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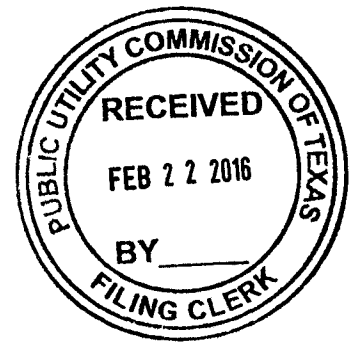
APPLICATION OF QUADVEST L.P. §
FOR A RATE/TARIFF CHANGE §

BEFORE THE STATE OFFICE OF
ADMINISTRATIVE HEARINGS

DIRECT TESTIMONY AND EXHIBITS

OF

JEFFREY EASTMAN



ON BEHALF OF

QUADVEST L.P.

FEBRUARY 22, 2016

DIRECT TESTIMONY AND EXHIBITS
OF JEFFREY EASTMAN

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Exhibits:

Exhibit QVLP-1	Quadvest Utility Affiliate Costs Allocation Report (Page 1 and 2)
Exhibit QVLP-2	QVLP Organizational Chart
Exhibit QVLP-3	Rate Case Expense Invoices

DIRECT TESTIMONY OF JEFFREY EASTMAN

ON BEHALF OF

QUADVEST L.P.

I. BACKGROUND AND QUALIFICATIONS

1

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

3 A. My name is Jeffrey Eastman. My business address is 26926 FM 2978, Magnolia, Texas,
4 77354.

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

6 A. I am the chief financial officer of the applicant, Quadvest LP ("QVLP" or "Quadvest").

7 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL**
8 **EXPERIENCE.**

9 A. I have a Bachelor's degree in accounting from Sam Houston State University. I have
10 over 15 years work experience in various accounting and finance roles with several
11 different companies, ranging from Deloitte and Touché, an international CPA and
12 consulting firm, to QVLP, a regulated water and sewer utility. I have worked at QVLP
13 for over three years and have attended NARUC's utility rate school during this period of
14 employment.

15 **Q. WHAT IS YOUR AREA OF RESPONSIBILITY FOR QVLP?**

16 A. I oversee and manage all accounting and financial matters related to QVLP. In addition,
17 I manage the development of QVLP's regulatory filings related to customer rates.

1 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

2 A. I will introduce each of the expert witnesses filing testimony in this case and provide
3 overall background of the operations and structure of QVLP, what is driving the need for
4 this rate request and a discussion of the Automated Meter Reading system that QVLP is
5 implementing.

6 **Q. HAVE YOU ATTACHED DOCUMENTS TO YOUR TESTIMONY?**

7 A. Yes, they are attached as follows: Exhibit QVLP-1, Exhibit QVLP-2.

8 **Q. PLEASE INTRODUCE THE OTHER WITNESSES WHO WILL BE FILING**
9 **TESTIMONY IN THIS CASE.**

10 A. QVLP retained the services of three expert witnesses to assist QVLP in overall
11 preparation, filing, support, and presentation of its rate case.

- 12 • Mr. Chuck Loy was retained by QVLP to assist in overall preparation, filing and
13 ultimate presentation of its rate case to the Public Utility Commission of Texas.
- 14 • Mr. Greg Scheig was retained by QVLP's council to assist in the development of
15 a reasonable and justifiable rate of return for a small family owned company with
16 limited access to capital.
- 17 • Mr. Morey Villareal was retained by QVLP to provide an assessment of the
18 reasonableness and competitiveness of the compensation practices of QVLP (as
19 compared to the practices of similar firms with comparable jobs in the Houston
20 market) and to provide QVLP management with recommendations to become
21 competitive as it relates to employee compensation and benefits.

22 **II. OVERVIEW OF QVLP**

1 **Q. PLEASE PROVIDE A BRIEF OVERVIEW OF THE HISTORY OF QVLP?**

2 A. QVLP is a state regulated investor owned utility headquartered in Magnolia Texas,
3 currently serving more than 9,400 water connections in 9 counties located in south east
4 Texas. The majority of our connections are located in rural areas, noting this is slowly
5 changing as the “Greater Houston Area” spreads northward. QVLP is a family owned
6 limited partnership, whose family members have been in or around the land development
7 / utility industry for more than 37 years. As in the past, QVLP continues to strive to
8 provide our customers with clean reliable drinking water, great customer service at
9 reasonable rates. As an example of this commitment, our currently proposed rates are
10 between 17% and 87% lower than rates charged by several of the larger investor owned
11 utilities in Texas. We believe this is further confirmed by our customers’ extremely low
12 protest rate to our most recent rate case notice, noting QVLP received approximately 10
13 protests out of 9000 plus water customers.

14 **Q. HOW MANY WATER SYSTEMS DOES QVLP NOW OWN AND OPERATE?**

15 A. QVLP currently owns 41 different water systems (PWS #), noting QVLP had 39 as of
16 rate application filing date and has since then acquired 2 additional systems. The
17 majority of these systems have been constructed by QVLP or Quadvest Construction;
18 therefore these systems share many similarities in regards to overall design, phasing,
19 materials, and components. The low cost of construction services provided by Quadvest
20 Construction is one of the many ways QVLP maintains its reasonable rates. Of the 41
21 system, QVLP operators oversee all but 4 of the systems day to day operations. The 4
22 small systems (less than 250 active connections) are located near the Texas coastline and
23 are managed day to day by a 3rd party operator. We are currently looking into purchasing

1 a larger system in the area to allow us to use internal resources to manage these systems
2 in the future.

3 **Q. DOES QVLP HAVE ANY AFFILIATES AND/OR RELATED PARTIES?**

4 A. Yes. For a high level overview of QVLP related parties, I would like to reference the
5 “Quadvest Utility Affiliate Costs Allocation Report” (specifically pages 1 and 2 of the
6 report) which was prepared by Chuck Loy. See Exhibit QVLP-1. This report was
7 submitted with our rate case application and is also discussed in greater detail in Chuck
8 Loy’s direct testimony. I would like to provide some additional detail as it relates to
9 post-test year changes to QVLP’s affiliates, specifically:

10 Quadvest Construction (“QC”): In late 2015, QC moved out of the offices it
11 shared with QVLP and into several work trailers located behind QVLP offices. QC is
12 currently paying for their utilities, general office expenses such as postage, trailer rental
13 and associated repairs and maintenance. In addition, QVLP is no longer providing any
14 payroll or accounting support to QC.

15 South Texas Development (“STD”): In October 2015, STD elected to foreclose
16 on its work force housing project, which had been previously sold to a 3rd party. Due to
17 the lack of oil field activity around Cotulla Texas, STD has decided to “mothball” the
18 project until it can be sold again. As a result, there is little management and/or
19 accounting resources dedicated to this affiliate.

20 Cotulla Development (“CDC”): Due to the lack of oil field activity around Cotulla
21 Texas, there are less management and/or accounting resources dedicated to this affiliate.

1 Quadlease ("QL"): In January 2016, QL received notice that its lessee will pay off
2 QL's lease receivable in 1Q 2016. As a result, there will be no management and/or
3 accounting resources dedicated to this affiliate.

4 In summary, QVLP resources are being used less now than during our rate case test year.

5 **Q. PLEASE DISCRIBE QVLP FINANCIAL RESOURCES? WHERE DOES QVLP**
6 **GET CAPITAL?**

7 A. QVLP's operating capital and capital to invest in long term capital assets comes from two
8 different sources. The first is cash generated from day to day operations of the utility.
9 The second is long term debt issued mostly by CoBank, noting during higher growth
10 periods general bank covenants can become restrictive.

11 QVLP's relative small size, ownership structure, and limited financial resources restrict
12 its access to many forms of capital. QVLP has attempted to obtain alternative long term
13 financing options from several commercial lenders with no success. To date, QVLP's
14 only long term financing option is CoBank, whom charge higher rates and impose more
15 restrictions than those lending to large publically traded investor owned utilities. Mr.
16 Greg Scheig goes into more detail about QVLP's financial constraints and why a
17 reasonable rate of return is critical to QVLP's growth and overall ability to provide
18 service to its customers.

19 **Q. PLEASE DESCRIBE THE LOCAL MANAGEMENT STRUCTURE?**

20 A. I have attached our current QVLP organizational chart to describe our company structure,
21 see Exhibit QVLP-2. QVLP has added/replaced several key positions since our last
22 water rate case in order handle customer growth and improve overall service quality,
23 noting our water connection count has increased over 30% since FY2012. These

1 positions include: 1) A Chief Financial Officer to replace a part time accounting/finance
2 consultant. 2) A Customer Service Manager to better coordinate and standardize our
3 customer service efforts. 3) A Human Resource Manager to assist our management team
4 in hiring/training/evaluating/compensating our 30 plus employees. 4) Expanded the
5 Operations Manager role requiring the recruitment of a more experienced and seasoned
6 individual. Finally, our organizational structure continues to remain fluid as our
7 management team adapts to customer growth, employee turnover and the search for
8 operating efficiencies.

9 **Q. WHAT IS QVLP'S CUSTOMER DEPOSIT POLICY?**

10 A. QVLP customer deposit policy is outlined in Section 2.04 of our current tariff. QVLP
11 does collect deposits from our customers and refunds such deposits back to our customers
12 after 18 consecutive billings without a delinquent payment or termination of service.
13 The refund is for the original deposit plus any accrued interest. The vast majority of
14 QVLP's customers have their customer deposits refunded. As such, the customer deposit
15 balance varies greatly from year to year. In addition, all customer deposit cash is
16 maintained in the bank to allow quick and easy refunds to our customers. For the reasons
17 stated above, I do not consider customer deposits a source of cost free capital to QVLP
18 but rather a partial insurance against delinquent accounts.

19 **Q. DOES QVLP MAINTAIN DEFERRED FEDERAL INCOME TAX BALANCES?**

20 A. QVLP is a limited partnership and thus considered a "pass through" entity for federal tax
21 purposes and therefore does not pay federal income taxes. Only the owners of QVLP are
22 required to pay federal income taxes, based upon their individual tax situation, which
23 would include their respective portion of QVLP's taxable income or loss. Now that the

1 PUC has approved new rules and filing requirements, QVLP will develop a protocol to
2 record deferred federal income taxes for rate making purposes on a go forward basis. Mr.
3 Chuck Loy addresses DFIT in his Direct Testimony regarding this case.

4 III. REASON FOR RATE INCREASE

5 Q. WHAT IS DRIVING THE NEED FOR A RATE INCREASE?

6 A. The last water rate case application QVLP filed was based upon a September 2010 test
7 year and was filed early 2011. Since 2010, QVLP has invested approximately six million
8 in capital assets including substantial investments in the following communities:
9 Bayer Water (aka Old Town Spring): QVLP purchase this aging water system, located on
10 the north of Houston, and has subsequently spent over \$700,000 in upgrades to the water
11 system. In addition to the water system improvements, QVLP also installed the town's
12 first gravity sewer system at a cost of over \$1,000,000 (not included in this rate
13 application). At December 2014, there were approximately 320 active customers and
14 currently we have about the same number of active customers. The local and county
15 authorities encouraged these improvements in order to increase tourism in the area.

16 Bauer Landing: During 2014, QVLP worked closely with publically traded home builder
17 LGI Homes to install and operate a new water system to service their new community
18 located west of Tomball Texas. QVLP has invested over \$1,000,000 in the water system.
19 At December 2014, there were approximately 40 active customers and currently we have
20 over 225 active customers.

21 Bella Vista: During 2013 and 2014, QVLP worked with a Texas based developer to
22 install and operate a new water system to service their new community located south of

1 Cleveland Texas. QVLPhas invested over \$700,000 in the water system. At December
2 2014, there were approximately 57 active customers and currently we have over 240
3 active customers.

4 Lake Windcrest: From 2011 and 2014, QVLP added a new water plant and additional
5 water storage capacity to accommodate the increased water demand from the residents in
6 this community. QVLP has invested over \$1,000,000 in the water system. At December
7 2014, there were approximately 870 active customers and currently we have over 880
8 active customers.

9 **Q. WHY IS QVLP PROPOSING AS PART OF THIS FILING TO INCLUDE**
10 **AUTOMATIC METER READERS (“AMR”) AS A “KNOWN AND**
11 **MEASURABLE” ADJUSTMENT?**

12 A. In 2014, QVLP made the decision to strategically migrate its entire service territory to
13 AMRs. QVLP believe AMRs will provide for a better customer service experience,
14 increase water system management, and improve employee safety. QVLP is currently
15 installing AMRs in all new connections and in existing connections requiring a
16 replacement meter. QVLP realize immediate financial benefit from 100% AMR
17 communities because manual meter reading is no longer required. This is not the case for
18 replacement AMRs as we must continue to manually read meters until the entire
19 community is converted to AMRs. The investment needed to complete this 100%
20 conversion to AMR is over \$2 million dollars. As a result, QVLP is proposing as part of
21 the rate case application to include these capital costs as a known and measurable
22 adjustment but defer charging our customers until all AMRs are placed into service (i.e.
23 make the investment before recovery of the investment). Phase II of our proposed rate

1 increase relates directly to the AMR conversion project and will not be implemented until
2 this project is complete and approved by Public Utility Commission Of Texas. QVLP's
3 proposed Phase II rate treatment will provide our lenders assurance that QVLP will be
4 able to begin recovery of its large investment almost immediately, which in turn will
5 reduce the risk of QVLP breaching bank covenants in the future.

6 **Q PLEASE DISCUSS QVLP'S PROPOSAL TO CONSOLIDATE FIVE DIFFERENT**
7 **TARIFFS UNDER SINGLE TARIFF RATES.**

8 A. Mr. Chuck Loy addresses why QVLP meets the regulatory requirements for regional
9 tariffs in his Direct Testimony. In addition, I will address some of the more practical
10 benefits that result from a regional rate tariff and consolidated rates, such as:

- 11 • More efficient and accurate communication with our both existing and future
12 customers: A one tariff environment allows our customer service department to
13 easily communicate with our entire population of customers as opposed to having to
14 develop separate communications for each of our tariff groups. In addition, it reduces
15 customer service call times because our customer service representatives do not have
16 to spend time determining a customer's applicable tariff before addressing his/her real
17 issue.
- 18 • Reduces the "rate shock" that would be experienced by communities that are either
19 small in size or early in development.
- 20 • Reduces the number and even the frequency of tariff, rate, and pass through filings
21 with the Public Utility Commission. The result is savings to both QVLP customers
22 and the State of Texas.

23 **Q. PLEASE ADDRESS THE RATE CASE EXPENSES QVLP HAS PAID TO DATE.**

A. The below figures represent rate case expenses incurred by QVLP (As January 31, 2016):

- GDS Associates (General Rate Case Consulting): \$84,464
- Cozen O'Conner (Rate Case Legal Representation): \$42,276**
- Robert E Degeyter, CPA (General Rate Case Consulting): \$5,500
- Southern Imaging & Laser Print (Mailing Rate Case Notices): \$8,495
- ValueScope (Mr. Greg Scheig - Rate of Return Services): \$14,215**
- Villareal & Associates (Mr. Morey Villareal – Compensation Services): \$7,570

***Total: \$ 162,520**

* See Exhibit QVLP-3 "Rate Case Expense Invoices" for invoice level detail.

** A portion of these have been incurred yet not yet invoiced by respective parties.

The below figures represent anticipated rate case expenses to be incurred as a result of QVLP's rate case being referred to SOAH:

- GDS Associates: \$80,000
- Cozen O'Conner: \$80,000
- Southern Imaging & Laser Print: \$9,000
- ValueScope \$8,000.
- Villareal & Associates: \$6,000.

*****Total: \$183,000.**

*** Anticipated rate case expenses include expenses associated with the filing of direct testimony, rebuttal testimony, associated hearings/briefs, and additional customer notifications.