STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

Petition for Approval of Special Contract with Anheuser-Busch, Incorporated	)))))	**Docket No. DW 11-018**

Direct Testimony and Schedule of

Michael Gorman

On behalf of

Anheuser-Busch, Inc.

Project 9349
March 31, 2011

BRUBAKER & ASSOCIATES, INC.
CHESTERFIELD, MO 63017

**STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION**

Petition for Approval of Special Contract with Anheuser-Busch, Incorporated	)))))	**Docket No. DW 11-018**

Direct Testimony of Michael Gorman

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A Michael Gorman. My business address is 16690 Swingley Ridge Road, Suite 140, Chesterfield, MO 63017.

Q WHAT IS YOUR OCCUPATION?

A I am a consultant in the field of public utility regulation and a Managing Principal of Brubaker & Associates, Inc., energy, economic and regulatory consultants.

Q PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A This information is included in Appendix A to my testimony.

Q ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?

A I am appearing on behalf of Anheuser-Busch, Inc. ("A-B"). A-B purchases water from Pennichuck Water Works, Inc. ("PWW" or "Company") pursuant to a special contract effective from July 1, 2005 to July 1, 2015. A-B accounts for more than 10% of PWW's annual volume of water sales. The special contract rates are based in part on

1 PWW's filed cost of service. Consequently, changes in PWW's tariff rates will have a
2 direct financial impact on A-B, and affect its rights and substantial interests.

3 Q **WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY IN THIS**
4 **PROCEEDING?**
5 A I will support the reasonableness of the proposed special contract rate for A-B
6 outlined in PWW witness Mr. Donald L. Ware's direct testimony (January 21, 2011).

7 Q **WHAT ARE THE NEEDS OF A-B WITH RESPECT TO ITS WATER SUPPLY?**
8 A Water is critical to A-B's business. A-B has four principal requirements:
9 (1) high-quality water; (2) reliable service; (3) operational cooperation with its supplier;
10 and (4) long-term, stable rates that are reasonable and cost-based. A-B has no
11 criticism of PWW with respect to the first three criteria.
12 In A-B's view, PWW's initial proposed rates in this docket did not accurately
13 reflect A-B's cost of service, and were inconsistent with the language and spirit of the
14 Third Special Contract. The proposed rates allowed A-B no alternative but to
15 terminate the Third Special Contract, potentially interrupting a relationship with PWW
16 spanning four decades. After difficult negotiations and compromises on both sides,
17 A-B and PWW were able to reach a new agreement in the Fourth Special Contract
18 ("FSC").
19 A-B continues to disagree with certain parts of PWW's revised cost of service
20 analysis, as further discussed below. A-B is willing to forego contesting those issues
21 solely because the FSC provides a reasonable accommodation by assuring adequate
22 future rate stability. A-B therefore withholds a full critique of PWW's cost of service

1 filings, in the spirit of cooperation and under the key assumption that the Commission
2 will approve the FSC.

3 Q **PLEASE DESCRIBE THE PROPOSED CONTRACT RATE FOR A-B.**
4 A The proposed contract rate for A-B is outlined at pages 7 through 13 of Mr. Ware's
5 testimony. As outlined in that testimony, he concludes that the proposed contract
6 rate is cost based, will fully compensate PWW for its cost of providing service to A-B
7 under the contract rate, and will benefit other customers by retaining A-B as a
8 customer of PWW.

9 Q **IS MR. WARE CORRECT THAT THE PROPOSED CONTRACT RATE IS BASED**
10 **ON PWW'S COST OF PROVIDING SERVICE TO A-B?**
11 A Yes. There are three elements to the contract rate. First, the FSC rate provides for
12 charges for the two six-inch meters that will be serving A-B at PWW's customer meter
13 charges. As such, the charge rate for PWW's customer service is based on the cost
14 of service study, and fully compensates PWW for the cost of the meters, reading the
15 meters, billing A-B, and responding to A-B service inquiries.
16 Second, the FSC rate includes a volumetric charge that is tied to the
17 operations and maintenance ("O&M") cost of water treatment plant, pumping for the
18 water treatment plant, and source of supply for the water treatment plant. These
19 costs are allocated among customers based on base usage and extra capacity – max
20 day and max hour demands. PWW then spreads these O&M costs between
21 customers as a uniform volumetric charge in the development of the FSC rate. The
22 development of a volumetric charge for unit production cost is outlined in PWW
23 witness John R. Palko's testimony on his Schedule 13, page 1.

1 The FSC rate volumetric charge also includes an allocated portion of
2 administrative and general ("A&G") expenses. A-B's FSC rate includes a combined
3 allocation of A&G costs using a base, max day and max hour allocation. PWW
4 developed A-B's base, max day and max hour allocation factors based on the
5 contract specified A-B loads. As such, the capacity and volume costs PWW will incur
6 to serve A-B under this contract were specifically identified in Mr. Palko's cost of
7 service study and used to design the FSC rate.

8 Finally, the FSC rate provides for a monthly carrying charge rate which is tied
9 to the return, depreciation and tax expense for PWW's source of supply investments
10 including the Supply Pond, Holt Dam, Water Treatment Plant ("WTP"), and the Fifield
11 Tank. A-B's allocated share of total carrying charges for these investments was
12 based on A-B's max-day demand.

13 I would note that PWW's transmission and distribution piping system was not
14 allocated to the FSC rate, because A-B directly compensated PWW for the
15 installation of a large water transmission pipe that directly connected A-B to PWW's
16 water treatment plant. Hence, A-B does not use PWW's transmission and distribution
17 system other than this direct connection. Therefore, A-B should not be allocated any
18 additional costs associated with PWW's transmission and distribution piping system.

19 Q **DO YOU BELIEVE THAT THE A-B SPECIAL CONTRACT RATE RECOVERS**
20 **PWW'S COST OF SERVICE?**

21 A Yes. The FSC rate is based on PWW's cost of service study and A-B contract load.

1 Q **DO YOU BELIEVE THAT THE PWW COST OF SERVICE STUDY PROPERLY**
2 **ALLOCATES COSTS TO A-B AND OTHER HIGH VOLUME USERS?**
3 A PWW witness Mr. Palko developed a class cost of service using the well-accepted
4 cost of service methodology of base and extra capacity. This methodology assigns
5 cost to customers based on their base volume and peak demands occurring during
6 the max day demand and the max hour demand. Based on my experience, this is a
7 well-accepted, commonly used water cost of service methodology.
8 However, I do have concerns with the development of cost allocation included
9 in Mr. Palko's study. In fact, I believe that PWW's cost of service study over-allocates
10 costs to A-B and other high volume users. For example, the PWW cost of service
11 study does not allocate a portion of the WTP to max hour extra capacity demands.
12 As a result, the PWW cost of service study under-allocates WTP costs to customers
13 who contribute more to peak hour demands. This results in an over-allocation of
14 costs to large users like A-B, and an under-allocation of costs to small residential and
15 commercial users.
16 Further, in the design of the FSC rate, Mr. Palko did allocate source of supply
17 and WTP O&M expensed based on base, and max day demand allocation factors
18 (Schedule 13 at 1). However, after those base and extra capacity allocations were
19 made, he converted this production O&M into a uniform volumetric charge.
20 Spreading production O&M on a uniform volumetric basis results in allocating too
21 much of this O&M cost to A-B.
22 For example, if the FSC volumetric rate for production O&M expenses had
23 been allocated to A-B using the base, max day and max hour A-B allocation factors
24 Mr. Palko developed on Schedule 13, page 3, and then the allocated A-B costs were
25 spread based on A-B's contract volume, then the volumetric charge for A-B would be

1 approximately $0.1039/CCF lower. This will result in A-B paying over $57,000 per
2 year more than its fairly allocated share of PWW production O&M costs. (See
3 Schedule MPG-1).
4 As such, A-B believes that while the FSC rate is cost based, the Company's
5 cost of service study had the effect of over-allocating costs to A-B in this FSC rate. A
6 more appropriate allocation of costs to A-B would have resulted in a lower FSC rate.

7 **Q ARE YOU PROPOSING CHANGES TO THE FSC RATE?**
8 A No. As noted above, the FSC rate represents a compromise of many issues in this
9 case, and A-B will accept the FSC rate.

10 **Q WILL THE A-B CONTRACT RATE BENEFIT PWW'S OTHER CUSTOMERS?**
11 A Yes. Since this contract rate includes recovery of fixed costs that are paid by A-B,
12 other customers benefit from the existence of this rate. Specifically, the carrying
13 charges and fixed O&M costs that are paid by A-B under the FSC rate would instead
14 be allocated to other customers, if A-B left the PWW system. Therefore, since the
15 FSC rate more than fully recovers PWW's cost of service to A-B, and reduces the
16 amount of PWW fixed costs that will be paid for by other customers of PWW if A-B left
17 the PWW system, then all PWW customers benefit from the existence of this contract
18 rate.
19 Further, the FSC rate has take-or-pay provisions which provide revenue
20 assurance to PWW. This revenue assurance will provide stability to PWW's credit
21 rating, and maintain its financial integrity. As such, other customers benefit from
22 retaining A-B on its system through revenue stability and an enhanced credit position.

1 **Q IN YOUR EXPERIENCE ARE SPECIAL CONTRACT RATES GENERALLY**
2 **APPROVED BY REGULATORY COMMISSIONS?**
3 A Yes. Based on my experience, if a special contract rate is necessary to retain or
4 attract additional load to a system, it is fully cost compensatory with the incremental
5 cost of serving that customer, and does not detrimentally impact other customers on
6 the system, then the contract rate is in the public interest.

7 **Q DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**
8 A Yes, it does.