Witness CCS - 2
Exhibit CCS-2

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

	)	Docket No.01-035-01
In the Matter of the Application of	)	
PacifiCorp for Approval of its	)	PRE-FILED DIRECT TESTIMONY OF
Proposed Electric Rate Schedules	)	HELMUTH W. SCHULTZ, III
and Electric Service Regulations	)	FOR THE COMMITTEE OF
	)	CONSUMER SERVICES

June 4, 2001

Non-Confidential

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INTRODUCTION

Q. WHAT IS YOUR NAME, OCCUPATION AND BUSINESS ADDRESS?

A. My name is Helmuth W. Schultz, III. I am a Certified Public Accountant licensed in the State of Michigan and a Senior Regulatory Analyst in the firm of Larkin & Associates, PLLC, Certified Public Accountants, with offices at 15728 Farmington Road, Livonia, Michigan 48154.

Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCIATES.

A. Larkin & Associates, PLLC, is a Certified Public Accounting and Regulatory Consulting firm. The firm performs independent regulatory consulting primarily for public service/utility commission staffs and consumer interest groups (public counsels, public advocates, consumer counsels, attorneys general, etc.). Larkin & Associates, PLLC, has extensive experience in the utility regulatory field as expert witnesses in over 400 regulatory proceedings including numerous water and sewer, gas, electric and telephone utility cases.

Q. HAVE YOU PREPARED AN APPENDIX WHICH DESCRIBES YOUR QUALIFICATIONS AND EXPERIENCE?

A. Yes. I have attached Appendix I, which is a summary of my experience and qualifications.

Q. BY WHOM WERE YOU RETAINED, AND WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. Larkin & Associates, PLLC, was retained by the Committee of Consumer Services (CCS or Committee) to analyze PacifiCorp dba Utah Power & Light Company's (UP&L or Company) request for an increase in general rates based on the twelve months ended September 30, 2000, and to make recommendations to the Utah Public Service Commission (Commission) based on that analysis.

I will be presenting specific adjustments to the September 30, 2000, test year.

The impact of my recommendations is included in the revenue requirement calculations presented in Exhibit 1.1 of CCS Witness Hugh Larkin, Jr.'s prefiled testimony.

INCENTIVE COMPENSATION

Q. WHAT ADJUSTMENT ARE YOU PROPOSING FOR INCENTIVE COMPENSATION?

A. Incentive compensation expense should be reduced by at least $6,619,734 on a Utah basis. The adjustment on CCS Exhibit 2.1 removes the incentive compensation expense identified in DPU 8.14 as the test-year amount that is attributed to earnings goals.

Q. WHY DO YOU STATE THAT INCENTIVE COMPENSATION SHOULD BE REDUCED "BY AT LEAST"?

A. There are three reasons. First, the Company has provided conflicting information. The information supplied in response to DPU 8.14(d) is not consistent with the information included in the revised response to CCS 5.14. The amount of expense differs between the two responses by $3,571,141 on a total Company basis, and the total incentive compensation amount differs by $28,794. The earnings goal portion of the difference is $817,465. An explanation has been requested to determine why the differences between the two responses exist.

Secondly, the level of incentive compensation is excessive in comparison to past years. In Docket No. 99-035-10, the incentive compensation in dispute was $5,977,542 on a Utah basis. In this proceeding, the incentive compensation expense on a Utah basis is somewhere between $17,813,195 and $19,128,071. The right amount is dependent on the data response relied on. In other words, the level of incentive compensation expense has at least tripled since the last rate case on a Utah basis.

Q. WHAT IS THE THIRD REASON FOR POSSIBLY ADJUSTING THE INCENTIVE COMPENSATION EXPENSE FURTHER?

A. The Company's incentive program is purportedly designed to motivate and reward employees for contributions to operational effectiveness, outstanding customer service and achieving high levels of profitability for PacifiCorp's shareholders. The level of effectiveness, customer service and achievement of profits is based on performance goals. There are concerns that the level of achievement is not verifiable and that the goals may not raise the level of performance to qualify as true incentives. There are questions outstanding for which we hope the responses will be sufficient to better evaluate the goals and performance standards.

Q. WHAT WOULD BE THE BEST WAY TO EVALUATE GOALS AND PERFORMANCE?

A. A goal is a point that you are directed toward. Since the plan's purpose is to reward employees for contributions to operational effectiveness, outstanding customer service and achieving high levels of profitability, one would expect that the goals would be at a level that would motivate higher performance. Therefore, one must determine whether the goals from one year to the next actually provide incentive to improve the efficiency of operations and provide better service to customers.

The measurement of performance is the other factor to be evaluated in determining whether the goals were achieved and the amount of incentive awarded was appropriate. As in Docket No. 99-035-10, the Company again has provided its calculated results, but not the calculations themselves. In Docket No. 99-035-10, the Company was specifically requested in CCS 24.37 to provide the numerator and denominator that resulted in each of the performance percentages. The response was as follows:

> For most work groups the performance percentages are the result of weighting numerous goals. Further most work groups have a performance scale for determining performance rather than a formula which involves a numerator and denominator. For instance, employees at the Carbon Plant have a goal related to equivalent availability. For the goal, the employees receive a 100 percent performance factor for 94.63% availability, an 80% performance factor for 92.51% availability and a 112% performance factor for 95.16% availability. The performance factor is not the actual performance divided by 94.63%. Performance scales relating levels of achievement and associated performance factors are provided in PacifiCorp's response to CCS Data Request 24.42.

In this docket, the Division of Public Utilities (Division) requested in DPU 8.14 the calculations used to convert goal and applicable performance to dollars. The response provided formulas, not calculations. Without the goals and the actual performance, the formulas are of no value. Another request has been made of the Company to provide the actual calculations for the results provided in DPU 8.14(b). Since responses in the previous dockets and this docket have avoided providing sufficient detail to evaluate the goals and the actual results, we are concerned that a response to the outstanding request will also be insufficient. There is no assurance or evidence that the results presented by the Company are based on true incentive goals and that the performance levels were achieved.

Q. ARE YOU QUESTIONING THE GOALS?

A. Based on a review of the plans in prior dockets and the 1999 and 2000 plans provided in response to DPU 8.14, there is a concern. Some goals are specific, while others are vague and suggest discretionary measurement. In addition, the fact that achieved results requested in the past have not been provided makes it impossible to determine if goals are raised or if something other than normal results are expected. Furthermore, the goals in some instances are routine activities that should be expected as part of normal daily operations, not incentive compensation measurements.

Q. COULD YOU PROVIDE SOME EXAMPLES OF THE ACTIVITIES?

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Q. PLEASE EXPLAIN YOUR CONCERN REGARDING THE AMOUNT OF INCENTIVE COMPENSATION.

A. The incentive compensation expense for 1998 was $16,879,848 on a total Company basis. The test-year incentive compensation expense is between $47,882,730 and $51,453,870, depending on the response relied on. A 300% increase in incentive compensation is of great concern. The Company has not provided sufficient detail to show that its goals promote efficient operations. The Company has not provided sufficient detail to verify the performance levels purportedly achieved. Without the supporting detail, the 1998 amount of incentive compensation is considered questionable, which makes the test-year level very unreasonable. One would have to wonder how performance was measured at such a high level of achievement to warrant a significant incentive compensation amount when the Company is seeking such a significant increase in rates.

Q. DID THE COMMISSION ALLOW THE INCENTIVE COMPENSATION IN DOCKET NO. 99-035-10?

A. Yes. A brief discussion on the incentive compensation was included with the discussion on long-term incentive compensation. The allowance was based on the conclusion that the expense was only associated with non-financial goals which benefit ratepayers. That is the perspective that one would get from the label that was attached to the goals by the Company. However, the problem is the real issue was not addressed, i.e., whether the goals were real and whether the goals were really achieved. You can put a Cadillac emblem on a Chevy Cavalier, but that does not make it a Cadillac. The Company has not provided evidence that the goals have been raised from year to year, and the Company has not provided the detail to evaluate and test the performance measures it alleged to have achieved. The amount of costs requested for incentive compensation should be supported not only as I have just described, but also by a study that quantifies the cost savings that ratepayers are purportedly receiving.

Q. ARE YOU RECOMMENDING AN ADDITIONAL ADJUSTMENT TO INCENTIVE COMPENSATION EXPENSE?

A. Yes. The Line-of-Sight Goals, or the purported non-financial goals, incentive compensation expense is between $11,180,766 and $12,508,340 on a Utah basis. Again, the amount is dependent on the response relied on. Since the Commission allowed $5,977,542 in Docket No. 99-035-10, and some measures can be justified, I recommended that 50% of the incentive compensation be disallowed. The Company has not provided support for the goals and calculated measures, and the amount is excessive. As shown on CCS Exhibit 2.2, an adjustment of $5,590,383 ($11,180,766 x 50%) on a Utah basis is recommended.

The combination of my two recommended adjustments results in a $12,210,117 reduction to Utah incentive compensation expense. This leaves between $5.6 million and $6.9 million in the test year, which is more reflective of prior case levels. Considering the decline in employee levels, this amount is reasonable and conservative.

PAYROLL

Q. ARE YOU RECOMMENDING ANY ADJUSTMENTS TO PAYROLL?

A. Yes. There are four adjustments that should be made. First, the Company's adjustment 4.5, which annualizes the general wage increase, includes an increase for employees who left during the year. Second, the Company payroll expense was adjusted for only a portion of the employees who left during the year. An additional adjustment is required to account for the additional decline in the employee complement. The third adjustment corrects the Company's adjustment 4.20. The fourth adjustment corrects and revises the Company's adjustment 4.18.

Q. PLEASE DISCUSS THE WAGE INCREASE ANNUALIZATION ADJUSTMENT.

A. The Company's adjustment 4.5 applied a 3% increase to actual test-year wages paid to the various employee groups prior to the actual increase date. If the employee complement did not change, the calculated annualization would be appropriate. However, Company adjustment 4.20 removes the payroll for the net 288 employees leaving as part of the transition plan. Adjustment 4.20 did not adjust for the portion of the annualization of the total test-year payroll expense. In response to CCS 5.48, the Company provided the increase attributed to employees leaving net of the backfill increase. Based on the response, Company adjustment 4.5 is overstated by $82,987 on a Utah basis. CCS Exhibit 2.3 provides the adjustment broken down by account.

Q. WHY IS AN ADDITIONAL ADJUSTMENT REQUIRED TO THE EMPLOYEE COMPLEMENT?

A. The test year began with 6,290 employees on a total Company basis. As of September 30, 2000, the employee complement had decreased 425 employees to 5,865. The average number of employees in the test year was 6,185.5. Company adjustment 4.20 removed a net of 287.5 positions. After Company adjustment 4.20, the test-year average employee complement would be 5,898. This is 33 employees above the year end complement of 5,865.

Q. COULD YOU PROVIDE AN EXPLANATION AS TO HOW YOU DETERMINED THE DIFFERENCE?

A. Yes. CCS Exhibit 2.4.1, Column A, provides the employee complement by month from September 1999 through September 2000. The average for the year is 6,185.5 employees. Column B reflects the change that occurred from one month to the next. For example, in September 1999 the count was 6,290. In October 1999, the count was 6,273. The difference of 17 is reflected in Column B. Column C represents the net transition plan change based on the Company response to CCS 5.48. This is the only change in employees that the Company reflected in the filing. Column D indicates the difference between the actual employee changes that occurred in each month of the test year and the transition changes by month that the Company adjusted for in the filing. The difference is 137.5 employees. Simply put, the difference in the employee complement between the beginning of the test year and the end of the test year is a reduction of 425 employees. The Company reflected an adjustment for a net change of 287.5 employees in the filing. The unaccounted for change is 137.5 employees (425-287.5).

Q. HOW IS IT YOU HAVE A 137.5 EMPLOYEE DIFFERENCE, AND EARLIER YOU REFERRED TO A 33 EMPLOYEE DIFFERENCE?

A. The 137.5 employee difference is based on actual employee counts throughout the test year. The 33 employee difference is the difference between the test-year average employee complement as adjusted and the test-year end complement of 5,865. In other words, the 137.5 is an actual unaccounted for change in the employee complement, and the 33 is the unaccounted for change in the test-year average.

On CCS Exhibit 2.4.1, I convert the 137.5 employee reduction to an average for the test year. In Column D, there is a difference of 17 less employees not accounted for in the Company transition plan adjustment. This 17 needs to be removed in each month for the year; therefore, by multiplying the 17 by the 12 in Column E, I get a weighted difference. Each month is adjusted by the corresponding number of months that the respective difference was unaccounted for. The test-year average of the 137.5 employee difference is 33.3 employees, which is comparable to the 33 employee difference referred to earlier.

Q. ARE YOU RECOMMENDING AN ADJUSTMENT FOR THE 33 EMPLOYEES?

A. Yes. As shown on CCS Exhibit 2.4, payroll expense should be reduced $683,316 on a Utah basis. This is based on an average payroll expense of $56,192 per employee.

Q. WHY IS IT NECESSARY TO CORRECT COMPANY ADJUSTMENT 4.20?

A. Company adjustment 4.20 reflects the savings in payroll for employees leaving in the test year offset by the amortization of estimated transition plan costs. The Company's estimated transition plan costs through the end of the transition period of 2005 is $156,000,000. Based on that estimate, the Company projected test-year costs to be $44,439,169. Amortized over five years, the transition plan savings were reduced $8,887,834 ($44,439,169 / 5 years).

The Company was requested in CCS 5.50 to provide the <u>actual</u> transition costs associated with the employees who left during the test year. The response indicated the actual cost was $28,818,967. That amount is $15,620,202 less than the estimate included in the filing. Based on a five-year amortization, the transition cost was overstated by $3,124,040 on a total Company basis. This resulted in an understatement in the net savings in the test year of $1,158,300 on a Utah basis.

In addition, the difference between actual and estimated transition plan costs reduces rate base $6,248,081 on a total Company basis and $2,316,601 on a Utah basis. The calculation of these adjustments is located on CCS Exhibit 2.5 and 2.5.1.

Q. PLEASE EXPLAIN WHAT CORRECTIONS ARE NECESSARY FOR COMPANY ADJUSTMENT 4.18.

A. Company adjustment 4.18 removes costs from the test year and amortizes them over three years. The costs adjusted by the Company purportedly are not merger costs, but are costs “triggered” by the merger. The adjustment by the Company removed six different costs from test-year expense and set the costs up as a rate-base item to be amortized over three years. Two of the costs were for accruals that had already been reversed on the Company’s books in July 2000. A portion of the Company adjustment associated with the reversed accruals was in error, resulting in double reversals. The Company agrees that this was an error. To correct this error, as shown on CCS Exhibit 2.6, expense is increased $1,149,387, amortization expense is decreased $383,129, and rate base is reduced $239,456, all on a Utah basis.

Q. WHAT ADDITIONAL REVISIONS ARE REQUIRED FOR COMPANY ADJUSTMENT 4.18?

A. The remaining costs on a total Company basis are as follows:

Special Bonuses not Merger Related	$2,388,000
Severance Accrual for Officers and Employees	2,984,000

Acceleration of Restricted Stock Plan	1,630,000
Acceleration of Non-Employee Director Stock (Cash)	400,000
	$7,402,000

The first problem is the Company's position that the costs are not merger costs, but were triggered by the merger. It is an oxymoron. If the costs were the result of the merger, then the costs are merger related costs. If not merger related costs, then they are costs that are not recurring.

The second problem is that if the Company adjustment setting up the costs in rate base was appropriate, the three-year amortization period is too short and inconsistent with the treatment afforded transition costs.

Q. WHY WOULD YOU CLASSIFY THE COSTS AS MERGER COSTS?

A. The $2,388,000 of "special" bonuses, according to the response to CCS 20.1, were bonuses that were paid earlier than they would otherwise be because of the merger. That is indicative that the level of costs is due to the merger. In response to CCS 20.2, a letter to officers describes the bonuses as follows:

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The next item includes $2,984,000 of severance accrual for officers and employees. Of the total, $2,775,100 (93%) was paid to four employees whose jobs were eliminated or substantially changed as a result of the merger. The response to DPU 2.20 continues its description, stating that "These are early transition costs - similar in nature to costs included in the Company's deferred transition cost application but incurred earlier." Since the costs were incurred earlier, they were known and should have been included as part of the transition cost application. The only reason for not including them in the transition cost application is that they are merger costs, or costs that could be classified as not recurring.

The third cost is the accelerated cost from the immediate vesting of the restricted stock plans. This cost recognition is the result of the merger. The cost was previously allowed in rates because it was associated with the retention of key employees. The basis for allowance no longer exists, and the cost is in reality a merger related cost that will not be recurring.

The final cost is for the accelerated non-employee director stock. This is a merger related cost that will not be recurring.

Q. IF THE COSTS ARE MERGER RELATED, ARE THEY REQUIRED TO BE DISALLOWED?

A. That depends on the Commission's interpretation of the Stipulation in the merger case, Docket No. 98-2035-04. The Stipulation states: "No merger transaction related costs shall be allowed in rates." The Company has indicated each of the four remaining costs are merger related. To the extent the terms of the merger prompted the event that triggered the cost, it could be attributed to being a merger transaction related cost. The stipulation states "Normal severance costs may be considered for allowance in rates." It is questionable as to whether this is normal severance. Even if, by a stretch of the imagination, it is classified as such, the terms of the Stipulation state "may be" not "will be". There is concern that some of the $2,388,000 and $2,984,000 could be enhancements to severance costs relating to the merger which is not to be allowed in rates. Finally, the Stipulation states that transition plan costs that result in net cost savings may be considered for allowance in rates. The level of costs the Company purported to be attributable to the transition plan are not reflected as an offset to cost savings which is necessary to be "considered" for allowance in rates. The fact is that merger related costs are either not allowed or "may be considered for allowance in rates." There is no assurance in the Stipulation that the costs will be allowed in rates. As shown on CCS Exhibit 2.7, the remaining rate base of $571,758 and amortization of $914,813 on a Utah basis should not be allowed.

Q. DO YOU HAVE ANY ADDITIONAL COMMENTS ON THE COMPANY'S REQUESTED PAYROLL?

A. Yes. On each of the areas discussed, requests for information remain outstanding. It may be necessary to supplement my payroll testimony upon receipt and evaluation of further information.

<u>PENSIONS & POSTRETIREMENT BENEFITS</u>

Q. WHAT AMOUNT OF EXPENSE IS INCLUDED IN THE FILING FOR NORMAL PENSION AND POSTRETIREMENT BENEFITS?

A. Based on the Company's response to DPU 5.1, pension expense and postretirement benefit expense is $10,822,119 and $13,117,638, respectively, on a total Company basis.

Q. IS THE TEST YEAR AMOUNT REASONABLE?

A. No. The amounts in the test year include costs that, according to the responses to CCS 25.1 and CCS 25.2, should be excluded, and the accrued amounts are different than actuarial determined expense amounts. The response to DPU 5.1 included actuarial cost information that the Company utilized to estimate the test-year expense. The Company's calculated expense suggests that test-year pension expense is overstated at $4,791,808, and test-year postretirement expense is understated by $2,268,479 on a total Company basis.

Q. DO YOU AGREE WITH THE COMPANY'S CALCULATION?

A. No. I do agree that test-year pension expense is overstated and postretirement expense is understated, but by different amounts. On a total Company basis, test-year pension expense is overstated by $6,422,854 and postretirement expense is understated by $2,006,014.

Q. PLEASE EXPLAIN HOW THE COMPANY DETERMINED THE ESTIMATED ACTUARIAL EXPENSE.

A. The Company has two periods of actuarial calculated costs for pensions and postretirement expense. The first time frame is January 1, 1999, to March 31, 2000. This 15-month period includes six months of the test year. The second time frame is April 1, 2000, to March 31, 2001. This 12-month period also includes six months of the test year. The Company added the two periods together and then multiplied the sum by 12/27 to arrive at their estimated actuarial expense for the test year. This calculation inappropriately allocates too much of costs outside the test period to the test year.

Q. HOW DOES THE COMPANY ALLOCATION INCLUDE TOO MUCH COSTS OUTSIDE OF THE TEST PERIOD?

A. The 15-month period cost ending March 31, 2000, was significantly greater than the 12-month period ended March 31, 2001. For example, the 15-month period pension expense was $23,848,349 and the 12-month period pension expense was a negative $10,280,149. By lumping the two together and prorating it, the

Company is recognizing a greater portion of the 15-month periods positive cost and a lesser portion of the negative cost. For the 15-month period, the Company included 12/27 (44.4%) of the positive cost as being in the test year when actually only 6/15 (40%) of the positive cost was in the test year. For the 12-month period, the Company again includes 12/27 of the negative cost when actually 6/12 (50%) of the negative cost was in the test year.

Q. WHAT IS YOUR RECOMMENDATION?

A. The test-year calculation of the actuarial cost of the pension and postretirement expense should be calculated based on the number of months of the test year included in each of the respective actuarial cost determinations. As shown on Exhibit CCS 2.8, I took 6/15 of the January 1, 1999, to March 31, 2000 costs and 6/12 of the April 1, 2000 to March 31, 2001 costs. This results in a pension expense of $4,399,265 and a postretirement expense of $15,123,652 on a total Company basis. Based on the $4,399,265, the test-year pension expense should be reduced $6,422,854 on a total Company basis. The Utah allocation using the SO Factor of 37.077% results in a reduction of $2,381,402.

Q. WHAT IS THE ADJUSTMENT TO POSTRETIREMENT EXPENSE?

A. The $15,123,652 of cost is $2,006,014 higher than the booked test-year expense. The increase to Utah expense based on the SO Factor (37.077%) is $743,770.

Q. ARE YOU RECOMMENDING ANY ADDITIONAL ADJUSTMENTS TO TEST-YEAR PENSION AND/OR POSTRETIREMENT EXPENSE?

A. Not at this time. We are awaiting responses to data requests on employee benefits that may result in additional employee cost adjustments. Specifically, we are concerned with an accrual to the Supplemental Executive Retirement Plan (SERP) reserve during the test year.

Q. WHAT IS YOUR CONCERN WITH THE SERP ACCRUAL?

A. In June of 2000, an accrual for $5,212,000 was made for a transition liability. It is not clear at this time whether the accrual was recorded as an expense or how it was treated in the filing. If the amount is included entirely in expense instead of being amortized over five years in the same manner as other transition costs, an adjustment would be recommended.

WORKING CAPITAL

Q. HAVE YOU REVIEWED THE COMPANY'S UPDATE TO CASH WORKING CAPITAL?

A. Yes. The Company prepared a lead/lag study in 1998. The results of that study increased the net lag days from 8.9 days to 12.7 days, resulting in an increase in the cash working capital requirement of $15,661,060 on a Utah basis.

Q. IS THE COMPANY REQUEST REASONABLE?

A. Absolutely not. The Company's request is based on an increase of 3.8 net lag days. This increase is attributed to both the other revenue lag and the general business revenue lag. Within the general business revenue lag, the billing lag component increased 3.5 days from 2.9 days to 6.4 days. The general business revenue collection lag increased 4.5 days from 26.5 to 31.0 days.

Q. WHY WOULD THE BILLING LAG INCREASE?

A. The Company was requested in CCS 28.9 to provide a detailed description of all factors that caused the billing lag to be so long in 1998. The Company replied that it is not possible to identify all of the factors, but certainly a contributing factor would be the change in the way bills are prepared. The description is as follows:

> In 1991 most customers with multiple meters would have received a separate bill for each meter. In 1998 a customer with multiple meters would likely have received a single bill generated by CSS, showing the

> usage on all meters. The CSS approach produces bills that are more convenient and useful for customers while reducing the total number of bills that need to be generated and mailed. Since it is possible that the customer's meters will be on different meter read cycles, CSS has been designed to hold the customer's final bill preparation until all meters have been read. There could be a difference of several weeks between the date of the first meter read and the final meter read. Since the lead/lag study compares the meter read date and the billing date at the individual meter level, the process of bill aggregation used by CSS may tend to increase the calculated billing lag.

This explanation suggests a significant inefficiency exists. The Company reads a meter at Customer A's house on Monday and does not bill them because Customer A has a second meter that will be read the next Monday. The Company continued its discussion that the 1998 billing lag is reflective of ongoing conditions. This inefficiency should be rejected.

Q. WHAT TYPE OF BILLING LAG WOULD YOU EXPECT?

A. The 2.9 day lag from the 1991 study is not unrealistic. In a Vermont case that was just completed, the Company indicated a 3 day billing lag was typical. With modern meter reading technology, one would expect 3 days or less. In fact, the Company response to CCS 28.10 stated it would be standard procedure for a customer with a single meter to have a "two-day lag." A Company inefficiency in meter reading and/or billing should not be justification for ratepayers to provide additional working capital to the Company.

Q. WHY IS THE INCREASE IN THE COLLECTION LAG A CONCERN?

A. The Company was having problems with the new CSS system which resulted in bills not being correct. This also affected collections, as was noted in Docket No. 99-035-10, when the Commission excluded 1997 and 1998 bad debt expense from the averaging calculation. The Commission order stated that "Because 1997 and 1998 are problematic and do not represent a normal, on-going ratio of write offs to receivables, we adopt the three-years proposed by the Committee."

This problem would impact the lead/lag analysis because the significant problems with collections noted in the previous case that affected bad debt expense in 1998 would also impact the collection lag in 1998.

Q. WAS THE COMPANY ASKED ABOUT THE IMPACT THE COLLECTION PROBLEMS HAD ON THE COLLECTION LAG CALCULATION?

A. Yes. The Company, in response to CCS 28.4, claimed that the CSS conversion took place in 1996 and problems "were resolved before 1998." The Company also stated "That 1998 is a year that reflects normal CSS operation and which experienced minimal disruption of normal collection activities," and that the halting of collection activities in 1997 and 1998 and the billing problems did not "materially" impact the collection lag days calculation. The Commission concluded otherwise in Docket No. 99-035-10. Even though collection efforts resumed in 1998, the results were not immediate. The level of uncollectibles in 1998 is evidence of that fact. The evidence in Docket No. 99-035-10 outweighs the Company's statements in response to CCS 28.4. Finally, the amount of write offs declined in 2000 and continued to decline in 2001, which is further evidence that collections were a problem in 1998.

Q. ARE YOU PROPOSING AN ADJUSTMENT TO THE REVENUE LAG CALCULATION IN THE 1998 LEAD/LAG STUDY TO CORRECT FOR THE BILLING LAG AND COLLECTION LAG PROBLEMS?

A. No. Instead, I am recommending the prior lead/lag study results be utilized. If one were to make recommended adjustments to the 1998 study, they would be based primarily on the 1991 results. For example, the billing lag of 2.9 days in the 1991 study is realistic. The alternative for the collection lag in the 1998 study would be to calculate a collection lag for the year 2000; however, the Company has indicated this information is not available. The 1991 study is the logical choice by default.

Q. WHAT IS THE IMPACT OF THE CHANGE TO REFLECT THE NET LAG DAYS FROM THE 1991 STUDY?

A. CCS Exhibit 2.9 shows the $15,665,287 reduction to the Company's filed cash working capital rate base component. CCS Exhibit 2.10 reflects the additional reduction to working capital in rate base as a result of the Committee's recommended adjustments to expenses.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.