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Idaho Public Utilities Commission
Office of the Secretary
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AUG 13 2004

Boise, Idaho

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

Case No. RES-W-04-01

DIRECT TESTIMONY OF JANE DOE

FOR RESORT WATER COMPANY

Q. Please state your name.

A. My name is Jane Doe[1]

Q. By whom are you employed and in what capacity.

A. I am employed by Harbor Mountain LLC in the capacity of Financial Analyst.

Q. Please describe your professional training and employment history.

A. I have worked for Harbor Mountain for 1½ years as a financial analyst, and have provided financial analysis for the utility company and real estate division. I have a Masters in Business Administration from the University of Washington concentrating in Finance & Operations.

Q. In preparation for this rate case filing did you examine the financial books and records of Resort Water?

A. Yes I did. I examined the 3 previous years general ledgers.

Q. Please describe the condition of Resort Water's books as you found them and what you did to obtain an accurate picture of Resort Water's financial circumstances.

A. I chose a "test year" to explore thoroughly, and develop a representative financial operating scenario for the purposes of the IPUC test year presentation. The test year chosen was FY2003 (ending August 31st 2003). In my review of the company records, I found accounting errors, charges that would not occur under normal operating conditions, the absence of some normal operating charges that were not on the books, and incorrect allocations of general & administrative expenses. It was also apparent that hookup fees or

[1] "Jane Doe" is a pseudonym. The true identity of the witness and the reasons for protection of her true identity will be explained confidentially to the Commission and Staff.

impact fees collected from new customers were used to pay normal operating expenses of the company.

I made numerous adjustments to correct these errors. My adjustments are fully explained in my work papers that are being filed with this Application and they are available for review and audit by the staff.

Q. As a result of your examination of the company's financial records have you prepared exhibits that accompany your testimony?

A. Yes, I have prepared three exhibits. Exhibit No. 1 is entitled Statement of Operating Income; Exhibit No. 2 is entitled Rate Base Summary and Exhibit No. 3 is entitled Calculation of Revenue Requirement.

Q. Turning your attention to Exhibit No. 1, please explain the adjustment entitled "Accounting Errors".

A. As noted above, I found numerous accounting errors, most of which were Resort Water invoices that had been coded to the Cable TV division, and Cable TV invoices had been coded incorrectly to Resort Water. I reversed these errors for the purposes of this Application. The adjustment of $35,906 is the sum of all adjustments, the details of which are disclosed by my work papers.

Q. Please describe each of the adjustments shown in column C, Known and Measurable changes.

A. These changes were a combination of the following: Resort Water had a general and administrative division that captured costs associated with the Mountain Utility Company as a whole. For the purposes of this Application I allocated these across all divisions benefiting from its use: RWC, the sewer and cable TV divisions. The G & A general account was also allocated and dismantled during the FY2004 year.

In addition, there were costs of operation that were captured and paid at the Harbor Mountain Company level that had not before been charged to Resort Water, for example; insurance costs, accounting software license charges and management fees.

Q. Based on your analysis is Resort Water currently operating at a profit?

A. No. As shown on Exhibit 1, Resort Water lost more than $6,000 in the test year.

Q. Please describe Exhibit 2.

A. Exhibit 2, consisting of two pages, sets our rate base calculations. Currently, the company's books record depreciation based on expected tax lives. Exhibit 2 page 1 adjusts these accounts to use the depreciation lives for utility accounting purposes.

Q. Please describe the major items of investment the Company is proposing for inclusion in rate base as shown on Exhibit 2 page 1.

A. Item 001, **Acquisition Price Allocated**, represents the purchase price of the system when it was purchased from the United States Bankruptcy. The Company hired an appraiser who used the income capitalization approach to determine the value of the Utility Company. The Value of the Water Company was then extrapolated using an allocation based on a net operating revenue approach.

Item 002/012, **Water System Reservoir**, represents the construction of a 65,000 gallon reservoir. When Resort Water bought the system, there was only with a 40,000 gallon reservoir. That reservoir was insufficient to provide for the existing customers. The new reservoir was necessary to provide additional capacity.

Item 002/007, **Water System Improvement & Design**, represents capitalized engineering and planning costs necessary for the study and design of necessary system improvements including the Water Reservoir, Source Development, Distribution System Upgrades, and Back-up Power system design.

Item 003/011, **Water Source Development** represents the cost of drilling two wells to provide an adequate water source for Resort Water customers. One well is in service now, and the other will go in service with the new reservoir. The Idaho Department of Environmental Quality, required that the Company abandon a well due to surface water influences Before drilling the wells Resort Water had problems with serving Resort Water customers during peak demand.

Q. Please describe items in the company's asset accounts you are proposing to remove from rate base.

A. Exhibit 2 page 1 lists several items which are carried on the company's books but which are not currently used and useful in providing water service to our customers. These items have been removed from the rate base calculation.

Q. Please describe Exhibit 2 page two.

A. This summary page collects the adjustments from Exhibit 2 and contains additional adjustments.

Q. Please describe the additional adjustments shown on Exhibit 2 page 2.

A. <u>Line 1 Utility Plant in Service:</u> There are several assets listed on RWC books that are not relevant for IPUC purposes. The total purchase price of these assets equals $133,554.00 and they have been removed from rate base. <u>Line 2 Accumulated Depreciation</u>: The amount of $90,509.00 is the difference of accumulated depreciated under our company book depreciation methods and the IPUC recommended book depreciation method. The company depreciates water company assets on 25 year straight-line GDS method in accordance with Publication 946 Cat. No. 13081F page 106 (Department of Treasury, Internal Revenue Service). It is my understanding that the IPUC uses the class life for water utilities, which is 50 years. Line 5 Contributions in Aid of Construction: The amount of $66,757.00 represents all impact fees collected by Resort Water from 1999 to 2004 excluding impact fees collected in FY03 which is shown in column A, an amount of $61,851.00. I have assumed that these amounts should be subtracted from the utility plant in service, signifying a contribution to capital, rather than a normal revenue stream of the Resort Water used to cover operating expenses.

Q. Turning your attention to Exhibit No. 2, why are you proposing a return on equity of 11%?

A. It is my understanding that for water companies that meet the Commission's definition of "small water company" the Commission generally allows a return on equity of 12% in recognition of the risks inherent with a small customer base. *See for example,* In the Matter of the Application of Falls Water Company, Case No. FLS-W-03-01, Order No. 29307 (2003). Because Resort Water has revenues in excess of $50,000 and serves more than 300 customers it is not a "small water company" as defined by Commission rules. *See* IDAPA 31.36.01.101. Resort Water may not face the same level of risk as does a company like Falls Water, for example.

Nonetheless, for the reasons stated in Mr. Elsea's testimony the company faces numerous operational risks. Resort Water is certainly more risky that a large water utility, such as United Water, which currently has an authorized return on equity of

10.6%. *See* Order No. 28505. I believe an 11% return fairly reflects the relative risk faced by Resort Water, when compared to the returns allowed other utilities.

The owners of Harbor Mountain Company require that all its lines of business produce a return of 14%. Because a utility company may face less risk than the other existing lines of business the investors are willing to reduce the return expectation to 11%. It should be emphasized, however, that the investors to date have received no return whatsoever from the utility company and have invested since purchase an additional $500,000.00.

Q. Why are you proposing a capital structure consisting of 100% equity and no debt?

A. Because that is Resort Water's actual capital structure. Resort Water has not issued any debt; all of its capital is supplied by equity investment from its related companies.

Q. Please explain how you derived the net to gross multiplier.

A. The net to gross multiplier takes the effect of taxes into account. I used a 6.3% State Tax rate and a 32.795% Federal Tax rate.

Q. Based on your analysis how much additional annual revenue is required to meet Resort Water's annual operating expense and produce a reasonable return on investment.

A. $131,291.00.

Q. Have you calculated the monthly rate for water service necessary to produce the required revenue and what is that rate?

A. Yes. The additional required revenue per user per month would be $28.96. Added to the current monthly rate, the new monthly rate would be $61.96 per equivalent residential unit.

Q. The new rate is more than double the current rate. Why do you believe such a significant increase in rates is justified?

A. The Resort Water Company has not been operating profitably since it was acquired in 1999. It has used hookup/impact fees to supplement operating income required to run the business. The investors have spent $500,000.00 on improvements and maintenance of the system in the last few years, in addition to buying the water system for $355,000.00, and they have had no return on their investment.

Q. Does that conclude your testimony?

A. Yes it does.

Exhibit No. 1
Doe, Di

Resort Water Inc.
Statement of Operating Income

Test Year Ended August 31st 2003

			Accounting Errors	Known & Measurable Change	Projections		
	Decription	**(A) Company per Books**	**(B) Company Adj.**	**(C) Company Adj.**	**(D) Company Adj.**	**(E) Company Adj.**	**(F) Company Adj. Test Yr.**
1.	Operating Revenues	**$ 208,103.73**		$ (61,851.25)			**$ 146,252.48**
	Operating Expenses						
2.	Operating & Maintenance	**$ 128,457.03**	$ (35,906.03)	$ 26,309.10			**$ 118,860.09**
3.	Depreciation	**$ 43,307.52**		$ (22,181.60)			**$ 21,125.92**
	Taxes Other Than Income						
4.	Ad Valoreum Taxes (Property)	**$ 23,927.31**		$ (17,227.66)			**$ 6,699.65**
5.	Payroll Taxes	**$ 4,067.92**		$ 1,547.00			**$ 5,614.92**
6.	Total Operating Expenses Excluding Income Taxes	**$ 199,759.78**					**$ 152,300.58**
7.	Op Income Before Income Taxes	**$ 8,343.95**					**$ (6,048.10)**
	Income Taxes						
8.	State Income Taxes						
9.	Federal Income Taxes	$ -					
10.	Total Income Taxes	$ -					
11.	Utility Operating Income	$ 8,343.95					$ (6,048.10)

Exhibit No. 2
Doe, Di

Rate Base Per Books and Adjustments

		A Original Cost	B Per Books Depreciated Cost	C Asset Not Qualified	D IPUC Depreciated Cost	E Less Hookup Fees Collected	Company Adjusted Rate Base
000001	ACQUISITION PRICE ALLOCATED	$ 355,000.00	$ 287,550.01		$ 321,275.01		$ 321,275.01
000002	WATER SYSTEM RESERVOIR	$ 174,734.07					
000002	WATER SYSTEM IMPROVEMENT & DESIGN	$ 42,676.65					
		$ 5,560.25					
		$ 222,970.97	$ 185,561.39		$ 204,266.18		$ 204,266.18
000003	WATER SOURCE DEVELOPMENT	$ 216,263.66					
000003	WATER SYSTEM MASTER PLAN	$ 72,049.33		$ (72,049.33)			
		$ 288,312.99	$ 245,066.05		$ 195,988.95		$ 195,988.95
000004	FIRE HYDRANTS - CRYSTAL SPRINGS	$ 2,512.20	$ 2,135.37		$ 2,323.78		$ 2,323.78
000005	BAILEY WATER SYSTEM TIE-IN	$ 1,896.02	$ 1,611.62		$ 1,753.82		$ 1,753.82
000006	WATER DIST SYS UPGRADE	$ 11,395.65	$ 9,686.29		$ 10,540.97		$ 10,540.97
000007	WATER SYSTEM IMPROVEMENT & DESIGN	$ 5,037.74	$ 4,332.45		$ 4,685.09		$ 4,685.09
000008	WATER SYSTEM MASTER PLAN	$ 6,088.95	$ 5,236.49	$ (6,088.95)			
000009	FIRE HYDRANTS - CRYSTAL SPRINGS	$ 1,429.71	$ 1,243.85		$ 1,336.78		$ 1,336.78
000010	BAILEY WATER SYSTEM TIE-IN	$ 496.85	$ 427.31		$ 462.08		$ 462.08
000011	WATER SOURCE DEVELOPMENT	$ 5,793.57	$ 4,982.48		$ 5,388.03		$ 5,388.03
000012	WATER SYSTEM RESERVOIR	$ 10,014.32	$ 8,679.09		$ 9,346.71		$ 9,346.71
000013	WATER DIST SYS UPGRADE	$ 7,165.99	$ 6,234.41		$ 6,700.20		$ 6,700.20
000014	STORMWATER IMPROVEMENTS - SELKIRK	$ 458.85	$ 391.57	$ (458.85)			
000015	SNO CAT	$ 15,082.20	$ 8,618.40	$ (15,082.20)			
000016	UTILITY LOCATING / MARKING	$ 9,014.62	$ 7,992.93	$ (9,014.62)			
000017	WATER SYSTEM TREATMENT	$ 16,613.01	$ 14,730.21		$ 14,730.21		$ 14,730.21
000018	WATER SYSTEM PLAN & ENGINEERING (Outback	$ 18,539.46	$ 16,438.31	$ (18,539.46)			
000018	WATER SYSTEM ULLR to BAILEY's	$ 12,320.70	$ 10,924.34	$ (12,320.70)			
	SNOW MOBILE	$ 7,741.65	$ 5,591.19		$ 5,591.19		$ 5,591.19
	HOOKUP FEES COLLECTED TO DATE					$ (128,609)	$ (128,609.00)
		$ 997,885	$ 827,434	$ 864,331	$ 784,389	$ 655,780	$ 655,780

Resort Water Inc.
Case No.
Pro Forma Rate Base Summary
Test Year Ended August 31st 2003

	Decription	End of Year (A) Company per Books	(B) Company Adj.	(C) Company Adj.	(D) Company Adj.	(E) Company Adj.	(F) Company Adj.	(G) Company Adj.	(H) Company Adjusted Rate Base
1.	Utility Plant in Service	**$ 997,885**	$ (133,554)						**$ 864,331**
2.	Accumulated Depreciation	**$ 170,452**	$ (90,509)						**$ 79,942**
3.	Net Utility Plant	**$ 827,434**							**$ 784,389**
4.	Customer Advances for Construction								
5.	Contributions in Aid of Construction	**$ 61,851**	$ 66,757						**$ 128,609**
6.	Utility Plant Acquisition Adjustment								
7.	Accumulated Deferred Income Taxes								
8.	Pre-1971 Investment Tax Credits								
9.	Deferred Charges								
10.	Working Capital								**$ 16,172**
11.	Total Rate Base	**$ 765,583**							**$ 671,953**

Exhibit No. 3
Doe, Di

Resort Water Inc.
Calculation of Revenue Requirement
Test Year Ended August 31st 2003

1.	Rate Base	$ 671,953
2.	Required Rate of Return	11%
3.	Required Net Operating Income	$ 73,915
4.	Adjusted Net Operating Income Realized	$ (6,048)
5.	Net Operating Income Deficiency	$ 79,963
6.	Net to Gross Multiplier	1.642
7.	Gross Revenue Increase	$ 131,291