BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

DOCKET NOS. R-2021-3027385, R-2021-3027386

AQUA PENNSYLVANIA, INC.
AQUA PENNSYLVANIA WASTEWATER, INC.

REBUTTAL TESTIMONY OF CHRISTOPHER M. HENKEL

Topics Addressed:

Certain Expense Adjustments and Adjustment Clauses

DATE SERVED: December 2, 2021
DATE ADMITTED: ____________

Aqua Statement No. 4-R

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I. INTRODUCTION AND SCOPE OF TESTIMONY

Q. Please state your name and business address?

A. My name is Christopher M. Henkel. My business address is 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010.

Q. Have you previously submitted testimony in this proceeding?

A. Yes, I sponsored AP Statement No. 4 on behalf of Aqua Pennsylvania, Inc. and Aqua Pennsylvania Wastewater, Inc. (collectively "Aqua PA", "AP", or the "Company").

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my testimony is to respond to various portions of the direct testimony presented by the Office of Consumer Advocate ("OCA") witnesses Smith and Watkins, Bureau of Investigation & Enforcement ("I&E") witnesses Wilson and Sakaya, and the Office of Small Business Advocate ("OSBA") witness Kalcic. My response includes rebuttal on the proposed Purchased Waster Adjustment ("PWA") and Energy Cost Adjustment ("ECA") mechanisms, and support for the following expenses: (a) general insurance expense, (b) purchased power expense, and (c) purchased water expense.

Q. Have you adopted any of the adjustments proposed by other parties?

A. No.

II. PURCHASED WATER ADJUSTMENT CLAUSE AND ENERGY CLAUSE ADJUSTMENT

Q. Witnesses Smith, Watkins, Wilson, Sakaya and Kalcic oppose the Company's proposed PWA and ECA clauses. Please comment.

A. The main arguments by these witnesses are: (1) that the PWA and ECA would violate the principle of "single issue ratemaking"; (2) that the PWA and ECA would be discriminatory because they would not apply to customers that receive service under negotiated contract rates established under AP's Competitive Rate Riders ("CRRs"); (3) that purchased water and energy costs are not volatile, unpredictable or significant; (4) that an adjustment clause removes incentives to control costs and achieve efficiencies; and (5) that automatic rate adjustments should not be used for costs that the utility has the ability to control.

Q. Please respond to the assertion that the PWC and ECA would be prohibited single issue ratemaking.

A. There are a number of examples where a utility is permitted to pass through certain costs through a rider or surcharge. I am advised by counsel that these mechanisms are authorized under Section 1307 of the Public Utility Code, 66 Pa.C.S. § 1307, as exceptions to general prohibition of single issue ratemaking. The Company believes it has established the criteria typically considered to allow such a mechanism.

Q. Please address the argument that the PWA/ECA should not be approved because purchased water and energy costs are not volatile, unpredictable or significant.

A. A number of witnesses describe certain criteria in order to qualify for recovery and receive Pennsylvania Public Utility Commission ("Commission") approval of an adjustment clause without citing any authority. What can be referred to are the Commission's approval of similar clauses, like the state tax adjustment surcharge or the Commission implementation of the reduced tax associated with Tax Cuts and Jobs Act. With respect to volatility, these witnesses overlook the fact that the bulk of AP's water purchases are made from municipalities or municipal authorities that are not subject to regulation by this Commission. Those entities have the authority to change rates as they deem necessary, which can result in substantial increases (or decreases) implemented quickly and unexpectedly.

Q. Please comment on the assertion that the proposed PWA and ECA would remove incentives for the Company to reduce costs and improve its efficiency.

A. I disagree with that assertion. Recovering purchased water and energy costs through the PWA and ECA, respectively, would not deprive the Commission of its authority to assure that purchased water and energy costs are prudently incurred. In fact, there would likely be greater review. If a seller's price change triggered a PWA/ECA filing, the resulting expense would be isolated for review, both at the time the filing was made and in a subsequent end-of-period reconciliation proceeding. The prudence of the Company's implementation of its purchased water and energy costs would be subject to greater scrutiny through such filings than as part of the myriad of issues that must be addressed in a base rate proceeding. In short, before claiming a cost increase for recovery under the PWA or ECA, the Company would have a greater incentive to assure that it had taken every reasonable step to minimize its purchased water and/or energy expense.

Q. What type of review would the Commission retain if the PWA and ECA were approved?

A. At the Commission's directive, all utilities, including AP, file quarterly earnings reports to allow the Commission to determine their operating results and achieved returns. The Commission already uses these reports to monitor AP's results of operation and achieved returns for purposes of administering the distribution system improvement charge ("DSIC"). In short, the Commission and other parties would have ample opportunity and ability to contest any individual proposed change in a PWA or ECA in the unlikely event it appeared that AP was earning more than a reasonable return.

Q. Please address I&E Witness Sakaya's argument that the PWA and ECA would be "discriminatory" because they would not apply to customers who have contracts established under AP's Commission-approved CRRs.

A. Under the CRRs, existing or new customers with competitive alternatives are furnished service under customer-specific contracts at prices designed to maintain sales that otherwise would be lost to the competitive alternative. Because the CRRs require the negotiated rate to be high enough to provide a contribution to AP's fixed cost recovery, keeping the CRR incremental sales provides a benefit to all customers, as compared to losing those sales altogether. For that reason, the Commission has approved the CRR as both reasonable and non-discriminatory. By contract, the price to the CRR customer increases annually based on an inflation-related index, in lieu of other periodic increases or surcharges. Witness Sakaya avers that the PWA and ECA would discriminate in favor of CRR customers and against all other customers because they would not apply to the former even though the CRR customers are served, at least in part, with purchased water. However, the exclusion of contract customers from the operation of the surcharges is not unduly discriminatory. I am advised that the Commission has approved various surcharge provisions that exempt negotiated contract rate customers. CRR customers' contract prices would not change based on increases (or decreases) in the cost of purchased water or energy regardless of whether those changes are implemented through the PWA and ECA or through changes in base rates. The CRR contract rates are not "discriminatory" because, as the Commission has recognized, increasing CRR customers' rates above their competitive alternative results in a loss of sales that, ultimately, would increase the revenues to be recovered from all other customers.

III. OPERATING EXPENSE ADJUSTMENTS

Q. Has I&E Witness Wilson at pages 14 – 15 of I&E Statement No. 1 recommended adjustments to the Company's general liability insurance expense in each of AP's divisions?

A. Yes. Ms. Wilson recommends a reduction of $298,499 to Aqua PA Water, a reduction of $17,825 to Aqua PA Wastewater Base, a reduction of $10,201 to Aqua PA Wastewater – Limerick, a reduction of $2,218 to Aqua PA Wastewater - East Bradford, a reduction of $17,661 to Aqua PA Wastewater – Cheltenham, a reduction of $11,355 to Aqua PA Wastewater – East Norriton, and a reduction of $6,245 to Aqua PA Wastewater – New Garden.

Q. On what basis does Ms. Wilson recommend these reductions to the Company's claimed General Liability Insurance Expense?

A. Ms. Wilson increased the Company's HTY insurance expense amount by 4.38%, which is the 3-year average of AP year-over-year insurance expense increases that occurred from fiscal year 2019 to fiscal year 2021, to calculate an allowance for the FTY. She applied the same increase to the FTY allowance to arrive at an allowance for the FPFTY. Ms. Wilson asserts that the 3-year average allows for consideration of more recent experience and that the 3-year average is consistent with Company's method for calculating uncollectibles and legal expense.

Q. Do you agree with this adjustment?

A. No.

Q. On what basis do you disagree with Ms. Wilson's adjustment?

A. To begin, the Company disagrees with utilizing a three-year average. The five-year average utilized by AP smooths out anomalies and volatility with respect to changes in insurance premium rates. Notwithstanding, for this proceeding, as explained later, I will accept the application of Ms. Wilson's 3-year average increase of 4.38% to update the Company's monthly insurance premiums for the last three months of the FPFTY (January to March of 2023).

Moreover, after filing its direct testimony and exhibits for this proceeding, the Company accrued its actual fiscal year ("FY") 2022 (Jan 2022 – Dec 2022) insurance expense. On a consolidated basis, the accrual results in a year-over-year increase of 8.49% between FY 2021 ($6,453,903) and FY 2022 ($7,002,098) which is much different than the 4.38% increase forecasted by Ms. Wilson; additionally, it is more accurate because it represents actual insurance premiums the Company will pay in fiscal year 2022.

The accrual update and the application of Ms. Wilson's 4.38% increase as described above affect the Company's FTY and FPFTY insurance expense claims; accordingly, the Company's updated FTY and FPFTY insurance expense claims are set forth in Schedule C-4.6 of Exhibits 1-A(a) through 1-G(g).

Q. Please explain in detail how the Company's updated FTY and FPFTY General Liability Insurance Expense claims were calculated.

A. I began by calculating AP's annual general liability insurance expense for fiscal years (January to December) 2021, 2022 and 2023. For fiscal year 2021, I relied upon the expenses that are recorded on the Company's books of record. For fiscal year 2022, I utilized the expense that was recently accrued as explained above.

I then applied Ms. Wilson's recommended three-year average increase of 4.38% to the expense that was accrued for fiscal year 2022 to arrive at the forecasted annual expense for fiscal year 2023.

Subsequently, the annual expense amounts for fiscal years 2021 to 2023 were divided by 12 to calculate the monthly expense for each respective year. From these calculations, I was able to derive the Company's updated FTY and FPFTY insurance claims.

Q. Please explain further.

A. The FTY insurance expense claim was updated by multiplying the monthly insurance expense for fiscal year 2021 by nine, then multiplying the accrued monthly insurance expense for fiscal year 2022 (as described above) by three and adding the two products together. The result reflects the Company's actual insurance expense for the FTY (April 2021 to March 2022).

Similarly, the FPFTY expense claim was updated by multiplying the updated monthly insurance expense for fiscal year 2022 by nine, then multiplying the updated monthly insurance expense forecasted for fiscal year 2023 (as described above) by three and adding those products together. The result reflects the Company's FPFTY (April 2022 to March 2023) general liability insurance claim.

Q. How are the Company's updated FTY and FPFTY General Liability Insurance Expense claims different than what was originally filed?

A. On a consolidated basis, the FTY claim increased by $28,453 and the FPFTY claim increased by $95,961.

Q. Please summarize your recommendation regarding Ms. Wilson's adjustments to the Company's claimed General Liability Insurance Expense.

A. The Commission should reject Ms. Wilson's recommended adjustments to the Company's originally filed General Liability Insurance Expense and accept AP's updated General Liability Insurance Expense as set forth on Schedule C-4.6 in Exhibits 1-A(a) through 1-G(g). The updated insurance expense claims reflect more recent and accurate information with respect to the insurance expense incurred by the Company.

Q. Has OCA Witness Smith at OCA Statement No. 1, pages 53 – 54 recommended an adjustment to AP's general liability insurance expense?

A. Yes. Mr. Smith recommends a $71,428 reduction to general liability insurance expense for water operations and a $710 reduction for wastewater operations. Similar to I&E Witness Wilson, Mr. Smith also disagrees with the Company's proposed 5.97% escalation rate to general insurance and calculates a 4.38% 3-year average year-over-year increase actual general insurance expense for 2019-2021. Notably, Mr. Smith accepted the Company's originally claimed FTY insurance expense. He applied the 4.38% 3-year average increase to the FTY to arrive at his recommended FPFTY insurance expense for the Company.

Q. Do you agree with this adjustment?

A. No. As previously mentioned, Mr. Smith's adjustment does not consider or include the fact that the Company's fiscal year 2022 Insurance Expense has been accrued to reflect the actual premiums AP will pay for the 12 months ended December 31, 2022. Although the

Company relies upon a 5-year average increase to forecast insurance expenses, for this proceeding, I will accept the application of Mr. Smith's 4.38% 3-year average increase to the Company's accrued fiscal year 2022 insurance expense to arrive at the forecasted fiscal year 2023 expense amount, as I did for I&E Witness Wilson. The Commission should otherwise reject Mr. Smith's adjustment and accept the Company's revised insurance expense claims for the FTY and FPFTY which have been updated to reflect actual expenses for fiscal year 2022.

Q. OCA Witness Smith at page 38 of OCA Statement No. 1 recommends an increase to Purchased Power Expense of $96,312, due to increase to water sales. Do you agree?

A. No. This adjustment is tied to Mr. Smith's acceptance of only a portion of the COVID usage adjustment. AP Witness Heppenstall in her rebuttal on page 19 - 20 discusses the COVID usage adjustment and rejects Mr. Smith's water sales adjustment; accordingly, I reject his increase to Purchased Power Expense.

Q. OCA Witness Smith at page 38 of OCA Statement No. 1 recommends an increase to Chemicals Expense (Water) of $66,787, due to increase to water sales. Do you agree?

No. This adjustment is tied to Mr. Smith's acceptance of only a portion of the COVID usage adjustment. For the same reasons that I reject Mr. Smith's increase to Purchased Power Expense, I also reject his increase to Chemicals Expense (Water).

IV. CONCLUSION

Q. Does that conclude your rebuttal testimony at this time?

A. Yes, it does, but I reserve the right to supplement my rebuttal testimony as needed during this proceeding.