

**IN THE TENNESSEE PUBLIC UTILITY COMMISSION
AT NASHVILLE, TENNESSEE**

IN RE:)	
)	
APPLICATION OF TENNESSEE)	
WATER SERVICE, INC. FOR)	DOCKET NO. 19-00028
ADJUSTMENT OF RATES AND)	
CHARGES, AND MODIFICATIONS TO)	
CERTAIN TERMS AND CONDITIONS)	
FOR THE PROVISION OF WATER)	
SERVICE.)	
)	
)	
)	

**PRE-FILED DIRECT SUPPLEMENTAL TESTIMONY
OF
DANTE M. DeSTEFANO**

**ON BEHALF OF
TENNESSEE WATER SERVICE, INC.**

September 16, 2019

1 **Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS ADDRESS?**

2 **A.** My name is Dante M. DeStefano, and my business address is 4494 Parkway Plaza
3 Boulevard, Suite 375, Charlotte NC 28217.

4 **Q. ARE YOU THE SAME DANTE M. DESTEFANO WHO SUBMITTED DIRECT**
5 **AND REBUTTAL TESTIMONY IN THIS PROCEEDING?**

6 **A.** Yes, I am.

7 **Q. WHAT IS THE PURPOSE OF YOUR SUPPLEMENTAL TESTIMONY?**

8 **A.** The purpose of my testimony is 1) To confirm responses for two particular questions
9 raised at the September 9, 2019 hearing, 2) to elaborate on the level of financial impact of
10 the proposed Regulatory Liability of Attorney General witness Hal Novak, 3) to support a
11 reasonable basis for a Regulatory Liability to be created in this proceeding due to under-
12 insured assets of Tennessee Water Service (“TWS”).

13 **Q. ARE YOU ADOPTING ANY EXHIBITS WITH THE SUBMISSION OF THIS**
14 **SUPPLEMENTAL TESTIMONY?**

15 **A.** Yes. I am adopting Exhibit 4, TWS Late Filed Exhibits in support of testimony given at
16 the September 9, 2019 hearing.

17 **Q. COMPANY WITNESSES MENDENHALL AND HEIGEL WERE ASKED**
18 **DURING THE SEPTEMBER 9TH HEARING HOW LONG TWS HAS**
19 **OPERATED THE CHALET VILLAGE WATER SYSTEM. CAN YOU**
20 **CONFIRM THE COMPANY’S RESPONSE?**

1 **A.** Yes. Per the Company's petition in the 2019 Emergency Proceeding, TWS was granted
2 its original Certificate of Convenience and Necessity in January 1984 in Docket No. U-
3 83-7240.

4 **Q. COMPANY WITNESSES MENDENHALL AND HEIGEL WERE ALSO ASKED**
5 **HISTORICAL PROPERTY INSURANCE PREMIUMS PAID BY THE**
6 **COMPANY PRIOR TO THE NOVEMBER 2016 GATLINBURG WILDFIRES.**
7 **CAN YOU PROVIDE AN ESTIMATE OF THIS FIGURE?**

8 **A.** Yes. Based on the above start date of January 1984, the Company operated the Chalet
9 Village water system for approximately 33 years at the time of the Gatlinburg Wildfires.
10 Using the property premium allocation of \$529 as noted in Mr. Mendenhall's rebuttal
11 testimony, this results in a rough estimate of \$17,457 in total property insurance
12 premiums over that 33 year period of operation. This number is likely higher than actual
13 premiums paid, as it doesn't account for inflation over that time nor the potential for
14 higher insured values in prior years.

15 **Q. CAN YOU PLEASE PROVIDE SUPPORT FOR THE FINANCIAL**
16 **IMPLICATIONS OF THE ESTABLISHMENT OF A REGULATORY**
17 **LIABILITY AS PROPOSED BY MR. NOVAK?**

18 **A.** The Company has calculated that imposing a Regulatory Liability in the amount of
19 \$757,006 would result in a ROE impact of 654 basis points, which is more than half the
20 proposed ROE in this proceeding. Please see Attachment 1 to this testimony for support
21 of the calculation.

1 **Q. PLEASE DESCRIBE THE COMPANY'S BASIS OF VALUE FOR INSURING ITS**
2 **ASSETS.**

3 **A.** The Company utilizes an estimated replacement cost value to insure its assets. The
4 estimates are provided from the Company's operations department. These estimates
5 represent what cost can reasonably be expected to be incurred if an insured asset requires
6 a complete replacement in the normal course of business.

7 The age of the insured asset is a significant consideration in estimating replacement cost.

8 If the asset was recently placed in service, the original cost of the asset can be prioritized
9 in the estimation determination. If the insured asset is materially aged, the Company's
10 operations staff considers other known, recently completed projects which best
11 approximate the scope and nature of what would be required to replace the insured asset.

12 Therefore, the Company consistently leverages recently-experienced actual project costs
13 as its basis for estimating a reasonable replacement cost for an insured asset. This is
14 necessary as it best reflects current economic and operating conditions, including but not
15 limited to contractor rates, materials, engineering considerations, and asset function and
16 use. In contrast, utilizing the aged asset's original cost would poorly reflect current
17 contractor costs and the modern standard materials required for a rebuild.

18 **Q. PLEASE EXPLAIN WHERE THE COMPANY ERRED IN ITS REPLACEMENT**
19 **COST VALUATION IN INSURING ITS ASSETS IN ADVANCE OF THE**
20 **GATLINBURGE WILDFIRES.**

21 **A.** First, in renewing its annual property insurance policy, the Company did not include the
22 Piney Butt booster site assets on the list of scheduled assets in its insurance policy.

1 Second, although the Wellhouse #1 (Clubhouse) booster site was included on the list of
2 scheduled assets on the insurance policy, the Company did not set a reasonable estimated
3 replacement cost for those site assets.

4 **Q. WHAT SHOULD THE COMPANY HAVE BEEN REASONABLY EXPECTED**
5 **TO HAVE INCLUDED IN ITS INSURANCE COVERAGE OF ASSETS IN THE**
6 **CHALET VILLAGE SYSTEM?**

7 **A.** The Company should have included the Piney Butt and Clubhouse booster site assets at a
8 reasonable replacement cost based on the best information known at the time of policy
9 renewal. Any best estimate can only take into account information available to the
10 Company at the time of policy renewal (i.e., late summer 2016). As such, the best
11 information available for estimating a reasonable replacement cost for these TWS assets
12 would have been the Sugar Mountain Booster Station project in North Carolina
13 concluding in June 2016. This project is noted in Mr. Mendenhall's rebuttal testimony
14 and described in further detail in Mr. Mendenhall's supplemental testimony

15 **Q. WHAT HAS THE COMPANY PROPOSED AS AN ADJUSTMENT TO ITS**
16 **REVENUE REQUIREMENT IN THIS PROCEEDING, TO ACCOUNT FOR THE**
17 **UNDER-INSURING OF TWS'S ASSETS AT THE TIME OF THE**
18 **GATRLINBURG WILDFIRES?**

19 **A.** The Company has proposed to create a Regulatory Liability in the amount of \$382,016 to
20 be included in rate base, with an annual amortization credit to income of \$5,730.

21 **Q. HOW DID THE COMPANY DERIVE THE AMOUNT OF THIS REGULATORY**
22 **LIABILITY?**

1 **A.** As noted above, the Company should have been expected to use recent experience with
2 similar replacement projects to estimate a reasonable replacement cost in its property
3 insurance policy renewal. Mr. Mendenhall's supplemental testimony enumerates the
4 basis for utilizing the Sugar Mountain Booster Replacement project as a reasonable proxy
5 for the Piney Butt and Clubhouse booster sites. As the Sugar Mountain project cost of
6 \$216,008 was not properly utilized to estimate insurance coverage for the two TWS
7 booster sites, the Company proposes to calculate a Regulatory Liability of \$432,016 (the
8 Sugar Mountain Booster Project cost times two TWS sites), less the property insurance
9 deductible of \$50,000, resulting in a Regulatory Liability of \$382,016.

10 **Q. WHY IS THE COMPANY REMOVING THE DEDUCTIBLE AMOUNT FROM**
11 **THE REPLACEMENT COST ESTIMATION OF THE TWS BOOSTER SITES?**

12 **A.** Regardless of the level of replacement cost coverage in the property insurance policy, had
13 the Company filed a claim for recovery of damages from the Gatlinburg Wildfires, the
14 policy deductible would not have been recovered from the insurance provider and would
15 be paid by the Company. That is, the Company could not be made fully whole for its
16 losses, even had the replacement cost coverage matched the actual final costs to replace
17 the assets.

18 **Q. DOES MR. NOVAK'S PROPOSED REGULATORY LIABILITY CONSIDER**
19 **THE INEVITABILITY OF THE DEDUCTIBLE'S VALUE BEING ABSORBED**
20 **BY THE COMPANY?**

1 **A.** No. Mr. Novak’s proposed Regulatory Liability is based on the full actual costs to
2 replace the two TWS booster sites, with no accounting for the property policy’s
3 deductible.

4 **Q.** **DOES THIS CONCLUDE YOUR TESTIMONY?**

5 **A.** Yes, it does. However, I reserve the right to update or amend this testimony upon receipt
6 of additional data or other information that may become available.

ATTACHMENT 1

Capital Structure, Position of Attorney General

	Rate Base	Ratio	Cost	RoR	Operating Income
Equity	520,971	50.00%	10.50%	5.25%	54,702
Debt	520,971	50.00%	5.04%	2.52%	26,257
Total	1,041,942	100.00%		7.77%	80,959

Adjustments: 757,006 Regulatory Liability

[1] 1,798,948 Adj Rate Base

[2] 80,959 Adj Operating Income

Adjusted Combined Capital Structure, Impact of Regulatory Liability

4.50% Adj RoR - [2] / [1]

	Rate Base	Ratio	Cost	RoR	Operating Income
Equity	899,474	50.00%	3.96%	1.98%	35,625
Debt	899,474	50.00%	5.04%	2.52%	45,333
Total	1,798,948	100.00%		4.50%	80,959

Rate Base Change 757,006 -6.54% ROE Lag - Operating Loss