Liberty Utilities

STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

Docket No. DG 20-105

Liberty Utilities (EnergyNorth Natural Gas) Corp. d/b/a Liberty Utilities
Distribution Service Rate Case

DIRECT TESTIMONY

OF

DAVID B. SIMEK

AND

CATHERINE A. MCNAMARA

July 31, 2020

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ATTACHMENTS

Attachment	Title
DBS/CAM-1	Lead-Lag Study Calculations

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1   **I.   <u>INTRODUCTION AND QUALIFICATIONS</u>**

2   **Q.   Please state your full name and business address.**

3   A.   (DS) My name is David B. Simek. My business address is 15 Buttrick Road,

4   Londonderry, New Hampshire.

5   (CM) My name is Catherine A. McNamara. My business address is 15 Buttrick Road,

6   Londonderry, New Hampshire.

7   **Q.   Please state by whom you are employed.**

8   A.   We are employed by Liberty Utilities Service Corp. ("Liberty"), which provides service

9   to Liberty Utilities (EnergyNorth Natural Gas) Corp. d/b/a Liberty Utilities

10   ("EnergyNorth" or "the Company").

11   **Q.   Please describe your educational and professional background.**

12   A.   (DS) I graduated from Ferris State University in 1993 with a Bachelor of Science in

13   Finance. I received a Master of Science in Finance from Walsh College in 2000. I also

14   received a Master of Business Administration from Walsh College in 2001. In 2006, I

15   earned a Graduate Certificate in Power Systems Management from Worcester

16   Polytechnic Institute. In August 2013, I joined Liberty as a Utility Analyst and I was

17   promoted to Manager, Rates and Regulatory Affairs in August 2017. Prior to my

18   employment at Liberty, I was employed by NSTAR Electric & Gas Company

19   ("NSTAR") as a Senior Analyst in Energy Supply from 2008 to 2012. Prior to my

20   position in Energy Supply at NSTAR, I was a Senior Financial Analyst with the NSTAR

21   Investment Planning group from 2004 to 2008.

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1   (CM) I graduated from the University of Massachusetts, Boston, in 1993 with a Bachelor

2   of Science in Management with a concentration in Accounting. In November 2017, I

3   joined Liberty as an Analyst in Rates and Regulatory Affairs. Prior to my employment at

4   Liberty, I was employed by Eversource Energy as a Senior Analyst in the Investment

5   Planning group from 2015 to 2017. From 2008 to 2015, I was a Supervisor in the Plant

6   Accounting department. Prior to my position in Plant Accounting, I was a Financial

7   Analyst/General Ledger System Administrator within the Accounting group from 2000 to

8   2008.

9 **Q.   Have you previously testified in regulatory proceedings before the New Hampshire**

10   **Public Utilities Commission?**

11 A.   (DS) Yes, I have testified on numerous occasions before the New Hampshire Public

12   Utilities Commission (the "Commission").

13   (CM) Yes, I have testified on multiple occasions before the Commission.

14 **II.   PURPOSE AND OVERVIEW OF TESTIMONY**

15 **Q.   What is the purpose of your testimony?**

16 A.   The purpose of our testimony is to explain the Company's lead-lag study, which is used

17   to determine the cash working capital ("CWC") requirement in rate base. Our analysis is

18   supported by the data presented in Attachment DBS/CAM-1.

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1 **Q.** **Please define the term "cash working capital" as a rate base component.**

2 A.   The term "cash working capital" refers to the net funds required by the Company to pay

3   for goods and services between the time of the cash outlay by the Company for such

4   goods and services and the time revenues are received from customers. For the

5   Company, the cost of goods and services includes operations and maintenance ("O&M")

6   expenses, including labor expenses and non-labor expenses, federal taxes, local taxes,

7   and payroll-related taxes.

8 **Q.** **How did you derive the cash working capital requirement?**

9 A.   The CWC requirement was determined using the results of a lead-lag study, which

10   measures the funds needed due to the net timing difference between the revenue lag and

11   the expense lag. The revenue lag represents the number of days between when the

12   Company provides services and when its customers pay for those services. The longer

13   the revenue lag, the more cash the Company needs to fund its day-to-day operations. The

14   expense lag represents the number of days between the time the Company incurs

15   expenses for goods and services used to provide service, and the time it must make

16   payments for those goods and services. The longer the expense lag, the less cash the

17   Company needs to fund its day-to-day operations. Together, the revenue lag and expense

18   lag are used to measure the net lead/lag to determine the CWC requirement, which

19   becomes a component of the Company's rate base when determining the Company's

20   revenue requirement.

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1   **Q.**   **Are the results of your lead-lag study an accurate calculation of the Company's CWC**

2   **requirement?**

3   A.   Yes. The study provides an accurate assessment of the Company's actual CWC needs

4   during the rate case test year.

5   **III.**   <u>**LEAD-LAG STUDY APPROACH**</u>

6   **Q.**   **Please summarize the results and the approach of the lead-lag study you conducted.**

7   A.   The lead-lag study shows a net lag of 25.72 days for the rate case test year, which is

8   January 1, 2019, through December 31, 2019. The lead-lag study is used to calculate the

9   CWC requirement, which is then applied to the rate case test year amounts for O&M

10   expenses and taxes.

11   **Q.**   **How did you develop the net lead/lag days in your study?**

12   A.   The revenue lag is measured from the time service is provided to customers to the time

13   payment is received from customers. Expense lags are measured from the time a good or

14   service is provided to the Company to the time payment is made by the Company for that

15   good or service. These time periods are measured in days, converted to dollar-days, and

16   summarized for each element in the lead-lag study. The difference between the revenue

17   lag and the expense lag determines if there is a net revenue lag (revenue lag days are

18   greater than the expense lag days for a component) or a net expense lead (revenue lag

19   days are less than the expense lag days for a component).

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1 **Q.** **Please describe the results of your lead-lag study.**

2 A. The results show the total number of revenue lag days and expense lag days for the

3 Company during the CWC test year. The net difference between the computed revenue

4 lag days and expense lag days was then multiplied by the average daily revenue

5 requirements of the system to produce the net cash working capital required by the

6 Company.

7 **IV.** **REVENUE LAG**

8 **Q.** **Please describe the components of the revenue lag.**

9 A. Revenue lag consists of three components: (1) the service lag; (2) the billing lag; and (3)

10 the collection lag. The total number of days produced by the three components

11 represents the amount of time between providing utility service to customers and the

12 receipt of the payments for such service. Together, these revenue lag components

13 comprise the total revenue lag days.

14 **Q.** **What is the service lag?**

15 A. The service lag represents the midpoint of the service period, *i.e.,* the time between the

16 start of the billing month and the end of the billing month. Our approach is to rely on the

17 midpoint of the service period, which assumes that service will be provided evenly over

18 the service period.

19 **Q.** **What is the billing lag?**

20 A. The billing lag is the time between the cycle bill read date and the date bills are sent to

21 customers. The billing lag begins the day the bill is read and ends with the recording and

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1   mailing of the customer bill. This lag includes the process for review and validation of

2   usage and billing.

3 **Q.   What is the collection lag?**

4 A.   Collection lag reflects the time between recording and bill mailing for the services

5   rendered and the receipt of payment from customers for the revenues billed. The

6   collection lag was determined by the accounts receivable turnover ratio method. This is

7   calculated by taking the average accounts receivable balance divided by the average daily

8   revenues for the test year.

9 **Q.   What is the total revenue lag component for the lead-lag calculation?**

10 A.   Each of these revenue lag components was totaled to arrive at the total revenue lag of

11   52.66 days, as shown on Attachment DBS/CAM-1, Page 2.

12 **V.   EXPENSE LAG**

13   **A.   Operation and Maintenance Expenses**

14 **Q.   How did you determine the expense lag days for O&M expenses?**

15 A.   We separated total system expenses into three groups: (1) regular payroll costs; (2)

16   annual incentive payroll costs; and (3) third-party O&M expenses. We measured the

17   expense lag days for each of these groups independently. A summary of the O&M

18   expense lag is shown on Attachment DBS/CAM-1, Page 5.

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1   **Q.**   **How were the lag days for the payroll expenses determined?**

2   A.   We based the expense lag days for payroll on the Company's wage payment process,

3   which pays employees on a bi-weekly or weekly basis. We calculated the expense lag

4   days for payroll costs by determining the average days of service being paid and adding

5   the midpoint of the service period to the number of days between the end of each service

6   period and the date of payment to employees. This calculation produced the number of

7   total days between the middle of the period for which employees' wages are recorded and

8   the date on which payments are disbursed. These calculations were based on actual

9   historical Company data for the CWC test year. Holidays are also based on actual

10   historical data for the CWC test year.

11   **Q.**   **Did you make any adjustment to the payroll lag days in your lead-lag study?**

12   A.   Yes. We made an adjustment for vacation pay because vacation pay is earned before it is

13   actually taken. The vacation pay adjustment is calculated based on the average payroll

14   lag days and the midpoint of the days in the year.

15   **Q.**   **How were the lag days for the annual performance incentive determined?**

16   A.   The Company's annual incentive pay is paid in the second quarter for the preceding

17   calendar year. The lag days were determined based on the midpoint of the performance

18   period and the date the incentives were paid.

19   **Q.**   **How were the lag days determined for third-party O&M expenses?**

20   A.   We based the measure of expense lag days for the expenses in this group on a sampling

21   of these expenses for the test year. We then identified the sample invoices that were

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1   larger than $50,000 and reviewed the invoice to see if a service period could be

2   identified. If the service period was identified, then the mid-point of the service period

3   and the payment date were used to calculate the expense lag for third-party O&M

4   expenses. If no service period was identified, we then used the invoice date and the

5   payment date to calculate the expense lag for third-party O&M expenses. The invoice

6   date was also used for all invoices that were not included in the sample. Since the sample

7   included only invoices larger than $50,000, and since in many cases the service period

8   can be expected to precede the invoice date, the results of our third-party O&M expense

9   lag can be considered conservative.

10   **B.   Income Tax Expense**

11 **Q.   How are the lag days determined for income taxes?**

12 A.   The lag days for federal and state income taxes are typically calculated using the calendar

13   year as the service period because the income would be earned throughout the year. The

14   midpoint of the service period would be June 30, 2019. Payment of estimated tax for the

15   year is made quarterly on April 15, June 15, September 15, and December 15. Since the

16   Company had a net operating loss during the test year there were no current taxes paid

17   and no corresponding lag was calculated.

18   **C.   Taxes Other than Income Taxes**

19 **Q.   What taxes are included in the taxes other than income taxes?**

20 A.   This group of taxes consists of: (1) payroll-related taxes (FICA, federal unemployment,

21   and state unemployment); and (2) property taxes.

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1 **Q.** **How were the lag days calculated for each of those taxes?**

2 **A.** The payment lags for FICA taxes were calculated from the pay period end date to the

3 respective payment dates of the taxes. Federal unemployment taxes are paid after the end

4 of each quarter based on that quarter's wages up to the annual limit. State unemployment

5 taxes were calculated from the pay period end date to the respective payment dates of the

6 taxes. The payment lag for property taxes was calculated from the midpoint of the period

7 for which the tax was assessed to the payment date.

8 **D.** **Non-Cash Items**

9 **Q.** **Please explain why you excluded non-cash items from your lead-lag study.**

10 **A.** This study uses the cash method and therefore excludes non-cash items. As such, non-

11 cash items, including depreciation, amortization, deferred income taxes, and return

12 (including return on equity, and interest on long-term debt), have not been included in our

13 lead-lag study.

14 **VI.** **CONCLUSION**

15 **Q.** **What were the results of the lead-lag study?**

16 **A.** As shown on Attachment DBS/CAM-1, Page 1, the CWC requirement for the Company

17 is $3,246,606 based on a net lag of 25.72 days for the rate case test year January 1, 2019,

18 through December 31, 2019.

19 **Q.** **Are the results of this lead-lag study reasonable?**

20 **A.** Yes, the results of the lead-lag study reflect the Company's practices and are fair and

21 reasonable. In addition, the methods used in the study are consistent with studies

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1   performed for other companies in New Hampshire and other jurisdictions. The resulting

2   CWC requirement should properly be included in the Company's rate base.

3 **Q.   Does this conclude your testimony?**

4 A.   Yes, it does.