–BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH–

IN THE MATTER OF WATERPRO INC.'S APPLICATION FOR A CULINARY WATER RATE INCREASE	))))))))	**DOCKET NO. 21-2443-01** **Exhibit No. DPU 1.0 DIR** **Direct Testimony**

FOR THE DIVISION OF PUBLIC UTILITIES
DEPARTMENT OF COMMERCE
STATE OF UTAH

Direct Testimony of

Paul Hicken

June 21, 2022

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INTRODUCTION

Q: PLEASE STATE YOUR NAME, BY WHOM YOU ARE EMPLOYED, AND WHAT CAPACITY.

A: My name is Paul Hicken. I am employed as a Utility Technical Consultant by the Utah Division of Public Utilities. I am the lead analyst on this case.

Q: PLEASE SUMMARIZE YOUR EDUCATION AND PROFESSIONAL EXPERIENCE.

A: I received a Master of Business Administration degree from Utah State University in 1985. I am also a Certified Government Financial Manager (CGFM). I have been employed by the Division of Public Utilities (Division or DPU) since June 2005. Prior to that, I was employed by the Office of the Legislative Auditor General for 19 years.

Q: HAVE YOU TESTIFIED BEFORE THE PUBLIC SERVICE COMMISSION (COMMISSION) BEFORE?

A: Yes, on several occasions. Most recently, I testified before the Commission as the Division's witness in a teleconference hearing on July 29, 2020, in the WaterPro, Inc. General Rate Case, Docket No. 20-2443-01.

BACKGROUND

Q: CAN YOU DESCRIBE THE BACKGROUND AND ISSUES OF THIS CASE?

A: Yes. On or about November 9, 2021, WaterPro, Inc. (WaterPro or Company) submitted a letter of intent to the Commission to file a petition for a general rate increase of culinary water rates. On March 30, 2022, the Commission received a comprehensive application from WaterPro and a docket number was assigned. The Division reviewed the application and found it to be substantially complete. During the next few months, the Division reviewed the application and initial documentation which included proposed rate increases, annual reports, consolidated audit reports, and summaries of expenses and revenues. The Division also sent a data request and additional follow-up questions to the Company in May, seeking further information and clarification. At the end of May the Division made a site visit to inspect the plant and facilities and to further review operations, assets and expense details. The Company cooperated fully and helped provide the information and clarification needed.

REVENUE REQUIREMENT

Q: CAN YOU EXPLAIN THE REVENUE REQUIREMENT MODEL USED IN THIS RATE CASE?

A: Yes. The Revenue Requirement shown in DPU Exhibit 1.1, compiles information from the Company's Annual Report to the Commission for the test year and considers revenues and expenses, applicable taxes and calculates the net operating income or loss along with the rate of return (ROR). The model also considers any upcoming known and measurable changes, and adjustments that may be needed. A revenue requirement and ROR is calculated based on the Company's requested rate increase. A recommended revenue requirement and ROR is also calculated based on the Division's analysis and what is deemed fair and reasonable.

RATE OF RETURN

Q: PLEASE EXPLAIN THE RATE OF RETURN USED IN THE MODEL.

A: The rate of return is the return on rate base (utility property) used to determine if the requested rate increase is just and reasonable. It is calculated by dividing the net operating revenue/loss by the total adjusted rate base. There are several rates considered in the model. The first is the actual ROR realized by the Company for the test period. This is shown to be 5.61% in line 81, column B of the model. The second is the requested ROR which incorporates the requested rate increase into the model. This is shown to be 7.53% in line 81, column F of the model. The third is the DPU's recommended ROR based on its analysis of Company's net operating revenue or loss, the current adjusted rate base, and the existing capital structure of the Company. This is shown as 8.62% in line 81, column I of the model.

Q: CAN YOU EXPLAIN THE CAPITAL STRUCTURE OF THE COMPANY?

A: The capital structure is shown in further detail in the ROR tab of the Revenue model spreadsheet. In 2021, the Company reported $38.6 million of retained earnings and stock shares (patronage capital) which accounted for 90.6% of the total capital. The Company also reported $4 million of long-term debt which accounted for 9.4% of the total capital. The cost of the capital for equity was estimated to be at 9% based on most recent figures from Kroll Inc., a worldwide consulting and equity firm. The actual cost of the debt was 4.95% which was established by the lending institution in 2013 at the time of the loan. By combining the debt and equity, the weighted average cost of capital comes out to be 8.62%. The DPU believes this to be a fair and reasonable return for the Company.

ADJUSTMENTS

Q: DID THE DIVISION MAKE ADJUSTMENTS FOR REVENUES OR EXPENSES?

A: Yes, there were several adjustments made for the revenue requirement.

1. The first adjustment is shown in line 2, column E of the Division's Exhibit 1. The Company's requested 5 percent increase to revenue is shown here. The Company requested a 5% increase to culinary water rates and this adjustment simply adds 5% to all reported 2021 culinary water sales.

2. The second adjustment adds $291,128 to Professional Services expense. This adjustment is shown in line 32, column G of the model. The Company's trial balance showed this amount as an entry under Professional Expense, with 100% of it being allocated to regulated operations. However, it was inadvertently left out of the Annual Report to the Commission.

3. The third adjustment adds back $22,125 to miscellaneous expense. It is shown in column G, line 55. The Company made a calculation error when allocating various shared expenses between the irrigation operations and the culinary operations. Expenses from several shared accounts were allocated to culinary operations at 77% when they should have been allocated at 80%, the difference being $22,125.

The allocation factors vary slightly from year to year and the 77% factor was from a prior year of operations.

Q: CAN YOU EXPLAIN FURTHER THE ALLOCATION FACTORS?

A: Yes, the Company periodically reviews the costs of operations and determines the percentage attributed to culinary water provision and the costs attributed to irrigation or secondary water provision. Some costs are easily determined as direct allocation to either culinary or irrigation. However, most costs are a mixture of part allocation to culinary and part to irrigation. The allocation factors consider assets, labor and overhead, and cost of goods including materials & supplies. The most recent general allocation factor for mixed costs is 80/20 with the larger part going to culinary operations. Some specific parts of Company operations may have specific allocation factors, but 80/20 is the general allocator.

DIVISION'S POSITION

Q: WHAT IS THE DIVISION'S POSITION AFTER REVIEW OF THE COMPANY'S OPERATIONS?

A: The Division believes that the Company's request for a 5% increase to culinary water rates is just and reasonable and in the best interest of the customers. The Division's analysis showed that a rate increase of more than 8% would have been supported based on costs and a fair rate of return. However, the Company believes a 5% increase will be adequate. The Board of Directors approved a 5% increase, and the Company wants to avoid rate shock to the customers.

SUMMARY

Q: WHAT IS THE DIVISION'S RECOMMENDATION?

A: The Division recommends the Commission approve the 5% rate increase to culinary water rates as submitted in the application.

Q: DOES THIS CONCLUDE YOUR TESTIMONY?

A: Yes, this concludes my testimony.

CERTIFICATE OF SERVICE

I certify that on June 21, 2022, I caused a true and correct copy of the foregoing Direct Testimony of Paul Hicken to be filed with the Public Service Commission and served by the Utah Division of Public Utilities to the following in Utah Docket 21-2443-01 as indicated below:

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