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Case No.:	WR-2017-0285 SR-2017-0286
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MISSOURI PUBLIC SERVICE COMMISSION

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

REBUTTAL TESTIMONY
REVENUE REQUIREMENT

OF

BRIAN W. LAGRAND

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

Exhibit No. 23
Date 3/9/18 Reporter MM
File No. WR-2017-0285

Exhibit 23
WR-2017-0285
Rebuttal Testimony – Revenue
Requirement of Brian W. LaGrand

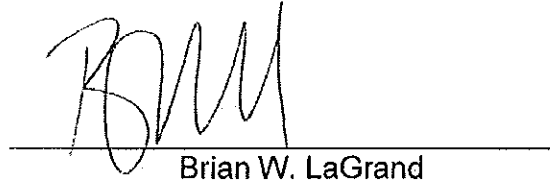
BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

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

AFFIDAVIT OF BRIAN W. LAGRAND

Brian W. LaGrand, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Rebuttal Testimony Revenue Requirement of Brian W. LaGrand"; 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.



Brian W. LaGrand

State of Missouri
County of St. Louis
SUBSCRIBED and sworn to
Before me this 12th **day of** January **2018.**

Notary Public

My commission expires:

MARY BETH HERCULES
Notary Public - Notary Seal
STATE OF MISSOURI
St. Louis County
My Commission Expires April 26, 2020
Commission # 96546828

REBUTTAL TESTIMONY
REVENUE REQUIREMENT
BRIAN W. LAGRAND
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WR-2017-0285
CASE NO. SR-2017-0286

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REBUTTAL TESTIMONY
REVENUE REQUIREMENT

BRIAN W. LAGRAND

I. INTRODUCTION

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

2 A. My name is Brian W. LaGrand, and my business address is 727 Craig Road, St. Louis,
3 Missouri 63141.

4 **Q. Are you the same Brian W. LaGrand who previously submitted direct testimony**
5 **in this proceeding?**

6 A. Yes.

7 ## II. OVERVIEW

8 **Q. What is the purpose of your revenue requirement rebuttal testimony in this**
9 **proceeding?**

10 A. The purpose of my revenue requirement rebuttal testimony is to respond to the Staff
11 Report on Cost of Service filed by the Missouri Public Service Commission
12 ("Commission") Staff ("Staff"), and to the direct testimony of the Office of Public
13 Counsel ("OPC") and other intervenors on the following topics: 1) Revenue
14 Requirement, 2) Present Rate Revenues, 3) Rate Base, 4) Depreciation Expense, 5)
15 Amortization Expense, and 6) Rate Case Expense

16 ## III. REVENUE REQUIREMENT

17 **Q. Did Staff propose a revenue requirement in the Staff Report filed on November**
18 **30, 2017?**

1 A. Yes. Using Staff's mid-point after-tax return of 6.86%, Staff calculated an additional
2 revenue requirement of $1,577,332. Additionally, Staff included $17,147,016 for an
3 estimate of items that will be included in the true up.

4 **Q. How does Staff's revenue deficiency compare to the deficiency calculated by the**
5 **Company and filed in direct testimony?**

6 A. The Company requested additional revenues of $89,405,258, which results in a
7 difference of $87,827,926. When Staff's true up estimate is included, the gap shrinks
8 to $70,688,381. In either case, there are significant differences between the Company's
9 position and Staff's position.

10 **Q. Is the Company's request for a future test year the biggest reason for the**
11 **difference?**

12 A. No, not at all. That's a common misperception. The future test year request in this
13 case accounts for less than 30% of the requested increase. The vast majority of the
14 requested increase would still exist under the methodology utilized in prior rate cases.
15 For example, as I will explain in greater detail later in my testimony, nearly all of the
16 difference in present rate revenues is independent of the future test year.

17 **Q. What are the main drivers of the differences between the Company and Staff?**

18 A. Table BWL-1 shows the main categories of differences as well as the split between the
19 traditional true up period and the Company's proposed future test year.

Table BWL-1

	True-Up	Future Test Yr	Total
Company Request	64,229,238	25,176,020	89,405,258
Cost of Capital & Structure	(26,493,986)	(1,853,948)	(28,347,934)
Revenues	(14,922,624)	(1,785,203)	(16,707,827)
Operating Expense	(6,398,523)	(14,190,037)	(20,588,560)
Rate Base	2,568,287	(7,346,832)	(4,778,544)
Total Differences	**(45,246,846)**	**(25,176,020)**	**(70,422,866)**
Staff Recommendation	**18,982,392**	**0**	**18,982,392**

1 *Note: Staff Recommendation is slightly increased in an updated EMS run after the initial filing*

2 **Q. Will the Company be addressing these differences in rebuttal testimony?**

3 A. Yes. The largest difference is in the cost of capital and capital structure. MAWC
4 witness Ann Buckley will be discussing cost of capital, and addressing Staff witness
5 Jeffrey Smith's recommended 9.25% return on equity and Office of the Public Counsel
6 ("OPC") and Missouri Industrial Energy Consumers ("MIEC") witness Michael
7 Gorman's recommended 9.00% return on equity. MAWC witness Scott Rungren will
8 be discussing the capital structure and addressing Staff's recommendation that the
9 Company use the consolidated capital structure of American Water rather than the
10 Company's stand-alone capital structure. MAWC witness Nikole Bowen will be
11 addressing most of the operating expense issues. MAWC witness Greg Roach and I
12 will be discussing revenues. Mr. Roach will address declining customer base usage,
13 and I will discuss present rate revenues. The last category of differences is rate base,
14 which I will address along with depreciation expense.

15 **Q. In light of the recent change in the Federal tax rates, is the Company proposing**
16 **any changes to their rate request?**

17 A. Yes. As detailed in the rebuttal testimony of Company witness John Wilde, the
18 Company is proposing several changes to reflect many of the impacts of the Tax Cuts
19 and Jobs Act of 2017 in association with the Commission granting the Company's

1 request for a future test year. First, the Company will provide to customers the entire
2 benefit of the reduction in the Federal corporate tax rate from 35% to 21%. Second,
3 the Company has reflected the best current estimate of the changes in Accumulated
4 Deferred Income Taxes to account for the changes that impact investment during the
5 rate case period. This includes the elimination of bonus depreciation, taxability of
6 Contributions in Aid of Construction and revaluing the incremental book-tax
7 depreciation difference using a 21% Federal tax rate. Because these tax changes are
8 complicated and difficult to ascertain with precision at this time, the Company is
9 proposing two separate AAO mechanisms to address these tax benefits. Please see the
10 rebuttal testimony of MAWC witness James Jenkins for more details.

11 **Q. What is the impact of that proposal on the revenue requirement and the requested**
12 **increase in this case?**
13 A. The impact on the requested rate increase in this case, in conjunction with the future
14 test year, is a reduction from $89,405,258 to $69,095,805. This is a reduction of
15 $20,309,453. Again, please see the rebuttal testimony of MAWC witness John Wilde
16 for more details.

17 **Q. Will the Company be providing true up data in this case?**
18 A. Yes. The Company will submit true up data by January 31, 2018.

19 **Q. Does the Company agree with the list of true up items Staff provides on pages 11**
20 **and 12 of the Staff Report – Cost of Service?**
21 A. Yes, with a few additions that have been previously discussed. The Company will also
22 provide true up information on main break expense, Rate J normalization, and customer
23 usage through December 2017.

1

IV. PRESENT RATE REVENUES

3 **Q. What level of present rate revenues did Staff calculate?**

4 A. Staff calculated present rate revenues of $296,650,341, including both water and

5 sewer revenues.[1]

6 **Q. How does this compare to the Company's calculation?**

7 A. In Company Accounting Schedule ("CAS") 8, provided with my direct testimony, the

8 Company calculated present rate revenue of $279,843,403.

9 **Q. Is that calculation still accurate?**

10 A. The Company's calculation is actually slightly overstated. Due to a minor calculation

11 error, present rate revenues were overstated by $155,355. The corrected amount would

12 be $279,688,048.

13 **Q. What is the difference between the Company's calculation and Staff's calculation?**

14 A. Based on the company's original filing, the difference is $16,806,938:

[1] Staff Accounting Schedule 9, Total Company, Line REV-10

Table BWL-2

	MAWC	Staff	Difference
Residential	$177,161,196	$192,526,737	$15,365,541
Commercial	52,430,126	54,445,267	2,015,141
Industrial	16,101,627	16,080,967	(20,660)
Other Public Authority	5,410,391	5,501,902	91,511
Sale for Resale	10,435,866	10,755,323	319,457
Private Fire	5,000,939	4,909,780	(91,159)
Miscellaneous Revenue	359,698		(359,698)
Other Revenues	3,420,163	3,695,695	275,532
Total Water Revenues	**$270,320,006**	**$287,915,671**	**$17,595,665**
Total Sewer Revenues	9,523,397	8,734,670	(788,727)
Total Present Rate Revenue	**$279,843,403**	**$296,650,341**	**$16,806,938**

1

2 **Q. This difference is substantial. What are the main drivers?**

3 A. As you can see, the most substantial difference is in the residential water revenues.
4 This is primarily driven by customer usage assumptions. Additional differences
5 include customer counts, and a calculation issue with Staff's residential usage in St.
6 Joseph and Parkville. I will describe and comment on those below.

7 **Q. Is the Company's proposal for a future test year a significant contributor to this**
8 **difference?**

9 A. No, it is not. The net impact in the future test year is $1,785,203, or a little over 10%
10 of the total revenue difference. Additional declining residential usage through the
11 midpoint of the future test year contributes $1,706,756 of the difference. Differences
12 in meter charges and fees increase the difference by $183,949, while price adjustments
13 to sale for resale contracts and other sewer items reduce the difference by $105,502.

14 **Q. Are there other areas of concern in Staff's calculation of present rate revenues?**

15 A. Yes. I will explain in detail Staff assumptions the Company disagrees with, specifically
16 related to the levels of Rate J usage and the methodology for calculating the customer

1 charges. Additionally, the Company included the impact of losing a large water district
2 as a customer, which Staff did not include in their calculations.

3 **a. RESIDENTIAL REVENUES**

4 **Q. Please describe Staff's approach to calculating residential present rate water**
5 **revenues.**

6 A. For all residential customers, Staff calculated a simple five-year (60-month) average of
7 daily usage per customer through June 30, 2017, with recently acquired systems having
8 shorter periods based on the available data[2]. That per customer usage was then applied
9 to the annualized meter count as of June 30, 2017, using the Company's currently
10 approved tariffs to determine total volumetric residential revenues. The same meter
11 count was used to calculate the fixed residential revenues, also using the currently
12 approved tariffs[3].

13 **Q. How does this compare to the Company's approach to projecting present rate**
14 **residential water revenues?**

15 A. As I described in my direct testimony[4], the Company began with average customers for
16 2016, and added customers through organic growth, as well as the Wardsville and
17 Pevely Farms acquisitions. To determine usage, we divide residential consumption
18 into two components: base usage and non-base usage. Base usage is average billed
19 usage for February, March and April, annualized for twelve months, while non-base
20 usage is the actual usage above base usage. A declining trend is applied to base usage,
21 based on a 10 year trend of residential base usage from 2007 through 2016. For non-

[2] Staff Report - Cost of Service, page 59
[3] Staff Report - Cost of Service, page 60
[4] LaGrand Dir, pages 16-17

1 base usage the Company used a 10 year average. This usage projection per customer
2 is applied to the number of customers to determine total usage. Company witness Greg
3 Roach will be addressing declining usage in his rebuttal testimony.

4 **Q. Does the Company agree with Staff's methodology or projected usage levels?**
5 A. No, we do not. Staff's methodology is flawed because using a simple 60-month
6 average fails to account for the declining trend in base usage. Staff provides limited
7 rationale for this methodology beyond saying that usage patterns have changed for
8 various reasons. Again, Company witness Greg Roach addresses this question in
9 greater detail in his rebuttal testimony.

10 **Q. What is the overall impact of the difference in residential customer usage**
11 **assumptions?**
12 A. As shown in Table BWL-3, the vast majority of the difference is in District 1. Staff's
13 usage per customer is almost 8,000 gallons per year higher. That is more than one
14 entire month of typical usage for that district. Staff's approach would essentially result
15 in the Company receiving revenue on 13 (not 12) months of usage each year.

Table BWL-3

	Customers	Annual Usage (000 gallons) per Customer	Total	Annual Revenue
MAWC Assumptions				
District 1	360,331	74.1	26,709,011	$110,573,479
District 2	34,608	51.1	1,769,886	8,385,367
District 3	34,272	48.1	1,648,022	6,167,559
Total	**429,212**	**70.2**	**30,126,919**	**$125,126,405**
Staff Assumptions				
District 1	359,659	81.9	29,472,930	$122,014,557
District 2	34,506	74.4	2,566,581	12,159,948
District 3	33,994	52.7	1,792,741	6,709,154
Total	**428,159**	**79.0**	**33,832,252**	**$140,883,659**
Differences				
District 1	(672)	7.9	2,763,919	$11,441,079
District 2	(102)	23.2	796,695	3,774,581
District 3	(278)	4.7	144,719	541,595
Total	**(1,053)**	**8.8**	**3,705,333**	**$15,757,255**

1 *Note: Staff number for District 2 includes incorrect usage for St. Joseph and Parkville*

2 **Q. Are there any corrections to the projections the Company thinks Staff should**
3 **make?**

4 A. Yes, there are a few. The Company has discussed these with Staff and our
5 understanding is that these corrections will be made. First, there was an inadvertent
6 calculation error in the average daily usage amount for St. Joseph and for Parkville.
7 For St. Joseph, six additional months of usage were included when calculating annual
8 usage per customer, resulting in the daily usage being overstated. Staff used 0.2022
9 for average daily usage, while the correct amount under Staff's methodology should be
10 0.1437. This difference overstates present rate revenue by $2,877,288. Additionally,
11 there was a minor error in the Parkville usage calculation. For the March average use
12 per customer in every year of Staff's five year average, the calculation uses the March
13 customers, but applies the April usage. This overstates present rate revenues by
14 $11,379. Second, when calculating the average daily revenue, Staff divided the annual
15 amount by 365 days. However, when converting the daily usage back to annual usage

1 to calculate the annual revenue, Staff multiplied by 365.25 days[5]. As long as the same
2 days are used in both cases, the results will be the same, but this difference overstates
3 present rate revenues by $96,430.

4 **Q. Are there any other concerns with Staff's calculation of present rate volumetric**
5 **residential revenues?**

6 A. Yes. The Company's data that Staff utilizes to produce their usage assumption is based
7 on the number of customers. The workpapers provided to Staff at the beginning of this
8 case include the number of customers and their usage history over the past 10 years.
9 From this data, Staff calculated average daily usage per customer over a five year
10 period. When incorporating data provided as part of the June 30, 2017 update, Staff
11 used the number of meters rather than the number of customers. The end result is that
12 for a 60 month period, the first 54 months would be based on customer count, and the
13 last 6 months on meter count. While the Company strongly disagrees with Staff's
14 methodology for determining residential usage, we recommend that Staff use the
15 customer count for all periods in their calculations for consistency purposes.

16 **Q. Did other parties file testimony about residential customer usage?**

17 A. Yes, OPC witness Lena Mantle provided testimony on usage. Company witness Roach
18 is addressing the issues raised in her testimony.

19 **Q. Given the significance of the residential usage assumptions, what do you**
20 **recommend to the Commission?**

[5] Staff Report - Cost of Service, page 60

1 A. I recommend the Commission adopt the Company's usage projections, which are based
2 on robust statistical analysis, and reject Staff's proposed five year average.

3 **Q. If the Commission were to adopt a five year average for residential customers, do**
4 **you have any recommendations regarding the appropriate time period for the**
5 **average?**

6 A. In the event the Commission orders a five year average, the average should be included
7 in the true-up and taken over the five year period ending with December 2017. This
8 is the most recent period used and will capture the most recent effect of declining use
9 per customer. Nevertheless, the Company believes that Mr. Roach's calculations are
10 far more accurate and based on actual data and nationally recognized trends.

11 **Q. What issues does the Company have with Staff's calculation of present rate fixed**
12 **residential revenues?**

13 A. To determine the fixed, or customer, charge, Staff annualized the meter count as of
14 June 30, 2017[6]. The Company disagrees with this approach because it will overstate
15 the annual revenues. The Company will have more active meters in June than in
16 December. This is due to people turning on service to vacation homes, utilizing
17 irrigation meters, etc. An improvement to Staff's approach would be to use a 12 month
18 average of the meter count to determine the fixed revenue. Annualizing the June 2017
19 meter count rather than using a 12 month average overstates the residential fixed
20 charges by $137,568.

21 **Q. Is that the only issue the Company has with fixed charge revenues?**

---

[6] Staff Cost of Service Report, page 60

1 A. No. One additional issue Staff did not consider is that District 1 has pro-rated meter
2 charges for customers that are only active for part of a quarter. Staff assumes all meters
3 are fully active for an entire quarter, which is inaccurate, and will overstate present rate
4 revenues. For 2017, there were 69,698 pro-rated residential bills sent out. Since the
5 pro-rated meter charge is less than the regular charge, these bills resulted in $467,774
6 less revenue than if they had been regular bills, and will overstate present rate revenue
7 by that same amount.

8 **Q. Are there any other residential revenue issues to address?**

9 A. Yes. The Company currently has a low-income pilot program for customers in St.
10 Joseph, Parkville and Brunswick. This program provides an 80% discount on the fixed
11 charge for qualifying customers. In this case, the Company has proposed making this
12 program open to all customers. In calculating the present rate revenues, Staff included
13 neither the pilot program nor the proposed expanded statewide program.

14 **b. <u>NON-RESIDENTIAL REVENUES</u>**

15 **Q. What is the overall impact of the difference in non-residential customer usage**
16 **assumptions?**

17 A. The non-residential usage assumptions for Staff and the Company are much closer than
18 for residential customers. However, Staff's assumptions result in present rate revenue
19 that is $1,614,175 higher than the Company assumptions. See the Table BWL-4 below
20 for the details of the differences.

Table BWL-4

	Annual Usage (000 gallons)						Annual
	Rate A	Rate B	Rate J	Rate F	Special	Total Usage	Revenue
MAWC Assumptions							
District 1	9,120,150	1,645,391	4,537,046	43,394	2,250,638	17,596,619	$51,012,084
District 2	1,225,757	843,338	1,382,047	220	759,260	4,210,623	13,164,114
District 3	1,375,720	355,196	951,839	46	505,795	3,188,596	9,402,199
Total	**11,721,627**	**2,843,924**	**6,870,933**	**43,660**	**3,515,693**	**24,995,838**	**$73,578,397**
Staff Assumptions							
District 1	9,699,206	1,705,689	3,860,805	46,750	2,361,404	17,673,855	$52,429,876
District 2	1,425,706	854,833	1,109,519	218	753,226	4,143,501	13,273,626
District 3	1,511,745	372,702	752,080	168	502,199	3,138,895	9,489,070
Total	**12,636,658**	**2,933,224**	**5,722,404**	**47,136**	**3,616,829**	**24,956,251**	**$75,192,572**
Differences							
District 1	579,056	60,298	(676,241)	3,356	110,766	77,236	$1,417,792
District 2	199,949	11,495	(272,529)	(2)	(6,035)	(67,121)	109,512
District 3	136,025	17,506	(199,759)	122	(3,596)	(49,701)	86,871
Total	**915,031**	**89,300**	**(1,148,528)**	**3,476**	**101,136**	**(39,587)**	**$1,614,175**

Q. Please describe Staff's approach to calculating non-residential present rate water revenues.

A. As with residential usage, Staff used a simple 60 month average of non-residential usage, and annualized the meter count as of June 30, 2017 to determine the customer charges for commercial, industrial, other public authority, and sale for resale customers. For two of the Company's special contracts[7], and for private fire service[8], on the other hand, Staff used 12 months of usage through June 30, 2017. Using a 12 month average, rather than 60 month average to calculate volume overstates present rate revenue by $88,592 for the special contracts, and by $17,855 for private fire service.

Q. How does this compare with the Company's methodology?

[7] Staff Cost of Service Report, page 61

[8] Staff Cost of Service Report, page 62

1 A. The Company used the 2016 actual usage for non-residential customers since usage
2 levels for non-residential customers do not vary in the same way as residential usage.
3 The Company used actual billing determinants to set the level of customer charges.

4 **Q. Given the difference in total usage for non-residential customers is very similar,**
5 **does the Company have any major concerns about Staff's methodology?**
6 A. Yes. The most significant issue is with Rate J normalization. Large water users can
7 qualify for the Rate J tariff, which is currently approved and in place. The tariffed
8 volumetric rate is substantially lower than Rate A, so having too much or too little
9 usage moving from Rate A to Rate J can have a material impact on the present rate
10 revenues.

11 **Q. Can you explain how Staff determined how much non-residential usage is Rate**
12 **A and how much is Rate J?**
13 A. Staff calculated the 12 months of usage ending June 30, 2017 for each non-residential
14 class, and calculated the percentage of that usage that is on the Rate J tariff. Staff
15 then applied that same percentage to the 5 year average usage to split the usage into
16 Rate A and Rate J[9].

17 **Q. Are there differences in the Rate J usage Staff and the Company are using?**
18 A. Yes. As seen in table BWL-4 and shown below in table BWL-5, Staff has included
19 1,148,528 thousand gallons of usage at Rate A in their calculation of present rate
20 revenues, while the Company included that usage as Rate J. In calculating the
21 amount of Rate J usage in the 12 months ending June 30, 2017, Staff didn't fully

[9] Staff Cost of Service Report, page 60-61

1 normalize the Rate J customers who moved to that rate during the 12 month period.
2 Only the usage occurring after the customers moved to Rate J was included. The
3 balance of the usage for those customers during the year was included as Rate A.
4 This understates the amount of Rate J usage, overstates the amount of Rate A usage,
5 and thus, overstates present rate revenues in this case by $2,364,353.

Table BWL-5

	Rate J Volume (000 gallons)			
	District 1	District 2	District 3	Total
MAWC Normalized Rate J				
Commercial	578,834	74,955	113,216	767,005
Industrial	3,958,212	1,235,858	827,210	6,021,280
OPA	0	71,234	11,413	82,647
Total	**4,537,046**	**1,382,047**	**951,839**	**6,870,932**
Staff Rate J Allocation				
Commercial	57,376	46,432	66,700	170,509
Industrial	3,803,429	996,949	596,434	5,396,813
OPA	0	66,137	88,946	155,083
Total	**3,860,805**	**1,109,519**	**752,080**	**5,722,404**
Difference				
Commercial	(521,458)	(28,523)	(46,516)	(596,496)
Industrial	(154,782)	(238,909)	(230,776)	(624,467)
OPA	0	(5,097)	77,533	72,436
Total	**(676,241)**	**(272,529)**	**(199,759)**	**(1,148,528)**

6

7 The Company has discussed this matter with Staff and Staff has agreed to look into
8 the matter. The Company's calculation of fully normalized level of Rate J volumes
9 as of June 30, 2017, are presented in Table BWL-6.

Table BWL-6

	Rate J Volume (000 gallons)			
	District 1	District 2	District 3	Total
MAWC Normalized Rate J				
Commercial	704,350	127,349	179,494	1,011,194
Industrial	4,125,809	1,272,376	909,563	6,307,749
OPA	0	79,577	76,029	155,607
Total	**4,830,159**	**1,479,303**	**1,165,087**	**7,474,549**
Staff Rate J Allocation				
Commercial	709,509	125,714	178,557	1,013,780
Industrial	3,833,378	1,222,873	803,410	5,859,661
OPA	0	81,435	77,923	159,359
Total	**4,542,886**	**1,430,023**	**1,059,890**	**7,032,799**
Difference				
Commercial	5,159	(1,635)	(938)	2,586
Industrial	(292,432)	(49,503)	(106,153)	(448,088)
OPA	0	1,858	1,894	3,752
Total	**(287,273)**	**(49,280)**	**(105,197)**	**(441,750)**

1

2 **Q. Is Staff's partial normalization the only issue with Staff's calculation of Rate J**
3 **revenues?**

4 A. No. While the Company appreciates Staff's willingness to reevaluate its initial
5 calculation, the Company is still left with a substantial shortfall. As is shown in Table
6 BWL-6, even at the updated volumes, the Company still has nearly half a billion
7 gallons of Rate J volume that is considered Rate A when calculating present rate
8 revenues. Staff's allocation of Rate J to the five-year average non-residential volume
9 creates this shortfall. When comparing the non-residential usage during the 12 months
10 ended June 30, 2017 to the five-year average ending June 30, 2017, the five-year
11 average is lower by 416,228 thousand gallons. However, the Rate J usage is reduced
12 by 441,750 thousand gallons. So even though Rate J is approximately 40% of the total
13 volume, over 106% of the gap that occurs when using a five-year average falls fully on
14 Rate J. Staff's methodology of allocating rate J volumes based on historical averages

1 is flawed as the changes in the relative shares of volumes between customer classes
2 over time can result in an outcome as we see above.

3 **Q. What is the impact to this shortfall on present rate revenues?**

4 A. Essentially the 441,750 thousand gallon shortfall is considered Rate A usage in the
5 present rate revenue calculations, despite the fact the Company will actually receive
6 Rate J revenues on that volume. The total impact of this shortfall is to overstate present
7 rate revenues by $927,506.

8 **Q. Are there alternatives that the Company would suggest the Commission should**
9 **consider?**

10 A. Yes, there are two alternatives that would alleviate the shortfall. First, using the last 12
11 months of non-residential revenues would solve the Rate J allocation problem.
12 Alternatively, if a 5 year average is to be used, the Commission should subtract the
13 normalized level of current Rate J usage from the 5 year average total to determine the
14 Rate A usage.

15 **Q. What issues does the Company have with Staff's calculation of present rate fixed**
16 **revenues for non-residential customers?**

17 A. To determine the fixed, or customer, charge Staff annualized the total meter count for
18 each customer class as of June 30, 2017. The Company disagrees with this approach
19 because using the total meter count will overstate the annual revenues. There are a
20 number of non-residential meters for which the Company does not collect a customer
21 charge. For example, the sale for resale special contract customers will have several
22 large meters. However, the contracts do not include a charge on those meters. Other
23 examples include backflow meters, battery meters and check meters. By including the

1 meters that do not generate a customer charge, present rate revenues are overstated by
2 $171,024, as shown in Table BWL-7. The Company has discussed this issue with Staff
3 and will be providing clarifying information as part of the true-up information that will
4 be provided by January 31, 2018.

Table BWL-7

	Non Residential Meter Counts				
	Commercial	Industrial	OPA	SFR	Totals
Total Meters					
District 1	19,425	192	1,285	27	20,929
District 2	3,294	164	307	27	3,792
District 3	3,840	101	327	9	4,277
Total	**26,559**	**457**	**1,919**	**63**	**28,998**
Remove Non-Rent Meters					
District 1	19,359	190	1,262	6	20,817
District 2	3,191	129	270	27	3,617
District 3	3,741	101	311	9	4,162
Total	**26,291**	**420**	**1,843**	**42**	**28,596**
Differences					
District 1	(66)	(2)	(23)	(21)	(112)
District 2	(103)	(35)	(37)	0	(175)
District 3	(99)	0	(16)	0	(115)
Total	**(268)**	**(37)**	**(76)**	**(21)**	**(402)**
Revenue Impact	**$51,672**	**$7,366**	**$15,267**	**$96,720**	**$171,024**

5

6 **Q. Is that the only issue the Company has with fixed charge revenues?**

7 A. No. As with residential customer charges, Staff annualized the meters as of June 30,
8 2017. Using a 12 month average of meters during the year will provide a more accurate
9 estimate of the meters. As shown in table BWL-8, annualizing the meters as of June
10 30, 2017, overstates present rate revenue by $83,133. As mentioned previously in my
11 discussion of residential revenues, Staff did not consider that District 1 has pro-rated
12 meter charges for customers that are only active for part of a quarter. Staff assumes all
13 meters are fully active for an entire quarter, which is inaccurate, and will overstate
14 present rate revenues. Failing to consider pro-rated meter charges when establishing
15 present rate revenues overstates the non-residential fixed revenues by $58,774.

Table BWL-8

Non Residential Meter Counts					
	Commercial	Industrial	OPA	SFR	Totals
Annualized Meters - June 2017					
District 1	19,359	190	1,262	6	20,817
District 2	3,191	129	270	27	3,617
District 3	3,741	101	311	9	4,162
Total	**26,291**	**420**	**1,843**	**42**	**28,596**
12M Average of Meters - June 2017					
District 1	19,331	194	1,251	7	20,782
District 2	3,193	131	258	27	3,608
District 3	3,721	108	312	9	4,151
Total	**26,245**	**432**	**1,821**	**43**	**28,541**
Differences					
District 1	(28)	4	(11)	1	(35)
District 2	2	2	(12)	0	(9)
District 3	(20)	7	1	0	(11)
Total	**(46)**	**12**	**(22)**	**1**	**(55)**
Revenue Impact	**$81,039**	**($7,809)**	**$11,017**	**($1,114)**	**$83,133**

1

2 **Q. Does the Company have any other issues related to non-residential revenues?**

3 A. Yes. In my direct testimony, I discussed an adjustment the Company made to reflect
4 the impact of Water District #2 in Audrain County's plan to stop purchasing water from
5 the Company[10]. Continuing to include this customer overstates present rate revenues
6 by $115,633. Staff did not address this adjustment in its direct testimony.

7 **c. SEWER REVENUES**

8 **Q. What are the overall differences between Staff and the Company calculations of**
9 **sewer present rate revenues?**

10 A. As shown in Table BWL-1, the Company calculated present rate sewer revenues of
11 $9,523,397, which is $788,727 higher than Staff's calculation of $8,734,670[11].

12 **Q. What are the main drivers of the differences?**

[10] LaGrand Dir., page 15-16
[11] Staff Accounting Schedule 9, Total Sewer

1 A. The calculation of present rate revenues on the Arnold sewer system are responsible for $749,279 of the difference. Staff has calculated present rate sewer revenues much lower than the Company, and in fact lower than the revenues the Company is currently collecting from Arnold customers. Staff annualized the number of customers as of June 30, 2017. The sewer customer charges are applied based on the number of "units", rather than customers. For example, an apartment building with 20 apartments could be one customer, but would be billed for 20 units. Therefore using customers will understate the present rate revenues. The Company has discussed this with Staff and is providing clarifying information. Additionally, Staff's two year average assumption for commercial usage through June 30, 2017 creates an additional difference of $105,430. Since the Staff's two year average begins just as the Company took ownership of the Arnold system, Staff should consider a two year average updated through December 31, 2017 to reflect a normalized level of customer usage.

14 **Q. What is the impact of Staff calculating present revenues so much lower for the Arnold system?**

16 A. By calculating present rate revenues that are lower than actual revenues in Arnold, Staff will create a revenue deficiency that is artificially high and as a result, the Arnold customers will pay higher rates than are necessary.

19 **d. <u>OTHER REVENUES</u>**

20 **Q. Are there differences between Staff's and the Company's calculation of Miscellaneous and Other Revenues?**

22 A. Yes, but they are relatively minor. The differences are outlined in Table BWL-9.

Table BWL-9

	MAWC	Staff	Difference
Miscellaneous	$359,698	$0	($359,698)
Reconnect Charges	672,717	672,717	(0)
Returned Check Charge	88,272	86,656	(1,616)
Application Fee	1,487,498	1,487,499	1
Miscellaneous Other Revenue	667,020	666,327	(693)
Rents from Water Property	504,657	782,496	277,839
Total Water	**$3,779,862**	**$3,695,695**	**($84,167)**
Returned Check Charge	1,200	1,200	0
Miscellaneous Service	742	742	0
Total Sewer	**$1,941**	**$1,941**	**$0**
Total Misc & Other	**$3,781,803**	**$3,697,636**	**($84,167)**

1

2 **Q. Can you explain how Staff calculated Miscellaneous and Other revenues?**

3 A. Yes. For most categories, Staff calculated a three year average of the miscellaneous

4 items[12], which is similar to the approach taken by the Company. For revenues related

5 to the provision of customer usage data to other entities for billing purposes and for

6 rents, Staff used the most recent 12 months. Lastly, Staff eliminated late fees.

7 **Q. Does the Company agree with Staff's calculations of Miscellaneous and Other**

8 **revenues?**

9 A. Generally, the Company is in agreement. However, I would like to address late fees

10 more broadly.

11 **Q. What is the Company's position on late fees?**

12 A. While some smaller, recently acquired systems have late fees in their tariffs, the vast

13 majority of the Company's customers are not subject to a late fee on any delinquent

14 payments. In my direct testimony[13] and in the tariff sheets filed to initiate this case, the

15 Company proposed instituting a 1.5% late fee, which is in line with the fee currently in

[12] Staff Report – Cost of Service, pages 62-63

[13] LaGrand Dir., page 16

1 place for other large utilities regulated by the Commission. Staff did not address the
2 proposed late fees in its direct testimony.

3 ## V. RATE BASE

4 **Q. What is Staff's recommended rate base?**

5 A. Staff recommends a rate base of $1,145,868,209.[14]

6 **Q. Pease explain how Staff developed its recommended rate base.**

7 A. Staff utilized the Company's updated rate base as of June 30, 2017, of $1,148,125,544,
8 which was provided by the Company as part of the first update in this case. From that
9 starting point, Staff made a variety of adjustments, which I will address in more detail
10 below, resulting in a rate base reduction of $2,215,792.

11 **Q. Did Staff, or any other intervenors, address the Company's 13-month average**
12 **rate base included in the future test year?**

13 A. No, they did not. While Staff witness Mark Oligschlaeger addressed the future test
14 year concept as a theory[15], Staff only made adjustments to the Company's June 30,
15 2017 rate base amount and ignored the future test year rate base as filed in the
16 Company's direct case.

17 ### a. NET UTILITY PLANT IN SERVICE

18 **Q. Please explain what adjustments Staff made to Utility Plant in Service and to**
19 **Accumulated Depreciation Reserve.**

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[14] Staff Accounting Schedule 2, Total Company
[15] Staff Report – Cost of Service, pages 3-11

1 A. Staff made two adjustments that impacted Net Utility Plant in Service. First, an
2 adjustment was made to reduce the net plant related to the recent acquisition of the
3 Wardsville Water and Sewer System (WA-2017-0181 and WA-2017-0182). Staff
4 removed $1,509,596 from Utility Plant and $547,399 from Accumulated Reserve
5 related to additional utility assets the Company received in the purchase of the
6 Wardsville system beyond what was known at the time of the acquisition case. The
7 second adjustment was to remove $684 from Accumulated Reserve related to
8 depreciation expense in a land account.

9 **Q. Does the Company agree with Staff's adjustments related to the Wardsville**
10 **acquisition?**

11 A. No. After closing the transaction, the Company inventoried additional utility assets
12 and properly reflected those assets as Utility Plant in Service. These assets were not
13 known to the Company at the time of the acquisition case. The Company acknowledges
14 Staff's prior request for information related to these assets and will provide the
15 information to Staff as soon as possible.

16 **Q. Does the Company agree with Staff's adjustment to Accumulated Reserve**
17 **related to land accounts?**

18 A. The Company agrees with Staff's $684 adjustment to Accumulated Reserve.

19 **b. NET CONTRIBUTIONS IN AID OF CONSTRUCTION**

20 **Q. What aspects of Contributions in Aid of Construction ("CIAC") will you**
21 **address?**

1 A. I will address two issues, the CIAC balance Staff adjusted, and Staff's specific
2 adjustments related to previously acquired systems.

3 **Q. Please describe the issues with the Company CIAC balance that Staff adjusted.**
4 A. Staff used the Company response to Staff DR 155, which showed a total CIAC balance
5 of $336,273,702. The balances in DR 155 include CIAC related to construction work
6 in progress. The Company rate base shown in Schedule CAS-3 provided in the June
7 2017 update properly excludes the CIAC related to construction work in progress, and
8 includes CIAC of $334,766,855. Thus, Staff's gross CIAC balance is overstated by
9 $1,506,848. The Company has discussed with Staff, and we both agree that CIAC
10 related to construction work in progress should not be included in rate base.

11 **Q. Please explain any adjustments Staff made to CIAC.**
12 A. Staff made two adjustments to CIAC, both related to previously acquired systems[16].
13 First, Staff increased the CIAC balance by $976,114, and increased Accumulated CIAC
14 Amortization by $582,845, related to the Jaxson Estates Wastewater acquisition (SM-
15 2017-0069). Second, Staff increased the CIAC balance by $108,148, and increased
16 Accumulated CIAC Amortization by $38,495, related to the acquisition of Woodland
17 Manor (WM-2016-0169).

18 **Q. Why did Staff make these adjustments?**
19 A. For Jaxson Estates, Staff claims all of the Jaxson Estates Sewer plant was contributed
20 by a developer[17], and therefore there is no rate base. Staff made offsetting adjustments
21 equal to the Company's Utility Plant in Service and Accumulated Reserve to

[16] Staff Report - Cost of Service, page 49.
[17] Staff Report - Cost of Service, page 49

1 effectively eliminate the Company's rate base. For Woodland Manor, Staff refers to
2 Woodland Manor's PSC Annual Report and adjusts CIAC and Amortization Reserve
3 to reflect the amounts shown by Woodland Manor.

4 **Q. Does the Company agree with the adjustment to Jaxson Estates?**

5 A. No, we do not. The Jaxson Estates sewer system was built in 2007 by Triad
6 Development. The developer contributed the treatment plant to the sewer company at
7 that time. Due to slower than expected development, the sewer plant did not have
8 enough flow to work properly, so the waste was hauled to a third party for treatment.
9 In 2007 the developer entered into a "Capital Recovery Fee Agreement" with the
10 owners of the system at the time. The Capital Recovery Fee Agreement would entitle
11 the developer to recover his costs of the treatment plant by collecting $10 per month,
12 to be placed on the sewer bill, from every customer once 100 homes were developed.
13 That level of development did not occur, and the Capital Recovery Fee was not
14 activated. When the Company acquired Jaxson Estates sewer in 2016, a payment was
15 made to the original developer, who terminated the Capital Recovery Fee Agreement.
16 During the acquisition approval process, Company management had several
17 discussions with Staff about this transaction, including discussions about what would
18 demonstrate that the treatment plant was now used and useful. In the Staff
19 Recommendation to approve the transfer of the assets[18], Staff notes there are rate base
20 questions, but makes no indication that rate base is zero. The Company has solved the
21 issues with the treatment plant, and it is operational today. The investment made by

[18] SM-2017-0069 Staff Recommendation to Approve Transfer of Assets, page 2, paragraph 6

1 the Company, which solved a longstanding problem, should be recognized as rate base,
2 and not additional CIAC as recommended by Staff.

3 **Q. Does the Company agree with the adjustment to Woodland Manor?**
4 A. Yes. The Company included the CIAC in the pro-forma filed with the application in
5 the acquisition case, and inadvertently left out the CIAC when booking the acquisition.

6 **c. PREPAYMENTS**

7 **Q. Please explain the adjustments Staff made for prepayments.**
8 A. Staff included a 13 month average of the prepayments balance through June 30, 2017.
9 This results in a $2,338,274 increase in rate base.

10 **Q. Does the Company agree with Staff's adjustment?**
11 A. Yes, the Company agrees with the adjustment.

12 **d. WORKING CAPITAL**

13 **Q. Please explain Staff's cash working capital recommendation.**
14 A. Staff included $9,088,941 in cash working capital with rate base offsets for taxes of
15 $489,746 and for interest expense of $1,886,448. This results in a total of $6,712,747
16 of cash working capital reflected in rate base.

17 **Q. Did Staff conduct a lead / lag study to determine working capital requirement?**
18 A. No. Staff utilized the analysis performed by the Company and included in the response
19 to Staff DR 0156. However, Staff made several significant adjustments to the
20 Company's analysis.

21 **Q. Please explain Staff's adjustments to the Company's methodology.**

1 A. Staff had adjusted the Company's methodology to use "miscellaneous cash vouchers" to determine the lag on Service Company costs, eliminated check clearing days, eliminated the preferred stock dividends, and calculated two different results, one for St. Louis and one for the rest of the state.

5 **Q. Please explain the adjustment for Service Company expense lag.**

6 A. Staff has rejected the Company's treatment of Service Company costs in the analysis and substituted its "miscellaneous cash vouchers" calculation to calculate the Service Company expense lag. Staff takes issue with the Company paying the Service Company bill in the first half of the month in which services are provided. The actual payment for these services results in an expense lead of 3.26 days. Staff utilizes a positive lag of 56.74 days.[19] Staff believes this practice is contrary to the treatment of payments to other vendors, and is simply done due to the affiliate relationship between MAWC and the Service Company.

14 Q. **Does the Company agree with Staff's approach in calculating the Service Company expense lag?**

16 A. No. The Service Company bills its affiliates in advance for its service. This is recognized in the 3.26 payment lead calculated by the Company. By utilizing a 56.74 expense lag, Staff has made the assumption that the Service Company bills in arrears for the service it provides. It does not. If the Service Company billed in arrears it would have an additional cash working capital requirement and would have to pass the cost of that cash working capital along to MAWC. Because Staff has made no corresponding adjustment to reflect these increased costs if the Service Company were

[19] Staff's Working Capital Workpaper - Newkirk

1 to bill in arrears, Staff has created a "gap" that unfairly and improperly deprives the
2 Company of cash working capital. The Company's recommendation is that the 3.26
3 payment lead, as calculated by the Company is correct.

4 **Q. Does the Company agree with Staff's approach in calculating two different**
5 **expense lags – one for St. Louis and one for the rest of the state?**
6 A. No. That approach is purely hypothetical, arbitrary and is not based on the actual
7 payments reflected on the Company's books. For example, the Service Company does
8 not issue two bills, one for St. Louis and one for everyone else .

9 **Q. Does the Company accept Staff's adjustment to eliminate check clearing days and**
10 **to eliminate the preferred stock dividends?**
11 A. Yes, the Company is willing to accept these adjustments.

12 **e. TANK PAINTING TRACKER**

13 **Q. Please explain the adjustments Staff made to the Tank Painting Tracker.**
14 A. Staff amortized the balance in the tracker that was established in the last rate case,
15 which was $1,382,938, through June 30, 2017. Additionally, Staff has offset the
16 balance in the regulatory asset with the regulatory liability for the "stub period", which
17 was also established in the last rate case. As of June 30, 2017, the net amount Staff
18 includes in rate base is $660,360.

19 **Q. Does the Company agree with Staff's calculation?**
20 A. Yes. This is the identical balance the Company included in the June 30, 2017 update
21 to rate base. The Company agrees with Staff's proposal to begin amortizing the

1 regulatory liability beginning in July 2017 through the original 60 month amortization
2 period.

3 **f. REGULATORY DEFERRALS**

4 **Q. Please explain any adjustments Staff made to regulatory deferrals.**

5 A. Staff did not specifically address regulatory deferrals in direct testimony, but did not
6 include any regulatory deferrals in their rate base calculation.

7 **Q. What regulatory deferrals did the Company include in rate base in this case?**

8 A. There were two items included in rate base in both the initial filing and the June 2017
9 update information. As described in my Direct Testimony, the Company included costs
10 of the pipeline funded by Emerald Pointe, but owned by the city of Hollister, and
11 receivership fees related to the acquisition of Hickory Hills water & sewer.

12 **Q. Please explain the background of the Emerald Pointe pipeline.**

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

18 **Q. Did Emerald Pointe own the entire pipeline?**

19 A. No. As part of their agreement with the City of Hollister, Emerald Point was required
20 to contribute to the City the portion of the pipeline within the Hollister city limits. The
21 construction costs associated with that portion of pipeline were $323,321.

1 **Q. Did the Commission review Emerald Pointe's decision to construct the pipeline to**
2 **Hollister's treatment plant prior to construction?**
3 A. Yes. As part of the certificate case mentioned above (SA-2012-0362) the Commission
4 reviewed the project. In fact, Staff's recommendation[20] in that case concluded the
5 pipeline was reasonable and cost effective. Additional benefits included the
6 elimination of the existing treatment facility, elimination of sewage discharge into
7 Table Rock Lake and having additional capacity available for future customers.

8 **Q. Did the Commission have any other opportunities to address the regulatory**
9 **treatment of the portion of the pipeline in Hollister?**
10 A. Yes. The Company acquired Emerald Pointe water and sewer in 2014 (WO-2014-0113
11 and SO-2014-0116). At the time of the acquisition, Emerald Pointe had just recently
12 completed a rate case (SR-2013-0016 and WR-2013-0017), in which the unamortized
13 cost of the pipeline was given rate base treatment. The Company relied on that rate
14 case outcome when acquiring Emerald Pointe, and in the acquisition case, there was no
15 discussion of anything other than full rate base treatment. In fact, Staff included the
16 unamortized portion as rate base in their recommendation in that case.[21] Rate base
17 treatment is both appropriate and consistent with how it has been treated by the
18 Commission in multiple regulatory proceedings.

19 **Q. Please explain the background of the Hickory Hills water and sewer acquisition.**
20 A. The Hickory Hills Water and Sewer system had long been a troubled system, which
21 had fallen into receivership in 2007 and was in noncompliance with DNR regulations

[20] Staff Recommendation, SA-2012-0362, page 4
[21] Staff Recommendation, WO-2014-0013 and SO-2014-0016, page 6

1 and permit effluent limitations. The Company's acquisition solved a long standing
2 problem for the Hickory Hills customers. The Hickory Hills receiver had taken out
3 personal loans to cover some of the ongoing costs, and to reimburse two customers for
4 sewer backup damage. The net book value of the assets was less that the amount of the
5 debt, so in order to complete the sale of the assets, the Company was required to pay
6 more than net book value. The purchase price paid by the Company was also approved
7 by the Circuit Court of Cole County, Missouri.

8 **Q. What did the Commission order in the Hickory Hills acquisition case (WA-2016-**
9 **0019)?**

10 A. Among the standard items in an acquisition order, the Commission order included two
11 items of significance[22]. First, the Company was to combine the Hickory Hills water
12 and sewer customers with the St. Louis Metro service area for ratemaking purposes.
13 Second, the Company was to establish a regulatory asset for the additional payment
14 above the net book value, and amortize it over 60 months, beginning the first month
15 after closing.

16 **Q. Please explain why the Company included the Hickory Hills receiver fees in rate**
17 **base.**

18 A. As with any acquisition, the purchase price paid by the Company is an outlay of capital.
19 Discretionary capital can be deployed in a variety of ways, including acquiring troubled
20 systems. As Staff stated in its Memorandum[23], "In Staff's view, the proposed payment
21 made by MAWC to Hickory Hills that allows Mr. Cover reimbursement of a portion

[22] WA-2016-0019, Order Denying Request for Public Hearings and Granting Application with Conditions, pages 11-15
[23] WA-2016-0019, Staff Memorandum, page 4, October 2, 2015

1 of his outstanding receivership fees and to pay off the personal loan was a reasonable
2 and necessary investment by MAWC to enable transfer assets of a "troubled" utility
3 under receivership to an experienced utility operator." The full purchase price of the
4 Hickory Hills system is the Company's investment, and as such, the Company should
5 be allowed its authorized return on this investment by including the full amount in rate
6 base.

7 **g. OTHER RATE BASE ISSUES**

8 **Q. Are there any other rate base issues raised by parties you would like to address?**
9 A. OPC witness Geoff Marke discusses the Company's recently approved Accounting
10 Authority Order related to the replacement of customer owned lead service lines.
11 Company witnesses James Jenkins, Gary Naumick, and Bruce Aiton will be providing
12 rebuttal testimony on this topic.

13 **VI. DEPRECIATION EXPENSE**

14 **Q. What aspects of depreciation expense will you address?**
15 A. I will address the depreciation rate recommendations of Staff and OPC, as well as
16 Staff's proposed capitalization of certain amounts of depreciation costs.
17
18 **Q. What was Staff's overall recommendation regarding Depreciation rates?**
19 A. Staff recommended the Company continue to use the Depreciation rates established in
20 the Company's last rate case (WR-2015-0301).

21 **Q. Did any other party address the Company's Depreciation rates?**

1 A. Yes. OPC witness John Robinette, also recommended the Company continue using the
2 rates established in the last rate case. In addition, Mr. Robinette recommended the
3 Company use a 5.0% deprecation rate for sewer NARUC account 390.9 – Structures
4 and Improvements – Leaseholds. At the time of the last rate case, the Company did
5 not have any assets in that account, but since then, investments related to that account
6 have been made.

7 **Q. Does the Company agree with this recommendation?**

8 A. The Company agrees with the recommendation to continue the depreciation rates set
9 in case WR-2015-0301, with one exception. The Company proposed changing the
10 depreciation rate on NARUC account 391.4 from 5.0% to 14.3%. Staff has not yet
11 addressed this proposal in testimony. The Company also agrees with OPC's
12 recommendation to use a 5% depreciation rate for NARUC account 390.9.

13 **Q. Please explain Staff's recommendation for the Company to capitalize certain**
14 **depreciation costs.**

15 A. In the Staff Report - Cost of Service, Staff states (Staff Report, p. 63) that "capitalized
16 expenses include depreciation expense associated with assets used in construction such
17 as power operated equipment and transportation equipment." Staff then goes on to
18 argue that "[c]apitalized depreciation expenses must be subtracted from the
19 depreciation expense calculated using MAWC's total plant-in-service balances in order
20 to prevent double recovery."

21

22 **Q. Does the Company agree with Staff's recommendation regarding capitalized**
23 **depreciation?**

1 A. No, we do not. The assets have already been capitalized once and depreciation expense
2 is being recovered currently in rates. There is no "double recovery" or "double
3 capitalization" in this case. By capitalizing costs that have already been capitalized,
4 the effect is to recover costs associated with shorter lived assets over a longer period.
5 This will result in intergenerational equity issues, as ratepayers of tomorrow will pay
6 more so today's ratepayers pay less.

7 **Q. Please describe the adjustment Staff made to capitalize depreciation expense?**
8 A. Staff totaled depreciation expense for NARUC accounts 392, 392.1, 392.2, 392.3,
9 392.4, 393, 394 and 396, which was $668,882 for the twelve months ended June 30,
10 2017. Staff applied a 42.14% capitalization rate, and excluded $281,867 from the
11 Company's depreciation expense.

12 **Q. Does the Company agree with Staff's adjustment to capitalize this portion of**
13 **depreciation expense?**
14 A. No, we do not. The Commission approved depreciation rates for these assets range
15 from 3.45% to 19.06%, and have a weighted average depreciation rate of 5.26% or just
16 over 19 years. By capitalizing these costs into other longer lived assets, Staff is creating
17 the intergenerational equity issue discussed above.

18

19 **VII. AMORTIZATION EXPENSE**

20 **Q. Please describe any adjustments Staff made to Amortization expense.**
21 A. Staff did not address any Amortization expense in the Company's future test year, and
22 made adjustments to the update information provided as of June 30, 2017. First, Staff

1 included Amortization related to the Tank Painting Tracker using the 48 month
2 amortization as proposed by Staff. Second, Staff annualized the amortization of the
3 MSD plant capacity for the Arnold Sewer system. Third, Staff excluded the
4 amortization of the Parkville sewer plant, which was fully amortized in September
5 2017. Lastly, Staff excluded amortization related to AFUDC regulatory assets.

6 **Q. Did any other parties address Amortization expense in direct testimony?**
7 A. Yes. OPC witness Keri Roth addressed the amortization of MSD plant capacity for
8 Arnold Sewer, Hickory Hills receiver fees, and the amortization of the Woodland
9 Manor transition services agreement.

10 **Q. Did OPC propose any adjustments to Amortization expense?**
11 A. It does not appear so.

12 **Q. Does the Company agree with Staff's proposed adjustments?**
13 A. Partially. The historic test year amortization related to the MSD plant capacity included
14 additional expense due to the agreed treatment in the Company's last rate case. Staff
15 has included the going forward annual expense, and the Company agrees. The
16 Company also agrees with the elimination of the amortization on the Parkville sewer
17 plant. The Company does not agree with the elimination of amortization related to the
18 AFUDC regulatory assets.

19 **Q. Did Staff explain why it excluded the amortization related to AFUDC regulatory**
20 **assets?**

1 A. No. Staff makes an adjustment in its Accounting Schedules,[24] but does not provide any explanation of the adjustment in its direct testimony.

3 **Q. Please describe the AFUDC regulatory assets being amortized.**

4 A. There are two types of AFUDC regulatory assets. The first is related to the gross up for AFUDC equity. This regulatory asset reflects the tax gross up of the equity portion of AFUDC that is recorded in construction work in progress. The second is related to the tax gross up treatment required with the implementation of FAS 109, issued in February 1992 relative to AFUDC Debt. Prior to the implementation of FAS 109, AFUDC Debt amounts were recorded to plant net of tax. After 1993, AFUDC Debt amounts are recorded to plant pre-tax instead of net of tax. The regulatory asset account represents the amounts that tax gross up that would have been recorded to plant on investments made prior to 1993

13 **Q. Why should the amortization of these regulatory assets by included in rates?**

14 A. The balances in these regulatory assets represents AFUDC costs that would otherwise be capitalized into utility plant and recovered through depreciation expense. The amortization of the regulatory assets should be treated no differently than depreciation expense, and included in rates. Beginning in the years after the implementation of FAS 109, the Company chose to change the way the tax effects of AFUDC were handled. AFUDC Debt is now recorded on a pre-tax basis rather than after-tax. For transition purposes, the amounts recorded on a pre-tax basis before the change were restated in a regulatory asset. As a result, the cost of service impacts are no longer seen on a net basis in tax expense, but instead are seen on a gross basis in pre-tax income. For

[24] Staff Accounting Schedule 9, Total Company, page 3 of 4, line 100.

1 AFUDC Equity, a similar mechanical choice was made. Instead of having the effects
2 of AFUDC Equity flow as cost of service embedded in the tax computation, The
3 amounts are grossed up to pre-tax amounts and carried in pre-tax regulatory assets. As
4 a result, denying the amortization amounts is not allowing the company full recovery
5 of its AFUDC amounts.

6 **Q. Are there any additional issues related to amortization expense?**

7 A. Yes, there are two. First, pending the regulatory treatment granted the miscellaneous
8 deferred debit related to the Company's lead service replacement line program,
9 additional amortization expense may need to be included. Please see the testimony of
10 James Jenkins for further discussion of the lead service line replacement program.
11 Second, as part of the last rate case, the Company implemented a low-income pilot
12 program in District 2. As ordered, the Company has accumulated the costs in a
13 regulatory asset. In my direct testimony in this case I proposed amortizing the costs
14 over three years[25].

15 **Q. Did Staff include any adjustments for these items in amortization expense?**

16 A. No.

17 **VIII. <u>RATE CASE EXPENSE</u>**

18 **Q. Please describe the adjustments Staff made to Rate Case Expense.**

19 A. Staff included costs incurred through September 30, 2017, excluding accrued legal
20 costs and accrued taxes. Staff included $786,529 of eligible costs in its calculation,
21 which it amortized over 30 months, resulting in $307,412 of annual amortization

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[25] LaGrand Dir, page 30

1 expense. The annual expense is then "shared" between rate payers and shareholders
2 by including expense in proportion to the percentage of the original revenue request
3 allowed by the Commission. This results in approximately 92% of the expense being
4 paid by the Company's shareholders. In addition to the $24,736 of allowed expense
5 from this case, Staff includes the unamortized balances of costs associated with the last
6 Company rate case, for a total of $77,730, in annual Rate Case Expense.

7 **Q. How does this compare to the Company's requested treatment of rate case costs?**
8 A. It is quite different. The Company proposed a total of $1,505,620 in costs associated
9 with this rate case. Additionally, we included the unamortized amounts of the
10 depreciation study completed in the last rate case in the amount of $39,229, and the
11 other unamortized costs of $186,030, for a total of $1,730,876. The Company proposed
12 to amortize this balance over 36 months, resulting in $576,959 of annual rate case
13 expense.

14 **Q. Does the Company agree with Staff's calculation of rate case expense?**
15 A. No, we do not. While it is understood that the final amount of rate case costs is not
16 known at this time, and that rate case costs will continue to accumulate well past the
17 true-up date, it is unclear how Staff developed the number used in the numerator of its
18 sharing calculation. Additionally, while the Company agrees the unamortized costs
19 from the prior case should be included in rate case expense, the Company does not
20 agree with Staff's calculations. In its workpapers, Staff calculates the total allowed
21 costs, excluding the depreciation study, at $171,373, which is significantly below the
22 costs allowed in the last rate case. As of 12/31/17 the Company has $331,632 of
23 unamortized rate case expense from the prior case.

1 **Q. Does the Company agree with Staff's proposed sharing of costs?**

2 A. No, we do not. Company witness James Jenkins will be addressing the issue of sharing
3 of rate case expense.

4 **Q. Did any other party address rate case expense?**

5 A. Yes. OPC witness Amanda Conner discussed rate case expense. OPC recommends
6 that the average costs of the five most recent large utility cases be allowed as costs,
7 which would then be subject to the same "sharing mechanism" proposed by Staff, and
8 that the amortization occur over 36 months.

9 **Q. Does the Company agree with OPC's proposal?**

10 A. Only in part. The Company agrees with OPC that the costs should be amortized over
11 36 months. The Company does not agree with the other parts of OPC's
12 recommendation. First, the idea of using other utilities' regulatory costs to set
13 MAWC's costs is nonsensical. Every utility is different, and will have different costs
14 based on the nature of their respective case. For example, a case that goes all the way
15 to hearing and has major issues fully litigated will be much more expensive than a case
16 that reaches settlement. As mentioned earlier, Company witness James Jenkins will be
17 addressing the sharing concept proposed by both Staff and OPC.

18 **Q. Does this conclude your revenue requirement rebuttal testimony?**

19 A. Yes, it does.