

RATE FILING
For
THE CITY OF WOONSOCKET WATER DIVISION
REBUTTAL TESTIMONY
OF
WALTER E. EDGE Jr. MBA CPA
SR. VICE PRESIDENT, B&E CONSULTING LLC

DOCKET # 4320

AUGUST 2012

1 **Q. Good morning Mr. Edge. Are you the same Walter Edge that has filed direct**
2 **testimony in this docket?**

3 A. Yes.
4

5 **Q. What is the purpose of your rebuttal testimony?**

6 A. My rebuttal testimony will address the issues raised by Ms. Crane and Mr. Mierzwa
7 in their direct testimonies filed on behalf of the Division of Public Utilities and Carriers
8 (DPUC). I have read their pre-filed testimonies in this docket and have a few comments
9 and observations relating to each of their testimonies.
10

11 **Q. Mr. Edge, how would you like to proceed?**

12 A. I would like to start with Mr. Mierzwa's testimony.
13

14 **Q. Ok then, please explain your comments relating to Mr. Mierzwa's testimony.**

15 A. Mr. Mierzwa reviewed the WWD pre-filed cost allocation and rate design testimony
16 and recommended no changes. He did however recommend that in WWD's next rate
17 case that WWD "re-examine and document the reasonableness of its historical allocation
18 factors in its next rate case as appropriate". The WWD agrees with Mr. Mierzwa's
19 observations and suggestions and will complete a thorough review of the historical
20 allocation factors given the changes relating to the new treatment facility when it files its
21 first rate filing including the new treatment facility.
22

23 **Q. Mr. Edge, please explain your observations and recommendations relating to**
24 **Ms. Crane's testimony.**

25 A. Ms. Crane started her testimony by recognizing that "WWD has done a relatively
26 good job of holding down operating costs" and that test year operating costs "were only
27 marginally higher than operating costs in fiscal year 2008". WWD appreciates Ms.
28 Crane's recognition of these achievements in her testimony.
29

1 Ms. Crane next pointed out that WWD has proposed increasing operating expenses by
2 \$324,030 over test year levels, while reducing restricted accounts by \$172,818 (net
3 \$151,211). The remainder of WWD’s rate request increase in this docket was related to
4 revenues. Ms. Crane concluded that “in spite of these modest increases, we still believe
5 that the WWD’s rate year claim is overstated”
6

7 **Q. Mr. Edge, how much did Ms. Crane think the WWD “modest increase” claim of**
8 **\$813,326 was “overstated”?**

9 A. She concluded that it was overstated by \$806,782.
10

11 **Q. How could a “modest increase” be 99% overstated?**

12 A. Ms. Crane only reduced the operating costs by \$261,273 which is 81% of the WWD
13 requested increase in operating cost, and she then reduced the funding of the restricted
14 accounts an additional \$545,509 more than the WWD reduction of \$172,818. Therefore,
15 if the Commission approves Ms. Crane’s recommended reductions in restricted accounts
16 the total reductions would reduced restricted account funding by \$718,327. WWD feels
17 that this funding level in the restricted accounts would be short sighted and eventually
18 result in either larger subsequent rate increases or an unwarranted decrease in the level of
19 service that WWD will (and must) be able to provide to its ratepayers.
20

21 **Q. What adjustment has Ms. Crane proposed?**

22 A. She has proposed 7 adjustments as follows:
23

Infrastructure Replacement Fund	\$456,000
City Services	175,130
Insurance Expense	81,425
Operating Reserve Allowance	59,509
Debt Service	30,000
Property and Fire Tax Expense	3,516
Light and Power	1,202
Total Reductions	\$806,782

24
25

1 **Q. I noticed that you have listed the adjustments in descending order based upon**
2 **the size of the adjustments. Would you like to discuss the adjustments in that**
3 **order?**

4 A. Yes. The first adjustment, a reduction of \$456,000 from the Infrastructure
5 Replacement Fund (IFR) is by far the largest adjustment and represents 56.5% of Ms.
6 Crane's adjustments. According to her testimony, Ms. Crane made the IFR adjustment
7 because: 1) "WWD has not undertaken the level of Infrastructure Replacement Fund
8 expenditure authorized by the Commission"; 2) "it is likely that much of WWD's
9 attention over the next few years will be focused on construction of the new treatment
10 plant. As a result, there may not be as much emphasis on Infrastructure Replacement (or
11 Renewal and Replacement) projects as there would otherwise be"; 3) "it is my
12 understanding that WWD does not have a permanent Superintendent in place at this time,
13 a fact that is likely to have an impact on the level of activity relating to Infrastructure
14 Replacement and Renewal and Replacement"; 4) "there is no reason to believe that
15 WWD will be spending considerably more from the Infrastructure Replacement Fund
16 than it has spent over the past few years; and 5) "Moreover, since I understand that WWD
17 intends to file another rate case within a relatively short period of time, the parties will
18 have the opportunity to examine more recent data and make adjustments in the next
19 case".

20

21 **Q. Do you agree with her analysis?**

22 A. Not at all. I believe that the facts are pretty much as she has stated but her
23 conclusions and recommendations are too extreme based upon the facts. It is true that
24 WWD has not undertaken the level of IFR expenditure that was approved by the PUC but
25 the reason for the reduction in spending (about \$700,000 per year in the last two years) is
26 not that WWD has decided not to do IFR projects, but rather is the direct result of the
27 underfunding of the IFR fund by \$2,634,915 over the last four years (\$1,277,649 in the
28 last two years). This shortfall is the direct result of revenues over the last few years not
29 achieving the projected revenue level approved in the last rate case.

30

1 Moreover, WWD has an approved IFR plan that must be achieved over the next few years
2 that cannot be completed if the IFR fund is cut by \$1,368,000 over those years. I am
3 concerned that these cuts will put WWD in non-compliance with the Department of
4 Health which as I understand it, requires that WWD implement its RIDOH approved
5 infrastructure replacement plan.

6

7 A second fallacy in her logic is that there is no direct correlation between under spending
8 in one year resulting in under spending in future years. In fact, the opposite is true; work
9 not completed in one year must be completed in the next year to catch-up with the work
10 required in the approved multi-year IFR plan. (See the rebuttal testimony of Sheila
11 McGauvran for more details relating to the approved IFR plan(s).) For this reason Ms.
12 Crane's analysis is incorrect.

13

14 **Q. Do you have any further responses to Ms. Crane's IFR testimony?**

15 A. Yes. Ms. Crane is correct, and it is likely that much of the WWD's attention will be
16 focused on the new treatment plant, but it is wrong to think that the WWD can only
17 complete one task at a time. The proposed IFR plan is also focused on important
18 projects related to WWD's transmission and distribution systems. WWD does not have
19 the staff to complete this type of work, so the work will most likely be outsourced.
20 Outsourcing this work will be accomplished by entering into an agreement with a
21 contractor (who successfully bids the job) who will do the work and be responsible for
22 the successful completion of the work. WWD will monitor the job to make sure that it is
23 properly done but the number of hours spent will be minimal. Spending \$2,000,000 a
24 year outsourcing cleaning, lining and replacing pipe is relatively easy and required by
25 WWD's approved IFR Plan. If the opportunity arises (adequate funding) I believe that
26 the WWD could spend far more than \$2,000,000 per year and catch up with its cleaning
27 and lining program, if it falls behind.

28

29 It is also true that there is no full time Superintendent at the WWD but the Director of
30 Public Works for the City (Sheila McGauvran) has stepped into the role on an interim

1 basis and has done a great job. It is unrealistic to believe that there will be no
2 Superintendent for the next three years, but if there isn't, the job will be completed under
3 the direction and management of the Public Works Director, and there will be no slippage
4 with any projects or the level of service provided to the ratepayers. Ms. Crane's
5 assumption that there will be slippage is merely one overly pessimistic opinion that has
6 no basis in fact. Ms. Crane produces no evidence that the City's Public Works Director
7 cannot follow through on important Water Division projects.

8
9 **Q. Do you have any further comments relating to Ms. Crane's IFR testimony?**

10 A. Yes. Ms. Crane is totally incorrect regarding evidence of future IFR need. There is
11 significant evidence that WWD will need at least \$1,956,000 (WWD requested a
12 continuance of the \$1,956,000 previously approved by the PUC) for IFR projects, and
13 given the proper funding, WWD will spend more on IFR programs in the future than they
14 have in the past.

15
16 The least convincing argument in Ms. Crane's testimony is the fact that WWD will be
17 filing another rate filing soon so that the parties will have a chance at that time to re-
18 evaluate the funding of IFR. "At that time" the IFR fund will already be down at least
19 \$1,000,000, which (if Ms. Crane is wrong) will result in a subsequent rate increase to
20 correct her adjustment which is not needed at this time. If the Commission accepts Ms.
21 Crane's adjustment and funds IFR at \$1,500,000 per year then that amount is all that will
22 be available and all that can be spent. This is a self fulfilling prophesy with severely
23 negative consequences to the utility and the ratepayers.

24
25 The result of her IFR funding reduction at this time will most likely create the need for an
26 increase in rates in the future when her proposed \$1,500,000 proposed funding level is
27 found to be inadequate to achieve the required IFR plan. Further, lost in her argument is
28 the fact that all of the IFR monies are restricted and therefore cannot be used for any other
29 purpose. The Commission has found, after significant review and testimony in prior
30 dockets, that the \$1,956,000 requested by WWD in this rate case (and previously

1 approved by the PUC) was reasonable and nothing that Ms. Crane has presented shows
2 otherwise. Ms. Crane just feels that the amount is too high, which is and of itself not a
3 valid reason for the Commission to slash this IFR account.
4

5 **Q. Do you agree with Ms. Crane's adjustment to City Services?**

6 A. No I don't. Ms. Crane actually made three separate adjustments to City services.
7 The first two adjustments reduced the city service costs of \$326,122 calculated and
8 provided by the City's Treasurer. Her two reductions were 1) to eliminate 100% of the
9 general property expenses of the City Hall for the 6 WWD employees that actually work
10 in the City Hall (\$73,435) and the elimination of the allocation to the WWD of certain
11 cost relating to the Mayor's office (\$10,718).
12

13 There are 48 employees working in the City Hall and the six of them that are WWD
14 workers, representing 12.5% of the total workers in City Hall. Therefore, the City
15 Treasurer reasonably and properly allocated 12.5% (6/48) of the total costs of the City
16 Hall to the WWD. I find this allocation approach very reasonable. Ms. Crane provides
17 no alternative allocation. Instead she proposes to eliminate all of the allocation for these
18 6 WWD employees. Likewise, some portion of the Mayor's office and staff should be
19 allocated to the WWD but Ms. Crane completely disregards this reality, suggesting that
20 even though the Mayor and staff do some activities on behalf of the Water Division, that
21 it is not good enough to support any charges for the services.
22

23 **Q. What is the third adjustment to City Service expense?**

24 A. The third portion of the City Service adjustment is for the hydrant off-set. Ms.
25 Crane amortized the offset (\$272,932) from FYE June 30, 2012 over three years (at
26 \$90,977 per year). The problem with this adjustment is the fact that the City recognized
27 the offset in FY 2012, so amortizing one third of the total over fiscal years 2013, 2014
28 and 2015 is double counting the off-set. For this reason the adjustment is simply wrong.
29 I don't agree with any of Ms. Crane's City Service adjustments.
30

1 **Q. Do you have any comments regarding Ms. Crane's next adjustment on your**
2 **table above; insurance expense?**

3 A. Yes, I do. However I would like to address Ms. Crane's property taxes and
4 insurance expense adjustments together as Ms. Crane adjusted both using the same
5 methodology. The smaller of the two adjustments is the property tax adjustment in the
6 amount of \$3,516. Normally, I would not spend much time on such a small adjustment
7 but Ms. Crane ties her Insurance adjustment (\$81,425) back to her property tax
8 adjustment even though the facts about the two adjustments are far different.
9 Nevertheless, she uses the same logic.

10

11 Ms. Crane's property tax adjustment is simply the elimination of the proposed WWD
12 increase for the rate year over the interim year expense level. Ms. Crane suggested that
13 the recognition of an increase in expense from the interim year to the rate year is
14 speculative and that there "is no evidence to suggest that the percentage increase
15 experienced in the interim year will also be experienced in the rate year".

16

17 I note that Ms. Crane is not from RI and maybe she is not aware of the serious financial
18 issues faced by RI communities including Woonsocket. Also, Ms. Crane does not
19 explain that her adjustment is basically for just one community (North Smithfield) and
20 the percentage used by WWD to calculate the increase for the rate year was only 2.96%.
21 It is difficult to believe that North Smithfield will increase taxes less than 2.96% in the
22 rate year. It is even more difficult to believe that North Smithfield will keep taxes level
23 in the rate year (no tax increase) as suggested by Ms. Crane.

24

25 **Q. Do you reject Ms. Crane's property tax adjustment?**

26 A. Yes. It should be pointed out that Ms. Crane made one additional point in her
27 property tax argument, that with the exception of the interim year, property tax expense
28 has been "very stable" over the past three years. This fact, although meaningless, is true
29 for property taxes, but not for insurance (see below).

30

1 **Q. So how did Ms. Crane calculate her adjustment for insurance?**

2 A. Ms. Crane made no calculation but rather simply eliminated the proposed increase
3 from the interim year to the rate year.

4 Ms. Crane expects that there will be no increase in insurance in the rate year.

5 Interestingly Ms. Crane does not make the same “very stable” argument for insurance that
6 she made for property taxes.

7

8 **Q. What did you find out when you researched this omission?**

9 A. The largest portion of the insurance increase by far (80% of the rate year adjustment)
10 from year to year is health insurance. The following table shows the health insurance
11 statistics that Ms. Crane omitted from her testimony.

12

13

FY	Amount
2008	\$331,899
2009	542,979
2010	568,672
2011	611,882
2012	671,000
Rate Year Projections	
Crane	671,000
WWD	735,829

14

15

16 **Q. What does the table above show?**

17 A. The table shows that Ms. Crane expects no increase in the health insurance costs for
18 the rate year while WWD projects a normal level of increase in health insurance cost.

19 Clearly the WWD projection is much more reasonable and based upon the last five years
20 of health insurance expense growth while Ms. Crane hopes that there will be no increase
21 in health insurance costs in the rate year which based upon the above table is very
22 unlikely.

23

1 **Q. What would you like to discuss next?**

2 A. The next item that I would like to discuss is the operating reserve allowance. Ms.
3 Crane reduced my request by \$55,590 by backing out the IFR, R&R and Debt service
4 funding from my calculation.

5

6 When I wrote my testimony, I was aware of the changes made by the RI PUC, allowing
7 increased operating reserve allowances to certain water utilities (Providence Water
8 Supply Board and Newport Water for example) to cover revenue shortfalls as well as the
9 normal expense overages. I was further aware that the PUC had not approved one of
10 these better methods of calculating the net operating reserve allowance for Woonsocket.
11 In fact, Woonsocket had been provided an allowance based upon net operating expense
12 less certain expenses that the PUC considered controllable.

13

14 Ms. Crane is correct that in the last rate case I agreed in my rebuttal testimony to the
15 method she used then and is proposing now. The reason for my agreement was two-fold.
16 1) WWD was attempting to reach a settlement on the entire case with the Division and
17 this issue was less important than other issues that the WWD needed. And 2) was the
18 fact that the PUC had already accepted her approach and it was kind of the law of the land
19 at that time.

20

21 **Q. What has changed?**

22 A. Providence Water was allowed a two piece net operating reserve to provide an
23 allowance for revenue shortfalls and expense overages and Newport was allowed a net
24 operating reserve of 3% of the net operating expenses. Either of these calculations
25 would result in a higher net operating reserve allowance for WWD than my proposed
26 1.5% of the total annual costs.

27

28 It was my intent to move the WWD net operating reserve from the previously approved
29 approach to this interim approach and then to one of the new approaches. My intent was
30 to make the move incrementally rather than all at once. Ms. Crane wants to stay with the

1 old approach that hurts Woonsocket and treats Woonsocket differently (and more
2 severely) than Providence and Newport. WWD respectfully believes that the PUC
3 should provide similar and as much as possible equally valued net operating reserves to
4 all water utilities. WWD would be receptive to receiving either the Providence or
5 Newport net operating reserve approach should my original proposal be rejected.
6

7 **Q. What is next?**

8 A. Debt service reserve. My Schedule WEE-12 shows that I have chosen to use
9 \$1,630,000 as the annual allowance for debt service for the rate year and the following
10 two years. Ms. Crane has reduced my allowance to \$1,600,000. The result is that Ms.
11 Crane recommends \$90,000 less funding to the debt service reserve than I do over the
12 next three years.
13

14 Ms. Crane and I are in agreement that the previous level of funding for the debt service
15 reserve (\$1,832,067) was excessive going forward and we both recommended
16 adjustments reducing the allowance. With my allowance the interim level surplus is
17 reduced from \$436,781 to \$217,444 by 2015. This is a little over 13% reserve which as a
18 CPA I feel comfortable with. Ms. Crane's allowance reduces the reserve after three
19 years to \$127,444 or 7.96%. Given the importance of paying debt service payments on
20 time; I believe that a reduction of the reserve to less than 10% is risky. Given the
21 financial status in the City at this time I am hopeful that the Commission decides that my
22 proposed reserve is more prudent.
23

24 **Q. That leaves only the light and power issue in the amount of \$1,202 for late
25 charges. Are you in agreement with Ms. Crane on this issue?**

26 A. When I read Ms. Crane's testimony I totally agreed with her that rate payers should
27 not pay late charges. I accept her adjustment.
28

29 **Q. Does that conclude your testimony?**

30 A. Yes.