

Exhibit No.: _____
Issue(s): Fire Hydrant Painting Project
OPEB Permanent Investment
Unamortized Security AAO Balance and ADIT
Witness/Type of Exhibit: Robertson/Rebuttal
Sponsoring Party: Public Counsel
Case No.: WR-2008-0311

REBUTTAL TESTIMONY
OF
TED ROBERTSON

Submitted on Behalf of the Office of the Public Counsel

MISSOURI-AMERICAN WATER COMPANY

CASE NO. WR-2008-0311

September 30, 2008

**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 and Sewer Service Provided in)
Missouri Service Areas.)


Case No. WR-2008-0311

AFFIDAVIT OF TED ROBERTSON

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

Ted Robertson, of lawful age and being first duly sworn, deposes and states:

1. My name is Ted Robertson. I am a Public Utility Accountant for the Office of the Public Counsel.
2. Attached hereto and made a part hereof for all purposes is my rebuttal testimony.
3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.



Ted Robertson, C.P.A.
Public Utility Accountant III

Subscribed and sworn to me this 30th day of September 2008.





Kathleen Harrison
Notary Public

My Commission expires January 31, 2010.

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MISSOURI AMERICAN WATER COMPANY
CASE NO. WR-2008-0311

A. Ted Robertson, PO Box 2230, Jefferson City, Missouri 65102-2230.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by the Missouri Office of the Public Counsel (OPC or Public Counsel) as a Public Utility Accountant III.

Q. WHAT IS THE NATURE OF YOUR CURRENT DUTIES AT THE OPC?

A. Under the direction of the OPC Chief Public Utility Accountant, Mr. Russell W. Trippensee, I am responsible for performing audits and examinations of the books and records of public utilities operating within the state of Missouri.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND OTHER QUALIFICATIONS.

A. I graduated in May, 1988, from Missouri State University with a Bachelor of Science Degree in Accounting. In November of 1988, I passed the Uniform Certified Public Accountant Examination and I obtained Certified Public

1 Accountant (CPA) certification from the state of Missouri in 1989. My CPA
2 license number is 2004012798.

3
4 Q. HAVE YOU RECEIVED SPECIALIZED TRAINING RELATED TO PUBLIC
5 UTILITY ACCOUNTING?

6 A. Yes. In addition to being employed by the Missouri Office of the Public Counsel
7 since July 1990, I have attended the NARUC Annual Regulatory Studies
8 Program at Michigan State University and I have participated in numerous
9 training seminars relating to this specific area of accounting study.

10
11 Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE MISSOURI PUBLIC
12 SERVICE COMMISSION (COMMISSION OR MPSC)?

13 A. Yes, I have testified on numerous issues before this Commission. Please refer
14 to Schedule TJR-1, attached to this testimony, for a listing of cases in which I
15 have submitted testimony.

16
17 **II. PURPOSE OF TESTIMONY**

18 Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

19 A. I will rebut the direct testimony of Company witnesses Mr. Frank I. Kartmann
20 regarding his proposal for a new fire hydrant painting project and Mr. Tyler T.
21 Bernsen regarding rate base treatment of certain postretirement benefits other

1 than pensions (OPEB) and unamortized costs deferred pursuant to a security
2 accounting authority order.

3
4 **III. FIRE HYDRANT PAINTING PROJECT**

5 Q. WHAT IS THE ISSUE?

6 A. Mr. Kartmann has proposed an adjustment to support a fire hydrant lead based
7 paint abatement and repainting project for 17,000 fire hydrants in St. Louis
8 County. He estimates the cost at \$250 per hydrant for total cost of \$4,250,000
9 or \$1,417,000 over a three-year life of the project. Public Counsel recommends
10 that the Commission not authorize the request.

11
12 Q. WHY IS THE COMPANY REQUESTING THE COMMISSION AUTHORIZE THE
13 FUNDING FOR THE PROPOSED PROJECT?

14 A. Company states that the hydrants' condition warrant special attention because,
15 1) peeling/flaking pose environmental hazard; 2) current coating makes poor
16 candidate for over coating; and 3) poor appearance.

1 Q. IS COMPANY'S INTENTION TO PURSUE THE PROJECT CONDITIONAL?

2 A. Yes. Subject to regulatory approval, Company would execute a contract on or
3 before the true-up date of this case and begin work as early as January 2009.
4 Mr. Kartmann states the project would be contracted to sandblast each hydrant,
5 in place, then repaint in compliance with EPA and MoDNR requirements for
6 containment and disposal. Company will not perform work if it does not receive
7 authorization for recovery of the expense in this rate case (Kartmann Direct
8 Testimony, p. 29, lines 12-15).

9
10 Q. WHY DOES PUBLIC COUNSEL OPPOSE THE COMPANY'S REQUEST FOR
11 FUNDING OF THE PROPOSED PROJECT?

12 A. In essence, since the costs have not been incurred, Company is requesting that
13 the Commission authorize a recovery of forecasted cost estimates. Public
14 Counsel does not believe that rates should be determined based on costs that do
15 not yet exist. Further, our position is supported by the fact that the Company has
16 the responsibility to perform required repairs and maintenance on its
17 infrastructure at all times. If the condition of the hydrants is such that they do not
18 fulfill their intended purpose and/or are a threat to the safety of the public, then
19 Company should have been addressing and correcting the problem in an
20 ongoing manner prior to this rate case. If it had, actual rehabilitation expenses
21 (not estimates) would have been incurred and likely included in the development

1 of an annual level of ongoing maintenance cost. Maintenance cost is a normal
2 utility expense that is always included in the development of rates. Thus, no
3 special ratemaking treatment of the proposed project is required to facilitate the
4 needs expressed by the utility.

5
6 **IV. OPEB PERMANENT INVESTMENT**

7 Q. WHAT IS THE ISSUE?

8 A. Mr. Bernsen has proposed that certain OPEB contributions authorized as
9 "permanent investment" by the Commission in Case No. WR-95-205 be included
10 in the determination of rate base. On page 4, lines 11-13, of his direct testimony,
11 he states:

12
13 The post-employment benefits ("OPEBs") contributed to external
14 funds included permanent investment recognized by the
15 Commission in Case No. WR-95-205.
16
17

18 Public Counsel recommends that the Commission authorize the Company to
19 begin amortizing the balance to expense over a period not less than five years
20 subject to certain conditions.

21
22 Q. WHAT DO THE CONTRIBUTIONS REPRESENT?

1 A. On page twenty-three of the *Report and Order* in Case No. WR-95-2005 the
2 Commission stated:

3
4 In August 1993, the Company began making quarterly contributions
5 to the three VEBAs for OPEBs based upon Towers Perrin actuarial
6 reports. These contributions represent cash contributions to the
7 three VEBAs for the sole benefit of the employees. They represent
8 actual expenditures made by the Company and are not available
9 for any other purpose. Moreover, these contributions earn a return
10 which helps to reduce future OPEB costs that will be reflected in
11 future costs of service.
12
13

14 Q. WHAT IS THE OPEB PERMANENT INVESTMENT BALANCE?

15 A. On page twenty-five of the aforementioned *Report and Order* it states:

16
17 Therefore, the Commission finds that it is appropriate that the
18 contributions which are the net of the PAYGO and the capitalized
19 portions of OPEBs should be included in the Company's rate base.
20 Based upon these findings, the Commission finds, in conclusion,
21 that Missouri-American's proposed FAS 106 proposition will benefit
22 current and future ratepayers and that it is in the public interest.
23 The Commission will approve the \$752,918 adjustment jointly
24 proposed by the Company and Staff.
25
26

27 Q. WHY IS PUBLIC COUNSEL PROPOSING THAT THE RATEMAKING
28 TREATMENT OF THE OPEB PERMANENT INVESTMENT BE MODIFIED?

29 A. The recent trend in ratemaking for pension and OPEB costs has seen an
30 increase in the number of cost tracker mechanisms, and related amortization

1 processes, that differ in one degree or another among the various large Missouri-
2 regulated utilities. The number of trackers along with their individual complexities
3 has created a situation where the determination of these costs for ratemaking
4 purposes has become more complicated, particularly as individuals (i.e.,
5 company and regulators) involved in their development have left their respective
6 employers. Public Counsel's proposal is merely an attempt to simplify the
7 accounting and ratemaking process for this cost as it relates to this utility.
8

9 Q. WHAT ARE THE CONDITIONS UPON WHICH THE AMORTIZATION SHOULD
10 BE AUTHORIZED IF PUBLIC COUNSEL'S PROPOSAL IS APPROVED BY THE
11 COMMISSION?

12 A. So that neither shareholder or ratepayer are harmed in any way, Public Counsel
13 proposes only two conditions. Effective with the date of a rate change for the last
14 Company rate case prior to the balance becoming fully amortized, the remaining
15 balance amortization amount will be recalculated so that the remaining balance
16 will become fully amortized effective with the date of a rate change in the next
17 subsequent rate case and that the cost of service upon which that rate change is
18 determined will not include any remaining balance in rate base or amortization
19 amount in expense.
20

1 For example, if the Commission approved an amortization period of five years, in
2 the current case, the annual amount included in expense would approximate
3 \$150,584. If Company implements a rate change based on a test period four
4 and one-half years later, only four and one-half years of the contribution (i.e.,
5 \$677,626) would have been recovered in rates as an expense. Public Counsel's
6 conditions would recalculate the future amortization of the remaining balance -
7 \$75,291 (i.e., \$752,918 less \$677,626) - so that it would be fully expensed based
8 on the effective date of its next rate case rate change.

9
10 **V. UNAMORTIZED SECURITY AAO BALANCE AND ADIT**

11 Q. WHAT IS THE ISSUE?

12 A. Mr. Bernsen has proposed that the unamortized costs associated with a security
13 accounting authority order (AAO) be included in the determination of Company's
14 rate base. On page 4, lines 18-21, of his direct testimony, he states:

15
16 Finally, the unamortized deferred cost associated with the
17 Company's security efforts was included in Rate Base. These
18 costs are being amortized over a ten year period as approved in
19 Case No. WO-2002-273.
20
21

22 Public Counsel recommends that the Commission not authorize the inclusion of
23 the unamortized AAO balance in rate base.

1
2 Q. DID THE COMMISSION ORDER IN CASE NO. WO-2002-273 AUTHORIZE
3 INCLUDING THE UNAMORTIZED AAO BALANCE IN RATE BASE?

4 A. No. Other than providing for an amortization over a ten-year period, the
5 Commission did not authorize any ratemaking treatment of the costs deferred
6 pursuant to the AAO. On page 42 of the *Report and Order On Remand* in Case
7 No. WO-2002-273, it states:

8
9 4. That the application for an Accounting Authority Order filed
10 by Missouri-American Water Company and its predecessors
11 on December 10, 2001, is granted as further specified
12 herein.

13
14 5. That Missouri-American Water Company is hereby granted
15 authority to defer and book to Account 186 expenditures
16 relating to security improvements and enhancements
17 beginning September 11, 2001, and continuing through
18 September 11, 2003.

19
20 6. That Missouri-American Water Company shall, upon the
21 effective date of this Order, immediately begin the
22 amortization over a ten-year period of any amount deferred
23 under the authority granted in this order.

24
25 7. That nothing in this Order shall be considered a finding by
26 the Commission of the value or prudence for ratemaking
27 purposes of the properties, transactions and expenditures
28 herein involved. The Commission reserves the right to
29 consider any ratemaking treatment to be afforded the
30 properties, transactions and expenditures herein involved in
31 a later proceeding.
32

1 8. That this Report and Order on Remand shall become
2 effective on November 20, 2004.

3
4 (Emphasis by OPC)
5
6

7 Q. WHAT IS THE UNAMORTIZED AAO BALANCE AS OF MARCH 31, 2008?

8 A. The AAO balance, as of March 31, 2008, is \$2,523,696.
9

10 Q. WHY DOES PUBLIC COUNSEL OPPOSE THE COMPANY'S REQUEST FOR
11 RATE BASE TREATMENT OF THE UNAMORTIZED AAO BALANCE?

12 A. The rationale for this position is that the Company is being given an effective
13 guaranteed "return of" the AAO deferred costs. It should not be allowed to earn a
14 "return on" those same costs.
15

16 Q. WHY WOULD IT BE INAPPROPRIATE FOR THE COMPANY TO EARN A
17 RETURN ON THE UNAMORTIZED AAO BALANCE?

18 A. The rationale for not including the unamortized AAO balance in rate base is
19 grounded in the view that the AAO process is allowing the utility to recover costs
20 in future rates which under the guidance of normal ratemaking would have been
21 recorded as an expense in a prior period, thus lowering the return on equity in
22 that period. The effect of the AAO is to increase historic earnings and future
23 cash flows. Allowing the unamortized balance in rate base would create the

1 situation of allowing the utility to achieve a return on equity earnings from a prior
2 period.

3
4 Furthermore, rates in Missouri are usually established based upon a historical
5 test period which focuses on four factors: (1) the rate of return the utility has an
6 opportunity to earn; (2) the rate base upon which a return may be earned; (3) the
7 depreciation expense related to plant and equipment; and (4) the allowable
8 operating expenses including income and other taxes. The security costs that
9 the Company was authorized to defer are already represented by each of those
10 four factors. What it seeks to gain by including the unamortized AAO balance in
11 rate base is an additional return on the remaining unamortized AAO balance.

12
13 Q. WHY SHOULD THE UTILITY NOT BE ALLOWED TO RECOVER THE
14 ADDITIONAL RETURN?

15 A. The AAO effectively eliminated the detrimental effects of the regulatory lag
16 Company's shareholders would have experienced absent its authorization. That
17 special accounting process, and ultimately ratemaking treatment, has benefited
18 shareholders enormously. Now, the utility requests authorization of an additional
19 return by implying that the unamortized AAO balance is an asset, similar in
20 nature to that of plant in service or a prepayment, that should be included in the
21 determination of rate base. However, it is Public Counsel's belief that the

1 unamortized AAO balance is not plant or a prepayment nor is it like any other
2 asset normally included in rate base. The unamortized AAO balance is nothing
3 more than the result of an abnormal accounting process that protects only
4 shareholders from the detrimental effects of regulatory lag. Further, there is little
5 precedent for allowing the additional return requested.

6
7 Q. WOULD COMMISSION AUTHORIZATION OF THE COMPANY'S REQUEST BE
8 UNFAIR TO RATEPAYERS?

9 A. Yes. To my knowledge, I know of no instance where a utility that was
10 overearning came to the Commission and requested that it be allowed to refund
11 the excess earnings to ratepayers due to rates being set at an inappropriately
12 high level. The one-sided nature of the current AAO process is grossly unfair to
13 ratepayers. Thus, Public Counsel believes that a sharing of the effects of the
14 regulatory lag associated with the AAO is in the best interests of both
15 shareholders and ratepayers. In order to obtain a small measure of fairness, I
16 believe that Company should continue to include in expenses a level of costs
17 pursuant to the amortization period authorized, but that the Commission not
18 approve the Company's request for rate base treatment of the unamortized AAO
19 balance.
20

1 Q. DOES PUBLIC COUNSEL BELIEVE THAT ACCUMULATED DEFERRED
2 INCOME TAXES (ADIT) ASSOCIATED WITH THE AMORTIZATION OF THE
3 AAO BALANCE SHOULD BE INCLUDED AS AN OFFSET IN THE
4 DETERMINATION OF RATE BASE?

5 A. Yes.
6

7 Q. WHY DOES PUBLIC COUNSEL BELIEVE THAT THE ASSOCIATED ADIT
8 SHOULD BE TREATED AS AN OFFSET TO RATE BASE?

9 A. Accumulated deferred income taxes are ratepayer supplied funds and therefore
10 are properly included as an offset in the determination of rate base. This is true
11 regardless of any subsequent regulatory treatment of the original costs that gave
12 rise to deferred income taxes. That is, a regulator's decision on whether or not a
13 cost incurred by a utility warrants rate base treatment has no relationship to the
14 cash provided to it by ratepayers for deferred income taxes. A decision by the
15 Commission to deny inclusion in rate base of the costs deferred pursuant to the
16 AAO does not change the fact that it is ratepayers which have provided the funds
17 to satisfy Company's tax requirements in conformance with the Internal Revenue
18 Service rules and regulations.
19

20 Q. PLEASE DESCRIBE DEFERRED INCOME TAXES AND WHY THEY ARE
21 TREATED AS AN OFFSET TO RATE BASE.

1 A. Deferred income taxes are the result of timing differences between when a
2 company deducts an expense on its tax return and when it deducts the expense
3 on its financial statement records (e.g., books or records utilized for ratemaking
4 purposes). In some cases the timing difference is permanent and in others, such
5 as where the utilization of accelerated depreciation occurs, it may have a
6 temporary effect. The Company's accumulated deferred tax reserve merely
7 represents a prepayment of income tax by ratepayers caused by the timing
8 differences.

9
10 For example, because Company is allowed to deduct depreciation expense on
11 an accelerated basis for income tax purposes, depreciation expense deducted on
12 its income tax return is greater than depreciation expense used for ratemaking
13 purposes. This results in a book-tax timing difference and a deferral of future
14 income taxes is created (i.e., ratepayers fund the full amount of the tax liability
15 but due to tax law Company gets to keep a portion of the funds for its own use
16 now, that it will actually pay to the taxing authority at a later date). Thus, the
17 credit balance booked in the accumulated deferred income tax account
18 represents a ratepayer-provided source of cost-free funds to the utility. In the
19 ratemaking process, rate base is reduced by the ADIT balance to avoid having
20 ratepayers pay a return on funds that they have already provided cost-free to the
21 Company.

1

2 Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

3 A. Yes, it does.

**CASE PARTICIPATION
OF
TED ROBERTSON**

<u>Company Name</u>	<u>Case No.</u>
Missouri Public Service Company	GR-90-198
United Telephone Company of Missouri	TR-90-273
Choctaw Telephone Company	TR-91-86
Missouri Cities Water Company	WR-91-172
United Cities Gas Company	GR-91-249
St. Louis County Water Company	WR-91-361
Missouri Cities Water Company	WR-92-207
Imperial Utility Corporation	SR-92-290
Expanded Calling Scopes	TO-92-306
United Cities Gas Company	GR-93-47
Missouri Public Service Company	GR-93-172
Southwestern Bell Telephone Company	TO-93-192
Missouri-American Water Company	WR-93-212
Southwestern Bell Telephone Company	TC-93-224
Imperial Utility Corporation	SR-94-16
St. Joseph Light & Power Company	ER-94-163
Raytown Water Company	WR-94-211
Capital City Water Company	WR-94-297
Raytown Water Company	WR-94-300
St. Louis County Water Company	WR-95-145
United Cities Gas Company	GR-95-160
Missouri-American Water Company	WR-95-205
Laclede Gas Company	GR-96-193
Imperial Utility Corporation	SC-96-427
Missouri Gas Energy	GR-96-285
Union Electric Company	EO-96-14
Union Electric Company	EM-96-149
Missouri-American Water Company	WR-97-237
St. Louis County Water Company	WR-97-382
Union Electric Company	GR-97-393
Missouri Gas Energy	GR-98-140
Laclede Gas Company	GR-98-374
United Water Missouri Inc.	WR-99-326
Laclede Gas Company	GR-99-315
Missouri Gas Energy	GO-99-258
Missouri-American Water Company	WM-2000-222
Atmos Energy Corporation	WM-2000-312
UtiliCorp/St. Joseph Merger	EM-2000-292
UtiliCorp/Empire Merger	EM-2000-369
Union Electric Company	GR-2000-512
St. Louis County Water Company	WR-2000-844
Missouri Gas Energy	GR-2001-292
UtiliCorp United, Inc.	ER-2001-672
Union Electric Company	EC-2002-1
Empire District Electric Company	ER-2002-424

**CASE PARTICIPATION
OF
TED ROBERTSON**

<u>Company Name</u>	<u>Case No.</u>
Missouri Gas Energy	GM-2003-0238
Aquila Inc.	EF-2003-0465
Aquila Inc.	ER-2004-0034
Empire District Electric Company	ER-2004-0570
Aquila Inc.	EO-2005-0156
Aquila, Inc.	ER-2005-0436
Hickory Hills Water & Sewer Company	WR-2006-0250
Empire District Electric Company	ER-2006-0315
Central Jefferson County Utilities	WC-2007-0038
Missouri Gas Energy	GR-2006-0422
Central Jefferson County Utilities	SO-2007-0071
Aquila, Inc.	ER-2007-0004
Laclede Gas Company	GR-2007-0208
Kansas City Power & Light Company	ER-2007-0291
Missouri Gas Utility, Inc.	GR-2008-0060
Empire District Electric Company	ER-2008-0093
Missouri Gas Energy	GU-2007-0480
Stoddard County Sewer Company	SO-2008-0289
Missouri-American Water Company	WR-2008-0311