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Direct Testimony of Stephen P. St. Cyr in DW 17-103

Q. Please state your name and address.

A. Stephen P. St. Cyr of Stephen P. St. Cyr & Associates, 17 Sky Oaks Drive, Biddeford, Me. 04005.

Q. Please state your present employment position and summarize your professional and educational background.

A. I am presently employed by St. Cyr & Associates, which provides accounting, tax, management and regulatory services. The Company devotes a significant portion of the practice to serving utilities. The Company has a number of regulated water utilities among its clientele. I have prepared and presented a number of rate case filings before the New Hampshire Public Utilities Commission. Prior to establishing St. Cyr & Associates, I worked in the utility industry for 16 years, holding various managerial accounting and regulatory positions. I have a Business Administration degree with a concentration in accounting from Northeastern University in Boston, Ma. I obtained my CPA certificate in Maryland.

Q. Is St. Cyr & Associates presently providing services to West Swanzey Water Company ("Company")?

A. Yes. St. Cyr & Associates prepared the various exhibits and supporting schedules and prepared the written testimony and other rate case filing requirements. In addition, St. Cyr & Associates assists the Company in preparing its year end financial statements, prepares the tax returns and prepares the PUC Annual Report.

Q. Are you familiar with the pending rate application of the Company and with the various exhibits submitted as Schedules 1 through 4 inclusive, with related pages and attachments?

A. Yes, I am. The exhibits were prepared by me, utilizing the financial records of the Company.

Q. What is the test year that the Company is using in this filing?

A. The Company is utilizing the twelve months ended December 31, 2016.

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Q. Before you explain the schedules, please provide a brief overview of the Company.

A. The Company was formed in 1986 and became a utility in 1988. It has three wells, 2 pump stations, 8,700 feet of mains, 83 non-fire services, 6 fire services and 83 meters. At December 31, 2016 the Company served 84 customers. In recent years its investment in plant has been minimal. The Company has no plans to replace and/or add plant. Its long term debt continues to decline. The Company's operating and maintenance expenses have increased significantly in 2016 due primarily to change in operators. In 2016 its net loss was $20,234. The 2016 net loss was due to a decline in revenues and increase in operation and maintenance and property taxes. With the proposed increase in rates and revenues, the Company should be able to eliminate the net loss and continue to provide service to its customers at fair and reasonable rates.

Q. Is there anything else prior to summarizing the schedules?

A. No.

Q. Would you please summarize the schedules?

A. Yes. The schedule entitled "Computation of Revenue Deficiency for the Test Year ended December 31, 2016," summarizes the supporting schedules. The actual revenue deficiency for the Company for the test year amounts to $31,677. It is based upon an actual test year with a 5 quarter average rate base of $343,624 as summarized in Schedule 3. The Company's actual rate of return is 5.05% for the actual test year. The rate of return of 5.05%, when multiplied by the rate base of $343,624, results in an operating income requirement of $17,367. As shown on Schedule 1, the actual net operating income (loss) for the Company for the test year was ($14,310). The operating income required, less the net operating income (loss), results in an operating income deficiency before taxes of $31,677. The Company did not calculate the tax effect of the revenue deficiency, resulting in a revenue deficiency for the Company of $31,677.

The proforma revenue deficiency for the Company for the test year amounts to zero. It is based upon a proformed test year rate base of $344,831, as summarized in Schedule 3. The Company is utilizing a proformed rate of return of 5.05% for the proformed test year. The proformed rate of return of 5.05% when multiplied by the rate base of $344,831, results in an operating net income requirement of $17,428.

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As shown on Schedule 1, the proformed net operating income for the Company for the test year was $17,428. The operating income required, less the net operating income, results in a deficiency of zero. The tax effect of the deficiency is zero, resulting in a revenue deficiency for the Company of zero. Please note that the Company has made minimal adjustments to rate base and no adjustments to the rate of return.

Q. Would you please explain Schedule 1 and supporting Schedule 1A – 1C?

A. Schedule 1 reflects the Company's Statement of Income. Column b shows the actual 2016 year end balances for the Company (as reported to the PUC in its 2016 PUC Annual Report). Column c shows the proforma adjustments for known and measurable changes to test year revenues and expenses. The proforma adjustments are further supported by schedule 1A, 1B and 1C. Column d shows the proforma 2016 year end balance. Column e and Column f are actual results for 2015 and 2014, respectively.

During the twelve months ended December 31, 2016, the actual operating revenues amounted to $69,906, a decrease of $8,047 over 2015. The decrease is due to no longer being able to charge customers a surcharge for previously unbilled revenue and less water being sold. At December 31, 2016 the Company had 84 customers. Its customers consumed 7,852 thousand gallons of water, a decrease of 852 thousand gallons of water compared to 2015.

The Company's total operating expenses amounted to $84,216, an increase of $21,008 over 2015. The significant increase in total operating expenses was due to the change in operators and the resulting increase in operating and maintenance expenses and the increase in property taxes. The 2016 Net Operating Income (Loss) amounted to ($14,310). Net Income (Loss) for 2016 was ($20,235).

The Company made 1 proforma adjustment to operating revenues totaling $39,872 and a number of proforma adjustments to operating expenses totaling $8,134. The specific proforma adjustments are identified on the Statement of Income – Proforma Adjustments (Schedule 1A). A brief explanation is as follows:

<u>Proforma Adjustment to Revenues</u>

Sales of Water – Amount Necessary to Earn Return and Cover Operating Costs - $39,872

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The Company has increased test revenues for the proposed amount of revenues necessary to cover its expenses and allow it to earn its proposed rate of return.

Proforma Adjustments to Expense

Operating Expenses:

The Company pays its owner / manager for meter reading ($700), customer records and collection ($3,800) and miscellaneous customer matter ($700) as well as oversight of the operations and maintenance of the system including oversight of the operator and general and administrative matters ($10,000). The Company proposes to increase the pay to its owner / manager for meter reading ($800), customer records and collection ($4,400) and miscellaneous customer matter ($800) as well as oversight of the operations and maintenance of the system including oversight of the operator and general and administrative matters ($11,500). The last increase was 2011 coming out of the last rate case. Overall, it represents approximately 2% per year for 6 years.

During 2016, the Company replaced Gordon Water LLC (“Gordon”) with Everett E. Houghton Co., Inc. (“Houghton”) as operator. As such, it eliminated Gordon’s costs of $600 for January – March 2016. The Company also added Houghton costs of $4,177 for January – March 2017.

In anticipation of a PUC audit, the Company estimated that it will incur $2,400. No such audit expenses are reflected in the test year. The Company is proposing to recover the proposed audit expense of $2,400 over 3 years, resulting in a test year adjustment of $800.

During 2016, the Company incurred $4,334 of additions to plant and record a half year of depreciation expense of $206 on such additions to plant. The Company is making a proforma adjustment for the additional half year depreciation of $206.

During 2016, the Company incurred $1,238 and $8,456 in state and local property taxes. At this point, the Company is unaware of any increase or decrease in property taxes. As such, the Company has not made any proforma adjustments. However, it preserves the right to increase and / or decrease property taxes for any known and measurable change likely to be known later this year.

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With the proposed increase in revenue offset by the proposed increase in expenses, there is also a related increase in the federal income and state business taxes. The increase in federal income taxes represents the additional tax liability due to the increase in taxable income. The increase in state business taxes represents the additional tax liability due to the increase in gross profits.

The Company has provided the calculation of the federal income taxes and the state business taxes (Schedule 1B). The Company has also provided the effective tax factor (Schedule 1C).

The total proforma adjustments to Operating Expenses amount to $8,134.

The net of the proforma adjustments to operating revenue of $39,872 and the proforma adjustments to operating expenses of $8,134 results in a net proforma adjustment of $31,738. When the net operating income associated with the proforma adjustments is added to net operating income from the test year, the proforma test year net operating income totals $17,428. The proforma test year net operating income of $17,428 allows the Company to cover its expenses and earn a 5.05% return on its investments.

Q. Does that complete your description of the proforma adjustments to revenues and expenses?

A. Yes.

Q. Please describe Schedule 2, the Balance Sheet.

A. The Company has $292,663 total assets at the end of 2016. $249,815 of the $292,663 total assets is net plant, of which is completed and providing service to customers. The Company has $20,711 of total equity capital. The Company incurred a significant loss in 2016, which reduced retained earning and total equity. The Company has $135,864 of long term debt. The long term debt balance has decreased due to payment of principal on the three outstanding loans. Accounts payable has increased during the test year due to the significant 2016 net loss and the resulting strained cash flow. At 12/31/16, the Company owed its owner / manager $30,650, its operator $6,534 and its water supplier $9,091. A portion of the plant has been contributed.

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Q. Please continue with an explanation of Schedule 3, Rate Base and the supporting schedule.

A. Schedule 3 reflects the Company's Rate Base for both the 5 quarter average and the proforma year end balance. Column b – f shows the actual balance at the end of the period. Column g shows the average of the 5 quarter balances. Column h shows the proforma adjustments. Column i shows the proforma year end balance.

Schedule 3A, Prepayments shows the monthly balances for prepaid insurance and property taxes and identifies the sum of the balances at the end of each quarter.

Schedule 3B shows 2 proforma adjustments to rate base: one, the additional half year accumulated depreciation on the 2016 additions to plant; and, two, the additional cash working capital due to the proposed increase in O&M expenses. The cash working capital balances are further supported by Schedules 3C.

The Total Proforma 5 quarter average Rate Base balance amounts to $344,831.

Q. Would you please explain Schedule 4, Rate of Return Information?

A. Schedule 4 reflects the overall rate of return for both the proforma test year and the actual test year. The weighted average rate of return for the actual test year is 5.05%. It was developed by taking the actual component ratios times the actual component cost rates to determine the actual weighted average cost rate. The sum of the actual cost rates for equity and debt equals actual weighted average rate of return. The Company made no adjustments to the actual rate of return. As such, the weighted average rate of return for the proforma test year is 5.05%.

Schedule 4 also reflects both the capital structure and the capital ratios. The Company has provided the capital structure for the actual test year and the proforma test year. It has also provided the actual capital structure for 2015 and 2014. Please note that the Company's debt to equity ratio has remained relatively constant.

In addition, Schedule 4 reflects the long term debt, interest expense, financing costs, total debt costs and debt costs rates for the actual test year. At 12/31/16 the Company has $135,864 of outstanding long term debt. Its 2016 total interest expense is $5,925. The 2016 actual cost of debt was 4.36%. There was no change to the long term debt, interest expense and financing costs for the proforma test year.

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Q. Please explain the Report of Proposed Rate Changes.

A. If the Company filing is approved as submitted, its total water Operating Revenues will amount to $109,672.

Q. Is the Company proposing any changes to the methodology used in calculating the rates?

A. No. The Company is generally using the same methodology. It is applying the rate increase to both general and fire protection customers.

Q. When is the Company proposing that the new rates be effective?

A. The proposed effective date is August 15, 2017 so that the Company can begin to bill the new rates the first week of October 2017 for the third quarter of 2017.

Q. Is there anything else that the Company would like to address?

A. Yes. The most recent Sanitary Survey dated 5/23/17 provided the Company with a few recommendations. Among them were recommendations pertaining to the installation of VFDs on the well pumps and installation of a SCADA system. The Company asked Houghton to provide an estimate of such work. He estimates that the work would costs $24,000. The Company has completed the pre-application form to borrow $26,400 ($24,000 plus 10% construction cost contingency of $2,400) from NHDES's DWSRF. If the NHDES approves the project, the Company will seek PUC approval of the financing. The Company anticipates a September 30, 2017 start date with an anticipated completion date of November 20, 2017.

The Company's ability to pay the principal and interest on the loan is contingent on PUC approval of the related step increase.

Q. Has the Company prepared Step Increase schedules? If so, please describe.

A. Yes. The proposed additional revenue requirement associated with the pump drives and SCADA is $2,989. It is derived from a net addition to rate base of $25,740. The return on the additional plant at 2.43% is $626. The additional operating expenses are $2,362. The sum of the return of $626 and the additional operating expenses of $2,362 results in an additional revenue requirement of $2,989. Please see Page 1 of 5 of the Step Increase schedule.

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Page 2 of 5 shows how the annual cost rate of 2.43% was derived. Page 3 of 5 shows the costs of the plant and the related depreciation. Page 4 of 5 shows the additional state and local property taxes and combined federal income and state business tax effect. Page 5 of 5 shows the effective tax factor.

Q. Is there anything else that the Company would like to address?

A. Yes. The Company has decided not to pursue temporary rates due to the additional costs and additional time to pursue the rate change. The Company respectfully requests that the Commission take that into consideration when establishing the effective date of the new rates.

Q. Is there any other rate matter that you would like to discuss?

A. Yes. The Company has engaged the services of Stephen P. St. Cyr & Associates to prepare the rate filing and pursue the rate increase throughout the rate case proceeding. St. Cyr & Associates and the Company have agreed on a per hour fee of $125.00 for each hour of work performed. The Company and I believe that the fees are fair and reasonable. At this point, the Company does not anticipate utilizing outside legal council.

Q. Would you please summarize what the Company is requesting in its rate filing?

A. The Company respectfully requests that the Commissioners approve an increase in annual revenues of $39,872 for permanent rates. Also, assuming NHDES approves the Company requests for DWSRF loan, the Company respectfully requests that the PUC approve the Company requests for DWSRF loan and the related step increase of $2,989.

Q. Is there anything further that you would like to discuss?

A. No, there is nothing further.

Q. Does this conclude your testimony?

A. Yes.

SPSt. Cyr
07/17/17