

Exhibit No. _____T (AW-1T)
Docket UW-110220
Witness: Amy White

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

SUMMIT VIEW WATER WORKS,

Respondents.

DOCKET UW-110220

TESTIMONY OF

Amy White

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

July 22, 2011

TABLE OF CONTENTS

I. INTRODUCTION 1

II. SCOPE AND SUMMARY OF TESTIMONY 2

III. DISCUSSION 5

 A. Revenue Requirement 6

 1. Restating Adjustments 6

 2. Pro Forma Adjustments 19

 3. Capital Structure and Rate of Return 24

 B. Rate Design 25

 C. Remaining Issues 26

1
2
3 **I. INTRODUCTION**

4 **Q. Please state your name and business address.**

5 A. I am Amy White. My business address is 1300 S. Evergreen Park Drive S.W., P.O.
6 Box 47250, Olympia, WA 98504.

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

8 A. I am employed by the Washington Utilities and Transportation Commission
9 (Commission) as a Regulatory Analyst 3 working for Regulatory Services.

10
11 **Q. How long have you been employed by the Commission?**

12 A. I have worked for the Commission for four years, since June 2007.

13
14 **Q. Would you please state your educational and professional background?**

15 A. I graduated in 1982 from the University of Washington with a Bachelor of Business
16 Administration with an emphasis in Accounting. I earned a Master of Business
17 Administration (1988) and a Master of Public Administration (1989) from City
18 University of Seattle. I hold a Certified Government Audit Professional credential
19 from the Institute of Internal Auditors.

20 Before my employment began at the Commission, I was an Internal Auditor
21 for the Department of Social and Health Services (DSHS) for five years. I also
22 worked for DSHS as a Medicaid Fraud Auditor for five years, as a Hospital Auditor
23 for three years, and as the manager of the Surveillance and Utilization Review unit,

1 which performed pre-audit analysis of suspected fraudulent providers, for three
2 years. In addition, I worked for DSHS as a rate analyst developing hospital rates in
3 the Medicaid program for seven years. I also developed rates for hospitals for one
4 year in the workers' compensation program at the Department of Labor and
5 Industries.

6 As a Regulatory Analyst 3, I review the tariff filings of regulated water
7 companies either as the lead analyst or as a member of a Staff team. I have
8 presented Staff recommendations to the Commission at numerous Open Public
9 Meetings.

10 I am also lead analyst in Docket UW-110107, a pending case filed by
11 Summit View Water Works, LLC ("Summit View" or "Company") regarding a
12 surcharge and facility charge for financing construction of a new well for domestic
13 water service.

14 15 **II. SCOPE AND SUMMARY OF TESTIMONY**

16
17 **Q. What is the scope of your testimony?**

18 A. This proceeding involves setting rates and charges for the Company's irrigation
19 service. My testimony presents Staff's analysis of Summit View's adjusted Results
20 of Operations for ratemaking purposes, including Staff's recommended revenue
21 increase for irrigation service based on that adjusted Results of Operations.

22 I also present Staff's recommendation for the appropriate rate design for the
23 Company's irrigation service.

1 **Q. Please summarize your recommendation regarding revenue requirement.**

2 A. Staff's analysis shows that the Company has an annual revenue requirement
3 deficiency from its irrigation operations of \$15,518. A 62.7 percent increase in
4 irrigation revenues will eliminate that deficiency.

5 This compares to the Company's proposal to increase annual irrigation
6 revenues by \$19,118. The Company's proposal would increase annual revenues
7 from irrigation service by 77.2 percent.

8

9 **Q. Have you prepared an exhibit that calculates the revenue requirement you**
10 **recommend?**

11 A. Yes. Exhibit No. ___ (AW-2) summarizes and applies Staff's revenue requirement
12 model in this case in order to determine whether and by how much the Company's
13 annual revenues from irrigation service are deficient.

14

15 **Q. Please describe your Exhibit No. ___ (AW-2).**

16 A. Page 1 shows the Company's Results of Operations for a test year ended December
17 31, 2009. Column (h) shows Staff's numbers reflecting a \$15,518 rate increase
18 using an overall rate of return of 5.25 percent.

19 Exhibit No. ___ (AW-2) contains nine schedules from Staff's revenue
20 requirement model:

21 • Schedule 1 is a Summary of Adjustments that compares the Staff and
22 Company ratemaking adjustments.

- 1 • Schedules 3.1 and 3.2 show the individual Staff Restating
2 Adjustments and Pro Forma Adjustments.
- 3 • Schedule 6 calculates the revenue requirement deficiency proposed by
4 Staff.
- 5 • Schedule 7 calculates the interest synchronization amount for interest
6 expense allowable to the Company.
- 7 • Schedule 8 calculates the Beginning-End-of-Year adjustment related
8 to plant assets and accumulated depreciation.
- 9 • Schedule 13 shows the calculations for all Staff adjustments not
10 automatically generated by the assumptions in Staff's model file.
- 11 • Schedule 27 uses actual customer acreage to model payments and
12 produce a rate design.
- 13

14 **Q. Please summarize your recommendation regarding rate design.**

15 A. Staff recommends an irrigation "outlet fee" of \$215 per year plus an irrigation fee of
16 \$280 per acre per year, prorated to reflect the actual lot size. An outlet fee is similar
17 to a base rate per year. Staff's rate design is detailed in Exhibit No. ____ (AW-3).

18 This compares to the Company's proposed outlet fee of \$250 per year plus an
19 irrigation fee of \$300 per acre per year, also prorated to reflect the actual lot size.
20 Currently, the Company charges only a flat \$400 annual fee irrespective of acreage
21 size. This current rate design results in customers on lots approximating one-half an
22 acre paying the equivalent of \$800 per acre for irrigation while customers on five-
23 acre lots pay the equivalent of \$80 per acre.

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Q. Do you have any remaining recommendation in this proceeding?

A. Yes. As I will describe in more detail later in this testimony, Staff's analysis was severely complicated by deficient plant asset accounting and employee time keeping practices of the Company. Staff was required to address these deficiencies in order to present an appropriate analysis of the Company for ratemaking purposes. I will describe employee time keeping requirements Staff recommends the Commission order for Summit View to correct those shortcomings.

III. DISCUSSION

Q. Please provide a brief history of the regulated operations of the Company.

A. The Company has been regulated by the Commission since March 2006. It operates near Kennewick, Washington both a metered drinking water system and an unmetered irrigation system that utilizes a flat rate structure.

Docket UW-090124 was filed when the Company began serving customers in developments where lot sizes ranged in size from one-half acre to five and one-half acres in size. The Company realized that charging irrigation water service customers with one-half acre lots the same amount as those with five and one-half acre lots was unfair. The filing proposed to change the Company's flat rate irrigation service to a rate structure that included an outlet fee, plus a prorated, per-acre charge.

However, Docket UW-090124 was withdrawn so the Company could file a rate case for domestic and irrigation water service, which occurred in Docket UW-

1 090732. That filing was also withdrawn after Staff discovered that nearly all the
2 assets used in water production were owned by two affiliated companies, Tri-City
3 Development Corporation (TCDC) and Candy Mountain LLC (CMLLC). The
4 Company has entered a Purchase and Sale agreement with its affiliates to transfer
5 those assets, although it has not yet executed the promissory note to consummate the
6 deal.

7 The Company currently has another filing (Docket UW-110107) pending
8 before the Commission concerning rates to finance construction of a new domestic
9 drinking water well.

10
11 **A. Revenue Requirement**

12
13 **1. Restating Adjustments**

14
15 **Q. Turning to Staff's restating adjustments on Exhibit No. __ (AW-2), Schedule 3.1,**
16 **please describe Staff Restating Adjustment 1 (SR-1), Beginning-End-of-Year**
17 **(BEOY) Adjustment.**

18 **Q.** This adjustment of \$2,294 decreases accumulated depreciation for plant assets
19 associated with the irrigation business. The BEOY adjustment is related to Staff's
20 adjustment of test year depreciation of \$4,589 in Adjustment SR-33 discussed later
21 in my testimony.

1 **Q. Please describe Staff Restating Adjustment 4 (SR-4), Regulatory Plant**
2 **Adjustment.**

3 A. Staff's adjustments decrease the value of plant assets from \$1,577,785 as filed by the
4 Company to \$133,609. First, Staff disallowed \$1,387,764 to reflect assets not
5 transferred to the Company from its affiliates in a Purchase and Sale Agreement;
6 items that Staff could not match to invoices; items allocated to the domestic water
7 service; and items included in the asset listing multiple times in error. Staff removed
8 an additional \$56,412 to reflect used and useful plant. These two adjustments totaled
9 \$1,444,176. After adjustment, the value of irrigation Utility Plant in Service is
10 \$133,609 (rounded).

11 The Company filed for accumulated depreciation of \$158,106. Staff
12 removed \$141,663 Accumulated Depreciation associated with the \$1,387,764 in
13 assets disallowed due to ownership issues. Staff also removed \$4,200 of
14 Accumulated Depreciation associated with the \$56,412 adjustment to reflect used
15 and useful plant. These two adjustments totaled \$145,864 (rounded). After
16 adjustment, the value of Accumulated Depreciation associated with irrigation Utility
17 Plant in Service is \$12,242.

18 The Used and Useful adjustment was made as a restating adjustment to allow
19 income tax effects favorable to the Company related to restating adjustments. Staff's
20 adjustment addresses excess capacity by allocating a percentage of total plant to
21 current customers. Full cost recovery will be allocated to all customers when the
22 Company's developments are complete in order to recover cost that is equitable to
23 both current and future customers.

1 To calculate the Used and Useful adjustment, Staff initially used 115 (52.8
2 percent) active customers as of July 2011 against an anticipated total customer count
3 of 218 in phases 1-6 of the Summit View development and the Badger View and
4 Sunrise Canyon developments. However, additional analysis showed that 115 (52.8
5 percent) current customers own 70.3 percent of all anticipated irrigated residential
6 acreage. Therefore, residential acreage already under irrigation compared to total
7 potential residential acreage for irrigation is a more fair allocation basis because the
8 preponderance of the lots yet to connect to the irrigation service are small.

9
10 **Q. Please describe Staff Restating Adjustment 5 (SR-5), Taxes, Fees, and Bad Debt.**

11 A. This adjustment adjusts utility taxes, regulatory fees and bad debts to reflect the
12 impact of the additional revenues recommended by Staff. Utility taxes are increased
13 \$1,454, regulatory fees are increased \$47, and bad debts are increased \$37 based on
14 the increased irrigation income. The net adjustment increases expenses by \$1,538.

15
16 **Q. Please describe Staff Restating Adjustment 7 (SR-7), Metered Sales / Domestic
17 Income.**

18 A. The test year included \$32,316 of income from domestic water service. This amount
19 was disallowed by Staff because it is not pertinent to the irrigation rate case.

20
21 **Q. Please describe Staff Restating Adjustment 12 (SR-12), Other Income (Hookup
22 Charges).**

1 A. Staff removed all Hookup Charges income of \$40,500 received by the Company for
2 the test year. These funds are Contributions-in-Aid-of-Construction for domestic
3 water service and not properly considered income for irrigation service.

4
5 **Q. Please describe Staff Restating Adjustment 13 (SR-13), Salary and Wages-**
6 **Employees.**

7 A. Two maintenance employees work for both Summit View and CMLLC. Only
8 payroll records for their work for Summit View were submitted by the Company.
9 Nor did the Company maintain time records allocating staff time to either domestic
10 or irrigation operations. Since the irrigation and domestic water systems are similar
11 in terms of overall cost and in lineal feet of pipeline, Staff assumed that the
12 maintenance staff works equally on both systems and, therefore, Staff allocated the
13 salaries paid to these employees equally between irrigation and domestic water
14 service. This resulted in \$2,215 being allocated to irrigation and allowed for
15 ratemaking, and \$2,215 being allocated to domestic and disallowed for ratemaking.
16 The Company stated in a data request response that it was likely that more employee
17 time was spent on the irrigation system due to the lower quality water. However,
18 since no time records are maintained to substantiate that claim, an equal division of
19 expenses for these two employees is reasonable.

20 In addition, the Company employs a bookkeeper for its total operations.
21 Staff allocated her salary between irrigation and domestic water service using the
22 number of annual bills issued by the Company: two bills for each of the 88 irrigation
23 customers and 12 bills for each of the 87 domestic water customers served during the

1 test year. Staff calculated the relative amount of work done at \$12,815 (85 percent)
2 related to the domestic water business, which Staff disallowed, and \$2,185 (15
3 percent) related to the irrigation business, which Staff allowed. All salary expenses
4 of \$30 for a temporary employee were allowed for the irrigation operation.

5 Overall, \$4,430 (22.8 percent) of the Company's total salary expense is
6 allowed for the irrigation business and the total amount disallowed for the domestic
7 operations is \$15,030. A corresponding adjustment of \$1,729 to decrease payroll tax
8 expense was made to disallow all but 22.8 percent of the payroll taxes in Staff's
9 Restating Adjustment 36 (SR-36).

10
11 **Q. Please describe Staff Restating Adjustment 16 (SR-16), Purchased Power and**
12 **Water.**

13 A. Summit View paid \$10,572 for power expenses related to the domestic water
14 business during the test year. Staff disallowed this amount since it is unrelated to the
15 irrigation business. A related adjustment was made in Staff Pro Forma Adjustment
16 17 (SP-17) to allow \$14,468 in purchased power expenses related to the Company's
17 Wholesale Water Agreement with CMLLC since that expense relates to irrigation. A
18 second related adjustment to Purchased Power and Water was made in Staff Pro
19 Forma Adjustment 9 (SP-9) pertinent to Staff's adjustment for growth of \$7,693.

20
21 **Q. Please describe Staff Restating Adjustment 17 (SR-17), Chemicals.**

1 A. Irrigation water is not treated, so no chemicals are used to provide irrigation service.
2 All chemicals are used only for treating domestic water. Staff, therefore, disallowed
3 \$983 representing the total test year cost of water treatment chemicals.

4
5 **Q. Please describe Staff Restating Adjustment 18 (SR-18), Material and Supplies.**

6 A. The Company's filing includes \$8,069 in Materials and Supplies. Of that amount,
7 invoices substantiated \$568 in expenses related to irrigation service, which Staff
8 allowed, and \$332 in expenses for domestic water service, which Staff disallowed.

9 General ledger payments substantiated an additional \$850 in expenses, with
10 \$425 allocated to irrigation operations, which Staff allowed, and \$425 allocated to
11 domestic operations, which Staff disallowed.

12 In addition, the general ledger contained an adjustment of \$6,319, which the
13 Company stated in its response to Data Request 4, Item 3, contained two expenses:
14 \$1,590 to purchase billing software and \$4,729 as a prior period payment for payroll
15 due to the bookkeeper for 2008, which was prior to the test year. The \$1,590 for
16 billing software was disallowed as a current expense, but Staff added the item to the
17 Company's plant assets with a three-year depreciable life. The \$4,729 for the prior
18 period payroll was disallowed as an out-of-period expense.

19 The sum effect of Staff's adjustment is to allow \$933 for irrigation service
20 and to disallow \$7,076 for domestic water service.

21

22 **Q. Please describe Staff Restating Adjustment 20 (SR-20), Contract Accounting**
23 **and Bookkeeping.**

1 A. Staff found that the \$3,329 test year expense for this item contained two items:
2 \$2,560 for the QuickBooks payroll preparation service and \$790 related to a payroll
3 expense account holding the expense for a late-year payroll check to a maintenance
4 employee that had not been cleared to the correct expense account by year's end.
5 The general ledger amount substantiated costs of \$3,349. Because of the \$21
6 difference (rounded) between the Company-filed and the general ledger amount,
7 Staff adjusted the expense amount upward by \$21. The payroll service expense was
8 allocated to the domestic and irrigation operations in the same proportion as salaries
9 had been allocated in Adjustment SR-13; \$1,977 (77.2 percent) of the expense was
10 allocated to domestic operations and thus disallowed. \$583 was allocated to the
11 irrigation operations and allowed. The \$790 salary expense from the payroll expense
12 account was disallowed completely. Since this employee's salary had previously
13 been allocated 50 percent to irrigation and 50 percent to domestic operations, the
14 same allocation was maintained, and an adjustment of \$395 was made to Salaries
15 Expense.

16 The total disallowed from the test year for the irrigation operations was
17 \$2,767 less the bookkeeping adjustment of \$21 for a net disallowance of \$2,746.
18 Salaries Expense was increased by \$395. Expenses were adjusted downward a total
19 of \$2,351 after all adjustments.

20
21 **Q. Please describe Staff Restating Adjustment 21 (SR-21), Contractual Legal**
22 **Expenses.**

1 A. The test year includes legal expenses of \$13,760. Examination of underlying
2 invoices showed that \$437 of the expenses related to water rights and work with the
3 Commission. Staff allowed these expenses.

4 The remaining \$13,323 in legal expenses relates to development of a
5 Purchase and Sale agreement to transfer assets from the affiliates CMLLC and
6 TCDC. These expenses were clearly related to issues that should have been resolved
7 at the time Summit View began operations or no later than the time the Company
8 became regulated in 2006. Staff, therefore, disallowed this amount from test year
9 expenses, allocated half the expenses to domestic and half to irrigation, and made an
10 adjustment to plant of \$6,661 in Staff Pro Forma Adjustment 22 (SP-22) to capitalize
11 and amortize the legal expenses over a five-year life. Staff chose a five-year life,
12 rather than the three-year life typically used for legal expenses, because these were
13 extraordinary expenses. Moreover, these expenses most closely resembled start-up
14 expenses, which would have a life matching the composite depreciable life of the
15 assets involved in the transfer. However, a much longer life would not accurately
16 reflect the cost in rates making the five-year life chosen by Staff a conservative
17 compromise.

18
19 **Q. Please describe Staff Restating Adjustment 22 (SR-22), Contractual Operations.**

20 A. The Company filed for expenses of \$7,969 in this expense category. This amount
21 includes \$900 for Anderson Water System Consultants, a water system operator who
22 worked only on the domestic water business. Therefore, all of these expenses were
23 disallowed.

1 \$745 paid to two other consultants (Rogers Surveying and Water Man
2 Consulting) were for services related to a groundwater permit that is used for both
3 domestic and irrigation purposes. Therefore, Staff allocated that amount equally
4 between the domestic and irrigation business, resulting in a \$373 disallowance.

5 Finally, \$6,324 was paid to HDR Engineering to develop of the Purchase and
6 Sale agreement to transfer assets from CMLLC and TCDC to Summit View. Staff
7 disallowed this amount from test year expenses, allocated half the expenses to
8 domestic and half to irrigation, and made an adjustment to plant of \$3,162 to
9 capitalize and amortize the legal expenses over a five-year period.

10 The total of all disallowances was \$7,596. Just as in Adjustment SR-21,
11 Contractual Legal Expenses, this expense was clearly related to issues that should
12 have been resolved at the time the Company began operations or no later than the
13 time the Company became regulated. Staff used a five-year life to be consistent with
14 Adjustment SR-21 for legal expenses related to the Purchase and Sale agreement.
15

16 **Q. Please describe Staff Restating Adjustment 24 (SR-24), Office Rental.**

17 A. There are currently 223 customers who potentially use the Company's office; 108
18 (48 percent) are domestic water customers and 115 (52 percent) are irrigation
19 customers. Staff allocated office rental expense using current customer count:
20 \$2,681 (48 percent) to domestic water customers, which was disallowed, and \$2,854
21 (52 percent) to irrigation service, which was allowed for ratemaking.
22

1 **Q. Please describe Staff Restating Adjustment 25 (SR-25), Transportation**
2 **Adjustment.**

3 A. The test year included \$3,266 for transportation expense. However, the Company
4 maintained no records for travel required for maintenance or other purposes.
5 Moreover, since the domestic and irrigation systems cover approximately the same
6 distance, it is reasonable to assume that similar amounts of travel are needed for each
7 system. Therefore, Staff allocated one-half of the total transportation expense to
8 each of the domestic and irrigation operations. The amount allocated to the domestic
9 water operations that was disallowed was \$1,633. The amount allocated to irrigation
10 that was allowed was \$1,633.

11
12 **Q. Please describe Staff Restating Adjustment 26 (SR-26), Insurance Adjustment.**

13 A. The test year included insurance expenses of \$2,738 for vehicle and general liability
14 insurance. The Company incurred workers' compensation premium costs of \$295
15 that were not included in the filing but were substantiated in the general ledger. Staff
16 allocated the insurance expenses evenly between the domestic and irrigation
17 operations. Because the domestic and irrigation systems have similar amounts of
18 plant assets in terms of cost, the need for vehicle and general liability insurance is
19 equivalent for each operation. The adjustment for the amount allocated to the
20 domestic water operations that was disallowed is \$1,369. The remaining \$1,369 was
21 allowed for irrigation operations.

22 Labor and Industries premium costs were \$295 and were allocated between
23 the domestic and irrigation operations on the same basis as payroll. This resulted in

1 \$67 (22.8 percent) of workers' compensation costs being allocated to the irrigation
2 and allowed. The remaining \$228 of workers' compensation premium was allocated
3 to domestic water service and disallowed. The net adjustment is a decrease of
4 \$1,302.

5
6 **Q. Please describe Staff Restating Adjustment 29 (SR-29), Travel, Education,**
7 **Consumer Confidence Reports (CCR), and Public Relations.**

8 A. Total expenses of \$404 in this category were allocated evenly between the domestic
9 and irrigation operations. These items were all related to dues, subscriptions,
10 education, and education-related meals that are equally related to both systems. This
11 resulted in a \$202 disallowance from the test year expenses.

12
13 **Q. Please describe Staff Restating Adjustment 30 (SR-30), Office, Postage, Phone,**
14 **and Bank Charges Expenses.**

15 A. The Company filed for \$3,448 in this expense category. Office supplies expense of
16 \$1,259 and postage expense of \$876 are allocated based on the overall number of
17 bills for the Company operations: 85 percent of bills were for domestic service and
18 15 percent were for irrigation services. This allocation results in disallowances of
19 \$1,070 for office supplies and \$745 for postage expense. Phone expenses of \$1,264
20 and bank fees of \$49 were split evenly between the domestic and irrigation
21 operations, resulting in \$656 being allocated to the domestic business and
22 disallowed. The total amount allocated to domestic operations and thus disallowed is
23 \$2,471. The remaining \$977 in expenses was allocated to irrigation and allowed.

1

2 **Q. Please describe Staff Restating Adjustment 32 (SR-32), Repair Expense.**

3 A. The total expense filed by the Company is \$7,023. Staff examined all invoices in
4 this expense category and allocated \$4,515 to the domestic water operations based on
5 the nature of each expense shown on each invoice. Two invoices showed amounts
6 related to freeze damage and, thus, were costs for the domestic water system because
7 the irrigation service does not operate during cold months when freeze damage is
8 possible. Staff also disallowed \$28 since it was for a farming irrigation pivot on
9 affiliate Candy Mountain Farm. The adjustment results in a total disallowance of
10 \$4,543. The expense amount allowed for the irrigation operations is \$2,480.

11

12 **Q. Please describe Staff Restating Adjustment 33 (SR-33), Depreciation Expense.**

13 A. The Company used \$8,080 as its beginning depreciation expense. That is the same
14 amount shown on its 2009 Annual Report filed with the Commission.

15 After review of detailed depreciation schedules submitted by the Company,
16 Staff determined that that amount tied to the three assets shown on the Annual
17 Report balance sheet: two different construction costs related to the irrigation pond
18 and the water system plan. Staff calculated the correct depreciation amounts for
19 these three items using NARUC service lives and the dates the assets were placed in
20 service. This calculation resulted in a depreciation expense amount of \$4,589,
21 showing that the \$8,080 amount used by the Company is excessive.

22 Also, Staff anticipated a large depreciation adjustment related to the assets
23 shown in the Purchase and Sale agreement and via the Company's depreciation

1 schedules. For clarity, Staff replaced the incorrect depreciation amount of \$8,080
2 with the correct depreciation amount of \$4,589 as calculated by Staff. This resulted
3 in a net disallowance of depreciation expense of \$3,491.

4
5 **Q. Please describe Staff Restating Adjustment 34 (SR-34), Excise Tax.**

6 A. The Company filed for a total expense of \$3,125. Using the Excise Tax rate of 5.029
7 percent, Staff calculated the expense amount related to the domestic operations as
8 \$1,710, which was disallowed from irrigation expenses. The remaining \$1,415
9 relates to irrigation service and was allowed. This amount nets against the \$1,454
10 additional expense calculated in Adjustment SR-5 related to increased revenue for a
11 total decrease to Excise Tax expense of \$256.

12
13 **Q. Please describe Staff Restating Adjustment 36 (SR-36), Payroll Taxes.**

14 A. The Company filed for \$2,238 in total payroll tax expense. Payroll taxes of \$1,729
15 related to the domestic water operations were disallowed using the same allocation
16 percentage (77.2 percent) as the salaries disallowance in Adjustment SR-13, Salaries
17 and Wages-Employees. This adjustment disallowed all but \$509 (22.8 percent) of the
18 payroll taxes for the irrigation water operation.

19
20 **Q. Please describe Staff Restating Adjustment 37, Other Tax and License Fees**
21 **(DOH/UTC/ESD/DOE).**

22 A. Staff reviewed these expenses and found that they were all related to work the
23 Company did with the Department of Health regarding the Company's Water System

1 Plan (WSP). The WSP does not address irrigation water, so all expenses (\$406)
2 were allocated to the domestic operations and disallowed.

3
4 **2. Pro Forma Adjustments**

5
6 **Q. Please describe Staff Pro Forma Adjustment 1 (SP-1), Pro Forma Interest**
7 **Synchronization.**

8 A. Pro forma interest expense is calculated based on the net pro forma average rate
9 base, the weighted average cost of debt, and the interest per books. The Company
10 has a highly unfavorable debt to equity position, with negative owners' equity and
11 debt equal to 144.5 percent of the debt plus equity total. All of the Company's debt
12 was with the owners or affiliated companies, which, for ratemaking, earns at prime
13 rate plus two percent, 5.25 percent in this case. The Commission has found this
14 formula reasonable for calculating the cost of debt for transactions between a
15 regulated company and an affiliated company that is not regulated by the
16 Commission. See *WUTC v. American Water Resources, Inc.*, 6th Suppl. Order at 6,
17 Docket Nos. UW-980072, *et. al* (January 21, 1999). An adjustment of \$6,632 was
18 calculated to allow the Company to recover allowable interest costs in rates.

19
20 **Q. Please describe Staff Pro Forma Adjustment 2 (SP-2), Pro Forma Income Tax.**

21 A. Income Tax expense is adjusted downward by \$2,203 to reflect decreased federal
22 income tax due from the Company because of the overall effect of Staff adjustments
23 to revenue and expense.

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Q. Please describe Staff Pro Forma Adjustment 3 (SP-3), Pro Forma Adjustment for Capital Improvements.

A. This adjustment adds depreciation expense for plant assets that are added during the year on a pro forma basis. In this case, \$12,663 in plant assets added were those that Staff disallowed from test year expenses in order to capitalize and amortize: \$7,911 of legal expenses in Adjustments SR-20 and SP-28, consulting expenses of \$3,162 in Adjustments SR-22, and \$1,590 related to software in Adjustments SR-18. A beginning-end-of year adjustment related to these assets results in additional plant assets of \$6,331. The first year's depreciation for all these items, after a beginning-end-of year adjustment was made, is \$1,372, which was added to the Company's allowed expenses.

Q. Please describe Staff Pro Forma Adjustment 5 (SP-5), Pro Forma Adjustment for Taxes, Fees, and Bad Debt.

A. Pro forma adjustments increasing regulatory commission fees \$40, increasing bad debt \$32, and decreasing utility excise taxes \$556 are netted for a total pro forma decrease to expenses of \$484. These variable expenses are adjusted as the result of changes to revenue and calculated expenses in all other adjustments.

Q. Please describe Staff Pro Forma Adjustment 9 (SP-9), Unmetered Irrigation Sales Revenue.

1 A. Summit View has experienced a significant amount of growth since the 2009 test
2 year when the Company served 88 irrigation customers to the present day total of
3 115, a 30.7 percent increase. Expected revenue has, therefore, been adjusted upward
4 by \$21,261 to reflect the collection of \$400 per year from each of the 115 current
5 customers, for total revenue of \$46,000.

6 Along with the revenue adjustment, Staff adjusted the variable expenses that
7 can be expected to increase as the customer base increased. Staff made variable
8 expense adjustments to Postage for \$58 and Office Supplies for \$40, using the 30.7
9 percent growth in customer count.

10 Additionally, Staff reviewed Purchased Power / Water expense in the context
11 of increased acreage being irrigated by customers. From the test year to present,
12 customer acreage under irrigation increased from 86 acres to 131.7 acres, a 53.2
13 percent increase. Staff increased the \$14,468 allowed expense in Purchased Power /
14 Water from Adjustment SP-17 using the 53.7 percent adjustment factor for an
15 increase of \$7,693 in this expense category. This brought the total Purchased
16 Power/Water adjustment to \$22,161. The total increase to expenses in Adjustments
17 SP-9 is \$7,792.

18
19 **Q. Please describe Staff Pro Forma Adjustment 17 (SP-17), Purchased Power /**
20 **Water.**

21 A. Under the terms of the Wholesale Water Agreement between CMLLC and Summit
22 View, Summit View makes an annual payment for a prorated share of power costs
23 related to the irrigation well after the end of the calendar year. The calculation is

1 based on the ratio of acreage under cultivation by Candy Mountain Farms and the
2 acreage owned by the homeowners in the Summit View, Badger View, and Sunrise
3 Canyon developments. In 2010, Candy Mountain billed and Summit View paid
4 \$15,298 for power related to the irrigation operation. Staff adjusted the irrigable
5 acreage of the homeowners to account for un-irrigable surfaces such as houses (using
6 minimum house size as shown in the development restrictive covenants) and
7 driveways (estimated as 25 percent of the house size) which dropped the acreage
8 attributed to the homeowners from 86 acres to 82 acres. As a result, Staff decreased
9 the \$15,298 paid expense by \$830 for a net Purchased Power / Water adjustment of
10 \$14,468. This amount, combined with the \$7,693 Purchased Power / Water
11 Adjustment in SP-9, related to the variable cost increase driven by the increasing
12 customer base, makes for a total adjustment to Purchased Power / Water of \$22,161.

13
14 **Q. Please describe Staff Pro Forma Adjustment 22 (SP-22), Contractual Legal.**

15 A. Legal expenses of \$13,323 related to the asset Purchase and Sale agreement that
16 were disallowed from test year expenses in Adjustment 21 (SR-21) are allocated
17 between the domestic and irrigation business and then capitalized to be amortized
18 over five years. Because the domestic and irrigation systems have similar amounts
19 of plant assets and the legal work involved pertained equally to both operations,
20 these costs were allocated equally to the two operations. Of the \$13,323 in legal
21 expenses, \$6,661 was allocated to the irrigation business to be capitalized and
22 amortized. In addition, a review of invoice detail found \$2,500 that the Company
23 documented as Rate Case Legal Expense was actually related to the Purchase and

1 Sale agreement. This amount was also adjusted into the capitalized amount after
2 allocating \$1,250 to the domestic operations and \$1,250 to the irrigation operations.
3 The total legal expense capitalized and amortized is \$7,911. The adjustment amount
4 of \$1,582 represents one year's worth of amortization expense related to these legal
5 costs.

6
7 **Q. Please describe Staff Pro Forma Adjustment 23 (SP-23), Contractual**
8 **Operations.**

9 A. Expenses of \$6,324 paid to consultants who worked on the asset Purchase and Sale
10 agreement that were disallowed from test year expenses in Adjustment 22 (SR-22)
11 are allocated equally between the domestic and irrigation businesses and then
12 capitalized to be amortized over a five-year life. Since the irrigation and domestic
13 systems have similar amounts of plant assets and the consulting work pertained
14 equally to both operations, these costs were allocated equally to the two operations.
15 Of the \$6,324 total cost, \$3,162 was allocated to the irrigation operation and
16 amortized over five years. The adjustment amount of \$632 represents one year's
17 worth of amortization expense related to these legal costs.

18
19 **Q. Please describe Staff Pro Forma Adjustment 28 (SP-28), Regulatory Legal**
20 **Expense.**

21 A. Staff examined legal invoices from the legal counsel representing the Company in
22 both Dockets UW-110107 and UW-110220 and found that the attorney had also
23 performed work on the Wholesale Water Agreement and the asset Purchase and Sale

1 agreement. These costs were removed in order to be capitalized and amortized in the
2 same manner as other professional service costs. Costs related to Docket UW-110107
3 were also removed since they do not relate to irrigation service.

4 Staff found that there were eleven months' worth of invoices and total costs
5 of \$9,763 related to the current docket. Based on those amounts, Staff calculated an
6 average monthly cost of \$888 related to Docket UW-110220 and assumed that
7 approximately two months' more work is likely to resolve that case in its entirety.
8 The total legal rate case costs in this docket are calculated at \$11,538 which is
9 amortized over three years. This results in a \$3,846 increase in expenses.

10
11 **Q. Does this conclude your discussion of all Staff Restating and Pro Forma**
12 **adjustments?**

13 A. Yes.

14
15 **3. Capital Structure and Rate of Return**

16
17 **Q. Please discuss the capital structure that Staff used to develop its revenue**
18 **requirement recommendation.**

19 A. The Company's capital structure is shown on Exhibit No. ___(AW-6). All debt is
20 held among the three affiliated companies or the two owners of the companies. Staff
21 adjusted the interest for this affiliated debt to 5.25 percent, which, again, is the prime
22 rate plus 2 percent. Staff also adjusted the value of the notes to CMLLC and TCDC
23 to reflect the actual value of the allowed assets for a total of \$264,079. Two notes

1 are held by the owners of all three affiliated companies totaling \$10,000. Total
2 affiliated debt due from Summit View to the affiliates or owners is \$274,079. Other
3 liabilities not included in the capital structure calculation include net Contributions-
4 in-Aid-of-Construction of \$113,700 and miscellaneous accounts payable of \$1,764,
5 which brought the Company's total liabilities to \$389,543.

6
7 **Q. Please discuss the rate of return that Staff used to develop the Company's**
8 **revenue requirement.**

9 A. The overall calculation of weighted average debt as shown on Exhibit No. ___(AW-
10 6) shows that debt comprises 144.6 percent of the debt-to-equity ratio while the
11 Company's equity amount is -44.6 percent. Since all debt is among affiliated parties,
12 it should earn a return of 5.25 percent.

13
14 **B. Rate Design**

15
16 **Q. Please discuss Staff's proposed rate design.**

17 A. My Exhibit No. ___(AW-3) shows the rate design recommended by Staff.

18 Staff recommends a rate design that includes an "outlet charge", which is a
19 term common to the irrigation industry. An outlet fee is equivalent to a base charge
20 for drinking water. Staff set the outlet charge at \$215 per customer so that the
21 Company could recover approximately 40 percent of the revenue requirement of
22 \$61,518 from the 115 current irrigation customers.

1 Additionally, Staff recommends a \$280 prorated per-acre charge to recover
2 60 percent of the revenue requirement. This charge uses the actual acreage of the
3 lots occupied by current customers billed at the rate of \$280 per acre, prorated by
4 actual lot size as established through county records.

5 Staff considered adjusting the acreage of each lot to reflect “un-irrigable
6 surfaces” defined as the minimum square footage of each lot’s house, as prescribed
7 in each development’s restrictive covenants, plus a 25 percent allowance for each
8 home’s driveways and other impermeable surfaces. However, it was apparent that
9 the savings to customers were minimal and would likely be outweighed by increased
10 administrative costs for the Company to prepare and maintain records reflecting the
11 actual lot acreage less the house and impermeable surface adjustment. This method
12 also creates potential conflicts between customers and the Company and would
13 require annual adjustments to reflect construction of out-buildings such as sheds,
14 barns, etc. and impermeable surfaces such as pools, patios, tennis courts, and
15 driveways.

16
17 **C. Remaining Issues**

18
19 **Q. You stated earlier in your testimony that Staff encountered issues with the**
20 **Company’s plant asset accounting. Please explain.**

21 A. In Dockets UW-090124 and UW-090732, Staff learned that Summit View’s plant
22 assets used in water production were still the property of affiliates CMLLC and
23 TCDC. In an affiliated interest filing in Docket UW-101903, the Company filed the

1 Purchase and Sale agreement transferring some of the plant assets from these
2 affiliates to Summit View. Notes payable from Summit View to the affiliates were
3 prepared for Summit View to sign, but the notes have not been executed so no
4 property has yet changed hands. Staff reviewed depreciation schedules listing assets
5 that had been prepared by the Company and its consultants and found that many of
6 the assets for which the Company was seeking a return had either not been included
7 in the Purchase and Sale agreement and thus still belong to either CMLLC or TCDC;
8 were listed on the depreciation schedules twice in error; had already been paid for
9 outright by Summit View and thus should not be included in the Purchase and Sale
10 agreement to begin with; or could not be traced to invoices submitted by Summit
11 View. Exhibit No. ___ (AW-4) summarizes the Company's errors or lack of
12 documentation regarding its plant assets.

13
14 **Q. Why is this issue a significant?**

15 **A.** This is significant because Summit View's case seeks to place \$1,577,785 in plant
16 assets onto its balance sheet while Staff has only been able to substantiate \$328,083
17 in assets. Staff allocated \$190,021 of those assets to the irrigation operations of the
18 Company and the remaining \$138,062 was allocated to the domestic water
19 operations. In its affiliated interest filing in Docket UW-101903, the Company
20 informed the Commission that these assets are to be financed 100 percent through
21 debt owed to affiliates CMLLC and TCDC.

22

1 **Q. Did you prepare a corrected balance sheet for the Company?**

2 A. Yes. Exhibit No. ____ (AW-5) is an adjusted balance sheet prepared by Staff. It
3 begins with the balance sheet filed in the Company's Annual Report for 2009. Staff
4 notes that the balance sheet filed by the Company was \$37,073 out of balance. Staff
5 then added amounts to bring the Company's assets up to the \$328,083 total asset
6 amount substantiated by Staff. Staff has also adjusted the accumulated depreciation
7 to the amount calculated using NARUC depreciation lives. Liabilities were adjusted
8 to reflect the actual Contributions-in-Aid-of-Construction (less accumulated
9 amortization) balance. Long-term debt was adjusted to reflect the entire amount of
10 plant assets adjusted onto the balance sheet since the Company intends to finance the
11 transfer of those assets from its affiliates using 100 percent debt. Finally, an
12 adjustment of \$120,493 was made to Retained Earnings to force the balance sheet to
13 balance. This aggregated the net effect of all the adjustments and the amount that the
14 Company's original balance sheet had been out of balance. The result of these
15 adjustments to the Company's balance sheet showed that the Company had negative
16 equity capital of \$89,792 and total liabilities of \$389,543, for a net liabilities plus
17 owners' equity total of \$299,751 compared to an asset base of \$299,751.

18
19 **Q. You stated earlier that Staff encountered issues regarding the Company's**
20 **record-keeping for employee time. Do you have any recommendation on this**
21 **issue?**

22 A. Yes. Staff recommends that the Commission order the Company to establish a time
23 system that produces accurate records of employee time related to either the
24 domestic or irrigation operation in order that accurate allocation of costs to each

1 operation can be done. This should alleviate the difficulties encountered by Staff in
2 its analysis in this case.

3

4 **Q. Does this conclude your testimony?**

5 **A. Yes.**