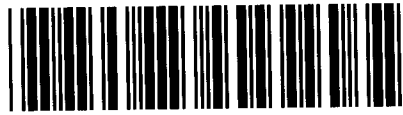


Control Number: 44236



Item Number: 85

Addendum StartPage: 0

**SOAH DOCKET NO. 473-15-4944.WS
PUC DOCKET NO. 44236**

**APPLICATION OF CUSTOM WATER
COMPANY, LLC. FOR WATER
RATE/TARIFF CHANGE**

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**BEFORE THE STATE OFFICE
OF
ADMINISTRATIVE
HEARINGS**

FILED
2015 OCT 23 AM 11:09
PUBLIC UTILITY COMMISSION
FILING CLERK



**DIRECT TESTIMONY OF
EMILY SEARS
WATER UTILITY DIVISION
PUBLIC UTILITY COMMISSION OF TEXAS
OCTOBER 23, 2015**

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Table of Contents

1	I. INTRODUCTION OF WITNESS.....	1
2	II. PURPOSE AND SCOPE OF TESTIMONY.....	2
3	III. RECOMMENDATION.....	2
4	A. SUMMARY.....	2
5	B. RATE OF RETURN.....	2
6	C. COMPANY POSITION.....	5
7	D. STAFF POSITION.....	5

ATTACHMENTS

Attachment ES-1 Resume of Emily Sears

Attachment ES-2 List of testimonies of Emily Sears

1

2 **I. INTRODUCTION OF WITNESS**

3 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

4 A. Emily Sears, Public Utility Commission of Texas, 1701 N. Congress Avenue, Austin, Texas
5 78711-3326.

6

7 **Q. BY WHOM ARE YOU CURRENTLY EMPLOYED AND IN WHAT CAPACITY?**

8 A. I have been employed by the Public Utility Commission of Texas (Commission) since
9 January 1, 2015, as a Financial Analyst in the Water Utilities Division.

10

11 **Q. WHAT ARE YOUR PRINCIPAL RESPONSIBILITIES AT THE COMMISSION?**
12

13 A. I am responsible for reviewing certificate of convenience and necessity (CCN) applications
14 and amendments, sale/transfer/merger applications, tariff/rate change applications, stock
15 transfers, and rate filings. I am also responsible for preparing testimony and exhibits for
16 contested case matters involving investor-owned, non-profit and governmental water and
17 sewer utilities, and assisting with settlement negotiations.

18

19 **Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL**
20 **EXPERIENCE.**

21 A. I have provided a summary of my educational background and professional experience in
22 Attachment ES-1 to my direct testimony.

1

2 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION OR THE**
3 **STATE OFFICE OF ADMINISTRATIVE HEARINGS (SOAH)?**

4 A. Yes. I have also testified before the Pennsylvania Public Utility Commission. Attachment
5 ES-2 provides a summary of the cases in which I have testified or submitted testimony.

6

7 **II. PURPOSE AND SCOPE OF TESTIMONY**

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

9 A. The purpose of my testimony is to present a recommendation for the rate of return for Custom
10 Water Company, LLC. (Custom).

11

12 **Q. WHAT IS THE SCOPE OF YOUR REVIEW?**

13 A. I reviewed the application of Custom, with respect to rate of return, including capital
14 structure, the cost of debt, the cost of common equity, and the overall fair rate of return.

15

16 **III. RECOMMENDATION**

17 **A. SUMMARY**

18 **Q. PLEASE SUMMARIZE STAFF'S RECOMMENDATION IN THIS PROCEEDING.**

19 A. Staff's recommendation is that Custom's overall rate of return of 5.11% be accepted.

20

21 **B. RATE OF RETURN**

22 **Q. PLEASE DEFINE THE TERM "RATE OF RETURN."**

1 A. Rate of return generally is the amount of revenue an investment generates (in the form of net
2 income), usually expressed as a percentage of the amount of capital invested, over a given
3 period of time. Rate of return is one of the components of the revenue requirement formula.
4

5 **Q. WHAT IS THE REVENUE REQUIREMENT FORMULA?**

6 A. The revenue requirement formula used in base rate cases is as follows:

7
$$RR = E + D + T + (RB \times ROR)$$

8 Where:

9 RR = Revenue Requirement

10 E = Operating Expense

11 D = Depreciation Expense

12 T = Taxes

13 RB = Rate Base

14 ROR = Overall Rate of Return

15 In the above formula the rate of return is expressed as a percentage. The calculation of
16 that rate is independent of the determination of the appropriate rate base value for
17 ratemaking purposes. As such, the appropriate total dollar return is dependent upon the
18 proper computation of the rate of return and the proper valuation of the Company's rate
19 base.
20

21 **Q. WHAT CONSTITUTES A FAIR AND REASONABLE OVERALL RATE OF**
22 **RETURN?**

Direct Testimony of Emily Sears

October 2015

- 1 A. A fair and reasonable overall rate of return is one which will allow the utility the
2 opportunity to recover those costs prudently incurred by all classes of capital used to
3 finance the rate base during the prospective period in which its rates will be in effect.
4 *The Bluefield Water Works & Improvements Co. v. Public Service Comm. of West*
5 *Virginia*, 292 U.S. 679, 692-93 (1923), and the *FPC v. Hope Natural Gas Co.*, 320 U.S.
6 591, 603 (1944) cases set forth the principles that are generally accepted by regulators
7 throughout the country as the appropriate criteria for measuring a fair rate of return:
8 1) A utility is entitled to a return similar to that being earned by other enterprises with
9 corresponding risks and uncertainties, but not as high as those earned by highly
10 profitable or speculative ventures;
11 2) A utility is entitled to a return level reasonably sufficient to assure financial soundness;
12 3) A utility is entitled to a return sufficient to maintain and support its credit and raise
13 necessary capital;
14 4) A fair return can change (increase or decrease) along with economic conditions and
15 capital markets.

16
17 **Q. HOW IS THE RATE OF RETURN CALCULATED?**

- 18 A. The overall rate of return in this rate proceeding is calculated using the weighted average
19 cost of capital method. To calculate the weighted average cost of capital, Custom's capital
20 structure must first be determined by calculating the percentage of each capitalization
21 component which has financed the rate base to total capital. The capital components consist
22 of long-term debt and common equity. Next, the effective cost rate of each capital structure

1 component must be determined. The cost rate of debt is fixed, and can be computed
2 accurately. The cost rate of common equity is not fixed and it is more difficult to measure.
3 Next, each capital structure component percentage is multiplied by its corresponding
4 effective cost rate to determine the weighted capital component cost rate. Lastly, the sum
5 of the weighted cost rates produces the overall rate of return. This overall rate of return is
6 multiplied by the rate base to determine the return portion of Custom's revenue requirement.

7

8 **C. COMPANY POSITION**

9 **Q. PLEASE SUMMARIZE THE COMPANY'S RATE OF RETURN CLAIM IN THIS**
10 **CASE.**

11 **A.** Based on the rate/tariff change application instructions, Custom recommended the
12 following rate of return:

<u>Type of Capital</u>	<u>Ratios</u>	<u>Cost Rate</u>	<u>Weighted Cost Rate</u>
Long-Term Debt	89.52 %	4.53 %	4.06 %
Common Equity	<u>10.48%</u>	10.00 %	<u>1.05 %</u>
Total	<u>100.00 %</u>		<u>5.11 %</u>

13 **D. STAFF POSITION**

14 **Q. PLEASE SUMMARIZE STAFF'S RECOMMENDED RATE OF RETURN IN THIS**
15 **CASE.**

Direct Testimony of Emily Sears

October 2015

1 A. I recommend the following rate of return for Custom:

<u>Type of Capital</u>	<u>Ratios</u>	<u>Cost Rate</u>	<u>Weighted Cost Rate</u>
Long-Term Debt	89.52 %	4.53 %	4.06 %
Common Equity	<u>10.48%</u>	10.00 %	<u>1.05 %</u>
Total	<u>100.00 %</u>		<u>5.11 %</u>

2

3 **Q. WHAT IS STAFF'S RECOMMENDED OVERALL RATE OF RETURN?**

4 A. Staff recommends that Custom's overall rate of return of 5.11% be accepted.

5

6 **Q. WHAT IS THE BASIS FOR YOUR RECOMMENDATION?**

7 A. Custom has provided support for its debt and equity dollar figures. Custom has also
8 provided support for its individual costs of debt, and Staff recommends that a 10% return on
9 equity is fully consistent with the requirements of *Hope* and *Bluefield*¹ that I referenced
10 earlier in my testimony.

11

12

13 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

14 A. Yes. I reserve the right to supplement this testimony during the course of the proceeding
15 as new evidence is presented.

¹ 292 U.S. 679, 692-93 (1923) and 320 U.S. 591, 603 (1944).
Direct Testimony of Emily Sears

Emily Sears

Professional Experience

- **Public Utility Commission of Texas**
Utility Rates Analyst
Water Utilities Division
January 2015 - Present
- **Commonwealth of Pennsylvania, Public Utility Commission**
Fixed Utility Financial Analyst
Bureau of Investigation and Enforcement
May 2009 – December 2014
- **Commonwealth of Pennsylvania, Public Utility Commission**
Fixed Utility Financial Analyst
Bureau of Fixed Utility Services
April 2008 – May 2009
- **Nationwide Insurance Company**
Personal Lines Underwriting Screener
October 2004 – May 2007

Education

- **University of Pittsburgh, College of Business Administration**
Bachelors of Science in Business Administration
Major – Finance
August 2004
- **Annual Regulatory Studies Program: Camp NARUC**
Week 1-Introduction to Regulation
August 2008
- **Pennsylvania Public Utility Commission Rate Case Training**
December 2008
- **Society of Utility and Regulatory Financial Analysts**
Certified Rate of Return Analyst
June 2010

Presentations

- **Pennsylvania Public Utility Commission Rate Case Training**
Presented on Rate of Return/Return on Equity
October 2012, September 2014

TESTIMONY SUBMITTED:

I have testified and/or submitted testimony in the following proceedings before the Pennsylvania Public Utility Commission:

- Duquesne Light Company, Docket No. M-2009-2093217
- West Penn Power Company d/b/a Allegheny Power, Docket No. M-2009-2093218
- Duquesne Light Company, Docket No. M-2009-2123948
- West Penn Power Company d/b/a Allegheny Power, Docket No. M-2009-2123951
- Utilities, Inc. – Westgate, Docket No. R-2009-2117389
- Utilities, Inc. of Pennsylvania, Docket No. R-2009-2117402
- PECO Energy Company - Electric Division, Docket No. P-2009-2143607
- PECO Energy Company – Gas Division, Docket No. P-2009-2143588
- Philadelphia Gas Works, Docket No. R-2009-2139884
- York Water Company, Docket No. R-2010-2157140
- City of Lancaster, Docket No. R-2010-2179103
- Columbia Gas of Pennsylvania, Inc., Docket No. R-2010-2215623
- CMV Sewage, Inc., Docket No. R-2011-2218562
- Pennsylvania American Water Company, Docket No. R-2011-2232243
- UGI Penn Natural Gas, Docket No. R-2011-2238943
- Aqua Pennsylvania, Inc., Docket No. R-2011-2267958
- Equitable Gas Company, LLC, Docket No. R-2012-2287044
- Peoples Natural Gas Company, LLC, Docket No. R-2012-2285985
- PPL Electric Utilities Corporation, Docket No. R-2012-2290597
- Columbia Gas of Pennsylvania, Inc., Docket No. R- 2012-2321748
- The City of Lancaster – Sewer Fund, Docket No. R-2012-2310366
- Columbia Gas of Pennsylvania, Inc., Docket No. R-2012-2321748 and M-2012-2323645
- UGI Penn Natural Gas, Docket No. R-2013-2361763
- City of DuBois – Bureau of Water, Docket No. R-2013-2350509
- Pennsylvania-American Water Company, Docket No. R-2013-2355276
- Duquesne Light Company, Docket No. R-2013-2372129
- Pike County Light and Power Company, Gas Division, Docket No. R-2013-2397353
- Pike County Light and Power Company, Electric Division, Docket No. R-2013-2397237
- UGI Penn Natural Gas, Docket No. R-2014-2420273
- Emporium Water Company, Docket No. R-2014-2402324
- City of Lancaster – Water Fund, Docket No. R-2014-2418872
- Peoples TWP, LLC, R-2014-2429613
- Peoples Natural Gas Company, LLC, R-2014-2429606

I have testified and/or submitted testimony in the following proceedings before the Public Utility Commission of Texas and the Texas State Office of Administrative Hearings:

- City of Austin water rate appeal, Docket No. 42857

- City of Austin wastewater rate appeal, Docket No. 42867