

Exhibit No.:  
Issues: Cost Allocation Manual  
Witness: Edward J. Grubb  
Exhibit Type: Surrebuttal  
Sponsoring Party: Missouri-American Water Company  
St. Louis County Water Company  
d/b/a Missouri-American Water  
Company  
Jefferson City Water Works  
Company d/b/a Missouri-American  
Water Company  
Case No.: WM-2001-309  
Date: August 15, 2001

**MISSOURI PUBLIC SERVICE COMMISSION**

**CASE NO. WM-2001-309**

**SURREBUTTAL TESTIMONY**

**OF**

**EDWARD J. GRUBB**

**ON BEHALF OF**

**MISSOURI-AMERICAN WATER COMPANY,**

**ST. LOUIS COUNTY WATER COMPANY**

**D/B/A MISSOURI-AMERICAN WATER COMPANY, AND**

**JEFFERSON CITY WATER WORKS COMPANY**

**D/B/A MISSOURI-AMERICAN WATER COMPANY**

**FILED<sup>2</sup>**

**AUG 15 2001**

**Missouri Public  
Service Commission**

**JEFFERSON CITY, MISSOURI**

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

**IN THE MATTER OF THE JOINT )  
APPLICATION OF MISSOURI-AMERICAN )  
WATER COMPANY, ST. LOUIS COUNTY )  
WATER COMPANY D/B/A )  
MISSOURI-AMERICAN WATER COMPANY )  
AND JEFFERSON CITY WATER WORKS )  
COMPANY D/B/A MISSOURI-AMERICAN )  
WATER COMPANY FOR AUTHORITY TO )  
MERGE ST. LOUIS COUNTY WATER )  
COMPANY D/B/A MISSOURI-AMERICAN )  
WATER COMPANY AND JEFFERSON CITY )  
WATER WORKS COMPANY D/B/A )  
MISSOURI-AMERICAN WATER COMPANY )  
WITH AND INTO MISSOURI-AMERICAN )  
WATER COMPANY WITH AND INTO )  
MISSOURI-AMERICAN WATER COMPANY )  
AND, IN CONNECTION THEREWITH, )  
CERTAIN OTHER RELATED TRANSACTIONS )**

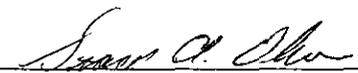
**CASE NO. WM-2001-309**

**AFFIDAVIT OF EDWARD J. GRUBB**

Edward J. Grubb, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Surrebuttal Testimony of Edward J. Grubb"; that said testimony was prepared by him and/or under his direction and supervision; that if inquiries were made as to the facts in said testimony, he would respond as therein set forth; and that the aforesaid testimony is true and correct to the best of his knowledge.

  
\_\_\_\_\_  
Edward J. Grubb

State of Missouri  
County of St. Louis  
SUBSCRIBED and sworn to  
before me this 13<sup>th</sup> day of August 2001.

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

My commission expires:

STACI A. OLSEN  
Notary Public - Notary Seal  
STATE OF MISSOURI  
St. Charles County  
My Commission Expires: Mar. 20, 2005

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1           **WITNESS INTRODUCTION**

2           **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS FOR THE**  
3           **RECORD.**

4           A. My name is Edward J. Grubb and my business address is 535 N. New Ballas Road.  
5           St. Louis, Missouri 63141.

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

7           A. I am employed by Missouri-American Water Company as the Director Rates and  
8           Revenues.

9           **Q. PLEASE ELABORATE UPON YOUR DUTIES AS DIRECTOR RATES AND**  
10           **REVENUES.**

11          A. As Director Rates and Revenues, I direct the preparation and presentation of all  
12          aspects of the rate increase applications for Missouri-American Water Company, St.  
13          Louis County Water Company d/b/a Missouri-American Water Company and  
14          Jefferson City Water Works Company d/b/a Missouri-American Water Company  
15          (collectively, the "Applicants").

16          My main responsibilities as Director Rates and Revenues are as follows:

- 17          1) Plan and oversee the preparation and presentation of all rate increase  
18             applications and supporting documents and exhibits as prescribed by  
19             management policies, guidelines and regulatory commission requirements.
- 20          2) Plan rate analyses based on a review of operating company budgets, forecasts,  
21             financial statements and reports. Oversee rate analyses and studies to evaluate  
22             the effect of proposed rates on the revenues, rate of return and tariff structure.
- 23          3) Oversee the implementation of rate orders, including development of the  
24             revised tariff pricing necessary to produce the proposed revenue level.
- 25          4) Provide support for financial analysis of proposed acquisitions and expansion  
26             of service territory, including preparation of applicable Commission filings.

1           5)     May plan and oversee all internal financial plans.

2     **Q.   HAVE YOU PREVIOUSLY PARTICIPATED IN REGULATORY**  
3     **MATTERS?**

4     A.   Yes, I have prepared rate cases and presented testimony before the Maryland Public  
5     Service Commission, West Virginia Public Service Commission, Tennessee Public  
6     Service Commission, Illinois Commerce Commission, Kentucky Public Service  
7     Commission, Iowa Utilities Board and this Commission.

8     **Q.   WOULD YOU PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND**  
9     **AND BUSINESS EXPERIENCE?**

10    A.   In June 1978, I was awarded a Bachelor of Science Degree in Business  
11    Administration from Drexel University with a major in accounting. In May 1989, I  
12    was awarded a Masters of Business Administration from the University of West  
13    Virginia College of Graduate Studies. In September 1993, I successfully completed  
14    the Certified Management Accounting program and received my certificate as a  
15    Certified Management Accountant (CMA). In January 1998, I successfully  
16    completed the Certified in Financial Management (CFM) program and received my  
17    certificate as a CFM from the Institute of Management Accountants.

18    I began my career in 1978 with American Water Works Service Company, Inc. as an  
19    Internal Auditor. As an Internal Auditor, I conducted financial and procedural audits  
20    of American System operating companies.

21    In 1983, I was promoted to Rate Analyst. In 1984, I was promoted to Revenue  
22    Requirement Specialist and in 1988, I was promoted to Assistant Director - Rates and  
23    Revenue. In these three positions, I have assisted, prepared and presented testimony  
24    and accounting exhibits before regulatory bodies concerning rate increase  
25    applications.

1 In January 1998, I was promoted to the position of Comptroller of Kentucky-  
2 American Water Company. In October 2000, I was promoted to my current position  
3 with Missouri-American Water Company as Director Rates and Revenues.

4 **PURPOSE**

5 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS CASE?**

6 A. The purpose of my surrebuttal testimony is to address the rebuttal testimony of Mr.  
7 Dittmer, witness for the Office of Public Council ("OPC") on the issue of a Cost  
8 Allocation Manual.

9 **COST ALLOCATION MANUAL**

10 **Q. WHAT IS THE APPLICANTS' GENERAL POSITION REGARDING THE**  
11 **PROPOSED MERGER CONDITIONS?**

12 A. The Surrebuttal Testimony of James M. Jenkins addresses the Applicants' position  
13 that there are no detrimental impacts associated with the proposed merger and, thus,  
14 no basis for any conditions. My testimony will only address the Applicants' response  
15 to the specific proposed conditions that are found in Mr. Dittmer's Rebuttal  
16 Testimony.

17 **Q. AT PAGES 1 AND 2 OF HIS REBUTTAL TESTIMONY, MR. DITTMER**  
18 **MAKES THE FOLLOWING RECOMMENDATIONS: 1) RECOMMENDS**  
19 **THAT THE COST ALLOCATION MANUAL (CAM) REQUIREMENTS**  
20 **THAT WERE PLACED ON ST. LOUIS COUNTY WATER COMPANY IN**  
21 **CASE NO. WR-2000-844, BE ALSO PLACED ON THE SURVIVING**  
22 **MISSOURI-AMERICAN WATER COMPANY; 2) RECOMMENDS THAT**  
23 **THE VARIOUS REPORTING REQUIREMENTS OF THE CAM THAT THE**  
24 **COMMISSION DIRECTED IN CASE NO. WR-2000-844 BE DIRECTED**  
25 **"DOWNSTREAM" TO THE EXISTING AND NEWLY-CREATED-**  
26 **PURSUANT-TO-THE-PROPOSED MERGER "DISTRICTS" OF MISSOURI-**

1 AMERICAN WATER COMPANY; 3) RECOMMENDS THAT TO THE  
2 EXTENT THERE ARE JOINT OR COMMON COSTS INCURRED AT THE  
3 "MISSOURI-AMERICAN WATER COMPANY" LEVEL FOR THE  
4 BENEFIT OF THE MISSOURI "DISTRICTS", THAT DOCUMENTATION  
5 BEING MAINTAINED FOR THE AWWSC CAM ALSO BE CREATED AND  
6 MAINTAINED IN COMPARABLE DETAIL FOR SUCH "COMMON  
7 MISSOURI" COSTS. DO YOU BELIEVE THE COMMISSION SHOULD  
8 APPROVE THESE CONDITIONS AS PART OF THE APPLICANTS'  
9 REQUESTS TO MERGE INTO ONE SINGLE ENTITY?

10 A. As discussed in Mr. Jenkins' testimony, the Commission looks to apply certain  
11 standards when considering whether or not to approve a merger. That standard is a  
12 "No Detriment Standard". The proposed merger being sought by the Applicants  
13 should not be conditioned on the OPC's recommendation for a CAM. The proposed  
14 CAM does not address or "fix" any alleged detriment caused by or related to the  
15 merger. In fact, Mr. Dittmer does not identify any specific "detriments" that will be  
16 caused by the merger if a CAM is not implemented.

17 **Q. SETTING ASIDE THIS OVERALL OBJECTION TO CONDITIONS, WHAT**  
18 **ARE THE APPLICANTS' RESPONSE TO EACH OF MR. DITTMER'S**  
19 **RECOMMENDATIONS?**

20 A. First, the Applicants do not object to recommendation number 1 as discussed on  
21 pages 1-2 of Mr. Dittmer's rebuttal testimony. This Commission has ordered St.  
22 Louis County Water Company d/b/a Missouri-American Water Company in Case No.  
23 WR-2000-844 to prepare a CAM for the American Water Works Service Company  
24 costs ("AWWSC"). The Applicants will prepare the CAM as outlined in the  
25 Commission's Order for the merged Missouri-American Water Company.

1 **Q. SINCE THE COMPANY WILL BE PREPARING THE CAM AS OUTLINED**  
2 **IN THE COMMISSION'S REPORT AND ORDER IN CASE NO. WR-2000-**  
3 **844, DO YOU BELIEVE IT IS IMPORTANT TO NOTIFY THE PARTIES**  
4 **WHAT THE COST WILL BE FOR THIS CAM?**

5 A. Yes. Since the Company will be preparing the CAM, it is important for the  
6 Commission to know what that cost will be. This information was not available at the  
7 time of the rate case. It is also important for the Commission to recognize that if the  
8 OPC's other two recommendations are accepted, additional costs will be incurred that  
9 must be reflected in rates. Therefore, it is the Applicants' goal that all costs be  
10 identified, so that the best use of the Applicants' and ratepayers' resources can result.

11 **Q. WHAT IS THE COST TO PREPARE THE CAM THAT THE COMMISSION**  
12 **ORDERED IN CASE NO. WR-2000-844?**

13 A. The Applicants have contracted the services of Patrick L. Baryenbruch, an  
14 independent consultant for this purpose. The cost for Mr. Baryenbruch to prepare the  
15 CAM will be approximately \$79,000. This cost does not include Company  
16 management review and analysis or the possible cost of computer software changes to  
17 address any need for new information system reports. These additional costs are  
18 currently projected to be approximately \$20,000. Therefore, the cost of preparing the  
19 ordered CAM will be approximately \$100,000. There will also be annual CAM  
20 update costs of about \$5,000. These costs do not include any additional amounts  
21 needed to meet Mr. Dittmer's 2<sup>nd</sup> and 3<sup>rd</sup> recommendations.

22 **Q. ON PAGE 2, LINE 7 OF HIS REBUTTAL TESTIMONY, MR. DITTMER**  
23 **DISCUSSES HIS SECOND RECOMMENDATION. HE WANTS THE**  
24 **APPLICANTS TO MAINTAIN STATISTICS AND OTHER REPORTING**  
25 **SIMILAR TO THE AWWSC CAM SO THAT AWWSC COSTS CAN BE**  
26 **ASSIGNED AND ALLOCATED TO EACH OF THE DISTRICTS OF**

1           **MISSOURI-AMERICAN WATER COMPANY. DO YOU AGREE WITH**  
2           **THIS RECOMMENDATION?**

3           A. No, I do not. The allocation of the AWWSC costs down to the district level books  
4           and records would be cumbersome, redundant, and inefficient. The Applicants  
5           believe that it is more cost efficient and effective to record the costs of the AWWSC  
6           to a corporate level business unit (cost center). To allocate these costs to district  
7           specific business units detracts from the Applicants' ability to manage, control and  
8           review these costs on a monthly basis. If the costs of the AWWSC billing were  
9           recorded to the 65 business units in the financial system, management review and  
10          analysis becomes quite difficult.

11          This is because Applicants' financial system is designed to record costs by account  
12          which are grouped into business units (cost centers), where the costs are the  
13          responsibility of specific individuals. Allocating AWWSC costs to a business unit  
14          where the Business Unit Manager is not responsible for, or cannot control is  
15          inappropriate. It serves no purpose from a management control perspective. The  
16          responsibility for reviewing the AWWSC costs are reviewed by the Comptroller and  
17          myself on a monthly basis.

18          **Q. ONE OF MR. DITTMER'S ARGUMENTS FOR ALLOCATING AWWSC**  
19          **COSTS IS BECAUSE OF DISTRICT SPECIFIC PRICING (DSP). HOW**  
20          **DOES MISSOURI-AMERICAN WATER COMPANY ("MAWC")**  
21          **ALLOCATE AWWSC COSTS IN A DSP ENVIRONMENT?**

22          A. MAWC has prepared many rate cases where the AWWSC costs were allocated from  
23          a corporate level business unit to individual districts. In these cases, neither the OPC  
24          nor the Commission Staff objected to the allocation or its methodology. Since rate  
25          cases can be done on 2-3 year cycles, it makes more sense to use the rate case  
26          process to allocate costs to allow for the determination of DSP.

1 Also, there is a cost consideration for allocating AWWSC costs onto the books and  
2 records of each specific district. The AWWSC costs would have to be analyzed and  
3 thoroughly reviewed in terms of allocations. Journal entries must be recorded. This  
4 would entail creating the entry through a process of review and analysis. Resources  
5 will be needed to review and approve the entry, then it must be recorded and posted.  
6 This monthly allocation process is redundant, is inefficient, and adds administrative  
7 costs to the organization. Mr. Dittmer's concern need only be addressed during a rate  
8 case. Therefore, the allocation of AWWSC costs to districts should be handled in a  
9 rate case so that proper rates (if DSP is required) can be determined.

10 **Q. DO YOU AGREE WITH MR. DITTMER'S THIRD RECOMMENDATION**  
11 **THAT TO THE EXTENT THERE ARE JOINT OR COMMON COSTS**  
12 **INCURRED AT THE CORPORATE LEVEL OF MISSOURI-AMERICAN**  
13 **WATER COMPANY, A CAM SHOULD ALSO BE CREATED AND**  
14 **MAINTAINED?**

15 A. No, I do not. Mr. Dittmer's recommendation is based on an assumption that the level  
16 of common "Missouri" costs will increase due to further "consolidation" of functions  
17 across the Company. Though this assumption may come to fruition, the level and  
18 complexity of the common costs do not warrant a CAM.

19 The Company's financial system is designed to capture costs in business units (cost  
20 centers). After the merger, the Company will have 65 business units. Only eight (8)  
21 of these business units will be used to capture common "Missouri" costs. These  
22 business units were set-up to capture labor and benefits for associates who provide  
23 services that benefit all districts. Also included in these business units will be  
24 AWWSC costs, Insurance Other Than Group, Leases, Rents, Regulatory Expense,  
25 Legal Fees, and other miscellaneous type expenses (electric, office supplies, etc.).

1 **Q. MR. DITTMER FURTHER JUSTIFIES HIS THIRD RECOMMENDATION**  
2 **STATING THAT IT WILL MAKE THE RATE REVIEW PROCESS MORE**  
3 **EFFICIENT AND CITES THREE AREAS OF RATE AUDITOR**  
4 **UNDERSTANDING AT LINES 27 AND 28 OF PAGE 6. DOES THE**  
5 **EXISTING STRUCTURE ADDRESS THESE CONCERNS?**

6 A. Yes. We believe that our existing business unit structure addresses these areas.  
7 First, the nature of any cost "pool" is identified by each business unit being charged.  
8 For example, our Human Resource department is a business unit (cost pool). The  
9 second area is that accounts charged within each business unit will identify the types  
10 of charges in a given "common Missouri" cost pool (i.e. labor, rent, office supplies).  
11 And third, the reasons for exemption from allocations are apparent. A cost will be  
12 charged to a "corporate" business unit if the cost is a "common" cost. If a cost is  
13 directly assignable and benefits a specific district, then the cost will be charged  
14 accordingly.  
15 In summary, we believe the Commission should evaluate the OPC's recommendations  
16 in terms of cost and benefits. The Company believes that: 1) the additional costs of  
17 tracking, allocating and recording of AWWSC costs by district is not warranted and  
18 that the use of a rate case to allocate costs for DSP is the preferred vehicle; and, 2)  
19 creating a CAM for common costs within Missouri-American is not needed and only  
20 adds administrative costs to the Company.

21 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

22 A. Yes, it does.