STATE OF NEW HAMPSHIRE

PUBLIC UTILITIES COMMISSION

May 24, 2013 - 1:08 P.M. Concord, New Hampshire

DAY 2 AFTERNOON SESSION

RE: DW 12-085
AQUARION WATER COMPANY OF NEW HAMPSHIRE, INC.
Notice of Intent to File Rate Schedules
(*Hearing regarding permanent rates*)

PRESENT:

Chairman Amy L. Ignatius
Commissioner Michael D. Harrington
Commissioner Robert R. Scott

Clare Howard-Pike, Clerk

APPEARANCES:

Representing Aquarion Water Co. of N.H.
Patrick H. Taylor (McLane, Graf...)
Steven V. Camerino (McLane, Graf...)

Representing Town of Hampton, N.H.:
Mark S. Gearreald, Esq.

Representing Town of North Hampton, N.H. and its Water Commissioners:
John J. Ratigan, Esq. (Donahue, Tucker...)

Representing Residential Ratepayers:
Rorie E. P. Hollenberg, Esq.
Stephen R. Eckberg
Office of Consumer Advocate

COURT REPORTER: Susan J. Robidas, LCR/RPR No. 44

APPEARANCES (CONT'D)

Representing PUC Staff:

Marcia A. Brown, Esq.
Mark Naylor, Director/Water & Gas Div.
Jayson P. LaFlamme, Water & Gas Div.
Robyn Descoteau, Water & Gas Div.

I N D E X

AFTERNOON SESSION

CHAIRMAN IGNATIUS: We're back on the record after the lunch break. Thank you everyone for being very prompt.

So, Mr. Parcell is on the stand, and we now have cross-examination from the Company.

Mr. Camerino.

MR. CAMERINO: Thank you.

EXAMINATION

BY MR. CAMERINO:

Q. Good afternoon, Mr. Parcell.

A. Good afternoon.

Q. You mentioned on your direct examination that you've written a book on cost of capital. I wanted to ask you just very briefly about that.

The last edition was 2010?

A. That is correct.

Q. Could you tell us who wrote the Forward to your book?

A. Ms. Ahern. A very nice one, I might add.

[Laughter]

A. A good friend of mine, I also might add.

Q. Would you agree that if a utility is an efficient and economically managed utility, it should be allowed to -- it should be able to earn its allowed return over time?
A. I didn't quite hear you.
Q. There's a lot of background. I'm sorry. And I actually don't want to trick you here.
I'm looking at Page 4, Line 10 of your testimony.
A. Okay.
Q. And what you said there is that, if a utility is an efficient and economically managed utility, it should be able to earn it's allowed return over time. I just wanted to confirm that.
A. It should have the opportunity to, yes.
Q. But that over time, if it's well managed, it should actually be able to earn it over time. Maybe not in any given year, but let's say on average. That's the whole point, is that it should be able to earn the return that's authorized. Not be guaranteed it, but it should be able to achieve it.
MR. GEARREALD: Just objection.

I think it says "will be able to maintain," not that it "should be able to maintain," if we're reading it.

CHAIRMAN IGNATIUS: Thank you.

(By Mr. Camerino)

Q. I'm not trying to quote it. I'm trying to ask you about the concept.

A. I understand your question. I'm hesitant to agree with that, because the corollary is if a company is not earning its authorized return, by definition, one might conclude the company was imprudent, and I'm not willing to say that.

Q. Well, actually, that is connected to part of what I'm asking you. One reason that a company can't earn its allowed return is it's not well managed; right?

A. It's what?

Q. Is that it is not well managed.

A. That could be an option, yes.

Q. Okay. But another reason might be that there are some other things happening that it is not able to manage beyond, such as reductions in consumption that are not reflected in the way the rates were set, or increases in expenses that go beyond what a well-managed utility can control.

A. I agree with that, yes.

Q. So if it is well-managed and it's not imprudent, it should, over time, be able to earn the return that's authorized by the Commission.

A. The way your question is stated, the answer is yes. But I don't know what your definition of "well managed" is. I don't know how we would measure that. But conceptually I agree with you.

Q. Okay. So if a well-managed utility consistently can't earn its authorized return, wouldn't that indicate some increased investment risk for investors?

A. It might or might not.

Q. Well, why are you qualifying it?

A. Well, you've got to understand, as I'm sure you do understand, that the role of regulation is to provide a balance between the interest of its ratepayers, the company's ratepayers, and its stockholders. And one of the items you mentioned was a reduction in usage. Well, if you have a reduction in usage and you pile on more cost to ratepayers, that's on the balance side of ratepayers. If you give it all to the stockholders, then you do it at the expense of the ratepayers. So if a utility commission is going to do its proper balancing act, you've got to consider both. And sometimes if you consider both, you may not expect to earn the authorized return over time. You may not under certain circumstances because of the balancing procedure.

Q. Well, the return that we're setting, isn't that in fact the return that the Commission is attempting to determine is demanded by investors?

A. Yes. By definition, yes.

Q. And so if the investors routinely can't earn the return that they demand, are they going to keep investing?

A. Well, that has been the case for many utilities over time. So I guess the answer is yes.

Q. Relative to other utilities -- in other words, if they can get the return elsewhere with an investment of similar risk, are they going to put it in the utility that's not earning the return that they demanded?

A. And investor will put his or her money where they expect to get a risk-adjusted rate of return, which would be in the case of dividends received in the DCF context.

So, in a low-interest rate environment, investors are concerned about dividends and put a lot of money in utility stocks over a couple years because of that. So there are other factors that go into why an investor would make a decision to invest in a utility or any other company other than that, as we've seen over the last couple years.

Q. Fair enough. So what you're saying is the ability to receive a dividend is a very significant part of what attracts that investment.

A. I would say for an investor, that's true. If you buy a stock, a publicly traded stock that's in the utility industry, you would do so, in significant part, I would define, for the dividend yield, maybe more so for industrial stock.

Q. And so if you were a investigator in a utility stock, and you saw that the company that you're thinking of investing in couldn't pay a dividend for three years in a row, that would have a pretty big impact on your perception of risk, wouldn't it?

A. You say "couldn't." "Couldn't" or "didn't" are two different things.

Q. Okay. Did not.

A. Well, if you did not, the question is: Why did it not? Did it not do so because it could not, or did it not do so because it chose to not receive a dividend from the parent, as opposed to making an equity infusion from a parent down?

So I guess there's two ways for a parent company to put stock in a subsidiary. One is to slow the dividend growth from the subsidiary to the parent, and the other is to keep the dividend and then place money and send it back down to the subsidiaries. So there's two ways to do it, with essentially the same result.

Q. Suppose that same utility that hadn't paid a dividend for three years also had steadily declining earned returns and declining retained earnings? Would that indicate a significant increase in risk to equity investors?

A. If you had a stand-alone company that couldn't pay dividends -- could not, you say?

Q. I said "did not."

A. I don't want to -- okay.

If you had utility, a stand-alone utility that did not -- sorry about that -- did not pay dividends, chose to, and at the same time retained earnings was declining, by definition, that implies that the company was losing money; otherwise, retained earnings would not be going down. And losing money over time would certainly not be a desirable situation.

Q. And suppose that the same utility had an increasing equity ratio -- sorry -- debt ratio over that time. Just hold that assumption for the moment. If it had paid a dividend, all things being equal, the debt ratio would have actually become higher; correct?

A. Well, we need one more assumption; and that is, the parent who helps control the capital structure of the subsidiary, at the same time that the parent implied or indicated to sell more debt also indicated we're not going to put in more equity into it. For both of those, yes. The answer is yes.

Q. And the parent is, in fact, in this case, the shareholder whose investment we're trying to attract and who's assessing the risk of that investment; correct?

A. Say that again, please?

Q. You said that that assumes that the parent hasn't put in more equity.

A. Yes.

Q. So the debt ratio will go up because --

A. You sold debt. The debt ratio goes up because you sold debt.

Q. You needed that debt because you didn't have sufficient internally generated equity, and you didn't bring it in from the outside; correct?

A. That's correct. Those two reasons, yes.

Q. And the opportunity to bring it in from the outside is to bring it in from the shareholder whose investment we're trying to attract.

A. In a generic sense, yes. In this case, it's not who the shareholder is, because there's so many tiers of ownership, and none of which are publicly traded, but in a conceptual shareholder sense, yes.

Q. Ultimately, that entity may itself have shareholders, but there is outside capital we're trying to bring in.

A. That is correct. Or at least internal capital from other sources. One of the two.

Q. But eventually, the managers of the utility or its parent, or the parent of that, are responsible to some shareholders to demonstrate that they got a return for the investment that they made; correct?

A. You just said "managers"; right?

Q. People operating the utility.
A. Yeah, that's right. Answer is yes.
Q. Okay. All things being equal, would you agree that a company that has a higher debt ratio is a riskier place for equity investors to put their money?
A. All other things equal, which would include the ownership structure, yes. All things equal.
Q. And on -- in your prefiled testimony, on the -- you have a chart of the debt ratio -- I'm sorry -- the equity ratios of your proxy group that's on Page 12.
A. Yes, I do.
CHAIRMAN IGNATIUS: Are you on the direct or the --
MR. CAMERINO: I'm on the direct, which, for the record, is Exhibit 13.
A. Yes, I do.
(By Mr. Camerino)
Q. So at the bottom of the page there, those ratios are equity ratios -- meaning, if we took 100 percent minus the number there, we would see what the debt ratio is.

So, for ease of reference, the 2009 figure would be 51 percent debt; is that correct?

A. Assuming no preferred stock, yes.

Q. Okay. So, the highest in those five years, the highest amount of debt is 53 -- 54 percent debt in 2010?

A. That is correct.

Q. And is it a fair statement, just looking at that, and based on my -- well, is it a fair statement that, to see a 50 percent debt level, even a 55 percent debt level for a water utility, is a fairly typical debt ratio in the industry?

A. Yes. I would say that the typical operating water utility in a rate case is about 50/50. Yes.

Q. Okay. And so, if a utility came in for a rate case and had a 50 percent debt ratio, even a 55 percent debt ratio, it would be -- usually that would just be used in the capital structure for purposes of determining the overall rate of return. There wouldn't normally be -- that wouldn't be considered imprudent, or it wouldn't be an imputed cap structure used; is that fair?

A. I think you're assuming it's the company's actual per-book capital structure, utilities.

Q. I want to ask you a few questions about your CAPM results.

A. Sure.

Q. If I understand your testimony, you're saying that a 6.1 percent return on equity is a reasonable return on equity, based on your CAPM methodology?

A. I wouldn't go that far. What I'm trying to convey here is that 6.1 percent return from CAPM is one factor investors would consider in deriving an expected return from a utility. In fact, I wouldn't recommend 6.1. But I think 6.1 is a factor that in the current environment an investor would consider as an alternative measure of capital costs.

Q. I guess I'm a little confused. Do you think 6.1 percent return on equity is sufficient to attract capital?

A. No, and I'm not recommending that.

Q. Okay.
A. But I -- well, I've said what I said.
Q. And in your methodology, though, you gave that 6.1 percent return equal weight.
A. Correct. One-third weight. That's right.
Q. Okay. I'd like to ask you some questions about your DCF methodology now.
A. You said "DCF"?
Q. Yes.
A. Yes. Sure.
Q. If you look at Page 19 of your testimony --
A. Yes, I'm there.
Q. -- you say -- you start with a range of 8.3 percent to 9.6 percent, and you say that's the current DCF-derived cost of equity for the proxy group. Do you see that?
A. Yes. In my judgment, yes.
Q. But again, as to what you would recommend using DCF, your recommendation would be in the 9.0 to 9.6 percent range?
A. That is correct. I took the high end of the range.
Q. And as you said earlier, you actually used a similar methodology to Ms. Ahern, so that at

the end of the day -- and thankfully for --
A. Similar results --
Q. -- yeah, everyone in the room --
A. Really the same way, similar results.
Q. One second. I'm going to try to skip over a bunch of questions about areas where you have differences.
A. Okay.
Q. But there's a lot of ink spilled in Ms. Ahern's testimony and yours about your methodologies on DCF. But your testimony is that the Commission doesn't really need to pay that a lot of mind. There may be credibility issues or things like that. But end results-wise, you and she, in your DCFs, come out to a similar range. Is that -- unadjusted. Is that a fair statement?
A. Well, not exactly how I would express it. But you're close.
Q. I am trying to skip over a bunch of --
A. Everybody, including me, likes that.
Q. I want to incentivize it.
Okay. And so now I'm going back to your overall ROE recommendation.

So you reach that result by taking three different methods -- your comparable earnings and your DCF and your CAPM -- and you average them; is that correct?

A. That is correct.

Q. So that each get equal weight.

A. That is correct.

Q. And again you treated the CAPM on a par with the CE and DCF; is that correct?

A. That is correct.

Q. Do you think it's important for an expert witness to have consistency in how -- the methodology that they use from case to case?

A. I do. And I recognize in this case, by using the CAPM results, which I've not done in a few years, that you might think I'm being inconsistent. But as I state in my testimony, I've been watching these low rates, low interest rates for, four or five years thinking they're temporary, and they're not temporary. They're still here. So it's time to move on and recognize the obvious.

But yes, I think in general it's important to be consistent.

Q. So, as part of that consistency, in every case you used those three methodologies; right?
A. Say it again?
Q. As part of being consistent, in every case you use those three methodologies, at least for water cases.
A. At least I show calculations for all three, yes.
Q. And I'm going to show you excerpts from your testimony in a few other cases. And I could ask you if you recall them, but I think what I want to do, to move it along again, I'm going to give you excerpts with the actual numbers.
A. Sure. That's fine.
Q. I'm going to hand these all out at once. I'm going to give you these one at a time; otherwise, I'm going to confuse myself.

(Atty. Camerino hands document to witness.)

Q. So this is an excerpt in your testimony in a Pennichuck Water Works rate case in 2007. And you see the figures that are --

A. You're telling me that; right?
Q. Excuse me?
A. You're telling me that; right?
Q. Yes.
A. If you're representing this is 2007, I'll accept that. This doesn't show that.
Q. Yes. Actually, let me say something about that.

MR. CAMERINO: I have complete copies of the testimonies that I'm showing Mr. Parcell excerpts from, and I'd be happy to share those, particularly with Mr. Gearreald, to make sure that they are what I'm representing. But I didn't want to make 10 copies of each of the testimonies that I'm going to go through. So whether he wants to see them now or at some point just to check, I'm happy to handle it however he or the Commission would like to do.

MR. GEARREALD: Well, if you're going over them one by one, I'd like a complete copy.

MR. CAMERINO: Okay.

(Atty. Camerino distributes copies.)

(By Mr. Camerino)

Q. So what this is, I will represent to you, it's an excerpt from your testimony in the 2007 Pennichuck Water Works rate case. And you see those three results from the same methodologies that you had in this case?

A. Yes.

Q. And if you look at the last line, your recommendation includes -- it is essentially the same as your DCF range; correct?

A. Well, it's all the ranges combined.

Q. I understand that. But I want to take this one step at a time.

A. Sure.

Q. But it includes your DCF range.

A. It certainly does, yes.

Q. And it includes your comparable earnings result?

A. Right. That's correct. Uh-huh.

Q. It does not include the entirety of your CAPM M result; correct?

A. No, it does.

Q. Oh, this one does?

A. Yes, yes.

Q. Okay. This includes all three.
A. Yeah.
Q. They're all in that range.
A. They're all in there, yes.
Q. So you included them all; right?
A. That's correct.
Q. Okay. The next one I want to show you is the Pennichuck case from 2009 that you were just referring to.
A. Okay.
Q. And if you look at the last line of that testimony --

MR. GEARREALD: I'm sorry, Steve. Do you have the whole one?

MR. CAMERINO: Oh, I'm sorry.

CHAIRMAN IGNATIUS: We're going to take a paper towel break for a second. It wouldn't be a water case without it.

(Pause in proceedings)

(By Mr. Camerino)
Q. All right. So if you look at the last line of that page --
A. Sure.
Q. -- you recommend a cost of equity rate of 9

to 10 percent. Do you see that?
A. I do, yes.
Q. And that, again, is the same as your DCF range?
A. Includes, yes, all of the DCF range.
Q. And it includes your comparable earnings results?
A. It does.
Q. It does not include the CAPM range, other than the high end; right?
A. That's right. It just includes the high end of the CAPM range. That's correct.
Q. Okay. The next one I want to show you is an excerpt from a 2011 United Water case.

(Atty. Camerino distributes document.)

CHAIRMAN IGNATIUS: As you're passing those out, Mr. Camerino, is it your intention to mark all of these?

MR. CAMERINO: I think that might be a good idea.

CHAIRMAN IGNATIUS: Why don't we go ahead. The first one was the 2007 PWW rate case excerpt which will be marked as Exhibit 28 for identification.

The second one, the 2009 PWW rate case, will be 29 for identification.

(Exhibits 28, 29 marked for identification.)

(By Mr. Camerino)

Q. Okay. And so, looking at the United Water excerpt, Page 25 --

MR. GEARREALD: I'm sorry, Steve. Do you have a full copy?

MR. CAMERINO: Oh, yeah. I'm a slow learner.

(Atty. Camerino hands document to Atty. Gearreald.)

MR. HARRINGTON: What was the date of the United one?

MR. CAMERINO: The testimony is dated August 5th, 2011.

(By Mr. Camerino)

Q. And in that case your DCF was 9 to 10 percent?

A. Yes.

Q. Your comparable earnings was 9-1/2 to 8-1/2 percent?

A. What did you say?

Q. I'm sorry. Your comparable earnings was 9-1/2 percent to 10-1/2 percent?
A. That's correct. Yes.
Q. And in that case, your CAPM was lower than any other cases. It was down to 8.1 to 8.2 percent?
A. That is correct.
Q. And in that case, you took the midpoint of your DCF and comparable earnings ranges; right?
A. That is correct.
Q. You did not average in the CAPM.
A. That is correct.
Q. Okay. And you had a recommended range of 9-1/2 to 10 percent, with a midpoint of 9.75 percent?
A. That is correct.
Q. And that range was the same as the midpoints of your DCF and comp earnings ranges; right?
A. That is correct.
Q. So it doesn't include your CAPM range.
A. That is correct.
Q. And then we get to a case in 2012, New Jersey American Water?

A. Hmm-hmm.
Q. Show you Page 24 from that case.

(Atty. Camerino distributes copies.)

MR. CAMERINO: And just for the record, this is a double-sided document. The numbers are actually on the back of the page.

CHAIRMAN IGNATIUS: We'll mark the United Water one as Exhibit 30 for identification, the 2011.

And then 32 would be the -- I don't actually know what it is yet. So I'll let you get that out first.

MR. CAMERINO: So the New Jersey American Water is 31?

CHAIRMAN IGNATIUS: I'm sorry. I just got that wrong. So, 31 would be New Jersey American Water. And what's the year?

MR. CAMERINO: 2012.

CHAIRMAN IGNATIUS: Thank you.

MS. HOLLENBERG: Excuse me, Commissioner. I think 30 is 2011 United Water, and 31 is 2012 New Jersey.

CHAIRMAN IGNATIUS: Let's go through them again.

So, 28 should be PWW, 2007; 29 should be PWW, 2009; 30 should be United Water, 2011; and 31 should be New Jersey American Water, 2012.

(Exhibits 30, 31 marked for identification.)

MR. CAMERINO: I agree.

(By Mr. Camerino)

Q. All set Mr. Parcell? I'm going to ask the next question.

A. Yes, yes. Please do.

Q. So, looking at that New Jersey American Water case, in that case the DCF range is 9.0 to 10.0; correct?

A. Yes. Uh-huh.

Q. And the comparable earnings is 9-1/2 to 10-1/2; correct?

A. Yes, it is.

Q. And the cap M has dropped further, to 6.8 percent?

A. That is correct. Yes.

Q. And in that case, you also took the midpoint of your DCF and comparable earnings ranges; right?

A. Right.
Q. You did not average in the CAPM.
A. Right. But as you can see in the next question and answer right below that, I have reference to "Why?" Yes.
Q. Yes. And you actually have an answer in this case as well to the same question; correct?
A. That's right. On a continuing basis, these low interest rates have proved not to be temporary. So I think it's proper to bring CAPM back into play.
Q. And by the way, your CAPM dropped over the course of five months from the New Jersey -- between the New Jersey and the Pennsylvania cases. It dropped from a range of 8.1-8.2 to 6.8 over five months?
A. I don't have the time period as to what years they are. So if you represent the dates, I'll accept that, no problem, if you have it.
Q. I'm actually going to -- so I don't have to represent it, I'm going to actually read it to make sure.
A. I'll accept that, no problem. I believe you.
Q. Well, the United Pennsylvania case, the

testimony is dated August 5th, 2011.
A. Hmm-hmm.
Q. And the New Jersey case, the testimony is dated January 13, 2012.
A. Good enough. Thank you. I'll accept that.
Q. So the CAPM dropped significantly during those five months.
A. It did. Yes. Uh-huh.
Q. And in the current case, the DCF and the comparable earnings ranges that you have, they're relatively close to the ones that are in the New Jersey case; right? They've dropped a little, but they're in that same area?
A. They are.
What I don't know, as I sit here, is whether the New Jersey case, my DCF results reflected the top end of the range like they do in this case. They might not. I just don't know.
Q. So you're following the same approach in each of these cases. But in those cases, when the CAPM was outside of the range of the DCF and the comparable earnings, you did not include

it in your recommendation; correct?
A. That is correct, because I thought it was a temporary phenomenon and it should be ignored in a temporary sense. Yes, that's correct.
Q. Now, in this case, you're giving it equal weight, and you're telling the Commission you do not think that that number would be a reasonable return to authorize for this utility because it would be insufficient to attract capital; correct?
A. By itself, yes. But it's a consideration that investors would take into consideration when they make their investment decisions in price stocks; therefore, establish cost of equity model results, yes.
Q. And is it a fair statement that the numbers in the other ranges you do consider to be reasonable cost of equity to authorize for the utility?
A. You mean Exhibits 28, 29 and 30, the other cases? Is that what you mean?
Q. Well, let's focus on this range. The ranges that you give, those are a range of reasonable outcomes; correct?

A. Oh, you mean ranges of other methods as opposed to other companies.

Q. Yes.

A. I'm sorry. I do get what you're asking now. Yes. The answer is yes.

Q. Okay. I want to ask you some questions about capital adjustment mechanisms.

A. Capital adjustment mechanisms.

Q. Yes. And actually, the first thing I want to do is get us on the same plane as to what a capital adjustment mechanism is.

A. That's a great idea.

Q. Okay. So I'm using the term to mean that it's a mechanism by which regulators adjust rates annually for specific types of capital additions. An example might be a main replacement program or some kind of other infrastructure replacement program.

A. Okay.

Q. Does that make sense to you?

A. Yes. I understand what you're saying.

Q. And so WICA, in that parlance, I would include in what I'm talking about as a capital adjustment mechanism. Does that make

sense?
A. Yes.
Q. When you look at your proxy group, can you tell me what capital adjustment mechanisms the nine companies have?
A. No, I did not address that or WICA in my testimony. WICA never appears in my testimony.
Q. I know that. But I'm not just asking about WICA.
You have nine companies. And presumably they have somewhat different regulatory situations. They may have different types of adjusters that are allowed or not allowed in their jurisdiction; correct?
A. I mean, it's so diverse. You may have a holding company, like United Water, that has multiple subsidiaries in the same states, plus subsidiaries in multiple states. So, I mean, I think American Water Works is in 22 states.
Q. Some of them have purchased water adjustment mechanisms; right?
A. And purchase power adjustments. But I've

never seen a study that lists everything for each subsidiary.
Q. And some of them might have WICA adjustments; right?
A. They might. I don't know.
Q. And some of them -- the same might be true for your gas group, for that matter.
A. I'm sorry. I missed the word.
Q. The same might be true for the gas companies you looked at. Some of them may have main replacement programs that they come in every year and get an adjustment for; right?
A. Or decoupling, yes.
Q. Or decoupling.
And you didn't look at that when you looked at the proxy group; right?
A. That is correct. I took the proxy group as a whole for all the companies in all the jurisdiction as a whole as opposed to a micro approach.
Q. Well, isn't it pretty important to know what mechanisms they have? I mean, is there some reason you didn't look at each company in the proxy group to see what mechanisms they had?

A. Well, let me just answer that in the nicest possible way. My client and me are not the Applicant here. I was hired to comment on the Company's case and provide analyses. And if those analyses were not in the Company's case, I don't see why -- answering this as nice as I possibly can -- I don't see why that burden would shift to me.

Q. I'm not asking about a burden. I'm just asking you about whether -- maybe it's the case that knowing what those mechanisms are isn't important. That's what I'm trying to understand.

Is knowing what mechanisms these companies have, is that not important because it's a proxy group? Is there something about it?

A. Well, it is a little bit and it's not. It's something on an overall risk standpoint. But when you consider a proxy group and you look at their security ratings and their debt ratings, and you see what the overall risk is and you compare -- you use that to develop a cost of capital for your subject company, like Ms. Ahern says, it's the Prego model. It's in there. That's the other side of the coin, I guess.

Suppose you had a company that did not have something like that at one point in time and suddenly got it. Then the relevant question is: How does that new regulatory mechanism impact that company? Or as we heard this morning, how does the fact that one company in this state may have it and the others do not, and the others have a certain stipulated rate of return. Maybe this company, because it has WICA, is different.

So there's a lot of aspects to that. But I have not explored that in my testimony. There's a lot of angles you could go to to get there, and not all with the same result.

Q. What I'm trying to understand is, when you pick a proxy group, if I understand correctly, these companies -- first of all, the companies you're looking at are actually made up of many subsidiary companies; correct?

A. In most cases, yes.

Q. And those subsidiaries have different types of mechanisms, and they're not all the same; right?
A. Definitely so.
Q. And the DCF method is based on taking that group of companies as a whole and coming up with a recommended return; correct?
A. That is correct.
Q. And because in this mix of companies there are various types of adjustment mechanisms, you don't make an adjustment for any specific one of them. Is that a fair statement?
You're not going in and saying these companies have purchased water adjustment clauses. I need to now adjust the results of my DCF for that.
A. Well, again, like I said in prior answers -- I'm going to try to keep this as brief as possible -- it depends on where you are. If a company is moving to an adjustment mechanism, the question is: Does this factor change the Company's risk prior to where it was before it got it?
Q. Well, who -- aren't you coming up with the

recommended return for the Company in this case? Aren't you doing that by reference to your proxy group? Not by reference to this company itself, but by reference to a proxy group. Isn't that how DCF done?

A. Yes. In fact, you asked me that in a data request, in which I responded that I made the implicit assumption that the overall risk to Aquarion of New Hampshire was the same as the proxy group.

Q. And that's how DCF is done; correct?

A. That's how my DCF is done and the way many DCFs are done, yes.

Q. So then, if an adjustment mechanism that the company -- maybe to keep it simple -- the Company for which you're trying to find the implied rate of return on equity, if that adjustment mechanism is already reflected in the proxy group, you certainly wouldn't adjust for it again; right?

A. Well, if you could demonstrate that the -- well, let me start over.

Let's just say, hypothetically, you determine that a proxy group subsidiary companies *in toto*, 57 percent of their revenues or plant were subject to some form of adjustment cost. You could conceivably compare that to the subject companies to see how that percentage related to the subject company and make some kind of adjustment. But you'd have to -- it requires a tremendous amount of data to do that because you've got to go into each company almost to see their tariffs to determine how they work.

So, just because a holding company has a subsidiary in a state that has some kind of mechanism doesn't mean that mechanism is applicable the same as the one in your state. You just don't know. And some have none at all.

Q. And that's not an analysis you did in this case.

A. Nor have I seen anybody do it. I've seen it done somewhat for gas companies, but never for water.

Q. And so you've never seen anybody do it, and you yourself have never done it; right?

A. No, I have not.

Q. I take it you're familiar with the NARUC Resolution that Mr. Dixon testified regarding -- concerning the need for infrastructure replacement?
A. Are you referring to Ms. Ahern's testimony?
Q. I was referring to Mr. Dixon's testimony. I think it also was referenced in Ms. Ahern's testimony.
A. If that's the case, yes.
Q. I'm going to give you a copy, just so you have it in front of you.
A. Sure. Thank you.
MR. CAMERINO: Actually, if we could mark this. It may actually be...
CHAIRMAN IGNATIUS: Is it --
MR. CAMERINO: We don't need to mark this separately. This may just be easier for reference. But this document is apparently attachment TMD3 to Mr. Dixon's testimony.
CHAIRMAN IGNATIUS: That's correct. Is it the NARUC Resolution on Best Practices?
MR. CAMERINO: Yes, dated 2005, because I think there may be an earlier one.

CHAIRMAN IGNATIUS: So that's Page 100 of 171 in this green binder.

(By Mr. Camerino)

Q. And if you look at that -- you may already be familiar with this -- that indicates that a massive capital -- significant capital requirements are leading to need for some kind of additional ratemaking mechanisms for accommodations. Is that a fair statement?

A. I don't know if "need" is the right word, but it's suggested here that they're useful to the utilities. And they made a resolution that, as many as -- it's on the back page -- in their recommendation, economic regulators consider and adopt as many as appropriate of the regulatory mechanisms identified herein as "best practices," yes.

Q. Well, could you look at the big paragraph in the middle of the first page?

A. First page?

Q. Yeah, where it says "To meet the challenges..."

A. Yes.

Q. Isn't the purpose of the items that are listed to respond to what is viewed as a significant challenge in the water industry?

A. Yes, that's the background for the resolved.

Q. And one of those items, if you look down -- it's Item L -- it refers to a fair return on capital investments.

A. Yes.

Q. When you read that, does that imply to you a reduced return on capital -- a reduced return on capital investment, that in order to meet this challenge, regulators should give the utility a lower return on equity than they would otherwise give?

A. A fair return would take into consideration any risk or changes in a risk associated with the implementation of these. So, a fair return is fair as determined "fair" by the regulators, the individual regulators.

Q. I understand that.

When you read this context, is your understanding that, as a cost-of-equity expert, that in order to incentivize this additional investment, regulators should give a return on equity -- should authorize a return on equity that is less than they would otherwise have given?

A. Doesn't say that. It just says "fair." And if "fair" means less because of lower risk, then it qualifies as "fair."

Q. Let me ask it this way: If regulators told the Company, If you accelerate your investment in infrastructure --

A. Accelerate?

Q. -- accelerate your investment in infrastructure, one of the things we will do is lower your return on equity, do you think that's going to incentivize the investor to put more capital into a business?

A. It could.

Let me give you an example: I've been involved in electric cases where so-called "decoupling" was an issue. And in an attempt to get approval for decoupling, the utility offered a lower return on equity to account for lower risk. I mean, it's recognized in those cases that there is less risk associated with these regulatory mechanisms. And the utility itself came in suggesting a reduction in what the fair return would be because of that mechanism. So I've seen it done by utilities, even.

Q. Decoupling --

A. It's usually not enough, but it's done.

Q. Decoupling affects 100 percent of a utility's revenues, doesn't it?

A. Not 100 percent, but a lot.

Q. Very, very high percentage.

A. Yes. But, again, conceptually, that's what I'm talking about.

Q. Do you know what percentage of Aquarion's revenues are affected by the WICA?

A. No, because, as I said, WICA is a cumulative thing. I've seen reference to how much it is on a year-to-year basis. But I don't know. It would take -- I couldn't do it. But I've seen the number on an annual basis. It's not large.

Q. Give me your sense of it. Please give me your sense of it. Approximately what percentage?

A. Well, again, I haven't addressed WICA in this case. I've seen other witnesses who did.

I've seen some data request that asked to quantify it. But I don't recall what the numbers were because I was not addressing that issue. I could look through my files and find it if you'd like.

Q. If you have it, I'd be --

CHAIRMAN IGNATIUS: Mr. Camerino, clearly, you know what the percentage is. Why don't we provide that to him and let him comment on it.

(By Mr. Camerino)

Q. Let me represent to you that Mr. Dixon indicates it's approximately 1-1/2 percent per year. And I would ask you, on a break, if you want to do what you need to do to make sure you're comfortable with that representation, that would be fine.

MR. GEARREALD: I object. We have a chart that we submitted already through Mr. Welch which shows the various breakdown from year to year. And I believe there's a higher percentage between years 2011 and 2012 than 1-1/2 percent.

CHAIRMAN IGNATIUS: Mr.

Camerino.

MR. CAMERINO: I think what we'll do is we'll see if we can find a document that's in the record, and I'll move past it.

CHAIRMAN IGNATIUS: All right. Thank you.

(By Mr. Camerino)

Q. Bottom line on WICA revenues, though, is it affects a very small part of the total revenues of a company; correct?

A. The annual WICA portion would be -- I would assume so, yes. But like I said, I really don't know. I've not examined that. That's not even mentioned in my testimony.

Q. All right. But I'm asking you. WICA came up in a cost of equity context --

A. But you asked me a technical question on an issue I did not address. I'm sorry. I apologize. I can't argue with you. I apologize for saying that.

I don't know, because I did not address it.

Q. I want to ask you a few things -- I'm going to see if I can keep this short -- about your

response to Ms. Ahern's testimony.
A. Sure.
Q. And on Page 4, Line 29 of your rebuttal, you said that --
A. Page 4?
Q. Yes. I'll let you get there. Sorry.
A. Uh-huh.
MR. HARRINGTON: Exhibit 14?
MR. CAMERINO: It's Exhibit 14, yes.
A. You said Page 4; correct?
Q. Page 4, Line 29. You'll recall she expressed some concerns about the DCF model in her testimony, as to what happens when the market price is above the book price of the stocks. Do you recall that?
A. Yes. I am looking at a copy of my testimony that I printed off of my own computer. And Page 4, Line 29, there's a line in the middle of a question. I'm wondering if you're seeing a different format than I've got, because this is a single line from a question on my copy.
Q. I'm going to --

CHAIRMAN IGNATIUS: That's true of all of ours.

MR. CAMERINO: Is it? I've got a different... you are correct. Hang on.

(Pause in proceedings)

(By Mr. Camerino)

Q. Yeah, it's a question -- I'm sorry. Maybe I didn't phrase it well.

Your question says that she maintains, quote, "that the DCF model cannot be used as an estimate of the cost of equity for a utility when the market price of utility stocks exceeds the book value." Do you see that?

A. Yes, I do.

Q. That's your characterization of what she said; right?

A. That is correct.

Q. She didn't actually say that anywhere, that you can't use it, did she?

A. Well, I reference her Pages 14 to 16. I'll have to --

Q. Take a look.

A. If I misinterpreted, I would gladly apologize to her in person and in public and put in whatever is right.

Q. Well, and then on Page 5, Lines 1 to 2, you say, "To make a modification of the DCF cost rates, as Ms. Ahern proposes," --

A. Yes.

Q. -- "amounts to an attempt to 'reprice' stock values in order to develop a DCF cost rate more in line with what she thinks the results should be."

A. Yes, sir.

Q. If you look at her testimony, she didn't make any change to address the issue of market to book prices, did she?

A. No, but she says you can't use the results because of that. So if you can't use the results -- either you use them or you don't. If you don't, you should be making some change.

Q. In fact, she develops a DCF result and simply has noted that this is a problem with DCF. Is that a fair statement?

A. I'll agree with that, yes.

Q. Thank you.

A. I'll agree with that. Yes.
Q. Again, I'm not going to try to take you through every one of these. But if you look at Page 6 and 7 --
A. Six and seven? Sure.
Q. -- of your rebuttal testimony --
A. Yeah.
Q. -- I counted six times where you indicated that she says "investors rely only on earnings per share projections."
A. Yes.
Q. Can you tell me where she says in her testimony that investors look at only earnings per share projections?
A. What she says is that, in a DCF context, the only growth factor you need to consider is earnings per share projections. So if you're going to use that, you are assuming that's all that's important to investors. So that is the nexus.
Q. Would you take a look at Page 17 of her testimony?
A. Sure.
Q. Lines 4 to 8.

CHAIRMAN IGNATIUS: And this is Exhibit 8; is that correct?

MR. CAMERINO: That is correct.

A. I'm sorry. Page 17 again?

(By Mr. Camerino)

Q. Page 17, Line 8.

A. Line 8?

Q. Four to eight.

If you look at that, doesn't she say that the analysts' forecast take into account historical and current information?

A. Right. Therefore, you don't have to look at anything else. That's what she said.

Q. So the analysts already take into account all of the information that is out there; right?

A. That's what she says.

Q. And they come up with their projections.

A. That's correct.

Q. And so the projections reflect the analysts' sense of all of the data that's out there.

A. According to the analysts, yes. But that's still the analysts' opinion based upon other facts.

Q. And that's what you say investors do. They

look at all the information that's out there?
A. And form their own opinions, which are not exclusively related to earnings per share forecast. Yes.
Q. And analysts are investors; right?
A. Some are. Some are not.
Q. They're pretty sophisticated people who gather a lot of information; correct?
A. Some are. Some are not.
Q. They have access to probably more information than regular investors?
A. Who?
Q. The analysts.
A. Oh, the analysts? I'm sorry. We were talking about analysts. It's stockholders a second ago. In my mindset, your question was stockholders, and my answers were in that regard. I apologize for that.
Q. I think I'm confused now. Let me take a --
A. Shall I say it again?
Q. No, let me try --
A. Okay. Please. We'll get to it.
Q. Okay. Stock analysts look at all the available information in the same manner that

regular investors do; correct?

A. Maybe more so. Maybe not. But stock analysts have access to lots of information and presumably consider much of it when making their earnings per share projections. Yes.

Q. So the things you said about what investors do, that's what analysts do; right?

A. Individual analysts, yes. But the question is: Do investors only consider one analyst's number, which is earnings per share projections? And I say no.

Q. But if we took the analyst projections which already incorporate all the historical data, and then we factored in the historical data again, we would effectively be double-counting that historical data, wouldn't we?

A. Only to the extent that you can verify that analysts mathematically factored it in.

What I'm saying here, and I hope it's clear, is that a savvy, or even a non-savvy investor is not going to make his or her investment decision exclusively based upon earnings per share forecast of security analysts. That's what I'm saying.

Q. Do you know who are -- investors in utilities, those are often -- there's a lot of institutional investors?

A. Yes, sometimes.

Q. And they utilize those analysts' projections; right?

A. Or create their own.

Q. After considering all the data.

A. Sure.

Q. They come up -- a truly sophisticated institutional investor might come up with their own projection of earnings per share.

A. Right. And the question is: Is that the only factor they use when making the decisions?

Q. So it's your opinion that, say an insurance company that buys a utility's stock and comes up with its own earnings per share projection, after looking at historical dividends, would then give the historical dividends weight yet again, separate and apart from how it came up with the earnings per share.

A. No, that's not what I'm saying. I'm saying -- that's a good example, an insurance company.

An insurance company who's required by law and statute to put aside certain money for reserves to ensure that insurance ratepayers will have their claims paid has to go through a lot of due diligence to make sure they're making proper decisions. And I can't imagine an insurance department who would make decisions for common stocks based exclusively on earnings per share projections of the companies. I would be appalled to find that an insurance company that had a policy doing that, because that would be a very naive on their part and very dangerous for my money.

There are other factors to consider. I mean, projected growth and dividends. There's lots of things to consider. Doesn't have to be just historic earnings. But there's lots of data out there, and they look at all of it to make decisions to invest based upon all that, not just a decision to create their own earnings per share projections. That's the distinction.

Q. The retention growth -- retention is just the amount of money that the company holds -- earnings that it holds to itself after it pays out dividends; right?

A. Times return on equity, yes.

Q. And the dividend growth is the part of the earnings, let's say, that gets paid out over time; right?

A. Say again.

Q. The dividend is the part of the accumulated earnings that gets paid out over time; correct?

A. Correct.

Q. So if you're trying to figure out what you're retention growth and your dividend growth would be, you need to know what your earnings growth would be; right?

A. Yeah, but not just your earnings growth. But, yeah, that's one factor, an important factor. And I use that.

Q. You can't have retention growth or dividend

growth without earnings; right?
A. That's correct. But you use them all.
Q. And over time, they are going to match each other; right?
A. Not necessarily. They might.
Q. How could you have retention and dividends without the supporting earnings?
A. You said "match."
Q. Over time the earnings growth is going to need to be equal to the retention and dividend growth; right?
A. Well, retention rates change over time, as do earnings and dividend -- earnings growth and dividend growth don't grow in tandem.
Q. But over time they need to stay together because the earnings are the source of either the dividends that get paid out or the dividends that get retained; right?
A. There's certainly a relationship. For example: A lot of electric utilities who used to be -- found themselves as being diversified activities, such as merchant energy generation, once they went that route, they actually reduced their payout ratios

because of a more risky business, and in many cases they lost their shirts doing it. Going back to the utility model, they're increasing their payout ratio again. And Virginia Power is a classic example of that.

So they change over time, not just because of change in the earnings per share, but because of change in philosophies.

Q. I'm going to try a different topic here just briefly.

On Page 10 of your testimony --this is your direct.

A. Direct? Sure.

Q. You're discussing the situation in the market and investor expectation. You see that?

A. Yes.

Q. And to support your point that investor expectations are reduced, you've got a footnote. And that footnote refers to an article that says, "S & P Looks to Utilities' ETFs in Downtrodden Equities Market." Do you see that?

A. Footnote 1?

Q. This is Footnote 2 in my copy, Page 10, at the bottom. It's an article from On Wall Street.

A. I don't have the testimony. I'm sorry. You said Page 10?

Q. Yes.

A. Sure. Yes, I have that. I see that.

Q. So you're relying on that 2011 article about downtrodden equities market?

A. I gave it as an example.

Q. Yeah. By the way, just for the record, "ETFs" are what?

A. Electronic transfer something. I forget exactly what --

Q. Electronically traded funds?

A. Yeah. It's a new class of stocks is what it is. It's a new way of trading stock.

Q. Okay. At the risk of testifying, my sense of it is it's a different kind of mutual fund. Is that fair statement? So in this case, it would contain utility stocks? Is that --

A. I'll accept that. I think that's right.

Q. All right. So you're discussing investor expectations, and you're supporting it with an article that talks about the downtrodden

equities market; correct?
A. As of 2011, yes.
Q. In fact, since 2011, since the date of this article, the equities markets have actually not been downtrodden at all. They've been up on the order of about 15 to 20 percent a year.
A. Absolutely. They've done very well, and so have utilities. But yes.
Q. And I'm interested -- do you have a copy of that article there?
A. I have it in my briefcase, not right up here.
Q. I printed out a copy. If you want to check to make sure it's the same one that you have, that's fine.
A. Yeah. Thank you.
(Atty. Camerino hands document to witness.)
(By Mr. Camerino)
Q. Can you just -- actually let me give it to everybody first.
(Atty. Camerino distributes document.)
(By Mr. Camerino)
Q. Can you just tell me where in that article it

refers to water utilities?
A. It makes reference to the so-called "utility sector" without reference to type of utility.
Q. Is it fair --
A. That's my -- quick perusal, that's what I see.
Q. Reading that article, it looked to me like it really is contemplating electric and gas utilities. Do you see all the references to --
A. It was -- well, it was probably focusing on it, yes.
Q. So you're arguing that investor expectations for returns are down because of the downtrodden market, and by reference to an article about utility ETFs. But in fact, since that article, the markets have rebounded considerably. And the article is actually focused on electric and gas utility performance.
A. Right. But the point I made on Page 10 of my testimony is that during the difficult times for the market, utilities did fairly well for the reasons stated, 2011 up until that point

in time.

CHAIRMAN IGNATIUS: Mr. Camerino, are you intending to mark this as an exhibit?

MR. CAMERINO: I don't need to mark it. That's okay.

(By Mr. Camerino)

Q. I have one -- I think this will be my last line of questioning.

I want to ask you about the relationship between the overall allowed return for a utility and its capital structure.

A. Okay.

Q. And so I'm going to walk you through some mathematical examples. And I'm going to actually give them to you, and you can check them.

A. Okay.

Q. But it's just a matter of trying to expedite having you do the math.

You have -- and just by way of reference, you have a Schedule 12 in your testimony that shows how you come up with the weighted average cost of capital, where you take the percentage of debt, you multiply it times the cost of debt, and you get a weighted cost of debt. And then you have a percentage for equity. You multiply it by the cost of equity, and you get a weighted cost of equity.

A. Actually, that's Schedule 1, yes.

Q. Okay. And the numbers we talk about normally in a case like this are referred to as the "after-tax cost of equity"; correct?

A. Correct.

Q. When that gets rolled into rates, you have -- in order for the investor to earn that, they have to actually earn a higher amount, because they're going to pay taxes on those earnings; right?

A. Well, stock -- ratepayers have to pay a higher amount so that the stockholders can pay taxes on it, yes.

Q. And those taxes get included in rates; right?

A. Yes. Ratepayers pay taxes. Yes.

Q. So there's a multiplier -- if we're doing this weighted average cost of capital for the equity component, we need to apply a multiplier to figure out what the tax effect is.

A. Right, which is usually done whether or not taxes are paid. But it's assumed they will be paid.

Q. Okay. And I'm asking those questions as a prelude so that you can explain what's on this chart that I'm going to show you.

A. Sure.

(Atty. Camerino distributing document.)

A. Thank you.

(By Mr. Camerino)

Q. And what you have here, I just want to, before I ask you the questions, tell you where these numbers come from. The first block is the settled -- the proposed settlement capital structure. And it shows the cost of capital calculation using the high end of your DCF, the 9.6 percent.

A. Yes. I see that.

Q. The second block applies that same cost of equity, but to a 55/45 debt-to-equity ratio.

A. Okay.

Q. And the third one -- and you see that that yields a pretax cost of capital -- weighted average cost of capital of 10.59 at the bottom?

A. Right. Same as the second one. Uh-huh.

Q. Well, I'm talking about the second one now.

So you see the second one has a weighted average cost of capital?

A. Yes, yes.

Q. The third one is the settled capital structure, and it takes that 10.59 percent. And if you look at the Cost column, it's telling you that the cost of equity there would be 10.24 percent. Okay?

A. Okay.

Q. Now I'm going to ask you questions to make sure that that was done properly. All right?

A. Okay. Sure.

Q. And I just want to make sure I have the schedule reference.

Do you know what the applicable tax multiplier is in this case?

A. Not exactly, no.

Q. I'm going to represent to you that it's 1.68, meaning that you would multiply the weighted cost of equity by 1.68 to get the pretax cost. Does that sound reasonable?

A. You have it listed here, and I'll accept that. Sure. No problem.

Q. So what I want to make sure of is that -- and you can get a calculator now or on a break. But I wanted to make sure if this was done the way I'm describing to you, that it would be correct. All right?

So, starting in the first block -- so, the first section up there at the top -- we would take the cost of equity of 40 -- weighted equity of 40.75 percent. We would multiply it -- if the Commission found 9.6 percent as the cost of equity, we would multiply that to get a weighted cost of 3.91 percent?

A. Yes.

Q. And then we would take that 3.91 and multiply it by the tax multiplier; correct?

A. Yes.

Q. And so if we did that correctly and the number was 6.57, that would mean that the overall pretax cost of -- weighted cost of

capital would be 10.16 percent; correct?
A. Yes.
Q. Okay. The second block, if, instead, we did the exact same thing, but the debt-to-equity ratio was 55 to 45 -- and you've testified that that would be quite common; correct?
A. It'd be common, yes.
Q. We would do the same thing. We would multiply 45 percent by the 9.6 percent, and assuming we did the math right, that would yield 4.32 percent?
A. Hmm. Yes.
Q. And then we would multiply the 4.32 times the 1.68 tax multiplier to give us 7.26.
A. I follow your arithmetic, yes.
Q. Okay. And so, by virtue -- simply by virtue, a utility coming in with a 55/45 debt-to-equity ratio, its weighted average cost of capital would become 10.59 percent; correct?
A. That's right, because they would have more equity at stake; therefore, they would deserve more money because they put their money where their mouth was.

Q. And so the very same company would have a higher allowed overall rate of return simply because it had come in with less debt and more equity.
A. Yeah, because they would have put more equity in the company, yes.
Q. Right. Now, if you did that, if you came in with that ratio -- I'm sorry.
If the goal, instead, was to say, okay, we think 10.59 is a reasonable overall return, if you took this company's actual capital ratios, it would take a cost of equity of 10.24 percent to get to the same result; correct?
A. With those assumptions, yes.
Q. So if this company had come in with a 55/45 cap structure and been awarded a 9.6 percent cost of equity, that would be the exact same result to customers as its current cap structure in a 10.24 percent cost of equity; correct?
A. Well, from -- that makes sense, yes.
Q. Okay. That's all I'm trying to establish. It's the same result.

A. The numbers are there, but it doesn't reflect the reality of the situation. But the numbers are correct.

Q. And that differential would be about 64 basis points; right?

A. Yes.

Q. Do you recall the adjustment that Ms. Ahern recommended to reflect the higher leverage that this company has than the proxy group?

MR. GEARREALD: Objection. That's, I think, discussed in testimony. The Company has a higher leverage, I think that's assumption.

CHAIRMAN IGNATIUS: All right. I didn't follow the question well enough. Can you ask again?

MR. CAMERINO: The question is: Does he recall the risk adjustment factor that Ms. Ahern recommended to reflect the higher leverage that this company has?

MR. GEARREALD: That's what she may have testified to, but that's not a fact.

CHAIRMAN IGNATIUS: Well, let's simply ask his understanding of what her risk adjustment factor is.

(By Mr. Camerino)

Q. Mr. Parcell?

A. Answer her question?

Q. Yes. That's fine. Her question always takes precedence.

[Laughter]

A. Ms. Ahern maintains it's because --

(By Mr. Camerino)

Q. I'm not asking because. I'm asking just the number.

A. Then I'm confused.

Q. Okay. She suggested a basis point adjustment --

A. Oh, is that what you asked for?

CHAIRMAN IGNATIUS: I think you were trying to give her reasons why in your questions. So if we can get back to what did she ask for, that would be --

A. Oh, you mean the actual number.

(By Mr. Camerino)

Q. Yes.

A. I can tell you that. Page 49 of her testimony is 86 basis points.

Q. And that was to reflect her --
A. Her financial risk adjustment, yes.
Q. Largely or totally associated with the fact that this company has a higher level of debt than the proxy group; correct?
A. That's her recommendation, yes.
Q. In fact, the average level of debt for that proxy group is less than the 55 percent that's in this example; right?
A. Say it again?
Q. The average level of debt in the proxy group is less than the 55 percent that's in this example; right?
A. Probably so, yes.
Q. Okay. And so, to the extent that this example may illustrate a similar type of adjustment, it's not going as far as she did; correct?
A. No. Neither one of them are right, but --
Q. I understand you don't agree --
A. -- this is less egregious.
Q. I understand you don't agree with it.
A. Yeah.
Q. But the point is, if I were to plug into this

example, if I were to have taken that middle block and put in the proxy group's debt-to-equity ratio, I would come up with an even higher pretax cost; right?
A. You would, yes. Yes.
Q. And then my rate differential line down there would get even bigger; right?
A. That would follow, yes.
Q. All right. Thank you.
MR. CAMERINO: Could we -- I don't think we marked this yet.
CHAIRMAN IGNATIUS: We have not. We're up to 32. Can we mark that for identification as 32. And this is developed by Aquarion; correct?
MR. CAMERINO: Yes.

(Exhibit 32 marked for identification.)

(By Mr. Camerino)
Q. And Mr. Parcell, I would ask you, if you decide when looking at this that there's any kind of mathematical error, please feel free to --

A. Just mathematical; right?

Q. Yes. I mean, otherwise, I was just trying to ask you about the concept.

A. Sure. Thank you.

MR. CAMERINO: I think I'm done. But if we could take a very short break, because of the water, I need to just make sure that we didn't use one of my pages for cross-examination to sop things up.

CMSR. HARRINGTON: I've heard some excuses before, but that's a good one.

CHAIRMAN IGNATIUS: That makes the dog ate my homework...

MR. CAMERINO: Did I go too far there?

CHAIRMAN IGNATIUS: All right. Let's take five minutes. We'll begin at 2:30.

MR. CAMERINO: Thank you.

(Brief recess taken.)

CHAIRMAN IGNATIUS: All right. So, Mr. Camerino, did you have anything further?

MR. CAMERINO: Nothing further.

CHAIRMAN IGNATIUS: Thank you.

We turn then to Mr. Ratigan.

Any questions?

MR. RATIGAN: No questions.

CHAIRMAN IGNATIUS: Ms. Hollenberg?

MS. HOLLENBERG: Thank you. No questions.

CHAIRMAN IGNATIUS: Ms. Brown?

MS. BROWN: No questions. Thank you.

CHAIRMAN IGNATIUS: Questions from the Commissioners?

MR. HARRINGTON: Just a couple questions.

INTERROGATORIES BY CMSR. HARRINGTON:

Q. I'm trying to get a few things straight. There was a lot of discussion on the financial risk and business risk factors from Ms. Ahern's testimony, the .86 and .40, and in recent discussion of Exhibit 32, when you were talking about the differential basis points there being 64. And you made a comment that neither of them are correct. So I'm trying to find out what your reasoning is on that.

You do recognize, I'm assuming, it seems to be a fact that the debt-to-equity ratio of Aquarion is higher than it is for the average of the proxies used in the analysis?

A. That is correct.

Q. And given that fact, it would seem as if there should be some adjustment, that the company with the higher debt would be -- present more risk than the company with the lower debt. Does that make sense?

A. You would think so, yes.

Q. Okay. Well, I think you're getting to where I'm heading on this. You would think so, and I guess you don't.

A. I don't.

Q. So tell us why.

A. I don't. This so-called "venture risk adjustment" has also been called a "leverage adjustment" in prior cases. The theory is that, if you have a lower equity ratio, you have more fixed capital costs -- that is, debt -- and therefore, you put stockholders at more risk.

Where this theory does not work out for Aquarion is that we don't know if this is a true capital structure. It's their book capital structure, but it's controlled by many layers of parents. And in fact, during the -- not at the end of the test period, but during the test period, a substantial amount of that debt was owned by a parent. And there's nothing wrong with that, but the point being that outside companies control this capital structure. They have the ability to put debt into it, to but equity into it. And that's their prerogative. But if you're going to create a subsidiary for a different capital structure and claim a higher cost of equity, you've got to demonstrate that's really the way it's financed, and that is not demonstrated here.

The Town of Hampton tried to get some information, and it was just not provided to us. They said it was not relevant. Well, I submit it is relevant if you're going to use that as an excuse or a reason to have a higher cost of equity. You've got to

justify, and they have not done so.
Q. So if this was a company that was a publicly traded company, where they had stock, in that case you'd agree there be would some adjustment for additional financial risk associated with the higher debt ratio.
A. Right. Not a so-called linear adjustment like we saw in Exhibit 32 before, but some adjustment might be necessary for a publicly traded firm with a true market-derived capital structure and market-tested capital structure.
Q. And what you're saying here is that there may or may not be a need for some adjustment on the financial risk. You simply -- evidence hasn't been presented to show that the structure of the company with these various holding companies or whatever, or parent companies, that there's no way of telling whether it's needed or not. Is that --
A. That's exactly right.
Q. -- what you're saying?
A. Yes.
Q. And the same thing would apply to a business

risk factor as well. That was involved in the size of the company --

A. Well, this is kind of the other side of the same shoe. And I'm not sure which one's up and which one's down. But what you've got here is a small subsidiary in New Hampshire -- and risk is defined for utilities as a risk of common stock, common shareholders. And there are no shareholders, public shareholders of Aquarion of New Hampshire. You just got to go way up the line. I mean, you got three Aquarion Water companies: Massachusetts, New Hampshire and Connecticut. You've got an Aquarion company above that. You've got Aquarion Utility Holdings above that, which also includes not only the water companies, but the Puget Sound Energy in Washington State; you got Duquesne Light in Pennsylvania, and you've got Hawaii Gas in Hawaii. And that's not the top of the heap.

So when you look at the true picture of capital rates, it's a huge company, not a small company. And if you try to make the argument, well, it's the use of funds, not the source of funds, the source of the funds is where the money is raised. That's where the risk is derived by the investors and decisions are made as to what the overall risk is.

So it's just not appropriate to take a small state subsidiary and say, because -- either a smaller state or we choose not to consolidate with other subsidiaries, it's therefore, smaller. Well, why not take the same company and have Aquarion Water of Hampton, Aquarion Water of North Hampton? They're even smaller. Voila. Bigger rate of return. They can do that.

Q. And as far as this -- you know, there's been a lot of discussion in this, as far as risk to investors and so forth. But in this case, there isn't a normal investor. I mean, it's not like you can go out there and say, okay, investor is a mutual fund. We buy their stock, or someone who's buying the utility stock as part of their portfolio.

So in your way of thinking, who is the

investors that are at risk that are looking for this return on equity?

A. Well, it's ultimately going to be the equity owners, ultimately, because there's just no level down the chute, so to speak, where you can invest in a smaller piece of it.

Q. And when you say Aquarion, that's Aquarion Water? Is that the --

A. It's the four Aquarions. Three Aquarion Water Companies of... you have Aquarion Water Company, which is the sum of those three; you have Aquarion Company, which is the level above that, and Aquarion Utility Holdings Limited, or something like that. So there's four levels of a company called Aquarion.

Q. And which one of those do you consider are the investors that are looking for their return on equity?

A. We haven't even started yet. We've got to go from there all the way to the parent owner in Australia to get the ultimate source of equity.

CHAIRMAN IGNATIUS: Mr. Camerino.

MR. CAMERINO: I just want to alert the Commission that this witness is testifying at length about the corporate structure of Aquarion incorrectly, almost completely incorrectly. And so we need to find a way for -- and I'd hate for it to lead to a rebuttal witness, to have someone come in and give the corporate structure, because we're getting a record filled with this witness's best answer. I understand that. But there were extensive discussions about other utilities and the like that is just 100 percent incorrect.

CHAIRMAN IGNATIUS: Well, there's a portion, Mr. Parcell, in your testimony, I think it's either an attached data request or part of your testimony that does lay out your understanding of the levels of ownership; correct?

THE WITNESS: Page 11. That's correct.

CHAIRMAN IGNATIUS: Of your direct or --

THE WITNESS: Direct testimony,

Page 11, top portion of the page.

CHAIRMAN IGNATIUS: Oh, okay. It's not a chart, but just in text?

THE WITNESS: Right. But there's a chart in response to Hampton 3-4 that shows the same information.

CHAIRMAN IGNATIUS: And I assume, Mr. Camerino, that if you found issue with his description, you would have raised that on cross-examination?

MR. CAMERINO: This statement is correct. It's completely at odds with what he just said, and he's not able to correct it because he doesn't know.

CHAIRMAN IGNATIUS: I want to take these one step at a time.

I asked you if you found any fault with his description on Page 11, and it sounds like you did not.

MR. CAMERINO: Well, we will double-check it, but I believe it is correct.

CHAIRMAN IGNATIUS: All right. Then let's -- unless, Mr. Parcell, you think what you stated in writing is incorrect and need to correct that, I'm assuming what you wrote in the text is reliable.

THE WITNESS: It was provided by the Company.

CHAIRMAN IGNATIUS: All right. Then why don't we strike your description of the levels of the different ownership structure that you spoke to just a few moments ago and stick with the description on Page 11 of your testimony.

THE WITNESS: Sure.

CHAIRMAN IGNATIUS: Now, I think you were also saying other things on what the Company could or couldn't do to create another form of structure. I think that's fair game, and that was just speculation on what else might be available.

But Mr. Camerino, if your concern is that the description of the different companies was not matching what was on 11, then we'll stick with what's at the top of Page 11.

MR. HARRINGTON: And just to be clear, my line of questioning was not to get into the level of detail of that, but, rather, just try to get a feel for the difference between this and a company that would be traded publicly. Limited just to that. So I think I'm done with that line of questioning, anyways.

BY CMSR. HARRINGTON:

Q. One question I also wanted to do is, in some of your previous, I guess expert testimony, there was a series of exhibits there, 30 and 31 and so forth. And in a lot of those you did not incorporate the CAPM into the average to calculate the --

A. Correct.

Q. So am I correct, if you use that same methodology in this case without incorporating the CAPM, would the recommended ROE be 9.4 percent?

A. That's probably correct. Let me just confirm that.

(Pause in proceedings)

A. Yes. You said two midpoints of DCF... would be 9.4 percent. That's correct.

MR. HARRINGTON: That's all the

questions I have. Thank you.

CHAIRMAN IGNATIUS: Thank you. Commissioner Scott.

CMSR. SCOTT: Yes. Thank you.

INTERROGATORIES BY CMSR. SCOTT:

Q. Good afternoon.

A. Good afternoon.

Q. Earlier, when Ms. Ahern was on the stand, there was a document produced which became No. 27, which basically -- Exhibit 27, which basically was an analysis of, if I understand it right, her recommendations for different cases compared to what was actually -- what the various commissions actually approved for an ROE.

A. Right.

Q. I was just curious. Since we got the benefit of that analysis for some of her recommendations, if we were to do the same thing for your history, can you characterize that?

A. Sure. I can provide -- I have information. I don't have that chart, but I have a -- I call it my score card. I have a list of every case since 1972 that I've ever testified in and what the company asked for and what I recommended and what was authorized. And I would -- I have a copy with me and would be glad to make that available.

Q. Or can you just characterize it? Is it generally a little bit lower, a little bit higher, right on, on average?

A. I would say... it be hard to generalize it. A lot closer than hers. Probably a good portion of mine, the awards were within my range. But not all the time. But at least half.

Q. Is it biased one way or another, higher or lower than --

A. I would say tend to be lower. Certainly not 144 basis points, but lower.

Q. Thank you. That's helpful.

And again, back to the questioning I had with Ms. Ahern on WICA impact. And that's been discussed back and forth. I know your analysis -- I think I got pretty clear you didn't include an analysis of WICA.

A. Correct.

Q. Is it, in your opinion, a fair -- and again, this is probably oversimplification -- a fair assumption that having a WICA would reduce risk for a utility?

A. I missed the word there before "WICA." The what --

Q. If a utility had a WICA --

A. Oh, had, yes.

Q. -- that that would tend to reduce --

A. Yes. I mean, other things equal, if you had to create a regulatory mechanism that increases cash flows, shortens the time where you can change rates, makes earnings more stable, that's beneficial to a company, and to a certain extent it involves a transfer of risk from ratepayer -- I mean from the stockholder to the ratepayer. The ratepayers take on some of that risk. And to the extent that they take on a level of involuntary risk, they should be compensated for that by paying in lower term equity.

Q. So I think you just answered where I was going.

So, all things being equal, there should be some --
A. Some risk reducing, yes.
Q. So there should be -- all things being equal, your opinion is there would be a somewhat lower return on equity with such a system in place.
A. Yes. With that type of mechanism, yes. Yes.
Q. But you haven't gone as far as analyzing what that might be.
A. No, I have not.
CMSR. SCOTT: I think that's all I have. Thank you.

INTERROGATORIES BY CHAIRMAN IGNATIUS:

Q. Mr. Parcell, when you were asked about this Exhibit 32 developed by the Company, you agreed with the math of it, but you didn't endorse it as something that you thought was sound. So can you explain a little more what --
A. I have two 32s on my desk. I think that's --this is the real 32, isn't it?
Q. That's the real 32.
A. Oh, okay.

Q. The other one was not marked, the resolution --
A. Oh, okay. I apologize.
Q. -- because it was already contained in other people's testimony.
A. I'm with you. Thank you.
Q. Now, you actually described 32 as less -- that one situation was "less egregious" than the Company's proposal to begin with. So, can you just elaborate on what you find troublesome about what was presented in this 32 chart?
A. Yes. It assumes that because this company and its parent companies have collectively chosen to finance the company the way it is, that they should be compensated for that lower equity ratio with a higher return on equity. That's what it assumes. And I disagree with that assumption.
Q. When you say when the parent company's "chosen to finance the company the way it has," you're referring to the high debt as compared to equity?
A. Right. In other words, as this company

spends money, it can finance it internally through retained earnings, profits, or externally through either raising debt or equity. It could raise debt either as an affiliate or from a public source like an insurance company. And it can raise equity, but only equity can come from a higher affiliate, whether in the form of common stock flowing down or lack of dividends flowing up. But it's a corporate decision they've made, and they have a right to make that decision.

Q. Did you say that the Connecticut structure is of a similar level of debt, the Connecticut affiliate?

A. Well, there was, at their request, supplied a Standard & Poore's report on Aquarion of Connecticut. And in that it cites their equity ratio being virtually the same, 42.1 percent.

Q. And do you know anything about the Massachusetts affiliate?

A. I do not.

Q. On Page 13 of your direct testimony,

Exhibit 13 --

A. Yes, ma'am.

Q. -- at line -- the answer at Lines 19 through 22, in the middle of that you say that the capital structure may not represent the effective capital structure of the Company. What do you mean by that?

A. Well, since we have debt coming from time to time from a parent source, we don't know if that debt is debt or equity or some combination, you know, the source of the funds. I don't -- they have a right to finance the company the way they want to. But as regulators, you have a right to hold them to a certain standard that shows us a marketable capital structure. As an intervenor, we have a right to try and see what their affiliates are. And we were not provided that, so we have no way of knowing.

Q. What would you have looked at if you'd been able to obtain more data on the affiliated or parent companies?

A. Capital structures of the different levels, both horizontal and vertical.

Q. What would that have shown you? Why is that important?

A. If would have shown you how the company is financed at the same level that investors invest money into it. In other words, if you had a large company that was 50 percent debt and 50 percent equity, that's the market capital structure of the whole enterprise. But if the subsidiary had 75 percent debt and 25 percent equity, you wouldn't know until you had further information if that's the true capital structure of that company. It's the book capital structure. But is that the way it's truly financed in the grand scheme of things, of how the enterprise is financed?

Q. There's been quite a lot of back and forth in the written testimony and today over some of the components you used in the DCF and the ones that Ms. Ahern did when she made corrections to your calculations.

But correct me if I'm wrong. The end result with the corrections today is that you came to a midpoint of -- excuse me -- 9.3, and she came to a midpoint of 9.43 on DCF?

A. Yes.
Q. So you --
A. That's a first for us.
Q. You may have gotten there, but it's a slightly different mechanism --
A. We'll be put out of business if we keep this up.
[Laughter]
Q. You also, I'm sure, know that the New Hampshire Commission, for years, has used the DCF method --
A. Yes, I've seen that.
Q. -- almost exclusively. And you've argued that you need to do more than that one alone.
In your opinion, what's lost by using only DCF?
A. Well, I think if you just used one method, over time, if that method changes a little bit, you have nothing to compare it to. It's sort of standard. And I have seen this Commission make reference to the CAPM end result as a "check" to a DCF.
But repeatedly I've seen your orders say that you primarily use the DCF. I think it's

important to look at other methods. If the other methods give you comfort, then stick with the DCF. But I think it's nice to look at them.

Plus, in my situation in this particular case, where I'm, I'll call it a first round, if you will, of a cost accountant testimony, I had to somewhat anticipate what else might come down the pike. If I just put in one, and the company on rebuttal added something else, my client would not have been well served by me.

Q. And am I right that, if you use your DCF alone, the midpoint would be 9.3; if you used your DCF and the comparable earnings together, it would be 9.4?

A. That is correct.

Q. And it drops down if you also include the CAPM, and then it would drop down to 8.3.

A. That is correct.

CHAIRMAN IGNATIUS: All right. I have no other questions.

Anything else from the Bench?

(No verbal response)

CHAIRMAN IGNATIUS: All right. Then, Mr. Gerreald, any redirect?

MR. GEARREALD: No, thank you.

CHAIRMAN IGNATIUS: All right. Thank you, Mr. Parcell. You're excused. I appreciate your testimony.

What is next on our agenda?

MR. RATIGAN: I think it's Mr. Landman.

CHAIRMAN IGNATIUS: That's fine with me. Is that acceptable with everyone?

(No verbal response)

MR. CAMERINO: While they're getting ready -- and this is a separate question --

CHAIRMAN IGNATIUS: Okay. You can go ahead and get set up if you'd like.

MR. CAMERINO: We're contemplating with how to the deal with the record that was created there, in terms of the ownership structure and obviously being very mindful of where we are in the schedule of the day. And one of the things we could offer, and it's not a complete fix, but there is a response to a data request from the Town of Hampton provided that shows, at least on a chart, the basic corporate structure. It doesn't fix all of the things that were said about the other utilities in other parts of the country, but I believe that it was this answer that was the basis of Mr. Parcell's testimony.

CHAIRMAN IGNATIUS: Either that or something like that is already in the record, because I've seen it.

MR. GEARREALD: This is in the record attached to our Selectmen Bean's testimony as Exhibit 1. So it's in the record.

MR. CAMERINO: So at least with regard to that, that was Hampton 3-4 that I'm referring to, in case you wanted to reference that.

CHAIRMAN IGNATIUS: Right. Thank you.

MR. CAMERINO: Thank you, Mr. Gerreald.

MR. GEARREALD: Sure.

CHAIRMAN IGNATIUS: Okay. Thank you.

(WHEREUPON, *ROBERT J. LANDMAN* was duly sworn and cautioned by the Court Reporter.)

EXAMINATION

BY MR. RATIGAN:

Q. Please state your name for the record.

A. My name is Robert J. Landman.

Q. And where do you live, Mr. Landman?

A. I live in North Hampton.

Q. Do you have a position with the North Hampton town government.

A. Yes. I'm the co-chairman of the North Hampton Water Commission. I have been for a number of years. I'm also a member of the zoning board, former member of the planning board, and Rockingham Regional Planning Commissioner, and Chairman of the Rockingham Region Planning Commission.

Q. Could you briefly state your professional qualifications.

A. Yes. I'm an electrical engineer. I'm a life senior member of the IEEE, the Institute of Electrical and Electronics Engineers. I own a business, a manufacturing company. I have some -- for 34 years. And my major in college was in physics, but I worked as a electrical engineer.

Q. Have you participated in prior dockets regarding the Aquarion Water Company?

A. Yes, I have. And also --

Q. Have you participated in prior dockets involving the Aquarion Water Company and its predecessors?

A. Yes, I have, and also the prior companies.

Q. You've prepared prefiled testimony?

A. Yes.

Q. Do you have any corrections to make?

A. Yes, I do.

On page -- well, there's no page number. But it's the -- well, it's the third page, which begins, "Do you have a proposal to eliminate this subsidy by non-water customer taxpayers?"

And the last paragraph, where it begins, "It is noteworthy," on the line, "separate public fire protection charge," I wish to amend that by adding -- what I meant to say was "for fire protection within the city's

boundaries."
Q. So on the third page of your testimony, in the second to the last sentence on that page, it would read, "It is noteworthy that neither Manchester nor Nashua has a separate public fire protection charge <u>for fire protection within the city's boundaries</u>"?
A. Yes, <u>within the city's boundaries</u>. That's what I meant.
Q. Do you have any changes to your testimony?
A. No, I -- no, I do not.
Q. Could you address briefly North Hampton's concerns about the fire protection category?
A. Yes. The problem has been, for many years, that the rate has been going up for water -- for fire protection. We're a very small town. We have 47 hydrants. We have about two to three structure fires a year.
As an engineer, some of my colleagues in the Commission, one of them is also a mechanical engineer/Ph.D., we don't believe that the Company's argument that the fire charge is appropriate. We believe it's excessive. We have looked throughout the

country for similar charges, and not only in New Hampshire, but throughout the country. We find the prices are very low. They're fire charges of $150, $200 a year. There have been studies.

The argument that the piping and the tanking and so forth that they have provided for a three-hour fire flows at 3,000 gallons a minute for three hours, by the Company's own testimony this week, it's clear, with 2.75 million gallons of water available -- and the biggest structure fire ever was on the beach, and they used about 250,000 gallons, which is one-tenth of the tank -- the idea that the pipe size -- and Mr. Walsh brought in the matter of the pipe size -- and looking around the country at various utilities, and some of my customers -- by the way, I'm in the electric utility business. I manufacture fiber optic communications equipment for electric utilities, and not just electric, but water and gas in small towns like in South Dakota and in cities like San Francisco -- Pacific

Gas & Electric Company is my biggest customer, and Disney World, Florida, is one of my customers -- so I'm very familiar with this business with municipal and private companies. And what they do is they -- about 10 to 15 percent of the capacity of the utility is for fire protection, and that includes tanks and piping.

We, in fact, asked at a technical session what would happen -- we pay $1551 per hydrant per year right now.

CHAIRMAN IGNATIUS: Mr. Landman, hold on a second.

THE WITNESS: Yes.

MR. TAYLOR: I just want to note that everything Mr. Landman said for the last, you know, say minute or so is completely outside the bounds of his direct testimony. It's not contained within his testimony here. This is all new information or new opinion that's coming in. And so I just want to note that for the Commission. I think we've been pretty good with all the other parties about keeping our direct testimony -- either foregoing them entirely or keeping them to a summary of what's in the direct, and I think Mr. Landman should be held to the same standard.

MS. HOLLENBERG: I'm going to formally object to it, actually, and not just note it. Thank you.

CHAIRMAN IGNATIUS: So are you asking that what he's been saying be stricken?

MS. HOLLENBERG: No, ma'am. Well, what I'm asking is that he be kept to the same requirements that the other parties have been kept to. His testimony is four pages long. I mean, in order to summarize it, I don't think that we need to go into information that's not contained and discussed within his testimony.

CHAIRMAN IGNATIUS: Mr. Ratigan.

MR. RATIGAN: I said the word "briefly." So I -- don't look at me.

[Laughter]

THE WITNESS: I guess you'd look at me.

CHAIRMAN IGNATIUS: It was quite

a sentence, I have to say, and you weren't done. Well, I think it is going into a lot of things beyond what you stated. And we do have your written testimony. There may be some questions about why you have the views that you do --

THE WITNESS: You can -- excuse me, Madam Chair. You can look at my prior -- the technical sessions, the comments I've made over the years, basically repeating that. So it's in the record.

MR. RATIGAN: Madam Commissioner, I'll ask more pointed and directed questions. And I'll be brief.

BY MR. RATIGAN:

Q. Is there something about the demographics about North Hampton and its land use that raises additional concerns?

A. Yes.

MS. HOLLENBERG: I'm going to object. I'm sorry. I really don't think there's a need for direct on a four-page testimony.

CHAIRMAN IGNATIUS: Well, we can

explore what's in the written testimony. We don't need it restated now.

THE WITNESS: Okay. Fine.

CHAIRMAN IGNATIUS: I think it's really just a quick summary, if there's anything further to add.

BY MR. RATIGAN:

Q. Okay. Fair to say that the fact that North Hampton, 50 percent of its landowners or residents are not on public fire protection and are not customers of Aquarion, does that drive some of North Hampton's concerns?

A. Yes, that's correct. Much of the town is not served by the Company. It's rural. Basically, the west side of Route 1 does not get water service.

Q. Drawing your attention to Page 12 and 13 of the Commission's order in the prior rate case, which is DW 08-098, which I passed out to the Commission the other day, if you could just -- we went over this a little bit with the Commission, and I just wanted to draw your attention to Page 13.

Is it your understanding that, if I read the last sentence of the last full paragraph of Page 13, the Commission writes that, We will revisit the allocations among customer classes at the time of Aquarion's next cost of service study, is your understanding that the adjustments to the fire protection class that were adopted in that case would continue until there was a fire -- a cost of service study?

A. Yeah.

MS. HOLLENBERG: Objection. This goes beyond his testimony. There's no mention in the prefiled testimony about relying on the Commission's prior order as a basis for continuing the allocation that existed in the last case.

CHAIRMAN IGNATIUS: Well, I'm not sure I'd agree with that. If you look at the second question, I'm not sure if I'm following -- if we're mixing apples and oranges, but --

MR. RATIGAN: No, I think you're right.

CHAIRMAN IGNATIUS: So I'll

allow the question.
A. Yes, certainly. We expected the same treatment until the next cost of service study.
BY MR. RATIGAN:
Q. And that's not the treatment that's proposed in the settlement agreement. The settlement agreement is silent on the issue; is that correct?
A. No.
Q. Do you have an understanding of whether there's an objection from the Company to the continued treatment for --
MS. HOLLENBERG: Objection.
CHAIRMAN IGNATIUS: On what basis?
MS. HOLLENBERG: On the same basis, that it's exceeding his prefiled direct testimony.
CHAIRMAN IGNATIUS: And Ms. Hollenberg, would you say that he has no opportunity to comment on the settlement agreement terms?
MS. HOLLENBERG: I guess I

wouldn't say that.

BY MR. RATIGAN:

Q. Do you have an understanding of whether the Company objects to the continued treatment from that last rate case?

A. I do have an understanding that they object to it.

MR. TAYLOR: I -- oh, I'm sorry.

A. Excuse me. I do.

BY MR. RATIGAN:

Q. What's your understanding?

A. That they want to change it. That they want to change the percentage. That's what I'm understanding. It's been a long hearing and I'm a little tired and very confused at this point, especially with the objections that are coming up. I may be confused at this point.

MR. TAYLOR: Well, I'm just going to object, because he's making a representation about -- again, this is not something that's addressed in his direct testimony. I mean, the Company's direct testimony is what it is. And, you know, we don't take issue with that. But he's, again, making some representations about objections on behalf of the Company. So --

THE WITNESS: Excuse me. But right in my direct testimony I talk about the last rate case, "70 percent of the cost of service study full application of fire demands was adopted, with the resultant reduction in public fire revenues. We would propose that the cost of service study be reduced further than [sic] 70 percent." I'm talking about the numbers. I don't see where you're saying I didn't discuss them. It's in my direct testimony, sir.

MR. TAYLOR: No, I'm...

CHAIRMAN IGNATIUS: I think the concern is representing what you think the Company's point of view is going forward.

THE WITNESS: Oh, yeah. That's...

CHAIRMAN IGNATIUS: We know what your position is. We know that the settlement as proposed doesn't talk about a changed allocation. It doesn't guarantee that it won't be changed. But that would be an issue for the next cost of service study and next rate case.

Correct? I guess I'm looking to the signatories to the settlement agreement.

MS. BROWN: Staff would not take that position.

MS. HOLLENBERG: I'm not sure I followed what you said. I'm sorry.

MS. BROWN: To the extent you are asking if the parties are in agreement that the last order in 08-098 states that we will revisit -- that we are precluded from revisiting rate design until they file a cost of service study, then Staff would not agree with that.

CHAIRMAN IGNATIUS: And you're right. And you made that distinction yesterday. I'm just trying to understand so that we can keep moving here.

There is nothing in today's proceedings -- and correct me if I'm wrong. There's nothing in today's proceedings that change the allocation that's established in the 08-098 case; is that correct?

MS. HOLLENBERG: My understanding is that the Company is proposing an across-the-board allocation of the revenue requirements. I don't know if that answers your question.

CHAIRMAN IGNATIUS: Is that the same or different from the prior order?

MR. RATIGAN: It's different from the prior order.

MS. HOLLENBERG: Yes, ma'am.

MR. RATIGAN: Yes, it is different. And yet, the prior order, I think, which was not appealed by anyone, put the parties on notice that there would be no changes until there was a new cost of service study.

MS. HOLLENBERG: And the OCA would respectfully disagree that there's not a good-faith argument that the Commission would revisit that in this case.

MR. RATIGAN: And I guess the only other thing I would add is -- and I'm done with this witness.

But, you know, I have an e-mail from you saying that Staff, you know -- we talked --

MS. HOLLENBERG: Objection.

MS. BROWN: I'd be happy to reiterate what Staff's position is with respect to whether they are precluded from revisiting rate design.

Staff, in participating in the partial settlement agreement, would recommend the increase in revenue requirement be applied equally to all classes and that there not be only, say, 70 percent allocation of that increase to fire protection.

MR. RATIGAN: I guess this is kind of Alice In Wonderland. I have an e-mail from you saying that it was agreeable. We talked about that, that you would go with the allocation from the last case. I have a statement from --

MR. TAYLOR: And I'm going to object. This is going into settlement discussion. And if he wasn't able --

MR. RATIGAN: We weren't --

(Court Reporter interjects.)

MR. RATIGAN: We weren't invited to the settlement discussion on this issue where they settled -- no one contacted me. When the three of you addressed your issues, I was not contacted. I was not brought into that. So don't tell me that they were part of settlement discussions which I was involved in.

MR. TAYLOR: If I may, I just want to make my representation. Mr. Ratigan was about to discuss an e-mail that I had sent to him. And my understanding at the time was that there was some sort of settlement being negotiated. I communicated our position at that time. And so I don't want to speak for the Staff. I don't know what happened. But I just was trying to put a stop to that, because that seemed to me to be communications between attorneys. I didn't expect that we would be discussing them in the hearing today.

MR. RATIGAN: I was a party to the second round --

CHAIRMAN IGNATIUS: I understand. You made that point. Hold on.

Ms. Hollenberg, something you want to say? Because what I'm inclined to do is take a break and let everybody have a discussion about what all of this is. It doesn't need to be all transcribed. We absolutely should not have settlement positions being discussed publicly. And so, unless this is sort of a tempest in a teapot and we're going to move on -- sounds like it's more significant than that -- it would make sense to have the parties and Staff caucus and figure out where exactly you are and make a recommendation on how to -- if there's issues that haven't gotten out that need to get out, you want to do that. I mean, this isn't a game. We're not trying to catch anyone. And we just want to get the facts out and have the record sound. So there may be a misunderstanding or a miscommunication. I'm not sure. But would that be acceptable, or is there something else, Ms. Hollenberg, you wanted to say?

MS. HOLLENBERG: I'm happy to have a discussion with the parties and take a break. I think this would be a good time to do that. I would just note that Mr. Naylor did testify on the stand yesterday that Staff was proposing an equal distribution of the -- or an equal allocation of the revenue requirement.

CHAIRMAN IGNATIUS: Yes, he did say that.

All right. Then let's take a break for 15 minutes.

THE WITNESS: Excuse me, Ma'am. Did the Commission want to ask me any questions?

CHAIRMAN IGNATIUS: We may. You're not done.

THE WITNESS: Okay. Just curious.

(Whereupon a brief recess was taken at 3:12 p.m., and the hearing resumed at 3:37 p.m.)

CHAIRMAN IGNATIUS: So are we picking up where we left off, or is there anything that we need to --

MR. RATIGAN: I have two questions for Mr. Landman.

And we had a very productive discussion, and the Staff will be putting on Mr. Naylor to explain an issue, which I think there was a little bit of collective misunderstanding, a good portion of which was mine, and we'll go from there.

CHAIRMAN IGNATIUS: Good. Thank you.

BY MR. RATIGAN:

Q. Mr. Landman, is it your understanding that this rate treatment for fire protection as to existing plant in service is receiving that coverage presently?

A. Yes, it is my understanding.

Q. Does North Hampton have a position as to whether they'd like to see that treatment continue as to new plant?

A. Yes, we would.

Q. What's position?

A. We would like it to continue to -- to be extended to new plant.

Q. Okay. And for the record, does North Hampton adopt the testimony of Mr. Parcell?

A. Yes, we do.

Q. Thank you very much. Nothing further.

CHAIRMAN IGNATIUS: Thank you.

So, questioning from -- why don't we just go around the room. Mr. Taylor?

MR. TAYLOR: I have no questions for Mr. Landman.

CHAIRMAN IGNATIUS: Mr. Gearreald.

MR. GEARREALD: Thank you. I have none either.

CHAIRMAN IGNATIUS: Ms. Hollenberg.

MS. HOLLENBERG: Thank you. Yes, I do.

EXAMINATION

BY MS. HOLLENBERG:

Q. Good afternoon, Mr. Landman.

A. Good afternoon.

Q. Do you have any experience or education in the field of utility ratemaking?

A. Utility ratemaking, a little bit, in that I have been a commissioner for a number of years and I had worked for a utility. I worked for Pacific Gas & Electric Company in San Francisco, and that goes back many years, to an organization called TURN, which stands for Towards Utility Rate Normalization. And it was the beginning of the Office of Consumer Affairs. And Sylvia Siegel founded it, and I know her. So, yes, I have some understanding of it.

Q. Thank you.

Did you -- do you have -- how about in the area of utility cost of service? Did you -- have you received any education in how to perform a cost of service study?

A. I have not received any education other than reading, talking with Mr. Costello, who did the one on the fire protection years ago. We had a session in town with our counsel and our consultants, and we went into great detail. Another member of my board is a Ph.D. mechanical engineer and experienced in flow modeling and so forth. So, between the two you us, you know, we certainly argued it back and forth with Mr. Costello about cost and so forth. And we've done a lot of

reading on the subject. Being commissioners, we want to be informed. I mean, it's not our -- you know, we try to be informed as to what other utilities are doing and what the norms are.
Q. Okay. Thank you.
You did not conduct a cost of service study concerning Aquarion's proposed revenue requirement increase, did you?
A. No, we did not.
Q. And in your testimony, you did not quantify the impact of the town's proposal on metered rates, did you?
A. On metered rates... we did consider -- we did talk about it, and we --
Q. I'm sorry. Did you do that in your testimony was my question.
A. No. No, I did not. Excuse me. It's my -- I'm confusing it with the technical sessions, where we have been proposing metered rates, you know, and monthly reads before the Commission and so forth for many years, for water conservation.
Q. But just for clarity, the impact, the

financial impact of the town's proposal is not quantified in your testimony; is that correct?

A. It is not, no.

Q. Okay. And just for clarity, also, you mentioned recommending that the Commission actually further decrease the allocation of the revenue requirement from 70 percent to 50 percent in your written testimony. Is it correct that you're no longer recommending the 50 percent allocation?

A. We are agreeing to the current -- because of the discussion we had with the break here, we're going along with the group that has -- we're willing to accept the 70 percent. I mean, you know, we would have preferred less. But we're accepting the 70 percent be continued until the next cost of service study.

Q. And along the lines of quantification of the impact of the town's proposal, there's no quantification in your testimony of how much money will be shifted from public fire customers to other customers if the town's

proposal is approved; is that correct?
A. There is not. When you say "other customers" --
Q. Metered customers. I'm sorry. Residential.
A. Yeah, metered. Because we have customers -- as a town we have the taxpayers. And there is certainly shifting happening there. We're shifting it away from taxpayers that don't have water service. So, you know --
Q. But I guess just for clarity again, my question was that there was no quantification of how much money would be shifted --
A. No.
Q. -- from one pot to another.
A. No.
Q. If the town's proposal is approved and fire protection allocation is reduced, and other customers are required to pick up the slack, for lack of a better word, or pick up the amount that's being shifted from fire protection, would you agree that residential customers in other communities, such as Hampton and Rye, will be required to pay a portion of that shifted dollar figure?

A. Yes. But also, of course, they have fire hydrants, and they're in the same boat we are. They have to either pay through the taxes or they have to pay for the use of the water. And fire hydrants, generally speaking, don't use water. They just -- the water is there. So, you know, that's why we have joined with Hampton in this proceeding and have hired Mr. Parcell. We have a different understanding than some people in this room about whether it's -- which cost shifting is actually happening. We happen to think it's going the other way, the wrong way, that it's being shifted to towns, because it's a way of keeping the true price of water down.

Q. Thank you.

You recognize in your testimony that public fire protection rates charged the Town provide access to a certain capacity of water should that be needed in the event of fire; is that correct?

A. Yes.

Q. And are you familiar with the Insurance

Services Office, also known as the ISO?

A. Yes, I am.

Q. And do you know what the ISO fire flow requirements are for the town?

A. It's 3,000 gallons per minute for three hours.

Q. And if the town's allocation of fire protection charges is reduced, would the Town be willing to accept less fire flow protection from the Company?

A. I don't see any way that could possibly happen, because we're not using 3,000 gallons per minute for three hours. The beach fire was 254,000 gallons, which is one tenth of the tank capacity, which is 2.75 million gallons. I don't know what they're going to do with the rest of the water, ma'am. There's not going to be a change. I just don't see that. I don't make that calculation. There will be no change, except the customers who use the water will pay for it.

Q. So in other words, there's no way for the Company to reduce the fire flow protection it

provides to the town --
A. No.
Q. -- and pays less than a 100 percent of the cost of the service?
A. No. I mean, as an example of the problem we've got as a town, in the technical session we talked with the water company and said, Well, the cost is so high, we'll take half the hydrants out. We'll just get longer hoses. And they said, Well, we'll charge you twice as much. So, I mean, is that what you do as a homeowner if you reduce the number of toilets? No. You pay a water rate per usage. It's different for towns. That's our conundrum here. It's a very -- it's not a true charge for cost of service.
Q. But --
A. So, you know, when you say it will be reduced or it will be shifted, I don't see any way that shifting can occur.
Q. But you didn't perform a cost of service study to access that, did you?
A. I didn't. But I looked at others. And all the cost of service studies show we are in

the stratosphere, and there's no explanation as to why except Mr. Crostino's [sic] study, who I argued with and we argued with. And we agreed to disagree.

Q. And by "others" you mean --

A. Other towns. City in Florida; Birmingham, Alabama. You name it. Just Manchester, New Hampshire; Portsmouth, New Hampshire. In this state and other states. There's nothing like we're paying for fire hydrants, ma'am.

Q. Those are municipal systems?

A. No, they are private systems and --

Q. What's the system in Manchester?

A. The system in Manchester is a public system. But people outside the city of Manchester pay a rate, just like Greenland pays for Portsmouth water, and Newfields, I believe, pays for Portsmouth water. Parts of Rye do. They pay a fire hydrant charge 150 or 130 a year. They're paying what presumably the company considers covers their cost.

Q. And what's the system in Nashua?

A. Nashua is now -- since it's now -- now it's Nashua. Outside Nashua it's a similar situation, where they charge a fee, a fire hydrant charge. Within the city they don't. It's just the city charging the city.

Q. But I guess I'm asking you what the company is -- or what the system is.

A. Well, since the break-up, I do not -- I have only -- I've been getting the correspondence since the Pennichuck-Nashua thing for years. And I don't -- since the change in ownership, I haven't kept up. I don't know.

Q. Thank you.

In your testimony, you talk about the subsidization of the town's water customers by the town's non-water customers. And you refer to the importance of customers who are benefiting from the Company services, paying for those services. Do you recall that testimony?

A. Yes, I do.

Q. Would you agree that the Town opposes subsidies?

A. Yes, I would.

Q. Thank you.

The Town passes along public fire

protection cost to its taxpayers through their property taxes; is that correct?
A. That's correct.
Q. It's a pass-through?
A. It's a pass-through, and it's just in the general fund. And it isn't allocated by the size of the house or anything like that, except you could say, well, the appraised value of the house, you know, does affect somehow what they pay for fire. And the town itself, of course, has sprinkler protection systems of its buildings.
Q. Would you agree that, to the extent these taxpayers pay their tax bills, that these -- they're entitled to deduct these payments in the calculation of their federal income taxes?
A. Yes.
Q. And that if the town's proposal is approved, residential customers in North Hampton will pay less in property tax and more in their water rates?
A. Run that by me again? I'm sorry.
Q. Sure. Do you agree that if the town's

proposal is approved, residential customers in North Hampton will pay less in property tax and more in their water rates directly to the Company?

A. Yes, they will.

Q. And the payments of water bills are not tax-deductible; is that correct?

A. That is correct.

Q. Okay. Thank you.

Is reducing the public fire protection cost a way for the Town to reduce its tax bills?

A. Yes, it is.

Q. You participated in the Company's last rate case, DW 08-098. Do you recall that?

A. Yes, I did.

Q. And this issue existed in that case as well; right?

A. That's correct.

Q. And do you recall discussions in that case about ways in which the Town could isolate the impact of the Company's public fire rates to only taxpayers who were customers of the Company?

A. I don't recall that discussion.

Q. Do you recall any discussions about the Town establishing a municipal water district so that it could achieve this result?

A. Yes, we have talked about that. We actually had a petition warrant article. It didn't pass. The Company was very aggressive, pointed to the fact that Nashua Pennichuck was involved. And postcards were sent out showing dollar bills going down the drain by the Company. And polling was done by a marketing organization, and it scared the property taxes [sic]. They were -- it was suggested that property taxes would go up by having a municipal water company, which is ridiculous, because a municipal water company is bonded. It's separate from the taxpayers. But they were scared. And we almost won. And all it was, was a study. We weren't asking to take over the company. We simply asked to study the idea.

Q. Has the Town investigated any options for -- any other options for ameliorating the impact of the Company's rates on non-company taxpayers?

A. No, we have not. And quite -- you know, thinking about this off the top of my head, I cannot imagine how we could do that. The DRA is pretty -- you know, has rules about how taxes are levied. And you can't -- you know, I don't know. Perhaps there's a -- I don't know. I'm just thinking off the top, is there a way of doing a fire district that would separate the people? I don't know. I don't know. We've never investigated it.

Q. And just for clarity, that was the kind of concept I was asking about when I mentioned the municipal water district.

A. It's never occurred to me. And it's never been discussed by the water commission, and I don't believe it was ever discussed at technical hearings.

Q. Do you recall a public statement that you filed in this docket in November of 2012?

A. Possibly. I'm certain if you help me recall, I'll be happy to confirm it.

Q. May I approach the Bench?

CHAIRMAN IGNATIUS: Of course.

(Ms. Hollenberg hands document to witness.)

MR. TAYLOR: While she's showing that, we'd just like to ask, before Ms. Hollenberg's done, we just want to confer with her for a moment before she concludes her cross of Mr. Landman.

CHAIRMAN IGNATIUS: All right.

(Off-the-record discussion among counsel.)

BY MS. HOLLENBERG:

Q. So I'd like to ask you about -- you filed a public comment -- and I apologize 'cause my copy has a little writing on the front. But do you recognize this public comment which is dated November 28, 2012?

(Witness reviews document.)

A. Let's see. Well, obviously it's got my name on the top of it. I'm just reviewing. It's been...

(Witness reviews document.)

A. Yes, I do.

MS. HOLLENBERG: And I don't want to make this an exhibit because it's already filed with the Commission. I just wanted to ask about a couple of the statements that are made in the attachment.

CHAIRMAN IGNATIUS: All right.

BY MS. HOLLENBERG:

Q. If you could turn to the attachments, starting on the first page of the article.

A. Yes.

Q. And it's really Page 9, if you see Page 9 at the bottom --

A. Yes, I do.

Q. -- of the magazine. It's -- do you agree that is an article entitled, "Municipalities: Stewards of New Hampshire's Water Infrastructure" --

A. Yes, I do.

Q. -- from the November/December 2012 issue of New Hampshire Town and City Magazine?

A. Yes.

Q. And again, looking at the third paragraph, starting with the third paragraph where it's highlighted, I'm going to read some of the language in that paragraph and ask if I've read it correctly.

Do you see where the author refers there

to "historic underpricing by municipalities for water and wastewater services..."?
A. I do.
Q. And the author continues, "These rates should reflect the full cost of providing these services... however, this has not happened?
A. I do."
Q. And it also states, "The United States has one of the lowest water and wastewater rates in the world, and New Hampshire has rates that are far lower than what one would pay for cable TV or Internet services on a monthly basis"?
A. Yes.
Q. "These services are routinely priced well below the full cost of sustainable operations"?
A. Yes.
Q. And if you'd turn to Page 11 of the magazine article, I believe -- okay. And then there is a paragraph in the bottom right corner that says, "Full Cost of Service Rate Setting." Do you see that?
A. Yes, I do.

Q. And there it says -- the author states, "Water rates should reflect the full cost of service"?
A. Yes.
Q. And turning to the next page, the author states at the top -- do you see the sentence that says, "The public is best served when the true cost of providing the infrastructure services is reflected in the rates they pay"?
A. Yes.
Q. Okay. Thank you.
A. And it's something I've been maintaining for many years, because it leads to conservation.
Q. Thank you.

MS. HOLLENBERG: If I could just have a moment?

(Pause in proceedings)

MS. HOLLENBERG: I don't have any other questions. Thank you.

CHAIRMAN IGNATIUS: Thank you. Ms. Brown.

EXAMINATION

BY MS. BROWN:

Q. Good afternoon, Mr. Landman.

A. Good afternoon.

Q. Do you have Exhibit 17, your testimony, in front of you?

A. Yes, I do.

Q. I'd like to draw your attention to Page 3 --

A. Page 3?

Q. Three lines up, to where you made an edit earlier.

A. Oh, wait. I'm sorry. Looking at the wrong one here. What's it start with? They don't have pages numbered.

Q. It is --

A. What's the question line?

Q. I'm drawing your attention to the sentence you changed, and it started with, "It is noteworthy that neither Manchester" --

A. Yes, okay.

Q. I'm trying make sure we are not talking over each other as well.

A. Okay.

Q. Just now -- and correct me if I'm wrong -- you testified that, with respect to Nashua, the city is charging the city. Do you recall that?

A. Yes. My understanding is that Nashua and Manchester are not charging the city. They're charging outside of the city to other communities they're serving. Nashua serves -- took over for Pennichuck, as I understand it, and serves other communities. They took over the whole Pennichuck system, or most of it.

(Ms. Brown distributing documents.)

Q. Mr. Landman, I just want to show you a document and have you read it. I've given a copy to your counsel. It is a copy of a tariff page from Pennichuck Water Works. And if you could read it to yourself, or not read it vocally.

(Witness reviews document.)

A. Yes. Okay.

Q. And would you agree that Pennichuck Water Works charges a hydrant charge --

A. Yes.

Q. -- for municipal fire protection service?

A. It looks like they do within the city, according to this, because they call it "municipal fire protection service."

"Municipal," I assume it means within the city --

Q. Sorry for interrupting. Do you then have a further alteration to this sentence on Page 3 in your testimony?

A. Well, yes. Apparently I'm in error about that. It would exclude Nashua, because apparently they do charge within the city for that service. They don't just charge external. They have a standard rate.

Q. Thank you. That was the only factual clarification Staff wanted to --

A. Thank you.

CHAIRMAN IGNATIUS: Thank you. Questions from the Commissioners? Commissioner Harrington.

MR. HARRINGTON: Yes.

INTERROGATORIES BY CMSR. HARRINGTON:

Q. Good afternoon. I think your position seems to be pretty clear. Let me make sure I got it.

What you're saying is that somewhere around half of the Town of North Hampton is not served by Aquarion Water Company.

A. That's correct.
Q. But Aquarion Water Company sends the bills for the hydrants in the portion of the town that they do serve to the Town itself, North Hampton.
A. Yes, sir.
Q. And then North Hampton distributes that as just another expense that goes on everybody's property tax bill.
A. That's correct. About $228,000 this past fiscal year -- this year.
Q. And what you're saying is that it would be fairer if the people that were served by Aquarion and had hydrants were the ones who paid for them and not the ones who do not.
A. Yes, because the insurance difference is about 6 percent higher if you don't have hydrants. But in our town, we either require hydrants or fire ponds. And we also have tanker trucks that deliver water so we can fight fires anywhere in town.
Q. Okay. So, as a follow-up to what Ms. Hollenberg said, isn't there any method that the Town could come up with, since it's your

tax dollars, to simply say that people that are served by the water company will pay the fees associated with that as part of a higher tax rate than the people who aren't served by that?

A. I don't know if it's allowed by New Hampshire law, sir. It's not something -- I just don't know. But it's an interesting suggestion, and I'll certainly bring it back to my town and my town manager. But I don't know if it's legally allowed.

Q. But it's safe to say the Town hasn't pursued that option.

A. Have not. Never in my history as commissioner. Never.

Q. That's what I was trying to get at. Thank you.

A. You're welcome.

CHAIRMAN IGNATIUS: Commissioner Scott?

CMSR. SCOTT: No questions.

INTERROGATORIES BY CHAIRMAN IGNATIUS:

Q. Mr. Landman, in your testimony you also described concerns about conservation and mixed messages being sent in this case. And on the final page of your testimony you said, "It may make sense to examine a multi-tier rate structure that will encourage conservation and send the correct price signals on water usage."

Do you know of any structures that you've seen or read about that follow the thinking that you have in your testimony?

A. Oh, absolutely. I mean, it's standard practice in municipalities, and my customers in the utility business -- City of Watertown, South Dakota; Lakeland, Florida; City of San Francisco -- it's common practice. The Company is reverting to that it's going to meter radio reads. And if they get to monthly reads, they cannot only do the tiered -- you know, block usage of water, but the bigger factor is, and the Commission's discussed it today, is leakage and the loss rates. And if you can meter the water and make a measurement at 2:00 or 3:00 in the morning, when hardly anybody's taking showers or flushing toilets or filling swimming pools, hopefully, you will be able to tell where the leaks are. And there are various systems of leak prevention. Itron has a very big system. And people who reduced leaks in their towns by 50 percent in six months, the water rate loss of 28 percent dropped to 14 percent. I mean, metering is essential to get conservation.

I know that DES -- we worked with the DES in technical sessions here at the water commission -- at the water utilities to try to get metering instead of quarterly reads. Even Mr. Naylor and I joked about it one time years ago -- and I'm sure, Mark, you remember -- that you get a shock when you get your bill in September and it's too late to do anything about it and you've used a lot of water to water your lawn. We had a library that had a leak in the toilet, and we got an enormous bill after three months of a water leak. So it eliminates those kinds of charges and waste.

And those of us who've lived here quite a while -- I'm originally from San Francisco, but I've been here since '94. In '95 we had a terrible drought. And you remember we had a moratorium on new hookups. We had, you know, to get conservation going. And we were looking for new wells. And the Company has tried to get new wells. We've got a Coakley Superfund site in our town. So there are a lot of areas with the aquifer, you can't get to it, and we only have so much water.

We've talked about desalinization. I've been on the Rockingham Planning Commission, and we've discussed that. Seabrook has water problems. Exeter has water problems.

So, conservation is what has to be done. And the signal -- the wrong -- the best signal is the cost of water. And if you want to water your lawn in the summertime, you should be paying for it and not the person who gets -- the HUD standard is 5 gallons per minute. And if you're using -- and the average water sprinkler takes about 2 gallons a minute; so if you've got 5 heads, that's 10. So, just sprinkling a lawn is 10 gallons a minute, twice the HUD standard, which is plenty for domestic use.

So there ought to be, you know, whether it's 56,000 gallons a year, whatever it is monthly, we have to change the way we're using -- we're charging for water. And the true cost isn't fire. It's usage. That's, you know...

Q. Thank you.

CHAIRMAN IGNATIUS: Mr. Ratigan, any redirect?

MR. RATIGAN: No.

CHAIRMAN IGNATIUS: All right. Then you're excused. Thank you very much, Mr. Landman. We appreciate your testimony.

MS. BROWN: Staff would like to call Mr. Naylor and Mr. Laflamme as our next witnesses. I believe that's the order.

CHAIRMAN IGNATIUS: All right. As a panel?

MS. BROWN: Yes.

CHAIRMAN IGNATIUS: I assume that's agreeable to everyone? We're kind of in no man's land here in how we're presenting this case. So that works for me.

MS. BROWN: Mr. Naylor has been previously sworn.

CHAIRMAN IGNATIUS: And while they're getting settled, is there anyone else who will be testifying, or is this the final set of witnesses?

MS. BROWN: I believe this is the final. I see some nodding heads.

CHAIRMAN IGNATIUS: All right.

MS. BROWN: Oh, Mr. Laflamme just reminded me he was already sworn in as well yesterday when he testified from the table.

CHAIRMAN IGNATIUS: Oh that's right. We had a group swearing in.

All right. Then the two of you will remain under oath.

MS. BROWN: But I never got a chance to qualify Mr. Laflamme. If I could just quickly do that?

CHAIRMAN IGNATIUS: Please.

(WHEREUPON, *MARK A. NAYLOR and JAYSON P. LAFLAMME* were duly sworn and cautioned by the Court Reporter.)

EXAMINATION

BY MS. BROWN:

Q. Mr. Laflamme, can you please state your name and position with the Commission for the record?

A. (Mr. Laflamme) My name is Jayson Laflamme. I'm a utility analyst with the New Hampshire Public Utilities Commission.

Q. And please describe your area of expertise.

A. (Mr. Laflamme) Accounting and finance.

Q. And is your testimony today within that area of expertise?

A. (Mr. Laflamme) Yes, it is.

Q. And did you file testimony in this proceeding?

A. (Mr. Laflamme) Yes, I did.

Q. And are you aware that it's been marked for identification as Exhibit 10?

A. (Mr. Laflamme) Yes.

Q. And do you have any changes or corrections to make to that testimony?

A. (Mr. Laflamme) No, I don't.

Q. Is that testimony also within your area of expertise?

A. (Mr. Laflamme) Yes, it is.
Q. And are you familiar with the terms of the partial settlement agreement?
A. (Mr. Laflamme) Yes.
Q. And you don't have any -- or do you have any changes or corrections to make to that document?
A. (Mr. Laflamme) No, I don't.
Q. With respect to --
CHAIRMAN IGNATIUS: Before we go any further, I just want to be sure we aren't going back into the settlement agreement. I assume that was addressed before with the panel, and we're not engaging in discussions of that. We're addressing the testimony filed by Mr. Naylor and Mr. Laflamme?
MS. BROWN: Thank you. Good catch. I was just trying to make sure that he was aware of the terms. But you're right. We already covered that yesterday.
CHAIRMAN IGNATIUS: Thank you.
BY MS. BROWN:
Q. Mr. Laflamme, the only question I have for you relates to some potential confusion

yesterday when we were talking about -- or there was testimony about your testimony, Exhibit 10, and Exhibit 18, and where the numbers came from. This was questioning from Mr. Harrington -- or Commissioner Harrington. Do you recall that?

A. (Mr. Laflamme) Yes. Yeah. And I would just like to just correlate the numbers between Exhibit 18 and my testimony.

If you go to Exhibit 18, and I believe it's Page 2 where it starts out on Line 1 and says "Rate Base," and then if you go to my testimony on Page 87 of 127 --

Q. Mr. Laflamme, I'll just ask you to continue. I believe the Commissioners have --

A. (Mr. Laflamme) Yeah. There was some question on the difference between my testimony and Exhibit 18. And if you look at my testimony, Page 87 of 127, it starts out with a rate base of 22,507,605. And that correlates to the rate base number indicated on Exhibit 18, Page 2, which I believe is on Line 2.

And then going back to my testimony, the fourth number down, Operating Income, 1,135,449, that correlates to Item No. 4 on Exhibit 18, indicated as 1,135,450.

So, really, the only difference between my testimony and what is laid out in the settlement agreement has to do with rate of return, and more specifically, ROE.

Q. Are those -- is that the extent of your clarifications?

A. (Mr. Laflamme) Yes.

Q. Thank you.

Mr. Naylor, it came up a few minutes ago that we may need some clarification on the partial settlement agreement and how any revenue requirement is applied to fire protection customers.

And my question to you is: Can you please explain, if Staff is seeking an across-the-board application of the revenue requirement, how that continues to preserve the rate design of Docket 08-098.

A. (Mr. Naylor) Sure. We found out during the break that everybody had a misunderstanding about one little piece of it or another.

But I did testify yesterday that, even

though the settlement agreement is silent on the issue, it was our expectation that the increase would be applied across the board evenly. The confusion came in because the Town of North Hampton is asking for a continuation of the rate design that was unique to the public fire class in the last case. And Mr. Ratigan had brought up the order, showed me a copy of it -- 25,019 is the order number from the last rate case. And so the issue became: Is an across-the-board increase in this particular case, at whatever rate change was found by the Commission to be reasonable, does that preserve the rate design from the last case with respect to the public fire class? And I think we've come to an agreement that the answer is "kind of." We like these "kind of" exact things we do in utility regulation. "Kind of" is something that actually has some value.

And the reason for the confusion is because, when we look at the revenues produced by the public fire class in the test year -- and I'm reading from the Company's filing; it's Page 3 of 171 -- and it shows that the public fire class in the test year contributed $712,387. So that's the amount of revenue the Company received from the public fire class in the test year.

And I think the misunderstanding came, at least on my part, from why is the Town objecting to an across-the-board increase in this particular case when an across-the-board increase still preserves the rate design from the last case? In other words, those revenues -- that $712,000 revenue is based on the rates that were approved in the last case. Those rates were based on a 70 percent allocation of the applicable costs for serving the fire protection class -- serving the fire protection customers.

In addition to that, there were some fees that were allocated, some increase, I believe, in miscellaneous service fees. That's discussed in the Commission's order. Settling parties in the last case agreed to dedicate those fees to the public fire class to help reduce those rates that were set for that class.

So where we are now is, I think we still have a disagreement with North Hampton, but at least we understand what we're disagreeing on. And that is: While an across-the-board increase in this particular case, for the most part, preserves that 70 percent allocation, it doesn't preserve or maintain or create a 70 percent allocation of any of the new plant or new costs that have -- that are going into rates in this case. So it's just that incremental piece. North Hampton and the three other public fire customers are getting just a simple allocation and an equal allocation of costs based on an across-the-board increase. I think once we -- if we did the numbers, we would probably find that the difference is very small. It's probably a pretty small number.

So I think the way we came out of that discussion was Staff continues to support an across-the-board increase. The four municipal -- the four public fire entities are still substantially benefiting from the rate design approved in the last case. And when the Company is in again, they will file a cost of service study with their next case, and we will begin the debate anew. But that's kind of where we stand at this point.

MS. BROWN: I have no further questions.

CHAIRMAN IGNATIUS: All right. Let's begin cross-examination with the Company.

Mr. Taylor, do you have any questions?

EXAMINATION

BY MR. TAYLOR:

Q. Mr. Naylor, Mr. Laflamme, good afternoon.

A. (Mr. Naylor) Good afternoon.

Q. Mr. Naylor, referring to your testimony on Page 7 -- and I'll specifically refer you to Lines 9 and 10. In this case, the Staff has utilized a return on equity that is lower than recently approved equity returns to reflect the reduction of risk with the WICA. Have I read that accurately?

A. (Mr. Naylor) Could you give me that page reference again?

Q. Sure. I didn't mean to get ahead of you. Page 7, just on Lines 9 to 10.

A. (Mr. Naylor) Yes, that's correct.

Q. Okay. This implies that the Staff believes that the Company would be entitled to a higher return on equity without the WICA. Is that an accurate statement?

A. (Mr. Naylor) Higher than the 9.25 that's here in the testimony?

Q. Yes.

A. (Mr. Naylor) Sure. Right. I mean, my testimony -- and I made it -- hopefully made it clear that I'm not sponsoring a particular number. I was using this more for illustrative purposes. But I was using -- taking off, I believe, from the 9.75 that the Company was awarded in the last case.

So, without a WICA, I guess all other things being equal, 9.75 would be the number.

Q. Okay. Well, you also note in your testimony, in No. 5, same page, that the most recently approved equity returns granted by the Commission to water utilities in several

dockets have been 9.75; correct?
A. (Mr. Naylor) That's correct.
Q. And in fact, Lakes Region Water Company received a 9.75 return on equity as recently as July 2012; is that correct?
A. (Mr. Naylor) I believe that's correct, yes. Yes, that was --
Q. I can show you a copy of --
A. (Mr. Naylor) It was the full rate case, yes.
Q. You've not done any specific analysis to determine what the amount of reduction on return on equity should be as a result of WICA; am I right?
A. (Mr. Naylor) You are right.
Q. You provided testimony in the most recent Pennichuck Water Works and Pittsfield Aqueduct cases, supporting the implementation of a WICA program for those companies; is that right?
A. (Mr. Naylor) Yes.
Q. And the Commission authorized a 9.75 percent return on equity in those cases?
A. (Mr. Naylor) I believe so.
Q. And in fact, Pennichuck Water Works and

Pittsfield Aqueduct do, in fact, have WICA mechanisms following those cases; is that correct?

A. (Mr. Naylor) They were both authorized to have WICA pilot programs, yes.

Q. Mr. Naylor, I'm going to give you -- bear with me for a moment. I'm going to give you an excerpt of your testimony in that case.

MR. TAYLOR: I'll provide copies to the Commission as well. This is a copy of testimony that was provided in a prior docket. I don't know that we need to mark it as an exhibit. I would ask you to take notice of it. And I'll just note that these are not the complete copies but excerpts.

CHAIRMAN IGNATIUS: Make sure they're distributed to counsel and others.

MR. TAYLOR: Oh, I'm going to.

(Atty. Taylor distributes document.)

BY MR. TAYLOR:

Q. Mr. Naylor, referring to Lines 18 and 19 on Page 3 of your testimony in the Pennichuck case --

CHAIRMAN IGNATIUS: Before we do

that, for the record, let me just -- this is in DW 10-091. And testimony dated March 31st, 2011 is what you've distributed --

MR. TAYLOR: Yes, this is a --

CHAIRMAN IGNATIUS: -- a short excerpt from it?

MR. TAYLOR: Yes. This is an excerpt of Mr. Naylor's testimony from DW 10-091.

BY MR. TAYLOR:

Q. Referring to Lines 18 to 19 on Page 3 of your testimony, you stated that Staff would support structuring a WICA for Pennichuck -- well, in PWW. But that is very similar to the pilot program in place for Aquarion. Have I read that correctly?

A. (Mr. Naylor) Yes.

Q. Nowhere in your testimony submitted in the Pennichuck or Pittsfield cases did you condition Staff support for the WICA program on a reduction to return on equity; am I correct?

A. (Mr. Naylor) You are correct.

Q. And Staff recommended the use of a 9.75

return on equity in those cases; is that correct?

A. (Mr. Naylor) As far as I know, yeah. Of course, they just barely started their WICA program. The company hasn't even filed for surcharges. So it's just getting started.

Q. And when the Commission approved -- in the orders approving permanent rates and the WICA mechanisms in those programs, in those cases the Commission did not condition approval of the WICA program upon any reduction in equity; is that correct?

A. (Mr. Naylor) Not to my recollection.

Q. Mr. Naylor, the Commission has approved various capital adjustment mechanisms for gas and electric utilities, such as the Cast Iron/Bare Steel Replacement Program and the Reliability Enhancement and Vegetation Management Plan. Are you familiar with those mechanisms?

A. (Mr. Naylor) To some extent, yes.

Q. Those mechanisms involve the replacement of infrastructure and annual rate adjustments; am I right?

A. (Mr. Naylor) Correct.
Q. And isn't it true that the Commission has not conditioned approval of those mechanisms on a reduction to a utility's return on equity?
A. (Mr. Naylor) To my knowledge, they have not.
Q. Mr. Naylor, you've provided your opinion that Aquarion's return on equity should be reduced due to the existence of the WICA mechanism. But you've not cited to any order from New Hampshire or any other jurisdiction supporting this premise; correct?
A. (Mr. Naylor) Well, sometimes we need to break new ground I think.
Q. But you've not cited any studies, scholarly articles, analyses, or anything of that nature supporting this premise in your testimony; is that correct?
A. (Mr. Naylor) No, just my opinion.
Q. And you've not provided any analysis demonstrating that, compared to its peers, WICA makes Aquarion a less risky investment; is that correct?
A. (Mr. Naylor) In comparison to its peers? No.
Q. And just to revisit something that was

addressed earlier, the actual -- and this was addressed with Mr. Parcell's testimony, I believe -- the actual percentage of WICA revenues relative to the Company's overall revenue is quite small; am I right?

A. (Mr. Naylor) Yes. The percentage of the revenues -- I think the first year their percentage was about 1.5, and then the second year was about an additional 2 percent. So it's relatively small. However, the percentage of the Company's total capital expenditures that are comprised of WICA expenditures is substantial. It's more than 50 percent of their capital spending on an annual basis. So, from that perspective, it's pretty significant.

Q. Mr. Naylor, I know you heard yesterday Mr. Welch and Mr. Bean, on behalf of the Town, gave statements opining that Aquarion was -- I believe one of them said it was an "outstanding company," and I believe -- I don't want to specifically characterize their testimony because I don't have it in front of me. But I believe the general tenor of their

opinion was that it was a well-run, well-operated company?
A. (Mr. Naylor) I did hear that testimony.
Q. Okay. Would you agree -- or is it in your view -- is it your view that Aquarion Water Company of New Hampshire is a well-managed and effectively run operation?
A. (Mr. Naylor) Yes.
Q. Is it fair to say that Lakes Region Water has had a history of management and operation problems?
A. (Mr. Naylor) Yes.
Q. And just to revisit what I said earlier, Lakes Region, within the past year, was given a return on equity of 9.75 percent; is that correct?
A. (Mr. Naylor) Yes, with no analysis. Just simply carrying forward the rate that a number of companies have been receiving in the last few years.
MR. TAYLOR: Can I have a moment just to...
CHAIRMAN IGNATIUS: Please.
(Pause in proceedings)

MR. TAYLOR: That will do it for the Company on cross.

CHAIRMAN IGNATIUS: All right. Thank you. Mr. Ratigan.

MR. RATIGAN: No questions.

CHAIRMAN IGNATIUS: Mr. Gerreald.

MR. GEARREALD: Thank you.

EXAMINATION

BY MR. GEARREALD:

Q. Mr. Naylor, your attention was drawn to Page 7 of your testimony. I'd like to go there once more.

Staff -- on Page 7, Line 8, you indicated Staff is utilizing a return -- a cost of equity of 9.25 percent in calculating Staff's revenue requirement recommendation, assuming continuation of the WICA. And no different figure is being put forth today by you for that purpose, is it?

A. (Mr. Naylor) No. No. As I indicated, it's simply -- I think I said it yesterday. It's essentially a placeholder to illustrate -- certainly from Staff's perspective, we wanted to present a revenue requirement recommendation. So Mr. Laflamme's testimony sponsoring a revenue requirement needed a number, so that's what we used.

But we also indicated on Lines 10 through 12 that we had an understanding that your client had retained the services of Mr. Parcell for sponsoring the cost of equity.

Q. Well, even more than being a placeholder, Mr. Laflamme engaged in a whole analysis of what the revenue requirement would be using the 9.25 percent; correct?

A. (Mr. Naylor) Yes, that's right.

Q. And the figure he came up to for a revenue requirement corresponding to 9.25 percent was -- and I guess I'm asking Mr. Laflamme this.

Mr. Laflamme, your figure utilizing 9.25 percent was $857,810; correct?

A. (Mr. Laflamme) My calculated revenue deficiency was 857,810.

Q. So if 9.25 percent were selected by the Commission, that would be the number rather than the Company's suggested 10.25 percent; correct?

A. (Mr. Laflamme) Yes.
Q. And their figure on 10.25 percent was $1,077,924; correct?
A. (Mr. Laflamme) I'm sorry. Could you repeat that number?
Q. The Company's figure at 10.25 percent was $1,077,924; is that right?
A. (Mr. Laflamme) Yes, but that was as a result of their response to Staff Data Request 3-11.
Q. Yes.

Mr. Naylor, turning back to you. You put out a footnote on Page 7, where you indicated that the most recently approved equity return granted by the Commission for water utilities was a certain number. Those particular cases were not litigated cases; is that correct?
A. (Mr. Naylor) That's right.
Q. And these particular cases -- of course, this one is a litigated case; correct?
A. (Mr. Naylor) Yes.
Q. And none of those other dockets had the DCF analysis presented; right?
A. (Mr. Naylor) That's right.

Q. None of them had the ranges of DCFs that were put forth as we have here of Mr. Parcell at 9.0 percent to 9.6, and Ms. Ahern's range as revised today within that same range; correct?
A. (Mr. Naylor) Correct.
Q. Now, you will continue to stand by, I take it, the position that having the WICA mechanism in place for as long as it's been in place here, with three years of increases added, should reduce the risk of the Company and, therefore, the return on equity; correct?
A. (Mr. Naylor) Yes, that's right.
Q. And I believe from my discussion with you, your opinion in this regard is also influenced by the fact that we are at very low borrowing rates that have been in place for a number of years now; correct? That's an influence on your view as well; is it not?
A. (Mr. Naylor) Well, I think that's true. And certainly the fact that, I think Mr. Parcell testified to this, to some extent there's a speed-up of the Company's cash flows and a

little bit more certainty in their revenues and their earnings. So I think that all plays into it.

MR. GEARREALD: Thank you.

CHAIRMAN IGNATIUS: Ms. Hollenberg.

MS. HOLLENBERG: Thank you.

EXAMINATION

BY MS. HOLLENBERG:

Q. Mr. Naylor, would you agree that the 9.75 return on equity that Lakes Region Water Company was awarded recently was the result of a comprehensive settlement agreement?

A. (Mr. Naylor) I asked myself that question when Mr. Taylor asked me. And I paused for a section because I just couldn't remember if we had a settlement in that docket. So I'm going to take from your question that, yes --

Q. Now you're making me wonder.

A. (Mr. Naylor) We do a lot of work here, so it's -- can't always remember from case to case. But --

Q. I'm being corrected. Then I guess it wasn't. So I'll withdraw my question. Thank you.

CHAIRMAN IGNATIUS: All I know is we had five or more days of hearings. So it didn't settle much.

[Laughter.]

MS. HOLLENBERG: I blocked it.

MR. CAMERINO: Well, this was a settlement, except for...

CHAIRMAN IGNATIUS: Ms. Brown.

MS. BROWN: I have no redirect, other than to state that Staff was an advocate in that docket of Lakes Region, designated as a Staff advocate. So I doubt we had a settlement.

MR. NAYLOR: Good point.

CHAIRMAN IGNATIUS: Questions -- you're done, Ms. Hollenberg?

MS. HOLLENBERG: Yes. Thank you. I apologize.

CHAIRMAN IGNATIUS: That's all right.

Questions from the Bench? Commissioner Harrington.

MR. HARRINGTON: Just a couple questions, just so I understand.

INTERROGATORIES BY CMSR. HARRINGTON:

Q. In your testimony on Page 7, Mr. Naylor, what you're basically -- you're using this as an indication. The 9.25 percent is not the one you're recommending to be awarded in the case, but simply that it should be something less than the 9.75 that was previously there because of the -- now that the WICA program's been around for a while.

A. (Mr. Naylor) Exactly right.

Q. And as was somewhat determined, the 9.75 that's been used for water companies is sort of a historical thing that's been carried along here, and no one seems to be exactly clear when the last analysis was done for that.

A. (Mr. Naylor) Yeah. I think it was the Pennichuck case, and I think Mr. Parcell actually provided some testimony in that case. And what was brought out this afternoon for exhibits were snippets of Mr. Parcell's testimony. So I think it was a Pennichuck case. I'm not sure if it was a '06 rate case or a '08 rate case, but...

Q. And you heard both of the expert witnesses, one for the Company and one for the Town. And they -- when you looked at the DCF rate, they were fairly close.

Do you have any opinion as to the accuracy of those figures for ROE?

A. (Mr. Naylor) I cannot really give you an opinion on it. I can't hold myself out as having any expertise in that area. As much as I tried to keep up with it and sort of gain, you know, an understanding of how it all fits together, I'm not comfortable with providing an opinion.

Q. Let's move on to a slightly different area then.

There's been, you know, testimony presented that the Company has been under-recovering since the last rate case; is that correct?

A. (Mr. Naylor) Yes.

Q. And what's the major reason for that?

A. (Mr. Naylor) Well, I don't recall specifically if there's things that the Company has indicated to us through discovery or in other ways. My suspicion would be that their circumstances are very similar to most other companies, particularly those companies that are in, you know, a mode of capital spending, you know, on a very regular basis and experiencing cost increases.

Q. But some of it would be associated with their reduction. They didn't sell as much water as they planned and the tax rate went up faster than they planned?

A. (Mr. Naylor) Absolutely. Yeah, absolutely. The only way a company is going to earn its authorized rate of return is if all the projections, if you will, from using the test-year data to set rates and provide some pro forma adjustments that are appropriate to that test year, if all those assumptions stay exactly the same, they sell the same amount of water they sold in the test year, their expense levels stay the same as they were in the test year, and their capital spending is no greater than the rate of depreciation on their existing plan of service, that way they'll earn exactly their rate of return going forward. In real life, that doesn't happen.

Now, how do companies -- because there are companies that are able to maintain their rate of return, even though their costs increase, even though they have capital spending, and that's because they have growth in their franchise areas. And so they're adding new customers. And the amount of incremental capital they need to invest to serve those customers is very small. Of course, that builds up over time until they need large investments. But there has been virtually no growth in this state for the last four or five years. No housing starts, no new developments, no -- very, very little commercial development. So that's a factor, too.

Q. And the authorized rate of return for the Company, would that be the same under this proposed settlement agreement as it was in the past? How does that work?

A. (Mr. Naylor) Well, the authorized rate of return is what you are being asked to approve through this hearing now.

What the settling parties here have agreed to and recommend to you is a capital structure in certain proportions, which is in the settlement agreement that was provided, and recommends to you a certain cost of debt. So all you have to do is make your determination as to what you think the appropriate cost of equity is, plug that in, assuming you also approve the settlement. That will establish the authorized rate of return for this company going forward. Then, each year subsequently, the Company will measure its achieved rate of return, its actual rate of return based on all of its operations, and measure that achieved return against what you authorized. That will help them make decisions as to the timing of their next rate relief and so on and so forth.

Q. One last thing on the ROE -- well, maybe you've probably addressed that sufficiently. That's all the questions I have.

CHAIRMAN IGNATIUS: Commissioner Scott.

INTERROGATORIES BY CMSR. SCOTT:

Q. Okay. So it's getting later, so I think I'm getting muddled now.

So does the Staff have a final position on cost of equity?

A. (Mr. Naylor) We're leaving that to your wisdom. I wish, now as I look back at my testimony, I wish I was more clear in this Page 7, in the Q&A that begins on Line 6, because I said on Lines 10 to 12, "It's Staff's understanding that the Town of Hampton has engaged the services of a cost of capital consultant to provide testimony in this case."

So I wish I had made it more clear that we expected the issue of return on equity to be ultimately something that was going to be, you know, thought out, whether we ultimately reached a settlement or not.

But you have to recall that when the Company made its original filing, it did not include testimony from an expert witness. The Company provided a recommendation for return on equity, but it was based on its study of returns granted in other jurisdictions. That was kind of the starting point for it.

At the time we did the testimony, we used the 9.25 as a placeholder, but we expected it to be -- expected it to get to this point and either settle between the Company and the Town or litigated.

Q. And perhaps to paraphrase, so you don't have a definitive number as your position, but you -- the number, in your opinion, again, would be because of the presence of a WICA that's been ongoing and continuing into the future, that that ROE number should be something less than if there was no WICA in place.

A. (Mr. Naylor) Correct. Yeah.

Q. All right. I'll move on then.

Yesterday, I believe it was, we had some discussions regarding peak demand and conservation and reduction efforts. I was just curious -- and for either of you -- if you had an opinion on was there much venue left for cost-effective measures to reduce peak demand? I'm just curious if there was any low-hanging fruit, in your opinion.

A. (Mr. Naylor) I know that prior to the query on ownership going back into the '90s, prior ownership had embarked on a considerable effort to encourage conservation. And in fact, one of the cases back in the '90s -- and I couldn't tell you which one; I would guess somewhere in like the '97 range -- they sought a recovery of costs related to a number of their conservation efforts. And this related to, you know, the shower head fixtures, other types of fixtures and some other things. I don't recall all the details of it. Plus sort of a marketing campaign. And they asked for a recovery of costs related to that.

It's important -- and I'm remembering the testimony yesterday, and it struck me that the folks that are here today representing the Company may not know the history back in the '90s when I was -- you know, first 10 or so years I was here. Mr. Landman, I think, alluded to it a little bit earlier. This was a company desperately seeking new sources of supply for quite some time. There was a lot of problems. The seacoast was growing substantially back at that time. This Company was very focused on seeking out new sources of supply.

And it struck me -- and I think it may have been your question to Mr. McMorran, I believe, about, you know, you got all this aging infrastructure. How come there wasn't a plan to deal with the distribution system a long time before this? And that's when it struck me that, at least for the period of time prior to the ownership of this utility by Aquarion, a lot of the focus, a lot of the money was going into new sources of supply. And there was a number of issues with that. And I think one of the proposed well sites was near a contaminated landfill or something. I forget all the details. But they had a lot of problems with supply.

So I think the Company, in those days, was making a lot of effort to try to tamp down demand because it was such a difficulty with the supply. I don't get the sense from hearing the testimony of the Company's witnesses now that there's as much of a problem with the supply. There seems like there's plenty of supply. So I don't know if -- really, I don't know how much of a real problem that is. I really don't have a good feel for that, whether that peak -- you know, the peak day is really a problem or not. So...

Q. So let me go back to my question.

So I was just curious. For conservation efforts, regardless of supply, do you think there's low hanging fruit that perhaps the Company hasn't addressed?

A. (Mr. Naylor) I'm not aware that there is any. I know that we've had limited discussions about looking at some rate design things. I mean, I think that's worth looking at again in more detail. You know, there's some problems that we were talking about inclining blocks, where, you know, higher users went into a higher block, where they pay a lot more per gallon or per 100 cubic feet or whatever for use. That can have some adverse effects, too, because that can -- that may change those behaviors quickly.

But, you know, if there's things we can do in rate design, we should definitely consider it. And I think the Company is understanding, coming from this case and our discussions that we've had, that there's an expectation in the next case that the Company should probably come in with some ideas for us to consider.

Q. In your earlier comments, you anticipated -- you went back to the questioning I had this morning regarding aging infrastructure. And I laid out to the Company -- I believe I asked them, effectively: Does the WICA fix the problem of the aging infrastructure? And I don't think I got a warm and fuzzy that it did.

I was just curious if you had a thought on how -- again, this is an industry-wide problem I think. But where do we go from here? Obviously, WICA is a help. Do you agree with that?

A. (Mr. Naylor) Well, I think so far, yes. My testimony does address that, in terms of the task was partly in this case to evaluate the WICA after so many years it's been in as a pilot. And of course, the recommendation is to continue it as a pilot for another rate case cycle. And I think, as I indicated in testimony, there is some data that the Company has accelerated the replacement. So, I mean, from that perspective it's helpful.

But we've had some interesting testimony yesterday and today, you know, what the push-pull is. You know, pressure of rates versus the pressure on the Company to improve its distribution system, to replace the 81,000 feet or whatever it is of a pre-World War II distribution main. I mean, it's just -- and it's not just this company. It's lots of systems that have -- that were installed either in the late 1800s, early 1900s. And, you know, they worked pretty well for a long time, and then things have changed. The Safe Drinking Water Act and other types of requirements, environmental regulation, is much stricter than it was years ago. So that kind of put us where we are.

But I think the WICA is worthy of extending, as we indicated in the partial settlement. And we'll look at it again when they come in the next time.

Q. And I think we have a record request for a five-year -- their five -- their existing five-year plan.

Would you agree that, certainly under those circumstances of this aging infrastructure, that long-term planning would be of great value?

A. (Mr. Naylor) Yup. Certainly. And interesting, too, that the partial settlement calls for the Company to make some changes to the WICA for the next cycle here, essentially continuing as a pilot. But the settlement calls for an updated main replacement prioritization analysis, an updated infrastructure inventory. So, we're going to get some new data that will help us in the next WICA filing, which, I guess, will be made by November 1st. I forget exactly. Somewhere in the late fall.

CMSR. SCOTT: Thank you. That's all I have.

INTERROGATORIES BY CHAIRMAN IGNATIUS:

Q. Mr. LaFlamme, we haven't forgotten about you.

If you remember, Exhibit 18 was the revenue requirement exhibit that took the adjustments that had been agreed upon in the post-settlement, as well as adjustments you had proposed in your testimony, and then it employed a 9.75 rate of return -- excuse me -- ROE. Do you remember that Exhibit 18?

A. (Mr. LaFlamme) Yes.

Q. Have you calculated what you would get to for a revenue requirement using different ROEs? Or could you do that?

A. (Mr. Laflamme) I have not. I have not previously, but...

Q. I'd like to ask you to do that -- and we'll reserve a record request -- of taking that same structure of Exhibit 18, but doing a couple of different runs. We already have 9.75. I guess what I'd ask you -- I haven't thought about all the numbers. One would be 10.25; one would be the two DCF numbers that we received, 9.3 and 9.43. And, I mean, they're all so close. The 9.4 was Mr. Parcell's number with his DCF midpoint and his comparable earnings midpoint. So, perhaps we don't need all of those. 9.3, 9.4 and 9.43, they're all fairly close.

But what would you recommend? What do you think is the soundest way to see some comparisons of the numbers we've been looking at?

A. (Mr. Laflamme) I could do the 10.25 and the 9.4.

MR. CAMERINO: Could we also clarify for the Chair? This might be helpful. We don't have any problem, obviously, with the running scenarios. But on the bottom of Exhibit 18 -- I'm not sure what line it was -- there was a "how many dollars for 100 basis points." And my understanding, and the witness can confirm this, is that you can literally do that pro rata. So if you wanted to add 400 basis points, you would add that. But if you only wanted to add 50, you would just take half of that dollar amount. It's not like there's some other factor that gets applied.

MS. BROWN: And that's in Dixon's testimony, correct, oral testimony?

MR. CAMERINO: It's right on the exhibit.

CHAIRMAN IGNATIUS: Yeah, you're right. It's that bottom box on the second page of that exhibit I'd forgotten about. So this is sort of like expanding a recipe. It will still work if you double it or if you cut it in half. All right.

Then maybe we don't need to reserve an additional record request for it. I just do want in the record to have some calculation of what the impacts are.

BY CHAIRMAN IGNATIUS:

Q. Actually, I do want it. Why don't you go ahead and do it, because then to run, what, the percentage increases as well would be helpful.

A. (Mr. Laflamme) Okay.

Q. So why don't we take the 9.4 and 10.25 as two numbers that we can get some sort of a sense of the impacts and percentage increases that would result, given the debt equity structure that is being proposed by -- in the settlement agreement.

MS. BROWN: Madam Chair, do you have a deadline by which you're suggesting this begin?

CHAIRMAN IGNATIUS: Well, we'll have to talk about that for all three record requests. Why don't we do that at the end.

MS. BROWN: Okay.

BY CHAIRMAN IGNATIUS:

Q. On Exhibit 32, which was the chart that Aquarion developed, looking at the capital structure and then applying a 9.6 ROE to the actual capital structure and to a hypothetical capital structure that was a little bit different, Mr. Naylor, have you looked at that chart, and do you have a -- do you remember what was being developed going through those numbers?

A. (Mr. Naylor) Yes. Yeah, I had a couple of concerns -- well, not concerns. Just a couple things didn't quite make sense to me.

Q. Why don't you elaborate on that.

A. (Mr. Naylor) Okay. In all three of the blocks, the Company is using the dollar amounts for their different capital. And they stay the same. I don't have the other numbers right in front of me. But I think that's their actual capital structure as it exists at the end of 2012.

But they change the component percentages in the second block. And I think it's kind of done on a *pro forma* basis. But that's not the actual percentage. In other words, for debt in the top block, it's 59.24 for the 13.9 million. It can't be 55 percent for the same 13.9; right? So I think it was done on a *pro forma* basis to illustrate, to make the points that they wanted to make, in that the effective change in the component percentages and factoring in the amount of tax, they have more or less equity in the capital structure than the Company. The revenue requirement has to change to accommodate more or less tax because taxable return on equity is taxable. So that was kind of what my question was.

I understood the premise of the exhibit and what they were trying to illustrate. And I think they successfully illustrated it. But that piece of it didn't really make sense to me.

Q. There was a question that Mr. Taylor asked at the beginning of this, of your taking the stand, noting that Aquarion's been described as a "well-run and well-managed company." I think you agreed with that, didn't you?

A. (Mr. Naylor) Yes, I did.

Q. And it is coming out of a prior case at a 9.75 ROE and then comparing that to a water utility that's had a more troubled past, in terms of management, and that that also recently received a 9.75 ROE. Do you recall that?

A. (Mr. Naylor) Yes, I do.

Q. I took the import of that question to be, then, a well-run company should have a higher ROE because it's better managed. And I'm not sure if that was what the meaning of it was.

But that's what I thought the point of where we were going with it.

Is that your view? Should an ROE be a reward for something that's well run?

A. (Mr. Naylor) Yeah, that's a good question. And conversely, should a company be, quote, unquote, punished for poor performance by having its return reduced? I don't know. I'm not sure. I think it's a valid point that the Company is making.

And, you know, I wondered when we did the testimony for this case if the approach we took was the right way to go with trying to make a point with respect to our feeling about risk, a little bit of a risk reduction. But we felt it was an important point to make. And we certainly heard Mr. Parcell echo that to some extent. But it kind of put us in a dilemma because we were sponsoring cost of capital testimony. So, you know, what do we do?

But to the point of whether the Company should be rewarded, the Company is of a size that it's sponsoring cost of capital testimony. And I'm not sure we could see companies like Lakes Region or some of the other ones -- I mean, the cost could be prohibitive. Rate case expense passed on to customers, it's not realistic I don't think.

Q. All right. Thank you. All right.

CHAIRMAN IGNATIUS: Any redirect, Ms. Brown?

MS. BROWN: Thanks for getting back to me. Even though I spoke out of turn earlier, I still have no redirect. Thank you.

CHAIRMAN IGNATIUS: And the witnesses are excused. Thank you very much for your testimony.

And I believe that's it for witnesses? Yes?

MS. BROWN: Correct.

CHAIRMAN IGNATIUS: Then the final issues that I think we have to take up, but please add to my list if I'm wrong, are to first to ask if there's any objection to striking identification and making all exhibits permanent exhibits, full exhibits in the file. Any objection?

MS. HOLLENBERG: Actually, I would like to make an objection to the portion of Ms. Ahern's testimony that relates to the risk adjustments, which are found at the end of the testimony. I think that those are not necessarily rebuttal of Mr. Parcell's testimony. Neither the Company on direct through Mr. Dixon, nor Mr. Parcell discussed risk adjustments. And so the risk adjustment -- so Ms. Ahern -- my understanding is that she goes through Mr. Parcell's testimony, the first part of it, and makes corrections to it, which arguably is appropriate to do in rebuttal, and then goes further and introduces these concepts of these risk adjustments that have not yet been provided on direct. So I would argue either that it be excluded -- that portion of the testimony be excluded or given no weight. Thank you.

CHAIRMAN IGNATIUS: Mr. Camerino.

MR. CAMERINO: I really don't understand the basis for not admitting it into evidence. The Company put forward its basis for allowed ROE. That was in Mr. Dixon's testimony. And he indicated why the Company did not hire an expert witness, which had to do with the practice of the water company and their desire to save money. The Town of Hampton responded with an analysis of ROE. And Ms. Ahern's testimony was submitted to say that's not a correct analysis; you need to make these corrections, and included in the corrections are these adjustments if you want to determine what the proper ROE is. So it was her response and a list of things that were incorrect. And one of the things that Mr. Parcell didn't do, obviously because he doesn't believe in it, was to make those adjustments. So it was very much responsive.

CHAIRMAN IGNATIUS: I'm going to deny the request. I think we do see at other times certain adders put onto ROEs after the base DCF analysis has been done. So I don't find that inappropriate to have asked for those adders, even in the context of it being described as rebuttal testimony.

I'm also troubled that it comes out now rather than at the time of the testimony being filed, when there could have been a motion to strike, or at the time of the testimony being cross-examined today. So I'm going to deny that request.

Is there any other objection to striking identification and making all of the documents full exhibits?

(No verbal response)

CHAIRMAN IGNATIUS: Seeing none we'll do so.

We have a question of when the record requests are to be filed. There are three that I'm aware of. Let me make sure we are all in agreement on this.

Exhibit No. 20 was Record Request 1. It was requested by Commissioner Harrington on the volume of water involved in the 17 leaks that were discovered in the leaks survey.

Exhibit 25 -- that's not right. Wait a minute. Exhibit 24 is the Company's five-year plan developed in 2013.

And Exhibit No. 33, I guess we didn't mark, is what I just asked for from the Staff, to develop some ROE comparisons using the different percentages that we talked about.

MS. BROWN: With respect to the record request, Exhibit 33, Staff can turn around, once it has the Excel spreadsheet or the formulas from the Company, it can turn it around in a day or so. So I don't expect we are going to be a hold-up in supplying the record request.

CHAIRMAN IGNATIUS: All right. And Mr. Camerino or Mr. Taylor.

MR. TAYLOR: I was going to say it shouldn't be a problem for us to provide Excel information about the leaks. Again, I think we can do that fairly quickly.

On the five-year plan, we'll need to confer with the Company to see how long that would take. Obviously, we'll turn that around as quickly as possible.

CHAIRMAN IGNATIUS: See, I would have thought that would have been the fastest to produce because it's a document that exists, and it's just a matter of reviewing the confidentiality issue and submitting it.

MR. TAYLOR: We can provide a response to that request next week.

CHAIRMAN IGNATIUS: All right. Is next Friday, a week from today, sufficient for all three record requests?

MR. TAYLOR: Yes.

MS. BROWN: From Staff, yes.

CHAIRMAN IGNATIUS: Then at the close of business Friday, June 1st, May 31st?

MR. CAMERINO: May 31st.

CHAIRMAN IGNATIUS: May 31st. All right.

Is there a request for written closings or a desire to have oral closing statements?

MR. TAYLOR: We would request that we provide oral closing statements. I don't think it will take a long time. If the Commission -- I realize that the hour is very late. But oral closings will enable us to bring this hearing in this rate case, at least this portion of it, to a conclusion today. With written -- pardon me.

With written closings, that will put additional time on this case. We'll have to stagger when they're due, because we would need a response -- or we would expect to be able to respond to what was provided in some of the other closings. Traditionally, we would have the opportunity to go last, I would think.

And so I think, just for purposes of getting the order out and bringing this to a conclusion, I think we can do it today if the Commission is willing to entertain us for a while longer.

CHAIRMAN IGNATIUS: Other parties' comments? Mr. Gerreald.

MR. GEARREALD: My thought on that is we have three exhibits, anyway, that are not even yet seen. We had changes that came in today from an expert on return on equity from the Company's end that we had not seen.

I believe a week -- a

simultaneous filing of closings, written closings, would be helpful. A week from the production of the extra exhibits would be the most fair, given the hour especially.

CHAIRMAN IGNATIUS: Ms. Hollenberg.

MS. HOLLENBERG: I am not opposed to doing oral closings, but I am opposed to doing them this afternoon. I've been battling not feeling well, and I feel extraordinarily sick at this point in time. So I'm not able to stay much longer.

MS. BROWN: Staff is prepared to go forward with its oral closing.

CHAIRMAN IGNATIUS: All right. One moment.

(Discussion off the record among Commissioners.)

CHAIRMAN IGNATIUS: All right. I think because we are, as Mr. Gerreald points out -- because there are three exhibits missing that are of importance to us, I think we are going to hold off on closings and wait until we receive those. What we'd like to do is have written closing statements. They don't have to be extensive. They don't have to be legal briefs. And they certainly don't have to recount every bit of testimony.

What I'm wondering is, do people want to have the transcript first before you do so or not? That would speed it up if it's without a transcript. I would say Mr. Gerreald's suggestion of one week after the final exhibits are received -- so, the following Friday -- would make sense, or two weeks later if you'd like. If you need a transcript, then we've got to extend that out a bit to have time for the court reporter to put it all together.

MS. BROWN: Staff can say we that don't need the transcript.

MR. TAYLOR: We don't need the transcript. And I think we'd like to do it sooner than later.

MR. GEARREALD: I think that's true as well. I agree.

CHAIRMAN IGNATIUS: All right. Good. Then is one week after the submission of the record requests -- well, actually, they may come in at staggered dates.

If the record requests are due no later than May 31st and written statements due no later than Friday, I think that's June 7th, is that acceptable to everyone?

MS. BROWN: Yes, ma'am.

CHAIRMAN IGNATIUS: I won't ask for a page limit because people seem to be concerned that they're being unfairly limited from what they need to say. But you don't need to write 100 pages. We don't judge the value of what you say according to how thick the stack is. And, you know, we have heard all the testimony. We've been attentive to your arguments. And so it's really sort of a summary of where you think we come out in your recommendations or solutions.

Mr. Ratigan.

MR. RATIGAN: Could there be a reward for --

[Laughter]

CHAIRMAN IGNATIUS: Sometimes it might be that way.

All right. Is there anything else? If not, again, I want to thank you for yesterday. It was very odd to begin at 2:30 in the afternoon and to go until a little after 7:00. That's hard, I know. And all of you had to go back and get prepared for the next day, and that makes it an even more difficult task. So we really do appreciate it. We're running late heading into Memorial Day weekend, and so thank you for all your time and focus and trying to do what we could to make it move expeditiously. I'm pleased we reserved another day and we don't need to take it. So, thank you for that.

And with that, we'll take all of this under advisement and are adjourned.

(Whereupon the hearing was adjourned at 5:12 p.m.)

C E R T I F I C A T E

I, Susan J. Robidas, a Licensed Shorthand Court Reporter and Notary Public of the State of New Hampshire, do hereby certify that the foregoing is a true and accurate transcript of my stenographic notes of these proceedings taken at the place and on the date hereinbefore set forth, to the best of my skill and ability under the conditions present at the time.

I further certify that I am neither attorney or counsel for, nor related to or employed by any of the parties to the action; and further, that I am not a relative or employee of any attorney or counsel employed in this case, nor am I financially interested in this action.

____
Susan J. Robidas, LCR/RPR
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N.H. LCR No. 44 (RSA 310-A:173)