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RHODE ISLAND PUBLIC UTILITIES COMMISSION

**DOCKET NO. 4171
PAWTUCKET WATER SUPPLY BOARD**

**PREFILED REBUTTAL TESTIMONY OF
CHRISTOPHER P.N. WOODCOCK
ON BEHALF OF
PAWTUCKET WATER SUPPLY BOARD**

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4 **PREFILED REBUTTAL TESTIMONY OF**
5 **CHRISTOPHER P.N. WOODCOCK**
6

7 **Q: Are you the same Christopher Woodcock that submitted prefiled direct testimony in this**
8 **docket on behalf of the Pawtucket Water Supply Board (Pawtucket or PWSB)?**

9 A: Yes I am.

10
11 **Q: Have you reviewed the direct testimony submitted on behalf of the Division by Ms. And-**
12 **rea Crane and Mr. Thomas Catlin?**

13 A: Yes I have. I will comment on each one individually. I understand that Mr. DeCelles and Mr.
14 Benson will comment on the Division's testimony as well.

15
16 **Mr. Catlin's Prefiled Testimony**

17 **Q: Mr. Catlin raised five issues in his prefiled testimony. What is your position on these**
18 **items?**

19 A: The five issues raised by Mr. Catlin were:

- 20 • Correcting the maximum hour allocation factor as it pertains to fire protection. Mr. Cat-
- 21 lin picked up a mistake I had carried over from the previous model (Docket 3945) I had
- 22 submitted to the Commission. I agree with Mr. Catlin's adjustment as described on
- 23 page 7 of his testimony and have corrected that.
- 24 • Adjusting the allocator used to assign meter and service line investment. This too was a
- 25 carry-over from Docket 3945. I agree with the adjustment to use the S allocator for
- 26 Services and Meter investments for the reasons presented by Mr. Catlin on page 8 of
- 27 his testimony.

- 1 • Revising the number of private fire service bills to reflect the proposed monthly billing.
2 In concept I agree; however, I have made a further adjustment as I will describe later.
- 3 • Partially restoring the P-M allocator used in Docket 3945 to mitigate the impact on ser-
4 vice charges. As I will discuss I am not in full agree with this adjustment.
- 5 • Changing the limit on the increase to public fire service charges. I will also discuss this
6 in more detail.

7

8 **Q: You indicated some disagreement on the adjustment of private fire service bills. Please**
9 **discuss this.**

10 A: Mr. Catlin has correctly noted that PWSB proposes to bill the private fire services monthly.
11 This was not correctly reflected in the number of billings used to determine a portion of
12 the proposed service charges. As discussed in the response to Div 4-1 and in Mr. Benson
13 rebuttal testimony, with PWSB's new billing system, it is proposed that the private fire ser-
14 vice charges be included in and made a part of the customer's overall water bill. As a re-
15 sult, there would be no additional billings for private fire service. Rather than assuming 12
16 separate bills for each private fire service, I have assumed no separate bills for this service.

17

18 **Q: Ms. Crane also made an adjustment for private fire services. Based on the response to**
19 **Div 4-1 she has included 20 additional 6 inch private fire services. Have you factored this**
20 **adjustment into the number of private fire service bills?**

21 A: Yes I have. My Rebuttal Sch. 2.0 shows adjustments for the test year to the number of pri-
22 vate fire services by size as of June 30, 2010. I have also revised the test year number of
23 public fire hydrants based on more recent information and adjusted these to the actual
24 number as of June 30, 2010 as well.

25

26

27

1 **Q: Noting significant increases in the proposed service charges, Mr. Catlin has proposed to**
2 **use an allocator adopted in Docket 3945 (P-M) to move some capital costs from the ser-**
3 **vice charges to the consumption charges. He has proposed that half the metering and**
4 **billing capital costs be reassigned to the commodity charges. Do you agree with this re-**
5 **vision?**

6 A: While I am sympathetic to the increase in the service charges that he has noted, I do not
7 fully agree with this adjustment.

8 1. The allocation I had presented in my direct testimony was cost based. That is, I have as-
9 signed the costs of metering and billing to metering and billing and not to some other
10 cost function. Mr. Catlin's proposed modification clearly deviates from the cost of ser-
11 vice.

12 2. The P-M allocator used in Docket 3945 came about as a result of a shift in the areas
13 where the distribution crews were working. Rather than ask for a huge increase in the
14 service charges, we suggested a phasing in. It has been two years since docket 3945.
15 We are proposing to phase this adjustment out in this case.

16 3. Part of the reason for moving some billing and metering costs to the consumption
17 charge was to encourage wiser water use through higher consumption rates. With the
18 recent drops in sales and the unused capacity at the new treatment facility, the urgency
19 to encourage water conservation is not as great.

20 4. Rhode Island water utilities have seen a large drop in sales in recent years. With large
21 percentages of costs based on variable use, the volatility of revenues is quite high. For
22 a utility with such high fixed costs it makes some sense to have higher fixed revenues.
23 The service charge is a fixed revenue.

24 5. In this docket, PWSB is only asking for a 1.5% rate stabilization fund. To help keep the
25 overall rate increase down, the Board decided to limit the request for this item. In
26 doing so, they have forgone a larger request that state law allows and that would pro-
27 vide Pawtucket with some protection against reduced water sales. I believe that the
28 combination of this low request for the rate stabilization fund coupled with the Divi-

1 sion's proposal to put more costs onto the variable consumption charges rather than
2 the fixed service charges puts PWSB at a greater financial risk.

3 6. The \$66 per year increase noted by Mr. Catlin on page 10 of his testimony amounts to
4 \$0.18 per day. The overall service charge we had proposed (\$11.74 per month) is only
5 \$0.39 per day. I do not believe this is too much to pay for an essential service.

6
7 **Q: You suggest that the adjustment to the service charge that was phased in with Docket**
8 **3945 now be eliminated. Mr. Catlin has suggested an additional step to phase this out**
9 **by only allocating 50% of the metering and billing capital costs to the consumption**
10 **charge. Do you disagree with this additional phase-out period?**

11 A: In theory I do disagree; however, I do recognize the impact of eliminating this adjustment
12 all together. If the parties can agree that this adjustment will be phased out all together in
13 the next full rate case (not an abbreviated case), I believe that is reasonable. I have in-
14 cluded Mr. Catlin's proposed adjustment with the P-M allocator with the understanding
15 that this can be phased out in the next full rate case.

16
17 **Q: Mr. Catlin has proposed to limit the increase in public fire service charges to a 20% over-**
18 **all increase rather than the 5% you recommended. Do you have any comments on this**
19 **matter?**

20 A: This is addressed in Mr. DeCelles rebuttal testimony. Having heard Mr. Wunschel at
21 PWSB's board meetings, I share Mr. DeCelles' concern. I think that having some level of
22 public fire protection charge is better than none. If increased public fire protection
23 charges cause Rhode Island municipalities to reintroduce the legislation that would enable
24 them to opt out of such charges all together, it would be unfortunate.

25
26 Public fire protection charges are a significant source of fixed revenues for the State's wa-
27 ter utilities. They can ill afford to lose this revenue source at a time when revenues from
28 variable charges have shown such extreme volatility and a continued downward trend.

1 **Q: Mr. Catlin has expressed some concern about the increase in the proposed service**
2 **charges and has proposed that the shortfall in public fire revenues be recovered through**
3 **the consumption charges rather than the fixed service charges. Do you agree with this**
4 **recommendation?**

5 A: I certainly understand his concern for the increase; however, I am not in full agreement
6 with his proposed solution. The public fire charges are recovered by the municipalities
7 through property taxes. This is a fixed charge that is independent of water use, the same
8 as the water service charges. While the dollars are not exactly the same for all customers,
9 to a large degree this is really a question of which pocket the fire protection costs are paid
10 from: the customer's property tax pocket or the water service charge pocket. In the end,
11 the same costs must be recovered and they are recovered from the same group of cus-
12 tomers¹.

13
14 Because the public fire charges are a fixed revenue I had proposed that the amount lost
15 through the lowering of the public fire charges be recovered fully through a fixed service
16 charge based on meter size. Mr. Catlin has proposed that the lost revenues be recovered
17 through the consumption charge to lessen the impact on small volume customers. I am
18 now proposing a compromise, similar to that which Mr. Catlin proposed for the P-M allo-
19 cator. I suggest that half the lost public fire protection revenue be recovered through the
20 fixed service charges and half through the retail metered rates. As shown on the attached
21 rebuttal schedules, this results in a proposed monthly service charge for customers with a
22 5/8" meter of \$10.81. This is an increase over the current \$9.47/month charge that is less
23 than the overall revenue increase we propose. The increase is only \$1.34 per month (less
24 than 4 ½ cents per day).

¹ Except tax exempt property that does not contribute to property taxes but do pay water bills.

1 **Ms. Crane's Prefiled Testimony**

2 **Q: On page 9, lines 10-11 of her prefiled testimony, Ms. Crane purports to provide "a more**
3 **meaningful comparison" by showing revenues with the current billing frequencies. Is**
4 **this really more meaningful?**

5 A: I am not sure how this is more meaningful. I believe it is really an apples to oranges com-
6 parison. In any case, I do not see how either comparison is particularly relevant to the
7 proceedings. The percentage or dollar increases from present to proposed are simply a
8 mathematical calculation. The question before the Commission is not what percentage or
9 dollar increase is right, but how much revenue should Pawtucket Water be allowed to re-
10 cover through its rates in order to operate its water system to provide for the public health
11 and safety of its customers. The decision of the Commission should not rest on alternative
12 comparisons of percentage increases. I respectfully suggest that this comparison is a red
13 herring with no relevance.

14

15 **Q: Also on page 9, line 19-21, Ms. Crane suggests that PWSB's customers "may be disap-**
16 **pointed" if they "expected rate increases to mitigate once the new treatment plant was**
17 **completed." Is there any basis for these assumptions?**

18 A: I am not sure where Ms. Crane determined there was such an expectation. First, the new
19 treatment plant was just put into operations two years ago. The operating contract calls
20 for annual increases in the operating costs. Further, the plan to rebuild/replace the distri-
21 bution system was a long term plan and this has been made clear in PWSB's capital im-
22 provement plans. New bond issues and annual capital contributions from rates were pro-
23 jected through 2012 in documents prepared for the 2003 bond issue. The Consulting En-
24 gineer's certificate that was issued with the 2005 bonds discusses ten more years of pipe-
25 line work (to 2015) and rate increases through 2014. I know of no claim or document that
26 would lead rate payers to make the assumptions that Ms. Crane suggests. This testimony
27 seems gratuitous.

1 **Q: Ms. Crane has rejected your proposal of declining water sales and revenues. She has in-**
2 **stead recommended the use of the test year sales. Do you agree with this recommenda-**
3 **tion?**

4 A: No I do not. This issue has been raised in each of the PWSB's recent rate cases, and in each
5 case the projected consumption is too high. Ms. Crane's recommendation is a continua-
6 tion of her history of unrealistic sales projections. I have prepared an exhibit to my rebut-
7 tal testimony labeled Woodcock Rebuttal Exhibit 1, which documents the PWSB's under
8 collection of revenue for fiscal years 2004 through 2010. The PWSB has lost \$12,380,047 in
9 authorized revenue due to decreased consumption during this time period. This is revenue
10 the Commission authorized for necessary expenses, which the PWSB has not collected.
11 While Ms. Crane has not recommended a multi-year average as she has in the past, I be-
12 lieve her recommendation to use the actual test year sales (page 12, line 15) is overly op-
13 timistic and will only lead to a further under collection of revenue.

14

15 I have updated my Schedule 2.1 to include the actual sales in the just completed year end-
16 ing June 30, 2010. As shown on this schedule, Ms. Crane's opinion that sales would not
17 continue to decline from FY 2009 was incorrect. There was a further drop in sales. While
18 the overall decline was only about 3%, there was a continued decline in metered water
19 sales – both retail and wholesale.

20

21 **Q: Have you changed your recommendations regarding the rate year sales?**

22 A: I have updated my Schedule 2.0 to included FY 2010 – the 12 months just completed. I
23 have also updated the five year average changes from the 2004-2009 period to 2005-2010.
24 The projected rate year sales are hardly changed using this new information. Our initial fil-
25 ing had retail sales of 3,397,251 hcf. The updated projection is 3,390,337, a change of just
26 under 7,000 hcf or about 14,000 gallons per day. Our revised projection using the most
27 recent year would seem to verify the methodology that we are proposing to the Commis-
28 sion.

1 **Q: What if your projections for the rate year are wrong, and sales do not continue to de-**
2 **cline as Ms. Crane has suggested?**

3 A: If I am incorrect and sales do stabilize or even increase, any increase in revenues over that
4 allowed could be directed to a restricted stabilization account, just as the Commission has
5 ordered for several other water utilities in RI. There is a mechanism for protection if sales
6 are higher than we project.

7

8 On the other hand, there is absolutely no protection if Ms. Crane is incorrect and sales
9 continue to decline. PWSB would not be able to fund all its restricted accounts – most
10 likely the IFR account.

11

12 **Q: Doesn't the rate payer get more protection under Ms. Crane's proposal to assume that**
13 **sales will go back up from the FY 2010 levels?**

14 A: No they don't. The rate payer is better off under our proposal. If the Commission adopts
15 Ms. Crane's position and she is incorrect (sales are less than the test year amounts), PWSB
16 will have insufficient funds to pay for its IFR program costs and PWSB will have to come
17 back to the Commission sooner with another rate case and all its inherent expenses.

18

19 If PWSB's IFR contributions are lacking, PWSB will have to adjust its capital program, most
20 likely extending it out even further. Not only will customers have to deal with pipes that
21 should be replaced and/or rehabilitated for an even longer period, but it is likely that the
22 costs in future years will be higher. Ms. Crane expressed concern about customer expecta-
23 tions in her direct testimony. I think that Pawtucket's customers have an expectation that
24 PWSB will complete its capital program on schedule and not have to extend it to future
25 years when the costs will be greater.

26

27 If I am incorrect and sales do stay at the test year or higher levels, any extra revenues
28 would go into a stabilization fund to offset future increased costs. PWSB's IFR program

1 could continue as planned, and PWSB would likely not have to incur the costs of another
2 rate case as soon.

3
4 **Q. Do you have any other issues you would like to address regarding Ms. Crane's consump-**
5 **tion adjustment?**

6 A. Yes, Ms. Crane's position in this case conflicts with the Division's position in a recent Nar-
7 ragansett Bay Commission ("NBC") rate case (Docket 4026). In that Docket, NBC argued
8 that the use of test year consumption levels to project rate year consumption had resulted
9 in significant revenue shortfalls. As such, NBC calculated its rate year consumption in the
10 same manner the PWSB has calculated its rate year consumption in this Docket. In short,
11 both calculations show a declining trend in consumption. In NBC Docket 4026, the Division
12 did not object to this method of calculating rate year consumption. Since NBC's consump-
13 tion is based on consumption data from water utilities, including the PWSB, it is contradic-
14 tory to use declining consumption for NBC and not for the PWSB.

15
16 **Q: Would you like to comment on Ms. Crane's recommendations relative to PWSB's ex-**
17 **penses for property taxes?**

18 A: Ms. Crane has asserted that the adjustment we have proposed "does not constitute a
19 known and measurable change" and that "PWSB has provided no basis for its estimate(d)"
20 adjustments.

21
22 As the Commission is well aware, its Rules of Practice and Procedure (Rules) do not require
23 only "known and measurable changes" to the test year. It is unclear why Ms. Crane has
24 assumed this, but Section 2.6 (c) of the Commission's Rules are clear that adjustments
25 other than just "known and measurable" are allowed.

1 Ms. Crane is also incorrect in stating that “PWSB provided no basis for its estimate”. Divi-
2 sion Data Request 1-35 asks “what is the basis” for the property tax adjustments. The
3 record is clear that a basis was provided.

4
5 Ms. Crane has recommended no change from the test year property taxes. The Commis-
6 sion has a long history of allowing adjustments to test year municipal property tax ex-
7 penses. By accepting Ms. Crane’s unfounded recommendation, the Commission would be
8 setting a precedent that is contrary to its own Rules as well as its long standing practice.

9
10 **Q: Have you adjusted your proposed amount for the rate year property taxes?**

11 A: Yes I have. As Ms. Crane noted, the amount I had initially presented – a 0.12% increase –
12 was incorrect. Based on our answer to DIV 1-35 I have assumed a 3% per year increase.
13 This is less than the statutory maximum discussed in response to DIV 1-35. Over the 2 ½
14 year period from the test year to the rate year, the overall adjustment is a 7.67% increase
15 as shown on my Rebuttal Schedule 1.1, page 1 of 2.

16
17 **Q: Ms. Crane has recommended an adjustment to PWSB’s claimed debt service costs. Do
18 you agree with these?**

19 A: No I do not. It is somewhat surprising that these issues keep coming up. Ms. Crane states
20 that the “inclusion of post-rate year debt service costs would violate the rate year concept
21 and the matching principle”.

22
23 In Docket 3945, I presented exactly the same concept as provided in this docket. In my
24 prefiled direct testimony Docket 3945 I stated:

25 **“Q: Please explain why you propose to use the FY 2010 debt requirement
26 (July 1 2009 – June 30, 2010) when the rate year is calendar year 2009.**

27 A: Under its bond indenture, Pawtucket Water is required to make
28 monthly deposits to its debt service fund each month in order to have suffi-

1 cient funds in the debt service fund to make the payments that are due to
2 investors every six months. In effect, Pawtucket Water must start prefund-
3 ing its debt payments six months before they are due. The largest pay-
4 ments are due in September of each year, right at the start of the fiscal
5 year. By using the FY 2010 debt payments, Pawtucket Water will raise suffi-
6 cient funds in the rate year to make the September 2009 (FY 2010) debt
7 payments.” (Woodcock prefiled testimony pg 10, lines 4-13)

8
9 Ms. Crane apparently accepted this in Docket 3945.

10
11 **“Q. How did the Board determine its debt service claim in this case?”**

12 A. As shown in PWSB Schedule CPNW 1.1, the Board’s fiscal year 2009 debt
13 service is \$6,673,455 and its fiscal year 2010 debt service is \$6,688,543. Al-
14 though the rate year in this case is calendar year 2009, PWSB has included the
15 fiscal year 2010 debt service of \$6,688,543 in its claim. However, it has offset
16 this debt service requirement with a credit from the debt stabilization fund of
17 \$952,529.” (Crane prefiled testimony, pg 32, lines 8-13)

18
19 This was all explained in my pre-filed direct testimony (page 12) in this Docket and was ac-
20 knowledged on page 28 of Ms. Crane’s direct testimony. This is also not new to the Com-
21 mission. This funding approach has come up in other cases, and has been approved by the
22 Commission, most recently in Newport Water.

23
24 PWSB has to make cash deposits each month to its debt service fund. Accordingly, the
25 amounts required for the September loan payment are actually derived from payments
26 made up to six months earlier in the case of interest and 12 months earlier in the case of
27 principal. These are not “post rate year expenses” as Ms. Crane asserts, most of the pay-
28 ments are actually made in the rate year.

1 **Q: In addition to her assertions regarding post rate year payments, Ms. Crane has also rec-**
2 **ommended a reduced debt service allowance because (1) the Board has a Debt Service**
3 **Reserve Fund, (2) the Board has a Debt Service Stabilization Account, and (3) “the**
4 **Board’s restricted accounts earn interest that has not been included as income in the**
5 **PWSB revenue requirement.” Do you have any comments on these claims?**

6 A: Yes I do. The Debt Service Reserve Fund is only to be used in extreme emergencies – it
7 should not be planned to be used as Ms. Crane would have the Commission order. Con-
8 templating the use of this fund is even more absurd when one considers that any funds
9 withdrawn from the Debt Service Reserve Fund must be replenished before the end of the
10 fiscal year. It is only for an extreme cash flow emergency and not to be used as a revenue
11 offset as Ms. Crane has recommended.

12
13 The Debt Service Stabilization Fund was used in Docket 3945 when there was an unexpect-
14 edly large balance. It was explained in my prefiled direct testimony in this Docket that
15 there are not sufficient funds in that account to offset rates like there was in the last dock-
16 et.

17
18 The interest on the restricted debt service fund must stay within the fund and cannot be
19 used as a revenue offset under both the Board’s Bond Indenture and prior Commission or-
20 ders.

21
22 **Q: Although Ms. Crane has agreed with your 1.5% proposal for the rate stabilization fund,**
23 **she has opined that it “may be unnecessary, given the Operating Reserve Fund of \$2.7**
24 **million”. Do you have any comments on this?**

25 A: Yes I do. First I am glad that Ms. Crane has acknowledged the recent legislation that calls
26 for the establishment of these funds. I believe that this legislation was needed given the
27 ongoing drop in water sales throughout Rhode Island. It seems clear that the Commission
28 recognized this before the recent legislation was passed in its recent orders allowing in-

1 creased allowances for revenue stabilization. In addition, the Commission opened Docket
2 4113 “to address, as a policy matter, operating revenue allowances of regulated water util-
3 ities.” In opening this docket, the Commission stated that it was “interested in reviewing
4 information regarding rate design methodologies that might address the impact of declin-
5 ing consumption on revenues while taking into account the State's stated policy of en-
6 couraging conservation, particularly through pending legislation that encourages conserva-
7 tion based rates.” Unfortunately, I don't believe the drops in water sales have allowed any
8 of the regulated water utilities to fund these rate stabilization accounts as contemplated
9 by the legislation and the Commission.

10
11 I am troubled by Ms. Crane's suggestions that these funds “may be unnecessary” due to
12 the existence of other reserve funds required by the bond indentures. We have been
13 down this road in numerous dockets and the overwhelming testimony has belied Ms.
14 Crane's suggestion over and over. The testimony presented to the Commission on this is-
15 sue has consistently noted that funds in the bond indenture required Operating Reserve
16 Fund are NOT a substitute for the rate stabilization (or former operating revenue) fund.
17 (See Woodcock Rebuttal Exhibit 2 (Woodcock Rebuttal Testimony Excerpt, Docket 3674)
18 and Woodcock Rebuttal Exhibit 3 (Woodcock Rebuttal Testimony Excerpt, Docket 3945)

19
20 The requirements for the Operating Revenue Fund are clearly outlined in the bond inden-
21 ture that has been supplied in previous dockets. Those funds can only be used if there are
22 insufficient revenues to fund operating expenses, BUT MUST be reimbursed by the end of
23 the fiscal year. Should PWSB have to use its Operating Reserve Fund due to a shortfall in
24 annual revenues, it would not have sufficient time to file a new rate case, have the re-
25 quired hearings, implement new rates and collect the increased revenues before the end
26 of the fiscal year. Ms. Crane should accept this once and for all and stop raising this dis-
27 traction in each of the PWSB's rate cases before this Commission.

28

1 **Q: Ms. Crane has suggested that a second phase rate increase is not used in most regulatory**
2 **commissions and “can result in single-issue ratemaking” resulting in “unreasonable and**
3 **unnecessary rate increases.” Do you have any comments on that testimony?**

4 A: I do, but at the outset I note that Ms. Crane’s disagreement is with the Rhode Island legis-
5 lature and the law itself, and is irrelevant to these proceedings. These questions have
6 been decided by the legislature.

7

8 However, because Ms. Crane has chosen to address the legislation itself, I will respond.

- 9 • One reason that most other jurisdictions do not use multi-year rates is that very few re-
10 gulate the rates of municipal water utilities.
- 11 • Any filing can be a single issue filing. The Commission is well aware of recent cases in
12 Rhode Island where water utilities have filed abbreviated cases essentially involving a
13 single issue. The Commission is well equipped to determine if a filing is “unreasonable
14 and unnecessary.” That a second step request *might* be involve a single issue is anothe-
15 r red herring.
- 16 • One of the purposes of the multi-step rate increase statute is to allow for quicker and
17 less frequent rate proceedings. The purpose of the legislation is to save rate payers
18 money by reducing the number and frequency of rate filings.

19

20 **Q: Ms. Crane has recommended a number of adjustments to the step two increase you**
21 **have proposed. Can you address these?**

22 A: I will summarize my responses to each of Ms. Crane’s recommendations below:

- 23 • Her first adjustment is to debt service. While Ms. Crane has suggested a higher debt
24 service adjustment on ACC-13, the adjustment is predicated on a lower base amount.
25 As discussed earlier, PWSB must make monthly deposits in order to accumulate suffi-
26 cient funds to make its semi-annual debt payments. Its cash payments are best
27 represented by the fiscal year amounts that are ultimately paid from the prior period
28 monthly deposits to the bond holders. For the same reasons that the fiscal year debt

1 should be used as the basis for the rate year debt, I believe the lower adjustment (but
2 to the higher base case amount) is the correct amount.

- 3 • Ms. Crane has recommended that no inflation adjustment be allowed based on her in-
4 terpretation that “the application of an inflation adjustment ... is too broad to be uti-
5 lized for multi-year rate plans.” There is no basis for this interpretation. The law is
6 quite explicit under section 39-15.1-3. Rates; it states:

7 The rates of water suppliers subject to commission rate regulation shall be re-
8 sponsible and adequate to pay for **all costs** associated with water supply includ-
9 ing, but not limited to, the costs of:

10 (1) Acquisition, treatment, transmission, distribution and availability of water;

11 (2) System administration and overhead, including the cost and/or value of all
12 services and facilities provided by the city or town to the water supplier includ-
13 ing, but not limited to, testing, **operation, maintenance**, replacement, repair,
14 debt service, and associated with, but not limited to, supply, production, treat-
15 ment, transmission, administration facilities, and metering and billing. (emphasis
16 added)

17 Under Section 39-15.1-1. Purposes. The law states:

18 “The purposes of this chapter are to: (1) Augment current principles for setting
19 the rates of public utilities that are water suppliers that are subject to commis-
20 sion rate regulation in a manner that facilitates:

21 (i) Managing demand, especially seasonal demand;

22 (ii) Investing in infrastructure repair and replacement;

23 (iii) **Recovering the full costs, including capital and operational**, of water sys-
24 tems through water system revenues; (emphasis added)

25
26 I see no basis whatsoever for Ms. Crane’s interpretation that only salary costs can carry
27 an inflation adjustment; on the contrary, it appears quite clear that all operational costs
28 are to be considered.

1 I am also troubled by Ms. Crane's suggestion that applying a second year, inflationary
2 step increase is too speculative. Rhode Island's law allows for up to *six* years. Under
3 the law, PWSB must request implementation of the next step and both the Division and
4 Commission have up to 60 days to review the step increase and, if they want, they can
5 hold additional hearings. Ms. Crane's apparent hesitancy to accept a single year's ad-
6 justment to non-salary operational costs essentially strips much of the intent from the
7 legislation.

- 8
- 9 • In recommending only \$8,635 for the rate stabilization fund in the second step, I again
10 believe Ms. Crane has failed to recognize the legislative intent of step increases. I be-
11 lieve that intent is to provide low cost changes to rates on a regular basis without hav-
12 ing to resort to expensive rate proceedings. If Pawtucket comes back a year from now
13 and files for a typical rate increase, there would be no questions that a request for a full
14 new 1.5% revenue stabilization allowance on the full cost of service would be reasona-
15 ble. Under Ms. Crane's theory, PWSB could only ask for 1.5% of the increase in costs
16 over its last approved revenue allowance. This is clearly not what has been done by the
17 Commission in the past; the operating revenue or rate stabilization allowances have
18 never been an incremental amount over a utility's last rate case.

19

20 The reduction to our requested rate stabilization fund is even more troubling when one
21 considers that PWSB has only asked for a 1.5% allowance when the Commission's re-
22 cent history is to provide greater amounts and the recent legislation provides for an ac-
23 cumulation up to 10%. If PWSB were actually able to collect and accumulate the allow-
24 ance for the two year period it would have accumulated just 3% through the second
25 phase.

26

27 **Q: Have you prepared rebuttal schedules based on your review of the Division's testimony?**

28 **A:** Yes I have, they are attached.

1

2 **Q: Does this conclude your testimony?**

3 A: Yes it does.

EXHIBIT 1

PAWTUCKET WATER SUPPLY BOARD COLLECTIONS

1. RATE FILINGS

Docket 3378

Filed August 20, 2001
Test Year CY00 (January 1, 2000 – December 31, 2000)
Rate Year CY02 (January 1, 2002 – December 31, 2002)
Decision – March 14, 2002
Revenues Allowed - \$11,869,742

Docket 3497

Filed February 28, 2003
Test Year FY02 (July 1, 2001 – June 30, 2002)
Rate Year FY04 (July 1, 2003 – June 30, 2004)
Decision – October 3, 2003
Total Cost of Service - \$13,933,789

Docket 3593 (abbreviated filing)

Filed February 23, 2004
Test Year – Expenses Approved In Docket 3945
Rates Effective – April 1, 2005
Decision – June 29, 2004
Total Cost of Service - \$17,348,873

Docket 3674

Filed April 11, 2005
Test Year FY04 (June 1, 2003 – June 30, 2004)
Rate Year CY06 (January 1, 2006 – December 31, 2006)
Decision – November 10, 2005
Total Cost of Service - \$17,874,873

Docket 3945

Filed March 28, 2008
Test Year FY07 (July 1, 2006 – June 30, 2007)
Rate Year CY09 (January 1, 2009 – December 31, 2009)
Decision September 30, 2008
Total Cost of Service - \$19,940,794

2. REVENUES COLLECTED – FISCAL YEARS 2004-2010

<u>Fiscal</u> <u>Year</u>	<u>Revenue</u> <u>Allowed *</u>	<u>Revenue</u> <u>Collected</u>	<u>Difference</u>	
2004	\$ 13,073,769	\$ 12,208,140	\$ (865,629)	
2005	\$ 14,218,370	\$ 13,686,446	\$ (531,924)	
2006	\$ 17,611,815	\$ 16,233,510	\$ (1,378,305)	
2007	\$ 17,874,873	\$ 13,372,433	\$ (4,502,440)	
2008	\$ 17,874,873	\$ 16,589,957	\$ (1,284,916)	
2009	\$ 19,079,994	\$ 16,872,329	\$ (2,207,665)	
2010	\$ 19,940,794	\$ 18,331,626	\$ (1,609,168)	
Total	\$ 119,674,488	\$ 107,294,441	\$ (12,380,047)	10%

* Prorated - assumed full allowed amount could be collected approx 2 months after decision

EXHIBIT 2

1 **Q: The Division has noted that the O&M Reserve Fund is projected to be \$2.2 million by**
2 **December 31, 2005. What relevance does this have to the issue of the operating reve-**
3 **nue allowance?**

4 A: In general it has no relevance at all and only seems to have been brought up to suggest that
5 Pawtucket will have sufficient funds available and does need the increased operating reve-
6 nue allowance. This matter was brought up by Ms. Crane in her direct testimony and in re-
7 sponse to PWSB data request 1-1. While Ms. Crane admittedly has no expertise in the re-
8 quirements of the O&M Reserve Fund, and appeared to be fully aware that it is not a substi-
9 tute for the operating revenue allowance, she has again brought it up in response to PWSB
10 Data Request 1-1. This required Reserve Fund is irrelevant to the issue; discussing the bal-
11 ance in this fund only detracts from the real issues at hand.

12

13 **Q: Does the 25% O&M Reserve Fund have any relevance to the issue of the operating**
14 **revenue allowance?**

15 A: The only possible relevance of the O&M Reserve Fund is the apparent misunderstanding of
16 the requirements for this fund that are spelled out in the Trust Indenture. This fund is re-
17 quired to be funded to 25% of Pawtucket's operating budget – not the allowance provided
18 by the Commission. Deposits are to be made monthly based on the Water Supply Board's
19 budget. Starting July 1 of the rate year, Pawtucket Water will have a new budget for the
20 next 12 months. The required deposits must be based on the budget for that year. Because
21 the fiscal year goes six months beyond the rate year, it is likely that the budget will be
22 higher (a full year of operations of the new treatment plant for example), necessitating larger
23 monthly deposits throughout the fiscal year.

24

25 As with other dockets we have requested funding equal to the operating costs in the rate
26 year. This is done for regulatory purposes. It is expected that Pawtucket Water will be pro-
27 vided with sufficient revenues, including a reasonable operating revenue allowance that will
28 provide some additional funds to make these higher payments in FY 2007.

29

1 **Q: To be clear – can the 25% O&M Reserve Fund required by the Trust Indenture be**
2 **used as a substitute for the operating revenue allowance?**

3 A: No it can not. As pointed out in my original prefiled testimony I have worked on a number
4 of engineering and financial feasibility studies related to municipal revenue bonds. I
5 worked closely with Pawtucket’s bond counsel in reviewing much of the bond indenture. I
6 have discussed this specific matter recently with bond counsel to be very clear. I have sent
7 her draft testimony to be sure that she concurred with what I was saying. In addition, I per-
8 form annual reviews for a number of RI water utilities to ensure that specified terms of the
9 indentures are being met and I have prepared financial feasibility certificates for a number of
10 recent water revenue bond issues in RI. I believe I am well aware of the terms and condi-
11 tions of the trust indentures in general and of the Pawtucket Water Supply Board’s indenture
12 in particular.

13

14 The Operation and Maintenance Reserve Fund established under the General Bond Resolu-
15 tion does **NOT** serve an identical function to the operating revenue allowance. The O&M
16 Reserve Fund can be used for specific purposes only: (1) to make principal and/or interest
17 payments if there are insufficient amounts available in the debt service fund, debt service re-
18 serve fund, renewal and replacement reserve fund or the renewal and replacement account
19 or (2) to make payments for operation and maintenance if the amounts in the operation and
20 maintenance fund is insufficient. Unlike the 1.5% operating revenue allowance, the O&M
21 Reserve Fund can not be used for other purposes such as payments towards IFR costs if
22 revenues are insufficient or to the O&M or R&R reserve funds. The O&M Reserve Fund is
23 also quite different in that this fund or account may not simply be used up if revenues are
24 insufficient – the fund must be repaid. It is only to be used for a short term cash flow. At
25 the end of each fiscal year, the O&M Reserve Fund must have an amount on deposit equal
26 to 25% of Pawtucket Water’s operating budget. While money can be withdrawn and used in
27 an emergency, unlike the 1.5% operating reserve it must be paid back in the fiscal year.
28 With the 1.5% operating revenue allowance, a shortfall in sales and revenues can be covered

1 by that allowance for the year and no repayment is needed. That is not the case with the
2 O&M Reserve Fund established in the General Bond Resolution.

3
4 **Q: How should the Commission consider the O&M Reserve Fund vis-à-vis the Operating**
5 **Revenue Allowance?**

6 A: The O&M Reserve Fund should be viewed as an account that is only used in an extreme
7 case or emergency, and possible for cash flow issues. It should not be viewed as something
8 that is used if gas prices rise, benefit expenses go up more than expected, or sales of water
9 drop a few percent. I believe that the operating revenue allowance established by the Com-
10 mission was intended to fill this purpose. I also believe that to do what was intended, that
11 the allowed percentage should be based on the full revenues as it initially was and that the
12 allowed percentage needs to be adjusted up to reflect today's conditions.

13
14 **Q: If revenues are insufficient, can't PWSB apply for emergency rate relief ?**

15 A: Theoretically this is possible; however, practically I don't think it is. First, Pawtucket
16 would have to recognize the shortfall in revenues in sufficient time to prepare an emergency
17 filing. It is unclear when this might be possible. For example, it would probably be unrea-
18 sonable to suggest an emergency exists for the whole year if billings in the fall (three or four
19 months into the fiscal year) are down. However, waiting until January or February might be
20 too late – their may only be one billing left after emergency rates are approved, and that one
21 quarter would not necessarily be sufficient to refund the O&M Reserve Fund so that 25% of
22 the budget (the amount required in the bond resolution) is in the account on June 30.

23
24 **Q: You have discussed the uncertainties associated with future water revenues and ex-**
25 **penses and why the Commission should provide for more realistic water sales estimates**
26 **and an operating revenue allowance on total revenues. Does Pawtucket need both of**
27 **these and a 5% operating revenue allowance?**

28 A: I recognize that this may seem to be asking a lot, but I believe it is necessary. In the case of
29 water sales and revenues, clearly they are decreasing over time and historic data about rain-

EXHIBIT 3

1 solely on past decisions in Pawtucket's rate filings and the claim that the O&M Reserve re-
2 quired by Pawtucket's bonds can make up for cash flow issues.

3

4 **Q: Regarding Commission precedence on this matter, has the Commission always allowed**
5 **a 1.5% operating revenue allowance on operating costs alone?**

6 A: No, the Commission's position has understandably varied over the years depending on cir-
7 cumstances faced by different utilities. In the past, the Commission provided the 1.5% oper-
8 ating allowance on total revenues. The Commission's position then shifted and it began
9 providing the allowance on operating costs only. Furthermore, different utilities currently
10 have different operating revenue allowances. For instance, Newport Water has an operating
11 revenue allowance that is equal to 1.5% of total expenses, and Providence has a 3% operat-
12 ing revenue allowance. I spent several pages in my prefiled direct testimony dealing with
13 this issue and how the Commission's position appears to have migrated in recent cases and
14 among different utilities. Yet, Ms. Crane appears to have ignored these recent changes,
15 choosing to dwell primarily on the Commission's ruling in the PWSB's last rate filing. This
16 issue is critical to Rhode Island's water utilities. In fact, the Commission itself discussed the
17 opening of a generic docket to study this specific issue. Remarkably, Ms. Crane has sug-
18 gested that an operating reserve may not be needed at all rather than the addressing the re-
19 cent developments addressed in my direct testimony.

20

21 **Q: Does Ms. Crane believe that any Operating Revenue Allowance is necessary?**

22 A: On page 30, line 16 of her prefiled testimony, Ms. Crane says, "... I believe that an Op-
23 erating Reserve Allowance is unnecessary, given the Operating Reserve Fund of almost \$2.7
24 million that has been funded by rate payers ..." Nevertheless, she goes on to agree to mini-
25 mal funding because the Commission has permitted the Operating Revenue Allowance in
26 past cases.

27

28

29

1 **Q. What is your reaction to this testimony?**

2 A. Quite frankly, I am very surprised. I thought this issue had been addressed in Docket
3 3674, and that it had been conclusively established that the O&M Reserve Fund – which
4 Ms. Crane refers to as the Operating Reserve Fund – is not a substitute for an Operating
5 Revenue Allowance. The O&M Reserve Fund was established in conjunction with the
6 PWSB’s borrowings with the Rhode Island Clean Water Finance Agency. The fund provides
7 security to bondholders and it improves Pawtucket’s credit rating, which in turn lowers bor-
8 rowing costs.

9

10 Nevertheless, Ms. Crane’s testimony in this Docket is almost identical to her prefiled testi-
11 mony in Docket 3674 where she testified on page 30 of her direct testimony that:

12 “In the event of revenue shortfalls or unanticipated expense increases, the Operating
13 Reserve Fund can be used, although the Operating Reserve would subsequently need
14 to be replenished. By December 31, 2005, the Operating Reserve is projected to have
15 a balance of \$2.2 million... While I believe that an additional Operating Income Al-
16 lowance is unnecessary, given the Operating Reserve of \$2.2 million that has already
17 been funded by ratepayers I recognize that the Commission recently rejected a similar
18 argument that I made in the Kent County Water Authority base rate case, Docket No.
19 3660.”

20

21 In her Docket 3674 surrebuttal testimony she said:

22 “In addition, the PWSB does have the \$2.2 million O&M Reserve available, the pur-
23 pose of which is to meet shortfalls that may occur from time to time.” (Crane Surrebut-
24 tal, Docket 3674, p. 14)

25

26 At the live hearings in Docket 3674, the PWSB’s financial advisor Ms. Maureen Gurghigian
27 from First Southwest provided testimony to clear this matter up. After hearing Ms.

28 Gurghigian’s live testimony, Ms. Crane testified:

29 “Well, I heard Miss Gurghigian ... testify today about the operating -- the O&M re-
30 serve fund and the fact that in her opinion that fund should not be used to cover operat-
31 ing and maintenance costs on an ongoing basis, and I just kind of want to clarify that
32 that’s our position, too. I mean, no where are we recommending that that fund that’s re-
33 quired under the bond indenture be used routinely to cover shortfalls or unforeseen in-
34 creases in expense.” (Tr. v.II, p. 157)

1

2 In Docket 3674, Ms. Crane seemed to acknowledge that the bond required O&M Reserve
3 Fund is no substitute for the Operating Revenue Allowance, yet she is now returning testi-
4 mony that is nearly identical to that which she offered in Docket 3674 suggesting that the
5 Operating Revenue Allowance is unnecessary but for the Commission's allowance of it in
6 past cases.

7

8 **Q: The Division has noted that the O&M Reserve Fund has approximately \$2.7 million;
9 what relevance does this have to the issue of the Operating Revenue Allowance?**

10 A: Just as in the last PWSB docket, it has no relevance at all and only seems to have been
11 brought up to suggest that Pawtucket will have sufficient funds available and does need the
12 increased operating revenue allowance. This matter was brought up by Ms. Crane in her re-
13 sponse to PWSB data request 1-1 in docket 3674. While Ms. Crane admittedly has no ex-
14 pertise in the requirements of the O&M Reserve Fund, and appeared to be fully aware that it
15 is not a substitute for the operating revenue allowance, she has again brought it up in this
16 docket. This required O&M Reserve Fund is irrelevant to the issue; discussing the balance
17 in this fund only detracts from the real issues at hand.

18

19 **Q: To be clear – can the 25% O&M Reserve Fund required by the Trust Indenture be
20 used as a substitute for the Operating Revenue Allowance?**

21 A: No it can not. As I pointed out in my original prefiled testimony I have worked on a number
22 of engineering and financial feasibility studies related to municipal revenue bonds. I drafted
23 much of the Kent County Water Authority's bond indenture which has served as a model for
24 Rhode Island's other water utility bond indentures. I worked closely with Pawtucket's bond
25 counsel in reviewing much of their bond indenture. I have discussed this specific matter
26 with bond counsel to be very clear, and I sent her my draft testimony to be sure that she con-
27 curred with what I was saying. In addition, I perform annual reviews for a number of Rhode
28 Island water utilities to ensure that specified terms of the indentures are being met, and I
29 have prepared financial feasibility certificates for a number of recent water revenue bond is-

1 sues in Rhode Island. I believe I am well aware of the terms and conditions of the trust in-
2 dentures in general and of the Pawtucket Water Supply Board's indenture in particular.

3
4 The Operation and Maintenance Reserve Fund established under the General Bond Resolu-
5 tion is **NOT** a substitute for the Operating Revenue Allowance. The O&M Reserve Fund
6 can be used for specific purposes only: (1) to make principal and/or interest payments if
7 there are insufficient amounts available in the debt service fund, debt service reserve fund,
8 renewal and replacement reserve fund or the renewal and replacement account or (2) to
9 make payments for operation and maintenance if the amounts in the operation and mainte-
10 nance fund is insufficient. Unlike the 1.5% operating revenue allowance, the O&M Reserve
11 Fund can not be used for other purposes such as payments towards IFR costs if revenues are
12 insufficient or to the O&M or R&R reserve funds. The O&M Reserve Fund is also quite
13 different in that this fund or account may not simply be used up if revenues are insufficient –
14 the fund must be repaid. It is only to be used for a short term cash flow. At the end of each
15 fiscal year, the O&M Reserve Fund must have an amount on deposit equal to 25% of Paw-
16 tucket Water's operating budget. While money can be withdrawn and used in an emergency,
17 it *must* be paid back in the fiscal year. With the 1.5% operating revenue allowance, a short-
18 fall in sales and revenues can be covered by that allowance for the year and no repayment is
19 needed. That is not the case with the O&M Reserve Fund established in the General Bond
20 Resolution (bond indenture).

21
22 **Q: How should the Commission consider the O&M Reserve Fund vis-à-vis the Operating**
23 **Revenue Allowance?**

24 A: It really should not be considered at all when discussing the Operating Revenue Allowance.
25 The O&M Reserve Fund should be viewed as an account that is only used in an extreme case
26 or emergency. It should not be viewed as something that is used if sales of water drop, gas
27 prices rise, or benefit expenses go up more than expected. I believe that the operating reve-
28 nue allowance established by the Commission was intended to fill this purpose. I also be-
29 lieve that to do what was intended, that the allowed percentage should be based on the full

1 revenues as it initially was and that the allowed percentage needs to be adjusted up to reflect
2 today's conditions.

3

4 **Q: You have discussed the uncertainties associated with future water revenues and ex-**
5 **penses and why the Commission should provide for more realistic water sales estimates**
6 **and an operating revenue allowance on total revenues. Does Pawtucket need both of**
7 **these and a 5% operating revenue allowance?**

8 A: I recognize that this may seem to be asking a lot, but I believe it is necessary. In the case of
9 water sales and revenues, clearly they are decreasing over time and historic data about rain-
10 fall or other factors do not change this pattern. While there may be a year when water use
11 goes up over a previous year, there is a clear trend of dropping water sales. We are simply
12 asking the Commission to take note of the downward trend in water use. By accepting the
13 PWSB's position, the Commission will help assure that Pawtucket Water can get the reve-
14 nues allowed. However, because of the downward trend in sales, it is still unlikely. That is
15 where the operating revenue allowance comes in.

16

17 In this docket we have discussed how the actual collection of allowed revenue increases lags
18 the implementation date – there is a built in shortfall. The allowance should be based on the
19 total revenues the way it was formerly applied by the Commission.

20

21 I also recognize that there has been considerable discussion about the proper level for the
22 operating reserve fund. The choice of 5% was not an arbitrary one. As shown on CPNW
23 Sch. 2.1, the sales variations over the four year period from FY 2004 to FY 2007 have
24 shown an average drop of just under 5%; the same as the six year average from FY 2002 –
25 FY 2007. Over the seven year period presented, the drop on sales (and thus drop in reve-
26 nues) has exceeded 5% in 3 of the 7 years. Over the past six years the sales and revenue
27 drops have been more than 5% half the time. While the historic data shows a clear trend in
28 dropping sales we have proposed sales that are actually higher than the test year sales. If re-
29 cent history is an indication of future trends, the PWSB needs at least a 5% operating reve-