

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Aqua Illinois, Inc.)	
)	
Proposed General Increase for Water and)	Docket No. 05-0071
Sewer Rates for the Woodhaven Division)	
)	
Proposed General Increase for Water Rates)	Docket No. 05-0072
For the Oak Run Division)	

Rebuttal Testimony of

JACK SCHREYER

Manager of Rates
of Aqua America, Inc.

June 15, 2005

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1 **I. WITNESS INTRODUCTION**

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

3 A. My name is Jack Schreyer and my business address is 762 West Lancaster Avenue,
4 Bryn Mawr, Pennsylvania 19010-3489.

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

6 A. Yes.

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

8 A. I will address all of the adjustments to the Company's case which have been proposed by
9 Staff.

10 **Q. How have you organized the Company's response?**

11 A. Initially, I address the Company's response to Staff witness Ms. Janis Freetly's position
12 on rate of return issues. Second, I set forth Aqua's response to the rate design proposed
13 by Staff witness Ms. Cheri L. Harden. Third, I address the adjustments proposed by Staff
14 witnesses Ms. Bonita A. Pearce and Ms. Burma C. Jones.

15 **Q. Please explain in more detail the Staff adjustments proposed by Ms. Pearce and
16 Ms. Jones that you will address.**

17 A. In my rebuttal testimony, I will address the following adjustments that are proposed by
18 Ms. Pearce and Ms. Jones:

Witness	Adjustment
Bonita A. Pearce	Interest Synchronization Gross Revenue Conversion Factor Cash Working Capital Bad Debt – Expense – Oak Run Division Rate Case Expense Management Expense
Burma C. Jones	Deferred Charges for Tank Painting Plant In Service – Reverse Osmosis Project Accumulated Deferred Income Taxes Depreciation Rates Retired Utility Plant

19 In addition, I will address certain issues not noted in the testimony of Staff as appropriate.

20 **Q. Have you prepared a schedule that sets forth Aqua’s rebuttal position?**

21 A. Yes. Because I am the primary accounting witness, I have incorporated the Company’s
22 rebuttal position into my Rebuttal Schedules. Schedule 6.1 shows the Company’s
23 original position (Col. a), Staff’s adjustments (Col. b), Staff adjustments accepted by the
24 Company (Col. c), the Company’s rebuttal adjustments (Col. d) and the Company’s
25 rebuttal position (Col. e).

26 **II. RESPONSE ON RATE OF RETURN**

27 **A. CAPITAL STRUCTURE**

28 **Q. How does Aqua respond to Staff’s proposed capital structure?**

29 A. Ms. Freetly proposes the adoption of Aqua’s updated forecasted average 2005 capital
30 structure comprised of 47.87% long-term debt, 0.32% preferred stock and 51.81%
31 common equity as set forth on Staff Schedule 3.01. Aqua will also accept Staff’s
32 proposed capital structure for purposes of this proceeding.

33 **B. COST OF COMMON EQUITY**

34 **Q. What is Aqua's response to Staff's proposal to adopt a common equity cost rate of**
35 **10.40%?**

36 A. Aqua is willing to accept Staff's proposed 10.40% return on equity for purposes of this
37 case. Aqua reserves its right to contest cost of common equity, including Staff's method
38 of analysis, in future rate cases.

39 **Q. By this testimony, are you intending to present yourself as an expert on cost of**
40 **common equity issues?**

41 A. No. Aqua has presented the expert testimony of Ms. Pauline Ahern on these issues in this
42 case. I am simply stating Aqua's acceptance of Staff's proposed cost of common equity
43 of 10.40% for purposes of this case.

44 **C. COST OF LONG-TERM DEBT**

45 **Q. Please describe Staff's adjustments to Aqua's cost of long-term debt.**

46 A. Staff proposes two adjustments to Aqua's cost of long-term debt: (i) applying straight
47 line amortization to unamortized balances for debt discount, premium and expenses over
48 the remaining life of each issue, and (ii) excluding Aqua's unamortized debt expense for
49 the Series W bonds and call premium associated with refunding the Series P bonds.

50 **Q. Does Aqua agree to use straight line amortization for its unamortized balances for**
51 **debt discount, premium and expenses?**

52 A. Yes.

53 **Q. Does Aqua agree with Staff's adjustment to exclude expenses related to the Series W**
54 **and P bonds?**

55 A. No, the Company does not agree with this adjustment and is not willing to accept it for
56 purposes of this case.

57 **Q. Please explain why Aqua is not willing to accept Staff's adjustment to exclude its**
58 **Series W and P bond expenses from its cost of long-term debt.**

59 A. These are legitimate expenses that are fully supported and verifiable.

60 **Q. If these are legitimate expenses, why has Staff objected to their recognition?**

61 A. Staff has not contested the legitimacy of these expenses. Rather, Staff's only objection
62 was that Aqua had not filed a report described at 83 Ill. Adm. Code 240 as required in
63 Docket No. 04-0626. Staff stated it was unable to verify the amount and timing of the
64 costs for this reason. (Staff Ex. 3.0, p. 13).

65 **Q. How do you respond?**

66 A. Aqua has provided Staff with full support to verify these costs in response to JF 2.03. A
67 copy of Aqua's original response to JF 2.03 is hereby provided as Attachment A. In
68 addition, Aqua made the filing pursuant to 83 Ill. Adm. Code Part 240 on June 9, 2005,
69 and provided a copy of the filing to Staff as a supplement to JF 2.03. Aqua's
70 supplemental response to JF 2.03 is also provided as part of Attachment A hereto.
71 Accordingly, Aqua has filed the report described in 83 Ill. Adm. Code 240, and has
72 otherwise made all of the relevant information available to Staff to verify the amount and
73 timing of its Series W and P bond expenses. The Illinois Commerce Commission ("ICC"
74 or "Commission") should recognize these legitimate expenses.

75 **III. RESPONSE ON RATE DESIGN**

76 **Q. What is Aqua's response to Staff's rate design proposals?**

77 A. With one exception, Aqua is willing to accept Staff's rate design proposals as set forth in
78 the direct testimony of Ms. Harden. Aqua reserves its right to contest all rate design
79 issues in future rate cases.

80 **Q. What is the exception?**

81 A. The Company disagrees with Staff's proposal to increase the availability charge at a
82 lower percentage than the customer charge for the Oak Run Division. Aqua proposed an
83 equal percentage increase for both of these charges. Aqua witness Mr. David R. Monie
84 stated the reasons why the availability charge should be increased by an equal percentage
85 as the customer charge in his direct testimony. (Aqua Ex. 4.0, pp. 4-6).

86 **Q. By this testimony, are you intending to present yourself as an expert on rate design
87 issues?**

88 A. No. Aqua has presented the expert testimony of Mr. Monie on rate design issues for the
89 Oak Run Division. I am simply stating the Company's acceptance of Staff's rate design
90 proposal, with the noted exception, for purposes of this case.

91 **IV. REBUTTAL TO MS. PEARCE'S TESTIMONY**

92 **A. INTEREST SYNCHRONIZATION**

93 **Q. Mr. Schreyer, with regard to Ms. Pearce's proposed interest expense adjustment as
94 shown on Staff Exhibit 1.0, Schedule 1.5, do you agree with the calculation?**

95 A. While I accept the mechanics of the calculation, the actual interest synchronization will
96 depend on final rate base and weighted cost of debt the Commission adopts in this case. I

97 believe the 3.38% weighted cost of debt utilized by Ms. Freetly in her calculation
98 understates Aqua's true cost of debt. As discussed above, Ms. Freetly's cost of debt does
99 not recognize legitimate expenses related to Aqua's Series W and P bonds. All of the
100 relevant information to verify these expenses has been provided to Staff in response to
101 JF 2.03 and as Attachments A hereto. The cost of debt utilized to make the interest
102 expense calculation should be modified to include these expenses.

103 **B. CASH WORKING CAPITAL**

104 **Q. Do you agree with Ms. Pearce's cash working capital adjustment?**

105 A. Ms. Pearce's cash working capital adjustment is the result of Staff's adjustments to the
106 Company's operations and maintenance ("O&M") expenses. In particular, cash working
107 capital is the result of multiplying 12.5% times O&M expense. Because I do not agree
108 with some of Staff's adjustments to the Company's O&M expense, I do not agree with
109 Staff's cash working capital adjustment. The Commission should calculate actual cash
110 working capital based on the final O&M expense it adopts in this proceeding.

111 **C. BAD DEBT EXPENSE**

112 **Q. Please address Ms. Pearce's adjustment to Oak Run bad debt expense of \$10,180**
113 **shown on Staff Exhibit 1.0, Schedule 1.09 (OR), Page 1 of 3.**

114 A. I do not agree with the adjustment. Currently, there are \$14,487 of receivables over
115 91 days for the Oak Run Division. This equates to \$4,829 annually allocated over
116 three years. The Company is amending its bad debt expense for Oak Run from \$10,180
117 to \$4,829 based on this information.

118 **Q. Do you wish to comment on Woodhaven bad debt expense?**

119 A. Yes. While Ms. Pearce made no adjustments, she reserved the right to do so upon further
120 review of the extraordinarily large amount of information requested by Staff and
121 provided by the Company during discovery. It is my request that Ms. Pearce consider my
122 supplemental response to BAP 5.04 (Woodhaven Water) in which I note that the updated
123 projection for bad debt expense is \$103,394 rather than the \$86,456 reflected on
124 Company Exhibit 4.0, Schedule WP-C-1, Column H, Line 18 (Water). Similarly, I
125 request that Ms. Pearce take note of my supplemental response to BAP 6.04 (Woodhaven
126 Sewer) in which I note that that the updated projection for bad debt expense is \$112,174
127 rather than the \$86,600 reflected on Company Exhibit 4.0, Schedule WP-C-1, Column H,
128 Line 18 (Sewer).

129 **Q. Please explain why the Company believes its original estimates of bad debt expense**
130 **for Woodhaven Water and Sewer to be insufficient.**

131 A. Currently, there are approximately 536 active accounts that are delinquent with no desire
132 to pay for both Woodhaven Water and Sewer. For Woodhaven Water, at the proposed
133 water rate of \$16.075 per month, the Company expects the annual bad debt expense to be
134 \$103,394 on a pro forma basis prior to the addition of late payment fees. For Woodhaven
135 Sewer, at the proposed sewer rate of \$17.44 per month, the Company expects the annual
136 bad debt expense to be \$112,174 on a pro forma basis prior to the addition of late
137 payment fees.

138 **Q. Why do you calculate bad debt expense based on the number of delinquent accounts**
139 **with no desire to pay instead of as a percentage of projected revenue?**

140 A. Bad debt expense is more directly tied to actual accounts that exhibit no desire to pay
141 than to revenues, in part because the identity of account holders remains fairly consistent.
142 The current existence of 536 delinquent accounts with no desire to pay is very likely
143 representative of the circumstances throughout the remainder of this 2005 test year.

144 **D. RATE CASE EXPENSE**

145 **Q. Please describe generally Staff's proposed adjustments to rate case expense.**

146 A. Staff witness Ms. Pearce proposes to disallow the following rate case expenses:

- 147 1. Aqua's entire cost for its rate of return expert witness
148 Ms. Ahern;
- 149 2. Amounts in excess of \$9,000 per division for London Witte
150 Group audit fees;
- 151 3. \$4,200 for London Witte representatives to prepare for,
152 travel to and participate in a meeting with Staff to review
153 work papers related to this case;
- 154 4. The entire amount for Aqua's rate department to prepare
155 the filings and handle the day-to-day aspects of the cases;
- 156 5. Any amount in excess of the most recent prior rate case
157 expenses for each of the three Divisions at issue in this
158 proceeding.

159 (Staff Ex. 1.0, pp. 11 to 26; Staff response to Aqua data request 1.10).

160 **Q. Please state your overall impression of Staff's adjustments to rate case expense.**

161 A. With the exception of the adjustment identified as number 2 above, I believe the
162 adjustments proposed by Staff are unfounded, unreasonable and inequitable. As
163 explained further herein, Staff ties projected rate case expense for this proceeding solely
164 to the rate case expenses Aqua incurred in its prior rate cases for each of the Divisions at
165 issue here. However, Staff fails to consider numerous reasons why the Company is

166 projecting more rate case expense in the instant proceedings than was incurred in the
167 prior cases for Oak Run, Woodhaven Water and Woodhaven Sewer. Staff also proposes
168 new and arbitrary rules that it asks the Commission to impose retroactively on Aqua
169 alone.

170 **1. STAFF'S TOTAL DISALLOWANCE OF AQUA'S RETURN ON**
171 **EQUITY EXPENSE**

172 **Q. What reasons does Staff advance for its proposal to totally disallow Ms. Ahern's**
173 **fees?**

174 A. Staff states two reasons for proposing zero recovery for this expense. First, Staff alleges
175 that Aqua could have avoided this expense if it had filed its rate cases for Oak Run and
176 the Woodhaven Divisions nineteen months or seven months earlier with either the
177 Kankakee or Vermilion Division filings. Second, Staff claims that Ms. Ahern's expense
178 is not justified because she allegedly did not have a good faith basis for presenting a
179 return on equity methodology that the Commission has not adopted previously even
180 though, in Ms. Ahern's expert opinion, the methodology is proper and is the one that the
181 Commission should utilize.

182 **Q. Taking Staff's asserted bases in turn, please explain why Aqua did not consolidate**
183 **the Oak Run filing either with Kankakee in May 2003 or Vermilion in May 2004.**

184 A. The Company considered filing its Oak Run Division along with its Vermilion Division
185 rate application in May 2004. However, as explained in response to Staff data request
186 BAP 1.04, "information relevant to support the rate filing for Oak Run at the time of the
187 Vermilion filing in May 2004 and Kankakee filing in May 2003 was not completely
188 available. Specifically, unresolved issues related to the possible construction of a

189 Reverse Osmosis Treatment Plant (such as whether or not to build the plant, timing of
190 such construction and rate impact etc.) existed at the time of the earlier filings.”

191 **Q. Staff witness Ms. Pearce claims that this could not be the reason that Aqua did not**
192 **file its Oak Run case earlier because Aqua allegedly did not have any further**
193 **information on the Reverse Osmosis Treatment Plant at the time Aqua made its**
194 **filing. (Staff Ex. 1.0, page 20). Please respond.**

195 A. At the time the Vermilion division rate application was being prepared (January - May
196 2004), it was not clear that a Reverse Osmosis Treatment Plant *would not* be built during
197 the test year. The Company prudently chose not to file a rate application until it knew
198 with reasonable certainty whether or not such a treatment plant would be reflected in the
199 rate base of its filing. To incorrectly include or exclude such a major investment would
200 significantly distort the Oak Run Division revenue requirement. By the third quarter of
201 2004 it was decided not to construct the Reverse Osmosis Treatment Plant in the near
202 term unless the Company was subjected to an IEPA Order to do so. Rather, any such
203 construction would only result from an affirmative customer survey response subsequent
204 to the conclusion of the instant proceeding. Accordingly, Aqua did have substantially
205 more information at the time of its Oak Run filing than in January – May of 2004.

206 **Q. Why did Aqua decide not to accelerate the Woodhaven cases for filing with**
207 **Kankakee or Vermilion?**

208 A. The Company also considered filing its Woodhaven Divisions along with its May 2004
209 Vermilion Division rate application. As explained in response to Staff data request
210 BAP 2.03, “information relevant to support the rate filing for the Woodhaven Water and
211 Sewer Divisions at the time of the Vermilion filing in May 2004 and Kankakee filing in

212 May 2003 was not completely available. Specifically, unresolved issues related to
213 possible Radium Removal capital expenditures and uncollectible accounts existed at the
214 time of the earlier filings.”

215 **Q. Has Staff alleged that this explanation is invalid?**

216 A. No. Staff has not directly disputed the fact that Aqua did not have sufficient information
217 available to accelerate the Woodhaven filings by either seven or nineteen months.

218 **Q. Has Staff indirectly disputed Aqua’s statement that it was not prepared to make
219 these filings?**

220 A. Yes. Staff has alleged that Aqua was ready to file these cases early in 2004, *i.e.*, when
221 the Vermilion filing was being prepared, simply because the decision to use outside
222 counsel was made at that time. (Staff Ex. 1.0, p. 24).

223 **Q. How do you respond?**

224 A. A decision to use outside counsel for an up-coming filing that is in the process of being
225 planned does not mean that the filing is ready to be filed. A decision to use outside
226 counsel occurs because the Company has to schedule its available resources to handle
227 filings over an upcoming planning horizon. The planning of resources does not mean
228 that a case is ready to be filed.

229 **Q. Is a lack of information as to significant capital expenditures a valid reason to hold a
230 rate case filing?**

231 A. Absolutely. Rate case proceedings necessitate the utilization of the best information
232 available. Were Aqua to have proceeded without sufficient information as to significant
233 capital expenditures, then the Commission’s findings would not be based on the most

234 reliable evidence. Consequently, it is probable that the end results of the cases would not
235 have matched future realities. Such a mismatch only prompts additional need for
236 information and clarification at an incremental expense to our customers.

237 **Q. Aside from Aqua’s lack of necessary information to support accelerated rate filings**
238 **for Oak Run and Woodhaven, are there any other problems inherent in Staff’s**
239 **suggestion that Aqua should have accelerated these filings?**

240 A. Yes. Staff presumes that customers would have benefited by accelerated filings for the
241 Oak Run and Woodhaven Divisions solely because Aqua’s rate of return expert’s fees
242 would have been allocated over a larger customer base. However, such a presumption is
243 not supportable. It is the result of an erroneous analysis that considers only a single
244 factor – the impact on the rate of return expert expense. Consideration of the total picture
245 reveals a far different “all-in” result than Staff presumes.

246 **Q. Please explain.**

247 A. Aqua’s allowed revenue increase would also have been accelerated by seven or nineteen
248 months if filings had been simultaneous with Vermilion or Kankakee, respectively. This
249 is a critical part of the equation that Staff does not consider at all. For purposes of
250 example, I will use Aqua’s requested annual revenue increases.

251 1. Seven month acceleration to file simultaneously with Vermilion:

252 ▪ **Oak Run:** The Oak Run cost of service reflects \$3,250 annually for rate
253 of return witness costs. This equates to a total savings of only \$1,896 had
254 Oak Run been accelerated seven months to the time of the Vermilion
255 application. However, for Oak Run, Aqua requested an annual revenue

256 increase of \$213,209. This amount less the \$3,250 annual rate of return
257 savings results in a net increase of \$209,959. Accelerating this net
258 increase seven months equates to \$122,476 more in revenues for our Oak
259 Run customers to pay.

260 ▪ **Woodhaven Water:** Similarly, with regard to Woodhaven Water, its cost
261 of service reflects \$3,875 annually for rate of return witness costs. This
262 equates to a total savings of only \$2,260 had Woodhaven Water been
263 accelerated to the time of the Vermilion application. Aqua requested an
264 annual revenue increase request of \$500,284. This amount less the \$3,875
265 annual rate of return savings results in a net increase of \$496,409 annually.
266 Accelerating this net increase seven months equates to \$289,572 more in
267 revenues for our Woodhaven Water customers to pay.

268 ▪ **Woodhaven Sewer:** Lastly, regarding Woodhaven Sewer, its cost of
269 service also reflects \$3,875 annually for rate of return witness costs that
270 would equate to a total savings of only \$2,260 had Woodhaven Sewer
271 been accelerated to the time of the Vermilion application. Aqua requested
272 an annual revenue increase of \$459,314. This amount less the \$3,875
273 annual rate of return savings results in a net increase of \$455,439 annually.
274 Accelerating this net amount seven months equates to \$265,673 more in
275 revenues for our Woodhaven Sewer customers to pay.

276 2. Nineteen month acceleration to file simultaneously with Kankakee:

277 ▪ **Oak Run:** As noted, the Oak Run cost of service reflects \$3,250 annually
278 for rate of return witness costs. This equates to a \$5,146 savings had Oak

279 Run been accelerated to the time of the Kankakee application. However,
280 the \$213,209 annual revenue request less the \$3,250 annual rate of return
281 savings results in an annual net increase of \$209,959 that, accelerated over
282 nineteen months, equates to \$332,435 more revenues for our Oak Run
283 customers to pay.

284 ▪ **Woodhaven Water:** With regard to Woodhaven Water, its cost of service
285 reflects \$3,875 annually for rate of return witness costs. This equates to a
286 \$6,135 savings had Woodhaven Water been accelerated to the time of the
287 Kankakee application. The \$500,284 annual revenue request less the
288 \$3,875 annual rate of return savings results in a net increase of \$496,409.
289 Accelerating this net increase over nineteen months equates to \$785,981
290 more revenues for our Woodhaven Water customers to pay.

291 ▪ **Woodhaven Sewer:** Lastly, regarding to Woodhaven Sewer, its cost of
292 service also reflects \$3,875 annually for rate of return witness costs. This
293 also equates to a \$6,135 savings had Woodhaven Sewer been accelerated
294 to the time of the Kankakee application. The \$459,314 annual revenue
295 request less the \$3,875 annual rate of return savings results in a net
296 increase of \$455,439. Accelerating this increase over nineteen months
297 equates to \$721,112 more revenues for our Woodhaven Sewer customers
298 to pay.

299 **Q. Does this seem reasonable to you?**

300 A. No. Oak Run and Woodhaven customers would not have saved money but rather would
301 have paid substantially more had Aqua accelerated these cases as Staff argues the
302 Company should have.

303 **Q. Do you believe the customers of the Oak Run and Woodhaven divisions would have**
304 **considered this a wise alternative to reduce their portion of rate of return costs?**

305 A. No, I do not believe that any reasonable person would consider it a good alternative.

306 **Q. Do you believe the Commission should accept any acceleration of rate increases in**
307 **order to save on rate of return expense?**

308 A. No, particularly when one considers the true impact on the customers as I have just
309 described.

310 **Q. What do you conclude regarding Ms Pearce's suggestion that the Oak Run and**
311 **Woodhaven filings could simply have been accelerated to avoid rate of return**
312 **witness costs?**

313 A. I have already explained that accelerating the filings were not options for reasons stated
314 previously. However, had the filings been accelerated seven months, the rate of return
315 cost savings would have resulted in \$677,721 more in revenues paid by the customers of
316 Oak Run and Woodhaven, assuming the requested rate increase was allowed in full. Had
317 the filings been accelerated nineteen months, the rate of return cost savings would have
318 resulted in \$1,839,528 more in revenues paid by the customers of Oak Run and
319 Woodhaven. This would be penny wise and pound foolish from our customers'
320 perspective.

321 **Q. Would Staff’s suggestion of accelerating the Oak Run and Woodhaven filing either**
322 **seven or nineteen months have any other adverse affect on customers?**

323 A. Yes, I believe it would. As discussed below, Staff has selected the intervals between the
324 previous and current rate case filing for each Division as Staff’s proposals for rate case
325 expense amortization periods. Any acceleration of these pending filings would reduce
326 the amortization period proposed by Staff by an equal amount, thereby further increasing
327 the cost to our customers.

328 **Q. In your opinion, would the disadvantages of accelerating the Oak Run and**
329 **Woodhaven cases for filing simultaneously with either of the previous Kankakee or**
330 **Vermilion filings outweigh the advantages?**

331 A. Yes, by a significant amount.

332 **Q. Turning now to Staff’s second basis for disallowing Aqua’s rate of return expense,**
333 ***i.e.*, that allegedly there is no good faith basis for presenting a return on equity**
334 **methodology that the Commission has not adopted previously. Please comment.**

335 A. I completely disagree with Staff’s assertion that there is no good faith basis for
336 Ms. Ahern’s return on equity analysis. Ms. Ahern is without dispute an expert in her
337 field. An expert’s opinion does not change simply because it is not adopted by a
338 regulatory agency or any other authority. Ms. Ahern presented her distinguished
339 qualifications in her direct testimony. (*See* Aqua Ex. 3.0 at pp. 1-2, App. A). The
340 Commission may not have adopted Ms. Ahern’s opinion previously; but, the materials
341 she relies upon and analysis she conducts as an expert still constitute a good faith basis
342 for her opinion.

343 **Q. Could Aqua have foregone submitting evidence to support its position on cost of**
344 **equity?**

345 A. Speaking as a lay person, I do not believe that Aqua can forego presenting evidence on
346 any issue with respect to which it would like the Commission to adopt its position.

347 **Q. Does past experience support Aqua's position that it needs to present evidence on**
348 **return on equity?**

349 A. Yes. In Docket No. 03-0403 addressing Aqua's Kankakee Division, Staff proposed a
350 return on equity of 9.86%. However, the Commission disagreed with Staff and, based on
351 Ms. Ahern's testimony, added thirty basis points ("bps") to Staff's proposal to recognize
352 a return of 10.16% per its Order dated April 13, 2004. Aqua filed its Vermilion rate case
353 just six weeks after the Commission's April 2004 Order. Under Staff's argument, there
354 would have been no basis for Ms. Ahern's testimony in the Vermilion proceeding.
355 However, the Commission again increased Staff's return on equity proposal by thirty bps
356 based solely on Ms. Ahern's testimony. If Aqua did not present evidence on return on
357 equity, then there would never be grounds for the Commission to question or make an
358 adjustment to Staff's proposals.

359 **Q. What recourse would the Company have had in the event it had not presented rate**
360 **of return evidence in Docket No. 04-0442?**

361 A. It is my belief the Commission would have had no basis to disagree with Staff on the
362 proper level of return on equity had the Company provided no testimony evidencing
363 Staff's flawed conclusion. Again, the Commission adjusted Staff's proposal by thirty
364 basis points based solely on Ms. Ahern's testimony.

365 **Q. Similarly, what recourse would the Company have had in the event the Company**
366 **had not presented rate of return testimony in this proceeding?**

367 A. Again, I believe the Commission would have had little basis to disagree with Staff a third
368 time on the proper level of return on equity. As it turns out, Staff has proposed a rate of
369 return analysis in this case that the Company is willing to accept. However, Aqua
370 certainly could not see into the future to foretell that result. Aqua had to support its
371 requested revenue requirement with evidence on its position as to the appropriate rate of
372 return for the Commission to utilize.

373 **Q. Has Staff even recognized that Aqua has a burden of proof that it must meet?**

374 A. Yes. Ms. Pearce notes that “[a] utility has the burden of proof to justify each element of
375 cost it seeks to recover through rates.” (Staff Ex. 1.0, p. 13, ln. 271-72). Return on
376 equity is without dispute an element of the cost Aqua seeks to recover through rates.

377 **Q. Could Aqua support a return on equity request based on an analysis presented in an**
378 **earlier case?**

379 A. No. Capital costs can change over time. This statement is supported by the fact that
380 Staff witness Ms. Freetly performed a new analysis in this case even though Staff had
381 submitted analyses in both the Vermilion and Kankakee cases. Indeed, Staff stated in
382 response to Company data request 1.04 that “Ms. Freetly performed a new cost of equity
383 analysis for Aqua’s Woodhaven Water and Sewer and Oak Run Water Divisions to
384 ensure that the Commission has a valid cost of equity recommendation based on the most
385 up-to-date and relevant information practicable.” Moreover, in each of Aqua’s more
386 recent rate cases (this pending case, the Vermilion case filed May 2004 and the Kankakee

387 case filed May 2003, respectively Docket Nos. 04-0442 and 03-0403), Staff has proposed
388 a different return on equity despite the fact that the Company is the same and the cases
389 were filed relatively close in time to each other. If it were as simple as relying on past
390 cases, then there would have been no need for Staff to spend government resources
391 preparing further analyses for the Commission’s consideration on the issue either.
392 However, because capital costs change over time and the Commission’s decision should
393 be based on the most up-to-date information available, it is appropriate for both Staff and
394 the Company to present the Commission with their most up-to-date expert analyses.

395 **Q. Did Staff in Docket No. 04-0442 propose to disallow the projected \$18,600 of rate of**
396 **return costs for the Vermilion Division based on the fact that Aqua filed the**
397 **Vermilion case just six weeks after the Commission’s Order on the Kankakee filing?**

398 A. No. Staff did not contest the appropriateness of Aqua presenting rate of return evidence
399 to support the Company’s requested revenue requirement for Vermilion.

400 **Q. Ms. Pearce notes estimated rate of return costs of \$18,600 and \$26,000 for Docket**
401 **Nos. 04-0442 and 03-0403, Vermilion and Kankakee respectively. Were these the**
402 **actual amounts incurred?**

403 A. No. The actual rate of return witness costs for Docket Nos. 04-0442 and 03-0403 were
404 \$64,492 and \$41,892, respectively. The Company significantly underestimated the
405 amount of costs it would incur to support the returns on equity ultimately approved by the
406 Commission.

407 **Q. Have the customers of Oak Run and Woodhaven actually reaped a type of**
408 **“economies of scale” benefit from the rate of return witness costs incurred in Docket**

409 **Nos. 03-0403 and 04-0442 even though the Oak Run and Woodhaven cases were**
410 **filed later?**

411 A. Yes, I believe so. As noted earlier, it was only through extensive testimony by
412 Ms. Ahern that the Commission was presented with evidence to approve adjustments of
413 thirty bps to Staff's proposals in both Docket Nos. 03-0403 and 04-0442. Based on
414 Aqua's extensive efforts in those cases, Staff has finally recommended a return on equity
415 that recognizes this adjustment. As a result, Aqua is able to accept Staff's proposal on
416 cost of common equity and forego the incursion of further expense for Ms. Ahern to
417 present rebuttal and surrebuttal testimony as well as assist on briefs and possibly
418 participate in the evidentiary hearings. In other words, the customers of Oak Run and
419 Woodhaven are spared the litigation costs supported at least in part by the customers of
420 Kankakee and Vermilion for Staff to recognize the thirty bps adjustment up front. In that
421 sense, the spreading of rate of return costs over a larger customer base as Ms. Pearce
422 recommends has in fact occurred.

423 **Q. Would the Company have incurred \$64,492 for the cost of rate of return witness**
424 **had Staff's return on equity conclusion been consistent in Docket No. 04-0442 with**
425 **that of the Commission's Order in Docket No. 03-0403?**

426 A. No. Had Staff's recommended return reflected the same 30 basis point risk adjustment
427 reflected in the Docket No. 03-0403 Order, the Company likely would not have been
428 forced to re-litigate this issue. Since the Staff of the instant proceedings properly
429 includes this risk adjustment, the Company and its customers are spared the cost of again
430 re-litigating this issue.

431 **Q. Has Aqua taken any other steps to mitigate its rate case expense related to return on**
432 **equity?**

433 A. Yes. Aqua filed its cases for Oak Run and Woodhaven Water and Sewer simultaneously,
434 thereby spreading its costs related to rate of return across all three divisions. As
435 discussed above, Aqua could not have filed these cases earlier due to insufficient
436 information to support the filings; but, Aqua did make every effort to file these three
437 cases together to mitigate expenses related to common issues to the extent possible.

438 **Q. Would you please summarize your position regarding Staff's assertion that costs of**
439 **the rate of return witness should be disallowed?**

440 A. Yes. The Company could not file the Oak Run, Woodhaven Water and Woodhaven
441 Sewer division rate applications at the time of the May 2003 Kankakee filing or the May
442 2004 Vermilion filing for reasons stated previously. Given that Oak Run, Woodhaven
443 Water and Woodhaven Sewer division rate applications could not be accelerated, it was
444 necessary to retain a rate of return witness for the instant proceeding. As such, the cost of
445 such service is reasonable, and should be recoverable over a reasonable amortization
446 period. The Company has under-recovered its actual rate of return costs in Docket Nos.
447 03-0403 and 04-0442. It seeks to recover actual costs incurred in the instant proceeding.

448 **2. STAFF'S REDUCED AUDITING EXPENSE TO \$9,000 PER**
449 **DIVISION**

450 **Q. Mr. Schreyer, please address Staff's proposal to disallow London Witte auditing**
451 **expense in excess of \$9,000 per each of the three divisions in this proceeding.**

452 A. I believe this adjustment is fair and accept it on behalf of the Company.

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**3. STAFF’S TOTAL DISALLOWANCE OF LONDON WITTE
SPECIFIC EXPENSE**

Q. You stated above that, pursuant to Staff’s response to Company data request 1.10, Staff refuses to recognize the \$4,200 costs for London Witte representatives to prepare for, travel to the Commission office and participate in a meeting for questioning and review of their work papers by Staff. Do you agree with this adjustment?

A. No. Staff erroneously discounts the time and effort put forth by London Witte to prepare for and make itself available at Staff’s request for this examination so that Staff could better understand the content and related assumptions reflected in the rate applications. Staff minimizes the time put forth by London Witte to do its part in order that the Company could meet its burden of proof, stating that “Staff met with the two representatives for approximately 3 hours; therefore, \$4,200 appears unreasonable for the amount of time spent.” However, Staff’s presumption that the only time and effort spent by London Witte responding to Staff’s request was the time that Staff saw the London Witte representatives face-to-face is wrong. In fact, 28 hours by three representatives were expended to meet the needs of Staff, including preparation for the meeting, organization and coordination of work papers to facilitate Staff review, travel time to Springfield and follow-up tasks which included copying and forwarding of work papers to ICC Staff. The total cost of time incurred was \$4,035. Expenses for mileage, copying and postage totaled \$196. While the total of costs was \$4,231, London Witte Group billed Aqua \$4,200.

475 **Q. Has Staff presented any basis for a total disallowance of these costs?**

476 A. No. A total disallowance equates to the incursion of zero costs or, in other words, zero
477 work performed by London Witte. Staff has not presented any evidence that would
478 support such a drastic conclusion. Indeed, the work London Witte performed was at the
479 request of Staff. I do not believe that Aqua could have instructed London Witte not to
480 perform the work requested. It is my opinion that the Commission should recognize
481 work performed responding to Staff's requests in a rate case as reasonable and justified.

482 **Q. Is Aqua proposing to recover the \$4,200 for London Witte to perform this work as**
483 **part of the Company's rebuttal position?**

484 A. Yes. This is a known and measurable change that has occurred subsequent to Aqua's
485 filing. As noted, the expense is for London Witte's performance of reasonable work as
486 requested by Staff. Because the work supported all three divisions, Aqua is
487 recommending that the expense be allocated equally between each Division. A copy of
488 London Witte's invoice to Aqua that verifies the amount of this expense is submitted as
489 Attachment B hereto.

490 **4. STAFF'S TOTAL DISALLOWANCE OF AQUA'S RATE**
491 **DEPARTMENT EXPENSE**

492 **Q. Staff disallows "the costs of Aqua America Inc.'s Rate Department and**
493 **miscellaneous expenses because the Company has not supported these costs." (Staff**
494 **Ex. 1.0, pp. 15-16). Do you agree with Staff's proposal?**

495 A. Once again, I do not. Aqua's rate department has done a substantial amount of work to
496 prepare the filings for these cases and handle the day-to-day aspects of the cases,
497 including handling the significant amount of discovery in this case that I discuss below.

498 It is unreasonable not to allow Aqua's recovery of its cost for this work, let alone
499 mandate a total disallowance. As mentioned, a total disallowance, or 100% adjustment,
500 equates to a finding that zero work was performed. A finding that Aqua did not perform
501 any work through its in-house rate department would defy logic.

502 **Q. Would you please give an example of the type and degree of work that Aqua's rate**
503 **department has been required to perform?**

504 A. Staff data requests BCJ 6.01R, 6.02R and 6.03R are submitted as Attachment C hereto.
505 These data requests are discussed further below for other purposes. However, they are
506 discussed here because they are illustrative of the degree of work many of Staff's data
507 requests require. One can readily see that these data requests seek a very large amount of
508 information dating back ten years. Notably, these data requests are ones that Staff even
509 revised by slightly raising the dollar thresholds when Aqua expressed its concern as to the
510 magnitude of the requests to Staff. Even with the revised thresholds, one can see that the
511 amount of information requested was enormous. A combined 1326 pages of attachments
512 were submitted as part of the responses to BCJ 6.01R, 6.02R and 6.03R. The efforts to
513 produce this response were substantial. The costs to scan each page for the purpose of
514 converting into a serviceable PDF file were not insignificant. Had the instant
515 proceeding's level of scrutiny similarly been applied to the Kankakee division in Docket
516 No. 03-0403, the total rate case expense per customer as shown on ICC Staff Exhibit 1.0,
517 Attachment A, Page 3 of 3 would without a doubt have been substantially higher.

518 **Q. How many Staff data requests has Aqua been required to respond to in this**
519 **proceeding?**

520 A. As of June 15, 2005, a total of 626 data requests including subparts have been received.
521 The data requests submitted by the Woodhaven Association are not included in this
522 count.

523 **Q. Are you questioning Staff's actions in seeking the information it believes is**
524 **necessary to review the filings for these Divisions?**

525 A. No. I respect Staff for dutifully seeking to obtain full disclosure of all relevant and
526 material facts to this proceeding. I do not question Staff's actions in seeking the
527 information requested. However, the Company feels it is incumbent upon Staff to
528 properly recognize the costs associated with responding to data requests—no matter the
529 number or complexity thereof—that Staff chooses to issue. Responding to 626 separate
530 and, in some instances, all-encompassing data requests has been a significant burden to
531 the Company. Staff's proposals for the Company to minimize rate case expense should
532 include self-examination with regard to the number and degree of requests it imposes
533 upon the Company.

534 **Q. Has the Company informed Staff of the burden the data requests have been**
535 **imposing?**

536 A. Yes. On several occasions the Company has informed Staff through counsel of the
537 significant burden the data requests have been placing on the Company. Aqua has also
538 asked for the scope of some data requests to be lessened, and Staff has made some
539 adjustments to its requests.

540 **Q. Why did you respond those data requests which were time-intensive and costly?**

541 A. Staff's attorney conveyed to our outside counsel Staff's intention to make adjustments,
542 *i.e.*, propose disallowances, in the event the Company did not respond to any requests.

543 **Q. Has Aqua provided Staff with support for the costs it rate department has**
544 **incurred?**

545 A. Yes. Since Staff's direct testimony, the Company has provided additional support for
546 rate case expenses actually incurred subsequent to the projections reflected in the
547 Company filings. These updates were provided as supplements to BAP 1.08, 2.07 and
548 3.06. I respectfully request that Staff reconsider its position on the costs of Aqua
549 America Inc.'s Rate Department and miscellaneous expenses in light of actual cost detail
550 and support provided.

551 **5. PROPOSAL TO DISALLOW ANY AMOUNT IN EXCESS OF THE**
552 **MOST RECENT PRIOR RATE CASE EXPENSES FOR EACH OF**
553 **THE THREE DIVISIONS**

554 **Q. Is it reasonable for Staff to tie rate case expense exclusively to the expenses Aqua**
555 **incurred in the most recent prior rate cases of each Division?**

556 A. No. The most recent rate cases for the Divisions are not representative of the costs Aqua
557 is expected to incur in this proceeding. Rather, those cases are highly distinguishable in
558 terms of cost-driving factors from the present case.

559 **Q. Why does Aqua project costs for Oak Run and Woodhaven Sewer to exceed the**
560 **costs of those divisions' most recent rate cases?**

561 A. The Company explained in the original filings and subsequent data request responses
562 why the projected costs in the instant proceedings are higher. For Oak Run and

563 Woodhaven Sewer, for which the most recent cases were filed as part of Docket No. 97-
564 0351, the reasons are:

- 565 1. Costs applicable to all divisions consolidated (including the larger Kankakee and
566 Vermilion divisions) in Docket No. 97-0351, such as those associated with cost of
567 equity, rate of return, development of total company schedules, common expense
568 and accounting issues, resulted in greater economies.
- 569 2. Docket No. 97-0351 was filed utilizing a historical test year whereas the instant
570 proceeding was filed under future test year filing requirements.
 - 571 a. The filing requirements for a future test year call for substantially more
572 data than was required under Docket No. 97-0351, thus resulting in a
573 substantial increase in costs.
 - 574 b. A future test year filing must be audited, also contributing to additional
575 costs incurred.
- 576 3. Inflation results in a greater amount of costs since the prior case was filed in 1997.
- 577 4. The increase is also based, in part, on the substantial amount of discovery
578 propounded by Staff to which the Company has been required to respond in more
579 recent rate cases as well as the nature of issues raised by Staff in recent cases,
580 trends that the Company correctly assumed would continue for purposes of
581 estimating the expense it will incur in this case.

582 **Q. Why does Aqua also project the cost for Woodhaven Water to exceed the cost of**
583 **that Division's most recent rate case?**

584 A. For the Woodhaven Water Division, filed as Docket No. 00-0338 consolidated with
585 Kankakee Division (Docket No. 00-0337) and Vermilion Division (Docket No. 00-0339),
586 the reasons identified as 1, 3, and 4 for Oak Run and Woodhaven Sewer Divisions also
587 apply. In addition, the Woodhaven Water case 00-0338 was settled. The Company was
588 able to avoid the significant costs related to the evidentiary hearing and subsequent
589 briefing. Also, for this case, the Company was able to utilize in-house legal counsel for
590 two reasons. First, it correctly anticipated that the issues and work involved in the case
591 would be less considerable. Second, other pending matters were not significant enough
592 to prevent Aqua's limited in-house legal staff from having the time necessary to attend to
593 what was correctly anticipated to be a less controversial rate case.

594 **Q. Given these enormous differences, are the costs Aqua incurred in its most recent**
595 **rate cases for these Divisions an appropriate basis for the Commission to rely upon**
596 **in approving rate case expense in this case?**

597 A. No, for all of the reasons I stated in response to the last two questions. The prior cases
598 simply are not good starting (or ending) points for the development of rate case expense
599 in this proceeding. The Commission's decision should be made based on evidence as to
600 Aqua's actual costs that are being reasonably incurred in this proceeding.

601 **Q. Does legal expense comprise part of those costs?**

602 A. Yes. Staff includes outside legal cost specifically as part of the expenses in excess of the
603 prior rate cases that should be disallowed. Staff alleges there is an unexplained increase

604 in costs from the prior rate cases. It makes no comparison as to the issues and demands
605 placed upon the Company in the prior cases which generated the lower expenses incurred
606 in those cases.

607 **Q. Please explain why legal expense is higher in the instant proceedings than the**
608 **previous rate filings for the Divisions at issue.**

609 A. The increase has been driven primarily by the increased review conducted by Staff, and
610 the number and complexity of the issues raised. As discussed above, I do not fault Staff
611 for performing its job and, indeed, agree that it has an obligation to do so. But, the
612 Commission should recognize that Staff's review causes costs to be incurred. The more
613 intensive the nature of Staff's review, the more time and effort needs to be spent in
614 responding. In this case, Staff has conducted a review that is in many respects more
615 intense and more time consuming than the reviews Staff previously conducted in Aqua's
616 other rate cases, including those for Aqua's large Divisions such as Kankakee. For
617 example, Staff has issued substantially more data requests in this case than it did in the
618 rate case for Aqua's Kankakee Division.

619 **Q. Please elaborate on the relationship of the number of data requests issued and rate**
620 **case expense as it relates to rate case expense in the most recent Kankakee**
621 **proceeding Docket No. 03-0403.**

622 A. While I believe that in Docket No. 03-0403 Staff investigated the Company's Kankakee
623 rate application thoroughly in order to meet its statutory obligation to obtain full
624 disclosure of all relevant and material facts to that proceeding, it did so by issuing
625 177 data requests. For the three divisions in the instant proceeding, which on a combined
626 basis have approximately half the customer base and less than 22% of rate base when

627 compared to the Kankakee Division, a total of 626 data requests have been issued
628 including subparts. This extremely large increase in discovery is representative of the
629 increased nature of Staff's review that, in turn, results in increased work on the part of
630 Aqua's outside legal counsel as well as its rate department.

631 **Q. Were some of the same questions issued for each of the three Divisions in this case?**

632 A. Yes. However, that does not mean that the questions amount to nothing more than a
633 single request. Rather, an identical request posed to each separate Division often requires
634 a completely separate response for each Division. Generally, the Company has had to
635 regard each such data request separately and respond based on the information specific to
636 each Division. As just one example, I will again reference Staff data requests BCJ 6.01R,
637 6.02R and 6.03R submitted as Attachment C. While these requests essentially pose the
638 same question to each Division (with the exception of the dollar threshold), the
639 information with respect to each Division is entirely different and quite substantial. Each
640 request, in reality, requires an entirely separate response. This is true with respect to
641 many of Staff's duplicative requests.

642 **Q. In your opinion, is it reasonable for Staff to substantially heighten the level of**
643 **review in this manner and simultaneously argue that Aqua's rate case expense**
644 **should not increase?**

645 A. No. In my opinion, it is extremely unfair for Staff to issue 626 separate data requests,
646 many of which required countless hours of research to gather, assimilate, copy and
647 review (in some instances dating back as the year 1997) only to allege that the Company
648 is being reckless in incurring rate case expense. Of the individual 626 data requests
649 issued by Staff, 448 were issued by Ms. Pearce. This is a substantial number.

650 Ms. Pearce's allegation that the Company should not incur the necessary legal expense to
651 process responses required by Staff is unjust and unreasonable.

652 **Q. Staff states that “the Oak Run Division, a small residential sub-division, is not large**
653 **enough to support the cost of the outside legal counsel used by Aqua for this**
654 **proceeding.” Staff also takes the same position with regard to Woodhaven, which**
655 **Staff notes “is a campground.” Is the size of these systems relevant to the cost of**
656 **processing rate applications?**

657 A. No. The size of these systems does not make it any less costly to prepare, review and
658 service discovery responses or otherwise process these cases. Moreover, I think it is
659 important to point out that while Staff takes the position that Aqua's rate case should not
660 increase because these are small divisions, Staff is treating these small systems as though
661 they were large systems. As noted, Staff has submitted a substantially greater number of
662 data requests in this case in comparison to the 2003 case that addressed Aqua's largest
663 Division Kankakee.

664 **Q. Do you have any further comments on Aqua's decision to use outside counsel for**
665 **these cases?**

666 A. Yes. The decision was the result of limited in-house resources. Aqua does not have an
667 extensive in-house legal staff, and must use outside resources to handle more time-
668 consuming cases. The only alternative would be to add additional head-count to Aqua's
669 in-house Staff. That would entail another annual salary and related benefits, the costs of
670 which would be allocated as rate-case expense.

671 **Q. Has Staff acknowledged that it does not cost Aqua any less to process rate cases for**
672 **small Divisions as opposed to large ones?**

673 A. Yes. In response to Company data request 1.11, Staff acknowledged that the filing
674 requirements for divisions the size of Oak Run and Woodhaven are no less stringent than
675 for those of larger divisions such as Kankakee and Vermilion.

676 **Q. Has the Company observed a lessened legal or witness presence by Staff in the**
677 **instant proceeding compared to Docket Nos. 03-0403 and 04-0442?**

678 A. No. I have observed no less legal or witness involvement by Staff as it fulfills its
679 statutory obligation to process the rate applications of the instant proceeding, nor would I
680 necessarily expect to. While I would not expect involvement to increase as it has, the
681 requirements for Staff to process a rate application for Oak Run and the Woodhaven
682 divisions are no less than for Staff to process a rate application for Aqua's Kankakee or
683 Vermilion Divisions.

684 **Q. Has Staff questioned that the outside legal fees requested for recovery in this case**
685 **have actually been incurred?**

686 A. No. Aqua has submitted copies of its actual legal invoices to Staff in response to
687 discovery. These invoices fully support the outside legal costs Aqua projected for these
688 cases.

689 **6. STAFF'S PROPOSALS FOR FUTURE RATE CASES**

690 **Q. Please identify the proposals that Staff makes for Aqua's future rate cases.**

691 A. Staff essentially makes three proposals:

- 692 1. Aqua must consolidate future rate filings for several divisions simultaneously
693 rather than on a piecemeal basis;
- 694 2. Aqua should file rate cases for smaller divisions simultaneously with at least one
695 of the larger divisions; and
- 696 3. Back-to-back rate cases should not be for the same test year.

697 (Staff Ex. 1.0, pp. 23-24).

698 **Q. Do you agree with these proposals?**

699 A. No, I do not. The Company needs no incentive or additional regulation to keep rate case
700 expense as low as possible for its customers. The Company at all times seeks to keep its
701 expenses to a minimum, including rate case expense. Further, since deferred rate case
702 expense is not allowed in rate base, a portion of Aqua's capital supplied by investors and
703 creditors is unearning, making the Company's ability to achieve its theoretically allowed
704 return on equity a mathematical impossibility. The higher rate case expense becomes, the
705 greater the unfavorable gap between actual and allowed return on equity becomes.

706 **Q. Do you have specific concerns with Staff's first two proposals regarding the timing
707 of rate filings?**

708 A. Yes. As a rule it will not always be prudent for Aqua to file cases for different divisions,
709 or for small and large divisions, simultaneously. For example, as I explained above with
710 respect to these pending cases, it would have imposed substantially greater costs on Oak
711 Run and Woodhaven customers had Aqua accelerated these cases solely to file them at
712 the time of one of Aqua's larger divisions.

713 **Q. Do you have any other concerns with Staff's first two proposals?**

714 A. Yes. Staff's recommended rules will almost always dictate either hasty action or
715 improper delay. In particular, if a large division case is being filed, there would be an
716 improper incentive to accelerate small division filings even though incomplete
717 information may be available to support the filing, simply to avoid the delayed cost
718 recovery associated with waiting for the next large division case to be filed. On the other
719 hand, it would also be improper to require Aqua to forego its authorized return in small
720 divisions by requiring it to wait to file a rate case, perhaps for a year or more, simply
721 because a large division is not ready for a filing at the same time. The timing of rate
722 cases is fact dependent, and Staff's proposal, as a matter of policy, would send the wrong
723 signals because it considers only a single factor to the exclusion of all others. Moreover,
724 Staff's suggestion that the Company file ill-timed rate applications simply to allocate the
725 cost of its rate of return witness among a larger customer base is not only illogical but
726 contrary to the sound management and decision-making qualities that Aqua's customers
727 expect. I further believe the Commission would question the prudence of a utility which
728 robotically packages divisional rate applications together to lessen rate of return expense
729 at the expense of otherwise sound rate case planning and timing.

730 **Q. Do you have any further comments concerning Ms. Pearce's recommendations**
731 **regarding future Aqua rate case filings?**

732 A. Yes. I feel it is important to emphasize that even in instances where it would perhaps
733 appear to be expedient to file several divisions simultaneously, the Company must
734 consider anticipated issues involved and its available human resources. Looking back, I
735 question whether the Company could have processed the pending Divisions with the

736 Vermilion Division even if the pending Divisions had been ready for filing, which they
737 were not. The Vermilion Division too was subject to an extraordinary amount of scrutiny
738 and review. The Company must, to the extent possible, schedule its rate applications
739 such that its limited amount of resources can adequately process them. This is no
740 different from Staff desiring to know in advance when the Company plans to submit
741 divisional rate applications such that it can better schedule its own assignments.

742 **Q. Do you agree with Staff’s third recommendation that back-to-back rate cases not be**
743 **for the same test year?**

744 A. No. This recommendation is not reasonable either. If anything, utilizing the same test
745 year in a subsequent filing should produce some “economies of scale” type savings. This
746 is because the test year information would have already been developed by Aqua and
747 examined by Staff. To disregard an existing test year that has been previously developed
748 by the Company and closely examined by Staff in a prior docket and instead incur the
749 additional cost of developing a new test year which Staff must in turn examine, would not
750 be prudent or reasonable. The customers of Oak Run and Woodhaven have benefited
751 because Aqua was able to utilize a portion of the rate template from Docket No. 04-0442
752 in the instant proceeding at no cost. It is likely that Staff would have issued even more
753 data requests in this case if the Company had utilized a test year other than the one used
754 in Docket No. 04-0442.

755 **Q. Do you have any further concerns with Staff’s rate case proposals?**

756 A. Yes. I am very concerned that these are new rules proposed exclusively for Aqua. Such
757 discriminatory application is inherently unfair. Moreover, I am concerned that Staff is, in
758 essence, proposing a retroactive application of these proposed rules to Aqua’s current

759 filing. In particular, Staff is proposing herein to require simultaneous rate case filings,
760 including small divisions with larger divisions, and at the same time proposing that
761 Aqua's current rate case expenses be disallowed, in part because Aqua did not file these
762 cases in either May 2003 or May 2004. Aqua had no prior notice of Staff's proposed
763 rules. Aqua could not go back in time to comply with the newly proposed rules even if
764 the Company believed that accelerating the instant filings would have been appropriate,
765 which the Company does not.

766 **Q. Do you have any final comments on alternative measures for lessening rate case**
767 **expense?**

768 A. Yes. All components of rate case expense are, to a large extent, a function of the number
769 of data requests issued by Staff, and of the number of issues taken by Staff and the
770 complexity thereof to which the Company must respond, rather than the clustering of
771 filings which typically do result in some economies. Staff witness Pearce correctly
772 observes that the rate case expense per customer of the instant proceeding divisions is
773 higher than those of the Kankakee and Vermilion Divisions.¹ One would expect that a
774 division with significantly more customers such as Kankakee would benefit from lower
775 rate case expense per customer. What Ms. Pearce fails to note is the marked difference in
776 the number of data requests issued by Staff in Docket No. 03-0403 and the instant
777 proceeding.

¹ Staff witness Pearce observes that the rate case expense per customer in the instant proceeding is higher than it was for the Vermilion Division, which one would expect for a Division like Vermilion with significantly more customers across which rate case expense can be spread. However, I wish to point out that Staff Exhibit 1.0, Attachment A, Page 2 of 3 is flawed because column (c) does not reflect Aqua's actual rate case costs incurred for Vermilion, which were substantially higher than those originally projected by the Company in large part because the Company experienced a more intensive review and greater number of data requests in Vermilion than it did in Kankakee.

778 **Q. Do you wish to make any further comments on this subject prior to making**
779 **concluding statements?**

780 A. Yes. Staff’s testimony improperly portrays Aqua as being all too willing to incur
781 unnecessary expense, and callous to the impact such unnecessary expense has on its
782 customers. As I have explained, nothing could be farther from the truth. In fact, the
783 Company has been extremely sensitive to rate case expense. Advantage has been taken
784 of available vacations and holidays, evenings and weekends to complete the rate
785 applications, address the Deficiency Notice and respond to over 600 individual data
786 requests. The work during these times was at no cost to our Oak Run and Woodhaven
787 customers. Further, the estimated rate case costs reflected in the Company’s filing do not
788 reflect the extraordinary efforts made by several of the local Aqua office staff who have
789 contributed countless hours responding to legitimate, but nevertheless voluminous,
790 requests of information from Staff. Lastly, the Company went to great lengths and some
791 amount of additional rate case expense to gather, review, photocopy, convert to PDF and
792 service information pursuant to Section 285.150 to save Staff from traveling to the
793 corporate office.

794 **Q. Do you believe your testimony provides the “uncontroverted justification for filing**
795 **the instant proceeding apart from the recently filed Kankakee and Vermilion rate**
796 **proceedings (Docket Nos. 03-0403 and 04-0442, respectively)” that Staff states it**
797 **requires per its response to Company data request 1.08?**

798 A. Yes, I do. No customer group would desire to pay an additional \$1,839,528 in order to
799 lessen the specific cost of service item of rate of return expense.

800 **Q. Please summarize your position on rate case expense.**

801 A. The Company seeks to minimize its rate case expense at all times consistent with meeting
802 its burden of proof. However, the Company has little control over the scope of its burden
803 of proof. Rather, its burden of proof is dictated by the number and complexity of data
804 requests issued by Staff and intervenors, and the issues which result from discovery. The
805 Company has no choice but to fully respond to all interrogatories. The Company
806 believes it should receive recovery of all rate case expense incurred and supported. We
807 have provided support for all costs incurred to date. We ask to recover nothing more than
808 these costs and the costs projected to be incurred to finalize this proceeding.

809 **E. RATE CASE AMORTIZATION PERIODS**

810 **Q. Please address Staff's proposed rate case amortization periods for Oak Run (7**
811 **years), Woodhaven Water (5 years) and Woodhaven Sewer (7 years).**

812 A. Staff's proposed amortization periods are based solely on the periods of time between
813 Aqua's current rate filings and Aqua's previous filings for each Division.

814 **Q. Do you agree that these are the appropriate periods to utilize?**

815 A. No. Staff's proposals fail to recognize that these are forward looking rate filings and, as
816 such, the Company's amortization periods should be a function of when Aqua will likely
817 file its next rate applications for these Division as opposed to when it submitted its most
818 recent historical ones. The Company was able to keep the Oak Run and Woodhaven
819 Divisions out of the rate arena for several years to customers' benefits. It should not be
820 unfairly penalized for doing so via a backward-looking approach to determining the
821 proper amortization period. The Company feels a four year amortization period is
822 appropriate for the Woodhaven Divisions and a three year period is appropriate for the

823 Oak Run Division. Any longer periods add to the Company's inability to achieve its
824 allowed return on equity because the deferred balance of rate case expense represents un-
825 earning capital.

826 **Q. Do you have any additional comments on why you believe the amortization periods**
827 **Aqua proposes are appropriate?**

828 A. Yes. The periods Aqua proposes are appropriate because they are the periods in which
829 Aqua is most likely to file its next rate cases for the Divisions. The periods are,
830 furthermore, reasonable ones in which to capture the continuing effects of inflation and
831 capital projects that are routinely incurred. Periodic rate applications every three to four
832 years avoid any degree of rate shock that would result from capturing these continuing
833 effects over longer intervals.

834 **Q. Do you have any further comment on the three year period Aqua proposes for Oak**
835 **Run?**

836 A. Yes. Mr. Bunosky testifies to the basis for the Company's projection that it will file its
837 next rate application for Oak Run in 2007. This evidence demonstrating the reasonable
838 likelihood that Aqua will file an Oak Run application in 2007 more than supports Aqua's
839 request for the longer three year amortization period that reflects the next rate filing being
840 made in 2008.

841 **F. MANAGEMENT EXPENSE**

842 **Q. Please address Staff's adjustment for management expense.**

843 A. Pursuant to the Company's supplemental response to JF-1.05, the Illinois Corporate
844 Allocation, which was charged to Account 634 – Contractual Services – Management in
845 prior years, was charged to Account 675 – Miscellaneous Expense in 2004 as follows:

846 Oak Run \$ 42,131

847 Woodhaven Water 122,981

848 Woodhaven Sewer 107,870

849 **Q. Staff maintains “the Company has neither supported the amounts of management**
850 **expense included in its filing nor explained the significant amounts by which its**
851 **forecasted amounts exceed actual 2004 expenses.” Please comment on this assertion**
852 **by Staff/**

853 A. The Total Company management expense included in the filing is the very same amount
854 as that used by the Company, reviewed by London Witte Group and examined and
855 accepted by Staff in Docket No. 04-0442. The allocation is the same as that utilized in
856 Docket No. 04-0442 with the exception of weighting Aqua Illinois Inc. availability
857 customers at one third as was explained in response to BAP 10.04 and in more detail in
858 response to WHA 2.02 F. Because Staff did not dispute the customer count allocation
859 methodology utilized in Docket No. 04-0442, Staff should consistently use this approach
860 in the instant proceeding.

861 **Q. Do you accept Staff's adjustment to substitute 2004 actual management expense in**
862 **place of 2005 projected test year data?**

863 A. I will accept Staff's approach as long as it properly incorporates the Illinois Corporate
864 Allocation amounts as supplemented by the Company in JF-1.05. With regard to the Oak
865 Run division, the result of Staff's approach should be a number no greater than our
866 original test year amount of \$58,005.

867 **Q. Would the Company be willing to consider weighting Woodhaven customers at less**
868 **than the current full weighting under a bulk billing agreement which eliminates the**
869 **collections issue which has plagued the Company for several years?**

870 A. Yes. Aqua would be willing to consider such a proposal. However, I must emphasize
871 that any proposal would need to recognize and account for the impact to Aqua's other
872 divisions that would result from a reduced allocation to the Woodhaven Divisions.

873 **V. REBUTTAL TO MS. JONES' TESTIMONY**

874 **Q. Does the Company dispute Staff's rate base and amortization adjustments related to**
875 **tank painting?**

876 A. No. Consistent with updated tank painting information provided to Staff via data
877 responses, the Company believes Ms. Jones' rate base and amortization adjustments are
878 reasonable.

879 **Q. Please address Staff's adjustment to remove from Plant in Service the cost of a pilot**
880 **study and the projected engineering plans related to a Reverse Osmosis ("RO")**
881 **Treatment Plant under consideration by the Company.**

882 A. Based on Mr. Bunosky's testimony, the likelihood of the Reverse Osmosis plant is not
883 uncertain as Staff presumes. Because the likelihood of the plant is reasonably certain,
884 Staff's adjustment should not be made. However, if the Commission for some reason
885 disagrees and adopts Staff's proposal to remove the \$68,180 from Plant in Service, then it
886 is appropriate to amortize this amount over a ten year period to account 675 -
887 Miscellaneous Expenses rather than defer the amount to Account 183 – Preliminary
888 Survey and Investigation Charges.

889 **Q. Do you wish to comment on Ms. Jones' adjustments to Accumulated Deferred**
890 **Income Taxes?**

891 A. Yes. The Company has reviewed Ms. Jones' deferred tax related adjustments and will
892 not contest them. However, there is a calculation error on ICC Staff Exhibit 2.0.
893 Schedule 2.04 (WS) page 1 of 2, line 18. Staff has confirmed this error and agrees with
894 the Company's calculation per response to Company data request 1.28.

895 **Q. Are you in agreement with Ms. Jones' depreciation rates utilized for purposes of**
896 **determining the requirement?**

897 A. I am. However, I suggest she utilize a more precise rate than 2% for the plant items for
898 which the Company was unable to provide support for specific rates. In light of proposed
899 rate case expense and Ms. Jones assertion that "[b]ecause of the wide range in asset lives,
900 depreciation rates by primary accounts seem more reasonable than one rate for all
901 depreciable plant," it would not be reasonable for the Company to do a cost of
902 depreciation study to support new rates for those plant accounts. I believe that rates that
903 accurately reflect the depreciable lives of these assets, whether less than or more than the

904 2% used by Ms. Jones, would be reasonable. Avoiding the cost of a depreciation expert
905 in the next Aqua sewer rate case benefits our customers via rate case expense avoidance.

906 **Q. Do you have any more comments regarding depreciation rates?**

907 A. Yes, I do. Contrary to Ms. Pearce’s testimony, and as noted already, the Company is
908 extremely sensitive to the cost of processing a rate case—particularly for those divisions
909 with a relatively small number of customers compared to its larger divisions. The
910 Company considered contracting a depreciation witness for the purpose of performing
911 studies for the instant proceedings. However, it opted to not incur the additional expense.
912 Rather, Aqua is choosing to work with Staff to determine the appropriate rates. The
913 Company does not discount, but rather fully supports periodic assessments of the
914 depreciation rates in effect for its various divisions.

915 **Q. Please comment on Staff’s proposed Utility Plant retirement adjustments.**

916 A. The Company has addressed these retirements with those who directly operate the Oak
917 Run and Woodhaven systems, and find too that these adjustments are warranted.

918 **Q. Are there any significant adjustments not reflected in the filing and not addressed in**
919 **the Staff’s testimony which should be brought to the attention of the Staff and**
920 **Commission?**

921 A. In response to data request BCJ 7.01, the Company provided an update to Pension
922 Expense based on the actuary’s latest 2005 estimate. Staff’s responded to Company data
923 request 1.27, “it is Staff’s opinion that the effect of recognizing the updated amounts on
924 the revenue requirement of each division is immaterial and no adjustment is warranted.”

925 **Q. Do you agree with Staff that the adjustments are immaterial?**

926 A. I believe them to be known and measurable changes that are material in the same way as
927 the tank painting and retirement adjustments made by Staff which happened to lower the
928 Company's revenue requirement. I respectfully ask that Staff reconsider its position on
929 the materiality of pension expense, and incorporate the entries reflected on Company
930 response to BCJ 7.01.

931 **Q. Is Aqua proposing this update to its pension expense as part of its rebuttal position?**

932 A. Yes. Aqua has included this update in its rebuttal position. A copy of Aqua's response
933 to BCJ 7.01 is submitted as Attachment D hereto.

934 **Q. With regard to the radium removal treatment plant being installed in 2005, do you
935 wish to update the rate application for any major known and measurable changes?**

936 A. Yes. As stated in the Company's response to BCJ-6.06, the results of the most recent
937 study by the Farnsworth Group quantifies required capital costs for "Filter Backwash
938 Equalization and Sludge Storage in Existing Backwash Holding Basin with yearly
939 Disposal" at \$346,868. Annual operating costs associated with this radium removal
940 process are \$44,500.

941 **VI. CONCLUSION**

942 **Q. Do you wish to make any concluding comments?**

943 A. The Company believes this rate increase is just, reasonable, and in fact necessary for it to
944 continue meeting its obligation to serve under the high standards expected by its
945 customers and required by various levels of regulations. Serving satisfied customers is of
946 great importance to Aqua. As such, we will work harder to counter any perception that

947 service has not improved in recent years. We respectfully request that this rate request
948 be adopted as updated for known and measurable changes in this rebuttal case filing as
949 set forth in Schedule 6.1, attached hereto, except for those adjustments accepted by the
950 Company as discussed herein.

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

952 A. Yes.