Q.Please state your name and business address?

A.My name is Robert E. Smith.  My business address is 472 West Washington Street, Boise, Idaho.

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

A.I am employed by the Idaho Public Utilities Commission.  My title is Senior Auditor.

Q.Please describe your educational background and professional experience.

A.I received my BBA degree majoring in Accounting from Boise State University in 1972.  Following graduation I was employed in the construction industry as Accountant/Office Manager until April 1975 when I accepted employment at the Idaho Public Utilities Commission.  During the course of my employment at the Public Utilities Commission, I have attended numerous training schools, programs and seminars in the field of regulation.

Q.Have you previously appeared as a witness in regulatory proceedings?

A.Yes, many times.

Q.What is the purpose of your testimony in this case?

A.I will present the Commission Staff’s recommendations concerning the Company’s Rate Base, Results of Operations and Revenue Requirement.

Q.Are you sponsoring any exhibits?

A.Yes.  I am sponsoring Exhibit Nos. 114 through 123.  Exhibit No. 114 presents Staff’s recommended rate base.  Exhibit No. 115, a two page exhibit, presents Staff’s adjusted Results of Operations which includes our recommended revenue increase of $1,080,581 shown on page 2, Column “Q”.  This revenue increase represents an increase in the Company’s rates of 4.88%.  Exhibit Nos. 116 through 123 are supporting schedules for adjustments made to the Company’s proforma rate base and operating results.

Q.During the course of your analysis in this case did you investigate transactions between United Water Idaho and it’s affiliated companies?

A.Yes.  I attempted to analyze the Company’s investment in the Information Technology (IT) program, increased costs for services provided by United Water Resources Management & Services Co. (M&S), increases in the Company’s vehicle leasing program, increased costs for computer service and support and other transactions between United Water Idaho and other affiliated companies.  Many of these transactions originate at United Water Resources world headquarters in New Jersey and I found the audit trail difficult to follow from United Water Idaho records.  Several conference calls between myself, Boise employees and employees in New Jersey were required to determine how various affiliated costs were determined and accounted for.

Q.Why were you concerned with these affiliated transactions?

A.The Company in the current case (UWI-W-97-6) has included nearly two million dollars ($2,000,000) in its rate base to recognize the investment in the new Information Technology Program, nearly one million dollars ($1,000,000) in expenses for fees paid to the M&S Co. and over two hundred thousand dollars ($200,000) of lease expenses arranged by the M&S Company.  These costs are significant and merit scrutiny in a rate case.  Of particular concern was the investment in the IT program.  This new investment is administrative only, producing no new revenues to help cover its cost.

Q.Are you proposing any specific adjustments to the Company’s investment in the IT program?

A.Yes, I will discuss later an adjustment to the Company’s depreciation expense.

Q.Did your investigation of the IT program raise any other concerns?

A.Yes.  Embedded within the IT program is a complete change in the Company’s accounting and time reporting systems and procedures.  The magnitude of this change raises the question of the quality of the test year data the Company is using in this case. Implementation of the new program was effective on January 1, 1997, midway through the test year.  One would expect that a change of this magnitude would initially produce a decline in efficiency and productivity as employees learn how the new systems function, learn new reporting procedures and identify and correct problem areas.  The Company, in response to Staff’s Production Request No. 53 stated:

...the Company has initiated a major

effort to completely replace its data

processing systems as discussed in the

testimony of Company witness Linam.

While these efforts have resulted in

some reductions, there were also off-

setting increases.  The full benefit

expected to result from the new systems

will not occur immediately but will occur

over time.  (emphasis added)

These productivity concerns are difficult to quantify.  I found auditing the test year using two accounting systems and general ledgers challenging.

Q.Where does United Water Idaho fit into the overall corporate structure of United Water Resources Inc.?

A.United Water Idaho is one of approximately eighty-two (82) operating units, both utility and non-utility, operating in fourteen U.S. states, Mexico, Canada and the United Kingdom.  A few of these appear to be paper shells for accounting convenience and consolidation purposes.  Exhibit No. 116 is a flow chart of the “United Water Resources Financial Reporting Rollup Structure.”  United Water Idaho is shown in the box at the bottom center of this exhibit.  For convenience, I have marked the location with an arrow.

Q.What is the magnitude of total charges made to United Water Idaho by affiliated companies under the United Water Resources Inc. corporate umbrella?

A.According to the Company’s response to Staff’s Production Request No. 71, the magnitude of these charges on the records of United Water Idaho were approximately $7.2 million dollars for the twelve-month period ended June 1995, $4.8 million dollars for the twelve-month period ended July 1996, and $4.0 million for the twelve-month period ended June 1997.

Q.Do you believe these charges are all reasonable?

A.It is difficult to tell.  I am sure many of the charges are justified but many of the charges may also be excessive for the Idaho operation.  What may appear to be a good corporate decision for United Water Resources Inc., U.S. or worldwide operations may not necessarily be the most economical decision for the Idaho operation in isolation.  My discussion in this testimony regarding the vehicle lease program is a case in point.  These corporate decisions may produce inter-corporate subsidies among the operating units.  The audit trail working from United Water Idaho records in Boise is often difficult to follow.  Many of the source documents are located in New Jersey.  Entries into the accounting records of United Water Idaho for affiliated transactions are most often performed by the corporate personnel in New Jersey.  The magnitude of these corporate charges would go a long way toward paying for local administrative and engineering services and stimulate the Boise local economy rather than the New Jersey economy.

Q.United Water Resources Inc. together with its subsidiaries is audited regularly by external accounting firms and the Internal Revenue Service is it not?

A.Yes.

Q.Don’t these audits provide assurance that United Water Resources Inc. is correctly accounting for its financial transactions?

A.These audits are intended to verify the accuracy of the corporate accounting transactions and insure that the financial statements and income tax returns of the corporation are presented fairly.  These audits do not provide the assurances a regulatory commission needs to insure fair, just and equitable rates.  These auditors do not care whether one of the consolidated subsidiaries is earning 5% or 50% return on equity.  Their only concern is that the total combined financial and tax reports are accurately presented.

Q.During the course of your review did you notice any other specific activities that led you to question United Water Idaho’s relationship with its affiliated companies?

A.Yes.  The United Water Resources subsidiary company operating in Rio Rancho, New Mexico was lost through a municipal condemnation proceeding.  The corporation received approximately $67 million that must be reinvested in like assets to avoid paying income taxes on a $4.3 million gain realized on the sale.  The $67 million reinvestment can be made by any one of the subsidiary companies or spread out among several or all of them.  This fact together with the recent construction and acquisition activity of United Water Idaho raised the suspicion of Staff regarding not only the timing but the need and the cost of construction and acquisition activities.  Staff witness Lobb in his testimony discusses some of Staff’s concern regarding timing and need for several of the Company’s recent Idaho projects.

Q.Has Staff made any adjustments to the Company’s rate base as a result of these concerns?

A.Yes.  Exhibit No. 114 presents Staff’s rate base recommendation including several adjustments for both acquisitions and construction projects as well as capitalized costs charged to Idaho by the M&S Company.

Q.Will you please explain the development of this exhibit?

A.Column “A” of the exhibit is a restatement of the proforma rate base proposed by Mr. Gennari on Company Exhibit No. 4, Schedule 1, page 2.  Columns “B” through “G” eliminate certain construction projects and acquisitions from the rate base.  Column “H” corrects an oversight in the Company’s case to retire old computer equipment.  Mr. Healy and I have discussed this adjustment and we agree.  Column “I” makes a correction for a change in the Company’s plans for replacing a vehicle and eliminates some capitalized costs of the Company’s vehicles leasing program.  Column “J” reflects Staff’s proposed rate base for this case of $80,901,734.

Q.Are you sponsoring testimony to discuss all of these adjustments?

A.No.  Staff witness Lobb discusses the adjustments shown in Columns “C”, “D” and “E” in his testimony.  Both Mr. Lobb and I discuss the adjustment shown in Column “B”.  I will discuss the remainder of the adjustments.

Q.Why do you propose to make the elimination shown in Column “B” to remove from rate base the Company’s acquisition of the Garden City service area?

A.Staff addressed its initial concern with this acquisition in Case No. UWI-W-95-2 when the Company first came to the Commission for approval of the exchange of service areas with Garden City.  Commission Staff Auditor Faunce expressed Staff’s concern in her testimony in that case.  I have reviewed that testimony and concur with her recommendations.  Simply put, Staff opposes including United Water Idaho’s acquisition cost in rate base for assets that were originally contributed by developers to public service.  Neither Garden City nor United Water contributed any capital for the construction of these facilities.  They were constructed with a combination of developer contributed funds and customer connection fees collected by Garden City.

Q.Did the Company provide Staff with an analysis of this acquisition that indicated that it was providing sufficient revenues to support the cost?

A.Yes.  However, absent from that analysis was any recognition of source of supply investment displaced to provide service to those customers.

Q.What do you mean by the term displaced?

A.In order to provide service to these customers, the Company had to use its existing investment in wells, reservoirs and water purchase contracts.  Use of these existing water supply sources to serve these customers hastens the need to add new water supply sources at incrementally higher cost.

The exchange of service area with Garden City was a discretionary decision made by the Company and municipal authorities.  The affected customers were already receiving adequate service from the Garden City water system.  Adding the cost of the acquisition to the Company’s cost of service without recognition of the additional burden placed on existing customers would create an injustice.  It would require the existing customers to forfeit their claim to water supply sources already embedded in the rates they pay.  Were the Garden City system owned by another public utility, as was Warm Springs Mesa, the transfer would have been subject to the accounting instructions contained in the Uniform System of Accounts adopted by this Commission.  Those instructions require that the assets would be recorded at the original cost when first devoted to public service.  Accumulated depreciation at the date of transfer would also be recorded.  Any excess cost would be recorded as an Aquisition Adjustment on the books of the purchasing utility.  For ratemaking purposes, the Commission could either include or exclude the balance in the Acquisition Adjustment Account in the Company’s rate base.  That determination is usually based upon an analysis of the effect on consumers.  If it is demonstrated that inclusion of the adjustment does not impose additional incremental cost to the consumer it may be allowed.  The mere fact that the selling entity is a municipality rather than a regulated public utility is not sufficient reason to abandon this basic principal.  In essence, this principal is intended to replicate circumstances that would exist today had the purchasing utility been the original provider of service.  Had United Water been the original provider, it would have exactly the same investment, accumulated depreciation and contributions on its books at June 30, 1997, would be in exactly the same water supply position but would not have the additional net investment of $577,664 requested in this case.

Absent this acquisition, United Water Idaho today would be in a better water supply position to meet future customer growth.  It is obvious that the consumers will be penalized should the Commission allow the Company to earn a return on the Acquisition Cost Premium coincident with the reduction in water supply resources available for future growth.

Q.You indicated that Staff witness Lobb addresses the adjustments shown in Columns “C”, “D” and “E”, so, moving on to Column “F” of this exhibit, why have you eliminated from rate base $78,432 that you term “Equity Gross-up AFUDC”?

A.This is another example of decisions that are made at the United Water Resources corporate level that affect the local operating subsidiary companies including United Water Idaho.  In July of 1995 a decision was made to change the way the United Water Resources group of companies calculated the Allowance for Funds Used During Construction (AFUDC).  Prior to that date, the Company used the universally accepted and Idaho Commission-approved method of capitalizing its weighted cost of Debt and Equity to construction projects based upon the most recent allowance determined by order of the regulatory commission.  In July 1995 the method was changed to add an additional component to the calculation.  The component added was an income tax  adder applied to the equity component of the calculation.  Not only was the method changed but a retroactive adjustment was made for AFUDC capitalized for the first six months of 1995.  Exhibit No. 117 is a copy of the Company’s response to Staff’s Production Request No. 72 that shows the equity gross-up component of $80,857 that has been capitalized to United Water Idaho’s construction projects since the change occurred in 1995.

Q.Are you aware of any other company that uses this equity gross-up method to calculate AFUDC?

A.No.  I performed several computer query searches of the “Public Utility Reports” (PUR) data base files for the years 1973 to date.  None of the searches produced any references to this method.  That does not necessarily mean that there isn’t a company somewhere using such a method; it simply indicates that the method is not discussed in any of the orders contained in the PUR data base.

Q.Did United Water Idaho request authorization from this Commission to change the AFUDC calculation method?

A.No.

Q.Did the Company in any formal or informal way inform either the Commission or Staff that it intended to change the calculation?

ANot that I am aware of.

Q.What is the adjustment to remove $787,735 from rate base shown in Column “G” on Exhibit No. 114?

A.This adjustment removes capitalized overhead costs charged to construction projects over the last three years for fees and expenses charged to United Water Idaho by United Water Resources and the M&S Company.  Exhibit No. 118 page 1, is a supporting schedule provided by the Company in response to Staff’s Production Request No. 73 that shows the overhead costs capitalized to construction for the three-year period ended June 30, 1997.  I have annotated the Company’s response to show total overheads charged for the three-year period.  The next to the last column to the right, that I have marked with an arrow, indicates the amount of M&S fees that have been added to the Company’s rate base over the three-year period ended June 1997.  Page 2 of Exhibit No. 118 shows my calculation of depreciation expense and accumulated depreciation at June 30, 1997.

As I discussed earlier, because of the potential inter-affiliate subsidies, the Staff is not convinced that the costs for services provided to United Water Idaho by the M&S Company are justified.

Q.What is the adjustment you show in Column “H” on Exhibit No. 114 to retire Data Point computer equipment?

A.This adjustment is necessary to recognize the retirement of equipment that was taken out of service but not retired on the Company’s books when the new IT system was activated.  Mr. Healy and I have discussed this adjustment and we agree it is appropriate.

Q.What is the adjustment for transportation equipment shown in Column “I” of this exhibit?

A.This adjustment removes from rate base the extra costs the Company incurred through its vehicle leasing program.  The details of this adjustment are calculated on page 1 of Exhibit No. 119.  That exhibit is used to develop adjustments to both rate base and operating expenses.

Q.Has Staff ever challenged these costs?

A.Yes.  Staff challenged the Company’s decision to switch from ownership of its vehicle fleet to leasing in the Company’s last rate case.

Q.Did the Commission accept Staff’s recommendations regarding the vehicle leasing program in the last case?

A.Not entirely.  The Commission did acknowledge Staff’s concern regarding the Company’s leasing program in its Order No. 26671 (Case No. UWI-W-96-3) beginning at page 5 where it stated:

Based on our review of the underlying

record in this case, we are unable to

find that the Company has presented the

Commission with a complete picture.

What the Company fails to present are

the enumerated and related savings

attendant from the switch to leasing.

For the Company to speculate on cross-

examination that there may be no

articulable savings, rings hollow when

one examines the record and exhibits

and realizes that the Company has not

seriously attempted to identify any

savings.  To speculate that there are

no actual savings, further discounts

the Company’s own prefiled testimony

when it alludes to savings in not

having to maintain a separate purchasing

and selling unit thus eliminating local

administrative time in procuring bids

and analyzing bids on new vehicles and

disposing of old vehicles (Tr.p.39), and

the Company’s ability under the lease

program to obtain free loaner vehicles

during maintenance downtime (Tr.pp.38, 39).

We acknowledge that the Company is incurring

increased out-of-pocket expense related to

leasing.  The Company does its customers a

disservice however when it seeks to recover

that expense without identifying and

matching related and contemporaneous

savings.  (emphasis added)

The Commission then attributed a level of offsetting savings to the leasing program by reducing the Company’s requested expense adjustment from $197,170 to $175,000.

Q.How much control does the local management of United Water Idaho have over the decisions made to replace its vehicle fleet with leased vehicles and replace its accounting system and computer software and equipment?

A.From what I have observed these decisions are made at the United Water Resources Inc. headquarters in New Jersey.

 Q.Did the Company, in response to the language of the Commission order, provide in its exhibits and testimony in this case any hard evidence that proved the benefits of leasing over ownership of the vehicle fleet?

A.No, its prefiled case is silent on this subject.  It did respond to Staff’s Production Request No. 82 seeking such information.  The Company’s response to that request is no more convincing than similar information provided in the Company’s last case.  The Cost/Benefit analysis is flawed and superficial.  Assumptions regarding vehicle residual values are artificially low and adjusted to favor leasing.  The actual experience of United Water Idaho over the last few years demonstrates unequivocally that the residual values are wrong and that leasing is more costly to the Company.

Q.Can you provide documentation to support that contention?

A.Yes.  Page 2 of Exhibit No. 119 is a copy of the Company’s response to Staff’s Production Request No. 83.  The document shows all of the owned vehicles that United Water Idaho has retired in the three-year period ended June 1997, the original cost of each vehicle and the salvage or sale price realized.  I have annotated the Company’s response to show the age of each vehicle at the date of sale and the realized percentage of original cost recovered through the sale.  This document shows that the Company realized average residual values of 31.4% for vehicles with an average age of six years.  This residual value for six-year old vehicles compares with an assumed residual value of 32% to 35% for three-year-old vehicles used by the Company in its analysis.

Referring back to Exhibit No. 118 where I discussed overhead loading, it is obvious that the Company’s own internal analysis indicates that the ratio of transportation expenses to direct payroll has increased from 6.5% to 11.5%.  The increase in this ratio coincides with the Company’s transition to the vehicle leasing program reflecting the higher transportation costs.

Q.Did you do any independent research into the residual values of vehicles?

A.Yes.  I accessed the Kelly Blue Book Official Guide of used car prices on the Internet.  There I compared the trade-in values, not resale values, of several very basic three-year-old vehicles in fair, not excellent or even good condition in Idaho and in New Jersey.  I learned that the trade-in values in Idaho generally exceed New Jersey values by 6% to 12%.  The Kelly Blue Book does not indicate what the original new price of the vehicles were.

I also reviewed the National Association of Automobile Dealers (NADA) Used Car Buyers Guide, Northwest Edition, for October 1997.  Using wholesale or trade-in values in that publication and the original retail price listed, I determined that on the average, three-year-old Ford pickups and vans retain more than 60% of their value.  A three-year-old Ford Taurus automobile retained 43% of its value.  These ratios are based upon the Manufacturers Suggested Retail Price (MSRP).  I don’t believe anyone ever pays full MSRP for the purchase of a new vehicle, particularly a repeat fleet customer.  I would expect the residual values to be much greater if calculated on the actual price paid for a vehicle rather than the MSRP.

Q.Exhibit No. 119 appears to produce two adjustments, one on lines 1 through 6, and another on lines 7 through 11.  How do these adjustments reflect the concerns you have just addressed?

A.The first adjustment I have discussed with Mr. Healy who agrees that it is appropriate.  This adjustment reflects changes in the Company’s budget used in preparation of this case.  The Company has since decided not to lease two vehicles originally contained in the budget and to retain one owned vehicle that it assumed would be retired.  This adjustment simply recognizes these changes to the Company’s case.

The second adjustment recognizes the change reflected by the first adjustment and reduces the remaining leasing expenses to a level comparable to the costs of ownership.  On lines 7 through 9 I have used the transportation overhead loading factors from Exhibit

No. 118 to calculate the increase in the overhead loading ratio.  The $119,536 adjustment shown on line 11, Column “B” was developed by applying the increase in the overhead ratio to the adjusted level of leasing expense shown on line 5.  Column “C” is the ratio of transportation expense Mr. Healy used to allocate the leasing expenses between operating expenses and rate base.  I have used this same ratio to allocate the adjustment.  Of the total $119,536 adjustment, $14,559 is related to rate base and $104,977 is related to operating expenses.  On lines 12 and 13, I have combined line 6 and line 11 adjustments and carried the respective results to Exhibit Nos. 114, Column “I”  and 115, Column “F”.

Q.Column “J” of Exhibit No. 114 then reflects Staff’s recommended rate base for use in this case?

A.Yes, Staff’s recommended rate base is $80,901,734.

Q.Would you now turn to Exhibit No. 115 and briefly describe the purpose of this exhibit?

A.This exhibit presents Staff’s recommended operating results.  Column “A” is the Company’s proforma results as presented by Mr. Healy on Exhibit No. 5, Column 4.  Columns “B” through “O” present Staff’s recommended adjustments to the Company’s case to produce Staff’s recommended proforma operating results shown in Column “P”.  Column “Q” represents the adjustments required to recognize the revenue increase of $1,080,581 necessary to produce the 8.86% return recommended by Staff witness Carlock.  Column “R” is the proforma operating results restated for Staff’s recommended increase in Column “Q”.

Q.Would you please explain the adjustments shown on this exhibit?

A.The adjustment shown in Column “B” simply corrects the Company’s case substituting the actual Ad Valorem tax levies for the Company’s estimates used to prepare its case.  Mr. Healy and I have discussed this adjustment and agree.

Column “C” presents a correction to the Company’s case for water tests the Company anticipated that will not have to be done.  Mr. Healy and I have discussed this adjustment and we agree.

Column “D” is a correction for a double count of storage costs at Anderson Ranch Reservoir that the Company inadvertently included in its case.  Mr. Healy and I agree on this adjustment.

Column “E” is a correction for employee dental insurance coverage that the Company overlooked in its case.  Mr. Healy and I agree on this adjustment.

Column “F” is the adjustment I discussed earlier regarding the Company’s vehicle leasing program.  The details of the adjustment are shown on page 1 of Exhibit No. 119.

Column “G” is an adjustment to correct the Company’s Thrift Plan adjustment to recognize the time Mr. Linam spends on non-Idaho utility business.  Mr. Healy and I agree on this adjustment.

Column “H” is an adjustment to correct the Company’s estimated costs of its telemetry expense.  The adjustment simply substitutes more recent known costs for the Company’s estimates.  Mr. Healy and I have discussed the adjustment and agree.

Column “I” eliminates depreciation expense related to the rate base adjustment I discussed earlier for the equity gross-up calculation the Company began using in its AFUDC calculations.  The depreciation expense adjustment is simply the $80,857 gross capitalized AFUDC divided by the average fifty-year life of the Company’s plant in service.

Column “J” eliminates the depreciation expense associated with the rate base adjustment I discussed earlier regarding the capitalized corporate overheads.  The calculation is shown on Exhibit No. 118, page 2.

On page 2 of Exhibit No. 115, Column “K” eliminates from O&M expenses 19.72% of the proforma payroll tax expenses the Company calculated on Exhibit No. 5, Schedule 3, page 2.  This adjustment simply represents the ratio of future payroll tax expenses that will be capitalized along with the associated payroll.

The adjustment in Column “L” to adjust PUC case expenses is detailed on Exhibit No. 120.  Staff has considerable reservations regarding the reasonableness of the fees the M&S Company is charging United Water Idaho.  Line 1 of Exhibit No. 120 shows the estimated cost of the current case that the Company built into the case.  The Company has indicated through its responses to Staff’s Production Request Nos. 55 and 56 and Ms. Ullman’s Request No. 14, that its estimated rate case expenses are based upon the Company’s last fully litigated rate case No. BOI-W-93-3.  Information provided by the Company’s responses indicate that $228,000 of the $300,000 was billed by the M&S Company.  In that case Mr. Matt Jost, a New Jersey employee of the M&S Company in New Jersey, presented the testimony and analysis that Mr. Healy is presenting in this case.  As an employee of United Water Idaho, not the M&S Company, Mr. Healy’s wages, benefits and overhead costs are already included in the Company’s payroll adjustments.  This simply constitutes, at a minimum, a double count of costs.

On the other hand, Mr. Healy’s participation supports Staff’s position that many if not all of the services provided by the M&S Company can be quite competently handled by the local operating company.

Q.Is the double count you referred to the sole purpose for this adjustment?

A.No.  As I have discussed earlier, Staff is skeptical of the charges imposed on United Water Idaho by the M&S company as well as the motivation to invest capital occasioned by the sale of the Rio Rancho, New Mexico system.  Billings by the M&S Company for the current case indicate that the Company was billed over $66,500 for one M&S employee in a four-month period of time.  In the month of November the Company was billed over $15,000 for this employee.

These charges don’t appear to be reasonable and should not be passed on to the consumer.  Staff recommends disallowing at least one-half of the Company’s estimated charges.  If the Company feels it must spend this kind of money to protect the interests of both its customers and its stockholders, the cost should be split among them.  Lines 2 through 5 of Exhibit No. 120 make this elimination and accepts the two-year amortization period recommended by the Company.

The lower half of this exhibit simply adjusts the Company’s proposed amortization period for costs incurred for other more specialized, non-recurring cases.  The Company requested a two-year amortization period for these costs.  Given the non-recurring nature of these cases, Staff believes a five-year amortization period is more reasonable.

Line 13 accumulates the effect of the two adjustments on the Company’s case.  The $86,044 is carried to Exhibit No. 115, page 2, Column “L”.

Q. Have you prepared an exhibit to explain the adjustment shown in Column “M” on page 2 of Exhibit No. 115?

A.Yes.  Exhibit No. 121 is a recalculation of Mr. Healy’s Exhibit No. 5, Schedule 1, pages 24 and 27.  The adjustments are intended to synchronize expenses with the effects of customer growth and weather on the Company’s variable operating expenses that are sensitive to these changes.  The numbers in Column “A” on this exhibit are taken directly from Mr. Healy’s exhibits.  Column “B” reflects the effects of Staff’s proposed changes in this case and substitutes proforma adjusted numbers in the case for some actual numbers used by Mr. Healy.  The calculations are otherwise identical.  The adjustments on lines 12 and 20 are simply the differences between Mr. Healy’s calculation and substituting Staff’s proforma expenses.  These two adjustment are combined on line 21 and carried forward to Exhibit No. 115, page 2, Column “M”

Q.What is the adjustment you show in Column “N” of Exhibit No. 115?

A.This adjustment simply reverses an adjustment the Company included in its case to budget for increases in fees paid to the M&S Company.  Given the discussion in this testimony regarding such fees, Staff cannot support an adjustment increasing those fees to even higher levels.

Q.What is the adjustment shown in Column “O” of this exhibit?

A.The Company in its case used a ten-year life for calculating depreciation expense on its investment in the IT Program and the Master Plan.  Mr. Linam, at page 17 of his direct testimony discussing the IT system, points out that this system replaces a “20+ year old main frame that was essentially obsolete.”  The magnitude of the conversion to a new information system such as this is not a normal occurrence.  It isn’t reasonable to think that every ten years the Company will have to basically scrap all of its technological equipment and software and start over from scratch.  Based upon the life realized on the old system, Staff recommends that the depreciation on the IT system investment should be based upon a twenty-year period.  Likewise, the Master Plan the Company is completing is a long-term project that is rather unusual for United Water.  Staff proposes that this investment also be depreciated over a twenty-year period.  The adjustment in Column “O” is simply a 50% reduction in the Company’s proforma depreciation adjustment.

Q.Column “P” then represents Staff’s proposed proforma operating results incorporating all the adjustments included in Columns “B” through “O”?

A.Yes.

Q.Where do the income tax expense numbers shown on Exhibit No. 115, page 2, Column “P” at lines 10 and 11 come from?

A.Exhibit No. 122 shows the calculation required to restate the income taxes for the proforma changes made on Exhibit No. 115, to synchronize the interest expense deduction with the rate base, and recognize the tax timing difference between book and tax depreciation.

Q.What are the last two columns labeled “Q” and “R”?

A.Column “Q” incorporates the revenue, expense and tax adjustments necessary to produce the rate of return proposed by Staff witness Carlock.  The calculations of these adjustments are shown on Exhibit No. 123.  Column “R” presents the proforma results of operations after applying the $1,080,581 increase in rates that Staff proposes.

Q.Does this conclude your direct testimony in this proceeding?

A.Yes, it does.