

STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

Docket No. DG 23-067

Liberty Utilities (EnergyNorth Natural Gas) Corp. d/b/a Liberty
Distribution Service Rate Case
Functional Cost of Service

DIRECT TESTIMONY

OF

C. DREW CAYTON

Black and Veatch Management Consulting, LLC

July 27, 2023



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LIST OF ATTACHMENTS

Attachment CDC-1	Summary of the Functional Cost Study
Attachment CDC-2	Functional Cost Study – Account Level Detail

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1 **I. INTRODUCTION AND BACKGROUND**

2 **Q. Please state your full name and business address.**

3 A. My name is C. Drew Cayton. My business address is 11401 Lamar Ave., Overland Park,
4 Kansas, 66221.

5 **Q. By whom are you employed, and in what position?**

6 A. I am employed by Black and Veatch Management Consulting, LLC as a Principal
7 Consultant.

8 **Q. What are your responsibilities in your current position?**

9 A. As a member of Black and Veatch Management Consulting, LLC's Global Advisory
10 practice, my responsibilities include providing advisory services that address strategic,
11 financial, reputational, and regulatory needs of energy and utility clients. My primary
12 areas of focus are regulatory advisory, accounting, civil litigation, and financial analysis.

13 **Q. Are you the same C. Drew Cayton who is submitting other direct testimony in this
14 case?**

15 A. Yes. I am also submitting testimony in support of Liberty Utilities (EnergyNorth Natural
16 Gas) Corp.'s ("Liberty EnergyNorth" or "the Company") Temporary Rates and Revenue
17 Requirement underlying the Company's permanent rate increase in this rate filing. The
18 Temporary Rate testimony sets forth my educational background and professional
19 qualifications.

20 **Q. On whose behalf are you submitting testimony in this proceeding?**

21 A. I am testifying on behalf of Liberty EnergyNorth.

1 **II. SCOPE OF TESTIMONY**

2 **Q. What is the purpose of your testimony in this proceeding?**

3 A. The purpose of my testimony is to discuss the functional cost of service study performed
4 by Black and Veatch and used to support the rates proposed by Liberty EnergyNorth in
5 this proceeding.

6 **Q. Are you sponsoring any exhibits to support your testimony?**

7 A. Yes, two attachments are provided with my testimony. Attachment CDC-1 is a summary
8 of the functional cost of service study. Attachment CDC-2 provides the detailed study at
9 the individual account level.

10 **III. FUNCTIONAL COST OF SERVICE STUDY**

11 **Q. What is a functional cost of service study and why was such a study performed for
12 this case?**

13 A. A cost of service study provides a measure of the cost responsibility based on cost
14 causation principles of a company's respective functions and various rate classes. A
15 functional cost study is necessary to arrive at the cost responsibility for each of the
16 functions because many of a company's costs are common, or indirect, and incurred to
17 provide service to all customers. In general, costs are first identified based on the
18 function for which they are incurred, then those costs are classified, typically as demand,
19 customer, and commodity, and finally directly assigned or allocated to the various
20 functions.

1 The functional cost of service study separates Liberty EnergyNorth’s revenue
2 requirement into four functions: delivery, direct gas cost, Liquefied Petroleum Gas
3 (“LPG”), and Liquefied Natural Gas (“LNG”) costs, and miscellaneous indirect costs.
4 The direct costs of purchasing gas, including LPG and LNG costs, as well as related
5 indirect costs, collectively referred to as production costs, are recovered through the Cost
6 of Gas (“COG”) mechanism rather than through base distribution rates. The costs of
7 delivering gas are recovered through base distribution rates. Therefore, the purpose of a
8 functional cost study is to ensure that there is neither duplication of cost recovery through
9 both distribution rates and the COG mechanism nor stranded costs that are not recovered
10 by either.

11 **Q. What is the relationship between this functional cost study and the marginal cost**
12 **study that is being filed with this case?**

13 A. The marginal cost study provides the basis for determining the level of distribution
14 revenues to be recovered from the various rate classes as well as the components that are
15 used to design rates. In contrast, this functional cost study divides the Company’s total
16 revenue requirement into the costs to be recovered through base rates and those that are
17 recovered through the COG mechanism.

18 **Q. What is included in each of the categories of costs?**

19 A. Purchased gas costs include supplier, storage and pipeline demand and commodity costs,
20 as well as commodity costs for LPG and LNG, all of which are considered direct costs.
21 Indirect gas costs include the LPG and LNG facility costs and expenses required to

1 provide the supply service. The costs associated with supplying the gas commodity to
2 customers that are not included in direct gas costs are indirect costs. Indirect costs
3 consist of the bad debt expense related to the supply function, working capital related to
4 the supply function, and other operations and maintenance expenses including gas
5 acquisition, dispatching, and administrative and general expenses related to the supply
6 function but not included in direct gas costs.

7 **Q. How are costs allocated in the functional cost of service study?**

8 A. Costs are directly assigned to the greatest extent possible or allocated based on certain
9 factors. Allocation factors can be developed using external factors or internal factors.
10 External factors, such as the number of customers or sales and transportation revenues,
11 are based on data from a separate independent analysis. An internal factor is calculated
12 within the functional cost study based on the combination of previously allocated costs.

13 **Q. How are facilities costs treated in the functional study?**

14 A. The Company's LPG and LNG facilities provide a dual service, gas supply and pressure
15 support for the distribution system. Company witness Kenneth A. Sosnick examined this
16 dual functionality and determined that 8.49% of the Tilton LNG facility is required for
17 the pressure support and the remaining 91.51% of the LPG and LNG is utilized for gas
18 supply for the system. These percentages are used to allocate the LPG and LNG facilities
19 costs between pressure support and supply service. All distribution facility costs, which
20 are identified on page 1 of Attachment CDC-1, are directly assigned to delivery service.

1 Intangible and general facility costs, which are set forth on page 1of Attachment CDC-1,
2 are allocated to the functions based on labor, an indirect allocation factor.

3 **Q. How are other rate base items treated in the functional study?**

4 A. Materials and supplies and accumulated deferred income taxes are allocated to the
5 functions based on plant. Cash working capital is allocated on Operation and
6 Maintenance (“O&M”) expenses, excluding gas costs and bad debt.

7 **Q. How are O&M expenses treated in the functional study?**

8 A. Production expenses related to gas acquisition are directly assigned to the supply function
9 and the remaining expenses are allocated between supply and delivery services. All
10 distribution, customer account, customer service, and sales expenses are directly assigned
11 to delivery service. Uncollectible expense is allocated between delivery and production
12 on a revenue basis.

13 **Q. How are Administrative and General expenses treated in the functional study?**

14 A. Administrative and General (“A&G”) expenses are allocated on labor except for
15 transferred costs and regulatory commission expense. Regulatory commission expenses
16 are allocated between delivery and production on a revenue basis, and the transferred
17 costs are allocated based on the other total functionalized A&G costs.

18 **Q. How are depreciation and taxes other than income expenses treated in the**
19 **functional study?**

20 A. Depreciation expenses are directly assigned to the functions based on the specific plant
21 accounts for each function. General and intangible depreciation expense follows

1 intangible and general plant allocation. Taxes other than income are allocated based on
2 specific plant or specific labor factors.

3 **IV. RESULTS AND CONCLUSION**

4 **Q. Please describe the results of the functional study.**

5 A. Attachment CDC-1, page 1, presents a summary of the results of the functional study, at
6 current rates, and shows the earned return for each function. Pages 2 and 3 present a
7 more detailed summary of the production costs, separating the costs into LPG and LNG
8 costs, miscellaneous production costs, and bad debt costs at current and proposed rates of
9 return. The net result of the analysis is that a revenue requirement of \$6,744,159¹
10 associated with the supply function should be recovered through the COG mechanism.
11 Of the total revenue requirement that should be recovered through the COG mechanism,
12 \$464,372² is being assigned to Keene customers with the balance, \$6,279,787,³ being
13 assigned to Liberty EnergyNorth customers excluding Keene. Attachment CDC-2
14 provides a detailed view of the allocation of the revenue requirement by each account and
15 the external and internal allocation factors used in the study.

16 **Q. Does this complete your testimony?**

17 A. Yes, it does.

¹ Of the total indirect cost of gas revenue requirement, \$6,777,802, \$33,643 is assumed to be collected through miscellaneous revenues, with the balance, \$6,744,159, being collected through the cost of gas mechanism.

² Attachment CDC-1, page 3, Line 56.

³ Attachment CDC-1, page 3, Line 57.