

1 **Q Please state your name, address, and occupation.**

2 A My name is Marci L. Norby. My business address is 2515 Warren Ave., Suite 304,  
3 Cheyenne, Wyoming, 82002. I am employed as a Senior Rate Analyst with the Office of  
4 Consumer Advocate.

5  
6 **Q Please describe your educational background, occupation, and experience.**

7 A I received a Master of Science degree in Finance from the University of Wyoming in 1999.  
8 The area of emphasis in my graduate work was the value of timing options in capital  
9 budgeting using the Black-Scholes model. After graduating I was employed as a financial  
10 analyst in the banking profession, where my duties included accounting, capital budgeting,  
11 financial budgeting, bond portfolio management and administration, institutional investing,  
12 economic analysis, and financial operations. I came to the Wyoming Public Service  
13 Commission in August of 2000 and then to the Office of Consumer Advocate in May of  
14 2003.

15  
16 **Q Have you testified before the Commission in previous proceedings?**

17 A Yes. I have testified in eight cases prior to this proceeding. I have testified in four general  
18 rate cases, one unbundled network element telecommunications cost case, two TSLRIC  
19 telecommunications cases, and one telecommunications service quality case.

20  
21 **Q On whose behalf do you appear today?**

22 A I appear in this case on behalf of the Office of Consumer Advocate (OCA).

23  
24 **Q As a member of the OCA do you advocate the interests of certain groups of  
25 consumers over others?**

26 A No. As a member of OCA it is my obligation to represent the interests of all Wyoming  
27 citizens and all classes of utility customers in the state.

1 **Q What is the purpose of your testimony in this proceeding?**

2 A The purpose of my testimony is to present the OCA review and recommendations  
3 pertaining to the Company's pass on and general rate increase application. I will present  
4 an alternative revenue requirement and return based on the OCA adjustments to Vista  
5 West's application in this case and OCA return analysis. I will also present an alternative  
6 rate design based on the OCA determined revenue requirement, profit margin, and  
7 proper rate structure.

8  
9 **Q Do you sponsor any exhibits in this proceeding?**

10 A Yes, I sponsor OCA Exhibits MLN-1 through MLN-6 in this proceeding. I will refer to my  
11 exhibits throughout my testimony.

12  
13 **Q How is your testimony organized?**

14 A First I will present an overview of the Company's requests in the application. Next, I  
15 illustrate the OCA's review and recommendations regarding the pass on portion of this  
16 application. I will then introduce the OCA's recommended revenue requirement and return  
17 in the general rate case portion of the application. Finally, I present testimony in regard to  
18 the proper rate design in this case.

19  
20 **I THE APPLICATION**

21  
22 **Q What is the rate increase that Vista West is requesting in this case?**

23 A Vista West is requesting a total volumetric increase of \$0.45 per 1,000 gallons, which  
24 consist of a \$0.13 increase in the commodity rate and a \$0.32 increase in the non-  
25 commodity rate. The Company is also requesting a 9.9% increase in the fixed monthly  
26 charges as indicated in the table below.

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	<b>Present Rate</b>	<b>Proposed Rate</b>	<b>Dollar Change</b>	<b>Percent Change</b>
Dry Meter Rate	\$ 18.43	\$ 20.27	\$ 1.84	9.984%
Fixed Rate	\$ 22.43	\$ 24.67	\$ 2.24	9.987%
Commodity Rate	\$ 1.17	\$ 1.30	\$ 0.13	11.111%
Non-Commodity Rate	\$ 1.81	\$ 2.13	\$ 0.32	17.680%
Total Volumetric Rate	\$ 2.98	\$ 3.43	\$ 0.45	15.101%

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The application requests an effective date of January 1, 2003 and, though it is not specifically stated in the application, a return of \$20,000 in the form of an annual dividend to the shareholder. Within the Company's revenue requirement, it is requesting increases in salary for the three employees, corresponding increases in retirement benefits, and increases in health insurance benefits.

10 **II THE PASS-ON**

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**Q Is the commodity portion of the requested increase in this a case being passed-on to the customers on a dollar for dollar basis?**

14 A Yes it is. Vista West is billed by the City of Casper on a per 1,000 gallon basis only. The current charge to Vista West from the City of Casper is \$1.30 per 1,000 gallons. The City of Casper increased this rate from \$1.17 to \$1.30 per 1,000 gallons of water, effective January 1, 2003. The Company is requesting to increase the commodity portion of its rates by \$0.13 to \$1.30 as indicated in the table above.

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**Q What is the effective date that Vista West is requesting for the increase in commodity cost in this case?**

22 A As stated above, Vista West is requesting an effective date of January 1, 2003 for the

1 increased commodity cost in this case.

2  
3 **Q Does the OCA agree that this is an appropriate effective date?**

4 A No. Clearly, to grant this requested effective date would be to engage in retroactive  
5 ratemaking. The OCA recommends the date of the Commission's decision in this case  
6 as the proper effective date. It is improper to authorize an effective date several months in  
7 the past, which would not give appropriate notice or price signals to the Company's  
8 customers.

9  
10 **Q Do you have any statutory basis for recommending the date of the Commission's**  
11 **decision as the appropriate effective date?**

12 A Yes. The OCA's recommendation is based in part on Wyoming Statute 37-3-102,  
13 which provides: **Only prescribed rates to be charged:**

14  
15 No public utility shall directly or indirectly, by any device whatsoever, or in  
16 anywise, charge, demand, collect or receive from any person a greater  
17 or less or different compensation for any service rendered or to be  
18 rendered by such public utility than that prescribed in the schedules of  
19 such public utility **then filed and published in the manner provided**  
20 **in this act**, nor shall any person receive or accept any service from a  
21 public utility for a compensation greater, less or in any way different from  
22 that prescribed in such schedules. (Emphasis added)  
23

24 Therefore, until the proper schedules are approved in this case the rates cannot be placed  
25 in effect.

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27 **Q Are there any other recommendations the OCA is making in the pass-on filing?**

28 A Yes. Pursuant to the Commission Rule 249<sup>1</sup>, the OCA recommends that the commodity

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1 Wyoming Public Service Commission Rule, Section 249(d) All pass on charges are filed as a separate rate rider or surcharge which will be blended into base rates at appropriate intervals in general rate case proceedings or as other wise ordered by the Commission.

1 portion of the volumetric rates be filed as a separate rate rider separate from the non-  
2 commodity portion of rates in the tariff pages. Unbundling the rates in this manner will  
3 allow for a straightforward identification of commodity versus non-commodity rates within  
4 the tariff pages. It will allow for easier analysis and tracking of the two different portions of  
5 the volumetric portion of the rate. When Vista West files for a general rate increase or a  
6 pass on application, or both, as it did in this case, without clearly identifying the separate  
7 rates, it is unnecessarily difficult to determine what portion is commodity and what portion  
8 is non-commodity. The OCA recommends that the Company resubmit the tariffs in this  
9 case with the commodity portion of the volumetric portion of the rates separate from the  
10 volumetric non-commodity portion.

### 11 12 **III THE GENERAL RATE CASE**

#### 13 14 **A. REVENUE REQUIREMENT**

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16 **Q How has Vista West determined its revenue requirement in this case?**

17 **A** Vista West has submitted a cash flow statement for the projected budget year in Exhibit B  
18 of the application. The Company has submitted its budget projections in this case  
19 purporting to include its projected revenues and expenses.

20  
21 The financials set forth in the Company's Exhibit B do not constitute an income statement;  
22 rather it is a cash flow statement. In order to encompass all of the cash flows, the  
23 company has included the budget projection for principal debt payments in the  
24 "Depreciation Expense" account in the "Budget Projection" column in its Exhibit B of the  
25 application instead of the actual depreciation expense. The historical years (2000  
26 through 2002) indicated in this expense account are the actual depreciation expenses for  
27 those years. Therefore, there are two separate items included in this account as

1 illustrated in Exhibit B of the application and OCA Exhibit MLN-1 (line 22). Including the  
2 principal payment obligation in the budget projection in this exhibit illustrates the cash  
3 flows of the company.

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5 In addition, the company has included a "Dividends" account as a part of the expense  
6 portion of the financial schedule. This is a liability account, however, the company treats  
7 this line item as an indication of profit embedded within the expenses in the cash flow  
8 statement presented in Vista West's Exhibit B. This account also appears in OCA Exhibit  
9 MLN-1 (line 23). This embedded return is taken into account when the OCA calculates the  
10 profit margin in OCA Exhibit MLN-1.

11  
12 **Q What are the adjustments the OCA has made to the revenue requirement in this**  
13 **case?**

14 **A** The OCA has made adjustments to the Company's Exhibit B as indicated in column G of  
15 OCA Exhibit MLN-1. The OCA adjustments increase the validity and reasonableness of  
16 the financial projections in this case.

17  
18 The Company is requesting an increase in the Bank Charges expense account of \$3,600  
19 for the new bill collecting system administered by First Interstate Bank and \$500 for other  
20 bank charges. Due to the fact that First Interstate Bank is taking over ½ of the billing and  
21 collection duties from the bookkeeper, the OCA adjustments include a \$1,800 decrease  
22 in accounting expense (where the bookkeeper's charges are booked). This adjustment is  
23 calculated by taking ½ of the \$3,600 increase in the Bank Charges expense account. The  
24 accounting expense reduction of ½ of the Bank Charges account increase of \$3,600 is  
25 used to account for the reduced bookkeeping expense due to the fact that the  
26 bookkeeper will still process and mail the bills to the customers, while the bank will collect  
27 and deposit the revenues from bills, a function previously performed by the bookkeeper.

1 Through discovery the OCA attempted to determine the dollar amount of efficiency this  
2 would create under the Accounting expense account. However, the Company could only  
3 offer the OCA an estimate of 15% to 20% that was not based on hours the accountant  
4 spent on billing and collecting. The OCA adjustment of \$1,800 is 16% of the current  
5 requested Accounting expense. The OCA adjustment made to Accounting expense is an  
6 appropriate estimate of the effect of the relinquishment of ½ of the billing and collection  
7 duties of the bookkeeper.

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9 The adjustment decreasing the Bank Charges by \$268 is based on a weighted average  
10 of the expenses in the year 2000 (weighting of 1), 2001 (weighting of 2), and 2002  
11 (weighting of 2). I used the weighted average adjustment for these expenses due to the  
12 significant variances in the account balances from year to year. The larger weighting is  
13 used in the more recent years to account for more recent expense patterns. This  
14 adjustment only takes into consideration those items in the Banks Charges expense  
15 account that are not related to the billing expense from First Interstate Bank. This  
16 adjustment normalizes the expense.

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18 The OCA has also decreased the Officer's Health Insurance expense by \$16,282 per  
19 annum. The expense posted to the Company includes 100% of the president's family  
20 health care coverage. This adjustment takes into consideration the Bureau of Labor  
21 Statistics report released August 26, 2003, entitled Employer Cost for Employee  
22 Compensation-June 2003 (USD L:03-446)<sup>2</sup>. In Table 16, page 20 of the report, statistics  
23 show that the per hour benefit cost of health insurance for public utilities per employee is  
24 \$3.23. I multiplied \$3.23 by 2,080 hours per year to calculate a total annual national  
25 average of per employee compensation paid by public utility companies for health care  
26 benefits of \$6,718.40. This represents a reasonable annual per employee health

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<sup>2</sup> United State Department of Labor, Bureau of Labor Statistics. USD L: 03-446. Released August 26, 2003. Employer Cost for Employee Compensation – June 2003. Page 20. OCA Exhibit MLN-5.

1 insurance expense for a utility company such as Vista West Water Company. In  
2 evaluating the health cost to the company, it is important to consider what is a reasonable  
3 cost to the ratepayers.  
4

5 The magnitude of the current and requested insurance costs is much larger than the  
6 national average costs incurred. The 2002 cost to Vista West ratepayers is \$19,475 or  
7 approximately 32% of the officer's salary expense and benefits. Vista West is requesting  
8 a health insurance expense of \$23,000 or approximately 33% of the requested officers  
9 salary and benefits in this case. The Bureau of Labor Statistics (Table 16) shows that the  
10 average percentage cost of total compensation paid to employees represented by health  
11 insurance is 8.1% nationally. Therefore, the Company is requesting that the ratepayers of  
12 Vista West pay 24.9% above the national average proportion of those costs, which is  
13 more than three times the average health benefit expense per employee. This is a large  
14 difference. The ratepayers of Vista West should not be responsible for paying an  
15 excessive amount of health care costs for the officer of this company. It is important to  
16 reasonably normalize this expense. The national average cost paid by utility companies  
17 used by the OCA in this analysis is an appropriate normalization of health insurance  
18 expense in this case.  
19

20 It is also important to note that 85% of professional employees with family coverage are  
21 required to make contributions toward their own health coverage.<sup>3</sup> In this case, the  
22 Company is currently paying, and is requesting to continue to pay, 100% of the health care  
23 cost for the officer's family health care coverage. In addition, the required dollar amount of  
24 employee out-of-pocket contributions required for employees with family coverage based  
25 on national averages, is 237% higher than what is required for out-of-pocket contributions

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3 United State Department of Labor, Bureau of Labor Statistics. USDL: 02-389. Released July 16, 2002. Employee Benefits in Private Industry, 2000. Page 5. OCA Exhibit MLN-6

1 from single coverage employees. This is because family coverage is much higher than  
2 single coverage.<sup>4</sup> Therefore, not only are 85%<sup>5</sup> of the nation's professional employees  
3 required to contribute a portion to their health care coverage, but also employees with  
4 **family** coverage are required to contribute more out-of-pocket because of the larger  
5 expense in covering additional insured's.

6 In addition, the health care coverage cost of the Company increased by 92% from 2000 to  
7 2001 and by 23% from 2001 to 2002. The Company is requesting another 18% increase  
8 in this case. The Commission must impose some limit to the appropriate cost to  
9 ratepayers for employees' health care insurance expenses. The OCA's adjustment  
10 aligning Vista West's health care expense with the utility company national average  
11 appropriately limits the ratepayer's burden. Linking this expense to the utility company  
12 national average will allow for increases due to nationwide health care coverage cost  
13 increases, yet will cap unreasonable continued escalation of this expense, such as is  
14 requested in this case. This adjustment made by the OCA will also allow the Company to  
15 recover an appropriate expense level to ensure the continuation of the Company as an  
16 attractive 'going concern'.

17  
18 The decrease of \$349 in office expense includes the removal of advertising expenses of  
19 \$99.20 and \$250 that were included in this account for the year 2002. In 2002, these  
20 numbers were posted to the Office Expense account not to the Advertising expense  
21 account. Due to the fact that the Company's Budget Projection in its Exhibit B of the  
22 application relies heavily on the year-end 2002 expense account balances, I removed  
23 these two balances from the Office Expense account in a normalizing adjustment.  
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4 United State Department of Labor, Bureau of Labor Statistics. USDL: 02-389. Released July 16, 2002. Employee Benefits in Private Industry, 2000. Page 5. OCA Exhibit MLN-6

5 United State Department of Labor, Bureau of Labor Statistics. USDL: 02-389. Released July 16, 2002. Employee Benefits in Private Industry, 2000. Page 5. OCA Exhibit MLN-6

1 The Advertising expense is increased by \$68, which is the weighted average of the years  
2 2000 (weighting of 1), 2001 (weighting of 2), and 2002 (weighting of 2). Within the  
3 weighted average calculation I including the 2002 Advertising expense removed from the  
4 Office Expense account (\$349.20).

5  
6 I have also decreased Engineering Expense account by \$3,000 and the Miscellaneous  
7 Income account by \$1,612.50. These same adjustment are made as engineering  
8 expense due to the expansion of the system is billed to the new customers who cause the  
9 expense. The income from these customers is booked to the miscellaneous income  
10 account. In the year 2002, \$1,612.50 was recovered from these new customers. Since  
11 this is a one-time event, these costs and income were eliminated to normalize these two  
12 accounts. Mr. Lowham testified in Docket No. 80007-WC-02-16 (McDonald vs. Vista  
13 West) that the total bill from the engineers, plus Mr. Holmquist's overtime pay, and the  
14 mailing expense was billed to customer (split eleven ways). The Company has recovered  
15 \$1,612.50 from customers according to the miscellaneous revenue account in 2002. I  
16 decreased the engineering expense in the Company's budget projection by the full  
17 amount of \$3,000 due to the fact that the Company testified in Docket No. 80007-WC-02-  
18 16 that the total amount of the engineering expense is recovered from the customers for  
19 which the engineering expense was incurred. The Company submitted the same  
20 engineering bills in this case as in Docket No. 80007-WC-02-16; therefore, the Company  
21 has clearly represented in a previous proceeding (Docket No. 80007-WC-02-16) that  
22 these bills are reimbursed by the customers that were the cost causers. These expenses  
23 should not be included in this case as they are not expenses that are appropriately  
24 recovered on a recurring basis from all ratepayers as well as the new customers.

25  
26 The decrease of \$122 per annum in Bad Debt expense is decreased in OCA Exhibit  
27 MLN-1 to account for the inconsistent balances from year to year in this account. I took a  
28 weighted average of the years 2000 (weighting of 1), 2001 (weighting of 2), and year

1 2002 (weighting of 2). I gave more weight to the years 2001 and 2002 due to the fact that  
2 it is a more recent balance. This adjustment normalized the account.

3  
4 I decreased the Repairs and Maintenance expense account by \$2,119 per annum. The  
5 calculation for the decrease in the Repairs & Maintenance expense account is based on a  
6 weighted average of the years 2000 (weighting of 1), 2001 (weighting of 2), and 2002  
7 (weighting of 2). I used the weighted average adjustment to account for a portion of the  
8 large increase and variance between the year 2000 and 2001. The increases are due  
9 largely to the construction of the new sewer system in the service area. This construction  
10 will not continue indefinitely. The adjustment does not pinpoint specific expenses due to  
11 the lack of information provided to the OCA by the Company.

12  
13 The decrease of \$104 per annum in the Supplies expense account is based on a  
14 weighted average of year 2000 (weighting of 1), 2001 (weighting of 2), and 2002  
15 (weighting of 2). I used the weighted average adjustment for these expenses due to the  
16 large variances in the account balances from year to year. The larger weighting is used in  
17 the more recent years to account for more recent expense patterns. The adjustment  
18 normalized the account.

19  
20 **Q In your review of the Company's records, what was included in the Travel/ Auto**  
21 **Expense account?**

22 **A** In review of the Company's records and through discovery requests I was able to  
23 determine that the items posted to this general ledger account are for travel and lodging  
24 for Mr. Lowham to various meetings in Casper and in Cheyenne. The company arrived at  
25 the projected expense by using the IRS mileage allowance of \$0.36 per mile for 5,600  
26 miles (\$2,016) and \$500 for meals and lodging. Lowham Associates furnishes the  
27 vehicle driven by Mr. Lowham for Vista West travel.

1 **Q How much have these expenses increased since the last rate case?**

2 A The account has increased from \$500 per year in the last rate case to \$2,000 per year in  
3 the year 2002 (Exhibit MLN-1).

4  
5 **Q What is included in this rate case in the Travel/Auto Expense account that was  
6 not included in the last rate case?**

7 A The same type of expenses is included in this account as seen in the previous rate case.  
8 The account includes expenses incurred when Mr. Lowham is required to travel to  
9 hearings and conduct other company business.

10  
11 **Q Why have these expenses increased since the last rate case?**

12 A The major reason is that Mr. Lowham has been required to travel to the Public Service  
13 Commission more often than in previous years. Unfortunately the Company could not  
14 provide a detail of these expenses, thus I used the weighted average approach to make  
15 the appropriate adjustment.

16  
17 **Q Did the OCA make an adjustment in the Travel/Auto Expense account?**

18 A Yes. I decreased these expenses by \$1,309 per annum. The decrease in the Travel/Auto  
19 Expense account in OCA Exhibit MLN-1 is based on a weighted average of year 2001  
20 (weighting of 1), year 2001 (weighting of 2) and 2002 (weighting of 2). I used the  
21 weighted average adjustment for these expenses due to the large variances in the  
22 account balances from year to year as well as the lack of information that would enable the  
23 OCA to make more specific adjustments. The larger weighting is used in the more recent  
24 year to account for more recent expense patterns. This adjustment normalizes the  
25 account. The large balance in the account in 2002 is not a normalized balance based on  
26 the historical differences in the account balance. In addition, the increase in the number of  
27 cases in the past year for which Mr. Lowham was required to travel appears to be an  
28 anomaly, and there is no basis for predicting a continued dramatic increase.

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**Q What is the result of your review of Vista West’s cost of debt in this case?**

A Through discovery, the OCA obtained a copy of the amortization schedule of the debt of Vista West. The company secured new financing on April 23, 2003. The total amount of the loan is \$300,000. The company was required by the lending institution to keep \$53,000 in reserve in a certificate of deposit (CD) in that institution. The company earns 3.15% per annum on that CD, which decreases the net interest rate on \$53,000 of the loan from 6.15% to 3% (6.15% - 3.15% = 3%). The remaining \$247,000 loan is a 6-year loan at 7.51% interest. In securing new financing, the Company has decreased its interest rate by 2.25% (using 9.76% prior loan – 7.51% majority of new loan balance).

**Q Are the salary ranges in the application within an acceptable range of reasonableness?**

A The Company is requesting an increase of 10% in regard to the salary of each of the employees. It is difficult to assess the appropriateness of the salary ranges for these employees as the duties of the employees of the Company were only vaguely described to the OCA. However, if the duties and responsibilities of the employees were known, it would remain difficult to determine whether the current salaries are appropriate given that each company, market, and individual credentials are vastly different. In addition, I was unable to gather data in order to assess the appropriateness of the salary levels with the duties that were provided by the Company. However, I did conduct a current comparative analysis of the proportion of the expenses salaries represent for other water companies in Wyoming. The table below indicates an average ratio of 15%. The requested proportion in the Vista West application is 21%. This exceeds the average for the sample, but is within the range of the sample itself.

	<b>Salaries % Expenses</b>
<b>Clingers</b>	7%

Gross Venture Utility Co.	25%
Lake Water Co. Ltd, LLC	13%
Orchard Valley Water Co.	11%
Red Lane Domestic Water Inc	20%
<b>Average</b>	<b>15%</b>

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**Q Did you conduct any analysis in order to determine the appropriateness of the 10% salary increases?**

A Yes. I conducted a cost of living increase analysis from the previous case to present using Wyoming regional inflation rates issued by the Wyoming Department Administration and Information Division of Economic Analysis.<sup>6</sup> The following table depicts the annual inflation rates for the central region of Wyoming.

Year	Inflation Rate <sup>7</sup>
2000	3.4%
2001	2.9%
2002	5.1%
<b>Total</b>	<b>11.4%</b>

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If the year 2000 number is adjusted to account for the 8 months (May through December) in which the previous rate case went into affect, the cumulative inflation rate for the area from 2000 through 2002 is 10.27%. Therefore, this analysis illustrates that the requested increase in salary, closely matches the region's inflation rate since the previous rate case, which increases the officer's salary to a level that is analogous to the corresponding increase in the cost of living in the area.

**Q Are all of the requested salary increases at a level of 10% in this case?**

A Vista West has requested salary increases over the current levels of salary. The

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<sup>6</sup> State of Wyoming, Department of Administration and Information, Economic Analysis Division. Wyoming Cost of Living for the Fourth Quarter 2002. Released March 27, 2003. Page 4.

<sup>7</sup> Source: Wyoming Cost of Living for the Fourth Quarter 2002, March 27, 2003, Table III, Annual Inflation Rates by Region, Central Region (Converse, Fremont, Natrona Counties).

1 requested increase is not a 10% increase over what was approved in the last rate case  
2 for all employees. The field personnel salaries have increased an average of 5.65% per  
3 year from 2000 through 2002 (total of 16.95%). The increase for officer salaries is a 10%  
4 increase over the previous rate case and the current level. This salary has not increased  
5 since the prior rate case.

6  
7 **Q Is the salary increase for the two field personnel a reasonable request?**

8 A Clearly the field personnel salaries have not only kept up with inflation (cost of living), but  
9 have surpassed the inflation rate for the area since the previous rate case. However, to  
10 determine the appropriateness of the salary level of two such personnel that corresponds  
11 to the duties and certification of these personnel is beyond the analysis conducted here.

12  
13 **Q Is the salary increases requested by the Company in this case reasonable?**

14 A It is hard to judge. In the case of the officer of the company, his salary increase request is  
15 in line with increases of the cost of living in the Casper area. However, the assessment of  
16 the base salary of the officer is beyond the capacity of this analysis. In the case of the  
17 field personnel, the increase must be considered an increase base salary, as the salary  
18 levels have more than kept pace with the cost of living increases in the area the past few  
19 years. However, the precise determination of appropriate base salaries for these  
20 individuals is beyond the capacity of this analysis.

21  
22 **Q How do the revenues and expenses approved by the Commission in the last rate  
23 case compare with the end of the year results for 2002?**

24 A By the end of the year 2002, the revenues have increased by 11.27% and the expenses  
25 have increased by 24.95% over the last rate case (OCA Exhibit MLN-3). The most  
26 notable increases are in Officer's Health insurance benefits, Office Expense, Travel/Auto  
27 Expense, Repairs and Maintenance, and Lab Analysis.

1  
2 **Q Which expense accounts illustrate a cost savings or cost reduction since the**  
3 **previous rate case?**

4 A In the previous rate case, the Company requested and the Commission approved a total  
5 of \$28,633 annual accounting expense. In this case the Company is requesting an annual  
6 expense of \$11,500 for accounting. The reduction in this expense is primarily due to a  
7 change in accounting firms made by the company. However, in reviewing the total  
8 expense for these same services the Bank Charges must be added to this number. The  
9 Bank Charges expense account now includes the bill collecting expenses as Vista West  
10 has implemented a new billing method.

11  
12 The Bank Charges account requested annual total in this case is \$4,100, of which \$3,600  
13 is for the payment of the collection services First Interstate Bank now provides to Vista  
14 West (OCA MLN-1, line 21, column F). This new collection system includes a lock box for  
15 bills at the bank as well as the option for customers to send payments directly to the bank.  
16 The bank then posts the payment to the customer's Vista West account. The bookkeeper  
17 then downloads all of the customer account payment information from the bank. This  
18 system creates a barrier between the accountant and the payments from customers,  
19 which is a good internal control.

20  
21 Unfortunately the financials submitted by Vista West in this case do not illustrate a  
22 decrease in accounting expenses from the 2002 expense to the budget projections.  
23 Therefore, the adjustment previously described was made to this account.

24  
25 **Q In the last case the new radio equipment had been installed. Is there now better**  
26 **detection of line losses due to this technology?**

27 A No. The Company has not been able to conclude with greater accuracy what the actual  
28 line losses are since the last rate case. This is due to the fact that the new sewer system

1 being constructed in the service area has led to a slight increase in the line losses related  
 2 to the construction, such as accidental cutting of water lines. It is expected that after  
 3 completion of the new sewer system installation in the area, this new equipment will  
 4 improve the detection of line loss.

5  
 6 **Q How are the Fire Hydrant and Valve repair expenses treated on the Vista West  
 7 expense accounts?**

8 **A** In the previous rate case, the Commission approved \$4,000 for annual repair or  
 9 replacement of fire hydrants and valves. However, in the Order (Docket No. 80007-WR-  
 10 99-8, paragraph 44), the Commission decided that these funds should be earmarked and  
 11 accounted for separately. It doesn't appear that these expenses have been separated.  
 12 The OCA recommends the Commission renew its instruction that these expenses to be  
 13 tracked separately.

14  
 15 **Q Did you conduct any analysis to determine if the Rent expense is appropriate?**

16 **A** Yes. I conducted an analysis of commercial property rent in the City of Casper. Currently  
 17 Vista West posts \$6,800 to Rent expense, which is the same amount it paid for rent when  
 18 the office was actually located in the City of Casper. The results of my review of  
 19 commercial property rent in the table below are inconclusive.

<b>Commercial Property Rent Study</b>				
	<b>Rent Per Annum</b>	<b>Rent Per Month</b>	<b>Square Footage</b>	<b>Rent Per Square Foot</b>
<b>Vista West</b>	\$ 6,800	\$ 567	550	\$ 1.03
<b>City of Casper Rent</b>				
1			Windowed office in Casper with Parking	\$ 7.50
2			Windowed office in Casper with Parking	\$ 8.50
3	\$ 2,220	\$ 185	444	\$ 0.42
4	\$ 4,500	\$ 375	898	\$ 0.42
5	\$ 1,500	\$ 125	150	\$ 0.83
6	\$ 4,500	\$ 375	632	\$ 0.59
7	\$ 1,200	\$ 100	138	\$ 0.72
8	\$ 10,200	\$ 850	1360	\$ 0.63

9	\$	11,400	\$	950	1454	\$	0.65
10	\$	9,420	\$	785	980	\$	0.80
11	\$	8,400	\$	700	1375	\$	0.51
12	\$	1,488	\$	124	150	\$	0.83
13	\$	11,700	\$	975	3800	\$	0.26
14	\$	14,400	\$	1,200	1200	\$	1.00
15	\$	23,700	\$	1,975	700	\$	2.82
16	\$	11,400	\$	950	1600	\$	0.59
<b>Average</b>		<b>\$ 8,287.71</b>	<b>\$ 690.64</b>	<b>1,063</b>	<b>\$ 1.69</b>		
<b>Standard Deviation</b>		<b>\$ 6,318.00</b>	<b>\$ 526.50</b>	<b>\$ 936.21</b>	<b>\$ 2.53</b>		
<b>Average Without 1 &amp; 2</b>		<b>\$ 8,287.71</b>	<b>\$ 690.64</b>	<b>\$ 1,062.93</b>	<b>\$ 0.79</b>		
<b>Standard Deviation</b>		<b>\$ 6,318.00</b>	<b>\$ 526.50</b>	<b>\$ 936.21</b>	<b>\$ 0.62</b>		

1  
2 This study is the result of gathering data from advertisements in the Casper area. The  
3 results are inconclusive because that assessment of the commercial rental space in  
4 Casper yielded results that vary widely, even on a square footage basis. The standard  
5 deviations in prices and square footage are larger than the averages in the study. The  
6 large variation decreases the value of the study. It is my opinion that there are most likely  
7 large differences in rental prices due to condition of the property and location. These  
8 differences cannot be calculated into this study, as an appraisal analysis would be  
9 required.

10  
11 I am including this study in my testimony to demonstrate that the rental expense is  
12 dependant on several factors other than the average annual or monthly price or the price  
13 per square foot. I also included it to point out that the Company could rent office space in  
14 Casper for the \$567 per month it posts to the Rent expense account. The Rent expense  
15 of Vista West does not seem unreasonable in comparing the average price per year or  
16 average price per month. However, the study presented here is only representative of the  
17 vast variation of rental expense for commercial property within the City of Casper.

18  
19 **Q What is significant about ensuring that the Company is a ‘going concern’?**

20 **A** It is important to ensure that the Company will perpetually exist and provide service to its  
21 customer even if the management or owner of the Company changes. In doing so, it is

1 important to allow rates to be set in a manner that captures reasonable and prudent  
2 expenses of the Company and allows for a reasonable return. Setting rates in this manner  
3 creates an incentive for the Company run efficiently and creates a financially healthy  
4 company that will continue to be attractive to potential managers or buyers.

5  
6 However, it is important to ensure that extravagant expenses that are inappropriate are  
7 not recovered from ratepayers. Although the allowance of such expenses could make the  
8 company more attractive to would be buyers (of the company) they may not reasonable  
9 and prudent to be recovered from ratepayers. It is important to set appropriate  
10 boundaries for expenses that are allowed to be recovered from ratepayers. It is important  
11 that items that become increasingly expensive or an unreasonable share of the overall  
12 expenses of the Company be appropriately assessed against market parameters, such  
13 as national utility company employee health care insurance expenses. It is unreasonable  
14 to expect that dramatically rising health insurance costs should be perpetually passed  
15 onto ratepayers without limit. Health care insurance not commodity costs and should not  
16 be treated as such.

## 17 18 **B. Return**

19  
20 **Q What is Vista West's requested rate of return?**

21 A Vista West has not specifically requested a rate of return in this case. However, the  
22 Company is requesting a \$20,000 dividend per annum.

23  
24 **Q What recommendations is the OCA making in regard to the annual allowed rate of  
25 return in this case?**

26 A The OCA recommends that the return component be set at a percentage in terms of the  
27 proportion of net income to revenues (excluding the revenues collected from commodity  
28 sales), or profit margin. The allowed profit margin should be set at 8.9% (see analysis

1 below).

2  
3 The OCA is recommending that the return from which dividends can be paid be  
4 specifically determined and stated in the Order in this case. In the past, the Company has  
5 taken all of the net income or more for distribution of dividends. There is no incentive for  
6 instillation of efficiencies within the Company if there are no consequences for dividend  
7 distributions that exceed the net income. This situation creates negative owners equity,  
8 which essentially is a loan to the shareholder. To properly align the incentive for efficiency  
9 within the business a cost should be associated with this type of loan. There is an  
10 opportunity cost in a debit balance (negative balance) for retained earnings as well as  
11 other negative equity balances within the business. For example, the money the  
12 shareholder is distributed against future earnings that could be used to pay down the debt  
13 of the company to create a more efficient debt structure, which eventually translates to  
14 lower rates to the customers. The use of the distributions now against future earnings is  
15 not an uncommon practice, however, they should be paid back to the company with  
16 interest (or opportunity cost) in order to protect the best interest of ratepayers.

17  
18 The OCA further recommends that the Commission states in its Order that if distributed  
19 dividends exceed the net income of the Company, the shareholder be required to pay  
20 interest on the deficiency (dividends minus net income) annually. If no interest is paid  
21 back to the Company, ratepayers are essentially loaning the shareholder money, free of  
22 charge. In addition, the OCA recommends that the interest payment be made annually to  
23 Vista West at the Company's weighted average cost of debt of 6.71%. I am advocating  
24 this rate because the owner's equity balance has been negative for several years;  
25 therefore, an interest rate that is a long-term interest rate is more appropriate.

26  
27 If the Commission decision in this required the shareholder to pay back this loan (in full)  
28 annually, an appropriate shareholder loan interest rate could be an index rate based on

1 continuous averages for a one-year Treasury security, which is the 1 year Treasury  
2 Constant Maturity Rate. If payment in full was required annually an appropriate rate could  
3 be the November ending 1 year Treasury Constant Maturity Rate so that the shareholder  
4 has enough time in which to assess the interest rate and make the payment by the end of  
5 the year.

6  
7 The history of distributions is troubling. In 1999, the Company paid out \$70,000 in  
8 dividends to the shareholder. Most of this money came from the \$60,000 sale of assets  
9 of the Company in that year. However, the ratepayers did not get a share of this sale. If  
10 there is a sale of assets from the Company, the ratepayers should not be responsible for  
11 a larger return. Instead, the ratepayers should have benefited from a smaller return in that  
12 year, as the balance of the assets would have decreased and the balance of the loan on  
13 those assets would have decreased. In a small company such as Vista West, the return  
14 and the financial health of the company is determined by ratio analysis or by net income  
15 for rate making purposes due to the fact that the assets are nearly fully depreciated. The  
16 ratepayers should gain efficiencies in a profit that is over and above a percentage set by  
17 the Commission in the form of increased principal payment of the debt that is held by the  
18 company, or eventually in, a rate reduction if the efficiency persists.

19  
20 **Q How does Vista West pay out a \$20,000 dividend if its net income was only**  
21 **\$13,755 for the year 2002?**

22 **A** Essentially, this money comes out of retained earnings. In OCA Exhibit MLN-2, line 35,  
23 there is a debit balance (negative balance) in the Retained Earnings owner's equity  
24 account from which the difference is booked (OCA Exhibit MLN-2), which is a common  
25 practice for companies. Nevertheless, it is alarming that the Retained Earnings account  
26 has been in a debit balance since the year 2000.

27  
28 A debit balance in the Retained Earnings account signifies that the shareholder has taken

1 a distribution against future earnings of the Company. In other words, the owner, or  
2 shareholder, owes the company money. If the owner of the S corporation (Vista West)  
3 distributes more dividends than the net income, basically, the owner is taking a loan from  
4 the company. These loans appear to have been taken without interest.

5  
6 **Q Does the OCA have other concerns in regard to the owner's equity accounts on**  
7 **the balance sheet?**

8 **A** Yes. In the owners equity portion of the balance sheet there is a debit balance (negative  
9 balance) in the Treasury Stock account (OCA Exhibit MLN-2). This account is used in  
10 corporations to illustrate the amount of equity the company has purchased back from  
11 shareholders. In this case, the balance is negative (debit balance) and illustrative of the  
12 fact that the company has purchased \$2,680 more stock back from the shareholder than  
13 the Common Stock and Additional Paid in Capital accounts combined.

14  
15 The Company has stated through discovery that the debit balance in Treasury Stock  
16 represents an actual payment Vista West made to a departing shareholder in redemption  
17 of common stock approximately 20 years ago. It is particularly troubling that the debit  
18 balance has remained in this account for approximately 20 years, and that the Treasury  
19 Stock negative (or debit) balance exceeds the Common Stock and Additional Paid-in-  
20 capital accounts by \$2,680, or over 50%. Essentially, this is another shareholder loan,  
21 which has opportunity cost associated with it. The OCA recommends that a cost to the  
22 shareholder be included as outlined above.

23  
24 In OCA Exhibit MLN-1, I created a revenue account entitled "Interest Income on  
25 Shareholder Loans". The balance of this account in Column G reflects an annually  
26 calculated interest payment in the amount of \$1,127. The calculation of the loan balance  
27 includes a weighted average of the account totals of the Treasury Stock and Retained  
28 Earnings accounts for the year 2000 (weighting of 1), 2001 (weighting of 2), and 2002,

weighting of 2) multiplied by the weighted average cost of debt of the Company of 6.71%.  
Therefore each of the recent preceding year balances is taken into account.

**Q How did the OCA conduct its analysis in determining that the appropriate profit margin for Vista West is 8.9% ?**

**A** First I conducted an analysis of large water companies using 2002 annual report data to determine the comparable profit margin for other water companies (see table below).

<b>Annual Report Statistics Water Companies -Year 2002<sup>8</sup></b>	<b>Operating Revenues</b>	<b>Income Available for Common equity</b>	<b>Net Income/ Revenues</b>
American States Water Co.	\$ 209,205,000	\$ 20,339,000	9.72%
American Waterworks Co.	\$1,715,173,000	\$ 146,918,000	8.57%
Artesian Resources Corp	\$ 33,644,000	\$ 4,125,000	12.26%
California Water Service	\$ 263,151,000	\$ 19,073,000	7.25%
SJW Corp	\$ 143,092,000	\$ 13,295,000	9.29%
Southwest Water Co.	\$ 130,800,000	\$ 6,002,000	4.59%
<b>Average</b>			<b>8.9%</b>
<b>Standard Deviation</b>			<b>2.57%</b>

I then conducted the same analysis using Wyoming water companies that are regulated by the Wyoming Public Service Commission.

<b>Wyoming Water Companies (2002 Annual Report Data)</b>	<b>Operating Revenues</b>	<b>Income Available for Common equity</b>	<b>Net Income/ Revenues</b>
Broken Wrench LLC	\$ 17,546	\$ 1,836	10.46%
Clingers	\$ 72,169	\$ 5,042	6.99%
Gross Venture Utility Co.	\$ 88,334	\$ 20,579	23.30%
Happy Valley Pipe Line Co.	\$ 4,321	\$ 3,110	71.97%
Lake Water Co. Ltd, LLC	\$ 23,340	\$ (4,147)	-17.77%
Orchard Valley Water Co.	\$ 14,332	\$ 1,648	11.50%
Red Lane Domestic Water Inc	\$ 34,407	\$ 12,376	35.97%
Soldier Creek Water Co	\$ 24,017	\$ (7,836)	-32.63%
<b>Average</b>			<b>11.7%</b>

<sup>8</sup> This data was collected from the annual reports on each of the respective company web cites.

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In the Wyoming water company analysis I initially rejected the high and the low numbers (shaded above) as the degree of variance from the mean of the sample was too large to make the sample significant. Therefore, I calculated the average of the sample excluding these two outliers.

In comparing the two analyses, I recommend that the 8.9% profit margin (net income/revenues) calculated from the respective company annual report data is the appropriate measure of the allowed return in this case. Although these water companies are significantly larger than Vista West, this data has a lower degree of variance than the data collected from the Wyoming water companies and represents comparable companies in the water company utility market. The Wyoming data illustrates a standard deviation from the mean of 18%, whereas the standard deviation in the larger company analysis is 2.57%.

**Q Did you conduct any other analysis in regard to return in this case?**

**A** I also conducted an analysis based on the C.A. Turner Utility Reports<sup>9</sup> data average debt to equity ratio and average allowed rate of return on equity (10.5%). In this analysis I used the weighted cost of debt of Vista West. The calculated weighted average cost of capital in the table below is 8.5%, which is significantly close to the 8.9% I calculated in the previous analysis. The comparative analysis of the water companies represents comparable companies by nature of business. These analyses indicate that in a competitive environment, a water company such as Vista West would reasonable expect to earn a return of 8.9% (profit margin). The results of the studies conducted illustrate a reasonable profit margin of 8.9%, which I recommend be set as Vista West's allowed rate

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<sup>9</sup> C.A. Turner Utility Reports, March 2003

1 of return as a profit margin.

	Weight <sup>10</sup>	Cost	WACC
Debt	53.00%	6.71%	3.56%
Equity	47.00%	10.50%	4.94%
Total	100.00%		8.5%

3  
4 The cost of debt in the table above is based on the weighted average cost of debt for  
5 Vista West as calculated in the table below.

Co. Loans	Weight	Cost	W. Aver
\$ 247,000	82.33%	7.51%	6.18%
\$ 53,000	17.67%	3.00%	0.53%
\$ 300,000	100.00%		6.71%

6  
7 It is important to indicate by Order an allowed rate of return. In this case, an appropriate  
8 return measure is the profit margin advocated by the OCA. By setting an allowed rate of  
9 return, the Commission will ensure that the interests of the ratepayers are address  
10 continually within the Company. An allowed rate of return will ensure that Vista West  
11 assesses efficiency gains financially and operationally while still allowing a reasonable  
12 return to be earned by the shareholder.

### 13 14 **C. RATE DESIGN**

15  
16 **Q What are the principles you used in analyzing the rate design in this case?**

17 **A** In analyzing the requested rate design, as well as in the development of the OCA rate  
18 design, I assessed the cost of providing the service to the customers (fixed and variable),  
19 the differences in the cost to serve between water users versus dry meter customers, any  
20 potential subsidization between the two different classes of customers, and assessment  
21 of the affordability of the final rate design recommendation.

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<sup>10</sup> This weighting is based on the industry average common equity ratio published in the C.A. Turner Utility Reports,

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The cost of service for the customer classes is an important aspect in setting rates where the cost causers are paying for the facilities they use. In designing rates that illustrates the proper cost signals to customers, subsidization between classes is minimized. However, the rate design should provide fairness and affordability to the ratepayers.

I used the same variations between customer classes as approved by the Commission in the previous rate case. I decreased the fixed customer charge for water users and Dry Meter customers by \$0.43 per month. I increased the commodity rate by \$0.13 per the pass on portion of the application. I did not change the non-commodity portion of the volumetric rate, rather I am proposing the same \$1.81 per 1,000 gallons as is currently in rates. This rate design produces revenues, which deduces a profit margin of 8.9%, which is the OCA recommendation in this case.

The OCA rate design increases the average customer's bill (based on 6,332 gallons per month) by \$0.35 or 0.85%. Vista West's rate design would increase the customer's bill by \$4.94 or 11.96%.

The OCA rate design maintains the integrity of the variation between the water users and dry meter customers determined in the previous rate case. Therefore, the dry meter customers and water users are still responsible for a share of the investment in the system capacity.

**D. TARIFFS**

**Q Has Vista West submitted tariff pages in this case?**

**A Yes.**

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March 2003.

1  
2 **Q Has Vista West requested any changes to its tariff language other than the**  
3 **increase in rates requested in this case?**

4 A No.

5  
6 **Q Is the OCA recommending any changes to the tariff language of Vista West?**

7 A Yes. The OCA recommends that the commodity portion of the volumetric rates be  
8 separated from the non-commodity portion of rates in the tariff pages. Unbundling the  
9 rates in this manner will allow for an easier identification of commodity versus non-  
10 commodity within the tariff pages. It will allow for clear identification and tracking of the  
11 two different portions of the volumetric portion of the rate. When Vista West files for a  
12 general rate increase or a pass on application, as it has in this case, without clearly  
13 identifying the separate rates, it is unreasonably difficult to determine what portion of the  
14 rate is commodity and what portion is non-commodity. Therefore, the OCA recommend  
15 that the Company adhere to the Commission Rule, Section 249 as discussed earlier in  
16 my testimony.

17

## 18 **IV Summary**

19

20 **Q Please provide a summary of the recommendations the OCA is making in this**  
21 **case.**

22 A The OCA recommends that the Commission approve the pass on increase as it has been  
23 submitted in the application on a dollar for dollar basis. The OCA recommends that the  
24 Commission adopt all of its revenue and expense adjustments in this case and  
25 specifically identify the allowed profit margin of 8.9% for Vista West in the Order in this  
26 case. The OCA further recommends that the negative equity balances be treated as  
27 loans to the shareholder and that those loans be paid back at an interest rate that is equal

1 to the weighted average cost of debt of the Company. I also recommend that the  
2 Commission adopt the rate design in OCA Exhibit MLN-4 as it keeps the integrity of the  
3 proper rate design set forth in the previous rate case, is a minimal impact to the Vista  
4 West customers, and deduces the proper profit margin determined by the OCA.

5

6 **Q Does this conclude your testimony?**

7 **A** Yes it does.