DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER OF the Investigation of the Montana Public Service Commission into whether Mountain Water Company's rates are Just and Reasonable	))))	REGULATORY DIVISION DOCKET NO. D2016.2.15

DATA RESPONSES OF THE MONTANA CONSUMER COUNSEL TO MOUNTAIN WATER COMPANY

MWC-045. RE: References to "Carlyle," Wilson Testimony
Witness: John Wilson

Dr. Wilson's testimony refers generally to "Carlyle" several times without indicating which entity Dr. Wilson is referring to. Please separately identify the entity Dr. Wilson is referring to for each reference to "Carlyle," including Page 5, line 10; Page 7, line 17 and fn. 2; Page 8, lines 11, 12 and fn. 3; Page 9, line 13; Page 12, line 14; Page 13, lines 3,6, 17, 18, and 9; Page 14, lines 18 and 19; Page 15, lines 2 and 4; Page 16, line 6; Page 17, line 6 and 13; Page 18, line 18; Page 19, line 3; Page 20, line 10, 15, 16 and fn. 11; Page 21, lines 13 and 14; Page 22, line 2; Page 23, line 2; Page 24, lines 8 and 11; Page 25, line 18; Page 26, line 16.

RESPONSE:

As Dr. Wilson testified in Docket No. 2014.12.99, “In this testimony I use the term “Joint Applicants” to refer jointly to the Carlyle entities plus the Algonquin entities. The named Carlyle entities in the Joint Applicants’ filings are Western Water Holdings, LLC and Mountain Water Company. The named Algonquin entities in the Joint Applicants’ filings are Liberty Utilities Co. and Liberty WWH, Inc. More generally as discussed in this testimony, I consider the Carlyle entities to include the Carlyle Group and Park Water and the Algonquin entities to include APUC.” In this testimony also, Dr. Wilson generally refers to the Carlyle entities as a consolidated whole.

In each response to the following data requests, please identify and refer to the appropriate entity, rather than Carlyle generally.

MWC-046. RE: "Carlyle" Returns, Wilson Testimony 8:11-9:3
Witness: John Wilson

Footnote 5 in Dr. Wilson's testimony appears to contend that Carlyle was allowed and earning a 16% return on the entire value of "Carlyle's equity interest in Park Water."

a. Please identify the value of Carlyle's equity interest on which Dr. Wilson contends Carlyle was earning 16%.

b. Please identify the Commission order or docket in which the Commission authorized a return on equity for Carlyle.

c. Please identify the Commission order or docket in which you contend the Commission authorized Carlyle to recover a return on capital.

d. Please identify the Commission order or docket in which you contend the Commission authorized Mountain Water or any other entity to recover a return on capital in excess of Mountain Water's rate-base.

RESPONSE:

a. Dr. Wilson did not testify or “contend” as to a specific rate that Carlyle’s equity interest was earning. Rather he testified that Mountain Water’s authorized rates in Montana included a cost of equity capital granted by the Commission in the Company’s most recent rate case that encompassed a 9.8% after tax ROE allowance (16.17% before tax). At that time, Mountain Water’s allocated equity was determined to be about 56% of its total capital.

b. Docket No. D2012.7.81

c. See responses to parts a and b of this question. Also note that rather than allowing “a return on capital” the Commission allows a return on rate base, which, in turn, produces a return to compensate for the cost of capital investment.

MWC-046 continued

d. No such contention was made. The Montana Commission allows a return on rate base (not a return on capital), which includes a cost of capital allowance. The allowed rate of return and the allowed rate base are separate and different concepts that appear to be confused in this question.

MWC-047. RE: "Carlyle" Returns, Wilson Testimony p. 9, fn. 5
Witness: John Wilson

The first calculation in footnote 5 calculates "finance cost reduction" of $19.2 million.

a. Please admit this calculation is based on the assumption that Carlyle was earning a return of 16% on $160 million of capital.

b. If the response to (a) is anything other than an unqualified admission, please explain your response.

c. If you admit (a), please identify the basis for the contention that the Commission authorized Carlyle to earn 16% on $160 million.

d. Please describe the amount of Carlyle's returns Dr. Wilson contends were included in Mountain Water's current rates.

RESPONSE:

a. No. It does not make that presumption.

b. The rate of return allowance is a capital cost allowance that utilities are permitted to incorporate in rates. It is not an earnings presumption.

c. Not applicable, but see response to MWC-046 (a) above.

d. Mountain Water's current rates incorporate the full 16.17% pre-tax equity capital cost allowed to Carlyle. APUC replaced $160 million of Carlyle's 16.17% cost equity with new capital costing 4.13%.

MWC-048. RE: "Carlyle" Returns, Wilson Testimony p. 9, fn. 5
Witness: John Wilson

The second calculation in footnote 5 calculates a potential "cost savings" of $32.9 million.

a. Please admit this calculation is based on the assumption that Carlyle was earning a return of 16% on $235 million of capital.

b. If the response to (a) is anything other than an unqualified admission, please explain your response.

c. If you admit (a), please identify the basis for the contention that the Commission authorized Carlyle to earn 16% on $235 million.

RESPONSE:

a. No. It does not make that presumption.

b. The rate of return allowance is a capital cost allowance that utilities are permitted to incorporate in rates. It is not an earnings presumption.

c. Not applicable. But see responses above.

MWC-049. RE: Commission Jurisdiction, Wilson Testimony pp. 12 -13
Witness: John Wilson

a. Please admit Mountain Water has not proposed a rate increase as a result of Liberty's acquisition of Western Water Holdings.

b. If the response to (a) is anything other than an unqualified admission, please explain your response.

c. Please describe any deterioration of service of which Dr. Wilson is aware of since Liberty's acquisition of Western Water Holdings.

d. Please admit The Carlyle Group was not a party to docket D2011.1.8.

e. If Dr. Wilson contends the Carlyle Group was subject to the jurisdiction of the Commission" regarding its acquisition of Park Water, please describe the basis for his contention, including cites to any documents supporting his contention.

RESPONSE:

a. It is not Dr. Wilson's contention that Mountain Water, Liberty or APUC have proposed a rate increase. Rather they have proposed to maintain current rates that were previously authorized to reflect the cost of Carlyle's capital investment in Mountain Water, when, in fact, that cost has been greatly reduced by virtue of the acquisition financing.

b. The explanation is included in the response to part (a).

c. Dr. Wilson has not investigated this matter.

d. Although the Petition in Docket D2011.1.8 was styled by the petitioner as a petition by Mountain Water for the sale and transfer of stock, the case was described as an "application of Mountain and Carlyle for approval of the sale and transfer of stock in Park Water Company…" Also, Carlyle was a signatory party to the Stipulation resolving the case.

MWC-049 continued

e. See response to part (d) and the Commission's Final Order in Docket No.D2011.1.8.

MWC-050. RE: "Carlyle's" Capital, Wilson Testimony 13:15-19
Witness: John Wilson

a. Please admit Dr. Wilson's calculations and testimony are based on the assumption that Carlyle did not use any debt to finance its acquisition of Park Water.

b. If the response to (a) is anything other than an unqualified admission, please explain your response.

c. If the response to (a) is an admission, please describe the steps Dr. Wilson took to verify Carlyle did not use debt for its acquisition of Park Water.

d. Please describe the basis for Dr. Wilson's testimony that Carlyle's "capital costs of ownership" are higher than Liberty or Algonquin.

e. Please describe in detail, including identification of source documents reviewed, any review of Carlyle's capital structure undertaken by Dr. Wilson, including a description of Dr. Wilson's contention as to the amount of Carlyle's cost of capital.

RESPONSE:

a. No. Dr. Wilson did not make that assumption. However, Dr. Wilson is not aware of any debt issuance that was made by Carlyle to fund its acquisition of Park Water's equity capital.

b. See response to part (a).

c. Not applicable. However, Dr. Wilson did review all of the evidence in the case regarding acquisition financing and independently researched Western Water Holdings and Carlyle Infrastructure Partners and found no evidence of debt issuances by these or any other Carlyle entities to acquire Park Water's equity capital.

MWC-050 continued

d. APUC's 4.13% acquisition financing cost is a matter of record in contrast to Carlyle's equity cost (16.17% pre-tax), as determined by the Commission.

e. Please see response to part (c) above. Carlyle's cost of capital is a matter of Commission determination. Please see the Commission's Final Order in Docket No.2012.7.81

MWC-051. RE: Liberty's Acquisition, Wilson Testimony 13:15-19
Witness: John Wilson

a. Please admit Mountain Water's actual capital structure remains 100% equity owned by Park Water.

b. Please admit Western Water Holding's interest in Park Water is equity.

c. Please admit Carlyle's ownership interest in Western Water Holdings was equity.

d. Please admit Liberty's ownership interest in Western Water Holdings is equity.

e. If the response to (a) through (d) is anything other than an unqualified admission, please explain your response.

RESPONSE:

a. Mountain Water does not issue its own debt. Its capital structure is determined in rate cases such as Docket No.2012.7.81 by allocation of Park Water's consolidated debt and equity.

b. Yes. That is my understanding.

c. Yes. That is my understanding.

d. It is my understanding that APUC/Liberty financed its acquisition and ultimate ownership of Park Water (and Mountain Water) equity capital largely through the issuance of low cost (4.13%) debt capital.

e. See responses above.

MWC-052. RE: Liberty's Acquisition, Wilson Testimony 13:15-19
Witness: John Wilson

a. Please admit that a buyer's use of debt as the source of funds to acquire an equity interest in a company, does not convert the buyer's ownership interest to debt.

b. If the response to (a) is anything other than an unqualified admission, please explain your response.

c. Please identify any statutory, administrative or other legal authority, or any academic or industry publication or treatise Dr. Wilson contends supports his response to (b).

d. Please provide copies of any documents identified in response to (c).

RESPONSE:

a. While the buyer's ownership interest is not converted to debt, the buyer's cost of capital is the cost of the debt issued to accomplish the acquisition.

b. See response to part (a).

c. This response is premised on elementary and unexceptionable logic. That is, the source of funding does not change what was acquired. And, the cost of the acquisition is the cost to the buyer of accomplishing the acquisition.

d. none

MWC-053. RE: Mountain Water's rates, Wilson Testimony 16:5-9
Witness: John Wilson

a. Please identify, by cite to testimony or provisions of an order, the basis for Dr. Wilson's testimony that Mountain Water's current rates are based on the cost of "Carlyle's" equity capital.

b. Please identify the portions of testimony Dr. Wilson offered in dockets D2011.1.8 or D2012.7.81 in which he identifies, analyzes or discusses Carlyle's cost of equity.

c. Please admit the Commission refused Dr. Wilson's request to adjust the rate of return it authorized Mountain Water in D2012.7.81 based on any Carlyle entity's ownership.

d. If the response to (c) is anything other than an unqualified admission, please explain your response.

RESPONSE:

a. These prior cases did not involve the refinancing of capital invested in the utility at lower cost. Therefore, there were no finance cost reductions to be addressed, and the Commission addressed cost of capital requirements in terms of Mountain Water's cost of capital. A reasonable reading of the Commission's Orders shows a clear understanding that Carlyle was providing the required financing and that it was Carlyle's financing costs that must be compensated through the establishment of just and reasonable rates. Thus, for example, in Order 7914d the Commission observed:

> According to Dove, Carlyle intends to retain Park and its subsidiaries, including Mountain, for a long period of time and invest capital into the system as necessary. However, during the hearing, Dove testified to a relatively short ownership period, which is discussed further below in paragraph 76. He explained that Carlyle will not try to quickly increase the value of the assets by increasing revenues or cutting expenses in order to sell the company for a large

MWC-053 continued

profit. Rather, he said Carlyle's investors expect to acquire low-risk assets that offer steady, predictable returns.

b. See response to part (a)

c. Dr. Wilson did not make a "request." He made a recommendation based on Carlyle's own previous contentions that were made at the time of the Park Water acquisition by Carlyle. It is essentially true that despite those previous contentions by Carlyle, the Commission did not conclude that Carlyle had a lower cost of equity capital for its Mountain Water equity ownership than did Park.

d. See response to part (c).

MWC-054. RE: Mountain Water's rates, Wilson Testimony
Witness: John Wilson

a. Please admit Mountain Water's current rates are based on a Commission-authorized ROE of 9.8%.

b. Please admit the Commission authorized this rate after considering testimony from both Dr. Wilson and Mountain Water's expert Thomas Zepp.

c. Please admit that both experts Wilson and Zepp developed ranges of potential ROE's in docket D2012.7.81, based on actual reported returns and analyst projections for a group of proxy companies.

d. Please admit the purpose of the use of the proxy group was to determine a reasonable return on equity for hypothetical equity investments in Mountain Water.

e. Please describe any changes to the proxy group Dr. Wilson previously used, which you contend would be required as a result of Liberty's acquisition of Western Water Holdings.

RESPONSE:

a. Yes, they are.

b. Yes.

c. Yes

d. Dr. Wilson's purpose was to determine a reasonable return reflecting the actual cost of Carlyle's actual equity capital invested in Park Water and allocated to Mountain Water for ratemaking purposes. Dr. Wilson assumes, but has not confirmed, that Dr. Zepp's purpose was the same.

e. Dr. Wilson does not recommend any such changes. He recommends recognizing the capital cost savings realized by APUC as a direct result of

MWC-054 continued

refinancing and replacing Carlyle's equity capital with much lower cost (4.13%) capital.

MWC-055. RE: Rate Adjustments, Wilson Testimony pp. 18-19
Witness: John Wilson

a. Please admit Dr. Wilson is advocating the Commission alter Mountain Water's rates by suspending or lowering Mountain Water's returns as punishment for Liberty's decision to close its acquisition of Western Water Holdings without Commission approval.

b. Please admit Dr. Wilson is not offering testimony about Mountain Water, Park Water, Liberty or APUC's actual costs of capital.

c. If the response to (a) or (b) is anything other than an unqualified admission, please explain your response.

d. Please identify the authority Dr. Wilson contends would allow the Commission to suspend Mountain Water's recovery of its equity return as a result of Liberty's decision to close its acquisition of Western Water Holdings without Commission approval, including identification of any statutory, administrative or other legal authority, or any academic or industry publication or treatise Dr. Wilson contends supports his testimony or response to this request.

e. Please identify the authority Dr. Wilson contends would allow the Commission to lower Mountain Water's equity return without a full analysis of Mountain Water's cost of capital as a result of Liberty's decision to close its acquisition of Western Water Holdings without Commission approval, including identification of any statutory, administrative or other legal authority, or any academic or industry publication or treatise Dr. Wilson contends support his testimony or response to this request.

RESPONSE:

a. No. This statement is incorrect. Dr. Wilson's recommendation deals only with retaining just and reasonable, cost-reflective rates, that recognize APUC's very substantial acquisition-enabled capital cost reduction. The Commission has the authority to administer any "punishment" for Algonquin/Liberty's described

MWC-055 continued

actions through the imposition of fines, but that is an entirely different matter that Dr. Wilson has not addressed in his testimony.

b. No. This is incorrect. As Dr. Wilson has testified, the actual cost of a large portion ($160 million) of Algonquin/Liberty's acquisition capital was and is 4.13% rather than the much greater 16.17% capital cost allowance now reflected in Mountain Water's rates.

c. Explanations are included in the answers to parts (a) and (b).

d. Dr. Wilson is not aware of any other cases involving the defiance of regulatory authority exhibited by Algonquin/Liberty in this case. Consequently, he does not offer such precedent as authority for Commission action in this case. However, it stands to reason that if Algonquin/Liberty's acquisition of the stock of Park Water/Mountain Water in Montana is not approved, it would be inappropriate to require Montana citizens to pay Algonquin/Liberty (or authorize Algonquin/Liberty to collect) a profit from Montana ratepayers for acquiring that stock – at least until such time as (if and when) regulatory approval is obtained.

e. This question misconstrues Dr. Wilson's testimony and recommendations. This is not a general rate case. The rate adjustment proposed here simply reflects acquisition enabled cost savings that are customarily passed through to ratepayers, as a condition of acquisition approval, without any need for a general cost of service or rate adequacy review. All cost of service and rate determinations in Mountain Water's last rate case remain as they were (until the Commission makes new cost and rate determinations in Mountain Water Company's next general rate case), with the exception of passing through to ratepayers acquisition-enabled cost savings as a condition of acquisition approval.

MWC-056. RE: Rate Adjustments, Wilson Testimony pp. 18-19
Witness: John Wilson

a. Please identify any order of any regulatory commission or court of which Dr. Wilson is aware in which a utility's cost of capital or rates were reduced under circumstances he considers similar to this case.

b. Please provide a copy of any order identified in response to (a).

RESPONSE:

a. See for example: 624 P.2d 481 (1981) MOUNTAIN STATES TELEPHONE AND TELEGRAPH COMPANY, a Colorado Corporation, Plaintiff and Appellant,
v.
The DEPARTMENT OF PUBLIC SERVICE REGULATION, Montana Public Service Commission et al., Defendants and Respondents. No. 80-99. Supreme Court of Montana.

b. The referenced decision is available at:

http://scholar.google.com/scholar_case?case=17538536062168809917&q=624+P.2d+481&hl=en&as_sdt=4,27

MWC-057. RE: Park Water Capital Structure, Wilson Testimony pp. 21-23
Witness: John Wilson

Does Dr. Wilson contend that the current regulatory capital structure of Park Water consists of total capital of $327 million consisting of $90 million of equity, $160 million of 30-year debt at 4.13%, and $77 million of existing debt at its actual blended rate?

a. If yes, please explain the basis for this conclusion. If no, please explain the significance of those values on pages 21 through 23 of his testimony.

b. If no, please describe the current regulatory capital structure Dr. Wilson contends exists for Park Water.

c. Please describe the total return to which Dr. Wilson contends Liberty would be able to recover from Park Water under the capital structure he describes in (b).

d. Does Dr. Wilson contend that 31.81% of the $90 million of equity capital he contends Liberty invested should be "assigned to Mountain Water"?

e. Please describe the basis for Dr. Wilson's response to (d), including an identification of the amount of equity he believes should be attributed to Mountain Water under the current ownership.

RESPONSE:

a. No, the significance of these values is that they reflect the components of APUC's acquisition financing, including $160 million of 4.13% debt that was used to acquire Carlyle's equity interest in Park Water.

b. The current regulatory capital structure is the capital structure approved by the Commission in docket D2012.7.81.

c. As stated above, this is not a general rate case and Dr. Wilson is making no recommendation as to the total return that Mountain Water should be able to recover. He is only recommending that acquisition enabled cost savings should be passed through to ratepayers. In all other respects, rates would be the same as those established in docket D2012.7.81. The total return that Mountain Water would be able to recover would depend on established water

MWC-057 continued

rates (less the pass-through of acquisition-enabled capital cost savings), current and future water sales levels, the number and type of water service customers and the costs incurred to provide reliable and efficient water service.

d. No.

e. Please see responses to parts (b) and (c) of this question and other responses above.

MWC-058. RE: Tax Loading, Wilson Testimony p. 19
Witness: John Wilson

Dr. Wilson contends the authorized ROE from D2012.7.81 must be grossed up by 40% to account for tax differences between debt and equity.

a. Is it Dr. Wilson's contention that the $160 million of Liberty's interest in Western Water he contends was financed with APUC debt should be treated as debt of Park Water?

b. If so, please identify the legal or financial theory basis which would authorize the debt of a parent company to be allocated to Park Water under these circumstances, including identification of any statutory, administrative or other legal authority, or any academic or industry publication or treatise Dr. Wilson contends support his testimony.

c. If not, please describe why Dr. Wilson contends the rate of return allowed on the $160 million of investment he contends was funded by APUC's debt issuance is not entitled to a mark up to account for tax differences between debt and equity.

RESPONSE:

a. This question misstates the reason for grossing up the after tax ROE. The reason for the gross up is to calculate the probable income tax expense that the company will incur on its allowed rate of return. It is not Dr. Wilson's contention that Liberty acquisition financing should be treated as debt of Park Water.

b. Not applicable. However, see response to MWC-056(a)

c. The recovery of the cost of APUC's $160 million debt issuance will not incur an income tax expense obligation. Interest expenses are a deductible cost in calculating income taxes.

MWC-059. RE: Rates of Return, Wilson Testimony pp. 21-23
Witness: John Wilson

a. Please admit Mountain Water's current rates are based on an allowed rate of return of 9.l8%.

b. Please admit Mountain Water's current rates are based on rate base of $36,185,831.

c. Please admit Mountain Water's capital for purposes of determining its allowed returns for Montana regulatory purposes is its rate base.

d. Please admit the maximum authorized return for Mountain Water is therefore $3,321,859.

e. Please describe how you contend Mountain Water can achieve financing cost savings in excess of its total authorized return.

RESPONSE:

a. Yes.

b. Yes.

c. No. Mountain Water's capital is not its rate base. However, capital is typically the largest component of rate base support, so the values are often reasonably close.

d. No. The allowed rate of return is not a maximum or a minimum or a guarantee. Regulated utilities are generally afforded a reasonable opportunity to earn their allowed rate of return. In virtually all cases the actual rate of return that is earned will be either above or below the "allowed" rate of return. Likewise, in most cases the actual dollar return will be increasingly above the required test year return established in the utility company's last rate case. That is so because, as time goes on, a company's actual rate base and earned return will typically grow as rates derived from an historic test year rate base

MWC-059 continued

and test year sales are applied under changing annual circumstances. Also, as in Mountain Water's case, other changes that occur between general rate case test years, such as the refinancing of high cost debt at lower interest costs while retaining the same test year rates for utility service can result in increased profits. In any event, it is clear that APUC financed a large part of its equity acquisition from Carlyle with capital costing 4.13%, which is dramatically below Mountain Water's and Park Water's "allowed" ROE that was established under Carlyle ownership and financing. It is also clear that the value of the equity obtained in this acquisition substantially exceeded test year equity value.

e. See response to part (d).

MWC-060. RE: Authority for Adjustments, Wilson Testimony
Witness: John Wilson

a. Please identify any statutory, administrative or other legal authority Dr. Wilson contends supports the Commission imposition of the adjustments advocated in his testimony.

b. Please identify any academic or industry publication or treatise Dr. Wilson contends support the adjustments advocated in his testimony.

c. Please identify any matter from any state in which Dr. Wilson contends the regulatory authority imposed adjustments similar or analogous to any of the adjustments advocated in his testimony.

d. Please identify any matter from any state in which Dr. Wilson contends the regulatory authority imposed a cost of capital adjustment on a utility without considering changes to the utility' s other costs.

RESPONSE:

a. As explained in detail in Dr. Wilson's testimony, all of the principles, statutes and precedents underlying cost of service ratemaking and the maintenance of just and reasonable rates support Dr. Wilson's recommendations. See also the response to MWC-056 above.

b. See response to part (a).

c. See response to part (a). Also see response to MWC-055(d)

d. The pass through of acquisition or merger - enabled savings in order to obtain acquisition or merger approval seldom, if ever, goes into consideration of non-acquisition or non-merger related costs. While it is the case that all cost changes are typically considered in general rate cases, acquisition approval cases are not general rate cases. Moreover, rate of return adjustment proceedings, in which other costs are not addressed or considered have become more frequent in recent years in a number of jurisdiction, including the FERC.

MWC-060 continued

See, for example, recent NEPOOL transmission ROR proceedings such as EL 13-33-002 and EL 14-86-000.