Liberty Utilities

STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

Docket No. DE 16-383

Liberty Utilities (Granite State Electric) Corp. d/b/a Liberty Utilities
Distribution Service Rate Case

REBUTTAL TESTIMONY

OF

CHRISTIAN P. BROUILLARD

TISHA A. SANDERSON

AND

GERALD P. TREMBLAY

February 3, 2017

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List of Attachments

Attachment CPB/TAS/GPT-1	Dudley Response to GSEC 1-52

I. INTRODUCTION AND QUALIFICATIONS

Q. Please state your names and business addresses.

A. My name is Christian P. Brouillard. My business address is 15 Buttrick Road, Londonderry, NH 03053.

A. My name is Tisha A. Sanderson. My business address is 15 Buttrick Road, Londonderry, NH 03053.

A. My name is Gerald P. Tremblay. My business address is 354 David Road, Suite 100, Oakville, ON L6J 2X1.

Q. By whom are you employed and in what capacity?

A. (CPB) I am employed as the Director of Engineering by Liberty Utilities Service Corp. In my capacity as Director of Engineering, I am responsible for delivery system planning and capital investments, engineering and design, and maps and records integrity for Liberty Utilities (Granite State Electric) Corp. ("Granite State" or the "Company").

A. (TAS) I am employed as the Director of Finance by Liberty Utilities Service Corp. In my capacity as the Director of Finance, I am responsible for budgeting, financial reporting, and accounting for the Company.

A. (GPT) I am employed as the Senior Vice President of Operations by Liberty Utilities Canada Corp. In my capacity as Senior Vice President of Operations, I am responsible for overall operational achievement of the approved business plans of Liberty Utilities, including at the local level. I have overall accountability for field operations including engineering.

Q. Have you previously submitted testimony in this proceeding?

A. (CPB) Yes. I submitted prefiled testimony as part of the Company's April 29, 2016, filing for an increase in distribution rates. My professional background and qualifications are contained in the prior testimony.

A. (TAS) No.

A. (GPT) No.

Q. Ms. Sanderson, please describe your educational background and certifications.

A. I have a Bachelor of Science in Business with a concentration in Accounting. I am presently pursing my Certified Public Accounting License with an expected completion date of August 2017.

Q. Ms. Sanderson, please describe your professional experience.

A. I have over 20 years of experience of increasingly senior positions within the construction, engineering, and utilities industries.

Q. Ms. Sanderson, have you previously testified before the Commission?

A. No.

Q. Mr. Tremblay, please describe your educational background and certifications.

A. I earned a bachelor's degree in Social Science with an honors degree in economics from the University of Ottawa in 1991. In 1999, I obtained a Certified General Accountant designation, a Canadian designation which is essentially equivalent to a Certified Public Accountant designation in the United States.

Q. Mr. Tremblay, please describe your professional experience.

A. I have over 24 years of experience in increasingly senior positions within the retail, energy, and utilities industries.

Q. Mr. Tremblay, have you previously testified before the Commission?

A. Yes. I submitted testimony in Docket No. DG 11-040, the docket in which the Commission approved the transfer of ownership of Granite State from National Grid to Liberty Energy Utilities Corp.

II. PURPOSE OF TESTIMONY

Q. What is the purpose or your testimony?

A. The purpose of our testimony is to provide comments on the testimony of Staff Witness Jay Dudley and on the testimony of the Liberty Consulting Group (LCG) with respect to capital budgeting and capital expenditures. First, we describe the process for approval of budgets as well as the approval of capital expenditures in excess of budgeted amounts. Second, we dispute Mr. Dudley's and LCG's conclusions that capital spending was not monitored or controlled. Finally, we demonstrate the prudence of the Company's capital investments since 2013 and the substantial benefits provided by the timing of those investments.

Q. Please provide a summary of your concerns about Mr. Dudley's and LCG's testimony.

A. In their testimonies, Mr. Dudley and LCG characterized Granite State's capital budget and capital expenditure processes in a misleading fashion. They dwelled on what they perceived to be issues with the processes that occurred in 2014 and 2015, making it appear that Granite State haphazardly incurred budget variances due to a lack of effective control of capital expenditures. However, both Mr. Dudley and LCG neglected to mention and completely ignored Liberty Utilities' response to LCG's audit report (Attachment SMHF/SEM-6 to the rebuttal testimony of Ms. Houghton-Fenton and Mr. Mullen), in which Liberty Utilities stated:

> [T]he variances that occurred in 2014 and 2015 were not the result of a lack of control over the spending process. To the contrary, the actual spending was the result of local decision-making and flexibility as circumstances changed. If there had been a strict limit on either total spending or on individual project spending, LU may have been in a position where it could not provide service to new customers as a result of budget constraints.
>
> LU does not agree that capital budgets were not monitored, nor do we agree with the characterization that there were "problems" with budget timing and performance. There was full visibility and business case documentation for the 2014/2015 projects. The capital budget was vetted and discussed with local management and head office management. The business cases included project analysis....

SMHF/SEM-6 at 8. They also failed to point out or follow up on the enhancements that Liberty Utilities has made to its capital budgeting process, which were also described in the response to LCG's audit report, and in the Company's response to Audit Issue 4 in the Audit Staff's report (page 84 of Attachment JED 2-1 to Mr. Dudley's testimony (Bates 000124)):

> LU acknowledges the need for continuous improvement in the capital budgeting process, and embraces continuous improvement as one of LU's core values. In an effort to improve its budgeting process, LU has implemented the following policies:
>
> - Reinforced monthly budget meetings
> - Increased the level of detail that is reviewed
> - A dedicated individual has been hired to manage and review the capital budget and spending
> - Month end accruals are now recorded at a job level to provide better visibility to job spending
> - Project governance documents are submitted in a timely fashion

Id. at 8. In this testimony, we will demonstrate that the capital budgeting and planning processes are detailed, thorough, and involve the appropriate review both at the local and corporate levels.

III. LOCAL CAPITAL BUDGETING PROCESS

Q. Mr. Dudley stated in his testimony that the Company's capital planning and budgeting process appears to be an *ad hoc*, hit-or-miss process. Do you agree with this characterization?

A. No, we do not. Mr. Dudley's comments reveal an apparent lack of familiarity with the Company's capital budgeting and management process.

Q. Please summarize the Company's process for preparing the annual capital budget.

A. Beginning in the second quarter, preliminary meetings are held with representation from Engineering, Operations, and Finance to discuss the appropriate prioritization and necessity of capital projects to be undertaken by Granite State in the following year. Prior to this meeting the Engineering and Operations Departments engage in substantial efforts to develop a long-term forecast, resource needs, and in certain circumstances detailed studies. This background information is incorporated into a second quarter meeting to evaluate proposed project funding levels for the coming year as they are dependent on growth trajectories, maturation of assets, reliability/risk management, statutory requirements, and extraordinary occurrences.

The Company uses five categories to assess and prioritize the proposed capital expenditure requests. The categories are as follows, in descending priority: safety, mandated, growth, regulatory supported, and discretionary. Expenditures categorized as "safety" are those used to reduce workplace hazards, prevent accidents, and reduce exposure to harmful situations and substances. Expenditures categorized as "mandated" are those used to meet statutory or regulatory compliance. Expenditures classified as "growth" are those used to expand physical plant in support of new customer connections and incremental additions to existing demand. Growth examples include the installation of new services or primary line extensions, or reinforcements to serve new load. Expenditures classified as "regulatory supported" include projects where special regulatory mechanisms have been established to allow the Company to more promptly recover the cost of targeted initiatives. An example of a regulatory supported investment is investment under the Reliability Enhancement Program. All other capital expenditures are grouped under the discretionary category and the merits of each project are assessed individually. Note that although the category is labeled as discretionary, many of the projects undertaken in this category mitigate or eliminate substantial operating risks.

The process to define the Company's capital budget is iterative, involving several meetings and information exchanges leading to a local operating company budget submission to Liberty Utilities' home office in Oakville, Ontario (the "Home Office") in late September. In order to provide further, detailed insight into the drivers of each project, a preliminary business case is prepared in conjunction with the annual budget submission. Local budgets are aggregated into regional and line of business budgets, culminating in a Board approved budget in December.

Q. Please summarize the Company's policies and procedures for managing capital expenditures.

A. Following Board approval of the annual capital budget in December, business cases are finalized and sent to local and regional leadership for approval, and as appropriate to the corporate parent for subsequent acceptance. In the event that an unplanned project emerges during the year—referred to as an "emergent" project—the Company will evaluate applicable aspects of the project including operational business risk, internal rate of return, cost/scope/schedule, and business objectives documented in a business case. If the unplanned project cannot be accommodated within the overall regional budget, then the business case must be approved by the appropriate authority.

The Company manages variances to budget and schedule through a monthly reporting process, detailed below. If any variance cannot be absorbed in the approved budget envelope, an Over Expenditure Application form must be completed and submitted for consideration.

Q. Please describe in detail the Company's monthly reporting process.

A. Following the financial closing each month a report detailing each project's cost to date is provided to the project managers. The Project Manager is responsible for providing an updated capital commitment to date, projected spending during the next quarter, estimated spending at completion, and anticipated variances in spending, scope, and schedule. Once these updates are received, a monthly meeting is conducted to discuss and review project statuses and variances in detail. Participants for this meeting include the New Hampshire State President, Vice President of Operations, Directors (Gas Operations, Electric Operations, Engineering, and Finance), and Project Managers. The information collected in this meeting is summarized and presented to a senior audience including; LU President, Sr. Vice President of Operations, Vice President of Finance, and Regional Presidents during a monthly operating call.

Q. Please describe the Project Close-out Reporting Process.

A. All capital projects require a formal close-out to be conducted. The Project Managers prepare and provide the close-out report to the Project Sponsor for review and approval. The project close out report documents cost and schedule variances, lessons learned, post implementation support plans, and the formal agreement of project closure.

Q. Is the overall budgeting process described above locally or centrally driven?

A. Actually, it is both. The Home Office has developed central policies and procedures that are followed by the various Liberty Utilities companies nationwide. We have described the local role above, and in the next section we describe the Home Office's role in the budgeting process.

IV. HOME OFFICE OVERSIGHT OF CAPITAL SPENDING IN 2014 - 2015

Q. Please give a broad overview of how the budgeting process worked for budget years 2014 and 2015 between the Home Office and the various regulated utilities, such as Granite State.

A. The budgeting process for Liberty Utilities' regulated business units follow similar timelines, as was the case in 2014 and 2015. As described above, all the utilities prepare their operating budget along with their capital plan by September. Several iterations occur within the local business unit during that timeframe. The budget is then reviewed by the Home Office and further discussions between the Home Office and the utility occur within the months of October and November. A budget presentation is then prepared for the Board of Directors to be approved in December.

Q. Please provide a more detailed description from the Home Office's perspective of the budgeting process that applied to Granite State for budget years 2014 and 2015.

A. Granite State prepared its budget within the timeframe outlined above. Both the operating budget and the capital plan were built locally using the prior year's five-year plan as a starting point. However, all operating revenues and costs along with the capital plan were justified from the ground up at a very detailed level by regional personnel. The capital budgets were prepared by line item and were grouped into three broad categories: replenishment, improvement, growth, and then further broken out into five other categories: safety, growth, mandated, regulatory supported, and discretionary. A review of Granite State's budget was then performed in the Home Office by comparing its operating and capital activities to the current forecast and prior actuals along with the long term model results. Several discussions happened within this timeframe between regional personnel and the Home Office staff. A summary of the analysis was prepared and provided to the Board of Directors within the New Hampshire section of the budget document.

Q. What was the Home Office's specific role in Granite State's budgeting process for 2014 and 2015?

A. The Home Office's role in 2014 and 2015 was the same as it is today: to review Granite State's operating and capital budgets to ensure that they met operational and customer needs and were in line with the financial goals set out in the long term forecast.

Q. How did the Home Office and/or Granite State determine the overall amount that Granite State could spend on capital?

A. As is the case today, all of the utilities, including Granite State, developed their capital plan locally each year. That is, the local engineering team along with operations personnel identified, by line item, the capital work for the coming year. For electric utilities, the target metrics for SAIDI and SAIFI served as drivers in developing the local capital plan along with managing forward operating risks. The Home Office then reviewed the capital budgets for all of its utilities to ensure they met operational and customer needs and were in line with the financial goals set out in the long term model. The Home Office also reviewed credit metrics to ensure that Algonquin Power & Utilities Corp.'s ("APUC") credit worthiness was in line. Once completed, the capital requirements envelope was approved for all of the utilities.

Q. Would underspending by one local utility allow another local utility to increase its spending? Please explain.

A. Yes, potentially. Underspending by one local utility can allow another local utility to increase its spending. Once the Home Office has its consolidated capital plan approved, this dollar amount then becomes a total envelope for all of its utilities. The Home Office tries to remain on plan by utility, but on occasion, due to delays in permitting and scheduling, capital expenditures can be delayed and thus some utilities may forecast underspending in certain years against their original capital plan. This 'frees up' capital dollars for other utilities that may require additional capital projects not originally planned for in their current year but scheduled in later years. The amount of capital dollars that other utilities may use should not exceed the original consolidated capital plan amount. Also, under the Home Office's capital expenditure planning and management policy document, the reallocation of capital occurs based on evolving requirements, and priority changes may be executed.

Q. Is it possible for projects planned for future years to be accelerated into the current budget year? Please explain.

A. Yes. As discussed in the previous response, if certain utilities are forecasting to underspend in the current year due to unforeseen events, this allows other utilities the opportunity to increase their capital spending. Some of this capital spending could come from additional unbudgeted expenditures due to a specific event, or from accelerating some capital expenditures from future years into the current year, always taking into account the total consolidated approved capital budget and the impact on rate level.

Q. Please describe what was reviewed for 2014 and 2015 budget years and please describe how that review was performed.

A. As previously described, the local businesses perform a bottom-up zero based budget for operating revenues, costs, and capital requirements, relying on historical requirements and justifications where appropriate. Upon completion, a review of the budget is then performed in the Home Office by comparing operating and capital activities to the current forecast and prior actuals along with the long term model results. Several discussions happen within this timeframe between local personnel and the Home Office staff. The results are then further reviewed by the executive team consisting of the President of Liberty Utilities, the Chief Financial Officer, and the Chief Executive Officer of APUC. A summary of the analysis is then prepared and provided to the Board of Directors. Furthermore, the Home Office conducts monthly operations meetings to review operational performance with the business units. The local businesses present their year-to-date activities, both operational and capital spending, to plan and provide a forecast for the rest of the year. Variances are discussed. It is at these meetings that the Home Office identifies capital underspending in certain utilities and allows for other utilities to accelerate or identify other unbudgeted prudent capital expenditures that may be required for the current year. These meetings consist of, but are not limited to, the following individuals: the President of Liberty Utilities, Senior Vice President of Operations, Vice President of Finance, and all the Regional Presidents.

Q. Staff alleges in its testimony that there was no control over, or oversight of, Granite State's budgeting process for 2014 and 2015. Do you agree?

A. No. As described above, one can clearly see that the Home Office does provide oversight of Granite State's budgeting process, and did so in 2014 and 2015. Not only is the Home Office involved with the annual budgeting along with the five-year forecast for all of its facilities, it also takes an active role in monthly reporting with all of the businesses, reviewing actual vs. budget variances and forecasting variances to the end of the year. This monthly meeting aids in ensuring that the Home Office achieves its overall operational and financial targets.

Q. Please describe the enhancements to the budgeting and review process that have been implemented since the 2015 budget year.

A. The Company has identified areas to enhance the availability of project level information under the Home Office's capital expenditure policy. In 2017, Granite State will continue to prepare preliminary business cases in parallel with the budgeting preparation process, as well as improving the timeliness of project closure and variance reports. In 2017, the Home Office also initiated a regional Board of Directors to further emphasize additional governance at the regional level. A focus on these regional boards will be capital expenditures and planning.

Q. Please generally describe the various ways that a "budget variance" may arise.

A. Project budgets are prepared in September of the preceding the budget year using the best information available, including per unit costs, historical costs and trends, and remaining construction. Given the timing and nature of the estimates, it is reasonable to expect some variance between actual expenditures vs. budgeted amounts. These variances are typically driven by changes to a project's scope, acceleration or deceleration of project schedule into or out of the budget year, changes driven by additional permitting/licensing requirements, and schedule/scope changes driven by the customer or municipal schedules and requirements.

Q. Please describe how the Home Office reviews and manages budget variances.

A. While the local personnel review their capital budget variances at a specific job-by-job level, the Home Office reviews the utilities' budget variances at a higher level. The Home Office conducts monthly operations meetings which include presentations on capital expenditures. The utilities present their year–to-date capital spending to plan, and provide a forecast for the remainder of the year. Variances are discussed. It is at these meetings that underspending in certain utilities is identified, which allows the opportunity for other utilities to accelerate or identify other unbudgeted prudent capital expenditures that may be required for the current year. These meetings consist of, but are not limited to, the following individuals: the President of Liberty Utilities, Senior Vice President of Operations, Vice President of Finance, and all of the Regional Presidents.

Q. Were there any projects discussed in Mr. Brouillard's pre-filed direct testimony in this docket about which the Home Office was not aware?

A. Yes, but only for emergent projects which were added to the budget under local management approval, and which did not exceed local management's authorized spending level. As discussed previously, the Home Office performs its capital review at the company and business line level, with visibility made available as necessary to key projects within the plan. Therefore, within the capital spending policy, the Home Office had a correct and appropriate level of knowledge of the projects comprising the capital plans for the period in review.

V. PRUDENCE OF CAPITAL SPENDING

Q. Please generally describe Mr. Dudley's conclusion regarding the prudence of the Company's capital expenditures since 2013.

A. Mr. Dudley erroneously concluded that approximately $5.8 million in capital expenditures were imprudently incurred and should be disallowed. This conclusion is based on Mr. Dudley's incorrect interpretation of the Company's responses to discovery questions, and on misleading evidence centered on the three atypical projects he selected for analysis.

Q. What comprises Mr. Dudley's recommended $5.8 million in disallowance to rate base?

A. Mr. Dudley based his recommended $5.8 million disallowance on the alleged imprudence arising solely from the actual-to-budgeted variances in each of 2014 and 2015 separately, not on any analysis of the money actually spent over the life of particular projects or the necessity for those projects. In 2014 the Company budgeted $18.4 million and spent $30.7 million on capital projects, with the full knowledge and approval of upper management. In 2015 the Company budgeted $10.0 million and spent $11.5 million, again with full management support. The total actual-to-budget variance for both calendar years is $13.8 million.

Q. Did Mr. Dudley make allowances for previously approved or agreed to adjustments to rate base?

A. Yes, Mr. Dudley correctly excluded $3.5 million in approved Reliability Enhancement Program ("REP") expenditures that the Commission previously approved in the annual REP dockets, and he excluded $4.5 million in Information Technology investments that were already taken into account in Granite State's filing in this docket. These exclusions reduced the $13.8 million total variance to a net variance over calendar years 2014 and 2015 of $5.8 million. This net budget variance is what Mr. Dudley recommended that the Commission disallow.

Q. More specifically, what does the $5.8 million figure represent?

A. The $5.8 million net budget variance consists of a $5.2 million variance in 2014 and a $0.6 million variance in 2015 and arises out of approximately 135 projects in 2014 and 90 projects in 2015.

Q. How do the projects break down in terms of underruns and overruns?

A. Understand that we do not agree with Staff's characterization of these calendar year budget variances as being budget "overruns" or "underruns" because a true budget overrun requires a more comprehensive analysis. That being said, of the 135 projects in 2014, 104 were either underruns under Mr. Dudley's definition, or were within the project variance guideline of +/- 10 percent or $50,000, whichever is greater. In 2015, 61 of the 90 projects were either underruns or within the variance. Thus, the category of overrun projects totaled 31 in 2014 and 29 in 2015, or roughly a quarter of capital projects had budget overruns in excess of either 10% or $50,000.

Q. Can you provide further details on the actual expenditures on these projects?

A. Yes. In 2014, 15 of the 31 overruns represented Growth, Mandatory, or REP category projects, and 16 were for discretionary category projects. In 2015, of the 29 total overruns, 16 represented Growth, Mandatory, or REP projects and 13 were for discretionary category projects. Excluding the REP projects, the Company has little control over the scope, cost, and timing of the Growth and Mandatory projects. Further, more than half of 2014 variances and almost all of the 2015 variances were on "blanket" projects. Blanket projects are comprised of hundreds of work orders covering investments in the categories of New Business, Public Requirements/Relocations and Street Lighting, Response to Damage/Failure, and on-going equipment asset replacement and system reliability requirements. The equipment and systems placed into service under these blanket projects are entirely necessary, and indeed mandatory, under the terms of the Company's franchise terms, agreements with the cities and towns in which we operate, and in order to continue to provide customers with safe and reliable service.

Interestingly, through discovery the Company asked Mr. Dudley which projects should not have been undertaken and/or completed in order to remain on budget. His response to GSEC 1-52 (Attachment CPB/TAS/GPT-1) states, in part: "Staff did not consider the necessity or the appropriate prioritization of the capital projects…." We find it troubling that Staff recommended a disallowance of $5.8 million due to cost variances, yet it failed to even consider whether the blanket projects causing the bulk of those cost variances were necessary. Although the budget variances may have given Staff reason to initially question the prudence of the underlying investments at the temporary rate stage of this docket, Staff had the opportunity during the balance of this case to investigate the capital projects to learn whether the money was prudently spent. Staff chose not to conduct that analysis.

Q. Did Mr. Dudley review these projects specifically in his testimony?

A. Of the 225 total projects in 2014 and 2015, the comprehensive information on all of which was available to Mr. Dudley through discovery, he reviewed 17 projects from 2014 and 10 projects from 2015. *See* Bates 000019 and 000020 of Mr. Dudley's testimony, Tables 1 and 2. The bulk of these 27 projects, in terms of project quantity and dollar value, are Growth, Mandatory, or the excluded REP category projects as discussed above.

Q. What analysis did Mr. Dudley undertake with regards to these projects?

A. Of the 27 projects Mr. Dudley analyzed, he selected three as sample projects for his in-depth analysis from the list of projects in Tables 1 and 2. The selected projects were (1) Project 8830-C18720, Refreshing of Existing Buildings, (2) Project 8830-CNN016, GSE Distribution Load Relief Blanket, and (3) Project 8830-Finance, and a Finance Accrual project.

Q. Can you comment on the analysis undertaken by Mr. Dudley?

A. Yes. Overall, the Company provided Staff with a substantial amount of information, which Mr. Dudley details on Bates 000018 of his testimony. It is unfortunate, and misleading, that two of the three projects Mr. Dudley selected, Refreshing of Existing Buildings and the Finance Accrual project, are inappropriate projects on which to base any prudence analysis because they are atypical of the Company's capital projects and, by their nature, are not good reflections of the capital budgeting and management process.

Q. Please provide your specific concerns over Mr. Dudley's analysis with respect to each project.

A. **Project 8830-C18720 – Refreshing of Existing Buildings** – The Refreshing of Existing Buildings project was for renovations to existing buildings in Lebanon and Salem. These projects were necessary to bring the buildings up to current operating and work environment conditions. Neither building had received any significant renovations since the mid-1980s. Following commencement of renovations, emergent issues arose such as the condition of the underlying foundation and the presence of material containing asbestos that required abatement. Also, the Company began this work at the same time as other facilities projects, including other work in Salem and for the customer walk-in centers in both Lebanon and Salem. Due to the simultaneous nature of these projects and the desire to minimize disruption to the workforce, the work progressed as rapidly as possible during 2014, and continued into 2015. The Company acknowledges that the magnitude and complexity of the building projects presented significant challenges to those who initially determined the scope of the projects, who estimated the costs, and who scheduled the construction. However, such challenges do not diminish in any way the need for, or prudence of, this work. In fact, in view of the deteriorating state of the buildings, it would have been imprudent to delay the work.

To help Staff better understand these projects, including how they developed over time and the costs associated with the projects, the Company provided additional information to the Audit Staff on October 24, 2016 (*see* Attachment JED 2-10.B to Mr. Dudley's testimony), and provided further details on the need for and nature of the expenditures during a November 17, 2016, technical session with Staff.

Some elements of Mr. Dudley's testimony regarding this project are misleading and incorrect:

- Mr. Dudley stated that Granite State performed no pre-construction site inspections. Bates 000021, lines 21- Bates page 000022, line 1. To the contrary, the Company worked with the construction vendor to develop construction plans of sufficient detail to begin building renovations based on existing conditions at the buildings. Site tours were made. However, more intensive site inspections that would have been necessary to uncover the sub-floor foundations and asbestos that were later discovered would have been difficult and time consuming.

- Mr. Dudley testified that the spending report for 2015 contained no forecasted amounts for 2016 through 2018, Bates 000020, lines 12-13. The 2015 spending plan report would not have contained any forecasted amounts for the building refreshing project because, at the time the plan was prepared, it was targeted to be completed in 2014. The same reasoning applies to the Capital Work Plan for 2015. Mr. Dudley's analysis failed to look at the year before or year after and examine the entire project to see if it was on budget. He inappropriately took calendar year snapshots of projects that spanned multiple years.

- Mr. Dudley asserted that no business case was prepared for a related project 8830-C18740 - Walk-in Centers that ultimately was included in the C18720 Refreshing of Existing Buildings project. Mr. Dudley omitted that the business case information was provided to management using the Capital Expenditure Application, a related business document containing similar information about the project and its need. Management thus had the necessary information to make an informed decision to approve the project.

- Mr. Dudley testified that the January – November spreadsheet tab of the Monthly Capital Report for 2015 was never compiled and is unavailable. Bates 000021. The January – November tab for the monthly capital report was indeed prepared and utilized. The Company simply failed to retain this document in its records, which was conveyed to Staff.

Project 8830-Finance – Finance Accrual – The Finance Accrual project was for accrual of capital charges to projects when goods and services were received in 2014, but invoices had not yet been processed. That is, this Accrual "project" was merely an accounting placeholder where the Company could record costs that were actually spent, but which were not yet allocated to their appropriate and specific projects. Once allocated, this Accrual "project" was zeroed out.

Mr. Dudley recognized in his testimony that this project is not mentioned in the Capital Work Plan because it does not constitute an actual project. Bates page 000028, lines 8-9. It is therefore unclear why Mr. Dudley selected this "project" for detailed analysis. A productive analysis of this project may have been to examine what dollars were allocated to which specific projects to see if there was evidence related to prudence. Mr. Dudley did no such analysis, but simply asserted that the entire $2.4 million "spent" under this project constitutes an additional project overrun, which is not correct. The $2.4 million was a conglomeration of accrued expenses from several projects across multiple categories, as Mr. Dudley himself pointed out. From an accounting perspective, this accrual method is entirely consistent with U.S. Generally Accepted Accounting Principles and with past regulatory reporting practice. In the subsequent year, 2015, the accrual account was credited and individual projects debited by the actual invoiced amount. Further, the accruals apply to all projects, including underruns, those within variance, and excluded projects, not just overrun projects as Mr. Dudley incorrectly asserted. Thus, there is absolutely no basis on which to conclude that the $2.4 million constitutes a project overrun, nor does it demonstrate any evidence whatsoever of alleged imprudence.

Project 8830-CNN016 – GSE Distribution Load Relief Blanket – The Distribution Load Relief Blanket project was prepared to record capital costs incurred to address distribution system requirements that arise during the year, such as over-utilized feeders, equipment, imbalance issues, transformer overloading, and other equipment and system capacity limitations. At Bates 000025 of his testimony, Mr. Dudley referenced the actual spend of this project as $780,409, which was the correct value at the time the 2014 Year-end Variance Report was prepared. Subsequent to that report, however, the Company processed accounting transfers to correctly allocate charges to other projects which reduced the actual spend of this blanket project to $246,684. Since the accounting transfers had not occurred at the time of the Company's response to Staff 10-40, it is understandable why Mr. Dudley based his analysis on the $780,409 value. The actual variance, however, was $220,684. Underscoring this variance was the explanation provided in the Year-end Variance Report, referenced by Mr. Dudley as JED 2-2. As stated in the Company's year-end 2014 report for the project,

> Over-charging of blanket projects occurred in 2014 due in part to the conversion of the work management system from NG Transition Services Agreement ("TSA") based STORMS system to LU based Quadra and WennSoft systems. This made establishment of timely work orders under specific projects difficult to establish and charge, resulting in use of established blanket projects to capture job charging.

During the conversion period for WennSoft, it was often not possible to establish work orders under new, specific projects. Therefore, an established blanket project was used to capture the work, resulting in a variance.

Q. Are there other aspects of Mr. Dudley's testimony that raise concern?

A. Yes. Although Mr. Dudley admitted that Granite State was consistent in filing and processing all of the standard documentation and reports required under Liberty Utilities' internal processes and procedures, Bates 000030, lines 5-7, he nonetheless questioned the detail of this documentation. What Mr. Dudley failed to mention is that the Home Office rolled out the Capital Policy in the summer of 2013, essentially becoming effective for the portfolio of projects planned for the 2014 budget year. As such, the documentation prepared for the 135 Granite State projects in 2014, as well as the documentation for EnergyNorth's gas business portfolio, represented the first time that the local team assembled such information for its capital investment portfolio. This was a significant undertaking and, despite this challenge, even Mr. Dudley acknowledged that the documentation was complete. This also underscores the issues with the timing of the Business Cases that Mr. Dudley raised. Despite this timing issue with the Business Case forms, local and Home Office management were nonetheless aware of the project line item categories, business drivers, and historical spending that the 2014 Capital Plan represented, independent of business case documentation. It is unfair and inaccurate to conclude, as did Mr. Dudley, that the requirements under Liberty Utilities' policy and procedure were largely ignored and not adhered to by Granite State, particularly in view of Mr. Dudley's own admission that the standard documents and filings were completed. Mr. Dudley unfairly and inaccurately assailed the schedules, plans, and reports prepared by the Company to plan and manage its capital investments, because he largely ignored the specific purpose of each report and he failed to request additional information to better understand each report. Although in some instances the monthly component of a series of reports was not available to reproduce, such omission in no way undermines the overall integrity of the capital management process nor the necessity of the underlying capital projects.

Q. Has the Company instituted any improvements to its capital budgeting and management processes?

A. Yes. In its response to the LCG audit, the Company described how it has added or reinforced key provisions of the capital budgeting and management processes. These include the following initiatives in order to provide further, detailed insight into the drivers of each project line item, particularly with respect to the business case for each project:

- The Company will prepare preliminary business cases in conjunction with the annual budget submission, followed by formal business cases once the budget is finalized; and
- The Company has added to the rigor and timeliness of year end project close out reports and variance analysis.

The Company has always recognized the need to monitor and control actual capital costs as compared to budgeted costs, not only on specific projects but in total. However, the variances that occurred in 2014 and 2015 were not the result of a lack of control over the spending process. To the contrary, the actual spending was the result of local decision-making and flexibility as circumstances changed. If there had been a strict limit on either total spending or on individual project spending, Granite State may have been unable to provide service to new customers as a result of budget constraints. That situation would clearly not be a positive outcome. The Company understands the need to control capital spending, tempered by the realities of the situation and changed circumstances as compared to the anticipated circumstances at the time of budget preparation.

The Company asserts that there was full visibility and business case documentation for the 2014/2015 projects. The capital budget was vetted and discussed with local and senior management. The business cases included project analysis and in some cases Commission approval. When determining capital needs, electrical and gas planners used SAIDI and SAIFI and other operating metrics as objectives for the planning process. Other considerations included specific programs and projects, which frequently have studies to support the project and often Commission Staff collaboration or approval. Recurring work orders are captured under blanket projects and are budgeted based on historical spending levels adjusted for known and measureable changes. Continuous improvement is one of the Company's core values. In an effort to improve its budgeting process, the Company has implemented the following specific policies, which were summarized above but are repeated here:

- The Company has reinforced the detail and rigor of the monthly capital budget meetings;
- An individual was hired in the local Finance organization to manage and review the capital budget and spending;
- The month-end accruals are now recorded at a job level to provide better visibility to job spending, particularly as the year-end threshold;
- Project governance documents, including year-end reports, reauthorization requests, and project closures are being prepared and submitted in a more timely fashion, notwithstanding that prior or current policy did not require full business cases ahead of capital budget approval; and

- During the monthly operating call, there is a review of year-to-date capital spending against budget along with a forecast to the end of the year. Any major variances are discussed. More in-depth detailed capital analysis is performed at the business unit level in accordance with the capital expenditure planning and management policy. It is worth noting, however, that both prior and current policy provide full authority for local management to undertake up to a $1 million investment.

The significantly reduced magnitude of projects over their budgeted amounts, reduced from $12.3 million in 2014 to $1.5 million in 2015, demonstrates the Company's attention to improved capital planning and management, notwithstanding the Company's position that this metric has no relationship to the underlying prudence of these investments.

Q. What has the Company achieved since 2013 by completing these projects?

A. The actual capital invested for the period 2013 – 2015 reflects a categorized allocation as detailed in the Company's April 29, 2016, direct testimony at Bates 0183-0184. The Company approximately doubled its annual capital investment, as compared to previous ownership, in order to make up for years of capital neglect. Granite State made prudent investments identified as necessary in studies or engineering analyses that the prior owner had delayed. These investments included opportunities for Bare Conductor Replacement, Single Phase Recloser and Trip Saver application, Mt. Support and Slayton Hill substation upgrades, Enfield Second Supply Line, Charlestown capacity upgrades, Hanover substation upgrades, SCADA/RTU implementation, and, on the expense side, in vegetation management.

The long-delayed infusion of capital and vegetation management expense funding was well justified and necessary to improve system and storm performance and to manage forward performance risk. The Company achieved noteworthy gains in its reliability performance, having improved its five-year reliability performance in SAIDI and SAIFI metrics every year since 2011.[1] This is a very significant accomplishment, achieved through an optimization of capital reliability projects, vegetation management practices, and operation and maintenance initiatives. Similar results were achieved in the gas business key metrics using the same investment strategy. Stated differently, the consequences of not undertaking the projects that were previously identified by National Grid and subsequently confirmed by Granite State, would have negatively impacted our ability to serve customers and municipalities in a timely manner, the performance metrics of the Company, the service levels experienced by our customers, our storm performance and resourcing, and the Company's reputation for living up to its stated commitment to be Local, Responsive, and Caring.

VI. CONCLUSION

Q. Can you summarize the Company's position with respect to the analysis and conclusions presented by Mr. Dudley?

A. The Company has presented evidence that refutes the bulk of Mr. Dudley's analysis and recommendation that $5.8 million in capital investments, undertaken by the Company for

[1] With one exception: in 2016, SAIFI was 1.36 compared to 1.33 in 2015.

the direct benefit of customers, should be deemed imprudent. Our testimony confirms the prudence of the Company's capital investments since 2013 as well as the substantial benefits provided by the nature and timing of these investments. Further, Mr. Dudley based his conclusions on misleading and poorly selected evidence, centered on three atypical projects which have no bearing on the prudence of the Company's investment portfolio or on the $5.8 million in investment questioned by Mr. Dudley. Mr. Dudley attempted to discredit the Company by accentuating inconsequential elements of the Company's internal capital investment process, but he failed to show that the projects themselves or corresponding expenditures were in any way imprudent. Mr. Dudley was incorrect in his conclusion that the costs were imprudent. The Commission should allow the Company to include all of the costs in rate base.

Q. Does this conclude your testimony?

A. Yes, it does.

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