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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.	)	
	)	
	)	
	)	

DIRECT TESTIMONY
OF
DANTE M. DeSTEFANO

ON BEHALF OF
TENNESSEE WATER SERVICE, INC.

March 22, 2019

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

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

Q. WHERE ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am Financial Planning and Analysis Manager for Tennessee Water Service, Inc. (“TWS” OR “Company”) in Tennessee and for Carolina Water Service of North Carolina ("CWSNC"), both of which are subsidiaries of Utilities, Inc. (“UI”).

Q. WHAT IS YOUR EDUCATIONAL AND PROFESSIONAL BACKGROUND?

A. I have been employed by CWSNC since October 2018. I graduated from Rutgers University with a Major in Accounting and am a Certified Public Accountant in the state of New Jersey. Prior to joining CWSNC, I was employed by American Water Works for 10 years - first as a Senior Accountant in the Accounting Department for two years, then in the Rates and Regulatory Department for eight years. During my last eight years with American Water, my duties consisted of preparing and assisting in regulatory filings and related activities for the Eastern Division. My responsibilities included preparing work papers and exhibits, providing testimony in support of rate applications and other regulatory filings, and addressing rate and tariff related matters.

Q. WHAT ARE YOUR DUTIES WITH TENNESSEE WATER SERVICE, INC.?

A. My primary responsibilities include forecasting, budgeting, and financial analysis for the Company. I am also responsible for the oversight of gathering data and preparation of rate cases, filing applications for rate cases, and providing data request responses for support of rate case filings.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is 1) to explain the preparation and structure of the filed exhibits and schedules, 2) identify the historical test year and attrition year, 3) detail the impacts of the Company's 2017 Emergency Petition and the Tax Cuts and Jobs Act ("TCJA"), 4) explain the Company's plan for implementing the proposed revenue requirement, 5) describe the pro-forma adjustments to rate base, 6) summarize the pro-forma capital structure, and 7) discuss updates to the TWS tariff.

Q. PLEASE DETAIL THE COMPANY'S SUPPORTING EXHIBITS AND SCHEDULES IN THIS FILING.

A. The Company's general rate case filing includes the following exhibits:

Exhibit 1 – Income Statement

Exhibit 2 – Rate Base

Exhibit 3 – Balance Sheet

Exhibit 4 – Capital Structure and Retention Factor

Exhibit 5 –Rate Base Return

Exhibit 6 – Total Revenue Requirement

Exhibit 7 – Proposed Tariff

Exhibit 8 – Testimony of Catherine E. Heigel

Exhibit 9 – Testimony of J. Bryce Mendenhall

Exhibit 10 – Testimony of Dante M. DeStefano

Exhibit 11 – Testimony of Anthony Gray

Exhibit 12 – Testimony of Jared Deason

The Company submits the following schedules to support its filing:

Schedule A – Pro-Forma Present and Proposed Revenues, Rate Design, and Customer Bill Comparisons

Schedule B – Pro-Forma Plant Additions

Schedule C – Pro-Forma Plant ADIT

Schedule D – Pro-Forma Deferred Charges

Schedule E – 2017 and 2018 Operating Losses

Schedule F – Return on Replacement Capital Investment

Schedule G – Pro-Forma O&M Expense Adjustments

Schedule H – Pro-Forma Purchased Water Expense

Schedule I – Pro-Forma Salary & Wages, Payroll Taxes

Q. PLEASE EXPLAIN THE CALCULATION OF THE COMPANY'S PROPOSED REVENUE REQUIREMENT.

A. TWS utilizes the rate base-rate of return method for computing its revenue requirement. This means that the proposed rate of return is multiplied by the pro-forma rate base to obtain an operating income level. Then, operating expenses are added to the computed operating income, and income tax and other operating gross-ups are calculated to determine the required revenue level, or revenue requirement, to produce the calculated operating income. The Company has included the new federal income tax rate of 21%, the Tennessee state income tax rate of 6.5%, the 0.425% regulatory fee, and an uncollectible expense rate in the gross-up formula.

Q. PLEASE DESCRIBE THE COMPANY'S TEST YEAR AND ATTRITION YEAR IN THIS PROCEEDING.

A. The Company is utilizing a Test Year of the twelve months ending September 30, 2018. TWS selected this Test Year period for several reasons. First, the Company selected a period that would allow for adequate time between the end of the Test Year and the rate case filing date to review historical activity and identify the nature and level of pro-forma adjustments. Additionally, TWS recognizes that much of its activities since the November 2016 Wildfire (the "Wildfire") are not necessarily representative of normalized operations for its water system, and therefore a significant amount of pro-forma adjustment would be required to any selected Test Year period. The Company endeavored to reflect a normalized level of operating expenses for its revenue requirement, which is better demonstrated by pre-Wildfire levels of expenses versus post-Wildfire expenses. Thus, utilizing a twelve-month period ending September 30th allowed historical twelve-month periods ending September 30th that occurred before the Wildfire to be leveraged for per-customer pro-forma determinations, without the "noise" of Wildfire-influenced activities.

The Company is utilizing an Attrition Year of the twelve months ending December 31, 2020 in this proceeding. A vital factor in the Company's selection of this Attrition Year period is the ability to include projected customer reconnections that can be used for supporting pro-forma present rate revenue levels. Identifying a reasonable pro-forma customer count into the next calendar year boosts the present revenue levels due to anticipated further customer reconnections, which helps mitigate the per-customer impact of the proposed revenue requirement to be borne by the customer base. In addition, utilizing a calendar year Attrition Year period allows a natural, clean flow to the Company's proposed rate phase-in plan, as well as management of the existing Operational Cost Pass-Through Mechanism and filing of required periodic reports.

Q. PLEASE EXPLAIN TWS'S BOOK ADJUSTMENTS ON EXHIBIT 1.

A. The Company removed the accrual of 2017 Operating Losses from Miscellaneous Revenues, as this amount is requested to be amortized to the income statement in this proceeding. TWS also removed $1,820 from Maintenance and Repair expense related to tank painting amortizations that will conclude before the Attrition Year. Salaries & Wages and Operating Expense Charged to Plant included a one-time adjustment for labor that occurred prior to the Test Year and thus was removed from the respective Test Year book amounts.

Q. PLEASE SUMMARIZE THE COMPANY'S 2017 EMERGENCY PETITION, INCLUDING THE KEY AUTHORIZED PROVISIONS PER THE TPUC.

A. On September 25, 2017, TWS filed a petition seeking emergency relief in the form of three monthly surcharges, an operational cost pass-through mechanism, and a deferral of costs and uncollectible revenues for potential future recovery. The deferral components consisted of operating losses beginning in 2017, returns on capital projects to restore the water system from its Wildfire damage incurred, and filing and processing costs related to the petition.

The Commission Final Order was issued February 21, 2018. The Order authorized certain deferrals and other actions for TWS: 1) deferral of actual operating losses incurred, beginning January 1, 2017, 2) deferral of return on capital projects necessary to repair Wildfire damage and restore the water system to operational status, 3) deferral of up to $30,000 of reasonable and necessary rate filing expenses, 4) increase of the TWS monthly base charge per active customer from $18.70 to $25.70, 5) establishment of an Interim Emergency Operational Cost Pass-Through Mechanism ("IEOCPTM") to address increases or decreases in costs for purchased water and power, 6) requirement to file a base rate case petition by July 1, 2019.

Q. HOW HAS TWS CONSIDERED THESE PROVISIONS IN THIS FILING?

A. The Company is filing the current base rate case request in order to comply with the required filing of a general rate case by July 1, 2019. The pro-forma present rate revenues are calculated using the $25.70/month base charge as authorized in the 2017 petition. TWS has also calculated the operating losses for 2017 and 2018, as well as the return on replacement asset additions as of their respective in-service dates, net of retirements and accumulated depreciation. These regulatory asset balances, as well as the costs incurred for the filing and processing of the 2017 petition, are proposed to be amortized over five years. Please see Schedules D, E, and F for more detail on these deferral calculations.

As the operating loss calculations have effectively captured increased costs for purchased water and power, the Company has yet to submit a filing for the IEOCPTM. Please see the proposed tariff, beginning on Sheet No. 13, for the Company's requested modifications to the IEOCPTM.

Q. WHAT IS THE PROPOSED REVENUE REQUIREMENT FOR TWS?

A. The Company proposes a revenue requirement of $469,767, an increase of 177% over pro-forma present rate revenues of $169,323.

Q. PLEASE DESCRIBE HOW TWS PLANS TO IMPLEMENT THE PROPOSED REVENUE REQUIREMENT?

A. In an effort to mitigate the initial impact of the proposed revenue requirement on customers, the Company proposes to initiate a three-year rate plan phase-in, which would break up the revenue increase into three rate changes, effective each January 1st for 2020, 2021, and 2022. The Company also requests that 2019 operating losses be deferred, and 60 days after new base rates are effective January 1, 2020 the Company will file its 2019 operating loss calculation in order to initiate a temporary surcharge, effective July 1, 2020. Please see Schedule A for the pro-forma present rate revenues and proposed phase-in rate design and revenues, as well as a comparison of average customer bills.

Q. PLEASE EXPLAIN THE PRO-FORMA ADJUSTMENTS TO RATE BASE.

A. The Company has reflected continued depreciation of the Test Year end depreciable plant and continued amortization of the Test Year end Contributions in Aid of Construction, through the mid-point of the Attrition Year. In addition, the Cash Working Capital balance was adjusted to reflect 1/8th of the pro-forma expense levels. Pro-forma plant additions, net of retirements, accumulated depreciation and accumulated deferred income taxes, are included as pro-forma adjustments to rate base. Please see Schedules B and C for the list of pro-forma projects and resulting calculated rate base adjustments. Pro-forma plant additions consist of service lines, meters, and meter installations due to projected continued reconnections to the mid-point of the Attrition Year, as well as two booster station projects that will be completed after the end of the Test Year and an upgraded SCADA system.

Q. PLEASE EXPLAIN THE IMPACTS TO THE COMPANY OF THE TAX CUTS AND JOBS ACT.

A. On December 22, 2017, President Donald Trump signed into law the Federal Tax Cuts and Jobs Act, or TCJA. The most impactful portion of the TCJA was the reduction of the federal corporate tax rate from 35% to 21%. This portion not only impacts the current tax rate for corporations but also impacts the deferred income taxes recorded on the Company's books prior to the TCJA. The second significant component of the TCJA is the fact that contributed plant is now treated as a form of income and subject to the corporate income tax.

The Company has reflected the 21% federal tax rate in this filing where applicable for purposes of computing revenue requirement. In addition, the Company remeasured its Accumulated Deferred Income Tax Liability as of December 31, 2017, with the excess deferred balance due to the tax rate change reclassified as a regulatory liability. This excess deferred balance consists of what the Internal Revenue Service ("IRS") tax code refers to as "protected" (i.e., subject to tax normalization rules) and "unprotected" deferrals. The Company has thus computed an amortization period of 59 years for the protection portion of the excess deferred balance consistent with IRS normalization rules, and proposes a five year amortization for the unprotected portion, consistent with the regulatory asset deferral amortization proposals described earlier in my testimony.

In addition, the Company proposes to update tariff Sheet No. 1.1 for Contributions in Aid of Construction, to reflect the change in effective federal income tax rate at 21% as stated in the TCJA. Please see Exhibit 7 for the proposed TWS tariff.

Q. WHAT IS THE COMPANY'S PROPOSED CAPITAL STRUCTURE?

A. The Company's filing includes a 50%/50% split for long-term debt and equity. This ratio is consistent with the recent history of the TWS's parent, Utilities, Inc. TWS is a wholly owned subsidiary of UI, which raises capital for its subsidiaries. Accordingly, adopting UI's capital structure to determine the overall cost of capital for TWS is appropriate. As shown in Exhibit 4, the Company is utilizing a pro-forma cost of long-term debt of 5.04%, and proposing a return on equity of 10.50%. The capital structure results in a rate of return of 7.77% and pre-tax rate of return of 9.63%.

Q. WHAT CHANGES DOES THE COMPANY PROPOSE TO THE EXISTING TWS TARIFF, IN ADDITION TO THOSE REFERENCED ABOVE?

A. The Company proposes changing certain language on Sheet Nos. 5, 7, and 11 related to metered service and fire service to more accurately reflect the required building codes and nature of service TWS provides to the Chalet Village system.

TWS also proposes certain changes to Sheet No. 13 through 17 to modify the language and calculations of the IEOCPTM, authorized in Docket No. 17-000108. First, the Company recommends removing "Interim Emergency" from the mechanism's name, in order to utilize the mechanism on a going-forward basis after new base rates and authorized expense levels are effective. Likewise, the Company proposes to modify the language related to Base Period and Base Period OCPTM Costs on Sheet No. 13. This change would allow the authorized expense levels in this proceeding to be utilized for reconciliation with actual Review Period expenses on a going-forward basis. The Company has modified the first paragraph on Sheet No. 17 accordingly to reflect the updated reconciliation process.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

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

STATE OF New Jersey)

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County of Atlantic)

PAUL A MARTIN
Notary Public - State of New Jersey
My Commission Expires Nov 26, 2023

DATED this 21st day of March, 2019.

Dante DeStefano

SUBSCRIBED AND SWORN TO before me this 21st day of March, 2019.

Notary Public for the State of New Jersey