ILLINOIS COMMERCE COMMISSION

Docket No. 14-0741

Exhibit No. 14.0

Surrebuttal Testimony of

Justin Kersey

on behalf of

UTILITY SERVICES OF ILLINOIS, INC.

**PREPARED SURREBUTTAL TESTIMONY
OF JUSTIN KERSEY
ON BEHALF OF
UTILITY SERVICES OF ILLINOIS, INC.**

Q. PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS ADDRESS.

A. My name is Justin Kersey. I am the Financial Planning & Analysis Manager of Utility Services of Illinois, Inc. ("USI" or "Company"). My business address is 2335 Sanders Road, Northbrook, IL 60062.

Q: MR. KERSEY, HAVE YOU PREVIOUSLY SUBMITTED TESTIMONY IN THIS PROCEEDING?

A: Yes, I have.

Q: WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

A: The purpose of my surrebuttal testimony is to respond to various recommendations and adjustments proposed in the rebuttal testimony of the Illinois Commerce Commission ("ICC") Staff and Attorney General ("AG") witnesses.

Q: WOULD YOU PLEASE BEGIN WITH THE ADJUSTMENTS PROPOSED BY STAFF THAT YOU WILL BE ADDRESSING.

A: Yes.

STAFF - FUEL EXPENSE

Q: DO YOU AGREE WITH STAFF'S ADJUSTMENT TO FUEL EXPENSE?

A: Although I do not agree with Staff's reasoning for adjusting USI's fuel expense, the Company will not oppose the fuel adjustment proposed by Staff in this proceeding.

The Company's historical fuel costs are on average 2% greater than the national average, in the next rate proceeding the Company will provide their fuel purchase policy.

STAFF – INSURANCE EXPENSE

Q: DO YOU AGREE WITH STAFF'S ADJUSTMENT TO INSURANCE EXPENSE?

A: No, I do not agree with Staff's adjustment to insurance expense. Staff has adjusted insurance expense for 2015 by reducing USI's 2014 amount by 2.2%, believing this is consistent with the explanation provided in USI Ex. 3.1. I addressed the misunderstanding surrounding the 2.2% insurance expense reduction at the Water Service Corp. ("WSC") level in my Rebuttal Testimony to the AG (USI Ex. 8.0: 114-125). Below is a table (Table 1) that will help address the issue more clearly.

Table 1

	2014	2015	Change
WSC All Insurance Costs	$ 2,848,824	$ 2,785,789	-2.2%
USI % of Utilities, Inc. ERC Base	6.90%	7.07%	2.5%
USI Insurance Costs	**$ 196,468**	**$ 196,978**	**0.3%**

As illustrated above, USI's customer base in 2015 is a larger percentage of Utilities, Inc.'s customer base than in 2014. Although WSC is forecasting a reduction in insurance costs year-over-year of 2.2%, the same reduction does not materialize at the USI level due to the increase in its share of the total UI customer base. Therefore, Staff's proposed adjustment does not account for fact that USI's current customer base constitutes a larger percentage of Utilities, Inc.'s system-wide customer base. Pursuant to the cost allocation formula in the Affiliated Interest Agreement approved by the Commission, common expenses such as insurance, are required to be allocated to affiliated operating utilities based upon the number of ERCs (Equivalent Residential Connections).

Q: WOULD YOU NOW PLEASE TURN TO EACH ADJUSTMENT PROPOSED BY THE AG THAT YOU WILL BE ADDRESSING?

A: Yes.

<u>AG - FUEL EXPENSE</u>

Q: PLEASE SUMMARIZE MR. RADIGAN'S REBUTTAL TESTIMONY WITH RESPECT TO HIS RECOMMENDED ADJUSTMENT TO FUEL EXPENSE.

A: Mr. Radian suggests the fuel price estimate be updated at the time the Commission makes its decision in this case. However, I believe that is too late in this process and the fuel price cannot be updated at that time, Mr. Lubertozzi's testimony addresses this timing issue in more detail. I have updated fuel price with the most recent U.S. Energy Information Administration projections. However, Staff witness Everson has already updated her position with the same projection and the Company does not oppose her adjustment.

<u>AG - UNCOLLECTIBLES</u>

Q: PLEASE SUMMARIZE MR. RADIGAN'S REBUTTAL TESTIMONY WITH RESPECT TO HIS RECOMMENDED ADJUSTMENT TO UNCOLLECTIBLE EXPENSE.

A: Mr. Radigan argues USI should not include the "Uncollectible Accounts Accrual" expense account when determining its uncollectible rate. Although Mr. Radigan believes that the analysis provided in my Rebuttal Testimony is "seriously flawed" (AG Ex. 2.0: 173), I will illustrate why my analysis is accurate.

Q: PLEASE ADDRESS MR. RADIGAN'S RATIONALE FOR EXCLUDING UNCOLLECTIBLE ACCOUNTS ACCRUAL.

A: Mr. Radigan concluded the Uncollectible Accounts Accrual expense account should not be considered in the rate-setting process as a result of his examination of the Accumulated Provision for Uncollectible Accounts balance. However, when performing this analysis one should consider examining why the account balance is changing prior to reaching a conclusion in the rate-setting process.

As stated in my Rebuttal Testimony with regard to how the Uncollectible Accounts Accrual expense account operates, "Once a customer's service is stopped, their account balance will be written off and the accrual will subsequently reverse." (USI Ex. 8.0: 96-97.) Said, another way, a customer must have service in order for their account balance to be written off via the Company's accounting system automated processes. This implies customers who do not receive service cannot have their service disconnected, and their account balance subsequently written off (*e.g.*, availability customers) via the automatic process.

Below is a table (Table 2) depicting USI's availability Accounts Receivable ("AR") aging balance (181+ Days old) from 2011-2014.

Table 2

	AR Balance			
	181+ Days	181+ Days	181+ Days	181+ Days
System	**2011**	**2012**	**2013**	**2014**
Apple Canyon - Availability	$ 59,025	$ 81,355	$ 97,552	$ 108,985
Lake Holiday - Availability	$ 14,773	$ 19,436	$ 25,730	$ 34,105
Lake Wildwood - Availability	$ 95,191	$ 107,891	$ 110,882	$ 148,141
Total Availability	**$ 171,000**	**$ 210,694**	**$ 236,177**	**$ 293,245**

As depicted above, USI's availability customer account balances, which are 181+ days old, continue to accrue year after year because their balances are not written off. Utilities, Inc. ("UI") performed an analysis and determined the likelihood of payment on these balances is 5%; therefore, 95% of these balances are accrued for though Accumulated Provision for Uncollectible Accounts on the balance sheet and Uncollectible Accounts Accrual on the income statement. Below is a table (Table 3) illustrating the increase in the provision account strictly related to the availability customer account balances shown in Table 2.

Table 3

	AR Provision		
	Provision Increase		
System	**2011-2012**	**2011-2013**	**2011-2014**
Apple Canyon - Availability	$ 21,213	$ 36,600	$ 47,462
Lake Holiday - Availability	$ 4,429	$ 10,409	$ 18,365
Lake Wildwood - Availability	$ 12,065	$ 14,906	$ 50,303
Total Availability	**$ 37,708**	**$ 61,916**	**$ 116,130**

The provision increase for this subset of USI customers materially impacts the Accumulated Provision for Uncollectible Accounts balance. Mr. Radigan failed to consider the impact of these provisions and how USI's provision balance accrues before he suggested, "USI could stop setting aside any money in the Uncollectable Accounts

Accrual." (AG Ex. 2.0: 216-217.) I would also like to point out that USI does not "set aside money" in any of its accounts but follows an accrual accounting concept that was not only reviewed by the Commission Staff but also UI's external auditors.

Q: PLEASE DETAIL THE THREE EXPENSE ACCOUNTS WHICH SHOULD BE INCLUDED IN DETERMINING THE UNCOLLECTIBLE EXPENSE RATE.

A:

1. Agency Expense: These are costs associated with contracting collection agencies in an attempt to collect on overdue balances and bad debts.
2. Uncollectible Accounts Expense: This account is a net account of both write-offs of account balances and payments on previously written off balances.
3. Uncollectible Accounts Accrual Expense: These costs are accruals for anticipated account balance write-offs. If an account were to be written off, this account will subsequently reverse any respective accrual which had already been expensed.

<u>AG - INSURANCE EXPENSE</u>

Q: PLEASE SUMMARIZE MR. RADIGAN'S REBUTTAL TESTIMONY WITH RESPECT TO HIS RECOMMENDED ADJUSTMENT TO INSURANCE EXPENSE.

A: Mr. Radigan believes the Company failed to prove its forecast expense is reasonable based on my argument that USI's current customer base should be considered when allocating costs from WSC and that I have not validated WSC's insurance expense forecast. I will address both concerns.

Q: PLEASE ADDRESS MR. RADIGAN'S ASSERTATION THAT THE COMPANY HAS NOT PROVIDED THE IMPACT TO USI FROM THE OAKWOOD SYSTEM.

A: Mr. Radigan argued that "the Company should produce the Oakwood insurance bill and show how this incremental change affects overall costs." (AG Ex. 2.0, p. 14). This argument fundamentally misunderstands the nature of USI's insurance expense. There is no separate "Oakwood insurance bill." Insurance costs incurred by WSC are a common expense that is allocated to the various UI operating affiliates in accordance with requirements of the Affiliated Interest Agreement approved by the Commission. As fully explained in my response to Staff's Insurance Expense adjustment, between the 2014 forecast and the 2015 forecast there was a year-over-year decrease in WSC's insurance expense of 2.2%. However, USI's allocated portion of this expense did increase because its percentage of ERCs increased relative to the other UI affiliates that are allocated the expense based on total ERCs. The Company provided the insurance expense allocated to each USI system via USI Ex. 2.2 and USI Ex. 3.2. Based upon USI's increased percentage of ERCs, the insurance expense allocated to USI is $196,468 in 2014 and $196,978 in 2015, for a year-over-year increase of $510. (USI Ex. 2.1, Sch. B, pg 1/4: 31).

Q: PLEASE ADDRESS MR. RADIGAN'S ASSERTATION THAT THE COMPANY HAS FAILED TO VALIDATE THAT ITS FORECASTED INSURANCE EXPENSE IS REASONABLE.

Within USI's forecast guidelines (USI Ex. 3.1) I explain that WSC's insurance expense forecast is based on review and analysis of current and projected insurance policies. Below is a table (Table 4) depicting the increase in WSC's business insurance premiums from

2013 to 2014. These business insurance premiums drove WSC's, and therefore, USI's insurance expense increase between 2013 and 2014.

Table 4

	2013 Policy	2014 Policy	Increase
Auto	$ 266,556	$ 341,979	28.30%
Workers Comp	$ 453,908	$ 510,340	12.43%
Property	$ 292,875	$ 344,906	17.77%
General Liability	$ 463,697	$ 612,530	32.10%
WSC Business Insurance Premiums	**$ 1,477,036**	**$ 1,809,755**	**22.53%**

As illustrated above, there was a steep rise (22.53%) in the cost of WSC's business insurance premiums between 2013 and 2014. The increase in cost was the result of an accumulation of claims spanning multiple years, closing in 2013. After these claims closed WSC's insurance providers reevaluated and subsequently increased WSC's business insurance premiums. The 2014 policies were in place during the creation of WSC's 2015 forecast and are the "current" policies I referenced within USI Ex. 3.1. The "projected" policies were projected by analyzing claims which remained opened at WSC during the forecast creation. Given the smaller amount of claims open at that time, WSC forecasted an insurance expense reduction of 2.2% between 2014 and 2015. As I stated in response to both Staff's Insurance Expense adjustment and AG's Insurance Expense adjustment, although there was a decrease of 2.2% forecasted at the WSC level; the same reduction does not materialize at the USI level because USI's increased number of ERCs results in a larger share of the total expense that is required to be allocated to USI pursuant to ERC-based formula in Affiliated Interest Agreement.

AG - SALARIES AND WAGES EXPENSE

Q: PLEASE SUMMARIZE MR. RADIGAN'S REBUTTAL TESTIMONY WITH RESPECT TO HIS RECOMMENDED ADJUSTMENT TO SALARIES.

A: Mr. Radigan continues to express his disagreement with the Company's forecast without actually analyzing and comprehending how the forecast was derived. In my opinion, after reviewing Mr. Radigan's Direct Testimony, it was clear he failed to review and understand all of the Company's discovery responses regarding Salaries & Wages, as he suggested the Company had provided no analysis of current and anticipated staffing levels. Although, Mr. Radigan asserts he reviewed all of the discovery responses prior to completing his Direct Testimony, in my opinion his misperception stems from his lack of reviewing or lack of understanding said responses.

With regard to salary expense by employee, Mr. Radigan claims there is, "no work paper to show how these values were allocated to the 23 systems that make up USI". (AG Ex. 2.0: 330-335). On January 28, 2015, the Company provided all parties with its supplemental response to Staff data request 4.03. Attached is USI Exhibit No. 14.0, Schedule 14.1, which is a screenshot of an email that was submitted to the Attorney General and contained the Company's supplemental response to Staff data request 4.03. That supplemental response contained the work paper which shows how the values from the Company's reply to Staff data request 4.03 are allocated to the 23 systems that make up USI. This information is located in the highlighted lead tab, "2015 Salaries and Wages". This highlighted lead tab contains all employees and their salary allocations to all USI systems. The second and third tabs are labeled "MHE 4.03." and are the direct output from the Company's reply to Staff data request 4.03 which are used to populate the lead tab, providing exactly what Mr. Radigan asserts is non-existent.

Q: WOULD YOU ADDRESS MR. RADIGAN'S ASSERTATION THAT THE COMPANY IS DOUBLE COUNTING SALARIES?

A: In his Direct Testimony Mr. Radigan acknowledges, "50% of their total time in 2015 will be spent on rate case activities" (AG Ex. 1.0: 339-340). This is in response to Mr. Radigan's apparent issue with the Company's forecasted maintenance expense charged to plant (*i.e.* Capitalized Time). Mr. Radigan also acknowledges, "Maintenance Expense Charged to Plant is a negative number (*i.e.*, credit to the income statement)" (AG Ex. 1.0: 295-296). However, in his Rebuttal Testimony Mr. Radigan contradicts his Direct Testimony by stating, "A review of the discovery responses on salaries shows no crediting for an employee's time being recovered under rate case expense." (AG Ex. 2.0: 351-353). Further, "I see no provision crediting for capital time." (AG Ex. 2.0: 359-360). I am unclear why Mr. Radigan changed his position in his Rebuttal Testimony.

Per USI Ex. 3.1, under the heading "Capitalized Time", I state, "Rate Case cap time: an assumption of 50% of salaries for Finance/Regulatory personnel has been reserved for capitalized time." To prove the 50% capitalized time, which is the credit to the income statement that Mr. Radigan is looking for, one could review the Company's supplemental response to Staff data request 4.03 and determine the personnel working within finance are grouped within the "President" cost center. These employees include:

Guttormsen, Robert A.

Halloran, Brian

Kersey, Justin

Lubertozzi, Steven M.

Neyzelman, Dimitry

Mr. Radigan suggests these employees have no provision crediting for capital time. However, in reviewing USI Ex. 3.2, one can see exactly 50% of the "President" allocated salaries are being credited through capitalized time. Again, the Company is not double counting salaries as evidenced in USI Ex. 3.2 and acknowledged in AG Exhibit 1.0.

<u>AG - SALES</u>

Q: PLEASE SUMMARIZE MR. RADIGAN'S REBUTTAL TESTIMONY WITH RESPECT TO HIS RECOMMENDED ADJUSTMENT TO SALES.

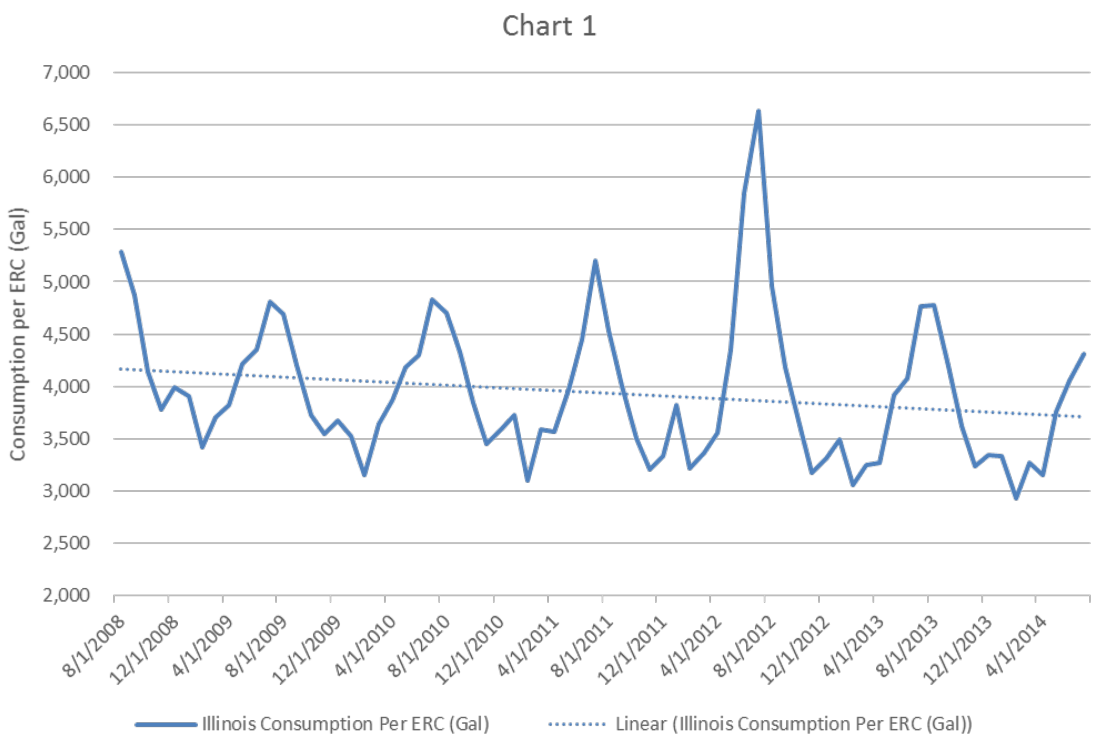
A: Mr. Radigan's has cherry-picked points from my Rebuttal Testimony in an effort to make it appear as though I support his position. To be clear, Mr. Radigan's position is a complete removal of the Company's 2.65% reduction in consumption, and my position remains the forecasted reduction in consumption is fully supported by the historical consumption patterns. Mr. Radigan concedes there could be correlation to water usage and variables, but has done nothing to show correlation. I discussed in my Rebuttal Testimony, water usage correlation to both rainfall and temperature. However, this is still not relevant in determining the declining usage trend which USI faces.

Mr. Radigan asserts that if the rainfall and temperature in the most recent six year period were consistent with average rainfall and temperature over a longer time period it would appear normalized. If it was inconsistent, it would not appear normalized. "Either way, Mr. Kersey provides no showing of the temperature and rainfall during those six years demonstrating that it is true." (AG Ex. 2.0: 88-95). Below is a demonstration of how something (rainfall) normalizes itself over time and why the same result is achieved if one was to normalize for every period or no periods, notice how the Sum and Mean are exactly the same in both instances.

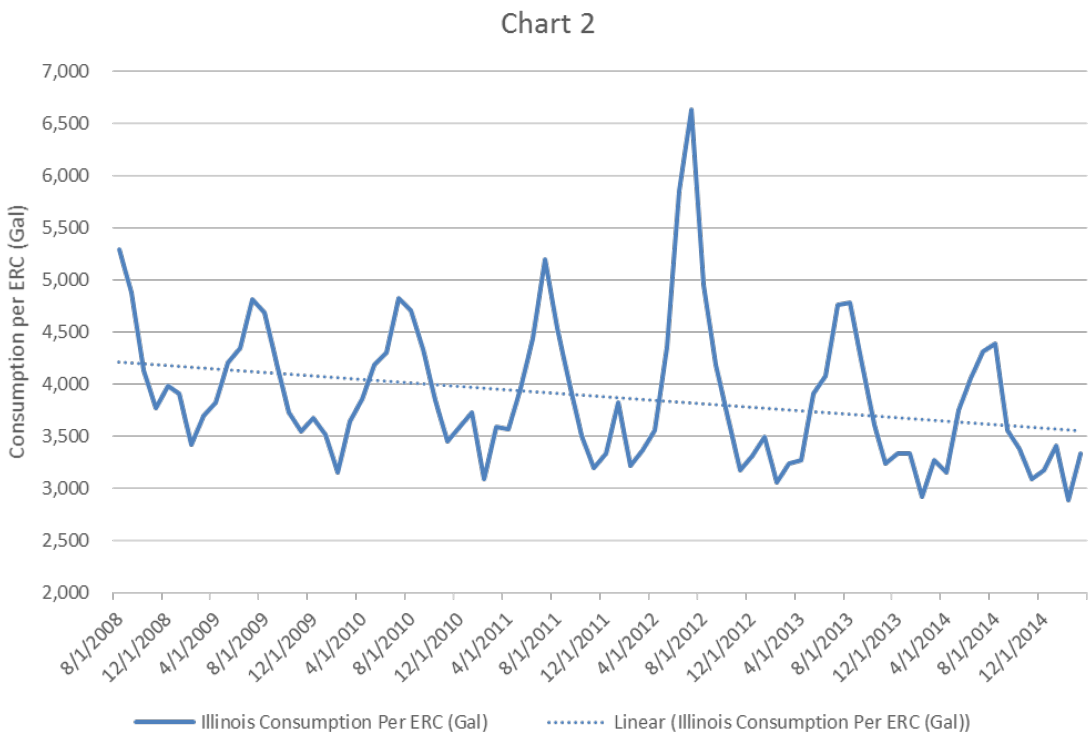
	Sample Rainfall (inches) [a]	# of Standard Deviations from the Mean [b]	Normalized Rainfall (inches) [c]
Day 1	1	(1.16)	2.29
Day 2	2	(0.26)	2.29
Day 3	3	0.64	2.29
Day 4	4	1.54	2.29
Day 5	3	0.64	2.29
Day 6	2	(0.26)	2.29
Day 7	1	(1.16)	2.29
Sum	16.00		16.00
Mean	2.29		2.29
Standard Deviation	1.11		

[c] Sample Rainfall - (# Standard Deviations from the Mean * Standard Deviation)

Below is a chart (Chart 1) depicting USI's consumption per ERC from August 2008 – July 2014 which was provided via the Company's response to AG data request 3.2. As is clearly seen by the linear trend line, the consumption trend is down. And as supported by the demonstration above, normalizing for every weather departure from the norm would not change the consumption decline trend.



Below is a chart (Chart 2) depicting USI's consumption per ERC from August 2008 – March 2015 which was provided via the Company's supplemental response to AG data request 3.2. Chart 2 contains the same data which was used to populate Chart 1, but has been updated for Consumption per ERC for the period August 2014 – March 2015. As is clearly seen by the linear trend line, the consumption trend continues downward as forecasted.



Lastly, I would like to address other issues that Mr. Radigan believes need to be "studied". "Namely, that consumption can vary greatly from one home to another depending on the number of bathrooms" (AG Ex. 2.0: 97-99). Although Mr. Radigan appears to be overlooking the fact that occupants in a home drive the usage of bathrooms, I did not address Mr. Radigan's irrational suggestion that the Company study the number of bathrooms in its customers' homes as it would not change the fact that water usage decline is a clear and expected trend.

Q: DOES THIS CONCLUDE YOUR PREPARED SURREBUTTAL TESTIMONY?

A: Yes, it does.

Docket No. 14-0741

USI Exhibit 14.0

Schedule 14.1

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Wed 1/28/2015 4:29 PM

Dimitry Neyzelman

RE: RE: 14-0741 DR to USI - MHE 4.03 Supplemental CONFIDENTIAL

To meverson@icc.illinois.gov; Seidel, W. Michael; Steve Lubertozzi; Justin P. Kersey; Brian Halloran

Cc Bridal, Richard; Cardoni, Jessica; Feeley, John; rjolly@atg.state.il.us; ssatter@atg.state.il.us; sdoshi@atg.state.il.us; kleiser@atg.state.il.us

Message | MHE 4.03 Supplemental - 2015 Salaries and Wages CONFIDENTIAL.xlsx (595 KB)

The password to the attached file is:
MHE 4.03 Supplemental - 2015 Salaries and Wages CONFIDENTIAL: [redacted]

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