Exhibit No.:	
Issues:	*Corporate Allocations and Expenses, Payroll and Payroll Taxes, Employee Benefits including Incentive Compensation*
Witness:	*Lisa K. Hanneken*
Sponsoring Party:	*MoPSC Staff*
Type of Exhibit:	*Direct Testimony*
Case No:	*WR-2007-0216*
Date Testimony Prepared:	*June 5, 2007*

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

DIRECT TESTIMONY

OF

LISA K. HANNEKEN

MSSOURI-AMERICAN WATER COMPANY

CASE NO. WR-2007-0216

Jefferson City, Missouri
June 2007

**** Denotes Highly Confidential Information ****

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TABLE OF CONTENTS

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OF

LISA K. HANNEKEN

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LISA K. HANNEKEN

MISSOURI-AMERICAN WATER COMPANY

CASE NO. WR-2007-0216

Q. Please state your name and business address.

A. Lisa K. Hanneken, 9900 Page Avenue, Ste. 103, Overland, Missouri 63132.

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

A. I am a Utility Regulatory Auditor IV for the Missouri Public Service Commission (Commission).

Q. Please describe your educational background.

A. In July of 2001, I earned a Bachelors degree in Accounting from Webster University in St. Louis. In December 2006, I completed my Masters of Business Administration with an emphasis in Accounting at Maryville University, St. Louis.

Q. Please describe your work background.

A. In August 1989, I began employment with Rinderer's Union Drug as a pharmacy technician and bookkeeper. Beginning in June of 1997, I was employed by Bucklick Creek, Inc., as the head of accounting and office manager. During 2000, I completed an internship at the Internal Revenue Service (IRS) as an auditor of small corporations and businesses. In September 2001, I commenced employment with the Commission's Staff (Staff).

Q. What is the nature of your duties at the Commission?

A. I am responsible for providing supervision and assistance in the audits and examinations of the books and records of utility companies operating within the state of Missouri.

Q. Have you previously filed testimony before this Commission?

A. Yes, please refer to Schedule 1, attached to this direct testimony, for a complete listing of testimony I have filed, including the related case numbers and issues involved.

Q. Did you make an examination and analysis of the books and records of Missouri-American Water Company (MAWC or Company) in regards to matters raised in this case?

A. Yes, in conjunction with other members of the Staff. I specifically examined the Company's workpapers and testimony, the Company's response to Staff data requests, minutes of the Board of Directors, portions of the Company's general ledger and trial balances, as well as the Company's Cost Allocation Manual (CAM). I also examined testimony, workpapers and Commission Report and Orders from recent rate proceedings involving the Company.

EXECUTIVE SUMMARY

Q. What matters will you address in your direct testimony?

A. I will explain and sponsor adjustments related to MAWC's payroll, payroll taxes, employee benefits, and incentive compensation. I annualized the amount of expense reflected in the Company's cost of service to include current employees and wage rates, related payroll tax and benefits. In regards to incentive compensation, I made an adjustment to remove amounts related to portions of the plans. I will explain the relationship between

MAWC, American Water Works Company, Inc., and the American Water Works Service Company (Service Company). In addition, I am sponsoring adjustments regarding the amount of allocated expense that MAWC receives from its service company.

TRAINING AND EXPERIENCE

Q. What knowledge, skill, experience, training and education do you have in these matters?

A. Through the accounting classes, training and internships required for my educational degrees, as well as my previous work experience, I have obtained a broad working knowledge of accounting. In addition, I regularly attend continuing professional education seminars and classes. From the review of workpapers and other information from this and previous rate cases, as well as researching the Commission's orders, I have acquired knowledge of my assigned issues related to MAWC and other companies. Since joining the Commission Staff, I have assisted with and directed audits and examinations of the books and records of various utility companies operating within the state of Missouri. I have also conducted audits of small water and sewer companies in conjunction with the Commission's small company rate increase procedure. Furthermore, I have received and continue to receive training and guidance from the experienced senior auditors at the Commission.

ALLOCATIONS

Q. Please discuss MAWC's relationship with American Water Works Company, Inc. (AW), and RWE AG (RWE).

MAWC is a subsidiary of AW, which in turn, is owned by RWE. RWE is a global, multi-utility company that does business through its subsidiaries and affiliates in over

120 countries. RWE is headquartered in Germany and its core businesses include electricity, gas, water, waste, and recycling. A subsidiary of RWE, Thames Water, completed its acquisition of AW during January 2003. At the end of 2005, RWE decided to withdraw from the water sector in the UK and North America. As a result, at the end of 2006, RWE sold Thames Water and currently plans to sell the majority of AW by the end of 2007. RWE intends to focus on Europe's gas and electricity markets.

AW is headquartered in Voorhees, New Jersey, and serves approximately 17 million customers in 29 states and three Canadian provinces. AW performs many functions and activities on a consolidated or centralized basis for many of its regulated and unregulated subsidiaries. These consolidated or centralized functions are carried out for the AW-owned subsidiaries by the AW wholly-owned Service Company. Through a process of direct assignment and allocation, Service Company employees' time and all other related costs are ultimately charged to the AW-owned utility subsidiaries receiving service. In addition to the Service Company, in 2000, American Water Capital Corporation (AWCC) was created to provide a single source of long and short term debt capital for AW and it utility subsidiaries. A service agreement exists between MAWC and both the Service Company and AWCC.

Q. What regulated subsidiaries and non-regulated affiliated entities receive direct assignment or allocation of Service Company costs?

A. The following subsidiaries or affiliated entities currently receive direct or allocated charges from the Service Company:

Regulated Entities

Arizona American Water
California American Water
Elizabethtown Water Company Inc.
Hawaii American Water
Illinois American Water
Indiana American Water
Iowa American Water
Kentucky American Water
Long Island Water Corporation
Maryland American Water
Michigan American Water
Missouri American Water
Mount Holly Water Company
New Jersey American Water
New Mexico American Water
Ohio American Water
Pennsylvania American Water
Tennessee American Water
Texas American Water
Virginia American Water
Virginia American Eastern District (formerly United Water)
West Virginia American Water

Unregulated Entities

American Water Enterprises (AWE)
American Water Capital Corporation (AWCC)
American Water Resources, Inc. (AWR)
American Water Works (AWK)
Edison Water Company
Elizabethtown Services LLC
Liberty Water Company

Q. How does the Service Company classify its costs?

A. Services performed by the Service Company can be grouped into the following cost centers, each with their own list of services provided:

Corporate: provides executive management, finance, human resources, engineering, water quality and operations support and is located in Voorhees, NJ.

Shared Services Center: provides financial, accounting, procurement, cash management and human resource benefits coordination and is located in Cherry Hill, NJ.

Call Center: national call centers which handle customer service calls; located in Alton, IL, and Pensacola, FL.

Belleville Lab: national trace substance laboratory located in Belleville, IL.

ITS: two ITS centers which provide information technology support and customer billing for operating companies, located in Haddon Heights, NJ, and Hershey, PA.

Region Offices: handle management, rates and revenues, external affairs, loss control, maintenance, legal, human resources, engineering and construction management, water quality and other operations support services for operating companies in their region as listed below:

Northeast Region (located in NJ): serves New Jersey and New York.

Southeast Region (located in WV): serves Kentucky, Maryland, Pennsylvania, Tennessee, Virginia, and West Virginia.

Western Region (located in CA): serves Arizona, California, Hawaii, and New Mexico.

Central Region (located in MO): serves Illinois, Indiana, Iowa, Michigan, Missouri, and Ohio.

Q. How do the above cost centers differ from what was presented in MAWC's last rate case, Case No. WR-2003-0500?

A. Since the last case, the Shared Services Center relocated to Cherry Hill from Voorhees; and one of the three ITS centers was eliminated and its work absorbed by the Hershey and Haddon Heights ITS centers. Also, an additional call center was added in Pensacola. Finally, in the last case there were 5 regional offices, two of these, the Illinois regional office and the Indiana regional office, were combined into the Central Region during the Company's reorganization process in 2005.

Q. Please explain the reorganization that took place.

A. The Company consolidated its offices and moved employees from its operating companies to its regional offices.

Q. Does each AW subsidiary take all of the services listed above?

A. Not all AW subsidiaries require all of the services listed. Several of the subsidiaries are capable of performing many of these activities and functions, in part or in total, at the local company level.

Q. What types of expenses are allocated from the Service Company?

A. Based on the Company's CAM, Service Company expenses can be categorized as follows:

Expense Category	Description	Direct Charged	Allocated	Comments
Labor	Base pay (salaries) of managerial, professional and technical employees	Yes	Yes	Professional personnel working for one or several operating companies
Support	Wages and salaries of office support personnel, including secretaries, clerical personnel, telephone operators and mail clerks		Yes	Administrative personnel support the professional staff, thus support costs are allocated on the basis of professional labor
Labor Related Overhead	Employee benefit costs (payroll taxes, medical coverage, pensions, disability insurance) and other general expenses	Yes	Yes	These are primarily employee benefit costs that relate directly to labor
Office Expense	Office rent, equipment leases, telephone, electric, office supplies, property taxes, office maintenance		Yes	Are all allocated on the basis of professional labor
Vouchers/ Journals	Travel expenses incurred by Service Company personnel; other items submitted for reimbursement by employees, including professional association dues; outside service contracts for such things as actuarial services; and various other expenditures, including data center expenses for software licenses and hardware maintenance	Yes	Yes	May be either directly in support of one operating company (e.g. an engineer traveling from the Corporate Office to the operating company) or allocated to several operating companies

Q. Please describe how the Service Company charges time and expenses to affiliate companies.

A. According to the Company's Cost Allocation Manual (CAM), Service Company transactions are assigned with information so that proper accounting for the service can take place. This information includes the affiliate company number (if a direct charge) or a formula number if a transaction is allocated, the number of hours the employee worked, and the appropriate account number for non-labor items. This method allows for direct charges to both regulated and non-regulated entities when the employee can clearly identify the hours spent providing service to a specific affiliate.

Q. What methodology does AW utilize to allocate costs to both its regulated and non-regulated companies?

A. Using the time reporting system, each employee has the ability to charge hours on their time sheet to billing formula numbers that allocate those hours (or portions of hours) among the group of companies (including regulated and non-regulated) receiving those services when it is not practicable to determine the actual time spent performing that task for each of the companies.

Q. What types of formulas are used to allocate these costs?

A. When a Service Company employee provides services that benefit both regulated and non-regulated entities, they choose one of the Tier-One allocation factors to use. An employee who only performs services for regulated companies will utilize a Regulated Formula based on customer counts, and while providing services to non-regulated companies will use a Non-Regulated Formula based on a combination of revenues, amount of plant and number of employees.

Q. How are the Tier-One formulas derived?

A. Tier-One Formulas are based on different criteria, such as revenues, employees, plant investment, and others. Some of the formulas are a composite of these criteria, while others are based on only one criterion such as employee numbers. The employee will choose the formula that matches with the service provided. For example, an employee in payroll will most likely choose a formula based on employee numbers.

Q. Do the formulas differ for services provided by regional cost centers?

A. Yes, regional offices have formulas for the regulated entities they serve based on customer numbers.

Q. Can the regional cost centers charge to other companies outside of their given service area?

A. Yes, if a particular regional office has the expertise in a certain area, such as engineering, that is lacking in another region, they may perform tasks for a specific operating company outside of their given service area. For example, if a certain type of plant project is under construction by California-American, but the only engineer that is familiar with the specifics of that type of plant is located in the Southeast region office, he will provide services to California-American and can charge his time directly.

Q. Are there a large number of charges to areas outside the region?

A. No, only a minimal amount of these charges appear in the Company's CAM.

Q. What type of adjustments did the Staff make to the allocated expenses in their filing?

A. The Staff made several adjustments, which I will describe in detail below.

Allocated External Affairs Expense Adjustment (Central Region)

Q. What adjustment was made for External Affairs?

A. Following the test year, two employees, who were employed at the Central Region office which supports Missouri American, were transferred to MAWC. These employees were transferred because they were spending 100% of their time providing services for MAWC. Therefore Staff removed this amount from the Company's allocated expense levels and included these individuals in its annualization of payroll.

Q. Did Staff make any other adjustments related to External Affairs?

A. Yes, Staff removed a portion of the amount of wages and the associated payroll tax, employee benefits, and incentive compensation associated with the Regional Vice President of External Affairs given that his job description indicates that he performs some lobbying related duties, as well as directs employees that perform lobbying duties.

Q. Has the Commission previously indicated lobbying expenses were not to be borne by a company's ratepayers?

A. Yes, in several past cases the Commission has disallowed the costs associated with lobbying. Specifically in Case No. 18,180 In the matter of Missouri Public Service Company, Kansas City, Missouri, 20 Mo.P.S.C. (N.S.) 68, 105 (1975) and Case No. ER-83-49, In the matter of Kansas City Power & Light Company, 26 Mo.P.S.C. (N.S.) 104, 116 (1983), the Commission stated that the beneficiaries of lobbying activities are usually the stockholders of the company involved in lobbying. The Commission has also stated that the stockholders of a company involved in lobbying should be the ones to assume responsibility for these expenses unless the company offers substantial evidence for their inclusion in rates.

Allocated Labor and FICA Expense Adjustments

Q. Please describe the adjustments made related to all allocated labor and FICA taxes.

A. The Staff increased the amount of the allocations MAWC receives to include changes for wage increases, discontinued labor and the related FICA taxes. The Staff adjustment recognized a wage increase that took effect on 4/1/2006. Another wage increase effective on 4/1/2007 will be considered as part of its true-up process.

Allocated Other Expenses Adjustment

Q. Please explain the Staff's adjustment for 'Other' items.

A. MAWC removed an allocated total of $84,252 related to membership dues, donations, lobbying, and other miscellaneous items it felt should not be considered as part of the rate case. Since the Staff was not provided with the detail for these items to make its own determination, Staff has disallowed these amounts.

Q. Did Staff discover other items such as these that it feels should be removed from the Company's level of allocation expense?

A. Yes. Staff disallowed $37,603 of other dues and miscellaneous items expensed by the Company during the test year. In the past it has been the Commission's position to disallow dues and donations that: (1) provided no direct, quantifiable benefit to the ratepayer, (2) were not necessary in providing safe and adequate service to the ratepayer, and (3) represented an involuntary contribution on the part of the ratepayer to an organization. The Staff contends that although the Company's management may choose to make these types of expenditures, the cost should be borne by the shareholder, not the ratepayer. While Staff tried to identify each item and make a determination, some items were not identified by the

Company through the data requests submitted by Staff. Therefore, Staff has removed these allocated items until such time as the Company provides an explanation.

Staff removed various items, including dues to the Leadership Missouri program, which is related to Missouri's Chamber of Commerce. The Staff has traditionally allowed dues to chambers of commerce on the local level. However, expenses related to similar organizations at the state or national level have been disallowed on the basis that such costs are duplicative.

Additionally, Staff removed expenses related to organizations that are known for their lobbying activities on the same basis as previously discussed.

Q. Were there other items that Staff removed?

A. Yes, Staff removed a total of $72,693 related to advertising. The Company provided a listing of the payee and amounts that were allocated; however Staff could not determine what these items were. Staff requested from the Company a more detailed description in order to determine what these expenses were, but to date Staff has not received that data. The Company did provide copies of 3 advertisements; however, these were just the ad copies without any reference to the listing of expenses, so Staff did not know how they related to the list. However, the Staff was able to identify what it believes to be expenses related to help wanted advertising, which it allowed. All the other items were disallowed.

Staff is willing to reconsider any allocated items that were removed at such time an adequate description and details are provided.

Allocated One-Time Expense Adjustment

Q. Please explain the Staff's adjustment related to one-time costs.

A. The Company identified costs that were passed through the Service Company that were considered to be one-time costs. Included in this amount were costs related to RWE's divestiture of AW and costs related to complying with the Sarbanes-Oxley Act of 2002 (SOX). Staff has eliminated these non-recurring costs from MAWC's expenses.

<u>Allocated Service Company Additions Adjustment</u>

Q. Please explain the adjustment Staff made to its allocation expense level.

A. This adjustment includes amounts related to increases at the Service Company for an increase in employees and increased expenses such as depreciation and interest related to increases in plant assets.

Q. Please discuss the increase in employee levels.

A. Staff included amounts for employees that were shown in the Company's workpapers as being filled positions. Staff requested data for an update of hires through December 31, 2006, but to date has not received such information. At such time this information is provided, Staff will consider it as part of its analysis. Staff will also consider the information it requested regarding any employees hired by May 31, 2007, as part of the true-up process.

Q. Please describe the increase costs related to assets.

A. These costs related to items such as software, hardware and building upgrades. Staff received a revised listing from the Company on May 14, 2007, which gave amounts for the items completed as of December 31, 2006, the update period in this case. Staff utilized these amounts in its cost of service level. The Company is to update Staff as to the amount completed by the end of the true-up period in this case (May 31, 2007) so that Staff may make a determination as to the amount to include its in true-up calculations.

Allocated National Shared Services Charges Capitalized

Q. Please explain Staff's adjustment related to capitalization of allocated costs.

A. Staff's adjustment represents the capitalization of the costs that were expensed during the test year associated with various accounting and financial services provided by National Shared Services. Based on discussions with the Company, some portion of the accounting services being provided to MAWC pertain to fixed assets and would, therefore, appropriately be a capitalized cost. Staff has calculated its adjustment based on amounts provided in the last case and a partial data request response in the current case. Staff will update its calculations when it receives a complete response to its request in the current case.

Allocated Transition Costs Related to Call Center and National Shared Services Center

Q. Please explain Staff's adjustments related to transition costs.

A. Staff removed one-time, transition costs that the Company capitalized as plant in service related to its decision to begin taking service from the Alton Call Center. Staff also removed a similar one-time, non-recurring transition cost from the Company's plant in service that was related to the Company's decision to begin taking service from the Service Company National Shared Services Center.

Q. How was the implementation of the Call Center and the Shared Services Center handled?

A. The implementation of the Call Center and the Shared Services Center was directed at the Service Company level. Most of the costs associated with the planning, development and implementation were incurred and recorded at the Service Company level and, therefore, allocated to each of the Companies which would be transitioning to the Call Center and to the Shared Services Center.

Q. What did these transition costs relate to?

A. During the last case, the Company indicated to the Staff that it had capitalized $5,263,822 of expenditures that were made to plan, design and implement the concept of the customer call center. Similarly, the Company indicated that it has capitalized $4,488,826 of expenditures that were made to plan, design and implement the concept of the shared services center.

These expenditures were for labor, travel expenses, consulting fees and other related expenses such as employee recruiting and training for the design and implementation of the Call Center and Shared Service Center.

Q. What is the basis of the Staff's proposed disallowance of these transition costs?

A. Staff contends that all of these costs are one-time, non-recurring expenses and as a result, these costs should not be reflected in MAWC's ongoing cost of service. The key point is that MAWC owns none of the assets at either the National Call Center or at the Shared Services Center. The Service Company owns all of these assets and controls all of the business processes related to these assets. Therefore, the Company's attempt to recover these costs through rate base has no basis. No tangible asset was created for MAWC. The Staff contends it is inappropriate for MAWC to capitalize these one-time transition expenses related to assets that it does not own and business processes that are not under its control.

Q. Has the Commission disallowed transition costs in any other rate proceedings?

A. Yes. In its Report and Order from Case No. WR-2000-844, involving St. Louis County Water Company, the Commission disallowed transition costs related to the Company's use of the name "MAWC Water Company." In this case, the Commission's ruling stated the following:

> The Commission finds that these costs are a direct result of Company's management's decision to operate under a new name. Furthermore, there is no evidence that these costs will be incurred in the future when the rates set in this case are in effect, and the Commission finds them to be non-recurring.

Q. Historically, what has been the Staff's position with regards to transition costs like those proposed for inclusion by MAWC in the current case?

A. The Staff's position with regard to transition costs has been to allow recovery for any un-recovered transition costs that generate actual cost savings to the ratepayers of a Company. The Staff has allowed recovery of transition costs over periods covering 10 or 20 years. The Staff has never allowed rate base treatment or a "return on" un-recovered transition costs. The Staff has historically disallowed one-time transition costs that do not generate measurable cost savings.

Q. Please explain why the Staff believes the Company's proposal for a recovery of transition costs related to the move to the Call Center is inappropriate.

A. Traditionally, the Staff has proposed "return of" un-recovered transition costs that relate to activities that result in achieved cost savings to ratepayers. For example, in Case No. EM-96-14 involving the merger of Union Electric and Central Illinois Public Service Company, Union Electric was able to demonstrate to the Staff that the resulting merger was likely to lead to sufficient efficiencies and cost savings to cover the amount of merger transition costs. The Staff ultimately agreed to an amortization over ten years, with no rate base treatment, for certain Union Electric un-recovered transition costs.

MAWC has proposed to receive both a "return of" and a "return on" Call Center transition costs. The Staff believes that neither of these proposed treatments are justified because the Call Center has not resulted in any achieved cost savings for MAWC. Instead the

Company proposes to significantly increase the total amount of Call Center costs and related customer service activities. Therefore, since these costs represent nothing more than one-time, non-recurring expenses that relate to business assets that MAWC does not own and does not control, they should not be included in rates. Even Company witness Thornburg in MAWC's last rate case admitted the costs are nonrecurring (See Thornburg rebuttal WR-2003-0500, page 8, line 7). Furthermore, the 2001 AW SEC 10K also characterizes these costs as "one-time."

Q. Why is it inappropriate for the Company to capitalize the transition costs related to National Shared Services Center?

A. The transition costs relate to assets that MAWC does not own and to business processes that they do not control. Seeking to recover a "return on" and a "return of" these costs is totally inappropriate. In the response to Staff Data Request No. 181 from the last rate case, the Company indicated through a cost benefit analysis that it expects to generate annual savings of $2,575,688. Taking the Company's prediction at face value, the Company has already recovered the entire cost of the transition through the savings thereby generated. MAWC transitioned to the Shared Services center on November 7, 2001, which occurred after the date that rates were established in Case No. WR-2000-281 for MAWC (September 14, 2000) and Case No. WR-2000-844 for St. Louis County Water Company (May 13, 2001). The following chart reflects the amount of savings the Company has and will continue to recapture to offset the Shared Services transition costs through the operation of law date in the current case:

PERIOD	SAVINGS GENERATED AND RETAINED BY MAWC
11/7/01-12/31/01	$ 388,117
1/1/02 – 12/31/02	$2,575,688
1/1/03-12/31/03	$2,575,688
1/1/04-12/31/04	$2,575,688
1/1/05-12/31/05	$2,575,688
1/1/06-12/31/06	$2,575,688
1/1/07-11/14/07	$2,253,727
Total Savings Realized	$15,520,284

This chart reflects that by the end of the operation of law date, by its own calculations, the Company will have already recovered approximately $11,031,457 ($15,520,284 - $4,488,827) more in cost savings from its participation in the National Shared Services Center than it actually incurred for transition costs. Allowing MAWC to include the transition costs in the cost of service for this case will afford the Company double recovery of these costs. In fact, the Company has not only enjoyed more savings than the Shared Services Center transition costs, but also the Alton Call Center transition costs. The Staff recommends that the Commission disallow these transition costs.

Additional Allocation Recommendations

Q. Does Staff have any additional recommendations regarding allocations?

A. Yes. During MAWC's last rate case, Case No. WR-2003-0500, Staff learned that MAWC is required to pay management fees in advance for services provided by the Service Company.

The Staff believes that this is inappropriate given the affiliated relationship between these two entities. The Company, on average, is not required to prepay for the goods and services from the various vendors that were included in the cash vouchers expense lag in its cash working capital analysis. The Staff also contends that while the affiliate Service

Company is requiring MAWC to prepay for services provided, the Service Company actually pays its invoices for goods and services in arrears. Therefore, under the current prepayment situation, the ratepayers of MAWC are being required to provide an unnecessary cash working capital allowance to the affiliate Service Company.

As was done in the last case, Staff has applied the cash vouchers expense lag to management fees. Please refer to Staff witness Edward F. Began's direct testimony for an explanation of the Staff's calculation of the cash vouchers expense lag. The Staff recommends that the Commission only include the cash working capital requirement associated with paying for services that it receives from its affiliated Service Company in a manner similar to the payments MAWC makes to other vendors as is represented by the cash vouchers expense lag.

PAYROLL

Q. Please explain the adjustments to payroll.

A. Staff's payroll adjustments represent the Staff's individual payroll annualizations to the various operating rate divisions in Missouri.

Q. What are the different components of Staff's payroll annualization?

A. The payroll annualization takes into account the wage increases for both union and non-union Company employees and differences in the on-going level of employees not reflected in the test year.

Q. Please explain the methodology you employed to determine annualized payroll.

A. Staff based its annualization on the Company's actual labor dollars for the test year ending June 30, 2006. Staff then made adjustments to increase the payroll levels to reflect the current union labor rates, the April 2006 non-union labor increase, and the number of employees at year end December 31, 2006, in an effort to bring the Company's labor expense current through the update period. Staff also took into consideration the amount of labor related to summer interns.

Q. Why did Staff not include the April 2007 non-union labor increase?

A. As this increase was outside of the update period, it would not be appropriate to include it in Staff's annualization. However, the Staff intends to re-examine the Company's labor expense for inclusion in its true-up estimate. Staff's true-up recommendation is further discussed in the direct testimony of Staff witness Stephen M. Rackers.

Q. Were there any union labor increases that took place subsequent to the update period, but prior to the true-up date?

A. No. The labor contracts indicate that the increases are scheduled to occur on dates subsequent to the true-up period; therefore, Staff will not include them in its true-up examination.

Q. Were there any other adjustments made to the Company's labor expense?

A. Yes, Staff removed the cost related to an employee who, according to the job description, participates in lobbying activities. The reasons for excluding lobbying expense were previously explained on page 10 of this testimony.

Q. Did Staff examine the level of overtime incurred by the Company?

A. Yes. Staff examined overtime from January 2003 – December 2006 and found that in several districts, there was an upward trend. In these districts, Staff adjusted the amount of test year overtime to the amount known for the 2006 calendar year as an ongoing level. However, in other districts, Staff saw fluctuation in the amount of overtime during this time period. Therefore, Staff calculated a 4-year average amount of overtime and adjusted the test year level to this 4-year average.

Q. Why did Staff not use a 5-year average?

A. Staff has not yet been provided with the data for 2002 in order to calculate the 5-year average; however Staff will review this data when it is provided.

Q. Please discuss which treatment was applied to each district.

A. The 4-year average was used for the Brunswick, Joplin, Parkville Water, St. Charles, St. Joseph, and St. Louis districts. Staff utilized the 2006 year totals as the current ongoing levels for all other MAWC districts, except the Jefferson City district, which displayed abnormal levels.

Q. What abnormal data did the Jefferson City district show?

A. In the Jefferson City District, Staff found that in 2004 and 2005 the district experienced an increase in its overtime hours related to O&M payroll of 155% and 33%, respectively. While most other districts increased their amount of overtime during these time periods, this extreme jump in 2005, which continued in 2006, was exceptional as compared to the other districts. In response to Staff Data Request No. 55, the Company responded that much of the increase in its overtime was due to vacancies, increased shut-offs and maintenance. In subsequent Data Request No. 249, Staff asked for the Company, in particular, to explain the situation in Jefferson City. In response to this data request the Company indicated that the hours experienced in 2005 and 2006 were higher than the more normal levels experienced in 2003. Based on this response Staff utilized a 2-year average of the normal level of overtime hours experienced in 2003 and 2004 to determine its adjustment.

Q. Did Staff notice any other district specific abnormalities?

A. Yes, the Cedar Hill district seemed to have a discrepancy in the amount of overtime hours incurred detailed in Staff Data Requests Nos. 55 and 55.1. Staff inquired about this discrepancy and to date has not received an explanation. Staff used the most current data request in its calculations; however, if that data request is incorrect Staff will need to revise its calculation based on the correct data when it is received.

Q. Are there any other items Staff noticed as part of its overtime analysis?

A. Yes, Staff became aware of the fact that the Company has employees who work an excessive amount of overtime. For example, one construction truck driver worked 2,514 hours of overtime during the test year, according to the data provided, which is more than working a double shift every single work day. Staff did not make an adjustment related to these workers, since most of the cost is capitalized and the specific adjustment would be immaterial to the revenue requirement at the St. Louis District. While Staff realizes that some positions require overtime and specific experience levels, hiring another truck driver seems warranted. Even with the added amount of labor overhead resulting from another employee, there should be cost savings, as well, there may be a safety issue related to employees who drive large trucks for 16 hours, 5 days a week.

PAYROLL TAXES

Q. Please explain the Staff's payroll tax adjustment.

A. This adjustment represents the Staff's annualization of Federal Insurance Contributions Act taxes (FICA), Federal Unemployment Tax (FUTA), and State Unemployment Tax (SUTA).

Q. Describe the Staff's annualization of payroll tax.

A. Staff calculated the amount for each individual employee included in its payroll annualization through the update period. Staff also recognized any other adjustments it made to payroll-related items, including incentive compensation as discussed later in this testimony, in its calculations.

Staff also annualized the amount of FUTA and SUTA associated with the Company's labor level. The annualization was based on the most current Company specific unemployment rate percentages available.

EMPLOYEE BENEFITS

Q. What types of benefits are provided by the Company?

A. The Company provides various benefits to the employee, including 401K matching, health insurance, a post-retirement medical cost saving account, accidental death and dismemberment, short-term disability, long-term disability, life insurance and incentive compensation. Staff will discuss incentive compensation in the section following this employee benefits section.

Q. Please describe Staff's adjustment for the Company's group insurance.

A. Staff considered the Company's health insurance, accidental death and dismemberment, short-term disability, long-term disability, and life insurance as the group insurance category. Staff was able to perform an analysis by employee with current rates. Therefore, Staff is making an adjustment to bring the level of group insurance up to the amount related to the employee level at year end December 31, 2006. Staff's adjustment represents a sizable increase in these costs over test year, which is due to the rise in health care costs.

Q. Please describe Staff's adjustment related to Voluntary Employees' Beneficiary Association (VEBA).

A. ** ____ **

Q. Please describe Staff's adjustment related to MAWC's 401K matching program.

A. As part of its employee benefits the Company contributes to the employees' 401K fund. Staff was able to analyze these contributions on a per employee basis as of December 31, 2006, and made an adjustment to reflect the changes in the employee levels and contribution elections.

INCENTIVE COMPENSATION

Q. Please discuss the Company's incentive compensation plans.

A. ** ____ **

Q. What criterion is set for eligibility?

A. ** ____

NP

**

Q. How many MAWC employees are eligible for the AIP?

A. ** **

Q. ** **

A. ** **

Q. How does the plan work?

A. **

. **

Q. ** **

A. **

**

Q. ** **

A. **

NP

**

Q. ** **

A. **

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Q. ** **

A. **

**

Q. ** **

A. **

**

Q. ** **

NP

A. ** ____________________ **

Q. Please explain how the funding for this plan works.

A. ** ____________________

____________________ **

Q. Did Staff make an adjustment regarding ** ____ **

A. ** ____
____
____
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____
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____
____________________________________ **

Q. Why did Staff make an adjustment related to the ** ________________ ______ **

A. ** ____
____
____
____
____ **

Q. Did Staff make any other adjustments to ** ____________ **

A. ** ____
____
____
______ **

Q. ** ______________________________ **

A. ** ______________________________ **

In the Southwestern Bell Telephone (SWB) Case No. TC-89-14, the Commission agreed with Staff that incentives based on goals related to non-regulated subsidiaries and non-Missouri portions of SWB should not be included in the Staff's amounts stating that:

> "achieving the goals of SBC and unregulated subsidiaries is too remote to be a justifiable cost of service for Missouri ratepayers". 29 Mo.P.S.C. (N.S.) 607, 627 (June 20, 1989).

These principles remain reasonable to consider in the current utility environment. In the 2004 Missouri Gas Energy case, GR-2004-0209, the Commission stated:

> Those financial incentives seek to reward the company's employees for making their best efforts to improve the company's bottom line. Improvements to the company's bottom line chiefly benefit the company's shareholders, not its ratepayers. Indeed, some actions that might benefit a company's bottom line, such as a large rate increase, or the elimination of customer service personnel, might have an adverse effect on ratepayers….the shareholders that benefit from that plan should pay the costs of that plan. 12 Mo.P.S.C.3d 581, 606-07.

** ______________________________ **

NP

Q. Did Staff take into consideration the incentive compensation received through allocations to MAWC?

A. ** ______________________________ **

Q. Did Staff make adjustments related to the ** ______________________________ **

A. ** ______________________________ **

Q. What adjustments did Staff make to the Company's allocated ** ______ **

A. ** ______________________________ **

Q. Did Staff make any additional adjustments to the ** ______ **

A. ** ______________________________ **

NP

Q. Does this conclude your testimony in this case?

A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Missouri-American Water Company's request for Authority to Implement a General Rate Increase for Water Service provided in Missouri Service Areas	))))	Case No. WR-2007-0216, *et al*

AFFIDAVIT OF LISA K. HANNEKEN

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Lisa K. Hanneken, of lawful age, on her oath states: that she has participated in the preparation of the foregoing Direct Testimony in question and answer form, consisting of 33 pages to be presented in the above case; that the answers in the foregoing Direct Testimony were given by her; that she has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of her knowledge and belief.

Lisa K Hanneken
Lisa K. Hanneken

Subscribed and sworn to before me this 4th day of June 2007.

D. SUZIE MANKIN
Notary Public - Notary Seal
State of Missouri
County of Cole
My Commission Exp. 07/01/2008

D Suzie Mankin
Notary Public

CASE PROCEEDING PARTICIPATION

LISA K. HANNEKEN

PARTICIPATION		TESTIMONY
COMPANY	CASE NO.	ISSUES
Laclede Gas Company	GR-2002-356	Direct - Cash Working Capital, Rate Case Exp./PSC Assessment, Advertising, Misc. Expense
Missouri-American Water Company	WR-2003-0500	Direct – Rate Base and Related Expenses, AFUDC, Dues and Donations, Waste Disposal Expense, Storage Tank Lease Expense, Deferred Maintenance Expense, Transportation Expense, Insurance Other Than Group, Cost of Depreciation Study Expense
Missouri-American Water Company	WR-2003-0500	Surrebuttal – AFUDC, Dues and Donations, St. Joseph Waste Disposal Expense, Transportation Expense, Property Taxes
Fidelity Telephone Company	IR-2004-0272	Direct - Rate Base and Related Expenses; Insurance Other Than Group; Miscellaneous Other Taxes
Atmos Energy Corporation	GR-2006-0387	Direct – Corporate Allocations and Expenses, Payroll and Payroll Taxes, PSC Assessment, Taxes Other, Legal Fees
AmerenUE Electric Company	ER-2007-0002 and GR-2007-0003	Direct – Corporate Allocations and Expenses, Payroll and Payroll Taxes, Employee Benefits, Incentive Compensation, Miscellaneous Expenses