Exhibit No.:	
Issues:	Future Test Year
Witness:	John M. Watkins
Exhibit Type:	Rebuttal-Rate Design
Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2020-0344
Date:	January 22, 2020

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-2020-0344

REBUTTAL TESTIMONY
RATE DESIGN

OF

JOHN M. WATKINS

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

AFFIDAVIT

I, John M. Watkins, under penalty of perjury, and pursuant to Section 509.030, RSMo, state that I am Senior Director Regulatory Services for American Water Works Service Company, that the accompanying testimony has been prepared by me or under my direction and supervision; that if inquiries were made as to the facts in said testimony, I would respond as therein set forth; and that the aforesaid testimony is true and correct to the best of my knowledge and belief.

John M. Watkins

January 22, 2021

REBUTTAL TESTIMONY
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JOHN M. WATKINS
MISSOURI-AMERICAN WATER COMPANY
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REBUTTAL TESTIMONY

JOHN M. WATKINS

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is John M. Watkins. My business address is 1 Water Street, Camden, NJ 08102.

Q. On whose behalf are you submitting this testimony?

A. Missouri-American Water Company ("MAWC" or "the Company").

Q. Did you previously provide Direct Testimony and Revenue Requirement Rebuttal Testimony in this proceeding?

A. Yes.

Q. What is the purpose of your Rate Design Rebuttal Testimony?

A. The purpose of my rate design rebuttal testimony is to address the appropriateness of utilizing a Revenue Stabilization Mechanism ("RSM") in response to the criticisms raised by Missouri Industrial Energy Consumers ("MIEC") witness Greg Meyer in his direct testimony regarding rate design.

II. REVENUE STABILIZATION MECHANISM

Q. Do any witnesses address the Company's proposed use of a RSM in their rate design direct testimony?

A. Yes. MIEC witness, Greg Meyer, addresses and objects to the Company's use of a RSM based on various criticisms. Those criticisms are misplaced and, in many cases, actually serve to demonstrate why the RSM is a particularly appropriate ratemaking mechanism for a water company.

Q. What customers classes are included in the Company's proposed RSM?

A. As stated in my direct testimony on page 16, the classes included in the Company's proposed RSM are residential, commercial, other public authorities (OPA) and sale for resale.

Q. Are industrial customers included in the RSM?

A. No. As stated in my Direct Testimony, "Industrial customers would be excluded from the RSM." (Watkins DT, p. 16, lines 12-13).

Q. Would any credit or surcharge impact industrial customers?

A. No. Industrial customers are excluded from the RSM and, therefore, they would not be impacted by any change to the RSM.

Q. Is Mr. Meyer correct in his statement that customers "get charged for water whether they use that water or not"? (Meyer DT, p. 2).

A. No, he is not correct. Customers are billed the rates authorized by the Commission, no more, no less. If a customer uses less water, they will be billed for the actual amount of water they use. Likewise, if a customer uses more water, they will be billed for that amount of water.

Q. How does the RSM reconciliation work?

A. The RSM, as proposed, would provide a credit to customers if the actual revenues less production costs are more than what was authorized by the Commission in setting rates.

Likewise, if the actual revenues less production costs are less than authorized a surcharge would be issued.

Q. Does this reconciliation therefore charge the customers for water whether they use it or not?

A. No, the reconciliation corrects the authorized rates for the actual usage that was incurred for the applicable time period. Since the usage for any future 12 month period is unknown, the revenue requirement that is established in the case will not actually be achieved, the revenues collected will either be more or less than the approved revenues based on actual water sales. As shown in Schedule JMW-1, filed with my Direct Testimony, 7 out of the 10 years (2010-2019) revenues were less than authorized. In total for the 10 years, revenues were $52.4 million less than authorized. The RSM reconciles the authorized revenues less production costs to the actual revenues less production costs. As proposed, a surcharge or credit will be issued to ensure only the amount authorized was actually collected. Thus, the RSM adjusts the rates authorized to what they should have been if the actual usage was known at the time rates were implemented. The RSM allows the price to flow up or down as sales volumes change in between rate cases.

Q. Does Mr. Meyer take issue with including production costs as part of the RSM?

A. Yes.

Q. Do you agree with Mr. Meyer's proposal to eliminate production costs from the RSM?

A. No, I do not. Production costs should be taken into account because they vary with sales volumes. Delivering more water costs more and delivering less water costs less. Netting production costs will ensure that both the Company and its customers are made whole; paying only those production costs associated with the actual amount of water delivered.

Q. Can you provide an example of why it makes sense to include production costs in the RSM?

A. Yes. Assume that revenues fall short of authorized by $5,000,000 due to water sales being 1,000,000 thousand gallons less than authorized at a cost of $5 per thousand gallons. If we ignore production cost in this example, the Company would surcharge the customers $5 million. But this is not the right thing to do because it costs the Company money to produce water, or in this case the Company saves money by not producing the amount of water authorized. If the cost per thousand gallons was $1 in this example, then the Company would over collect by $1 million. The reason for this is that the Company did not produce 1,000,000 thousand gallons at a cost of $1 per thousand gallons. The Company's proposal would have taken the $5 million shortfall in revenues and offset it with the $1 million savings in production costs, therefore it would have only charged the customers $4 million dollars instead of the $5 million ignoring production costs.

Q. Would the same thing occur if the RSM was in a credit position?

A. Yes, but it would be opposite. For example, assume that revenues exceed authorized by $5,000,000 due to water sales being 1,000,000 thousand gallons more than authorized at a cost of $5 per thousand gallons. If we ignore production cost in this example, the Company would credit the customers $5 million. But this is not the right thing to do because it costs the Company money to produce the additional water sold. If the cost per thousand gallons was $1 in this example, then the Company would credit the customers $1 million too much. The reason for this is that the Company produced an additional 1,000,000 thousand gallons at a cost of $1 per thousand gallons that was not included in authorized revenues. The Company's proposal would have taken the $5 million increase in revenues and offset it with the additional $1 million in production costs, therefore it would have only credited the customers $4 million dollars instead of the $5 million ignoring production costs.

Q. Does Mr. Meyer propose a change to the Company's proposed RSM methodology?

A. Yes. Mr. Meyer discusses taking the annualized level of production costs and dividing them by water sales. He then proposes "the rate per K gallon of production costs should be subtracted from all revenue adjustments made in the RSM in between rate cases." (Meyer DT, p. 11).

Q. Do you agree with Mr. Meyer's recommendation?

A. No. If the total of the production costs divided by water sales is $1, it's unclear how subtracting the $1 from all revenue adjustments would eliminate the production costs from the calculation. Doing so would also allow the Company to surcharge more money or refund more money than appropriate. Please refer to the examples shown previously in this Rebuttal Testimony that show how and why production costs impact the RSM calculation.

Q. Is the Company's proposal the preferred RSM methodology to use?

A. Yes, I believe the Company's proposal is the best method. It allows all numbers to be verified easily by reviewing the billed revenues for the residential, commercial, OPA and Resale customers as well as the production costs booked by the Company.

Q. Are there alternative methodologies the Company could use to quantify the RSM?

A. Yes. Another alternative is to use a cost per thousand gallons established in the rate case and multiply that cost by the actual usage level incurred. Therefore, if the Company in the example above sold an additional 1,000,000 thousand gallons and the cost authorized in the rate case was $1 per thousand gallons, it would be able to offset the additional revenues by the $1 million in expenses (1,000,000 thousand gallons x $1 cost per thousand set in rate case). Also, if the Company in the example fell short of authorized sales by 1,000,000 thousand gallons, it would reduce its request by $1 million in expense savings (1,000,000 thousand gallons x $1 cost per thousand set in rate case).

Q. Mr. Meyer states that the Company is "hiding the fact that it wants to continually adjust production costs in between rate cases through the RSM". (Meyer DT, p. 12). Is this true?

A. No. There is nothing hidden in the Company's proposal. The actual costs incurred would flow through the adjustment. The customers would pay the actual cost of the production costs, no less and no more. The RSM adjusts water sales and the costs to produce the water. Changing just water sales either overstates a surcharge or overstates a credit.

Q. Do American Water subsidiaries operate any RSM or similar mechanism in other states in which they operate?

A. Yes, American Water has RSMs in three states (CA, IL and NY).

Q. Do these three states reconcile production costs?

A. Yes, all three make an adjustment for production costs.

Q. Does Mr. Meyer agree with how the Company proposes to credit customers through

the RSM?

A. No, Mr. Meyer believes that any adjustment should be volumetric based.

Q. Did the Company address why a onetime credit is preferred?

A. Yes, in my direct testimony, on page 18, I stated:

> A one-time credit that is equal to all customers would benefit the lower-usage customers at a greater percentage, rewarding customers who conserve water at a higher percentage than those that use more water. For example, in the 2012 RSM calculation (see Schedule JMW-1), the credit for 2012 would have been $11.2 million. Assuming the customer count for RSM customers is 471,823, then the one-time credit per customer would be $23.82 ($11,239,647/471,823).

Q. Has your opinion changed since your Direct Testimony?

A. No. The Company's proposal remains the best method for a credit because it benefits the customers that use less water. A surcharge would be based on a volumetric charge which also ensures that the lower-usage customers would continue to benefit from their conservation because the volumetric rate would be equal for the entire Company. "Therefore, if a customer conserves water, he or she will save more money not only on the current bill, but also on any adjustment applied the following year. No matter what happens with sales, customers who use less will pay less." (Watkins DT, p. 18).

Q. Does this conclude your Rate Design Rebuttal Testimony?

A. Yes.