# GENERAL RATE FILING

REBUTTAL TESTIMONY
OF GARY S. PRETTYMAN

July 2018

Submitted to:
State of Rhode Island and Providence
Plantations Public Utilities Commission

RIPUC Docket No. 4800

Submitted by:

SUEZ Water Rhode Island Inc.

**Q. Please state your name, occupation and business address.**

A. My name is Gary S. Prettyman and I am Senior Director, Regulatory Business at SUEZ Water Management and Services, Inc. My business address is 461 From Rd, Paramus, NJ 07652.

**Q. Are you the same Gary Prettyman that previously submitted testimony in this proceeding?**

A. Yes, I am.

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

A. I will be discussing SUEZ Water Rhode Island Inc.'s (the "Company" or "SWRI") request for a Distribution System Improvement Charge ("DSIC") and responding to the comments made by Mr. Smith on behalf of the Rhode Island Division of Public Utilities and Carriers ("Division"). I will also be addressing the Cash Working Capital ("CWC") adjustments made by Mr. Smith.

Additionally, I will be addressing the testimony of Mr. David Bebyn who filed testimony on behalf of the Towns of South Kingston and Narragansett and the Union Fire District ("Intervenors").

**Q. How is your rebuttal testimony organized?**

A. I will address all of the issues raised by the Division for which I am responding to and thereafter I will address concerns raised by the Intervenors.

**Q. Please summarize the Company's proposal with regard to the DSIC program.**

A. In my direct testimony I detailed the Company's proposal, however, I did so in narrative form. Attached to this testimony as Exhibit GSP-1 is the Company's proposal in bullet form which is being provided for clarity.

**Q. Have you made any changes to your original DSIC proposal?**

A. Yes, I made one change. The Company originally proposed that the Rhode Island Public Utilities Commission ("Commission") and the Division would have 30 days to review the Company's DSIC filing before rates are adjusted. Given Mr. Smith's concerns that a 30-day review period is too short, the Company now proposes a 60-day review period.

**Q. What comments do you have regarding Mr. Smith's testimony on the DSIC program.**

A. I will address each of Mr. Smith's comments in turn.

1) Mr. Smith proposed that DSIC Eligible plant should be limited to replacement of non-revenue producing transmission and distribution mains and services.

**Response:** The Company agrees with Mr. Smith's assertion; this is the intent of the program. However, as details in Exhibit GSP-1, qualified additions in the DSIC program may include among other things: mains; main cleaning and lining; services, hydrants; valves; short mains and valves; meters; dead-end looping;

and re-location due to government requirements.

2) Mr. Smith asserted that the way that SWRI is financing its prospective replacement of utility infrastructure, such as old, leak-prone transmission and distribution mains and services, between rate cases should be carefully monitored. For example, if such infrastructure replacement investment can be financed with short-term debt or bonds between rate cases, Mr. Smith asserted that ratepayers should not be charged with an equity return. Additionally, since there would be virtually no risk of recovery for the DSIC-includable projects, Mr. Smith argues that the return on equity applicable for the surcharge should be reduced to reflect the lower risk.

**Response:** The Company disagrees. The concept behind the DSIC is to enable the Company to invest and replace needed infrastructure in a timely manner. The revenue requirement of the surcharge should reflect the same treatment as in a rate case. That is why the last allowed rate of return is utilized. This treatment is consistent with the DSIC program in the three other states where SUEZ has a DSIC program.

3) Mr. Smith proposed that at no point shall there be (i) utility plant assets that are simultaneously included in base rates and a DSIC Rate Component or (ii) a base rate that provides or will provide the Company with recovery of revenues associated with the revenue requirement on investments for which an

DSIC Rate Component provides or will provide simultaneous recovery (and vice versa). Calculations of utility plant in service and revenue requirements in each base rate case and the annual DSIC filing will include appropriate adjustments to ensure these outcomes do not occur.

**Response:** The Company agrees that there should be no double recovery, however the rule can be simplified by limiting DSIC projects to those that are incremental to projects included in previous base rate cases. For example, between rate cases, all DSIC projects would be incremental as they were not allowed in the previous rate case. In a current rate case any DSIC projects that are being recovered through a surcharge, the DSIC rate would go to zero and those projects would be rolled into base rates.

4) Mr. Smith proposed that the Company should not have a base rate case and a DSIC filing simultaneously pending before the Commission.

**Response:** The Company disagrees. That is the purpose of a DSIC. There shall not be a Gap Period or overlapping of projects. Because of the length of time that a rate case may take, it is possible to have a DSIC semi-annual filing be effective during the time that a rate case is pending. However, there will be no double counting of investments. A Gap Period would exist if the rate case utility plant in-service allowed reflected investments through say December 31 of a given year and those rates were not effective until May of the following year. The period between December and May would be the Gap period. The DSIC program however would allow a new DSIC program to start and include investments beginning January 1 so that the Company could earn a return on those investments.

5) Mr. Smith proposed that in each annual DSIC filing or amendment to a DSIC filing, the DSIC Rate Component proposed to be collected in the succeeding annual period (inclusive of the impact of any reconciliation scheduled for implementation during that period) be limited to an amount that does not exceed 2.5% of the revenue requirement authorized in the Company's most recent base rate case.

**Response:** The Company disagrees. DSIC surcharges are semi-annual. The DSIC program as proposed has an overall cap of 7.5%. This may be achieved in semi-annual increments between rate cases but not limited to annual caps within that. Although the program is to assist the Company from making much needed investment, the Company would still have budget limitations as to how much could be completed in each six-month period and as such would limit the DSIC surcharge percentage.

6) Mr. Smith proposed that in each annual DSIC filing or amendment to a DSIC filing, the DSIC Rate Component proposed to be collected in the succeeding annual period (inclusive of the impact of any reconciliation scheduled for implementation during that period) will be limited to an amount that, when

combined with the percentage increase(s) implemented through previous DSIC filings since the most recent rate case, does not exceed 7.5% of the revenue requirement authorized in the most recent base rate case.

**Response:** This is consistent with the intent of the Company's original proposal. The Company therefore agrees.

7) Mr. Smith proposed that estimated amounts for plant additions used in DSIC applications shall be trued-up to actual amounts in the subsequent DSIC filing.

**Response:** The Company disagrees. Mr. Smith misunderstands the intent of the program. DSIC filings only reflect <u>actual</u> costs and must be in service to qualify. Thus, there would be no estimated costs within the DSIC to be trued-up.

8(a) Mr. Smith proposed that the Company not be permitted to implement a DSIC Rate Component after a DSIC investment base reset to zero following a base rate case order.

**Response:** The Company is unable to address this issue as it needs further explanation.

8(b) Mr. Smith proposed that the Company not be permitted to implement a DSIC Rate Component if an annual DSIC Rate Component is already in place, to increase the existing DSIC Rate Component with a subsequent calendar year's incremental projected investment in DSIC Facilities.

**Response:** As mentioned above, only projects that are completed and in-service are DSIC eligible; thus, the DSIC will never include any projected projects. As such, the Company needs further explanation on this comment.

8(c) Mr. Smith proposed that the Company not be permitted to implement a DSIC Rate Component if the Company's achieved return on average equity investment for regulatory accounting purposes and measured on a calendar year basis exceeds the authorized return on common equity set in the Company's most recent base rate case.

**Response:** The Company agrees. In such a situation, the Company will still make its annual DSIC filing, but only for purposes of maintaining the existing DSIC Rate Component (if any) and for addressing any needed reconciliations of costs and revenues from previous years.

9) Mr. Smith proposed that the DSIC rate base reflect deductions for an amount equivalent to the annual depreciation expenses imbedded in the base rates for the types of plant that are being addressed by the DSIC capital investment, such that there will be no DSIC adjustment for a year until and unless the new capital spending for non-revenue producing transmission and distribution mains and services exceeds the amount of annual depreciation

allowed for mains and services in the Company's most recent rate case.

**Response:** The Company disagrees. The DSIC program is intended to reflect the Company's current investment in applicable projects. It should not be related to annual depreciation expense, as proposed by Mr. Smith, because the program does not consider all other investments in Company facilities that continue to increase between rate cases which increase rate base with no recovery. The DSIC also does not reflect increases in operating expenses which cannot be reflected in rates until the Company's next rate case.

10) Mr. Smith proposed that the DSIC terminate after five years or until the utility has its base rates reset in a base rate case, whichever occurs sooner.

**Response:** The Company agrees.

11) Mr. Smith proposes that the DSIC rate base reflect a reduction for the provision for the accelerated tax depreciation on the DSIC-includable plant additions, i.e., the DSIC rate base will be reduced to reflect the ADIT amounts on DSIC includable plant.

**Response:** The Company agrees based upon the Company's book calculation of ADIT. The Company would also include accumulated depreciation on the DSIC eligible plant. These two items were included in the Company's original proposal.

12) Mr. Smith proposed that as recognition of the reduction in risk related to regulatory lag and for recovery of the revenue requirement associated with capital investment in replacing mains and services between rate cases, the cost of capital for the DSIC should be lower than the cost of capital used in the general rate case.

**Response:** The Company disagrees with this comment as stated in its response to Point 2 above.

13) Mr. Smith proposed that the Division and the Commission have at least 120 days to review the Company's DSIC filing before rates are adjusted.

**Response:** The Company disagrees. The Company modified its original position from 30 days to 60 days, however the Company disagrees with a 120-day review period because it is unnecessary. The purpose of the review period is to verify the Company's calculation and to ensure that only DSIC projects are included. It is not intended as a pre-approval process. For comparison, the review periods in the other states in which SUEZ has a DSIC program are as follows: Delaware - 30 days; Pennsylvania - 30 days; New Jersey - 60 days.

14) Mr. Smith proposed other reporting requirements, such as reporting on improvements in the quality of service, reductions to leaks, and reductions to lost and unaccounted for water, etc.

**Response:** The Company disagrees. As we have seen in other states where we have DSIC, it can take several years before results show up in statistics so early reporting is not a good indicator of the program's success.

**Q. What adjustments did Mr. Smith make with regard to CWC?**

A. Mr. Smith made three adjustments to the Company's CWC. First, he eliminated the amortization of tank painting because the unamortized balance of tank painting is included in rate base as a regulatory asset. Second, he made flow through adjustments to reflect his adjustments to O&M expenses. Third, he reflected the change in the Company's billing cycle from quarterly to monthly.

**Q. Do you agree with these adjustments?**

A. Partly. I agree with the removal of the tank painting amortization from CWC and the flow through impacts of O&M adjustments. I do not agree with the adjustment related to the billing cycle.

**Q. Please explain.**

A. Mr. Smith reduced the 1/8 formula by 2/3 to reflect the Company's transition from quarterly billing to monthly billing. However, he neglected to mention that the 1/8 methodology already reflects monthly billing and is regularly being used instead of a lead/lag study which is costly. The American Water Works Association recognizes this and so stated in Manual M-35, Revenue Requirements, as follows:

> "In the absence of a lead-lag study, the 45 day rule is frequently used when monthly billing is practiced. The average daily amount of costs is multiplied by 45 to determine the working capital allowance to reflect the billing period plus a lag in payment."

To illustrate this statement for each dollar day of revenue divided by 365 days times the 45 days mentioned above or 1/365x45 = 12.33%. The 1/8 formula equal 12.50% (1/8=12.50%).

Therefore, for the reasons stated, Mr. Smith's adjustment to the 1/8 formula should be rejected.

**Q. What issues were raised by the Intervenors?**

A. Mr. Bebyn raises four issues. Rate of Return, specifically Return on Equity. This will be addressed by Mr. Walker. The inclusion of unamortized rate case in rate base, which based upon the testimony of the Division and Mr. Bebyn, the Company agrees that in Rhode Island it should not be included. Present rate revenues and the flow through impact on certain operating expenses. Lastly, I will address Mr. Bebyn's comments regarding the Company's DSIC proposal.

**Q. What area will you be addressing?**

A. I will address the present rate revenue adjustment made by Mr. Bebyn and why it should not be considered. I will also address Mr. Bebyn's comments on the Company's DSIC proposal.

**Q. Please discuss Mr. Bebyn's revenue adjustments.**

A. Mr. Bebyn's revenue adjustments are based solely on the fact that different revenue classes have different percentage changes. He has not performed any detailed analysis to reach his conclusions. He criticizes the Company for different analyses for the different classes however the detailed and supported analyses made by Company Witness Elda Gill are more representative of that class of customer.

For example, Company Witness Elda Gill looked at the difference between baseload usage and weather related usage. It is clear from her analysis that base load continues to decline for the reasons she stated. Therefore for that portion a trend is appropriate. Regarding the weather related usage, Company Witness Elda Gill looked at that usage over the last five years and since it varies from year to year she used an average. The pro forma usage reflects a trend for the base load to 2019 because that is the rate year plus the average of weather related. The fact that Mr. Bebyn only uses the twelve months ended September 30, 2017 is not indicative of anything and not supported and should be rejected.

With regard to resale, Mr. Bebyn states that the resale class consists of residential and commercial and the Company reflects a decrease of 10% to the rate year. While this may be true, based upon the data, the resale class continues to decline. There is no explanation provided by Mr. Bebyn why this trend should not continue in setting rates other than it should be 2018 and not the projection for 2019.

**Q. Please address the Intervenors concerns regarding the DSIC program.**

A. Mr. Bebyn lists four areas of concern. First, the Intervenors believe that they will have an opportunity to give pre-approval of the projects. Second is the period for review. Third is how funds from the surcharge should be handled. Lastly, that fully depreciated utility plant of non-DSIC assets should be considered.

The first two items have been addressed above in the discussion regarding the Division. The DSIC program is not intended to have a pre-approval process. Also the Company has increased the review process to 60 days.

Regarding the third issue, the funds are to be treated as any other revenue the Company receives and should not be restricted. The funds from DSIC, just like base rates, are used to fund the daily operations of the Company including investment in facilities. If the DSIC funds were restricted the Company would need to find other funds to replace those.

The last issue pertains to depreciation expense. Mr. Bebyn gives an example of the CIS depreciation expense. That example is not appropriate for two reasons. First the CIS asset is a short lived asset and is only being amortized over 8 years. Second, although Mr. Bebyn was unaware at the time of his testimony, Division has proposed and adjustment to the CIS expense which the Company has agreed to. Regardless of both of these items this issue was addressed in Point No.9 on Page 7 of this testimony in response to the Division position and Mr. Bebyn's position should not be considered here.

**Q. Does this conclude your testimony at this time?**

A. Yes, it does.

**Exhibit GSP-1**

## DSIC PROCEDURE

1) The DSIC should reflect qualified additions for the previous six-month period that are non-revenue producing and include additions that are replacing and rehabilitating in nature.

2) Qualified additions may include among other things: mains; main cleaning and lining; services, hydrants; valves; short mains and valves; meters; dead-end looping; and re-location due to government requirements.

4) The rate of return would be based upon the Company's last base rate case

5) Rate base would include accumulated depreciation and deferred federal income tax on qualified additions

6) Depreciation expense on the DSIC plant would be included.

7) Revenue taxes would be grossed-up and the revenue requirement would be on a pre-tax basis.

8) 7.5% cap on the DISC surcharge.

9) The surcharge calculation should be filed within 15 days after the end of the 6 month DSIC period. The Surcharge will go into effect 45 days later (or 60 days after the DSIC surcharge period)

   Note: this review period is to review the calculation and that the projects included are qualified projects. There is no review period prior to projects commencing. Revenues from DSIC projects is considered temporary until rolled into base rates.

10) A surcharge would be applied to all customer bills equal to the percentage calculated by dividing the DSIC revenue requirement by the Company's projected revenues for the next six months. The surcharge will be applied on a bills rendered basis.

11) After the first 12 month period, the Company would need to include an earnings test.

If a company is over earning, then the surcharge would stop until such time as the company is in an under earning position.

12) Some states also perform an annual audit of the program to review the actual projects implemented by the company.

13) On each six month submittal, a reconciliation on the over(under) recovery of DSIC surcharge would be included.

14) There should not be any "Gap Period" as a result of base rate case. The Gap Period represents the time period between when qualified additions are reflected in base rates and the Company's subsequent DSIC filing. For example, if increased rates become effective in April and that increase only includes qualified DSIC additions through the prior December, the next DSIC surcharge after the rate increase would include qualified additions from January through September (i.e., six months after the April effective date).