STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

PENNICHUCK WATER WORKS, INC.

DOCKET NO. DW 13-130

NOTICE OF INTENT TO FILE RATE SCHEDULES

DIRECT PREFILED TESTIMONY

OF

DONALD L. WARE

May 31, 2013

<u>Professional and Educational Background</u>

Q. What is your name and what is your position with Pennichuck Water Works, Inc.?

A. My name is Donald L. Ware. I am the Chief Operating Officer of the Pennichuck Water Works, Inc. ("the Company"). I have worked for the Company since 1995. I am a licensed professional engineer in New Hampshire, Massachusetts and Maine.

Q. Please describe your educational background.

A. I have a Bachelor in Science degree in Civil Engineering from Bucknell University in Lewisburg, Pennsylvania and I completed all the required courses, with the exception of my thesis, for a Masters degree in Civil Engineering from the same institution. I have a Masters in Business Administration from the Whittemore Business School at the University of New Hampshire.

Q. Please describe your professional background.

A. Prior to joining the Company, I served as the General Manager of the Augusta Water District in Augusta, Maine from 1986 to 1995. I served as the District's engineer between 1982 and 1986. Prior to my engagement with the District, I served as a design engineer for the State of Maine Department of Transportation for six months and before that as a design engineer for Buchart-Horn Consulting Engineers from 1979 to 1982.

Q. What are your responsibilities as Chief Operating Officer of the Company?

A. As Chief Operating Officer, I am responsible for the overall operations of the Company, including customer service, water quality and supply, distribution, engineering and water system capital improvements. With regard to capital improvements overseen by the Company's Engineering Department, I work closely with the Department and the Company's Chief Engineer regarding project selection, project design, project management and construction management.

Q. What is the purpose of your testimony?

A. I will be discussing the operations of the Company's and the impact of these operations on the requested rate increase. My testimony will interface with Larry Goodhue's and John Boisvert's testimony in regards to addressing the operational proformas that are part of Schedule 1 and the capital investments that impact Schedule 3.

Q. Before beginning a detailed analysis for the Rate Case Schedules please comment on how the change in ownership has impacted the operations of the Company.

A. The Company continues to operate its system in the same way as prior to the acquisition. The operations work in each department continues to be done by the same people as prior to the acquisition. The focus of the operations employees, both before and after the acquisition, is to meet the needs of our customers. The Company is supportive of the operations staff and has developed strategic initiatives to insure that the Company maintains highly motivated and well trained employees. These initiatives are listed in Pennichuck Corporation's Strategic Plan, which can be found on Pennichuck's web site, www.pennichuck.com under the Company Reports section.

Q. Please discuss the impact of the operating expenses and proformas detailed in Schedule 1, the Operating Income Statement.

The operating expenses reflected in the test year ending in December 31, 2012 in conjunction with the proformas that I will be discussing provide the basis for the Company's Schedule 1. I will focus my discussions on the differences in the Operating Income Statement between the year ending 12/31/2010 and the proformed test year ending 12/31/2012. As a matter of context, it is worth noting that the Company's requested increase in revenues of 0.12% is far less than the 9.10% increase it would have filed for as a publicly owned company. The lower rate increase being sought is a direct reflection of the benefits of the acquisition of Pennichuck Corporation by the City of Nashua, which are primarily derived from:

1. Reduced Return on Investment from 7.86% to 5.94% that translates into a lower cost of funds for capital investments.
2. Reduction in Public Company costs of approximately $1.87 million reflecting the total cost savings associated with the change in ownership as detailed in Mr. Goodhue's testimony.

Q. Why do you compare the operating expenses for the year ending 12/31/2010 (Calendar Year 2010 or CY 10) to the proformed expenses for the year ending 12/31/2012 (Calendar Year 2012 or CY 12)?

A. The comparison was made for the following reasons:

1. The CY 10 data is readily available on the Company's Schedule 1.
2. The CY 12 data represents the expense data adjusted to what we expect to experience during 2013. The proformed expenses reflect the annualization of part year 2012 expense changes as well as the inclusion and annualization of the known and measurable expenses that will be incurred within 12 months of the test year ended on 12/31/2012. The comparison of the expenses between CY 10 and CY12 presents a look over a 3-year time frame, which should eliminate the majority of expense anomalies that may occur year over year, but are unlikely to occur when doing an analysis over a series of years.

Q. Please discuss elements of the Operating Income Statement, beginning with the Production expense line explaining the difference between the CY 10 expense and the CY 12 proformed expense.

A. The proformed CY 12 production expense is $148,457 more than the CY 10 expense or about 3.9% over 3 years (about 1.3% per year). The primary cause for this expense increase is purchased water costs associated with the completion of the Derry – Drew Woods Interconnection. In 2012, the Company purchased $123,204 of water from Derry versus $0 in 2010.

Q. **Please explain the production expense proformas found in Schedule 1, Attachment B, Page 1.**

A. This proforma adjustment reflects an annualized increase of $19,921 associated with a 2.5% increase in union wage rates, a $26,315 increase in non-union wages, and an increase in sludge disposal costs resulting from an increase in sludge disposal rates. As an offset to these increased costs, the Company expects a reduction in its electric costs of $71,713 based on bids received for the supply portion of its electric power bill in the fall of 2012. The new, lower electric supply costs went into effect on November 1, 2012. The proforma for the Company's electric costs accounts for an additional 11 months of savings that the Company will experience in 2013

Q **Please explain the changes to the proforma income statement resulting in a $4,505 increase in Transmission and Distribution expense incurred between the CY 10 and CY 12.**

A. This increase resulted from increases in nonunion and union labor wage rates amounting to an annualized wage increase of $51,010. The increase in wage rates was offset by decreased expenses associated with main and service repairs in the amount of about $53,000. The cost savings were primarily the result of fewer main repairs in 2012 versus 2010. This is consistent with the ebb and flow of operating expenses the Company has discussed in previous rate cases where the cost to repair water mains and services is higher some years and less in others. For instance, the cost of service and main repairs in 2011 was $40,000 greater than the cost of service and main repairs in 2012.

Q. Please explain the Transmission and Distribution expense proforma found in Schedule 1, Attachment B, Page 2.

This proforma adjustment reflects the annualization of the increase to the union wages of 2.5% amounting to a $31,393 wage increase in conjunction with an increase in non-union salaries in the amount of $19,617, resulting in an overall proformed wage impact of $51,010.

Q. Please explain the $238,444 increase in Engineering Expense between CY 10 and CY 12.

A. The CY 12 expenses include two additions to the engineering staff in 2013; a Water Supply Engineer in training and an Asset Management Project Leader. The Water Supply Engineer in training is a replacement for the Company's water supply engineer who left in the spring of 2009. The Asset Management Project Leader is the Company's lead on its Asset Management, Data Presentation and Collection and GIS projects. The value of these projects to the Company is described in Mr. Boisvert's Pennichuck Water Works testimony. In addition to these two new staff positions, the Company added an AUTOCad Technician in 2011. These three positions account for $174,000 of the $238,444 increase. The remaining amount of the increase in engineering expense is the result of three years of annual wage increases and about $8,500 in fuel expense increases between 2010 and 2013.

Q Please explain the $40,520 decrease in Customer Accounts and Collection expense incurred between CY 10 and CY 12.

A. The Company is proforming a decrease in print management costs of $39,415 as detailed in Schedule 1, Attachment B, Page 4. This reduction in operating expenses is the result of a recent request for bids to provide the Company's print management, which resulted in a lower amount of $42,800 with an offset for increased postage costs of $3,385. The bid process was completed in advance of the expiration of the existing 2-year contract for these services, which was set to expire at the end of 2013, realizing these cost reductions in advance of 2014.

Q. Please explain the $405,781 increase in Administrative and General Costs between CY 10 and CY 12?

A. The majority of the administrative savings achieved were the result of a reduction in the number of Company officers and their related compensation, resulting in total savings in wages of $1.2 million between the 2010 and 2012 expenses, after proforming the salaries for former officers out of the 2012 expenses. Other expense savings associated with the acquisition are detailed in Mr. Goodhue's testimony.

Acquisition savings, however, were offset by the following increases:

1. Increased Insurance Expenses--approximately $228,000;
2. Increased Retirement Expenses--approximately $520,000;
3. Increased Health Care Expenses--approximately $280,000;

4. Increased Computer Equipment Maintenance Expenses--approximately $42,000; and

5. Three years of annual wage increases for the Company's customer service, information technology, administrative and accounting staff.

Q. Please explain the proforma found in Schedule 1, Attachment C, Page 1.

A. This proforma annualizes the April 2013 wage increases included in the Administrative and General Expense account. The proforma also eliminates all salaries paid in 2012 to the former executives (discussed above) through their departure/termination dates, between late January and early May of 2012.

Q. Please explain the more significant proforma adjustments detailed on Schedule 1, Attachment C, Page 2

A. The proformas detail some of the changes in expenses discussed previously. Additionally, the insurance proforma details the savings that will result in 2013 as the result of the Company's renewal insurance premiums for the policy year beginning January 1, 2013. The $17,873 reduction in insurance expenses from these 2013 policy renewals is an offset to the $228,000 in insurance costs incurred by the Company between 2010 and 2012. The $33,701 of increased Computer Maintenance Expenses is associated with the Company's Asset Management and GIS programs.

Q. There are no proforma increases associated with Health Care expense. Please explain.

A. The Company is in the process of transitioning to a health care plan with a $3,000/$9,000 deductible from a plan with a $2,000/$6,000 deductible. The new plan will have higher Co-pays and a four-tiered drug plan. The transition between plans is expected to keep health care costs flat in 2013 relative to those experienced in 2012. The change in plans is set to occur in 2014.

Q. Please explain the reduction in Interdivisional Management fee, pursuant to the 2006 Cost Allocation Agreement, of $375,330 between CY 10 and CY 12.

A. This reduction is the direct result of the City's Acquisition of Pennichuck Corporation and reflects the savings at the Corporate Level of decreased expenses associated with being privately owned versus a publicly traded company.

Q. What is the overall impact of the operating expense proformas and the CY 12 operating expenses when compared to the CY 10 operating expenses?

A. The CY 12 operating expenses are $381,338 greater than the year ending CY 10 operating expenses or about 3.4% over 3 years.

Q. Please discuss the Property Tax section of operating deductions section of the Operating Income Statement.

A. Property taxes continue to escalate at rates well in excess of inflationary levels. The increase in property taxes between 2010 and 2012 of $650,052 translates to an increase of just over 23.4%. During this same time frame Plant in Service, net of depreciation expense and the Municipal Acquisition Regulatory Asset increased by 2.1%. Schedule 1, Attachment D captures the projected increase in property taxes associated with the asset additions and retirements reflected in Schedule 1.A. Attachments A and B.

Q. Relative to impacts on the operating revenues please explain what has happened to the consumption patterns in the Company?

A. The Company evaluated consumption patterns by focusing on the winter quarter consumption as it is not impacted by summer usage and irrigation, and is considered in the industry to be representative of base residential consumption. Exhibit DLW-1 details the current consumption patterns. This exhibit shows a clear drop in base residential per day household consumption, amounting to 9.4% over the past 3 years. The impact on revenues of the drop in base consumption of 10.2 CCF per household per year was partially offset by a 2.6% increase in customers. CY 12 revenues were slightly higher than those granted as part of DW10-091 as a result of higher summer sales. The base consumption in 2012 was 8.5% less, or 352,928 CCF in comparison to the 2009 based consumption. The seasonal consumption in 2012 was 435,074 CCF greater than in 2009 with the net result being that volumetric sales in 2012 ended up being 82,146 CCF greater than in 2009.

The variance in seasonal load of 435,074 CCF at current rates of $3.30 per CCF translates into a revenue swing of $1,468,744 or a potential operating loss of about $750,000. This swing in operating revenues due to summer usage and the resultant variance in net income presents a challenge to Pennichuck with its current rate structure. The minimal amount of equity in the business limits the return that can be used to cover reductions in operating revenues.

Q. Does the Company plan to increase its level of equity to deal with this challenge?

A. In DW11-026 the Company indicated its desire to keep equity levels low in order to keep rates as low as possible. The level of equity in the Company may increase slightly in the future in the event the Company has year-end retained earnings that it can reinvest in its water systems.

Q. Has the Company promoted conservation?

A. The Company has promoted conservation through semi-annual mailings that have discussed proper lawn irrigation practices and that have promoted the use of water saving fixtures. Additionally, the Company's move to monthly billing allows a pricing signal to be sent in a timely manner to customers who choose to irrigate.

Without a change in rate design, promoting conservation further will affect those who are least able to buy water saving fixtures. As more conservation occurs, the water rate associated with the volumetric charge will need to go up to capture enough revenues to pay for the fixed costs that are paid for with volumetric revenue dollars.

Q. Does the Company seek temporary rates?

A. Yes. The Settlement Agreement requires that the Company seek temporary rates. Because the permanent rate relief sought for PWW is so low, however, the Company is requesting that temporary rates be set at current rates. Because the Company does not seek temporary rates at a level above current rates, I have not provided separate testimony in this case, as I have for Pennichuck East Utility, Inc. and Pittsfield Aqueduct Company, Inc. where we seek temporary rate increases.

Q. Will the proposed increase be spread uniformly across the various customer classes?

A. Yes.

Q. Was a Cost of Service Study prepared as part of this case?

A. No. The last cost of service study was prepared as part of DW 10-091. Inasmuch as there was little change in the mix of customers, assets and expenses since DW10-091, the Company determined that preparing a Cost of Service Study was not justified.

Q. Please summarize the impact of the Company's rate increase request by Customer Class.

A. The Tariff pages and Report of Proposed Changes sheets which detail the impact or the rate increase by customer class are found in Sections 6 and 13 of the filing.

Q. What is the status of the Company's Water Infrastructure and Conservation Adjustment Charge (WICA) Pilot Program?

A. The Commission issued Order No. 25,510, on May 15, 2013, in Docket No. DW 12-359, approving the Company's schedule of 2013 capital projects. The Commission indicated in its order that the scope of this proceeding will include an evaluation of the benefits of the WICA program. The WICA process is a multi-step, multi-year endeavor that will take several years' worth of data to fully evaluate with respect to the ultimate benefits related to the rate of infrastructure replacement, frequency of rate cases, magnitude of rate increases, and effect on system reliability. For purposes of this first evaluation and whether to extend the pilot program, the process is working as expected in that we identified a three-year list of projects, focused largely on water main replacement, established a system for prioritizing main replacements, and coordinated main replacement work with the municipality to achieve sharing of costs. The first round of capital projects has been approved and we will follow up with a request for cost recovery for these projects by year end, at which time we will submit our request for pre-approval of 2014 capital projects. The WICA program shows great promise in terms of customer benefits by creating an analytical device that identifies and prioritizes critical infrastructure replacement projects and linking it with a sound cost review and cost recovery mechanism. As a result, the Company requests that the Commission extend the WICA pilot to permit it to develop fully so that program benefits may be realized.

Q. How does the Company plan to notify its customers of the pending rate increase?

A. In accordance with Puc 1203.02(c) and (d), the Company will be notifying its customers regarding the rate filing by providing a form of notice. The notice will be included in mailings to customers as part of its regular cycle billing. Additionally, when the Commission issues the order to suspend tariffs and schedule a prehearing conference, the Company will provide notification in area newspaper(s).

Q. Do you have any other testimony to offer?

A. No.