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IDAHO PUBLIC
UTILITIES COMMISSION

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF UNITED WATER IDAHO INC. FOR AUTHORITY TO INCREASE ITS RATES AND CHARGES FOR WATER SERVICE IN THE STATE OF IDAHO	**Case No. UWI-W-04-04**

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

REBUTTAL TESTIMONY OF JEREMIAH J. HEALY

Q. Please state your name and business address?
A. Jeremiah J. Healy, 8248 West Victory Road, Boise, Idaho 83709.
Q. Are you the same Jeremiah J. Healy who sponsored direct testimony in this case?
A. Yes, I am.
Q. What is the scope of your rebuttal testimony?
A. My rebuttal testimony will address the following:

- an update to my original Exhibit No. 2 that will include the Company's original overall rate request, the Idaho Public Utilities Commission's (IPUC) Staff overall position as proposed in their testimony and I will indicate the Company's overall rebuttal position. I will also update my original Exhibit No. 1, which again reflects the Company's original rate base position, IPUC Staff's position and the Company's rebuttal position and I will update Exhibit No.3. showing the same comparison with regard to operating expenses;
- an update to the Company position regarding adjustments to individual operating expense adjustments and I will address the operating expenses that remain in dispute between the Company and Staff.

Q. Please explain the organization of your adjustments.
A. Continuing the operating expense adjustment numbering scheme that I employed in my original testimony and Staff Witness English referenced in his direct testimony, I will address the following adjustments:

No.1 Payroll to Operations and Maintenance Expense,
No.2 401(k) Plan Company Matching Contribution,
No.4 Pension Expense,
No.6 Payroll Overhead,

No.7 Deferred Early Retirement Cost Amortization,

No.8 Deferred Enhanced Severance Program Amortization,

No.9 Purchased Water Expense,

No.11 Purchased Power Expense,

No.12 Amortization of Deferred Power,

No.14 Water Quality Testing Expense,

No.17 Transportation Expense,

No.22 Uncollectibles Expense,

No.23 IPUC Annual Adjustment,

No.24 Rate Case Expense Amortization,

No.25 Relocation Expense Amortization,

No.26 Business Insurance,

No.27 Adjustment Dues, Eliminate Lobbying and Charitable Giving,

No.28 Information Technology,

No.30 Expenses Related to Customer Growth,

No.31 Expenses Related to Weather Normalization,

No.32 Outside Expenses Legal,

No.38 Depreciation Expense and

No.41 Payroll Taxes.

Q. Have you introduced any new operating expense component that was not included in your direct testimony?

A. Yes. As indicated in the rebuttal testimony of Company Witness Wyatt, the Company is now proposing to adopt monthly billing in this proceeding after several parties to the case recommended it. Company Witness Wyatt has identified the additional annual expense associated with the conversion to monthly billing ($1,086,000) in his testimony. Should the Commission find monthly billing to be a prudent and reasonable expense, the incremental personnel expense, employee benefit expense, transportation expense and customer billing, postage and collection expense associated with this change in operations would have to be added to the Company revenue requirement. I have included as Exhibit No 15, Schedule 1, the Company response to Staff Production Request No. 38. This Response identifies in detail the expense items that produce the incremental $1,086,000 of operating expense.

Q. Please continue with the description of the scope of your rebuttal testimony.

A. As the third component of my rebuttal testimony I will address issues related to rate base. Company Witnesses Peseau and Wyatt will discuss the impact of the Staff's decision to utilize a thirteen-month average rate base. I have updated the Company's rate base schedules to reflect the most recent information on plant in service as provided through the Company's last update to Company Witness Rhead's Exhibit No.8 (filed Wednesday April 27 as a continuing response to Staff Production Request No.26, 2nd update). I will also discuss Staff's decision to cut off capital spend included in rate base as of December 31, 2004.

Q. What other specific rate base issues will you discuss?

A. I will address other issues as follows:

- Staffs discrete plant in service adjustments and the Company's position with respect to each adjustment
- Staff's decision to remove deferred power expense from rate base
- Staff's decision to remove deferred relocation expense from rate base
- Staff's decision to remove Carriage Hill rate base elements using the thirteen-month averaging technique

- Staff's calculation of Accumulated Deferred Income taxes
- The Company's adjustment to remove from rate base $175,000 of the Arrowhead Canyon Reservoir project
- Staff's adjustment to the equity gross-up of AFUDC

Q. Please briefly discuss your revised summary Exhibit's No's. 2, 1 and 3.

A. Exhibit No. 2 states the Company's overall rebuttal position in this case. As indicated, the Company now seeks a $6,785,523 rate increase with a rate base of $140,148,149 and a rate of return of 8.90%. Exhibit No. 1 indicates the elements of the Company's rebuttal rate base. Exhibit No. 3 indicates the Company's rebuttal position with respect to operating expense adjustments.

Payroll Expense Charged to Operations and Maintenance

Q. Please begin your discussion of the Company's rebuttal position with regard to operating expenses.

A. Staff Witness English reduces the Company's adjustment to payroll expense by $159,126 by the removal of the salary of the newly hired Public Affairs Manager of $56,500; the removal from inclusion in rates of incentive pay of $135,607 and a third category that includes the updating of employee wage and salary information and other minor issues that account for the balance of the difference, a negative $32,095. These figures represent a gross pay total of $160,012 and a net difference to operations expense of $119,869 when multiplied by the Company's ratio of payroll to operations and maintenance expense of 74.64%. The Company's revised rebuttal Exhibit No. 3, Schedule 1, Page 1 of 34 shows the details of the Company's rebuttal position of $3,348,453; this is $39,686 lower than our original position of $3,388,139.

Q. Please discuss initially the $32,905 reduction and what it represents.

A. Staff Witness English removes a total of $17,717 of pro forma wage increases for non-union employees beyond the 3.3% actual increase or $10,525; removes $4,238 of budgeted overtime pay above the test year level and removes the pro forma wage for the Chief Operator beyond the actual wage, an adjustment of $2,954. In preparing my rebuttal testimony, I re-priced all positions at the current known and measurable rates and derived a difference from my original pricing of negative $49,812. This represents not only the reduction of the merit increase for salaried from 3.6% to 3.3%, but also the fact that routinely when the Company hires a new bargaining unit employee to replace an existing employee, savings are realized because starting wages for entry level bargaining unit positions such as meter reader and utility person are substantially lower than the employee wage being replaced. The $49,812 actually increases the eliminations made by Mr. English of $17,717 by $32,905.

Q. Mr. English states in his direct testimony that he believes United Water employees are paid a generous base salary. What is your reaction to his belief?

A. First of all, Mr. English makes an exaggerated claim that United Water Idaho employees received an average base wage of $23.25 per hour in 2003 (English Di, pg 9). Included in this calculation are both non-exempt and exempt employees. Exempt employees are not paid by the hour; they are paid an annual salary and therefore should be excluded from his analysis. Based on the numbers included in this rebuttal case for bargaining unit employees of United Water Idaho, the 53 employees work 110,240 hours per year (2,080 X 53) for $2,299,406 or an average of $20.86 cents per hour. Mr. English also incorrectly states that United Water Meter Readers receive an average hourly wage of

$16.68 per hour (English Di, pg 8) compared to the national average of $15.58 per hour. He does, however, correct himself in his response to United Water Production Request No. 1 by indicating that the U.S. average wage is actually $16.58 per hour, not the $15.58 per hour wage stated in his testimony. This indicates United Water meter readers are paid right at the national average. Based on the numbers included in the Company's rebuttal case and assuming monthly meter reading is adopted, United Water Idaho's average meter reader pay will be $15.63 in the near future, almost a dollar an hour less than the national average.

Q. How does United Water Idaho employee pay compare to the pay of other local utilities such as Idaho Power?

A. Favorably. In Idaho Power Case IPC-E-03-13, Mr. English's colleague IPUC Staff Witness Alden Holmes testified in re-direct testimony, when addressing the generosity of Idaho Power pay, that he had conducted a variety of comparisons besides those used in his direct testimony. He states, "I compared the salaries to the average salaries of Intermountain Gas and United Water Idaho and found that Idaho Power salaries are substantially higher than those two companies (Holmes Re-Di, Pg.1485, lines 13 through 16).

Public Affairs Manager

Q. Do you agree with Witness English's removal from the Payroll to Operations and Maintenance Expense Adjustment the Salary of the Public Affairs Manager?

A No. Company Witness Wyatt discusses this issue in his rebuttal testimony. I have incorporated the position of Public Affairs Manager into my testimony and exhibits.

Incentive Pay

Q. Do you agree with Witness English's elimination of $135,607 of incentive pay United Water seeks to include in payroll and thus in customer rates?

A. No. Mr. English cites five reasons for eliminating incentive pay as follows:

- United Water Idaho already sufficiently compensates its employees with generous base salaries and benefits,
- Short Term Incentive Plan payments fluctuate from year to year and are not known and measurable,
- The objectives of the STIP are financial objectives aligned with the financial performance of a Parent Company,
- The STIP rewards an employee for merely doing a job they are already being compensated for,
- Incentive Plans are self-funding, they only make sense if savings achieved are greater than the amount of incentive payments made.

I will address Witness's English's reasons in order. First, Mr. English's characterization of United Water Idaho's employee pay as "generous" has already been shown to be at least partially if not totally without credibility. He was incorrect in his assertion that United Water's meter readers are overpaid, and his own colleague suggested in the recent Idaho Power Rate Case that Idaho Power employees are paid substantially more than United Water employees. Also as stated is this case, incentive pay is only $134,207 of total payroll dollars of $4,485,861, or less than 3%. This does not represent extravagant levels of incentive pay and the dollars are spread through every level of the organization. Second, incentive payments may fluctuate from year to year. However, many revenue requirement items do. Generally these items are normalized, such as purchased water in this case. The incentive payments United Water Idaho includes in this case are normalized. Third, of the eight employees who were STIP participants, seven of them had 10% of their goals tied to the financial performance of United Waters regulated business's as a whole; 30% was tied to the financial performance of United Water Idaho and 60% were not tied to overall financial performance. The other participant was 20%, 30% and 50%. There is no linkage between the financial performance of Suez and the STIP plan. There are several points I would like to make regarding this: Mr. English is incorrect, the bulk of STIP goals are directly related to United Water Idaho financial or non-financial objectives, not the financial goals of a parent Company. However, Mr. English seems to believe that financially oriented goals are not in the best interest of the customer. With respect to the 30 % of each STIP participant's goals that are concerned with the financial performance of United Water Idaho, I believe there are clear benefits to the customers of United Water Idaho. When department heads are held accountable for their budgets, the customer benefits. When department heads are challenged to innovate and be creative in their thinking to reduce costs or increase efficiency, this is in the best interest of the customer. Also, with respect to the 60% of goals that are not tied to financial performance, actual examples of goals in 2004 are as follows: Strengthening of production facility security; improve quality of real property records; investigate usage of a predictive dialer in place of 24-hour notice; automation of customer overpayment refund process; document "on the job training" for purchasing, dispatch and cross-connection functions; improve distribution facility security; develop plan to bring large meter testing in house;

develop meaningful "key performance indicators" and create a monthly report of same; streamline the billing processes for MJ's and bulk water sales and improve collection process; develop SOP's for new financial system; secure approvals and control of surface water rights for CWTP; strengthen relationships with community officials and leaders; develop and submit clean version of Rules and Regulations in rate filing; develop employee wellness program. These are all goals that may or may not pay for themselves but will improve customer service. Fourth, Mr. English believes that incentive payments compensate employees for doing a job they are already paid to do. In fact, the prevalence in compensation is to shift to a "total cash compensation policy", with less emphasis on base pay and more emphasis on variable pay. United Water has shifted its compensation philosophy from paying at the 75th percentile of the market place for base pay in year 2000 to paying at the market median. According to Investor Owned Water Utility Survey of 2004, an average of 81.3% of the positions surveyed which represent like positions to United Water Idaho's STIP eligible positions, participate in Short Term Incentive Programs. The minimum participation is 61.3% with a maximum participation of 100%. The purpose of STIP programs is to put pay at risk and have employees achieve stretch goals. This does not increase base pay and therefore does not increase benefit cost linked to base pay. Also, STIP goals should not be designed to have employees perform their normal jobs, but should be outside of their normal job descriptions. Fifth, Mr. English states incentive plans should be self-funding. However, in many cases, employee STIP goals are not intended to be self-funding but are linked to improving service. Examples of non self-funding goals are security related goals or goals that improve efficiency so as to delay the need for additional personnel.

Company 401(K) Match

Q. Please continue with Adjustment No. 2, the Company 401(k) employee matching contribution. Do you agree with Staff Witness English's elimination of the $1,321 adjustment?

A. No. Mr. English disallows the pro forma adjustment because "The Company simply took an estimated amount (contribution percentage) and multiplied it by another estimated amount (pro forma payroll) and claims the result is known and measurable" (English Di, pg 14). However, Mr. English largely accepted a pro forma payroll amount in adjustment No. 1 but fails to use it in this adjustment because it is an estimate. He also claims that the test year based calculation of the contribution percentage is also an estimate. In my opinion, the application of a contribution percentage based on actual test year employee participation rates, applied to pro forma payroll based on pay rates to be in effect April 1, 2005 meets the definition of "known and measurable" in this proceeding. The details of the Company's rebuttal position are indicated on revised rebuttal Exhibit No. 3, Schedule No.1, Page 2 of 34.

Pension Expense

Q. Please describe the situation with regard to pension expense, your adjustment No. 4.

A. The Company included in its direct case pension expense of $637,046, an adjustment of $12,279 over the test year level. This adjustment was based upon actuarial calculations performed in accord with Statement of Financial Account Standards No. 87 (FAS 87) and is consistent with methodology used in the past by the Company and accepted by this Commission. Staff Witness English has adjusted downward the pension expense to be recovered in rates by $474,592 to $162,454. The Company disagrees with the logic employed by Mr. English and Company Witness Degann, Executive Vice President of Aon Consulting, the Company's actuary, in his rebuttal testimony, will address this issue in detail. I have incorporated Witness Degann's recommendation into revised rebuttal Exhibit 3, Schedule 1, Page 4.

Payroll Overhead

Q. Please discuss Adjustment No. 6, Payroll Overheads and the Company's rebuttal position.

A. The Company has adjusted this "credit to expense" item from its original position of ($912,751) to a rebuttal position pro-forma credit of ($902,059), a reduction to operating expense of $42,264 from the test year credit of $859,264. This revised rebuttal position is shown on Exhibit 3, Schedule 1, page 6 of 34. Staff has recommended a gross credit of $925,229. The Payroll Overhead is a methodology to remove from operating expense a portion of employee benefits costs and a portion of non-productive employee time (vacation, holiday and sick time) and capitalize it or charge it to non operations and maintenance accounts such as inter-company labor or labor charged to merchandising and jobbing activities. The payroll overhead calculation is derived from the calculation of company payroll and employee benefit cost along with an additive for non-work days. The Staff accepted the Company's methodology and substituted their numbers for pro forma payroll, payroll taxes, health insurance, workers compensation insurance, pension expense and 401(k) matching contribution into the equation. In my rebuttal I have updated the formula to reflect the Company's opinion of the correct level of pro forma payroll and employee benefit cost.

Q. Is the Staff's adjustment to the payroll overhead credit correct? Please explain.

A. No. The test year level of account 922-000 was a negative $859,795 as indicated on my Exhibit No.3, Schedule 1, page 6 of 34 and also on my Exhibit indicating the Company's rebuttal position. Like any other pro forma adjustment, the pro forma level of payroll overhead credit should be compared to the test year level of such credit to properly reflect the adjustment to the test year. Mr. English's Exhibit No. 108, Schedule 6, calculates a pro forma level of overhead credit of $752,361 on line 6. However, on line 7 he compares this to an incorrect test year expense credit of $711,883, not the $859,795 I refer to above. Had he compared the pro forma level, $752,361, to the correct level of test year expense, $859,759, the adjustment would be $107,434. I do not understand why Mr. English indicates on line 23 of Schedule 6 that Staff's adjustment to the Company's filing is only $12,478.

Deferred ERP and ESP Amortization

Q. Do you agree with Staff Witness English's removal of the amortization expense associated with the Company's deferred early retirement plan expenses (ERP) and deferred enhanced severance package expenses (ESP) referred to in your Adjustment No. 7 and Adjustment No. 8

A. No, I do not. The rebuttal position of the Company remains the same as the original position.

Q. Please explain the removal by Staff Witness English of the Company's adjustment for recognition of the currently deferred costs associated with the Company's Early Retirement Program (ERP) offered in 2000.

A. Mr. English makes this adjustment for two stated reasons. First, the Company hasn't proven that the benefits exceed the costs and second, the Company didn't follow established regulatory procedures.

Q. Did Staff request the Company to provide an analysis of the savings associated with the program?

A. Not exactly. In Staff's Production Request No. 180, Staff requested a cost/benefit analysis. In all previous requests by Staff Witness English in the area of pension, he had acknowledged and accepted the fact that the information is provided on a Corporate-wide basis. All pension information requested had been provided on a total basis without Idaho-specific detail.

Q. Did the cost/benefit analysis provided to Staff show an overall benefit?

A. Yes. In fact, Staff stated that the analysis provided was prepared by the Company's actuary and that the study clearly indicated that on a United Waterworks level, there were significant savings, but on a United Water Idaho (UWI) level the savings were not so clear, (English Di. 26).

Q. Is it reasonable to assume that there were significant savings at the parent of United Water Idaho (the parent of utilities alone) and United Water Idaho incurred the costs without the savings like the balance of the other utilities in the group?

A. Not in my opinion. Mr. English acknowledges that the actuary calculates costs on a business unit basis and therefore costs recorded on United Water Idaho's books are not allocated from the corporate level but are those of United Water Idaho, (English, Di. 16).

Q. Staff performs calculations that determine the savings that United Water Idaho has derived from this program. Do you agree with the method used?

A. No. Staff simply took the combined salaries of the six employees that accepted the offer ($252,527 annually) and concluded that the savings don't justify the cost. This simplistic view is inaccurate and incomplete. There are savings beyond the salaries that include employee benefits such as reduced healthcare benefits, reduced pension and OPEB expense. According to the revised calculation of payroll overheads that is shown on revised Exhibit 3, Schedule 1, Pg. 6 of 34, the ratio of benefits expense to payroll expense is 63.03%. If I apply this to the salary savings calculated by Mr. English, the total savings are not $252,527 annually, they are $411,695, an increase in annual savings of $159,168. The customers of United Water Idaho have benefited from the savings from this program in this current rate case and will continue to benefit into the future through the continued savings. Some examples of the savings are certainly through a reduced employee complement and the associated salary and benefits costs. Additionally, there are savings that result from these employees being excluded from the development of pension and OPEB expense. The customers have also benefited through these savings since the savings allowed the Company to extend the time between rate increases.

Q. Is this program the same as that approved by the IPUC in the Company's last rate case?

A. Yes it is.

Q. Has Staff made any judgment about the Commission's approval of the 1999 ERP?

A. Yes and I disagree with the conclusion. Staff has acknowledged the Commission's approval of the prior ERP but takes no position and proceeds to remove the current costs of the 2000 ERP because the clear savings of the program can't be clearly seen at United Water Idaho based on Witness English's simplistic calculations. Companies like United Water Idaho pursue business efficiencies that will provide future savings for customers through programs like the ERP. If any company were to be denied recognition of the costs associated with implementing cost saving programs there would be little incentive for pursuit of such programs. The Company had no reason to believe that it wouldn't receive reasonable recovery of these costs when just one year earlier this Commission approved recovery of the costs of an identical program.

Q. Turning now to Staff's second reason for removal of the expense, please address the assertion that the Company didn't follow regulatory procedures.

A. Staff cites Commission action in an Idaho Power and an Avista proceeding as confirmation of the practice that a company must seek approval of a significant deferral, but continues by conceding that the circumstances surrounding the events in the cases cited as being different from that of United Water (English Di. 28).

Q. Staff further states that the Company did not seek, nor did the Commission grant, approval of the deferral which is a procedure clearly established by precedent. Do you agree with this statement?

A. No. Staff acknowledges that the Company sent a letter to the Commission notifying it of the costs that were being deferred and the intent to seek recovery in a future rate case. This procedure is consistent with the Company's actions for the 1999 ERP costs and consistent with the Company's internal policy for deferral of costs. The Commission has not previously objected to the Company's practice nor does the Commission have a specific rule requiring approval of a deferral.

Purchased Water Expense

Q. Moving on to Adjustment No. 9, purchased water expense. Do you agree with Staff Witness English's removal of $77,479 from the Company's pro forma level of purchased water expenses of $195,316, dropping the normalized level of expense to $117,837?

A. No. Company Witness Rhead discusses in his rebuttal testimony the unusual nature of the 2005 water year and its impact on the Company. I have incorporated into my operating expense adjustments Witness Rhead's recommendation of a normalized level of purchased water expense: $185,484 as indicated on his Exhibit No.16, Schedule 7. This represents a decrease of $9,832 from the Company's original filing, and an increase of $67,647 over Staff's position. The Company rebuttal position is shown on revised Exhibit No. 3, Schedule 1, Pg. 9 of 34.

Purchased Power Expense

Q. Moving on to Adjustment No. 11, purchased power expense, do you agree with Witness Sterling and Witness English's downward adjustment of $260,042 from the Company's original level of purchased power expense, $1,756,803?

A. No, I do not. First of all, the Company has updated its position to reflect Idaho Power Company rates proposed to be in effect June 1, 2005 in Case No. IPC-E-05-15. The rebuttal position of the Company is summarized on revised Exhibit 3, Schedule 1, Pg. 11 of 34. My understanding is that Idaho Power has requested a consolidation of Case No. IPC-E-05-10, a 1.84% overall ongoing increase related to the new Bennett Mountain facility. In Case No. IPC-E-05-14, Idaho power has requested an additional 4.45% increase in rates to Comply with Commission Order No. 29601 in Case IPC-E-03-13. 2.25% of the 4.45% increase is proposed to be an ongoing increase in base rates; the remaining 2.20% will expire in one year. The Company anticipates the Commission will issue its order in the Idaho Power proceeding prior to the hearing dates in United Water's case and these rates will be known and measurable in all respects. The Company's revised rebuttal power expense is $1,826,432, an increase of $69,629 from our original position. The $1,826,432 reflects re-priced test year usage for Schedule 7, Schedule 9 (secondary service) and Schedule 19P (Marden treatment plant) facilities, as well as all power necessary to run the raw water pump station that supplies the Columbia Water Treatment Plant (CWTP) and the plant itself.

Q. Why do you disagree with Staff's adjustment?

A. Staff Witness Sterling indicates in his testimony that he has removed the effects of Idaho Power's PCA from both the test year and from current rates. United Water Idaho, and I suspect all other Idaho Power customers, is acutely aware that the PCA is an integral part of the price paid for power. The PCA represents an expense to Idaho Power customers (including United Water) just as much as the kWh rate, the demand charge, the base load capacity charge, customer service charge or any other component of a power bill. United Water in this case is attempting to build known and measurable Idaho Power rate's into its base rates on a going forward basis, as well as recovering deferred power expense calculated in accord with IPUC Order No. 28800 issued in case UWI-W-00-1. Upon approval of rates in this case, United Water will cease deferral of power costs because our rates will then include current Idaho Power rates. For the record, the Company does accept Mr. Sterling's adjustment downward of $3,640 related to updated figures the Company supplied with regard to the cost of redundant power for CWTP.

Q. Please address Mr. Sterling's calculation of power expense for the CWTP and the raw water pump station and why you disagree with it?

A. Witness Sterling reduces the Company's estimated power expense for these facilities from $236,400 to $192,509, a reduction of $43,891. First, he again removes the PCA from the kWh charge. As I have explained earlier, this is incorrect. If Staff recommended that the PCA portion of all Idaho Power rates be removed from the calculation of power expense, and that the Company be allowed to recover the PCA portion of power expense through a customer surcharge, the Company may consider it. However, Staff has not recommended use of a surcharge mechanism to collect the PCA portion of power rates. Mr. Sterling's statement on page 32 of his testimony that he reduced the Company's $0.045 per kWh price to $0.0368 per kWh by removing the PCA is not logical nor is it fair to the Company to deny recovery of the PCA component of power rtaes in its revenue requirement.

Deferred Power Expense Amortization

Q. Please comment on Witness Sterling's position regarding your adjustment No. 12 for deferred power expense amortization of $516,667.

A. Mr. Sterling recommends that the total amount to be recovered should be reduced from $1,550,000 to $1,034,098 and the amortization period extended from the three-year period proposed by the Company to four years, thus reducing the proposed amortization expense by $258,142 and implying the Company should write off approximately $515,902 of deferred expense without recovery. He proposes that the Company be allowed to recover only costs deferred between May 2001 and May 2003 inclusive, an amount of $1,034,098 (Sterling Di. Pg.47), rather than the actual amount deferred in accordance with

Commission Order No. 28800 from May 2001 until the Company's next rate case award, or effectively through June 2005.

Q. What basis does Mr. Sterling use for this assertion?

A. Witness Sterling has interpreted the Commission's Order to conclude that the Commission did not intend to permit deferral of power costs due to poor water conditions but was only intended to "provide temporary relief from the extremely high power costs resulting from the short-term energy crises" (Sterling Di. Pg. 46).

Q. Are there any statements in Order No. 28800 that support Mr. Sterling's assertion?

A. No. A copy of the Order is included as Exhibit No. 15, Schedule 2. The Order recites that the Company requested a deferral of PCA costs "ordered by the Commission in Cases IPC-E-01-7 and IPC-E-01-11 and any subsequent PCA rate increase or related surcharge that may be authorized prior to the Company's next general rate case" (Order Pg.1 and 2). Also, the ordering paragraph of the Order provides, "The Commission does hereby approve establishment of a deferral account for incremental cost related to recent and future PCA related increases in Idaho Power Company electric power rates beginning May 1, 2001" (Order Pg.4). The Order does not limit the deferral nor does it specify that the Company be only authorized to defer increased costs if they are associated with certain events. In good faith reliance on the plain language of Order No. 28800, the Company has been deferring on its books and records excess PCA costs with the legitimate expectation that the Commission would allow amortization of these costs. These costs were actually incurred and paid by the Company to provide water service to its customers. Whether the PCA costs resulted from an energy crisis or poor stream flows is irrelevant. The expectation of permitted amortization is one of the factors that enabled the Company to extend the time period between general rate cases as opposed to United Water's recent sequence of cases.

Q. Was there any subsequent Commission Order modifying the original Accounting Order?

A. No.

Q. Mr. Sterling also proposes that the reduced deferral amount be amortized over a period of four years. Do you believe this is appropriate?

A. No. The Company has filed five cases in the last twelve years, or an average of a case every 2.4 years. In light of this fact, a thirty-six month amortization period seems appropriate. Mr. Sterling considers only the period between our current case and the immediately prior case. Second, he offers no support for "his belief" that the amortization period should stretch over a period at least as long as the time over which the deferral was accumulated (Sterling Di. Pg. 47).

Q. To summarize, what is the Company's rebuttal position with respect to the total amount of deferred power expense to be amortized and the amortization period?

A. The Company's position is that through the month of April 2005, the Company has deferred power expense on its books amounting to $1,456,596. This does **not** include a carrying charge. The Company has incurred an average deferral of $6,348 over the last four months and will use this average as a reasonable yet conservative estimate of the deferral to be recognized in May and June of 2005. Thus, the Company is requesting a recovery of total deferred power of $1,469,292. As stated above, the Company believes a three-year amortization period is appropriate. The annual amortization expense included in the

Company's rebuttal case is $489,764. This is $26,903 lower than our original position and $231,239 more than Staff's position. The details of this adjustment are shown on rebuttal Exhibit No. 3, Schedule 1, Page 12 of 34.

Water Quality Testing

Q. Do you agree with Mr. English's disallowance of $14,340 from the Company's pro forma level of water quality testing expense of $86,010, your Adjustment No. 14?

A. I partially agree. I agree with his adjustments for Nitrites of ($978; from $1,100 to $122) based on the fact the testing is required on a nine year cycle; I agree with his adjustment for Fe/Mn ($262: from $1,000 to $738); I agree with his elimination of $3,500 for miscellaneous testing since the Company was not able to provide a 10 year history of this expense. However, I disagree with his adjustment to the LT2ESWTR testing expense. Mr. English believes that because the Company will be required to expend $12,000 annually over the next two years (a total of $24,000) to comply with this mandated testing requirement, the Company should only be able to recover 1/5 of the annual level of expense or $2,400 annually rather than $12,000. His rationale is that the Company will only perform this testing for two years, and after that the Company will make a windfall by over-collecting for water quality testing expense. While this may be true with regard to the specific test in question, it fails to provide for the ever increasing number of test required, the increasing sophistication of the testing and the increasing number of contaminants to be tested for, and their associated costs. I believe a fair adjustment is to propose a compromise between the two positions by reducing the Company's original pro form testing expense by the sum of the three adjustments Mr. English makes that the Company does not contest ($978 + $262 + $3,500), $4,740, but retain the $12,000 annual LT2ESWTR testing costs. The details of this rebuttal adjustment are shown on rebuttal Exhibit 3, Schedule 1, page 14 of 34.

Transportation Expense

Q. Do you agree with the adjustment Staff Witness English made to transportation expense, your Adjustment No. 17, whereby he removes $18,661 from your pro forma expense amount of $406,265, reducing transportation expense to $387,404? Please explain.

A. Actually, I believe Staff erred in their calculation of this adjustment and I propose to correct the error. Staff Witness English states correctly that the Company suggested Staff remove the Mechanic position salary and benefits from this calculation as the Company had inadvertently included it twice. This amounts to $72,879. Mr. English also states that, in his opinion, the Company understated the lease disposal proceeds to be realized from the sale of lease disposals by $21,858 (his estimate of proceeds $53,300, the Company estimate $31,442). Thus, it appears Staff intended to remove a gross amount from the transportation "pot" of $94,737. When the transportation to O&M ratio of 68.69% is applied to the $94,737, an adjustment to operating expense of $65,075 is derived. Staff, however, appears to have removed only $18,861.

Q. Will the Company's rebuttal position incorporate this $65,075 downward adjustment to transportation expense? Please explain.

A. No. While I obviously agree with the removal of the Mechanic payroll and benefits expense, I do not agree with Mr. English's determination of the disposal proceeds to be realized on the sale of the vehicles. The Company's experience has shown that Company vehicles typically sell for 15 to 20% less than Kelly

Blue Book trade-in values. There are several reasons for this, chief among them: Company vehicles are not equipped with the types of options that non-utility buyers typically want and secondly, the vehicles sustain excessive wear and tear on their interiors and exteriors in the conduct of utility work. Mr. English stated to me that he intended to come to the Company yard on Victory Road to inspect the vehicles in question but he never did. I recommend in rebuttal only the net adjustment of $50,204 ($72,879 times 68.69%) for the Mechanic payroll and benefits, reducing the Company costs to $356,061. The details of this rebuttal adjustment can be seen at Exhibit No. 3, Schedule 1, Pg. 17 of 34.

Customer Postage and Outside Collection Expense

Q. With respect to your adjustments No. 18 and No. 19 for customer postage and outside collection expense, do you agree with Witness English's downward adjustment of $1,678 and $30,015 to these two items, respectively? Please explain.

A. No. The Staff agreed in their response to Company Production requests No.6 and No.7 that the Company positions were acceptable to them and their downward adjustments were withdrawn.

Uncollectibles Expense

Q. With respect to your Adjustment No. 22 for uncollectibles expense, do you agree with Staff Witness English's downward adjustment of $5,529 from the Company's pro forma expense of $131,045 to $125,516? Please explain.

A. No. The Company recognized the test year level of bad debt expense was high due to some unusually high bills written off in the test year. Consequently, a four fiscal year average was intentionally used to mitigate the pro forma expense from a test year level of $162,706 to a pro forma level of $131,045, a reduction of $31,661. The trend over the four years indicates a low but increasing percentage of bad-debt expense expressed as a percentage of annual revenue: 0.37% in fiscal 2001, 0.35% in fiscal 2002, 0.42% in fiscal 2003 and 0.52% in fiscal 2004. A four-year average composed of years ending in July 2004, 2003, 2002 and 2001 was also intentionally utilized so that it would encompass the period after the Company's last rate increase (September 2000) and reflect the fact that bad debt expense naturally tends to increase after a rate increase. The uncollectibles ratio for the year ended July 2000 was 0.34%, the lowest of all five periods. Mr. English states he is concerned with the Company's use of a four-year average of uncollectibles characterizing the choice of the four year average to be both arbitrary and purposefully chosen to eliminate consideration of prior years where the bad debt expense ratio was "significantly" lower. As explained above, the Company's use of a four-year average was not arbitrary and, in view of the trend information provided, he is correct that it was **intended** to eliminate prior years data that is not representative of the more recent trend. Also, Mr. English utilized a five-year period composed of years ending in December 2000, 2001, 2002 and 2003, however, his fifth "year" is the nine-month period ending September, 2004. The Company questions why Staff did not specify in their Audit Request No. 81, the response to which forms the basis of Mr. English's adjustment, that the ten year history be prepared on a fiscal year basis so as to be comparable to data the Company used. Use of a partial calendar year ending in September of 2004 could certainly bias the data downward as the bad debts from larger summer bills tend to be written off late in a calendar year, since they are not incurred until the months of latter July, August and September of the calendar year. Indeed, the bad debt ratio for the nine months ended

September 2004 was 0.431%. For the entire calendar year it was 0.446%. Thus, the Company maintains its original position and disagrees with Mr. English's reduction of uncollectibles expense of $5,529.

IPUC Regulatory Assessment

Q. Do you agree with Staff Witness English's reduction of the your Adjustment No. 23, the pro forma level of IPUC regulatory fee assessment expense from $75,823 to $72,347, a reduction of $3,476? Please explain.

A. No, but I do appreciate Staff Witness English's reasonable proposal that should the Company adopt a rebuttal position using the actual known and measurable 2005 actual assessment rate, Staff is willing to accept and incorporate the actual assessment into the revenue requirement. The actual assessment rate as communicated to the Company on April 20, 2005 by David Hattaway, Administrator, IPUC, is 0.2562 %. When applied to pro forma revenue of $31,540,460, the result is $80,807. This results in a change from the Company's original position of $4,984 and an increase over Staff's position of $8,460. The details of this adjustment are shown on Exhibit 3, Schedule 1, Pg. 23 of 34.

Rate Case Expense Amortization

Q. With regard to your Adjustment No. 24, amortization of deferred rate case expense, do you agree with Staff Witness English's disallowance of $12,500 of rate case expense related to the Company's public information campaign and do you agree with his extension of the amortization period three years to five years? The result of these adjustments is a reduction of $35,167 to the Company's original level of pro forma amortization expense from $81,667 to $46,500.

A. I will not contest the reduction of one half of the expenses due to the sharing of the costs of the public information campaign, however, the total Steele and

Associates billings are $17,065, not the estimated $25,000, so the appropriate reduction is $8,533. I do not agree with the length of the amortization period and I also have an update to total deferred rate case expense.

Q. Please elaborate.

A. The Company now expects to incur $305,000 in total deferred rate case expense (Exhibit 15, Schedule 3). The participation in this case by Staff and the other parties, the substantial discovery conducted, and the significant adjustments to the Company's case were all more intensive than anticipated based on the Company's prior rate case experience. All this has caused substantial additional effort to be expended by consultants and by our attorney. I reduce the $305,000 by the sharing of public information campaign expense of $8,533 to arrive at total estimated recoverable rate case expense of $296,467. This is detailed on Exhibit 15, Schedule 3 showing actual costs incurred to date and estimated costs to complete the case. Staff Witness English is of the opinion that because the Commission found a five-year amortization of deferred rate case expense reasonable in Idaho Power's recent case (Case IPC-E-03-13), then this is not only reasonable for United Water Idaho but consistent with the Idaho Power Order as well. The amortization treatment given Idaho Power's deferred rate case expense has no particular relevance in determining a reasonable amortization period for United Water's deferred expense. United Water's recent filing history is a more appropriate gauge and is as follows: beginning with Case BOI-W-90-1 filed in March 1990, United filed its next case (BOI-W-93-1) 34 months later; (BOI-W-93-3) followed eleven months later; (UWI-W-96-3) followed thirty months later; (UWI-W-97-6) followed seventeen months later; (UWI-W-00-01) followed twenty six months later and the present case followed fifty-seven months later. The average period between these cases was twenty-nine months. The three-year amortization period used by the Company is more realistic and conservative based on the actual experience of United Water Idaho. The correct amount of annual amortization expense in this case is $98,822. This rebuttal adjustment is shown on Exhibit No. 3, Schedule 1, Pg. 24 of 34.

Deferred Relocation Expense Amortization

Q. Please describe Staff Witness English's treatment of Adjustment No. 25, amortization of deferred relocation expense.

A. The Company requested $27,165, an increase of $1,477 over the test year expense of $25,688. Mr. English has recommended that the Company not be authorized to recoup any of this expense because Mr. English believes that $130,093 is too much to pay to relocate, from Southern California to Boise, a highly skilled employee. He also believes that the employment pool in Boise is large enough that the Company could have filled the position locally, or promoted from within.

Q. Do you agree?

A. No. I believe that given the population growth taking place in the Treasure Valley, there are many companies that relocate employees to the Boise area on a routine basis. I believe that local companies assist many of these new employees with relocation expenses to attempt to avoid the risk of loosing valuable experience. Relocation policies, similar to United Water's, are in place to encourage, rather than discourage, the employee to relocate. The Company contacted two local companies regarding their relocation policies that preferred their names not be disclosed, and following is a comparison of the attributes of their policies compared to United Water's. Company A and Company B provided the relocation policy information with the understanding that no disclosure of proprietary information other than the following table would be made:

Attribute	UWID	Company A	Company B
Duplicate Living Expenses	Yes	Yes	Yes
Extraordinary Living Expenses	Yes	Yes	Yes
Spousal Aid	Yes	NM	Yes
House Finding Allowance	Yes	Yes	Yes
Return Home Allowance	Yes	NM	Yes
Moving Household Effects	Yes	Yes	Yes
Misc. Moving Expenses	Yes	Yes	Yes
Home Relocation Assistance	Yes	Yes	Yes
Equity Advance	Yes	NM	Yes
Dual Mortgage/Rental Expense	Yes	Yes	Yes
Mtg. Interest Differential	Yes	Yes	No
Personal Tax Liability Allowance	Yes	No	No

The letters "NM" stand for not mentioned.

Excepting the Personal Tax Liability Allowance, both companies have very similar relocation policies to that of United Water Idaho. The Company currently has two long-term, highly qualified and experienced employees on board who have relocated to Boise after working for United Water at other locations: General Manager Greg Wyatt (1999) and Coordinator of Planning and Rates

Jeremiah Healy (1994). All of the moving expenses associated with the relocations of the named employees as well as those of the Company's prior President, William Linam (1996), were allowed in rates through an amortization provision in cases UWI-W-97-6 and UWI-W-00-1. The average relocation expense incurred by these three individuals, when adjusted by 2.5% annual inflation up to 2003, the year Mr. Vandegriff relocated to Boise, is $66,000. The only difference with regard to Mr. Vandegriff's relocation expense level is that he happened to live in a high cost of living area, which escalates residence selling and other related costs incurred by the Company. The Company agrees with Mr. English that Mr. Vandergriff's relocation expenses are high relative to the other examples cited, however, the correct answer is not to throw out the entire deferred expense. In light of the higher than normal level of relocation expense the Company proposes to share the relocation expense of Mr. Vandegriff with the shareholders absorbing $50,093 of the $130,093, and leaving $80,000 to be amortized over five years or $16,000 annually. The Company disagrees with the assertion made by Mr. English that the Company could have found a design-build project manager experienced in the construction of water treatment plants in the local labor market. In fact the CWTP is the only water treatment plant of its kind in all of Idaho and the probability of finding a qualified candidate for this highly sophisticated and technical role within the Boise area is small. Mr. English provides no support for his assertion other than conjecture. The Company acted prudently in its decision to bring the experience of Mr. Vandegriff to Boise to guide the CWTP project. Details of this adjustment are shown on revised Exhibit 3, Schedule 1, Pg. 25 of 34.

Business Insurance

Q. Do you agree with Staff Witness English's treatment of Adjustment No. 26, Business Insurance, in which he reduces the Company's pro forma expense from $1,083,300 to $899,036, an adjustment of $184,264? Please explain.

A. No I do not. Mr. English disallows a major portion of business insurance expense due to his belief that the expense is not known and measurable and is based on estimates and therefore speculative. The amounts in the Company's operating plan that Mr. English refers to as estimates are based on actual policy premium costs that were provided to Staff in the Company's response to Audit Request No. 50. The attachments to that audit request contained each type of insurance in effect for the Company for each of the last three years. The response further contained a summary of the insurance with its limits of liability, deductible, the supplier of the coverage, the policy period and the costs. Attached to that summary was the actual policy declaration page for each policy detailing the premium for each (See Healy Exhibit 15, Schedule 4).

Q. Are these policies specific to United Water Idaho?

A. No, however in the Company's response to Staff's Production Request No. 173, the Company supplied the explanation requested by Staff that illustrated how the amounts charged to United Water Idaho are derived along with an example of each allocation.

Q. Are the policies that were included with the Response to Staff Audit Request No. 50 current policies?

A. Yes. Most of the policies were renewed during 2004 and reflect current costs for 2005 and 2006 and therefore are not speculative or estimates. To summarize, the Company's rebuttal position is that the proper level of business insurance expense to be reflected in the revenue requirement is $1,083,300.

Elimination of Charitable Giving, Lobbying and Country Club Dues

Q. The Company had eliminated from the test year charitable contributions, lobbying related expenses and Country Club dues of $14,005. However, Mr. English goes on to remove an additional $17,433 related to scholarships ($3,800), Christmas Party and Summer Picnic expenses ($11,833) and additional lobbying expense ($1,800). Do you agree with Staff Witness English's treatment of Adjustment No. 27? Please explain.

A. First, the error Mr. English claims the Company made in computing the lobbying expense portion of the NAWC dues is in fact not an error at all. In a letter from the NAWC dated February 13, 2004 and attached in the Company files to the membership invoice, the NAWC clearly states " for income tax purposes, the percent of nondeductible dues attributable to lobbying expenses for 2004 has been estimated to be 18% (see Healy Exhibit 15, Schedule 5). The 27% Mr. English refers to is in fact related to the 2003 NAWC lobbying estimate. With regard to the very small amount of total operating expense the Company spent on water-related scholarships and employee events during the test year, Mr. English claims it is not appropriate to recover these costs from customers. United Water Idaho, in recent history (the last 15 years), has never had these types of expenses removed in a rate case. The Company is very frugal in it's spending on both scholarships and employee events and believes these expenses are reasonable and should be recovered in rates. They contribute to United Water's position in the community as a respected corporate citizen and emphasize the messages that the Company wishes to communicate to its customers, such as conservation and wise water use. In addition, Company employee events help in maintaining good employee morale, which fosters the delivery of good quality customer service.

The Company's rebuttal position is to respectfully disagree with Staff's position and restore the $17,433 to operating expenses.

Information Technology Expense

Q. What is your reaction to Staff Witness English's treatment of your Adjustment No. 28, corporate and local information technology expense in which he reduces the Company's pro forma level of expense from $156,140 back to the test-year level of $105,094, a reduction of $51,046?

A. I disagree with Staff Witness English's position. He claims that the Company's adjustment is not supported by contracts or agreements and that the increase is largely due to the conversion of the financial system software and that this conversion is not a recurring expense.

Q. Do you agree with his reasoning?

A. No. The Company fully explained, in detail, each component of the expense and what was driving the increase in each area. Admittedly, the Company neglected to attach the contacts, but the costs are fully supported by those contracts and agreements, which have subsequently been supplied to Staff (see Healy Exhibit 15, Schedule 6).

Q. Is Mr. English correct in his conclusion that the IT costs are non-recurring?

A. No he is not. While the Company's conversion of its financial system can be considered a nonrecurring event in the short term, the expenses associated with continuing operation certainly are recurring. The Company's response explained the need for continuing and new hardware support and maintenance, data communications lines, vendor supplied application support, hosting fees, licensing fees and Oracle database maintenance. These are annual expenses associated with the ongoing operation of the finance and accounting system and certainly recurring in nature. The Company's rebuttal position is therefore the same as it's original position, $156,140 included in the revenue requirement.

Customer Growth Related Variable Expenses

Q. Do you agree with Staff Witness English's position with regard to Adjustment No. 30, the reflection of additional variable expense associated with customer growth? Mr. English reduces the Company's $73,022 pro forma adjustment by $16,480 to $56,542? Please explain.

A. I have re-worked the adjustment (see revised Exhibit No.3, Schedule No. 1, Pg. 30 of 34) utilizing a combination of Company rebuttal positions and Staff positions. I have revised power expense to the Company rebuttal position; for chemical expense I accepted Staff's position; for transportation expense I reduced it to the Company rebuttal position; for business insurance I have included the Company's rebuttal position and for T & D excluding payroll I have left Mr. English's number unchanged. This produces a variable cost ratio of 12.76%. When this ratio is applied to Witness Gradilone's growth revenue of $749,828, the result is a $95,645 increase in variable costs due to growth, an increase of $39,103 from Staffs position and $22,623 over the Company's original position.

Weather Normalization Adjustment to Variable Expenses

Q. Do you agree with Staff Witness English's position with regard to Adjustment. No. 31, the impact of Mr. Gradilone's weather normalization and its impact on variable expense like power and chemicals? Mr. English increases the Company's pro forma credit to expense from $8,792 to $10,860, an increase of $1,888?

A. I do not disagree with the methodology, only the result. I have recalculated the Company rebuttal position using Staff's chemical expense and the Company power expense and applied the ratio (6.86%) to Mr. Gradilone's weather normalization revenue adjustment (negative $184,354) to produce a credit to expense of $12,641. This credit is $1,781 more than Staff calculated and $3,849 more than the Company's original adjustment. Please see revised Exhibit No.3, Schedule 1, Pg. 31 of 34.

Outside Legal Expenses

Q. Do you agree with Staff Witness English's position with regard to Adjustment. No. 32, outside services legal expense, where he decreases the Company's original pro forma expense from $54,000 to $36,355, a decrease of $17,745?

A. No. I do not think the methodology used by Mr. English to determine pro forma legal expense is correct. Mr. English reviews the test year legal expense spend and then eliminates items he characterizes as "extraordinary and unusual", $11,046. He also finds in the test year a modest amount of expense related to the Company's intervention in Idaho's Power's recent case, a total of $8,374 and decides to amortize that amount over five years, thus eliminating another $6,699 from test year expense. The Company, through years of actual experience, knows that each year various matters will arise in the routine course of business that require the services of outside counsel to resolve. These matters range from assistance in collecting past due accounts to contract review to minor regulatory assistance. Although Mr. English is correct that a particular legal issue and the costs of resolving it may not recur it is both illogical and inequitable to claim an underlying level of legal expenses will not recur. The Company's original position of $54,000 represents a fair and normal level of expense and thus our rebuttal position is the same as our original position.

Depreciation Expense

Q. Do you agree with Staff's calculation of depreciation expense of $5,845,188, representing a reduction of $541,321 from the Company's original position of $6,386,509? Depreciation expense is Adjustment No. 37. Please explain.

A. No. Obviously the depreciation calculations of the Staff and the Company vary significantly based on Staff's use of the thirteen-month average of test year adds and the fact they only allowed one-thirteenth of pro forma adds, other than CWTP investments. The Company has made several adjustments to depreciation expense on rebuttal: first, we have trued-up plant investment through the March 2005 forecast as discussed by Witness Rhead. I have incorporated this updated information into my rebuttal calculation of depreciation expense. I have also reduced plant $175,000 for an investment in the Arrow Head Canyon project that is recorded on the books and records of the Company in plant in service, however, the Company has not at this time paid the developer our share of the costs. I have also accepted Staffs adjustment to rate base of $258,772 of AFUDC calculated on the membrane order that was canceled and incorporated its impact on depreciation expense. I have accepted as well Staff's adjustment to plant in service of $684,962 for AFUDC gross up. The Company's pro-forma depreciation calculation in rebuttal is $6,372,848. This represents a $13,661 decrease from our original position and a $527,660 increase over Staff's position. This is shown on revised Exhibit No. 3, Schedule 2, Pg. 1 of 4.

Q Have you reflected Staff Witness Harm's recommended change in the depreciable life of the membranes from the life the Company proposed, 7-years, to the 10-year life Ms. Harms recommends?

A. No. Staff Witness harms bases her recommendation on hearsay. She claims she overheard a CDM representative say that the membrane filters are lasting ten years in many plants. The Company objects to the use of hearsay evidence and relies on the seven-year warranty of the membrane manufacturer.

Aggregate Payroll Taxes

Q. Do you agree with Staff's calculation of aggregate payroll taxes (FICA, SUTA and FUTA of $335,848 representing a $16,423 reduction from the Company's original position of $352,271? The aggregate payroll tax adjustment is Adjustment No. 41.

A. No, I don't. The Company has re-priced labor to reflect the most current known and measurable information. Base on this re-pricing, I have re-computed payroll taxes. The aggregate total is now $348,317. This is $3,900 less than the Company's original position and $12,469 more than Staff's position. This rebuttal adjustment is contained on Exhibit No. 3, Schedule 3, Pgs 2-4.

Rate Base

Q. Please continue with your rebuttal testimony regarding rate base. Do you agree with the methodology Staff has utilized to calculate United Water Idaho's rate base in general? Please explain.

A. No I do not. As indicated in the rebuttal testimony of Witness Peseau and Witness Wyatt, the Company disagrees with Staffs use of thirteen month averaging of the test year and the fact that, other than investment related to the

Columbia Water Treatment Plant, Staff has only allowed the Company to earn a return on one-thirteenth of pro forma investment. The difference in methodology makes it difficult to compare the Company's rebuttal rate base position with the Staff's position. I will provide an overview of the impact of Staffs approach, then I will address discrete adjustments Staff has made to rate base and the Company's position with respect thereto.

Q. Please continue with the overview.

A. Following is a summary of the elements of rate base and the numerical position of the Company and Staff:

	Company	**Staff**	**Difference**
Plant in Service	$259,567,713	$242,557,781	($17,009,932)
Accum Depr, etc	($ 60,180,731)	($ 57,087,076)	$ 3,093,655
Advances	($ 6,365,357)	($ 6,876,446)	($ 511,089)
CIAC	($ 43,009,699)	($ 43,202,977)	($ 193,278)
UPAA	$ 600,762	$ 600,762	$ 0
ADFIT	($ 13,938,270)	($ 14,521,667)	($ 583,397)
Pre-1971 ITC	($ 13,257)	($ 14,328)	($ 1,071)
Deferred Chg.	$ 1,945,796	$ 1,023,232	($ 922,564)
Work. Capital	$ 2,045,126	$ 2,045,126	$ 0
Grand Total	**$140,904,443**	**$124,524,407**	**($ 16,380,036)**

Obviously, plant in service accounts for the bulk of the difference. Following is a synopsis of the individual adjustments that make up the plant in service difference:

Plant in Service Adjustment Description

- Impact of 13 Month Average on Test Year Proper ($ 6,345,675)

- Impact of 13 Month Average on Pro Forma Plant ($ 8,791,833)
- Impact of 13 Month Average on Carriage Hill Adj $ 494,009
- Impact of 13 Month Average on Pro Forma Retirements $ 604,367
- Columbia Water Treatment Plant Group ($ 440,277)
- Company Arrowhead Canyon Adjustment $ 175,000
- Staff AFUDC Adj. on Membranes: Company Accepts $ 0
- Staff Adjustment: CWTP oversize land & building ($ 533,084)
- Staff Adjustment: Initial Butte Used & Useful ($ 677,452)
- Staff Adjustment: IMAP Used & Useful ($ 644,700)
- Staff Adjustment: Ground Water Recharge ($ 29,697)
- Staff Adjustment: AFUDC Gross Up: ($ 684,962)
- Staff Adjustment: Capitalized Incentive Pay ($ 135,630)

The first two bullets, lines 14 and 15, amounting to $15,137,508 of lost investment that is used and useful and currently providing service to customers have a devastating impact on the Company's case.

Q. Please address the remaining bullets regarding plant in service.

B. The bullets on lines 25 and 1 are a product of the thirteen-month average methodology. I believe that the Commission intended that Carriage Hill be completely removed from the books and records of the Company so I disagree with Staff's one-thirteenth removal (line 2). The retirement discrepancy (line 3) is also a product of the averaging methodology and serves to allow the Company to earn a return on plant that is no longer providing service to customers. The bullet on line 4 represents additional investment in the Columbia Water Treatment Plant that is included in the Company's rebuttal case as a refinement of actual investment. Line 5 represents investment in the Arrowhead Canyon project that is recorded as plant on the Company's books but is offset by a payable to the developer as final special facility contract details are finalized. Line 6 represents Staff's $258,772 adjustment to plant in service regarding excess AFUDC that the Company applied to membrane investment that was eventually repaid or written off. The Company accepts this adjustment. Lines 7 through 10 represent adjustments to plant in service made by Staff that the Company disagrees with. Company Witness Rhead addresses these four adjustments in his rebuttal testimony. The Company disagrees with Staff's adjustment on line 11 to plant in service of $684,962 representing the gross up for income taxes of the equity portion of AFUDC. The Company disagrees with the adjustment on line 12 Staff makes to eliminate capitalized incentive pay from plant in service ($135,630).

Q. Staff Witness Stockton is of the opinion that the Company is not correctly calculating its AFUDC rate applied to construction work in progress in its association with the gross-up of the equity portion of the rate. Do you have any comment?

A Yes I do. As stated by Witness Stockton, AFUDC recognizes capital costs associated with financing construction before it is placed in service and compensates the Company for the debt and equity costs before the asset is fully in service where it will then earn a return and depreciation expense during its service life.

Q. Is there authority and guidance for the application of AFUDC?

A. Yes. This authority and guidance resides in the National Association of Regulatory Utility Commissioners (NARUC) chart of accounts and in the

Financial Accounting Standards Board Statements (FAS) 71 (Accounting for Certain Types of Regulation) and 109 (Accounting for Income Taxes). Specifically, FAS-109 requires: "recognition of a deferred tax liability for the tax benefits that flow through to customers when temporary differences originate and **for the equity component of the allowance for funds used during construction"** emphasis added.

Q. Does Staff disagree with the equity gross-up and its application to capital projects?

A. No. Staff appears to recognize the need and requirement of the AFUDC gross-up and its inclusion as part of FAS-109, but believes that inclusion of the gross-up in the AFUDC calculation overstates the asset value and ultimately, rate base and concludes that the depreciation expense calculated on the higher asset value is where an adjustment is warranted.

Q. Rather than the theories set forth in numerous pages of testimony and other written guidance, can any of this theory be tested?

A. I believe so. I have prepared rebuttal Exhibit 15, Schedule 10, in an attempt to show the effect of the gross-up on the earnings and return on equity, both measures used in ratemaking and deficiency calculations. This exhibit shows how the Company's return on equity is calculated including and excluding the gross-up component. It illustrates that without the gross-up, the Company does not have the opportunity to earn its authorized return and because of this, a deficiency is created.

Q. Is there any other demonstration that can be made?

A. I believe that the depreciation of the plant that represents the AFUDC gross-up would be offset by lower tax expense because the tax liability related to the temporary difference would already have been recognized at the time the AFUDC was recorded. This being said, there would be no impact either positive or negative to the customer or the Company, which is the intent of FAS-109 that was designed to be neutral when the accounting is concluded.

Q. Please comment on Staff's recommendation that the Commission order the Company to analyze and restate all prior balances since the adoption of FAS-109.

A. Obviously the Company does not agree with Staff's assertion that it was and is recording this gross-up incorrectly and certainly does not agree that even if the Commission were to agree with Staff that it should be ordered to retroactively restate the past ten years of plant balances. The effort involved in such an undertaking is extremely large and would require a review of every asset, record of retirements, adjustments to deferred and current taxes, the depreciation reserve and other items. Staff's calculated estimate from May 2000 to the present only amounts to a rate base adjustment of $7,067 which includes the significant addition of the Columbia Treatment Plant additions. Certainly there is no material impact warranting such an effort.

Q. With respect to other utilities under its jurisdiction, has the Commission previously considered whether it is appropriate to gross-up the equity component of AFUDC for income taxes?

A. Yes. In a Washington Water Power case, U-1008-209, parties disputed the the proper amount of AFUDC to be allowed for a failed construction project. The Commission resolved that dispute then recognized that the allowed amount should be grossed up for taxes. The Commission said: "Finally, the amortization that we approve must be grossed-up to take into account marginal income tax rates. After applying the revenue-to-income multiplier, the total amount of amortization that we authorize for Skagit/Hanford is $8,575,000". Order No. 19411.

Q. Are there any Idaho statutes bearing on this issue?

A. Yes. Idaho Code 61-502A provides in part: "when construction work in progress is excluded from rate base, the Commission must allow a just, fair and reasonable allowance for funds used during construction or similar to be accumulated, computed in accordance with generally accepted accounting principles". By statute an allowance for funds used during construction is mandatory, and the allowance must be "just, fair and reasonable" and it must "be computed in accordance with generally accepted accounting principals". As I have discussed, the adjustment Staff Witness Stockton proposes meets neither of those standards.

Q Why do you disagree with Staff's elimination of the $135,630 in capitalized incentive pay?

A. For the reasons stated in my rebuttal testimony regarding incentive pay, the Company believes incentive pay is a reasonable way to motivate employees to perform at a high level. Because the Company believes in the legitimacy of incentive pay, and because it is reasonable to capitalize a portion of incentive pay, the Company disagrees with the removal of five years worth of capitalized incentive pay from plant in service.

Q. Staff Witness Stockton claims on page 4 of her testimony that AFUDC was improperly charged on water rights. She recommends that $94,918 be removed from plant in service and that her adjustment is incorporated into Staff Exhibit No. 101. Do you agree with her assertion? Please explain.

A. No I do not. First, Staff Exhibit No. 101 has to do with Staff's elimination from plant in service of the component of AFUDC associated with the gross-up of the equity portion for income taxes. I believe Staff Witness Stockton mentions this potential $94,918 adjustment but Staff failed to actually reflect the adjustment in their case. That being said, I disagree with Witness Stockton's blanket statement that it is improper to charge AFUDC to all water right related projects. Purchasing a water right may be a simple process in which case the newly acquired water right may provide service to customers very shortly after it was purchased. In this case, I agree that AFUDC would be inappropriate. However, the Initial Butte water right is an example of a water right purchase that the Company did accrue AFUDC on, and appropriately so. Funds were expended to purchase the Initial Butte water right under which water was diverted from the Snake River. After the Company purchased the water right, application was made to the Idaho Department of water resources to change the point of diversion to the Boise river. This process took several months time and until the water right was officially transferred, the asset was very similar in nature to CWIP. The funds were expended, the water right took time to perfect, and it was a legitimate application of AFUDC. Witness Stockton is mistaken, this has nothing to do with concepts of used and useful or plant held for future use. Once Initial Butte was perfected and the Company was able to use the water right asset, it was placed in service and the application of AFUDC was stopped.

Accumulated Depreciation, UPAA & PHFU Amortization

Q Do you agree with Staff's calculation of the balances of Accumulated Depreciation, Accumulated Reserve for Depreciation of CIAC, Accumulated Amortization of Plant Held for Future Use and Accumulated Amortization of

Utility Plant Acquisition Adjustments which reduce the Company's original aggregated balance from $60,180,731 to $57,131,443. Please explain.

A. No I do not. The driver of the large difference here is Staff's use of the thirteen-month average approach. I disagree with this approach for the primary reasons stated in Witness Peseau's rebuttal testimony: first, the use of the average is not consistent with the pro forma revenue and expense figures Staff has used in the case and second, the average methodology produces a result that denies the Company the ability to earn it's authorized rate of return. The Company's case is consistent in it's matching of pro forma revenue, expense and rate base. The Company pro formed the aggregate accumulated balances of the four components mentioned above consistently with the other elements of the case.

Advances for Construction

Q. Do you agree with Staff's calculation of Advances for Construction, $6,876,446, an increase of $511,089 over the Company's balance of $6,365,357? Please explain.

A. No. For the same reasons mentioned above for Accumulated Depreciation, I disagree with the use of the thirteen-month averaging methodology and the way it creates a mismatch in this case between revenue, expenses and investment. In addition, the Staff calculation does not reflect the full removal of Carriage Hill nor does it reduce the balance of outstanding advances for refunds that have been paid in the pro forma period.

Contributions in Aid of Construction

Q. Do you agree with Staff's calculation of CIAC of $44,202,977 or $193,278 more than the Company's calculation of $43,909,699? Please explain.

A. No. For the same reasons mentioned above for Advances for Construction, I disagree with the use of the thirteen-month averaging methodology and the way it creates a mismatch in this case between revenue, expenses and investment. In addition, the Staff calculation does not reflect the full removal of Carriage Hill as directed in the Commission Order.

Accumulated Federal Deferred Income Taxes

Q. Please describe Staff's adjustment to Accumulated Federal Deferred Income Taxes (AFDIT).

A. Staff increases the recorded balance of AFDIT at July 31, 2004 of $11,144,389 by $3,377,2799 to a pro forma balance of $14,521,668. This adjustment is wrong because Staff applies an incorrect tax depreciation rate to the utility plant additions it is recommending in this case. As a result, Staff has significantly overstated the adjustment to AFDIT.

Q. Please explain the error made by Staff in their calculation of tax depreciation.

A. Staff applied the special Bonus tax depreciation rate of 51% to both the 2004 and 2005 utility plant additions it is recommending in this case. The Internal Revenue Service (IRS) Code requires that the Bonus rate can only be applied to additions made by December 31, 2004 (see Exhibit 15, Schedule 9) since the Bonus rate is no longer in effect in 2005. This error is significant because the incorrect tax depreciation rate is applied to $19,707,594 of plant additions related to CWTP, which is largely a 2005 addition. The applicable IRS tax depreciation rate in 2005 for this plant is 2%. By using the Bonus rate of 51% for 2005 additions, Staff has overstated by $4,571,082 the amount of tax depreciation that is then compared to book depreciation. As a result the difference between tax and book depreciation is overstated by $4,571,082, ADFIT is overstated by $1,599,879, and rate base is understated by the same amount.

Q. Does the Company agree with the Staff's calculation of book depreciation in this case?

A. No, it does not since the Staff substitutes the actual book amounts with an average amount. However, for the purposes of illustrating the correction to Staff's adjustment to AFDIT, I have used Staff's recommended book depreciation expense.

Q. Have you prepared an exhibit showing a corrected calculation of the Company's tax depreciation based on the amount of plant additions recommended by Staff in this case?

A. Yes. I have prepared Exhibit 15, Schedule 7 illustrating the calculation of tax depreciation using 2004 rates for 2004 plant additions and 2005 rates for 2005 plant additions. If the Commission adopts the Staff average rate base, the corrected amount of tax depreciation as shown on Exhibit 15, Schedule 8 is $10,974,257. If the Commission also adopts Staff's calculation of book depreciation expense, the corrected ADFIT is increased by $1,777,400 to $12,921,789.

Q. Have you prepared an exhibit showing a corrected calculation of the Company's AFDIT based on the corrected tax depreciation amount and the Company's proposed plant additions?

A. Yes. As explained in detail in the Company's rebuttal testimony, Staff's average rate base is not proper ratemaking for United Water Idaho. Exhibit 15, Schedule

9 shows the correct tax depreciation of $14,355,365, ADFIT is increased by $2,793,881 to $13,938,270.

Pre 1971 Deferred ITC

Q. With regard to Witness Stockton's ITC adjustment of $1,071 to pre-1971 deferred ITC, do you agree it?

A. No I do not. She utilizes the thirteen-month average methodology and the Company has consistently disagreed with its use in all rate base applications and we disagree with its use here as well.

Deferred Charges

Q. Do you agree with the adjustments made by Staff to reduce by $1,008,460 the deferred debit balance of $2,031,692 the Company included in rate base? Please explain.

A. No, I have several adjustments that I disagree with and one adjustment I agree with. First, the Company has updated its position with regard to deferred debits to a balance of $2,630,758. The components of this balance are as follows:

• Power Expense	$1,469,292
• Rate Case Expense	$ 296,467
• Relocation Cost	$ 80,000
• Tank Painting	$ 77,162
• Deferred Rent	$ 18,998
• Terra Grande (agree with Staff)	$ 3,877
Grand Total	**$1,945,796**

Staff has recommended the disallowance of the balances of deferred power expense and deferred relocation expense. Staff has allowed deferred rate case expense of $232,500, which the Company has now updated to $296,467. Staff has allowed deferred tank painting at $77,162, deferred rents at $18,998 and deferred cost associated with Terra Grande at $3,877 and the Company agrees with these balances.

Q. Please discuss the two areas of disagreement, deferred power expense and deferred relocation expense.

A. The Staff objects to the inclusion of deferred power expense because, Staff Witness English states in his testimony (English Di., Pg. 32, line 17 to 22), "the Company was awarded a carrying charge on the deferred balance". In fact, the Commission Accounting Order No. 28800 approving the deferral of excess power cost did not award the Company a carrying charge and Witness English admits this fact in his response to Company Production Request No. 11. The fact is that the Company has spent and deferred, through April 2005, $1,456,596 in deferred power. The Company reasonably and conservatively expects to incur an additional $12,696 of deferred power expense by June 30, 2005. As in the case of deferred tank painting expense or working capital, the $1,469,292 total pro forma deferred power balance represents funds expended by the Company to provide service to customers. The deferral Order provided reasonable assurance to the Company that these costs would be recovered in the future. It is also prudent to allow the Company to earn a return on these funds as compensation for their use. With respect to deferred relocation expense, Staff Witness English believes the Company should not recover any of the expense it incurred to relocate an employee to Boise because the costs were excessive. The Company has reasonably rebutted his recommendation previously by sharing the expense with shareholders, reducing the balance to a level in line with the costs of prior employee relocation expense deferrals that have been recovered in rates as well as included in rate base in prior Commission orders. It is prudent to treat the deferred relocation expense balance in question in the same way.

Income Tax: Production Credit

Q. Please address Staff Witness Stockton's income tax calculation and her credit adjustment to income tax expense as a result of her application of the production credit from the American Jobs Creation Act of 2004.

A. Staff Witness Stockton uses a "proxy" to estimate the impact of the production credit on the federal income tax return of United Water Idaho. Witness Stockton uses a conservative "proxy" because the IRS has yet to provide guidance to the utility companies as to how to calculate the production credit. Witness Stockton stretches the concept of "known and measurable" to it's outer limits by guessing the intent of the IRS. Should the Commission believe it reasonable to "insure customers are not overcharged", as Witness Stockton seeks to accomplish, it could direct the Company to monitor the impact of the production credit in future rate years when the calculation of the credit will actually be known and measurable. The Company could be directed to adopt accounting procedures, if necessary, to track the benefit of the production credit and have this information ready should the Commission desire to review it.

Q. Does this conclude your rebuttal testimony?

A. Yes.