STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

In the matter of

Liberty Utilities (Granite State Electric) Corp.

Docket No. DE 19-064

Petition for Permanent Rate Increase

REDACTED
DIRECT TESTIMONY

OF

Bion C. Ostrander

On Behalf of the
New Hampshire Office of the Consumer Advocate

December 6, 2019

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I. INTRODUCTION

Q. Please state your name, business address and occupation.

A. My name is Bion C. Ostrander; I am President of Ostrander Consulting. My business address is 1121 S.W. Chetopa Trail, Topeka, Kansas 66615-1408. I am an independent regulatory consultant specializing in revenue requirement/accounting issues related to electric, gas, renewable energy, and telecommunication industries.

Q. On whose behalf are you testifying in this proceeding?

A. I am testifying on behalf of the New Hampshire Office of Consumer Advocate ("OCA") in this rate case proceeding before the New Hampshire Public Utilities Commission ("PUC" or "Commission") regarding the revenue requirements of Liberty Utilities (Granite State Electric) Corp. ("Liberty", "G.S." or the "Company").

Q. Please describe your formal education and professional experience.

A. Please see Attachment BCO-1 for my curriculum vitae and Attachment BCO-2 for a list of regulatory proceedings (by jurisdiction/docket/client) where I have participated. I am an independent regulatory consultant with a specialization in regulatory utility issues, and particularly revenue requirement/accounting issues. I have over forty years of regulatory and accounting experience, including twenty-nine years with my firm Ostrander Consulting.

I started my current consulting practice in 1990 after leaving the Kansas Corporation Commission ("KCC"). I previously served as the Chief of Telecommunications for the KCC from 1986 to 1990, and was the lead witness on most major telecom issues, while still assisting with electric/gas utility issues on a periodic basis. I served as Chief Auditor for the KCC from 1983 to 1986, addressing issues regarding the telecom, gas, electric, and transportation industries.

In addition, I have worked for international and regional certified public accounting firms, including Deloitte, Haskin and Sells (now Deloitte) and Mize, Houser, Mehlinger and Kimes (now Mize Houser and Company P.A.).

I previously held a permit to practice as a CPA in Kansas up until recent years, but I no longer perform any CPA-type services requiring a permit to practice. I remain a member of the American Institute of CPAs and the Kansas Society of CPAs.

I received a Bachelor of Science degree in Business Administration with a major in Accounting from the University of Kansas in 1978.

I have addressed many regulatory issues for various state regulatory agencies and for international regulatory and other governmental entities. My experience includes addressing issues related to rate cases under rate of return regulation, alternative regulation/price cap plans, management audits, specialized accounting and regulatory issues and other matters. I have addressed a broad range of regulatory issues in my career, including the levelized cost of renewable energy alternatives, specialized accounting matters, affiliate transactions/Cost Allocation Manual, income taxes (including net operating loss carryback), sale/leaseback, compensation, cross-subsidization, depreciation, retail and wholesale cost studies for telecom, competition, affordable rates/universal service, service quality, infrastructure/modernization, rate design for telecom, sales/acquisitions and many other matters.

Below is a high-level summary of clients I have consulted with in various jurisdictions:

Client Summary	
Consumer Advocates/Attorney General	***Public Service Commissions***
Indiana UCC	Arizona
Florida OPC	Georgia
Kansas CURB	Kansas
Kentucky AG	Maryland
Michigan AG	Minnesota
Maine OPA	North Dakota
Maine AARP	Oklahoma
Maryland OPC	***Other***
Michigan AG	Alaska Competitive Local Exchange Carrier
Minnesota DPS	Maryland - Montgomery County
Nevada AG	Virginia - CWA
New Hampshire	Kansas Counties (911 implementation issues)
Oklahoma AG	***International***
Utah OCS	Fair Trading Commission - Barbados
Vermont DPS	Eastern Caribbean Telecomm. Authority (ECTEL -
Washington AG	St. Lucia, St. Kitts/Nevis, St. Vincent, Grenada, Dominica)
Wyoming	Armenia - USAID
	Russia/Ukraine Energy Utility Training
	Saudi Arabia

Q. Have you previously provided testimony before this Commission?

A. No.

Q. Have you ever provided testimony and performed regulatory consulting services for other U.S. and international regulatory agencies, other international governments, and other entities?

A. Yes. Please see Attachment BCO-2 for a list of regulatory entities by jurisdiction, along with other clients.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to present my analysis and recommendations regarding Liberty's revenue requirements, including addressing related accounting, regulatory, and policy issues. I am also addressing the Company's 2019 Step Increase, although these amounts are not included in the Company's revenue requirement calculations.

Q. Please discuss how your testimony is organized.

A. My testimony consists of three sections:

I. Introduction – Addresses various background information, my qualifications, and a summary of my adjustments and recommendations.

II. Revenue Requirements – Addresses revisions to Liberty adjustments, and additional adjustments that I have identified, along with related policy recommendations when applicable.

III. 2019 Step Increase – Addresses adjustments to Liberty's proposed 2019 Step Increase.

Attachments BCO-1 and BCO-2 address my credentials and a list of cases/proceedings that I have addressed. I am referring to my credentials and qualifications information as "Attachments" to this testimony and referring to my proposed revenue requirement and documentation supporting my proposed adjustments as "Exhibits" to this testimony.

Attachment BCO-1 is my curriculum vitae and Attachment BCO-2 is list of regulatory proceedings where I have participated.

Exhibit BCO-1 is OCA's proposed revenue requirement and related adjustments to rate base and operations. Exhibit BCO-2 is OCA's proposed adjustments to Liberty's 2019 Step Increase. Exhibit BCO-3 and all subsequent exhibits include supporting documentation for my proposed adjustments, such as Liberty's responses to data requests and other documentation as applicable.

Q. What is the test year for this case, and what period does Liberty use for adjusting amounts in this rate case?

A. The test year is the calendar year ended December 31, 2018.

For those operating expense accounts where Liberty proposes an adjustment, it typically adjusts to a "2019 going-forward amount" based on changes in cost that I sometimes consider to be known-and-measurable, and other times I do not consider to be known-and-measurable (or some combination). Sometimes the Company relies on its 2019 Budget to adjust costs (such as the base payroll amount in the Company's payroll adjustments), although most of the time Liberty does not rely on its 2019 Budget amounts. I will address the underlying basis for Liberty's adjustments when this is relevant or a concern.

Q. Will you summarize Liberty's prior electric rate case filing for some perspective on this rate case?

A. Liberty's prior electric rate case, filed on April 29, 2016 in Docket DE 16-383, used a test period ending December 31, 2015 and requested a revenue increase of $5,328,583, a temporary increase of $3,180,666, and a step increase of $2,420,717 (based on additional capital spending of $14,227,039 during 2016). Liberty proposed a return on equity ("ROE") of 10.30 percent and an overall rate of return ("ROR") of 8.32 percent. Liberty proposed to implement the step increase at four different dates, on May 1, 2018, 2019, 2020, and 2021.

On March 17, 2017, the parties submitted a Settlement to resolve all issues, and it provided for a revenue increase of $3,750,000 (about 70 percent of Liberty's original request), coupled with a step increase of $2,473,723, with related step increases to be phased in May 1, 2018 and May 1, 2019. Although certain policy positions were stipulated related to rate design and other matters, the Settlement was a black box revenue requirement agreement and did not address specific rate case adjustments that comprised the agreed-upon revenue requirement. The Settlement uses a ROE of 9.40 percent and ROR of 7.64 percent.

The Commission approved the Settlement on April 12, 2017, in Order No. 26,005.

Q. Will you summarize Liberty's current proposed rate filing?

A. On April 30, 2019, Liberty filed a Petition for permanent and temporary rate increases, including a proposed increase to permanent rates that will yield an annual revenue increase of $5,683,102, a temporary increase in revenues of $2,093,349 (37 percent of the Company's requested total increase), and a step increase of $2,293,431 related to recover the cost of projects completed through December 31, 2019.[1] On June 28, 2019, the Commission approved a temporary rate increase of $2,093,349, an increase of about $2.48 or 2 percent of the total monthly bill.[2]

Liberty proposes a ROE of 10 percent with a related overall ROR of 8.19 percent. Liberty proposes an adjusted rate base of $106,180,186 and an operating income at present rates of $4,552,039.

On November 22, 2019, Liberty filed its Corrections and Updates[3] with the Commission, and the net impact of this filing was an additional revenue deficiency of $990,390, resulting in a revised revenue deficiency of $6,673,493 (compared to the original amount of $5,683,102).

Liberty's revised filing results in an adjusted rate base of $103,024,219 and an operating income at present rates of $3,571,374. The revised filing includes Liberty-proposed adjustments that reduce net rate base by $36.7m, along with revenue and expense adjustments that decrease net income by $5.7m before income taxes.

Q. Will you summarize the OCA's revised revenue requirement and certain significant adjustments and recommendations?

[1] This includes projected capital spending through December 31, 2019 of $14,967,736 (Attachment PEG/DBS-2 Schedule Step, p. 1 of 2).

[2] Commission Order No. 26,267 in DE 19-064.

[3] Liberty's revised corrections and updates schedules are identified with an additional caption of "CU" (corrections and updates).

A. I will summarize the results of the review of revenue requirements.

Chart 1 – Summary Revenue Requirement Calculation

A	B	C	D	E
			Liberty	
		Liberty	Nov. 22, 2109	OCA
Line	Description	Application	Update	Proposed
1	Adjusted Rate Base	$ 106,180,186	$ 103,024,219	$ 102,932,498
2	ROR	8.19%	8.19%	7.21300%
3	Required Return	$ 8,696,157	$ 8,437,684	$ 7,424,521
4				
5	Adjusted Net Operating Income	$ 4,552,040	$ 3,571,374	$ 4,886,653
6				
7	Return Deficiency (Surplus)	$ 4,144,117	$ 4,866,310	$ 2,537,869
8	Revenue Conversion Factor	1.3714	1.3714	1.3714
9				
10	**Revenue Deficiency**	**$ 5,683,335**	**$ 6,673,765**	**$ 3,480,489**

Chart 1 above, shows information related to Liberty's original filing in column C, its November 22, 2019 revised filing in column D, and the OCA/Ostrander recommendation in column E. Line 10 of each column shows that Liberty originally sought a revenue increase of $5,683,335, and this was increased to $6,673,765 in the Company's revised filing. The OCA/Ostrander recommendation is a revenue increase of $3,480,489, and this represents about a $3.2m (or 48 percent) reduction from the Company's revised filing. In addition, this chart shows that Liberty proposes a ROR of 8.19 percent, compared to the OCA proposed ROR of 7.213 percent.

Chart 2 – Operating Adjustments Proposed by Liberty and OCA

Co. Adj.	Liberty Adjustments	Liberty Original	Liberty Revised	OCA Adj.	OCA Adjustments	OCA Proposed
1	Payroll expense	$ 947,257	$ 947,257	1	Payroll expense	$ (601,678)
2	Payroll taxes	$ 148,639	$ (164,334)	2	Incentives	$ (392,614)
3	Pensions and benefits	$ 294,314	$ 612,004	3	Payroll tax expense	$ (94,744)
4	Property & liab. Insur.	$ (10,689)	$ (10,689)	4	Depreciation expense	$ (661,150)
5	Tax reform adjs.			5	Pole rental fees	$ (53,619)
6	Other maint. exp.	$ (12,246)	$ (12,246)			
6	Depreciation - res. surplus	$ 781,434	$ 781,434			
7	Intercompany rent exp.	$ (7,964)	$ (345)			
8	Depreciation - new rates	$ 447,926	$ 1,561,586			
9	No adjustment	$ -	$ -			
10	Vegetation man.	$ 799,252	$ 799,252			
11	Property taxes	$ 168,744	$ 124,983			
12	Injuries and damages	$ 22,647	$ 22,647			
13	Other revenue	$ 192,548	$ 192,548			
14	Normalize distrib. revenue	$ 602,425	$ 618,740			
15	Income tax accrual					
16	Branding advertising		$ (2,990)			
16	EEI dues		$ (516)			
16	Lost base revenue		$ 280,584			
16	Expenses - water heater		$ (73,923)			
16	Revenues -water heater		$ 11,712			
	Total Operating Adjs.	**$ 4,374,287**	**$ 5,687,704**		**OCA Operating Adj.**	**$(1,803,805)**

Chart 2 above, shows the amount of operating adjustments (expenses and revenues) proposed by Liberty and OCA, all amounts are shown before any offset for income taxes. Liberty's original filing included $4.4m of net adjustments that decreased operating income (increased expenses and decreased revenues), Liberty's revised filing including total net adjustments that decreased operating income by $5.7m, and OCA proposes total net adjustments of $1.8m that increase operating income. Liberty's revised filing included some additional adjustments previously identified during the discovery process by OCA or Staff (and Liberty), and the Company's inclusion of these adjustments in its revised filing means that OCA does not need to address these issues.

Chart 3 – OCA Adjustments to 2019 Step Increase Plant Additions

A	B	C
		2019
		Step Increase
Line	Adjustments	Adjustments
1	Beginning 2019 Step Increase	$14,967,736
2	Adjustments:	
3	1 - Reduce internal capitalized labor	($2,680,000)
4	2 - Battery back-up for customer meters	($1,000,000)
5	3 - Unidentified discretionary projects	($100,000)
6	4 - Londonderry project removed by Liberty	($660,000)
7	5 - ARP breakers & closers project cancelled	($225,000)
8	Total capital costs removed	($4,665,000)
9	Revised 2019 Step Increase	$10,302,736

Chart 3 above shows the OCA adjustments to the capital plant additions included in Liberty's 2019 Step Increase, which began with a balance of $14.9m and was adjusted to a balance of $10.3m.

Chart 4 – OCA Proposed Cost of Capital

	Capital		Weighted
Description	Structure	Cost	Cost
Equity	55%	8.23%	4.527%
Debt	45%	5.97%	2.687%
Total	100%		7.213%

Chart 4 above shows the OCA's proposed cost of capital, including an 8.23 percent cost of equity and overall ROR of 7.213 percent, as supported by OCA witness Pradip K. Chattopadhyay.

Q. How will you cross-reference Liberty adjustment schedules when explaining your related adjustments?

A. If Liberty has not proposed a revision to a particular adjustment in its November 22, 2019 Corrections and Updates filing ("CU filing"), then I will refer to the original-filed schedule, and if Liberty has proposed a revised adjustment in its CU filing, then I will refer to the Liberty revised schedule which includes the designation "CU".

II. Revenue Requirement Adjustments

Adjustment BCO-1: Payroll – Exhibit BCO-1, Schedule 2.1

Q. Will you summarize your adjustment to payroll expense?

A. Liberty proposes to increase payroll expense by $947,257 (Adjustment 1, Sch. RR-3-01) to approximate its 2019 budget for going-forward payroll expense levels, and I am proposing an offsetting reduction to payroll expense of $601,678. There are a significant problems with Liberty's payroll adjustment, and some of the adjustments and primary concerns are summarized below:

1) Liberty's largest and most controversial payroll adjustment component includes an increase to payroll expense of $758,355 to impute and add back the cost impact of virtually all vacancies and employee turnover, to treat the Company as if it

always operates at 100 percent full employment capacity, and will continue to do so on a going-forward basis without any future vacancies or turnover. Liberty has not adequately supported its rationale for this adjustment, the amounts are not known-and-measurable, and no precedent has been cited for this new type of payroll adjustment.

2) Liberty's proposed total payroll expense adjustment of $947,000 reflects a 13.4 percent increase over 2018 actual book costs, and appears excessive and unusual compared to historical trends of actual payroll cost changes from 2015 to 2018.

3) The Company includes short-term incentives in its base payroll amount of $7,081,853, and I will address adjustments to incentives at Adjustment BCO-2 of my testimony.

4) A significant portion of Liberty's payroll costs come from the category of "common employees" that perform work for both electric and gas operations, but the Company cannot identify the amount of payroll costs included in the revenue requirement that is charged by those "common" electric employees. Without this information, I cannot determine if there is a normal or reasonable level of "common" electric employee payroll costs included in this rate case. This is a concern, and I am recommending that the Commission require the Company to begin tracking these common electric/gas employee costs immediately by specific account coding, so that trends and changes in these costs can be identified and analyzed in future rate cases.

Q. Will you explain Liberty's payroll expense adjustment in this case, and those components that you oppose?

A. Liberty's payroll Adjustment 1 calculation is shown at Sch. RR-3-01. The adjustment begins with 2018 per book payroll expense of $7,081,853 and consists of three primary components:

1) The largest and most controversial component of Liberty's payroll adjustment includes a $758,000 increase to recoup and impute into the revenue requirement the payroll costs related to vacated and subsequent filled positions in 2018 and early 2019, costs of new positions in 2018 and early 2019, and the costs of some positions that were vacated in 2018 and not subsequently filled in 2018 or 2019 to-date. Liberty's adjustment essentially treats the Company as if it operates at 100 percent full employment capacity without any turnover or vacancies on a regular continuing basis, but this is not representative of the Company's actual payroll

costs on its books from year-to-year. Also, this treatment is not accurate because all sizeable businesses incur normal vacancies and turnover as part of their business cycle.

Much of the vacancy and turnover payroll costs are not known and measurable, because Liberty has not filled all of these related vacancies in 2018 or through 2019 to-date. Although the Company imputes the cost of these "2018" vacancies into its "2019 going-forward payroll costs", the Company has failed to remove the actual costs of these same positions (and others) that are subsequently being vacated or turned over in "2019" - and this continuing turnover is recurring in nature and is not reflected in the Company's adjustment. In the prior rate case, the Company's payroll adjustment sought to recover the costs of 21 "new positions", but it did not seek to impute and recover the payroll costs of vacancies and turnover as if the Company operated at 100 percent full employment capacity. The Company has not adequately supported its rationale for this adjustment and it has not identified any precedent for this new type of adjustment that it proposes in this case.

2) Liberty takes 2018 per book payroll expense of $7,081,853 and multiplies this by 3 percent, to arrive at estimated 2019 post-test period pay raises of <u>$177,047</u> that are effective for the periods February to April 2019 for union and non-union employees.[4] I do not entirely agree with this Company adjustment, but I do not propose a counter adjustment. This type of adjustment was proposed by the Company in the prior rate case.

3) Liberty calculates 3 percent pay raises of <u>$11,856</u> on $474,230 of Regional Allocated Labor. Liberty's Schedule RR-3-01 explains that Regional Allocated Labor is not included in the Company's test year labor of $7,081,853, and this is because these amounts reflect labor charges from affiliates that do not originate from Liberty's books. Although I do not completely agree with this new adjustment,[5] the adjustment is relatively immaterial and I have not adjusted these costs.

[4] OCA 1-24.

[5] This adjustment is "new" from the perspective the Regionalization process first began in 2018.

Q. Does Liberty's proposed payroll adjustment appear unusual and excessive compared to historical trends in payroll costs?

A. Yes. The information included at Table 1 below will be used to explain the unusual and significant payroll increase proposed by Liberty in this rate case.

Table 1 – Payroll Cost Trends 2015 through 2018 Compared to Liberty Adjusted Payroll

A	B	C	D	E	F	G
	(amounts in millions)	Books	Books	Books	Books	Co. Adjusted
Ln	Description	2015	2016	2017	2018	Payroll - 2019
1	Payroll expense	$7.0	$6.9	$6.4	$7.1	$8.0
2	Short-term incentives	($0.50)	($0.40)	($0.30)	($0.50)	($0.50)
3	Net payroll expense	$6.5	$6.5	$6.1	$6.6	$7.5
4	Payroll capitalized	$3.3	$3.5	$4.0	$3.8	$3.6
5	Total Payroll	$9.8	$10.0	$10.1	$10.4	$11.1
6						
7	Payroll Exp. - % Change		0.00%	-6.15%	8.20%	13.64%
8	Payroll Exp. - $ Change		$0.00	-$0.40	$0.50	$0.90
9						
10	Total Payroll - % Change		2.04%	1.00%	2.97%	6.73%
11	Total Payroll - $ Change		$0.20	$0.10	$0.30	$0.70

<u>Notes/Sources related to above Table 1:</u>

Note 1 – Source document for payroll expense and payroll capitalized in columns C, D, E, and F are from OCA 1-12, adjusted payroll expense of $8.0m in column G is from Liberty Schedule RR-3-01, and OCA 2-47 provides the "capitalized" payroll included in the 2019 Budget of $3.6m (per column G, line 4 of the above table).

Note 2 – Source documents for the short-term incentive amounts in columns C through G are from OCA 1-43 and OCA TS 1-2, and these amounts are deducted from base payroll expense in the above table to provide more comparable payroll expense amounts without the impact of fluctuating incentives from year-to-year.

Note 3 – Liberty's response to OCA 7-4 indicates its reliance on the 2019 Budget (including the related 2019 budgeted payroll costs) in determining final adjusted payroll expense of $8.0m in this case at column G, line 1 – although the Company's responses to OCA 7-4 and OCA 2-17 provided different 2019 budget payroll expense amounts of $7.8m and $7.4m, respectively.

Liberty's payroll adjustment begins with per book 2018 payroll expense of $7,081,853 ($7.1m) and proposes several adjustments to increase payroll expense by $947,257 ($0.9m) or 13.0 percent, to arrive at a final 2019 going-forward payroll expense of $8,029,110 ($8m). Liberty's proposed payroll expense increase of $0.9m and adjusted 2019 payroll expense of $8m appear unusual and excessive compared to prior years' payroll costs and trends, as explained below.

- Payroll adjustment exceeds increases of the combined prior three-years - Liberty increased its actual 2018 per book payroll expense of $6.6m (column F, line 3) to the 2019 going-forward amount of $7.5m (column G, line 3), resulting in a total payroll adjustment of $0.9m (column G, line 8), although payroll expense only increased $0.1 m in total from $6.5m in 2015 (column C, line 3) to $6.6m in 2018 (column F, line 3) - for the combined three-year period 2015 to 2018. Liberty's payroll expense adjustment of $0.9m in this case is excessive because it is nine times greater than the combined payroll expense change of $0.1m from 2015 to 2018, and this unwarranted increase is due primarily to Liberty's $0.8 m adjustment to reflect payroll costs at 100 percent full employment levels.

- Payroll expense has been very stable in prior years - Payroll expense was very stable from 2015 to 2018, with 2015 and 2016 at the same amount of $6.5m (column C and D, line 3), and then payroll expense declined to $6.1m in 2017, a reduction of 6.15 percent (or $0.4m) (column E, lines 6 and 7), and then payroll expense subsequently increased to $6.6m in 2018, but this is near its prior 2015 and 2016 levels of $6.5m) – a resulting increase of 8.2 percent (or $0.5m) (column F, lines 7 and 8). Liberty's payroll expense adjustment of $0.9m appears excessive and unusual compared to the stability in payroll expense from years 2015 to 2018, and this unwarranted increase is due primarily to Liberty's $0.8 m adjustment to reflect payroll costs at 100 percent full employment levels.

- Payroll expense adjustment greater than any prior year "total" payroll increase – Liberty's adjustment increases payroll expense increase of $0.9m, although the largest increase in total payroll (payroll expense plus payroll capitalized)[6] for any single year was only $0.3m (column F, line 11) from 2017 to 2018, from total payroll

[6] Total payroll costs include both expensed payroll and capitalized payroll, and capitalized payroll consists of both payroll capitalized to plant construction/asset accounts and capitalized deferred storm costs.

of $10.1m in 2017 to $10.4m in 2018 (column E, line 5 and column F, line 5). The payroll adjustment appears excessive based on this information.

- <u>Payroll expense adjustment exceeds total payroll cost increases</u> – Liberty's adjustment increases payroll <u>expense</u> increase by $0.9m, although <u>total</u> payroll costs only increased $0.6m (or 6 percent), from $9.8m to $10.4m (column C, line 5 and column F, line 5), for the combined 3-year period 2015 to 2018. It appears very unusual that the Company's proposed payroll <u>expense</u> adjustment for one period of $0.9m is greater than the increase in <u>total</u> payroll costs over this extended time period of three years.

Q. Is there a problem relying on the Company's 2019 budget for establishing going-forward payroll expense, and perhaps other costs, in this proceeding?

A. Yes. Liberty indicated that its adjusted payroll costs of $8m are based on its 2019 Budget, and so OCA 7-4.b asked the Company to reconcile its payroll adjustment to its 2019 Budget. Liberty's response shows that its 2019 Budget payroll expense of $7,799,303 is $229,807 less than its proposed adjusted payroll costs of $8,029,110. Liberty claims this difference of $229,807 is due to a different method in calculating budgeted payroll costs versus the method used for its payroll expense adjustment in this rate case, although the description of both calculation methods appear to be the same and no further detailed reconciliation of the difference was provided by Liberty.

If the 2019 Budget was to be relied upon for the payroll adjustment, then it appears the payroll adjustment could be overstated by at least $229,807. However, my point is not to propose an additional downward payroll adjustment of $229,807 by relying on the 2019 Budget, but rather to point out that the 2019 Budget should not be relied upon for adjusting costs in this rate case unless substantial detailed supporting calculations and reconciliations can be provided for budgeted costs compared to prior year actual costs. Most importantly, this raises concerns with any other adjusted costs in this rate case that are based on the 2019 Budget, because this could also produce unreconciled differences due to calculation methods or other reasons.

Q. Does Liberty's proposed payroll adjustment in this case appear unusual and excessive compared to the Company's payroll adjustment in the prior rate case?

A. Yes. The Company's payroll adjustment in the prior case started with 2015 payroll expenses per books of $7.0m, and proposed an adjustment of $0.1m, to arrive at a 2016 going-forward level of payroll expenses of $7.1m.[7] This compares to a $0.9m payroll expense adjustment, and going-forward 2019 adjusted total payroll expense of $8m in this case, the proposed payroll expense adjustment in this case of $0.9m is nine times greater than the $0.1m payroll adjustment proposed in the prior case. This significant increase in the payroll adjustment appears unusual and excessive given prior payroll cost trends that were previously addressed.

The total payroll adjustment of $0.9m in this case consists of one primary component that increases payroll expense by $0.8m to reflect 2018 vacant positions that were subsequently filled in 2018 and early 2019, 2018 and 2019 vacant positions that have not been subsequently filled in 2018 or early 2019, along with several new positions created or unfilled in 2018 and early 2019. The effect of this adjustment is to treat the

[7] The prior case used a 2015 test period, in Docket No. DE 16-383, with the related payroll adjustment at Sch. RR-3-01.

Company as if it was operating at 100 percent full employment capacity on a 2019 going-forward basis without any subsequent employee vacancies or turnover. However, in the prior rate case, the Company did not propose a similar adjustment to reflect 100 percent full employment capacity, instead the Company adjustment proposed to include only the additional $0.1 m costs related to 21 new hires in the 2016 period (subsequent to the 2015 test period). This significant difference in the payroll adjustment format from the prior rate case contributes to an adjustment that is about $0.7m greater in this rate case.

Q. Has the Company explained the reason for its change in payroll adjustment format from the prior rate case to reflect 100 percent full employment capacity in this rate case?

A. No. The Company has not explained the reason for this change in its payroll adjustment format from the prior rate case, and has not adequately supported its significant payroll increase in this case. The Company has the discretion to propose new or different adjustments and related calculation methods in each rate case, but those changes should be supported by adequate documentation and explanation. In this case, the Company has not met a reasonable burden of proof to support this new type of payroll adjustment.

Q. Does Liberty's direct testimony adequately explain its payroll adjustment related to 100 percent full employment capacity?

A. No. Liberty's direct testimony does not adequately explain its payroll adjustment related to 100 percent full employment capacity adjustment. Liberty's written testimony only states that its payroll adjustment reflects the annual cost of a "full complement" of Granite State employees as of December 31, 2018, including wage increases and labor costs for vacancies during the test year, and planned new hires in 2019.[8] However, the Company did not explain that its adjustment also included payroll costs of employee vacancies that were not subsequently filled in 2018 or early 2019, included payroll costs of some new positions that were not subsequently filled, and essentially removed the impact of on-going and recurring payroll cost offsets or reductions related to recurring employee vacancies and turnover.

Liberty did not explain that it had essentially added back the payroll costs of all employee vacancy and turnover in 2018 and early 2019 on a going-forward basis, treating the Company as if it will always operate at 100 percent full employment capacity in 2019 and the future, despite known and measurable employee vacancy and turnover in 2019 and the future that causes continuing related decreases in payroll costs. Without a detailed explanation for this adjustment in Liberty testimony, related information was gleaned from Company responses to OCA data requests along with my own analysis.

[8] Joint Direct Testimony of Philip E. Greene and David B. Simek, p. 12, lines 3 to 6 (Bates II-088).

Q. Will you explain Liberty's 100 percent full employment capacity adjustment of $0.8m that treats vacancy and employee turnover as it if will not exist on a going-forward basis?

A. Liberty proposes a payroll adjustment of $758,355 ($0.8m) which significantly increases payroll costs by treating the Company as if it operates at 100 percent full employment with no vacancy and employee turnover when calculating its adjusted 2019 going-forward payroll costs. This adjustment incorrectly treats the Company as if it always operates at 100 percent full employment capacity, and will actually operate in that mode on a going-forward basis without any vacancies or turnover in the future - which is not representative of reality and which reflects payroll costs that are not known and measurable. The Company calculates payroll costs that were avoided for positions that were vacant in 2018 and then subsequently filled in 2018 and early 2019, along with positions that were vacant in 2018 and <u>never</u> subsequently filled in 2018 and 2019 to-date (along with new positions for 2018 and 2019 to-date), and it imputes these costs back into its 2019 going-forward adjusted payroll for rate case purposes.

For example, if a position was vacated in April 2018 and subsequently filled in December 2018, then for that period of 9 months when payroll expense was not recorded on the 2018 books for this position, the Company retroactively imputes nine months of payroll costs into its payroll adjustment for this position to treat the position as if it was never vacated during the test period and will never be vacated again on an on-going basis in the future. I am not totally opposed to a reasonable portion of this adjustment as I will explain later.

However, my primary concern is that Liberty's payroll adjustment goes one step further, and not only retroactively adds back the payroll costs for positions vacated and filled in 2018, it actually includes the payroll costs of positions that were vacated in 2018 and never subsequently filled in 2018 or 2019 to-date (and also includes the costs of some new positions that have not been filled in early 2019) – and these costs are clearly not known-and-measurable. The Company's 100 percent full employment capacity adjustment of $0.8m includes payroll costs for the following categories:

1) Existing positions that were vacated in 2018 and subsequently filled in 2018, and through the post-test period April 1, 2019 (this type of adjustment was not proposed in the prior rate case). I oppose part of this category of payroll costs.

2) Existing positions that were vacated in 2018 and through March 2019, but have <u>not</u> yet been backfilled in 2018 or 2019 to-date or are "on-hold" (this type of adjustment was not proposed in the prior rate case). I oppose this entire category of payroll costs.

3) New positions created in 2018 and through January 2019, with several of these positions remaining unfilled in 2018 or 2019 to-date (this type of adjustment was proposed in the prior rate case, but only for some new positions created subsequent to the test period). I primarily oppose the payroll costs of new positions created in 2018 or 2019 and not yet filled in 2018 or 2019 to-date.

4) Existing part-time Customer Care positions (55 positions) that were vacated in 2018, although it is not clear when these positions were filled in 2018 or 2019 (this type of adjustment was not included in the prior case). Although there is missing information, I am not opposing these costs, mostly because the related costs are not significant.

Q. Does any sizeable business operate at 100 percent full employment capacity all the time without any vacancies and turnover as Liberty's payroll adjustment depicts for this rate case?

A. No. Liberty's adjustment increases payroll costs by $0.8m to artificially and unreasonably treat the Company as if it will always operate at 100 percent full employment capacity going-forward with no employee vacancies or turnover based on its 2019 going-forward period (and into the future).

The 100 percent full employment capacity rationale is unreasonable because no sizeable company ever operates at 100 percent full employment capacity, especially for an extended time basis and certainly not forever in the future as depicted by the Company's payroll adjustment. This is because employee vacancies and turnover are a normal part of conducting business and the business cycle. Employee turnover is a function of conscious decisions sometimes influenced by the Company and other times reflect discretionary decisions made by employees. In other words, the Company initiates and creates some vacancies and turnover when not satisfied with employee job performance or when downsizing to improve earnings, and some employees voluntarily leave to pursue better pay, preferred jobs, improved work conditions, more work flexibility, or a host of other reasons. Virtually every sizeable business has some level of employee vacancies and turnover as a normal part of conducting business.

Q. Are Liberty's employee vacancies and turnover recurring every year, such that the Company will never operate at 100 percent full employment capacity into perpetuity as its adjustment depicts?

A. Yes. If it is the Company's intent to convey that its vacancies and turnover adjustment is intended to reflect 100 percent full employment capacity which it will actually achieve in 2019 and on a permanent basis into the future, that assumption is clearly incorrect. The Company will never operate at 100 percent full employment capacity, especially for an extended time period, and never into perpetuity as its adjustment depicts. Liberty will always operate with some level of vacancies and turnover. Liberty has not been able to demonstrate that it has ever operated at 100 percent full employment capacity without vacancies and turnover. If the Company was awarded recovery of the entire $758,000 of its 100 percent full employment adjustment in this case, it would receive a significant windfall related to vacancy and turnover related payroll costs.

Q. Will you explain the adjustment that you have made to Liberty's 100 percent full employment capacity adjustment of $758,355?

A. I propose to remove $601,678 of the Company's $758,355 full employment capacity adjustment. The calculation of my adjustment is shown in the table below, and I will explain the rationale for this adjustment after the table. The table below identifies the Company's 100 percent full employment adjustment of $758,355 by various categories, and shows the number of positions and payroll expenses associated with each of those categories. For example, column D, line 1, provides the amount of payroll costs associated with "Existing positions vacated and filled in 2018", and this consists of 21 employees as indicated at column C, line 1. Column E shows the adjustment that I am proposing, and it consists of a Part 1 adjustment of $334, 439 related to the 100 percent cost removal in column F, and a Part 2 adjustment of $267,239 related to the 50 percent cost removal in Column F.

Table 2 – OCA Adjustment to Liberty's 100 percent Full Employment Capacity

		Highlighted Payroll Costs are Confidential				
A	B	C	D	E	F	G
		No. of	Payroll	OCA	Percent	
Ln	Category	Employ.	Expense	Adj.	Remove	Sce.
1	Existing positions vacated & filled 2018	21	[redacted]	[redacted]	50%	1
2	Existing positions vacated in 2018 & filled 2019	1	[redacted]	[redacted]	50%	1
3	New positions vacated & filled 2018	3	[redacted]	[redacted]	50%	1
4	New positions created & filled 2019	1	[redacted]	[redacted]	50%	1
5	New positions vacated in 2018 & filled 2019	1	[redacted]	[redacted]	50%	1
6	Customer care positions	55	[redacted]	[redacted]	50%	1
7	**Part 2 - Payroll costs at 50 percent removal**	82	$534,478	**$267,239**		
8						
9	Exist. positions vacated in 2018/unfilled 2018 & 2019	6	[redacted]	[redacted]	100%	1
10	New positions created in 2018/unfilled 2018 & 2019	1	[redacted]	[redacted]	100%	1
11	Subtotal OCA 2-49	7	$801,465	$266,987		
12						
13	2018 positions "on hold" - costs not removed from test period (Note 1)			[redacted]	100%	2
14	2018 position removed & replaced, costs not removed from test period			[redacted]	100%	3
15						
16	Contractor savings		($43,110)			1
17	**Part 1 - Payroll costs at 100 percent removal**		$758,355	**$334,439**	100%	1
18						
19	**Grand Total Payroll Expense**		$758,355	**$601,678**		1
20				OCA Adj.		
21	Source 1 = OCA 2-49.a., Source 2 = OCA 1-20.d.1, Source 3 = OCA 2-50.d					
22	Note 1 - These are estimated costs, the Company did not provide the actual payroll costs.					

My payroll adjustment is comprised of two components, I will refer to these as Part 1 and Part 2.

<u>**Part 1 of OCA Payroll Adjustment:**</u>

Part 1 of my payroll adjustment is straight-forward and is supported by the known-and-measurable regulatory principle. This adjustment removes $334,349 of the payroll costs included in the Company's 100 percent full employment payroll adjustment of $758,355. This adjustment removes all payroll costs which the Company's response to OCA 2-49 indicates are related to existing positions vacated in 2018, but not subsequently filled in 2018 or 2019 to-date, along with all new positions created in 2018 and 2019 which have not been subsequently filled. This adjustment removes all payroll costs that are not known-and-measurable, and which have not been subsequently incurred by the Company through 2019 to-date because the positions have not been filled.

Even if some of these positions are subsequently filled in the post-test period approximately April to December 2019, I would not support inclusion of these payroll costs in the rate case. This is because it would then be necessary to remove the off-setting reduction in payroll costs related to new vacancies and turnover for this same period April to December 2019 in order to achieve a proper matching of all payroll-related costs for this same period. It would not be reasonable or consistent with the regulatory matching principle to include only payroll cost increases for subsequent filled positions, without also reflecting offsetting payroll cost decreases for subsequent positions that were vacated or for on-going turnover.

The payroll costs of $334,349 that I have removed in Part 1, are reflected in the previous table at column E, with a subtotal amount of $266,987 shown at line 11 (lines 9 and 10), plus lines 13 and 14 ($67,452), equal the total adjustment of $334,439 at line 17. For this Part 1 adjustment, column F, indicates these costs have been removed 100 percent. The 100 percent removal is the distinction between Part 1 and Part 2 of my adjustment.[9]

Part 2 of OCA Payroll Adjustment:

Part 2 of my adjustment removes an additional $267,239 of the payroll costs included in the Company's 100 percent full employment payroll adjustment of $758,355. The table (column D, line 7) identifies payroll costs of $534,478 (included in the Company's total payroll adjustment of $758,355) that are related to existing positions vacated in 2018 or 2019 to-date, and subsequently filled in 2018 or 2019 to-date, along with all new positions created in 2018 or 2019 that were subsequently filled in 2018 and 2019 to-date. I have removed 50 percent of these costs of $534,478, resulting in an additional adjustment of $267,239 (column E, line 7).

Q. Will you continue by explaining the rationale to remove 50 percent of vacancy/turnover costs under Part 2 of your payroll adjustment?

A. The rationale for removing 50 percent of all vacancy/turnover payroll costs that were subsequently filled in 2018 or early 2019 consists of two primary supporting reasons as addressed below:

1) **Comparing Actual Year-to-Date 2019 Vacancy/Turnover Costs** - At first blush, it might be interpreted that the $534,478 of payroll costs related to 2018 vacancies

[9] All of these related payroll costs and related status are identified in the Company's response to OCA 2-49, OCA 2-50, and OCA 1-20.

that were subsequently filled in 2018 and early 2019 to-date are known and measurable amounts that should be allowed for recovery in this rate case. However, this assumption is still flawed, because this $534,478 of payroll costs restores the Company to an unreasonable and untenable position of 100 percent full employment capacity without any vacancies or turnover on a going-forward basis and in perpetuity for ratemaking purposes. And this remains unreasonable and not indicative of reality or on-going actual vacancies and turnover that will continue to occur in 2019 (and future years), which is the going-forward period that the Company's payroll adjustment is intended to represent (because the Company's payroll adjustment is based on 2019 Budgeted payroll costs).

OCA 2-50.c asked the Company to provide and identify the number of positions and related costs for vacancies that began in 2019 and remain unfilled through the most recent date in 2019.[10] The Company's response identified nine positions with a cost of $345,546. This is proof that vacancies and turnover is on-going, cannot be avoided, and are known and measurable. And because the actual cost of these vacancies is for the same 2019 period that the Company's payroll adjustment is attempting to replicate, it would be reasonable to propose an offsetting adjustment and decrease in 2019 payroll costs of $345,546, so that some level of actual vacancies and turnover is reflected in the Company's 2019 going forward payroll costs in the revenue requirement. However, instead of removing

[10] Liberty's response at Attachment OCA 2-50.c showed positions from March 22, 2019 through June 28, 2019 (although most positions were for the months of April and June 2019).

these actual 2019 vacancy payroll costs of $345,546, I am proposing to reduce payroll by a lesser amount of $267,239 - which is 50 percent of the Company's vacancy costs included in this rate case as previously identified in the previous table. This is a reasonable approach, and provides the Company with some recovery of these payroll costs, even when a more strict approach could be supported to remove additional payroll costs.

2) **Normal Levels of Turnover** – The Company's response to Staff 6-1 shows actual employee turnover/replacement for years 2016, 2017, and 2018, and this consists of electric-only employees of 20 in 2016, 27 employees in 2017, and 56 employees in the 2018 test period. Thus, the 2018 test period has had about twice the turnover of the two prior years with 56 employee positions turning over compared to 20 to 27 in the two prior years.

Per the previous table, the $534,478 of Company payroll costs related to actual 2018 and 2019 positions subsequently filled by the Company (and included in the Company payroll vacancy/turnover adjustment of $758,355) is related to 82 employees as shown at column C, lines 1 to 7.

The Part 2 adjustment proposes to remove one-half of the costs of these 82 employees (making up the $534,478 of Liberty's payroll adjustment amount), which is an adjustment of $267,239. Therefore, my adjustment is essentially removing the costs of one-half of the 82 employees, which means that I am removing the costs associated with about 41 employees but also allowing the costs of about 41 employees. The Company's response to Staff 6-1 appears to indicate that in a more normal year (such as 2016 or 2017) the Company had turnover of 20 to 27 employees compared to the unusually high turnover of 56 employees in 2018.

Therefore, my 50 percent adjustment that allows the Company to retain vacancy/turnover payroll costs related to 41 employees (and $237,239) is actually conservative and favorable to the Company because I am allowing the Company to retain payroll turnover costs associated with what appears to be a higher level of turnover than is normal, allowing for 41 turnover employees compared to the normal 20 to 27 turnover employees. I am not proposing to allow the Company to keep payroll turnover costs related to the unusually high turnover level of 56 employees for 2018, because payroll costs should not be established based on this type of one-off or unusually high level of turnover that is not recurring or representative of normal turnover based on information provided by Liberty. Therefore, I believe Part 2 of my payroll adjustment is reasonable, conservative, and very fair to the Company because an argument could be made to disallow Liberty's imputation of all vacancy/turnover costs (although considering some reasonable allowance for new employees).

Q. Have you seen a similar type of adjustment in other rate cases, where a utility company seeks to recover costs in order to achieve 100 percent full employment capacity on an on-going basis for rate-setting purposes?

A. No. I do not recall having seen or addressed this type of proposed payroll adjustment by a utility company in a rate case, particularly in the most recent seven years of rate cases that I have reviewed. I am not sure if Liberty has proposed this type of adjustment in other rates cases and if it has been adopted by a regulatory agency, but Liberty has not made me aware of any precedent for this adjustment in their other jurisdictions. I am not aware if the New Hampshire PUC has ever addressed this type of payroll adjustment, but Liberty has not made me aware of any precedent in the state.

Q. Are you proposing a payroll adjustment associated with "common employees" and what are your concerns?

A. I am not proposing an adjustment at this time related to common employees, but I also cannot state that an adjustment is not justified. A significant portion of Liberty's payroll costs come from the category of common employees that perform work for both electric and gas operations, there were 216 "common electric/gas" employees on average for 2018, and 54 "electric" only employees on average for 2018.

However, the Company cannot identify the amount of payroll costs included in the revenue requirement that is charged by these "common" electric employees. The Company also apparently does not track or analyze these costs on a routine basis, because they cannot identify these costs. Without this information, I cannot determine if there is a reasonable level of "common" electric employee payroll costs included in this rate case. The amount of costs assigned by these common employees to electric operations (and gas operations) could vary each year, and if these common costs would include an amount that is 20 percent greater than normal in this rate case, then customers could be paying excessive rates for the over-recovery of these costs in this rate case.

Q. What is your recommendation regarding the tracking and accounting for payroll costs related to common employees?

A. I am recommending that the Commission require the Company to begin tracking these common electric/gas employee costs immediately by specific account coding, so that trends and changes in these costs can be identified and analyzed in future rate cases. Also, I believe this is important information that the Company should have available for its own analysis related to internal budgeting and cost control tracking.

Adjustment BCO-2: Short & Long-Term Incentives – Exhibit BCO-1, Schedule 2.2

Q. Will you summarize your adjustment to short-term incentives ("STI") and long-term incentives ("LTI")?

A. Liberty does not propose any adjustments to STI or LTI expense. However, I am proposing to reduce the 2018 STI expense by $322,308, and reduce the 2018 LTI expense by $70,307, for a total incentives adjustment of $392,615. My adjustment includes two components. First, I have removed the amount of unsupported and excessive growth in the incentive expense for the 2018 period compared to previous periods, which reduces STI and LTI by $157,786. Second, I have disallowed 50 percent of the remaining incentive balance that is primarily driven by financial-focused incentive performance measures that benefit shareholders over the interests of customer-focused performance measures, and this reduces STI and LTI by $234,829. The total of these two components of $157,786 plus $234,829, equals the total adjustment of $392,615. For comparison purposes, if I would have reduced the total STI and LTI expense by 50 percent (without first reducing the balances for excessive and unsupported growth), this would produce a reduction in STI and LTI expense of $313,721.

A 50 percent disallowance of incentive expense that is based on financial-focused performance measures that unduly favors shareholders over customers is an adjustment that is commonly accepted by state regulatory agencies in numerous jurisdictions. I am not proposing that incentive compensation payments or plans be eliminated by the Company; I am only proposing that incentive compensation expense be reduced for regulatory ratemaking purposes as discussed below.

Q. What is the purpose of "incentive" compensation?

A. Incentive compensation should promote "pay-for-performance" and represent "pay at risk," such that incentives are paid only if reasonable documented performance measures are met, and the performance measures should be challenging but realistic. Incentive compensation is paid if certain reasonable performance measures are achieved, and if these performance measures are not met then incentive compensation should either be reduced or not paid. The incentives for any particular employee often include both company goals and individual goals tied to certain financial, customer, or operating performance measures. All goals should be established in advance of the beginning of an incentive plan's performance period to promote objectivity and eliminate any possible manipulation of the performance measures and results achieved.

Q. Will you explain the difference between financial-focused performance measures and customer-focused performance measures of incentive plans and how this can lead to regulatory adjustments?

A. Incentive plans can include a mix of incentive performance measures that are both financial-focused and customer-focused, the financial-focused incentive measures are primarily beneficial to shareholder interests instead of customers, and customer-focused incentive measures can provide benefits to customers. For some incentive plans, the financial-focused performance measures are primarily included in the LTI, but both Liberty's STI and LTI plans are heavily weighted with financial-focused performance measures. Examples of financial-focused performance measures include those that establish targets and track actual results for return on equity ("ROE"), earnings before interest, taxes, depreciation, and amortization ("EBITDA"), stock price, and other financial or operational statistics or key data. Examples of customer-focused performance measures include those that establish targets and track actual results for service quality, customer service, safety, and other customer-related statistics or data that have some benefit to customers.

The underlying rationale for excluding any incentive costs associated with financial-focused performance measures is that these types of measures primarily benefit shareholder interests over customer interests. This is because common financial-focused performance measures such as ROE, EBITDA, and stock price serve to benefit shareholder interests, but do not provide any significant, meaningful and tangible benefits to customers. For example, if a company is successful in increasing its ROE as a financial-focused performance measure, then this will cause employee incentive pay to increase and shareholders can realize significant tangible benefits such as appreciation in stock price or increases in dividends. However, customers realize virtually little or no quantifiable or significant meaningful benefit. And these financially-focused performance measures are not intended to directly benefit customers, because the company's incentive plans do not formally document any benefits to be passed along to customers if there is an increase in ROE or earnings - - such as rate refunds, permanent rate reductions, or even a freeze of existing rates for some duration.

Q. Does Liberty agree that its "Efficiency" performance measure is financial-focused, and does it link the LTI plan with shareholder interests?

A. Yes. Liberty uses the term "Efficiency" and "Financial" interchangeably at times, but the Efficiency measure of both the STI and LTI plans is "financially-focused", per the Company's response to OCA TS 1-18.c and OCA TS 1-18.d.

Also, the 2018 LTI Plan, Appendix C, addresses the "Total Shareholder Return" Modifier ("TSR"), and indicates this component is used "…to promote further alignment between employees and shareholders of the Company."[11] This is an indication that the LTI is intended to be aligned with shareholder interests and not customer interests, because the Company does not mention alignment with any customer interests.

[11] OCA TS 2-12, Attachment OCA TS 2-12.3, page 6 of 8.

Q. What percent of STI and LTI expenses are you proposing to exclude as the second part of your incentive adjustment, and how is this tied to Liberty's financial-focused performance measures included in its incentive plans?

A. I am proposing to remove 50 percent of both STI and LTI expenses, because both plans are heavily weighted with financial-focused performance measures. The 50 percent adjustment is reasonable and conservative, because I could justify a greater disallowance given that Liberty's STI plan is 70 percent or more weighted with financial-focused performance measures and the LTI plan is 85 percent weighted with financial-focused performance measures. This information is shown in the two tables below, the first table is Liberty's STI plan, and the second table is the LTI plan.

Table 3 – Short-Term Incentives (Source: OCA TS 1-18.a)

STI	Financial	Operations & Stakeholders	Customers, Communities & Regulators	Employees	Total
2015 Perf. Meas.	**70%**	**10%**	**10%**	**10%**	**100%**
2015 Ranges	50, 60, 65, 70	10, 15, 20	10, 15	10, 15	
2016 Perf. Meas.	**70%**	**10%**	**10%**	**10%**	**100%**
2016 Ranges	50, 60, 65, 70	10, 15, 20	10, 15	10, 15	
2017 Perf. Meas.	**70%**	**10%**	**10%**	**10%**	**100%**
2017 Ranges	50, 60, 65, 70, 100	10, 15, 20	10, 15	10, 15	
2018 Perf. Meas.	**70%**	**10%**	**10%**	**10%**	**100%**
2018 Ranges	50, 55, 60, 65, 70, 100	10, 15, 20	10, 15, 20	10, 15	

Liberty's STI plan in the table above shows four categories of performance measures, with 70 percent related to "Financial" (financial-focused) performance measures, and the three remaining combined performance measures of 30 percent (10 percent each) are primarily customer-focused.[12] This weighting of 70 percent financial-focused and 30 percent customer-focused for STI performance measures has been in place for the four most recent years 2015 to 2018 as shown in the table, although there have been some changes within the details of the STI plan from year-to-year.

Also, the table shows additional numbers in the individual categories of performance measures. Using the "Financial" measure as an example, it shows "2015 Ranges" of 50, 60, 65, and 70,[13] and this represents the various percentages of financial-focused performance measures that apply to different employee positions,[14] some employees are subject to a weighting of 50 percent to 100 percent for the Financial performance measure.[15]

And although the Financial measure which is 70 percent financial-focused (with benefits to shareholders) could justify an exclusion of 70 percent of STI expenses, I am

[12] However, some of these three other categories include some individual measures that could be interpreted as financial-focused.

[13] These amounts are intended to represent "percentages", but the limited size of the fields did not allow percentage signs to be placed with these items.

[14] Examples of employee positions include President, Vice President, Assistant General Counsel, Director, Senior Business Manager, Area Manager, etc.

[15] The STI is also based on two components of "Balanced Scorecard Achievement" and "Individual Performance Achievement" which vary by position level.

proposing to only remove 50 percent of these expenses (along with removing part of the 2018 excessive STI balance, which is addressed later in this section).

Table 4 – Long-Term Incentives (Source: OCA TS 1-18.e.1, e.2, e.3, OCA TS 2-12):

LTI	Financial	Safety	Customer Service	Total
2013	60%	20%	20%	100%
2014	85%	10%	5%	100%
2015	85%	10%	5%	100%
2016	85%	10%	5%	100%
2017	85%	10%	5%	100%
2018	85%	10%	5%	100%

Liberty's LTI plan in the table above shows three categories of performance measures, and for the five most recent years 2014 to 2018 it shows 85 percent related to "Financial" (financial-focused) performance measures, 10 percent related to "Safety" (customer-focused), and 5 percent related to "Customer Service" (customer-focused).[16] Similar to LTI plans of other companies, the Liberty LTI plan is more heavily weighted with financial-focused performance measures of 85 percent compared to its STI plan with financial-focused performance measures of 70 percent.

[16] The 2013 period shows 60% Financial, 20% Safety, and 20% Customer Service.

And although the Finance measure of 85 percent financial-focused (with benefits to shareholders) could justify an exclusion of 85 percent of LTI expenses, I am proposing to only remove 50 percent of these expenses (along with removing part of the 2018 excessive balance, which will be addressed later in this section).

Q. The second part of your adjustment proposes to remove 50 percent of STI and LTI expense as part of your adjustment, although up to 70 percent of STI and 85 percent of LTI is tied to financial-focused performance measures. Was Liberty able to quantify the specific amount of STI and LTI expense that is tied to financial-focused versus customer-focused STI and LTI expense?

A. No. The second part of my incentive adjustment only proposes to remove 50 percent of STI and LTI expense tied to financial-focused performance measures, although a larger adjustment could be justified because at least 70 percent of STI and 85 percent of LTI is tied to specific financial-focused performance measures as I previously addressed at Tables 3 and 4. I am reducing incentive expense using the approximate "percentage of financial-focused" incentives, because Liberty did not quantify the requested amount of STI and LTI expense that is specifically related to financial-focused versus customer-focused performance measures. OCA 1-44 requested the amount of STI, LTI, and shared bonus pool expenses specifically related to financial-focused and customer-focused performance measures. However, Liberty's response to OCA 1-44.b states that the incentive payments are not broken down for each incentive criterial or measurement, and only a single amount is determined using an overall blended score.

It would be more accurate to remove the specific amount of STI and LTI expense that is paid based on financial-focused incentives, but Liberty did not provide this amount. However, the method that I used, which removes STI and LTI expense related to the percentage of financial-focused performance measures is also used in other jurisdictions (or sometimes a 50 percent generic split or other approach is used). This is the best approach when the Company does not provide the specific amount of STI and LTI expense related to financial-focused performance measures.

Q. If you had used a method of removing the actual amounts of Liberty's STI expense that is financial-focused (70 percent) and LTI expense that is financial-focused (85 percent), would this result in a larger adjustment than the two-part method that you propose?

A. Yes. this information is shown in the table below.

Table 5 – Comparing Removal of 70% STI and 85% LTI to OCA Proposed Incentives Adjustment (Source: OCA 1-43 for incentive amounts)

	STI	LTI	Total
Total 2018 expense	$528,944	$98,498	
Financial-focused 70% STI & 85% LTI	70%	85%	
Potential adjustment to remove 70% & 85%	$370,261	$83,723	$453,984
OCA proposed adjustment to remove 50%,			
plus unreasonable growth in STI & LTI	$322,307	$70,306	$392,613
70% & 85% Adjustment exceeds OCA Adj.	$47,954	$13,417	$61,371

It would be justified to exclude 70 percent of STI expenses and 85 percent of LTI expenses that are both tied to financial-focused performance measures, and the Commission can still consider this option. This alternative approach would produce an adjustment that is $61,371 greater than the adjustment that I am proposing as demonstrated in the table above.

As a reminder, the method that I propose is an initial adjustment to reduce Liberty's STI and LTI to a more reasonable and normalized level representative of prior year incentives expense, and then reduce the remaining balances by a 50 percent financial-focused factor. This information indicates the adjustment that I propose is reasonable, conservative, and more favorable to the Company.

Q. Are you merely proposing to exclude these incentive costs from the revenue requirement, and you are not requesting that Liberty discontinue or cease incentive payments?

A. That is correct. I am merely proposing the removal of incentive costs as a regulatory adjustment, similar to any other regulatory adjustment that may exclude a portion of costs from the revenue requirement. I am not proposing that the Company discontinue its incentive plans or cease making payments under its incentive plans.

Q. Some utility companies claim that adopting an adjustment that excludes part of incentive expenses impairs a utility's ability to attract and retain employees, do you agree?

A. No. I am aware that utility companies have made this claim in other regulatory proceedings. However, I am not aware of a utility company that has been able to prove (and provide verifiable documentation) this type of incentive adjustment has actually impaired its ability to attract and retain employees. It is easier to make this claim of impairment, but more difficult to support it with verifiable documentation. Because this type of incentive adjustment is now common in other jurisdictions, if there was verifiable proof it was actually impairing a utility company's ability to attract and retain employees, this would have become well-known in the industry by now. I am not aware there exists a movement to dismiss this type of adjustment due to proof it impairs a utility company's ability to attract and retain employees.

Q. Moving on to the other component of your incentive adjustment, why did you first remove part of the significant increase in STI and LTI expense for 2018, prior to removing 50 percent of the remaining incentive expense tied to financial-focused performance measures?

A. It has become fairly common practice for state regulatory agencies to adopt the removal of 50 percent or greater (as applicable) of the incentive expense tied to financial-related performance measures. However, and especially in this case, I believe it is important to begin with a proper normalized level of incentive expense, otherwise incentive expense can still be unreasonably overstated or excessive even after removing 50 percent of incentive expense tied to financial-related performance measures. The starting point of incentive expense should first be normalized to reasonable levels so they are free of significant or unusual increases in incentive expense that cannot be properly identified, reconciled, and supported by proper objective incentive performance measures.

I have concerns with the significant increase in Liberty's STI and LTI expense in recent years, which has not been properly documented, explained, and reconciled by the Company to incentive performance measures and results, and these incentive amounts are not reasonably known-and-measurable. In addition, the concerns that I have related to the significant increase in incentive expense in recent years can also be used to justify in part the other part of my incentive adjustment that supports 50 percent exclusion of STI and LTI expenses.

Q. Can you show the significant increases in STI and LTI in recent years?

A. The overall significant upward trend in both STI and LTI for years 2015 to 2018 is shown in the table below, per the Company response to OCA 1-43.

Table 6 – Changes in STI and LTI from 2015 to 2018 (Source: OCA 1-43):

Incentives	2015	2016	2017	2018
Short-Term Incentives	$496,198	$439,714	$303,908	$528,944
Increase $		($56,484)	($135,806)	$225,036
Increase %		-11%	-31%	74%
Long-Term Incentives	$33,554	$34,963	$100,633	$98,498
Increase $		$1,409	$65,670	($2,135)
Increase %		4%	188%	-2%

Regarding STI expense in the table above, I am primarily concerned with the $225,000 (and 74 percent) increase from 2017 to 2018 (increasing from $303,908 in 2017 to $528,944 in 2018), especially when STI was decreasing 11 percent and 31 percent from

2015 to 2016, respectively. Also, the increase from 2016 STI of $439,714 to 2018 STI of $528,944 is about 20 percent.

Regarding LTI expense in the table above, I am primarily concerned it has tripled in amount from the two years 2015 and 2016 ($33,554 and $34,963 for 2015 and 2016), to the two years 2017 and 2018 ($100,633 and $98,498) with a 188 percent increase from 2016 to 2017 - and then with 2018 LTI expense remaining about the same as 2017.

In addition, OCA 1-43 requested the amount expensed by account number for short-term incentives, shared bonus pool, and the performance and restricted share unit plan (long-term incentives) for 2015 to 2018. The amounts provided by Liberty are shown in the table above, and include $98,498 for LTI expense. However, Liberty's response to Staff 6-6, appears to identify an additional 2018 accrued expense of $151,568 for LTI (in addition to the amount of $98,498 included in the table above). I have relied on the lesser amount of LTI expense of $98,498 for my adjustment, although it appears my adjustment could be understated if Liberty provided the wrong amount of 2018 LTI expense in response to OCA 1-43 (or if Liberty failed to separately identify amounts related to the shared bonus pool as requested in OCA 1-43).

Q. Has Liberty specifically identified and quantified the various reasons causing the significant increase in STI and LTI expense in recent years (as requested by OCA)?

A. No. Although Liberty originally identified, and then subsequently revised, some of the reasons related to the recent increases in STI and LTI expense, the Company has not specifically quantified any of the reasons it gave for the recent increase in STI and LTI expense as shown in Table 6. I will identify some of the reasons that Liberty gave for the recent increase in STI and LTI expense, and show how the Company failed to quantify these impacts in data request responses. The Company's failure to specifically quantify the reasons for the recent significant increase in STI and LTI expense justifies the first part of my adjustment which reduces and normalizes these incentive expenses to a more reasonable level, prior to applying the 50 percent adjustment as the second part of my incentive adjustment.

Q. Are you concerned that the recent increase in STI and LTI expense could result in New Hampshire customers subsidizing the better (or improved) financial performance in other jurisdictions compared to New Hampshire's lesser financial performance in recent years?

A. Yes, but initially it is important to understand the foundation and assumptions for this concern. First, STI and LTI are driven by significant weightings of 70 percent financial-focused performance measures for STI and 85 percent financial-focused performance measures for LTI (per prior Tables 3 and 4), this should mean that financial performance is a significant driver of STI and LTI expense (especially compared to lesser weightings for customer-focused performance measures).[17] Second, STI expense has

[17] Although as previously indicated, OCA 1-44 requested a break-out of STI and LTI expense between financial and customer-focused performance measures, but Liberty's response states that the incentives payout is not broken out by each of these criteria.

increased significantly in 2018 (per prior Table 6)[18], compared to prior years 2015 to 2017, although New Hampshire Liberty financial-focused performance has been challenged and is not indicative of increased incentive payments for the recent years. Similarly, LTI expense has increased significantly in 2017 and 2018 (per prior Table 6)[19], compared to prior years 2015 and 2016, although New Hampshire Liberty financial-focused performance has been challenged and is not indicative of increased incentive payments for the recent years. And additional documentation supporting concerns with New Hampshire Liberty's financial performance in recent years (and when compared to peer East Region members Georgia and Massachusetts) is generally inconsistent with increasing STI and LTI expenses tied primarily to financial-focused performance measures) as illustrated by the following:

1) The direct testimony of Liberty states that for the test year December 31, 2018, the Company earned return on rate base was 6.43 percent, and this is less than the Company's allowed ROR of 7.69 percent using the current capital structure.[20]

2) Given that return on equity ("ROE") is one of the financial-focused performance measures under the incentive plan, Liberty New Hampshire's reported ROE for recent years has lagged its other peer companies in other jurisdictions as shown in the Confidential information below from Liberty's response to OCA 7-34 Attachment OCA 7-34.b.1 (2016), Attachment OCA 7-34.b.2 (2017), Attachment OCA 7-34.b.3 (2018), and Attachment OCA 7-34.b.4 (2019 to-date) that is from the Quarterly Management Report – East Region:

[18] 2018 STI expense of $528,944 increased by $225,036 and 74 percent over 2017 STI expense of $303,908.

[19] 2017 and 2018 LTI expense levels of $100,633 and $98,498, respectively have just about tripled compared to 2015 and 2016 LTI expense levels of $33,554 and $34,963, respectively.

[20] Joint direct testimony of Philip E. Greene and David B. Simek, page 3 of 9 (Bates II-007).

BEGIN CONFIDENTIAL***

[redacted]

*****END CONFIDENTIAL.**

Q. Do you have some further concerns regarding incentive costs based on the previous Confidential information comparing the financial performance of New Hampshire to other jurisdictions?

A. I understand it may be reasonable for a Company to have different ROE incentive performance goals among various jurisdictions due to different challenges and issues that exist in each jurisdiction. However, I am concerned that Liberty is paying elevated LTI expense levels based on claimed elevated financial performance for prior years 2015 to 2017, yet the actual ROE (and even the ROE goals) earned in those prior years is not representative of elevated financial performance. **BEGIN CONFIDENTIAL***** [redacted]

[redacted]

*****END CONFIDENTIAL**

Although my review of Financial/Efficiency performance measures was limited to just the ROE component in the previous Confidential data included in the Quarterly Management Reports – East Region for the period 2016 through 2nd quarter of 2019, this data did not support a significant increase in STI or LTI expense for 2018 over the 2016 to 2017 incentive expense levels. Although a more comprehensive review of all Financial-focused measures (besides ROE) could be undertaken in an attempt to determine if these additional measures have justified a significant increase in STI and LTI expense in recent years, the review that I have performed surpasses the absence of Company-provided explanation and quantification of reasons for increases in STI and LTI expense in recent years.

I also understand that 2018 incentive expense can be influenced by Financial-related performance measures for the three prior years, and that 2018 incentive expense can include estimated costs related to projected future year incentive performances. Regardless, I was unable to determine why a significant increase in 2018 incentives expense was justified when compared to 2016 to 2017 periods. Although, for LTI expense, part of this significant increase for 2017 and 2018 can be tied to an increase in the number of shares for recent years 2017 and 2018, and I will explain later that these increased shares are not necessarily directly tied to improved Financial-focused performance.

Q. Because you could not identify any substantial Financial-focused improvement for New Hampshire operations for 2016 to 2018 to justify a significant increase in STI and LTI expense, is it a concern that increases in STI and LTI expense are primarily driven by improved Financial-focused measured in other regional state jurisdictions?

A. Yes. I understand that STI and LTI expense in this rate case are driven in part by regional and Company-wide financial performance, and not just by the financial performance of New Hampshire. And I understand from an incentives policy standpoint, that executive/management personnel that influence financial-related performance in all of these jurisdictions should be evaluated and paid incentives on that regional/Company-wide basis.

However, for regulatory rate-making purposes, I do not believe it is reasonable that customers of New Hampshire Liberty electric operations should pay increased electricity rates due to improved or better Financial-focused performance in other state jurisdictions (compared to under-performing financial results in New Hampshire) which has contributed to significant increases in incentive expense in recent years as included in this rate case for Liberty New Hampshire operations. This is another reason supporting my two-part adjustment to STI and LTI expense, especially when Liberty has not met a reasonable burden of proof in justifying the significant increase in STI and LTI expense in recent years.

Q. What reason did the Company initially give for the $225,000 significant increase in STI from 2017 to 2018 in the prior table, and what are your concerns?

A. I will explain this below, along with numerous concerns regarding the Company's reasons and related responses.

First, OCA 1-43 asked the Company to explain the reasons for changes in STI expense from 2015 to 2018, and the Company stated the increase from 2015 to 2018 is "directly related to an increase in staff," and no further explanation or documentation was provided. Based on the brief response to OCA 1-43 which seemed unusual[21] and did not include supporting documentation, I decided to issue a follow-up data request OCA 7-17.

OCA 7-17.f referred to the response to OCA 1-43, and asked the Company to provide the number of employees eligible for STI during the periods 2015 to 2018, and the reasons for changes in the number of eligible employees. The Company's response to OCA 7-17.c. and OCA 7-17.f did not address the change in eligible STI employees, but now provided new reasons for the increase in STI (from 2017 to 2018) by referring to

[21] Liberty's response appeared unusual based on my analysis of the change in headcount which did not support the Company's statement.

changes in the structure of the bonus plan, changes in the corporate scorecard,[22] and increase in the New Hampshire employee population supporting Granite State Electric.

The Company did not provide any detailed written explanation of how these changes caused increases in STI from 2017 to 2018, or how much dollar impact each of the changes had on STI expense – mostly the Company referred to pre-existing attachments with a lot of numbers and data in the fields, but no explanation of what this information means. For example, Liberty's response to OCA 7-17.d provided a copy of a document called "2018 Bonus Plan Changes", but this document only states what the new 2018 "objectives, indicators, target, and stretch target" will be, it does not compare or explain what the prior 2017 data was, and it does not explain why these changes were made, and it does not identify the quantitative or qualitative impact of such 2018 changes.

The Company's vague response to OCA 7-17 referred to a change in scorecard as a reason for the increase in LTI expense from 2017 to 2018, so follow-up data request OCA TS 2-10.b asked the Company why it changed to a unified Liberty utilities scorecard from an individual state basis. The Company's response was, "All STIP measures moved to a unified Liberty Utilities scorecard in 2018. Please refer to Attachment 7-17.c." This response provided no reason for the change, and merely circled me back to the Company's original vague response to OCA 7-17 that did not provide the requested information.

[22] The Company changed to a unified Liberty Utilities Scorecard rather than state scorecards that had been used since 2015.

The Company's responses to OCA 7-17 caused me concern because it did not point to what should be the most obvious and important factor causing an increase in STI, which would be improved employee performance under the STI. Instead, the response points to more administrative and less-people focused reasons, such as changes in how the plans or scorecards were structured - which are all reasons that could make it easier for employees to qualify for increased incentive payments (leading to increased STI expense in 2018) without actually improving their performance. I am unable to state with certainty the reasons for the increase in STI expense from 2017 to 2018, because the Company did not provide a specific written explanation with supporting calculations that quantify the impact by type of factor causing the increase.

Also, the Company's response to OCA 7-17.d states that there was an increase in the balanced measures (performance) from 2016 to 2017, although this seemed to be contrary to a reduction in the actual STI expense from 2016 to 2017 (if performance increases or improves, this should lead to an increase in incentive expense). And although the Company refers to several Excel attachments for an "explanation of the increase", the related attachments did not include any written explanation or clarification.[23]

The burden of proof rests with the Company to explain and support the significant increase in STI expense, and these Company data request responses do not meet that

[23] The related Excel attachments OCA 7.17.d.1, 7-17.d.2, and 7-17.d.3 only included numbers and data in thousands of fields but did not include any written explanation of these results. I reviewed the data but did not attempt to interpret these results, because the Company provided no further explanation.

standard. The Company's initial explanation that increasing headcount was causing an increase in STI expense did not make sense, and I became further concerned that the Company required me to initiate a subsequent follow-up data request in order to elicit a revised response with a significantly different reason for the increase in STI expense from 2017 to 2018. However, the Company's subsequent response was again lacking an adequate explanation with supporting documentation for the Company's rationale.

Q. Will you continue to explain your second concern with the significant increase in STI expense from 2017 to 2018?

A. Although the Company subsequently appeared to back off its initial response that the increase in STI from 2017 to 2018 was due to increase in headcount, I decided to analyze headcount and determine if this was valid. The headcount data is shown in the table below, followed by my related analysis which indicates there is no strong correlation between headcount and STI expenses.

Table 7 - Headcount

Headcount (Source - OCA 1-23)			
	Average for each calendar year		
	2016	2017	2018
Electric Only	51	52	54
Electric/Gas Common	148	159	162
Total	199	211	216
Change in Electric #		1	2
Change in Electric %		2.0%	3.8%
Change in Common #		11	3
Change in Common %		7.4%	1.9%
Change in Total #		12	5
Change in Total %		6.0%	2.4%

I will use information from the table above to address the Company's assertion about the correlation between STI expense and headcount.[24] It is important to understand that for the category "Electric/Gas Common" employees shown above, this represents a group of common employees who work on both electric and gas matters, but for any specific year the Company is unable to identify either equivalent number of employees or the specific amount of payroll dollars assigned to specific electric or gas operations by this group. With that caveat, I am providing the information in the best format available from the Company.

1) STI expense decreased 31 percent from 2016 to 2017, but the headcount for all categories above increased from 2 percent to 7.4 percent, so there does not appear

to be any direct correlation from this data that the change in STI expense is tied to headcount changes.[25]

2) STI expense increased 74 percent from 2017 to 2018, but the maximum increase in headcount for any category above is 3.8 percent, so there does not appear to be any direct correlation from this data that the change in STI expense is tied to headcount changes.

In conclusion, the Company has not provided adequate explanation and supporting documentation to justify the significant increase of $225,000 (74 percent) in STI from 2017 to 2018, therefore it is reasonable to adjust STI downward to a more reasonable level of historical STI expense levels.

Q. Shifting to LTI expense now, what reason did the Company give for the tripling of LTI incentive expense from years 2015 and 2016, to years 2017 and 2018, (prior Table 6) and what are your concerns?

A. OCA 1-43.a asked Liberty to explain the reasons for changes in LTI expense from 2015 to 2018, and the Company stated the increase from 2016 to 2017 was based on, "…an increase in the total number of shares granted." Liberty also stated that the number of LTI shares granted is approved by the compensation committee and the board of directors and is based on Company performance and the number of qualified employees. The Company provided no further explanation, and no additional documentation or calculations supporting the increase in LTI expense.

[25] I understand that percentage change in STI expense percent for any specific year would not agree with the specific percentage change in headcount, but there should be a correlation in the general direction or magnitude of these changes, such that a large or small change in STI expense would correlate to a large or small change in the direction of headcount.

One of the most significant concerns is the increase in LTI expense appears to be primarily driven by an increase in the number of shares granted to a limited number of executive employees, yet the increase in the number of shares granted to these executives does not appear to be strongly tied, if at all, to executive's incentive performance. Therefore, regardless of specific executive performance under the LTI plan, the number of executive shares granted can increase significantly and may be the primary factor that is causing LTI expense to increase. This is a concern because it diminishes the justification and purpose of an LTI plan that is not primarily driven by incentives, and the LTI plan become just another avenue for giving executive employees increased pay.

Q. Can you elaborate on this substantial concern that increases in LTI expense appears to be driven by increases in the number of shares granted, and the increase in number of shares granted does not appear to be primarily driven by employee performance?

A. I do agree with the Company's response to OCA 1-43.a that the significant increase in LTI expense from the 2015-2016 period to the 2017-2018 is tied to an increase in the number of shares granted primarily. However, my concern is that the increase in shares does not appear to be primarily driven by executive performance under the LTI plan.

The Company's response to OCA 7-14.a is the primary support for my position and related concern. First, Liberty's response to OCA 7-14.a states, "No, there is no correlation between the number of awards granted in a given year and the ultimate performance factor for these grants."[26] Second, Liberty's response to OCA 7-14.d states that the significant increase in awards that started in 2017 was driven by a new policy (and 2017 was the first year of the significant increase in LTI expense per the previous table).

I interpret Liberty's response as meaning the number of executive awards can increase in any given year and this is not tied to an executive's performance under the LTI plan. Therefore, regardless of whether an executive does or does not meet specific incentive performance measures in any particular year, an executive could be granted a significant increase in shares. Thus, it appears the increase in the number of shares may be the most important individual factor that increases LTI expense from the 2015-2016 years to the 2017-2018 years (instead of executive performance under the incentive plan).[27]

Q. Can you elaborate on your concerns regarding the absence of supporting documentation to support the new policy change in 2017, along with concerns about LTI market studies?

A. Yes. To compound my prior concerns, the Company states that its increased number of shares is a result of a policy change in 2017, but the policy change has not been quantified, explained, or adequately supported. OCA TS 2-7.e, asked Liberty why this

[26] The Company's last statement in response to OCA 7-14 appears to provide somewhat of a conflicting statement, by stating that employee performance can increase or decrease the number of awards.
[27] The market value of the shares has also increased from years 2015-2016 to years 2017-2018, but that is not my concern.

new policy was implemented in 2017 and requested supporting documentation regarding the pros and cons of implementing such policy.

Liberty's response merely stated the change brings the LTI in alignment with industry practice, and the Company only cited to some market study results at Attachment OCA TS 2-7.e - - but the Company did not provide the actual market studies and underlying supporting documentation, and did not explain these market study results. OCA TS 2-7.f asked if the "new" policy was consistent with similarly sized and situated utilities as Liberty, and asked for related supporting documentation. Again, the Company only referred to the same prior market study results, but the response to OCA 2-7.e and OCA 2-7.f did not provide any supporting documentation for the Company-cited market studies related to LTIP.

Q. What does your experience tell you about market studies for comparing LTI?

A. It has been my experience that market studies for comparing actual LTI amounts for various similarly-sized and situated companies does not exist, rather these market studies show "total" executive compensation and the amount of LTI included in the total compensation amounts is based on a high-level estimate and is not based on actual LTI payments or expenses. However, because Liberty did not provide the actual LTI market studies supporting documentation, I cannot confirm if the LTI amount is based on actual results, is based on a high level estimate, or if Liberty has properly compared itself to similar-sized and situated utilities in the same geographic area. Regarding compensation studies, the devil is in the significant level of details, and there are numerous assumptions that can affect results and conclusions, so it is always important to review the underlying supporting documentation.

In conclusion, Liberty does not quantify specific reasons for the increase in LTI expense from the 2015-2016 years to the 2017-2018 years. And I find it unusual that LTI expense is not primarily driven by executive performance under the LTI plan, and this is contrary to the basic concept that incentive pay is premised upon – which is "pay for performance." If my interpretation of the Company's statements are correct, this and other concerns provide substantial justification for reducing 2018 LTI expense.

Q. Is it your position that executive performance does not have some impact on LTI expense?

A. No, it is my position that LTI expense appears to be primarily driven by the number of shares that is not influenced by executive performance, but I still believe LTI expense is driven to some degree by executive performance.

Q. Will you show the significant increase in shares for years 2017 and 2018 (caused by a policy change in 2017), that is primarily contributing to an increase in LTI expense?

A. The table below shows the significant increase in LTI-related shares for 2017 and 2018, compared to 2015 and 2016.

Table 8 – Significant Increase in LTI Shares or 2017 and 2018

	No. of		Source - OCA TS 1-15			
	Eligible	Grant	No. of Shares			
	Employees	Price	2015	2016	2017	2018
2013 Grant	7	$8.22	6,680			
2014 Grant	11	$8.22	18,967	18,967		
2015 Grant	12	$9.75	15,998	15,998	15,998	
2016 Grant	8	$11.66		7,667	7,667	7,667
2017 Grant	8	$13.65			24,562	24,562
2018 Grant	9	$12.63				23,013
Total 3-year performance period			41,645	42,632	48,227	55,242
Increase shares				987	5,595	7,015
Increase %				2%	13%	15%

The table above shows the number of shares have increased significantly, from 23,665 shares (15,998 and 7,667) in 2015 and 2016, to 47,575 shares (24,572 and 23,013) in 2017 and 2018, an increase of 101 percent. Although this trend began in 2016, the number of increasing shares have become concentrated among fewer executives over time, from a peak of 12 executives in 2015 to the current level of 8 or 9 executives from 2016 to 2018. Liberty's response to OCA 1-43.a states that the number of LTI shares is based on the number of qualified employees, but this is not an accurate statement because the number of shares has increased from 2016 to 2018 with a reduction in the number of qualified employees.

Q. What is your next concern with the significant increases for LTI in recent years from a known-and-measurable regulatory perspective?

A. I am concerned that LTI expense for the 2019 going forward period in this rate case, and any particular year, is not known-and-measurable from a regulatory perspective under the current incentive structure.

In this proceeding, the Company has not adjusted LTI expense, so Liberty's actual 2018 LTI expense is also its 2019 going forward estimate for this rate case. Because the 2019 going forward amount of LTI expense is not known-and-measurable, I believe it is reasonable to adjust the 2018 LTI expenses to a more normalized level reflective of actual past performance by using a 3-year average of 2015, 2016, and 2017 LTI expenses as the first step in my adjustment – prior to reducing LTI by the 50 percent financial-focus reduction as the second part of my adjustment.

The Company statements and reasons which support my conclusion that the 2019 going forward level of LTI expense (which is the 2018 actual LTI expense) is not known-and-measurable are set forth below.

First, LTI for any particular year is determined based upon a three-year performance and vesting period. For 2018 LTI awards, the performance period is 2018, and future years 2019 and 2020, and Company results for the third performance year are not usually available until the first quarter of the subsequent year. The total expense for the three-year period is recognized straight-line over the three-year performance period, and adjustments are made as necessary when information about updated performance factors are received. Also, the 2018 period includes true-up accruals related to prior performance years, primarily for the 2015 grants that were paid in 2018.[28]

[28] Liberty's response to OCA TS 2-10.d and OCA TS 2-10.e.

The final payout amount is only determined after the three-year performance period, and uses a blended score of the LTI efficiency/financial-focus,[29] safety, and customer service measures looked at collectively over that three-year period, so the 2013, 2014, and 2015 awards were paid out in 2016, 2017, and 2018, respectively.[30] For example, to the extent 2015, 2016, and 2017 actual performance affected 2018 LTI expense, the actual Efficiency/Financial-Focus measure (which is more heavily weighted than the other two factors) for these three prior years was much higher (and would result in greater LTI expense) than the 2018 Efficiency/Financial Focus measure. Therefore, the 2016, 2017, and 2018 performance measure had a three-year average Efficiency/Financial Focus measure of 136 percent, compared to the 2018 Efficiency/Financial Focus measure of 85 percent.[31]

This statement by Liberty raises concerns because this appears to indicate that the 2015 to 2017 three-year average Efficiency/Financial Focus measure of 136 percent was greater than the single-year 2018 Efficiency/Financial Focus of 85 percent, and that is supposed to explain why the 2017 and 2018 LTI expense is greater than the 2015 and 2016 LTI expense. I am concerned about this mis-match for regulatory rate-setting purposes, in test year 2018 the Company experienced inferior Efficiency/Financial performance (85 percent result), yet customer rates could reflect a higher level of LTI expense in 2018 due

[29] The efficiency performance measure is the same as the "financial-focused" performance measure.

[30] Liberty's response to OCA TS 1-18.b (Revised).

[31] Liberty's response to OCA TS 2-7.a, shows 2015, 2016, and 2017 Efficiency measures of 153 percent, 153 percent, and 102 percent, compared to the 2018 Efficiency measure of 85 percent.

to the supposed better financial performance in the three prior years 2015, 2016 and 2017. But even this statement by itself does not make sense, because prior years' 2015 and 2016 LTI expense was significantly lower than 2017 and 2018 LTI expense, and this would appear to indicate inferior financial performance for years 2015 and 2016 (and not better financial performance), which does not remedy the concerns about increased LTI expense in 2018 (using a three-year performance factor).

One mitigating factor could be the lower level of LTI expense in 2015 and 2016 was significantly impacted by the prior three-year performance period lag (2012, 2013, and 2014), regardless of what the actual performance was in 2015 and 2016. The bottom-line is that customer rates in 2018 should not reflect a higher level of LTI expense for better financial performance in the three prior years 2015 to 2017 compared to test year 2018 (although the LTI expense suggests financial performance was worse in 2015 to 2016, compared to 2017 and 2018) just because the LTI plan is set up in that manner by the Company.

Second, the response to OCA TS 2-7.c states that the projected performance factors for a future year are based on the most recent year as a proxy, and OCA TS 2-7.a indicates that estimated 2019 and 2020 performance is based on actual 2018 performance measures. However, using <u>one period</u> of historical performance to project future years' performance is not reasonable, especially when performance is based on a rolling three-year period (and not based on just a one-year period).

With this combination of above factors, the amount of actual 2019 going-forward LTI expense is an estimate, and is not based on actual known performance, thus it is not known-and-measurable. This supports using a three-year average of LTI expense to normalize this expense as the first part of my LTI adjustment.

Q. Will you explain your adjustment to remove part of the excessive and unsupported increase in 2018 STI and LTI expense (this adjustment occurs before the 50 percent adjustment is applied)?

A. First, I adjusted the STI and LTI 2018 expense to reasonable normalized amounts by removing the unsupported and excessive levels based on the concerns addressed previously in this section of my testimony, and then I removed 50 percent of the remaining balance to remove financially-focused incentive performance measures that are primarily beneficial to shareholder interests, and do not provide any significant or meaningful benefits to customers.

For STI, I started with the 2015 to 2017 3-year average of STI expense of $413,273 and deducted this from the actual 2018 STI book balance of $528,944, and disallowed the difference of $115,671 that reflects unsupported and excessive 2018 levels of STI. For the remaining balance of $413,273, I removed 50 percent of these costs or $206,636 related to financial-focused incentive measures that benefit shareholders, for a total adjustment to STI of $322,307 ($115,671 plus $206,636).

For LTI, I started with the 2015 to 2017 3-year average of LTI expense of $56,383 and deducted this from the actual 2018 STI book balance of $98,498, and disallowed the difference of $42,115 that reflects unsupported and excessive 2018 levels of LTI. For the remaining balance of $586,383, I removed 50 percent of these costs or $28,191 related to financial-focused incentive measures that benefit shareholders, for a total adjustment to STI of $70,306 ($42,115 plus $28,191). Therefore, the total incentive expense adjustment is $392,615.

Adjustment BCO-3: Payroll Taxes – Exhibit BCO-1, Schedule 2.3

Q. Will you summarize your adjustment to payroll tax expense?

A. Liberty originally proposed an Adjustment 2 to increase payroll taxes by $148,639, and its Corrections and Update filing revised this adjustment to a decrease in payroll taxes of $164,334. I am proposing an adjustment to reduce payroll taxes by an additional amount of $94,744.

My revision to the Company's payroll tax adjustment reflects adjustments that I made to payroll expense and short-term incentives, and I used the same format of the Company at its Payroll Tax Adjustment 2 at Schedule RR-3-02 (CU) with the exception described below.

The Company's payroll tax adjustment includes an amount of "2019 Salary & Wage Increase" of $1,421,487 at line 7, and this amount includes the Company's proposed

Adjustment 1 to increase payroll expense of $947,257, plus the Company's Regional Allocated Labor of $474,230. First, because I reduced payroll expense by an adjustment of $601,678, the base amount of $1,421,487 should be reduced by this amount. Second, the Regional Allocated Labor included in Liberty's base amount of $1,421,487 is not a "payroll increase" in this rate case, the Company only calculates a 3 percent increase on this payroll amount in its payroll adjustment. Therefore, the amount of $474,230 should also be removed from this portion of the payroll tax calculation.

Adjustment BCO-4: Depreciation Expense & Amortization Adjustment – Exhibit BCO-1, Schedule 2.4

Q. Will you summarize your adjustment to depreciation & amortization expense?

A. Liberty's original filing proposed to increase depreciation & amortization expense by $447,926 at Adjustment 8 and by $781,434 at Adjustment 6, and its Corrections and Updates filing now proposes to increase depreciation & amortization expense by $1,561,586 at Adjustment 8 (Schedule RR-3-08 CU) and there is no change from the original filing for Adjustment 6 (Schedule RR-3-06 CU). The increase in Liberty's proposed Adjustment 8 depreciation expense from $447,926 to $1,561,586 is due to: a) the removal of depreciation on water heater assets of $120,758; and b) an increase in depreciation expense of $1,234,419 to offset the reduction to depreciation expense of this same amount in the Company's original filing.[32]

[32] This depreciation expense is shown at Schedule RR-5-4 in the Company's original filing, and is related to the removal of the acquisition adjustment assets of $6, 172,095 in DG 11-040.

I am proposing an offsetting reduction to Liberty's Adjustment 8 depreciation & amortization expense of $661,150, which consists of the two following components:

1) <u>Impact of Liberty Proposed Depreciation Rates (Liberty Adjustment 8)</u> – Liberty depreciation rate witness Dane Watson has proposed new depreciation rates for various accounts which have an overall impact of increasing depreciation expense by about $546,852 (this does not include the reservice deficiency amortization impact of $233,300). The OCA has accepted Liberty's proposed amortization rates for intangible plant, but OCA is using existing depreciation rates for all other plant accounts and has removed the impact of proposed depreciation rates for all other plant accounts. This results in an adjustment to reduce depreciation expense by $427,850.

2) <u>Impact of Liberty Proposed Reserve Deficiency (Liberty Adjustment 8)</u> - Liberty depreciation rate witness Dane Watson has proposed amortization of a new reserve deficiency, and this results in an increase in depreciation expense of $233,300 (Schedule RR-3-09). I am removing the impact of this proposed reserve deficiency.

Q. Prior to addressing your concerns with the Liberty's depreciation expense adjustments, what position does OCA take on the Company's proposed new depreciation rates and reserve deficiency amortization?

A. Liberty's depreciation rates witness Dane Watson, proposes new depreciation rates (and a related overall increase in depreciation expense) and a new theoretical depreciation reserve deficiency of $1,399,800, and when amortized over six years this reserve deficiency produces an annual increase in depreciation expense of $233,300 (Sch. RR-3-09). I am primarily addressing Liberty's depreciation expense adjustment from an accounting/revenue requirement perspective, and I am not addressing the details of the proposed depreciation rates and reserve deficiency from the perspective of a depreciation rates expert.

I have accepted the Company's new proposed amortization rates for intangibles/software, and the related depreciation/amortization expense adjustment that I propose includes these new amortization rates. The changes in proposed amortization rates for intangibles/software are less complex. However, I have removed the impact of Liberty's proposed depreciation rates for all other plant accounts and I have removed the impact of Liberty's proposed theoretical reserve deficiency. Thus, I have reduced depreciation expense by $427,850 for the impact of Liberty's proposed depreciation rates on all other plant accounts except intangible assets. Also, I have removed the reserve deficiency amortization expense of $233,300.

Q. Will you explain your adjustment to depreciation and amortization expense and compare it to the adjustment proposed by Liberty?

A. The table below compares the depreciation and amortization expense adjustments proposed by Liberty and OCA, and I will explain these amounts.

Table 9 – Comparing Liberty and OCA Depreciation & Amortization Adjustments

A	B	C	D	E	F	G
Ln	Description	Liberty Adj.	Per Books	Difference between Liberty Adj. & Books	OCA Adj.	Difference between Liberty & OCA Adj.
1	Reserve surplus amort. from 2018	$781,434	-$781,434	$0	$781,434	$0
2	Amort. of acquistion assets in Liberty adj. & on books	$1,234,419	$1,234,419	$0	$1,234,419	$0
3	Deprec. expense at proposed rates for Liberty & OCA	$8,418,033	$7,871,181		$7,990,183	($427,850)
4	Liberty & OCA adjusted deprec. exp.	$9,652,452		$0	$9,224,602	
5	Liberty deprec. & amort expense per books		$8,324,166			
6	Liberty proposed reserve defic. amort.	$233,300			$0	($233,300)
7	Liberty & OCA adjusted deprec. exp.	$9,885,752	$8,324,166	$1,561,586	$9,224,602	($661,150)
8	Liberty/OCA adjusted deprec. and reserve surplus	$10,667,186	$8,324,166	$2,343,020	$10,006,036	($661,150)
9	Note 1 - Liberty adjusted depreciation expense per Company Schedule RR-2-1					**OCA Adj.**

I am proposing to reduce depreciation and amortization expense by $661,150 (column G, lines 7 and 8), and this consists of the two components: a) reducing depreciation expense by $427,850 (column G, line 3), which is the impact of Liberty's proposed depreciation rates applied to all other accounts except intangible plant accounts (I have used Liberty's proposed amortization rates for intangible assets); and b) reducing amortization expense by $233,300 (column G, line 6) related to Liberty's proposed theoretical reserve deficiency amortization. Both of the adjustment components reflect the difference between Liberty's proposed depreciation expense (column C lines 3 and 6) and OCA's proposed depreciation expense (column F, lines 3 and 6).

Liberty's proposed adjustment for depreciation and amortization expense of $1,561,586 (column E, line 7) is also reflected at Liberty's Schedule RR-3-08 (final column, line 43), and this adjustment reflects the difference between Liberty's final adjusted depreciation and amortization expense of $9,885,752 (column C, line 7) and the Company's per book amount of $8,324,166 (column D, line 7).

Liberty's adjusted depreciation and amortization expense of $9,652,452 (column C, line 4) is shown at Liberty Schedule RR-3-08 (final column, line 38), and Liberty's final adjusted amount of $9,885,752 including the $233,300 reserve deficiency (column C, line 6) is also reflected at Liberty Schedule RR-3-08 (final column, line 39). The OCA adjusted depreciation and amortization expense at column F, along with related calculations, is shown at related OCA exhibits for this adjustment.

Q. Will you explain how the Company treated the $781,434 of expiring reserve surplus amortization credit in its depreciation expense adjustment?

A. The amount of $781,434 is the Company's annual amortization of the accumulated reserve surplus[33] that expires in April 2019, and is reflected at Liberty Schedule RR-3-06 (CU). Because this amount was a reserve "surplus" the accounting entry was to debit Accumulated Amortization – Other Regulatory Asset (account 1823) and to credit Depreciation Expense (account 4030) - the amount is treated as a reduction or offset to depreciation expense on the 2018 books (and all prior applicable years). Thus, as shown at the previous table, the 2018 per book depreciation and amortization expense of $8,324,166 consists of depreciation/amortization expense of $9,105,600 ($1,234,419 plus

[33] Docket 13-063, Order No. 25,638, per the response to OCA TS 2-34.a, p. 3 of 3, the amount is amortized over five years as shown at Company Adjustment 6, Schedule RR-3-06 (CU).

$7,871,181 at column D, lines 2 and 3 of prior table), less the credit/offsetting amount of $781,434 related to the reserve surplus amortization.

Although it may be somewhat confusing, my understanding is that the Company proposed a separate adjustment to increase amortization expense by this reserve surplus amount of $781,434 to offset the credit amount recorded in the per book amounts so that depreciation expense is reflected on a proper going-forward basis, and so the credit amount of $781,434 is not reflected as a recurring amount in the future because this related amortization expires in April 2019. Per the prior table, the amount of $781,434 is shown as a debit adjustment to Liberty's adjustment (column c, line 1) and is shown as a credit amount per books (column d, line1), and these amounts properly offset each other to ensure that no going-forward amounts for this component are reflected in future rates.

Q. Will you explain how the Company treated the $1,234,419 of amortization expense related to acquisition assets from Docket DG 11-040 (Liberty Schedule RR-3-06)?

A. The related $1,234,419 of amortization expense and the related assets and accumulated depreciation reserve for these intangible acquisition assets should be removed from the rate case to be consistent with approved prior Commission practice. Because this amortization expense of $1,234,419 is included in both the Company's adjusted depreciation/amortization expense (prior table, column C, line 2) and in the 2018 per book amounts (prior table, column D, line 2), when the Company's adjusted depreciation balance is deducted from the 2018 per book depreciation balance, this amount gets zeroed out and is not reflected in the going-forward level of adjusted depreciation expense. This appears to be correct treatment.

Liberty's technical statement of Philip E. Greene and David B. Simek (page 4, item 9),[34] indicates it included an increase of $1,234,419 to its revised depreciation adjustment to offset this same credit amount that was incorrectly included in the Company's original depreciation expense adjustment. I reviewed the Company's proposed adjustments at Schedule RR-3 (CU), pages 1 to 3, and it does not appear that a formal adjustment was made by the Company to increase depreciation expense by this amount of $1,234,419. Because the amount of $1,234,419 is included in both the Company's adjusted depreciation expense and depreciation expense per books, these amounts properly offset each other and it is not necessary to increase the Company's adjustment a second time for this same amount of $1,234,419. It does not appear that the Company has made a second formal adjustment to increase depreciation expense by $1,234,419, and that appears to be the correct treatment. However, if I have overlooked a second adjustment, then depreciation expense would be overstated by this amount of $1,234,419 because it would be recovered twice in the revenue requirement.

[34] This document was filed with the Company's Corrections and Update filing on November 22, 2019 to explain revised adjustments proposed by Liberty.

Q. Do the Company's workpapers properly calculate amortization expense on the intangibles plant balance of $6,172,095 related to the acquisition asset from Docket DG 11-040?

A. It does not appear so, but the difference is likely immaterial. First, the plant balance of $6,172,095, along with the related accumulated depreciation, and amortization expense of $1,234,419 should be properly removed from rate base and the depreciation expense adjustment calculation. However, if the related amortization expense of $1,234,419 is properly included in both the depreciation expense adjustment and the amounts per books (which Liberty appears to have done), then this amount is effectively removed from the case when the per book amounts are deducted from the Company adjusted amount in determining the related adjustment for depreciation expense.

However, there may be a minor reconciliation issue that causes a slight difference in the amount of amortization expense calculated on the $6,172,095 acquisition asset included in the Company's adjustment. Per Liberty's Schedule RR-3-08, under the column titled "Adjustments to Plant Balances", the Company removed total intangibles plant of $10,987,554, and then re-allocated these amounts to specific intangibles accounts based on their specific and applicable amortization rate (so there is no net change in intangible plant amounts, just a re-allocation of these amounts). However, as this Schedule shows, after re-allocation, none of the re-allocated amounts are as great as the acquisition asset of $6,172,095, so it does not appear that the acquisition asset was entirely allocated to one account with the proper related amortization rate of 20 percent, so part of the re-allocated balance could have been shifted to one or several accounts with amortization rates that vary from 10 percent, to 20 percent, to 33 percent (and there should not be a change in amortization rate for this related acquisition asset). I have made an adjustment in my workpaper exhibit to re-allocate these amounts so that the maximum amount of $6,172,095 is allocated to an intangible asset account using the proper 20 percent amortization rate (and this also means that asset amounts of other accounts had to be reduced as part of this re-allocation). This does not have a significant impact on my final proposed adjustment.

Adjustment BCO-5: Pole Rental Fees – Exhibit BCO-1, Schedule 2.5

Q. Will you summarize your adjustment to pole rental fees?

A. Liberty does not propose any adjustments to pole rental fees, but I am proposing an adjustment to increase pole rental fees by $53,619, in addition to the amounts already recorded on 2018 Company books of $250,438. The OCA calculation supporting pole rental fees uses Liberty's spreadsheet provided with OCA 2-23, and because this document is voluminous the OCA's detailed adjustment calculation will be provided in a supporting workpaper (and not provided as an Exhibit).

Q. Why are you proposing an adjustment to increase pole rental fees?

A. OCA data requests sought additional information from the Company about pole rental fees. The Company's response to OCA 2-23 supported an increase in pole rental fees.

First, The Company's response to OCA 2-23 states that pole rental fees have not increased since Liberty acquired the National Grid assets. Therefore, it is reasonable to update pole rental fees.

Second, the Company's response to OCA 2-23 states that contracts for wireless facilities provide for a yearly increase. I do not believe Liberty has been increasing these fees based on its various responses to OCA 2-23.

Third, the Company's response to OCA 2-23 states the adoption of the current version of the Puc 1300 rules on September 1, 2018 require pole owners to adopt the FCC calculation among other things. The Company reviewed its pole attachment fees in 2018 using the related formula to ensure fees were consistent with the FCC formula because those calculations had not been performed in the past. The Company determined there could be an increase in the Standard Rate from $20.03 to $24.33 (for solely owned poles), although the Company has not updated these rates because there are 21 different attachers and each contract would need to be reopened.

Q. Should pole rental fees be reflected at cost, per FCC requirements?

A. Yes. Based on my experience and understanding of the FCC formula for pole rental fees calculation, the cost standard is fully allocated costs. I believe it is reasonable to update pole rental fees to help ensure, at the very least, that the Company's pole rental rates are closer to cost. If pole rental fees are below cost, then arguably the amount of fees collected by the Company from pole attachers are not adequate to cover its costs, and any related cost deficiency will be subsidized and born by ratepayers, who will then effectively subsidize both the Company and pole attachers. It is neither reasonable nor sustainable that ratepayers should subsidize any party for below-cost pole rental fees, particularly when the Company has the necessary legal basis and cost-causation foundation to seek and support a reasonable increase in these pole rental rates from attachers.

Q. Do you have the cost and supporting documentation that would enable you to determine the current cost to support updated pole rental fees?

A. No. Therefore, I am relying on information provided by the Company in its response to OCA 2-23 which indicates it determined that an increase in rate from $20.03 to $24.33 could be justified by the present formula. Thus, I am using the amount of $24.33 as the amount for pole rental fees (solely owned poles) in my calculation.

Q. How did you calculate updated pole rental fees for other types of poles, give you only have the updated rate of $24.33 for Standard Rate – Solely Owned Poles?

A. The Company's increase in rate for the Standard Rate – Solely Owned Poles from $20.03 to $24.33 reflects a 21.47 percent increase. For the three remaining types of Pole Rates shown below, I applied this same 21.47 percent increase as a reasonable surrogate pole rental fee increase to arrive the adjusted fees below. I then applied these revised pole rental fees to the number and type of poles provide in response to Attachment OCA 2-23.b.1, to arrive at my proposed adjustment of $53,619.

	Current Rate	Proposed Rate	% Increase
1) Standard Rate – Solely Owned Pole	$20.03	$24.33	21.47%
2) Standard Rate – Jointly Owned Pole	$10.02	$12.17	21.47%
3) Cable Rate – Solely Owned Pole	$13.84	$16.81	21.47%
4) Cable Rate – Jointly Owned Pole	$6.92	$8.40	21.47

Q. The Company's response to OCA 2-23.d states there are other complications in negotiating revised pole rental rates with other parties. Regardless of the Company position, are you proposing to impute additional revenues for pole rental fees which will effectively avoid any claimed complications?

A. Yes. The Company's full response to OCA 2-23.d states that Puc 1300 rules provide for negotiation between parties, but there are other considerations in Puc 1304.06 that complicate the question of whether the proposed FCC rate of $24.33 would be just and reasonable for each attaching entity.[35] I don't know which complications the Company is specifically referring to and the related implications for this rate case. The Company has not formally asserted that the cost of negotiating new pole rental rates would exceed the benefit of increased revenues, and I would not necessarily agree with that conclusion without substantiation. In addition, any cost of negotiation could be borne by the Company's internal legal staff, and if additional outside legal assistance was needed then these types of costs are recoverable in a rate case (as are the Company's payroll costs for its internal legal staff).

[35] The Company's response to OCA TS 1-29 makes the same point, but does not lend any further detail regarding specific complications or related costs.

However, I am proposing that additional pole rental fees and related revenues of $53,619 be imputed into the revenue requirement of this case. Imputing these pole rental revenues helps ensure that customers are not subsidizing the Company or pole attachers for below-cost fees, and it also avoids imposing any time and cost imposition upon the Company that they might normally assert would develop from negotiations. Adopting this imputation method does not mean that the Company is actually collecting these increased pole rental fees from attachers, but this method avoids any argument of new imposed costs on the Company, and it can also give the Company an incentive to negotiate new pole rental fees if it believes that would be beneficial to offsetting any negative impacts it perceives from this revenue imputation.

Q. The Company's Confidential response to OCA 7-34.b.4, page 18 of 45, addresses poles, how does this situation bear upon your recommendation?

A. The Company's Confidential response indicates **BEGIN CONFIDENTIAL*****

[redacted]

[redacted] *****END CONFIDENTIAL.**

Q. Without disclosing any Confidential information, did the previous Q & A about poles include any information to undermine your proposed adjustment?

A. No.

Adjustment BCO-6: Income Tax Expense – Exhibit BCO-1, Schedule 2.6

Q. Will you summarize your adjustment to true-up income taxes?

A. This adjustment adjusts income tax expense for the incremental impact of the adjustments that I propose, and results in an increase in income taxes of $488,525.

Adjustment BCO-7: Cash Working Capital – Exhibit BCO-1, Schedule 2.7

Q. Will you summarize your adjustment to cash working capital?

A. I used the same cash working capital ("CWC") formula as Liberty and this produced a reduction in CWC of $91,721.

Q. Are you proposing an adjustment to interest synchronization?

A. No. This impact would appear to be immaterial, so no adjustment is proposed.

III. 2019 Step Increase

2019 Step Increase – Exhibit BCO-2

Q. Are you proposing adjustments to Liberty's 2019 Step Increase capital plant additions?

A. Yes.

Q. What amount are you using for the starting point of your adjustments to the 2019 Step Increase?

A. I am using a starting point of $14,967,736 (gross plant) for the 2019 Step Increase, and this is the same amount included in Liberty's original filing at Attachment PEG/DBS-2, Sch. Step, p. 1 of 2 (also cited as the "2019 Capital Budget" at this schedule) and cited in the Joint Direct Testimony of Philip E. Greene and David

B. Simek.[36]

OCA 2-10 asked Liberty to reconcile its proposed 2019 Step Increase of $14,967,736 to the amount of $20,034,736 referred to as the "Current Year 2019 Capital Budget" at the Filing Requirements Puc 1604.01 (a)(8). Liberty's response stated the 2019 Step Increase of $14,967,736 inadvertently excluded three projects totaling $3,342,000,[37] and the remaining difference of $1,725,000 is due to the removal of the Reliability Enhancement Plan (REP) projects.

I anticipated that Liberty's November 22, 2019 Corrections and Update Filing would include the revisions and additions to the 2019 Step Increase of $14,967,736, but the filing did not address the 2019 Step Increase or any revisions to these amounts. Therefore, I will rely on the 2019 Step Increase of $14,967,736 because this is the amount supported in the Company's original filing by its witnesses and underlying schedules.

Q. Will another OCA witness address the timeline for recovery of the 2019 Step Increase?

A. Yes. Liberty proposes to recover the revenue requirement impact of this 2019 Step Increase, which is $2,293,431, upon implementation of permanent rates but no earlier than January 1, 2020 (for these projects completed by December 31, 2019). OCA witness Ron Nelson will propose a timeline for recovery of these capital projects.

[36] Page 17, line 14, Bate II-093.

[37] These three projects included Project 8830-1937 GSE-DIST-New-Resid Blanket - $1,000,000, Project 8830-1938 GSE-DIST-New Bus- Comm Blanket - $1442,000, and Project 8830-1958 Install Services to Tuscan Village South Line - $900,000.

Q. Are the Step Increase plant additions added to rate base of this case and recovered in the same manner as the traditional revenue requirements?

A. No, these amounts are not included in rate base and are not recovered from customers in the same manner via permanent rates to be established in the revenue requirements of this case. Instead, these amounts are handled consistently with the treatment in the past, whereas the Company seeks to recover the revenue requirement impact of these post-test period plant additions (constructed during 2019) from customers as soon as possible after construction is completed at December 31, 2019 - and before the completion of hearings in this case and a final Order that will establish the new customer rates for the traditional revenue requirement in this proceeding.

Q. Should the revenue requirement calculation inputs for these Step Increases be updated after the amount of these capital additions is determined?

A. Yes. The existing components of rate of return and property taxes should be updated for any adjustments/revisions in this case.

Q. Can you summarize the adjustments you are proposing to the 2019 Step Increase plant additions?

A. I am proposing the following adjustments to the 2019 Step Increase:

Table 10 – Adjustments to 2019 Step Increase:

A	B	C
		2019
		Step Increase
Line	Adjustments	Adjustments
1	Beginning 2019 Step Increase	$14,967,736
2	Adjustments:	
3	1 - Reduce internal capitalized labor	($2,680,000)
4	2 - Battery back-up for customer meters	($1,000,000)
5	3 - Unidentified discretionary projects	($100,000)
6	4 - Londonderry project removed by Liberty	($660,000)
7	5 - ARP breakers & closers project cancelled	($225,000)
8	Total capital costs removed	($4,665,000)
9	Revised 2019 Step Increase	$10,302,736

Q. Why did you adjust the 2019 Step Increase plant additions related to internal capitalized labor?

A. Liberty's response to OCA TS 1-21 states the estimated internal capitalized labor[38] included in the 2019 Step Increase was $5,092,000, although the Company cannot identify capitalized labor by specific project. In contrast, Liberty's response to OCA 2-47 indicates that Liberty's internal capitalized labor per the 2019 Budget will be $3,600,000 (at 33 percent capitalized and 67 percent expensed), although part of this internal capitalized

[38] The term "internal" refers to capitalized labor only from Liberty's work force and does not include labor of outside vendors.

labor could be related to deferred storm costs and the data request response did not identify these amounts separately.

Liberty's response to OCA 1-12.a identifies 2018 actual internal capitalized plant-related labor of $2,578,756 (along with other capitalized labor of $1,265,260 that is presumably storm-related), which results in total internal capitalized labor of $3,844,017, and the ratio of capitalized plant labor to total internal labor is 67 percent ($2,578,756 divided by $3,844,017). I next applied the actual 67 percent ratio of plant-related labor for 2018, to the estimated 2019 Budget total capitalized labor of $3,600,000 (from OCA 2-47),[39] and this produces estimated plant-related labor of $2,412,000 for 2019.

This calculation indicates the Company's total internal capitalized labor related for plant of $5,092,000 (related to plant, per OCA TS 1-21) exceeds the Company's 2019 Budget internal capitalized labor for plant of $2,412,000 (as calculated above), by an amount of $2,680,000. Thus, my adjustment will reduce capitalized plant additions by $2,680,000.

Part of my concern regarding this adjustment is to make sure the Company does not gain a benefit by overstating its capitalized labor for purposes of the 2019 Step Increase (to increase rate base and customer rates), and in contrast trying to understate its capitalized labor for purposes of the payroll adjustment (which would increase the amount of payroll expensed and increase customer rates). The Company should not be

[39] I applied the actual 2018 plant-related capital labor ratio of 67 percent to the 2019 Budgeted total capitalized labor (total includes "plant" and "storm" capital labor) to arrive at estimated 2019 Budgeted plant-related capital labor. This calculation is performed to create a match between 2019 Budget plant-related labor and the related 2019 Step Increase plant additions (because this 2019 plant-related labor will be part of the cost included in the 2019 Step Increase plant additions).

able to unduly benefit from overstated capitalized labor for one adjustment (2019 Step Increase) while also unduly benefitting from the understatement of labor for the other adjustment (payroll expense adjustment).

Q. Why did you remove $1,000,000 from the discretionary category of the 2019 Step Increase plant additions related to battery back-up?

A. I have removed the $1,000,000[40] of Tesla batteries for backing up customer meters because Liberty has not proved it is compliant with terms of the Commission's 2019 Order in DE 17-189 related to this matter, the Company has not included any offsetting adjustments for customer payments for these batteries (in order to provide proper matching for all impacted revenue requirement components), and this cost is included in the "discretionary" and is a lower priority with less certainty and support.

The Commission's Order in DE 17-189,[41] page 39-41, expressed concern that the Company costs presented only as estimated in the proceeding could be much greater than anticipated, including costs related to the battery price, installation cost, Cogsdale billing system upgrade costs and meter programming expenses. If these costs are significantly more expensive than was anticipated, this would reduce the net benefits of the program. Thus, the Commission required Liberty to promptly inform the Commission, Staff, and parties if any program cost items are expected to be greater than

[40] Attachment PEG/DBS-2, Schedule Step, p. 1 of the filing related to the 2019 Capital Budget, and project # 8830-1933 of OCA 7-25, OCA 1-2.3, and the filing requirements Puc 1604.01(a)(8), p. 1 of 2.
[41] Commission Order No. 26,206, dated January 17, 2019, *Petition to Approve Battery Storage Program, Order Approving Settlement Agreement and Implementation of Pilot Program and Granting Motions for Confidential Treatment.*

estimated because this might warrant a re-evaluation of the decision to authorize implementation of the pilot program.

Also, the Commission was not satisfied that Liberty had completely evaluated the potential of cybersecurity risks, or that these could be adequately mitigated. Before Phase I of the pilot is implemented, the Commission required that Liberty complete a comprehensive evaluation of the cybersecurity risk and confirm there are no risks. And an evaluation of the related vendors' practices must be completed by Liberty and deemed to be sufficient, along with a written certification confirming that such evaluations have been completed and conclusions reached, including documentation describing the supporting methods used and a copy of the Cybersecurity Plan. There are other requirements to be met also, including a customer education and information program to be collaborated with Staff, OCA and other parties.

OCA TS 1-27.a asked Liberty for the per unit costs of batteries included in its $1,000,000 budget and related copies of purchase orders, bids, and other documents to support the price. Liberty's response only referred to its estimated battery prices provided in DE 17-189, and it did not provide the actual battery prices and related purchase orders or invoices supporting the $1,000,000 budget. Liberty's response to OCA TS 1-27.c makes a statement about battery prices being reduced to $6,500, but it is not clear if this has been achieved because the contract has not been signed yet so there is no documentation to support this statement. Liberty states that the $1,000,000 budget for 2019 was prepared in 2018 when the pilot had not yet been approved and the final number of batteries was not yet known. Finally, the Company states it has not included any offsetting impacts in this rate case such as potential payments by customers, because it does not have a list of customers signed up regarding their choice of payment options.

Q. Are you aware of recent activity in Docket No. DE 17-189, and does this change your opinion regarding this adjustment?

A. I am aware of recent information provided by the Company and some of this may help satisfy some prior Commission concerns,[42] but this does not change my opinion because there are remaining concerns. I am aware that on October 17, 2019, Liberty filed a Motion to delay its battery installation to February 28, 2020, and this issue was addressed in Heather M. Tebbetts Technical Statement provided to the Commission on November 25, 2019. This delay for the install date is significantly beyond the December 31, 2019 date when Liberty states that all of its plant additions related to the 2019 Step Increase will be in service. These batteries will not be considered completed, installed, or treated as Plant in Service at December 31, 2019, given installation is not until February 28, 2020.

In addition, the Company's October 17, 2019 filing included a detailed spreadsheet with costs and benefits, and Liberty's $1,000,000 Step Increase adjustment does not include any of the offsetting benefits identified in this spreadsheet. The full impact of battery installation should be reflected in revenue requirements, and not just the "cost" portion that increases revenue requirements.

[42] Such as the cybersecurity review, which is now complete.

There are still questions regarding Company compliance with the Commission's Order, therefore, this line item of $1,000,000 should be removed from the 2019 Step Increase.

Q. Why did you remove $100,000 from the discretionary category of the 2019 Step Increase plant additions related to reserve for unidentified discretionary projects?

A. I have removed $100,000[43] of reserve for unidentified discretionary projects because the descriptions, purpose and benefits are vague and "unidentified", and this appears to be a highly discretionary item. Also, per Liberty's response to OCA TS 1-22, the "reserve for unidentified discretionary projects" was not included as a line item in prior 2016 to 2018 budgets and this was the first year it was included.

Q. Why did you remove $660,000 from the discretionary category of the 2019 Step Increase plant additions related to reserve for Londonderry reconfiguration projects?

A. I have removed $660,000[44] related to the Londonderry reconfiguration because Liberty's response to OCA 7-25 and OCA TS 2-18.i indicates this project has been removed from the 2019 budget.

[43] Project # 8830-1926 of Staff 3-28.h, OCA 7-25, Staff 3-28, and the filing requirements Puc 1604.01(a)(8), p. 1 of 2.

[44] Project # 8830-1948 of Staff 3-28.h, OCA 7-25, Staff 3-28, and the filing requirements Puc 1604.01(a)(8), p. 1 of 2.

Q. Why did you remove $225,000 from the discretionary category of the 2019 Step Increase plant additions related to reserve for ARP breakers & reclosers projects?

A. I have removed $225,000[45] related to ARP breakers & reclosers because Liberty's response to OCA 7-25 and OCA TS 2-18.g confirm that this project has been cancelled and all costs are reclassified to expenses.

Q. Does this conclude your testimony?

A. Yes.

[45] Project # 8830-1940 of Staff 3-28.h, OCA 7-25, Staff 3-28, and the filing requirements Puc 1604.01(a)(8), p. 1 of 2.