COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION

APPLICATION OF

VIRGINIA-AMERICAN WATER COMPANY **CASE NO. PUR-2021-00255**

For a general increase in rates

APPLICATION OF

VIRGINIA-AMERICAN WATER COMPANY **CASE NO. PUR-2019-00176**

For an Annual Informational Filing

APPLICATION OF

VIRGINIA-AMERICAN WATER COMPANY **CASE NO. PUR-2020-00249**

For an Annual Informational Filing

REPORT OF ALEXANDER F. SKIRPAN, JR., CHIEF HEARING EXAMINER

December 2, 2022

VAWC requested implementation of the second of three rate consolidation steps and an overall increase in rates of approximately $14.3 million. In addition, issues related to two ongoing AIF cases were addressed in this proceeding. A Stipulation between VAWC, Staff, and Alexandria was offered to resolve all issues in these cases, except for the Staff's AIF recommendation to refund a portion of the WWISC revenues collected from Alexandria customers. Among other things, the Stipulation provided for an overall increase in rates of approximately $10.75 million. Consumer Counsel supported the Stipulation. The Committee opposed the Stipulation, especially the proposal to allocate an additional third of the PWS to all water districts. Based on the record, I find the Commission should approve the Stipulation subject to keeping the existing rate structure for Hopewell's potable industrial customers with each existing volumetric rate block changing by the same percentage. Finally, based on the additional revenues collected from Alexandria customers pursuant to rate consolidation, I find there should be no refunds of WWISC revenues.

HISTORY OF THE CASE

On November 15, 2021, Virginia-American Water Company ("VAWC" or "Company") filed with the State Corporation Commission ("Commission") an application for a general increase in rates, together with testimonies and exhibits, and certain schedules filed under seal pursuant to Rule 170[1] of the Commission's Rules of Practice and Procedure ("Procedural

[1] 5 VAC 5-20-170 ("Rule 170").

Rules")[2] ("Application").[3] The Company filed its Application pursuant to Chapter 10 of Title 56 of the Code of Virginia ("Code")[4] and the Commission's Rules Governing Utility Rate Applications and Annual Informational Filings of Investor-owned Gas and Water Utilities ("Rate Case Rules").[5] Among other things, the Company requests authority to increase its rates to produce additional annual jurisdictional sales revenues of $14,317,277, or an increase of 27.60 percent over present pro forma revenues.

Concurrent with the filing of its Application, the Company filed a Motion for Protective Ruling. A Hearing Examiner's Protective Ruling was entered on December 22, 2021.

On December 21, 2021, the Commission issued its Order for Notice and Hearing in which, among other things, the Commission: (i) docketed this matter as Case No. PUR-2021-00255; (ii) scheduled a telephonic hearing for the receipt of testimony from public witnesses for September 23, 2022; (iii) scheduled a hearing to receive the testimony and evidence from the Company, any respondents, and Staff for September 27, 2022; (iv) prescribed notice to the public; and (v) appointed a Hearing Examiner to conduct all further proceedings in this matter on behalf of the Commission.

On January 10, 2022, the Hopewell Committee for Fair Water Rates ("Committee") filed its notice of participation. On February 14, 2022, the City of Alexandria ("Alexandria") filed its notice of participation. On March 17, 2022, the Office of the Attorney General's Division of Consumer Counsel ("Consumer Counsel") filed its notice of participation.

On February 17, 2022, VAWC filed its Motion to Modify Notice, to Prescribe Additional Notice, to Modify Procedural Schedule, and for Expedited Consideration ("Notice Motion"). In its Notice Motion, the Company requested the Commission or Hearing Examiner:

> (1) modify the prescribed notice to the public; (2) prescribe additional notice of the rate changes requested in the Company's Application in this proceeding pursuant to § 56-237.1 [B] of the [Code]; and (3) modify the procedural schedule in this proceeding for the limited purpose of providing the Company sufficient time to complete the modified notice requirements.[6]

VAWC's Notice Motion was granted in a Hearing Examiner's Ruling dated February 18, 2022. VAWC filed its Proof of Publication and Notice on March 30, 2022.

On March 3, 2022, the Commission entered its Order in Case No. PUR-2019-00176 and Case No. PUR-2020-00249 ("AIF Proceedings") that among other things directed "the Hearing

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[2] 5 VAC 5-20-10 *et seq.*

[3] The Application was complete on December 9, 2021.

[4] Code § 56-232 *et seq.*

[5] 20 VAC 5-201-10 *et seq.*

[6] Notice Motion at 1.

Examiner appointed to conduct all further proceedings in Case No. PUR-2021-00255 hereby is also appointed to conduct all further proceedings in [the AIF Proceedings] on behalf of the Commission and to file a final report in each case containing the Hearing Examiner's findings and recommendations."[7] A Hearing Examiner's Ruling dated March 14, 2022, established that the AIF Proceedings would proceed concurrent with Case No. PUR-2021-00255.

On May 26, 2022, Consumer Counsel filed its Motion to Revise Procedural Schedule for Respondent Testimony in which Consumer Counsel requested that the date for the filing of respondent testimony be extended from June 28, 2022, to July 19, 2022. A Hearing Examiner's Ruling dated May 26, 2022, granted Consumer Counsel's motion.

On July 13, 2022, VAWC filed its Motion for Leave to File Supplemental Testimony ("Supplemental Testimony Motion"), along with the supplemental direct testimony of John S. Tomac and Scott T. Grace. A Hearing Examiner's Ruling dated July 14, 2022, provided for the filing of expedited responses and a reply. On July 21, 2022, Staff filed its response in which it did not object to VAWC's Supplemental Testimony Motion subject to: (i) maintaining the remaining procedural timeline; and (ii) permitting respondents to supplement their prefiled direct testimony on or before August 16, 2022. On July 25, 2022, VAWC filed its reply in which the Company stated that it did not oppose Staff's qualifications. A Hearing Examiner's Ruling dated July 26, 2022, granted VAWC's Supplemental Testimony Motion, subject to Staff's qualifications.

On July 19, 2022, Alexandria, the Committee, and Consumer Counsel filed their direct testimony and exhibits.

[7] Order at Ordering Paragraph (1). In a footnote to Ordering Paragraph (1), the Commission stated: "We leave to the Hearing Examiner's discretion whether and how to combine and/or consolidate Case Nos. PUR-2019-00176, PUR-2020-00249, and PUR-2021-00255." Order at 5, n.19.

During the proceeding, 247 public comments were filed in opposition to VAWC's Application.[8] A public comment was filed that did not oppose the Application.[9] One public comment was filed in support of the rate increase.[10]

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[8] The public comments in opposition to the Application were filed by: Brian Goldberg, Elizabeth Sprinkel, Danielle Hagerty, Charles McCarthy, Ashley Smith, John Turner, Kevin Turner, Julia Heald, Deborah Dimon, William Rooney, Rachel VanJohnson, Barbara Beach, Jane Knops, Chris Salameh, Cheryl Vann, Noah Sweet, D. Koslov, Sarah Wholey, Diana Willis, Nathan Lefler, Sharon Guthrie, Danielle Wolf, Jason Sweat, Francesco Palmeri, Mark Hagood, Lily Knol, John Mudd, Megan McIntyre, Jeff Bandy, Marilyn Stegman, Martha Schiele, Aleasa Chiles, Andrew Palmer, Peter Kim, Nicole Thompson, Brooksene Ambos, Carla Kooij, Liz Bostick, Edward Welch, Susan Lefler, Felix Fernandes, Lynette Foste, Nancy Blanton, Bob Morgan, Abel Mengisteab, Ehsanullah Hayat, George Jackson, Sally Bawcombe, Brenda Doherty, Carole Kordich, Adam Grossman, Harold Adams, Ryan Reynolds, Sally Reinholdt, Kathryn Salerno, Allan Krinsman, Amy Anda, Dolores Murray, Bea Porter, L. McCaslin, Monte Joyce Cross, Jeff Yake, Lauren Shanks, Rebecca Cointin, Victoria Bradley, Alicia Hempfling, Marietta Saunders, Karen Hughto, Louis Turnage, Caywood Black, Katherine O'Connell, Margaret Canale, William Lipsett, Stephanie Wurth, Sudipta Banerjee, Leander Wick, Carol Maggio, Jill Zajac, Germaine Schaefer, Joe Hirsch, John Craig, Mary Ann Rehnke, John Crocker, Daniel Reifsnyder, Maria Bolden-Turner, Daniel Hamilton, Anne Keady, Orr Ganel, Timothy Jordan, Jorge Caballero, Jr., Norman Lisy, Andrew Sudano, Diane Webster, Blaine Reyes, Chris Barrazotto, Avi Mersky, Marie Slusher, Nanci Edwards, Jonathan Hartwick, Virginia McGee, Joseph Williams, Stephen Karoly, Leslie Ziegler, Karen Downey, Edward Garcia, Cameron Crippa, Shabbar Saifee, Sarah Miller, Holly Johnson, Dr. Poorvi Shah, Robert Tanner, Lauren Troupe, Matthew Bigman, Albert Turnbull, Kerri Sweet, Kathleen Pisch, David Mudarri, Cheryl Malloy, Jacqueline Chimento, Arthur Impastato, John Blizard, Ana Rodriguez, Jody Mazzarese, Ahmet Gerdaneri, Robert Marin, Taylor Mountain, Julie Wieland, Isaac DSouza, Robert Irmer, Lynthia Robinson, Lynne Russillo, Jazmin Delgado, Robert Erickson, Shetia Wells, Megan Waterhouse, Kanessa Trent, Seth Tinkham, Martin Schwetizer, Hilda Danshaw, Laura Kanthula, Barbra Byington, Sokthida Nguon, Paige Roy, Louise Van Diepen, Kathryn Buscaglia, Bryce Harper, Stephanie Buscaglia, El Bert, Megan Brown, Mary Crutchfield, Howard Weiss, Hong Goh, Anne Houston, Molly Weaver, Deirdre Kelly, Lauren Heslep, Jeff Snavely, Melissa Wader, Gregory Miller, Helen Westmoreland, Shi Lee, Meghan Reppond, Jennifer Schneider, Samantha Morgan, Angela Kyprianou, Patrick Murphy, Ashley Newcomer, Emily Vernon, Kelsey Scalera, Thom Downing, Megan Eckhardt, Emily Allen, Kristen Gonzalez, Christina Amatos, Gerrish Flynn, Megan Amsalem, Mehrnoosh Behzadi, Greta Bertinot, Julie Selby, LeRonda Brooks, Jessica Bylunx, Hadj Osmani, Sarah Manning, Diana Rodriguez, Catherine Silvey, Ellen Brown, Audrey Brown, Christine Coker, Frank Mikolajczak, Donald Heald, Tara Cain, John Brockhouse, Dan Sheehan, Carhy Matus, Karen Rae, Kristin Kvasnyuk, Hannah Goetz, Dara Rosenfeld, Catherine Corp, Aaron Hall, Deborah Williams, Dawn Bursk, Katherine Borg, Denise Hasley, Gianfranco DiStefano, Maria Garcia, Charles Snyder, Michael Foley, Emily White, Jen Gaines Bender, Wade Miller, Shaun Villanueva-Unger, Jeremy Hogg, David Touhey, Meredith Pollock, Melanie Eckberg,

The Commission's Procedural Order scheduled a hearing to begin on September 27, 2022; and left the question of whether the hearing would be conducted virtually or in-person to further order or ruling. Based on the opening of the Commission's building to the public, a Hearing Examiner's Ruling dated August 12, 2022 ("August 12th Ruling"), advised case participants that the portion of the public hearing commencing on September 27, 2022, would be conducted in the Commission's courtroom and adopted special procedures for such proceeding. Directing Paragraph 2 of the August 12th Ruling provided persons experiencing COVID-19 symptoms, a fever, or having been diagnosed with COVID-19 in the past 10 days will be prohibited from entering the Tyler Building. Due to a change in circumstances, a Hearing Examiner's Ruling dated September 20, 2022, advised case participants that the portion of the public hearing commencing on September 27, 2022, would be conducted virtually, via Teams.

On August 16, 2022, Consumer Counsel filed its supplemental testimony and exhibits, and Staff filed its direct testimony and exhibits.

On September 6, 2022, VAWC filed its rebuttal testimony and exhibits.

On September 26, 2022, VAWC filed a Stipulation and Joint Motion to Accept Stipulation in which VAWC, Staff, and Alexandria ("Stipulating Participants") requested approval of a Stipulation resolving all issues raised in this proceeding.[11] The Stipulating Participants advised that Consumer Counsel was not opposed to the Stipulation. The Committee did not join the Stipulation and continued to address issues related to the Purchased Water Surcharge ("PWS") and other issues including cost allocation and rate design.[12]

On September 27, 2022, the evidentiary hearing was held virtually, via Teams, as scheduled. Lonnie D. Nunley, III, Esquire, Timothy E. Biller, Esquire, James G. Ritter, Esquire, and Andrea D. Gardner, Esquire, of Hunton Andrews Kurth, LLP, appeared on behalf of VAWC. S. Perry Coburn, Esquire, and Dannieka N. McLean, Esquire, of Christian & Barton, L.L.P., appeared on behalf of the Committee. Karen S. Snow, Esquire, of the City of Alexandria Attorney's Office, and Justin W. Curtis, Esquire, of AquaLaw PLC, appeared on behalf of Alexandria. C. Meade Browder, Jr., Esquire, John E. Farmer, Jr., Esquire, and R. Scott Herbert, Esquire, appeared on behalf of Consumer Counsel. Kiva Bland Pierce, Esquire, Kelli Cole,

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Michael Cubbage, Tracy White, Lisa Marie Burnham, Arin Roney, Hamilton Martin, Julie Weisgerber, Steven Deitz, Douglas McDonld, Danny Murillo, Jeff Bernholz, Matthew Shaffer, Larcy McCarley, Anne Koster, Pamela Underhill, Jennifer Wylie, Sara Moorman, John Tiernery, Nancy McLernon, Raymie Walters, Norman Henderson, Sandra Yamamoto, Reagan Shaffer, Ellen Walker, Anna Henderson, Illriana Mushkolaj, Ted Moorman, Jean Schumann, Dannie Ferrell, James Corrie, Randy Gafner, and Chè Young.

[9] Claire Dorrell filed the public comment not opposed to the Application.

[10] Eli Nelson filed the public comment supporting the rate increase.

[11] Exhibit No. 2.

[12] Coburn, Tr. at 25-29.

Esquire, and Sean Barrick (Bar Admission Pending) appeared on behalf of Staff. One public witness presented testimony telephonically during the hearing.

On November 2, 2022, Staff, Alexandria, Consumer Counsel, VAWC, and the Committee filed post-hearing briefs.[13]

SUMMARY OF THE RECORD

In its Application, VAWC contended "[t]he primary driver of this case is ongoing investment in infrastructure."[14] The Company requested an annual increase in water revenues of $11,565,880, or an increase of 27.35 percent, and an annual increase in wastewater revenues of $2,751,397, or an increase of 28.71 percent for a total annual increase of $14,317,277, or a combined increase of 27.60 percent.[15] Consistent with § 56-235.11 of the Code and the Commission's *2018 Rate Order*,[16] VAWC is proposing the second of three steps to move all district-specific rates for water service to a consolidated statewide single tariff pricing ("STP").[17] In this case, the Company proposed consolidated tariff pricing ("CTP") as the second step toward STP.[18]

VAWC proposed a Revenue Stabilization Mechanism ("RSM"), or "an automatic rate adjustment clause [("ARAC")] that will work in a symmetrical manner to ensure that the Company receives, and customers pay, the revenue level found appropriate in this case; no more and no less."[19] The Company also proposed an Uncollectibles ARAC and a COVID-19 regulatory asset and amortization.[20] Finally, VAWC included certain adjustments related to its acquisition of the Waverly Water System.[21]

VAWC requested that its proposed rates become effective on May 1, 2022, on an interim basis, subject to refund.[22] The rate year in this case is the twelve months ended April 30, 2023 ("Rate Year").

[13] On November 3, 2022, the Committee filed a Motion to File Corrected Version of the Post-Hearing Brief of the Hopewell Committee for Fair Water Rates. The Committee's motion was granted in a Hearing Examiner's Ruling dated November 3, 2022.
[14] Exhibit No. 3, at 1.
[15] *Id.* at 2.
[16] *Application of Virginia-American Water Company, For a general increase in rates*, Case No. PUR-2018-00175, 2020 S.C.C. Ann. Rep. 236 ("*2018 Rate Order*").
[17] Exhibit No. 3, at 3-4.
[18] *Id.* at 4.
[19] *Id.* at 5.
[20] *Id.* at 6-7.
[21] *Id.* at 7-8.
[22] *Id.* at 9-10.

VAWC Direct Testimony

In support of its Application, VAWC filed the direct testimony of Barry L. Suits, president of VAWC; Casey Allen, vice president of operations for the Company; Kristina E. McGee, P.E., director of engineering for the Company; Scott T. Grace, senior manager of rates and regulatory for the Company; John S. Tomac, senior director of rates and regulatory for the Company; Harold Walker, III, consultant; James S. Pellock, principal regulatory analyst for the Company; Patrick L. Baryenbruch, consultant; Charles B. Rea, director of rates and regulatory for American Water Works Service Company ("AWWSC"); John M. Watkins, senior director of regulatory services for AWWSC; and Ann E. Bulkley, consultant. The prefiled testimony of each witness is summarized below.

Barry L. Suits introduced the other Company witnesses. He confirmed VAWC is seeking an overall increase in revenues of $14.3 million or 27.60 percent, which includes an increase in water service revenues of $11.6 million or 27.35 percent, and an increase in wastewater revenues of $2.7 million or 28.71 percent.[23] Mr. Suits also affirmed that the major driver of the Company's request is the over $137 million invested in facilities since its prior case to serve Virginia customers.[24] He indicated VAWC's rate base has increased approximately 48 percent since its prior rate case.[25]

Mr. Suits maintained VAWC's rates are affordable and the Company offers assistance programs for residential customers at or below 150 percent of the federal poverty level ("FPL").[26] He testified the Company offers: (i) a budget billing plan; (ii) flexible payment arrangements; and (iii) the Help to Others ("H2O") program, an emergency bill paying assistance program funded by VAWC and donations from customers.[27] In addition, Mr. Suits stated the Company has received $657,492 through the CARES Act and $597,737 through the American Rescue Plan Act ("ARPA") to help customers.[28]

Mr. Suits discussed VAWC's three ratemaking proposals and mechanisms: (i) the continued consolidation of the Company's tariff rates; (ii) the requested RSM; and (iii) an uncollectible expense ARAC.[29] He noted that this will be the second of three steps towards STP, and advised the overall requested rate increase will not have the same impact on each of the Company's Virginia districts.[30] Mr. Suits stressed the RSM proposal is symmetrical "as it simply reconciles the Company's actual revenue to the revenue authorized in the rate order."[31] In addition, he maintained these ratemaking proposals support efforts to improve water

[23] Exhibit No. 4, at 3-5.
[24] *Id.* at 5.
[25] *Id.* at 5-6.
[26] *Id.* at 9-10.
[27] *Id.* at 10-11.
[28] *Id.* at 11.
[29] *Id.* at 11-12.
[30] *Id.* at 12.
[31] *Id.* at 13.

efficiency through more effective maintenance and investment in the system.[32] Mr. Suits testified:

> Our goal is to continue to provide quality water and wastewater service as efficiently as possible, and by doing so, to increase the value of the service that we provide our customers.[33]

Mr. Suits contended: "[a] combination of a relatively low equity return, the imposition of the consolidated capital structure for ratemaking purposes, and an after-the-fact earnings test that, among other things, readjusts for changes to the consolidated capital structure every year, provides a disincentive to direct proactive capital investment to [VAWC] operations."[34] He warned that a return on equity ("ROE") that is significantly below that of other American Water Works Company ("AWK") subsidiaries, and other utilities "will adversely impact the Company's ability to secure proactive investment."[35]

Mr. Suits described VAWC's community outreach activities and provided the following examples:[36]

- The James River Association ("JRA") received funding from VAWC to partner with the Hopewell City Public Schools to provide 7th grade students with an experiential day of learning within their local watershed.

- The American Water Charitable Foundation also made a contribution to JRA to further its engagement with students in Hopewell City Public School System to understand their roles to ensure a healthier, brighter, and safer future.

- Friends of the Lower Appomattox River [("FOLAR")] received funding to engage and expand environmental opportunities for youth of the tri-cities communities. Firefighter grants were given to support community fire protection. Grants were given to 5 volunteer fire departments in 2021.

- AWK provides matching funds for two workplace-giving programs, supporting the United Way and Water for People. Each year, employees participate in these campaigns in which the American Water Charitable Foundation matches volunteer hours and gifts up to $1,000 per year.

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[32] *Id.* at 15.
[33] *Id.* at 16.
[34] *Id.* at 16-17.
[35] *Id.* at 17.
[36] *Id.* at 19-21.

- Assisted in developing water/wastewater curriculum for Alexandria City Public Schools students with the City of Alexandria and Alexandria Renew ("AlexRenew")[.]

- Participated in an annual Water Discovery Week[.]

- Sponsored an "Imagine a Day Without Water" outreach effort in Old Town Alexandria.

- Celebrated Drinking Water and Wastewater Professionals Appreciation Day.

- Sponsored and provided water for City Point 5K in Hopewell, the [FOLAR] Kayak Race and the United Way (Hopewell/Prince George) Golf Tournament.

- Supported Hopewell [Veterans of Foreign War's ("VFW's")] "Back the Blue" event and Hopewell Arts Festival and served as "water sponsor" for the Hopewell Downtown Partnership, including the 3rd Thursday outdoor farmers market and "Harvest-ween" celebration.

Mr. Suits listed several environmental and community activities undertaken by VAWC's employees.[37] He noted VAWC is an active member of Alexandria and Prince George/Hopewell Chambers of Commerce, FOLAR and the United Way.[38]

Casey Allen presented an overview of VAWC's operations and facilities.[39] Mr. Allen advised that the Company serves approximately 60,600 water service customers and approximately 20,600 wastewater customers in 22 distinct public water and wastewater systems in ten counties organized into five operating districts:

- **Alexandria District** – serves the City of Alexandria and parts of Fairfax County and Arlington County,

- **Hopewell District** – serves the City of Hopewell and parts of Prince George County,

- **Prince William Water District** – serves the Dale City community in Prince William County,

[37] *Id.* at 22-23.
[38] *Id.* at 23.
[39] Exhibit No. 5, at 2-3.

- **Prince William Wastewater District** – serves the Dale City community in Prince William County, and

- **Eastern District** – serves 18 subdivisions through 18 distinct public water systems in Westmoreland County, Northumberland County, Lancaster County, Essex County, and King William County.[40]

In addition, Mr. Allen noted VAWC is adding, if approved by the Commission, approximately 905 customers to the Hopewell district through the purchase of assets from the Town of Waverly.[41]

Mr. Allen described the operations of each district as follows:

- **Alexandria District** – serves approximately 27,600 jurisdictional customers in the City of Alexandria through a system that was started in 1850 and by purchasing water from the Fairfax County Water Authority ("Fairfax Water") by which VAWC has 28.3 million gallons of water capacity per day ("MGD").[42] He confirmed that Alexandria district is classified as a "Consecutive System" by the Virginia Department of Health ("VDH") and conducts routine testing at its Alexandria Operations Center, with more complex tests performed by AWWSC's Central Laboratory ("Central Lab") in Belleville, Illinois.[43]

- **Hopewell District** – serves approximately 9,600 jurisdictional customers, and treats and delivers approximately 21.3 MGD of both potable and non-potable water sourced from the Appomattox River.[44] He described the two water treatment trains in the Hopewell treatment plant, one for potable water and one for non-potable water used by certain industrial customers, as well as the separate potable and non-potable distribution systems.[45]

- **Prince William Water District** – serves nearly 20,600 jurisdictional customers, purchases its water from Fairfax Water with a capacity of 9.6 MGD, and is classified as a "Consecutive System" by VDH.[46] Mr. Allen stated routine testing

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[40] *Id.* at 2.
[41] *Id.* at 2-3. Granted on April 15, 2022. *Petition of Virginia American Water Company, For authority to acquire utility assets at fair market value pursuant to the Utility Transfer Act, Va. Code § 56-88 et seq. and 20 VAC 5-210-10 et seq. and for a certificate of public convenience and necessity pursuant to the Utility Facilities Act, Va. Code § 56-265.3*, Case No. PUR-2021-00090, Final Order (April 15, 2022), Clarifying and Correcting Order (May 10, 2022).
[42] Exhibit No. 5, at 3.
[43] *Id.*
[44] *Id.* at 4.
[45] *Id.* at 5-6.
[46] *Id.* at 6.

is performed at the Alexandria Operations Center and more complex tests are performed by the AWWSC Central Lab.[47]

- **Prince William Wastewater District** – with a few exceptions, serves generally the same customers in the Dale City community and employs two 4.6 MGD sequencing batch reactor wastewater treatment plants.[48]

- **Eastern District** – serves approximately 2,800 residential customers spread out over 18 separate and unique systems.[49] Mr. Allen affirmed routine testing is performed at VAWC's Hopewell laboratory and more complex tests are performed by the AWWSC Central Lab.[50]

Mr. Allen testified that the Company's success in providing its customers with high quality and efficient water service can be measured by: (i) VAWC's record of safety and water quality "report cards" from governmental agencies and awards from governmental agencies and peer groups; (ii) expense trends over time; and (iii) measures of affordability.[51] He highlighted operation and maintenance ("O&M") expenses over the most recent decade, which was $324 per customer in 2011, and $328 per customer for the Rate Year.[52]

Mr. Allen outlined VAWC's water efficiency efforts and maintained such efforts reduce capital and operating costs, and help to protect and preserve natural resources.[53] He contended VAWC gains efficiencies through AWWSC's expertise and purchasing power.[54] Mr. Allen pointed to the Company's efforts to accurately map its water and wastewater system and implementation of MapCall, "an application that provides a more intuitive – and thus more efficient – spatial interface among the Company's enterprise software, [geographic information system ("GIS")] and its employees in the field."[55]

Mr. Allen testified VAWC's appropriate staffing level is 122 full-time employees.[56] He reported that as of June 30, 2021, the Company had 114 full-time employees, has since hired 3 additional employees, and anticipates 5 employees will be hired prior to the Rate Year.[57]

Mr. Allen asserted "[t]he Company considers safety to be both a core value and a business strategy."[58] He described the Company's Near Miss Reporting Program, implemented

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[47] *Id.* at 6-7.
[48] *Id.* at 7.
[49] *Id.* at 9.
[50] *Id.* at 10.
[51] *Id.*
[52] *Id.* at 11.
[53] *Id.* at 12-13.
[54] *Id.* at 14.
[55] *Id.* at 17.
[56] *Id.* at 21.
[57] *Id.*
[58] *Id.* at 22.

in 2020,[59] for "an event or condition that did not result in injury, illness, or damage, but had the potential to do so."[60] Mr. Allen affirmed that "[a]ll [of the Company's] employees participate in some form of safety training."[61]

Mr. Allen acknowledged that "[w]ater quality is of paramount importance to the health and well-being of our customers."[62] He listed improvements and investments directed towards water quality as follows:

- The addition of an ultraviolet ("UV") disinfection system in Hopewell that among other things destroys taste and odor compounds;[63]

- Investments to improve the flocculation/settling process at the Hopewell treatment plant;[64]

- Automations and controls ("SCADA") to monitor critical steps in the water treatment process;[65]

- Sample 1 View, which is a customized water sample collection application that provides a real time geospatial overview of sampling assignments, collection activity, analysis, and reporting;[66]

- Upgraded several domestic turbidimeters, pH analyzers, and chlorine (CL17) analyzers;[67] and

- Advanced metering tools for real-time alerts for backflow events.[68]

Mr. Allen reported that in 2019, 2020, and 2021 year-to-date, VAWC had no environmental violations, and "only two sanitary sewer overflows . . . which represents great service."[69]

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[59] *Id.* at 31.
[60] *Id.* at 25.
[61] *Id.* at 27.
[62] *Id.* at 31.
[63] *Id.* at 32-33.
[64] *Id.* at 33.
[65] *Id.*
[66] *Id.* at 33-34.
[67] *Id.* at 34.
[68] *Id.*
[69] *Id.* at 34-35.

Kristina E. McGee, P.E., addressed VAWC's investments in water and wastewater utility plant and equipment for the period of May 1, 2020, through April 30, 2023.[70] Ms. McGee affirmed: "[t]he Company uses a standardized Capital Program Management ("CPM") process to manage all of its capital investments."[71] She stated VAWC uses a fifteen-year planning horizon, as well as separate studies for projects that emerge between updates of the Company's comprehensive planning studies. Projects are prioritized based on "safety, regulatory compliance, capacity and growth, infrastructure renewal, efficiency, resiliency, reliability, and quality of service."[72]

Ms. McGee described the Company's GIS based prioritization model for identifying and prioritizing pipeline replacement investments across its approximately 750 miles of water piping and 200 miles of collection piping.[73]

Ms. McGee testified VAWC controls capital expenditure costs by maintaining a list of qualified bidders and through materials and supplies purchased through AWWSC.[74] She affirmed that "[i]n general, the overall investment in plant through the [R]ate [Y]ear will remain stable."[75]

Ms. McGee affirmed VAWC plans to invest $137.6 million of gross plant additions through April 2023 in water and wastewater facilities since its prior rate case.[76] She advised that net of retirements, the net plant additions are estimated to be $109.6 million.[77] Ms. McGee maintained approximately $60.4 million of the $137.6 million of investment will be in routine, recurring projects ("RPs"), which includes: (i) approximately $31.5 million for water and wastewater infrastructure replacement for pipes (*i.e.*, mains, services and valves) near the end of their useful lives; (ii) approximately $14.1 million for process plant facilities and equipment (*i.e.*, replacement of filter media, chemical feed system improvements, and drilling replacement production and observation wells); and (iii) approximately $3.2 million for SCADA and security systems.[78]

Ms. McGee stated: "[t]he remaining $77.2 million of the $137.6 million in investment pertains to [large discrete projects ("IPs")] investments that support the adequacy and resiliency of the water and wastewater treatment facilities, and also includes investments that further enhance the Company's hardware, software, and related technology appurtenances and systems."[79] She highlighted the following projects:

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[70] Exhibit No. 6, at 2.
[71] *Id.*
[72] *Id.* at 3-4.
[73] *Id.* at 4.
[74] *Id.* at 6.
[75] *Id.* at 8.
[76] *Id.*
[77] *Id.*
[78] *Id.* at 9-10.
[79] *Id.* at 10-11.

- **Prince William District Operations Center** **$3,030,984**
  Construct a 17,000 square foot operations center providing office space, training facilities, and warehousing spaces placed into service in December 2020.[80]

- **Edsall Road Water Main Replacement** **$1,151,808**
  Replace 3,800 feet of existing 12-inch cast iron and asbestos water main in the City of Alexandria with 16-inch class 54 ductile iron pipe with zinc coating and v-bio poly wrap placed into service in December 2020.[81]

- **Prince William Wastewater Stair & Platform Replacement** **$246,507**
  Replace the stairs on three tanks and the stairs and platforms on ten tanks and placed in service in March 2021.[82]

- **Westmoreland Shores Well 3B** **$1,511,606**
  Construct a new pump station to increase the system's storage and well capacity to meet VDH requirements placed in service in August 2021.[83]

- **Hopewell Industrial Pump Station** **$28,224,087**
  Replace station built almost 100 years ago, with the project placed in service in September 2021.[84]

- **Hopewell Water Treatment Plant ("WTP") Domestic Flocculator Replacements** **$474,489**
  Replace vertical mixers and motors, power panels, wiring, and variable frequency drives in the Jewel flocculation basins to agglomerate particles to help them settle during the sedimentation process and to continue to meet water quality regulations.[85] Ms. McGee expected the project to be in service by December 2021.[86]

- **Hopewell WTP Industrial Flocculator Replacements** **$542,018**
  Similar to the previous project, but for the industrial treatment, to allow finished water turbidity levels to be consistently met.[87] Ms. McGee expected the project to be in service by December 2021.[88]

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[80] *Id.* at 11.
[81] *Id.* at 12.
[82] *Id.* at 13.
[83] *Id.*
[84] *Id.* at 14-16.
[85] *Id.* at 16-17.
[86] *Id.* at 17.
[87] *Id.*
[88] *Id.*

- **Hopewell Low Service Generator Replacement** **$1,095,000**
  Replace the existing generator and transformer located at the Hopewell low service intake station to increase reliability and resiliency.[89] Ms. McGee expected the project to be in service by December 2021.[90]

- **Domestic Filtering Overflow Piping** **$660,000**
  Install new domestic filter overflow piping at Hopewell WTP to meet current engineering practice.[91] Ms. McGee expected the project to be in service by December 2021.[92]

- **Ebb Tide Beach Well No. 8 Storage Tank and Booster Pumps** **$430,000**
  Required to meet VDH requirements and to meet anticipated growth.[93] Ms. McGee expected the project to be in service by December 2021.[94]

- **PW Wastewater Section 8 Sequencing Batch Reactors ("SBR") Tank Decanters Replacement** **$780,092**
  Replace components of the existing decanter system to reduce solids carryover to the surge pond.[95] Ms. McGee expected the project to be in service by December 2021.[96]

- **Polymer (Filter Aid) System Improvements** **$464,492**
  Replace three aging polymer systems at the Hopewell WTP due to deteriorations caused by corrosion from chlorine fumes.[97] Ms. McGee expected the project to be in service by April 2022.[98]

- **Low Service Pump Station Improvements** **$904,000**
  Reinforce walls and floors as well as improve ventilation in the Hopewell low service pump station building, which was placed into service in 1915.[99] Ms. McGee expected this project to be in service by April 2022.[100]

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[89] *Id.* at 17-18.
[90] *Id.* at 18.
[91] *Id.*
[92] *Id.*
[93] *Id.* at 18-19.
[94] *Id.* at 19.
[95] *Id.*
[96] *Id.*
[97] *Id.* at 20.
[98] *Id.*
[99] *Id.*
[100] *Id.*

- **South Hill Banks Pressure Tank Replacement** **$860,000**
  Provide a new pump station and tank at an existing well site that is currently out of service to comply with VDH requirements and increase system resiliency.[101] Ms. McGee expected this project to be in service by June 2022.[102]

- **SCADA Master Plan** **$2,392,795**
  Replace obsolete platforms across VAWC's system to provide enterprise-wide monitoring and control access.[103] Ms. McGee expected this project to be in service by December 2022.[104]

- **Hopewell WTP Generator Replacement** **$900,000**
  Replace generator at Hopewell WTP due to its age, condition and automation limitations.[105] Ms. McGee expected this project to be in service by December 2022.[106]

- **PW Wastewater Crescent Street Sewer Main Upgrades** **$2,174,329**
  Stop sewage back-ups into basements, the Company installed a parallel sewer main approximately 4,500 feet in length and a pump station.[107] Ms. McGee expected this project to be in service by December 2022.[108]

- **Chemical Clarifier 1 Section 1 Replacement** **$2,681,977**
  Replace one of two chemical clarifiers at the Section 1 wastewater treatment plant ("WWTP") to improve treatment reliability and reduce the risk of future failures.[109] Ms. McGee expected this project to be in service by December 2022.[110]

- **Convert Pre-Caustic to Liquid Lime** **$500,000**
  Convert the pre-caustic feed system at the Hopewell WTP to liquid lime, which is safer to handle and work around.[111] Ms. McGee expected this project to be in service by December 2022.[112]

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[101] *Id.* at 20-21.
[102] *Id.* at 21.
[103] *Id.*
[104] *Id.*
[105] *Id.*
[106] *Id.*
[107] *Id.*
[108] *Id.*
[109] *Id.* at 22.
[110] *Id.*
[111] *Id.*
[112] *Id.*

- **Hopewell WTP Domestic Sedimentation Basin Project** **$5,510,730**
  Build a new domestic clarifier to provide redundancy that will allow for timely maintenance of the basins.[113] Ms. McGee expected this project to be in service by December 2023.[114]

- **Hopewell Elevated Storage Tank** **$4,950,000**
  Construct an elevated storage tank with a total capacity of 2.5 million gallons ("MG"), which is needed for VDH regulatory compliance.[115] Ms. McGee expected this project to be in service by December 2023.[116]

- **Chemical Clarifier 2 Section 1 Replacement** **$1,066,667**
  Replace one of two chemical clarifiers at the Section 1 WWTP to improve treatment reliability and reduce the risk of future failures.[117] Ms. McGee expected this project to be in service by December 2023.[118]

- **Hopewell Low Service Intake Replacement** **$12,666,667**
  Design and construct a new intake and pumping structure on the existing low service pump station property.[119] Ms. McGee stated it will be bid in December 2021 and is expected to be in service by June 2024.[120]

- **Enterprise Solutions** **$4,014,418**
  Implement various enterprise solutions ("ES") projects from May 1, 2020, through April 30, 2023, designed to improve efficiencies through technology while maintaining system safety and better serving customers.[121]

Scott T. Grace sponsored schedules supporting VAWC's revenue requirements and discussed the following:[122]

- Overview of the Filing
- Overview of Schedules Filed
- Revenue Adjustments
  - Elimination of Unbilled Revenue
  - Elimination of [PWS] Revenue
  - Elimination of WWISC Rider True-Up Revenue

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[113] *Id.*
[114] *Id.*
[115] *Id.* at 23.
[116] *Id.*
[117] *Id.*
[118] *Id.*
[119] *Id.*
[120] *Id.* at 23-24.
[121] *Id.* at 24.
[122] Exhibit No. 7, at 2-3.

- Removal of [Tax Cut and Jobs Act of 2017 ("TCJA")] Catch-Up Period [Excess Accumulated Deferred Income Tax ("EDIT")] Sur-Credit Revenue
    - Removal of Adjustments for Interim Rates Outside of the Test Year
- [O&M] Expense
    - Purchased Water Adjustment
    - Regulatory Expense Adjustment
    - Labor and Labor Related Adjustments
    - Support Service Expense Adjustments
- Tariff Revisions

Mr. Grace maintained the VAWC filing supports an increase in annual revenue requirements of $14,317,277, or 27.60 percent over present pro forma revenues, including an annual water service rate increase of $11,565,880 or 27.35 percent and a wastewater service rate increase of $2,751,397 or 28.71 percent.[123] He defined the test year as the twelve months ended June 30, 2021 ("Test Year") and adjusted the Test Year through the Rate Year.[124] Mr. Grace referred to § 56-235.2 of the Code and contended the Company's rate year adjustments to O&M reflect adjustments that "can be reasonably predicted to occur."[125]

Mr. Grace eliminated accrued or "unbilled" revenues "because the bill analysis utilized by the Company in designing rates includes a full year's worth of billing."[126] He removed PWS revenue associated with purchased water for Alexandria and Prince William water districts as the cost of purchased water is recovered through a revenue surcharge and not through base rates.[127] He eliminated WWISC Rider true-up revenues of $396,905, which are not part of base rates.[128] Mr. Grace added back $327,672 for the TCJA catch-up period EDIT sur-credits passed back to customers from January 1, 2021, through June 30, 2021, of the Test Year.[129] He also added back $988,662 of prior period revenue adjustments related to interim rates in VAWC's prior rate proceeding.[130]

Mr. Grace testified VAWC is seeking O&M expense, net of purchased water expense, of $26,934,309 for the Rate Year.[131] He emphasized the annual O&M expense on a per jurisdictional customer basis has increased by only $4.00 during the eleven-year period of 2011 to the Rate Year.[132]

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[123] *Id.* at 3.
[124] *Id.* at 3-4.
[125] *Id.* at 6.
[126] *Id.* at 11.
[127] *Id.*
[128] *Id.* at 12.
[129] *Id.*
[130] *Id.* at 13.
[131] *Id.*
[132] *Id.* at 14.

Regarding the O&M expense adjustments addressed by Mr. Grace, he confirmed VAWC eliminated purchased water expense of $13,668,188 for the Test Year to reflect purchased water expense recovered in a separate surcharge.[133] Mr. Grace also noted the PWS is impacted by the second phase of rate consolidation.[134] Mr. Grace estimated the cost to file and adjudicate this rate case to be $907,000.[135] He stated that "[c]onsistent with the prior rate case, the Company normalizes regulatory expense over five years[,]" which results in a Test Year adjustment of $27,356.[136]

Mr. Grace addressed the following labor and labor related costs:[137]

1) Salaries and Wages
2) Group Insurance
3) Other Benefits, including:
    a. 401k
    b. Defined Contribution Plan ("DCP")
    c. Employee Stock Purchase Plan ("ESPP")
4) Annual Performance Plan
5) Payroll Taxes
6) Pension and [Other Post-Employment Benefits ("OPEB")]

Mr. Grace confirmed the Rate Year level of labor and labor related costs reflect 122 full-time positions, which is an increase of two from the Company's prior case.[138] He noted there were 114 employees at the end of the Test Year.[139] Mr. Grace stated the capitalization percentage is based on a three-year average (*i.e.*, average of the twelve months ended June of 2019, 2020, and 2021) of dollars charged to capital versus O&M.[140] He projected Rate Year wages based on collective bargaining agreements and actual rates effective as of March 8, 2021, adjusted through the Rate Year based on the three-year average percentage increase.[141] Mr. Grace based overtime pay and meals for union employees on three-year averages.[142] He advised that performance pay was adjusted to reflect each position's target percent for the Annual Performance Plan.[143] Mr. Grace testified that overall, VAWC adjusted Test Year salaries and wages expense by $940,090.[144]

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[133] *Id.* at 15.
[134] *Id.* at 16.
[135] *Id.*
[136] *Id.* at 17.
[137] *Id.*
[138] *Id.* at 18.
[139] *Id.*
[140] *Id.* at 19.
[141] *Id.* at 19-20.
[142] *Id.* at 20.
[143] *Id.*
[144] *Id.*

Mr. Grace calculated the pro forma adjustment for basic life, short-term disability, long-term disability, and accidental death and disability ("AD&D") insurance by applying the plan rates for 2022 for each employee position projected for the Rate Year.[145] Similarly, he calculated the pro forma adjustment for medical, dental and vision insurance using the 2022 plan rates, costs and contributions applied on a position-by-position basis for projected Rate Year employees.[146]

Mr. Grace described the other benefits expense to include 401k, DCP, retiree medical expense, and ESPP.[147] He calculated the pro forma 401k costs for each position based on the Rate Year wages, current employee contribution levels, and the level of match for each employee.[148] Mr. Grace determined the pro forma DCP by multiplying the Rate Year regular time pay for each eligible position by 5.25 percent.[149] He advised that the retiree medical expense is for union employees who are not eligible for OPEB and is in the amount of $600 per eligible employee.[150] For ESPP, he calculated the pro forma amount by multiplying participating employees' Rate Year wage, times each employees' individual contribution amount, applied to the 15 percent Company discount for AWK stock purchases.[151]

For pension and OPEB expenses, Mr. Grace relied upon a third-party actuary, Willis Towers Watson ("WTW"), to forecast for AWK for both service and non-service components to calculate a jurisdictional Rate Year pension expense adjustment of ($6,513) and a jurisdictional Rate Year OPEB expense adjustment of $63,998.[152] He noted the Company will update these adjustments when actuarial forecasts are provided for 2022.[153]

Mr. Grace outlined the services provided to VAWC by AWWSC to include "customer service, water quality testing, environmental compliance, human resources, communications, information technology, finance, accounting, legal, engineering, supply chain, and risk management."[154] He stated VAWC is seeking to recover $6,941,371 in jurisdictional expenses for the Rate Year.[155] Mr. Grace advised that in this case, postage and customer accounting expenses and software licensing and maintenance fees are now included in the AWWSC service expenses instead of directly on VAWC's books.[156] He noted adjustments were made to these items to reflect updated postage rates and the addition of Waverly.[157]

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145 *Id.* at 22.
146 *Id.*
147 *Id.*
148 *Id.* at 23.
149 *Id.*
150 *Id.*
151 *Id.* at 23-24.
152 *Id.* at 25-26.
153 *Id.* at 27.
154 *Id.*
155 *Id.* at 29.
156 *Id.* at 30-31.
157 *Id.* at 31.

Mr. Grace testified that the Company is revising Tariff Sheets Nos. 1, 3, 4, 4A, 5, 5A, and 5.1 to reflect the proposed rates effective May 1, 2022.[158] He confirmed that the Company proposed to further consolidate purchased water costs by allocating two-thirds of the purchased water costs to all districts and one-third to the customers of Prince William and Alexandria.[159]

John S. Tomac addressed: (i) computation of rate base; (ii) capital structure and earnings test; (iii) interest synchronization; (iv) TCJA update; (v) COVID-19 regulatory asset; and (vi) Uncollectibles ARAC.[160]

Mr. Tomac noted VAWC's proposed rate base in this proceeding of $286,915,082 is $92,749,605 or approximately 48 percent higher than VAWC's rate base in its prior proceeding.[161] He confirmed the Company's proposed rate base is a thirteen-month average, following a methodology that is consistent with the one which the Company used for forecasted plant investment in its prior two rate cases.[162] Mr. Tomac pointed out that VAWC is providing a complete lead-lag study and balance sheet analysis for calculating cash working capital ("CWC").[163] He explained the Company's working capital request includes the materials and supplies unadjusted balance as of June 30, 2021, because the Company does not anticipate a material change to these balances in the Rate Year.[164]

Mr. Tomac sponsored VAWC's proposed standalone capital structure:[165]

Type of Capital	Ratio	Cost Rate	Weighted Cost Rate
Short-Term Debt	3.27%	0.34%	0.01%
Long-Term Debt	55.66%	4.09%	2.27%
Preferred Stock	0.00%	0.00%	0.00%
Stockholder Equity	40.75%	10.90%	4.44%
Job Development Credits	0.32%	6.97%	0.02%
Total	100.00%		6.75%

Mr. Tomac advised that short-term debt is the thirteen-month average of projected monthly all-in commercial paper rates for the Rate Year.[166]

Mr. Tomac maintained use of a stand-alone capital structure reflects the capital structure used to finance VAWC's rate base.[167] He argued, VAWC's "capital structure and rate of return

[158] *Id.* at 31-32.
[159] *Id.* at 32.
[160] Exhibit No. 13, at 1-2.
[161] *Id.* at 2.
[162] *Id.* at 4.
[163] *Id.*
[164] *Id.* at 4-5.
[165] *Id.* at 6; Exhibit No. 3, Schedule 8.
[166] Exhibit No. 13, at 7.
[167] *Id.*

should be based on the capital devoted to serve the public in Virginia."[168] Mr. Tomac acknowledged that since 2010, the Commission has used a consolidated capital structure to set VAWC's rates.[169] He contended Staff and the Commission's reasons for using a consolidated capital structure are invalid and risk further investment in Virginia:[170]

> A lower ROE combined with a consolidated capital structure subject to an after-the-fact earnings test limits proactive capital investment in Virginia as well as discourages further expansion and the acquisition of water and wastewater systems facing challenges associated with the increased need for the replacement of aging infrastructure replacement and meeting evolving regulatory standard. Capital flows to where it is treated most favorably. Less capital deployed to Virginia will mean the loss of jobs while shifting those jobs to other states in which [AWK] operates. Regulatory policy which dampens proactive capital investments is not in the best interest of the customers over the long term.[171]

Mr. Tomac referred to the earnings tests for the annual informational filing ("AIF") and Water and Wastewater Infrastructure Surcharge ("WWISC") as "annual equity ratio adjustments" and asserted "[a]nnual adjustments to the capital structure violate the underlying tenets of *Hope*[172] and *Bluefield*;[173] result in a disconnect between the operations of VAWC and its financing structure and limits the availability of proactive capital investment for VAWC."[174]

Mr. Tomac calculated the amortization of EDIT using the Average Rate Assumption Method ("ARAM") for protected assets and eight years for unprotected assets, which amounted to $704,095 on a jurisdictional basis.[175]

Mr. Tomac testified that based on the Commission's *COVID Regulatory Asset Order*,[176] VAWC deferred COVID-related uncollectible expense, incremental O&M expense, lost revenues associated with suspending late fees, costs related to financing activity to ensure adequate liquidity, and savings from travel and conferences that did not occur with a net

[168] *Id.*
[169] *Id.* at 8.
[170] *Id.* at 8-17.
[171] *Id.* at 15-16.
[172] *Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) ("*Hope*").
[173] *Bluefield Waterworks & Improvement Co. v. Pub. Serv. Comm'n*, 262 U.S. 679 (1923) ("*Bluefield*").
[174] Exhibit No. 13, at 17.
[175] *Id.* at 20.
[176] *Commonwealth of Virginia, ex rel. State Corporation Commission, Ex Parte: Authority to create regulatory asset*, Case No. PUR-2020-00074, 2020 S.C.C. Ann. Rep. 498 ("*COVID Regulatory Asset Order*").

financial impact of $1,001,873 through September 30, 2021.[177] He calculated the COVID-related uncollectible expense as the difference between the actual level of bad debt expense for each month beginning March 2020, compared to the amount of uncollectible expense embedded in VAWC's existing rates.[178] Mr. Tomac confirmed VAWC received $657,492 under the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act"), which helped to reduce the incremental uncollectible expense deferred.[179] He described the incremental O&M expenses as "facility preparedness, personal protective equipment, sanitizers, signage, rental equipment, enhanced cleaning in areas where positive COVID-19 cases have been confirmed, etc."[180]

Regarding the financing activity to ensure adequate liquidity included in COVID-related deferrals, Mr. Tomac testified $154,132 of interest expense was allocated to the Company from American Water Capital Corp. ("AWCC") associated with a $750,000,000, 364-day term loan credit facility ("Term Loan") used to ensure liquidity for its regulated operating utilities.[181] He maintained "[t]he interest expense on the Term Loan is analogous to insurance premiums (or to an availability fee), which are paid to mitigate risk and are reasonable whether or not a claim is ever made."[182]

Mr. Tomac stated the Company proposes to recover the total COVID-related deferred costs through September 30, 2021, of $1,001,873 over a three-year period, with costs deferred after September 30, 2021, which will not include uncollectible expense, recovered in the next rate case.[183] He proposed a separate ARAC for uncollectible expense.[184] More specifically, Mr. Tomac proposed a pro forma uncollectible expense based on the average of 2017, through 2019, and an ARAC to reconcile actual incurred uncollectible expense with the base level established in this rate case.[185]

Harold Walker, III, addressed the Company's working capital allowances and conducted a separate lead-lag study for each of VAWC's four water districts and Prince William Wastewater.[186] Mr. Walker pointed out that VAWC's working capital is comprised of cash (*i.e.*, lead/lag), materials and supplies, and prepayments.[187] He advised that the focus of his testimony is the cash component.[188]

Mr. Walker's results are shown in the table below.[189]

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[177] Exhibit No. 13, at 21.
[178] *Id.* at 22-23.
[179] *Id.* at 23.
[180] *Id.*
[181] *Id.* at 24-25.
[182] *Id.* at 26.
[183] *Id.* at 26-27.
[184] *Id.* at 27.
[185] *Id.*
[186] Exhibit No. 9, at 1.
[187] *Id.* at 2.
[188] *Id.* at 2-3.
[189] *Id.* at 3-5.

	Alexandria District	Hopewell District	Prince William District	Eastern District	Prince William Wastewater
Earnings Test					
Cash	$279,153	$118,464	$459,798	$71,069	$329,668
Balance Sheet	-$2,738,825	-$842,337	-$1,919,421	-$91,196	$979,978
Total	-$2,459,672	-$723,873	-$1,459,623	-$20,127	$1,309,646
Adjusted					
Cash	$360,656	$152,288	$530,741	$69,565	$404,369
Balance Sheet	-$2,738,825	-$842,337	-$1,919,421	-$91,196	$979,978
Total	-$2,378,169	-$690,049	$1,388,680	-$21,631	$1,384,347

Mr. Walker stated the purpose of a lead-lag study is to measure "the level of funding required to operate on a day-to-day basis in providing for the cost of service."[190] He maintained it is determined:

> by calculating the net lag between the amount of time elapsed between when a company provides a service to its customers and when the company receives payments from its customers, and the amount of time elapsed between when a company receives goods and services and when the company pays its suppliers for those goods and services.[191]

Mr. Walker confirmed he used the Test Year to determine the net lag (lead) days.[192]

Mr. Walker stated the revenue lag includes the service period lag, billing lag, and collection lag.[193] He focused on the Alexandria district and reported a service period lag of 12.1 days, billing lag of 3.2 days, and a collection lag of 17.7 days for a revenue lag of 33.0 days.[194] Mr. Walker explained that the lead days for cost of service expenses are comprised of the following four major sub-accounts and other items: (i) operating expenses; (ii) depreciation and amortization expense; (iii) income taxes; and (iv) taxes other than income.[195] He affirmed for operating expense sub-account items "the lead days were determined for each invoice or account sampled based on the midpoints of the service periods to the dates the Company paid the invoices or accounts."[196] Mr. Walker assigned zero to the lead days for depreciation and amortization.[197] He calculated the lead days for current federal income taxes based on the

[190] *Id.* at 5.
[191] *Id.* at 5-6.
[192] *Id.* at 7.
[193] *Id.* at 11.
[194] *Id.* at 12.
[195] *Id.* at 12-13.
[196] *Id.* at 13.
[197] *Id.* at 14.

midpoint of the tax period to the payment date, weighted by the percent of the payment required to be 36.8 lead days.[198] Mr. Walker assigned zero lead to deferred income taxes.[199]

For the lead days for the consumer utility tax, Mr. Walker used the statutory payment dates, but noted payments to the cities of Alexandria and Hopewell are remitted prior to the statutory payment dates.[200]

James S. Pellock supported Test Year and Rate Year adjusted "production expenses, insurance other than group [("IOTG")] expense, tank painting expense, uncollectible expense, charitable contributions, employee related (travel) expense, other miscellaneous expense adjustments, and general (non-income) taxes."[201] Mr. Pellock outlined his Rate Year adjustments as follows:

> Production expenses were calculated based on projected water sales and applicable rates or pricing . . . . Revenue taxes were calculated based on adjusted operating revenue taxed at rates currently set by the various government taxing authorities. In order to obtain representative levels of expenses that vary, I employed a three-year average for pro forma expense purposes. I also used this method for employee related (travel) expense and uncollectible expense. Finally, I applied an inflation factor to the total amount of present rate pro forma expenses that were not otherwise adjusted (e.g., contract services, miscellaneous expense) to bring those expenses to levels that will exist in the rate year.[202]

Mr. Pellock discussed the following adjustments:

Purchased Water Expense – Eliminated jurisdictional purchased water expense of $13,668,188 to reflect purchased water expense is recovered through a surcharge.[203]

Chemicals – Increased Test Year amount by $295,946 to reflect estimated chemical contract pricing for 2022 and to reflect changes in chemical use.[204]

Fuel and Power – Increased Test Year amount by $32,229 to reflect changes in vendor pricing, customer growth, and declining use per customer.[205]

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[198] *Id.* at 15.
[199] *Id.*
[200] *Id.* at 16-17.
[201] Exhibit No. 10, at 2-3.
[202] *Id.* at 3.
[203] *Id.* at 4.
[204] *Id.* at 5.
[205] *Id.* at 6.

Waste Disposal – Reduced Test Year amount by $33,321 based on current rates and system delivery statistics.[206]

IOTG – Increased Test Year amount by $178,954 to reflect premiums adjusted for anticipated increases for 2022.[207]

Tank Painting Costs – Reduced Test Year amount by $6,799 based on five years of actual and projected annual tank painting costs through the Rate Year.[208]

Revenue Based Taxes – Reduced Test Year amount by $358,658 based on adjusted jurisdictional operating revenues, net of uncollectible expense, multiplied by tax rates.[209]

Property Taxes – Increased Test Year amount by $272,101 to reflect the effective property tax rate for each district applied to the projected taxable plant in service and construction work in progress ("CWIP") for the Rate Year.[210]

Uncollectible Expense – Reduced Test Year amount by $75,627 based on a forecasted uncollectible percentage of revenue derived from the three twelve-month periods ended December 31, 2017, December 31, 2018, and December 31, 2019.[211]

Contributions, Donations, and Community Relations Expense – Reduced Test Year amount by $1,145 to reflect 50 percent of Test Year amount consistent with prior rate cases and the elimination of promotional expenses occurring during the Test Year.[212]

Employee Related Expenses – Reduced Test Year amount by $66,489 a three-year average of employee travel, conference, meals, and relocations for the twelve-month periods ended December 31, 2017, December 31, 2018, and December 31, 2019.[213]

Other O&M Expense – Reversed one-time Test Year expenses for an AIF reserve of $767,999 and for regulatory expense above capped amount of $188,491.[214]

Unadjusted O&M Expense – For O&M not otherwise adjusted, such as for maintenance supplies, contracted services, building maintenance, telecommunications, office supplies, and miscellaneous expenses, an inflation factor based on the Federal Reserve's average Gross

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[206] *Id.* at 6-7.
[207] *Id.* at 8.
[208] *Id.* at 9.
[209] *Id.* at 10.
[210] *Id.* at 10-11.
[211] *Id.* at 11.
[212] *Id.* at 12.
[213] *Id.*
[214] *Id.* at 13.

Domestic Product Price Index forecast was applied to increase Test Year O&M expenses by $242,311.[215]

Mr. Pellock testified that Rate Year operating expenses reflect the cost of operating the Waverly system, including an adjustment of $52,112 for miscellaneous expenses.[216]

Patrick L. Baryenbruch presented the results of his study evaluating the services provided by AWWSC during the Test Year.[217] Mr. Baryenbruch stated his study addressed the following four questions:[218]

1. Were AWWSC's charges to VAWC during the Test Year reasonable?

2. Was VAWC charged the lower of cost or market value for managerial and professional services provided by AWWSC during the Test Year?

3. Were Test Year costs of AWWSC's customer accounts services comparable to those of other utilities?

4. Are the services VAWC receives from AWWSC necessary?

Regarding the reasonableness of AWWSC's charges to VAWC during the Test Year, Mr. Baryenbruch contended AWWSC's Test Year cost per VAWC customer of $96 per customer for administrative and general ("A&G")-related services compares to an average of $115 per customer for services companies reporting to the Federal Energy Regulatory Commission ("FERC") is reasonable.[219]

Mr. Baryenbruch found VAWC was charged the lower of cost or market for managerial and professional services during the Test Year.[220] He maintained on average the hourly rates for outside service providers are 117 percent higher that AWWSC's hourly rates.[221]
Mr. Baryenbruch asserted that if VAWC were to contract with outside firms for the managerial and professional services provided by AWWSC, VAWC would have to add at least one position to manage the activities of the outside firms.[222] He further contended that outsourcing the services provided by AWWSC would have increased Test Year expenses by approximately $6.8 million.[223] Mr. Baryenbruch testified his study's hourly rate comparison understates the

[215] *Id.* at 13-14.
[216] *Id.* at 14-15.
[217] Exhibit No. 11, at 3.
[218] *Id.*
[219] *Id.*
[220] *Id.* at 4.
[221] *Id.*
[222] *Id.*
[223] *Id.*

cost advantage of AWWSC because outside providers generally bill for every hour worked, while AWWSC exempt personnel charge a maximum of eight hours per day.[224] He pointed out that it would be difficult for VAWC "to find local service providers with the same specialized water and wastewater industry expertise as that possessed by [AWWSC] staff."[225] Finally, Mr. Baryenbruch affirmed AWWSC fees "do not include any profit markup."[226]

Mr. Baryenbruch compared the costs of AWWSC's customer account services for the Test Year of $21.88 to the neighboring electric utility group's average per-customer cost of $31.14 for 2020. He argued the costs of AWWSC's customer account services for the Test Year were reasonable.[227]

Mr. Baryenbruch concluded that the services provided by AWWSC to VAWC are necessary and "[t]here is no redundancy or overlap in the services provided by [AWWSC] to VAWC."[228]

Charles B. Rea sponsored VAWC's revenue adjustments, cost of service study, rate design proposals, and affordability analyses.[229]

Mr. Rea adjusted VAWC's Rate Year revenues to reflect trends in declining use, weather normalization, and the impact of COVID-19.[230] He made these determinations based on statistical linear regression models.[231] More specifically, Mr. Rea used "a multiple regression statistical model for each customer class that relates the dependent variable, water use per customer, to a collection of independent variables."[232] He advised that the residential model uses 66 months of data (March 2016 through September 2021), and the commercial model uses 120 months of data (October 2011 through September 2021).[233] Mr. Rea reported the R-Squared statistics to be 89 percent for his residential usage model, and 82 percent for his commercial usage model.[234] He maintained "[t]his indicates that in both models, the explanatory variables (weather, COVID-19 impacts, declining use, etc.) do a very good job of explaining the variability in use per customer over time."[235]

Mr. Rea pointed out that both models show a trend of declining use per customer.[236] He contended a decline in use per customer is consistent with the experience of other AWK states

224 *Id.*
225 *Id.* at 5.
226 *Id.*
227 *Id.*
228 *Id.* at 6.
229 Exhibit No. 15, at 3.
230 *Id.* at 5.
231 *Id.* at 6.
232 *Id.* at 15.
233 *Id.*
234 *Id.* at 18.
235 *Id.*
236 *Id.* at 20.

and are driven by the incremental introduction of low-flow fixtures and appliances, new regulations reducing fixture flow-rates, conservation programs, and public initiatives.[237]

Mr. Rea noted weather in VAWC's service territory was cooler and wetter than normal during the Test Year, which served to require a positive adjustment to residential and commercial usages.[238] He asserted COVID-19 had the impact of increasing residential usage and reducing commercial usage.[239]

Mr. Rea maintained "that once weather effects and the one-time effects of COVID-19 have been accounted for, there is a significant downward trend in both residential and commercial usage."[240] He provided the following table to show the sum of his adjustments to residential and commercial use per customer related to weather, COVID-19 impacts and declining usage:[241]

Use per Customer Adjustments	Residential	Commercial
Weather	644	4,568
COVID-19	-4,317	11,132
Declining Use	-1,937	-4,250
Total	**-5,610**	**11,450**

Mr. Rea outlined the following revenue adjustments at present rates for the Test Year:[242]

<u>Water Service</u>

R-01: Remove Net Change in Accrued Revenues
R-02: Remove [PWS]
R-03: Remove Water Infrastructure Surcharge
R-04: Remove TCJA/EADIT Surcredit
R-05: Remove Rates Under Bond for Interim Rates
R-06: Customer Growth (Loss) Adjustments
R-07: Declining Usage Adjustment
R-08: Residential and Commercial Usage Normalization
R-09: Industrial Potable Customers Usage Normalization
R-10: Industrial Non-Potable Usage Normalization
R-11: Remove One-Time Credit to Commercial Customer
R-12: Antennae Lease Adjustment
R-13: Late Payment Fee Adjustment
R-14: Reconnect Fee Adjustment
R-15: Include Town of Waverly Base Revenues

[237] *Id.* at 20-21.
[238] *Id.* at 25.
[239] *Id.* at 25-29.
[240] *Id.* at 29.
[241] *Id.* at 31.
[242] *Id.* at 32-33.

Wastewater Service

R-01: Remove Net Change in Accrued Revenues
R-05: Remove Rates Under Bond for Interim Rates
R-06: Customer Growth (Loss) Adjustments
R-07: Declining Usage Adjustment
R-08: Residential and Commercial Usage Normalization
R-11: Remove One-Time Credit to Commercial Customer
R-12: Antennae Lease Adjustment
R-13: Late Payment Fee Adjustment

Mr. Rea testified the total revenue adjustments for water service "is ($13,059,939) of which ($12,607,022) are accounting-related adjustments (workpapers R-01 through R-05) and ($488,917) are revenue adjustments related to forecasted changes in consumption, customer counts, and miscellaneous revenues."[243] He stated the total revenue adjustments for wastewater service "is ($947,390) of which ($494,404) are accounting-related adjustments (workpapers R-01 through R-05) and ($452,987) are revenue adjustments related to forecasted changes in consumption, customer counts, and miscellaneous revenues."[244] Mr. Rea calculated Rate Year revenues at present rates for water service to be $42,287,467, and for wastewater service to be $9,583,012.[245]

Regarding the Company's class cost of service study ("CCOSS"), Mr. Rea affirmed the methodologies used by the Company in this case are consistent with the AWWA M1 Manual titled "Principles of Water Rates, Fees, and Charges" and the methodology used in the Company's most recent general rate case, Case No. PUR-2018-00175.[246] He confirmed that as in its prior case, VAWC's CCOSS analysis is done on a consolidated statewide basis.[247]

Mr. Rea testified that the CCOSS uses the Base/Extra to allocate several categories of capacity costs, including transmission mains, to customer class.[248] He described calculation of the "Base" component of the allocator as the average daily consumption for the year for each class divided by the total sum of average consumption for all classes.[249] Mr. Rea described the calculation of the "Extra" component of the allocator as the difference between the maximum daily consumption for a given class and the average daily consumption for that class, divided by the total sum of extra consumption for all customer classes.[250] He stated: "[t]he Base component is weighted by the total system load factor expressed as a percentage, and the Extra component is weighted by one minus the system load factor."[251]

[243] *Id.* at 39.
[244] *Id.*
[245] *Id.*
[246] *Id.* at 40.
[247] *Id.* at 42.
[248] *Id.* at 44-48.
[249] *Id.* at 45.
[250] *Id.*
[251] *Id.* at 45-46.

For distribution mains, Mr. Rea pointed out that the Company modifies the Base/Extra method to include maximum hourly demand instead of maximum daily demand.[252]

For metering costs, Mr. Rea advised they are allocated to customer classes based on a weighted number of customers' calculation, which are "based on the ratio of existing meter charges by meter size to the existing 5/8[-inch] meter charge."[253]

Mr. Rea summarized VAWC's CCOSS at current rates as follows:[254]

Customer Class	Revenue at Present Rates	Cost of Service	Revenue Difference	Percentage Difference
Residential	$19,457,819	$23,788,182	$4,330,362	22.3%
Commercial	$12,901,878	$17,801,414	$4,908,536	38.0%
Industrial - Potable	$4,143,827	$5,090,276	$946,449	22.8%
Industrial - Non-Potable Small	$1,223,208	$1,351,570	$128,362	10.5%
Industrial - Non-Potable Large	$3,554,266	$4,806,436	$1,252,170	35.2%
Total	**$41,280,999**	**$52,846,878**	**$11,565,879**	**28.0%**

Regarding rate design, Mr. Rea testified the Company is not proposing any changes to its current rate design for water or wastewater service other than the second of three steps toward a statewide STP structure.[255] He explained the workings of the second step as follows:

> The Company proposes that all existing rates are to be increased by the overall percentage increase granted in this proceeding, with starting revenues by class and district calculated based on those uniformly increased rates, and an adjustment made in each rate to bring revenues for each combination of district and customer class one half of the way from the starting revenue figure to target revenues.[256]

Mr. Rea confirmed the Company is not proposing any changes to its monthly meter charge for the Alexandria, Hopewell, or Prince William districts, and no change to the monthly fixed charge for wastewater service.[257] He indicated that for the Eastern district, VAWC is proposing to reduce the 5/8" and ¾" meter charge to $30.[258]

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[252] *Id.* at 49.
[253] *Id.* at 51.
[254] *Id.* at 52.
[255] *Id.* at 55.
[256] *Id.* at 58.
[257] *Id.*
[258] *Id.*

Mr. Rea provided the current and proposed volumetric rates:[259]

Customer Class and District	Current Volumetric Rate	Proposed Volumetric Rate
Residential – Alexandria	$0.34833	$0.73972
Residential – Prince William	$0.52661	$0.82311
Residential – Hopewell	$0.73125	$1.01773
Residential – Eastern	$0.91486	$1.73148
Commercial – Alexandria	$0.22163	$0.34797
Commercial – Prince William	$0.40851	$0.48200
Commercial – Hopewell	$0.49134	$0.53466

Customer Class and District	Current Volumetric Rate	Proposed Volumetric Rate
Industrial Potable Rates		
Alexandria – First 7,480,000 gpm	$0.23125	$0.28663
Alexandria – Over 7,480,000 gpm	$0.15032	$0.18632
Hopewell – First 2,000 gpm	$0.00000	$0.42994
Hopewell – Next 13,000 gpm	$0.74808	$0.42994
Hopewell – Next 2,229,000 gpm	$0.52959	$0.42994
Hopewell – Next 5,236,000 gpm	$0.31007	$0.42994
Hopewell – Next 37,400,000 gpm	$0.12129	$0.18632
Hopewell – Over 44,880,000 gpm	$0.16315	$0.18632

Customer Class and District	Current Volumetric Rate	Proposed Volumetric Rate
Industrial Non-Potable Rates		
Large Customers – First 7,480,000 gpm	$0.17497	$0.17497
Large Customers – Over 7,480,000 gpm	$0.11373	$0.15318
Small Customers – First 7,480,000 gpm	$0.23307	$0.23307
Small Customers – Over 7,480,000 gpm	$0.15149	$0.19701

Mr. Rea calculated the current rate revenue, proposed rate revenue, and the percentage increase as follows:[260]

[259] *Id.* at 59.
[260] *Id.* at 60.

District/Class	Current Rate Revenue	Proposed Rate Revenue	Percentage Increase
Alexandria Residential	$7,003,858	$9,533,581	36%
Alexandria Commercial	$10,273,866	$14,261,735	39%
Alexandria Industrial	$351,412	$433,844	23%
Prince William Residential	$7,285,984	$9,360,288	28%
Prince William Commercial	$1,548,945	$1,734,551	12%
Eastern Residential	$1,892,183	$1,614,703	-15%
Hopewell Residential	$3,275,792	$3,827,838	17%
Hopewell Commercial	$1,079,068	$1,146,188	6%
Hopewell Industrial Potable	$3,792,414	$4,740,245	25%
Hopewell Industrial Non-Potable	$4,777,475	$6,137,004	28%
Prince William Wastewater	$9,500,418	$12,233,874	29%
Other Operating Revenue	$1,089,062	$1,163,553	7%
Total	**$51,870,477**	**$66,187,404**	**28%**

Mr. Rea testified that affordability of water service in VAWC's service territory, as measured by average annual water bills to annual median household income ("MHI"), have ranged from 0.40 percent to 0.45 percent, with the proposed rates expected to produce a bill to income ("BTI") of 0.43 percent during the rate year.[261]

Regarding affordability for low-income customers, Mr. Rea focused on multiples of the FPL and adjusted water usage to basic water service, which he defined as "a usage level that reflects water consumption provided for basic human services (cooking, cleaning, sanitation, and general health requirements), which is then assumed to be constant from month-to-month and not subject to significant seasonality or weather conditions."[262] He estimated there are approximately 5,600 residential customers with household incomes at or below 150 percent of FPL with a BTI ratio of approximately 2.2 percent for basic water service, which is also 40 gallons of water per household per day.[263] Mr. Rea maintained the generally accepted benchmark for affordability expressed as a total bill's percentage of MHI, is less than 2.0 percent or 2.5 percent for water and 4.0 percent to 4.5 percent of MHI for combined water/wastewater.[264] He reported the affordability benchmark for lower income groups for water service of 3.0 percent to 4.5 percent of household income has also been proposed.[265]

Mr. Rea acknowledged that the MHI varies across VAWC's districts with Alexandria and Prince William being higher than Hopewell and Eastern.[266]

[261] *Id.* at 64-65.
[262] *Id.* at 67.
[263] *Id.* at 69-70.
[264] *Id.* at 70.
[265] *Id.*
[266] *Id.* at 71.

Mr. Rea described VAWC's H2O Program, which offers grants of up to $500 for customers with household income at or below 150 percent of FPI and who otherwise qualify.[267] He advised that the grants are funded through a Company donation and customers and employee donations.[268] In addition, Mr. Rea stated the Company works with customers to develop installment plans, distributed Coronavirus relief funds, and will use ARPA funds for residential customer arrearages of more than 60 days as of August 31, 2021.[269]

John M. Watkins supported VAWC's proposal to implement an RSM to "ensure that the Company receives, and the customers pay, the revenue level found appropriate in this case; no more and no less."[270] Mr. Watkins maintained VAWC's proposed RSM "addresses the unpredictable changes in volume of water sold due to factors beyond the control of the Company."[271] He asserted that most of VAWC's costs are fixed, but its rate structure is based largely on volumetric charges.[272]

Mr. Watkins expressed concern regarding a long-term trend of declining use per customer, and the variable usage of water due to seasonal weather variability.[273] He testified that 92 percent of the Company's costs to provide water service are fixed, but only 38 percent of its water revenues are fixed.[274] In addition, Mr. Watkins affirmed approximately 77 percent of the Company's wastewater system costs are fixed, compared with 55 percent of its wastewater revenues being fixed.[275]

Mr. Watkins acknowledged that declining usage can be factored into the rate case sales forecast but pointed out this only covers the rate year and not subsequent years.[276] He contended one of the impacts of the disconnect between projected and actual sales is that it incentivizes water utilities to sell more water and disincentivizes water conservation.[277]

Mr. Watkins presented a study that showed from 2013-2020, VAWC collected less water revenue, net of production costs, than was authorized in five of the eight years, with actual revenues less than authorized by approximately $5.2 million for the eight-year period.[278] He reported that for the period 2017-2020, VAWC collected less wastewater revenue, net of treatment costs, than authorized in two of the four years, with actual revenues less than authorized by approximately $4.8 million for the four-year period.[279] Mr. Watkins warned: "any

[267] *Id.* at 73.
[268] *Id.*
[269] *Id.* at 73-74.
[270] Exhibit No. 12, at 3.
[271] *Id.* at 4.
[272] *Id.*
[273] *Id.* at 5.
[274] *Id.* at 6-7.
[275] *Id.* at 8.
[276] *Id.* at 10.
[277] *Id.* at 12.
[278] *Id.* at 13.
[279] *Id.*

mismatch in revenues will create unnecessary pressure on the ability of the utility to invest in a timely manner."[280]

Mr. Watkins noted that gas utilities in Virginia have a weather normalization adjustment mechanism ("WNA") in their tariffs.[281] He advised the RSM will mitigate some of the difficulties associated with a WNA for a water utility, which is impacted by more than temperature.[282] Furthermore, Mr. Watkins explained that its proposed RSM "is fundamentally different than adjusting rates to allow for recovery of changing expenses."[283]

Mr. Watkins described implementation of VAWC's proposed RSM as follows:

> The Company is seeking Commission approval for the establishment of a level of Authorized Revenues and production costs in this proceeding. Once approved, the RSM would then compare the Authorized Revenues to actual billed revenues for the residential and commercial classes, and defer/accrue the difference, less the applicable change in production costs, on a monthly basis. Production costs would include power, chemicals and water waste disposal (a percentage of usage for other customers would be removed). Treatment costs would include power chemicals and wastewater disposal. The annual amount of metered revenues and the annual amount of expenses for all production costs would be prorated to monthly amounts. The Company proposes that the proration be set using the Company's last two years of system delivery to obtain a reasonable monthly amount of Authorized Revenues and production costs. These monthly amounts would be reset in the next base rate case proceeding.[284]

Mr. Watkins stated VAWC would compare actual metered revenues and Authorized Revenues, and actual production costs to the amount included in authorized rates for production costs by month by rate class.[285] He indicated that actual revenue shortfall would be treated as regulatory assets. If actual revenues exceed Authorized Revenues, "[t]he ending balance for each month would accrue interest at the Company's short-term borrowing rate."[286] Mr. Watkins further proposed an annual reconciliation to be filed by January 30 of the following year and subject to a 60-day review and approval period.[287] He recommended the return of revenues to customers via a one-time per customer credit, and collection of any shortfall through a

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[280] *Id.* at 14.
[281] *Id.* at 17.
[282] *Id.*
[283] *Id.* at 19.
[284] *Id.* at 20.
[285] *Id.* at 21.
[286] *Id.*
[287] *Id.*

volumetric charge to be collected from April 1 through December 31.[288] Mr. Watkins contended: "[n]o matter what happens with sales, customers who use less will pay less."[289]

Ann E. Bulkley provided testimony on VAWC's ROE and the reasonableness of its capital structure for ratemaking purposes.[290] Ms. Bulkley determined the Company's ROE by developing a proxy group of utilities that face similar risk as VAWC to which she applied: (i) the constant growth form of the Discounted Cash Flow ("DCF") model; (ii) the Capital Asset Pricing Model ("CAPM"); and (iii) the Empirical Capital Asset Pricing Model ("ECAPM").[291] She developed her recommendation by considering the following:

- The *Hope* and *Bluefield* decisions that established the standards for determining a fair and reasonable allowed ROE, including consistency of the allowed return with the returns of other businesses having similar risk, adequacy of the return to provide access to capital and support credit quality, and the requirement that the result lead to just and reasonable rates.

- The effect of current and projected capital market conditions on investors' return requirements.

- The results of several analytical approaches that provide estimates of the Company's cost of equity.

- The Company's regulatory, business and financial risks relative to the proxy group of comparable companies, and the implications of those risks.[292]

Ms. Bulkley found the reasonable range for VAWC's ROE to be from 9.90 percent to 11.00 percent and recommended an authorized ROE of 10.90 percent.[293]

Ms. Bulkley emphasized the importance of projected market data to estimate the return for a forward-looking period.[294] She maintained ROE for regulated utilities is affected by: "(1) the dramatic shifts in market conditions during 2020 and 2021 . . .; and (2) effects of Federal tax reform on utility cash flows."[295]

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[288] *Id.* at 22.
[289] *Id.* at 23.
[290] Exhibit No. 16, at 2.
[291] *Id.* at 3.
[292] *Id.* at 4-5 (footnote omitted).
[293] *Id.* at 7.
[294] *Id.* at 10.
[295] *Id.*

Ms. Bulkley pointed to increased levels of inflation and the prediction of equity analysts indicating that long-term interest rates are expected to rise.[296] She advised that utilities are considered a defensive sector that "tend to perform well during periods of uncertainty where the prospect of slowing economic growth increases."[297]

In selecting a proxy group, Ms. Bulkley affirmed VAWC is a wholly-owned subsidiary of American Water Works Company ("AWK") and accesses debt markets through AWCC.[298] She testified she began with a group of utilities classified by Value Line as "Water Utilities" and "Natural Gas Distribution Companies."[299] Ms. Bulkley applied the following screening criteria to select her proxy companies:

- pay consistent quarterly cash dividends because companies that do not cannot be analyzed using the Constant Growth DCF model;

- have investment grade long-term issuer ratings from S&P and/or Moody's;

- are covered by at least two utility industry analysts;

- have positive long-term earnings growth forecasts from at least two utility industry equity analysts;

- derive more than 60.00 percent of their total operating income from regulated operations; and were not parties to a merger or transformative transaction during the analytical periods relied on.[300]

In addition, Ms. Bulkley considered 36 companies classified by Value Line as "Electric Utilities."[301] She advised that the screening criteria she applied to these companies was the same as listed above, plus two additional screening criteria:

- have owned generation comprising less than 10 percent of the Company's [megawatt hour ("MWh")] sales to ultimate customers to ensure that the electric utilities included did not own a substantial amount of generation and therefore had operations that were primarily transmission and distribution; and

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[296] *Id.* at 17.
[297] *Id.* at 20-21.
[298] *Id.* at 26.
[299] *Id.* at 27.
[300] *Id.*
[301] *Id.*

- own water and wastewater operations.[302]

Based on the criteria described above, Ms. Bulkley selected the following proxy group:[303]

Company	Ticker
American States Water Company	AWR
Atmos Energy Corporation	ATO
California Water Service Group	CWT
Essential Utilities, Inc.	WTRG
Eversource Energy	ES
Middlesex Water Company	MSEX
New Jersey Resources Corporation	NJR
NiSource Inc.	NI
Northwest Natural Gas Company	NWN
ONE Gas Inc.	OGS
SJW Group	SJW
South Jersey Industries, Inc.	SJI
Spire, Inc.	SR
York Water Company	YORW

Ms. Bulkley supported the inclusion of gas and electric companies in her proxy group based on the small number of water companies and because the electric and gas utilities generate a large portion of their operating income from regulated operations.[304] She also cited to four other state commissions that have included natural gas distribution companies in the proxy groups used to estimate the ROE for a water utility.[305]

Ms. Bulkley testified: "[b]ecause the cost of equity is not directly observable, it must be estimated based on both quantitative and qualitative information."[306]

For her Constant Growth DCF model, Ms. Bulkley used the following formula:[307]

$$k = \frac{D_0(1+g)}{P_0} + g$$

Where:

k = Required ROE
D_0 = Current Dividend Yield
P_0 = Current Stock Price
g = Expected Dividend Yield Growth

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[302] *Id.* at 27-28.
[303] *Id.*
[304] *Id.* at 29.
[305] *Id.* at 30.
[306] *Id.* at 33.
[307] *Id.* at 37.

Ms. Bulkley maintained "[t]he Constant Growth DCF model requires the following assumptions: (1) a constant growth rate for earnings and dividends; (2) a stable dividend payout ratio; (3) a [Price/Earnings ("P/E")] ratio; and (4) a discount rate greater than the expected growth rate."[308] She advised if these assumptions are not met, "considered judgment and/or specific adjustments should be applied to the results."[309]

Ms. Bulkley used market data for the dividend yield "based on the proxy companies' current annual dividend and average closing stock prices over the 30-, 90-, and 180-trading days as of September 30, 2021."[310] She asserted the average of stock prices should not be skewed by anomalous events and "be reasonably representative of expected capital market conditions over the long-term."[311] Nonetheless, Ms. Bulkley contended these market prices are unsustainably high, cannot be expected to continue throughout the rate period, and are inconsistent with forward-looking market expectations.[312] Thus, she maintained the Constant Growth DCF model may understate the forward-looking ROE and recommended more weight be placed on the mean to mean-high results.[313]

Ms. Bulkley adjusted the dividend yield for the first year's growth by one half to reflect dividend growth occurs at different times throughout the year.[314]

Ms. Bulkley used long-term growth rates from the following sources: "(1) consensus long-term earnings growth estimates from Zacks Investment Research; (2) consensus long-term earnings growth estimates from Thomson First Call (provided by Yahoo! Finance); and (3) long-term earnings growth estimates from Value Line."[315] Ms. Bulkley calculated her minimum DCF for the proxy group using the lowest growth rate from the sources listed above, the high result using the highest growth rates for each proxy company, and the mean results by using the average growth rates from all her sources.[316] Finally, she identified individual proxy companies with results of 7.00 percent or below because such a result would fail to provide a reasonable equity risk premium as calculated by her CAPM.[317] In calculating mean DCF results Ms. Bulkley eliminated the results for proxy companies that were 7.00 percent or below.[318] In calculating the median DCF result, she did not eliminate the low results as the median is not affected by outliers.[319]

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[308] *Id.*
[309] *Id.* at 38.
[310] *Id.*
[311] *Id.*
[312] *Id.*
[313] *Id.*
[314] *Id.* at 39.
[315] *Id.* at 40.
[316] *Id.* at 40-41.
[317] *Id.* at 41-42.
[318] *Id.* at 42.
[319] *Id.* at 43.

Ms. Bulkley summarized her Constant Growth DCF results as follows:[320]

Constant Growth DCF with exclusions			
	Mean Low	Mean	Mean High
30-Day Average	8.80%	9.95%	11.71%
90-Day Average	8.71%	9.85%	11.61%
180-Day Average	8.75%	9.88%	11.64%
Constant Growth Average	8.75%	9.89%	11.66%
Average of All Mean Constant Growth DCF – with exclusion			10.10%
Constant Growth DCF without exclusions			
	Median Low	Median	Median High
30-Day Average	8.48%	9.61%	10.90%
90-Day Average	8.39%	9.65%	10.70%
180-Day Average	8.39%	9.68%	10.70%
Constant Growth Average	8.42%	9.64%	10.77%
Average of All Median Constant Growth DCF			9.61%

Regarding her CAPM analysis, Ms. Bulkley described CAPM as "a risk premium approach that estimates the cost of equity for a given security as a function of a risk-free return plus a risk premium to compensate investors for the non-diversifiable or 'systematic' risk of that security."[321] She provided the following formula for CAPM:[322]

$$K_e = r_f + \beta(r_m - r_f)$$

Where:

K_e = the required market ROE;
β = Beta coefficient of an individual security;
r_f = the risk-free [rate of return]; and
r_m = the required return on the market as a whole.

Ms. Bulkley explained that "Beta is a measure of the volatility of a security as compared to the market as a whole."[323] She indicated that "Beta represents the risk of the security relative to the general market."[324] For her risk-free rate, Ms. Bulkley relied on: (1) the current 30-day average yield on 30-year U.S. Treasury bonds of 1.93 percent as of September 30, 2021; (2) the projected 30-year U.S. Treasury bond yield for Q1 2022 through Q2 2023 of 2.50 percent; and

[320] *Id.* at 43-44.
[321] *Id.* at 44.
[322] *Id.* at 45.
[323] *Id.*
[324] *Id.*

(3) the projected 30-year U.S. Treasury bond yield for 2023 through 2027 of 3.50 percent.[325] Nonetheless, she advised that she placed more weight on the projected yields.[326]

For Market Risk Premium, Ms. Bulkley calculated the expected return on the S&P 500 Index using the Constant Growth DCF model to be 12.94 percent.[327] In support, she noted that in 46 of the past 94 years, "the realized total equity return was at least 12.94 percent or greater."[328]

Ms. Bulkley also considered the results of the ECAPM, which is derived from the following formula:[329]

$$K_e = r_f + 0.75\beta(r_m - r_f) + 0.25(r_m - r_f)$$

Where:
K_e = the required market ROE[;];
β = Adjusted Beta coefficient of an individual security[;]
r_f = the risk-free rate of return[; and]
r_m = the required return on the market as a whole[.]

Ms. Bulkley maintained the ECAPM corrects the tendency for the CAPM to underestimate ROE based on academic research.[330]

Ms. Bulkley reported the following results for her CAPM and ECAPM models:[331]

	Current Risk-Free Rate (1.93%)	**Q1 2022- Q1 2023 Projected Risk Free-Rate (2.50%)**	**2023-2027 Projected Risk-Free Rate (3.50%)**
CAPM			
Value Line Beta	11.13%	11.22%	11.39%
Bloomberg Beta	10.61%	10.74%	10.95%
Long-term Avg Beta	9.85%	10.01%	10.29%
ECAPM			
Value Line Beta	11.58%	11.65%	11.77%
Bloomberg Beta	11.20%	11.29%	11.44%
Long-term Avg Beta	10.62%	10.74%	10.95%

325 *Id.* at 46.
326 *Id.*
327 *Id.* at 47.
328 *Id.* at 48.
329 *Id.* at 49-50.
330 *Id.* at 50.
331 *Id.* at 51.

Ms. Bulkley concluded based on the DCF, CAPM, and ECAPM analyses that a reasonable ROE range for VAWC is 9.90 percent to 11.00 percent, and recommended the Commission set the Company's ROE at 10.90 percent.[332]

Ms. Bulkley testified several additional risk factors must be considered when determining where the Company's ROE falls within the range of results. She pointed to VAWC's plans to make capital investments of approximately $192.7 million for the period 2022 through 2026, which will impose strains and risks on the Company.[333] In addition, Ms. Bulkley maintained there is risk related to the declining average use per customer.[334] Furthermore, she advised that VAWC's lower equity ratio makes VAWC more risky than the proxy group and "[w]ithout . . . an adjustment, the comparable return standard that was established by the U.S. Supreme Court in the *Hope* and *Bluefield* decisions would be violated . . . ."[335]

Ms. Bulkley compared her weighted ROE to other recent weighted ROEs authorized by the Commission and contended her weighted ROE is at the low end of the range of recent Commission decisions.[336]

Regarding capital structure, Ms. Bulkley testified VAWC is proposing to rely on its actual capital structure of 40.75 percent equity, 55.66 percent long-term debt, 3.27 percent short term debt, and 0.32 percent Job Development Investment Tax Credits ("JDITC").[337] She supported use of VAWC's stand-alone capital structure "because that is the capital structure that reflects the actual financing of the Company's rate base."[338] Ms. Bulkley acknowledged the Commission has used AWK's consolidated capital structure since 2010, but maintained "[t]he consolidated capital structure is not specific to the VAWC operations . . . ."[339] She asserted that if AWCC issues debt to purchase a new affiliate, it would increase the leverage of the consolidated group, but VAWC's rate base would remain unchanged.[340] Ms. Bulkley pointed out that Pennsylvania and New Jersey have incentives for financially sound utilities to purchase troubled water and wastewater systems.[341]

VAWC Supplemental Testimony

On July 13, 2022, VAWC filed the supplemental testimony of John S. Tomac and Scott T. Grace. The supplemental testimony of each witness is summarized below.

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332 *Id.*
333 *Id.* at 52.
334 *Id.* at 54-55.
335 *Id.* at 56.
336 *Id.* at 57-58.
337 *Id.* at 60.
338 *Id.* at 61.
339 *Id.* at 62.
340 *Id.* at 64.
341 *Id.* at 65.

John S. Tomac updated the cost rates associated with short-term and long-term debt.[342] Mr. Tomac stated in May of 2022, VAWC received long-term debt at a rate of 4.45 percent, which is significantly higher than the estimated 3.0 percent in the Company's Application.[343] In addition, he updated the forecasted 2023 long-term debt cost rate to 4.8 percent. Mr. Tomac testified these changes increase VAWC's overall cost of long-term debt from 4.086 percent to 4.265 percent; and increases long-term interest expense by $290,000.[344]

Mr. Tomac updated the cost of short-term debt to 2.672 percent, which increases short-term interest expense by $221,355.[345] He advised the effect of the adjustments to short-term and long-term debt is to increase the Company's proposed weighted average cost of capital from 6.749 percent to 6.925 percent.[346]

Scott T. Grace updated forecasted pension and OPEB expense.[347] Mr. Grace reported "due to a significant decline in global investment returns," VAWC's AWK retirement plan actuary, WTW, projected pension and OPEB costs "to increase beyond the level of expense originally forecasted for 2023."[348] He recommended an adjustment to increase VAWC's allocated pension expense by $581,711 and an adjustment to increase OPEB expense by $62,750.[349] For AWWSC pension and OPEB expense allocated to VAWC, Mr. Grace increased pension expense by $191,530 and OPEB expense by $7,439.[350]

Alexandria Direct Testimony

On July 19, 2022, Alexandria filed the direct testimony of Carl W. Eger, III, Energy Manager for Alexandria; and J. Bartholomew Kreps, Vice President with Raftelis Financial Consultants. A summary of each testimony is provided below.

Carl W. Eger, III, maintained the Company's proposed volumetric rate increase for residential and commercial classes for the Alexandria district of approximately 112 percent and 57 percent, respectively, are unreasonable and inconsistent with the principles of gradualism.[351] Mr. Eger took issue with average bill impacts provided by Company witness Rea based on customers who use 4,000 gallons per month.[352] Mr. Eger contended the average monthly usage for Alexandria residential customers is nearly 4,500 gallons per month, and Mr. Rea failed to

[342] Exhibit No. 14, at 1.
[343] *Id.* at 2.
[344] *Id.*
[345] *Id.*
[346] *Id.* at 2-3.
[347] Exhibit No. 8, at 1.
[348] *Id.* at 1-2.
[349] *Id.* at 2.
[350] *Id.* at 2-3.
[351] Exhibit No. 17, at 4.
[352] *Id.* at 5.

consider the surcharges proposed by VAWC such as the Purchase Water Surcharge, WWISC, RSM, and uncollected expense surcharge.[353]

Mr. Eger reported based on Alexandria's 2020 Resident Survey, it is estimated that 18 percent of Alexandria residents live in single-family detached houses, 80 percent of Alexandria residents live in a building with two or more units.[354] He also estimated that 51 percent of Alexandria residents are renters and 49 percent own their residence.[355] Mr. Eger testified that there are multi-family buildings in Alexandria that are served by a master meter and billed under VAWC's commercial tariff.[356] He maintained "[b]ecause a greater percentage of a commercial water bill comprises the volumetric portion of the rate, the proposed rate increases will result in a higher burden on residents in multi-family dwellings who are billed according to a commercial rate class."[357]

Mr. Eger affirmed Alexandria is a diverse community, and although Alexandria is generally considered an affluent area, "[a]t least 1 in 10 Alexandrian households are reported as living in poverty, including nearly 1 out of 5 children in the [c]ity."[358] He contended the unprecedented increases in rates for water service proposed by VAWC "will be felt most acutely by low-income families . . . ."[359]

Mr. Eger reiterated Alexandria's objection to VAWC's initiative to institute consolidated tariff pricing across its Virginia water systems.[360] He asserted Alexandria ratepayers are subsidizing other districts, and pointed to the massive capital investment in the Hopewell district.[361] Mr. Eger argued this rate increase "cannot be characterized as a gradual adjustment."[362] He noted that in the VAWC's prior case, Case No. PUR-2018-00175, he objected to VAWC's consolidation proposal, but Alexandria, by counsel, consented to a stipulated agreement to move toward consolidated rates over the course of three rate cases.[363] Mr. Eger advised that in the prior case, Alexandria residential bills increased 12.6 percent, while a resident using approximately 4,500 gallons per month would see his/her water bill increase by nearly 41.25 percent in this case.[364] He argued VAWC's proposed rate increase violates the Code and the stipulation in Case No. PUR-2018-00175 "that rate increases be reasonable, gradual, and conducted over an appropriate period."[365]

[353] *Id.*
[354] *Id.* at 6.
[355] *Id.*
[356] *Id.* at 6-7.
[357] *Id.* at 7.
[358] *Id.* at 9.
[359] *Id.*
[360] *Id.* at 10.
[361] *Id.*
[362] *Id.* at 11.
[363] *Id.*
[364] *Id.* at 12.
[365] *Id.* at 13.

Regarding the Company's proposed RSM, Mr. Eger advised that the Commission rejected RSM in the Commission's *2015 Rate Order*.[366] He continued to oppose RSM based on the unlikelihood for large swings in water usage due to weather, especially in Alexandria, and the lack of statutory authority for implementing an RSM.[367] Mr. Eger also questioned the added cost of the annual filing and reconciliation process for RSM.[368] Finally, he maintained "there does not appear to be any identifiable benefit for customers to the proposed RSM."[369]

J. Bartholomew Kreps addressed gradualism, ROE, the cost-of-service analysis, and proposed surcharges.[370]

Gradualism

Mr. Kreps focused on the proposed changes to the volumetric rates for residential customers in Alexandria and advised that most customers' bills would increase at least 21 percent, with approximately 20 percent of residential customers experiencing increases of more than 50 percent.[371] He highlighted the "materially greater" rate increases to be faced by residential customers with larger households, and master-metered multi-family customers.[372] Mr. Kreps took issue with the public notice given by VAWC for failing to capture the surcharges, riders, and automatic adjustment mechanisms proposed by the Company.[373]

Mr. Kreps testified that the concept of "gradualism" recognizes that the capacity of customers to adjust to an increased cost is limited and takes time.[374] He argued the proposed increases are not gradual and "far exceed what customers could have expected based on VAWC's last rate case."[375] For Alexandria residential customers, Mr. Kreps contended the Company's proposed rates would more than double the Step 1 increase, which was approximately 12.6 percent.[376] He asserted the size of the proposed increase, along with the short window between rate cases contribute to rate shock.[377]

While Mr. Kreps agreed with the testimony of Company witness Rea that water service under the proposed rates remains affordable for the vast majority of VAWC's residential

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[366] *Id.* at 14; *Application of Virginia-American Water Company, For a general increase in rates*, Case No. PUE-2015-00097, 2017 S.C.C. Ann. Rep. 288 ("*2015 Rate Order*").
[367] *Id.* at 14-15.
[368] *Id.* at 15-16.
[369] *Id.* at 16.
[370] Exhibit No. 18, at 2.
[371] *Id.* at 4.
[372] *Id.* at 6.
[373] *Id.* at 7.
[374] *Id.* at 8.
[375] *Id.* at 9.
[376] *Id.* at 13.
[377] *Id.* at 14.

customers, Mr. Kreps stressed there are groups of customers for whom affordability of water service may be an issue, even in communities such as Alexandria.[378]

Cost of Capital

Mr. Kreps agreed with the testimony of Company witness Bulkley that utilities and their investors are entitled to a fair and reasonable return.[379] He also agreed with Ms. Bulkley's general approach for calculating a fair and reasonable ROE.[380] However, Mr. Kreps indicated he disagreed "with certain perspectives on variables driving the calculations and the comparability of the proxy group used, as well as a lack of consideration for risk mitigating mechanisms that reduce VAWC's risk profile."[381]

Mr. Kreps disagreed with the inclusion of natural gas and electric utilities in Ms. Bulkley's proxy group because they face the additional risk of competition and other structural differences than water utilities.[382] He also disagreed with her estimated market return of 12.94 percent, which is higher than what the S&P 500 has returned historically.[383]

Mr. Kreps disagreed with Ms. Bulkley's conclusion that it is reasonable for VAWC to receive an ROE near the top of her "reasonable range."[384] He maintained at a macro-level vertically integrated water utilities are less risky than natural gas and electric utilities.[385] On a micro-level, Mr. Kreps pointed to mechanisms such as WWISC, fixed charge revenue recovery, and Rate Year adjustments for declining per capita consumption that reduce risk for VAWC.[386] He disagreed with Ms. Bulkley's assertion that declining average per-customer usage should be factored into VAWC's risk profile relative to the proxy group as such declines are experienced across both water and energy sectors.[387] He noted another risk mitigation measure enjoyed by VAWC is CTP, which allows the Company to spread its cost of service across a larger, multi-district customer base.[388]

Mr. Kreps agreed with Ms. Bulkley's statement that VAWC's equity ratio results in an increased financial risk relative to the proxy group.[389] Nonetheless, he contended that there are other structural issues that should be considered when assessing leverage and its relationship to

[378] *Id.* at 15.
[379] *Id.* at 16.
[380] *Id.* at 17.
[381] *Id.*
[382] *Id.* at 17-18.
[383] *Id.* at 18.
[384] *Id.* at 19.
[385] *Id.*
[386] *Id.* at 19-20.
[387] *Id.* at 20.
[388] *Id.* at 23-24.
[389] *Id.* at 25.

risk.[390] Mr. Kreps asserted "VAWC's equity ratio alone is not sufficient to reflect an upward adjustment to its ROE."[391]

Mr. Kreps maintained a fair and reasonable ROE would lie at the mid to lower end of Ms. Bulkley's range.[392]

Mr. Kreps reviewed Ms. Bulkley's analysis of capital market conditions and noted some of her predictions have not proven to be accurate.[393] He pointed to federal fund rates, and other Treasury rates, which are now inverted and often indicate a coming recession.[394] He also noted Ms. Bulkley advised that demand for utility stocks increase during a recession, which, all other things being equal, increases utility stock prices and reduces dividend yields.[395]

Mr. Kreps proposed the use of the following proxy group, which is based on the Company's proxy group without utilities that provide only natural gas and/or electric services:

American States Water Company;
California Water Services Group;
Essential Utilities, Inc.;
Eversource Energy;
Middlesex Water Company;
Northwest Natural Gas Company;
SJW Group; and
York Water Company.[396]

Mr. Kreps rendered the constant DCF model using the following formula:[397]

$$K = (D_1/P_0) + g$$

Where:
K = Required rate of return
D_1 = All expected future dividends
P_0 = Current stock price
g = Expected growth rate

[390] *Id.* at 25-26.
[391] *Id.* at 26.
[392] *Id.*
[393] *Id.* at 27.
[394] *Id.* at 28-29.
[395] *Id.* at 30.
[396] *Id.* at 31.
[397] *Id.* at 32.

Mr. Kreps disagreed with Ms. Bulkley's decision to exclude mean DCF results below 7.0 percent, which eliminates 50 percent of the water only utilities, and disagreed with her assertion that the DCF is likely to understate ROE.[398]

Mr. Kreps used dividend yields in his DCF based on the proxy companies' current annual dividend and average stock closing prices over the 30-, 90-, and 180-trading days as of June 15, 2022.[399] He reported ROE results for the entire proxy group from 8.34 percent to 10.85 percent, with a mean of 9.48 percent; and ROE for the proxy group excluding energy only utilities of 7.99 percent to 10.34 percent, with a mean of 9.12 percent.[400]

Regarding the CAPM analysis, Mr. Kreps used the following formula:[401]

$$K = R_f + \beta(R_m - R_f)$$

Where:

R_f	= Risk-Free Rate of Return
β	= Beta, or the Stock's market risk . . .
R_m	= Market Equity Return
$(R_m - R_f)$	= Expected Market Equity Risk Premium

Mr. Kreps disagreed with the greater weight Ms. Bulkley placed on projected yields for 30-year Treasury bonds.[402] He also disagreed with her estimate of the market return of 12.94 percent, which is higher than the simple average arithmetic mean of the S&P 500 from 1926 through 2021 of 12.39 percent and a geometric or compound annual growth rate of 10.49 percent.[403] Mr. Kreps opined that the geometric or compound annual growth rate of 10.49 percent "is a more realistic expectation for an expected return in equities over time."[404]

Mr. Kreps calculated the following CAPM results:[405]

[398] *Id.* at 33.
[399] *Id.* at 34-35.
[400] *Id.* at 35.
[401] *Id.* at 37.
[402] *Id.*
[403] *Id.* at 38.
[404] *Id.*
[405] *Id.* at 39.

Description	Market Return (Mean) Arithmetic	Geometric
Proxy Group		
Value Line Beta	10.87%	9.28%
Long-term Average Beta	9.79%	8.42%
Mean	10.33%	8.85%
Proxy Group (Excluding Energy Only Utilities)		
Value Line Beta	10.54%	9.02%
Long-term Average Beta	9.74%	8.38%
Mean	10.14%	8.70%

Based on the mid-point of his DCF analysis of 9.30 percent and the midpoint of his CAPM analysis of 9.51 percent, Mr. Kreps recommended an ROE near the mid to lower end of the range between 9.3 percent to 9.4 percent would be fair and reasonable for VAWC in this proceeding.[406]

Cost of Service and Rate Design

Mr. Kreps contended the overall increase of 28 percent is unreasonable based on the Company's requested ROE, and that the Alexandria district is unfairly apportioned greater costs as compared to the other districts.[407] He maintained Company witness Rea's CCOSS uses peaking factors that employ unsupported weekly and hourly adjustments and allocates too little cost associated with mains smaller than 10 inches to industrial classes.[408]

Regarding the weekly adjustment, Mr. Kreps asserted Mr. Rea's weekly adjustment is entirely anecdotal and pushes the diversity ratio outside of the typical 1.1 to 1.4 range.[409] Instead, Mr. Kreps recommended a weekly usage adjustment adjusted to 1.0, which places all districts within the typical range.[410]

For the hourly adjustment, Mr. Kreps pointed out that the hourly adjustment factor used by Mr. Rea in this proceeding is 1.8 for residential customers, and 1.5 for commercial and industrial customers, but was 1.45 for all customers in Case No. PUR-2018-00175.[411] Mr. Kreps testified this change "significantly increases the estimated maximum hour demands of residential customers relative to the other classes, without any analysis or evidence."[412] In the absence of evidence, Mr. Kreps recommended all hourly adjustment factors be set to 1.45.[413]

[406] *Id.* at 39-40.
[407] *Id.* at 42.
[408] *Id.* at 42-43.
[409] *Id.* at 45.
[410] *Id.*
[411] *Id.*
[412] *Id.* at 46.
[413] *Id.*

For allocation of mains, Mr. Kreps stated for transmission mains, VAWC allocated approximately 18 percent of costs to industrial potable customers, but for distribution mains, the Company allocated only 3 percent of costs to industrial potable customers.[414] He maintained the Company's approach singles out industrial customers for special treatment based on the characteristics of individual customers as opposed to the whole class.[415] Mr. Kreps also argued this approach ignores VAWC's movement towards consolidated rates.[416] He recommended that the distribution factor used in the CCOSS should be set to 1.0 for all customer classes to ensure industrial customers pay their proportionate share "based on the demand of the class, not the characteristics of the individual customers."[417] Mr. Kreps calculated that the Company's allocation of distribution mains adds approximately $370,000 to the revenue requirement for Alexandria.[418]

Surcharges

Mr. Kreps testified the Company's proposed RSM "would essentially eliminate VAWC's risk associated with its volumetric revenue."[419] He warned the RSM could reduce the Company's incentive to maintain accurate meters and argued institution of an RSM is not justified by VAWC becoming "indifferent" to selling less water.[420] Mr. Kreps asserted that water efficiency is an increasing national trend based on choices made by customers.[421] He further contended an RSM is not necessary for VAWC to maintain a reasonable and prudent level of investment in its system.[422]

In addition, Mr. Kreps objected to the implementation of the proposed RSM.[423] Among other things, he recommended that refunds of RSM credits be based on usage, and that RSM be tested as a pilot program.[424]

Regarding VAWC's proposed Uncollectibles ARAC, Mr. Kreps disagreed that there is a need and pointed to the Commission's treatment of uncollectibles related to COVID-19.[425] He asserted the Uncollectibles ARAC "would add costs without any discernible benefit."[426]

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[414] *Id.* at 47-48.
[415] *Id.* at 48.
[416] *Id.* at 48-49.
[417] *Id.* at 52-53.
[418] *Id.* at 53.
[419] *Id.* at 54.
[420] *Id.*
[421] *Id.* at 55.
[422] *Id.* at 56.
[423] *Id.* at 57-58.
[424] *Id.* at 59.
[425] *Id.* at 60.
[426] *Id.* at 61.

Committee Direct Testimony

On July 19, 2022, the Committee filed the direct testimony of Michael P. Gorman, Managing Principal of Brubaker & Associates, Inc. Mr. Gorman's testimony is summarized below.

Michael P. Gorman recommended an ROE range for VAWC of 8.90 percent to 9.80 percent, with a midpoint of 9.35 percent.[427] Mr. Gorman further recommended an overall rate of return of 5.95 percent, based on the projected test year capital structure of VAWC's parent company, AWK.[428] In addition, he took issue with the Company's proposed revenue spread and CCOSS.[429] Mr. Gorman disagreed with the Company's proposed overall revenue decrease to the Eastern district and question VAWC's proposal that will result in certain customer classes paying rates in excess of their cost of service.[430] Regarding the Company's CCOSS, Mr. Gorman disagreed with: (i) the classification of water pumping costs between potable and non-potable usage; (ii) VAWC's reliance on unsupported weekly usage adjustment factors in developing the maximum day and maximum hour peaking factors; and (iii) the distribution multiplier used to reflect the portion of industrial usage served from small distribution mains.[431] Based on his corrected CCOSS, Mr. Gorman proposed an alternative revenue spread.[432]

Mr. Gorman recommended the Commission reject VAWC's proposed two-third allocation of purchased water costs across all customers.[433] He argued "[m]aintaining the current allocation of purchased water costs by spreading one-third of the costs across all districts, and allocating two-thirds of the costs to Alexandria and Prince William will produce volumetric charges for all customers and districts that are reasonably aligned with one another and will constitute a meaningful step towards establishment of a single tariff pricing scheme."[434]

Mr. Gorman recommended rejection of VAWC's proposed RSM and contended the Company failed to demonstrate it is not allowed to fully recover its cost of service.[435] He maintained the Company has been provided with a reasonable opportunity to earn its authorized ROE.[436]

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[427] Exhibit No. 19, at 2.
[428] *Id.* at 3.
[429] *Id.*
[430] *Id.*
[431] *Id.* at 3-4.
[432] *Id.* at 4.
[433] *Id.*
[434] *Id.* at 5.
[435] *Id.*
[436] *Id.* at 5-6.

Mr. Gorman opposed the Company's proposed Uncollectibles ARAC and asserted VAWC has not shown its proposal "would ensure that customers' bills reflect only just and reasonable charges."[437]

Mr. Gorman pointed to VAWC's growth in rate base since its prior rate case and stated: "the authorized overall rate of return generally, and the return on equity specifically, have supported VAWC's access to capital, on reasonable terms and at reasonable prices, and are generally perceived . . . as providing reasonable competition for necessary infrastructure investments."[438] He acknowledged recent increases in interest rates but maintained: "the projected increases relative to the past are relatively modest, and demonstrate that VAWC's proposal to increase its authorized [ROE] in this case to 10.90 [percent] is simply not reflective of current market capital costs."[439]

Mr. Gorman disagreed with the Company's proposal to use VAWC's stand-alone capital structure for ratemaking purposes.[440] He pointed to VAWC getting most of its equity and debt capital directly from its corporate parent, AWK, and affiliate, AWCC.[441] Mr. Gorman contended: "the parent company's capital structure more accurately reflects the capital structure mix that capital market participants consider when valuing the debt and equity securities that are and will be used to fund investments in VAWC's water and wastewater infrastructure assets."[442]

Mr. Gorman proposed the following capital structure based on AWK's actual five-quarter average consolidated capital structure as of March 31, 2022:[443]

Description	**Regulatory Weight**	**Investors Weight**
Short-Term Debt	3.97%	
Long-Term Debt	56.79%	59.17%
Preferred Equity	0.02%	0.02%
Common Equity	39.16%	40.80%
Job Development Credits	0.06%	
Total	**100.00%**	**100.00%**

Mr. Gorman cited to *Bluefield* and *Hope* and testified: "a fair rate of return is established with the expectation that the utility's costs of service reflect efficient and economical management, and is designed to produce investment returns at – but not exceeding – levels sufficient to support the utility's continued credit standing and reasonable access to capital."[444]

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[437] *Id.* at 7.
[438] *Id.* at 8-9.
[439] *Id.* at 20.
[440] *Id.* at 30.
[441] *Id.*
[442] *Id.* at 30-31.
[443] *Id.* at 34.
[444] *Id.* at 37.

Except for excluding South Jersey Industries because they agreed to be acquired in February 2022, Mr. Gorman used the same proxy group as Company witness Bulkley.[445]

Mr. Gorman's DCF model is based on the following formula:[446]

$$K = (D_1/P_0) + G$$

Where:

K	= Investor's required return
D_1	= Dividend in first year
P_0	= Current stock price
G	= Expected constant dividend growth rate

For the current stock price, Mr. Gorman used an average of the weekly high and low stock prices of the utilities in his proxy group over the 13-week period ended June 10, 2022.[447] He calculated the dividend in the first year by multiplying actual quarterly dividends reported by *Value Line* in April and May 2022, by four, to annualize, and by one plus the growth rate.[448] As for the growth rate, Mr. Gorman used an average of earnings growth estimates from Zacks, S&P Global Market Intelligence ("MI"), and Yahoo! Finance that were available online on June 10, 2022.[449]

Mr. Gorman stated the DCF results were as follows: (i) the average and median returns for his gas proxy group were 9.21 percent and 8.99 percent, respectively; and (ii) the average and median return for his water proxy group were 8.73 percent and 7.89 percent, respectively.[450]

Mr. Gorman calculated a Sustainable Growth DCF, based on an analysis of earnings retention ratios, which produced an average and median return for his gas proxy group of 8.62 percent and 8.30 percent, respectively; and an average and median return for his water proxy group of 8.39 percent and 8.15 percent, respectively.[451]

Mr. Gorman conducted a multi-stage growth DCF model to reflect three growth periods: "(1) a short-term growth period consisting of the first five years; (2) a transition period, consisting of the next five years (6 through 10); and (3) a long-term growth period starting in year 11 through perpetuity."[452] He maintained that a utility cannot indefinitely sustain growth rates that exceed the growth rate of the economy in which they serve.[453] For a long-term growth rate, Mr. Gorman used the consensus projection for gross domestic product ("GDP"), projected

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[445] *Id.*
[446] *Id.* at 39-40.
[447] *Id.* at 40.
[448] *Id.* at 41.
[449] *Id.* at 42.
[450] *Id.* at 42-43.
[451] *Id.* at 45-46.
[452] *Id.* at 47.
[453] *Id.* at 48.

five- and 10-year average of 4.45 percent as published by *Blue Chip Financial Forecasts*.[454] He reported the results of his multi-stage growth DCF model to be an average and median return for his gas proxy group of 7.99 percent and 8.21 percent, respectively, and an average and median return for his water proxy group of 6.74 percent and 6.77 percent, respectively.[455]

Mr. Gorman testified that his DCF studies indicate a fair ROE for VAWC in the range of 8.60 percent to 9.20 percent, with a midpoint of 8.90 percent.[456]

Mr. Gorman offered estimates of equity risk premium based, in part, on data ranging from 1986 through 2022.[457] He testified that his Treasury bond risk premium of 9.21 percent and his utility bond risk premium of 8.72 percent "indicate a return on equity for VAWC of 9.00 percent."[458]

Mr. Gorman presented the formula for his CAPM as follows:[459]

$$R_i = R_f + B_i \times (R_m - R_f)$$

Where:
R_i = Required return for stock i
R_f = Risk-free rate
R_m = Expected return for the market portfolio
B_i = Beta (Measure of the stock risk and price volatility)

Mr. Gorman calculated a CAPM return of about 9.81 percent using a market return of 12.04 percent, a projected risk-free rate of 3.60 percent, and normalized utility beta of 0.74.[460] He contended "the current elevated betas do not reflect the low industry risk for VAWC or the utility industry as a whole."[461] Therefore, Mr. Gorman maintained the CAPM indicated a reasonable ROE for VAWC of 9.80 percent.[462]

Based on his DCF result of 9.00 percent, risk premium of 9.00 percent, and CAPM of 9.80 percent, Mr. Gorman recommended VAWC's ROE to be in the range of 8.90 percent to 9.80 percent, with a midpoint of 9.35 percent.[463] He argued Company witness Bulkley's estimated ROE produced excessive results for various reasons including:

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[454] *Id.* at 51.
[455] *Id.* at 53.
[456] *Id.* at 54.
[457] *Id.* at 55.
[458] *Id.* at 60.
[459] *Id.*
[460] *Id.* at 68.
[461] *Id.*
[462] *Id.*
[463] *Id.*

1. Her constant growth DCF results are based on unsustainably high growth rates;

2. Ms. Bulkley's methodology of excluding low-end results below 7.0 [percent] is subjective and should be rejected;

3. Her CAPM is based on inflated market risk premiums;

4. Ms. Bulkley's [ECAPM] is based on a flawed methodology[;] and

5. Both Ms. Bulkley's CAPM studies are based on projected interest rates that are highly uncertain.[464]

Mr. Gorman testified that "with prudent and sound adjustment to correct the flaws referenced above . . . Ms. Bulkley's studies show that my 9.35 [percent] recommended [ROE] for VAWC is more reasonable and consistent with the current capital market environment."[465]

Regarding revenue spread, Mr. Gorman expressed concern that VAWC proposed an overall bill decrease for Eastern district customers and an increase above cost of service for industrial potable customers.[466] He proposed that Eastern district customers receive no change in revenues and the increase for industrial potable customers be limited to the cost of service.[467]

For CCOSS, Mr. Gorman raised issues concerning: (i) the allocation of water pumping costs between potable and non-potable service; and (ii) VAWC's maximum day and maximum hour peaking factors by customer class.[468] He recommended "combining potable and non-potable [w]ater [p]umping costs and allocating them across both potable and non-potable customers using Factor 3." Mr. Gorman maintained the water pumping costs are associated with pumping raw water and is designed to meet the combined peak and base requirements of potable and non-potable customers.[469] He argued: "it is not necessary to classify these costs as potable or non-potable prior to allocating them across customer classes in the CCOSS."[470]

As for customer class peaking factors, Mr. Gorman contended VAWC failed to support the Weekly Usage Adjustments used to develop each class's peaking factors.[471] He compared the Weekly Usage Adjustments for each class used in this case and the Company's prior case:[472]

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[464] *Id.* at 74.
[465] *Id.*
[466] *Id.* at 99.
[467] *Id.*
[468] *Id.* at 101-02.
[469] *Id.* at 104.
[470] *Id.*
[471] *Id.* at 105.
[472] *Id.* at 106.

Class	Current Weekly Usage Adjustments	Prior Weekly Usage Adjustments
Residential	1.15	1.20
Commercial	1.15	1.10
Industrial	1.10	1.10

Because the Company is unable to explain or support the change in Weekly Usage Adjustments, Mr. Gorman recommended the Company "continue using the same adjustment factors from the last case until better and more accurate information is available."[473]

Mr. Gorman asserted the distribution multiplier of 0.13 was unreasonable because some of the customers the Company counts as served by distribution mains are served by transmission mains.[474] Based on the Company's response to Committee Data Request #1-043, he calculated a distribution multiplier of 0.096.[475] Mr. Gorman recalculated the CCOSS and presented the following comparison:[476]

Description	Revenue at Current Rates ($)	VAWC Increase to Reach Cost of Service $	VAWC Increase to Reach Cost of Service %	Committee Increase to Reach Cost of Service $	Committee Increase to Reach Cost of Service %
Residential	19,457,819	4,330,362	22.3	4,851,061	24.9
Commercial	12,901,878	4,908,536	38.0	4,906,722	38.0
Ind. Potable	4,143,827	946,449	22.8	949,862	22.9
Ind. Non-Potable	4,777,474	1,380,532	28.9	858,233	18.0
Total	**41,280,999**	**11,565,879**	**28.0**	**11,565,879**	**28.0**

Based on these results, Mr. Gorman recommended bringing each class to cost of service.[477]

Mr. Gorman opposed VAWC's proposal for two-thirds of the PWS to be billed to all potable customers.[478] He maintained that the Company's proposal does not support CTP, and that the Commission did not decide the issue in its *2018 Rate Order*.[479]

Except for the Eastern district, Mr. Gorman recommended a 9.5 percent increase in meter charges for all meters larger than one inch.[480] He recommended reducing VAWC's proposed

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473 *Id.* at 107-08.
474 *Id.* at 109.
475 *Id.* at 110.
476 *Id.* at 111.
477 *Id.*
478 *Id.* at 112-14.
479 *Id.* at 114-15.
480 *Id.* at 118.

reduction to the meter charges for 5/8-inch, ¾-inch, and one-inch meters by 52 percent for the Eastern district.[481]

In addition, Mr. Gorman opposed the proposal to move industrial potable customers to a two-block rate structure from the current six-block rate structure.[482] He contended the two-block structure would fail to provide accurate price signals and result in large industrial customers subsidizing smaller customers.[483] Mr. Gorman recommended an equal percentage increase across the six industrial potable volumetric blocks.[484]

Mr. Gorman objected to proposed rates for non-potable industrial customers.[485] Instead of an increase of about 19 percent for small non-potable customers and an increase of 32 percent for large non-potable customers, he recommended the same percentage increase be applied to both groups of customers.[486] Because VAWC failed to provide details of the delivery infrastructure for non-potable service, Mr. Gorman asked the Commission to direct the Company to provide such detail in its next rate case.[487]

Mr. Gorman opposed the Company's proposed RSM.[488] He took the position that customer rates should change only when the Company's cost of service has changed.[489]

Finally, Mr. Gorman testified that the Company's proposed Uncollectibles ARAC is unreasonable.[490]

Consumer Counsel Direct Testimony

On July 19, 2022, Consumer Counsel filed the direct testimony and exhibits of Ralph C. Smith, CPA, Senior Regulatory Consultant for Larkin & Associates, PLLC, Certified Public Accountants. Mr. Smith's testimony is summarized below.

Ralph C. Smith, CPA, addressed the following aspects of VAWC's Application:

- Impact on the revenue requirement of using a different return on equity;

- [COVID-19] deferrals – use of May 31, 2022, balance which reflects updated amounts and the Company's application of

[481] *Id.*
[482] *Id.*
[483] *Id.* at 118-19.
[484] *Id.* at 120.
[485] *Id.* at 121.
[486] *Id.* at 121-22.
[487] *Id.* at 121.
[488] *Id.* at 123.
[489] *Id.*
[490] *Id.* at 126.

[ARPA] funds, removal of foregone late fee revenue, removal of interest expense resulting from an affiliated Company's [T]erm [L]oan pursuant to which no cash was provided to VAWC, uncollectibles, and expense savings for travel and meetings being lower than budgeted levels as an offset to other [COVID-19] deferrals;

- Using a different estimate for declining residential per customer usage impact on water sales and revenues at current rates than VAWC has proposed, and related impacts on operating expenses such as purchased power expense and chemicals expense;

- VAWC's proposed [RSM]; and

- VAWC's proposal for an [U]ncollectibles [A]utomatic [R]ate [A]djustment [C]lause.[491]

To demonstrate the revenue requirement impact of ROE, Mr. Smith used the ROE established for WWISC purposes of 9.60 percent, along with VAWC's proposed capital structure and proposed cost of debt. He calculated that reducing the ROE from the Company's proposed 10.90 percent to 9.60 percent would reduce revenue requirements by approximately $2.0 million.[492] He also calculated that each 10-basis point change in ROE has a revenue requirement impact of approximately $153,700.[493]

Mr. Smith cited to the Commission's *COVID Regulatory Asset Order* and stressed the deferral was solely for accounting purposes and has no ratemaking impact.[494] He described VAWC's COVID-19 regulatory asset, which totaled $1,001,873 as of September 30, 2021.[495] Mr. Smith further noted that VAWC seeks to amortize this amount over three years, or $310,558 annually.[496] However, he advised that VAWC does not reflect the offset for ARPA funding the Company received in January 2022.[497] Thus, Mr. Smith proposed using the COVID-19 regulatory asset balance as of May 31, 2022, of $688,589, which includes ARPA funds.[498] He adjusted the COVID-19 uncollectibles expense deferral to reflect the net credit amount of $347,691 as of May 31, 2022.[499] Mr. Smith updated deferred incremental costs related to

[491] Exhibit No. 27, at 4-5.
[492] *Id.* at 6.
[493] *Id.* at 7.
[494] *Id.* at 8-9.
[495] *Id.* at 9.
[496] *Id.* at 10.
[497] *Id.* at 12.
[498] *Id.* at 12-13.
[499] *Id.* at 15.

COVID-19 to reflect $332,338 as of May 31, 2022.[500] He also updated incremental cost savings associated with COVID-19 of $294,040 as of May 31, 2022.[501]

Mr. Smith took issue with the inclusion of a *de minimis* $200 reconnection fee, and with VAWC's proposal to include $731,498 for late fee revenue in its COVID-19 regulatory asset as of September 30, 2021.[502] He stated the COVID-19 regulatory asset balance as of May 31, 2022, included lost late fee revenue of $843,650.[503] Mr. Smith referred to communications provided by VAWC to its customers that the Company voluntarily suspended late payment fees.[504] He pointed out that the late fee revenue VAWC is now attempting to collect was not billed to customers.[505] Mr. Smith testified:

> It is not reasonable to charge VAWC ratepayers for voluntarily foregone amounts of [l]ate [f]ee revenue. VAWC and its parent [c]ompany, [AWK], have clearly told VAWC's customers and the general public that the Company was voluntarily <u>not</u> charging late fees because it was the right thing to do. Attempting to defer and charge its customers for late fees that VAWC previously told its customers that it was voluntarily foregoing should not be permitted.[506]

Therefore, he eliminated the $843,650 amount for late fee revenue from the updated COVID-19 regulatory asset balance as of May 31, 2022.[507] Mr. Smith also contended that some of the foregone late fee revenue may be deemed recovered based on an earnings test for those periods.[508]

Mr. Smith testified VAWC received no cash from the Term Loan taken by AWCC related to COVID-19.[509] Because the Term Loan was not used by VAWC, he proposed an adjustment to remove the $154,132 of interest allocated to VAWC and included in its COVID-19 regulatory asset.[510] Mr. Smith noted AWK did not reduce its dividends to shareholders and was able to raise $1.736 billion in debt capital and lower cost of long-term debt.[511]

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[500] *Id.* at 17.
[501] *Id.* at 18.
[502] *Id.* at 19-20.
[503] *Id.* at 20.
[504] *Id.* at 21-22.
[505] *Id.* at 22.
[506] *Id.* at 22-23.
[507] *Id.* at 23.
[508] *Id.* at 23-24.
[509] *Id.* at 25.
[510] *Id.* at 25-26.
[511] *Id.* at 26-27.

In summary, for the COVID-19 deferral and related amortization, Mr. Smith reduced the amortization expense claimed by the Company by $406,463.[512]

Regarding declining residential usage, Mr. Smith disagreed with the use of only 66 months of data rather than 120 months as used in its regression analysis for commercial customers.[513] He maintained the Company has 120 months of data for residential customers.[514] Mr. Smith contended use of 120 months of data for residential customers produces a usage decline of 463 gallons per residential customer per year instead of the Company's usage decline of 1,076 gallons per residential customer per year.[515] He calculated this change in usage decline would increase Rate Year revenue for water operations at current rates by $305,247 over the Company's amount.[516] Mr. Smith calculated a similar adjustment for wastewater operations to increase Rate Year at current rates by $117,549 over VAWC's amount.[517]

Consistent with the adjustment to increase Rate Year revenues, Mr. Smith adjusted purchased power costs by $5,325 and chemical costs by $1,590.[518]

Mr. Smith opposed VAWC's proposed RSM and recommended it be rejected for the following reasons:

- The proposed RSM would lock in a revenue stream that would inure to the benefit of the Company's investors.

- The risk associated with fluctuations in water sales as revenue levels between rate cases would shift from the Company's investors to ratepayers.

- The Company has not demonstrated that the lack of an RSM is a major obstacle to the promotion of water efficiency. The Company has been able to implement methods to improve water efficiency without an RSM.

- The proposed RSM could provide a disincentive to ratepayers to undertake water conservation efforts because they would be required to pay for water they did not use.

- If the proposed RSM was implemented and if revenues decreased as a result of a downturn in the economy, ratepayers would be required to make up the resultant shortfall in

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[512] *Id.* at 29.
[513] *Id.* at 31.
[514] *Id.*
[515] *Id.* at 33.
[516] *Id.* at 34.
[517] *Id.*
[518] *Id.* at 34-35.

revenues. Under traditional ratemaking, utilities bear some of the risks of such economic downturns, as is the case with many other types of business and industries.

- Decreased sales associated with a downturn in the economy have nothing to do with water efficiency.

- Changes in usage that were created by the weather have nothing to do with VAWC's water efficiency performance.

- The Company has not proposed to reduce its equity return to reflect the reductions in risk associated with implementation of an RSM.[519]

Regarding the Company's proposed Uncollectibles ARAC, Mr. Smith advised this would also shift risk away from investors onto customers and should be rejected.[520]

Consumer Counsel Supplemental Testimony

On August 16, 2022, Consumer Counsel filed the supplemental testimony of Ralph C. Smith. Mr. Smith's supplemental testimony is summarized below.

Ralph C. Smith, CPA, addressed the supplemental testimony of Company witness Grace concerning updates to VAWC's forecasted pension expense and forecasted OPEB expense.[521] Mr. Smith noted that the updated estimates presented by Mr. Grace are estimates for the calendar year 2023 and not the Rate Year, which ends on April 30, 2023.[522] Mr. Smith calculated that the Company's pension expense estimate should be reduced by $387,808, and the OPEB expense estimate should be reduced by $41,835, to limit the increased estimates to the end of the Rate Year.[523]

Mr. Smith pointed out that the Company's new estimates for pension and OPEB expenses are not based on final actuarial reports by its actuary, WTW, and is not part of the normal scope of work for the actuarial services provided to AWWSC.[524] He expressed concern regarding the reliability of the "out of scope" estimates and whether focusing heavily on the first half of 2022, a period of historically poor stock and bond performance, skews or overstates results.[525]

Mr. Smith reported that the discount rates used in WTW's May 2022 forecast were:[526]

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[519] *Id.* at 38-39.
[520] *Id.* at 41-42.
[521] Exhibit No. 28, at 1.
[522] *Id.* at 4.
[523] *Id.*
[524] *Id.* at 5.
[525] *Id.* at 6-7.
[526] *Id.* at 7.

	2022	2023
Defined Benefit Pension Plan	2.94%	4.54%
OPEB Plan	2.90%	4.57%

Mr. Smith questioned differences in growth in discount rates and faulted VAWC for failing to conduct any sensitivity analysis.[527] In addition, Mr. Smith contended that the Company's estimates fail to consider increases in interest rate hikes that have occurred in June and July.[528]

Mr. Smith recommended placeholder amounts for pension and OPEB expense amounts based on eight months of 2022, and four months of 2023, with these amounts to be further adjusted "once information about the impact of using a higher discount rate is obtained from VAWC and can be reviewed."[529]

Staff Direct Testimony

On August 16, 2022, Staff filed the direct testimony and exhibits of Daniel M. Long, Principal Utility Specialist with the Commission's Division of Utility Accounting and Finance ("UAF"); Phillip M. Gereaux, Principal Utility Specialist for UAF; Edward Kaufman, Principal Utility Specialist for UAF; and Marc A. Tufaro, Principal Utilities Analyst in the Commission's Division of Public Utility Regulation. A summary of the direct testimony of each witness is provided below.

Daniel M. Long addressed the following topics:

1. the Company's Earning's Test ("ET") analysis for the [Test Year], and Staff's recommendations;

2. Staff's recommendations related to the 2020 [AIF] ET,[530] 2019 AIF[531] ET, and Alexandria [WWISC] ET ("Alexandria ET");[532]

[527] *Id.* at 8.
[528] *Id.* at 9.
[529] *Id.* at 11.
[530] See *Application of Virginia-American Water Company, For an Annual Informational Filing*, Case No. PUR-2020-00249 (filed Jan. 5, 2021) (footnote in original).
[531] See *Application of Virginia-American Water Company, For an Annual Informational Filing*, Case No. PUR-2019-00176 (filed Jan. 5, 2021) (footnote in original).
[532] The Company filed the Alexandria ET in the 2019 AIF docket, Case No PUR-2019-00176, on July 29, 2021. The Commission directed the 2019 and 2020 AIF cases to be addressed as part of the instant base rate case. See *Application of Virginia-American Water Company, For an Annual Informational Filing*, Case No. PUR-2019-00176, Doc. Con. Cen. No. 220310080, Order (March 3, 2022) (footnote in original).

3. Staff's Rate Year analysis and recommended base rate revenue increase of $5,934,647 for water operations and $2,301,436 for wastewater operations;

4. Staff's Rate Year adjustments, including those pertaining to revenues, service company costs, O&M expenses, and the [l]ead/[l]ag study; and

5. The Company's proposed Uncollectibles [ARAC].[533]

Mr. Long offered the following findings and recommendations:

1. The Commission should find reasonable, Staff's proposed adjustments to the Rate Year Analysis, and authorize a total base rate revenue increase for water operations of $5,934,647 and a total base rate revenue increase for wastewater operations of $2,301,436; based on the 9.20 [percent] mid-point of Staff witness Kaufman's [ROE] range.

2. The Commission should direct the Company to expeditiously refund Alexandria ratepayers $419,803 of WWISC collections, with interest, due to the Company's over-earnings in the Alexandria [ET], as recommended in Staff's Supplemental Report in [the AIF Proceedings].[534] . . . .

3. The Commission should direct the Company to write off the entire book balance of regulatory assets as of June 30, 2020, as recommended in Staff's Supplemental Report in [the AIF Proceedings].[535] . . . .

4. The Commission should approve Staff's proposed regulatory accounting adjustments to operating expenses, income taxes, and cash working capital in the [Test Year ET] analysis.

5. The Commission should deny the Company's proposed Uncollectibles [ARAC].

6. The Commission should accept Staff's proposed adjustments to the Rate Year Analysis to remove rate base and operations and

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[533] Exhibit No. 25, at 5.

[534] *See Id.* at Appendix D at 76-77. Note that Staff revises the recommended refund amount, as explained in Mr. Long's testimony (footnote in original).

[535] *See Id.* at Appendix D at 77 (footnote in original).

maintenance items pertaining to an outage that occurred in the Hopewell [d]istrict during the Test Year.[536]

ET Analysis

Mr. Long described an ET to be a historical measurement of the Company's ROE based on "per books revenues, expenses, and average rate base, with limited adjustments to reflect earnings of a regulatory accounting basis."[537] He advised in this proceeding the ET "is to evaluate whether regulatory assets on the Company's books have been recovered more quickly than anticipated."[538] Mr. Long confirmed this case involves four ETs: (1) the Test Year ET; (2) the 2020 AIF ET; (3) 2019 AIF ET; and (4) Alexandria ET.[539] He provided Staff's recommendations regarding the four ETs as follows:

1. The Company's COVID-19 [d]eferral regulatory asset was subject to evaluation in the [Test Year] ET to determine whether any write-offs would be necessary.
2. Staff's [Test Year] ET analysis for the combined water and wastewater operations resulted in a 9.39 [percent] ROE, which is below the 9.6 [percent] ROE to be used for [ET] purposes per the stipulation in the [*2018 Rate Order*]. Thus, Staff does not recommend any write-offs of the COVID-19 deferral for the [Test Year] ET.
3. The Commission should approve Staff's proposed regulatory accounting adjustments to operating expenses, income taxes, and cash working capital in the [Test Year] ET analysis.
4. The Company had the following regulatory assets for evaluation in the 2020 AIF ET:
    - Depreciation Reserve Deficiency
    - [OPEB] Deferral
    - COVID-19 Deferral
5. Staff recommends that the above regulatory assets as of June 30, 2020, totaling $528,742, be written off entirely.
6. Pertaining to the 2019 AIF ET, Staff recommends no action at this time.
7. Pertaining to the Alexandria ET, Staff recommends that $419,803 of WWISC collections, with interest, be expeditiously refunded to Alexandria ratepayers. This recommendation is independent of Staff's other ET recommendations and represents money that should be refunded to Alexandria ratepayers as soon as practicable.[540]

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[536] *Id.* at 5-6.
[537] *Id.* at 6.
[538] *Id.*
[539] *Id.* at 7.
[540] *Id.* at 7-8 (footnote omitted).

Regarding the Test Year ET, Mr. Long stated Staff calculated a total Company earned ROE of 9.39 percent, as compared to VAWC's calculated earned ROE of 8.97 percent.[541] He noted that because both ROEs are below the stipulated 9.60 percent, "no action is required concerning the Company's COVID-19 deferral regulatory asset."[542] A summary of the differences are provided in the table below:[543]

Item	Staff Amt	VAWC Amt	Stated Reason
EADIT Amortization	$2,055,912	$2,092,030	Staff used updated actual amount
Amortization of OPEB Deferral	$-1,167		Staff treated the OPEB Deferral as written off before the beginning of the Test Year
Charitable Contributions, Donations, and Lobbying			Staff removed all three, VAWC only removed Charitable Contributions
Incentive Compensation Expense	-$46,232		Staff reduced expense to target levels
AWWSC Long-Term Incentive Compensation Expense	-$31,807		Staff reduced expense to target levels
Regulatory Costs	$143,705	$422,746	Staff reflects actual; VAWC includes amortization of deferred regulatory costs and a write-down of costs above an assumed authorized level

For the 2020 AIF ET, Mr. Long testified that Staff recommends the write-off of $528,742 comprised of a reserve deficiency of $362,630, OPEB deferral of $42,827, and COVID-19 deferral of $123,286.[544]

Regarding Alexandria ET, Mr. Long adjusted the WWISC refund to remove 100 percent of charitable contributions, donations, lobbying, and community relations expense.[545] Because he determined the Alexandria district earned 10.03 percent ROE for the 28-month WWISC period, Staff recommends refunds of $419,803.[546] Mr. Long noted adjusting for the refunds produces an ROE of 9.57 percent, which is above the weighted average benchmark for this period of 9.55 percent.[547]

[541] *Id.* at 9-10.
[542] *Id.* at 10.
[543] *Id.* at 10-12.
[544] *Id.* at 14.
[545] *Id.* at 17.
[546] *Id.* at 18.
[547] *Id.*

Rate Year Analysis

Mr. Long calculated a Rate Year ROE of 4.45 percent for water services and -0.98 percent for wastewater services, or a combined ROE of 3.62 percent.[548] He noted Staff used actual revenues and expenditures through March 31, 2022 ("Update Period").[549] Mr. Long reconciled Staff and the Company's originally requested revenue requirement as follows:[550]

Description	Water Operations	Wastewater Operations	Total Combined
Company's Prefiled Incremental Revenue Requirements	**11,565,880**	**2,751,397**	**14,317,277**
Reconciling Difference to Achieve 10.9% ROE	139,692	22,314	162,006
Staff's Proposed Capital Structure	(289,364)	(44,897)	(334,261)
Staff's Proposed [ROE]	(2,237,045)	(347,094)	(2,584,139)
Revenue Conversion Factor, Uncollectibles, & GRT Rates	73,401	(37,859)	35,543
Staff's Revenue Adjustments	(1,536,676)	(432,233)	(1,968,909)
Payroll, Benefits, Insurance, and Payroll Taxes	130,060	93,677	223,737
Service Company Adjustments	(332,735)	(18,005)	(350,740)
Other O&M Exp, D&A Exp, and TOTI Adjustments	(282,445)	17,114	(265,331)
Rate Base Adjustments (Other than for Hopewell Outage)	(910,073)	298,954	(611,120)
Hopewell Outage Adjustments	(386,678)	(1,849)	(388,527)
Other Miscellaneous Differences	631	(82)	548
Staff's Proposed Incremental Revenue Requirements	**5,934,647**	**2,301,436**	**8,236,084**

Mr. Long outlined the revenue requirement impact of Staff's revenue adjustments:[551]

548 *Id.*

549 *Id.* at 19.

550 *Id.* at 20.

551 *Id.* at 21.

Description	Water Operations	Wastewater Operations	Total Combined
Staff's Exclusion of the Residential and Commercial Usage Normalization Adjustment	(836,477)	(369,596)	(1,206,072)
Staff's Exclusion of the Declining Usage Adjustment	(606,750)	(219,965)	(826,715)
Antennae Lease Adjustment	(1,393)	(714)	(2,108)
Staff's Exclusion of the Adjustment to Remove Unbilled Revenues	26,535	(27,098)	(563)
Late Payment Fee Adjustment	3,506	(3,138)	369
Reconnect Fee Adjustment	3,594	-	3,594
Waverly Base Revenues Adjustment	13,025	-	13,025
Customer Growth (Loss) Adjustment (which takes into account Revenues under Bond, Industrial usage normalization, and Silverlion adjustments	(138,716)	188,277	49,561
Total Adjustment Differences	**(1,536,676)**	**(432,233)**	**(1,968,909)**

Mr. Long testified that instead of VAWC's residential and commercial usage normalization, and declining usage adjustments, Staff used updated customer counts and consumption through March 2022 to calculate a Rate Year level of base revenues.[552] He maintained VAWC failed to establish its declining usage adjustment reasonably predicts Rate Year usage.[553] Mr. Long compared water usage per customer ("UPC") for the Test Year with the UPC for the TME March 31, 2022, and reported residential UPC declined 3.5 percent, while commercial UPC increased 2.6 percent.[554] He asserted these results "are reflective of a post-pandemic environment."[555]

Mr. Long stated the difference in customer growth adjustments are that Staff used actual updated data through March 31, 2022, and included industrial customers in its adjustment.[556] He noted the differences in Waverly's revenue adjustment include, among other things, the elimination of an out-of-town premium for volumetric charges per the stipulation in that case.[557]

Regarding service company expense, Mr. Long updated billings to VAWC for the actual amounts for the twelve months ended March 31, 2022.[558] He also made the following Rate Year adjustments: (i) removed non-ratemaking and non-recurring charges; (ii) reallocated certain costs to reflect changes in the organization of AWWSC; (iii) annualized labor and labor related benefits based on the most recent billings and merit increases; (iv) reduced incentive

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552 *Id.*
553 *Id.* at 22.
554 *Id.* at 25.
555 *Id.* at 26.
556 *Id.* at 27.
557 *Id.* at 28; See *Petition of Virginia-American Water Company, For authority to acquire utility assets at fair market value pursuant to the Utility Transfers Act, Va. Code § 56-88 et seq. and 20 VAC 5-210-10 et seq. and for a Certificate of Public Convenience and Necessity pursuant to the Utility Facilities Act, Va. Code § 56-265.3*, Case No. PUR-2021-00090, Doc. Con. Cen. No. 220420150, Final Order (Apr. 15, 2022).
558 Exhibit No. 25, at 28.

compensation to target levels; (v) annualized pension, depreciation, interest, and postage expenses based on the most recent billings; (vi) reflected the end of the Alton call center lease; (vii) increased pension and OPEB expense; and (viii) increased allocations to VAWC to reflect the purchase of the Waverly system.[559] Mr. Long explained Staff did not include projected labor increases or generalized inflation for service company billings due to the unpredictable nature of AWWSC billings each year.[560]

Mr. Long recommended that "the Company and its affiliates continue to track any future tax credits received and other offsets and/or factors that impact [One Water Street's ("OWS")] net book cost."[561] He confirmed VAWC was charged the lower of cost or market for costs related to OWS.[562]

As for other O&M expense adjustments, Mr. Long provided the following summary:[563]

Adjustment	Difference from Company	Driver of Difference Between Staff and Company
Payroll Expense	$72,555	Staff's adjustment uses updated information; appropriately includes overtime for non-union hourly employees; includes an employee that was inadvertently excluded from the Company's adjustment; and adjusts the calculation of union and non-union going level wages.
Payroll Tax Expense	($26,889)	Staff's adjustment uses more updated information, including new payroll tax limits effective for 2022, and corrects for an error in the Company's adjustment where overtime wages were included twice in calculating payroll tax.
APP Expense	$14,248	Staff's adjustment to APP expense uses updated actual employee data, 2022 APP rates, and a jurisdictional factor based on the Company's APP accounts.
Group Insurance Expense and 401K, DCP, ESPP and VEBA[564] Expense	($50,880)	Staff's adjustments, similar to payroll, use updated information and remove the VEBA benefit that was included in the non-union line in the Company's benefits adjustment.
Pension and OPEB Expense Adjustments	($542,372)	Staff's adjustment allocates the 2022 and 2023 expense to align with the Rate Year. This is in contrast to the Company's supplemental pension and

[559] *Id.* at 29.
[560] *Id.* at 30.
[561] *Id.* at 32.
[562] *Id.* at 31-32.
[563] *Id.* at 33-34 (footnotes omitted).
[564] Voluntary Employees Beneficiary Association ("VEBA").

		OPEB adjustments, which solely use 2023 expense as a proxy for the Rate Year level.
Insurance Other than Group Expense	($19,823)	Staff's adjustment uses updated premiums and allocates all premiums other than property using its Rate Year labor expense. Staff's adjustment does not incorporate the Company's projected increase to premiums.
Uncollectibles Expense	($13,849)	Staff's adjustment uses a three-year average net charge-off rate through March 2020 and applies its fully adjusted Rate Year revenues.
O&M Unadjusted Expense: Inflation	($242,311)	Staff does not incorporate a broad, sweeping adjustment to reflect inflation to the Company's other O&M expenses that have not been adjusted elsewhere. Staff maintains that inflation is difficult to reasonably predict, and thus, leaving these expenses at a Test Year level is reasonable.
O&M Unadjusted Expense: Waverly	($52,112)	Staff does not incorporate an adjustment to increase the O&M expenses for Waverly that have not been adjusted elsewhere. The Company calculated a cost per customer for existing customers to estimate incremental Waverly expense; however, the Company has not analyzed how each of the other O&M expense categories will increase in the Rate Year due to the addition of Waverly customers. Thus, Staff maintains it is inappropriate to include this adjustment.
Account 820 – Amortization of Debt	($105,102)	Staff makes an adjustment to exclude other interest expense/(income), or Account 820 – amortization of debt, since Staff witness Gereaux includes it in his going forward capital structure and cost of capital.
Fuel and Purchased Power Expense	$131,891	Staff calculates its adjustment using updated expense through March 31, 2022, and incorporates an estimated increase in the Dominion Energy Virginia ("Dominion") fuel charge. Staff's total jurisdictional Rate Year adjustment increases expense by $164,120 and is approximately $132,000 higher than the Company's adjustment.
Chemicals Expense	$75,499	Staff calculates its adjustment using the most recently available chemical prices, which replaces the need for a projected price increase.
Hopewell Outage O&M	($339,633)	Staff includes an adjustment to remove O&M expense recorded during the Test Year related to a Hopewell outage. As this expense is unusual in nature and is not anticipated to occur during the Rate Year, Staff appropriately removes the O&M expense recorded during the Test Year.

Regarding the CWC component of Rate Base, Mr. Long testified that the differences between Staff and VAWC include:

1. Staff created a separate lead/lag category for uncollectible expense;

2. Staff updated the revenue lag for the going forward analysis to incorporate data from the period ending March 31, 2022; and

3. Staff updated the balance sheet analysis to reflect balances as of the 12 months ending March 31, 2022.[565]

Mr. Long outlined the differences between Utility Plant in Service ("UPIS"), CWIP, Accumulated Depreciation, Customer Advances, and Contributions in Aid of Construction ("CIAC") as shown below:[566]

Component	Staff	Company	Difference
UPIS/CWIP	$523,543,498	$526,728,844	$(3,185,345)
Accumulated Depreciation	$(158,347,487)	$(152,669,047)	$(5,678,440)
Customer Advances	$(2,835,622)	$(3,926,669)	$1,091,047
CIAC (net)	$(38,000,194)	$(36,726,721)	$(1,273,474)
Total	$324,360,195	$333,406,408	$(9,046,213)

Mr. Long stated both Staff and VAWC calculated rate base to reflect a projected 13-month average ended April 30, 2023.[567] He attributed the differences to Staff's use of actual amounts as of March 31, 2022, and "revised projected capital investment, depreciation, customer advances, and CIAC activity for April 1, 2022, through April 30, 2023."[568] In addition, Mr. Long explained that the Company used three-year averages to apply the same percentage to each division while Staff, consistent with Staff's methodology from prior cases, used a separate percentage for each district.[569]

For accumulated deferred income taxes ("ADIT"), Mr. Long advised the difference between the Company and Staff stemmed from Staff's use of actual ADIT balances as of March 31, 2022, and revised projections for April 1, 2022, through April 30, 2023.[570]

For the COVID-19 deferral amortization, Mr. Long confirmed Staff adjusted the COVID-19 deferral balance as of the end of the Test Year (*i.e.,* June 30, 2021), adjusted for Staff's write-off of the entire balance as of the end of June 30, 2020, based on the earnings test.[571] He took the position that it would be improper to amortize COVID-19 deferrals

[565] Exhibit No. 25, at 46.
[566] *Id.* at 47.
[567] *Id.*
[568] *Id.* at 48.
[569] *Id.*
[570] *Id.* at 49.
[571] *Id.* at 51.

accumulated after June 30, 2021, because such deferrals have not been subjected to an earnings test.[572]

Mr. Long opposed VAWC's proposed Uncollectibles ARAC.[573] He maintained "a standalone RAC for a single O&M expense item is unnecessary."[574] In addition, Mr. Long pointed out that the Company already has a method to recover incremental uncollectible expense through the COVID-19 deferral.[575]

Phillip M. Gereaux addressed capital structure and cost of capital for VAWC.[576] Mr. Gereaux contended: "[b]ecause [VAWC] obtains both its debt and equity capital from [AWK], Staff recommends the use of a consolidated [AWK] capital structure for ratemaking purposes."[577] He made the following findings and recommendations:

- I recommend the continued use of the consolidated [AWK] capital structure, as of March 31, 2022, to calculate the overall cost of capital for [VAWC].

- For purposes of this case, I conclude that [the] Company's analyses and recommendation to use a *projected* [VAWC] *stand-alone* capital structure should be rejected. An *actual* ratemaking capital structure for [AWK] more reasonably reflects the cost of capital that supports [VAWC's] rate base.

- My recommended capital structure, in conjunction with Staff witness Kaufman['s] recommended 9.20 [percent ROE], supports an overall weighted cost of capital of 5.957 [percent].[578]

Mr. Gereaux testified AWK is "the entity that directly accesses the capital market to raise all external debt and equity capital supplied to [VAWC]."[579] Based on Staff witness Kaufman's recommended ROE range of 8.700 percent to 9.700 percent, with its midpoint of 9.20 percent, and AWK's actual consolidated capital structure as of March 31, 2022, Mr. Gereaux provided Staff's recommended capital:[580]

[572] *Id.*
[573] *Id.* at 52.
[574] *Id.*
[575] *Id.* at 52-53.
[576] Exhibit No. 21, at 1.
[577] *Id.*
[578] *Id.* at 2-3.
[579] *Id.* at 3.
[580] *Id.* at 3-4.

Component	Consolidated Ratemaking Capital	Weight	Cost Rate	Weighted Cost
Short-Term Debt	$655,888,617	3.562%	0.252%	0.009%
Long-Term Debt	$10,286,000,211	55.858%	3.968%	2.217%
Preferred Stock	$2,679,645	0.015%	7.133%	0.001%
Common Equity	$7,460,338,509	40.513%	8.700% 9.200% 9.700%	3.525% 3.727% 3.930%
ITCs	$9,608,854	0.052%	5.958% 6.168% 6.378%	0.003% 0.003% 0.003%
Total	**$18,414,515,836**	**100.000%**		5.755% 5.957% 6.160%

Mr. Gereaux acknowledged the adoption of legislation for water and wastewater companies for cases filed on or after January 1, 2022, that requires the use of a stand-alone capital structure.[581] He noted that because VAWC filed its case on November 15, 2021, Staff continues to support the use of AWK's consolidated capital structure.[582]

Mr. Gereaux took the position that use of a projected capital structure is an estimate, reflecting assumptions and projections "subject to change until they are realized."[583] He maintained projected capital structures are not suitable for future earnings tests, which require an average capital structure and cost of capital based on the methodology approved in the prior rate case.[584] Mr. Gereaux cited to the Commission's *2010 Order*,[585] and contended the Commission found a "forecasted capital structure does not contain projections that 'reasonably can be predicted to occur during the rate year' . . . ."[586] He asserted the Commission has also rejected the use of projected interest rates for purposes of estimating a utility's ROE.[587] In addition, Mr. Gereaux argued that a projected capital structure is not suitable for earnings test purposes because the Commission's Rate Case Rules require an average capital structure and cost of capital for the test period based on the methodology approved in the last rate case.[588]

Mr. Gereaux maintained the use of AWK's capital structure has not impeded VAWC's growth or prevented it from raising capital from AWK.[589]

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581 *Id.* at 4; *See* § 56-235.2 of the Code.
582 *Id.*
583 *Id.* at 5.
584 *Id.* at 7; *See* 20 VAC 5-201-90.
585 *Application of Virginia-American Water Company, For an increase in rates,* Case No. PUE-2010-00001, 2011 S.C.C. Ann. Rep. 316 ("*2010 Order*").
586 Exhibit No. 21, at 6; *2010 Order* at 318.
587 Exhibit No. 21, at 6; *Application of Virginia Electric and Power Company, For the determination of the fair rate of return on common equity pursuant to § 56-585.1:1 C of the Code of Virginia,* Case No. PUR-2019-00050, 2019 S.C.C. Ann. Rep. 403.
588 *Id.* at 7; *See* 20 VAC 5-201-90.
589 *Id.* at 12-13.

Edward R. Kaufman made the following recommendations:

- A market [ROE] estimate of 9.20 [percent], the mid-point of my recommended range of 8.70 [percent] to 9.70 [percent], should be used to set rates in this proceeding based on the results of analyses from a [DCF] model in conjunction with two risk premium methods, including the [CAPM].

- My 9.20 [percent] [ROE] recommendation should be used in conjunction with the consolidated [AWK] capital structure, as recommended by Staff witness [Gereaux], to calculate [VAWC's] overall cost of capital.

- [VAWC's] models and recommendation rely on several elements, such as forecasted interest rates, and the sole use of forecasted earnings per share data to estimate growth, which have been repeatedly rejected by this Commission.[590]

Mr. Kaufman estimated VAWC's ROE based on an analysis of market data for AWK and a proxy group, including Essential Utilities, Inc., and relying upon a DCF model, CAPM, and the results from a risk premium study.[591] In addition to AWK, he selected the following six companies for his proxy group: American States Water, California Water, Essential Utilities, Middlesex Water, SJW Group, and York Water.[592] Mr. Kaufman noted Company witness Bulkley did not provide an analysis of AWK, but included the other six utilities in her proxy group.[593]

Mr. Kaufman provided the following summary of his ROE analysis:[594]

[590] Exhibit No. 23, at 4.
[591] *Id.* at 5-6, Attached Schedule 3.
[592] *Id.* at Attached Schedule 12.
[593] *Id.* at 6.
[594] *Id.* at 8.

	Low-End of Range	Mid-Point of Range	High-End of Range
DCF Analysis			
AWK	9.58%	10.07%	10.56%
Water Group	7.62%	8.11%	8.60%
Risk Premium – CAPM			
AWK		9.10%	
Water Group		8.48%	
Risk Premium – Staff Study (Ex Ante)		8.55%	
AWK Cost of Equity Estimate	9.00%		10.00%
Proxy Group ROE Estimate Range	8.00%		9.00%
Financial Risk Adjustment		0.40%	
Overall Adjusted Proxy Group ROE Estimate Range	8.40%		9.40%
VAWC ROE Estimate	8.70%	9.20%	9.70%

Mr. Kaufman acknowledged that long-term Treasury bond yields have increased from the lows of 2020 but maintained "it is critical to recognize long-term interest rates are still at historically low levels."[595]

Mr. Kaufman provided the following list of issues that contribute to the most significant differences between VAWC and Staff:

1. *Sole Reliance on EPS Growth Estimates:* The Company's DCF analysis relies exclusively on forecasted EPS growth, while Staff considers three projected growth rates to develop a long-term sustainable growth rate consistent with the assumptions of the DCF model. The Commission has . . . rejected the sole reliance on EPS growth estimates in previous cases.

2. *Projected Interest Rates:* The Company relies on projected interest rates in its CAPM and [ECAPM] analyses. The use of projected 30-Year Treasury Bonds would inflate Staff's CAPM Analysis by 77 basis points. The Commission has regularly rejected the use of projected interest rates.

3. *Overstated Market Risk Premium:* The Company's analysis relies on an unrealistically high estimated market risk premium. When evaluated through Staff's CAPM analysis, Ms. Bulkley's market risk premium increases the cost of equity by 151 to 272 basis points. The Commission has rejected the use of overstated market risk premiums.

[595] *Id.* at 9.

4. *ECAPM:* In addition to the traditional CAPM, the Company relies on the ECAPM. Use of the ECAPM is redundant and unnecessarily increases the results of the traditional CAPM. Based on Staff's analysis, the ECAPM result is 43 basis points higher than the traditional CAPM.

5. *High End Estimated ROE:* The Company's recommended 10.90 [percent] ROE is from the high end of its range of 9.90 to 11.00 [percent], which is 45 basis points above the midpoint of the range. In contrast, Staff's recommended ROE of 9.20 [percent] is from the midpoint of its range of 8.70 to 9.70 [percent].

6. *Asymmetrical Elimination of Low Cost of Equity Estimates:* The Company eliminates low end results in its DCF analyses. The Commission has also expressed concerns about the use of asymmetrical elimination of low ROEs.

7. *VAWC Proactive Capital:* The Company states the Commission's regulatory policies provide a disincentive to direct "proactive capital investment" to [VAWC] operations; however there is no supporting data in the Company's testimony regarding how [AWK] directs proactive capital investment.[596]

Regarding Staff's DCF analysis, Mr. Kaufman determined the estimated growth-rate range for each proxy company based principally on growth data for each company.[597] However, he noted he calculated and reviewed historical growth rates for each proxy company "because they reflect information readily available to investors and provide a reference check of each company's demonstrated ability to sustain growth in dividends over time."[598] Moreover, Mr. Kaufman disagreed with the Company's sole reliance on earnings per share ("EPS") growth, while ignoring available projected dividend growth rates.[599] He contended the Company's sole reliance on projected EPS growth creates an upward bias in VAWC's DCF analysis and causes the Company's CAPM analysis to be overstated.[600]

Mr. Kaufman based his Ex Ante Risk Premium ROE estimate of 8.55 percent on Staff's study of the change in the risk premium relative to interest rates over the study period of 1980 – 1993, which showed a one-percentage point change in interest rates corresponding to an inverse

[596] *Id.* at 11-12.
[597] *Id.* at 12, Attached Schedule 4.
[598] *Id.* at 13, n.7.
[599] *Id.* at 13.
[600] *Id.* at 13-14.

change of about 37 basis points in the risk premium.[601] He also used the current three-month average yield on 30-year Treasury bonds of 2.76 percent.[602]

In his CAPM, Mr. Kaufman began his calculation by adjusting the long-horizon historical market risk premium of 7.46 percent for the risk of each of his proxy companies based on their beta values.[603] He then added the result to the current risk free rate (*i.e.*, average yield on 30-year Treasury bonds of 2.76 percent) to produce a CAPM cost of equity for each proxy company, which ranged from 7.61 percent to 9.85 percent with an average of 8.48 percent.[604] Mr. Kaufman also provided a CAPM calculation for AWK of 9.10 percent.[605]

Mr. Kaufman disagreed with the projected interest rates used in the Company's CAPM analysis.[606] He argued the current yield "provides the best estimate available for the market's expectation regarding future interest rates."[607] Moreover, Mr. Kaufman maintained current yields incorporate publicly available projections.[608]

Mr. Kaufman also disagreed with the market risk premium used in the Company's CAPM, built on a single stage constant growth DCF based on the S&P 500.[609] He asserted such analysis is appropriate "for regulated, mature utility companies because they exhibit more stable growth relative to the broad market."[610] Mr. Kaufman testified: "[t]he use of a high expected return on the S&P 500 produces an excessive market risk premium."[611] He supported his lower market risk premium through the following sources that are well below the Company's estimated market risk premium of 9.44 percent:

- SBBI Long-term historical risk premium: 7.46%
- Ibbotson-Chen Supply Side Model: 6.22%
- Supply Side Model since 2003: less than 6.5%
- Kroll current market risk premium: 5.5%
- Kroll market risk premium since 2008: 5.0 to 6.0%[612]

Regarding Staff's recommended financial risk adjustment, Mr. Kaufman acknowledged AWK's lower equity ratio compared to its peers; and made a 40-basis point adjustment to the final ROE range of his proxy group to make an apples-to-apples comparison.[613]

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[601] *Id.* at 15-16, Attached Schedule 7, Appendix B at 3.
[602] *Id.* at 16.
[603] *Id.*
[604] *Id.*; Attached Schedule 9.
[605] *Id.*; Attached Schedule 8.
[606] *Id.* at 17.
[607] *Id.*
[608] *Id.*
[609] *Id.* at 18.
[610] *Id.*
[611] *Id.*
[612] *Id.* at 19.
[613] *Id.* at 20.

As a check on Staff's results, Mr. Kaufman considered: (i) the estimate of 9.38 percent for United States equity returns by the SBBI 2022 Yearbook; and (ii) the estimate of 9.00 percent for base United States ROE by Kroll published in June 2022.[614] Mr. Kaufman contended these observations for the United States market as a whole, which should be higher than less risky utilities, validate the reasonableness of Staff's ROE estimate for VAWC.[615]

Mr. Kaufman advised that if the Commission were to adopt either or both of the Company's proposed RSM or Uncollectibles ARAC, this would shift risk between utility investors and utility ratepayers and would likely justify a lower authorized ROE.[616]

Marc A. Tufaro addressed: (i) the Company's CCOSS; (ii) the Company's continued movement towards CTP; and (iii) the Company's proposal for RSM.[617]

Mr. Tufaro accepted the CCOSS filed by VAWC and found "the Company's CCOSS is reasonable and should be used in allocating the cost of service in the instant case."[618] He pointed out the Company's CCOSS is consistent with the CCOSS adopted by the *2018 Rate Order*, and was used to develop the first step towards CTP.[619] Mr. Tufaro advised that the partial stipulation adopted by the *2018 Rate Order* "was implicitly predicated on the revenue allocation proposed by the Company . . . ."[620] He asserted the allocation of revenues should be consistent during all three cases of the CTP.[621] Therefore, Mr. Tufaro also accepted the Company's revenue allocation.[622]

Mr. Tufaro recommended VAWC maintain its current customer charges for the Alexandria, Hopewell, and Prince William districts; and did not object to the Company's proposal to lower the fixed monthly charge to $30.00 for the Eastern district.[623] Regarding VAWC's proposed volumetric rates, he contended they are a direct function of movement towards CTP and appear consistent with the Commission's *2018 Rate Order*.[624]

As for VAWC's wastewater rates, Mr. Tufaro noted that since the Company only provides wastewater service in the Prince William district, there are no CTP issues.[625] He agreed with VAWC's proposal to apply the increase to the flat volumetric charge.[626]

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614 *Id.* at 21-22.
615 *Id.* at 22.
616 *Id.* at 22-23.
617 Exhibit No. 24, at 1.
618 *Id.* at 12.
619 *Id.*
620 *Id.* at 16.
621 *Id.*
622 *Id.*
623 *Id.* at 17.
624 *Id.* at 18.
625 *Id.* at 19.
626 *Id.*

Mr. Tufaro supported VAWC's proposal concerning the PWS which he found to be consistent with the Commission's *2018 Rate Order* and another one-third movement towards CTP.[627]

Mr. Tufaro opposed VAWC's proposed RSM and cited to language in the Hearing Examiner's report adopted in the Commission's *2015 Rate Order* that such a proposal is not in the public interest.[628] Moreover, he opposed VAWC's proposed implementation methodology, which would permit the Company to increase expenses subject to only an after-the-fact sixty-day review, without the benefit of possible offsetting savings of the Company's expenditures elsewhere.[629] Mr. Tufaro asserted: "[a]llowing the Company to independently adjust [production] expenses without review, would provide the Company no incentive to limit the production expense items."[630] While he acknowledged the Company would be indifferent to the sale of the commodity, Mr. Tufaro argued the benefits for investors are clear but benefits to customers are "unknown & uncertain at best."[631] He also maintained "[t]he RSM as proposed could provide a disincentive to ratepayers to undertake water conservation efforts because they would be required to pay for water regardless of whether they used it or not."[632]

VAWC Rebuttal Testimony

On September 6, 2022, VAWC filed the rebuttal testimony of Casey Allen; Kristina E. McGee, P.E.; Harold Walker, III; Charles B. Rea; James S. Pellock; Thomas O'Drain, Senior Manager, Procurement – National Category Management for AWWSC; John M. Watkins; Scott T. Grace; John S. Tomac; and Ann E. Bulkley. The rebuttal testimony of each witness is summarized below.

Casey Allen addressed: (i) Staff's exclusion of unadjusted O&M expense for the Waverly system; (ii) Staff's exclusion of VAWC's pro forma usage adjustment and expense increase for water treatment chemical, sodium hypochlorite; and (iii) the contention of Alexandria witness Kreps that the proposed RSM may reduce VAWC's incentive to perform maintenance and ensure meter accuracy.[633]

Mr. Allen stated VAWC calculated the Waverly unadjusted O&M expense based on the per-customer amount for existing Company customers and multiplying that amount by the number of new Waverly customers.[634] He defended this calculation as a conservative,

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[627] *Id.* at 20-21.
[628] *Id* at 22-23; See *Application of Virginia-American Water Company, For a general increase in rates,* Case No. PUE-2015-00097, Doc. Con. Cen. No. 161140065, Report of Howard P. Anderson, Jr., Hearing Examiner (Nov. 29, 2016).
[629] Exhibit No. 24, at 26.
[630] *Id.*
[631] *Id.* at 27.
[632] *Id.* at 28.
[633] Exhibit No. 29, at 1-2.
[634] *Id.* at 2.

reasonable approach until the Company understands the actual costs to operate the Waverly system.[635] Mr. Allen asserted that actual costs of operating and maintaining Waverly exceed those of VAWC's existing system, including repair of "a noticeably higher number of leaks . . ."[636]

Mr. Allen testified in June 2021, the Company transitioned from the use of chlorine gas and ammonia gas at the Hopewell water treatment plant to sodium hypochlorite and liquid ammonium sulfate.[637] He disagreed with Staff's modification to exclude adjustments to reflect the amount of sodium hypochlorite reasonably predicted to be used during the Rate Year.[638]

Mr. Allen disagreed with the testimony of Mr. Kreps that the RSM may reduce VAWC's incentive to perform meter maintenance and ensure meter accuracy.[639] Mr. Allen stated the Company has incentives to perform meter maintenance and ensure meter accuracy including: (i) changing meter technology; (ii) Virginia Department of Environmental Quality ("DEQ") regulations; and (iii) a meter reading exception process, which is a part of monthly reading and billing activities.[640]

Kristina E. McGee, P.E., updated VAWC's capital investments.[641] Ms. McGee advised the Company has extended the scheduled in-service date of June 2024 for the Hopewell low service intake replacement project, due to DEQ and other agency permitting.[642] Thus, she stated the Company "no longer expects to incur the entirety of the $12.6 million in spend[ing] estimated through the [R]ate [Y]ear."[643] However, Ms. McGee affirmed "[t]he Company is committed to maintaining its capital investment as profiled in its initial filing as updated through March 2022 and has taken actions to do so."[644]

Harold Walker, III, responded to the testimony concerning working capital allowances of Staff witness Long.[645] Mr. Walker disagreed with Mr. Long's recommended lead days for uncollectible expense of 493-days used for the earnings test, or 485-days, used for going-forward analysis recommendations.[646] Mr. Walker asserted such "lead days for uncollectibles expense are not plausible in the context of a lead-lag analysis."[647] He maintained uncollectible expense represents customers not paying for service and is more like a large revenue lag.[648] Mr. Walker

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[635] *Id.*
[636] *Id.* at 3.
[637] *Id.*
[638] *Id.* at 4.
[639] *Id.* at 5.
[640] *Id.*
[641] Exhibit No. 30, at 1.
[642] *Id.* at 1-2.
[643] *Id.* at 2.
[644] *Id.* at 3.
[645] Exhibit No. 31, at 1.
[646] *Id.* at 2.
[647] *Id.*
[648] *Id.* at 3.

recommended "a zero lead day be assigned for uncollectible accounts expense to recognize the full revenue lag related to this expense."[649] Mr. Walker calculated this change would increase Mr. Long's cash working capital by $463,905 for total Company earnings test results, and $336,707 for total Company going-forward analysis.[650]

Charles B. Rea addressed cost of service, rate design, declining use modeling, revenue requirement allocations, revenue adjustments and affordability.[651]

Cost of Service

Mr. Rea acknowledged that Staff witness Tufaro generally supports the Company's CCOSS.[652] He addressed the following issues raised by Alexandria witness Kreps and Committee witness Gorman: (i) allocation of transmission and distribution mains to industrial customers; (ii) determination of peaking factors; and (iii) potable vs. non-potable allocation of water pumping costs.[653]

For the allocation of distribution mains, Mr. Rea testified:

> The Company's proposed allocation of distribution cost to customer class is based on a Base/Extra capacity allocation factor that recognizes maximum hourly demand but multiplies the resulting allocation factor that results from that calculation by the percentage of sales for each class that happen at the distribution level, which the Company defines to be mains with a diameter of 8" or less.[654]

Mr. Rea disagreed with Mr. Kreps's concern that the Company unfairly singles out the industrial class for special treatment based on the characteristics of individual customers. Mr. Rea pointed out that the very small number of customers in the industrial class enables them to be analyzed to determine what level of sales is taken at different sizes of mains.[655] Mr. Rea disagreed with Mr. Kreps's recommendation to use the transmission allocator for the allocation of distribution costs because "a large majority of the usage for the industrial class is not served by distribution mains."[656]

Mr. Rea agreed with Mr. Gorman's proposed distribution multiplier of 0.096 in lieu of the 0.126 value used in VAWC's CCOSS.[657]

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649 *Id.* at 4.
650 *Id.* at 5-6.
651 Exhibit No. 37, at 1.
652 *Id.* at 3.
653 *Id.* at 3-4.
654 *Id.* at 4.
655 *Id.* at 6.
656 *Id.* at 7.
657 *Id.* at 8.

Regarding peaking factors, Mr. Rea maintained the Company's estimated peaking factors comport with standards outlined in the AWWA M1 Manual.[658] Nonetheless, Mr. Rea agreed with Mr. Kreps's recommendation to use an Hourly Usage Adjustment Factor ("HUA") of 1.45 for all classes as used in Case No. PUR-2018-00175.[659] Mr. Rea disagreed with Mr. Kreps's recommendation to set the Weekly Usage Adjustment Factor to 1.00 for all classes as this would indicate there is no difference in usage between weekdays and weekends for any customer class.[660] Mr. Rea disagreed with Mr. Gorman's recommendation to use the Weekly Usage Adjustment Factors from Case No. PUR-2018-00175 because the difference is slight and the changes are not material.[661]

For water pumping costs, Mr. Rea did not object to Mr. Gorman's recommendation to allocate water pumping cost across all potable and non-potable customers collectively using Factor 3.[662]

Rate Design

Mr. Rea disagreed with Committee witness Gorman's proposal to increase meter rates of 1" meter and above by 9.5 percent.[663] Mr. Rea maintained the CCOSS does not support increases in meter charges at this time.[664]

Mr. Rea disagreed with Mr. Gorman's recommendation to limit the Company's proposed reduction in meter charges for the Eastern district so that it receives no base rate change relative to current rates.[665] Mr. Rea contended "[a]ny movement to STP necessarily reduces some component of rate design for Eastern [d]istrict customers."[666]

Regarding Mr. Gorman's proposal to retain the six-block rate structure for Hopewell industrial potable customers, Mr. Rea did not oppose rebalancing rates between lower blocks and higher blocks in the industrial potable class to even out the impacts between smaller and larger customers.[667] However, Mr. Rea advised VAWC does not support keeping the six-block rate structure.[668] Mr. Rea stressed that once the revenue requirement is allocated to a class, debate over the rate structure is effectively a zero-sum game only for the customers within that class.[669]

[658] *Id.* at 9.
[659] *Id.* at 11.
[660] *Id.*
[661] *Id.* at 12.
[662] *Id.* at 13.
[663] *Id.* at 17.
[664] *Id.*
[665] *Id.*
[666] *Id.*
[667] *Id.*
[668] *Id.* at 18.
[669] *Id.* at 19.

Declining Usage Modeling

Mr. Rea noted Consumer Counsel witness Smith generally agrees with VAWC's methodology for estimating declining usage for residential and commercial customers, only taking issue with the Company's use of 66 months of sales data for residential customers, and recommending the use of 120 months of sales data as used for commercial customers.[670] On the other hand, Mr. Rea acknowledged Staff witness Long disagreed with VAWC's methodology for estimating declining usage, as well as adjustments for weather and COVID-19.[671]

Mr. Rea confirmed Mr. Smith's results using 120 months of sales data for residential customers.[672] However, Mr. Rea asserted the residential data prior to March 2016 has both monthly and quarterly billing data, which makes a model based on 120 months less reliable.[673]

Mr. Rea disagreed with Mr. Long that usage for the TME March 2022 is the best predicted value for the TME April 2023.[674] Mr. Rea asserted: "[t]his is pure conjecture on Mr. Long's part with no data or evidence to back it up."[675] Mr. Rea presented charts illustrating the downward trend in usage per residential and commercial customer and how those trends compare to Staff's recommendation.[676] For commercial usage, Mr. Rea recommended use of the weather adjusted value of 785,000 gallons per customer per year for TME July 2022 as the best available estimate of usage for the Rate Year.[677]

Revenue Requirement Allocation

Mr. Rea responded to the testimony of Staff witness Tufaro and Committee witness Gorman concerning revenue requirement allocation to customer classes.[678]

Mr. Rea stated Mr. Tufaro generally supported VAWC's allocation of revenues to customer classes; and recommended following the Company's methodology if Staff's lower revenue requirement is adopted.[679]

Mr. Rea disagreed with Mr. Gorman's approach for revenue allocation that limits increases to cost of service for certain favored groups.[680]

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[670] *Id.* at 21.
[671] *Id.* at 22.
[672] *Id.*
[673] *Id.* at 23-24.
[674] *Id.* at 25.
[675] *Id.* at 26.
[676] *Id.* at 28-30.
[677] *Id.* at 30-31.
[678] *Id.* at 32-36.
[679] *Id.* at 33.
[680] *Id.* at 35.

Revenue Adjustments

Mr. Rea disagreed with Staff witness Long's adjustments to VAWC's Rate Year revenues to: (i) use actual revenues and consumption for the TME March 2022 for the Rate Year; or (ii) include unbilled revenues in the calculations of Rate Year revenues.[681] Mr. Rea noted Staff's revenue calculations are not adjusted for weather, COVID-19, or any other usage anomalies.[682] Mr. Rea also disagreed with Mr. Long's customer growth adjustment which is based on customer growth from March 2021 through March 2022, while the Company uses the average rate of growth or decline for the period July 2018 through June 2021.[683]

Mr. Rea contended Mr. Long overstated revenues by including unbilled revenues for the current period, but failed to account for the reversal of the prior period unbilled revenues.[684] Mr. Rea testified the average billed days per customers for the TME June 30, 2021, or the TME March 31, 2022, is 365 days.[685] He stated including unbilled revenues adds an additional 20 days, which will overstate revenues if the service days outside the twelve-month period are not subtracted.[686] Mr. Rea maintained "[b]y including unbilled revenues, Mr. Long's calculation of Rate Year revenues is overstated by approximately $600,000."[687]

Affordability

Mr. Rea responded to the testimony of Alexandria witnesses Eger and Kreps concerning the affordability of the Company's proposed rate increase on the customers of Alexandria.[688] Mr. Rea faulted both witnesses for focusing on the increase in volumetric rates rather than the bill impacts.[689] He analyzed basic water service (*i.e.*, 40 gallons of water per household member per day) under the Company's present and proposed rates for residential customers in Alexandria and found:

> that when all rate elements are considered, including the reduction in PWS expected for customers in Alexandria, the actual dollar increases for most customers for basic water service are less than $10 per month and for more than half of the customers in Alexandria the increases are approximately $5 per month or less. This shows that despite the large percentage increase in the volumetric rate for Alexandria residential customers, the impact on the overall bills for these customers is much more modest.[690]

[681] *Id.* at 36.
[682] *Id.* at 37.
[683] *Id.* at 37-38.
[684] *Id.* at 39.
[685] *Id.*
[686] *Id.* at 39-40.
[687] *Id.* at 40.
[688] *Id.*
[689] *Id.* at 41.
[690] *Id.* at 43-45.

Mr. Rea concluded that basic water service under VAWC's proposed rates is and will continue to be affordable for the vast majority of the Company's residential customers, including single family customers taking service under residential rates and multifamily households taking service under commercial rates.[691]

James S. Pellock addressed Staff witness Long's recommendations for production costs, IOTG, donations, and unadjusted O&M.[692]

Mr. Pellock noted that adjustments to fuel and power, chemical and waste disposal expenses related to declining usage per customer should also be made if the Commission accepts the Company's declining use adjustment.[693] He advised VAWC accepts Staff's adjustments to fuel and purchased power expense and waste disposal expense, but opposes Mr. Long's adjustment to chemical expense.[694] Mr. Pellock updated chemical expense for the Rate Year to capture contractual chemical prices as of July 2022 and updated projections of future chemical prices for 2023.[695] He calculated the total updated expense is $2,373,478.[696] Mr. Pellock also testified that use of March 31, 2022, as a proxy for the Rate Year omitted 2.5 months of usage of sodium hypochlorite, equating to $64,000 of additional cost.[697]

Mr. Pellock disagreed with Mr. Long's complete exclusion of a 7 percent annual increase reasonably predicted to occur effective January 1, 2023, and recommended inclusion of 4/12 of the increase for the January through April 2023 period.[698] Mr. Pellock calculated the total jurisdictional Rate Year adjustment increases from Staff's $159,131 to approximately $181,782.[699]

In support of VAWC's charitable contributions and donations, Mr. Pellock testified the charitable contributions primarily relate to supporting local fire departments and environmental programs, while the donations relate to the funding of the Virginia Utility Assistance Program.[700]

Mr. Pellock disagreed with Mr. Long's elimination of VAWC's inflation adjustment to the Company's unadjusted O&M expenses.[701] Mr. Pellock contended "[a]n inflation adjustment is reasonable for these expenses because they can reasonably be expected to increase at a rate

[691] *Id.* at 46-47.
[692] Exhibit No. 32, at 1-2.
[693] *Id.* at 2.
[694] *Id.*
[695] *Id.* at 3.
[696] *Id.* at 4.
[697] *Id.*
[698] *Id.* at 5.
[699] *Id.* at 6.
[700] *Id.* at 7.
[701] *Id.* at 9.

greater than or equal to the rate of inflation."[702] Mr. Pellock also noted the Company's objection to Staff's rejection of the expected costs for the Waverly system.[703]

Thomas O'Drain addressed Staff's recommendations pertaining to VAWC's chemical expense.[704] Mr. O'Drain disagreed with Staff's use of actual chemical prices as of April 2022 as the prices for Rate Year chemicals.[705] He affirmed VAWC has 27 unique chemical, supplier, plant combinations that carry agreed upon prices, with 8 of these having annual agreements for 2022, and 19 with updated prices effective July 1, 2022, through December 31, 2022.[706] Mr. O'Drain maintained because of the volatility in chemical prices many suppliers are no longer willing to lock in chemical prices for the calendar year.[707] He pointed to transportation costs, supplier consolidation, energy costs, and demand for other products as reasons why prices have increased in 2022 and are expected to continue to increase in 2023.[708]

Mr. O'Drain stated VAWC's contractual prices at the start of 2022 increased 30 percent from 2021 and increased by 31 percent as of July 2022.[709] He contended: "[b]ased on current market trends and discussions with multiple suppliers, VAWC anticipates another increase above current pricing levels for 2023."[710] Mr. O'Drain testified that AWWSC supply chain division forecasts VAWC faces a 17 percent increase in chemical prices from 2022 to 2023.[711]

John M. Watkins addressed issues related to VAWC's proposed RSM, pension and OPEB expense.[712]

<u>RSM</u>

Mr. Watkins disagreed with Alexandria witness Eger's claims that changes in volume of water sold is not a major concern for water utilities because "[w]ater utilities rely heavily on variable revenues for collecting fixed costs."[713] He cited to a resolution adopted by the National Association of Regulatory Utility Commissioners ("NARUC") in 2013 that supports use of mechanisms such as an RSM.[714]

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[702] *Id.*
[703] *Id.* at 10.
[704] Exhibit No. 33, at 3.
[705] *Id.* at 4.
[706] *Id.* at 5.
[707] *Id.* at 5-6.
[708] *Id.* at 7-8.
[709] *Id.* at 9-10.
[710] *Id.* at 10.
[711] *Id.* at 11.
[712] Exhibit No. 35, at 1-2.
[713] *Id.* at 4.
[714] *Id.* at 4-6; Attached Exhibit JMW-2R.

Mr. Watkins responded to the testimony of Alexandria witness Kreps and Committee witness Gorman that VAWC has not demonstrated an RSM is necessary to recover its cost of service and earn a fair ROE, in part, by stating:

> VAWC's ability to recover its cost of service and earn its authorized rate of return is a result of several factors, including the actual costs it incurs (both capital and expenses), the rates set by the Commission in this case, and the extent that VAWC is able to collect the revenue requirement authorized by the Commission in this case.[715]

Regarding the testimony of Mr. Kreps, Mr. Gorman, and Consumer Counsel witness Smith that the RSM is not likely to incentivize or improve water efficiency, Mr. Watkins asserted they are unsupported suppositions.[716] He advised that the Company has implemented supply-side programs to improve water efficiency but maintained VAWC's rate structure creates disincentives to promote demand-side initiatives.[717]

Mr. Watkins disagreed with Mr. Gorman's claim that an RSM would eliminate economic incentives for customers to undertake conservation-related investments by noting even with a surcharge, customers who use less will pay less.[718] He supported the netting of revenues and production cost and pointed to other states that have adopted such mechanisms.[719]

Mr. Watkins confirmed Staff witness Tufaro's testimony that if an RSM had been in place, the surcharges would have been significantly higher than the credits.[720]

Mr. Watkins responded to arguments by Messrs. Tufaro, Kreps, and Smith that the RSM would shift risks for changes in revenue and production costs from the Company to its customers. He also responded to their concerns that the Company has not reflected this shift in risks in its requested ROE by stating that NARUC, and other regulatory bodies have recognized ratemaking approaches such as an RSM as an appropriate response to new risks in the water industry.[721]

Mr. Watkins disagreed with Mr. Kreps's recommendation that, if approved, the RSM should be a pilot program.[722] Mr. Watkins contended "there is ample evidence in this case and throughout the utility industry of the value of an RSM."[723]

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[715] *Id.* at 6.
[716] *Id.* at 7.
[717] *Id.*
[718] *Id.* at 9-10.
[719] *Id.* at 11-13.
[720] *Id.* at 13-14.
[721] *Id.* at 14.
[722] *Id.* at 15.
[723] *Id.*

Mr. Watkins argued both customers and investors benefit from an RSM because it is symmetrical.[724]

Pension and OPEBs

Mr. Watkins agreed with the mechanics of Staff's pension and OPEB calculation, but maintained Staff used an incorrect 2022 OPEB amount in its calculation.[725] He contended the expense associated with the union medical VEBA should be excluded to keep from overstating the credit to operating expense for the Rate Year.[726] Mr. Watkins calculated this change increases jurisdictional OPEB expense by $268,315.[727]

Mr. Watkins supported use of the WTW pension and OPEB expense projections for 2023, which were calculated in the normal course of business.[728] He maintained that the updates were the result of WTW updating all the inputs into the model.[729] Mr. Watkins testified pension and OPEB expense fluctuations are reasonably predicted to occur going forward, with significant fluctuations between 2022 and 2023.[730] He requested that the Company be permitted "to record any amounts above or below the amount authorized in rates to a regulatory asset or liability, as appropriate, from the effective dates of new rates in this proceeding until the Company's next base rate case."[731] Mr. Watkins asserted the pension and OPEB expense increase is extraordinary, with VAWC seeing extreme volatility in this expense, which is outside the Company's control.[732]

Scott T. Grace responded to Staff's recommendations concerning the 2020 AIF Earnings Test and the Alexandria Earnings Test.[733] Mr. Grace stated that based on the 2020 AIF, Staff recommends the write-off of: (i) a reserve deficiency of $362,630; (ii) OPEB deferral of $42,827; and (iii) COVID-19 deferral of $123,286.[734] He advised that VAWC agreed with Staff's write-off of the reserve deficiency and the OPEB deferral, but disagreed with Staff's stated COVID-19 deferral balance on June 30, 2020.[735] Mr. Grace testified that the Company updated its COVID-19 deferral balance as of June 30, 2020, to $82,943.[736]

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[724] *Id.* at 16.
[725] *Id.* at 18.
[726] *Id.* at 18-20.
[727] *Id.* at 21.
[728] *Id.* at 24.
[729] *Id.* at 25.
[730] *Id.* at 27.
[731] *Id.* at 28.
[732] *Id.* at 29.
[733] Exhibit No. 36, at 1.
[734] *Id.* at 2.
[735] *Id.*
[736] *Id.* at 3.

Regarding the Alexandria Earnings Test, Mr. Grace disagreed with Staff's recommendation that $419,803 of WWISC collections be refunded with interest.[737] He stated that VAWC's principal objection is that Staff's recommendation is not consistent with the Commission's *2015 Rate Order.*[738] Specifically, Mr. Grace quoted from the *2015 Rate Order* that "refunds should be made to ratepayers, with interest, to the extent WWISC collections result in annual earnings above the rate of return on common equity of 9.25 [percent]."[739] He equated "result in" to "the *cause of*" earnings to be above authorized.[740] Mr. Grace took the position that the first step in rate consolidations fully accounts for the "overearnings."[741]

In addition, Mr. Grace testified Staff's WWISC overearnings are for the 28-month period January 1, 2019, through April 30, 2021, which includes the 12-month period of May 2019 through April 2020, where VAWC had no WWISC collections.[742]

Mr. Grace argued: "Staff's approach, if accepted by the Commission, would eliminate the utility of the WWISC mechanism as a means to facilitate the accelerated infrastructure replacement it was designed to encourage."[743] He further warned: "if Staff's approach is adopted, it is difficult to imagine the circumstances in which any Company would choose to file a WWISC."[744]

John S. Tomac reconciled Staff and VAWC's rebuttal positions, on a total company basis, as follows:[745]

Revenue Requirement per Staff	$8,236,084
Revenue Requirement Effects of Company Adjustments	
<u>Adjustments to Capital Structure and Cost:</u>	
Adjustment to Capital Structure	104,444
Adjustment to Debt Costs	897,892
Adjustment to Cost of Equity	2,517,306
<u>Adjustment to Rate Base:</u>	
Adjustment to Cash Working Capital	30,504
<u>Adjustments to Revenue:</u>	
Adjustment to Residential Revenue	1,437,800
Adjustment to Commercial Revenue	13,309
Adjustment to Industrial Revenue	142,656
<u>Adjustments to Expenses:</u>	
Adjustment to Chemical Expense	582,881

[737] *Id.* at 3-4.
[738] *Id.* at 4-5.
[739] *Id.* at 5; *2015 Rate Order* at 291.
[740] *Id.* at 5 (emphasis in original).
[741] *Id.*
[742] *Id.* at 5-6.
[743] *Id.* at 9.
[744] *Id.* at 9-10.
[745] Exhibit No. 38, at Attached Exhibit JST-1R.

Adjustment to OPEB Expense	277,170
Adjustment to IOTG Expense	22,959
Adjustment to Donations Expense	13,819
Adjustment to Other Operating Expense for Inflation	249,980
Adjustment to Other Operating Expense for Waverly	53,921
Revenue Requirement per Company	$14,580,725

Regarding the COVID-19 regulatory asset, Mr. Grace agreed with Consumer Counsel witness Smith that the balance for incremental uncollectible expense, incremental direct costs and cost savings should be updated to as of May 31, 2022.[746] Mr. Grace disagreed with Mr. Smith's recommended disallowance of immaterial lost reconnect fees of $200 and asserted materiality should not be a consideration for individual components of the deferral.[747] Mr. Grace disagreed with Mr. Smith's recommendation to disallow voluntarily suspended late fees.[748] Mr. Grace acknowledged that initially the Company voluntarily waived late fees for customers, but complied with the Commission's *April 9th Order*,[749] which directed that "late payment fees shall not be assessed."[750] Mr. Grace disagreed with Mr. Smith's recommended disallowance on interest expense associated with the Term Loan, which Mr. Smith asserted was not used by VAWC.[751] Mr. Grace contended Mr. Smith ignores the issues during the early stages of COVID-19 "when access to commercial paper and sources of long-term financing were adversely impacted and called into question."[752] Mr. Grace testified VAWC benefited from the Term Loan because it provided additional liquidity during a difficult period.[753]

Mr. Grace continued to support establishment of the Uncollectibles ARAC and disagreed with Mr. Smith's contention that deferral mechanism constitutes single issue ratemaking and a shifting of risk from investors to customers.[754] Mr. Grace asserted the Uncollectibles ARAC protects "both customers and the Company from expected fluctuation in this expense."[755] Mr. Grace advised the Company's uncollectible expense has not returned to normal.[756]

Regarding tariff consolidation, Mr. Grace noted the opposition of Alexandria witness Eger and his contention that Alexandria customers are subsidizing VAWC's other districts.[757] Mr. Grace stated: "[o]ver time, consolidation of rates smooths out rate increases over all

[746] *Id.* at 5.
[747] *Id.* at 5-6.
[748] *Id.* at 6-7.
[749] *Commonwealth of Virginia, ex rel. State Corporation Commission, Ex Parte: Temporary Suspension of Tariff Requirements*, Case No. PUR-2020-00048, 2020 S.C.C. Ann. Rep. 467, Order Extending Suspension of Service Disconnections (Apr. 9, 2020) ("*April 9th Order*").
[750] Exhibit No. 38, at 6; *April 9th Order* at 468.
[751] *Id.* at 9.
[752] *Id.*
[753] *Id.* at 10.
[754] *Id.* at 12.
[755] *Id.*
[756] *Id.* at 13.
[757] *Id.* at 14.

districts."[758] Mr. Grace noted the eventual allocation of PWS among the districts will offset the rate base reallocation.[759] Mr. Grace disagreed with Mr. Eger that the consolidation of rates is not being phased in over a gradual period and that this case was filed one year after the prior rate case settlement.[760] Mr. Grace asserted there was a three-year period between the first and second phases, with interim rates becoming effective on May 1, 2019, for the first phase, and May 1, 2022, for this second phase.[761]

As for capital structure and short- and long-term interest rates, Mr. Grace confirmed the long-term debt of the company is 4.265 percent, as shown in his supplemental testimony, does not include any estimated amounts.[762] He continued to support use of a VAWC standalone capital structure and noted the equity ratio of the Staff's consolidated capital structure of 40.513 percent is similar to VAWC's standalone equity ratio of 40.75 percent.[763]

Mr. Grace disagreed with Staff's calculation of the short-term interest rate using a three-month average of the daily balance of consolidated short-term debt for AWK for the period ended March 31, 2022.[764] Mr. Grace argued Staff "ignores the realities of the current economic conditions that are now taking place and will be reflected during the [R]ate [Y]ear."[765] Mr. Grace testified "interest rates are rising, and it is reasonable to believe that they will continue to rise into the [R]ate [Y]ear in accordance with the Federal Reserve policy."[766]

Ann E. Bulkley responded to the ROE testimony of Staff witness Kaufman, Committee witness Gorman, and Alexandria witness Kreps; and the capital structure testimony of Staff witness Gereaux.[767] Ms. Bulkley updated her ROE analyses to reflect market data through July 29, 2022. The results confirm her ROE recommendations of a range of 9.90 percent to 11.00 percent, and an ROE within that range of 10.90 percent.[768] She indicated that reasonable adjustments to the models used by other witnesses confirm her ROE recommendation.[769]

Ms. Bulkley supported her ROE recommendation by stating that the low end of her ROE range of 9.90 percent is only: (i) "28 basis points higher than the average authorized ROE of 9.62 percent for water and natural gas utility authorized ROEs since 2019;"[770] and (ii) "30 basis points higher than the 9.60 percent ROE adopted for future earnings tests in VAWC's last rate

[758] *Id.* at 15.
[759] *Id.*
[760] *Id.* at 16.
[761] *Id.* at 16-17.
[762] *Id.* at 17.
[763] *Id.* at 18.
[764] *Id.* at 20.
[765] *Id.*
[766] *Id.* at 21-22.
[767] Exhibit No. 39, at 1.
[768] *Id.* at 2.
[769] *Id.* at 3.
[770] *Id.* at 6.

proceeding."[771] She stressed that interest rates have increased and are expected to continue increasing in response to inflation.[772] Ms. Bulkley asserted that ROE models that rely on current or historical market data "will likely underestimate the cost of equity over the near-term."[773]

Ms. Bulkley disagreed with Mr. Kaufman's contention that adoption of the RSM or Uncollectible ARAC will reduce VAWC's risk.[774] Ms. Bulkley took the position that because he provided no analysis, Mr. Kaufman had no basis to conclude ROE should be lowered if either mechanism is approved.[775]

Ms. Bulkley argued that the authorized returns of other jurisdictions are relevant to the reasonableness of ROE recommendations.[776] Nonetheless, she cautioned that many recent authorized ROEs are not based on current market conditions and likely understate currently required ROEs.[777] Ms. Bulkley reported that the ROE recommendations of Mr. Kaufman of 9.20 percent, Mr. Gorman of 9.35 percent, and Mr. Kreps of 9.30 percent to 9.40 percent are all lower than average of comparable authorized ROEs for water and natural gas utilities since January 2019 of 9.62 percent, and are lower than the 9.60 percent approved in the *2018 Rate Order* for future earnings tests and WWISC.[778]

Ms. Bulkley updated her ROE analyses based on market data through July 29, 2022.[779] She adjusted her proxy group to eliminate South Jersey Industries, because it is the target of a proposed acquisition, and York Water Company, because it failed to meet her screening criteria of being covered by more than one analyst and having positive growth rates from at least two utility industry equity analysts.[780] Ms. Bulkley provided the following summary of her updated ROE analyses:[781]

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[771] *Id.*
[772] *Id.*
[773] *Id.* at 6-7 (footnote omitted).
[774] *Id.* at 8.
[775] *Id.*
[776] *Id.* at 13.
[777] *Id.* at 14.
[778] *Id.* 14-15.
[779] *Id.* at 16.
[780] *Id.* at 16-17.
[781] *Id.* at 17.

Constant Growth DCF with Exclusions			
	Mean Low	Mean	Mean High
30-Day Average	9.14%	10.27%	11.38%
90-Day Average	9.07%	10.20%	11.32%
180-Day Average	9.15%	10.28%	11.37%
Constant Growth Average	9.12%	10.25%	11.36%
Constant Growth DCF without Exclusions			
	Median Low	Median	Median High
30-Day Average	8.38%	9.73%	10.25%
90-Day Average	8.35%	9.61%	10.25%
180-Day Average	8.37%	9.64%	10.38%
Constant Growth Average	8.37%	9.66%	10.29%
CAPM			
	Current 30-day Average Treasury Bond Yield	**Near-Term Blue Chip Forecast Yield**	**Long-Term Blue Chip Forecast Yield**
Value Line Beta	11.03%	11.09%	11.15%
Bloomberg Beta	10.71%	10.79%	10.86%
Long-term Avg Beta	10.29%	10.37%	10.46%
ECAPM			
Value Line Beta	11.51%	11.55%	11.60%
Bloomberg Beta	11.27%	11.33%	11.38%
Long-term Avg Beta	10.95%	11.02%	11.08%

Ms. Bulkley adjusted the average equity ratio for her proxy group in 2020 from 51.99 percent to 53.43 percent.[782]

Ms. Bulkley disagreed with the following areas of Mr. Kaufman's analysis:

> 1) the composition of the proxy group; 2) the calculation of stock prices used in the Constant Growth DCF model; 3) the appropriate growth rates to be considered in the Constant Growth DCF model; 4) the appropriateness of applying a 7 percent outlier screen to the results of the Constant Growth DCF; 5) reliance on the results of the Constant Growth DCF model under current market conditions; 6) the risk-free rate and market risk premium relied on in the CAPM; 7) the reliance on a study from 1995 to calculate the results of an Ex Ante Risk Premium analysis; 8) Mr. Kaufman's proposal to reduce the recommended ROE if the Company's proposed RSM is approved; and 9) the financial risk adjustment to account for the difference in leverage between Staff's use of the

[782] *Id.* at 18.

AWK consolidated capital structure and Mr. Kaufman's proxy group.[783]

Ms. Bulkley adjusted Mr. Kaufman's Constant Growth DCF, "making the appropriate changes," and increased his mean ROE estimate from 8.11 percent to 9.73 percent or 9.77 percent.[784] Ms. Bulkley adjusted Mr. Kaufman's CAPM and increased his estimate from 8.49 percent to 10.87 percent.[785]

In response to Mr. Kaufman's Ex Ante Risk Premium analysis, Ms. Bulkley developed a risk premium analysis based on natural gas companies, actual authorized returns from 1992 through July 2022, and calculated ROEs of 9.86 percent (30-day average of 30-year Treasury bond yield of 3.16 percent and a risk premium of 6.70 percent), 9.99 percent (near-term projected 30-year Treasury bond yield of 3.48 percent and a risk premium of 6.51 percent), and 10.12 percent (longer-term projected 30-year Treasury bond yield of 3.80 percent and a risk premium of 6.32 percent).[786]

Ms. Bulkley took issue with the magnitude of Mr. Kaufman's adjustment for financial risk of 40 basis points.[787] Ms. Bulkley supported an adjustment of 77.11 basis points.[788]

Based on her adjustments to Mr. Kaufman's analyses, Ms. Bulkley calculated an ROE range of 9.22 percent to 10.87 percent and a midpoint of 10.05 percent.[789] She noted, that considering financial risk, "it is reasonable to place VAWC's ROE towards the high-end of Mr. Kaufman's adjusted range."[790]

Regarding Mr. Gorman, Ms. Bulkley disagreed with his selection of 8.60 percent as the low-end of his DCF results range because it is over 100 basis points below the average authorized ROE since 2019, and below the ROEs authorized for any natural gas or water utility since January 2019.[791] She disagreed with Mr. Gorman's use of earnings retention as sustainable growth for dividend growth.[792] Ms. Bulkley corrected an error in Mr. Gorman's Constant Growth DCF analysis, which increased his results from 8.99 percent to 9.45 percent.[793] She also questioned the inclusion of the DCF result of 3.97 percent for Middlesex Water Company, which is below the cost of debt.[794] Ms. Bulkley adjusted and recalculated Mr. Gorman's DCF and

[783] *Id.* at 18-19.
[784] *Id.* at 19-20.
[785] *Id.* at 20.
[786] *Id.* at 23-24.
[787] *Id.* at 25.
[788] *Id.*
[789] *Id.* at 29.
[790] *Id.*
[791] *Id.* at 31.
[792] *Id.* at 32.
[793] *Id.* at 33.
[794] *Id.* at 34.

increased his range from 8.60 percent to 9.20 percent, to a range of 8.90 percent to 9.70 percent.[795]

For Mr. Gorman's Treasury Bond Approach, Ms. Bulkley contended the use of a near-term projected Treasury bond yield of 3.60, rather than a 5-year rolling average 30-year Treasury bond yield over 1986-2022, produced "arbitrary downward bias."[796] She noted his risk premium methodology in this case is inconsistent with his methodology in other recent cases.[797] Ms. Bulkley recalculated Mr. Gorman's Bond Yield Plus Risk Premium analysis to reflect expected capital market conditions and to use his methodology from other recent cases which produced results of 10.83 percent and 11.13 percent.[798]

For Mr. Gorman's CAPM analysis, Ms. Bulkley proposed adjustments to reflect current betas, and to reflect her estimate of the market return.[799] Ms. Bulkley calculated that these adjustments would increase Mr. Gorman's CAPM results of 9.98 percent and 9.81 percent to 10.68 percent and 10.84 percent.[800]

Ms. Bulkley testified Mr. Gorman's ROE analyses, when reasonably adjusted produces a midpoint of 10.14 percent, without consideration of capital market conditions and financial risk.[801]

Ms. Bulkley listed the following areas of disagreement with Mr. Kreps:

> (1) the overall recommended ROE for VAWC given the current market environment[;] (2) the relevant data to rely on in the analysis of interest rates and the effect of current and projected capital market conditions on the models used to estimate the cost of equity for VAWC; (3) the relevance of the Constant Growth DCF model results under current market conditions; (4) various assumptions in the development of the CAPM analysis; (5) the business and financial risk of VAWC relative to the proxy group companies; and (6) the effect of the Company's proposed capital structure on the return on equity.[802]

Ms. Bulkley recalculated Mr. Kreps's DCF to reflect dividends as of June 15, 2022, instead of September 30, 2021, and to eliminate significant low-end outliers, and reported the median results in a range of 9.37 percent to 9.70 percent.[803]

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[795] *Id.* at 34-35.
[796] *Id.* at 36.
[797] *Id.* at 37.
[798] *Id.* at 37-38.
[799] *Id.* at 39.
[800] *Id.* at 40.
[801] *Id.*
[802] *Id.* at 45.
[803] *Id.* at 48-49.

Regarding Mr. Kreps's CAPM, Ms. Bulkley disagreed with the following assumptions he relied upon: "1) sole reliance on the historical yield on the 30-year Treasury bond as an estimate of the risk-free rate, 2) the use of historical market returns, and 3) the use of the geometric average to calculate the historical return on the market."[804] Ms. Bulkley adjusted Mr. Kreps's CAPM to reflect projected interest rates and a projected market return and produced an ROE estimate of 10.25 percent to 11.23 percent.[805] Overall, Ms. Bulkley contended "[r]easonable changes to Mr. Kreps's analyses demonstrate that a more appropriate ROE range resulting from the corrections to his analysis is between 9.54 percent and 10.73 percent."[806]

As for capital structure, Ms. Bulkley noted "[s]ince the Commission's decision in the Company's last rate proceeding, VAWC has adjusted its actual equity ratio to 40.75 percent and thus is currently financing its rate base using the Commission-authorized level of equity."[807] She maintained the financial risks of VAWC are not comparable to AWK as AWK's capital structure is not specific to VAWC and "would result in the rates customers pay in Virginia being affected by the regulatory policies employed by commissions in AWK's other operating states."[808] Ms. Bulkley continued to support use of VAWC's capital structure as of April 30, 2023, and stressed the incremental risks faced by VAWC as compared to the proxy group companies.[809]

Stipulation

On September 26, 2022, the Stipulating Participants filed a Stipulation and a Joint Motion to Accept Stipulation. At the hearing, Consumer Counsel stated: "[w]hile not a signatory to the [S]tipulation, Consumer Counsel supports the [S]tipulation as a reasonable resolution of the issues addressed therein, given the statutory context for this case and we recommend its approval by the Commission."[810] The Stipulating Participants maintained "this Stipulation resolves all issues between the Stipulating Participants regarding the Company's Application in Case No. PUR-2021-00255."[811] As for the AIF Proceedings, the Stipulating Participants stated: (i) the Stipulation resolves issues related to the amounts of certain deferrals in the Company's 2020 AIF Earnings Test; and (ii) the Stipulation does not resolve the Alexandria Earnings Test issues.[812]

The Stipulation states as follows:

[804] *Id.* at 51.
[805] *Id.* at 51-52.
[806] *Id.* at 52 (footnotes omitted).
[807] *Id.* at 54.
[808] *Id.* at 57.
[809] *Id.* at 59.
[810] Farmer, Tr. at 37.
[811] Joint Motion to Accept Stipulation at 1.
[812] *Id.*

1. The Stipulating Participants agree to a rate increase that would produce additional annual jurisdictional revenues of $10.75 million.

2. For future cases requiring a capital structure and cost of capital until such time as [VAWC] files its next base rate case, the Stipulating Participants agree to a 9.7% ROE and the following actual capital structure and cost of capital:

Component	Ratemaking Capital	Weight	Cost Rate	Weighted Cost
Short-Term Debt	$20,144,129	7.335%	1.838%	0.135%
Long-Term Debt	$141,673,355	51.590%	4.222%	2.178%
Preferred Stock	$0	0.000%	0.000%	0.000%
Common Equity	$111,850,200	40.730%	9.700%	3.951%
Investment Tax Credits	$946,123	0.345%	6.594%	0.023%
Total Capitalization	$274,613,807	100.000%		6.286%

3. The Stipulating Participants agree to move forward with the second phase of consolidation for water service rates and the [PWS] as proposed by the Company and consistent with the Partial Stipulation approved by the Commission in Case No. PUR-2018-00175.

4. The Stipulating Participants agree to a 3-year amortization of the Company's COVID-19 regulatory asset balance as of June 30, 2021, resulting in an annual jurisdictional amortization amount of $272,812, as calculated in Staff's pre-filed adjustment. The Company will stop deferring COVID-19 related costs as of June 30, 2021, and will start amortization for book purposes as of May 1, 2022.

5. Stipulating Participants agree that the Company may record any amounts above or below the total Company amount of 2023 pension expense equal to $255,101 and OPEB expense equal to ($437,969) authorized in rates to a regulatory asset or liability, as appropriate, from the effective date of new rates in this proceeding until the Company's next base rate case. Such deferral will be subject to earnings tests during the deferral period based on total Company earnings.

6. The Stipulating Participants agree that the Alexandria WWISC Earnings Test issue in Case Nos. PUR-2019-00176 & PUR-2020-00249 will be [litigated] before the Commission based on the record and post-hearing briefs.

7. The Stipulating Participants agree to the level of write-offs for the Depreciation Reserve Deficiency, OPEB Deferral, and COVID-19 Deferral in the June 2020 Earnings Test (in Case No[]. PUR-2020-00249 as updated by Staff in this Rate Case (Case No. PUR-2021-00255) as presented below:

- Depreciation Reserve Deficiency: $362,630
- OPEB Deferral: $42,827
- COVID-19 Deferral: $123,286

8. The Stipulating Participants agree that the rates set forth on Attachment A should be approved by the Commission and implemented by the Company effective May 1, 2022.

9. This Stipulation represents a compromise for the purposes of settlement in this proceeding only and shall not be regarded as a precedent with respect to any ratemaking or any other principle in any future rate case. The Stipulating Participants agree that the resolution of the issues herein, taken as a whole, and the disposition of all other matters set forth in the Stipulation, are in the public interest. This Stipulation is conditioned on and subject to acceptance by the Hearing Examiner and the Commission and is non-severable and of no force or effect and may not be used for any other purpose unless accepted in its entirety by the Hearing Examiner and the Commission, except that this paragraph shall remain in effect in any event.

10. In the event the Hearing Examiner or the Commission does not accept the Stipulation in its entirety, including the issuance of a recommendation by the Hearing Examiner that the Commission not approve the Stipulation, the Stipulating Participants retain the right to withdraw their support for the Stipulation. In the event of an action by the Commission or the Hearing Examiner, any Stipulating Participant will be entitled to give notice exercising its right to withdraw their support for the Stipulation; provided that the Stipulating Participants may, by unanimous consent, elect to modify the Stipulation to address any modifications required, or issues raised, by the Commission or Hearing Examiner. Should the Stipulation not be approved by the Commission, it will be considered void and have no precedential effect, and the Stipulating Participants reserve their rights to participate in all relevant proceedings in the captioned case notwithstanding their agreement to the terms of the Stipulation. If the Commission or Hearing Examiner chooses to reject the Stipulation, the Stipulating Participants may request that additional evidentiary hearings be convened at which time, additional testimony and evidence may be

presented by the case participants and cross-examination may occur thereon, regarding any issues arising in those proceedings. Further, to the extent that the Hearing Examiner's Report has been filed, the Stipulating Participants may seek leave to file additional comments on the Hearing Examiner's Report.[813]

Attachment A of the Stipulation included the following concerning present and proposed rates:

Water:

Meter	Present VA $	Present Eastern $	Proposed VA $	Proposed Eastern $
5/8"	15.00	45.00	15.00	30.00
3/4"	22.50	45.00	22.50	30.00
1"	37.50	45.00	37.50	37.50
1 ½"	75.00		75.00	
2"	120.00		120.00	
3"	225.00		225.00	
4"	375.00		375.00	
6"	750.00		750.00	

2nd Volumetric Step Rates		Present $	Proposed $
Alexandria	Residential	0.34833	0.66101
	Commercial	0.22163	0.32392
Hopewell	Residential	0.73125	0.91763
	Commercial	0.49134	0.49788
Prince William	Residential	0.52661	0.74564
	Commercial	0.40851	0.44805
Eastern	Residential	0.91486	1.48293

Industrial Potable	Present Alexandria $	Present Hopewell $	Proposed Alexandria $	Proposed Hopewell $
1st 2,000 Gal.	0.23125	-	0.27110	0.40665
Next 13,000 Gal.	0.23125	0.74808	0.27110	0.40665
Next 2,229,000 Gal.	0.23125	0.52959	0.27110	0.40665
Next 5,236,000 Gal.	0.23125	0.31007	0.27110	0.40665
Next 37,400,000 Gal.	0.15032	0.12129	0.17623	0.17623
Over 44,880,000 Gal.	0.15032	0.16315	0.17623	0.17623

813 Exhibit No. 2.

Non-Potable Large	Present Hopewell $	Proposed Hopewell $
1st 7,480,000 Gal.	0.17497	0.17497
Over 7,480,000 Gal.	0.11373	0.14437

Non-Potable Small	Present Hopewell $	Proposed Hopewell $
1st 7,480,000 Gal.	0.23307	0.23307
Over 7,480,000 Gal.	0.15149	0.18188

Wastewater:

Meter Size	Prince William Wastewater $
5/8"	20.00
3/4"	30.00
1"	50.00
1 1/2"	100.00
2"	160.00
3"	300.00
4"	500.00

Prince William Wastewater	Present Residential $	Present Commercial $
1st 2,000 Gal.	-	-
Over 2,000 Gal.	0.45457	0.45457
Unmetered	31.00	31.00

Prince William Wastewater	Proposed Residential $	Proposed Commercial $
1st 2,000 Gal.	-	-
Over 2,000 Gal.	0.67408	0.67408
Unmetered	37.00	37.00

PUBLIC WITNESSES

During the public hearing, one public witness appeared. A summary of his testimony is provided below.

John McCauley of Alexandria expressed concern with the sewage bill he received from Alexandria Renew Enterprises.[814] The sewage rates of Alexandria Renew Enterprises are not addressed in this proceeding.

DISCUSSION

There are two issues to be discussed, (1) the proposed Stipulation, and (2) Staff's proposed refund of WWISC revenues.

Stipulation

The Stipulation represents an agreement between VAWC, Staff, and Alexandria, and was supported by Consumer Counsel.[815] The Stipulating Participants agreed that the Stipulation resolved all of the issues between the parties in VAWC's current Application in Case No. PUR-2021-00255.[816]

The Committee did not support the Stipulation and on brief, focused its opposition on the Company's proposal to spread an additional third of the PWS[817] to all customers.[818] The Committee's Brief also addressed VAWC's cost of capital, including capital structure and ROE.[819]

Regarding the proposal to spread an additional third of the PWS to all customers, the Committee argued the Commission should base its ruling on the record of this case, which does not support the proposal.[820] The Committee asserted: "[t]he record evidence and findings of [Committee witness] Gorman illustrate the breadth and magnitude of the disparate impacts the PWS Adjustment will impose – by more than doubling the annual PWS cost burden of certain customer classes while at the same time reducing others."[821] Among other things, Mr. Gorman presented a scheduled that he contended demonstrated that assigning an additional third of the PWS to all customers "moves away from consolidated volumetric charges rather than moving closer to it."[822] As will be explained in more detail below, I disagree with Mr. Gorman's contention.

In 2017 the General Assembly added § 56-235.11 to the Code.[823] Among other things, § 56-235.11 of the Code provides:

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[814] McCauley, Tr. at 12-15.
[815] Farmer, Tr. at 37.
[816] Joint Motion to Accept Stipulation at 1.
[817] As defined above, "PWS" refers to the Purchased Water Surcharge.
[818] Committee Brief at 1-2 (note, the Committee's Brief does not contain page numbers, this assumes consecutive numbering of pages).
[819] *Id.*
[820] *Id.* at 2-5.
[821] *Id.* at 5.
[822] Gorman, Tr. at 99; Exhibit No. 19, Attached Exh. MBG-23.
[823] 2017 Va. Acts ch. 822.

B. In any proceeding commenced on and after July 1, 2017, to establish or approve the rates of a water utility that is in a water utility network, the Commission shall ensure that the rates of each water utility in the water utility network are not unjustly discriminatory by ensuring that equal fixed and volumetric rates are charged for each customer class of each water utility that is in the water utility network.

C. Upon the commencement of a proceeding described in subsection B, the Commission shall make each water utility that is a member of the applicable water utility network a party to the proceeding and may review each member water utility's rates. In such proceeding:

1. The Commission shall review the rates of each member of the applicable water utility network and order gradual adjustments to such water utility's rates over an appropriate period in order to implement the provisions of subsection B; and

2. The Commission is authorized to aggregate the revenues and costs of the water utilities that are members of the applicable water utility network.

In its *2018 Rate Order*, the Commission adopted the first one-third step toward statewide STP[824], specifically including allocation of 1/3 of the PWS to the Hopewell and Eastern districts.[825] In this case, the proposal is for the second one-third step to be taken toward statewide STP. The Committee does not oppose the allocation of two-thirds of Hopewell's water production costs to all VAWC customers, with only one-third allocated directly to Hopewell. This allocation of an additional third of Hopewell's water production costs to all VAWC customers serves to lower Hopewell's revenue requirement and increase the revenue requirements for the Alexandria, Prince William, and Eastern districts as compared to what the revenue requirements would be without the additional one-third allocation.

However, the Committee opposes a similar, or reciprocal treatment of the PWS, which equates to the cost of water produced for the Alexandria and Prince William districts. That is, the allocation of an additional third of the PWS to all VAWC customers will lower the revenue requirements of the Alexandria and Prince William districts and increase the revenue requirements for the Hopewell and Eastern districts. Because the revenue requirement impacts are moving in different directions depending upon which district's water production costs are subject to an additional one-third allocation to all VAWC customers, the water production costs for all districts must be considered to ensure the resulting rates produce gradual adjustments that are not unjustly discriminatory.

[824] As defined above, "STP" refers to single tariff pricing.
[825] *2018 Rate Order* at 240-41.

Furthermore, Committee witness Gorman merely demonstrated that Hopewell customers are better off if an additional one-third of Hopewell's water production costs are allocated to all VAWC customers without the reciprocal additional allocation of production related costs (*i.e.*, PWS) from the Alexandria and Prince William districts. The table below is based on the residential rates shown in Mr. Gorman's Attached Exh. MPG-23.[826] The first three lines are total amounts taken from Mr. Gorman's Attached Exh. MPG-23, lines 3, 6, and 9, respectively. The Proposed Increase shows the percent increase from current volumetric rates based on the Company's proposed rates (in its Application), including the allocation of two-thirds of the PWS to all customers. The Adjusted Increase shows the percent increase from current volumetric rates based on the Company's proposed rates (in its Application), adjusted (as proposed by the Committee) to include an allocation of only one-third of the PWS to all customers.

Description	Alexandria (per 100 gals)	Prince William (per 100 gals)	Hopewell (per 100 gals)	Eastern (per 100 gals)
L. 3 Total Current	$0.55403	$0.75671	$0.78607	$0.96968
L. 6 Total Proposed	$0.92856	$1.02957	$1.13107	$1.84482
L. 9 Total Adjusted	$0.94739	$1.06603	$1.07440	$1.78815
Proposed Increase[827]	67.6%	36.1%	43.9%	90.3%
Adjusted Increase[828]	71.0%	40.9%	36.7%	84.4%

It must be remembered that "[t]he primary driver of this case is ongoing investment in infrastructure."[829] As outlined by Company witness McGee, Hopewell is responsible for the largest share of the infrastructure investments.[830] Thus, both the proposed increase and adjusted increase amounts already reflect the allocation of an additional one-third of Hopewell's costs to the other divisions. Seen in this light, Mr. Gorman's analysis shows that allocation of an additional one-third of the PWS costs to all other customers serves to mitigate a portion of the increase for the Alexandria and Prince William districts resulting from Hopewell and produce a more gradual movement towards statewide STP.[831] Therefore, based on the record of this case, I recommend that the Commission continue with the second one-third step towards statewide STP, by moving all rates, including the PWS, one-third closer to STP.

Regarding issues raised by the Committee concerning VAWC's capital structure and ROE, VAWC maintained "the Stipulation provides a 'Black Box' revenue requirement that does not require the Commission to rule on individual adjustments advocated by the participants to

[826] Exhibit No. 19, at Attached Exh. MPG-23, at 1.

[827] The Proposed Increase equals (L. 6 Total Proposed minus L. 3 Total Current) divided by L. 3 Total Current.

[828] The Adjusted Increase equals (L. 9 Total Adjusted minus L. 3 Total Current) divided by L. 3 Total Current.

[829] Exhibit No. 3, at 1.

[830] Exhibit No. 6, at 14-24, Attached Exh. KEM-1.

[831] The Eastern district volumetric rates are increased by additional allocations from both Hopewell and the PWS but is mitigated by reductions in the fixed monthly charge.

this proceeding."[832] That is, acceptance of the Stipulation should be based on determining whether taken as a whole, it provides a full and fair resolution to the issues presented in the Company's Application. The Committee takes specific issue with use of VAWC's standalone capital structure and ROE of 9.7 percent "[f]or future cases requiring a capital structure and cost of capital until such time as [VAWC] files its next base rate case."[833] However, I find these issues do not call into question the reasonableness of the Stipulation because neither of these issues would produce significantly different results in this case. There is little difference between the consolidated and standalone capital structure in this case.[834] Moreover, the ROE of 9.7 percent is within the ROE range of Committee witness Gorman of 8.9 percent and 9.8 percent.[835] Therefore, based on the record in this proceeding, and with one exception, I find the Stipulation offers a reasonable and just resolution to all the issues raised in this case.

The exception concerns redesigning the rates of the Hopewell potable industrial customers by reducing the number of rate blocks from six to two. The proposed Stipulation in this case departs from the Commission's *2018 Rate Order*, which directed "retention of the industrials prior six-block rate design for potable customers as well as application of an equal percentage increase across all six rate blocks."[836] The *2018 Rate Order* maintained the existing rate design for these customers.[837] On brief, VAWC asserted:

> The Company proposes reducing [Hopewell potable industrial rate design of six blocks] to a two-block declining block rate structure. The proposed rate structure not only better aligns with the existing two-block industrial rate structure in Alexandria—consistent with the need to move to a consolidated, state-wide industrial rate structure—it also is a simpler rate structure to administer and understand for billing purposes.[838]

According to Company witness Rea, there is one industrial customer in Alexandria and "ten or so" industrial customers in Hopewell.[839] Moreover, Hopewell's industrial customers are served from a system that includes water treatment facilities, whereas Alexandria's industrial customer is served from a system that purchases its water and has no water treatment facilities.[840] I find that the existing rate structure of a system that serves more, and more diverse customers from a system that has more facilities would appear to provide the better basis for rate design. Furthermore, using such a rate design would provide no impediment to moving to a consolidated state-wide industrial rate. First, the six-block rate structure was adopted in the *2018 Rate Order*, which accomplished the first one-third step towards a consolidated state-wide

[832] VAWC Brief at 5-6.
[833] Exhibit No. 2, Stipulation at ¶ 2.
[834] *See* Exhibit No. 38, at 18-19; Exhibit No. 21, at 10-11.
[835] Exhibit No. 19, at 69.
[836] *2018 Rate Order*, at Ordering Paragraph (5).
[837] Rea, Tr. at 199-200.
[838] VAWC Brief at 21 (footnote omitted).
[839] Rea, Tr. at 200-01.
[840] *Id.* at 200.

industrial rate. Second, Mr. Rea acknowledged "you could very easily, just as easily, say, put that one Alexandria customer on a six-step rate than the ten or so Hopewell customers on a two-step rate."[841] Finally, regarding a simpler rate structure being easier to administer and understand for billing purposes, I agree a simpler rate structure can be easier to administer and understand. However, the six-step rate structure is not new and VAWC has at least several years of experience in its administration. Also, this structure has been applied to almost all of the Company's industrial customers, the understanding of which should not be a problem.

Furthermore, VAWC maintained: "[b]y retaining the six-block rate design for the Hopewell industrial class, this will retain the existing differentials between the rates paid by higher and lower usage industrial customers despite there being little basis for this differential."[842] This statement shows that VAWC proposes to redistribute the revenue responsibility within the industrial class. As to the Company's contention that there is little basis for the current differential, I find there is little to no evidence in this record concerning the current differential, one way or the other. In addition, the magnitude of the rate increase in this case will be amplified unnecessarily for some customers due to the Company's proposal to depart from the six-block rate design. Therefore, absent evidence in this record supporting a change in rate design for Hopewell's industrial customers, I recommend that the Commission continue to use the existing rate structure, consistent with its decision in its *2018 Rate Order.*

Proposed Refund of WWISC Revenues

Not covered by the Stipulation is Staff's recommendation regarding the refund of $419,803 of WWISC revenues collected from the Alexandria customers based on the Alexandria Earnings Test from the AIF Proceedings. On this issue, the Company opposes Staff's recommendation, while Staff, Alexandria, and Consumer Counsel support Staff's recommended refund.[843]

Staff calculated that the Alexandria district earned a 10.03 percent ROE over the 28-month period of January 1, 2019, through April 30, 2021 ("Alexandria ET Period").[844] Staff maintained the Company's WWISC collections contributed to the Alexandria district's overearning.[845] In addition, Staff contended that after the proposed refund of $419,803, Alexandria's ROE would be 9.57 percent, which is above the weighted average benchmark of 9.55 percent as determined by authorized ROEs during the Alexandria ET Period.[846]

VAWC made four arguments against Staff's recommended refund of $419,803 of WWISC revenues from Alexandria. First, the Company contended the Commission's *2015 Rate Order* provided for WWISC refunds only where WWISC collections "result in" or are the cause

[841] *Id.* at 201.
[842] VAWC Brief at 22.
[843] *Id.* at 22-30; Staff Brief at 6-10; Alexandria Brief at 21-22; Consumer Counsel Brief at 17-20.
[844] Staff Brief at 8; Exhibit No. 25, at 18.
[845] Staff Brief at 9.
[846] *Id.*

of earnings above the amount authorized.[847] Second, VAWC asserted earnings above the authorized amount for the Alexandria district are the direct result of rate consolidation.[848] Third, because VAWC collected WWISC revenues for only 16 of the 28 months of the Alexandria ET Period, the Company argued the Alexandria ET Period is improper for determining WWISC refunds.[849] Finally, VAWC maintained Staff's approach, if adopted, would eliminate the intended benefit and utility of the WWISC mechanism.[850]

In the *2015 Rate Order*, among other things, the Commission held:

> that the use of an Earnings Test should accompany the annual WWISC review and finds that refunds should be made to ratepayers, with interest, to the extent WWISC collections result in annual earnings above the rate of return on common equity of 9.25% approved below.[851]

VAWC interpreted the above language to mean "WWISC refunds are appropriate only when WWISC collections are the cause of earnings above authorized."[852] The Company pointed to the additional revenues collected in the Alexandria district associated with rate consolidation.[853] VAWC further argued WWISC collections in the Alexandria ET Period cannot be the source of the earnings above the amount authorized because such revenues were based on a 9.25 percent ROE.[854]

The effect of rate consolidation on WWISC refunds will be discussed separately below.

I disagree with VAWC's interpretation of the Commission's *2015 Rate Order*. By subjecting WWISC collections to an earnings test, the Commission indicated that WWISC collections would be treated similar to regulatory assets. That is, their treatment or disposition would depend upon the aggregate revenues and aggregate cost measured in the earnings test. Earnings tests, by their nature, are not designed for the granular causation analysis suggested by the Company. Treatment of the WWISC collections (or regulatory assets) are driven by whether the utility has overall earnings above its authorized return. Indeed, VAWC's argument that because WWISC collections were based on a 9.25 percent ROE they cannot be the source of the earnings above the authorized return, demonstrates why such granular analysis is not part of an earnings test. Under the Company's approach, WWISC collections would never be subject to refund as long as they are set based on an ROE equal to or below the benchmark ROE, even in situations where the Company is earning well in excess of its benchmark.

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[847] VAWC Brief at 23-25.
[848] *Id.* at 25-28.
[849] *Id.* at 28-29.
[850] *Id.* at 29-30.
[851] *2015 Rate Order* at 291.
[852] VAWC Brief at 23-24.
[853] *Id.* at 25-26.
[854] *Id.* at 26.

Regarding that WWISC revenues were collected for only 16 months of the 28-month Alexandria ET Period, VAWC faulted Staff for failing "to explain why this mismatch comparison is appropriate for evaluating earnings relative to the WWISC."[855] However, Staff took the position that the 28-month Alexandria ET Period was based on the stipulation in Case No. PUR-2019-00185.[856] On brief, Staff maintained: "[n]ot only did the Company agree to the 28-month [Alexandria ET Period], it could have proactively requested a different [earnings test] period, but it did not do so."[857] Based on the stipulation in Case No. PUR-2019-00185 and the circumstances of the instant case, I find that the Alexandria ET Period is an appropriate period to use for earnings test purposes.

Based on the discussion above, I do not find that Staff's approach, if adopted, would eliminate the intended benefit and utility of the WWISC mechanism.

I believe the Commission could find that based on the Alexandria ET Period results, Staff's proposed refund of $419,803 of WWISC revenues collected from Alexandria customers is appropriate, based on the discussion above. However, while I find that earnings tests, by their nature, are not designed for granular causation analysis, in my opinion this case presents a situation for which the Commission should make an exception. VAWC showed that beginning in May 2019, the legislatively mandated consolidation to STP and the Commission's *2018 Rate Order* "resulted in an approximately $1,045,049, increase in annual revenue for the Company's Alexandria [d]istrict (which was balanced with decreases in other districts)."[858] The Company further maintained that for the Alexandria ET Period, "[t]his means that during that period, $2,090,098 of revenues collected in the Alexandria [d]istrict -- $895,756 on an annualized basis – were due *solely* to rate consolidation."[859] Thus, it appears the additional rate consolidation revenues collected from the customers of the Alexandria district exceeds the level of revenues that Staff recommended be refunded.

Staff did not address the Company's contention regarding the additional revenues collected from the Alexandria district due to rate consolidation. Based on the unique circumstances of this case and the identified rate consolidation revenue, I find the Commission should reject Staff's proposed refund of $419,803 of WWISC revenues.

FINDINGS AND RECOMMENDATIONS

In conclusion, based on the Stipulation and the other evidence received in this case, I find that the proposed Stipulation, except as specified below, should be adopted. Among other things, I find that:

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[855] *Id.* at 28.
[856] *Application of Virginia-American Water Company, For approval of a WWISC Rider True-Up Factor*, Case No. PUR-2019-00185.
[857] Staff Brief at 10.
[858] VAWC Brief at 24; Exhibit No. 36, at 7.
[859] VAWC Brief at 26 (emphasis in original). Note: $895,756 equals $2,090,098 divided by 28 times 12.

(1) Based on the record and Stipulation, VAWC requires a rate increase that will produce additional annual jurisdictional revenues of $10.75 million;

(2) VAWC's ROE is 9.7 percent, and the actual capital structure and cost of capital is as provided in the Stipulation and shown above, to be used for future cases requiring a capital structure and cost of capital until such time as VAWC files its next base rate case;

(3) VAWC should move forward with the second phase of consolidation for water service rates and the PWS as proposed by the Company;

(4) VAWC should use a 3-year amortization of the Company's COVID-19 regulatory asset balance as of June 30, 2021, stop deferring COVID-19 related costs as of June 30, 2021, and begin amortizing for book purposes as of May 1, 2022;

(5) VAWC may record any amounts above or below the Company's amount of 2023 pension expense equal to $255,101 and OPEB expense equal to ($437,969) authorized in rates to a regulatory asset or liability, as appropriate, from the effective date of new rates in this proceeding until the Company's next base rate case. Such deferral will be subject to earnings tests during the deferral period based on total Company earnings;

(6) VAWC should not be required to refund any WWISC revenues collected from Alexandria district customers during the Alexandria ET Period;

(7) As specified in the Stipulation, VAWC should be directed to write-off the Depreciation Reserve Deficiency of $362,630, OPEB Deferral of $42,837, and COVID-19 Deferral of $123,286;

(8) Except for the rates for Hopewell industrial potable water customers, VAWC should implement the rates set forth on Attachment A of the Stipulation effective May 1, 2022. The rate design for the Hopewell industrial potable water customers should be designed based on the current six-block rate structure with each existing volumetric rate block changing by the same percentage; and

(9) VAWC should refund, with interest as prescribed by the Commission, amounts collected as interim rates based on its Application in excess of the rates approved herein.

In accordance with the above findings, ***I RECOMMEND*** that the Commission enter an order that:

1. ***ADOPTS*** the findings in this Report and the Stipulation as amended; and

2. ***DISMISSES*** this case from the Commission's docket of active cases and passes the papers herein to the file for ended causes.

COMMENTS

The parties are advised that, pursuant to Rule 5 VAC 5-20-120 C of the Commission's Rules and § 12.1-31 of the Code, any comments to this Report must be filed on or before **December 28, 2022**. In accordance with the directives of the Commission's *COVID-19 Electronic Service Order*[860] the parties are encouraged to file electronically. If not filed electronically, an original and fifteen (15) copies must be submitted in writing to the Clerk of the Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia 23218. Any party filing such comments shall attach a certificate to the foot of such document certifying that copies have been served by electronic mail to all counsel of record and any such party not represented by counsel.

Respectfully submitted,

Alexander F. Skirpan, Jr.

Alexander F. Skirpan, Jr.
Chief Hearing Examiner

Document Control Center is requested to send a copy of the above Report to all persons on the official Service List in this matter. The Service List is available from the Clerk of the State Corporation Commission, c/o Document Control Center, 1300 East Main Street, First Floor, Tyler Building, Richmond, VA 23219.

[860] *Commonwealth of Virginia, ex rel State Corporation Commission, Ex Parte: Electronic service among parties during COVID-19 emergency*, Case No. CLK-2020-00007, Doc. Con. Cen. No. 200410009, Order Requiring Electronic Service, (April 1, 2020) ("*COVID-19 Electronic Service Order*").