STATE OF NEW HAMPSHIRE

PUBLIC UTILITIES COMMISSION

DW 04-184 / DW 04-196

In the Matter of:
Hampstead Area Water Company, Inc.
Petition to Acquire Assets and Incur Debt
and Petition for Permanent Rates

Direct Testimony

of

Jayson P. Laflamme
Utility Analyst III

March 16, 2005

New Hampshire Public Utilities Commission

Hampstead Area Water Company, Inc.

DW 04-184 / DW 04-196

Petition to Acquire Assets and Incur Debt
and Petition for Permanent Rates

Direct Testimony of Jayson P. Laflamme

Q. Would you please state your full name.

A. My name is Jayson P. Laflamme.

Q. By whom are you employed and what is your business address?

A. I am employed by the New Hampshire Public Utilities Commission (NHPUC) and my business address is 21 South Fruit Street, Suite 10, Concord, New Hampshire.

Q. What is your position at the NHPUC?

A. I am a Utility Analyst III in the Gas and Water Division.

Q. Please describe your duties at the NHPUC.

A. I am responsible for the evaluation of rate and financing filings, including the recommendation of changes in revenue levels that conform to regulatory methodologies. I represent Staff in meetings with company officials, outside attorneys and accountants relative to rate case and financing matters as well as the Commission's rules, policies and procedures.

Q. Would you please describe your educational background.

A. I received a Bachelor of Science Degree in Accounting from Lyndon State College in 1989. In 1998, I attended the NARUC Annual Regulatory Studies Program at Michigan

State University. In 2002, I attended the 22nd Annual Western Utility Rate School in San Diego, California.

Q. Would you please describe your work experience?

A. In 1989, I was hired as a Staff Accountant by Driscoll & Company, a CPA firm located in Littleton, New Hampshire. I performed audits, reviews and compilations as well as prepared tax returns for a variety of entities. I was eventually promoted to the position of Manager. In 1997, I was hired as a Utility Examiner in the Audit Division of the NHPUC. In that position, I participated in field audits of the books and records of regulated utilities in the electric, telecommunications, water, sewer and gas industries. I examined reports and filings submitted to the Commission by regulated utilities and performed rate of return analyses. In 2001, I was promoted to my current position as a Utility Analyst III.

Q. What is the purpose of your testimony?

A. My testimony will first provide Staff's recommendation with regard to Hampstead Area Water Company, Inc.'s (HAWC or the Company) request in docket DW 04-184 to incur debt in order to acquire the assets of a certain water system which was previously approved by the Commission in docket DW 03-150. My testimony will then provide Staff's recommendation with regard to HAWC's request in docket DW 04-196 for permanent rates for four systems including the one under consideration in DW 04-184 as well as three other systems which were previously approved by the Commission in docket DW 02-198.

Q. Please provide a brief summary of HAWC's petition in docket DW 04-184 as well as some background regarding the system under consideration in that docket.

A. On October 6, 2004, HAWC filed a petition with supporting attachments requesting approval to purchase the assets of the water system serving two condominium developments in the Town of East Kingston, New Hampshire known as "Cricket Hill / Maplevale Farms and Woods" and "Residences at Maplevale" (Cricket Hill / Maplevale). The petition also asked for authority to incur debt in order to purchase these assets. The Cricket Hill / Maplevale franchise was previously approved by Commission Order No. 24,299 (March 26, 2004) in docket DW 03-150. The system assets are currently owned by Lewis Builders Development, Inc. (Lewis Builders or LBD) which constructed the system. When fully built-out, the water system will serve a total of 106 condominium units as well as 22 additional subdivision lots. The Company's response to Staff Data Request 1-7 indicated that 73 customers were being served at Cricket Hill / Maplevale as of December 31, 2004. In the Settlement Agreement approved by Commission Order No. 24,299, HAWC agreed to file a petition to purchase the assets of Cricket Hill / Maplevale as well as request financing approval by July 1, 2004. This date was subsequently modified by the Stipulation in docket DW 02-128, which was approved by Commission Order No. 24,362 (August 19, 2004). Per that Stipulation, the filing date for these petitions was amended to be no more than 60 days from the date of the Commission's order in approving that Stipulation in DW 02-128.

Q. Did the Commission also approve rates in the DW 03-150 docket?

A. Yes. Commission Order No. 24,299 also approved an initial flat rate for the Cricket Hill / Maplevale system of $25.49 per customer per quarter to be implemented on a billsrendered basis on the date of the Commission’s order in DW 03-150 which was March 26, 2004.

Q. Please describe the system assets which HAWC is proposing to acquire?

A. The Cricket Hill / Maplevale water system assets which HAWC is proposing to acquire include the following: a well house; two bedrock wells; 435 feet of 4” water pipe extending from the well house to the main water line; pumps, piping and valves within the well house; two 25,000 gallon storage tanks; 6,825 feet of 4” and 2,860 feet of 3” transmission and distribution mains; 106 1” service lines.

Q. Are there any Cricket Hill / Maplevale system assets which HAWC is not proposing to acquire at this time?

A. Yes. There are 128 meters which HAWC will be purchasing separately from the other system assets. Per the Company’s response to Staff Data Request 2-1, the cost per meter is $273.53 for a total cost of approximately $35,012.

Q. What is the total construction cost of the Cricket Hill / Maplevale system assets under consideration for purchase in this docket?

A. Attachment 2 to the Company’s filing in DW 04-184 indicates a total construction cost of approximately $209,521 excluding meters. The Company also included copies of the Continuing Property Records (CPR’s) for the Cricket Hill / Maplevale system with its filing.

Q. Did Staff review these costs?

A. Yes. The Commission Audit Staff performed an examination of the CPR’s for the Cricket Hill / Maplevale system in order to verify that they corresponded to the various supporting documents. A discussion of this examination is contained in the Final Audit

Report for Hampstead Area Water Company, Inc. dated February 15, 2005. While the Audit Staff determined that the majority of the construction costs could be traced to the supporting documentation, a number of exceptions were found. Staff submitted data requests to the Company in this docket in an attempt to follow-up on the exceptions noted by the Audit Staff in their examination. While some of these exceptions were later resolved through the Company's responses to these data requests, some issues still remained especially with regard to certain inventory transfers from LBD and with regard to certain labor burden percentages used by the Company during construction.

Q. In light of these exceptions, what is Staff's recommendation?

A. A number of issues pertaining to record keeping and asset valuation arose during the course of both docket DW 02-128 and docket DW 02-198. Staff, the Company and the other parties to those dockets were able to work towards resolving these issues through the Settlement Agreements that were submitted to and approved by the Commission. It is Staff's belief that the Cricket Hill / Maplevale project is transitional in nature in that cost data and CPR's for that system were compiled during the time that these various asset valuation and record keeping issues were first coming to light but yet before a complete resolution of these issues had been reached. As will be discussed subsequently, the Company is proposing a rate base amount for the Cricket Hill / Maplevale assets that is substantially less than the original cost of construction. Given this, Staff believes that it would be pointless to pursue these issues further in this docket and is willing to accept the cost data submitted by the Company. Further, Staff has noted that the Company is making strides towards compliance with the Stipulation in docket DW 02-128 and is hopeful that the exceptions noted in DW 04-184 and prior dockets will be resolved in future filings submitted to the Commission.

Q. What is the purchase price being proposed by HAWC for the acquisition of the Cricket Hill / Maplevale system assets?

A. The Company's filing initially indicated a purchase price of $106,000. This amount was the product of the 106 condominium dwelling units multiplied by a $1,000 per residential unit "hook-up" fee which the Company has proposed. HAWC later amended the proposed purchase price to $128,000 in its response to Staff Data Request 1-1, where it stated that the number of residential dwelling units should be 128 instead of 106.

Q. Please explain how the $1,000 per residential unit "hook-up" fee was derived.

A. The concept of the residential unit hook-up fee has its basis in the Stipulation in docket DW 02-128 which was approved by Commission Order No. 24,362 (August 19, 2004). Section III.A.3 of that Stipulation indicated that under circumstances where Lewis Builders builds a new development and installs a water system which it intends to have HAWC operate, the purchase price of the water system assets will be based on a fixed fee per residential or commercial connection. The intent of this mechanism was to insure that any profit that may have been built into the construction cost of the water system assets by Lewis Builders would not be recognized in rate base since both Lewis Builders and HAWC have common ownership interests. With regard to the specific dollar amount proposed, the Company explained in its response to Staff Data Request 1-2: "*At the time of the Stipulation Agreement, HAWC was using $1,000 per connection for discussion purposes. The parties seemed to agree that $1,000 per connection was appropriate as long as the sum of the connection fees were less than the total cost of the water system.*

In this case, the sum of the connection fees is approximately 61% ($128,000 / $209,521) of the costs of the water system (exclusive of the costs of water meters).”

Q. Does Staff concur with the $1,000 per residential unit “hook-up” fee?

A. Yes. Given that the proposed purchase price for the Cricket Hill / Maplevale assets is an amount no greater than the actual cost of construction, Staff concurs with the $1,000 per residential unit hook-up fee in this case.

Q. How is HAWC proposing to record the acquisition of the Cricket Hill / Maplevale system on its books?

A. In accordance with Section III.A.3 of the Stipulation in docket DW 02-128, only the $128,000 purchase price of the Cricket Hill / Maplevale assets will be reflected in HAWC’s rate base. The Company has proposed to record the original construction cost of each asset category in the appropriate plant accounts. The difference between the original construction costs totaling $209,521 and the purchase price to be paid by HAWC in the amount of $128,000 will be recorded as Contributions in Aid of Construction (CIAC) in an amount totaling $81,521. Total CIAC will be pro-rated amongst the various plant accounts based on the original cost of construction. Attachment JPL-1 illustrates this accounting treatment.

Q. Does Staff agree with this accounting treatment?

A. Yes. Staff believes this accounting treatment meets the requirements of Section III.A.3 of the Stipulation in docket DW 02-128.

Q. What amount is HAWC seeking to borrow in order to finance this purchase of assets?

A. In its initial filing, HAWC requested permission to borrow $106,000, an amount which coincided with the original purchase price indicated in that filing. As discussed previously, the Company later amended the proposed purchase price to $128,000 and thus also amended the proposed financing to $128,000 as well.

Q. What are the terms of this financing?

A. The initial filing contained a copy of the $106,000 note payable (Attachment 9) dated September 1, 2004. The repayment terms called for payments of one one-hundred twentieth of principal to take place on the 10 subsequent anniversary dates of the note plus interest on the unpaid balance at an interest rate equal to 2.25% above the prime rate published in the Wall Street Journal on the last business day of each calendar year. Further, this note indicated that all outstanding principal and interest would be due and payable on the tenth anniversary of the note. Subsequently, however, along with the change in the amount of the note to $128,000, HAWC also changed the repayment terms of the note. The Company changed the term of the note from 10 years to 20 years, citing in its response to Staff Data Request 1-6 that the 20 year term was more appropriate because it more closely approximated the life of the assets and was better for cash flow and earnings purposes. The Company also revised the amortization of the loan to 240 equal monthly installments of principal and interest at rate equal to 2.25% above the prime rate published in the Wall Street Journal on the last business day of each calendar year. For 2005, the interest rate would be 7.50% based on a Wall Street Journal published prime rate of 5.25% as of December 31, 2004. The Company provided a copy of the amended note payable in its response to Staff Data Request 2-3(b) which is included in my testimony as Attachment JPL-2.

Q. Does Staff have any concerns with regard to the proposed financing?

A. Yes. HAWC is a completely debt financed company. HAWC's last filed Annual Report for the year ended December 31, 2003 reported total owners' equity of negative $389,195 while long-term debt amounted to $911,501. (See Attachment JPL-3) During 2004, the Company added to its long-term debt. In docket DW 02-128, the Company received approval in Commission Order No. 24,362 (August 19, 2004) for financing in the amount of $398,068 for the purchase of three supplemental systems (Bartlett Brook, Settler's Ridge and Cogswell Farms). In Commission Order No. 24,386 (October 22, 2004) in docket DW 04-132, HAWC received authorization to borrow an amount up to $1,383,887 in Drinking Water State Revolving Fund (SRF) financing for the construction of a water storage facility and other improvements. HAWC has also recently submitted a filing which has been docketed as DW 04-215 where it requests approval of financing in the amount of approximately $625,000 for additional water system acquisitions and improvements. Even though the majority of the outstanding loans are owed to HAWC's affiliate, Lewis Builders, Staff still has a concern with regard to the Company's heavily leveraged position and its associated risk. Further, much of HAWC's current debt is at relatively high interest rates ranging from 8.50% to 10.00%. Staff recommends that the Company investigate the possibility of refinancing its debt at lower interest rates. However, Staff is also concerned that HAWC's heavily leveraged position may make it prohibitive for obtaining more competitive financing.

Q. What are Staff's recommendations concerning HAWC's current financing request as well as concerning its overall level of debt financing?

A. Despite Staff's concerns with regard to HAWC's overall debt position, Staff is recommending that the Commission approve HAWC's current financing request for an amount up to $128,000 in order to purchase the proposed water system assets of the Cricket Hill / Maplevale system under the terms and conditions expressed in the draft note payable indicated as Attachment JPL-2. However, with regard to HAWC's overall debt situation, Staff recommends that the Company investigate its options with regard to refinancing. Staff also recommends that HAWC investigate the possibility of obtaining further capital injections from ownership in an effort to bring its debt to equity ratio closer to a more reasonable and prudent level. HAWC is a Company that has sustained net losses from its operations for a number of years, and it is clear that these operating losses have made it very difficult for the Company to make payments on some of its loans. In addition, these annual net losses are further eroding HAWC's already negative owners' equity position. Staff mainly attributes these net losses to the fact that the Company has not obtained rate increases for its systems for as long as, in some cases, 15 to 20 years. As provided in the Stipulation in DW 02-128, HAWC may file a new general rate case once it has fulfilled all of its compliance obligations in that Stipulation. Staff believes that the Company should file for new rates for all of its systems as soon as possible in order to facilitate a positive accumulation of funds in order to 1) handle its heavy debt burden, 2) further improve its debt to equity position, and 3) give the Company further options with regard to future financings.

Q. Are there any other documents pertaining to the purchase or financing which you have attached to your testimony?

A. Yes. HAWC's original filing mentioned an easement deed (Attachment 8) that had been conveyed by Peter A. Lewis to the Company but which was not included in the filing. In response to Staff Data Request 1-3, the Company provided a copy of this easement deed which is included in my testimony as Attachment JPL-4.

Q. Please summarize Staff's recommendations with regard to HAWC's requests in docket DW 04-184.

A. Staff recommends that the Commission authorize HAWC's purchase of the Cricket Hill / Maplevale system assets from LBD in an amount up to $128,000. Staff further recommends that the Commission authorize HAWC to incur debt up to an amount of $128,000 in order to finance the purchase of the Cricket Hill / Maplevale assets in the form of a note payable to LBD under the terms previously mentioned in my testimony.

Q. Turning attention now to docket DW 04-196, please provide a brief summary of HAWC's petition as well as the procedural background regarding the systems under consideration in this docket.

A. On October 19, 2004, HAWC submitted a petition with supporting testimony and schedules requesting approval for the establishment of permanent rates for the following four systems: Cricket Hill / Maplevale located in the Town of East Kingston, New Hampshire; Camelot Court located in the Town of Nottingham, New Hampshire; Cornerstone Estates (Cornerstone) located in the Towns of Sandown and Fremont, New Hampshire; and Lamplighter Estates (Lamplighter) located in the Town of Kingston, New Hampshire. As mentioned previously, the Cricket Hill / Maplevale franchise was approved by Commission Order No. 24,299 (March 26, 2004) in docket DW 03-150. That order also approved an initial rate of $25.49 per customer per quarter which was based on operation and maintenance costs only since the assets of that system had not yet been purchased by HAWC. The Camelot Court, Cornerstone and Lamplighter systems were approved by Commission Order No. 24,296 (March 19, 2004) in docket DW 02-198. No initial rates were established for those systems. The Stipulation approved by the Commission in docket DW 02-198 deferred consideration of permanent rates for the three systems until docket DW 02-128 was considered by the Commission. In the Stipulation approved by Commission by Order No. 24,362 (August 19, 2004) in docket DW 02-128, the parties agreed that HAWC would make a filing for permanent rates for the three systems within 60 days from the date of the Commission's order in that docket.

Q. Considering first the Cricket Hill / Maplevale system, please summarize the Company's request for permanent rates.

A. The Company's initial filing requested rates in order to generate annual revenues of $42,612. This translated into an annual charge per customer of $402.00. Upon realizing that its previous schedules for Cricket Hill / Maplevale were based on 106 customers rather than 128 customers, HAWC submitted revised schedules on January 12, 2005 showing an increase in the proposed revenue requirement to $47,616 but a decrease in the annual charge per customer to $372.00.

Q. What is the revenue requirement for the Cricket Hill / Maplevale system being proposed by Staff?

A. As indicated on Attachment JPL-5, Schedule CM-1, Staff is recommending a revenue requirement of $49,112. This is a $1,496 increase over the Company's proposed revenue requirement of $47,616. Staff's recommended revenue requirement is calculated on a total rate base of $161,134, as computed on Schedule CM-2 of Attachment JPL-5. An overall rate of return of 7.50% was applied to rate base resulting in an operating income requirement of $12,085 which is $1,496 greater than the proforma operating income of $10,589 calculated by Staff on Schedule CM-3 of Attachment JPL-5. There is no federal or state tax effect.

Q. Please explain how the 7.50% rate of return percentage was derived.

A. In the Company's original filing, HAWC applied the company-wide composite rate of return percentage of 8.97% to the rate base of Cricket Hill / Maplevale in order to derive its proposed income requirement. A calculation of this rate of return percentage was also included in the Company's filing. Staff questioned the Company with regard to the use of the company-wide rate of return when the majority of the Cricket Hill / Maplevale system's assets were to be financed by a single note payable which was discussed previously in my testimony regarding docket DW 04-184. In response to Staff Data Request 1-19, HAWC agreed that it was more appropriate to use the interest rate associated with the note payable for the purchase of the Cricket Hill / Maplevale assets as the rate of return for that system. As indicated in my discussion regarding docket DW 04-184, the interest rate for that note as of December 31, 2004 is 7.50%.

Q. Please explain why there is no federal or state tax effect in the determination of Staff's proposed revenue requirement.

A. The calculation of the tax effect percentage appears on Schedule 6 of Attachment JPL-5. On this schedule a tax rate of 0.00% is indicated for both the Federal Income Tax Rate as well as the NH Business Profits Tax Rate. The reason for this, with respect to the Federal

Income Tax Rate, is that HAWC is a “Subchapter-S” corporation, meaning that, in most cases, any taxable income that is generated by HAWC is not taxed for federal purposes at the corporate level but instead at the shareholder level. Because of this a Federal Income Tax Rate of 0.00% is indicated on Schedule 6, effectively resulting in a $0 Federal Income Tax effect. With respect to New Hampshire Business Profits Taxes, however, the “Subchapter-S” designation does not apply which would normally result in the recognition of state income taxes at the corporate level. However, in HAWC’s case, the Company has also recognized a consistent stream of net operating losses for the past several years which may be carried forward to subsequent years to offset any future taxable income. Staff believes that HAWC’s current accumulated net operating losses should be at such a level so as to enable it to not incur any state income tax liability for the next several years. Because of this, a NH Business Profits Tax Rate of 0.00% is also indicated on Schedule 6, effectively resulting in a $0 state income tax effect. It should be noted that, for the same reasons as stated above, no federal or state tax effect was applied to the revenue requirements of the other three systems under consideration in this docket.

Q. Please discuss the rate base amount calculated by Staff on Schedule CM-2 of Attachment JPL-5.

A. The “Per Company Filing” column shows the calculation of the Company’s proposed rate base in the amount of $136,575 which was contained in the revised schedules for Cricket Hill / Maplevale submitted by HAWC on January 12, 2005. The “Staff Proforma Adjustments” column summarizes Staff’s adjustments to the Company’s proposed rate base from Schedule CM-2A of Attachment JPL-5. Staff’s adjustments result in a

$24,559 net increase in the Company's proposed rate base to an amount of $161,134 as shown in the "Proforma Rate Base" column.

Q. Please explain Adjustment # 1 to Total Plant in Service.

A. Schedule CM-2B of Attachment JPL-5 was compiled by Staff as a representation of total plant in service and accumulated depreciation for the Cricket Hill / Maplevale system as of December 31, 2004 under a fully built-out scenario. The cost column was derived from copies of the Company's CPR's submitted with its filing in DW 04-184 with the exception of the amount for Meters and Meter Installation. An amount $28,994 reflecting 106 meters was indicated in the Company's CPR for meters. This amount was included in the Company's original filing as well. However, the Company's response to Staff Data Request 2-1 indicated that plant in service should reflect 128 meters rather than the 106 meters, therefore an additional $6,018 (22 meters x $273.53/meter) was reflected in the cost of meters on Schedule CM-2B and was included in Adjustment # 1 as well. The second part of Adjustment # 1 is to increase the Company's plant in service amount by an additional $5 so as to agree with Schedule CM-2B. The total of Adjustment # 1 is $6,023.

Q. Please explain Adjustment # 2 to Accumulated Depreciation.

A. Adjustment # 2 amends the Accumulated Depreciation balance which appeared in the Company's filing to the amount reflected in Schedule CM-2B. This adjustment results in an increase of $4,169 in Accumulated Depreciation which are the result of two changes included in Schedule CM-2B. The first of these changes stems from the increase in the cost of meters (Adjustment # 1) which increased the annual depreciation expense for meters by $271. The second change results from the fact that the Company's filing only indicated one full year of depreciation in rate base when, according to the Company's response to Staff Data Request 1-8, the Cricket Hill / Maplevale assets were placed in service in January 2003. Therefore an additional half-year of depreciation amounting to $3,898 is reflected in Schedule CM-2B for depreciation expense taken during the first year of asset service to customers.

Q. Please explain Adjustment # 3 to Contributions in Aid of Construction (CIAC).

A. The Company's filing reflected a purchase price for the Cricket Hill / Maplevale system based on 106 service connections at $1,000 per connection, or $106,000. HAWC's response to Staff Data Request 1-1 indicated that the purchase price for the Cricket Hill / Maplevale system should be increased to $128,000 in order to reflect 128 total service connections in this system. Adjustment # 3 decreases CIAC by $22,000 to an amount of $81,521 in order to increase the amount reflected in the Company's rate base by an additional $22,000 for the 22 additional connections used in the determination of the appropriate purchase price for the Cricket Hill / Maplevale system. The effect of this adjustment is shown on Schedule CM-2C which shows Staff's determination of CIAC and Accumulated Amortization of CIAC as of December 31, 2004. The amounts appearing in the "CIAC" column were compiled based on the information contained in Attachment JPL-1.

Q. Please explain Adjustment # 4 to Accumulated Amortization – CIAC.

A. Adjustment # 4 amends the Accumulated Amortization – CIAC balance which appeared in the Company's filing to the amount reflected in Schedule CM-2C. This adjustment results in an increase of $557 in Accumulated Amortization – CIAC which are the result of two changes reflected in Schedule CM-2C. The first of these changes stems from the increase in the decrease in CIAC recorded in Adjustment # 3 which, in turn, decreases the annual amortization expense for CIAC by $653. The second change is due to the fact that the Company's filing only indicated one full year of amortization in rate base when, according to the Company's response to Staff Data Request 1-8, the Cricket Hill / Maplevale assets were placed in service in January 2003. Therefore, an additional half-year of amortization amounting to $1,210 is reflected in Schedule CM-2B for amortization of CIAC recorded during the first year of asset service to customers. The net of these two changes results in the $557 total adjustment.

Q. Please discuss Adjustment # 5 to Cash Working Capital.

A. Adjustment # 5 records the change in the Cash Working Capital calculation resulting from Staff's proforma adjustments to the Cricket Hill / Maplevale operation and maintenance expenses. Schedule CM-3 of Attachment JPL-5 shows that total operation and maintenance expenses after Staff's proforma adjustments is $30,114. This results in an Adjusted Cash Working Capital Allowance of $6,188 which is a $149 increase over the amount that was submitted by the Company in its filing.

Q. Please discuss the Operating Income Statement for Cricket Hill / Maplevale presented on Schedule CM-3 of Attachment JPL-5.

A. The "Per Company Filing" column presents the amounts proposed by HAWC for operating revenues and expenses for the Cricket Hill / Maplevale system which result in a net operating income amount of $12,252. Staff made a total of five adjustments to the Company's proposed operating expenses for this system which are summarized in the next two columns of Schedule CM-3. Together, Staff's adjustments result in a decrease of $1,663 in the Company's proposed net operating income for an amount of $10,589.

This is detailed in the "Proforma Operating Income" column of Schedule CM-3. The last two columns entitled "Revenue Deficiency" and "Operating Income Requirement" are intended to show in detail the effect of Staff's calculated revenue requirement from Schedule CM-1 on the Cricket Hill / Maplevale system's net operating income.

Q. Please explain how the Company derived its operation and maintenance expense amounts for the Cricket Hill / Maplevale system.

A. Because this system was not yet fully built out and a full year of operational data was not available at the time the Company made its filing, HAWC, for the most part, relied upon the most current data available from its Colby Pond system in order to develop estimates for the annual operation and maintenance expenses of a fully built-out Cricket Hill / Maplevale system.

Q. What is Staff's position with regard to the use of these estimates in this circumstance?

A. Under normal circumstances, Staff would not concur with the use of estimates in the determination of the operating activity of a water system because of the subjective nature of estimates. The Commission strongly prefers the use of historical cost data because it provides a more objective measure for evaluating a company's activity. However, with this being the first rate case filed for Cricket Hill / Maplevale, accurate historical data was simply not available regarding its annual anticipated expenditures. Staff performed a detailed analysis of the estimates and projections utilized by the Company to derive the proposed operation and maintenance expenses for this system. It is Staff's conclusion that these estimates and projections are, for the most part, both reasonable and prudent. Therefore, Staff agrees with the use of these estimates in this circumstance. It should be noted that HAWC also used estimates for the operating data of the other three systems under consideration in this docket and for the same reasons as expressed above, Staff also concurs with the Company's use of estimates for those systems as well.

Q. Please explain Adjustment # 6 to Customer Accounts Expenses.

A. This adjustment resulted from the HAWC's response to Staff Data Request 2-12 where it revised the original estimate for the Cricket Hill / Maplevale system's Customer Records and Collection Expense from $292 to $500 for an increase of $208.

Q. Please explain Adjustment # 7 to Administrative & General Expenses.

A. The Company's response to Staff Data Request 2-13 increased the original estimate for General Rents Expense from $309 to $827 for an increase of $518.

Q. Please discuss Adjustment # 8 to Depreciation Expense.

A. As a result of the changes to fixed plant which are reflected in Schedule CM-2B and explained previously under my discussions regarding Adjustments # 1 and # 2, the annual Depreciation Expense of $7,526 proposed by the Company in its filing should be increased by $271 to an amount of $7,797. The revised amount is reflected under the "2004 Depreciation Expense" column on Schedule CM-2B.

Q. Please discuss Adjustment # 9 to Amortization Expense – CIAC.

A. As a result of the changes to CIAC which are reflected in Schedule CM-2C and which were previously explained under my discussions regarding Adjustments # 3 and # 4, the annual Amortization Expense – CIAC of $3,074 should be decreased by $653 to an amount of $2,421. The revised amount is reflected under the "2004 Amortization Expense" column on Schedule CM-2C.

Q. Please explain Adjustment # 10 to Property Taxes.

A. The Company's original filing contained an estimate for the State Utility Property Tax which was based on the amount of Net Plant in Service reflected in rate base multiplied by the appropriate rate of $6.60 per $1,000 of valuation. The amount proposed by HAWC for the Cricket Hill / Maplevale system was $1,524. However, the previous adjustments made to fixed plant and depreciation and which are reflected in Schedule CM-2B also necessitate an adjustment to this expense. The revised calculation results in a State Utility Tax of $1,537 which is $13 higher than the amount proposed by the Company.

Q. Please discuss Schedule CM-3B of Attachment JPL-5.

A. The purpose of this schedule is to display the tax effect of Staff's adjustments to Net Operating Income which were previously discussed. Adjustments # 6 through # 10 result in a $1,663 reduction in the Net Operating Income amount proposed by the Company in its filing. However, there is no tax effect resulting from these adjustments for either federal or state tax purposes as shown on Schedule CM-3B. With regard to federal income taxes, HAWC is a "Subchapter-S" corporation, meaning, that in most cases, any taxable income that is generated by HAWC is not taxed at the corporate level but instead at the shareholder level. Because of this a federal tax rate of 0.00% is indicated on Schedule CM-3B which effectively results in $0 federal income taxes. With regard to the New Hampshire Business Profits, the "Subchapter-S" designation does not apply which would normally result in the recognition of state taxes at the corporate level. However, in HAWC's case, the Company has recognized a consistent stream of net operating losses for the past several years which may be carried forward to future years to offset any recognizable taxable income. Staff believes that HAWC's current accumulated net operating losses should be at such a level so as to enable it to not incur any state tax liability for the next several years. Because of this, a state tax rate of 0.00% is also indicated on Schedule CM-3B which effectively results in $0 state income taxes.

Q. Please discuss Schedule CM-3C of Attachment JPL-5.

A. This schedule is based on the detailed operating revenue and expense amounts proposed by HAWC for the Cricket Hill / Maplevale system in its filing and mirrors to a certain extent Schedule CM-3 but includes more account detail. The "Per Company Filing" column reflects the detailed account estimates included in the Company's schedules for Cricket Hill / Maplevale but grouped according to operation and maintenance expense category, ie, Source of Supply, Pumping Expenses, Water Treatment Expenses, etc. The middle two columns show, in detail, Staff's adjustments to the Company's proposed income and expense amounts including the calculated revenue deficiency from Schedule CM-1. The "Operating Income Requirement" column provides a detailed presentation of Staff's proposed income requirement as well as the resulting net operating income for the Cricket Hill / Maplevale system.

Q. How does the revenue requirement proposed by Staff for the Cricket Hill / Maplevale system translate into rates for customers?

A. Schedule CM-4 shows a calculation of rates for the Cricket Hill / Maplevale system based on the $49,112 revenue requirement proposed by Staff. This schedule shows an annual charge per customer of $384 ($96 per quarter) under this revenue requirement scenario, based on the estimate of consumption as discussed below. Staff's calculations maintained the $100 annual base charge per customer proposed by the Company in its filing and calculated a $3.31 per 100 cubic foot consumption rate. The consumption amounts utilized in the calculation of these rates were estimates derived from customer usage at the Company's Colby Pond system. As indicated in the Company's response to Staff Data Request 2-6, actual annual consumption amounts for the Cricket Hill / Maplevale system were not available since scheduled meter readings were not initiated until the spring of 2004. Although Staff does not usually accept estimated amounts for consumption, in this circumstance with this being the first rate case filed for this system, Staff concurs with the use of estimates in this circumstance.

Q. Before giving specific attention to the remaining three systems under consideration in this docket, please discuss the rate of return proposed by the Company for these systems.

A. In its filing, HAWC proposed a rate of return of 8.97%. The Company included schedules showing how this percentage was derived. In order to calculate this rate the Company considered the balances of its owners' equity accounts and long-term debt as of December 31, 2003. However, because total owners' equity amounted to a negative $389,195, that component essentially did not figure into the determination of HAWC's overall rate of return. Instead, the Company's cost of debt calculated at 8.97% became the number applied by the Company.

Q. What is Staff proposing for a rate of return to be applied to the Camelot Court, Cornerstone and Lamplighter systems?

A. Staff is proposing an overall rate of return of 8.14%. The calculation of this rate appears on Schedules 5 and 5A of Attachment JPL-5. Staff's calculation is essentially the same as that originally proposed by the Company with the only exception being the inclusion of an additional note payable which was recently approved by the Commission. This note payable, identified as Loan # 11 on Schedule 5A, was for the purchase of the assets of the Bartlett Brook, Settler's Ridge and Cogswell Farm systems and was approved by Commission Order No. 24,362 (August 19, 2004) in docket DW 02-128. The interest rate of 6.25% indicated for this note was derived based upon the Stipulation in docket DW 02-198 which fixed the initial interest rate of this note for a three year period at a percentage no higher than 2.25 points above the Wall Street Journal prime interest rate as of December 31, 2003 which Staff found stood at 4.00%.

Q. Have all of the loans that were included in the determination of an overall rate of return been approved by the Commission?

A. No. Specifically, Staff has found that loan #'s 2, 3, 4, 5, 6 and 9 either require initial Commission approval or Commission approval for certain changes in the terms of loans that have been previously approved.

Q. Has the Company filed a petition with the Commission requesting approval of previously incurred debt?

A. Yes. On November 23, 2004, HAWC filed a petition with the Commission which in part requested Commission approval for certain debt that had been previously incurred but not approved by the Commission. This petition, which was docketed as DW 04-215, was filed by the Company in compliance with provision III.L.2 of the Stipulation approved in docket DW 02-128. The Company's filing is currently being reviewed by Staff.

Q. What is Staff's recommendation with regard to the inclusion of the previously unapproved debt in the determination of the Company's rate of return in the instant proceeding?

A. At this time, Staff concurs with the inclusion of these debt issues in the calculation of the Company's rate of return. However, if the Commission were to ultimately deny any of those debt issues in docket DW 04-215, there could be an impact on rates approved in the instant proceeding. Staff will be prepared to provide a calculation of that potential impact if such an event were to occur.

Q. Now turning our attention to Camelot Court; please give a brief description of this system and summarize the Company's request for permanent rates.

A. The Camelot Court system serves a 20-lot subdivision in Nottingham, New Hampshire. The system is not fully built-out and per the Company's response to Staff Data Request 1-7, was only serving ten customers as of December 31, 2004. The Company's filing requested rates for this system in order to generate annual revenues of $9,837. This translates into an annual charge per customer of $491.87.

Q. What is the revenue requirement for the Camelot Court system being proposed by Staff?

A. As indicated on Schedule CC-1 of Attachment JPL-5, Staff is recommending a revenue requirement of $9,102. This is a $735 decrease from the Company's proposed revenue requirement of $9,837. Staff's recommended revenue requirement is calculated on a total rate base of $5,110, as computed on Schedule CC-2 of Attachment JPL-5. An overall rate of return of 8.14%, as calculated on Schedule 5, was applied to rate base resulting in an operating income requirement of $416 which is $735 less than the proforma operating income of $1,151 calculated by Staff on Schedule CC-3 of Attachment JPL-5. There is no federal or state tax effect for the same reasons that were given in my discussion regarding the Cricket Hill / Maplevale system.

Q. Please discuss the rate base amount calculated by Staff on Schedule CC-2 of Attachment JPL-5.

A. The "Per Company Filing" column shows the calculation of the Company's proposed rate base for Camelot Court in the amount of $5,330 contained in HAWC's filing. The "Staff Proforma Adjustments" column summarizes Staff's adjustments to the Company's proposed rate base from Schedule CC-2A. Staff's adjustments result in a $220 net reduction in the Company's proposed rate base for an amount of $5,110 as detailed in the "Proforma Rate Base" column.

Q. Please explain Adjustment # 11 to Accumulated Depreciation.

A. Schedule CC-2B of Attachment JPL-5 was put together by Staff as a representation of total plant in service and accumulated depreciation for Camelot Court as of December 31, 2004 under a fully built-out scenario. The cost column totaling $143,641 agrees with the amounts for Camelot Court contained in the Stipulation that was approved in docket DW 02-198. The depreciation rates contained in this schedule were those that were proposed by the Company in its filing with the exception of the depreciation rate pertaining to transmission & distribution mains where a 2.20% rate was originally proposed. However, in its response to Staff Data Request 2-5, HAWC indicated that this depreciation rate should be changed to 2.00% in order to agree with the NHPUC typical service life and rate for transmission & distribution mains that is indicated in the "Small Water Company Information Booklet" which is distributed by the NHPUC. This change is reflected in both Schedule CC-2B and Adjustment # 11 and results in a $76 decrease in accumulated depreciation. A second change included in Schedule CC-2B and reflected in Adjustment # 11 is due to the fact that the Company's filing only indicated one full year of depreciation in rate base when, according to the Company's response to Staff Data Request 1-8, the Camelot Court assets were placed in service in August 2003. Therefore an additional half-year of depreciation amounting to $2,816 is reflected in Schedule CC-2B for depreciation expense taken during the first year the Camelot Court assets were placed in service. Both of these changes result in a net increase of $2,741 to accumulated depreciation which is reflected in Adjustment # 11.

Q. Please explain Adjustment # 12 to Accumulated Amortization – CIAC.

A. Schedule CC-2C of Attachment JPL-5 was put together by Staff as a representation of Contributions in Aid of Construction (CIAC) and Accumulated Amortization – CIAC for Camelot Court as of December 31, 2004 under a fully built-out scenario. The CIAC column totaling $139,842 agrees with the amounts for Camelot Court contained in the Stipulation that was approved in docket DW 02-198. The amortization rates contained in this schedule were those that were proposed by the Company in its filing with the exception of the amortization rate for transmission & distribution mains which was changed from 2.20% to 2.00% for the same reason expressed under the discussion of Adjustment # 11. This change is reflected Adjustment # 12 and results in a $76 decrease in accumulated amortization – CIAC. Schedule CC-2C and Adjustment # 12 also provide for an additional half-year of amortization amounting to $2,731 in order to reflect that the Camelot Court assets were placed in service in August 2003 as was also previously discussed under Adjustment # 11. Both of these changes result in a net increase of $2,655 to Accumulated Amortization – CIAC for the Camelot Court system which is reflected in Adjustment # 12.

Q. Please discuss Adjustment # 13 to Cash Working Capital.

A. Adjustment # 13 records the change in the Cash Working Capital calculation resulting from Staff's adjustments to the Camelot Court system's operation and maintenance expenses which will be discussed in detail later in my testimony. Schedule CC-3 of Attachment JPL-5 indicates that Total Operation and Maintenance Expenses after Staff adjustments is $7,622. This results in an Adjusted Cash Working Capital Allowance of $1,566 which is a $135 decrease from the amount that submitted by the Company in its filing of $1,701.

Q. Please discuss the Operating Income Statement for Camelot Court presented on Schedule CC-3 of Attachment JPL-5.

A. The "Per Company Filing" column presents the amounts proposed by HAWC for operating revenues and expenses for the Camelot Court system which result in a net operating income amount of $478. Staff made a total of five adjustments to the Company's proposed operating expenses for this system which are summarized in the next two columns of Schedule CC-3. Combined, Staff's adjustments result in an increase of $673 in the Company's proposed net operating income for an amount of $1,151. This is detailed in the "Proforma Operating Income" column of Schedule CC-3. The last two columns entitled "Revenue Surplus" and "Operating Income Requirement" are intended to show in detail the effect of Staff's calculated revenue requirement from Schedule CC-1 on the Camelot Court system's net operating income.

Q. Please explain how the Company derived its proposed operation and maintenance expense amounts for the Camelot Court system.

A. Because this system was not yet fully built out and a full year of operational data was not available at the time the Company made its filing, HAWC estimated the annual operation and maintenance expenses for a fully built-out Camelot Court system based on a partial year of activity for this system ended August 31, 2004.

Q. Does Staff concur with the use of these estimates?

A. Staff has previously expressed its position regarding the Company's use of estimates in this docket under the discussion regarding the Cricket Hill / Maplevale system. Staff performed a detailed analysis of the estimates and projections utilized by the Company to derive the proposed operation and maintenance expenses for Camelot Court. It is Staff's conclusion that these estimates and projections are, for the most part, both reasonable and prudent.

Q. Please explain Adjustment # 14 to Water Treatment Expenses.

A. HAWC's filing included an estimate for Operation & Labor Expense – Water Treatment in the amount of $1,200 for the Camelot Court system. Staff found that this estimate was much greater than the estimates for the same account provided for the Cornerstone system ($500) as well as the Lamplighter system ($750) even though these systems served more customers than Camelot Court. In its response to Staff Data Request 2-9, the Company stated: "*The first year costs of water testing is generally higher than the second year due to the number of water test(s) and the type of water test(s). The "Actual 8/31/04" treatment expense for Camelot Court reflects some of the higher first year costs. The "Actual 8/31/04" treatment expenses for Cornerstone and Lamplighter reflect lower* *second year costs.*" Based on this response, Staff is proposing to reduce the Operation & Labor Expense – Water Treatment estimate for Camelot Court to an amount that is more reflective of the expense that would normally be incurred for this account on an annual basis. In order to determine an appropriate expense level, Staff relied upon the amount recorded for this expense by the Colby Pond system as of December 31, 2004 which was included in the Company's response to Staff Data Request 1-9. Using the amount provided of $4,071, Staff determined that this translated into a per customer cost of approximately $158. This amount was then multiplied by the 20 full build-out customer base of Camelot Court which resulted in a projected annual Operation & Labor Expense – Water Treatment of $515. Therefore, Adjustment # 14 reduces the Company's original estimate of $1,200 by $685 to the expense level calculated by Staff.

Q. Please explain Adjustment # 15 to Administrative & General Expenses.

A. The Company's response to Staff Data Request 2-13 increased the original estimate for General Rents Expense for Camelot Court from $100 to $129 for an increase of $29.

Q. Please discuss Adjustment # 16 to Depreciation Expense.

A. As a result of the change in the depreciation rate for transmission & distribution mains that is reflected in Schedule CC-2B and was explained previously in my discussion regarding Adjustments # 11, the annual Depreciation Expense of $5,708 proposed by the Company in its filing should be reduced by $76 to an amount of $5,632.

Q. Please discuss Adjustment # 17 to Amortization Expense – CIAC.

A. As a result of the change in the amortization rate for transmission & distribution mains that is reflected in Schedule CC-2C and which was previously explained in my discussion regarding Adjustments # 12, the annual Amortization Expense – CIAC of $5,537 proposed by the Company in its filing should be reduced by $76 to an amount of $5,461.

Q. Please explain Adjustment # 18 to Property Taxes.

A. The Company's original filing contained an estimate for the State Utility Property Tax which was based on the amount of Net Plant in Service reflected in rate base multiplied by the appropriate rate of $6.60 per $1,000 of valuation. The amount proposed by HAWC for the Camelot Court system was $910. However, Adjustment # 11 made to accumulated depreciation and which is reflected in Schedule CC-2B also necessitates an adjustment to this expense. The revised calculation results in a State Utility Tax of $892 which is $18 less than the amount proposed by the Company.

Q. What is the purpose of Schedule CC-3B of Attachment JPL-5?

A. The purpose of this schedule is to display the cumulative tax effect of Staff's adjustments to the net operating income of Camelot Court. Adjustments # 14 through # 18 result in a $673 increase in the net operating income amount proposed by the Company in its filing. However, for the same reasons provided in my discussion regarding the tax effect calculated for the Cricket Hill / Maplevale system, there is no tax effect resulting from Staff's adjustments to the operating income of the Camelot Court system for either federal or state tax purposes as indicated on Schedule CC-3B.

Q. What is the purpose of Schedule CC-3C of Attachment JPL-5?

A. This schedule is similar to Schedule CM-3C for Cricket Hill / Maplevale and is discussed in my previous testimony regarding that system.

Q. How does the revenue requirement proposed by Staff for the Camelot Court system translate into rates for customers?

A. Schedule CC-4 shows a calculation of rates for the Camelot Court system based on the $9,102 revenue requirement proposed by Staff. This schedule shows an annual charge per customer of $455 ($114 per quarter) under this revenue requirement scenario. Staff's calculations maintained the $100 annual base charge per customer proposed by the Company in its filing and in addition calculated a $4.14 per 100 cubic foot consumption rate. The consumption amounts utilized in the calculation of these rates were estimates derived from customer usage at the Company's Colby Pond system. For the same reasons expressed in a similar discussion regarding the calculation of the Cricket Hill / Maplevale system rates, Staff concurs with the use of consumption estimates in this circumstance.

Q. Next, turning our attention to Cornerstone; please give a brief description of this system and summarize the Company's request for permanent rates.

A. The Cornerstone system serves a 37-lot subdivision in Sandown, New Hampshire. The system is fully built-out and per the Company's response to Staff Data Request 1-7, was serving 54 customers as of December 31, 2004. The Company's filing requested rates for this system in order to generate annual revenues of $15,584. This translates into an annual charge per customer of $421.20.

Q. If the Cornerstone system was built to serve a 37-lot subdivision, please explain why it was serving 54 customers at the end of 2004?

A. The Company provided the following explanation in its response to Staff Data Request 2-4: "*The Company has recently started to provide water service to an additional phase of*

Cornerstone. The additional phase includes 21 new customers. The Company has not yet purchased/financed the infrastructure associated with the additional phase. For purposes of setting a rate for Cornerstone, the Company believes that its proposed rate is appropriate because the rate base, the rate of return and the operating expenses are associated with the 37 customers." Staff, at this point, concurs with HAWC's explanation but encourages the Company to file for purchase/financing approval of the additional system assets related to this new Cornerstone phase as soon as possible. Staff also suggests that the Company submit periodic reports to the Commission regarding the Cornerstone system's earnings and expenses so that it can be determined whether the rate for Cornerstone that is established in this proceeding is, if fact, appropriate.

Q. What is the revenue requirement for the Cornerstone system being proposed by Staff?

A. As indicated on Schedule CS-1 of Attachment JPL-5, Staff is recommending a revenue requirement of $15,291. This is a $293 decrease from the Company's proposed revenue requirement of $15,584. Staff's recommended revenue requirement is calculated on a total rate base of $9,180, as computed on Schedule CS-2 of Attachment JPL-5. An overall rate of return of 8.14%, as calculated on Schedule 5, was applied to rate base resulting in an operating income requirement of $747 which is $293 less than the proforma operating income of $1,040 calculated by Staff on Schedule CC-3 of Attachment JPL-5. There is no federal or state tax effect for the Cornerstone system for the same reasons that were given in my discussion regarding the revenue requirement calculated for the Cricket Hill / Maplevale system.

Q. Please discuss the rate base amount calculated by Staff on Schedule CS-2 of Attachment JPL-5.

A. The "Per Company Filing" column shows the calculation of the Company's proposed rate base for Cornerstone in the amount of $9,375 contained in HAWC's filing. The "Staff Proforma Adjustments" column summarizes Staff's adjustments to the Company's proposed rate base from Schedule CS-2A. Staff's adjustments result in a $195 net reduction in the Company's proposed rate base for an amount of $9,180 which is detailed in the "Proforma Rate Base" column.

Q. Please explain Adjustment # 19 to Accumulated Depreciation.

A. Schedule CS-2B of Attachment JPL-5 was put together by Staff as a representation of total plant in service and accumulated depreciation for Cornerstone as of December 31, 2004. The cost column totaling $354,485 agrees with the amounts for Cornerstone contained in the Stipulation that was approved in docket DW 02-198. The depreciation rates contained in this schedule were those that were proposed by the Company in its filing with the exception of the depreciation rate pertaining to transmission & distribution mains where a 2.20% rate was originally proposed. In its response to Staff Data Request 2-5, HAWC indicated that this depreciation rate should be changed to 2.00% in order to agree with the NHPUC typical service life and rate for transmission & distribution mains that is indicated in the "Small Water Company Information Booklet" which is distributed by the NHPUC. This change is reflected in both Schedule CS-2B and Adjustment # 19 and results in a $299 decrease in accumulated depreciation. A second change included in Schedule CS-2B and reflected in Adjustment # 19 is due to the fact that the Company's filing only indicated one full year of depreciation in rate base when, according to the

Company's response to Staff Data Request 1-8, the Camelot Court assets were placed in service in August 2003. Therefore, an additional half-year of depreciation amounting to $6,146 is reflected in Schedule CS-2B for depreciation expense taken during the first year the Cornerstone assets were placed in service. Both of these changes result in a net increase of $5,847 to accumulated depreciation which is reflected in Adjustment # 19.

Q. Please explain Adjustment # 20 to Accumulated Amortization – CIAC.

A. Schedule CS-2C of Attachment JPL-5 was put together by Staff as a representation of Contributions in Aid of Construction (CIAC) and Accumulated Amortization – CIAC for Cornerstone as of December 31, 2004. The CIAC column totaling $347,285 agrees with the amounts for Cornerstone contained in the Stipulation that was approved in docket DW 02-198. The amortization rates contained in this schedule were those that were proposed by the Company in its filing with the exception of the amortization rate for transmission & distribution mains which was changed from 2.20% to 2.00% for the reason expressed under the discussion of Adjustment # 19. This change is also reflected Adjustment # 20 and results in a $299 decrease in accumulated amortization – CIAC. Schedule CS-2C and Adjustment # 20 also provide for an additional half-year of amortization amounting to $5,984 in order to reflect that the Cornerstone assets were placed in service in August 2003 as was also previously discussed under Adjustment # 19. Both of these changes result in a net increase of $5,685 to Accumulated Amortization – CIAC for the Cornerstone system which is reflected in Adjustment # 20.

Q. Please discuss Adjustment # 21 to Cash Working Capital.

A. Adjustment # 21 records the change in the Cash Working Capital calculation resulting from Staff's adjustments to the Cornerstone system's operation and maintenance expenses which will be discussed in more detail later in my testimony. Schedule CS-3 of Attachment JPL-5 indicates that Total Operation and Maintenance Expenses after Staff adjustments is $12,002. This results in an Adjusted Cash Working Capital Allowance of $2,466 which is a $33 decrease from the amount that was submitted by the Company in its filing of $2,499.

Q. Please discuss the Operating Income Statement for Cornerstone presented on Schedule CS-3 of Attachment JPL-5.

A. The "Per Company Filing" column presents the amounts proposed by HAWC for operating revenues and expenses for the Cornerstone system which result in a net operating income amount of $840. Staff made a total of four adjustments to the Company's proposed operating expenses for this system which are summarized in the next two columns of Schedule CS-3. Staff's adjustments result in an increase of $200 in the Company's proposed net operating income for an amount of $1,040. This is detailed in the "Proforma Operating Income" column of Schedule CS-3. The last two columns entitled "Revenue Surplus" and "Operating Income Requirement" are intended to show in detail the effect of Staff's calculated revenue requirement from Schedule CS-1 on the Cornerstone system's net operating income.

Q. Please explain how the Company derived its proposed operation and maintenance expense amounts for the Cornerstone system.

A. Because a full year of operational data for this system was not available at the time the Company made its filing, HAWC estimated the annual operation and maintenance expenses for the Cornerstone system based on a partial year of activity ended August 31, 2004.

Q. Does Staff concur with the use of these estimates?

A. Staff has previously expressed its position regarding the Company's use of estimates in this docket under the discussion regarding the operation and maintenance expenses for the Cricket Hill / Maplevale system. Staff performed a detailed analysis of the estimates and projections utilized by the Company to derive the proposed operation and maintenance expenses for Cornerstone. It is Staff's conclusion that these estimates and projections are, for the most part, both reasonable and prudent.

Q. Please explain Adjustment # 22 to Administrative & General Expenses.

A. The Company's response to Staff Data Request 2-13 reduced the original estimate for General Rents Expense for Cornerstone from $400 to $239 for a decrease of $161.

Q. Please discuss Adjustment # 23 to Depreciation Expense.

A. As a result of the change in the depreciation rate for transmission & distribution mains that is reflected in Schedule CS-2B and was explained previously in my discussion regarding Adjustments # 19, the annual Depreciation Expense of $12,590 proposed by the Company in its filing should be reduced by $299 to an amount of $12,291.

Q. Please discuss Adjustment # 24 to Amortization Expense – CIAC.

A. As a result of the change in the amortization rate for transmission & distribution mains that is reflected in Schedule CS-2C and which was previously explained in my discussion regarding Adjustments # 20, the annual Amortization Expense – CIAC of $12,266 proposed by the Company in its filing should be reduced by $299 to an amount of $11,967.

Q. Please explain Adjustment # 25 to Property Taxes.

A. The Company's original filing contained an estimate for the State Utility Property Tax which was based on the amount of Net Plant in Service reflected in rate base multiplied by the appropriate rate of $6.60 per $1,000 of valuation. The amount proposed by HAWC for the Cornerstone system was $2,257. However, Staff Adjustment # 19 which was made to accumulated depreciation and reflected in Schedule CS-2B also necessitates an adjustment to this expense. The revised calculation results in a State Utility Tax of $2,218 which is $39 less than the amount proposed by the Company.

Q. What is the purpose of Schedule CS-3B of Attachment JPL-5?

A. The purpose of this schedule is to display the cumulative tax effect of Staff's adjustments to the net operating income of Cornerstone. Adjustments # 22 through # 25 result in a $200 net increase in the net operating income amount proposed by the Company in its filing. However, for the same reasons provided in my discussion regarding the tax effect calculated for the Cricket Hill / Maplevale system, there is no tax effect resulting from Staff's adjustments to the operating income of the Cornerstone system for either federal or state tax purposes as indicated on Schedule CS-3B.

Q. What is the purpose of Schedule CS-3C of Attachment JPL-5?

A. This schedule is similar to Schedule CM-3C for Cricket Hill / Maplevale and is discussed in my previous testimony regarding that system.

Q. How does the revenue requirement proposed by Staff for the Cornerstone system translate into rates for customers?

A. Schedule CS-4 shows a calculation of rates for the Cornerstone system based on the $15,291 revenue requirement proposed by Staff. This schedule shows an annual charge per customer of $413 ($103 per quarter) under this revenue requirement scenario. Staff's calculations maintained the $100 annual base charge per customer proposed by the Company in its filing and calculated a $3.65 per 100 cubic foot consumption charge. The consumption amounts utilized in the calculation of these rates were estimates derived from customer usage at the Company's Colby Pond system. For the same reasons expressed in a similar discussion regarding the calculation of the Cricket Hill / Maplevale system rates, Staff concurs with the use of the Colby Pond consumption rates to estimate the Cornerstone system consumption in this circumstance.

Q. Finally, turning our attention to Lamplighter; please give a brief description of this system and summarize the Company's request for permanent rates.

A. The Lamplighter system serves a 56-unit condominium development in Kingston, New Hampshire. The system is fully built-out and per the Company's response to Staff Data Request 1-7, was serving 56 customers as of December 31, 2004. The Company's filing requested permanent rates for this system in order to generate annual revenues of $17,436. This translates into an annual charge per customer of $311.36.

Q. What is the revenue requirement for the Lamplighter system being proposed by Staff?

A. As indicated on Schedule LL-1 of Attachment JPL-5, Staff is recommending a revenue requirement of $17,035. This is a $401 decrease from the Company's proposed revenue requirement of $17,436. Staff's recommended revenue requirement is calculated on a total rate base of $13,407, as computed on Schedule LL-2 of Attachment JPL-5. An overall rate of return of 8.14%, as calculated on Schedule 5, was applied to rate base resulting in an operating income requirement of $1,092 which is $401 less than the proforma operating income of $1,493 calculated by Staff on Schedule LL-3 of Attachment JPL-5. There is no federal or state tax effect for the Lamplighter system for the same reasons that were given in my discussion regarding the revenue requirement calculated for the Cricket Hill / Maplevale system.

Q. Please discuss the rate base amount calculated by Staff on Schedule LL-2 of Attachment JPL-5.

A. The "Per Company Filing" column shows the calculation of the Company's proposed rate base for Lamplighter in the amount of $13,708 contained in HAWC's filing. The "Staff Proforma Adjustments" column summarizes Staff's adjustments to the Company's proposed rate base from Schedule LL-2A. Staff's adjustments result in a $301 net reduction in the Company's proposed rate base for an amount of $13,407 which is detailed in the "Proforma Rate Base" column.

Q. Please explain Adjustment # 26 to Accumulated Depreciation.

A. Schedule LL-2B of Attachment JPL-5 was put together by Staff as a representation of total plant in service and accumulated depreciation for Lamplighter as of December 31, 2004. The cost column totaling $165,734 agrees with the amounts for Lamplighter contained in the Stipulation that was approved in docket DW 02-198. Schedule LL-2B and Adjustment # 26 reflect an amendment to accumulated depreciation resulting from the fact that the Company's filing only indicated one full year of depreciation in rate base when, according to the Company's response to Staff Data Request 1-8, the Lamplighter assets were placed into service in August 2003. Therefore, an additional half-year of depreciation amounting to $3,287 is reflected in both Schedule LL-2B and Adjustment #

26 to reflect the depreciation expense for the first year the Lamplighter assets were placed into service.

Q. Please explain Adjustment # 27 to Accumulated Amortization – CIAC.

A. Schedule LL-2C of Attachment JPL-5 was put together by Staff as a representation of Contributions in Aid of Construction (CIAC) and Accumulated Amortization – CIAC for Lamplighter as of December 31, 2004. The CIAC column totaling $154,534 agrees with the amounts for Lamplighter contained in the Stipulation that was approved in docket DW 02-198. Schedule LL-2C and Adjustment # 27 provide for an additional half-year of amortization amounting to $3,575 in order to reflect that the Lamplighter assets were placed in service in August 2003 as was also previously discussed under Adjustment # 26.

Q. Please discuss Adjustment # 28 to Cash Working Capital.

A. Adjustment # 28 records the change in the Cash Working Capital calculation resulting from Staff's adjustments to the Lamplighter system's operation and maintenance expenses which will be discussed in more detail later in my testimony. Schedule LL-3 of Attachment JPL-5 indicates that Total Operation and Maintenance Expenses after Staff adjustments is $14,421. This results in an Adjusted Cash Working Capital Allowance of $2,963 which is a $49 decrease from the amount that was submitted by the Company in its filing of $3,012.

Q. Please discuss the Operating Income Statement for Lamplighter presented on Schedule LL-3 of Attachment JPL-5.

A. The "Per Company Filing" column presents the amounts proposed by HAWC for operating revenues and expenses for the Lamplighter system which result in a net operating income amount of $1,230. Staff made a total of two adjustments to the Company's proposed operating expenses for this system which are described in detail on Schedule LL-3A but summarized in the adjustment columns on Schedule LL-3. Staff's adjustments result in an increase of $263 in the Company's proposed net operating income for an amount of $1,493 which is detailed in the "Proforma Operating Income" column of Schedule LL-3. The last two columns entitled "Revenue Surplus" and "Operating Income Requirement" are intended to show, in detail, the effect of Staff's calculated revenue requirement from Schedule LL-1 on the Lamplighter system's net operating income.

Q. Please explain how the Company derived its proposed operation and maintenance expense amounts for the Lamplighter system.

A. Because a full year of operational data for this system was not available at the time the Company made its filing, HAWC estimated the annual operation and maintenance expenses for the Lamplighter system based on a partial year of activity ended August 31, 2004.

Q. Does Staff concur with the use of these estimates?

A. Staff has previously expressed its position regarding the Company's use of estimates in this docket under the discussion regarding the operation and maintenance expenses for the Cricket Hill / Maplevale system. Staff performed a detailed analysis of the estimates and projections utilized by the Company to derive the proposed operation and maintenance expenses for Lamplighter. It is Staff's conclusion that these estimates and projections are, for the most part, both reasonable and prudent.

Q. Please explain Adjustment # 29 to Administrative & General Expenses.

A. The Company's response to Staff Data Request 2-13 reduced HAWC's original estimate for General Rents Expense for Lamplighter from $600 to $362 for a decrease of $238.

Q. Please explain Adjustment # 30 to Property Taxes.

A. The Company's original filing contained an estimate for the State Utility Property Tax which was based on the amount of Net Plant in Service reflected in rate base multiplied by the appropriate rate of $6.60 per $1,000 of valuation. The amount proposed by HAWC for the Lamplighter system was $1,043. However, Staff Adjustment # 26 to accumulated depreciation also necessitated an adjustment to property tax expense. The revised calculation results in a State Utility Tax of $1,018 which is $25 less than the amount originally proposed by the Company.

Q. What is the purpose of Schedule LL-3B of Attachment JPL-5?

A. The purpose of this schedule is to display the cumulative tax effect of Staff's adjustments to the net operating income of Lamplighter. Adjustments # 29 and # 30 together result in a $263 net increase in the net operating income amount proposed by the Company in its filing. However, for the same reasons provided in my discussion regarding the tax effect calculated for the Cricket Hill / Maplevale system, there is no tax effect resulting from Staff's adjustments to the operating income of the Lamplighter system for either federal or state tax purposes as indicated on Schedule LL-3B.

Q. What is the purpose of Schedule LL-3C of Attachment JPL-5?

A. This schedule is similar to Schedule CM-3C for Cricket Hill / Maplevale which is discussed in my previous testimony regarding that system.

Q. How does the revenue requirement proposed by Staff for the Lamplighter system translate into rates for customers?

A. Schedule LL-4 shows a calculation of rates for the Lamplighter system based on the $17,035 revenue requirement proposed by Staff. This schedule shows an annual charge per customer of $304 ($76 per quarter) under this revenue requirement scenario. Staff's calculations maintained the $100 annual base charge per customer proposed by the Company in its filing and calculated a $2.38 per 100 cubic foot consumption charge. The consumption amounts utilized in the calculation of these rates were estimates derived from the actual recorded customer usage at the Company's Colby Pond system. For the same reasons expressed in a similar discussion regarding the calculation of the Cricket Hill / Maplevale system rates, Staff concurs with the use of the Colby Pond consumption amounts to project the Lamplighter system's customer consumption rate.

Q. Does this conclude your direct testimony?

A. Yes.