Before the

STATE OF NEW HAMPSHIRE

PUBLIC UTILITIES COMMISSION

DE 13-063

In the Matter of:
Granite State Electric Company d/b/a Liberty Utilities

Distribution Service Rate Case – Request for Temporary Rates

Direct Testimony

of

Steven E. Mullen
Assistant Director – Electric Division

May 24, 2013

Q. Please state your name, position and business address.

A. My name is Steven E. Mullen. I am employed by the New Hampshire Public Utilities Commission as Assistant Director of the Electric Division. My business address is 21 South Fruit Street, Suite 10, Concord, New Hampshire.

Q. Please summarize your educational background and work experience.

In 1989, I graduated *magna cum laude* from Plymouth State College with a Bachelor of Science degree in Accounting. I attended the NARUC Annual Regulatory Studies Program at Michigan State University in 1997. In 1999, I attended the Eastern Utility Rate School sponsored by Florida State University. I am a Certified Public Accountant and have obtained numerous continuing education credits in accounting, auditing, tax, finance and utility related courses.

From 1989 through 1996, I was employed as an accountant with Chester C. Raymond, Public Accountant in Manchester, New Hampshire. My duties involved preparation of financial statements and tax returns as well as participation in year-end engagements. In 1996, I joined the Commission as a PUC Examiner in the Finance Department. In that capacity I participated in field audits of regulated utilities' books and records in the electric, telecommunications, water, sewer and gas industries. I also performed rate of return analysis, participated in financing dockets and presented oral testimony before the Commission. In 1998, I was promoted to the position of Utility Analyst III and continued to work in all of the regulated industry fields, although the largest part of my time was concentrated on electric and water issues. As part of an internal reorganization of the Commission's Staff in 2001, I became a member of the Electric Division. I was promoted to Utility Analyst IV in 2007 and then Assistant Director of the Electric Division in 2008. Working with the Director of the Electric Division, I am responsible for the day-to-day management of the Electric Division including decisions on matters of policy. In addition, I evaluate and make recommendations concerning rate, financing, accounting and other general industry filings. I represent Staff in meetings with company officials, outside attorneys, accountants and consultants relative to the Commission's policies, procedures, Uniform System of Accounts, rate case, financing and other industry and regulatory matters.

Q. Have you previously testified before this Commission?

A. Yes. I have testified before the Commission on numerous occasions.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to provide Staff's recommendation concerning Granite State Electric Company d/b/a Liberty Utilities' (Liberty's) March 29, 2013 request to establish temporary rates at a level that would provide for an additional $9,215,479 in annual distribution revenues, based on a twelve-month period ended June 30, 2012. According to Liberty, the requested increase would result in an annual increase to distribution revenues of 37.4%.

Q. What would be the result of the increase on customers' bills?

A. Liberty calculated that the increase would result an in average increase to customers' total bills of 11.7%. For a residential customer using 500, 600 or 674 (annual average residential usage) kilowatt-hours per month, Liberty calculated that the increase to total bills would be $7.56, $9.26 and $10.52, respectively.

Q. Did Liberty subsequently revise its request for temporary rates?

A. Yes, although it was not formally filed with the Commission. On April 29, 2013, Liberty sent revised schedules to Staff and the parties revising the requested increase to $8,669,928.[1] In response to a discovery request, Liberty confirmed that the revised schedules represented a revised request for a temporary rate increase.[2]

Q. What is Staff's recommended temporary increase to Liberty's distribution service revenues?

A. As shown on Attachment SEM-3, Schedule 1, Staff recommends a temporary increase to distribution revenues of $6,187,306. This represents an increase of 24.9% as compared to the proformed test year distribution revenues of $24,819,306. This revenue requirement is calculated on a total rate base of $64,379,899, as computed on SEM-3, Schedule 2, and provides for an overall rate of return of 8.03%, as detailed on Attachment SEM-3, Schedule 1B.

Q. What is the foundation for a request for temporary rates?

A. Temporary rates are specifically allowed pursuant to RSA 378:27 which reads as follows:

> **378:27 Temporary Rates. –** In any proceeding involving the rates of a public utility brought either upon motion of the commission or upon complaint, the commission may, after reasonable notice and hearing, if it be of the opinion that the public interest so requires, immediately fix, determine, and prescribe for the duration of said proceeding reasonable temporary rates; provided, however, that such temporary rates shall be sufficient to yield not less than a reasonable return on the cost of the property of the utility used and useful in the public service less accrued depreciation, as shown by the reports of the utility filed with the

[1] See Attachment SEM-1.
[2] See Attachment SEM-2, Liberty's response to Staff 1-1.

> commission, unless there appears to be reasonable ground for questioning the figures in such reports.

Following the completion of the full proceeding, a "permanent rate" level is determined, and the difference between the temporary rate level and the permanent rate level is then reconciled through either collection from or refund to customers.

Q. Referencing that statute, how did Liberty prepare its filing?

A. For purposes of the temporary rate filing, Liberty used the twelve-month period ended June 30, 2012 because, at the time of filing, that was the most current date of the "reports of the utility filed with the commission." Liberty did not make any adjustments to the amounts included in the June 30, 2012 reports other than to gross-up the requested revenue increase for income taxes and bad debts.

Q. Please comment on that approach.

A. While Staff can appreciate a straightforward approach to a temporary rate filing, it is important not to lose sight of the last clause of the statute, specifically, "unless there appears to be reasonable ground for questioning the figures in such reports." As relates to this case, Staff believes there are reasonable grounds for questioning some of the figures and, therefore, proposing certain adjustments.

Q. What adjustments has Staff made to Liberty's proposal?

A. Staff has made two adjustments that deal with the "reasonable ground for questioning" criterion: a) adjustments to the capital structure and overall cost of capital, and b) additional adjustments that can be characterized more as computational adjustments.

Q. Please describe the "reasonable ground" adjustments.

A. The first adjustment deals with cross-border sales. Currently, there are electric distribution customers in Massachusetts who are served by Liberty's distribution system yet are not billed. This is an issue that has been discussed in Liberty's recent default service hearings and is a carry-over from National Grid's prior ownership of Granite State Electric. An agreement was recently negotiated between Liberty and National Grid for Liberty to be compensated for those sales, but such compensation did not begin until November 2012. The twelve-month period ended June 30, 2012 contained zero distribution revenue from the cross-border customers. In its follow-up response to OCA 1-3, Liberty provided the cross-border revenues received during the months of November and December 2012 in the amounts of $9,888 and $10,941, respectively. On an annualized basis, the total such revenues approximate $125,000, and that revenue has been included as shown in Adjustment #2 on SEM-3, Schedule 3A. Staff notes that Liberty included a full year of cross-border sales revenue in its request for permanent rates.

The second adjustment is also shown on SEM-3, Schedule 3A and involves the removal of approximately $1.5 million of information technology (IT) costs incurred by Liberty through June 30, 2012[3] related to Liberty preparing for the acquisition of Granite State and the conversion of various computer systems and data. Those costs are particular to the acquisition proceeding and are not appropriate for inclusion in the temporary rate calculations.[4] Staff notes that Liberty removed those costs from its request for permanent

[3] As noted in Liberty's response to Staff 2-6, a subsequent downward adjustment to those costs of $475,908was recorded in August 2012. However, as the $1.5 million was included in the June 30, 2012 totals, that amount has been removed for purposes of the temporary rate calculations.

[4] See DG 11-040, Exhibit 2, Settlement Agreement, Section V.D.1.a which reads: "The Companies shall not seek rate recovery of any transaction costs, which, as used herein refers to financing, legal and regulatory costs incurred in connection with the closing of the transaction; the acquisition premium; or transition costs, which as used herein

rates.

Q. Please describe the adjustments made to the capital structure and the overall cost of capital.

A. The table below shows the differences between overall cost of capital used by Liberty and as calculated by Staff:

LIBERTY			
	Component		Average
Component	Ratio	Cost Rate	Cost Rate
Common Equity	50.00%	9.67%	4.84%
Long-Term Debt	50.00%	7.54%	3.77%
	100.00%		8.61%

STAFF			
	Component		Average
Component	Ratio	Cost Rate	Cost Rate
Common Equity	55.00%	9.67%	5.32%
Long-Term Debt	45.00%	6.02%	2.71%
	100.00%		8.03%

In preparing its request for temporary rates, Liberty utilized the hypothetical capital structure and overall cost of capital included in the settlement agreement in DG 06-107. That capital structure was 50% equity and 50% debt with the cost rates being 9.67% for the equity component and 7.54% for the debt component, resulting in an overall cost of capital of 8.61%. It is common in temporary rate proceedings for simplicity and timing purposes to use the most recent Commission-approved return on equity, and, as shown above, Staff has incorporated the 9.67% return on equity into its calculations. Regarding the cost of long-term debt, however, Liberty has additional debt outstanding that has

refers to temporary costs incurred to effect the transaction.

lowered the overall cost of debt since the time the settlement agreement was executed in DG 06-107. Rather than using the outdated cost of debt, Staff updated the cost of debt to reflect the weighted cost of debt outstanding as of December 31, 2012.

With respect to the capital structure, as stated earlier, the 50% equity/50% debt structure used in DG 06-107 was a hypothetical capital structure as Granite State's capital structure at that time was heavy on equity. As of December 31, 2012, Liberty's capital structure consisted of approximately 64% equity and 36% debt, still relatively heavily weighted to the equity side. For purposes of temporary rates, Staff used a capital structure consisting of 55% equity and 45% debt, component percentages that were discussed as part of DG 11-040, the proceeding wherein Liberty Utilities acquired Granite State from National Grid.[5] The resulting overall cost of capital of 8.03% used by Staff is consistent with the overall cost of capital expected following the acquisition.

Q. What are the computational adjustments you referred to earlier?

A. The computational adjustments are as follows:

- Adjustment of federal income tax rate from 35% to 34%;
- Removal of the bad debt gross-up factor;
- An adjustment to the cash working capital component of rate base that relates solely to the operation and maintenance expense adjustments described above; and
- Necessary adjustments to reflect the federal and state income tax effects resulting from other adjustments to income and expenses.

Q. Please explain each of the computational adjustments.

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[5] See, for example, DG 11-040, Exhibit #14, October 7, 2011 testimony of Steven E. Mullen at 17-18 and Exhibit #15, April 10, 2012 testimony of Steven E. Mullen.

A. The federal income tax rate was adjusted to reflect the appropriate tax rate for Liberty's tax bracket. The 34% rate appears on SEM-3, Schedule 1A and Schedule 3B.

Regarding the bad debts gross-up factor, that is not a factor that is currently in place for Liberty, nor for any other New Hampshire utility. Such new proposals should be subject to the full discovery process provided in the permanent rates portion of the proceeding. As such, Staff has removed the bad debts gross-up factor from the temporary rate calculations.

The adjustment to the cash working capital component of rate base is simply a function of the calculation that is based on a percentage of operation and maintenance expenses. As Staff has made an adjustment to decrease Liberty's operations and maintenance expenses, a corresponding decrease to cash working capital is necessary. The calculation of the adjustment is shown on SEM-3, Schedule 2A.

Finally, as adjustments to income and expenses have corresponding impacts on taxable income, it is necessary to include the appropriate adjustments to federal and state income taxes. In this case, the adjustments made by Staff increased Liberty's taxable income. Thus, Staff has included an increase of $656,222 to Liberty's income tax expense as calculated on SEM-3, Schedule 3B.

Q. Do you have any final comments regarding Staff's temporary rate recommendation?

A. Yes. As the permanent rates portion of the proceeding progresses, it is quite possible that additional information will be gathered with respect to items at issue for temporary rates. By taking certain positions as described above, Staff is not in any way tying its hands with respect to positions it might otherwise take during the permanent rates portion of the proceeding. Rather, Staff's temporary rate recommendation is a straightforward presentation of limited adjustments that provides for a reasonable return and results in a reasonable level of temporary rates.

Q. Does this conclude your testimony?

A. Yes, it does.