiency program and collaborative proposed by MoDOE?

**MAWC Position:** The Commission should approve a modified deferral mechanism to promote supply-side water and energy efficiency. The proposed deferral mechanism would apply to investments made in excess of a \$50M annual investment threshold in non ISRS plant, up to a limit of \$100 million between rate cases. Projects reviewed and discussed with Staff, OPC, and DE would be eligible to be installed, if MAWC has additional capital available above the threshold amount.

MAWC disagrees with the proposed demand-side water efficiency as it ignores MAWC’s current disincentive to promote demand-side efficiency as MAWC’s revenues are dependent on volumetric charges. Moreover, the investment level suggested by the Division of Energy (0.5% of revenues) is arbitrary until such time as these investments can be planned, staffed, and assessed (i.e., reasonable, measurable and cost effective).

Norton for Kartmann (MAWC)<sup>7</sup> (Kartmann Cor. Dir., p. 26-37)  
Dunn (MAWC) (Reb., p. 6-8)  
Watkins for Wood (MAWC)<sup>8</sup> (Wood Reb., p. 3-7)

## 11. Depreciation Issues

For purposes of this case, MAWC retained the services of John J. Spanos, Senior Vice President of Gannett Fleming Valuation and Rate Consultants, LLC to perform a depreciation study of the Company's depreciable water and wastewater accounts. Mr. Spanos' study (which is attached to his direct testimony) contains detailed calculations, graphs and tables relating to the service lives and net salvage estimates of all accounts. The Company is proposing to implement new depreciation accrual rates in accordance with the results of Mr. Spanos' study and further proposes to adjust its test year depreciation expense by applying those rates to the various plant accounts as of the day that new rates for plant in service go into effect. The differences between Mr. Spanos' recommended depreciation rates and those recommended by Staff in this proceeding center on the use by the Company of Remaining Life Accrual method and implementation of General Plant Amortization as opposed to the Whole Life method of determining depreciation rates recommended by Staff. The Company maintains that Mr. Spanos' study and resulting rates are the most appropriate to use for purposes of this case.

A. What is the appropriate depreciation rate to apply to sewer CIAC?

**MAWC Position:** The appropriate rate to apply to depreciation of sewer CIAC is the depreciation rate applied to sewer assets.

B. Should amounts relating to sewer assets placed by MAWC in water rate base accounts and vice versa be excluded from the cost of service calculation?

**MAWC Position:** No. The Company has committed to correcting this matter and to exclude the amounts from cost of service would be punitive and inappropriate.

C. Given that every water and sewer district has at least one USOA account improperly carrying a negative reserve balance, should Staff's recommended adjustments be adopted?

**MAWC Position:** No. Reserve adjustments should only apply if past transactions at the Company level created negative reserves at the Company level. Additionally, reserve adjustments of any kind should only take place between accounts in the same function.

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<sup>7</sup> Ms. Norton will stand cross on this issue on Monday, March 14, 2016.

<sup>8</sup> Mr. Wood's testimony on this issue will be adopted by Mr. Watkins.

D. Should the depreciation reserve adjustment of \$23,555 recommended by Staff for Ozark Meadows be adopted to offset the improper negative reserve account and, if so, should it be amortized to rates over five years?

**MAWC Position:** No. Past rates have been established on the company level and assigned to district level which created the negative reserve for Ozark Meadows. However, proper application of rates established at the company level should be applied to the Company level for which there is no negative reserve amount for each account. Additionally, use of the remaining life method addresses the reserve issue over the life of the assets so no amortization period is necessary.

E. Has MAWC failed to depreciate the Business Transformation Program as required by the Stipulation and Agreement in Case No. WR-2011-0337, and, if so, how should this be resolved?

**MAWC Position:** No. The Company and Staff agreed to a five percent (5%) rate in MAWC's prior rate case for Business Transformation ("BT") assets before they were put into service to have a rate in place when the software was actually placed in service with the rate to be re-examined when nature of the software application was better understood. The BT assets are information technology ("IT") items that were placed in mid-2012. The Company was not prohibited from recommending a different rate in the next rate case and has recommended a 10-year amortization be applied. Even the assumption of a 10-year service life is optimistic when considering the quick pace at which IT assets are obsoleted.

F. Should the depreciation rates ordered in Case No. ER-2011-0337 be continued in effect as recommended by Staff?

**MAWC Position:** No. As stated above, MAWC is proposing to implement new depreciation accrual rates in accordance with the results of Mr. Spanos' study and further proposes to adjust its test year depreciation expense by applying those rates to the various plant accounts. Additionally, the rates ordered in Case No. WR-2011-0337 do not take into effect the changes in plant activity as well as updated life characteristics.

G. Should MAWC be permitted to use the Remaining Life Method on all but general plant accounts?

**MAWC Position:** MAWC contends that the Remaining Life Method should be employed for all depreciable accounts, including general plant accounts.

H. How should the retirement of the Parkville Water Treatment Plant be handled?

**MAWC Position:** The Parkville Water Treatment Plant and related assets should be depreciated by May 2018. In order to accomplish full recovery by time of retirement, the



Remaining Life Method should be utilized and rates specific to the Parkville assets calculated.

Spanos (MAWC) (Dir., all; Reb., all; Sur., all)  
Haye for Petry (MAWC) (Petry Reb.)  
Wright (MAWC) (Reb., p. 3-5)

## 12. Capitalized O&M Depreciation

Should MAWC capitalize a portion of depreciation expense on tools and equipment partly used on capital projects?

**MAWC Position:** No. These assets have already been depreciated in accordance with their expected service life, generally 5 to 20 years. Staff's proposal would take a portion of the depreciation expense associated with these assets and place that depreciation expense in accounts having lives between 40 and 90 years. MAWC approach allows the costs to be recovered in the same time frame as when the asset will be replaced, thereby maintaining inter-generational equity.

Wright (MAWC) (Reb., p. 12-13; Sur., p. 2-3)

## 13. Property Taxes Expense

Should Property Tax Expense be calculated based on actual known and measureable expenses or on estimated expenses not payable until December 2016?

**MAWC Position:** It is the Company's position that its property tax expense should be based upon its latest known tax assessment rate times its true-up net plant in service. While the Company may not pay its property taxes until December of 2016, it has begun accruing for those taxes on its books beginning on January 1, 2016. This accrual amount is a more accurate representation of the property tax expense that the Company will incur in 2016 and is the most appropriate amount to be used for setting rates in this case.

Tinsley (MAWC) (Dir., p. 44; Reb., p. 31-32)

## 14. Main Break Expense

How should Main Break Expense be calculated?

**MAWC Position:** MAWC believes that main break expense should be calculated by using a three-year average number of main breaks (i.e., years 2012 through 2014) of 807 times the average cost per main breaks for that same three-year period of \$3,306. Bowen for Wood (MAWC)<sup>9</sup> (Wood Dir., p. 29; Reb., p. 2-3)

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<sup>9</sup> Mr. Wood's testimony on this issue will be adopted by Ms. Bowen.

## 15. Lobbying Expense

Should the following items be excluded from the cost of service calculation?

A. MEDA expense?

**MAWC Position:** No. The dues that the Company pays to the Missouri Energy Development Association (MEDA) should not be disallowed in their entirety, as MEDA performs valuable services for its member companies which are not related to lobbying. Only the portion of MEDA's activities relating to lobbying should be disallowed from the Company's MEDA dues.

B. A portion of 10 Service Company salaries for lobbying-related job duties?

**MAWC Position:** No. During the test year (2014), the Company's Director of Government Affairs position was vacant and, as a result, other MAWC and Service Company employees had to step in and provide assistance with legislation pending in the 2014 Missouri legislative session. This was a one-time event for these employees that will not be repeated, as the Director of Government Affairs position has now been filled. Therefore, any adjustment to disallow lobbying-related salaries for these employees who are not engaged in lobbying activities on a regular basis should be disallowed.

Tinsley (MAWC) (Reb., p. 8-9)

## 16. Legal Expense

Should Legal Expense be based on actual payments or on accruals?

**MAWC Position:** The difference between accruals and actual payments is primarily one of timing. Legal expense should be based on actual payments, once those payments have been made, and on accruals when they have not yet been paid.

Tinsley (MAWC)

## 17. Affiliate Transaction Rulemaking

Should the Commission open a separate case to consider adopting an affiliate transaction rule for water companies?

**MAWC Position:** No such rule is necessary as it would be a rule for one company. The Commission has the ability to examine MAWC's affiliate transactions within its rate cases. In particular, Service Company charges are already fully audited and auditable by the Commission Staff and OPC.

Haye for Petry (MAWC) (Petry Reb., p. 20-21)

## 18. Payroll & Payroll Taxes

A. Should a scheduled raise that will take effect after the end of the true-up period be included in the cost of service calculation?

**MAWC Position:** Yes. MAWC is proposing to include in its cost of service a 2.77% wage increase for non-union employees that becomes effective on March 14, 2016. While this date is beyond the true-up date by 43 days, it is well before the operation of law date of June 30, 2016, by 108 days. The annual increase in wage expense associated with this increase is approximately \$294,000. Without recovery of this wage increase, the Company will not recover nearly \$900,000 of expense over the next three years, assuming its next rate case is not filed until mid-year 2018.

B. How much overtime should be included in the cost of service calculation?

**MAWC Position:** The Company used a three-year average to normalize its overtime expense. This three-year average is consistent with the approach followed by both Company and Staff in prior rate cases and results in a reasonable amount of overtime for setting rates in this case.

C. How much Service Company payroll and related expenses should be included in the cost of service calculation?

**MAWC Position:** The Company believes that utilizing the true-up amount of actual annual expense for its Service Company is the most appropriate method for establishing test year Service Company expenses. The Service Company provides a variety of services to MAWC, such as legal, finance, accounting, engineering, design, environmental, and customer services. The Service Company provides these services at its direct cost. As found by an independent study, these costs are lower than the cost or market for similar managerial and professional services. In fact, if all the managerial and professional services now provided by the Service Company had been outsourced during 2014, MAWC and its ratepayers would have incurred more than \$22 million in additional expenses. Therefore, the test year amount of Service Company costs (as of true-up) is a reasonable and appropriate level of expense to include in MAWC's cost of service.

Haye for Petry (MAWC) (VerDouw, Dir., p. 5-12; Petry Reb., p. 2; Sur., p. 2-4)

Tinsley (MAWC) (Dir., p. 38)

Baryenbruch (MAWC)<sup>10</sup> (Reb., all)

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<sup>10</sup> Mr. Baryenbruch will stand cross-examination on all his issues on Wednesday, March 16, 2016.

## 19. Dues & Donations Expense

Should state-level Chamber of Commerce expenses be excluded from rates?

**MAWC Position:** No. The state Chamber of Commerce provides valuable services to its member companies, including MAWC that is not duplicative of the services local Chamber of Commerces provide. The state Chamber deals with larger scope issues and industries and is dedicated to creating a stronger environment for business growth and economic development at the state level. The state Chamber is also focused on broader educational and economic development issues that impact the state or region as a whole, as opposed to the local Chambers which are more focused on the smaller locale they represent.

Tinsley (MAWC) (Reb., p. 34-38)

## 20. Atrazine Settlement

A. Should the amount received through the Atrazine Settlement be shared 50-50 between ratepayers and shareholders or 100 percent be allocated to ratepayers as a reimbursement for amounts they have previously paid?

B. What is the appropriate amortization period to return the regulatory liability amount to ratepayers, three years or five years?

**MAWC Position:** The Atrazine settlement payment represents an out of period, nonrecurring litigation settlement payment in the amount of \$1.16 million received by MAWC as a result of a lawsuit filed against the makers of Atrazine and settled in 2012. MAWC proposes to share the settlement payment 50/50 between the customers and the shareholders. The portion returned to customers should be amortized over a five year period.

Tinsley (MAWC) (Dir., p. 35-37; Reb., p. 13-16)

## 21. Other Employee Benefits & Group Insurance

A. What is the appropriate level of other employee benefits to include in rates for MAWC and Service Company?

**MAWC Position:** MAWC agrees with the amounts for Other Employee Benefits for MAWC and Service Company that are contained in the Staff's true-up workpapers.

B. What is the appropriate level of group insurance to include in rates for MAWC and Service Company?

**MAWC Position:** MAWC agrees with the amounts of Group Insurance for MAWC and Service Company that are contained in Staff's true-up workpapers.

Tinsley (MAWC)

## 22. Pension and OPEBs

A. What is appropriate amount of pension and OPEBS expense to include in the cost of service calculation?

B. Should the pension tracker allow for rate base treatment of differences between the amount of MAWC's cash investment in its pension trust fund and its rate recovery for pension expense?

**MAWC Position:** MAWC proposes to account for pension and OPEBs expense, as well as the pension tracker consistent with the terms of the Stipulation and Agreement from Company's last rate case (Case No. WR-2011-0337, et al.).

Tinsley (MAWC) (Dir., p. 41; Reb., p. 24-25)

## 23. Rents & Leases Expense

A. What amount should be included in the cost of service calculation for Transportation Lease Expense?

**MAWC Position:** MAWC agrees with the amount of Transportation Lease Expense contained in Staff's true-up work papers.

B. What amount should be included in the cost of service calculation for other leases?

**MAWC Position:** MAWC agrees with the amount of expense for other leases contained in Staff's true-up workpapers.

Bowen (MAWC) (Dir., p. 4; Reb., p. 9-11)

## 24. Miscellaneous Expenses

What miscellaneous expense items should be included in the cost of service calculation?

**MAWC Position:** MAWC believes that miscellaneous expenses related to community events and community partnerships which help educate its customers are appropriate expenses and should be included in its test year cost of service. These community events are focused on watershed and water education projects and staffed by Company volunteers. The educational programs benefit customers by increasing their understanding of water resources and systems. Community partnerships work to bring

business and industry into the service area, helping to improve the economy and ultimately reducing rate increases.

Tinsley (MAWC) (Reb., p. 39-40)

## 25. Rate Case Expense

- A. Over what period should rate case expense be normalized?
- B. Should certain rate case expenses be shared between ratepayers and shareholders? If so, which expenses and how?
- C. What expenses should be included in rate case expense?

**MAWC Position:** Rate case expense should be amortized over a 30 month period. MAWC does not believe that rate case expense should be shared. However, if it is, certain expenses such as those associated with the depreciation study required by Commission rule, the individual customer notices, and the outside auditor expenses incurred by MAWC as a result of the Staff review of auditor workpapers should be recovered in total, separate from any sharing. Further, all of the Company's other expenses, to include outside attorneys, consultants, and the Service Company, should be taken into consideration in any sharing.

Tinsley (MAWC) (Reb., p. 16-24)

Haye for Petry (MAWC) (Petry Reb., p. 22-25)

## 26. Purchased Water Expense

What is the appropriate level of expense to reflect in rates for the Spring Valley district for purchased water?

**MAWC Position:** MAWC agrees with the level of purchased water expense contained in Staff's true-up workpapers.

Bowen (MAWC) (Dir., p. 3; Reb., p. 3-4)

## 27. Emerald Pointe Pipeline Rate Base Treatment

Should the cost associated with the portion of a pipeline that was contributed to the City of Hollister be included in rate base?

**MAWC Position:** In order to eliminate a failing sewer treatment plant, Emerald Pointe built a pipeline to a treatment plant owned by the City of Hollister. The pipeline started in Emerald Pointe's legacy certificated area, continued into certificated area granted for purposes of the pipeline (Case No. SA-2012-0362), and then crossed into the city limits of the City of Hollister. The project was placed into service in January of 2013.

As a part of its agreement with Hollister, Emerald Pointe was required to contribute to Hollister that part of the line that sits within the city limits of Hollister. The Emerald Pointe investment related to that portion of the pipeline was \$323,321. This project was reviewed by the Commission both in a certificate case and a financing case related to its construction. Staff's Recommendation concluded that the pipeline project was reasonable and, in, fact cost effective from a capital cost standpoint, with the benefits of elimination of existing treatment facility and sewage discharge into Table Rock Lake as well as making additional capacity available for future customers.

In Emerald Pointe's first rate case after construction, the Staff included the unamortized balance of \$323,321 associated with this portion of the pipeline and an amortization in its calculations of the Emerald Pointe rates that was accepted by the Commission.

The unamortized balance of the investment Emerald Pointe made in this portion of the pipeline was further treated as a part of rate base when MAWC purchased Emerald Pointe.

The Commission should allow MAWC to continue to treat the unamortized balance as rate base along with the amortization that was started in the Emerald Pointe rate case and which was acknowledged when MAWC purchased these properties.

Tinsley (MAWC) (Reb., p. 40–41)

Wright (MAWC) (Wright Sur., p. 3–7)

## **28. Electricity, Fuel and Heating Oil Expense**

What is the appropriate level of electricity, fuel and heating oil expense to include in rates?

**MAWC Position:** Electricity, fuel and heating oil expense should reflect the most current rates for electricity, fuel and heating oil that the Company is experiencing. In addition, the amount of electricity, fuel and heating oil to be consumed should be adjusted to be consistent with the test year revenues and usage amount.

Bowen (MAWC) (Dir., p. 3; Reb., p. 4-5)

## **29. Cash Working Capital**

A. What is the appropriate billing lag?

B. What is the appropriate expense lead or lag treatment for Service Company expenses?

**MAWC Position:** Cash working capital is included in a company's rate base to compensate investors for "upfront" capital that is required in order to fund the daily operations of the business. The timing difference between incurring expenses and the

receipt of the revenue will result in either a net (lead) or lag.

There is a difference between the Company and Staff in this case as to the appropriate calculation of the expense lag for Service Company fees to be used in the Lead/Lag Study. MAWC pays the monthly Service Company bill on or about the 7th or 8th day of the month services are to be provided. This actual payment pattern supports a negative expense lag of 6.01 days.

In addition, there is a difference between the Company and Staff as to the appropriate billing lag (i.e., time from the meter reading date to the time the customer is billed). The Company acknowledges the internal lead/lag study conducted included cancel/rebills within the calculation which lead to billing lags of 5.56 days for St. Louis Metro and 4.81 for all other districts. The Company believes removing the cancel/rebills from its original lead/lag study for this item more accurately reflects the actual experience of the Company of 3.42 days for St. Louis Metro and 3.53 days for all other districts – and should be adopted by the Commission.

Wright (MAWC) (Reb., p. 5-12)

### **30. Arnold Plant Amortization**

A. Should costs related to treatment plant owned by MSD but used by MAWC under contract be amortized over the life of the asset or the term of the contract?

B. Should the difference between the contractual amount being amortized over the contract term or life of the asset be included in rate base?

**MAWC Position:** The City of Arnold entered into an agreement with MSD which, in exchange for principal and interest payments, provided for capacity associated with Arnold's needs in the construction of the MSD Lower Meramec waste water treatment plant. MAWC accepted this obligation when it purchased the City of Arnold sewer system. MAWC proposes that the amounts associated with this agreement be amortized over the expected service lives of the underlying plant (45-50 years) and recovered through rate base.

The net amount of the facility and collection plant is providing service to MAWC's customers. Treating the obligation as rate base in accordance with the expected service life maintains inter-generational equity for current and future customers.

Further, MAWC's proposal reduces the rate impact in this case and the annual cost to the customer is less while receiving the benefits of the plant construction from the agreement.

Tinsley (MAWC) (Reb., p. 42-43)

Wright (MAWC) (Sur., p. 7-9)



### 31. District Consolidation/Consolidated Pricing

Should the Commission adopt the consolidation of districts proposed by Staff, the alternative consolidation proposed by MAWC, or maintain the status quo as proposed by OPC?

**MAWC Position:** It is MAWC's position that its existing water and sewer districts be further consolidated into three (3) water districts and no more than five (5) sewer districts. In its initial filing, the Company proposed consolidation of its water districts into three rate zones and that the rates for service for the customer classes within those zones be the same (i.e., sometimes referred to as Consolidated Tariff Pricing (CTP)). The justification for CTP is the long-term rate stability that results from a consolidated tariff, the similar operating characteristics of each district within a consolidated group, the equivalence of services offered within each group, the equivalent value of service, and the principal of gradualism. The Company's proposed consolidation was based upon its desire to mitigate rate increases based on its proposed overall requested increase. Staff has also proposed three (3) consolidated rate groups in this proceeding; however, Staff has based its consolidation on the similar geographic and operational characteristics of each rate group. The Company has no objection to Staff's proposed rate group consolidation.

In its direct case, the Company proposed to consolidate all of its sewer districts into two (2) rate zones – one for Arnold and a consolidated tariff for all the remaining districts. All of the reasons for consolidating water districts similarly apply to consolidating sewer districts. Staff has proposed consolidation of the existing sewer districts into five (5) rate groups. The Company does not oppose this proposal, as long as rates for sewer service within those groups are uniform.

McDermott (MAWC) (Dir., all; Reb, all; Sur., all)

Herbert (MAWC) (Dir., p. 12-13, 15-19, 21; Reb., p. 3, 10-13; Sur., p. 2-4)

Tinsley (MAWC) (Wood, Dir., p. 26-29; Reb., p. 8-9)

### 32. Rate Design & Customer Charge

A. How should rates be designed?

**MAWC Position:** Rates resulting from this case should be designed to recover the respective costs of service as indicated by the Class Costs of Service (CCOS) submitted by Company witness Herbert in this case. Rates should be uniform for each customer class within each consolidated rate zone. Rates for sewer/wastewater service should also be consolidated (i.e., uniform) for either the sewer/wastewater rate zones proposed by Company or those proposed by Staff.

B. How should the customer charge be adjusted?

**MAWC Position:** The customer charge should be set at a level to recover the actual customer-related costs as shown in the Company's CCOS. In its initial filing, the Company proposed uniform customer charges statewide. Alternatively, the Company would agree to uniform customer charges within each rate zone.

C. How should purchased power expense be allocated?

**MAWC Position:** The purchase power expense should be allocated to each customer class consistent with the demand portion of power costs allocated to extra capacity costs to the degree that it varies with the demand pumping requirements. This is the manner in which the Company has allocated power costs in its CCOS and consistent with the AWWA rates manual.

Herbert (MAWC) (Dir., p. 4-15, 21; Sup., all; Reb., p. 2-10; Sur., p. 4)

### **33. Incentive Compensation Expense**

Should Incentive Compensation related to earnings per share ("EPS") and other financial goals be included in the cost of service calculation?

**MAWC Position:** Yes. MAWC retained the services of Mr. Robert Mustich with the compensation and benefits consulting firm of Towers Watson to review MAWC's compensation program. Mr. Mustich concludes that MAWC's compensation program, including its incentive compensation plans, are comparable to and competitive with market practices of other similarly sized utilities. The compensation programs at MAWC fall within a broad range of market norms and are not excessive in design or level of pay. In fact, while MAWC's target total direct compensation is competitive, it is at the low end of the market median range. Moreover, MAWC's target total direct compensation without short-term and long-term at-risk compensation would not be competitive because it would fall 28% below median from a national perspective and 19% below median from a Midwest regional perspective. Accordingly, MAWC believes its incentive compensation plan (to include financial incentives) is necessary and reasonable to attract and retain quality employees at a level of compensation that is at or below the industry norm. This ability to attract and retain quality employees at a reasonable compensation level is clearly a benefit to MAWC's ratepayers.

Mustich (MAWC)

Haye for Petry (MAWC)

Baryenbruch (MAWC)<sup>11</sup>

Haye for Wood (MAWC)<sup>12</sup>

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<sup>11</sup> Mr. Baryenbruch will stand cross-examination on all his issues on Wednesday, March 16, 2016

<sup>12</sup> Mr. Wood's testimony on this issue will be adopted by Mr. Haye.

### 34. Low-Income Tariff

Should the Commission adopt a low-income tariff for MAWC?

**MAWC Position:** Several parties have raised the issue of affordability depending on the increase in the level of rates as a result of the Commission's decision in this case. If the Commission believes that the rates resulting from this case creates an affordability problem for low-income residential users, the Company has proposed a low-income tariff for the Commission's consideration. The Company's proposed low-income customer rate would provide eligible low-income customers with an 80 percent (80%) discount on the customer charge for a residential 5/8-inch meter.

Tinsley (MAWC) (Sur., p. 4-6; Sur. Sch. JMT1)

### 35. Relocation Expense

What amount of relocation expense should be included in the cost of service calculation?

**MAWC Position:** MAWC agrees with Staff's position.

Tinsley (MAWC)

### 36. Waste Disposal Expense

What amount of waste disposal expense should be included in the cost of service calculation?

**MAWC Position:** MAWC contends that the appropriate level of waste disposal expense to be included in rates should recover the annual amount of waste disposal expense and the amount accrued. The accrual amount is in addition to the actual expense incurred by MAWC. The accrual represents costs expected to be incurred for future scheduled cleanings and waste disposal. The amounts being accrued by MAWC in addition to actual expense are more appropriate for setting rates as they more accurately reflect the waste disposal costs MAWC will experience during the period rates set in this proceeding will be in effect.

Bowen (MAWC) (Dir., p. 4; Sur., p. 11-14)

### 37. Residential Customer Usage/Revenues

How should normalized residential usage be determined for calculating revenues? Is the Company experiencing declining usage?

**MAWC Position:** In establishing rates for MAWC, it is important to calculate a "normalized" level of usage (i.e., gallons per day per customer) and, thus, a

“normalized” level of revenues. A “normal” usage level should represent the customer’s usage that would occur based on average weather patterns. In order to capture a normalized level of usage and revenues, the Company analyzed residential customer base (i.e., non-discretionary) usage for the past ten (10) years. Base usage primarily occurs during winter months when little or no outdoor usage of water occurs. The difference between the customer’s base (non-discretionary) usage and their total usage for the year represents the non-base or discretionary amount of water used by a customer, which is heavily influenced by weather and reflected in outdoor water uses such as lawn-watering, car-washing, cleaning, etc. This bifurcated type of analysis is appropriate because the Company has experienced a significant and continuing decline in residential base water usage, which is attributable to a number of factors, including the prevalence of low-flow (water-efficient) plumbing fixtures and appliances, conservation by customers, and price elasticity. In order to account for this trend in declining residential customer usage, Company witness Roach performed a linear regression analysis on ten (10) years of historical base residential usage to create a best fit trend line. He then performed a separate analysis of the non-base (or discretionary) residential usage to normalize for weather effects. The trend projection of the base usage was then added to the ten (10) year average of discretionary usage to determine the projected residential customers’ usage (and revenues) for 2016. The Company’s bifurcated approach to analyzing base and non-base water use is superior to using a simple average of customer use because such an average is biased by the varying weather conditions experienced during the years to be averaged and, more importantly, fails to capture the significant decline in residential customer base usage. If rates are not set on a normalized level of non-base discretionary usage and do not reflect the continuing declining trend in customer base usage, test year revenues will be over-stated and the Company will not have a reasonable opportunity of achieving those overstated revenues and earning its authorized return.

Roach (MAWC) (Dir. Sup.; Reb.; Sur., all)

Dunn (MAWC) (Dir., p. 15-22)

Tinsley (MAWC) (Dir., p. 32-35)

### **38. Non-Residential Revenues**

A. What is the appropriate annualized customer level for each revenue class?

**MAWC Position:** The appropriate annualized customer level for the residential class is as described above. The appropriate annualized level of usage for other customer classes should be based on the actual test year usage for each customer class (i.e., commercial, industrial, etc.).

B. What is the appropriate annualized revenue to include in rates for all non-residential categories?

**MAWC Position:** The appropriate annualized revenue to include in rates for all non-residential categories is the actual test year usage for each class of customers. This is

because usage for these non-residential customer classes does not exhibit the sensitivity to weather that residential usage exhibits. Moreover, the use of the most recent usage for these non-residential customer classes reflects the decline in customers and usage, which has actually been experienced by MAWC.

C. Should 5-year averages be used in calculating Miscellaneous Revenues or should the Test Year values be used?

**MAWC Position:** MAWC believes that actual test year values should be used for calculating miscellaneous revenues.

Tinsley (MAWC) (Dir., p. 32-35)

### **39. Miscellaneous Charges**

Should existing miscellaneous charges be modified and, if so, how?

**MAWC Position:** No. Staff's proposal to adjust, and, in most cases reduce, existing miscellaneous charges is based on a high level, district cost study for miscellaneous charges which only includes average labor costs. This study was performed at the request of Staff but, because of the time constraints, was not able to be fully developed. An appropriate cost study should reflect the fully-loaded costs and overheads attributable to the service function in question. Inasmuch as the Company has not performed a fully-loaded cost study for miscellaneous charges, it does not believe that modifying miscellaneous charges at this time is appropriate.

Dunn (MAWC) (Sur., p. 9-11)

### **40. Infrastructure System Replacement Surcharge (ISRS)**

How should the Commission address the Western District Court of Appeal's opinion in WD78792?

**MAWC Position:** The Commission need not address the referenced order in this case. The Company's ISRS will be set to zero at the conclusion of this case as required by statute and rule and no additional ISRS may be charged unless so ordered by the Commission in a separate proceeding. Moreover, the referenced order is not yet final and, even if it was, any remedy will be addressed separately when the case is returned to the Commission.

No testimony should be necessary in regard to this issue as it is a legal issue more appropriately addressed in the briefs of the parties.

Tinsley (MAWC) (Reb., p. 43-45)

#### 41. Chemicals Expense

What amount of chemicals expense should be included in the cost of service calculation?

**MAWC Position:** The amount of chemical expense to be included in the cost of service is an amount needed to treat water and wastewater under normal conditions and demands at current contract prices. For purposes of this case, the Company used the most current known costs for chemicals and then calculated chemical costs based on the Company's normalized level of usage and revenues.

Bowen (MAWC) (Dir., p. 43; Reb., p. 28-31, p. 33-34)

#### 42. Insurance Other Than Group Expense

What amount of insurance expense should be included in the cost of service calculation with respect to the following items:

- A. Directors and Officers Liability Policy? Kidnap and Ransom Insurance?
- B. MAWC's proposed retrospective accrual adjustment?

**MAWC Position:** The premiums associated with Directors and Officers Liability and Kidnap and Ransom Insurance should be included in the cost of service. These are both necessary and customary business expenses for the Company in order to recruit persons to serve on the Board of Directors and in executive management. In particular, the D & O insurance is important given the many statutes and regulations that apply to a publicly traded corporation. In particular, the duty to defend is an important aspect of this policy.

As to Retrospective Insurance, an adjustment for the three year average should be included in the cost of service. This is a common form of insurance for large corporations that allows the insured to pay for losses associated with workers compensation, general liability and auto liability as they are incurred rather than paying for an enormous guarantee cost premium up-front at the beginning of the insurance policy period.

Tinsley (MAWC) (Reb., p. 28-31)

#### 43. Advertising Expense

What amount of advertising expense should be included in the cost of service calculation?

**MAWC Position:** MAWC agrees that certain advertisements should be disallowed that are truly institutional or political in nature; however, the Company does not agree with Staff's characterization of certain ads as institutional or political in nature. For example,

Staff has disallowed expenses associated with ads relating to MR350 River Race, Wings Over Water, Magnificent Missouri, Trash Bash, Tap Water Quality, Hydrant Flushing, Watershed Education and Earth Day. These advertisements, in Company's opinion, are more appropriately categorized as informational advertising or advertising which conveys the ways to safely use water and avoid accidents. Accordingly, the Company believes the expenses for these ads should be included in its cost of service.

Tinsley (MAWC)

#### **44. Promotional Items Expense**

What amount of expense relating to promotional giveaway items should be included in the cost of service calculation?

**MAWC Position:** MAWC disagrees with Staff's proposed disallowance of certain promotional expenses related to water bottles which MAWC distributes at multiple community events. These bottles promote the use of tap water (over bottled water) and provide MAWC's web address so customers can get additional information. These bottles are provided as part of the Company's community outreach efforts and underscore the environmental stewardship mission of the community events that MAWC supports.

Tinsley (MAWC) (Reb., p. 38-39)

#### **45. Tank Painting Expense & Tank Painting Tracker**

- A. Should the tank painting tracker be continued?
- B. If so, what should the base be?
- C. How much tank painting expense should be included in the cost of service calculation for the amortization of the regulatory asset?

**MAWC Position:** Failure to timely replace the coatings may lead the tank to fail prematurely (i.e., shorten its life span) because of the destructive impact of corrosion. The cost to paint varying sizes and types of tanks is vastly different and setting an annual expenditure to recover this variability is not easily accomplished. For example, the 11 million gallon Stratmann Tank #2 will need to be painted in the next few years at an estimated cost of \$2.2 million. The tank painting tracker is an appropriate mechanism to address the variability and insure that MAWC recovers no more and no less than its actual tank painting expense. The Tank Painting Tracker should be continued at an annual amount of \$1,300,000.

Further, the tracker balance at the end of January 31, 2016, should be amortized over a period of three years, and to include the unamortized balance of the regulatory asset in rate base.

Dunn (MAWC) (Reb., p. 2-6; Dunn Sur., p. 2-5)

#### 46. Postage Expense

What amount of postage expense should be included in the cost of service calculation?

**MAWC Position:** MAWC believes that the amount of postage expense included in its test year cost of service should reflect the new postage rate increase that became effective January 17, 2016, and also reflect any increase in postage expense that will occur as a result of new sewer and water acquisitions acquired prior to the true-up date.

Tinsley (MAWC) (Dir., p. 43; Reb., p. 42)

#### 47. Union Issues

A. Should the Commission condition any rate increase upon MAWC's filling unfilled bargaining unit positions?

**MAWC Position:** No. MAWC has worked diligently to review staffing opportunities resulting from attrition and to continually evaluate the needs and priorities of its business. MAWC fills positions as business needs dictate. MAWC continually evaluates its business to identify costs savings and efficiencies. Reductions in workforce may occur when it is determined there is a more efficient way to perform operations, for example, replacing obsolete equipment and automating processes. As a result, MAWC provides safe and adequate service, meets the high standards required by the Missouri Department of Natural Resources, the Partnership for Safe Water, and continues to receive high customer satisfaction rating. There is no evidence to require the Commission to condition any rate increase upon the filling of unfilled bargaining unit positions, particularly when there has been no provision for such positions in the Company's cost of service in this case.

B. Should the Commission order semi-annual reporting of various items as urged by the Unions?

**MAWC Position:** No. The semi-annual reporting recommended by the Union relates to the Company's valve maintenance program and, as described below, such a valve maintenance program is neither necessary nor cost beneficial for MAWC or its customers.

C. Should the Commission order MAWC to comply with and implement American Water Works' valve maintenance program?

**MAWC Position:** No. While MAWC's parent, American Water Works, does have a recommended practice for valve exercising, it is not mandatory and each subsidiary is



free to adopt all or part of the practice if the benefits exceed the cost of such a program. In MAWC's case, there is no need to adopt the American Water Works valve maintenance program. Because nearly 10,000 valves are operated annually in response to main breaks that occur in St. Louis. MAWC also assigns valve maintenance work (repairing known broken valves) as fill-in work for crews when main breaks are at low levels. Accordingly, it is not necessary or appropriate to require MAWC to adopt American Water Works' valve maintenance program.

Norton for Wood (MAWC)<sup>13</sup> (Wood Dir., p. 8-9; Reb., p. 10-13)

Dunn for Wood (MAWC)<sup>14</sup> (Wood Dir., p. 8-9; Reb., p. 10-13)

#### **48. Corporate Franchise Tax**

What amount should be excluded from the cost of service calculation for the expired Missouri franchise tax?

**MAWC Position:** The Company agrees that franchise tax liability has expired and franchise tax expenses should be excluded from the cost of service calculation.

#### **49. Outside Services**

What amount of outside services should be excluded from the cost of service calculation?

**MAWC Position:** MAWC believes its test year expense related to Service Company charges is appropriate and no adjustment for outside services, as proposed by Staff, is appropriate.

#### **50. General Ledger**

Should the Commission require MAWC to keep its General Ledger in accordance with the USOA?

**MAWC Position:** MAWC believes that it keeps its General Ledger in accordance with the Commission's rules and the Uniform System of Accounts.

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<sup>13</sup> Ms. Norton will adopt Mr. Wood's testimony on unfilled positions.

<sup>14</sup> Mr. Dunn will adopt Mr. Wood's testimony on valve maintenance.

**WHEREFORE**, MAWC respectfully requests that the Commission consider these statements of position.

Respectfully submitted,

/s/ Dean L. Cooper

William R. England, III      MBE# 23975  
Dean L. Cooper                MBE# 36592  
Paul A. Boudreau            MBE#33155  
BRYDON, SWEARENGEN & ENGLAND P.C.  
312 East Capitol Avenue  
P.O. Box 456  
Jefferson City, MO 65102-0456  
Telephone: (573) 635-7166  
[dcooper@brydonlaw.com](mailto:dcooper@brydonlaw.com)

ATTORNEYS FOR MISSOURI-AMERICAN  
WATER COMPANY

### **CERTIFICATE OF SERVICE**

The undersigned certifies that a true and correct copy of the foregoing document was sent by electronic mail on March 11, 2016, to counsel for the parties to Case No. WR-2015-0301.

/s/ Dean L. Cooper