

**STATE OF IOWA
DEPARTMENT OF COMMERCE
BEFORE THE IOWA UTILITIES BOARD**

IN RE:	:	DOCKET NO. RPU-2020-0001
	:	TF-2020-0250
IOWA-AMERICAN WATER COMPANY	:	
	:	

REPLY BRIEF OF IOWA-AMERICAN WATER COMPANY

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I. AFFORDABILITY AND THE ECONOMY

The Office of Consumer Advocate (“OCA”) filed its Brief in this proceeding on April 19, 2021. Iowa-American Water Company, Inc. (“Iowa-American,” “IAWC” or “the Company”) files this Reply Brief to respond to the claims made by OCA.¹ As will be shown, those claims are, in many cases, exaggerated and contrary to the facts established on this record.

Iowa-American’s President Randy Moore described the many ways that the Company’s employees work to positively impact the quality of life of its customers and the communities the Company serves.² Iowa-American’s commitments to its customers is the commitment to provide safe, reliable and affordable water service at a reasonable price.³ To satisfy this commitment the Company has provided evidence of its efforts to provide safe water service, which include source water monitoring and protection, source water and environmental stewardship, water treatment, water quality monitoring at its treatment plants, and contingency planning for contamination events and workplace safety.⁴

Iowa-American’s efforts to protect and enhance safety and reliability include the replacement of aging infrastructure through the support of the Qualified Infrastructure Plant (“QIP”) mechanism approved by the Board in the Company’s last rate case.⁵ The proposed modifications to this program will result in the avoidance of substantial costs that Iowa-American would have otherwise incurred to replace such infrastructure under emergency conditions as it wears out.⁶ These modifications also include a proposal to fund service line replacement, particularly lead service line replacement to protect its customers from lead exposure.⁷ This systematic replacement program avoids disruption to customer’s lives as work can be planned in a methodical way, taking into account the available labor pool, the time of year, supply chain issues and the needs of the community.⁸ At the same time as the Company’s investment in plant,

¹ To the extent that this Reply Brief has not addressed every issue discussed in OCA’s Initial Brief, Iowa-American relies on the arguments made on such issues in its Initial Brief.

² Moore Direct pp. 12-14.

³ Moore Direct pp. 8-12.

⁴ Nielsen Reply pp. 3-13.

⁵ Simmons Direct pp. 31-43; 15-22.

⁶ Tr. 90-91; Simmons Reply pp. 15-17; OCA Hearing Exh. 4, pp. 25-28; OCA Hearing Exhibit 6 pp. 18-19.

⁷ Nielsen Direct p. 7; Nielsen Reply pp. 6-13; Tr. 66-88, 93-97, 394-424.

⁸ OCA Hearing Exhibit 4, pp. 25-28; OCA Hearing Exh. 6, pp. 18-19.

equipment, and replacement of aging infrastructure improves safety and reliability, allowing the Company to operate in a cost-effective manner. The record in this case demonstrates that Iowa-American's efforts to slow and mitigate cost increases have been very successful.⁹

In this case, the Board is being asked to consider technical, factual record-based information and to reach a decision that will set just and reasonable rates that are fair to both customers and investors. OCA's brief must be read with caution, however, as OCA appears to favor hyperbole over facts, exaggeration over reasoned argument.

OCA argues, for example, that in setting reasonable rates, the Board must take into account that Iowa is "in the midst of a recession and global pandemic."¹⁰ What OCA does not say is that the current Iowa unemployment rate of 3.7% is now the same as the pre-pandemic unemployment rate in June 2016.¹¹ Although Iowa's unemployment rate did spike to slightly over 11% in April 2020, it declined to 5% by the end of Summer 2020 and has fallen steadily since then.¹² OCA also cites to a CNBC report claiming that 63% of Americans had been living paycheck to paycheck since the pandemic.¹³ Again, close scrutiny of that source reveals that it is based on a survey done by a private company of only 2000 people, with no relation to Iowa, or any other relevant comparison.¹⁴

OCA conspicuously ignores the continued recovery from the pandemic. In early April, the Iowa Business Council released its first-quarter Economic Outlook Survey for 2021 measuring member expectations for sales, capital spending and employment for the next six months. It marked the third positive quarter in a row, projecting continued confidence as the state emerges from the pandemic.¹⁵ As of April 24, 2021 KRCG reported that "A total of 2,174,800 COVID-19 vaccine doses have been administered

⁹ Moore Direct p. 7; Nielsen Direct, pp. 11-26; Cephas Direct p. 5.

¹⁰ OCA Initial Brief pp. 1-2.

¹¹ Data.bls.gov/timeseries/LASST1900000000000003; *see also* <https://www.desmoinesregister.com/story/money/business/2020/11/20/iowa-unemployment-rate-drops-near-pre-covid-19-low-now-3rd-lowest-u-s/6354884002/>.

¹² <https://www.desmoinesregister.com/story/money/business/2020/11/20/iowa-unemployment-rate-drops-near-pre-covid-19-low-now-3rd-lowest-u-s/6354884002/>.

¹³ OCA Initial Brief p. 2.

¹⁴ <https://www.cnbc.com/2020/12/11/majority-of-americans-are-living-paycheck-to-paycheck-since-covid-hit.html>.

¹⁵ <https://www.iowabusinesscouncil.org/news/eos/>.

in Iowa so far, an increase of 32,929 since the same time on [April 23, 2021]. 951,514 people have completed their vaccination course, either through the two-shot vaccines or the one-shot Johnson & Johnson vaccine, an increase of 20,949.”¹⁶ The report notes further that “Iowa ranks 16th in the United States in terms of the percentage of the population fully vaccinated with around 30.2% of people in the state meeting that standard.”¹⁷

OCA complains that “this would be the fourth rate increase in ten years”,¹⁸ ignoring that the last case was in 2016 and failing to recognize the continuing investment in Iowa infrastructure that has created the need for that rate relief. Since 2010, Iowa-American has invested nearly \$140 million in rate base necessary to provide safe, reliable and clean water to its customers. Iowa-American has more than doubled its annual capital investments since that time, investing over \$20 million annually in 2020 compared to \$8.6 million in 2010 and just under \$5 million in 2008. OCA also ignores the fact that, through that investment and working diligently to control costs, Iowa-American’s 2019 O&M expense per customer was lower than its 2010 O&M expense per customer.¹⁹ While the Company’s O&M expense has increased since the last case, its O&M expense per customer has remained relatively flat compared to 2010 levels.²⁰ OCA’s claims that Iowa-American has not met its commitment to the needs of its customers²¹ ring hollow when compared to the significant investment the Company has made in Iowa and its demonstrated record of efficiency and costs containment.

OCA also continues to insist that Iowa-American has requested a return on equity (“ROE”) of 10.5%.²² In fact, Iowa-American’s witness, Ms. Bulkley, identified that a reasonable “range” of ROE lay within 9.75% to 10.6%.²³ Although OCA contends that if the Company cared for its low-income customers, it would have reduced its requested return on equity,²⁴ Iowa-American’s rate request is fully supported.

¹⁶ <https://www.kcrg.com/2021/04/24/over-30-of-iowas-population-has-completed-covid-19-vaccination/>.

¹⁷ *Id.*

¹⁸ OCA Initial Brief p. 2.

¹⁹ Nielsen Direct p. 27.

²⁰ Nielsen Direct p. 26.

²¹ OCA Initial Brief p. 3.

²² *Id.*

²³ Bulkley Reply p. 39.

²⁴ OCA Initial Brief p. 3.

Ms. Bulkley considered the Company's risk factors as compared to the proxy group, including: (1) the Company's small size; (2) the Company's capital expenditure requirements; (3) the risk associated with the Company's declining average use per customer; and (4) the effect of environmental regulations on water and wastewater utilities and the costs associated with compliance.²⁵

These factors were not utilized to make any specific adjustment but were instead considered when determining where Iowa-American's ROE should fall within the range of analytical results.²⁶ Again, Ms. Bulkley determined a range of ROE estimates between 9.75 percent and 10.6 percent for the Company.²⁷ If the Board were not to approve the RSM and expanded QIP and authorize an equity ratio below the Company's proposal, the ROE should be near the higher end of the range given the added risk relative to the proxy group, which typically has similar adjustment mechanisms and a thicker equity ratio.²⁸

OCA further claims that the Company's "proposal fits with the historical pattern – Iowa-American's residential rates have gone up 91 percent ... from 2008 to what the Company projects for 2021."²⁹ Here, again, OCA exaggerates. OCA's argument that Iowa-American's water service is becoming less affordable is misleading and actually contrary to its own evidence and the evidence in this case. OCA's criticism of the affordability of Iowa-American's water service is based entirely on a comparison between the Company's rates and median household income.³⁰ The relevant comparison, however, is between Iowa-American customers' bills and median household income, not rates and median household income. In other words, does the customer have the income necessary to pay the bill received for water service each month? OCA's own witnesses agreed with this proposition.³¹

OCA's comparison does not reflect the impact on average bills that has occurred because usage has declined over time and its analysis does not reflect trends in actual customer usage (over the relevant time

²⁵ Bulkley Direct pp. 68-90.

²⁶ Bulkley Direct p. 68.

²⁷ Bulkley Reply p. 43.

²⁸ Bulkley Reply p. 77.

²⁹ OCA Initial Brief p. 2.

³⁰ *Id.*

³¹ Tr. pp. 318-19; 371-72.

period). Roach Direct Exhibit 7 shows that use per customer has declined 14% from 2010 to 2019, going from 4,341 gallons per month in 2010 to 3,710 gallons per month in 2019. Based on rates in Krueger Rebuttal Exhibit 4 and usage in Roach Direct Exhibit 7, the average monthly bill in 2010 was \$29.60 [(43.41 hundred gallons x \$0.40172) + \$12.16]. The average monthly bill in 2019 was \$35.71 [(37.10 hundred gallons x \$0.58500) + \$14.00]. This is a 21% increase. A 21% increase is about what inflation was from 2010 to the present.³² In contrast, median household income in Iowa grew by 28% over that same period.³³ This shows that increases in customer bills have tracked the approximate rate of inflation over the last several years and when compared to changes in household income, the Company's cost of service and monthly bills have become more, not less, affordable over that same time period.³⁴ Iowa-American serves all its customers' needs for drinking, cooking, cleaning, and washing, for about \$1.40 per day.³⁵

Despite the demonstrated affordability of its service, Iowa-American recognizes that there will always be those who struggle to afford the basic necessities of life. To meet this need, the Company proposed a Low Income Water Assistance ("LIWA") program. Under the Company's proposed LIWA program, approximately 1,500 customers who may be having difficulty paying their bill for basic water services will receive a nearly \$12 monthly discount, which could be as much as a 30% discount on their total bill (and approximately 0.5% of an annual \$30,000 household income).³⁶

If OCA were truly concerned for the plight of low-income customers, it would have supported the Company's proposed low-income rate program. Instead, OCA argues that "[t]he Board should reject Iowa-American's proposed LIWA program, claiming it will make water affordability more challenging, not less." Here again, OCA is engaging in hyperbole, not fact-based argument. As noted above, Iowa-American strives to operate its business in the most cost-effective ways possible so that the Company's cost of service

³² See www.inflationtool.com.

³³ Krueger Rebuttal Exh. 4.

³⁴ Tr. 181-82.

³⁵ Moore Direct pp. 10-11.

³⁶ Proposed Tariff Original Sheet 4M; Simmons Direct, pp. 46-49; Tr. 178-80; IAWC Response to OCA Data Request 171, included in Tessier Direct Exh. 4.

and customer bills remain affordable to all its customers.³⁷ OCA completely ignores the impact of discounts for lower income customers that will make water more affordable for those customers.

The Company has shown that it is open to modifications to the proposed program to reach even more customers.³⁸ The existence of a low-income discount program does not increase revenue requirements over and above what they otherwise would have been, contrary to OCA's claims, and therefore does not materially affect affordability of water service. Customers using significant water resources in the summer for discretionary seasonal uses would be asked to pay approximately an additional \$0.30 cents per month, which for most households would be barely noticeable.³⁹ Although OCA would use the pandemic as an excuse to recommend reducing rates below sustainable levels, OCA ignores the pandemic's teachings that underscore water's special status as essential to public health and makes adopting sustainable programs to ensure access for vulnerable customers an important goal that is in the public interest.

For all these reasons, OCA's claims should be carefully scrutinized and viewed with skepticism. Despite OCA's exaggerations and hyperbole, the evidence in this case demonstrates that Iowa-American is operating, maintaining, and investing in its system in a cost-effective manner that serves the long-term interests of its customers. The evidence also demonstrates that Iowa-American's forecasts and ratemaking proposals in this case support the Company's plans to continue providing safe and reliable water service at a price its customers can afford.

II. REVENUE AND RSM

A. OCA Has Failed to Rebut Iowa-American's Ample Evidence of Declining Use

The evidence demonstrates that, just like other water systems across the country, Iowa-American's usage per customer is declining. In both the residential and commercial classes, the decline is at an annual

³⁷ Even with sound planning and management by Iowa-American, there will always be some customers who will struggle to pay their water bills, as well as their gas, electricity and telephone bills, particularly when unexpected events like the COVID-19 pandemic hit, but even in normal times. Iowa-American recognizes this and offers several targeted customer assistance programs to help its most vulnerable customers. These include budget billing, flexible payment plans, and the Help to Others ("H2O") Program. Moore Direct pp. 11-12.

³⁸ Simmons Reply p.12; Tr. 179-80; IAWC Response to OCA Data Request 171, part C, included in Tessier Direct Exh. 4.

³⁹ Tr. 319-21.

rate of approximately two percent, has been ongoing for decades, and is expected to continue. This declining use makes perfect sense considering conservation efforts by customers and federal laws that require significantly less water usage in new plumbing fixtures such as toilets and shower heads, and in appliances such as washing machines and dishwashers. When older fixtures and appliances are replaced, water usage inevitably declines.

In the face of such seemingly incontrovertible evidence, OCA nevertheless claims that its witness, Dr. Dismukes, concluded that he observed a trend of increasing revenue per customer.⁴⁰ The record evidence demonstrates that OCA's claims are misleading at best.

First, it is surprising and disappointing that OCA's witness would intentionally confuse and conflate revenue with usage. Mr. Rea noted that Dr. Dismukes is ignoring the elementary fact that revenue can increase due to issues other than increased usage or more customers.⁴¹ Primary among these other causes is a rate increase, which can mask a usage decline.⁴²

Second, the Company's residential and commercial forecasts explicitly capture growth in numbers of customers. Mr. Rea explained that customer growth was projected by applying average monthly growth rates for the most recent available three years to historical customer counts. Weather normalized use per customer for the calendar years 2020, 2021, and 2022 is based on Mr. Roach's regression analyses demonstrating declining use per customer. Total annual sales for the forecast period were developed using the use per customer values provided in Mr. Roach's analyses multiplied by an increasing forecast in customer counts and allocated down to month and district based on historical relationships from 2018 and 2019.⁴³ The Company's revenue forecast thus captures growth in numbers of customers.

Third, OCA argues that "During that period residential usage fell by 0.4%, or 0.1% percent per year, as the impact of declining existing residential customer usage and usage growth from new residential

⁴⁰ OCA Initial Brief p. 5.

⁴¹ Rea Reply pp. 14-15.

⁴² *Id.*

⁴³ Rea Direct pp. 18-19.

customers largely offset.”⁴⁴ A closer look at OCA’s forecast for test year usage reveals that Dr. Dismukes based his forecast on a short 2015-2019 time period and made no effort to normalize those sales for weather - a peculiar omission given the powerful effect weather has on seasonal usage. Upon closer review, OCA Witness Dismukes’ analysis actually shows declining usage per customer for 2015, 2016, 2018 and 2019.⁴⁵ Only the single, non-normalized year of 2017 showed an increase in use and that was an extremely dry year, which would naturally bolster outdoor water usage.⁴⁶ As Company witness Roach pointed out, by concentrating his analysis on historic sales as opposed to weather normalized water sales or usage per customer (“UPC”), OCA witness Dismukes failed to observe any effects of customer usage trends or the impact of “customer growth.” Rather, he has simply observed the changing response of total customer usage to varying annual weather conditions from one year to the next, thus ignoring the one catalyst to water sales that has the single largest effect on water sales volumes in any particular time period across the industry.⁴⁷

OCA simply cannot seriously contest the Company’s forecast which is based on declining use per residential and commercial customer combined with forecasted increasing levels of customers in those classes. Dr. Dismukes admitted that “the Company has seen a contraction in UPC, and that contraction has likely been the result of ratepayer efficiency activity.”⁴⁸ He further conceded that usage per customer has been decreasing over the last several years.”⁴⁹ Moreover, Dr. Dismukes’ speculation that the decline in usage per customer “may be flattening out”⁵⁰ is just that – idle speculation unsupported by any analysis and flatly contrary to the evidence the Company produced about the continuation of the nationally recognized trend. In contrast, the Company identified, with statistically reliable, long-term regression analyses, a trend of declining UPC of about 2% per year for the residential and customer classes. This trend is consistent

⁴⁴ Dismukes Direct pp. 16-17.

⁴⁵ Roach Reply pp. 5-6.

⁴⁶ *Id.*

⁴⁷ Roach Reply p. 3.

⁴⁸ Dismukes Direct p. 19.

⁴⁹ *Id.*

⁵⁰ *Id.* at 20.

with the trend across the country and is well correlated with legal and technological changes that make replacement fixtures and appliances more efficient and less water intensive. The Company then matched that trend with forecasts of new customers that OCA does not dispute. For all these reasons, Iowa-American's revenue forecasts are the only reliable forecasts proposed in this case.

B. The RSM is a Fair, Established, Best Practice Regulatory Tool

Iowa-American's proposed RSM is a regulatory tool which is designed to align the Company's actual revenues with the level the Board uses to set rates in this case. OCA attempts to paint the RSM as a profound departure from ratemaking practice. NARUC and the numerous jurisdictions that have adopted similar mechanisms would disagree. RSMs and similar mechanisms have been used to align the ratemaking process with reality in regulatory jurisdictions throughout the country, and Iowa-American urges the Board to do so here.

OCA Witness Dismukes argues that the RSM does not account for customer growth besides acquisitions.⁵¹ This is demonstrably false. In fact, the proposed RSM focuses on total net revenues which is a combination of use per customer, total number of customers, and other factors.⁵² Simply put, increases in revenue due to increases in customers due to organic growth are explicitly taken into consideration by the RSM.⁵³ In arguing to the contrary, OCA⁵⁴ cites Dr. Dismukes, who in turn cites Company Witness Rea for the opposite proposition – that organic growth is not taken into consideration. In fact, Mr. Rea says the complete opposite in the testimony cited by Dr. Dismukes:

Q: At page 14, lines 14-16 of his Direct Testimony, Dr. Dismukes states that the Company's proposed RSM would offset the expected decline in Company revenues due to declining use per customer but would not offset the expected increase in revenues due to customer growth. Is this correct?

⁵¹ Dismukes Rebuttal p. 6.

⁵² Rea Reply p. 14.

⁵³ Dr. Dismukes appears to be confused as to how the RSM provides for customer growth. In the event the Company grows through acquisitions, the Company will exclude the acquisition revenue and production costs from the RSM until they are recognized in the next rate case. Rea Direct p. 44. Incremental customer growth i.e., not based upon customers gained by an acquisition is tracked and included as part of the RSM. Rea Reply p. 15.

⁵⁴ OCA argues that the RSM does not account for non-acquisition customer growth. OCA Initial Brief p. 53. As authority for its argument, OCA cites page 6 of Dr. Dismukes's Rebuttal Testimony, which cites page 15, lines 13-14 of Company Witness Rea's Reply Testimony.

A: No. the Company's proposed RSM is based on total net revenue, which as I previously stated, results from a combination of changes in use per customer, changes in the total number of customers, and fluctuations in usage caused by weather or perhaps other intervening factors. The RSM, therefore, explicitly accounts for growth in customers and Dr. Dismukes's criticism is incorrect.⁵⁵

OCA also argues on one hand that "the RSM is not necessary because Iowa-American does not face significant risk of declining revenues,"⁵⁶ and on the other hand, that Iowa-American should bear the risk of reduced sales volumes."⁵⁷ Both of these arguments miss the mark. An RSM simply will allow Iowa-American to collect the revenue authorized by the Board to establish these rates. Under the RSM, actual revenues are tracked against the Board authorized revenue requirement, and revenues are "trued-up" on a periodic basis to the authorized revenue requirement using an automatic rate adjustment. If actual revenue is higher than authorized, the net differences will be credited to customers. If actual revenue is lower than authorized, the RSM will permit the Company to collect the net difference through a surcharge. Thus, both the Company and its customers are treated fairly. If the revenue requirement can be reliably recovered, then the Company is in the best position to plan, operate, maintain, and invest in its system, which is in the best interest of Iowa-American's customers. Further, given the trend of declining use, the RSM is a tool that could enhance the ratemaking process by permitting the Company to extend the time between future rate case filings based on shortfalls in the collection of Board authorized revenues.

C. The RSM is Consistent with Iowa's Future Test Year Statutory Framework

The OCA suggests that Iowa-American's proposed RSM "may" be inconsistent with the subsequent proceeding provided for in Iowa Code § 476.33(4)(b).^{58,59} Specifically, OCA suggests that the proposed RSM reconciliation would be similar to the determination made in a subsequent proceeding. OCA notes that the subsequent proceeding takes place once while the RSM reconciliation would take place

⁵⁵ Rea Reply p. 15.

⁵⁶ OCA Initial Brief pp. 50-51.

⁵⁷ OCA Initial Brief pp. 51-53.

⁵⁸ OCA Initial Brief p. 53.

⁵⁹ Iowa Code § 476.33(4)(b) requires that the Board "conduct a proceeding subsequent to the effective date of a rate resulting from a rate regulatory proceeding utilizing a future test year to determine whether the actual costs and revenues are reasonably consistent with those approved by the board."

yearly, which OCA suggests might be inconsistent with § 476.33 and its reference to a single subsequent proceeding. In support of its argument, OCA references an earlier Board decision prohibiting Interstate Power and Light Company (“IPL”) from filing a rate case with multiple future test years.⁶⁰

OCA misses the mark. The RSM proposal envisions a reconciliation filing each year, not a proceeding. Unlike the subsequent proceeding, there will be no prospective adjustment of rates.⁶¹ In this regard, the RSM is much like MidAmerican’s revenue sharing reconciliation filing.⁶² Neither does Board precedent related to IPL’s attempt to file a multiple future test year case apply. In that case, the Board concluded that the Legislature intended that each rate case involve only one future test year because the statute references test year.⁶³ Here, the revenue projection adopted by the Board does not change until rates are reset in a subsequent base rate case. All that happens is that the RSM harmonizes actual revenue to the revenue authorized to set rates. If the revenue projection changed from year to year, OCA might have a point. But the RSM simply trues up revenue to the Board’s revenue finding. The IPL case has absolutely nothing to do with the Company’s RSM proposal.

III. QUALIFIED INFRASTRUCTURE PLANT MECHANISM

A. The QIP is Critical to Addressing Iowa-American’s Infrastructure Needs

Iowa-American’s QIP mechanism was approved by the Board in the Company’s 2016 rate case. In so doing, the Board specifically found that “[i]t is reasonable to implement a qualified infrastructure plan[t] replacement mechanism, as otherwise described in this order, to more quickly replace aging infrastructure.”⁶⁴ The Board’s order set out its rationale for that finding:

1. Use of adjustment mechanisms to address certain costs is authorized by Iowa Code § 476.6(8) and the Board has approved such mechanisms when they meet certain criteria.⁶⁵

⁶⁰ OCA Initial Brief p. 54.

⁶¹ Iowa Code § 476.33(4)(b) provides in pertinent part that “[i]f the actual costs and revenues are not reasonably consistent with those approved by the board, the board shall adjust rates accordingly.”

⁶² *MidAmerican Energy Company*, Docket No. RPU-2013-0004 “Order Approving Settlement, with Modifications, and Requiring Additional Information” p. 103 (IUB 3/17/2014).

⁶³ *Interstate Power & Light Co.*, Docket No. RPU-2018-0004 “Order Rejecting Notices, Opening Dockets and Scheduling Technical Conferences” p. 18 (IUB 2/6/2019).

⁶⁴ *Iowa-American Water Co.*, Docket No. RPU-2016-0002 “Final Decision and Order” p. 61 (IUB 2/27/2017).

⁶⁵ *Id.* at 21.

2. The Board has recognized . . . the occasional need for adjustment mechanisms that do not necessarily meet the traditional standards . . .⁶⁶
3. The Board acknowledges that newer infrastructure is likely to be more efficient and reliable . . .⁶⁷
4. The Board agrees that improved reliability and stability would provide a customer benefit and it also wishes to encourage replacement of aging infrastructure.⁶⁸
5. The Board recognizes that rate case expenses have a relatively greater impact for a utility like Iowa-American that has a smaller number of customers than other rate-regulated utilities in Iowa. Consequently, the Board finds that a reduction in rate case expenses would likely be a benefit to Iowa-American's customers.⁶⁹
6. Iowa-American has supported this plan with a financial impact study that was not present in the prior two rate cases where the Board did not allow a QIP or similar mechanism.⁷⁰
7. An annual QIP filing will still allow Iowa-American to increase its infrastructure investment without overly burdening its ratepayers with multiple rate increases per year.⁷¹
8. QIP-eligible projects shall be those that replace aging infrastructure and do not otherwise increase Iowa-American's revenue.⁷²

In the present case, OCA is asking the Board to turn back the clock, contending that the QIP has not reduced the Company's O&M costs, has not provided any other customer benefits, and has not provided benefits in proportion to its costs.⁷³ OCA's collateral attack on the QIP is simply a rehash of the arguments it made against the QIP in the 2016 case, without providing a scintilla of new evidence.

OCA ignores the basic rationale for adoption of the QIP. The critical need for timely infrastructure replacement and the management thereof is a vexing problem facing the entire water industry,^{74,75} and Iowa-

⁶⁶ *Id.* at 22.

⁶⁷ *Id.*

⁶⁸ *Id.* at 23.

⁶⁹ *Id.*

⁷⁰ *Id.* at 24.

⁷¹ *Id.*

⁷² *Id.*

⁷³ See OCA Initial Brief pp. 44-50.

⁷⁴ *Iowa-American Water Co.*, Docket No. RPU-2016-0002 "Direct Testimony of Jeffrey T. Kaiser", filed in this Docket as OCA Hearing Exh. 4, pp. 12-13, 16-20. See, e.g., Resolution Endorsing Consideration of Alternative Regulation that Supports Capital Investment in the 21st Century for Water and Wastewater Utilities, sponsored by the NARUC Committee on Water and adopted by the NARUC Committee of the Whole (11/30/2013); Resolution Supporting Consideration of Regulatory Policies Deemed as "Best Practice", sponsored by the NARUC Committee on Water and adopted by the NARUC Board of Directors (7/27/2005), all cited in OCA Hearing Exhibit 6 in this Docket, footnotes 2 and 3. See also *American Society of Civil Engineers 2013 Report Card on Infrastructure*, <http://www.infrastructurereportcard.org/fact-sheet/drinking-water> and <https://2013.infrastructurereportcard.org/iowa/iowa-overview/> all cited in OCA Hearing Exh. 5 in this Docket, footnotes 3 and 4.

⁷⁵ See also U.S. EPA, "Drinking Water Infrastructure Needs Survey and Assessment: Fifth Report to Congress," <https://www.epa.gov/sites/production/files/2015-07/documents/epa816r13006.pdf>, cited in OCA Hearing Exhibit 4 in this Docket, footnote 3.

American has a pressing need to replace distribution infrastructure that has met or exceeded its life expectancy.⁷⁶ The QIP allows the Company to make capital improvements to its aging system and recover the costs of such improvements on a timelier basis, thus enhancing the Company's ability to do so.⁷⁷ Through the QIP, the Company is accelerating the rate of investment to replace its aging water infrastructure in a systematic, responsible manner that addresses the long-term replacement needs of the system in a cost-effective way.

The value of continued accelerated infrastructure replacement is substantial, benefiting customers today and well into the future with improved water quality, and fewer main breaks and service interruptions.⁷⁸ Importantly, replacing pipes that are near the end of their useful lives will result in lower costs for customers over time than deferring replacement.⁷⁹ Responsible, systematic replacement is far more cost efficient than is *ad hoc* repair and replacement when a main breaks, with the attendant adverse effects on service and public convenience.⁸⁰ For example, a reduction in the number of emergency projects will yield cost savings not only in terms of mobilizing manpower and equipment, but also in enabling the Company to leverage its ability to strategically source and procure materials in advance.⁸¹ There are costs to increasing pipe breaks, service disruptions, property damage, and health risks from potential drinking water contamination exposure as well as related community opportunity costs tied to community health and economic development.⁸² The QIP is a necessary and proven regulatory mechanism to support the Company's efforts to accelerate the replacement of its aging infrastructure.

⁷⁶ OCA Hearing Exh. 4, pp. 16-17.

⁷⁷ *Id.* at 13-14.

⁷⁸ *Iowa-American Water Co.*, Docket No. RPU-2016-0002 "Direct Testimony of Susan E. Krohn", filed in this Docket as OCA Hearing Exh. 6, p. 18.

⁷⁹ *Id.* at 18-19; OCA Hearing Exh. 4, pp. 20-21, 24-26.

⁸⁰ OCA Hearing Exh. 6, pp. 19-20. Planned pipe replacements are also much less costly on a unit cost basis compared to the steep increase in future pipe replacements resulting from prior deferrals of those replacements. OCA Hearing Ex. 4, p. 28

⁸¹ *Id.* at 26-27.

⁸² *Id.* at 27-29.

B. The OCA Has Not Provided Any Evidence that the QIP Should be Rejected

Despite the clear need for the QIP, OCA witness Mr. Tessier has recommended that the Board reject the QIP because it has not reduced the Company's O&M costs, has not provided any other customer benefits, and has not provided benefits in proportion to its costs.⁸³ OCA ignores the fact that Iowa-American's 2019 O&M expense per customer was lower than its 2010 O&M expense per customer.⁸⁴ OCA also ignores that, over that, the Company's cost of service and monthly bills have become more, not less, affordable.⁸⁵ These are clearly customer benefits that the Company has achieved, in part, through responsible, systematic replacement investment and working diligently to control costs.

The QIP has operated as intended. In its 2016 case, the Company anticipated that the approval of the QIP would enable the Company to invest an additional \$6 to \$8 million annually to accelerate the replacement of aging distribution and water treatment infrastructure.⁸⁶ In fact, the Company's annual QIP investment has increased from \$4.2 million in 2016 to \$7.6 million in 2020 and is expected to grow to over \$10 million by the end of the test year.⁸⁷ Without an alternative cost recovery method such as the QIP, the Company's ability to sustain an accelerative infrastructure replacement program will be difficult.⁸⁸ Contrary to Mr. Tessier's claims that the QIP has not fulfilled its intended purpose of infrastructure replacement and customer benefits, the record demonstrates that it has done so. The QIP enables the Company to plan and manage the consistent deployment of Company and contractor resources to more efficiently and effectively attain and maintain a replacement program that better serves the long term interests of customers.⁸⁹ None of OCA's objections provides a reasoned basis to withdraw the QIP and deny the Company's customers the long-term benefits of it.

⁸³ See Tessier Direct p. 24. and OCA Initial Brief pp. 44-50.

⁸⁴ Nielsen Direct p. 27.

⁸⁵ See discussion at p.3, *supra* and at pp. 23-24, *infra*.

⁸⁶ OCA Hearing Exh. 6, p. 23.

⁸⁷ IAWC Simmons Direct Exh. 23.

⁸⁸ Simmons Direct pp. 31-35.

⁸⁹ Moore Direct p. 6; OCA Hearing Exh. 4, pp. 23-27.

C. The Company's Proposed Modifications to the QIP Will Make it More Effective

1. The inclusion of additional plant accounts in the QIP is warranted

The Company's QIP projects are prioritized based on current and future service needs, assessments of the physical condition of existing plant, economic and risk factors, performance characteristics, regulatory compliance, and the potential to coordinate with municipalities and other utilities in joint improvement projects.⁹⁰ Iowa-American is proposing to add Account 310 – Power Generation Equipment and Account 311 – Pumping Equipment to the QIP Rider.⁹¹ The inclusion of these additional plant accounts as eligible for the QIP supports the Company's efforts to proactively address potential threats to system reliability and safety in a way that supports the long-term interest of its customers.⁹²

2. The QIP Threshold and Debt Only Return Limits the Effectiveness of the QIP

The Company was deeply appreciative of the Board's adoption of the QIP, which, as explained above, has worked as it was intended to encourage additional infrastructure investment. Nevertheless, the continued imposition of a threshold to the QIP mechanism will put Iowa utilities on unequal footing when attracting investment.⁹³ Both the threshold and the allowance of only a debt cost rate are not calculated to make the most of this cost recovery mechanism.

The QIP is intended to support the Company's efforts to make capital improvements to its aging system and recover the costs of such improvements on a timelier basis. Mr. Simmons explains how these two provisions impair Iowa-American's ability to recover a significant portion of QIP eligible costs.⁹⁴ As Mr. Simmons observed "If very little qualifies for the QIP and investment isn't properly compensated, any increased investment puts pressures on rates."⁹⁵ The QIP has already provided tangible benefits for customers by allowing Iowa-American to extend the time between rate cases while materially increasing the size of its QIP-eligible investments. These benefits could be advanced further by providing for a fully

⁹⁰ *Id.* at 4.

⁹¹ Simmons Direct pp. 41-42.

⁹² Kull Direct p. 21.

⁹³ Simmons Direct pp. 34-35.

⁹⁴ Simmons Direct pp. 31-43; *see also* IAWC Initial Brief pp. 34-37.

⁹⁵ Simmons Reply, p. 18.

cost based return (not limited to debt capital) and an expanded cap. The Company urges the Board to consider these changes in light of the benefits already derived from the QIP.

IV. LEAD SERVICE LINE REPLACEMENT PROGRAM

A. The Company's Proposal Is Well Grounded in Safety and Efficiency Concerns

Iowa-American is not currently in violation of federal or state regulatory standards established by the United States Environmental Protection Agency ("EPA") or the Iowa Department of Natural Resources, including the Lead and Copper Rule ("LCR")⁹⁶ because the Company has implemented a variety of proactive measures, including: 1) corrosion control treatment and research; 2) customer education; and 3) elimination of Lead Service Lines ("LSL"). Iowa-American has not triggered the LCR action level requirements in any portion of its system, which is a testament to the effectiveness of the Company's corrosion control measures and management of its distribution system.⁹⁷

The current LCR requires utilities, among other things, to test drinking water inside older homes for lead and take additional action if more than 10% of tap water samples exceed the lead concentration limit (i.e., 15 parts per billion),⁹⁸ including replacement of utility-owned and customer-owned lead piping. Consequently, remaining in compliance with applicable drinking water regulations necessarily requires taking steps to address possible sources of lead contamination from customer-owned property. Iowa-American, however, can only replace the lines and or segments it owns. If a customer is unable or unwilling to pay for replacing the portion of the service piping for which the customer is responsible, the Company cannot replace the customer's pipe and capitalize the cost of replacement.⁹⁹ Iowa-American's options are further limited by the current ownership structure in Davenport reflected in First Revised Tariff Sheet Nos. 12 and 13, which do not authorize the Company to replace a customer's Service Line. Under First Revised Tariff Sheet Nos. 12 and 13, the customers have full responsibility for the installation, repair, replacement, and maintenance of all Service Lines. The Company's proposed Tariff, if approved, along with changes in

⁹⁶ Nielsen Reply pp. 8-10; Tr. p. 69, 72.

⁹⁷ Nielsen Reply pp. 7-10; Tr. pp. 73-78, 84-85, 87, 410.

⁹⁸ IAWC Hearing Exh. 5, p. 1.

⁹⁹ Tr. pp. 411-13.

the ordinance will enable Iowa-American to replace lead customer-owned service lines, retain partial ownership and leave with the affected customers the ownership and responsibility to maintain, repair and replace the new Service Line after it is installed.¹⁰⁰

By providing the Company with the ability to replace customer-owned LSLs, the Board will limit partial lead service line replacements thereby protecting customers from significant lead exposure. Replacing both parts of the service line at the same time as replacing a main makes economic sense and greatly simplifies the replacement process. There is a reduction in coordination requirements between customer and Company as well as an elimination of a costly financial burden to the customer.¹⁰¹ As summarized in the Company's Initial Brief:

Iowa-American ... plans to replace lead service lines that are found as they replace mains throughout the service territory. If this method does not result in the replacement of its stated replacement goals of 1,400 lines per year, Iowa-American will then proceed to other methods.¹⁰²

Despite OCA's allegations that there is no immediate danger to customers, lead in water service lines creates major safety and reliability concerns for customers,¹⁰³ and can cause a range of health effects including adverse health and developmental effects, especially in young children.¹⁰⁴ The fact that Iowa-American's current practices have proved effective so far does not mean that lead is not a continuing hazard. Current protections against lead exposure such as corrosion control, however, may be insufficient when lead service lines are disturbed as a result of main replacements.¹⁰⁵ Additionally, while replacing the entire portion of the entire lead service line, including both the Company portion and the customer portion, is best practice within the water utility industry, replacing only a portion of the lead service line can create just as much lead exposure as it seeks to eliminate.¹⁰⁶

By providing the Company with the ability to replace customer-owned LSLs, the Board will limit

¹⁰⁰ Proposed 2nd Revised Sheets 12, 13, 22-27.

¹⁰¹ Tr. pp. 412-13, 185-86.

¹⁰² Nielsen Reply p. 10.

¹⁰³ *Id.* at 6-7.

¹⁰⁴ IAWC Hearing Exh. 5, p. 1.

¹⁰⁵ Tr. pp. 419-20.

¹⁰⁶ [Long-Term Behavior of Simulated Partial Lead Service Line Replacements | Environmental Engineering Science \(liebertpub.com\)](https://www.liebertpub.com/Long-Term-Behavior-of-Simulated-Partial-Lead-Service-Line-Replacements-Environmental-Engineering-Science).

partial lead service line replacements thereby protecting customers from significant lead exposure. The Company is open to meet with Staff and OCA to discuss the continued development and improvement of the Company's LSL replacement program. The Company will meet with the parties, if requested, to discuss the program and its implementation, and OCA may review and challenge the Company's replacement program in future proceedings.

B. OCA's Objections to the Company's LSL program Are Misguided

OCA argues that Iowa-American's LSL replacement program does not meet the EPA inventory requirement of lead service lines.¹⁰⁷ OCA's argument is misguided because, although there is no current inventory requirement, Iowa-American has undertaken an analysis of where and how many lead service lines are in its service territories and expects to continue that analysis.¹⁰⁸ These actions will satisfy EPA's upcoming requirements for a lead service line inventory.¹⁰⁹ Further, until a service line is excavated, there is no way to know for certain whether it contains lead. Iowa-American's plan is a case-study in common sense; it will replace lead service lines that are found as it replaces mains throughout its service territory.¹¹⁰ OCA's misstatement of present requirements and Iowa-American's efforts to-date will only lead to an increased administrative burden that will result in delay, potential harm and increased costs.¹¹¹

OCA also argues that Iowa-American has not explained how it determines whether service lines contain lead or how it trains its workers to identify lead service lines, safety measures, and disposal. These too are false obstacles. Iowa-American maintains a professional workforce that is trained and experienced in working with lead.

OCA advances an entirely new argument, devoid of evidence, when it asserts that Iowa-American's lead service line replacement program is designed to benefit American Water Resources' service line protection program. OCA urges the Board to be "skeptical" of lead service line replacement because it fears

¹⁰⁷ OCA Initial Brief pp. 26.

¹⁰⁸ Nielsen Reply pp. 7-10; Tessier Rebuttal Exh. 3, Tessier Direct Exh. 4, IAWC Responses to OCA Data Request Nos. 173 and 179.

¹⁰⁹ Tr. 66-68.

¹¹⁰ Tr. 75-76.

¹¹¹ Tr. 74-75.

that if Davenport's service line ownership structure changes, and lead service lines are replaced, American Water Resources will somehow benefit from fewer claims. OCA relies on a single data request response, buried in a voluminous exhibit, as its support for the proposition. Yet that response states and proves the opposite of OCA's claim.¹¹² American Water Resources charges the same amount to customers in Davenport and Clinton, which undermines OCA's unfounded assertion that the change in ownership and the beginning of the lead service line replacement program (which both already exist in Clinton) somehow benefits American Water Resources.¹¹³

C. Customer Outreach, Cost Recovery and Reporting

The Company will perform customer outreach and implement a communication plan to notify potentially affected customers with lead service lines through various means, including direct mailings, bill inserts, and information on the Company's website as it has with its current service line replacement efforts.¹¹⁴ Additionally, the Company is willing to share its communications and work collaboratively with the Staff and the OCA to ensure that affected customers receive accurate, timely, and detailed information concerning the replacement program.

The Company proposes to record customer owned LSL costs in a sub-account of the Company's Account 333 – Services (this account generally tracks the costs associated with installation of services pipes and accessories leading to the customer's premises). If Iowa-American replaces a lead line, then that cost is recorded to the program, but if lead lines are not replaced, then there are no costs to record. All of this activity will be subject to Board and OCA review.

OCA argues that Iowa-American should not be allowed to recover the costs of remediating lead lines if it does not own the lead line in its entirety. OCA's argument should be rejected because a utility has an ongoing obligation to remediate damage caused when it replaces main or service lines and lead as

¹¹² Tessier Direct Exh. 4, IAWC Response to OCA Data Request No. 181.

¹¹³ Moreover, American Water Resources is also not the only company that offers such policies, and line age is among the many factors considered when setting policy rates. OCA's unsupported argument is no reason to delay an important safety program

¹¹⁴ See Tr. pp.403-15; IAWC Hearing Exhibits 7, 8, 9 and 10.

much as it does for the restoration of other property (e.g., streets, sidewalks and other third-party property restoration as part of its main replacement program) in the ordinary course of business. Fixing what the Company disturbs is proper corporate citizenship and basic decency. This is true for roads, sidewalks, plants, broken service lines of any material *and a disturbed lead service line*. These are all necessary and prudent expenditures. While necessary restoration work, Iowa-American has never retained ownership of those roads, sidewalks, lawns, plants, and other service lines.

The OCA also contends that it would be inappropriate for the Company to earn a return on the costs associated with customer-owned property not for public use.¹¹⁵ If utilities are prevented from recovering the prudently incurred costs of remediating and restoring customer, city and business property, work will grind to a halt. OCA's short-sighted opposition to the Company's LSL program is neither consistent with sound public utility ratemaking policy nor in the best interests of customers.

The Company will track customer-owned LSL replacement costs in a separate sub-account in Account 333 – Services to record LSL replacement costs. Only customer-side replacement costs will be included in this sub-account. Iowa-American will report those costs as part of its QIP filings and will also provide to the Board and OCA an annual report on the number of customer-owned LSLs replaced, the cost of those replacements broken down by customer rate class, as well as geographic location.

D. The Company's LSL Replacement Program Is Prudent and In the Best Interest of Iowa-American's Customers

Iowa American's customers will benefit from the replacement program as the risk of lead exposure from service lines will be reduced through implementation of the replacement program. The replacement costs to be recorded in a subaccount under Account 333-Services will enable Staff and OCA to determine which portion of Account 333-Services is related to lead service line replacement for easier review. Based on the foregoing and the record evidence presented in this case, Iowa-American respectfully requests that the Board find that the Company's LSL replacement program is in the best interests of Iowa-American's customers. The Board should, accordingly, approve Iowa-American's proposed Tariff revisions, and

¹¹⁵ OCA Initial Brief, p. 32.

authorize the Company to move forward with the replacement of customer-owned LSLs.

V. LOW-INCOME WATER ASSISTANCE PROGRAM

A. The Low-Income Water Assistance Program Is a Reasonable Program Needed Now to Assist the Company's Most Vulnerable Customers

As the COVID-19 pandemic and economy improve, Iowa-American understands that some of its customers will continue to struggle and did so before the pandemic as well. As a result, Iowa-American has proposed the LIWA to assist its most vulnerable customers to maintain access to water service in a cost-effective way. For all of its professed concern about affordability, OCA's entrenched opposition to the proposed LIWA program is difficult to understand. At the broadest level, the question facing the Board is whether the program will create an unreasonable burden. The evidence in this case demonstrates that it will not.¹¹⁶ While OCA argues that the program will make the rates less affordable for others, the opposite is true. This is not a "zero sum game." Iowa-American's bills are very affordable for the majority of customers. For the limited subset of customers who are struggling financially, the LIWA program is a valuable program that the Board should approve. Moreover, as discussed below, the cost of the program is not unfairly assigned to other customers.

B. The LIWA Program Is Consistent with the Statutory Scheme, Board Rules, and Iowa Precedent

OCA argues that the LIWA program violates Iowa Code §§ 476.3, 476.5 and 476.6. OCA's argument should be rejected because the program is not discriminatory and does not grant an "unreasonable preference." In making its argument, OCA mischaracterizes the holding of *State of Iowa v. City of Iowa City*.¹¹⁷ In the first place, the case OCA relies on was a dispute by a university with a city water system's pricing under a statute that differs from the one upon which public utilities are regulated. In any event, the Court held that the university did not prove the flat municipal sewer rates based upon water consumption charged to all customers, including the complaining university, were discriminatory. OCA ignores the Court's explicit finding, rejecting the university's claim, that "[r]ecognizing that ratemaking is an inexact

¹¹⁶ Tr. 319-321; Simmons Reply p. 12.

¹¹⁷ 490 N.W.2d 825 (Iowa 1992).

science, courts have determined that several other considerations beyond the actual dollar cost of providing service are permitted.”¹¹⁸ Here, Iowa-American wants to give its most economically challenged customers a small discount. The fact that other customers would support a small part of that discount does not make rates discriminatory. That is, using the court’s language, the resulting rates to customers are not “grossly out of proportion” to the burden they are placing on the system. *Id.* at 832. Perhaps even more important, OCA patently ignores the Court’s quotation of Justice Frankfurter’s admonition that “[i]t was a wise man who said that there is no greater inequality than the equal treatment of unequals.”¹¹⁹ Iowa-American seeks merely to use increased revenue related to higher consumption to provide a small rate discount for a class with unequal usage and very unequal economic means. This is hardly undue discrimination.

OCA also states that this case stands for the proposition that whether a rate is unlawfully discriminatory involves a consideration of whether one group of customers would subsidize another group. The Court made no such finding. Instead, the Court noted that subsidization may be a result of a discriminatory rate where the cost to serve the two customers, or the two classes of customers, is grossly out of proportion to the burden placed on the utility system by each of them.¹²⁰ Given the small discount under the LIWA program and the resulting very small impact on the rates of the other customers, this is not a case of the resultant rate being grossly out of proportion to the cost to serve either customer.

OCA further argues that Board Rules 19.12 and 20.14 authorizing flexible rates for gas and electric utilities should be utilized to determine whether Iowa-American’s proposed program is discriminatory. These rules do not apply to water utilities. Moreover, even if they were applicable, it is clear the flexible rate rules/tariffs are not intended to apply to individual residential customers, as the Board’s order adopting the gas and electric flexible rates rules and the notices commencing the rulemakings, make it is clear these rates and rules are geared towards business customers.¹²¹

¹¹⁸ *Id.* at 831.

¹¹⁹ *Id.* citing *Dennis v. United States*, 339 U.S. 162, 184 (1950).

¹²⁰ *Id.*

¹²¹ *In Re Incentive Rates for Natural Gas Customers and Electric Utility Customers*, Docket Nos. RMU-86-7 and 86-10 “*Order Adopting Rules*” (IUB 8/22/1986); see also the notices commencing the rulemakings published in the Iowa

Neither does OCA's citation to *Iowa Southern Utilities Co. v. Iowa State Commerce Commission*¹²² advance its argument as *Iowa Southern* only stands for the simple proposition that the Board decides as a factual matter whether rates are just and reasonable based on costs justified and policy considerations.¹²³ In that case, the Court determined that a 27% discount for utility employees was not just and reasonable. Unlike that case, Iowa-American seeks no rate subsidy, but instead to help its most vulnerable customers with a targeted rate for basic usage. In other words, a reasonable discrimination based on sound policy reasons.

OCA also suggests for the first time that LIWA is a charitable contribution. This argument should be rejected. Iowa-American cannot deduct LIWA amounts on its tax return, nor are individual customers charitable organizations. Instead, these individual customers would be paying rates determined to be just and reasonable by the Board.

Contrary to OCA's suggestions otherwise, there is no present program, nor future program, that is guaranteed to address this issue. Vulnerable customers should not have to wait for aid that may never materialize. Instead, the Board should utilize its authority to set just and reasonable rates, which can include the LIWA program, and which are clearly in the Board's purview.

VI. IOWA-AMERICAN'S OPERATING EXPENSES ARE REASONABLE AND SHOULD BE APPROVED

The unreasonableness of OCA's approach to this case is perhaps most apparent when one considers its position on Iowa-American's O&M Expenses. Company witness Nielsen provided extensive evidence of the Company's commitment to water quality, while improving water treatment effectiveness, safety and cost efficiencies.¹²⁴ The Company's efforts to improve water and energy efficiency includes supply-side

Administrative Bulletins dated 5/21/1986 and 6/4/1986. For example, the rules define "competing customers" as the customers who "make the same product, or offer the same service, or the same group of ultimate consumers."

¹²² 372 N.W.2d 274 (Iowa 1985).

¹²³ The Court found that "[T]he evidence shows the employee gas discount averages approximately 27.7 percent and the discount is not cost justified. Moreover, we do not believe it would be reasonable to approve a Company policy that encourages employees to ignore the actual cost of energy they consume." *Iowa Southern Util. v. Iowa State Commerce*, 372 N.W.2d 274, 277 (Iowa 1985).

¹²⁴ Nielsen Direct pp. 5-10.

practices such as improved pump efficiency, more accurate meter reading and leak detection, and main replacement and repair programs as well as demand-side strategies such as customer efficiency and public education programs to support water and energy efficiency.¹²⁵ Mr. Nielsen also explained how the Company's efforts to improve water, energy and operational efficiencies mitigate cost increases and protects the environment.¹²⁶ The Company's O&M costs in 2019 were less than its O&M costs in 2010,¹²⁷ and OCA Witness Kruger "applaud[ed]" the Company for its cost-control measures.¹²⁸

The Company is projecting test year O&M expense of approximately \$19 million in this case, which is only a 2 percent increase over the level approved in the 2016 case.¹²⁹ Moreover, although that Iowa-American is projecting O&M cost increases in this case, they arise because, as Mr. Nielsen further testified, Iowa-American is performing proactive condition assessments of its facilities and enhanced maintenance activities, including critical valve inspection program, chemical storage and delivery system modifications, flushing, leak detection, and hydrant inspection.¹³⁰ These efforts may increase operating expenses but they also improve operational integrity and mitigate operational risk.¹³¹ O&M costs also have increased because the Company has experienced an increase from locating lines as a new internet service company has been installing fiber optic cable in rights of way in the Quad Cities area.¹³² Importantly, OCA has not contested any of these Company efforts.¹³³

In preparing this case, the Company relied on Board precedent in proposing its O&M expense, with respect to the actual and projected number of employees authorized in the Company's organizational chart,¹³⁴ performance pay,¹³⁵ and interest synchronization.¹³⁶ OCA takes issue with these and in addition it

¹²⁵ Nielsen Reply pp. 14-16.

¹²⁶ *Id.* pp. 11-26.

¹²⁷ Moore Direct p. 7; Nielsen Direct p. 27.

¹²⁸ Tr. 379.

¹²⁹ Cephas Direct p. 5.

¹³⁰ *Id.*

¹³¹ *Id.*

¹³² *Id.*

¹³³ Nielsen Reply p. 14.

¹³⁴ *Iowa-American Water Co.*, Docket No. RPU-2016-0002 "Final Decision and Order", pp. 9-11 (Feb. 27, 2017).

¹³⁵ *Id.* p. 9.

¹³⁶ *Id.* pp. 13-14.

objects to service company costs and the inflation adjustment used to forecast certain expenses. In total, OCA proposes to reduce Iowa-American's proposed O&M expense by nearly a million dollars.¹³⁷ As will be shown, OCA's claims are exaggerated and misplaced.

A. Number of Employees

Iowa-American's projected employee level for the test year in this case is 77 and includes one unfilled position. OCA seeks to exclude all expense associated with the one position. It is generally recognized and commonly understood that employment levels fluctuate regularly in every organization, and probably at the Board as well. In the 2016 case, the Board approved the Company's labor and labor-related costs associated with the Company's projected employee levels, even though the Company was not at full employment at the time the case was filed. The Board should approve the Company's labor and labor related expense associated with full employment level of 77 employees.

B. Performance Pay

Performance pay has been included in every Iowa-American rate case since the performance pay plans were adopted in 2004 and 2007 and have never been challenged by OCA or the Board,¹³⁸ nor should they be. Performance pay allows Iowa-American to compete with other companies to attract a quality labor force.¹³⁹ The Company's plans include performance metrics for its employees including, safety, customer satisfaction, operational efficiency, as well as environmental and financial performance. OCA concedes that it has no objection to Iowa-American offering performance pay to its employees and it has no reason to conclude that the Company's total compensation package, including performance pay, is unreasonable.¹⁴⁰

OCA's claim that Board precedent on this issue is not relevant because the "plan has changed", is simply not correct. The performance pay plans have not changed. They are the same as those that existed in the 2016 case. OCA's real objection is that the number of employees who can participate in the plans

¹³⁷ Kruger Rebuttal p. 12, Table II.

¹³⁸ Nielsen Reply p. 17.

¹³⁹ *Id.* at 18.

¹⁴⁰ OCA Initial Brief p. 9.

has increased.¹⁴¹ Yet OCA ignores that having more Company employees incentivized by the plans to work to their highest capabilities is in the customers' best interest. OCA ignores that the Company's overall Labor and Labor-Related Expense including performance pay is less than the amount approved in Iowa-American's last rate case, despite the increase in the total number of employees and the increase in the number of employees who are eligible to participate in the performance plans.¹⁴² OCA's proposed exclusion of performance pay costs should be rejected.

C. Interest synchronization

Both the Company and OCA made interest synchronization adjustments in this case.¹⁴³ As explained by Company Witness Cade Simmons, the difference between their adjustments is that Iowa-American applied the appropriate interest rate from the beginning when it built its revenue requirement while OCA built its revenue requirement with the incorrect interest rate and then made an adjustment to reflect the appropriate interest rate at the end.¹⁴⁴ OCA completely ignores this testimony and simply states that its methodology should be approved. If OCA's methodology is applied to the Company's proposed revenue requirement, the result will be that interest synchronization will be applied twice and will "unsynchronize" the interest. OCA's proposed doubling of interest synchronization should be rejected, and the Company's methodology used.

D. Service Company Cost

OCA proposes that the Board reject the allocation of additional Service Company costs to Iowa-American that will result from the sale of New York American Water Company ("NYAW"), arguing that the costs are speculative and do not take into account cost reductions that will be achieved by virtue of the sale or organic and acquisitional growth that will cover the lost customers of NYAW.¹⁴⁵ In fact, it is OCA's case on this issue that is speculative. OCA has provided no evidence that any costs will be reduced by

¹⁴¹ *Id.* at 21.

¹⁴² Nielsen Reply p. 22.

¹⁴³ Tr. 177-78, 190-91, 279-83; Kruger Direct Exh. 2, Sch. F; Wilde Direct Exh. 1, ll. 12, 48-51; Wilde Reply Exh. 2, ll. 13, 43-46.

¹⁴⁴ Tr. 279-83.

¹⁴⁵ OCA Initial Brief pp. 11-12.

virtue of the sale or that there will be organic and acquisitional growth that will mitigate the loss of customers. In contrast, Company Witness Baryenbruch's testimony showed conclusively that most of the costs involved are fixed and that any anticipated cost reductions have been accounted for in the proposed allocation of the costs to Iowa-American.¹⁴⁶ There is no doubt that American Water intends to divest itself of NYAW. At that time, the Service Company costs previously allocated to NYAW must be reallocated among the remaining American Water subsidiaries. Mr. Baryenbruch has shown clearly that those costs are reasonable.

E. Inflation Adjustments

Iowa-American used an inflation factor to forecast certain test year O&M expenses that are not known and measurable at this time or because a three-year average of past expense was not a reliable indicator of expected future costs.¹⁴⁷ OCA's proposed forecasting method for these expense items is to simply assume these expenses will not change from the historical period (2019) through the future test year in this case (2022). OCA's effort to wish away inflation is simply not reasonable.

Iowa-American performed a check on the reasonableness of the use of inflation factors, comparing the total actual O&M expense for calendar year 2020 to the Company's projections for that period. The result is that the actuals for the 12 months ending December 31, 2020 were \$18.5 million compared with its \$18.4 million forecast, which includes the Company's pro forma inflation amount of \$79,564.¹⁴⁸ OCA claims that because the Company predicted that it would incur costs related to the COVID pandemic, 2020 should be considered an anomaly.¹⁴⁹ What OCA fails to acknowledge is that COVID-related costs are the subject of the Non-Recurring Expense Rider and are not included in the 2020 results. The use of 2020 results as a check on the propriety of Iowa-American's use of inflation factors to forecast certain O&M expenses is thus appropriate.

¹⁴⁶ Baryenbruch Rebuttal pp. 5-18.

¹⁴⁷ See Cephas Direct p. 4; OCA Kruger Direct Exh. 4, IAWC Response to OCA Data Request 189.

¹⁴⁸ Simmons Reply p. 9.

¹⁴⁹ OCA Initial Brief p. 10.

OCA further argues against the reasonableness of Iowa-American's use of inflation factors to forecast certain O&M expenses by claiming that the Company committed in the 2016 case that O&M expenses would be reduced through implementation of the QIP rider.¹⁵⁰ OCA misstates the record on this issue, too. Iowa-American has never claimed that current O&M costs will be reduced by the rider. During the hearing in this matter, OCA asked Company Witness Randy Moore to read several excerpts from his testimony in that case and that of Susan Krohn. An objective reading of the entire testimony of these witnesses, and that of Jeffrey Kaiser in the same case, is that the QIP rider will allow the Company to *avoid future O&M costs that would otherwise be incurred* in the absence of the QIP rider.

VII. RATE BASE

A. Capitalized Labor

Labor is capitalized when it is associated with capital projects; capitalized labor cost is included in rate base and recovered over time, rather than as an immediate expense.¹⁵¹ OCA agrees that it is appropriate to capitalize labor in such circumstances¹⁵² and for this reason, OCA has not proposed any adjustment to remove capitalized labor from rate base. OCA has only raised the subject to argue that the Company's overall O&M expense is not less than approved in the Company's last rate case.¹⁵³ However, it is to be completely expected that labor expense would decrease, and capitalized labor would increase due to the accelerated infrastructure program that the Company has put into effect. More labor hours are being expended on capital projects now than in the past.

B. Cash Working Capital-Collection Lag Days and Service Company Expense Lag Days

OCA's argument that Iowa-American should not be permitted to use its actual calculated collection lag days was rejected by the Board in the Company's 2016 rate case and there is no basis for the Board to depart from that precedent here. Prepayment of the service company bill by 4.61 days is reasonable because it supports cash expenses and payroll incurred by the Service Company on behalf of Iowa-American.

¹⁵⁰ OCA Initial Brief p. 10.

¹⁵¹ Tr. 379-80.

¹⁵² *Id.*

¹⁵³ OCA Initial Brief p. 9.

Moreover, OCA has not proposed an offsetting adjustment to Service Company expense, which would be required if OCA's position on expense lag were to be adopted. Given the precedent and OCA's failure to make any matching adjustment to expense, its position is not reasonable.¹⁵⁴

With respect to Service Company Expense Lag Days, Iowa-American used the same methodology as it did in its 2016 case, which was allowed in that case. Again, there is no need to depart from the methodology here.

VIII. UNPROTECTED EADIT AMORTIZATION PERIODS

OCA contends that Iowa-American should be required to credit all unprotected excess accumulated deferred income taxes amortization ("EADIT") to customers over a three-year period as an offset to the Non-Recurring Expense Rider, or through the current tax rider.¹⁵⁵ The Company has proposed to return all *plant-related* unprotected EADIT using the average rate assumption method ("ARAM").

It is worth noting again that the cost that gave rise to the EADIT benefit is not included in the Company's cost of service and has not yet been recovered from or funded by the customer.¹⁵⁶ It is also worth noting that, if the Board approves OCA's short amortization period, Iowa-American customers will see a steep increase in revenue requirement in a single year (approximately \$3 million), and customers over the entire relevant period will pay almost \$6.5M more in total revenue.¹⁵⁷

Both OCA and the Company agree that unprotected EADIT may be amortized over any reasonable period selected by the Board. Company witness Wilde's Attachment 2 details how alternative amortization periods for plant-related unprotected EADIT— 10 years, 20 years and 40 years – would be more cost-effective amortization periods for Iowa-American's customers than the short amortization period recommended by OCA.

¹⁵⁴ Simmons Reply pp. 7-8.

¹⁵⁵ OCA Initial Brief pp. 19; Kruger Direct pp 36-43; Kruger Rebuttal pp. 42-49.

¹⁵⁶ IAWC Initial Brief pp. 73.

¹⁵⁷ Wilde Attachment 2.

IX. RATE OF RETURN

A. Capital Structure

The only capital structure issue before the Board is OCA's attempt to relitigate the discarded double leverage adjustment through the artifice of a suggestion that Iowa-American has manipulated its capital structure. Nowhere, however, does OCA or its witness, Mr. Munoz, ever show evidence of such manipulation. Instead, OCA only offers the contention that because Iowa-American has not shown the source of funds for future test year equity infusions, manipulation must be afoot. Although OCA steadfastly argues that it is not engaging in a double leverage adjustment, OCA's remedy for this phantom manipulation is the double leverage adjustment that the Board discarded in the Company's last rate case.

The test year capital structure must include a projection of forecasted test year capital, including both debt and equity. Iowa-American's proposed future test year capital structure includes equity infusions totaling \$15 million that are planned to occur through June of 2022 in the form of paid in capital from American Water. These equity infusions will be used to pay down short-term debt that was and will be employed by Iowa-American to fund additions to utility property.¹⁵⁸ In addition to the equity infusions, Iowa-American also has three new debt issuances scheduled between 2020 and 2022.¹⁵⁹ The result of these infusions of equity and debt is a capital structure that is consistent with capital structure approved by the Board in the Company's last rate case and which is fully consistent with the capitalization of the proxy group used to determine the Company's ROE. OCA has not even tried to show otherwise.

In arguing for a lower equity ratio, OCA contends that its witness, Mr. Munoz, is "merely arguing that some capital infusions must not be included in equity balances because Iowa-American has not proven that they will in fact be funded with equity."¹⁶⁰ OCA argues that this treatment is appropriate because Iowa-American has not proven that the *future* equity infusions will be funded with parent company equity.¹⁶¹ OCA is essentially arguing that Iowa-American did not prove the impossible -- show the *source* of funds

¹⁵⁸ *Id.*

¹⁵⁹ Simmons Direct pp. 13-14.

¹⁶⁰ OCA Brief p. 63.

¹⁶¹ *Id.*

to be used by the parent, American Water, to make future equity infusions before those equity infusions even occur. That is what OCA witness Munoz calls “manipulation.”

OCA witness Munoz then proposes to “remedy” this alleged “manipulation” by applying Iowa-American’s parent company’s equity and debt cost rates to future equity capital, treating only 68.44 percent of the forecasted test year equity infusions as equity and the remaining 31.56 percent as long-term debt.¹⁶² OCA’s protestations to the contrary, Mr. Munoz’s manipulation of the equity infusion is clearly just another attempt to impose the double leverage adjustment. This cannot be disputed because the source of the funds that become equity infusions in Iowa-American is irrelevant. Once they become equity in Iowa-American, they are factually and legally “equity” with only the rights and obligations of equity securities. They are not debt, which Mr. Munoz, himself, conceded is an entirely different and lower risk investment.¹⁶³ No matter how much OCA tries to deny this fact, treating the parent’s future equity investments as partially debt is the very double leverage adjustment that the Board rejected in the last case. OCA’s continued denial does not change that one iota.

OCA then goes further out on a limb by trying to tie the Board’s stated vigilance for capital structure “manipulation” with a truncated quotation of the remedy the Board offered if it were to find such manipulation.¹⁶⁴ OCA conspicuously ignores the Board’s direct and unequivocal finding that the remedy for capital structure manipulation would be the use of a hypothetical capital structure:

...if manipulation is evident in future rate cases, the Board may address this issue in the same manner as other jurisdictions by imposing a hypothetical capital structure on the utility, if necessary. OCA acknowledges that other states use this instead of double leverage and that a hypothetical capital structure can help to address the concerns arising from a parent-subsidiary relationship. (Tr. at 298).¹⁶⁵

¹⁶² Munoz Direct p. 15.

¹⁶³ Tr. 218-19.

¹⁶⁴ OCA Initial Brief p. 64.

¹⁶⁵ *Iowa-American Water Co.*, Docket No. RPU-2016-0002 “Final Decision and Order, pp. 41-42 (I.U.B. Feb. 27, 2017).

Here, however, not only has OCA failed to prove any capital structure manipulation, but there is no need to deviate from Iowa-American's actual capital structure for the forecasted test year because it is in line with the proxy group and the capital structure found reasonable in the Company's last rate case.¹⁶⁶

OCA's lament, that Iowa-American's argument would prevent OCA from ever contesting equity infusions,¹⁶⁷ is self-evidently wrong and easily dismissed. If projected equity infusions would produce a capital structure that is unrepresentative of the way peer utilities are financed or that the Board finds unreasonable, all OCA need do is to show that. Here, OCA has not done so. The failure lies not in OCA's theory but in its utter inability to demonstrate that Iowa-American's capital structure has been manipulated or that the Company's current and proposed capital structure is unrepresentative of the way a water utility should be capitalized or how Iowa-American was capitalized in past cases approved by the Board.

B. Rate of Return on Equity

OCA contends that "[t]he Board should adopt OCA witness Munoz's return on equity because it is reasonable and consistent with recent decisions."¹⁶⁸ It is neither. OCA begins its polemic on rate of return on equity ("ROE") with a citation free discourse on the virtues of the Discounted Cash Flow ("DCF") methodology and its potential pitfalls.¹⁶⁹ One noteworthy admonition offered by OCA is its concern that, with the DCF "to ensure reliable results, the analyst must ensure that the proxy group companies fairly and accurately represent the business, risk and financial characteristics of the target utility."¹⁷⁰ OCA neglects

¹⁶⁶ Ms. Bulkley testified that "A hypothetical capital structure can be considered, especially if there are concerns that the actual per books capital structure is not reflective of the optimal capital structure for the company. The hypothetical capital structure can be based on comparable companies (e.g., set within the range of the proxy group) or determined by the commission based on other risk factors. Bulkley Reply p. 13.

¹⁶⁷ OCA Initial Brief p. 64.

¹⁶⁸ *Id.* at 65.

¹⁶⁹ OCA contends that the Board has considered but given little weight to methods other than the DCF. OCA Brief p. 65, citing Iowa-American's last two rate cases. Respectfully, that is not exactly what the Board said. What the Board said in the 2017 rate case (*Iowa-American Water Co.*, Docket No. 2016-0002 "Final Decision and Order" pp. 34-35 (I.U.B. Feb. 27, 2017)) was: "Both parties use the CAPM, either as part of the analysis or as a check on the DCF results. Historically, the Board has not given as much weight to any CAPM analysis because there were concerns about its reliability. However, more recently the Board has considered results from the CAPM method as another tool in its ROE determination and will do so here as well. . . . All of the models used by the parties produced results worth considering, although the Board has traditionally given more weight to some models than others. In this proceeding, none of the models appeared to produce results that were contrived or so unreasonable as to be thy of consideration after reflecting the adjustment to the proxy group."

¹⁷⁰ OCA Initial Brief p.66.

to realize that Mr. Munoz failed to adhere to this warning. Although he appears to recognize that a DCF result of 5.20 percent would not provide a sufficient risk premium to account for the additional risk associated with an equity investment, Mr. Munoz's proxy group average DCF result still includes DCF results of 5.8 percent for California Water Services Group and 6.0 percent for York Water.¹⁷¹ Mr. Munoz admitted that no regulatory commission has allowed a return for a water company in the 5 to 6 percent range in the last five years.¹⁷²

OCA next tries a sleight of hand by arguing that Mr. Munoz's Capital Asset Pricing Model ("CAPM") result of 9.5% doesn't really refute his DCF result of 9% because the proxy group contains gas companies that are riskier than water companies and, when the gas companies are removed, the resulting 9.1% CAPM supports Mr. Munoz's DCF.¹⁷³ There are more than a few aspects about OCA's claim that do not withstand closer investigation. First, OCA ignores the stunning circularity of its argument. Mr. Munoz's proxy group did include gas companies. OCA next asserts that the proxy group CAPM result is unduly inflated by two gas companies with betas above 1.0, which OCA argues renders them more risky than the group as a whole.¹⁷⁴ If, indeed, those two gas companies are riskier and their removal from the CAPM is deemed appropriate, query why they should not also be removed from the DCF. If that were done, Mr. Munoz's abnormally low DCF result would be driven even lower. In other words, adding and removing companies to prove that Mr. Munoz's CAPM confirms his DCF is more of a shell game than serious analysis.

OCA further claims that Mr. Munoz's ROE is closer to recently authorized rates of return on equity and that a few of those ROEs are lower than the ROE of 9.0% recommended by its witness.¹⁷⁵ Here, again, OCA is trying to hide the ball. The figure below, from Ms. Bulkley's Reply Testimony, shows the authorized returns for water utilities in other jurisdictions since January 2010, and the return recommended

¹⁷¹ Bulkley Reply p. 101.

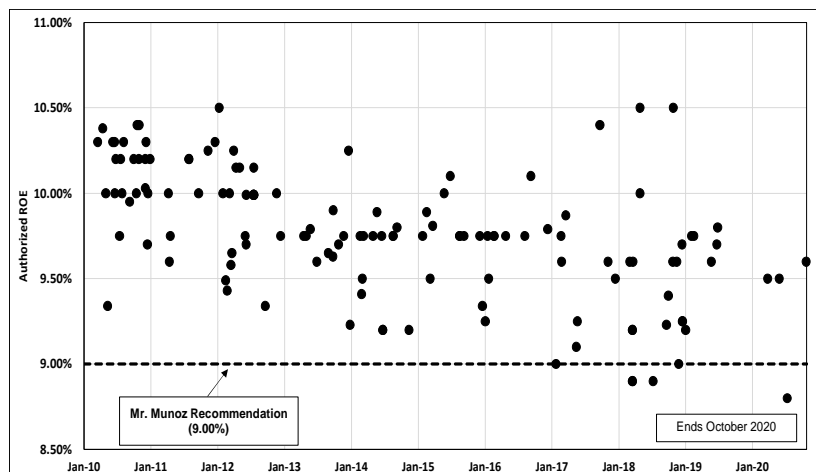
¹⁷² Tr. 237.

¹⁷³ OCA Brief p. 67.

¹⁷⁴ *Id.*

¹⁷⁵ *Id.* p. 69.

for Iowa-American’s water operations by Mr. Munoz. Mr. Munoz’s recommended ROE of 9.00 percent is only 20 basis points greater than the lowest comparable ROE authorized since January 2010 of 8.80 percent. Figure 8, below, from Ms. Bulkley’s Reply Testimony, shows starkly that the recommendation of Mr. Munoz for Iowa-American does not meet the comparable return standard.



OCA also ignores several important facts about the few authorized ROEs that were lower than Mr. Munoz’s. There was an ROE authorized that was lower than 8.80 percent during this time period; however, the referenced authorized 7.46% ROE should not be considered comparable because the ROE authorized by the South Carolina Public Service Commission for Blue Granite Water Company in Docket No. 2019-290-WS takes into consideration service quality issues.¹⁷⁶ With respect to the ROEs of 8.8% and 8.9%, they were both awarded by the New York PSC. They are also dramatically dissimilar from this case in several respects. First, they are settled, not litigated cases. Second, they are based on fully forecasted test years, with reconciliation clauses for revenue, purchased power and chemicals and property taxes – recovery mechanisms that Iowa-American does not have. Finally, the New York utilities were “permitted to retain 100% of earnings...up to and including 9.45%, with earnings above 9.45% and... up to and including 10.45% shared equally (50%/50%) between ratepayers and shareholders” demonstrating that the

¹⁷⁶ *Application of Blue Granite Water Company for Approval to Adjust Rate Schedules and Increase Rates, Order Ruling on Application for Adjustments in Rates* at p. 3 (SCPSC April 9, 2020).

New York commission found an ROE of 9.45 to be in a range of reasonableness.¹⁷⁷ When those factors are considered, Mr. Munoz's meager ROE of 9.0% remains a distinct outlier.

In an effort to try to paint Ms. Bulkley's recommended range of equity returns as unreasonably high, OCA focused only on the upper end of Ms. Bulkley's recommended range. Unlike Mr. Munoz, who – contrary to Board practice – identified only a single ROE and not a range, Ms. Bulkley noted that that updated market-based data for the proxy group companies as of November 30, 2020 supports a range of ROEs for Iowa-American between 9.75 percent and 10.60 percent.¹⁷⁸ Although Ms. Bulkley identified several factors that, in her opinion, argued for an ROE at the upper end of the range, that does not change the fact that her recommended range of reasonable ROEs is as previously stated.

OCA then contends that "this is not unreasonable quibbling by OCA" because Iowa-American filed its case based upon a 10.5% ROE. But, here, too, OCA proves too much. Ms. Bulkley clearly articulated various factors that would warrant the Board finding an ROE near the top of the range. She testified that "if Board were not to approve the RSM and expanded QIP and authorize an equity ratio below the Company's proposal, the reasonable cost of equity for Iowa-American would be at the highest end of my 9.75 percent to 10.50 percent range."¹⁷⁹ Ms. Bulkley also testified that the relatively small size of Iowa-American versus the proxy group companies would justify an ROE at the upper end of the range.¹⁸⁰ Iowa-American offered the Board compelling evidence of where that ROE range of reasonableness lies. In contrast, OCA neither offered a range nor a reasonable ROE estimate.

¹⁷⁷ *Proceeding on Motion of the Comm'n. As to the Rates, Charges, Rules and Regulations of Suez Water New York, Inc., Suez Water Westchester, Inc., and Suez Water Owego-Nichols, Inc., for Water Serv.. Joint Petition of Suez Water New York, Inc., Suez Water Westchester, Inc., and Suez Water Owego-Nichols, Inc., for Approval, Pursuant to New York State Pub. Serv. Law Sections 89-H and 108, to Merge and Become Suez Water New York, Inc.*, 2020 WL 4059533, at *17 [July 16, 2020].

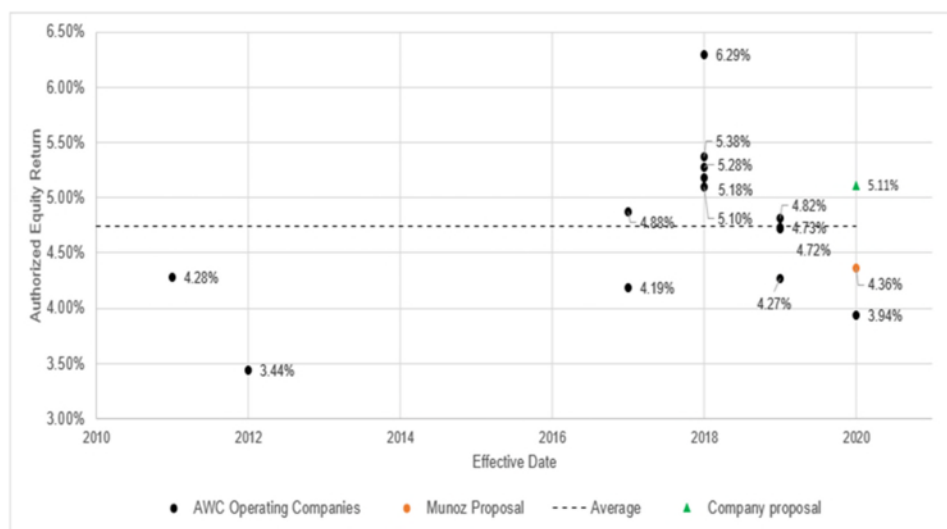
¹⁷⁸ Bulkley Reply pp. 10-11. OCA rather archly calls this range "a newly adopted range" (OCA Brief p. 70) but the only change was that Ms. Bulkley adjusted her previous range for an updated market analysis.

¹⁷⁹ Bulkley Reply p. 77.

¹⁸⁰ Bulkley Direct p. 79.

OCA's criticism of Ms. Bulkley's analyses¹⁸¹ should also be viewed with the caution such an unsupported attack merits. OCA, for example, scolds Ms. Bulkley for using the weighted ROE of 9.78% rather than the filed-for 10.5%.¹⁸² It is OCA who is confused, not Ms. Bulkley.

Ms. Bulkley used the chart printed below to demonstrate that Mr. Munoz's proposed weighted ROE of 4.36 percent is lower than the weighted equity returns of most of American Water's other operating subsidiaries,¹⁸³ which would place the Company at a distinct disadvantage in the competition for discretionary capital.



The Company "proposal" shown as 5.11% merely used the average authorized ROE of the American Water utility companies compared to the 52.28% equity ratio proposed by Iowa-American. Even if the weighted return had been derived using the top of Ms. Bulkley's ROE range of 10.5%, the 5.4% weighted result would not have been the highest of the affiliates and would not be appreciably different from the next two weighted costs of equity of affiliate companies. Moreover, nothing OCA says changes the fact that Mr. Munoz's weighted ROE cost rate would be among the lowest of the American Water affiliates and place Iowa-American at a distinct disadvantage in competing for discretionary capital.

¹⁸¹ OCA Brief pp. 70-71.

¹⁸² Bulkley Direct p. 79.

¹⁸³ Bulkley Reply p. 29.

Finally, OCA contends that, if the Board approves the RSM or the Company's proposed changes to the QIP, "the Board should recognize the significant reduction in risk and set Iowa-American's ROE at the lower end of reasonable ROEs."¹⁸⁴ Given that Mr. Munoz did not propose a range, but only a single ROE of 9.0%, it is unclear what OCA is really asking the Board to do. In any event, OCA's concept is fatally flawed.

Although Mr. Munoz concluded that Iowa-American's ROE should be reduced if the Board approves the Company's expanded QIP and RSM, it is not appropriate to conclude that, because a company has a capital tracking mechanism or a decoupling mechanism, that the ROE for that company should be reduced from the proxy-group derived result. As Ms. Bulkley explained, the appropriate approach is to compare the regulatory mechanisms of the Company to the regulatory mechanisms of the proxy group being used to develop the ROE.¹⁸⁵ If the Company is determined to have greater risk than the proxy group due to having fewer comprehensive regulatory mechanisms, then an ROE towards the higher/lower end of the proxy group results would be warranted. Mr. Munoz, however, did not review which companies contained in the proxy group had such mechanisms.¹⁸⁶ Absent this comparison, he had no basis to conclude that Iowa American has less relative risk than the proxy group.

Ms. Bulkley showed that a majority of the proxy group companies have both infrastructure and capital recovery mechanisms that address significant capital expenditure requirements and revenue decoupling mechanisms or other clauses that mitigate volumetric risk.¹⁸⁷ Because the proxy group companies have infrastructure recovery mechanisms and volumetric risk mitigation measures, Iowa-American would not have less risk than the benchmark group as a result of its proposed expanded QIP and RSM. Furthermore, to the extent that Iowa-American is not granted its proposed expanded QIP and RSM in this rate case, its risk would be substantially elevated, relative to the proxy group and a higher ROE within the range would be warranted.

¹⁸⁴ OCA Initial Brief p. 72.

¹⁸⁵ Bulkley Reply p. 76.

¹⁸⁶ *Id.*

¹⁸⁷ Bulkley Direct pp. 84 and 90 and IAWC Bulkley Direct Exh. 9.

The record supports the range of equity returns and the capital structure proposed by Iowa-American. The Company's equity ratio and ROE are comparable to other utilities, consistent with Board practice and appropriate for ratemaking purposes, while OCA's recommendations are below the ROEs and capital structures in place for comparable utilities. Iowa-American's proposed capital structure and ROE are supported by evidence, are consistent with the Board's practices and precedent and should be approved.

X. COST OF SERVICE AND RATE DESIGN

The Board should approve Iowa-American's Class Cost of Service Study ("CCOS") and rate design. While the OCA disagrees with the Company's allocation inputs for its CCOS, OCA has proposed no specific changes to the allocation methodologies utilized by Iowa-American and does not offer its own CCOS. Instead, OCA's proposed modifications to the revenue allocation to residential customers are based on OCA's changes to the revenue requirement, *not the allocation process itself*.¹⁸⁸ As a result, the Company's CCOS is the only cost of service analysis in the record, it has not been challenged, and it should be accepted by the Board.

OCA also criticizes the flat-rate ratios utilized by the Company to set rates. Instead, OCA appears to want to continue to negotiate rate design in the tariff compliance process, which is not appropriate and could indefinitely extend the case.¹⁸⁹ Instead, once the Board sets the revenue requirement in this case, then the CCOS proposed by the Company should be rerun and the flat rate ratios set to conform to the CCOS.¹⁹⁰ Setting the flat rate ratios to conform to the Company's CCOS does not mean a fresh debate as to rates.

XI. TARIFF ISSUES

A. The Board Should Approve Iowa-American's Proposed Tariff Changes Regarding Company Liability

OCA continues to fail to make any substantive argument against Iowa-American's proposed changes in the Liability of Company tariff.¹⁹¹ While it might prefer to open an entirely new proceeding and

¹⁸⁸ OCA Initial Brief p. 22; Tessier Direct pp. 7-11; Tessier Rebuttal pp. 6-7; Rea Reply p. 3.

¹⁸⁹ OCA Initial Brief p. 23.

¹⁹⁰ Rea Reply p. 11; Tr. 289-91.

¹⁹¹ Proposed Tariff Sheet No. 46.

assess the tariff in a different forum¹⁹² OCA does not argue that the Board lacks authority to approve the revised tariff in this general rate case. It merely states that Interstate Power and Light Company, in its own general rate case a few years ago,¹⁹³ withdrew a proposed liability tariff during that case. How this is relevant to Iowa-American's current request is not explained. And beyond the unsupported assertion that the issue "is too far-reaching and complicated" to be dealt with in a rate case, OCA does not try to explain why the Board is unable to deal with it here. Given OCA's failure to provide any legal grounds for its objection and given that such provisions result in lower insurance costs, Iowa-American respectfully requests that the proposed tariff be approved.

XII. CONCLUSION

For all the reasons discussed in the Company's Initial Brief and in foregoing Reply Brief, Iowa-American asks the Board to approve its Application for a rate increase in its entirety.

Dated this 4th day of May 2021.

Respectfully submitted,

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¹⁹² OCA Initial Brief pp. 58-59.

¹⁹³ *Interstate Power & Light Co.*, Docket NoTF-2016-0026 "Motion to Withdraw Tariff" filed with the IUB on July 8, 2016.