

DIRECT TESTIMONY

OF

KAREN A. GOLDBERGER

ACCOUNTING DEPARTMENT

FINANCIAL ANALYSIS DIVISION

ILLINOIS COMMERCE COMMISSION

ILLINOIS COMMERCE COMMISSION
ON ITS OWN MOTION

-VS-

ILLINOIS-AMERICAN WATER COMPANY
DOCKET No. 00-0340

AUGUST 2000

1 **Witness Identification**

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

3 A. My name is Karen A. Goldberger. My business address is 527 East Capitol
4 Avenue, Springfield, Illinois 62701.

5 Q. **By whom are you employed and in what capacity?**

6 A. I am a Senior Accountant in the Accounting Department of the Financial Analysis
7 Division of the Illinois Commerce Commission.

8 Q. **Please describe your background and professional affiliations.**

9 A. I am a licensed Certified Public Accountant with a Bachelor of Arts Degree in
10 Accountancy from Sangamon State University and a Master of Arts Degree in
11 Accountancy from the University of Illinois at Springfield and a member of the
12 American Institute of Certified Public Accountants. I joined the Staff of the Illinois
13 Commerce Commission (Staff) in August 1993.

14 Q. **What is the function of the Accounting Department of the Illinois Commerce
15 Commission?**

16 A. The Department's function is to monitor the financial condition of public utilities as
17 part of the Commission's responsibilities under Article IV of the Public Utilities Act

18 (Act) (220 ILCS 5/4-101 et seq.) and to provide accounting expertise on matters
19 before the Commission.

20 Q. **Have you previously testified before this Commission?**

21 A. Yes, I have.

22 Q. **What are your responsibilities in this case?**

23 A. I have been assigned to this case by the Director of the Accounting Department of
24 the Commission. I am to review Illinois-American Water Company's (IAWC or
25 Company) filing, analyze the underlying data and propose adjustments when
26 appropriate.

27 **Purpose of Testimony**

28 Q. **What is the purpose of your testimony in this proceeding?**

29 A. The purpose of my testimony is as follows:

- 30 1. to present the Staff adjusted operating statement and rate base for each
31 district of the Company, and
32 2. to propose adjustments to the Company's operating statement and rate
33 base concerning cash working capital, rate case expense, charitable
34 contribution expense, deferred income taxes, Alton Plant property taxes,
35 reengineering costs, and solid waste disposal expense.

36

37 Q. **List the Districts for which the Company is requesting a change in base**
38 **rates and show your designation for each District.**

39 A. The Company is requesting a change in base rates for the following Districts:

- 40 • Southern and Peoria (S&P)
- 41 • Champaign (CP)
- 42 • Sterling (STG)
- 43 • Streator (STR)
- 44 • Pontiac (PT)

45 Q. **Are you sponsoring any schedules as part of ICC Staff Ex. 1.0?**

46 A. Yes. I prepared the following schedules for the Company, which show data as of, or
47 for the test year ending December 31, 2001:

48 Schedule 1.1-S&P - Statement of Operating Income with Adjustments

49 Schedule 1.2-S&P - Adjustments to Operating Income

50 Schedule 1.3-S&P -Rate Base

51 Schedule 1.4-S&P -Adjustments to Rate Base

52 Schedule 1.5-S&P -Revenue Effects of Adjustments

53 Schedule 1.6-S&P - Interest Synchronization Adjustment

54 Schedule 1.7-S&P - Gross Revenue Conversion Factor

55 Schedule 1.8-S&P - Adjustment to Cash Working Capital

56 Schedule 1.9-S&P - Adjustment to Rate Case Expense

57 Schedule 1.10-S&P -Adjustment to Charitable Contribution Expense

- 58 Schedule 1.11-S&P - Adjustment to Accumulated Deferred Income Taxes
- 59 Schedule 1.12-S&P - Adjustment to Alton Plant Property Tax Expense
- 60 Schedule 1.13-S&P - Adjustment for Reengineering Costs
- 61 Schedule 1.14-S&P - Adjustment for Solid Waste Disposal Expense
- 62 Schedule 1.15 S&P - Adjustment to Deferred Income Taxes for Change in
63 Depreciation Expense.
- 64
- 65 Schedule 1.1-CP - Statement of Operating Income with Adjustments
- 66 Schedule 1.2-CP - Adjustments to Operating Income
- 67 Schedule 1.3- CP -Rate Base
- 68 Schedule 1.4-CP -Adjustments to Rate Base
- 69 Schedule 1.5-CP -Revenue Effects of Adjustments
- 70 Schedule 1.6-CP - Interest Synchronization Adjustment
- 71 Schedule 1.7-CP - Gross Revenue Conversion Factor
- 72 Schedule 1.8-CP - Adjustment to Cash Working Capital
- 73 Schedule 1.9-CP - Adjustment to Rate Case Expense
- 74 Schedule 1.10-CP -Adjustment to Charitable Contribution Expense
- 75 Schedule 1.11-CP - Adjustment to Accumulated Deferred Income Taxes
- 76 Schedule 1.12-CP Adjustment to Champaign Office Lease Expense
- 77 Schedule 1.1-STG - Statement of Operating Income with Adjustments
- 78 Schedule 1.2-STG - Adjustments to Operating Income
- 79 Schedule 1.3- STG -Rate Base
- 80 Schedule 1.4-STG -Adjustments to Rate Base

- 81 Schedule 1.5-STG -Revenue Effects of Adjustments
- 82 Schedule 1.6-STG - Interest Synchronization Adjustment
- 83 Schedule 1.7-STG - Gross Revenue Conversion Factor
- 84 Schedule 1.8-STG - Adjustment to Cash Working Capital
- 85 Schedule 1.9-STG - Adjustment to Rate Case Expense
- 86 Schedule 1.10-STG -Adjustment to Charitable Contribution Expense
- 87 Schedule 1.11-STG - Adjustment to Accumulated Deferred Income Taxes
- 88 Schedule 1.12-STG - Adjustment to Champaign Office Lease Expense
- 89 Schedule 1.1-STR - Statement of Operating Income with Adjustments
- 90 Schedule 1.2-STR - Adjustments to Operating Income
- 91 Schedule 1.3- STR -Rate Base
- 92 Schedule 1.4-STR -Adjustments to Rate Base
- 93 Schedule 1.5-STR -Revenue Effects of Adjustments
- 94 Schedule 1.6-STR - Interest Synchronization Adjustment
- 95 Schedule 1.7-STR - Gross Revenue Conversion Factor
- 96 Schedule 1.8-STR - Adjustment to Cash Working Capital
- 97 Schedule 1.9-STR - Adjustment to Rate Case Expense
- 98 Schedule 1.10-STR -Adjustment to Charitable Contribution Expense
- 99 Schedule 1.11-STR - Adjustment to Accumulated Deferred Income Taxes
- 100 Schedule 1.12-STR - Adjustment to Champaign Office Lease Expense
- 101 Schedule 1.1-PT - Statement of Operating Income with Adjustments
- 102 Schedule 1.2-PT - Adjustments to Operating Income

- 103 Schedule 1.3- PT -Rate Base
- 104 Schedule 1.4-PT -Adjustments to Rate Base
- 105 Schedule 1.5-PT -Revenue Effects of Adjustments
- 106 Schedule 1.6-PT - Interest Synchronization Adjustment
- 107 Schedule 1.7-PT - Gross Revenue Conversion Factor
- 108 Schedule 1.8-PT - Adjustment to Cash Working Capital
- 109 Schedule 1.9-PT - Adjustment to Rate Case Expense
- 110 Schedule 1.10-PT -Adjustment to Charitable Contribution Expense
- 111 Schedule 1.11-PT - Adjustment to Accumulated Deferred Income Taxes
- 112 Schedule 1.12-PT Adjustment to Champaign Office Lease Expense

113 **Revenue Requirement Schedules**

114 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.1, for each District, Statement**
115 **of Operating Income with Adjustments.**

116 A. Schedule 1.1, for each District, derives the required revenue at the Staff proposed
117 rate of return. Column (B) presents the Company's pro forma operating statement
118 at present rates for the test year as reflected on Company Exhibit 12.0, Schedule C-
119 2. Column (C) reflects the total of all Staff adjustments shown on ICC Staff Ex. 1.0,
120 Schedule 1.2. Column (D) reflects the pro forma operating statement at present
121 rates per Staff. Column (E) presents the Company proposed increase to revenue.
122 Column (F) is Staff's O&M Statement inclusive of the Company's proposed revenue
123 increase. Column (G) adjusts revenue to reflect Staff's Gross Revenue Conversion

124 Factor. Column (H) is the necessary reduction from the Company's proposed
125 revenues, adjustment for Staff's Gross Revenue Conversion Factor, to arrive at
126 Staff's computed revenue requirement as reflected in Column (I). Column (J) is the
127 difference between current revenues and required revenues as determined by Staff.
128 Column (K) is Staff's calculated percentage change in revenues. Net Operating
129 Income in Column (I), line 24, is the product of Rate Base, line 25, and Rate of
130 Return, line 26.

131 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.2, for each District,**
132 **Adjustments to Operating Income.**

133 A. Schedule 1.2, for each District, identifies Staff's adjustment to Operating Income.
134 The source of each adjustment is shown in the heading of each column. Column (K)
135 is carried forward to ICC Ex. 1.0, Schedule 1.1, Column (C).

136 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.3, for each District, Rate Base.**

137 A. Schedule 1.3, for each District, compiles Staff's rate base. Column (B) reflects the
138 Company's proposed rate base. Column (C) summarizes Staff's adjustment to rate
139 base. Column (D) is the net of Columns (B) and (C), and reflects Staff's computed
140 rate base.

141 Q. **Please describe ICC Staff Ex. 1.0 , Schedule 1.4, for each District,**
142 **Adjustments to Rate Base.**

143 A. Schedule 1.4, for each District, identifies Staff's adjustments to rate base. The
144 source of each adjustment is shown in the heading of each column. Column (K) is
145 carried forward to ICC Ex. 1.0, Schedule 1.3, Column (C).

146 Q. **What is the purpose of ICC Staff Ex. 1.0, Schedule 1.5, for each District?**

147 A. Schedule 1.5, for each District, is a three page document which identifies the
148 approximate effect of each Staff adjustment on the Company's revenue
149 requirement. It is an analysis, not the development, of Staff's position. As such, it is
150 intended to assist in identifying the relative monetary significance of each
151 adjustment.

152 **Interest Synchronization**

153 Q. **Please explain ICC Staff Ex. 1.0, Schedule 1.6, for each District, Interest**
154 **Synchronization Adjustment.**

155 A. Schedule 1.6, for each District, computes the interest component of revenue
156 requirement. The interest expense (component) is computed by multiplying the rate
157 base by weighted cost of debt. The calculated interest expense is then compared
158 against the interest expense used by the Company in its computation of test year

159 income tax expense. The tax effect of the difference in interest expense is the
160 adjustment for interest synchronization. The effect of this adjustment is to ensure
161 that the revenue requirement reflects the tax savings generated by the interest
162 component of revenue requirement.

163 **Gross Revenue Conversion Factor**

164 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.7, for each District, Gross**
165 **Revenue Conversion Factor (GRCF).**

166 A. Schedule 1.7, for each District, shows my proposed GRCF. The GRCF is
167 multiplied by the income deficiency to determine the total amount of revenue
168 required for the income deficiency and the associated increase in income tax
169 expense and uncollectible expense. Company Exhibit 12.0, Schedule No. C-14
170 shows the Company's GRCF calculation. The Company included the proposed
171 increase in invested capital tax expense in the calculation of its GRCF. However,
172 this is inconsistent with Staff's capital structure as shown on ICC Staff Ex. 3.0,
173 Schedule 3.1, sponsored by Staff Witness Michael McNally. Therefore, I have
174 adjusted the Company's GRCF calculation to reconcile with Staff's proposed cost
175 of capital structure. My proposed GRCF is used in the calculation of the Staff'
176 proposed revenue requirement.

177 **Cash Working Capital**

178 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.8, for each District, Adjustment**
179 **to Cash Working Capital.**

180 A. The Company based its cash working capital computation on the operating
181 expense amount presented in its filing. Subsequently Staff has made adjustments
182 to the Company's operating expense amount and cash working capital has
183 changed accordingly as shown on Schedule 1.8, for each District, to reflect Staff's
184 proposed adjustments to expenses. This adjustment will be updated to reflect the
185 operating expenses approved by the Commission.

186 **Rate Case Expense**

187 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.9, for each District, Adjustment**
188 **to Rate Case Expense.**

189 A. Schedule 1.9, for each District, shows my adjustment to reduce rate case expense.
190 The Company included the expense for an outside consultant's Cost of Service
191 Study (COSS) in its rate case expense. However, the Company did not include a
192 Cost of Service Study in its filing. Therefore I am proposing an adjustment to
193 remove the expense for an outside consultant's COSS from the rate case expense.

194 **Charitable Contribution Expense**

195 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.10, for each District,**
196 **Adjustment to Charitable Contribution Expense.**

197 A. Schedule 1.10, for each District, shows my adjustment to reduce charitable
198 contribution expense to a more normalized amount based on the Company's prior
199 years level of expense. Company response to Staff Data Request IAWC-056
200 shows the charitable contribution expense for the years 1997 through 2001. The
201 Company's charitable contribution expense fluctuated anywhere from 22% to 38%
202 each year from 1997 to 2000. Because there were large fluctuations over that four
203 year period prior to the test year, I averaged the four year expense to determine a
204 normalized level of charitable contribution expense.

205 **Accumulated Deferred Income Taxes**

206 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.11, for each District,**
207 **Adjustment to Accumulated Deferred Income Taxes.**

208 A. Schedule 1.11, for each District, shows my adjustment to reduce the amount of
209 accumulated deferred income taxes as a component of the rate base calculation.
210 When a utility files a rate case with a future test year and the rates go into effect
211 before the end of the test year, the amount of test year deferred income tax expense
212 that is added to the accumulated deferred income taxes is to be prorated over the

213 period between the time the rates go into effect and the end of the test year
214 Treasury Regulation Section 1.167(l)-1(h)(6) (Income Tax Regulations). Without this
215 proration, the rate base would be reduced at an accelerated rate because
216 accumulated deferred income taxes are a reduction of rate base. The Company
217 prorated the deferred income tax expense appropriately; however, the Company
218 had negative deferred income taxes and the proration of the negative deferred
219 taxes had the opposite effect of the intent of the United States Treasury Regulation
220 and caused an accelerated decrease in rate base. Therefore, I am proposing an
221 adjustment to reverse the Company's proration adjustment. The effect of reversing
222 the Company's proration adjustment is to reduce the amount of accumulated
223 deferred income taxes as a reduction from rate base.

224 **Alton Plant Property Taxes**

225 **Q. Please describe ICC Staff Ex. 1.0, Schedule 1.12 -S & P, Adjustment to Alton**
226 **Plant Property Tax Expense.**

227 A. Schedule 1.12- S&P, reduces the amount of property taxes for the new Alton Plant
228 and is an adjustment to the Southern and Peoria District. When the Company
229 determined the amount of property taxes for the new Alton Plant, it used an incorrect
230 property tax rate for the determination of the property taxes on the taxable portion of
231 the new plant. The correct rate was provided to Staff by the Company during Staff's
232 field audit. Therefore, I am proposing an adjustment to reduce the amount of

233 property taxes for the new Alton Plant to reflect the use of the correct property tax
234 rate.

235 **Reengineering Costs**

236 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.13 -S & P, Adjustment for**
237 **Reengineering Costs.**

238 A. Schedule 1.13-S&P, removes the one year amortization of reengineering expense
239 from operating expense and the unamortized portion from rate base. This
240 adjustment is to the Southern and Peoria District. Company Witness Scott Cazadd
241 states on page 8 his direct testimony:

242 Reengineering costs are costs the company incurred in conjunction with
243 severing 22 associates in a restructuring at Illinois-American in 1999. The
244 costs include a severance package, limited continuation of insurance
245 coverage, and costs for an outside employment outside counseling firms'
246 work.

247 The restructuring in 1999 included the merger of IAWC and Northern-Illinois Water
248 Company (Docket No. 99-0418, Order Entered March 29,2000 and United Water
249 (Docket No 99-0457, Order Entered May 10, 2000). In the Order in Docket No 99-
250 0418, the Commission states on pages 15 and 16:

251 In determining the treatment of merger costs in Docket Nos. 98-0555 and
252 98-0866, the Commission distinguished transactional costs (those costs and
253 expenses incurred in connection with the merger transaction) from costs
254 directly associated with the utility's provision of service. The Commission
255 concluded that transactional costs should not be recovered from ratepayers,
256 while costs directly associated with the utility's provision of service should be
257 recovered. The Commission indicated customers should not pay for the
258 business end of the deal. ...The Commission concludes that employee
259 separation and relocation costsare transactional costs that should not be

260 recovered from ratepayers of Illinois-American. In Docket No. 98-0555, the
261 Commission concluded that these type of costs are transactional costs
262 The reengineering costs, which are employee separation costs as described by the
263 Company, are transactional costs as defined by the Commission and are not
264 recoverable. In the Order in the Order in Docket No. 99-0418, the Commission
265 ruled that employee separation and relocation costs associated with that merger
266 were not allowed to be recovered in rates. Therefore, I am proposing an adjustment
267 to remove the reengineering expense from operating expenses and the
268 unamortized portion from rate base.

269 **Solid Waste Disposal Expense**

270 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.14 -S & P, Adjustment for Solid**
271 **Waste Disposal Expense.**

272 A. Schedule 1.14 - S&P shows my adjustment to include the solid waste disposal
273 expense for the new Alton Water Treatment Facility (Alton Plant). This adjustment is
274 to the Southern and Peoria District. In his Direct Testimony on pages 8-10,
275 Company Witness Mark Johnson discusses the cost associated with the disposal
276 of the residual solids from the new Alton Plant. The cost of the disposal would be
277 \$4,150,000 amortized over a 10 year period for an annual expense of \$415,000.
278 The Company provided adequate supporting documentation for this cost; however,
279 the Company did not include the cost in the determination of its proposed rates for
280 the Southern and Peoria District. Therefore, I am proposing an adjustment to

281 include the \$415,000 expense for the solid waste disposal in operating expenses
282 for the Southern and Peoria District.

283 **Deferred Income Taxes Related to Change in Depreciation Expense**

284 Q **Please describe ICC Staff Ex. 1.0, Schedule 1.15 -S & P, Adjustment to**
285 **Deferred Income Taxes for Change in Depreciation Expense.**

286 A. Schedule 1.15 - S&P shows my adjustments to deferred income tax expense and
287 accumulated deferred income taxes due to Staff's proposed adjustment to
288 depreciation expense as shown on ICC Staff Ex. 2.0, Schedule 2.2 - S&P.
289 Because Staff is proposing a reduction in the depreciation expense, I am proposing
290 the corresponding adjustments to the deferred income tax expense and
291 accumulated deferred income taxes for the change in depreciation expense as
292 shown. The change to the income tax expense is reflected on ICC Staff Ex. 1.0,
293 Schedule 1.2, Column J, Lines 19 and 20.

294 **Champaign Office Building Lease Expense**

295 Q. **Please describe ICC Staff Ex. 1.0, Schedule 1.12 - CP, Schedule 1.12 - STG,**
296 **Schedule 1.12 - STR, and Schedule 1.12 - PT, Adjustment to Champaign**
297 **Office Lease Expense.**

298 A. Schedule 1.12 shows my adjustment to the Champaign, Sterling, Streator, and
299 Pontiac Districts to reduce the Champaign office lease expense allocated to those
300 Districts. After the merger of Northern Illinois Water Company and Illinois-American
301 Water Company (Docket No. 99-0418, Order Entered March 29, 2000), personnel
302 and certain functions/departments were transferred from the Champaign office to
303 the IAWC Belleville, Illinois office. Company response to Staff Data Request KG-30
304 shows that 16% of the office building, excluding common areas, is no longer being
305 used for utility purposes due to the reduction in personnel and functions performed
306 at the Champaign office building. One of the standards used by the Commission in
307 determining the value to the ratepayers of a cost incurred by a utility is used and
308 useful, Section 9-211 of the Public Utilities Act. Because a percentage of the
309 building is no longer being used to provide services to the ratepayers, I am
310 proposing an adjustment to reduce the lease expense in proportion to the
311 percentage of the building that is no longer used for utility purposes. The lease
312 expense is allocated to the Champaign, Streator, Sterling and Pontiac Districts;
313 therefore, I am proposing an adjustment to each of those Districts based upon their
314 allocated portion of the lease expense.

315 **Conclusion**

316 Q. **Do you have any additional comments regarding the Company's filing?**

317 A. Yes. Section 9-224 of the Public Utilities Act states:

318 The Commission shall not consider as an expense of any public utility
319 company, for the purpose of determining rate charge, any amount expended
320 for political activity or lobbying as defined the "Lobby Registration Act."

321 The Company included lobbying expense in operating expenses for each District.

322 Although the lobbying expenses are not recoverable, the amount of Company
323 lobbying expenses included in this proceeding is so immaterial that if an adjustment
324 were made, there would be no effect on the revenue requirement. So, in effect, the
325 Company will not be recovering any lobbying expense in rates. Therefore, I am not
326 making an adjustment to remove those costs. However, the record should reflect
327 that the Company shall not include lobbying expenses in future proceedings.

328 Q. Are there any other expenses where the difference between your calculation of the
329 expense for the test year and the Company's proposed expense amount was
330 immaterial?

331 A. Yes. The Company used their capital structure to calculate the invested capital tax
332 expense. Using Staff's proposed capital structure as shown on Staff Ex. 3.0,
333 Schedule 3.1, I recalculated the invested capital tax. The difference was immaterial;
334 therefore, I am not proposing an adjustment. However, the record should reflect that
335 Staff's proposed invested capital tax expense would be based on Staff's capital
336 structure. Therefore, if the Company changed its capital structure in its rebuttal
337 testimony and the difference between Staff's invested capital tax expense based on
338 Staff's capital structure and the Company's invested capital tax expense would
339 become a material amount, I would propose an adjustment to reflect Staff's capital
340 tax expense based upon Staff's capital structure.

341 Q. **Does this conclude your prepared direct testimony?**

342 A. Yes.