Exhibit No.:

Issue: Rate of Return
Witness: David Murray
Sponsoring Party: MoPSC Staff
Type of Exhibit: True-up Direct Testimony

Case No.: WR-2007-0216

Date Testimony Prepared: July 19, 2007

MISSOURI PUBLIC SERVICE COMMISSION UTILITY SERVICES DIVISION

TRUE-UP DIRECT TESTIMONY

OF

DAVID MURRAY

MISSOURI-AMERICAN WATER COMPANY **CASE NO. WR-2007-0216**

Jefferson City, Missouri July 2007



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| 1 | TRUE-UP DIRECT TESTIMONY | |
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| 2 | OF | |
| 3 | DAVID MURRAY | |
| 4 | MISSOURI AMERICAN WATER COMPANY | |
| 5 | CASE NO. WR-2007-0216 | |
| 6 | Q. Please state your name. | |
| 7 | A. My name is David Murray. | |
| 8 | Q. Are you the same David Murray who filed direct and rebuttal testimony in this | |
| 9 | proceeding on behalf of the Staff of the Missouri Public Service Commission (Staff)? | |
| 10 | A. Yes, I am. | |
| 11 | Q. What is the purpose of your true-up direct testimony? | |
| 12 | A. The purpose of this true-up direct testimony is to update my recommended | |
| 13 | capital structure for Missouri-American Water Company (MAWC) and provide | |
| 14 | revised overall rate of return (ROR) as of May 31, 2007. It is also to update the embedde | |
| 15 | costs of long-term debt, short-term debt and preferred stock to reflect the actual costs as of | |
| 16 | May 31, 2007. | |
| 17 | Q. Could your true-up direct testimony have been filed on the same date as | |
| 18 | rebuttal testimony (July 13, 2007), which is when it was supposed to be filed according to the | |
| 19 | procedural schedule? | |
| 20 | A. No. MAWC did not provide me with American Water's financial statements | |
| 21 | as of the update period (December 31, 2006) or the true-up period (May 31, 2007) until | |
| 22 | July 12 and July 13 respectively. This did not allow me adequate time to review this | |
| 23 | information and still file rebuttal and true-up direct testimony. However, I have now beer | |

| | True-Up Direct Testimony of David Murray | | |
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| 1 | able to analyze this information and update my recommendation based on information as of | | |
| 2 | the true-up date. | | |
| 3 | Q. | Have the financial statements that you relied upon for your updated | |
| 4 | recommendation been audited? | | |
| 5 | A. | No. Therefore, it is possible that these financial statements may be revised in | |
| 6 | the future. | | |
| 7 | CAPITAL S | STRUCTURE CONTROL OF THE STRUCTURE | |
| 8 | Q. | Did you perform an analysis of American Water's capital structure | |
| 9 | (your recommended ratemaking capital structure for MAWC) as of May 31, 2007? | | |
| 10 | A. | Yes, I did. | |
| 11 | Q. | What was the result of your analysis? | |
| 12 | A. | As of May 31, 2007, American Water's capital structure was as follows: | |
| 13 | ** | | |
| 14 | | ** | |
| 15 | Q. | What is the primary difference in the capital structure as of the true-up | |
| 16 | date compared to the test year? | | |
| 17 | A. | ** | |
| 18 | | | |
| 19 | | ** compared to less than 30 percent | |
| 20 | in the capital structure I recommended in my direct testimony. | | |
| 21 | Q. | What caused such a significant change in American Water's capital | |
| 22 | structure? | | |

| | True-Up Direct Testimony of David Murray | | |
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| 1 | A. ** | | |
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| 12 | | | |
| 13 | ** | | |
| 14 | Q. Are there any other possible changes that may occur to American Water's | | |
| 15 | capital structure after it is spun-off? | | |
| 16 | A. Yes. Based on MAWC's response to Staff Data Request No. 101.1, American | | |
| 17 | Water plans to refinance ** ** that Staff currently has in its | | |
| 18 | recommended capital structure (the rest of the preferred stock is held at American Water's | | |
| 19 | subsidiaries). However, because the timing and the terms of this event are uncertain, Staff | | |
| 20 | has decided to use the known capital components at May 31, 2007, the Commission ordered | | |
| 21 | true-up cut-off date, in its capital structure recommendation. | | |

| | True-Up Dia David Murra | rect Testimony of ay | |
|----|----------------------------------|--|--|
| 1 | EMBEDDED COST OF LONG-TERM DEBT | | |
| 2 | Q. | Did you perform an analysis of the embedded cost of long-term debt as of | |
| 3 | May 31, 2007? | | |
| 4 | A. | Yes, I did. | |
| 5 | Q. | What was the result of your analysis? | |
| 6 | A. | As of May 31, 2007, Staff recommends an embedded cost for long-term debt | |
| 7 | of ** | ** (see Schedule 2). | |
| 8 | EMBEDDED COST OF PREFERRED STOCK | | |
| 9 | Q. | Did you perform an analysis of the embedded cost of preferred stock as of | |
| 10 | May 31, 200 | 07? | |
| 11 | A. | Yes, I did. | |
| 12 | Q. | What was the result of your analysis? | |
| 13 | A. | As of May 31, 2007, Staff recommends an embedded cost for preferred stock | |
| 14 | of ** | ** (see Schedule 3). | |
| 15 | <u>OVERALL</u> | RATE OF RETURN | |
| 16 | Q. | What effect did your changes to capital structure and embedded costs have on | |
| 17 | your recommended ROR for MAWC? | | |
| 18 | A. | My recommended ROR for MAWC has increased. Staff recommends a ROR | |

NP

cost of common equity of 8.60 percent to 9.60 percent with a midpoint of 9.10 percent.

How has this ROR recommendation been incorporated in the determination of

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21

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range of **

Q.

revenue requirement in this case?

** (see Schedule 4) based on my original estimated

True-Up Direct Testimony of David Murray

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- A. The Supplemental True-up Direct Testimony of Staff witness Stephen M. Rackers discusses the revenue requirement resulting from this ROR recommendation.
 - Q. Does this conclude your prepared true-up direct testimony?
- 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) |
|--|---|
| AFFIDAVIT OF I | DAVID MURRAY |
| STATE OF MISSOURI)) ss. COUNTY OF COLE) | |
| preparation of the following True-up Testim of pages to be presented in the a True-up Testimony were given by him; that | nis oath states: that he has participated in the ony in question and answer form, consisting bove case; that the answers in the following he has knowledge of the matters set forth in and correct to the best of his knowledge and |
| | Durid Muns |
| | David Murray |
| Subscribed and sworn to before me this/ | 9th day of July, 2007. |
| D. SUZIE MANKIN Notary Public - Notary Seal State of Missouri County of Cole My Commission Exp. 07/01/2008 | Motary Public |

SCHEDULES 1 through 4

HAVE BEEN DEEMED

PROPRIETARY

IN ITS ENTIRETY