

Exhibit No.:
Issues: Inclining Block Rates, CTP, RSM, Fixed
Charges, LSLR
Witness: James M. Jenkins
Exhibit Type: Rebuttal-Rate Design
Sponsoring Party: Missouri-American Water Company
Case No.: WR-2017-0285
SR-2017-0286
Date: January 24, 2018

MISSOURI PUBLIC SERVICE COMMISSION

**CASE NO. WR-2017-0285
CASE NO. SR-2017-0286**

**REBUTTAL TESTIMONY
RATE DESIGN**

OF

JAMES M. JENKINS

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

Exhibit No. 208
Date 3/13/18 Reporter MH
File No. WR-2017-0285

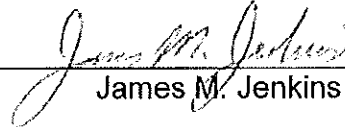
Exhibit 20P
WR-2017-0285
Rebuttal Testimony – Rate Design of
James M. Jenkins - Public

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

IN THE MATTER OF MISSOURI-AMERICAN)	
WATER COMPANY FOR AUTHORITY TO)	
FILE TARIFFS REFLECTING INCREASED)	CASE NO. WR-2017-0285
RATES FOR WATER AND SEWER)	CASE NO. SR-2017-0286
SERVICE)	

AFFIDAVIT OF JAMES M. JENKINS

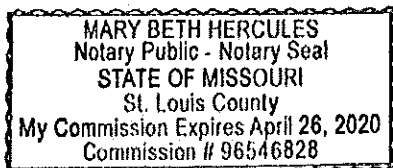
James M. Jenkins, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Rebuttal Testimony Rate Design of James M. Jenkins"; that said testimony was prepared by him and/or under his direction and supervision; that if inquiries were made as to the facts in said testimony, he would respond as therein set forth; and that the aforesaid testimony is true and correct to the best of his knowledge.


James M. Jenkins

State of Missouri
County of St. Louis
SUBSCRIBED and sworn to
Before me this 16th day of January 2018.


Notary Public

My commission expires:



**REBUTTAL TESTIMONY
RATE DESIGN
JAMES M. JENKINS
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WR-2017-0285
CASE NO. SR-2017-0286**

TABLE OF CONTENTS

I. INTRODUCTION.....	2
II. OVERVIEW.....	2
III. INCLINING BLOCK RATES.....	2
IV. CONSOLIDATED TARIFF PRICING.....	7
V. PROPOSED REVENUE STABILIZATION MECHANISM.....	16
VI. FIXED CHARGES.....	19
VII. LEAD SERVICE LINE REPLACEMENT COST ALLOCATION	20

**REBUTTAL TESTIMONY
RATE DESIGN**

JAMES M. JENKINS

I. INTRODUCTION

1

2 **Q. Please state your name and business address.**

3 A. My name is James M. Jenkins and my business address is 727 Craig Road, St. Louis,
4 Missouri 63141.

5 **Q. Are you the same James M. Jenkins who previously submitted direct testimony
6 and revenue requirement rebuttal testimony in this proceeding?**

7 A. Yes.

II. OVERVIEW

8

9 **Q. What is the purpose of your rate design rebuttal testimony?**

10 A. The purpose of my rate design rebuttal testimony is to address at a policy level certain
11 issues raised by various parties on rate design matters, including: inclining block rates,
12 consolidated tariff pricing; Missouri-American Water Company's ("MAWC",
13 "Company" or "Missouri-American") proposed Revenue Stabilization Mechanism
14 ("RSM"), fixed customer charges, and cost allocation of the Company's proposed lead
15 service line replacement ("LSLR") program.

III. INCLINING BLOCK RATES

16

17 **Q. Is the Company aware of the Missouri Public Service Commission's
18 ("Commission") interest in the concept of inclining block rates?**

1 A. Yes. As indicted in my direct testimony (at page 36), in the Report and)Order issued
2 in the Company’s most recent rate case, the Commission requested information on
3 inclining block rates be provided in the Company’s next rate case for consideration in
4 setting just and reasonable rates. (*In the Matter of Missouri-American Water Company,*
5 *Report and Order, Case No. WR-2015-0301, p. 41, (May 26, 2016), (“2015 Rate*
6 *Order”*)).

7 **Q. Did the Company propose inclining block rates in this case?**

8 A. No. The Company proposed uniform rates, given that the trend of declining usage per
9 customer experienced by the Company, and suggested that the introduction of inclining
10 block rates would be an unnecessary step in Missouri.

11 **Q. Did any other parties address inclining block rates?**

12 A. Yes. Both the Staff of the Commission (“Staff”) and Missouri Department of
13 Economic Development, Division of Energy (“DE”) addressed the issue. (Dietrich,
14 *Dir., p. 3, ln. 1-11; Hyman, Dir., p. 9, ln. 5-15)*

15 **Q. What do these parties propose regarding implementation of inclining block rates?**

16 A. Staff does not support introduction of inclining block rates in this proceeding. (Dietrich,
17 *Dir., p. 3, ln. 9-11*). DE indicates it would only support their introduction under certain
18 conditions that mitigate bill impacts for some customers, while at the same time
19 implementing targeted efficiency measures. (Hyman, *Dir., p. 19, ln. 3-9*)

20 **Q. Do you interpret DE witness Hyman’s testimony as proposing inclining block**
21 **rates in this proceeding?**

1 A. No. Mr. Hyman states that “depending on the consolidation and revenue requirement
2 decisions in this case, MAWC should be required to implement residential inclining
3 block rates in this or a subsequent case, based on an evaluation of bill impacts.” (Hyman
4 Dir., p. 12; ln. 18-19). Since this is dependent on decisions that will occur later in this
5 case, I read Mr. Hyman’s testimony as proposing that the Company be potentially
6 ordered to implement inclining block rates sometime in the future.

7 **Q. What potential structures for inclining block rates does DE witness Hyman**
8 **discuss?**

9 A. Mr. Hyman posits that the first block for an inclining block structure should encompass
10 the basic amount of indoor water usage for an average household and that rates should
11 be designed not just to recover costs from cost causers and encourage efficiency, but
12 with an understanding of bill impacts on customers at varying levels of usage. (Hyman
13 Dir., p. 11, ln. 10-13; p. 12, ln. 1-7)). He concludes by noting that initially, inclining
14 block rate designs should avoid severe bill impacts on high-use customers: for example,
15 rates could be designed such that customers at the 95th percentile of use experience no
16 greater than a five percent monthly bill impact under a new rate design on a revenue-
17 neutral basis. (*Id.* p. 12, ln. 4-7)

18 **Q. Do you agree with DE witness Hyman regarding how inclining block rates should**
19 **be designed as applied to MAWC?**

20 A. In general, no. I disagree that inclining block rate designs should avoid bill impacts
21 on high-use customers such that they experience no greater than a five percent monthly
22 bill impact under a new rate design on a revenue-neutral basis. As explained further in
23 Company witness Heppenstall’s rate design rebuttal testimony, there is no reason to

1 implement inclining block rates unless there is a bill impact sufficient to send a
2 customer an appropriate price signal to encourage conservation. Artificially capping
3 the impact on high use customers that have the greatest potential for achieving
4 conservation defeats the purpose for implementing inclining block rates.

5 **Q. Although not proposed in its direct testimony, is the Company willing to consider**
6 **an inclining block rate structure under specific, controlled conditions?**

7 A. Yes. If the Commission is interested in pursuing inclining blocks, the Company would
8 propose the implementation of a pilot program with inclining block rates in the
9 Company’s Joplin service area, conditioned on the approval of the proposed RSM
10 across the Company’s whole service area.

11 **Q. Why is the Company proposing a pilot program as opposed to an immediate**
12 **system-wide implementation of inclining block rates?**

13 A. As Staff witness Dietrich noted at page 3 of her direct testimony, there are uncertainties
14 associated with inclining block rate implementation. To minimize these uncertainties,
15 the Company is proposing a limited inclining block pilot program (“Inclining Block
16 Pilot Program”). The use of a pilot program in the Joplin district only means that the
17 initial use of inclining block rates will be done in a controlled manner in a specified
18 geographic area. The pre-condition that the Inclining Block Pilot Program only move
19 forward with approval of a Company-wide RSM further mitigates uncertainty and
20 negative revenue impacts that may result.

21 **Q. Why does the Company believe that the Joplin district would be the most**
22 **appropriate area to consider for an Inclining Block Pilot Program?**

1 A. As explained in the direct testimony of MAWC witness Roach, “there is a continuing
2 annual decline of residential water use across all MAWC districts averaging 1,356
3 gallons per customer.” Mr. Roach further explains:

4 This decline can be attributed to several key factors, including but not limited
5 to: increasing prevalence of low flow (water efficient) plumbing fixtures and
6 appliances in residential households, customers’ conservation efforts,
7 conservation programs implemented by the federal government, state
8 government, MAWC and other entities, and price elasticity.

9 (Roach Dir., p 5).

10 As we all know, a devastating EF5 tornado struck Joplin on May 22, 2011. As a result
11 of the Joplin Tornado, over fourteen percent of the number of households replaced all
12 of their appliances (Roach Dir., p. 25, ln. 10). Consequently, one would expect to better
13 discern the effect of an inclining block rate on customer consumption in the Joplin
14 district than in any other MAWC district because a significant amount of water
15 efficiency has recently taken place by customers. Moreover, MAWC experiences
16 conditions of strained water supply from time to time in the Joplin area, and use of an
17 inclining block rate structure could potentially encourage water conservation among
18 higher use customers. A pilot program in the Joplin area would provide an opportunity
19 to see how higher marginal water rates could encourage conservation in an area with
20 strained water resources.

21 **Q. Please expand further on the proposed Inclining Block Pilot Program and the**
22 **blocking structure developed by the Company.**

23 A. The details of the blocking structure and its development are set forth at length in
24 Company Witness Heppenstall’s rate design rebuttal testimony (p. 7-9). As discussed
25 above, as a result of rebuilding from the recent tornado, many customers in the Joplin
26 system replaced their old water fixtures with new water savings fixtures. This

1 accelerated change-out will aid in isolating any resulting reductions in water usage as
2 due to price sensitivity and not due to other conservation methods.

3 **Q. In summary, what are the benefits of implementing the Company's proposed**
4 **Inclining Block Pilot Program?**

5 A. The implementation of the Inclining Block Pilot Program will provide the Company
6 with experience in offering an inclining block rate and will enable the Company and
7 the Commission to achieve a better understanding of how inclining block rate designs
8 impact actual customer behavior and resulting conservation while minimizing
9 uncertainty.

10 **IV. CONSOLIDATED TARIFF PRICING**

11 **Q. Would you please summarize the parties' responses to the Company's proposed**
12 **consolidated tariff pricing (CTP)?**

13 A. The Company proposes the current three district tariffs be consolidated into a single
14 tariff for water service. (LaGrand Dir., p. 17, ln. 18-19). In response to this proposal,
15 several parties have raised objections:

- 16 • Staff recommends retaining the current three water district pricing,¹ and objects to
17 further consolidation based on the following allegations:
 - 18 ○ The current three district pricing combines benefits from CTP by
19 minimizing rate impacts of large capital costs while at the same time
20 aligning rates paid with costs incurred because the current three districts
21 contain areas with similar operating characteristics. (Missouri Public

¹ For sewer, Staff recommends the districts with the highest rates be set on a flat fee of \$66.93/month with the other lower rate districts bearing any rate increases resulting from this case. (Staff COS Report, p. 14)

- 1 Service Commission Water and Sewer Department, Staff Report - Class
2 Cost of Service and Rate Design (“Staff Report - CCOS”), p. 11, ln. 25-30))
- 3 ○ The current three districts are more manageable from an operations and
4 regulatory perspective. This allows the Company to continue to invest while
5 at the same time operating as a restraint on the Company overspending on
6 any project. (*Id.*, p. 12, ln. 1-6)
 - 7 • Office of the Public Counsel (“OPC”) objects to further consolidation because it
8 alleges:
 - 9 ○ Costs of providing water service are “local” and therefore any further
10 consolidation of rates will send inappropriate price signals. (Marke Dir., p.
11 2, ln. 9- p. 6, ln. 6; p. 7, ln. 18 – p. 9, ln. 21)
 - 12 ○ The Company will have a resulting incentive to overinvest. (*Id.*, p. 9, ln. 23-
13 p. 13, ln. 11)
 - 14 • The Missouri Industrial Energy Consumers (“MIEC”) objects on the following
15 grounds:
 - 16 ○ The Company does not provide economic or other studies to justify the
17 purported benefits of further consolidation. (Collins, Dir., p. 4, ln. 1-5; p. 4,
18 ln. 10-11)
 - 19 ○ There is no common or economic cost structure across the three districts.
20 (Collins, Dir., p. 5, ln. 11 – p. 6, ln. 2)
 - 21 ○ CTP ignores the cost differences between districts. (*Id.*, p. 6, ln. 3 - p. 14)
 - 22 ○ Water system efficiency could be eroded (*Id.*, p. 6, ln. 15 – p. 7, ln. 14)
 - 23 ○ The Company may not undertake appropriate due diligence when
24 purchasing new water systems. (*Id.*, p. 7, ln. 15-20)

1 • The Coalition Cities disagree with the benefits of CTP as described in my direct
2 testimony and conclude that the Commission should reverse its decision in the 2015
3 Rate Order moving back to eight districts either through de-consolidation of tariffs
4 or a transfer payment scheme that would benefit the Coalition Cities and paid for
5 by the Company's other customers. (McGarry, Dir., p. 14 ln. 8-19)

6 **Q. What is your overall response to these objections?**

7 A. For the most part, these objections have been leveled at CTP in previous cases and by
8 the same parties. In my opinion, the **only** legitimate concern raised by the parties is that
9 of cost-causation and its related effect on prices. In its 2015 Rate Order, the
10 Commission addressed this issue and concluded from the facts in that case, which are
11 substantially the same as this case, the following:

12 Despite the inherent differences in the various water systems,
13 Missouri-American's annual cost to serve a residential customer
14 is fairly consistent across the existing districts. (2015 Rate Order
15 ¶21)

16 The consistency in costs to serve customers between districts is
17 attributable to the fact that most of the costs of providing service
18 to Missouri-American's customers are very similar, if not the
19 same, from district to district because a portion of Missouri-
20 American's statewide costs are allocated to the various districts.
21 (2015 Rate Order ¶22)
22

23 **Q. Do you agree with the Commission's conclusion in the 2015 Rate Order as applied**
24 **to the facts in this case?**

25 A. I do. For the most, part costs are similar across districts for the very reasons that the
26 Commission identified. While one could point to some cost differentials between areas
27 of a current district or between districts, and the Commission identified such

1 differences, the question remains one of what policy is likely to promote the public
2 interest.

3 **Q. How does *policy* fit into this decision?**

4 A. It is instructive to read the Commission's decision on this issue from the 2015 Rate
5 Order:

6 The Commission's task in this case is to devise a rate structure
7 that is just and reasonable for all Missouri-American's
8 customers, no matter where they live within the company's
9 service area. The Commission must also ensure that the rates it
10 authorizes do not unduly or unreasonably grant a preference or
11 impose a prejudice on any person, corporation, or locality. That
12 is a difficult task that requires a great deal of balancing differing
13 interests. Missouri-American's cost to serve its customers is one
14 factor to be balanced, but it is not the only factor.

15
16 The needs of the customers must be met no matter where they
17 happen to live, or how recently the company's infrastructure in
18 their area was installed or replaced.

19
20 Consolidated pricing will help to meet the needs of all customers
21 by sharing the cost of providing needed services among a larger
22 group of customers, making the cost of service more affordable
23 for all. Consolidation will limit rate shock when new
24 infrastructure must be installed in a district with a small
25 population, and all districts will eventually face that prospect.

26
27 Consolidation is not without risk. It averages rates and inevitably
28 some customers will pay more than they pay now, and some will
29 pay less. At least in the short term that will be seen by some as
30 unfair, but, over the long term, the effects of consolidation will
31 even out across the state. It is not reasonable to keep patching
32 the current group of rate districts to deal with the needed, but
33 unaffordable, infrastructure repairs and improvements as they
34 occur. (2015 Rate Order, p. 27)

35 In this decision, the Commission is articulating a public policy rationale for
36 consolidation. That rationale takes into account the Company's current historic
37 depreciated cost of service yet also takes into account other factors such as the needs
38 of customers regardless of where they live, mitigating rate shock to the extent possible,

1 and providing a mechanism that will allow for the necessary investment to provide
2 service to all customers, not just those lucky enough to live in an area that has enough
3 customers to help minimize the effect of the fixed costs of investment or has older plant
4 that serves that area.

5 **Q. Did the Commission further address full single-tariff pricing?**

6 A. Yes. The Commission noted that “[f]ull single-tariff pricing is an attractive option but
7 since none of the parties proposed that option during the case it was not fully considered
8 by the parties.” (2015 Rate Order, p. 28).

9 **Q. Has the Company proposed further consolidation of its pricing in this case?**

10 A. Yes. The Company has proposed to take additional steps toward single-tariff pricing
11 in this case (LaGrand, Dir., p. 17 -18) and the parties are now fully considering the
12 issue. As I noted above, the issues or concerns raised by the parties are substantially
13 the same as raised in the previous case. Moreover, the public policy grounds that the
14 Commission based its consolidation decision upon in the 2015 Rate Order remain fully
15 applicable in this case. The evidence in this case and the Commission-articulated
16 public policy grounds support the implementation of consolidated tariff pricing as
17 proposed by the Company.

18 **Q. What is your response to the proposals to retain the current three district tariffs
19 cited above?**

20 A. In my direct testimony, I listed a series of potential benefits of CTP. (Jenkins Dir., p.
21 40, ln. 17- p. 42, ln. 6). Each of these arguments in favor of CTP have been recognized

1 by regulators as legitimate benefits of CTP.² Indeed, the EPA CTP Report cites several
2 other arguments in favor of CTP, including setting rates on a basis similar to other
3 utilities, physical interconnection of systems being unnecessary for CTP, promoting
4 universal service, encouraging private investment in water systems, and promoting
5 ratepayer equity on a regional basis. While this report also lists the arguments that have
6 been proffered against CTP—largely focusing on the cost of service issues noted
7 above—the purpose of the report is to identify for policymakers the trade-offs of CTP
8 such that regulators can make an informed decision. Importantly, Staff has articulated
9 two benefits of CTP that should not be overlooked:

- 10 • Allocation of common costs can be difficult when utilizing district-specific
11 pricing. (Staff Report - CCOS, p. 12, ln. 7-13)
- 12 • The cost spreading effect can be beneficial to smaller water systems in need
13 of investment. (Id., p. 12, ln. 14-25)

14 While Staff cites these benefits in support of its proposal to maintain three districts,
15 these benefits are not limited to Staff's proposal and are equally supportive of the
16 Company's proposed consolidation. Indeed, while the allocation of common costs
17 remains a problem with Staff's proposal, it does not for the Company's proposal.
18 Moreover, the cost-spreading effect is stronger under the Company's proposal than
19 Staff's. One can only conclude that these benefits, which I agree exist, are more
20 favorable to the Company's proposal.

² See e.g., "Consolidated Water Rates: Issues and Practices in Single-Tariff Pricing," September 1999, US Environmental Protection Agency and NARUC, ("EPA CTP Report") p. viii.

1 **Q. Staff claims that “the current size of the districts is logistically more manageable,**
2 **both from an operations and regulatory perspective” (Staff Report - CCOS, p.**
3 **12). Do you agree?**

4 A. No, I do not agree that the current size of the districts is more manageable from an
5 operations and regulatory perspective than a single consolidated tariff pricing structure.
6 The Company currently operates its system as a whole, and manages its districts with
7 a common focus on safe, reliable, and efficiently-provided service. This does not
8 change due to arbitrary tariff pricing lines drawn throughout the system. There are also
9 costs to maintain separate tariff rate structures that would not be incurred under CTP.
10 For example, customer care functions must be designed with multiple tariff rates in
11 mind. Consolidation of the Company’s tariff pricing is preferable because it will lead
12 to lower administrative cost. As I explain in my direct testimony (p. 41-42),
13 simplifying rate structures also leads to lower administrative costs as utilities can more
14 easily help customers who have questions and lower the cost of billing and collections.
15 CTP can also reduce the regulatory cost of separate filings within a single rate
16 proceeding.

17 **Q. As noted in the summary of the parties’ positions in this section of your rebuttal**
18 **testimony, some parties, including Staff, maintain that CTP will lead to**
19 **“overspending” on the part of the Company. How do you respond to this**
20 **assertion?**

21 A. First, the parties making these claims have provided no evidence that such an incentive
22 exists and that the Company would, or has, “overspent.” The Company has had some
23 version of consolidated pricing for many years. (A brief history of the issue through
24 2010, is found in Missouri-American Water Company’s Brief in Case No. SW-2011-

1 0103, pp. 3-5; *also see* 2015 Rate Order, ¶9, pp. 7-8.) To my knowledge, there is no
2 evidence that the Company systematically has “overspent” as a result of consolidation
3 of tariff rates.

4 Second, as a practical matter, the Company invests in its system to provide the same
5 quality of water for all customers, while applying the appropriate technologies, plant
6 and equipment. Whether rates are consolidated or not, this approach will not change,
7 and the Commission should expect that the Company will maintain its focus on
8 providing water in an efficient manner.

9 Third, the Company is always at risk for a prudence disallowance if it can be shown that
10 it spent in an imprudent way. In addition, we would be doing a disservice to our owners
11 if we systemically install equipment imprudently.

12 Fourth, I do not see how consolidating tariffs will lead to more complicated prudence
13 reviews. (Collins Dir., p. 7, ln. 3-13). Prudence reviews are the mechanism used by
14 regulators to prevent any alleged “overspending.” MIEC witness Collins claims that
15 we will no longer maintain “separate books and records by district.” That is only true
16 in its literal sense. All of the data, analysis, and other supporting documentation for
17 our investments and other spending will still be available to the Commission, and
18 through the proper channels, all stakeholders. Indeed, this argument puzzles me since
19 electric and gas utilities operate under consolidated tariffs in nearly every jurisdiction
20 in the country and there does not seem to be a concern about regulatory oversight of
21 these utilities. In Missouri, MAWC currently operates under tariffs that are
22 consolidated such that about 80 percent of our customers and sales are in District 1, yet

1 no one has shown or even alleged that we are “overspending” currently or that the
2 Commission has diminished ability to discharge its authority over the Company.

3 **Q. Will CTP lead to an erosion of the efficiency of the system?**

4 A. No. MIEC witness Collins makes two separate arguments. First, he claims that
5 customers in “high” cost regions are less likely to undertake conservation if prices are
6 lower. Second, he claims that prudence reviews will be more difficult. I addressed the
7 second issue above. On the first issue, Mr. Collins makes a mountain out of a molehill.
8 For example, if it is true that customers in “high cost” regions will recklessly increase
9 usage because their prices are lower than some hypothetical level that could have been
10 charged, it must also be true that customers in “low cost” areas will decrease their usage
11 because the price is above some hypothetical price that could have been charged. The
12 efficiency or “price elasticity” effects, if there are any, are unclear from Mr. Collins
13 testimony. Moreover, as the Commission has noted, the costs between districts are
14 relatively close. Any alleged inefficiency in usage is likely to be small and, to the extent
15 that demand is relatively inelastic, the effects are even smaller.

16 **Q. Will the Company’s proposed CTP reduce the Company’s incentive to perform
17 due diligence before acquiring new water systems?**

18 A. No. There is no basis for this speculative argument. Mr. Collins appears to ignore
19 critical aspects of the economics and financing associated with acquiring new water
20 systems. Prior to acquiring a new system, the Company must determine if an
21 expenditure of capital is justified from an economic or strategic perspective and must
22 determine what upgrades or other expenditures might be required to integrate the new
23 system into the Missouri-American system. This requires an adequate due diligence

1 process to obtain critical information necessary for such a determination. Without a
2 proper due diligence process, the Company could be left with uneconomic properties.
3 This is not to say that CTP cannot provide some help to incorporate small systems more
4 easily. This, however, is quite a different issue than if CTP affects the due diligence
5 process as Mr. Collins claims.

6 **Q. The Coalition Cities (McGarry Dir.) would have the Commission move backward**
7 **toward de-consolidating tariffs through either an explicit move back to eight**
8 **districts or through a convoluted transfer payment mechanism. How do you**
9 **respond to the Coalition Cities' proposal to return to eight pricing districts?**

10 **A.** This is wholly unacceptable as a matter of policy as I have outlined above. Further, Mr.
11 McGarry's transfer payment mechanism is unworkable and not fully defined. Ms.
12 Heppenstall will address the rate design issues involved in Mr. McGarry's ill-conceived
13 proposal.

14 **V. PROPOSED REVENUE STABILIZATION MECHANISM**

15 **Q. On page 16 of the Staff Report - CCOS, Staff identifies benefits associated with**
16 **RSMs. Do you agree with Staff's listed benefits?**

17 **A.** I agree that RSMs in general eliminate what Staff labels the "throughput disincentive."
18 In my direct testimony (p. 20), the same concept is referred to as the "throughput
19 incentive," which is that the more water customers use, the more revenue the Company
20 collects and the better its financial performance. The RSM promotes conservation
21 efforts by breaking this link and removing the Company's disincentive to support
22 customer efficiency and conservation. I also agree with Staff's benefit that an RSM
23 will stabilize the Company's revenue stream and potentially lower debt costs. As noted

1 at length in my direct testimony (p. 16, 22), the RSM effectively removes the errors
2 that are inherent in the process of forecasting the test year level of sales by eliminating
3 the significance of changes in volume of water sold due to factors beyond the
4 Company's and the Commission's control. Once the revenue requirement is set, the
5 RSM allows the price to flow up or down as sales volume changes between rate cases.
6 The RSM also stabilizes revenues and rates between base rate cases. With this revenue
7 stability, the Company is able to maintain ongoing investments in its facilities and
8 improvements in operations.

9 **Q. Staff also mentions some criticisms of RSMs in the Staff Report-CCOS. On page**
10 **16 of the Staff Report-CCOS, Staff simply notes that "some of the cons may**
11 **include shifting the risk from the utility to the consumer, increasing rates on those**
12 **consumers who have already undertaken conservation measures on their own,**
13 **and increasing rates on those consumers who cannot lower their consumption."**
14 **Do you agree with Staff's criticisms?**

15 A. No, I do not. Staff notes that it will address the specifics of MAWC's proposal,
16 including any alternatives to the Company's proposal, in Staff's rebuttal testimony, but
17 I will address Staff's initial criticisms here.

18 **Q. Staff alleges that the RSM shifts risk to customers. Do you agree?**

19 A. No. An RSM mitigates risk from weather variability or failure to meet sales forecasts
20 for both the utility and customer. The empirical evidence demonstrates that RSM
21 adjustments are both surcharges for under-collections of revenues for fixed costs and
22 credits for over-collections of revenues. In the credit situation, the utility has foregone
23 the opportunity to collect more revenue than the amount authorized in its last general

1 rate case. While opponents of revenue stabilization mechanisms tend to testify
2 extensively about the risk reduction associated with the possibility of surcharges to
3 adjust for under-collection of revenues, acknowledgements of lost opportunities
4 associated with possible credits are far more infrequent. In essence, a company is
5 surrendering upside revenue potential associated with weather conditions that result in
6 a higher-than-expected level of sales in exchange for downside protection against the
7 potential that weather conditions will cause lower-than-expected sales.

8 Another element of risk that an RSM could affect is the failure to meet sales forecasts.
9 It is reasonable to assume that the revenue forecast upon which rates are based is the
10 revenue forecast that the Commission believes is most likely to represent the utility's
11 actual revenue. If a utility is consistently failing to meet its revenue forecast – likely
12 because the revenue forecast does not properly account for water efficiency gains and
13 conservation – then that is a shortcoming of regulation that needs to be corrected and
14 not an element of risk for which there needs to be a cost of equity adjustment. A RSM
15 would simply provide MAWC with the ability to collect the revenue that the
16 Commission found to be appropriate.

17 **Q. Staff also alleges that the RSM increases rates on those consumers who have**
18 **already undertaken conservation measures on their own, as well as those**
19 **consumers who cannot lower their consumption. Do you agree?**

20 **A.** No. Under the proposed RSM, customers who use less will pay less. They will also
21 pay less when and if a surcharge is applied because the surcharge is volume based.
22 Customers who use less water will pay a lower surcharge. They will also pay less when
23 and if a credit is issued because the credit is a one-time fixed amount. The lower the

1 customer's consumption the higher credit he or she receives as a percentage of their
2 bill. The RSM simply allows for the recovery of Commission-approved revenues.

3 **Q. Staff further states that the main benefit of the "traditional ratemaking model"**
4 **"is the stability of rates that are established by the Commission after a thorough**
5 **review and audit of all of the utilities books and records." Do you agree?**

6 **A. No, as explained by Staff on page 15 of the Staff Report – CCOS:**

7 The role of the Missouri Commission is to set just and
8 reasonable rates for public utilities. Just and reasonable rates are
9 those rates that are "fair to both the utility and its customers."
10 Setting such rates is accomplished by balancing the interests of
11 all stakeholders, which include the utility, consumers, and any
12 intervenors. The Commission must set rates that allow a utility
13 to cover its cost of service, including a reasonable opportunity
14 to earn a profit upon its investments.

15 This balancing of interests is the main benefit of traditional ratemaking, and is not lost
16 with the RSM. As I explain in my direct testimony (p. 25-26), the RSM aligns the
17 interests of Missouri-American, its customers, and the state of Missouri.

18 **VI. FIXED CHARGES**

19 **Q. Do any parties support the Company's proposed increase to the fixed customer**
20 **charge for customers billed quarterly?**

21 **A. No. Two parties addressed the Company's fixed charge. Staff recommended that the**
22 **Company maintain its current fixed customer charge. Similarly, DE witness Hyman**
23 **also testified that the fixed customer charges should not go up.**

24 **Q. What was the basis for their recommendations?**

25 **A. Staff did not provide any reasoning. DE witness Hyman (p. 7-9) argued that the**
26 **Company should not be allowed to recover service capacity and minimum consumption**

1 in its customer charge because: 1) reliance on volumetric charges creates equity; 2)
2 high fixed charges are an affordability challenge; and, 3) it would discourage
3 conservation. Mr. Hyman also argued (p. 9) that an increase in fixed charges could
4 result in rate shock, particularly for low income customers, since the Company's last
5 increases were less than two years old.

6 **Q. Do you agree with DE witness Hyman's position?**

7 A. No. Mr. Hyman appears to misinterpret the Company's rate design proposal for fixed
8 charges. In the Company's proposed rate design, the Company voluntarily lowered the
9 monthly 5/8-inch customer charge to \$10.00 and set its quarterly charge equal to
10 \$30.00, or three times the proposed monthly customer charge. This rate design would
11 increase the quarterly customer's monthly customer charge by \$2.55 (\$10.00 minus
12 \$7.45), mitigating the increase in customer charge for these customers as they are
13 moved from quarterly billing to monthly billing in between rate cases. The Company's
14 proposal to lower the monthly customer charge to \$10.00 for customers billed monthly
15 is specifically contingent upon its proposal to move quarterly billed customers to
16 monthly billing. If for any reason the Company is not permitted to move from quarterly
17 to monthly billing, then it proposes to maintain the customer charges at current levels.

18 **VII. LEAD SERVICE LINE REPLACEMENT COST ALLOCATION**

19 **Q. Do MIEC witness Collins and OPC witness Marke raise concern regarding the**
20 **allocation of LSLR program costs?**

21 A. Yes. In his direct testimony (p. 11, ln. 4-5), Mr. Collins states that "[b]ecause these
22 costs are associated with residential service lines, these costs should be allocated to the
23 residential customer class and recovered in residential class rates." OPC witness Marke

1 also expresses a concern regarding having the cost of replacing individual lead service
2 lines allocated across all rate classes (Marke Dir., p. 15, ln. 7-9).

3 **Q. How do you respond to MIEC witness Collins and OPC witness Marke?**

4 A. As I explain in my revenue requirement rebuttal testimony, the Company is proposing
5 to record LSLR costs in Uniform System of Accounts (“USOA”) account 345 –
6 Services as restoration costs. Restoration costs are normally capitalized to plant as
7 part of overall project costs and LSLRs should be treated no differently. As such,
8 they should be recorded in the same manner as all restoration costs and be allocated
9 across customer classes in the manner described by Company witness Heppenstall in
10 her rate design rebuttal testimony.

11 **Q. Does OPC witness Marke raise other issues regarding the Company’s LSLR
12 program?**

13 A. Yes. OPC witness Marke raises a concern regarding the total cost of the Company’s
14 LSLR program; alleges that the LSLR program, in combination with single-tariff
15 pricing will “essentially lead to a complete privatization of water service in Missouri”;
16 and, asserts that “there is no plan to reopen previous main excavations to account for
17 individual lead service lines that were previously passed over.” (Marke Dir., p. 14-16)

18 **Q. How does MAWC respond to OPC witness Marke?**

19 A. As to total LSLR program cost, Company witness Aiton addresses this issue in his
20 testimony in the LSLR AAO proceeding (WU-2017-0296), which is attached to his
21 revenue requirement rebuttal testimony as Schedules BWA-1, BWA-2 and BWA-3.
22 OPC witness Marke’s conclusory statement regarding privatization is nonsensical. It
23 is hard to understand how an investment made for safety reasons - to mitigate the

1 potential increased risk of lead contamination following physical disturbances related
2 to infrastructure work in the area – leads to the complete privatization of water services
3 in the state of Missouri. Finally, Company witness Aiton will address the Company’s
4 LSLR program, including its scope, in his surrebuttal testimony in this case.

5 **Q. Does this conclude your rate design rebuttal testimony?**

6 **A. Yes, it does.**