**STATE OF NEW HAMPSHIRE**
**BEFORE THE**
**PUBLIC UTILITIES COMMISSION**

Docket No. DG 20-105

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

# REBUTTAL TESTIMONY

**OF**

**DAVID B. SIMEK**

**AND**

**KENNETH A. SOSNICK**

April 29, 2021

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## ATTACHMENTS

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## I. INTRODUCTION AND BACKGROUND

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

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

(KS) My name is Kenneth A. Sosnick. My business address is 200 State Street, 9th Floor, Boston, Massachusetts.

**Q. By whom are you employed, and in what position?**

A. (DS) I am employed by Liberty Utilities Service Company, which provides services to Liberty Utilities (EnergyNorth Natural Gas) Corp. ("EnergyNorth" or the "Company"). My title is Manager, Rates and Regulatory Affairs.

(KS) I am employed by FTI Consulting ("FTI"), which is a worldwide consulting firm dedicated to helping organizations manage change, mitigate risk, and resolve disputes. Our Power & Utilities practice brings these services to firms in regulated and competitive energy industries. The services we provide our utility clients include expert testimony, regulatory advice, support for strategic decision-making, and advice regarding investments and capital allocation. Our team is comprised of former utility executives, regulators, investors, and financial analysts that combine for hundreds of years of experience in the regulated energy space. My title is Managing Director.

**Q. Have you previously submitted testimony in this proceeding?**

A. Yes. We submitted joint pre-filed testimony as part of the Company's July 31, 2020, filing for an increase in distribution rates. Our professional backgrounds and qualifications are contained in that testimony. Terms defined in our pre-filed direct testimony have the same meaning in this rebuttal testimony.

## II. PURPOSE AND SUMMARY OF TESTIMONY

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

A. Our testimony responds to the revenue requirement recommendations of Staff witness Donna H. Mullinax. Our testimony explains that the Company agrees with several of these recommendations, but that the majority of Staff's proposed adjustments are unwarranted and should be rejected by the Commission. As noted below, our testimony includes an updated revenue requirement analysis that incorporates the Company's rebuttal positions.

**Q. Are you submitting any attachments with your testimony?**

A. Yes, we are submitting the following attachments:

- Attachment DBS/KAS-1-Rebuttal, updated revenue requirement schedules reflecting the Company's rebuttal positions.
- Attachment DBS/KAS-2-Rebuttal, copies of certain data responses referred to in this rebuttal testimony.
- Attachment DBS-KAS-3-Rebuttal, a breakout of regulatory assets on December 31, 2017, used in the determination of the excess accumulated deferred income taxes ("EADIT").
- Attachment DBS-KAS-4-Rebuttal, the updated functional cost of service model reflecting the Company's rebuttal revenue requirement.

**Q. Please summarize the results of your testimony.**

A. The Company agrees with four changes proposed by Staff, which are described as follows in reference to the schedules where the changes appear in Attachment DBS/KAS-1-Rebuttal:

- Adjustment of Payroll Expense annualization to reflect the actual payroll percent increase for 2020 (Adjustment #1 on page 2 of Attachment DBS-KAS-Rebuttal-1, reflected on Schedule RR-EN-3-2, lines 4 and 13).
- Adjustment to normalize CSR 2019 Ratification Bonus over the term of the contract (Adjustment #2 on page 2 of Attachment DBS-KAS-Rebuttal-1, reflected on Schedule RR-EN-3-2, lines 22 and 23).
- Adjustment to remove the double count of New Hampshire property tax true-up (Adjustment #3 on page 2 of Attachment DBS-KAS-Rebuttal-1, reflected on Schedule RR-EN-3-7, line 89).
- Adjustment to remove $5,313 in additional Keene production costs (Adjustment #4 on page 2 of Attachment DBS-KAS-Rebuttal-1, reflected on Schedule RR-EN-3-10, line 21).

Aside from these changes and those contained in the Company's March 3, 2021, Corrections and Updates ("CU") filing, the Company disagrees with the balance of the revenue requirement adjustments recommended in Staff's testimony. These additional adjustments are unwarranted and should be rejected for reasons discussed below in our rebuttal testimony.

**Q. Did you update the revenue requirement to reflect the Company's rebuttal position?**

A. Yes. The Company last updated the revenue requirement in the CU filing, which demonstrated a reduced revenue increase of $4,933,718. The Company's rebuttal position results in an additional decrease of $358,410 or a total revenue requirement of $4,575,308. The Company's updated schedules are attached as DBS/KAS-1-Rebuttal.

**Q. Please summarize Staff's proposed revenue requirement adjustments.**

A. Ms. Mullinax recommended fourteen[1] adjustments to the Company's revenue requirement. The table below summarizes Staff's proposed adjustments:[2]

| | Description | Rate Base | Operating Income | Revenue Deficiency |
|---|---|---|---|---|
| Adj-1 | Normalize M&S Reflected in Rate Base | (849,232) | | (77,679) |
| Adj-2 | Cash Working Capital | (72,407) | | (6,623) |
| Adj-3 | Modify Amortization of Non-Protected EADIT | | 533,216 | (731,234) |
| Adj-4 | Payroll Expense – 2020 Increase | | 68,201 | (93,528) |
| Adj-5 | Normalize CSR 2019 Ratification Bonus Over Term of Contract | | 10,500 | (14,399) |
| Adj-6 | Long-Term Incentive Compensation | | 183,978 | (252,301) |
| Adj-7 | Payroll Tax | | 297,051 | (407,365) |
| Adj-8 | Sharing of D&O Liability Insurance | | 10,410 | (14,275) |
| Adj-9 | Property Tax-Remove Doubled State of NH TRUE UP | | 168,225 | (230,698) |
| Adj-10 | Remove Additional Keene Production Costs | | 3,874 | (5,313) |
| Adj-11 | Modify Presentation of Pelham Risk Sharing | | (47,092) | 64,580 |
| Adj-12 | Remove Amortization of Depreciation Reserve Imbalance | | 1,119,705 | (1,535,526) |
| Adj-13 | Capitalized Fleet Depreciation | (445,959) | (325,180) | 405,149 |
| Adj-15 | Interest Synchronization | | 26,043 | (35,714) |
| | Impact of Staff's Recommended Cost of Capital | | | (3,797,586) |
| | Pelham Risk Sharing | | | (95,837) |
| | iNATGAS | | | (301,742) |
| | Keene Risk Sharing | | | (43,742) |
| | | (1,367,598) | 2,048,930 | (7,173,832) |

[1] Staff lists fifteen adjustments but in fact only makes fourteen adjustments.
[2] Source: Direct Testimony of Donna H. Mullinax dated March 18, 2021, Bates 000006.

## III. RESPONSE TO STAFF REVENUE REQUIREMENT ADJUSTMENTS

**Q. Please summarize Staff's Adjustment #1 regarding Working Capital.**

A. Staff argues that the most current 13-monthly average of Materials and Supplies are not expected to continue during the rate effective period and therefore should be adjusted downward based on the average working capital balance for thirty-nine months.[3]

**Q. Is this adjustment appropriate?**

A. No, for several reasons. First, Staff's adjustment is not a known and measurable change to the test year and is purely speculative. Additionally, Staff's position is based on a misreading of the Company's response to Staff TS 3-14,[4] which it cites in support of its adjustment. In this response, the Company answered a question about the Company's expectations for continued *increases* in Materials and Supplies balances going forward: ". . . Pipeline replacement is leveling off and the Company expects to see some improvement in Materials and Supplies planning as a result of the move towards an integrated system under SAP." Staff misconstrues the Company's use of the term "leveling off" in this context, which was intended to convey the expectation that Materials and Supplies expense is expected to remain steady and not decline as Staff suggests.[5] Lastly, Staff's adjustment inappropriately relies on annual balances as of December 31, which are not representative of actual costs. As acknowledged by Staff in

[3] Mullinax Direct Testimony, Bates 000014, lines 23 through 27.

[4] Staff did not submit TS 3-14 into the record or cite it directly in its testimony only identifying the source of the Company's response in data response LU 1-1; both responses are included in Attachment DBS/KAS-2-Rebuttal.

[5] "Leveling off" is generally defined as "to approach or reach a steady rate, volume or amount." *See* https://www merriam-webster.com/dictionary/level%20off

its response to LU 1-2,[6] the month of December is outside the construction season and at a time when inventory balances are typically lower. In summary, Staff's adjustment is not known and measurable, is not supported by the facts, and does not appropriately reflect an average of inventory balances carried throughout the year, and therefore the proposed adjustment to Materials and Supplies should be rejected.

**Q. Please summarize Staff's Adjustment #2 regarding Cash Working Capital.**

A. Staff proposes to update the amount of Cash Working Capital included in the Company's rate base for changes related to Staff's various revenue and expense adjustments.[7]

**Q. Do you agree with this adjustment?**

A. Yes, in concept. Staff took no issue with the Company's proposed Cash Working Capital rate. The Company supports updating the Cash Working Capital calculation based on the outcome of revenue and expense adjustments in this proceeding.

**Q. Please summarize Staff's Adjustment #3 regarding the amortization of Non-Protected EADIT.**

A. Staff adjusts the amortization period for Non-Protected EADIT amortization to five years.[8] For the Non-Protected Non-Property related EADIT, Staff states that because the largest contributor to Non-Protected Non-Property related EADIT was regulatory assets, and regulatory assets are "characteristically short lived,"[9] the appropriate amortization

[6] Attached as Attachment DBS/KAS-2-Rebuttal, pages 3–4.
[7] Mullinax Direct Testimony, Bates 000015, lines 3–9.
[8] Mullinax Direct Testimony, Bates 000018, lines 18–22.
[9] Mullinax Direct Testimony, Bates 000019, line 7.

period should be five years. For Non-Protected Property related EADIT, Staff claims that due to the delay in the start of amortization, Non-Protected Property related EADIT should be returned over the same five-year period.[10]

**Q. Are these adjustments appropriate?**

A. No. EnergyNorth is proposing the same EADIT treatment that was allowed for its sister company, Granite State, in its recent rate case. That is, the Company proposes to return the Non-Protected EADIT to customers over the same period of time as the protected EADIT.

Staff's generalization that regulatory assets are "characteristically short-lived" is incorrect. Its position is purely speculative and is not based on a detailed analysis of the regulatory assets that were in existence on December 31, 2017. In fact, a review of the EnergyNorth's December 31, 2017, regulatory assets[11] shows the regulatory assets are long-lived items that are primarily related to environmental costs and pension and other post-retirement employment benefits. Environmental regulatory assets, for example, have lives closer to thirty years. More importantly, of the $77.5 million of regulatory assets in existence on December 31, 2017, environmental regulatory assets make up $48.1 million or 62 percent of the entire balance. Therefore, Staff's recommendation to amortize Non-Protected Non-Property EADIT related to these assets over five years is not reasonable and should be rejected. The Company continues to believe that

[10] Mullinax Direct Testimony, Bates 000019, lines 12–14.
[11] Attached as Attachment DBS/KAS-3-Rebuttal.

amortizing all EADIT over the average remaining life produces an equitable result for both EnergyNorth and its customers, as was allowed for Granite State.

**Q. Do you agree with Staff's proposal to return Non-Protected Property related EADIT over five years?**

A. No. Staff cites[12] the delay in EADIT amortization the Company requested to determine if it had adequate information to calculate the Average Rate Assumption Method ("ARAM") rate as support for its recommendation for returning Non-Protected Property related EADIT over five years. However, if the Company had failed to utilize ARAM, assuming it had the information required to calculate ARAM, it would have been in direct conflict with the 2017 Tax Act. The 2017 Tax Act required companies with the ability to calculate ARAM to return Protected Property related EADIT under that method. Failure to calculate ARAM would have created a tax normalization violation, thus jeopardizing the Company's ability to utilize accelerated depreciation for income tax purposes, which would be a completely unacceptable outcome for the Company and its customers. Accelerated depreciation allows the Company to access cash free capital while customers enjoy the benefit of that cash free capital through a deduction in rate base. Additionally, customers were not materially harmed by the Commission-approved slight delay in the start of the amortization as all the EADIT created by the tax rate change will flow back to customers. Staff admits that returning Non-Protected Property related EADIT over the average remaining life is not an unreasonable approach.[13] For

[12] Mullinax Direct Testimony Bates 00019, lines 8–14.
[13] Mullinax Direct Testimony Bates 000019, lines 8 and 9.

these reasons, Staff's recommendation to return Non-Protected Property related EADIT over five years should be rejected.

**Q. Please summarize Staff's Adjustment #6 regarding long term incentive compensation (LTIP).**

A. Staff proposes to remove LTIP costs from the Company's revenue requirement.[14]

**Q. Is it reasonable to exclude LTIP costs from recovery in the Company's revenue requirement?**

A. No. These plans are part of the Company's market-based compensation and enable the Company to attract and retain a highly qualified senior management team. Incentives are part of the Company's overall compensation package. The incentive compensation (i.e. variable pay) is tied to the Company's performance, which is a widely utilized method of compensating employees by placing a portion of compensation at risk. The plan includes financial performance goals that are designed to drive cost efficiencies in Company operations. The Company's compensation program creates incentives for its employees to reduce costs to the ultimate benefit of customers. Because the Company operates in a return-regulated environment with an obligation to serve its customers, the incentive plan serves an important purpose of aligning the interests of the Company and its customers to reduce costs and identify operational efficiencies. Further, the LTIP program also measures achievements in the areas of safety and customer satisfaction, which have direct customer benefit and are not associated with Company earnings (Staff's witness did not

[14] Mullinax Direct Testimony Bates 000027, lines 13–16.

make note of these additional areas, although they were recognized by Staff's revenue requirements witness in EnergyNorth's prior rate case). For these reasons, the Commission should reject Staff's proposal to exclude these costs.

**Q. Please summarize Staff's Adjustment #7 regarding payroll taxes.**

A. Staff makes two adjustments to the Company's payroll taxes. First, Staff substitutes the Company's payroll tax loading factor with that of its sister company, Granite State, from Docket No. DE 19-064.[15] Second, Staff updates the payroll tax expense amount based on other proposed changes to the Company's proposed labor expense.[16]

**Q. Do you agree with Staff's adjustment to substitute Granite State's payroll tax load factor for the Company's?**

A. No. Staff's adjustment fails to consider the Company's accounting for capitalized payroll tax expense. The Company records all payroll taxes in FERC Account No. 408 Taxes Other Than Income Taxes, for both capitalized and operating labor. The capitalized portion is then removed from Account No. 408 through a credit to FERC Account No. 922 Administrative Expenses Transferred – Credit, and a debit to FERC Account No. 107 Construction Work in Progress – Gas as part of the overhead burden rate applied to construction projects. Staff's adjustment essentially only calculates, and would only allow the Company to recover, payroll tax expense related solely to operating labor. If payroll tax expense is calculated solely applied to operating labor, the Company will under-collect. The Company's method of calculating payroll tax expense provides a

[15] Mullinax Direct Testimony Bates 000028, lines 10–18.
[16] Mullinax Direct Testimony Bates 000028, lines 20–23.

more accurate estimate of payroll tax expense for both capitalized and operating labor on a prospective basis while Staff's adjustment would result in a revenue deficiency for the Company.

**Q. Do you agree with Staff's proposed adjustment to include the effects of its labor increase percentage and CSR Ratification Bonus amortization in the calculation of payroll tax expense?**

A. Yes, in theory. Any changes to labor expense should be considered when determining the appropriate amount of payroll tax expense going forward.

**Q. Please summarize Staff's Adjustment #8 regarding Directors and Officers ("D&O") Liability Insurance.**

A. Staff adjusted the Company's requested D&O insurance to assign fifty percent of the cost responsibly to the Company's shareholders.

**Q. Do you agree with Staff's proposed adjustment to assign fifty percent of D&O cost to shareholders?**

A. No. D&O insurance is a necessary business expense and is prudently incurred by the Company. D&O insurance, like property insurance or any other type of insurance the Company requires to operate its business, is designed to protect the Company from financial risks in conducting its business, which, in effect, protects customer interests. D&O insurance policies not only protect the directors and officers individually, but also protect the assets of the Company. As such, recovery of the entire amount of D&O

insurance costs through distribution rates is appropriate. Accordingly, Staff's proposal to assign fifty percent of the cost to shareholders should be rejected.

**Q. Please summarize Staff's Adjustment #11 regarding the presentation of Pelham risk sharing.**

A. Staff adjusted the Company's revenue requirement for Pelham risk sharing based on the Company's inclusion of projected revenues from a committed large industrial customer that has yet to take service.[17]

**Q. Is this adjustment appropriate?**

A. No. The joint rebuttal testimony of Company witnesses William J. Clark and Steven E. Mullen discusses the Company's position regarding Pelham risk sharing. Attachment DBS/KAS-1-Rebuttal includes no adjustment related to Pelham risk sharing.

**Q. Please summarize Staff's Adjustment #12 regarding the amortization of the Company's depreciation reserve imbalance.**

A. Staff recommends that the Company's current depreciation imbalance should stop, and the amortization removed from the Test Year.[18]

**Q. Is this a reasonable adjustment?**

A. No. The rebuttal testimony of Mr. Mullen discusses the Company's response to the Staff's position on the depreciation reserve imbalance amortization. Attachment

[17] Frink Direct Testimony Bates 000037, line 20–Bates 00038, line 2
[18] Frink Direct Testimony Bates 000042, lines 12–16.

DBS/KAS-1-Rebuttal includes no adjustment related to EnergyNorth's current depreciation imbalance amortization.

**Q. Please summarize Staff's Adjustment #13 regarding capitalized fleet depreciation.**

A. Staff recommended the Company remove from its rate base allocated capitalized fleet depreciation expense and recover the removed amount in depreciation expense.[19] Specifically, Staff's position is that the Company is incorrectly capitalizing a portion of its fleet vehicle depreciation expense as a component of gas plant costs and should instead expense the entire amount.

**Q. Is Staff's position correct?**

A. No. The Company's accounting treatment of these costs complies with the FERC Uniform System of Accounts ("FERC USoA"). The Gas Plant Instructions in 18 C.F.R. Pt. 201, 3 - *Components of construction cost*, sections (4) and (5) state:

> (4) "Transportation" includes the cost of transporting employees, materials and supplies, tools, purchased equipment, and other work equipment (when not under power) to and from points of construction. It includes amounts paid to others as well as the cost of operating the utility's own equipment. (See item 5 following.)
>
> (5) Special machine service includes, the cost of labor (optional), materials and supplies, *depreciation*, and other expenses incurred in the maintenance, operation and use of special machines, such as steam shovels, pile drivers, derricks, ditchers, scrapers, material unloaders, and other labor saving machines; also expenditures for rental, maintenance and operation of machines of others. It does not include the cost of small value or short life which are include in the cost of materials and supplies. (See item 3, above.) When a particular construction job requires the use for an extended period of time of special machines, transportation or other equipment, the net book value thereof, less the appraised or salvage value

[19] Mullinax Direct Testimony Bates 000042, lines 8–13.

> at the time of release from the job, shall be included in the cost of construction. (Emphasis added)

Fleet vehicles are routinely utilized to perform activities and to transport employees to and from construction sites. Section 4 above makes it clear that the cost of operating the "utility's own equipment" is an allowable capitalized cost. Depreciation is a cost of operating the fleet vehicles and is even called out specifically under section 5 of FERC's components of construction costs. Further, Note B to the instructions for Account 403 Depreciation Expense states:

> Depreciation expenses applicable to transportation equipment, shop equipment, tools, work equipment, power operated equipment and other general equipment may be charged to clearing accounts as necessary in order to obtain a proper distribution of expenses between construction and operation.

Thus, the capitalization of depreciation expense under these conditions is necessary and appropriate under US GAAP standard ASC 360, and the Uniform System of Accounts. For those reasons, Staff's proposed adjustment to capitalized fleet depreciation expense is unfounded and should be rejected.

**Q. Do you have any other concerns with Staff's testimony regarding its adjustment to rate base and depreciation expense for capitalized fleet depreciation?**

A. Yes. Contrary to Staff's view, the accounting treatment in question is a benefit to customers. For rate making purposes, uncapitalized operating expenses are recovered annually while capitalized expenses are recovered over the life of the underlying asset. In essence, what the Company does is take a small amount of depreciation expense, recognizing it as a cost of construction and therefore correctly including it in the cost of a long-lived asset, and amortizing recovery of that amount over many years. Through capitalization, future customers will pay their fair share of all of the costs involved with installation of a new asset, including fleet depreciation, while under Staff's approach costs would only be borne by the current generation of customers.

**Q. Please summarize Staff's Adjustment #15 regarding interest synchronization.**

A. Staff's adjustment synchronizes rate base and cost of capital with the tax calculation using Staff's proposed weighted cost of debt.[20]

**Q. Do you agree with this adjustment?**

A. Yes, in theory. The Company agrees that interest synchronization should be adjusted to reflect any final adjustments to rate base and the cost of capital. That approach is consistent with the approach taken by the Company in its original filing and CU filing. Schedule RR-EN-3-8, line 11 shows the adjusted amount of synchronized interest expense of $7,626,555, which is $407 lower than the $7,626,962 included in the CU filing.

[20] Mullinax Direct Testimony Bates 000042, lines 16–19.

**Q. Does the Company agree with Staff's proposed adjustments relative to the cost of capital?**

A. No. Liberty supports its initial filing with respect to the return on equity and capital structure. This is discussed in the rebuttal testimony of Company witness John Cochrane of FTI Consulting.

**Q. Ms. Mullinax's testimony also includes adjustments that are labeled "iNATGAS" and "Keene Risk Sharing." What is the Company's position with respect to those adjustments?**

A. Both of Staff's proposed adjustments should be rejected. These topics are addressed in the joint rebuttal testimony of Messrs. Clark and Mullen.

**Q. Did you update the functional cost of service model to reflect the Company's rebuttal revenue requirement position?**

A. Yes. We have provided an updated functional cost of service model based on the Company's rebuttal revenue requirement.[21] The proposed revenue increase related to the cost of gas has decreased by $20,207 from the CU filing amount of $2,033,998, to $2,013,791.

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

A. Yes, it does.

[21] Attached as Attachment DBS/KAS-4-Rebuttal.