

**STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS  
PUBLIC UTILITIES COMMISSION**

**IN RE PROVIDENCE WATER SUPPLY )  
BOARD APPLICATION TO CHANGE )  
RATE SCHEDULES )**

**DOCKET NO. 3832**

**DIRECT TESTIMONY**

**OF**

**THOMAS S. CATLIN**

**ON BEHALF OF THE**

**DIVISION OF PUBLIC UTILITIES AND CARRIERS**

**JULY 2007**

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**EXETER**

ASSOCIATES, INC.  
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Columbia, Maryland 20904

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1 Introduction

2 Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS  
3 ADDRESS?

4 A. My name is Thomas S. Catlin. I am a principal with Exeter Associates, Inc. Our  
5 offices are located at 5565 Sterrett Place, Suite 310, Columbia, Maryland 21044.

6 Exeter is a firm of consulting economists specializing in issues pertaining to public  
7 utilities.

8 Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.

9 A. I hold a Master of Science Degree in Water Resources Engineering and Management  
10 from Arizona State University (1976). Major areas of study for this degree included  
11 pricing policy, economics, and management. I received my Bachelor of Science  
12 Degree in Physics and Math from the State University of New York at Stony Brook  
13 in 1974. I have also completed graduate courses in financial and management  
14 accounting.

1 Q. WOULD YOU PLEASE DESCRIBE YOUR PROFESSIONAL  
2 EXPERIENCE?

3 A. From August 1976 until June 1977, I was employed by Arthur Beard Engineers in  
4 Phoenix, Arizona, where, among other responsibilities, I conducted economic  
5 feasibility, financial and implementation analyses in conjunction with utility  
6 construction projects. I also served as project engineer for two utility valuation  
7 studies.

8 From June 1977 until September 1981, I was employed by Camp Dresser &  
9 McKee, Inc. Prior to transferring to the Management Consulting Division of CDM in  
10 April 1978, I was involved in both project administration and design. My project  
11 administration responsibilities included budget preparation and labor and cost  
12 monitoring and forecasting. As a member of CDM's Management Consulting  
13 Division, I performed cost of service, rate, and financial studies on approximately 15  
14 municipal and private water, wastewater and storm drainage utilities. These projects  
15 included: determining total costs of service; developing capital asset and depreciation  
16 bases; preparing cost allocation studies; evaluating alternative rate structures and  
17 designing rates; preparing bill analyses; developing cost and revenue projections; and  
18 preparing rate filings and expert testimony.

19 In September 1981, I accepted a position as a utility rates analyst with Exeter  
20 Associates, Inc. I became a principal and vice-president of the firm in 1984. Since  
21 joining Exeter, I have continued to be involved in the analysis of the operations of  
22 public utilities, with particular emphasis on utility rate regulation. I have been  
23 extensively involved in the review and analysis of utility rate filings, as well as other  
24 types of proceedings before state and federal regulatory authorities. My work in  
25 utility rate filings has focused on revenue requirements issues, but has also addressed

1 service cost and rate design matters. I have also been involved in analyzing affiliate  
2 relations, alternative regulatory mechanisms, and regulatory restructuring issues.  
3 This experience has involved electric, natural gas transmission and distribution, and  
4 telephone utilities, as well as water and wastewater companies.

5 Q. HAVE YOU PREVIOUSLY TESTIFIED IN REGULATORY  
6 PROCEEDINGS ON UTILITY RATES?

7 A. Yes. I have previously presented testimony on more than 200 occasions before the  
8 Federal Energy Regulatory Commission and the public utility commissions of  
9 Arizona, California, Colorado, Delaware, the District of Columbia, Florida, Idaho,  
10 Illinois, Indiana, Kentucky, Louisiana, Maine, Maryland, Montana, Nevada, New  
11 Jersey, Ohio, Oklahoma, Pennsylvania, Utah, Virginia and West Virginia, as well as  
12 before this Commission. I have also filed rate case evidence by affidavit with the  
13 Connecticut Department of Public Utility Control.

14 Q. ARE YOU A MEMBER OF ANY PROFESSIONAL SOCIETIES?

15 A. Yes. I am a member of the American Water Works Association (AWWA) and the  
16 Chesapeake Section of the AWWA. I serve on the AWWA's Rates and Charges  
17 Committee and on the AWWA Water Utility Council's Technical Advisory Group on  
18 Economics.

19 Q. ON WHOSE BEHALF ARE YOU APPEARING?

20 A. I am presenting testimony on behalf of the Division of Public Utilities and Carriers  
21 (the Division).

22 Q. HAVE YOU PREVIOUSLY TESTIFIED ON WATER UTILITY ISSUES  
23 BEFORE THIS COMMISSION?

24 A. Yes, I have been asked by the Division to address water utility issues on numerous  
25 occasions. I testified on revenue requirement, cost of service and/or rate design

1 issues in Newport Water Division, Docket Nos. 2029, 2985, 3457, 3578, 3675 and  
2 3818; Providence Water Supply Board, Docket Nos. 2022, 2048, 2304, 2961, and  
3 3163 and 3446; Kent County Water Authority, Docket No. 2098, Woonsocket Water  
4 Department, Docket Nos. 2099 and 2904; United Water Rhode Island, Inc., (formerly  
5 Wakefield Water Company), Docket Nos. 2006 and 2873; and Pawtucket Water  
6 Supply Board, Docket Nos. 3193, 3378, 3497 and 3674.

7 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

8 A. Exeter Associates was retained by the Division to assist it in the evaluation of the rate  
9 filing submitted by the Providence Water Supply Board (Providence Water or PWSB)  
10 on March 30, 2007. This testimony presents my findings and recommendations with  
11 regard to the overall revenue increase to which Providence Water is entitled. My  
12 associate, Jerome D. Mierzwa, is presenting testimony on cost allocation and rate  
13 design.

14 Q. HAVE YOU PREPARED SCHEDULES TO ACCOMPANY YOUR  
15 TESTIMONY?

16 A. Yes. I have prepared Schedules TSC-1 through TSC-8. Schedule TSC-1 provides a  
17 summary of revenues and expenses under present and proposed rates. Schedules  
18 TSC-2 through TSC-8 present my adjustments to Providence Water's claimed  
19 revenues and operating expenses.

20 Q. WHAT TIME PERIODS HAVE YOU UTILIZED IN MAKING YOUR  
21 DETERMINATION OF PROVIDENCE WATER'S REVENUE  
22 REQUIREMENTS?

23 A. Consistent with Providence Water's filing, I have utilized a test year that corresponds  
24 to the fiscal year ended June 30, 2006 and a rate year that corresponds to the calendar  
25 year (CY) ending December 31, 2008 as the basis for determining the PSWB's

1 revenue requirements and the revenue increase necessary to recover those  
2 requirements.

3 Q. WHAT IS YOUR RECOMMENDATION WITH REGARD TO THE  
4 APPROPRIATE INCREASE IN REVENUES IN THIS PROCEEDING?

5 A. As shown on Schedule TSC-1, it is my recommendation that Providence Water  
6 receive a revenue increase of \$7,389,179 in this proceeding. This amount is  
7 \$2,299,142 less than the increase of \$9,688,321 that Providence Water has identified  
8 as necessary based on rate year revenues at present rates.

9 Q. HOW IS THE REMAINDER OF YOUR TESTIMONY ORGANIZED?

10 A. The remainder of my testimony is divided into sections corresponding to the issues  
11 being addressed. These sections are set forth in the Table of Contents for this  
12 testimony.

13

14

**Wholesale Water Sales**

15 Q. HOW DID PROVIDENCE WATER DEVELOP ITS ESTIMATE OF RATE  
16 YEAR WATER SALES?

17 A. PWSB based water sales for both retail and wholesale customers on average sales for  
18 the fiscal years ending June 30 of 2003 through 2006 (FY 2003 through FY 2006).  
19 The one exception is that PWSB adjusted the sales to the Bristol County Water  
20 authority (Bristol County) to reflect a projected reduction from 1.8 million hundred  
21 cubic feet (Hcf) per year to 780,000 Hcf per year.

22 Q. WHAT ADJUSTMENTS ARE YOU PROPOSING TO MAKE TO PWSB'S  
23 ESTIMATES OF RATE YEAR WATER SALES?

24 A. Over the past four years, water sales for PWSB have fluctuated from year to year and  
25 have not shown a discernable trend, upward or downward. Accordingly, I am

1 accepting Providence Water's use of a four-year average to estimate rate year water  
2 sales. However, I have identified two adjustments that should be made to PWSB's  
3 estimates.

4 First, during the period FY 2003 through FY 2006, it was determined that a  
5 problem existed with the water meters serving the Town of Johnstown that caused  
6 consumption to be understated. This problem was corrected and the Town was billed  
7 for the additional volumes. However, those additional volumes were not included in  
8 the recorded water sales that Providence Water utilized to calculate the four-year  
9 average sales to Johnstown. Accordingly, I am proposing to adjust the estimated rate  
10 year sales to the Town of Johnstown to include the back-billed volumes for FY 2003  
11 through FY 2006. As shown on Schedule TSC-3 this adjustment increases estimated  
12 wholesale water sales by 79,029 Hcf. The resulting increase in revenue at present  
13 rates is \$73,065.

14 The second adjustment to PWSB's estimate of rate year sales that I am  
15 proposing relates to the projected reduction in sales to Bristol County. According to  
16 the response to DIV 3-9, the projected reduction in sales to Bristol County from  
17 historical levels to 584 million gallons or 780,749 Hcf per year was based on a June  
18 2005 letter from Bristol County. That letter notified Providence Water that Bristol  
19 County expected to reduce its purchases to that level in 2006 when it completed an  
20 expansion project designed to increase its own water supply. In response to the  
21 Division's data request, PWSB contacted Bristol County, which indicated that its  
22 expansion project had been delayed and that it now does not expect to reduce its  
23 purchases until 2010. Bristol County also indicated that it has budgeted purchases  
24 from PWSB of 940.6 million gallons (1,257,500 Hcf) in FY 2008. This is consistent  
25 with the volumes purchased from PWSB by Bristol County in FY 2007.

1 Accordingly, I have adjusted the rate year sales to Bristol County from the 780,749  
2 Hcf included by PWSB to 1,257,500 Hcf. This increases wholesale revenue at  
3 present rates by \$440,771, as shown on Schedule TSC-3.

4 **Capital Reimbursement**

5 Q. WHAT ADJUSTMENT ARE YOU PROPOSING TO MAKE TO THE  
6 CAPITAL REIMBURSEMENT RECOGNIZED AS AN OFFSET TO O&M  
7 EXPENSE?

8 A. The term capital reimbursement is utilized to refer to the portion of total payroll,  
9 benefits, and materials and supplies that are recognized as chargeable to capital  
10 projects. In its filing, PWSB has recognized a capital reimbursement for the test year  
11 of \$743,041. As shown on Schedule WEE-2, the capital reimbursement recognized  
12 as an offset to rate year O&M was increased to a rate year level of \$758,616.

13 The capital reimbursement credit of \$743,041 that PWSB recognized for the  
14 test year includes \$150,771 for materials and supplies used on IFR projects plus  
15 \$591,270 for payroll and benefits. The payroll and benefits credit was based on the  
16 average of the \$405,532 payroll and benefit credit approval in Docket No. 3446 for  
17 the rate year ended December 31, 2003 and the \$777,009 credit for payroll and  
18 benefits approved in Docket No. 3684 for the rate year ended December 31, 2006. In  
19 response to DIV 3-6, PWSB noted that \$777,009 should be recognized as the ongoing  
20 credit. Accordingly, I am proposing to adjust the capital reimbursement credit to  
21 reflect the ongoing credit in lieu of the average reflected in PWSB's filing.

22 Q. HAVE YOU PREPARED A SCHEDULE THAT SHOWS YOUR  
23 ADJUSTMENT?

24 A. Yes. Schedule TSC-4 shows the development of my adjustment. As indicated there,  
25 I have adjusted the credit of \$777,009 for the year ended December 31, 2006 to

1 reflect wage increases for two years at 3 percent per year to determine the rate year  
2 labor and benefits portion of the capital reimbursement. Similarly, I have escalated  
3 the materials and supplies charged to IFR projects to rate year levels by applying the  
4 overall inflation factor that PWSB applied to materials and supplies expense to  
5 determine that portion of the capital reimbursement. This results in an overall credit  
6 of \$984,719. This represents an increase in the capital reimbursement of \$226,103  
7 compared to that recognized by PWSB.

8  
9 **Retiree Health Reimbursement**

10 Q. PLEASE SUMMARIZE PWSB'S REQUEST WITH REGARD TO  
11 REIMBURSING THE CITY OF PROVIDENCE FOR RETIREE HEALTH  
12 BENEFITS.

13 A. PWSB is requesting that it be allowed to reimburse the City of Providence (the City)  
14 for the cost of health insurance provided for PWSB retirees during the period 1997-  
15 2005. In conjunction with the implementation of Government Accounting Standards  
16 Board Statements 43 and 45 (GASB 43/45), it was discovered that Providence Water  
17 had not been paying for its retirees' health benefits on a monthly basis since some  
18 time prior to 1997. PWSB was able to reimburse the City for the amounts related to  
19 2006 and is not seeking recovery of those amounts. The City has agreed to waive  
20 collection of the amounts for periods prior to 1997.

21 Q. WHAT IS THE TOTAL AMOUNT PWSB HAS SOUGHT TO REPAY THE  
22 CITY?

23 A. In its filing, PWSB identified the amount owed the City as \$1,635,592 and requested  
24 that it be allowed to repay this total at the rate of \$300,000 per year over  
25 approximately 5.5 years. In response to DIV 3-1, PWSB provided a corrected

1 calculation that reduced the total amount identified as owed to the City to \$1,489,081.  
2 That response continues to request an annual repayment allowance of \$300,000 for a  
3 period of just under five years.

4 Q. WHAT IS YOUR RECOMMENDATION WITH REGARD TO THIS  
5 REQUEST?

6 A. PWSB is requesting retroactive recovery for costs applicable to prior periods for  
7 which it failed to seek timely recovery. If PWSB was an investor-owned utility, it  
8 would be my position that such recovery should be disallowed as retroactive  
9 ratemaking. However, given that Providence Water is a municipal utility whose rates  
10 are set on a cash basis and recognizing the financial difficulty that the City of  
11 Providence, as well as other Rhode Island municipalities, face in dealing with GASB  
12 43/45, I am not opposing recovery of the corrected amount owed the City of  
13 \$1,489,081<sup>1</sup>. However, I am proposing to amortize that balance over six years. This  
14 results in an annual expense of \$248,180. As shown on Schedule TSC-5, this  
15 adjustment reduces rate year expenses by \$51,820.

16  
17 **Purchased Power Expense**

18 Q. PLEASE SUMMARIZE HOW PWSB'S CLAIMED ALLOWANCE FOR  
19 PURCHASED POWER EXPENSE WAS DETERMINED.

20 A. In his testimony, Mr. Edge notes that Providence Water experienced a 46 percent  
21 increase in purchased power expense from FY 2004 to the FY 2006 test year. To  
22 develop the filed claim for purchased power expense, Mr. Edge assumed that  
23 Providence Water would experience a similar increase from FY 2006 to FY 2008. He

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<sup>1</sup> In accepting this request, I have also considered that the City waived any claim for costs prior to 1997 and that PWSB has not sought recovery for 2006 amounts.

1 then further increased these estimates by an additional 5 percent to arrive at the pro  
2 forma level of purchased power expense for the rate year. Mr. Edge noted that when  
3 FY 2007 experience was available, he would recalculate PWSB's expense claim.

4 Q. WHAT ADJUSTMENT ARE YOU PROPOSING TO MAKE TO PWSB'S  
5 CLAIM FOR PURCHASED POWER EXPENSE?

6 A. The period from 2004 through 2006 was unquestionably one in which Rhode Island  
7 experienced significant increases in purchased power costs due to changes that were  
8 experienced in the wholesale power markets. However, there is no reason to believe  
9 that the same type of cost increases will be experienced again during the period 2006  
10 through 2008. In fact, in March 2006, a new contract was approved between PWSB  
11 and Constellation, Inc., New England for the purchase of electricity at a fixed rate of  
12 9.642 cents per kWh through December 2008. This contract was expected to result in  
13 saving of at least \$70,000 in 2006. Therefore, I have adjusted purchase power  
14 expense to eliminate the projected increases included by Mr. Edge and have set  
15 purchased power costs at their test year level. As shown on Schedule TSC-6 this  
16 results in a reduction in rate year expense by \$543,699.

17  
18 **PUC Assessment**

19 Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO THE PROJECTED PUC  
20 ASSESSMENT INCLUDED IN RATE YEAR EXPENSE BY PWSB?

21 A. Mr. Edge projected the PUC Assessment for the rate year by escalating the expense  
22 recorded in the test year for this assessment by 10 percent (approximately 4 percent  
23 per year for two and one-half years). However, the PUC assessment for 2007 actually  
24 declined slightly from the 2006 assessment. In light of this experience, I am  
25 proposing to set the rate year allowance for the PUC Assessment equal to the test year

1 expense. As shown on Schedule TSC-7, this adjustment reduces rate year expense by  
2 \$14,008.

3 **Administrative and General Contract Services**

4 Q. WHAT ADJUSTMENTS ARE YOU PROPOSING TO MAKE TO THE  
5 COSTS INCLUDED BY PWSB FOR ADMINISTRATIVE AND GENERAL  
6 CONTRACT SERVICES?

7 A. I am proposing to make adjustments to the claimed levels of two contractual services  
8 accounts included in the Administrative and General (A&G) cost function. In  
9 particular, I am proposing adjustments to the amounts included in the Contractual  
10 Services - Engineer and Legal Accounts.

11 Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO THE ENGINEERING  
12 RELATED EXPENSE.

13 A. During the test year, PWSB incurred \$24,377 for engineering related A&G  
14 contractual services. An inflation factor was applied to this cost to arrive at a rate  
15 year expense claim of \$25,932. According to the response to DIV 1-17 the test year  
16 expense was incurred for appraisal services related to the Scituate valuation litigation.  
17 This does not represent a normal, recurring cost. Furthermore, based on the level of  
18 engineering related A&G contractual services costs incurred in FY 2004 and FY 2005  
19 (\$6,652 and \$0, respectively), as shown on Schedule DGB-2, PWSB does not  
20 normally incur similar costs for other engineering services in the A&G cost function.  
21 Therefore, I have adjusted rate year expenses to exclude the \$25,932 allowance for  
22 A&G Contractual Services - Engineer.

23 Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO A&G - LEGAL  
24 CONTRACTUAL SERVICES.

1 A. Similar to the engineering related account, PWSB developed its claim for A&G  
2 Contractual Services - Legal of \$93,312 for the rate year by applying an inflation  
3 factor to the actual test year expense of \$87,716. In comparison, the costs incurred  
4 for these services were only \$41,536 in FY 2004 and \$8,925 in FY 2005. As a result,  
5 it appears that the level of A&G - Legal contractual services incurred in the test year  
6 is not representative of normal recurring costs.<sup>2</sup> Accordingly, I am proposing to  
7 adjust rate year expenses to reflect the three-year average of the costs incurred in FY  
8 2004, FY 2005 and FY 2006. As shown on Schedule TSC-8, this adjustment reduces  
9 A&G Contractual Services - Legal expense by \$47,253. In total, my adjustment to  
10 these two contractual services accounts reduces Providence Water's rate year  
11 expenses by \$73,185.

12  
13 **Chemical Costs**

- 14 Q. PLEASE SUMMARIZE PROVIDENCE WATER'S CLAIM FOR  
15 CHEMICAL AND SLUDGE MAINTENANCE COSTS.
- 16 A. Providence Water has requested an annual allowance of \$3,132,565 for chemical and  
17 sludge maintenance costs. This includes \$2,784,524 for chemicals and sludge  
18 maintenance costs in the rate year, \$148,042 for the true-up of prior (Cycle 2) sludge  
19 maintenance costs, and \$200,000 for additional restricted fund contributions to  
20 balance the account and in anticipation of future cost increases.
- 21 Q. HAVE YOU REVIEWED THIS CLAIM?
- 22 A. Yes. PWSB based its rate year expense on projected chemical quantities to be  
23 utilized and current fiscal year prices. Since the time of the filing, new bid prices

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<sup>2</sup> In response to DIV 1-17 requesting a breakdown of the costs incurred during the FY 2006 test year, PWSB only identified the costs as legal services and did not provide any further information to support the \$87,716 as representative of ongoing cost levels.

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1 have been received and the chemical prices are generally higher than those used to  
2 develop the initial cost estimate included in the filing.

3 Q. ARE YOU PROPOSING ANY ADJUSTMENT TO PWSB'S CLAIM?

4 A. No. I am proposing to accept PWSB's initial claim for two reasons. First, even  
5 though the updated chemical prices are higher than those used in developing the rate  
6 year estimate, the projected quantities of chemicals that PWSB has projected it will  
7 utilize appear to be conservatively high when compared to the actual quantities used  
8 in prior years. Second, the carryover funds in the chemical and sludge restricted fund  
9 were \$1,193,920 according to the response to DIV 1-29. This is approximately  
10 \$270,000 higher than reflected in the restricted account analysis presented on  
11 Schedule WEE-10F. Hence, it appears that even if chemical costs run somewhat  
12 higher than originally projected in PWSB's filing, there should be sufficient funds in  
13 the restricted account to absorb those cost increases and to allow PWSB to cover  
14 chemical costs through FY 2009 and perhaps 2010.

15

16

**GASB 43/45 Costs**

17 Q. PLEASE SUMMARIZE PROVIDENCE WATER'S REQUEST WITH  
18 REGARD TO GASB 43/45 COSTS.

19 A. As the result of GASB 43/45, the City of Providence and other governmental entities  
20 are required to recognize their future liabilities for postretirement benefits. (This is  
21 similar to the requirements of Statement of Financial Accounting Standard No. 106 or  
22 SFAS 106 for publicly owned corporations.) As a result, the City will be required to  
23 begin funding this liability. Similarly, Providence Water will be required to  
24 recognize the portion of the total City liability associated with its employees and  
25 retirees and to fund that liability.



1           There are also two other enterprise funds that are part of the City's overall operations  
2           that are not included in the General Fund expenses. Although the expenditures are  
3           small, for consistency, these two additional funds (the "Non-major Civic Center" and  
4           the "PPBA") should be included in the denominator in calculating PWSB's share of  
5           total City expenses.

6           Second, Providence Water has included \$5,000 for City Services as part of its  
7           estimated rate case expenses for this proceeding, but has not provided any details as  
8           to the nature of those costs. Unless PWSB can demonstrate that the services included  
9           result in true incremental costs to the City that are not included in the \$1.24 million  
10          being requested for City Services, then additional City Services costs should not be  
11          included in rate case expense.

12        Q.           HAVE YOU MADE AN ADJUSTMENT TO PWSB'S CLAIMED COST OF  
13                      SERVICE RELATED TO THESE TWO ISSUES?

14        A.           No. I have not made an adjustment for either of the two issues discussed above.  
15                      Revising the general overhead allocation factor to include the two additional  
16                      enterprise funds would have the effect of reducing rate year City Services costs by  
17                      only \$5,597. To the extent Mr. Bebyn agrees with the revision, I would anticipate  
18                      that he would reflect this change in his rebuttal schedules. If not, I will incorporate  
19                      the revision in the Division's final recommendation when I submit my surrebuttal  
20                      testimony. The revision to rate case expense to exclude City Services costs can be  
21                      made, if appropriate, when the final determination of the costs of this proceeding are  
22                      determined.

1 **Property Taxes**

2 Q. HOW WAS PROVIDENCE WATER'S ESTIMATE OF PROPERTY  
3 TAXES FOR THE RATE YEAR DEVELOPED?

4 A. Mr. Edge utilized property tax bills for FY 2007 as the starting point for developing  
5 his rate year estimates. With four exceptions, Mr. Edge projected rate year property  
6 taxes by increasing those assessments by 5 percent per year for one and one-half  
7 years. For Johnston, FY 2007 property taxes were increased by 4.37 percent for one  
8 and one-half years. For the Harmony Fire District, Chepachet Fire District and  
9 Warwick, Mr. Edge did not make any change since the taxes for these three entities  
10 are all less than \$150 and have not changed significantly in recent years.

11 Q. ARE YOU PROPOSING ANY ADJUSTMENT TO PROPERTY TAX  
12 EXPENSE?

13 A. Not at this time. Mr. Edge did not explain the basis for assuming most taxes would  
14 increase by 5 percent per year and actual increases for the last two years have been  
15 less than the 5 percent level.<sup>3</sup> However, Mr. Edge has stated he intends to provide a  
16 revised estimate for the rate year if needed once actual FY 2008 tax bills are received.  
17 Accordingly, I will reevaluate Providence Water's rate year projections of property  
18 taxes after Mr. Edge provides the updated information. To the extent necessary, I  
19 will address any changes to PWSB's projection in my surrebuttal testimony.

20  
21 **Operating Revenue Allowance**

22 Q. PLEASE SUMMARIZE PROVIDENCE WATER'S PROPOSED CHANGE  
23 IN ITS OPERATING REVENUE ALLOWANCE.

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<sup>3</sup> The overall increase for FY 2007 of 1.25 percent was affected by a one-time reduction for Cranston. However, even excluding Cranston, the overall reduction was less than 5 percent (4.66 percent).

1 A. Historically, Providence Water's operating revenue allowance has been set equal to  
2 1.5 percent of total operating expenses less miscellaneous revenue. In this  
3 proceeding, PWSB is requesting that the operating revenue allowance be increased to  
4 3.0 percent of total operating expenses less miscellaneous revenue (net operating  
5 expenses).

6 Q. WHAT IS YOUR POSITION WITH REGARD TO THIS INCREASE?

7 A. It is my recommendation that the operating revenue allowance continue to be set at  
8 the historical level of 1.5 percent of net operating expenses. In developing rate year  
9 expenses, PWSB has not only made adjustments for known and measurable changes  
10 to bring expenses to rate year levels, it has also applied an inflation factor to all other  
11 expenses for which known and measurable changes were not made. In addition, the  
12 amounts included as contributions to the insurance and chemicals and sludge  
13 restricted funds include amounts in excess of rate year expenses to improve the  
14 financial position of the restricted accounts and allow for future cost increases.  
15 Finally, all of Providence Water's restricted accounts rate fully reconcilable. In the  
16 event expenditures exceed projections, PWSB's ratepayers are required to make up  
17 the shortfall when rates are reset. Therefore, I do not believe that an increase in the  
18 operating revenue allowance is justified.

19 I would also like to point out that, in its recent decisions in Docket Nos. 3707  
20 and 3797 involving the Narragansett Bay Commission (NBC), a non-investor owned  
21 utility providing wastewater collection and treatment service, the PUC reduced the  
22 operating reserve allowance to 1.5 percent of operating expenses excluding payroll  
23 related costs. Although the Division did not recommend that action in those cases,  
24 and is not doing so here, these decisions point to a policy of reducing the operating  
25 revenue allowance, not increasing it as PWSB has proposed.

1 Q. IF THE COMMISSION ELECTS TO INCREASE THE OPERATING  
2 REVENUE ALLOWANCE, ARE THE OTHER CHANGES THAT YOU  
3 WOULD PROPOSE?

4 A. Yes. First, if the Commission elects to increase the operating revenue allowance, the  
5 adjustment to escalate costs not otherwise adjusted for inflation should be eliminated.  
6 The largest component of these expenses is contractual services, with the remaining  
7 items being materials and supplies and miscellaneous expenses. A review of the  
8 historical amounts expended on these items during FY 2004 through FY 2006  
9 indicates the amounts vary from year-to-year and do not show an upward trend.  
10 Nevertheless, I accepted this adjustment to be conservative because PWSB is a cash  
11 basis utility. If the operating revenue allowance is increased to 3 percent to account  
12 for unanticipated increases in expenses, then an inflation adjustment should not also  
13 be recognized.

14 Second, as noted previously, all of PWSB's restricted accounts are fully  
15 reconcilable and ratepayers are required to make up any shortfall when rates are reset.  
16 However, none of the operating revenue allowance is contributed to the restricted  
17 funds to reduce the amount that must be recovered from ratepayers if the allowance is  
18 not used to cover other unexpected cost increases or revenue shortfalls. Therefore,  
19 the restricted fund expenditures for capital related items should be excluded from the  
20 calculation of the operating revenue allowance if the allowance is increased to 3  
21 percent.

22 Q. HOW WOULD EXCLUDING THE CAPITAL RELATED RESTRICTED  
23 ACCOUNTS AFFECT THE OPERATING REVENUE ALLOWANCE?

24 A. Based on the Division's revenue requirement, a 3 percent operating revenue  
25 allowance based on total net operating expenses would be \$1,698,455. Excluding the

1 restricted accounts would result in an operating allowance of \$1,158,093. In  
2 comparison, the operating revenue allowance that I have recommended based on 1.5  
3 percent of net operating expenses is \$849,228.

4 Q. DOES THIS COMPLETE YOUR DIRECT TESTIMONY?

5 A. Yes, it does.

**STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS**

**PUBLIC UTILITIES COMMISSION**

**IN RE PROVIDENCE WATER SUPPLY )  
BOARD APPLICATION TO CHANGE )  
RATE SCHEDULES )**

**DOCKET NO. 3832**

**SCHEDULES ACCOMPANYING THE**

**DIRECT TESTIMONY**

**OF**

**THOMAS S. CATLIN**

**ON BEHALF OF THE**

**DIVISION OF PUBLIC UTILITIES AND CARRIERS**

**JULY 2007**

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**EXETER**

ASSOCIATES, INC.

5565 Sterrett Place

Suite 310

Columbia, Maryland 20904

# ***SCHEDULE TSC- 1***

PROVIDENCE WATER SUPPLY BOARD

Summary of Revenues and Expenses at  
Present and Proposed Rates  
Rate Year Ended December 31, 2008

	Rate Year Amount Per PWSB	Division Adjustments	Rate Year at Present Rates	Increase from Proposed Rates	Rate Year at Proposed Rates
<b>Revenue</b>					
Retail Water Sales	\$ 30,088,423	\$ -	\$ 30,088,423	\$ -	\$ -
Wholesale Water Sales	12,829,126	513,835	13,342,961	-	-
Retail Service Charges	3,895,171	-	3,895,171	-	-
Private Fire Protection	1,222,140	-	1,222,140	-	-
Public Fire Protection	1,526,521	-	1,526,521	-	-
Miscellaneous	1,245,739	-	1,245,739	-	-
Total Revenue	\$ 50,807,120	\$ 513,835	\$ 51,320,955	\$ 7,389,179	\$ 58,710,135
<b>Expenses</b>					
Operation & Maintenance	27,599,305	(856,995)	26,742,310	-	26,742,310
Insurance	2,967,655	-	2,967,655	-	2,967,655
Chemical & Sludge	3,132,565	-	3,132,565	-	3,132,565
City Service Expense	1,245,952	-	1,245,952	-	1,245,952
Property Taxes	6,570,792	-	6,570,792	-	6,570,792
Capitalized Labor	(758,616)	(51,820)	(810,436)	-	(810,436)
Net Operations	\$ 40,757,653	\$ (908,815)	\$ 39,848,838	\$ -	\$ 39,848,838
Capital Improvements	2,450,000	-	2,450,000	-	2,450,000
Western Cranston Fund	62,069	-	62,069	-	62,069
Infrastructure Replacement	13,900,000	-	13,900,000	-	13,900,000
Meter Replacement	1,000,000	-	1,000,000	-	1,000,000
Equipment Replacement	600,000	-	600,000	-	600,000
Net Restricted	\$ 18,012,069	\$ -	\$ 18,012,069	\$ -	\$ 18,012,069
Total Expenses	\$ 58,769,722	\$ (908,815)	\$ 57,860,907	\$ -	\$ 57,860,907
Operating Reserve	1,725,719	(876,492)	849,228	-	849,228
Total Cost of Service	\$ 60,495,441	\$ (1,785,307)	\$ 58,710,135	\$ -	\$ 58,710,135
Revenue Surplus/(Deficiency)	\$ (9,688,321)	\$ 2,299,142	\$ (7,389,179)	\$ 7,389,179	\$ -

# ***SCHEDULE TSC- 2***

PROVIDENCE WATER SUPPLY BOARD

Summary of Division Adjustments to  
Rate Year Revenues and Expenses at Present Rates  
Rate Year Ended December 31, 2008

<u>Description</u>	<u>Amount</u>	<u>Source</u>
Wholesale Water Sales Revenue	\$ 513,835	Schedule TSC-3
Total Revenue Adjustments	\$ 513,835	
Capital Reimbursement	(226,103)	Schedule TSC-4
Retiree Health	(51,820)	Schedule TSC-5
Purchased Power	(543,699)	Schedule TSC-6
PUC Assessment	(14,008)	Schedule TSC-7
A&G Contract Services	(73,185)	Schedule TSC-8
Property Tax Expense	-	See Note (1)
Operating Reserve	(876,492)	See Note (2)
Total Expense Adjustments	\$ (1,785,307)	
Total Revenue Requirement Effect of Division Adjustments at Present Rates	<u>\$ (2,299,142)</u>	

Note:

(1) No adjustment has been made pending receipt of FY 2008 property tax bills.

(2) Based on 1.5% of total expenses net of miscellaneous revenue.

# ***SCHEDULE TSC-3***

PROVIDENCE WATER SUPPLY BOARD

Adjustment to Wholesale Water Sales Revenue  
Rate Year Ended December 31, 2008

Johnston-Under-Registered Purchases (Hcf) (1)	
FY 2003	39,756
FY 2004	64,477
FY 2005	111,975
FY 2006	99,907
Total	<u>316,115</u>
Increase in 4 year Average-Hcf	79,029
Wholesale Rate	<u>\$ 0.92453</u>
Additional Revenue	<u>\$ 73,065</u>
Bristol County Water Authority	
Revised Estimate of Purchases (Hcf) (2)	1,257,500
Original Estimate per PWSB (3)	<u>780,749</u>
Additional Purchases	476,751
Wholesale Rate	<u>\$ 0.92453</u>
Additional Revenue	<u>\$ 440,771</u>
Total Adjustment to Revenue at Present Rates	<u>\$ 513,835</u>

Notes:

- (1) Per response to DIV 3-2.
- (2) Per response to DIV 3-9.
- (3) Per Schedule WEE-1A.

# ***SCHEDULE TSC-4***

PROVIDENCE WATER SUPPLY BOARD

Adjustment to Annualize the  
Capital Reimbursement Offset to O&M  
Rate Year Ended December 31, 2008

Ongoing Capitalized Labor and Benefits (1)	\$	777,009	
Rate Year Effect of Contractual Wage Increases (2)		<u>1.0609</u>	
Rate Year Labor and Benefits Capital Reimbursement			\$ 824,329
Test Year Materials and Supplies Charged to IFR Projects (3)		150,771	
Inflation Factor (4)		<u>1.0638</u>	
Rate Year Materials & Supplies Capital Reimbursement			<u>\$ 160,390</u>
Total Capital Reimbursement			\$ 984,719
Capital Reimbursement per PWSB (3)			<u>758,616</u>
Adjustment to Rate Year Expense			<u><u>\$ (226,103)</u></u>

Notes:

(1) Per response to DIV 3-6.

(2) Reflects 3% wages increases for 2 years from year ended 12/31/2006 to rate year ending December 31, 2008.

(3) Per Schedule WEE-2.

# ***SCHEDULE TSC– 5***

PROVIDENCE WATER SUPPLY BOARD

Adjustment to Retiree Health Reimbursement Expense  
Rate Year Ended December 31, 2008

Updated Amount Owed to City of Providence (1)	\$ 1,489,081
Proposed Amortization Period	<u>6 Years</u>
Annual Amortization	\$ 248,180
Amount per Providence Water (2)	<u>300,000</u>
Adjustment to Rate Year Expense	<u><u>\$ (51,820)</u></u>

Notes:

(1) Per response to DIV 3-1.

(2) Per Schedule WEE-6.

# ***SCHEDULE TSC- 6***

PROVIDENCE WATER SUPPLY BOARD

Adjustment to Purchased Power Expense  
 to Eliminate Projected Increase  
 Rate Year Ended December 31, 2008

Account	Amount per Division (1)	Rate Year Amount per PWSB (2)	Adjustment to Rate Year Expense
61523--Pumping	\$ 701,668	\$ 1,086,709	\$ (385,041)
61530--Water Treatment	179,720	265,409	(85,689)
61550--T&D	9,027	11,195	(2,168)
61580--Administration	119,872	190,673	(70,801)
Total Insurance Expense	\$ 1,010,287	\$ 1,553,986	\$ (543,699)

Notes:

(1) Reflects actual test year expense per Schedule WEE-9.

(2) Per Schedule WEE-9.

# ***SCHEDULE TSC-7***

PROVIDENCE WATER SUPPLY BOARD

Adjustment to PUC Assessment  
Rate Year Ended December 31, 2008

PUC Assessment per Division (1)	\$ 140,079
PUC Assessment per Providence Water (2)	<u>154,087</u>
Adjustment to Rate Year Expense	<u>\$ (14,008)</u>

Notes:

- (1) Reflects actual test year expense per Schedule WEE-7.
- (2) Per Schedule WEE-7.

***SCHEDULE TSC- 8***

PROVIDENCE WATER SUPPLY BOARD

Adjustment to Administrative & General Contract Services Expense  
Rate Year Ended December 31, 2008

Legal Contractual Services (1)	
FY 2004	\$ 41,536
FY 2005	8,925
FY 2006	87,716
Total	<u>\$ 138,177</u>
Three Year Average	\$ 46,059
Amount per Providence Water (2)	<u>93,312</u>
Adjustment to Legal Contractual Services	\$ (47,253)
Remove Engineering Contract Services (2)	<u>\$ (25,932)</u>
Total Adjustment to A&G Contractual Services	<u><u>\$ (73,185)</u></u>

Notes:

(1) Per response to DIV 3-1.

(2) Per Schedule WEE-6.