

AQUARION WATER COMPANY OF NEW HAMPSHIRE

DW 12-085

Aquarion Water Company's Responses to Staff Data Requests—Set 2

Data Request Received: September 26, 2012
Request No.: Staff 2-28

Date of Response: October 10, 2012
Witness: C. McMorran

REQUEST: Has the company applied any specific metrics to its WICA performance in NH?
If so, please provide and explain.

RESPONSE: Please refer to the Company's response to data request Staff 2-27. Increased levels of capital spending are demonstrated below by a comparison of capital budgets for each category pre-WICA (2007-2009) and post-WICA (2010-2012).

Category	Pre-WICA 2007-2009	Post-WICA 2010-2012
Main replacement costs	\$1,538,000	\$1,776,000
Feet of main replaced	7,230	6,355
Meters, cost	\$154,000	\$343,000
, count	2,448	3,738
Hydrants	\$65,000	\$84,000
, count	10	19
Services	\$88,000	\$100,000
, count	71	110
Valves	\$17,000	\$70,000
, count	2	10
Control Valves	\$0	\$0
Production Meters	\$2,600	\$20,000
, count	1	4

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Aquarion Water Company's Responses to Staff Data Requests—Set 3

Data Request Received: November 5, 2012
Request No.: Staff 3-12

Date of Response: November 19, 2012
Witness: T. Dixon
Page 1 of 2

REQUEST: Please provide any and all evidence, especially objective evidence, that the WICA pilot program has produced benefits to customers and to the company.

RESPONSE: As the Staff testified in DW 08-098, WICA is a recognized concept for water utilities adopted by numerous states other than New Hampshire. Order No. 25,019 at 16. The benefits of a WICA program, as testified to by Aquarion the OCA, and the Staff, include the incentive to increase the rate of infrastructure replacement; increased oversight of Aquarion infrastructure replacement projects; the mitigation of rate shock between rate cases; and the potential to delay future rate cases. Id. at 15 – 16. In its order authorizing the current WICA program on a pilot basis, the Commission stated that the program “appears to strike a reasonable balance between reducing rate shock to customers at the time of each rate case and providing an incentive to Aquarion to accelerate needed infrastructure replacement.” Order No. 25,019 at 17. As described below, the Company has unquestionably accelerated its infrastructure replacement, as was intended by the Commission when it approved the program on a pilot basis. The purpose of accelerating infrastructure replacement is to reduce the various problems related to an aging system, such as leaks, main breaks, water quality deterioration, and reduced service reliability. These benefits, as opposed to the direct expenditure of capital funds, are inherently difficult to quantify because they would be measured over the long term and consist of problems avoided.

Aquarion’s rate of infrastructure replacement.

Incentivizing Aquarion to accelerate needed infrastructure replacement was a key factor cited in the Commission’s order authorizing the WICA program on a pilot basis. As set forth on pages 27-28 of the prefiled testimony of Mr. Dixon, since the WICA was authorized by the Commission, the Company’s spending on infrastructure replacement has increased by nearly 20% on an annual basis when compared to the level of spending prior to authorization of the WICA and by nearly 80% on an annual basis when compared to the amounts included in the capital budget at the time the WICA was approved. This substantial increase in spending on necessary infrastructure replacement is consistent with the stated primary purpose of the WICA, as set forth in Order No. 25,019.

To date, under the WICA program, main replacements have been installed on Atlantic Avenue between Mill Road and Maple Road. Since installing the new

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main, the Company has not received any calls from customers on Atlantic Avenue regarding taste, odor or discoloration, and there have been no main breaks or service interruptions on the section of main replaced since installation. In addition, the fifteen services replaced in 2010 and 2011 have reduced the risk of short-term service interruptions.

Oversight of projects.

Prior to the WICA program, the Company first completed capital projects and later sought recovery of costs through the rate case process. In Dockets DW 09-211 and DW 10-293, the Commission, Staff, OCA and Towns have all had the opportunity to express an opinion or preference with respect to which projects the Company is anticipating to complete in the forward three years, and the Company cannot undertake such projects under the WICA program without first obtaining Commission approval. Projects included in the Company's most recent filing, DW 12-325, will be subject to the same review. As noted above, this is consultative process was cited by the Commission as a benefit to all stakeholders.

Mitigation of rate shock between rate cases.

While the WICA program provides the Company with more timely cost recovery, the customer receives the benefit of more gradual rate increases. Without the WICA program, the rate increase being sought in this case would be approximately 22.8%, rather than 18.3%.

Potential to delay rate cases.

As stated in Mr. Dixon's testimony, it is likely that the Company would not have had to file a rate case in 2012 were it not for increases in expenses and property taxes. This is because the Company's rate base growth since its last general rate case has been incorporated into the Company's revenue requirement through the existing WICA surcharge. The WICA program was not intended to address Company's non-WICA related expenses increases, and therefore to the extent that these increases persist, rate increases will continue to be necessary on a periodic basis, albeit at a lower level than would otherwise have been the case.

1 to improve or protect the quality and reliability of service to customers. Aquarion's
2 proposal indicates that such projects would include mains, valves, services, meters, and
3 hydrants; main cleaning and re-lining projects; relocations of infrastructure that are not
4 reimbursable; purchase of leak detection equipment; and installation of production meters
5 and pressure reducing valves. Aquarion proposes that the WICA surcharge be limited to
6 5% of each customer bill in any 12 month period, and capped at 7.5% in total prior to the
7 filing of its next general rate case. Following completion of that rate case, the WICA
8 surcharge would be subsumed into the new permanent rates and be reset to zero.

9 **Q. What benefits to customers does Aquarion cite in this WICA proposal?**

10 A. Aquarion cites mitigation of rate shock, less frequent rate cases, and reduction of lost
11 water as benefits to customers. In addition, Aquarion has told the parties to this docket
12 that Aquarion, and water utilities in general, need to be further incented to speed up
13 critical infrastructure replacement. Aquarion points to the endorsement of the
14 distribution system improvement charge (DSIC), a similar measure, by the National
15 Association of Regulatory Utility Commissioners (NARUC) in 1999. That endorsement
16 also cites benefits such as improved water quality, increased pressure, and fewer main
17 breaks and service interruptions.

18 **Q. Has the WICA surcharge mechanism been previously approved in New
19 Hampshire?**

20 A. No it has not. The DSIC has been approved for use in a number of other jurisdictions,
21 including Pennsylvania, California, Delaware and others, as cited in Mr. Bingaman's
22 testimony.

23 **Q. What is your view of the proposed WICA surcharge?**

1 A. I believe the WICA proposal proffered by Aquarion in this proceeding has merit, but I
2 can only support it with a corresponding adjustment to Aquarion's cost of equity.
3 Aquarion has suggested that the WICA mechanism has substantial benefits to customers.
4 Mr. Bingaman's testimony suggests that customers will benefit through a more reliable
5 system with improved water quality, through the mitigation of rate shock since rate
6 increases based on capital spending will occur to some extent between rate cases, and
7 through less frequent rate cases and their associated cost to prosecute. Although I agree
8 that these all represent some level of benefit to customers, it is my opinion that the utility
9 receives much greater benefit. The benefits to the utility include enhanced cash flow and
10 a reduction in regulatory lag. There are also other likely impacts of implementing a
11 WICA surcharge that are of concern.

12 **Q. Please elaborate on your other concerns with the WICA surcharge.**

13 A. Approval of a WICA surcharge where customer rates can be increased between rate
14 cases is a significant change to the traditional method of ratemaking. It is my view that
15 the existing framework for setting rates has worked well. Well managed utilities with
16 capital budgets implement system improvements in an orderly way, by acquiring the
17 needed capital, deploying that capital in the field, and seeking rate adjustments all in a
18 coordinated manner. The rate of return granted by regulatory bodies is reflective of the
19 level of risk inherent in the provision of traditional utility service. It is my opinion that
20 the introduction of a WICA mechanism alters the relative risk of a utility in the utility's
21 favor because it will speed up its cash flows, reduce regulatory lag, and will mitigate its
22 litigation risk in future rate proceedings.

1 Another concern with implementation of a WICA surcharge is that the introduction of a
2 mechanism such as a WICA can open the door to other similar pass-through of costs.
3 Although I recognize that Aquarion's proposal includes Commission scrutiny not only of
4 the list of eligible projects, but of the calculated surcharge to be applied to customer bills,
5 I do not believe that mechanisms that provide for changes to customer rates without a full
6 analysis of all of the utility's costs are particularly fair to customers, and may further
7 upset the balance of risk in utility ratesetting.

8 **Q. Do you have a recommendation for addressing your concerns with a WICA**
9 **surcharge?**

10 A. Yes. I believe that if the Commission finds that a WICA surcharge is appropriate for
11 Aquarion, the terms of its implementation be carefully defined. Most of all, however,
12 consistent with my earlier comments that I believe that the WICA surcharge provides
13 greater benefits to the utility than to the customer, I believe that implementation of a
14 WICA surcharge should be accompanied by a reduced return on the company's equity
15 capital. It is difficult to quantify the amount of reduction in return that would return the
16 balance between the utility and its customers. I am recommending a starting point of 25
17 basis points, and thus Staff's recommendation for a cost of equity in this proceeding
18 would be 9.50% if a WICA proposal is adopted. Staff looks forward to discussing these
19 issues with the parties at our scheduled settlement conference on June 16.

20 **IV. SYSTEM DEVELOPMENT CHARGE (SDC)**

21 **Q. Please describe the SDC proposal that Aquarion has made in this proceeding.**

22 A. As explained in Mr. Bingaman's testimony, Aquarion proposes a SDC, also known as
23 a connection charge, to offset the cost of system improvements needed to accommodate

AQUARION WATER COMPANY OF NEW HAMPSHIRE, INC.
DW 12-325

Aquarion Water Company's Responses to
Staff's Data Requests – Set #1

Date Request Received: November 21, 2012 Date of Response: November 30, 2012
Request No.: Staff 1-5 Witness: Carl McMorran

REQUEST: Re: Testimony of Mr. McMorran at page 6, lines 7-8. Please elaborate on the financial and scheduling factors referenced.

RESPONSE: Financial factors that affect the number of hydrant, service and valve replacements proposed for a WICA program year (Oct. 1 through Sep 30) involve trades of funds between particular budget line items. Actual costs for individual projects rarely match the exact budget so funds are shifted as needed to keep total capital spending on budget. When project costs are higher or lower than budgeted, other projects are canceled/postponed or increased appropriately.

Scheduling factors that affect the proposed number of hydrant, service and valve replacements are as follows. First, the number of replacements is primarily driven by how many broken or defective units are discovered in any given period of time. Second, except for hydrants, few service and valve replacements are scheduled for immediate repair and occur over subsequent months in conjunction with other water system operating and maintenance activities. Lastly, although the proposed number of replacements per program year is based on the Company's historical annual averages, a WICA program year does not line up with the Company's capital budget year (Jan. through Dec.) – and it was shorter in 2009 (WICA implementation year) and in 2011 (rate case test year) -- adding another scheduling variable that must be considered in the Company's projections.

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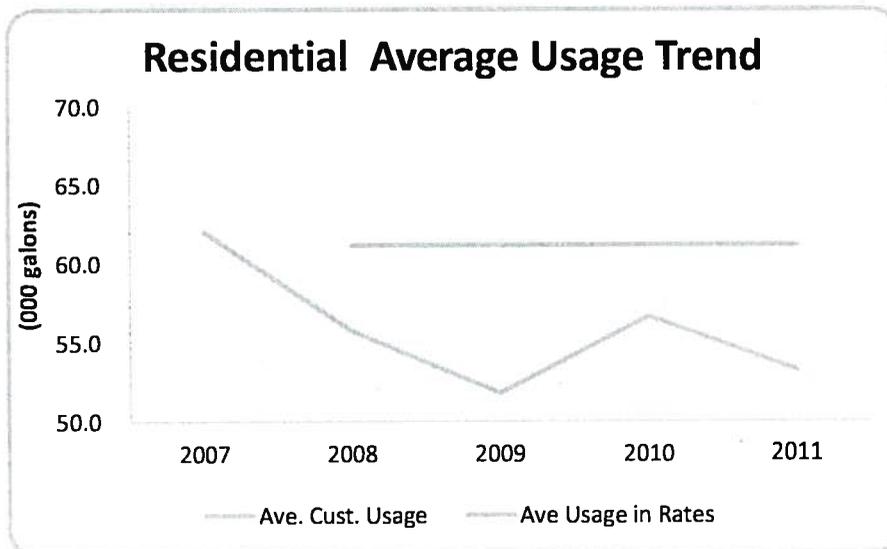
Data Request Received: September 26, 2012
Request No.: Staff 2-25

Date of Response: October 10, 2012
Witness: T. Dixon

REQUEST: Aquarion has stated that its sales volume has declined and for temporary rates, Aquarion estimated the average annual residential ratepayer usage at 53,300 gallons, or 7,100 ccf. Please provide information documenting this decline such as a calculation of the average annual residential consumption for each of the past three years.

RESPONSE: The average residential consumption takes the annual residential consumption divided by the year end residential customers. The table provided below illustrates the annual average residential consumption for the last five years.

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>
Residential Consumption	483,835	440,067	411,267	451,899	428,762
Residential Customers	7,794	7,885	7,933	7,967	8,042
Consumption/Customers	62.1	55.8	51.8	56.7	53.3



EDUCATION AND WORK EXPERIENCE OF MARK A. NAYLOR

My educational achievements include a Bachelor of Science degree in Social Science from Plymouth State College in 1978, and a Master of Science degree in Accounting from New Hampshire College in 1985.

I completed the National Association of Regulatory Utility Commissioners (NARUC) Annual Regulatory Studies Program at Lansing, Michigan in August of 1992, and I completed the Nineteenth Annual Eastern Utility Rate Seminar co-sponsored by NARUC, the Florida Public Service Commission and the University of Utah in Hollywood, Florida in October of 1991. I am a member of the NARUC Staff Subcommittee on Accounting and Finance.

My professional work experience began as a Planner working for the Central New Hampshire Regional Planning Commission and the City of Manchester during the years from 1978 to 1984.

Upon receiving my MS in 1985, I was hired by Foxhill Interiors, Inc. in Bedford, NH as Controller. There I was responsible for all accounting, administrative, and financial functions of the Company. In October of 1986 I joined Landmark Title, Inc. in Manchester, NH as Controller. In this position I assumed responsibility for the accounting and finance functions of the Company and its two start-up subsidiaries, including preparation of financial statements and tax returns, budgeting and forecasting, and internal reporting to the parent company in Houston, Texas. I was named a Vice President by the Company Board of Directors in 1987.

In November of 1990 I joined the Finance Department of the New Hampshire Public Utilities Commission as a PUC Examiner. In that capacity I worked primarily on water and wastewater utility matters. I participated in Staff audits, conducted financial analysis and prepared written testimony, and testified in those cases before the Commission. I was promoted to Assistant Finance Director in August of 1995. In January of 1998 I was named Acting Finance Director, and in August of that year was promoted to Finance Director. My responsibilities in that position included management of the Finance Department and review and approval of the Department's work products, review of financial statements and earnings levels of the regulated utilities, and providing advice and testimony on revenue requirements, earnings levels, financings, accounting and related matters to the Commissioners, department heads, regulated utilities, and the general public. Following a reorganization of the Commission's Staff in late 2001, I was named Director of the Gas & Water Division. In that capacity I manage and direct the Staff of that division, and am responsible for Staff involvement in all dockets concerning gas, water, sewer and steam utilities that are pending before the Commission.