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Direct Testimony of Stephen P. St. Cyr in DW 19-177

Q. Please state your name and address.

A. Stephen P. St. Cyr of Stephen P. St. Cyr & Associates, 17 Sky Oaks Drive, Biddeford, Me. 04005.

Q. Please state your present employment position and summarize your professional and educational background.

A. I am presently employed by St. Cyr & Associates, which provides accounting, tax, management and regulatory services. The Company devotes a significant portion of the practice to serving utilities. The Company has a number of regulated water utilities among its clientele. I have prepared and presented a number of rate case filings before the New Hampshire Public Utilities Commission. Prior to establishing St. Cyr & Associates, I worked in the utility industry for 16 years, holding various managerial accounting and regulatory positions. I have a Business Administration degree with a concentration in accounting from Northeastern University in Boston, Ma. I obtained my CPA certificate in Maryland.

Q. Is St. Cyr & Associates presently providing services to Lakes Region Water Company ("LRWC" or "Company")?

A. Yes. St. Cyr & Associates has been asked to prepare the various Dockham Shores ("DS") rate case schedules, to prepare written testimony and to prepare other rate case filing requirements. In addition, St. Cyr & Associates prepares the LRWC's PUC Annual Report.

Q. Are you familiar with the pending rate application of DS and with the various exhibits submitted as Schedules 1 through 4 inclusive, with related pages and attachments?

A. Yes, I am. The exhibits were prepared by me, utilizing the financial records of DS.

Q. What is the test year that DS is using in this filing?

A. The Company is utilizing the twelve months ended December 31, 2018.

Q. Before you explain the schedules, please provide a brief overview of some recent developments pertaining to DS.

A. In DW 16-619 the PUC approved LRWC's request to include certain plant in rate base and increase its DS customer's annual revenues by $6,620. The $6,620 assumed estimated total plant additions of $60,000. LRWC later petitioned for a step adjustment of $53,894. That request was based on $300,599 of actual total plant additions. The $300,599 of actual plant additions included state and federally mandated structural improvements to DS' well meter pits and pump station. The plant additions were detailed in an April 2018 engineering design report.

During the review of the improvements and related expenditures, the PUC Staff acknowledged that the Company made great efforts to improve the quality of water service at DS and that the upgrades to plant addressed state and federally mandated structural improvements. The PUC Staff further observed that the new facilities provide improved water quality, all of which have been inspected and approved by the New Hampshire Department of Environmental Services. The PUC's audit staff reviewed the associated costs and confirmed that the total requested plant improvements have been placed in service and are used and useful.

This rate case is largely the result of the difference between estimated total plant additions of $60,000 (which are reflected in rate base and rates) versus actual total plant additions of $300,599 (which are not yet reflected in rate base and rates).

In DW 19-135 LRWC petitioned for approval of long term debt totaling $633,000 from CoBank including $215,000 associated with the 2017 & 2018 improvements at DS. The DS portion of the financing is intended to reimburse the Company for the funds expended.

Q. Is there anything else that you would like to include before addressing the schedules?

A. Yes. DS believes that all assets placed in service during the test year should be fully reflected in rate base and a full year's depreciation on such assets should be fully reflected in depreciation expense and accumulated depreciation. This is particularly true in this case since the DS improvements and related expenditures are so significant, the amount of the plant additions are known and measurable and all the additions were fully in use for the customers' benefit at December 31, 2018.

Q. Is there anything else prior to summarizing the schedules?

A. No.

Q. Then, would you please summarize the schedules?

A. Yes. The schedule entitled "Computation of Revenue Deficiency for Permanent Rates" for the Test Year ended December 31, 2018 summarizes the supporting schedules. The actual revenue deficiency for the DS for the test year amounts to -$16,471. It is based upon an actual test year with a 5 quarter average rate base of $141,098 as summarized in Schedule 3, column g. DS actual rate of return is 1.04% for the actual test year. The rate of return of 1.04%, when multiplied by the rate base of $141,098, results in an operating income requirement of $1,468. As shown on Schedule 1, column b, line 11, the actual net operating income for DS for the test year was -$15,003. The operating income required, less the net operating income, results in an operating income deficiency before taxes of -$16,471. DS did not calculate the tax effect of the revenue deficiency, resulting in a revenue deficiency for DS of -$16,471.

The pro forma revenue deficiency for DS for the test year amounts to zero. It is based upon a pro formed test year rate base of $394,897, as summarized in Schedule 3, column i. DS is utilizing a pro formed rate of return of 5.56% for the pro formed test year. The pro formed rate of return of 5.56% when multiplied by the rate base of $394,897, results in an operating net income requirement of $21,957. As shown on Schedule 1, column d, line 11, the pro formed net operating income for DS for the test year is $21,957. The operating income required, less the net operating income, results in a deficiency of zero. The tax effect of the deficiency is zero, resulting in a revenue deficiency for DS of zero.

Q. Would you please explain Schedule 1 and supporting schedules?

Schedule 1 reflects DS' Operating Income Statement. Column b shows the actual test year results for DS. Column c shows the proforma adjustments for known and measurable changes to test year revenues and expenses. The proforma adjustments are further supported by schedule 1A – 1C. Column d shows the proforma test year results.

During the twelve months ended December 31, 2018, the actual operating revenues amounted to $36,840. At December 31, 2018 DS had 61 customers. DS has no growth in the number of customers during 2018. DS customers consumed 2,509,240 gallons of water.

DS' total operating expenses amounted to $51,843. The 2018 Net Operating Income amounted to -$15,003. Net Income for 2018 was -$16,162.

The Company has made 2 proforma adjustments to operating revenues totaling $51,868. The specific proforma adjustments are identified on Schedule 1A. A brief explanation is as follows:

Proforma Adjustment to Operating Revenues

1. Operating Revenues - Step Adjustment - $6,620.

In DW 16-619 the PUC approved LRWC's request to include certain plant in rate base and increase its DS customer's annual revenues by $6,620.

2. Operating Revenues – Amount Necessary to Earn Return and Cover Operating Costs - $45,248

The Company has increased pro forma test year revenues for the proposed amount of revenues necessary to cover its expenses and allow it to earn its proposed rate of return.

The Total Pro forma Adjustments to Operating Revenue amounts to $51,868.

Proforma Adjustments to O&M Expense

3. Operating and Maintenance Expenses – PUC Audit - $1,000.

In anticipation of a PUC audit on DS 2018 financial statements, DS is estimated that it will incur $3,000 of outside services (accounting and legal) to assist DS in reviewing/responding to audit requests, reviewing draft audit report, reviewing/responding to audit finds and review final audit report. DS proposes to adjust the $3,000 estimate to actual cost upon completion of the audit. DS proposes to recover such PUC audit cost of 3 years.

4. Operating and Maintenance Expenses – Source of Supply – $1,500.

During the test year DS did not incur any source of supply expenses. It is not likely DS will not incur such expenses in 2019 and future years. As such, DS proposes $1,500 for source of supply labor, material and expenses and maintenance of wells.

5. Operating and Maintenance Expenses - treatment - $2,065.

In 2018, DS incurred $1,195 of treatment expenses. In 2019, DS anticipates increased testing, resulting in an increase of $2,065.

6. Operating and Maintenance Expense – T&D Maintenance - $2,000

During the test year, DS incurred $369 of T&D maintenance expenses. It is not likely DS will incur such a minimal amount in 2019 and future years. As such, DS proposes $2,369, an increase of $2,000 for maintenance associated with mains, services, meters, etc.

7. Operating and Maintenance Expense – A&G Expenses – $0.

In 2018, DS incurred $14,935 of administrative and general expenses. DS is monitoring its 2019 level of A&G expenses. DS currently believes that such amount is appropriate. As such, no pro forma is currently required.

The total proposed pro forma adjustment to O&M expenses is $6,565.

8. Depreciation Expense - $6,429.

The Company is proposing to include the additional half year depreciation on the 2018 additions to plant. The amount of the depreciation expense increase is $6,429.

9. Amortization of Organizational Costs - $1,914.

In DW 16-619 LRWC incurred $38,273 of organizational costs in pursuing PUC approval of its purchase of DS. DS considered various amortization periods, i.e., 5, 10, 20, etc. While DS believes that a shorter period may be appropriate, given age of its plant and its ultimate replacement of some of the plant, it decided that 20 years was appropriate. As such, it proposes to recover the organization costs over a 20 year period, resulting in annual amortization of $1,914.

10. Taxes other than Income – State Utility Property Taxes - $0.

While LRWC is expecting an increase in its state utility property taxes, attributed in part to DS improvements, such an increase in not known at this time. If, in the future, DS becomes aware of an increase in state utility property taxes due to an increase in the DS plant, DS will propose an adjustment.

11. Taxes other than Income – Town of Gilford Property Taxes - $0.

Similarly to state utility property taxes, LRWC is expecting an increase in its Town of Gilford property taxes, attributed in part to DS improvements, such an increase in not know at this time. If, in the future, DS becomes aware of an increase in state utility property taxes due to an increase in the DS plant, DS will proposes an adjustment.

12. Federal Income Taxes - $0.

In 2018, LRWC allocated federal income taxes to DS. It allocated 3% based on number of customers. A more appropriate basis may be based on taxable income. LRWC/DS is reviewing its allocation method. As such, there is no adjustment at this time.

13. State Business Taxes - $0.

In 2018, LRWC allocated state business taxes to DS. It allocated 3% based on number of customers. A more appropriate basis may be based on gross business income. LRWC/DS is reviewing its allocation method. As such, there is no adjustment at this time.

The total pro forma adjustments to Operating Expenses amount to $14,908.

The net of the pro forma adjustments to operating revenue $51,868 and the pro forma adjustments to operating expenses $14,908 results in net pro forma adjustment of $36,960. When the net operating income associated with the pro forma adjustments is added to net operating income from the test year, the pro forma test year net operating income totals $21,957. The pro forma test year net operating income of $21,957 allows the Company to cover its expenses and earn a 5.56% return on its investments.

Q. Does that complete your description of the pro forma adjustments to revenues and expenses?

A. Yes.

Q. Are there additional schedules that support Schedule 1?

A. Yes, Schedule 1B & 1C. Schedule 1B shows the income tax computation. Because the equity component of DS' cost of capital in negative, DS is utilizing 0.00%, resulting in no federal income or state business taxes. Schedule 1C shows the effective tax factor.

Q. Please describe Schedule 2, the DS Balance Sheets.

A. DS has $381,438 total assets at the end of 2018. $351,594 of the $381,438 total assets is net utility plant, all of which is completed and providing service to customers. In 2018 DS added $... of plant in service, offset by $... of plant retired. Most significantly, it added $... for the new pump station building, new generator, new pumps and a new tank. DS also has $38,393 of organizational costs related to pursuing and receiving PUC approval of the purchase of the water system.

DS has total equity capital and liabilities of $381,438 at the end of the year. Total equity capital amounts to -$5,297. The negative equity is the result of net losses and negative retained earnings. DS has long term debt owed to CoBank amounting to $128,986. DS also has $243,676 of miscellaneous current and accrued liabilities owed to LRWC.

Q. Please continue with an explanation of Schedule 3, Rate Base and the supporting schedule.

A. Schedule 3 reflects the Company's Rate Base for both the actual 5 quarter average test year and the 2018 pro forma test year. Columns b – f shows the actual quarter end balances. Column g shows the 5 quarter average balances. Column h shows the pro forma adjustments. Column i shows the 2018 pro forma balances. The balances are further supported by Schedules 3A, 3B and 3C.

The rate base consists of Utility Plant in Service less Accumulated Depreciation, plus Material and Supplies, less Contributions in Aid of Construction plus Accumulated Amortization of CIAC and Cash Working Capital.

The total 5 quarter average rate base amounts to $141,098. The total pro formed year end rate base balances amounts to $394,897.

Q. Would you please explain Schedule 3A, Rate Base – Pro forma Adjustments?

A. Schedule 3A shows the various adjustments to rate base. As stated earlier in my testimony, DS believes that all assets placed in service during the test year should be fully reflected in rate base and a full year's depreciation on such assets should be fully reflected in depreciation expense and accumulated depreciation. Likewise, DS believes that other rate base items should be fully reflected in rates. As such, DS has adjusted the actual 5 quarter average balances to year end balances. The rate base items affected by the reflection of year end balances are (1) plant in service, (3) accumulated depreciation, (6) material and supplies and (7) accumulated amortization of CIAC. Please note that LRWC has not yet separated accumulated deferred income taxes related to the DS book and tax depreciation differences.

In addition to the pro forma adjustments to rate base for the year end balances, the Company made other pro forma adjustments as follows:

2. Plant in Service – 2018 Organization Costs - $38,273.

This rate base pro forma is related to the pro forma adjustment number 9 on the income statement. In DW 16-619 LRWC incurred $38,273 of organizational costs in pursuing PUC approval of its purchase of DS. DS proposes to transfer $38,273 from miscellaneous deferred debits to plant in service, account 301, Organization.

4. Accumulated Depreciation - $6,429.

The Company is proposing to include the additional half year depreciation on the 2018 additions to plant. The amount of the depreciation expense increase is $6,429, resulting in the same increase in accumulated depreciation.

5. Accumulated Amortization of Organization Costs - $957.

DS considered various amortization periods, i.e., 5, 10, 20, etc. While DS believe that a shorter period may be appropriate, given age of its plant and its ultimate replacement of some of the plant, it decided that 20 years was appropriate. As such, it proposes to recover the organization costs over a 20 year period, resulting in annual amortization of $1,914 and a ½ year accumulated amortization of $957.

9. Cash Working Capital - $1,349

The Company adjusted cash working capital for the pro forma increase in operating and maintenance expenses.

The total pro forma adjustments to Rate Base amount to $253,799.

Q. Please explain Schedule 3B.

A. Schedule 3B shows the acquisition costs of $38,273 at the 5% rate, resulting in an annual amortization of $1,914 and ½ year accumulated amortization of $957.

Q. Please explain Schedule 3C.

A. Schedule 3C shows the computation of cash working capital for 2018 pro forma amount and 2018 actual amount. The pro forma cash working capital is based on the pro forma test year operation and maintenance expenses.

Q. Would you please explain Schedule 4, DS Rate of Return Information?

A. Schedule 4 reflects the overall rate of return for both the actual test year and the pro forma test year. The weighted average rate of return for the actual test year is 1.04%. It was developed by taking the actual component ratios times the actual component cost rates to determine the actual weighted average cost rate. The sum of the actual cost rates for equity and debt equals actual weighted average rate of return.

The weighted average rate of return for the pro forma test year is 5.48%. It was developed by taking the pro forma component ratios times the pro forma component cost rates to determine the pro forma weighted average cost rate. The sum of the pro forma cost rates for equity and debt equals the pro forma weighted average rate of return.

Schedule 4 also reflects both the capital structure and the capital ratios. DS has provided the capital structure for the actual test year and the pro forma test year. DS is utilizing the Commission determined cost of common equity of 9.56% plus

.50%, totaling 10.06%.

In addition, Schedule 4 also reflects the long term debt, interest expense, financing costs, total debt costs and debt costs rates for the actual test year. At 12/31/18 DS has $128,986 of outstanding long term debt with related interest of $1,836 and a cost of debt of 1.42%. It should be noted that 2018 only reflects a partial year of interest expenses.

Finally, Schedule 4 reflects the long term debt, interest expense, financing costs, total debt costs and debt costs rates for the pro forma test year. The pro forma outstanding balance is $343,986 of outstanding long term debt. The increase in the outstanding balance is due to the proposed financing of $215,000 with CoBank. The pro forma interest expense related to the debt is $19,126. The increase in the interest expense is due to additional interest on the existing CoBank loan and new interest on the proposed CoBank financing. The 2018 pro forma cost of debt is 5.56%.

Q. Please explain the Report of Proposed Rate Changes.

A. If DS filing is approved as submitted, its total water Operating Revenues will amount to $88,288. The Total Residential Sales of Water amount to $88,708 comes from DS 61 metered customers.

Q. Is the Company proposing any changes to the methodology used in calculating the rates?

A. No.

Q. When is the Company proposing that the new rates be effective?

The Company requests that the proposed rate increase be effective as of the date of publication of the Commision's Order of Notice of its request for permanent and temporary rate increases.

The Company plans to make a separate, temporary rate filing in a week or two proposing temporary rates. The Company therefore proposes that permanent and temporary rates be effective the date of publication of the Commission's Order of Notice, subject to reconciliation as provided by RSA 378:29.

The temporary rate filing will be essentially the same as the permanent rate filing except for the elimination of certain pro forma adjustments. The temporary rate filing will contain what is necessary for the PUC Staff to conduct a limited review and hopefully join with DS in presenting a settlement agreement on temporary rates to the PUC for approval.

Q. How will rates set in this proceeding impact the Company's remaining customers?

The proposed permanent rates are higher than current rates for existing customers due to the significant capital investments in the DS system in 2018. However, the Commission should be aware that the Company plans to file a general permanent rate increase for all of its customers in 2020 based on a 2019 test year. The Company plans to request that rates for DS and Wildwood customers be consolidated with those of existing customers.

The Company recommends that the Commission and Staff consider options for rate consolidation in this proceeding. Consolidated rates benefit all customers by reducing ‘rate shock’ that can occur when significant capital improvements are required in a particular system. Over time, this benefits all customers as each system is upgraded over time.

Q. Is there anything that you would like to discuss?

A. Yes. The Company prepared and issued a request for proposal for legal and accounting / rate services for the rate case. Mr. Richardson of Upton & Hatfield was engaged to provide legal services. Mr. St. Cyr of Stephen P. St. Cyr & Associates was engaged to provide accounting / rate services. As such, Mr. Richardson and Mr. St. Cyr will be providing legal, accounting and rate services for DS during the course of the proceeding.

Q. Would you please summarize what the Company is requesting in its rate filing?

The Company respectfully requests that the Commissioners approve an increase in annual revenues of $45,248 for permanent rates.

Q. Does this conclude your testimony?

A. Yes.

SPSt. Cyr
12/17/19