

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
BEFORE THE IOWA UTILITIES BOARD

**FILED WITH  
Executive Secretary  
March 31, 2014  
IOWA UTILITIES BOARD**

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| IN RE:<br><br>IOWA-AMERICAN WATER COMPANY | DOCKET NOS. RPU-2013-0002<br>TF-2014-0030 |
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**RESPONSE OF IOWA-AMERICAN WATER COMPANY  
TO OCA'S OBJECTION TO COMPLIANCE FILING AND NEW RATES**

Comes now Iowa-American Water Company ("IAWC" or "Company") and for its response to the Office of Consumer Advocate's ("OCA") Objection to Iowa-American Water Company's Compliance Filing and New Rates ("Objection"), states to the Iowa Utilities Board ("Board") as follows:

**INTRODUCTION**

1. On February 28, 2014, the Board issued its Final Decision and Order ("Order") in the above-captioned matter. In that Order, the Board made a number of decisions regarding contested issues that impacted both IAWC's revenue requirement and its proposed rate design. Of significance to the pending filing which is the subject of OCA's Objection is the fact that 1) the Board disallowed IAWC's adjustment for changes in residential usage for weather normalization and declining usage; 2) the Board, sua sponte, determined to recover 50% of the Public Fire costs from the customer charge and 50% from the volumetric rates (as compared to the Company's initial filing which recovers 100% of these costs from the customer charge); and 3) the Board, sua sponte, determined that 25% of Private Fire costs be recovered from all

customer classes, with 50% of this 25% (i.e., 12.5%) to be recovered from the customer charge and 50% (i.e., 12.5%) to be allocated to the volumetric rate (as compared to the Company's initial filing which allocated 100% of Private Fire costs to its Private Fire customers).

2. Also, of significance, was the Board's decision regarding IAWC's class cost-of-service study. Specifically, the Board rejected two adjustments that OCA proposed with respect to the Company's class cost-of-service study. First, the Board rejected OCA's proposed peak day ratio and adopted a peak day ratio that was very close to that proposed by the Company (i.e., 1.63 instead of the Company's proposed 1.65). (Order, p. 41) In addition, the Board rejected OCA's proposed cost allocation method for determining customer costs, finding that it is appropriate to allocate some common costs to the customer charge and IAWC's allocation will be used for purposes of this proceeding. (Order, p. 43) Thus, noting that IAWC's cost-of-service study was performed in a manner consistent with the AWWA Rate Manual, the Board generally adopted IAWC's approach. (Order, pp. 46-47)

3. After making these decisions regarding revenue requirement and rate design, the Board directed IAWC to "file an updated class cost-of-service study (including the functionalized costs by cost category) that reflects the Board's decision on the issues in this proceeding and corresponds with Iowa-American's approved revenue requirement." (Order, p. 51)

4. On March 6, 2014, IAWC made its filing in compliance with the Board's Order, including a revised cost-of-service study, updated bill analysis and final tariff sheets. On March 11, 2014, after discussions with Board Staff and OCA, IAWC filed

additional data related to its March 6 compliance filing. Finally, after further discussions with Board Staff and OCA, IAWC filed, on March 18, additional documents in support of its compliance filing, to include a narrative description of its compliance rate design, and various comparative analyses comparing its compliance tariffs and cost of service with an alternative cost of service and rate design which reflected OCA's position regarding the development of the customer charge and resulting volumetric rates.

5. On March 18, 2014, OCA filed its Conditional Objection to Iowa-American Water Company's Compliance Filing and New Rates primarily objecting to the Company's compliance rates with respect to the calculation of the volumetric charge and the customer charge. Ten days later, on March 28, 2014, OCA removed its "conditional" modifier and essentially filed the same objection to IAWC's compliance tariff filing. The gist of OCA's Objection is that IAWC has employed different methodologies for calculating the proposed rates in its compliance filing than those used in its original filing with the Board and, as a result, has allocated more costs to the customer charge and to the first block of the volumetric rates which, in OCA's view, disproportionately impacts the Company's residential customers.

6. As will be discussed more thoroughly below, IAWC's compliance class cost-of-service study is not only consistent with the study it filed initiating this rate case, but it is also consistent with the Board's directive to "file an updated class cost of service study . . . that reflects the Board's decisions on the issues in this proceeding and corresponds with Iowa-American's approved revenue requirement." As a result, while admittedly more costs are being allocated to the customer charge and the first block of the volumetric rates than OCA would apparently prefer, this allocation is being made in

a manner that is fully consistent with the Company's class cost-of-service study as approved by the Board. On the other hand, if the Board accepts OCA's proposal regarding the calculation of the customer charge and volumetric rates, it will, in effect, be acting in a manner that is inconsistent with its own directive and, more importantly, it will have the effect of allocating a disproportionate and unreasonable amount of costs to the Company's large water customers.

### **CUSTOMER CHARGE**

7. As noted above, the Company, in its initial filing to begin this case, proposed to recover 100% of the Public Fire costs through its proposed customer charge. In addition, it proposed to recover 100% of the Private Fire costs from the Private Fire customers in their customer charge. The Board, however, decided, sua sponte, that only 50% of the Public Fire costs be recovered through the customer charge and the remaining 50% be recovered through the volumetric rate. With respect to Private Fire, the Board again, sua sponte, determined that 25% of the Private Fire costs should be recovered from all customers, with 50% of those costs (i.e., 12.5%) being collected through the customer charge and 50% (i.e., 12.5%) being collected through the volumetric rate. Since the Board made these determinations after the conclusion of the evidentiary hearing, IAWC was left to develop rates that it believed best reflected the Board's intentions in ordering this rate design and which complies with the Company's cost-of-service study. Accordingly, if all Public Fire costs and a portion (i.e., 25%) of Private Fire costs are going to be recovered from the general body of ratepayers (with 50% coming from the customer charge and 50% coming from the volumetric rate), IAWC believes that it is most appropriate to do so in a manner that 1)

is consistent with the principles contained in the AWWA Rate Manual; and 2) does not disproportionately and unfairly impact one class of customers.

8. In its original filing, the Company calculated customer costs per 5/8 inch meter per month using meter equivalents to recover all the costs related to Public Fire (which was included in the costs related to meters). Customers generally benefit from public fire service commensurate with the size of their property. By recovering the Public Fire costs based on meter equivalents, IAWC was able to allocate costs to customers based on the relative size of the customer's premise. However, in its Order, the Board determined that it was more appropriate to recover only 50% of the Public Fire costs and 12.5% of Private Fire costs from the customer charge and the remaining 50% of the Public Fire costs and 12.5% of the Private Fire costs from the volumetric charges. By recovering 50% of the recoverable fire costs from the volumetric charge, the Board is effectively charging the larger customers more, as these larger customers will typically consume more water. Therefore, the portion of the Public and Private fire costs to be recovered from the customer charge should be allocated based on the number of customer bills (as opposed to meter equivalents) since more costs have already been allocated to the larger customers through the partial allocation to the volumetric rates. Following this rationale, the Company developed a customer charge of \$14.08 per month, per 5/8 inch meter. A comparison of both the customer charge and the volumetric rates using customer bills or meter equivalents is depicted in the document entitled "Comparison of Proposed Rates per Order", p. 2, which was filed with the Board on March 18 and is attached hereto as Exhibit 1. Using meter equivalents for purposes of allocating fire costs to customer charges, as proposed by OCA, results in a

customer charge of \$13.36 per month per 5/8 inch meter and shifts more cost recovery to the resulting volumetric rates. (Exh. 1, p. 2, Column 2) Large customers are already paying a significantly higher customer charge in relation to the residential customers. For example, a commercial customer with a 2" meter will be paying a monthly customer charge that is eight (8) times that of a 5/8 inch meter customer (i.e., \$112.62 versus \$14.08). Recovering these fire costs through a customer charge based on meter equivalents and thus moving more cost recovery to the volumetric rates, as OCA contends, would effectively be charging the larger customers twice because of their size.

9. In short, it is more equitable (as well as consistent with the AWWA Rate Manual's cost-of-service principles) to recover the 50% of Public and Private Fire costs attributable to the customer charge based on the number of customer bills rather than on meter equivalents.

### **VOLUMETRIC RATES**

10. Once the appropriate customer charge is calculated, the remaining Public and Private Fire costs must be recovered from the volumetric rates. While OCA correctly notes that the compliance tariffs place more cost recovery on the first block of the volumetric rates than the second block (i.e., 17.9% vs. 7.9%), this is neither inconsistent with the Company's initial class cost-of-service filing nor, more importantly, is it unreasonable.

11. The change in the relative percentage increases in the first and second blocks is due to the change in the compliance class cost-of-service study after giving effect to the Board's determination of various revenue requirement and rate design

issues. As a result of the Board's Order, costs were allocated differently to the customer classes resulting in a greater percentage increase of costs being allocated to the residential class. Since 97% of the residential class consumption is in the first block, the first block should receive a larger increase than the other blocks. This change in the class cost-of-service study, and resulting rates, is due more specifically to the following determinations by the Board:

- a. The Board disallowed the Company's proposed adjustment to residential revenues to reflect normal weather and declining usage. (Order, pp. 43-46) The Board's refusal to make these adjustments increases the consumption attributable to the residential class and thus increases the percentage of costs allocated to the residential class. The first block of the volumetric rates must therefore be increased to recover these additional costs as 97% of the residential usage occurs in the first block.
- b. Of the 25% of Private Fire costs that are being reallocated to other customer classes, 50% of these costs are recovered in volumetric rates (i.e., 12.5%). 77% of these private fire costs are then allocated to the residential class as these costs are allocated on meter equivalents. Again, the first block of the volumetric rates must be increased as 97% of the residential usage is in the first block.
- c. 50% of Public Fire costs are also being recovered through volumetric rates and, again, 77% of these costs are allocated to the residential class. The first block must be increased commensurately as 97% of the residential usage is in the first block.<sup>1</sup>

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<sup>1</sup> See "Description of Compliance Rate Design and Additional Information Requested by "OCA" filed March 18, 2014.

12. OCA complains that IAWC has used a new methodology to allocate the fire costs to the volumetric rates. However, that is simply not true. Since IAWC's initial cost-of-service study did not propose to allocate any fire costs to the volumetric rates, it is disingenuous of OCA to claim IAWC is using a different methodology when it is merely making adjustments to its cost-of-service study in compliance with the Board's directive. In order to comply with the Board's decision to allocate a portion of the fire costs to the volumetric rates, IAWC was required, for the first time in this case, to allocate those costs among customer classes in order to calculate the resulting volumetric rates. In its initial filing, IAWC used Factor 9 (which is based on meter equivalents) to allocate all of the fire costs to the customer charge. In light of the Commission's decision to allocate 50% of the Public Fire costs and 12.5% of the Private Fire costs to the volumetric rates, the Company consistently and properly used Factor 9 to allocate those costs to the volumetric rates. This is both consistent with IAWC's initial class cost-of-service study and, more importantly, with the AWWA Rate Manual.

13. Finally, it is significant to note that OCA offers no support (and no stand alone cost-of-service study of its own) to substantiate its Objection. It simply asserts, without benefit of a cost study, that residential rates are receiving a disproportionate amount of costs.

## **CONCLUSION**

14. In light of the foregoing, IAWC respectfully requests the Board act expeditiously to deny OCA's objection to IAWC's compliance tariff filing and allow the compliance tariffs to go into effect.

Respectfully submitted,

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