

Exhibit No.:  
Witness: Michael Gorman  
Type of Exhibit: Rebuttal Testimony  
Issue: Rate Design  
Sponsoring Parties: Missouri Industrial Energy Consumers  
Case No.: WR-2008-0311

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

<u>In the Matter of Missouri-American</u>	)	
<u>Water Company's Request for</u>	)	
<u>Authority to Implement a General Rate</u>	)	Case No. WR-2008-0311
<u>Increase for Water and Sewer Service</u>	)	
<u>Provided in Missouri Service Areas</u>	)	

Rebuttal Testimony of

**Michael Gorman  
on Rate Design Issues**

On Behalf of

**Missouri Industrial Energy Consumers**



September 30, 2008  
Project 8980

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

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)  
)  
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Case No. WR-2008-0311

STATE OF MISSOURI       )  
                                      )  
COUNTY OF ST. LOUIS    )       SS

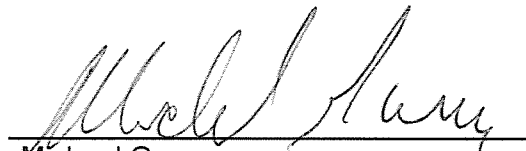
**Affidavit of Michael Gorman**

Michael Gorman, being first duly sworn, on his oath states:

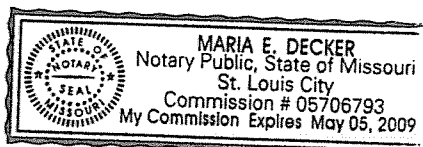
1. My name is Michael Gorman. I am a consultant with Brubaker & Associates, Inc., having its principal place of business at 16690 Swingley Ridge Road, Suite 140, Chesterfield, MO 63017. We have been retained by the Missouri Industrial Energy Consumers in this proceeding on their behalf.

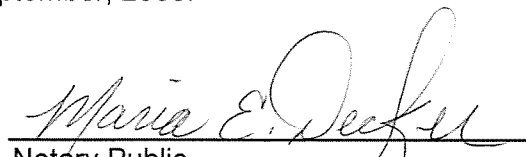
2. Attached hereto and made a part hereof for all purposes is my rebuttal testimony on rate design issues, which was prepared in written form for introduction into evidence in Missouri Public Service Commission Case No. WR-2008-0311.

3. I hereby swear and affirm that the testimony is true and correct and that it shows the matters and things it purports to show.

  
\_\_\_\_\_  
Michael Gorman

Subscribed and sworn to before me this 29th day of September, 2008.



  
\_\_\_\_\_  
Notary Public

**BEFORE THE PUBLIC SERVICE COMMISSION  
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<b>In the Matter of Missouri-American</b>	)	
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**Rebuttal Testimony of Michael Gorman**

1    **Q     PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2    A     My name is Michael Gorman and my business address is 16690 Swingley Ridge  
3           Road, Suite 140, Chesterfield, MO 63017.

4    **Q     ARE YOU THE SAME MICHAEL GORMAN WHO PREVIOUSLY SUBMITTED**  
5           **TESTIMONY IN THIS CASE?**

6    A     Yes.

7    **Q     WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

8    A     I will respond to Staff's cost of service study and proposed rate design for the  
9           St. Louis County District as included in the document "Staff Report Class Cost-Of-  
10          Service & Rate Design, September 3, 2008 sponsored by Staff witness James M.  
11          Russo.

12   **Q     PLEASE SUMMARIZE YOUR COMMENTS CONCERNING MR. RUSSO'S COST**  
13          **OF SERVICE AND RATE DESIGN FOR THE ST. LOUIS COUNTY DISTRICT.**

14   A     Mr. Russo's cost of service is severely flawed and should not be relied upon.

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1 Mr. Russo's cost of service study produces an incorrect and flawed allocation of costs  
2 between customer classes in the St. Louis County District. Flaws in his cost of  
3 service study include the following:

- 4 1. Mr. Russo agrees that mains should be functionalized as Distribution and  
5 Transmission, but he nevertheless allocates significant costs associated with  
6 small distribution mains to customers that are not connected to small mains. The  
7 Company found that only approximately 1.3% of distribution mains are used to  
8 provide service to Rate J customers. Staff has not provided any evidence to  
9 refute this finding and has simply allocated significant costs to Rate J customers  
10 despite the non-contested findings that distribution mains are not and cannot  
11 serve large customers. As such, Mr. Russo has significantly over-allocated the  
12 distribution main costs to Rate J customers, and under-allocated these costs to  
13 customers that actually use these small distribution mains.
- 14 2. Staff fails to include a max-hour component in its Allocation Factor 6. This is  
15 inconsistent with what the Company has done, and what is normal practice for  
16 allocating pumping equipment, and other equipment that are sized to meet  
17 peak-day and peak-hour conditions. As a result, Staff's analysis improperly  
18 allocates pumping equipment costs between classes because the allocation factor  
19 does not properly differentiate between average, peak-day and peak-hour loads.
- 20 3. Inexplicably, Staff inflated transmission mains and distribution mains costs relative  
21 to what the Company included in its filing. Specifically, for the St. Louis County  
22 District, the Company cost study included \$2.16 million of transmission and  
23 distribution main costs in its cost of service study for the St. Louis Metro District.  
24 In contrast, Staff had over \$3.96 million in main costs for the smaller St. Louis  
25 County District. This inexplicable increase in main costs resulted in a  
26 misallocation of these costs between customer classes.
- 27 4. Staff also had a significantly different contract sales revenue included in its cost  
28 study relative to the Company. The Company showed contract sales for the  
29 St. Louis Metro District of over \$3 million. In contrast, Staff included only  
30 \$857,000 of contract sales revenue for the St. Louis County District. Again, the  
31 Districts were not directly compatible but this differential is large enough that Staff  
32 should explain it. If Staff significantly understated the amount of contract revenue  
33 available to Missouri-American, it has over-allocated the amount of revenue  
34 needed to be recovered through retail rates.
- 35 5. Staff reallocated fire hydrant costs, or Rate E costs, to other customers rather  
36 than leaving the fire hydrant rate as a stand-alone class. Similarly, Staff allocated  
37 Rate D sales for resale, among other classes rather than leaving it as a stand-  
38 alone rate class. Staff's proposal prevents the Commission from ensuring that the  
39 rates for Rate E and Rate D customers fully reflect their cost of service, because  
40 Staff's cost of service fails to establish the level of rates appropriate for Rate E  
41 and Rate D customers. Further, by misallocating the development of rates for  
42 these two rate classes, Staff's cost of service study then creates subsidies

1                   between rate classes and those for Rate E and Rate D customers. This  
2                   subsidization is inappropriate and should not be allowed.

3    **Q       HOW DO YOU PROPOSE TO MODIFY STAFF'S COST OF SERVICE STUDY?**

4    A       There are so many flaws in Staff's cost of service study that I have not been able to  
5           properly adjust it to reasonably allocate Missouri-American's cost of service for the  
6           St. Louis County District between rate classes. Therefore, I recommend Staff's cost  
7           of service study be rejected.

8    **Q       DID STAFF CONTEST THE COMPANY'S FINDING THAT TRANSMISSION MAINS**  
9           **SHOULD BE CONSIDERED MAINS 10 INCHES AND LARGER, AND**  
10          **DISTRIBUTION MAINS SHOULD BE CONSIDERED MAINS SMALLER THAN**  
11          **10 INCHES?**

12   A       No. In the Staff Report, Class Cost-Of-Service & Rate Design, Pages 6-7, Staff  
13           asserts that the main distinction between transmission mains and distribution mains is  
14           based on function and is not based on size. It states that all mains are used to  
15           provide service to customers, and where larger mains are used to directly serve  
16           customers, they should be considered to provide a distribution function.

17   **Q       IS STAFF'S BELIEF THAT CUSTOMERS TAKING SERVICE OFF LARGE MAINS**  
18          **MEANS THAT ALL MAINS PROVIDE DISTRIBUTION FUNCTION ACCURATE?**

19   A       No. Staff's simplistic assessment does not properly recognize that the Company  
20           manages its cost of service by installing Transmission mains to service all customers  
21           but installs smaller Distribution mains for the final distribution and connection to  
22           smaller customers. A company that takes service from a water meter that is directly

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1 connected to a transmission main, cannot physically take service from any of the  
2 Company's investment in distribution mains. Further, it would be imprudent and more  
3 expensive for the company to run a 10-inch transmission main down a residential  
4 street when a 4-inch distribution main is adequate to serve the customers on that line.  
5 Therefore, it is not appropriate to allocate all main costs to all customers irrespective  
6 of the size of the customer. Staff's allocation does not reflect cost-causation and is,  
7 therefore, flawed and inappropriate.

8 **Q DID STAFF CONTEST THE COMPANY'S FINDINGS THAT RATE J CUSTOMERS**  
9 **USE A VERY SMALL PERCENTAGE OF DISTRIBUTION MAINS?**

10 A No.

11 **Q HOW DID STAFF'S ALLOCATION OF DISTRIBUTION MAINS DIFFER FROM**  
12 **THAT OF MISSOURI-AMERICAN?**

13 A Staff's cost of service study had allocated 9.01% of small main costs to Rate J  
14 customers. In significant contrast, the Company allocated 0.84%. As set forth in my  
15 direct testimony, I recommend that 0.12% be allocated to Rate J customers. Staff's  
16 allocation of Distribution mains to Rate J customers is simply erroneous and should  
17 be rejected.

18 **Q HAS STAFF WITNESS RUSSO OFFERED ANY EVIDENCE THAT IT IS**  
19 **APPROPRIATE TO ALLOCATE RATE J CUSTOMERS A PERCENTAGE OF**  
20 **DISTRIBUTION MAINS HIGHER THAN WHAT YOU HAVE RECOMMENDED AND**  
21 **WHAT THE COMPANY HAS RECOMMENDED?**

22 A No. Indeed, Mr. Russo's testimony is completely silent on this issue.

1    **Q     WHAT IS THE IMPACT ON RATE J CUSTOMERS, FROM STAFF ALLOCATING**  
2           **DISTRIBUTION MAINS ABOVE THAT WHICH MISSOURI-AMERICAN USES TO**  
3           **SERVE THIS CLASS OF CUSTOMERS?**

4    A     Staff's over-allocation of distribution mains to Rate J customers increased Rate J  
5           customers' cost of service by approximately \$4.99 million relative to my  
6           recommended distribution main cost allocation to this rate class.

7    **Q     DO YOU HAVE ANY OTHER ISSUES WITH STAFF'S COST OF SERVICE**  
8           **STUDY?**

9    A     Yes, Staff's development of Allocation Factor 6 is flawed. This factor is used to  
10          allocate pumping equipment and expenses. This factor is flawed because Staff did  
11          not include a max-hour component in the allocation factor. This is erroneous,  
12          because pumping equipment investment is sized for max hour and the expenses are  
13          increased due to max-hour conditions. Therefore, Staff's development of Allocation  
14          Factor 6 is flawed and its cost study is not reliable.

15   **Q     DID STAFF EXPLAIN WHY IT EXCLUDED MAX-HOUR FACTORS IN**  
16          **CONSTRUCTING ALLOCATION FACTOR 6?**

17   A     No.

18   **Q     DO YOU HAVE ANY ADDITIONAL CONCERNS WITH STAFF'S COST OF**  
19          **SERVICE STUDY?**

20   A     Yes. In contrast to the Company's cost study, Staff inappropriately allocated  
21          customer-related expenses on the basis of total operating expenses rather than on

1 the number of customers. This inappropriately allocated significant customer-related  
2 expenses to the largest customers.

3 **Q DID STAFF WITNESS RUSSO PROVIDE AN EXPLANATION OF WHY HE**  
4 **ALLOCATED CUSTOMER BILLINGS USING A PERCENT OF TOTAL**  
5 **OPERATING EXPENSES RATHER THAN NUMBER OF CUSTOMERS TO**  
6 **ALLOCATE CUSTOMER BILLINGS?**

7 **A** No.

8 **Q DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

9 **A** Yes.

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