

Exhibit No.:  
Issues: Plant in Service  
Witness: James A. Merciel, Jr.  
Sponsoring Party: MO PSC Staff  
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Case No.: WR-2008-0311  
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**MISSOURI PUBLIC SERVICE COMMISSION**

**UTILITY OPERATIONS DIVISION**

**SURREBUTTAL TESTIMONY**

**OF**

**JAMES A. MERCIEL, JR.**

**MISSOURI AMERICAN WATER COMPANY**

**CASE NO. WR-2008-0311**

**Jefferson City, Missouri  
October 2008**

Notary Public

**SURREBUTTAL TESTIMONY**  
**OF**  
**JAMES A. MERCIEL, JR.**  
**MISSOURI AMERICAN WATER COMPANY**  
**CASE NO. WR-2008-0311**

Q. Please state your name.

A. My name is James A. Merciel, Jr.

Q. By whom are you employed

A. I am employed by the Missouri Public Service Commission.

Q Are you the same James A. Merciel, Jr. who participated in the Staff Report on Cost of Service that was filed on August 18, 2008?

A. Yes. My qualifications are within that document on pages 27 through 30.

Q. What is the purpose of your surrebuttal testimony?

A. The purpose of my surrebuttal testimony is to address the Staff's recommended disallowance of the capital expense associated with a project to expand the capacity of the Cedar Hill Sand Creek sewage treatment facility (the "Sand Creek Plant"), which is one of two treatment facilities in the Company's Cedar Hill sewer service area. This issue was addressed in the Staff Report on page 16, and was addressed by Missouri American Water Company ("MO American" or "Company") in the rebuttal testimony of Kevin H. Dunn. In addition to addressing the Staff's disallowance, the Company also addresses the accounting treatment in the rebuttal testimony of Dennis R. Williams. The Staff is responding to Mr. Williams' testimony in the surrebuttal testimony of Kimberly K. Bolin.

Surrebuttal Testimony of  
James A. Merciel, Jr.

1 Q. Why do you recommend disallowance of the cost of the Sand Creek Plant  
2 expansion?

3 A. The reason I recommend the disallowance is because the treatment capacity of  
4 the facility was expanded to serve new customers in a newly developing area, from 75,000  
5 gallons per day (gpd) to 150,000 gpd, along with a quadrupling of rate base for the service  
6 area. But, there are very few new customers connected as yet. Inclusion of the cost of the  
7 expansion without the new customers available to pay results in both rate shock, and an  
8 undesirable impact upon existing customers in that they are being required to pay the entire  
9 cost of an expansion project that is necessary to serve future customers.

10 Q. Do you believe that the Sand Creek Plant expansion was imprudent, or  
11 unnecessary, or too costly?

12 A. No. I believe that the expansion project was prudently undertaken. I also  
13 believe that it is necessary for future growth, which appeared imminent at the time the project  
14 was undertaken but unfortunately has not proceeded as was anticipated.

15 Q. Do you believe that the Company should be able to recover its capital funds  
16 related to this project?

17 A. Yes, I do. I do not wish to recommend denying recovery of the funds  
18 expended for this project. However, since the new customers are not yet available to pay for  
19 the plant expansion, I also do not wish for existing customers to bear the substantial cost that  
20 is needed for the future customers, even though the facility is in fact in service and available  
21 for new customers.

22 Q. Can you please explain the rationale for the disallowance?

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James A. Merciel, Jr.

1           A.     Yes. Although Missouri American is a large utility company, the Company's  
2 Cedar Hill service area, with its "stand-alone" rates and only about 730 customers, has  
3 characteristics that are similar to small utilities. The Sand Creek Plant expansion was sized to  
4 serve approximately an additional 200 customers. The cost of the project was approximately  
5 \$2.1 million, although some of the cost is related to general improvements to the facility that  
6 benefit all customers, and the developer of the proposed subdivision has already paid  
7 contribution-in-aid-of-construction (CIAC) charges. The actual amount of the disallowance  
8 recommended by the Staff is in the surrebuttal testimony of Kimberly K. Bolin. The annual  
9 revenue associated with this recommended disallowance would be \$257,218, or  
10 approximately \$29.32 per month per customer, as compared to the existing residential rate of  
11 \$23.52 per month. Arguably, this facility would not have been constructed, and much of the  
12 capital cost would not have been incurred by the Company if not for the potential growth.  
13 Many small utilities rely on developers to fund all of the initial capital expense of treatment  
14 capacity, then the utilities repay the developers as customers actually connect, such that the  
15 developers and not existing customers take the risk of capital expense for future customers.  
16 MO American's tariff permits collection of CIAC charges from developers up front, but is not  
17 set up for temporary funding of the Company's investment by developers.

18           Q.     Are methods available that would result in the Company's ability to collect the  
19 appropriate revenue without the substantial rate impact upon the Cedar Hill customers?

20           A.     Yes. One possible method is a subsidy from the company's water revenue.  
21 Another method would be to include portions of the cost of the Sand Creek Plant expansion  
22 project. Arguably, some of the costs are for items that benefit existing customers as well as  
23 future customers, such as an office building, improvements to the plant grounds, and existing

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1 facility rehabilitation. In addition to these items, if and when the cost of the expansion that is  
2 actually related to capacity is included in rate base, it is likely that existing customers will  
3 experience an impact since the rate base on a per customer basis will increase even when  
4 future customers are included. A phase-in of rate base recovery, and/or expense allocation,  
5 could also be used.

6 Q. Will you please summarize your testimony?

7 A. Yes. I recommend disallowance of the cost of the Sand Creek Plant expansion  
8 in this case, because the future customers for which the project was undertaken do not yet  
9 exist. However, I do not wish to permanently disallow the Company the cost recovery of the  
10 plant expansion in the future. Alternative ways to allow the Company to collect the  
11 appropriate revenue are available.

12 Q. Does this conclude your surrebuttal testimony?

13 A. Yes.