STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

AQUARION WATER COMPANY OF NEW HAMPSHIRE, INC.
DOCKET NO. DW 12-085

DIRECT TESTIMONY
OF
TROY M. DIXON

May 14, 2012

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I. INTRODUCTION AND OVERVIEW OF TESTIMONY

Q. Please state your name and business address.

A. My name is Troy M. Dixon. My business address is 600 Lindley Street, Bridgeport, Connecticut.

Q. Are you the same Troy M. Dixon who prepared written testimony in support of temporary rates in this case?

A. Yes.

Q. What is the purpose of your testimony in this case?

A. The Company's application in this case seeks an overall increase of $1,113,931, or 18.3%, in annual revenues over and above those amounts currently authorized in the last rate case and the most recent WICA proceeding. My testimony discusses the Company's (i) current financial condition and need for rate relief; (ii) pro forma revenue and expense adjustments to the historical test year data; (iii) balance sheet and pro forma rate base; (iv) pro forma capitalization and rate of return; (v) billing analysis, revenue adjustments, rate design and tariff changes; (vi) the Water Infrastructure and Conservation Adjustment ("WICA") surcharge; (vii) a proposed step increase in this rate case as a means of implementing the next WICA rate adjustment; and (viii) a deferral request related to the Town of Hampton's newly established right of way ("ROW") tax.

II. FINANCIAL CONDITION AND NEED FOR RATE RELIEF

Q. Please describe the Company's current financial condition.

A. Since the Company's last general rate case, which had a March 2008 test year, the Company's rate base has increased by approximately $1.2 million and it has made more than $4.5 million of utility plant additions as of the end of the current test year, December 31, 2011. Those improvements are discussed in detail in Mr. McMorran's testimony. At the same time, the pressures of increasing operating expenses, especially the burden of steadily and substantially increasing property taxes, combined with declining consumption have depressed the Company's earnings and made its authorized return on equity essentially unachievable. The impact of these forces is shown in the table below.

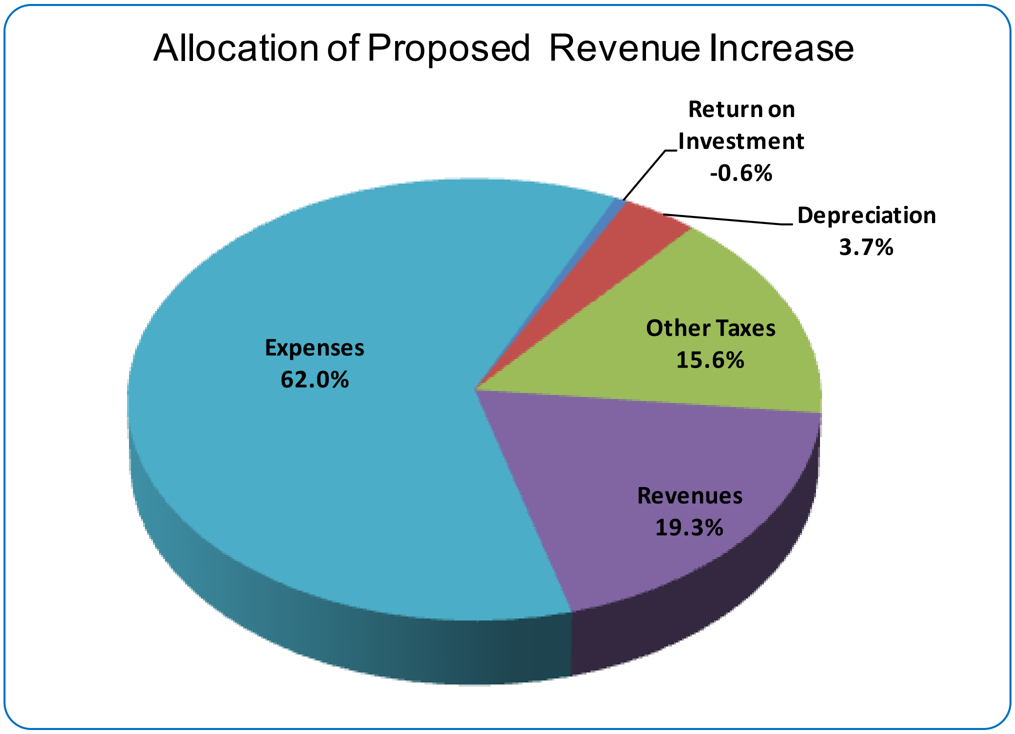
					Test Year			
		2009		2010		2011		Pro Forma
Revenue	$	5,623	$	6,009	$	5,970	$	6,087
Expenses		2,662		2,950		2,952		3,147
Other Taxes		497		444		585		670
EBITDA	$	2,464	$	2,616	$	2,432	$	2,270
Depreciation & Amortization		929		934		932		956
EBIT	$	1,535	$	1,682	$	1,500	$	1,314
Interest Expense		667		768		792		799
EBT	$	868	$	914	$	708	$	515
Income Taxes		337		379		324		222
Net Income	$	531	$	536	$	383	$	293
Return on Equity (ROE)		6.4%		5.6%		3.9%		3.0%

Even with a full year of rate relief realized in 2010 and 2011 from the rates approved in DW 08-098, the Company could only achieve 5.6% and 3.9% equity returns, respectively, compared to the 9.75% authorized. Upon consideration of the pro forma adjustments put forth in this case, the Company's ROE will decline to 3.0% absent rate relief.

This rate application is critical to the Company and its financial integrity. Full rate relief is necessary to enable the Company to operate on a stand-alone basis, generate sufficient funds necessary to maintain its utility plant, pay a reasonable return to its shareholder, and keep its borrowing needs at reasonable levels, all the while providing safe and reliable service to customers.

Q. What are the components that are driving the need for rate relief?

A. The chart below itemizes the key components of the request as compared to the overall amounts authorized in DW 08-098 and the additional revenues, utility plant, depreciation and property taxes as authorized in DW 11-293.

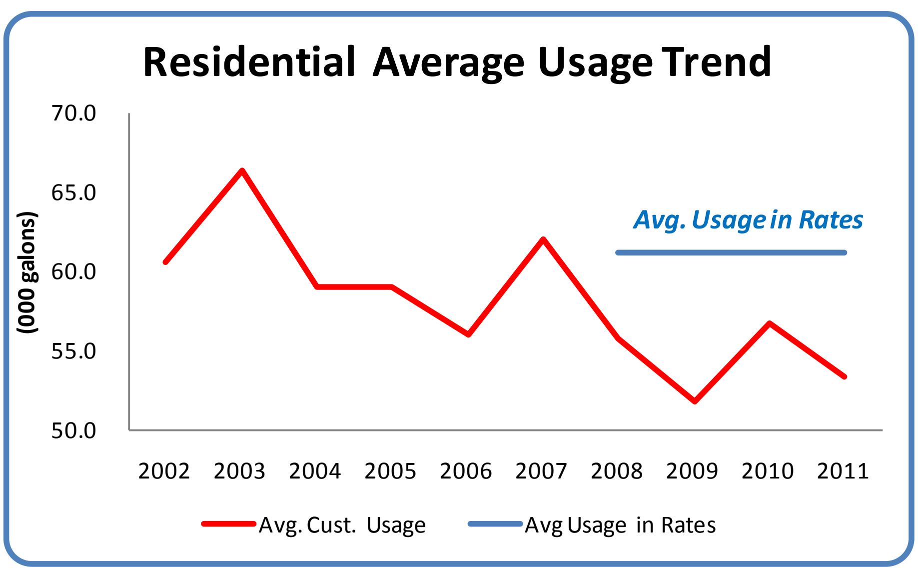


Return on Investment: Previous rate cases filed by the Company have been driven heavily by increases in rate base. While rate base has increased by $1.2 million since the last general rate case, all of that rate base growth has been incorporated into the Company's revenue requirement through the existing WICA surcharge. Were it not for increases in expenses and property taxes, it is likely that the Company would not have had to file a rate case. Absent the WICA mechanism, and assuming that capital spending occurred at the same levels, the revenue increase sought in this rate case would have been approximately $222,000 higher, for an overall increase of 22.8%. (Section VII of my testimony further discusses WICA and the associated benefits.) The combined effect of rate base changes and change in rate of return on a net basis result in a small ($6,000) increase in the revenue requirement.

Depreciation: A significant portion of the increase in depreciation expense since the last general rate case has already been reflected through the WICA surcharge. Accordingly, $23,000 of the $65,000 in total depreciation expense increase from the last case is not part of the 18.3% increase sought herein. The remaining $42,000 of increased depreciation expense accounts for 3.7% of the overall increase being sought.

Other Taxes: Other taxes is comprised of payroll taxes as well as property and right of way taxes from the Towns of Hampton, North Hampton, Rye and Stratham and the State of New Hampshire. Payroll tax increases of $11,000 are directly related to the increases in the Company's wages discussed later in my testimony. More significantly, property and right of way taxes from the towns have increased by 37% when compared to the amounts from the last general rate case. In particular, the right of way tax from the Town of Hampton is an entirely new cost that the Company is facing and therefore was not reflected at all in the rates set in the Company's last rate case. These taxes are discussed in more detail in Sections III and IX of my testimony. When combined, all of these taxes account for $174,000, or 15.6%, of the total increase in the revenue requirement.

Revenue: In DW 08-098, the Company's rates were calculated based on an assumed level of residential consumption of approximately 61,200 gallons per customer. Actual consumption, however, has consistently been below that level and is generally declining. This is consistent with an overall trend of reduced consumption per customer that has been experienced by the Company's other affiliates as well as across the nation. The overall impact of this conservation is approximately $214,000, or approximately 19.3% of the revenue requirement increase proposed in this case. The chart below demonstrates this trend in reduced usage per customer.



Expenses:

In DW 08-098, the approved settlement agreement recognized operating and maintenance expenses of approximately $2.5 million. The proposed operating and maintenance expenses in this case total $3.2 million. Accordingly, in addition to the significant increases to property taxes discussed above, some of the other more significant cost increases include:

- Maintenance expenses have increased by $121,000. These increases are discussed further in Mr. McMorran's testimony.
- Salaries and Wages have increased approximately $109,000 since DW 08-098 in order to keep pace with industry standards and retain a capable workforce and meet the Company's contractual obligations to its union employees.
- Pension and Post-retirement Healthcare expenses increased approximately $107,000 and $67,000, respectively, since the last general rate case. This is primarily due to the impact on actuarial funding determinations from lower interest rates, market volatility, and an aging workforce. To mitigate further increases, the Company has discontinued participation in its pension plan for new employees.

These and other increases are discussed further in this testimony as well as that of Mr. McMorran.

Q. Have you prepared, or caused to be prepared, financial schedules in support of the Company's application to increase rates?

A. Yes, I have. The Company has filed schedules that reflect its accounting and financial condition and that support the Company's request for increased rates. The schedules that I am supporting with direct testimony were prepared by me or under my supervision and direction.

Q. What is the source of the information in these schedules?

A. The schedules have been prepared utilizing the general books and records of the Company and other supporting data for a test year of the twelve months ended December

31, 2011. The test year data has been adjusted on a pro forma basis, where appropriate, to reflect known and measurable changes which were not fully reflected in the test year results and which will continue to impact operations in the future. These adjustments will be explained in the following schedules.

Q. What are the results displayed on Schedule A?

A. **Schedule A** summarizes the computation of the total revenue deficiency and the proposed revenue increase after pro forma adjustments. It shows that the Company is experiencing an overall revenue shortfall of $1,113,931 on a pro forma basis, resulting in the need for a 18.3% increase to pro forma revenues based on the existing rates and WICA surcharge.

Q. What is the impact of the proposed increase on customer rates?

A. During the test year, the average residential customer used approximately 53,300 gallons of water. Based on current rates a residential customer with average consumption would pay $365.16 annually. With the proposed increase, that same customer would see an increase of $68.17 per year ($17.04 per quarter, $5.68 per month, $0.19 per day).

III. REVENUE AND EXPENSES

Q. Please summarize the contents of Schedule 1.

A. **Schedule 1**, page 1 of 3 sets forth the income statement for the Company for the twelve months ending December 31, 2009, 2010 and 2011. It also reflects pro forma adjustments to the test year (explained in detail later in my testimony) to arrive at a pro forma income statement at present rates as well as pro forma net income at proposed rates. Page 2 of 3 also depicts the income statement; however, the format is modified to capture the calculation for Utility Operating Income (versus Net Income on page 1). Page 3 of 3 displays the quarterly consumption levels for each quarter of the test year, and the customer count at December 31, 2011.

Q. Please explain the results presented on Schedule 1A.

A. **Schedule 1A** compares pro forma revenues at present and proposed rates. It begins with book revenues. Pro forma adjustments are then applied to arrive at pro forma revenues at present rates. A further adjustment is then made to reflect the revenue increases from proposed rates, which then produces total pro forma revenues at proposed rates. The pro forma revenues at both present and proposed rates match the results derived in the billing analysis in Schedule 5.

Q. Please describe the pro forma adjustments to revenues at present rates, as shown on page one of Schedule 1A.

A. The pro forma adjustments are itemized more fully on Page 2 of the schedule and are for three major areas:

1. Unbilled Elimination
2. WICA Adjustments
3. Miscellaneous Items

Q. Please discuss the unbilled elimination adjustment.

A. This adjustment removes the revenue impact created by unbilled revenues booked in December 2011, which are offset by the reversal of the December 2010 entry for unbilled revenues. Although minimal, elimination of these entries allows for examination of actual billed revenues within the twelve month test year without the impact of estimates.

Q. Please discuss the WICA adjustments.

A. By order 25,311 dated December 30, 2011 the Commission approved an increase of the Company's existing WICA surcharge from 1.5715% to 3.7269% effective January 1, 2012. Given that this increase did not occur until after the end of the test year, a pro forma adjustment is required to reflect the known and measurable change to the Company's rates.

Q. Please discuss the miscellaneous adjustments.

A. The miscellaneous adjustments include 1) adjustment of antenna rental income based on contractual increases and corrections for new and/or expired leases and 2) adjustment to late payment fees based upon all other pro forma adjustments made to operating revenues.

Q. Please discuss in detail the pro forma adjustments represented in Schedule 1B through Schedule 1Z.

A. **Schedule 1B is entitled** Summary of Pro Forma Adjustments to O&M Expense. This schedule simply summarizes the operation and maintenance expense adjustments to the test year figures as well as the corresponding detailed schedule references and major account classifications. As can be seen, the Company is proposing to increase test year operating expenses by $194,262 on a pro forma basis.

Schedule 1C, Salaries and Wages, details all wages and salaries incurred by or charged to the Company. Total wages, which are comprised of two components, are calculated as follows:

1) The first component of the wages relates to the direct charges for the employees of the Company. Pro forma officer wages are based on a portion of the current annualized salary levels for the Vice President of Operations, who is in charge of both the New Hampshire and Massachusetts subsidiaries of Aquarion Water Company. The amounts included reflect 37.5% of his total wages and are based on time allocated to the New Hampshire operation. These officer wages are combined with the current annualized wages for two additional exempt, non-union employees for a pro forma total of $203,526. In addition, there are also one full-time and two part-time non-exempt, non-union employees. Pro forma wages of $88,417 are based on current annualized salary levels. Lastly, pro forma wages of $447,882 relate to annualized salary levels at December 1, 2011 for eight union employees. A 3.5% union contract salary increase will become effective as of December 1, 2012. Finally, pro forma standby and shift differential pay are based on the amounts included in the test year plus the 3.5% union contract increase for these charges. The resulting amount of gross pro forma wages of $786,529 was multiplied by the expense ratio to arrive at pro forma wages charged to expense. Test year wages were subtracted from the pro forma wages to arrive at the pro forma adjustment.

2) The second component of wages represents service company personnel whose time was charged to the New Hampshire operations in the test year. This time represents services from AWCCT's Accounting, Finance, Accounts Payable, Engineering, Human Resources, Administration and Water Quality departments. The only adjustment made to the amount of salaries charged to utility expense in the test year was a 3% pay increase that went into effect on April 1, 2012.

Schedule 1D, **Employee Welfare**, includes employee medical costs, 401K plan expense, auto allowance, life insurance and long-term disability. Medical costs are based on a premium-based plan for twelve full-time New Hampshire employees. The Company moved to a premium-based medical plan on July 1, 2008 and away from the prior self-insured plan in an effort to control medical expense and to reduce the risk of incurring large claims for serious illnesses in any particular year. Medical expense for the Vice President, of which 37.5% of the cost is allocated to the New Hampshire operations, is provided through CIGNA. Pro forma expenses for medical expense are based on the current annualized costs of those plans, less the amount contributed by employees. 401K plan expense is based on the current annualized matching expense based on each employee's current contribution. Union employees receive a 50% Company match and non-union employees receive a 75% Company match. Pro forma auto allowance is based on a $500 per month allowance for the Operations Manager. Pro forma life insurance and long term disability expense are based on multiples of base wages, as shown on Schedule 1C, times the current insurance rates. For pro forma purposes, all of the above costs have been reduced to reflect only the amount charged to utility expense.

Schedule 1E, **Employee Bonus Program**, shows the expense associated with the bonus program for non-union employees**.** The program is designed to help the Company and its affiliates retain and attract employees and to incentivize positive employee behavior that supports the Company's customer service, service quality and product quality goals. Amounts for the bonus are based on a percentage of the participating employees' annual salary for those employees achieving their goals and meeting performance targets. Pro forma amounts are based on those percentages applied to the wage levels utilized in Schedule C. The pro forma amounts have been reduced for the percentage charged to utility expense.

Schedule 1F, **FAS 106 – Post Retirement Healthcare**, shows the current expense level for post-retirement healthcare benefits as determined by the Company's actuary, Deloitte.

Schedule 1G, **Pension**, shows the current expense level for pension expense as determined by the Company's actuary. As noted earlier, the Company has discontinued participation in the pension plan for any new employees in an effort to mitigate the significant cost increases associated with this type of benefit.

Schedule 1H – Legal reflects expense for general legal services and yearly legal expense related to the Company's WICA filings.

Schedule 1I, Chemicals Expense, shows actual current chemical prices and adjusted test year chemical usage. The current chemical prices reflect the Company's yearly bidding process. On a yearly basis the Company requests bids from chemical vendors to provide the lowest cost of required chemicals to treat the specific sources for potable water for consumption. The current prices will be in effect for the calendar year 2012. The test year usage has been adjusted to reflect a chemical change that was made at several of the Company's facilities. At these facilities, the Company has converted from using potassium hydroxide, which costs $6.41/gal., to using sodium hydroxide, which costs $2.395/gal. The Company proposes a reduction to chemical expense of $3,668 from the Test Year expense of $51,746 for a pro forma chemical expense of $48,078. Further details regarding the change in the use of the chemicals are discussed within the testimony of Mr. McMorran.

Schedule 1J, Purchased Power – Electric, reflects the Company's electric expense. The Company has two electric providers, Public Service of New Hampshire and Unitil Energy Services. For Unitil, rates increased in the middle of the test year, and therefore pro forma power costs are based on the test year usage at the most recent prices. For Public Service of New Hampshire, there was no rate change in the test year, and therefore pro forma power costs are based only on actual bills during the test year. Included in the amounts covered by this schedule are the costs of electric supply that is purchased from a competitive supplier, Nextera. Mr. McMorran discusses this item in more detail.

Schedule 1K, Elimination of Non-Recurring Items, shows several changes that were made to adjust for items which are considered non-recurring, one of which results in an additional charge**.**

Schedule 1L, Building Lease Expense, shows the change in expense related to the Company's building lease expense. In particular, the Company is consolidating its storage facility at Mill Road and its administrative office space at One Merrill Industrial Drive by moving them both to a new location at 7 Scott Road in Hampton. The decision to consolidate the two facilities is based on the need to meet the DES wellhead protection standards and the efficiencies associated with centralizing the Company's office and distribution center. The pro forma expense is based on the annualization of the new lease expense for the 7 Scott Road location. Mr. McMorran's testimony discusses this change in more detail.

Schedule 1M, Corporate Insurance, reflects the Company's allocated insurance expense as of the January 1, 2012 policy year. The Schedule sets forth the type of policy as well as the methodology behind the Company's allocation for each insurance expense item. The latest policy year yields a pro forma increase in expense as compared to the test year expense.

Schedule 1N, Audit Fees shows pro forma audit fees, which are based on the engagement letter from the Company's external auditors, Dworken, Hillman, Lamorte and Sterzala. The pro forma amount reflects minor increases which are offset by excess accruals in the test year.

Schedule 1O, Deferral of Right of Way Property Taxes, the information in this schedule is discussed in more detail in Section IX of this testimony. The Company is requesting that it be authorized to establish a deferred asset account for the amount of the Town of Hampton's right of way property taxes billed in April 2011, which the Company is actively disputing and has not yet paid. The tax is pro forma to the point temporary rates become effective or 15 months from April 2011. Aquarion is requesting that the unpaid amount be deferred and amortized over three years once it is included in rates. The three year amortization coincides with the frequency of the Company's rate case filings. While the Company is actively contesting this tax, and the ultimate amount of the tax paid may change, the Company proposes to include the annual amortization in rates now and reconcile any difference in the future if the amount is ultimately adjusted as a result of the abatement process. If the amount of the tax becomes finally known during this proceeding the Company will update its request accordingly.

Schedule 1P, Tank Painting Amortization, reflects the amortization expense for tank painting costs for the Jenness Beach tank and the Glade Path tank which were painted in 2007 and 2000, respectively. The Glade Path tank incurred additional spot painting costs during the test year and the Company began amortizing these costs over 5 years, a time span indicative of the frequency at which the Company would anticipate performing similar painting. The adjustment to test year expense equates to the additional annual amortization of the Glade Path tank.

Schedule 1Q, Shared Facility Costs, presents the allocation of costs associated with common facilities for the various Aquarion Water Company subsidiaries. AWCCT maintains three common facilities: an operations center, a corporate office and the customer service call center. The shared office costs are calculated by deriving a building overhead rate per facility then applying such rate to labor charged from each facility to the Company, which is based on the formula contained in the Service Agreement with Aquarion Water Company. The resulting amount of $46,724 for all three buildings requires a pro forma reduction of $202 to test year expense.

Schedule 1R, Management Allocation, sets forth the derivation of the Company's allocated share of management expense from Aquarion Company, the parent company of Aquarion Water Company, which in turn owns Aquarion Water Company of New Hampshire. These charges include charges to Aquarion Company for services provided by its corporate parent Macquarie Utilities Inc. ("MUI"), which are provided under a separate service agreement between MUI and Aquarion Company. Under the service agreement between MUI and Aquarion Company, MUI provides corporate audit and consulting services, strategic planning, asset management, legal and financial services, and board of director services. The audit and consulting expenses include fees for internal and external audits, as well as accounting, tax and pension advisory services. Asset management and director costs include charges allocated by MUI for the time and expense devoted to assist Company management in the governance of the business. These costs are allocated between the parent's regulated utilities and non-regulated entities based on the Massachusetts formula methodology. The three-part formula uses a weighted cost average ratio comparing gross revenues, plant and payroll. Costs allocated to the regulated utilities are then spread to the individual utilities based on each utility's respective customer count. The utilities received 98.8 % of the overall cost, of which 4.29% is allocated to the Company, yielding an overall 4.23% allocation. Based on this methodology, pro forma corporate expenses will decrease $150 to $55,018.

Over the course of the past decade, management fees have trended downward as Aquarion Company pursued efforts to streamline corporate functions and to remove overheads from the business. During this period of time, Aquarion Company went from being an independent, publicly traded company, to a U.S. based water utility for the U.K. based Kelda Group in 2000, to a wholly owned subsidiary of MUI. Today, these corporate management charges are significantly less than when the Company was publicly traded and also under the previous ownership of Kelda. These costs in 1996 amounted to approximately $2.5 million when Aquarion Company operated independently. Similarly, in 2003, under Kelda ownership, the charges were approximately $2.5 million. Today, the combined charges for the services from MUI and

Aquarion Company amount to $1.3 million, a 48% reduction from Kelda and independent ownership. The Company's allocated share of these costs totals $55,018.

Schedule 1S, Shared Customer Service Costs, sets forth the Company's allocation of shared customer service costs. As agreed to in the approved settlement in DW 06-094, the Company maintains an office in New Hampshire for bill payments and customer inquiries. As has been the case in the past however, there continue to be many customer service functions that are performed by the Company's Connecticut affiliate at its centralized customer service center. These services include the overall administration of customer service, the collection of cash payments for New Hampshire's water bills through a lock box, management of uncollectibles, late payments and delinquencies, and support for service representatives located in New Hampshire to assist with non-routine issues.

The customer service employees in Connecticut do not directly charge payroll time to any affiliate, and they are not included on Schedule 1C, Salaries and Wages, as service company wages. To reflect the cost of these services, for pro forma purposes, a portion of the Connecticut company's customer service cost is allocated to the New Hampshire operation. As Schedule 1S shows, the allocation of costs is based on customer count. The customer count used for the New Hampshire operation allocation is 4,550, which is half of the actual count of 9,100 customers. This allocation reduction recognizes the fact that calls are directly answered in the New Hampshire office, but administrative and support services are still provided by the Connecticut operations. As a result of this computation, pro forma expense is $43,055.

Schedule 1T, Shared IT Costs, sets forth the Company's share of information technology ("IT") costs incurred for computer and networking services, software and hardware maintenance, and data processing services provided by AWCCT under the Service Agreement with Aquarion Water Company. Those services include SAP software systems and licenses along with technical support. All costs incurred in rendering shared IT services to Aquarion Water Company's water subsidiaries are allocated among all utilities receiving such services based on the number of customers served at the immediately preceding calendar year end. The allocated costs also include the return on investment and depreciation of the SAP software. The schedule shows a downward adjustment reflecting the reduced software investment as well as expense reductions due to savings on software maintenance that are the direct result of a competitive bidding arrangement by the Connecticut utility. The pro forma expense amounts to $229,463, as shown on Schedule 1T.

Schedule 1U, Depreciation Expense, sets forth the Company's pro forma depreciation expense, which was computed by multiplying utility plant in service as of December 31, 2011 by the authorized depreciation rates in Docket DW 08-098. In addition, an amount was added to the total depreciation expense in order to amortize the difference between book and calculated depreciation reserves over a ten-year period, consistent with the depreciation study filed in Docket DW 08-098 and approved in Order No. 25,019. Test year expense was subtracted from the resulting pro forma depreciation expense to arrive at the pro forma adjustment.

Schedule 1V, Payroll Taxes shows the adjustment in payroll taxes that results from the change in wages reflected on Schedule 1C. FICA, federal and state unemployment insurance are adjusted to correspond to the new salary and wage levels. This includes payroll taxes relating to both full and part time employees as well as service company employees.

Schedule 1W, Property Taxes, sets forth pro forma property tax expense based on the latest property tax bills received by the Company in July 2011. The most recent bills reflect an increase in property taxes as compared to the test year amount. Additionally, the Company was assessed an additional tax of $63,513 referred to as a right of way property tax in April of 2011 by the Town of Hampton. This tax was discussed earlier with regard to the deferral treatment being sought for the amount billed, but not yet actually incurred for 2011. Given the magnitude of the property tax increase, the

Company plans to update this expense for the property tax bills that will be received in July 2012 during this proceeding.

Schedule 1X, Interest Expense, sets forth pro forma interest expense, which includes interest charges on the long-term debt borrowings shown on Schedule 4D and discussed later in my testimony.

Schedule 1Y, State Income Taxes, shows the calculation of the state business profits tax, which is applied to state taxable income for the Company. State Income taxes are computed as follows: the Company first calculates pre-tax income by reducing revenues by the amount of Operations and Maintenance expenses, depreciation, other taxes, interest expense and net other income. The pre-tax income is adjusted for timing differences as shown on Schedule M to arrive at state taxable income.

Schedule 1Z, Federal Income Taxes, shows the computation of Federal Income Taxes. Federal Income Taxes are computed by starting with taxable income from the state tax calculation page, Schedule Y, Line 17. From that value, State Income Taxes are deducted to arrive at taxable income, and the federal statutory rate of 35% is applied. To that value the Company adds, for rate making purposes, the annual amortization of a tax regulatory asset carried forward from the Company's previous owner, American Water Works, and a deferred federal income tax. Additionally, a pro forma adjustment is made to remove the non-recurring "provision to return" adjustment for amounts related to a prior period.

IV. BALANCE SHEET AND RATE BASE

Q. Please discuss the contents of Schedule 2 and its supporting sub-schedules.

A. **Schedule 2** provides the Company's balance sheet as of December 31, 2011 as well as the two prior 12 month periods. Additionally the schedule shows the 13 month average balance from the period ended December 31, 2011. A column is also present to reference the detailed supporting schedules of key balance sheet items.

Schedule 2A provides balance sheet detail for each month included in the computation of the 13-month average shown in **Schedule 2**.

Schedule 2B provides a monthly balance sheet account level detail of the Utility Plant line item from **Schedules 2** and **2A**.

Schedule 2C shows monthly balances of Property Held for Future Use, a component of Utility Plant as per Schedule 2.

Schedule 2D shows accumulated depreciation by account at December 31, 2011, and at the end of the two prior 12-month periods ending December 31. Additionally, Pages 2 and 3 reflect a summary of individual retirements over $5,000.

Schedule 2E presents, by account, materials and supplies balances for the months December 2010 through December 2011, as well as a 13-month average. The schedule also provides annual materials and supplies balances as of the end of the test year as well as the years ending December 31, 2010 and December 31, 2009, respectively.

Schedule 2F presents, by account, deferred tax balances for the months December 2010 through December 2011 and a corresponding 13-month average.

Schedule 2G presents, by account, deferred expense balances for the months December 2010 through December 2011 and a corresponding 13-month average.

Schedule 2H presents, by account, contributions in aid of construction (CIAC) balances for the months December 2010 through December 2011 and a corresponding 13-month average. Additionally, activity is shown since the Company's acquisition by Aquarion Water Company in 2002.

Q. Please discuss the contents of Schedule 3 and its supporting sub-schedules.

A. **Schedule 3** depicts the Company's rate base as of December 31, 2011, as well as the two prior years ending December 31, 2010 and December 2009, respectively. Additionally the schedule shows the 13-month average balance for the period ended December 31, 2011, as well as the Company's computation of rate base on a present pro forma basis.

Q. Has the Company used a 13 month average of rate base for ratemaking purposes?

A. No. For computation of pro forma rate base, the Company used values for plant in service and accumulated depreciation as of December 31, 2011, rather than a thirteen-month average. The Company believes that, consistent with evolving practice at the Commission, it is critical that a year-end rate base balance be used in order to give the Company a reasonable opportunity to achieve its authorized return. The Company is experiencing a steady decline in consumption by its customers and its rate base additions are almost exclusively non-growth in nature.

Q. Please describe the detailed schedules supporting Schedule 3, Rate Base.

A. **Schedule 3A** provides a monthly account level of detail of the Utility Plant grouping from Schedule 3. Schedule 3A is identical to Schedule 2B.

Schedule 3B shows, on a monthly account level basis, accumulated depreciation and rate base additions for materials and supplies, prepayments, deferred expenses and a working capital allowance.

Schedule 3C shows, on a monthly account level basis, rate base deductions for customer advances, contributions in aid of construction and deferred taxes.

Schedule 3D shows the detailed calculation for working capital for the test year and the two prior 12 month periods ending on December 31, 2010 and December 2009, respectively, as well as a 13-month average for the months December 2010 through December 2011. The rate used of 6.83% is calculated in a lag study included in the Standard Filing Requirements, item number 28.

Q. Are all of the rate base additions included in the Company's rate case filing used and useful in providing service to its customers?

A. Yes.

V. RATE OF RETURN

Q. What overall rate of return is the Company seeking in this application?

A. The Company is requesting an overall rate of return of 7.87%

Q. How did the Company derive this proposed overall rate of return?

A. As shown on **Schedule 4A**, the Company began with its actual capital structure as of December 31, 2011, reflecting the balances for three factors: (i) long-term debt, including inter-company debt, (ii) preferred stock and (iii) common equity. Next, the Company established the overall weighted costs for each of the three capital components with the results shown on **Schedule 4**. The weighted cost of long-term debt, inter-company debt and preferred stock were calculated as detailed on **Schedule 4D, Schedule 4E** and **Schedule 4F,** respectively. The weighted cost of common equity was derived based on the Company's recommended 10.25% cost of common equity, which is discussed in greater detail below.

Q. Has the Company made any adjustments to its cost of long term debt?

A. Yes, on April 17, 2012, the Company filed a petition (DW 12-098) to issue $5 million of general mortgage bonds. The transaction refinances a $4 million unsecured promissory note and also provides for financing of an additional $1 million of capital spending (not included in this case). As a result, on **Schedule 4D** the Company has reduced the cost rate on the $4 million note that was part of the Company's test year end capital structure. The coupon rate reduction, from 4.62% to 4.45%, will be a known and measureable event and provides for ratepayer savings.

Q. Has the Company retained a cost of capital consultant for this case?

A. No, not at this point. The Company is attempting to limit its rate case expense by eliminating the need to hire a rate of return expert to determine a fair rate of return. Rate of Return consultants can cost in excess of $50,000 per rate filing. In addition, the litigation of rate of return can add substantially to legal expense and may also result in additional costs if the Commission finds it necessary to hire a consultant and charge the Company for that costs. If a cost of equity can be developed that is determined to be reasonable by the Company and the Commission's Staff, the Company believes that it is likely to be possible to avoid such costs. The Company does, however, reserve the right in this proceeding to hire an expert if an agreement cannot be reached with Staff. For now, in the interest of cost savings, the Company believes that the approach it has taken is the most expeditious and beneficial for it and its customers.

Q. How was the 10.25% return on equity arrived at?

A. The Company surveyed investor owned water utilities throughout the United States in an effort to obtain recently authorized rates of return on equity ("ROE"). The survey results, shown in Attachment TMD-1, reflect the authorized ROE's of sixteen companies located across multiple regulatory jurisdictions. The average ROE of these companies is 10.00%. The Company, however has proposed an ROE of 10.25%, because that is the authorized ROE determined in its recently concluded rate case before the Massachusetts Department of Public Utilities in D.P.U. 11-43, which was a fully litigated case. That decision was issued just over one month ago. Given the extremely recent nature of that result, the relatively small size of the Company and the fact that it is smaller than its Massachusetts affiliate, it is reasonable that an ROE slightly above the average of the Company's surveyed should be authorized.

VI REVENUE , RATE DESIGN AND TARIFF CHANGES

Q. Please discuss the billing analysis compiled for this case.

A. The billing analysis is contained within **Schedule 5**. Using actual test year billing detail and the adjustment as per Schedule 1A as its basis, **Schedule 5A** sets forth the pro forma revenues by class at both present and proposed rates. **Schedules 5B through 5F** represent each of the metered classes of customers based on the detailed billing units and quantities from the test year. **Schedules 5G and 5H** provide pro forma revenues for public and private fire service. Finally, **Schedule 5I** represents miscellaneous revenues.

Q. Please comment on the accuracy of the billing analysis.

A. The accuracy of the billing analysis is measured by taking its derived results and comparing them to the actual book revenues after taking into consideration any appropriate pro forma adjustments. A minimal variance is needed as the units contained within the billing analysis are multiplied by the proposed rates to produce the ultimate revenues requested within the case. The results in this case are extremely accurate. For example, within the residential class, which accounts for over 73% of metered revenues, the difference between bill analysis and adjusted billed revenues is a mere 0.3%. Similar results exist for the remainder of the metered classes.

Q. Please describe the development of the rate design.

A. The Company is proposing an "across the board" increase which produces the same rate impact to all classes of customers. Schedule A of the rate filing shows a required revenue increase of $1,113,931 over pro forma revenues at present rates of $6,086,688, or a 18.3% increase. Within the $6,086,688 of revenues, though, are miscellaneous charges which will not be increased. Subtraction of these unaffected miscellaneous revenues yields a revenue pool of $5,953,837 to be increase at the rate of 18.71%. This percentage is applied to the late payment fee revenues of $47,848, an increase of $8,952. This leaves $1,104,979 to be collected from the remaining $5,693,787 of pro forma revenues. As the WICA surcharge will be reduced to zero, the $1,104,979 must be increased by the pro forma WICA revenues $212,202 to $1,317,181. The required increase of 23.13% is applied to all non WICA rates. The resultant rates produce the proposed revenue requirement within $33 due to rounding.

Q. Has the Company proposed any other revisions to its Tariffs?

A. Yes, changes to the Company's tariffs have been proposed relating to 1) wording modifications, and 2) two newly proposed charges.

Q. Please discuss the wording modifications?

A. First, on the proposed First Revised Page 6, under item 25, the Company proposes to strike the words "in writing", which will allow for termination of service without formal written correspondence. Additionally, on the proposed Third Revised Page 13, the Company has modified the language regarding the billing of seasonal customers to provide better indication to customers that billing for water consumption will be on a monthly basis, or as otherwise deemed appropriate.

Q. Please discuss the two newly proposed charges.

A. The Company has proposed a "Collect at the Door" charge for customers who wait to pay their bills until a technician arrives on premise to perform a shut off. The charge is intended to encourage customers not to wait until they are at risk for a termination before making payments as well as improve efficiency for our service personnel. This charge is not intended as a revenue generating mechanism, but rather as a deterrent for customers who unduly delay payment. The proposed fee of $44 is consistent with the Company's current turn on charge as it involves the same resource commitments.

The Company is also proposing a "Missed Appointment Fee" to reflect the costs associated with scheduling and committing resources to a service appointment which the customer fails to be available for. Similar to the collect at the door fee above, the charge is intended to foster good customer behavior and increased service efficiencies. The fee is proposed at $44. Again, the proposed fee of $44 is consistent with the Company's current turn on charge as it involves the same resource commitments. Because the Company does not expect to generate material revenues from either of these charges, it has not reflected any such amounts in its rate design.

VII. WATER INFRASTRUCTURE AND CONSERVATION ADJUSTMENT (WICA)

Q. Please provide some background on the existing WICA program.

A. The Company's existing WICA program was approved as a pilot program as part of its last rate case in DW 08-098. WICA was implemented to assist the Company in systematically replacing its aging infrastructure in a timely and cost-effective manner. The WICA, which is similar to the Distribution System Improvement Charge ("DSIC") that has been implemented in a number of states, was intended to increase system reliability, improve service to the customer, and reduce water lost due to leakage.

Q. Which other states participate in a WICA or DSIC program?

A. There are currently 11 states (inclusive of New Hampshire) which have approved a WICA or DSIC program. Refer to Attachment TMD-2 for the complete listing and brief description obtained from the website of the National Association of Water Companies ("NAWC").

Q. Has the National Association of Regulatory Commissioners ("NARUC") taken a position in regard to this type of surcharge mechanism?

A. Yes. On February 24, 1999, NARUC sponsored a resolution whereby they cosponsored and endorsed the DSIC that was approved by the Pennsylvania Public Utility Commission and the Pennsylvania legislature as a promising and unique regulatory approach that encourages the acceleration of needed remediation of an aging water utility infrastructure. The NARUC resolution is attached as Attachment TMD-3.

Q. Please describe the WICA program as adopted by the PUC?

A. The WICA surcharge is based on capital spending for an identified list of eligible projects. It is calculated as a percentage, based on the original cost of completed approved projects, multiplied by the last allowed rate of return, grossed up for income taxes, associated depreciation, and property tax expense, and divided by the total retail water revenues approved in the most recent filing for the regulated activities of the Company. Eligible projects include those that are intended to improve or protect the quality and reliability of service to customers including: replacement of mains, valves, services, meters and hydrants; main cleaning and re-lining projects; relocations that are non-reimbursable; purchases of leak detection equipment; and the installation of production meters and pressure reducing valves. The terms of the WICA filing were outlined in the settlement agreement adopted by the Commission in the Company's last general rate case. A copy of those terms is provided as Attachment TMD-4 to this testimony.

Q. Please summarize the Company's WICA filings to date.

A. The Company has submitted three WICA filings to date.

On October 30, 2009, the Company filed its three year, 2010-2012, list of projects with the Commission. By Order 25,065 dated January 15, 2010 in DW 09-211, the Company's proposed 2010 projects were approved and its 2011 projects were approved on a preliminary basis. The 2012 projects were provided for informational purposes only.

On November 1, 2010, the Company filed its three year, 2011-2013, list of projects with the Commission. The petition also requested approval of a WICA surcharge for projects completed between January 1, 2010 and September 30, 2010. By Order 25,186 dated December 22, 2010, the Company's proposed 2011 projects were approved and its 2012 projects were approved on a preliminary basis. Additionally a WICA surcharge of 1.5715% was authorized effective January 1, 2011 to enable the Company to recover the costs associated with the 2010 projects.

Finally, on October 27, 2011 the Company filed its three year, 2012-2014, list of projects with the Commission. The petition also requested approval of a WICA surcharge for projects completed between October 1, 2010 and September 30, 2011. By Order 25,311 dated December 30, 2011, the Company's proposed 2012 projects were approved and the 2013 projects were approved on a preliminary basis. Additionally the WICA surcharge was increased to 3.7269% effective January 1, 2012 to enable the Company to recover the costs associated with the cost of projects completed through September 30, 2011.

Q. Has the WICA filing achieved its intended objectives?

A. Yes. The Commission order reflected the purpose of the WICA program, stating:

> In support of the program, the **OCA** testified that the WICA may help to delay future rate cases, address needed non-revenue producing asset additions on a timely basis, have limited rate impact, and would include the parties in the review process before the dollars are actually spent. Order at 15-16.
>
> **Aquarion** testified that due to the need to replace a considerable amount of infrastructure, it is consistently and significantly under-earning on its return and that the WICA is one way to continue the replacement of aging infrastructure and allow Aquarion to receive a timely return on its investment. Order at 16.
>
> As a pilot program, **Staff** testified that it is interested in seeing whether the program provides the incentive necessary to increase Aquarion's rate of infrastructure replacement. Staff testified that it believes that, under the WICA process, the Commission will have greater oversight of projects for Aquarion, including more review and debate concerning priorities. In addition, the WICA charge is expected to mitigation rate shock between rate cases, which will benefit ratepayers by making rate increases more gradual. Order at 16 (citations omitted).

In approving the WICA pilot, the Commission stated:

> The WICA program appears to strike a reasonable balance between reducing rate shock to customers at the time of each rate case and providing an incentive to Aquarion to accelerate needed infrastructure replacement. For these reasons, we will approve Aquarion's WICA proposal, as modified by the settlement agreement, on a trial basis. Order at 17.

The greatest benefit arising from the implementation of the WICA program has been the increased level of capital spending by the Company to address the problems associated with aging infrastructure that can enhance service reliability and quality and reduce unaccounted for water levels over time. Given the elimination of significant regulatory lag, the Company has significantly increased its spending over historical levels. Before WICA, between the years 2002 through 2009, the Company invested on average of approximately $879,000 annually in water mains, meters, services and hydrants, the major WICA-eligible plant categories. The average of the actual spending in 2010 and 2011 combined with the budgeted spending for 2012-2014 is $1,040,000, or an increase of over 18%. Additionally, as a result of the WICA program, the Company has seen an increase to its capital budget as a whole. In the Company's 2009 business plan, compiled prior to the approval of WICA, the Company's five year capital budget for 2009 through 2013 had average overall annual capital spending of $1,020,600. The Company's most recent five year capital budget for 2012 through 2016 had average overall annual capital spending of $1,822,600, an increase of 79% over pre-WICA levels.

In addition, as part of the WICA process, the Company presents three years of projects for informational and/or approval purposes. In DW 09-211, the OCA, the Towns of Hampton and North Hampton, and the North Hampton Water Commission were all participants and had the ability to provide input into the Company's planned capital spending for the upcoming three years. The Towns of Hampton and North Hampton and the North Hampton Water Commission also participated in DW 10-293, and the Town of Hampton again participated in DW 11-238. Through the WICA process, combined with the Company's existing advisory groups and other public forums, key stakeholders have been afforded numerous opportunities to provide input, advice and suggestions related to the capital spending of the Company.

With regard to the timeliness of recovery, assuming the Company files a general rate case every three years (which has been its practice), on average the Company would be required to wait fifteen months to recover the cost of its infrastructure investments. With WICA surcharges being revised potentially every twelve months, recovery of WICA eligible investments occurs on average after six months from when the assets are placed in service. This represents a significantly shorter lag from the traditional ratemaking model utilized in New Hampshire and provides incentive for increased capital spending. Moreover, while the proposed rate increase in this case is 18.3%, the increase would have been 22.8% in the absence of the WICA surcharges.

For all of the reasons above, the Company urges the Commission to continue the WICA program indefinitely so that the Company can continue making much needed infrastructure improvements at accelerated levels.

Q. Please comment on the ability of WICA to delay rate cases.

A. As was discussed previously, this rate case was driven primarily by increased expenses and property taxes combined with reduced usage. Absent those drivers, the Company would not have had to file a rate case until the point at which the WICA surcharge reached the 7.5% maximum and would have required a rate case to reset the WICA surcharge. As long as expenses and property taxes continue to increase, rate cases will be needed at regular intervals, almost without regard to the level of capital spending. The Company continues to believe that it will file rate cases on a three year cycle, but the WICA will certainly mitigate the level of the increases required.

VIII. WICA AND PROPOSED STEP INCREASE

Q. When will the WICA surcharge be reset to zero?

A. The WICA surcharge will be set to zero with the implementation of permanent rates because the amount being collected through the surcharge is expected to be folded into base rates.

Q. When will the Company make its next WICA filing?

A. The Company's annual WICA filing is scheduled to be submitted on or before October 31, 2012. The filing will include investment from January 2012 through September 2012, which is not included in the Company's filing in this case. It is likely that an order on the Company's 2012 WICA filing will come prior to an order regarding permanent rates in this case. The WICA surcharge is expected to be implemented on January 1, 2013. The Company proposes that the revenue requirement for the WICA surcharge be added to the revenue requirement determined in this case effective as of the date new permanent rates are implemented and the WICA surcharge percentage be reset to zero. The amount of the WICA surcharge that is included in base rates would not be part of the permanent increase that is reconciled with temporary rates. The Company believes this would be an effective means by which to continue the WICA process uninterrupted through the rate case proceeding.

IX. DEFERRAL EXPENSE REQUEST

Q. Does the Company have any other proposals it wishes to make?

A. Yes, as addressed in Schedule 1O of my testimony, the Town of Hampton has assessed a new right of way tax. This assessment was approved in April of 2011 and allocated to the five public utility companies serving the Town of Hampton. This tax is separate and apart from the property taxes that the Company normally experiences. Instead of being based on the value of property owned by the Company, it is based loosely on the extent to which the Company's mains require use of the town's public rights of way.

Q. Does this new tax represent a significant financial impact to the Company?

A. Yes, the tax represents nearly 17% of the Company's test year net income. While the Company continues to invest in infrastructure, new and significant costs such as the right of way tax hinder the Company's ability to make these investments.

Q. What ratemaking treatment is the Company proposing to address this problem?

A. The Company has included the right of way tax as a part of its overall revenue requirement on a going-forward basis. In addition, the Company is requesting authorization to treat the obligation to pay the tax assessed to the Company at the end of 2011 as a deferred asset along with the amount relating to 2012 until temporary rates are granted and to amortize the total over three years. Assuming that temporary rates are authorized and become effective as of July 1, 2012, the deferral would be for 15 months of the tax. The amortization expense has been included in the Company's proposed revenue requirement (see Schedule 1O). The Company has not yet paid the tax, and if the Company's efforts to have it abated or abolished are ultimately successful, it proposes to reconcile the amount collected from customers with the amount it is ultimately obligated to pay.

Q. Mr. Dixon, does this conclude your testimony?

A. Yes, it does.