

**BEFORE THE  
PUBLIC UTILITIES COMMISSION  
OF RHODE ISLAND**

**PROVIDENCE WATER SUPPLY BOARD ) DOCKET NO. 4618**

**DIRECT TESTIMONY**

**OF**

**JEROME D. MIERZWA**

**ON BEHALF OF THE  
DIVISION OF PUBLIC UTILITIES AND CARRIERS**

**October 14, 2016**

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**EXETER**

**ASSOCIATES, INC.**

10480 Little Patuxent Parkway, Suite 300  
Columbia, Maryland 21044

BEFORE THE  
PUBLIC UTILITIES COMMISSION  
OF RHODE ISLAND

PROVIDENCE WATER SUPPLY BOARD ) DOCKET NO. 4618

DIRECT TESTIMONY OF JEROME D. MIERZWA

1 **I. INTRODUCTION**

2 Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS  
3 ADDRESS?

4 A. My name is Jerome D. Mierzwa. I am a principal and Vice President of Exeter  
5 Associates, Inc. ("Exeter"). My business address is 10480 Little Patuxent Parkway,  
6 Suite 300, Columbia, Maryland 21044. Exeter specializes in providing public utility-  
7 related consulting services.

8 Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND  
9 EXPERIENCE.

10 A. I graduated from Canisius College in Buffalo, New York, in 1981 with a Bachelor of  
11 Science Degree in Marketing. In 1985, I received a Master's Degree in Business  
12 Administration with a concentration in finance, also from Canisius College. In July  
13 1986, I joined National Fuel Gas Distribution Corporation ("NFG Distribution") as a  
14 Management Trainee in the Research and Statistical Services Department ("RSS").  
15 I was promoted to Supervisor RSS in January 1987. While employed with NFG  
16 Distribution, I conducted various financial and statistical analyses related to the  
17 Company's market research activity and state regulatory affairs. In April 1987, as  
18 part of a corporate reorganization, I was transferred to National Fuel Gas Supply  
19 Corporation's ("NFG Supply") rate department where my responsibilities included

1 utility cost of service and rate design analysis, expense and revenue requirement  
2 forecasting and activities related to federal regulation. I was also responsible for  
3 preparing NFG Supply's Federal Energy Regulatory Commission ("FERC") Purchase  
4 Gas Adjustment ("PGA") filings and developing interstate pipeline and spot market  
5 supply gas price projections. These forecasts were utilized for internal planning  
6 purposes as well as in NFG Distribution's purchased gas cost proceedings.

7 In April 1990, I accepted a position as a Utility Analyst with Exeter  
8 Associates, Inc. ("Exeter"). In December 1992, I was promoted to Senior Regulatory  
9 Analyst. Effective April 1, 1996, I became a principal of Exeter. Since joining  
10 Exeter, my assignments have included water and gas utility class cost of service and  
11 rate design analysis, evaluating the gas purchasing practices and policies of natural  
12 gas utilities, sales and rate forecasting, performance-based incentive regulation,  
13 revenue requirement analysis, the unbundling of utility services, and the evaluation of  
14 customer choice natural gas transportation programs.

15 Q. HAVE YOU PREVIOUSLY TESTIFIED IN REGULATORY  
16 PROCEEDINGS ON UTILITY RATES?

17 A. Yes. I have provided testimony on more than 200 occasions in proceedings before  
18 the FERC, utility regulatory commissions in Delaware, Georgia, Illinois, Indiana,  
19 Louisiana, Maine, Massachusetts, Montana, Nevada, New Jersey, Ohio,  
20 Pennsylvania, Texas, Utah, and Virginia, as well as before the Public Utilities  
21 Commission of Rhode Island ("Commission").

22 Q. HAVE YOU PREVIOUSLY TESTIFIED ON WATER UTILITY ISSUES  
23 BEFORE THIS COMMISSION?

24 A. Yes. I previously testified before this Commission in the following proceedings:

- 25 • Providence Water Supply Board ("Providence Water") Docket Nos. 2048,  
26 3163, 3832, and 4406;

- 1 • Kent County Water Authority Docket Nos. 2555, 3311, and 4611;
- 2 • City of Newport-Water Division Docket Nos. 2985, 4355, and 4295; and
- 3 • Pawtucket Water Supply Board Docket Nos. 2674 and 3945.

4 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

5 A. My testimony addresses the Class Cost of Service (“CCOS”) Study and rate design  
6 proposals presented in this proceeding by Providence Water.

7 Q. PLEASE SUMMARIZE YOUR RECOMMENDATIONS CONCERNING  
8 PROVIDENCE WATER’S CCOS STUDY AND RATE DESIGN  
9 PROPOSALS IN THIS PROCEEDING.

10 A. My recommendations concerning Providence Water’s CCOS Study and rate design  
11 proposals in this proceeding are as follows:

- 12 • As part of the settlement agreed to and approved by the Commission in  
13 Docket No. 4406, Providence Water agreed to hire an independent consultant  
14 to verify the accuracy of its plant asset values. These plant asset values are  
15 utilized to allocate Infrastructure Replacement and Capital Fund costs in  
16 Providence Water’s CCOS Study. It is my understanding that this verification  
17 process has not been completed. It is also my understanding that Providence  
18 Water will further address the verification process in its rebuttal testimony.  
19 The Division will present its recommendations concerning plant asset values  
20 after review of Providence Water’s rebuttal testimony.
- 21 • The functionalization of bad debt expense and the allocation of the expenses  
22 included Account 63560 reflected in Providence Water’s CCOS Study are  
23 unreasonable. However, because there are offsetting factors that should be  
24 considered, I am accepting Providence Water’s functionalization of bad debt  
25 expense and allocation of Account 63560 expenses in this proceeding.
- 26 • With the exceptions just described, I generally find Providence Water’s CCOS  
27 Study to be reasonable and appropriate for determining cost responsibility and  
28 establishing rates in this proceeding.
- 29 • Unless otherwise indicated by the CCOS Study approved by the Commission  
30 in this proceeding, the 15 percent increase in fire protection rates proposed by  
31 Providence Water should be maintained and not reduced in the event that the

1 Commission authorizes an increase for Providence Water that is less than its  
2 requested increase.

3 Q. HOW IS THE REMAINDER OF YOUR TESTIMONY ORGANIZED?

4 A. Following this introductory section, my testimony is divided into the additional  
5 sections. The first section provides an overview of water utility cost of service  
6 methodologies. Next, I address Providence Water's CCOS Study. Finally, I present  
7 my recommendations concerning rate design.

8

9 **II. OVERVIEW OF COST OF SERVICE METHODOLOGIES**

10 Q. WHAT IS THE OBJECTIVE OF A COST OF SERVICE STUDY?

11 A. A cost of service study is conducted to assist a utility or commission in determining  
12 the level of costs properly recoverable from each of the various classes to which the  
13 utility provides service. Allocation of recoverable costs to each class of service is  
14 generally based on usage and cost causation principles.

15 Q. WHAT ARE THE PRIMARY COST OF SERVICE STUDY  
16 METHODOLOGIES UTILIZED FOR WATER UTILITIES?

17 A. The two most commonly used and widely recognized methods of allocating costs  
18 to customer classes for water utilities are the base-extra capacity method and the  
19 commodity-demand method. Both of these methods are set forth in the American  
20 Water Works Association's ("AWWA") *Principles of Water Rates, Fees and*  
21 *Charges* ("AWWA M1 Manual").

22 Q. PLEASE SUMMARIZE EACH OF THESE METHODS.

23 A. Under the base-extra capacity method, investment and costs are first classified into  
24 four primary functional cost categories: base or average capacity, extra capacity,  
25 customer, and direct fire protection. Customer costs are commonly further divided

1 between meter and service related and account or bill related costs. Extra capacity  
2 costs may also be divided between maximum day and maximum hour costs. Once  
3 investment and costs are classified to these functional categories, they are then  
4 allocated to customer classes. Base costs are allocated according to average water  
5 use, and extra capacity costs are allocated on the basis of the excess of peak demands  
6 over average demands. Meter and service related customer costs are allocated on the  
7 basis of relative meter and service investment or a proxy thereof. Account-related  
8 customer costs are allocated in proportion to the number of customers or the number  
9 of bills. The CCOS Study presented by Providence Water in this proceeding utilizes  
10 the base extra-capacity methodology.

11 The commodity-demand method follows the same general procedures.  
12 However, usage related costs are classified as commodity and demand related rather  
13 than as base and extra capacity related. Commodity related costs are allocated to  
14 customer classes on the basis of total water use (which is equivalent to average  
15 demand), and demand related costs are allocated on the basis of each class'  
16 contribution to peak demand rather than on the basis of class demands in excess  
17 of average use.

18  
19 **III. EVALUATION OF PROVIDENCE WATER'S CLASS**  
20 **COST OF SERVICE STUDY**

21 Q. PLEASE IDENTIFY THE CUSTOMER CLASSES INCLUDED IN  
22 PROVIDENCE WATER'S CCOS STUDY.

23 A. Providence Water provides retail service to three customer classes:

- 24 • Residential  
25 • Commercial  
26 • Industrial

1 Providence Water also provides Public and Private Fire Protection service and serves  
2 wholesale (water for resale) customers. Each of these customer classes is included in  
3 Providence Water's CCOS Study.

4 Q. HAS PROVIDENCE WATER REVISED THE CCOS STUDY INITIALLY  
5 INCLUDED IN ITS MAY 16, 2016 FILING WITH THE COMMISSION?

6 A. Yes. Providence Water submitted a revised version of the CCOS Study initially  
7 included in its May 16, 2016 filing to the parties in this proceeding on September 13,  
8 2016, and a second revised version of the CCOS Study was submitted to the parties  
9 on September 27, 2016.

10 Q. DO YOU HAVE ANY CONCERNS WITH PROVIDENCE WATER'S  
11 CURRENT VERSION OF THE CCOS STUDY?

12 A. Yes, I have several concerns with Providence Water's current version of the CCOS  
13 Study which include:

- 14 • The plant asset values utilized to allocate Infrastructure Replacement and  
15 Capital Fund costs;
- 16 • The functionalization of bad debt expense; and
- 17 • The allocation of the expenses included in Account 63560 Contractual  
18 Services - Other.

19 Q. WHAT ARE YOUR CONCERNS WITH PROVIDENCE WATER'S ASSET  
20 VALUES?

21 A. In Providence Water's last general rate case, Docket No. 4406, there were concerns  
22 expressed with respect to the accuracy of Providence Water's plant account asset  
23 values, including the accumulated depreciation and contribution in aid-of-  
24 construction ("CIAC") balances. As part of the settlement agreed to and approved by  
25 the Commission in Docket No. 4406, Providence Water agreed "...to have an

1 independent consultant verify the accuracy of each plant account, including  
2 depreciation and CIAC to resolve any questions and provide a level of confidence  
3 that future allocations are accurate.” These plant asset values are utilized to allocate  
4 Infrastructure Replacement and Capital Fund costs in the current version of  
5 Providence Water’s CCOS Study. While Providence Water did hire an independent  
6 consultant to verify its asset values, it is my understanding that the verification  
7 process has not been completed. It is also my understanding that Providence Water  
8 will further address the verification of plant asset values in its rebuttal testimony. The  
9 Division will present its recommendations concerning plant asset values after review  
10 of Providence Water’s rebuttal testimony.

11 Q. HOW HAS BAD DEBT EXPENSE BEEN ASSIGNED IN PROVIDENCE  
12 WATER’S CCOS STUDY?

13 A. Bad debt expense has been assigned 50 percent to the meters/services cost function  
14 and 50 percent to the billing/collection cost function.

15 Q. DO YOU AGREE WITH PROVIDENCE WATER’S ASSIGNMENT OF  
16 BAD DEBT EXPENSE?

17 A. No. Bad debt expense relates to the failure to recover all of Providence Water’s  
18 functional costs, including base, maximum day, and maximum hour functional costs,  
19 not just meter/services and billing/collection costs. As such, bad debt expense should  
20 be assigned to all retail functional costs, and this would be consistent with the  
21 assignment of bad debt expense in the AWWA M1 Manual that Providence Water is  
22 using as a guide for its CCOS Study (page 67, 6<sup>th</sup> Edition). Bad debt expense should  
23 not be assigned to wholesale customers because they experience their own bad debt  
24 expense from their retail customers.



1 Q. ARE YOU RECOMMENDING THAT THE CURRENT VERSION OF  
2 PROVIDENCE WATER'S CCOS STUDY BE REVISED TO REFLECT  
3 YOUR RECOMMENDED FUNCTIONALIZATION OF BAD DEBT  
4 EXPENSE?

5 A. No. Although I disagree with Providence Water's functionalization of bad debt  
6 expense, I am not recommending that the current version of the CCOS Study be  
7 revised to incorporate my recommendation. Adopting my recommendations would  
8 reduce the costs assigned to the meters/services and billing/collection cost function.  
9 There are a number of the cost allocation factors included in Providence Water's  
10 CCOS Study (e.g., Y4, Com Y, Com Z, DY, HMY) that provide for the reassignment  
11 of costs that would ordinarily be assigned to the meters/services and billing/collection  
12 cost functions to the other functional cost categories (e.g., base, maximum day,  
13 maximum hour). The effect of Providence Water's reassignment is to shift costs from  
14 the retail monthly service charge to the retail volume charge. These reassignments  
15 were introduced in prior dockets to mitigate increases in service charges, and have  
16 been continued in this proceeding.

17 The monthly retail service charges proposed by Providence Water in this  
18 proceeding generally do not vary significantly from the existing service charges. For  
19 example, the existing monthly service charge for a customer with a 5/8-inch meter is  
20 \$7.89 and the proposed charge is \$7.82. Adopting my recommended change to the  
21 functionalization of bad debt would further reduce Providence Water's proposed  
22 monthly service charges. Because there are other costs that could be included,  
23 assigned to the meters/services and billing/collection functional cost categories and  
24 recovered through monthly service charges that would offset the impact of adopting

1 my proposal with respect to the assignment of bad debt expense, I am accepting  
2 Providence Water proposed functionalization of bad debt expense in this proceeding.

3 Q. PLEASE EXPLAIN HOW THE COSTS INCLUDED IN ACCOUNT 63560  
4 CONTRACTUAL SERVICE - OTHER HAVE BEEN ALLOCATED IN  
5 PROVIDENCE WATER'S CCOS STUDY.

6 A. Account 63560 has historically included the costs incurred by Providence Water in  
7 connection with the repair of leaks on customer service lines. Therefore, in  
8 Providence Water's CCOS Study, these costs have been assigned to the  
9 meter/services function.

10 Q. IS THE ASSIGNMENT OF THE COSTS INCLUDED IN ACCOUNT 63560  
11 TO THE METER/SERVICES FUNCTION REASONABLE?

12 A. No. As explained in the response to Div. 2-7, pro-forma expenses under Account  
13 63560 are predominately associated with police details for mains repair and flushing  
14 activity. Therefore, it would appear appropriate to allocate these expenses consistent  
15 with the allocation of transmission and distribution mains operating and maintenance  
16 expenses.

17 Q. ARE YOU RECOMMENDING THAT PROVIDENCE WATER'S  
18 CURRENT CCOS STUDY BE REVISED TO REFLECT YOUR  
19 RECOMMENDED ALLOCATION OF THE COSTS INCLUDED IN  
20 ACCOUNT 63560?

21 A. No. As previously explained, certain costs that could have been assigned to the  
22 meters/services function and included in monthly service charges have been assigned  
23 to other functional cost categories. Because of this, for the same reasons I am  
24 accepting Providence Water's assignment of bad debt expense in this proceeding, I

1 am also accepting Providence Water's assignment of the expenses included in  
2 Account 63560.  
3

4 **IV Rate Design**

5 Q. HOW DID PROVIDENCE WATER DEVELOP THE RATES IT IS  
6 PROPOSING IN THIS PROCEEDING?

7 A. Generally, Providence Water is proposing to adopt the rates indicated by its CCOS  
8 Study. An exception to this is the rates for fire protection services. For fire  
9 protection services, Providence Water is proposing a 15 percent increase to avoid the  
10 potential for rate shock. If fire protection service charges were to increase to the level  
11 indicated by Providence Water's CCOS Study, the increase would be approximately  
12 84 percent.

13 Q. DO YOU AGREE WITH PROVIDENCE WATER'S PROPOSAL TO  
14 LIMIT THE RATE INCREASE FOR FIRE PROTECTION SERVICES TO  
15 15 PERCENT?

16 A. Yes. However, unless otherwise indicated by the CCOS Study approved by the  
17 Commission in this proceeding, the 15 percent increase proposed by Providence  
18 Water should be maintained and not reduced in the event that the Commission  
19 authorizes an increase for Providence Water that is less than its requested increase.

20 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

21 A. Yes, it does at this time.