

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

CASE 11-W-0200

PROCEEDING ON THE MOTION OF THE COMMISSION AS TO THE
RATES, CHARGES, RULES AND REGULATIONS OF
LONG ISLAND WATER CORPORATION D/B/A
LONG ISLAND AMERICAN WATER FOR WATER SERVICE

Rebuttal Testimony of John N. Casillo

October 3, 2011

1 **1. Q. Please state your name and business address.**

2 A. My name is John N. Casillo. My business address is 733 Sunrise Highway,
3 Lynbrook, New York 11563.

4 **2. Q. By whom are you employed and in what capacity?**

5 A. I am the Financial Manager of the Long Island Water Corporation, d/b/a Long
6 Island American Water ("LIAW" or the "Company"), and also serve as the
7 Company's Chief Accounting Officer.

8 **3. Q. Did you file direct testimony in this proceeding?**

9 A. Yes.

10 **4. Q. What are the areas you will address in your rebuttal testimony?**

11 A. I will respond to the testimony of the Mr. Bailey with respect to property tax
12 expense, actuarial study amortization and Pension and Other Post-
13 Employment Benefits.

14 **Property Tax Expense**

15 **5. Q. Please summarize Staff's testimony on property taxes.**

16 A. Staff is proposing property tax expense of \$10,860,629 for the rate year. This
17 is a \$3,504,649 reduction to the \$14,365,278 rate year property tax expense as
18 projected by the Company.

19 **6. Q. What was the basis of the Company's initial projection?**

20 A. The property taxes are the sum of the Nassau County/Town of Hempstead
21 general tax, the school tax district taxes billed the Town of Hempstead and the
22 various village property taxes. In the Company's projection, the 2011 general
23 tax is the actual tax for 2011. The projection for 2012 and the rate year

1 general tax are based on an increase of 23.23% in 2012 and a 9.15% increase
2 in 2013. The 2011 school tax is the annualized tax for the 2011/2012 tax year.
3 The projection for the 2011 school tax is based on the actual school tax bill for
4 the first 6 months and the projected tax for the last 6 months of the year. The
5 school tax for the period July 2011 through June 2012 is expected to increase
6 23.23% over the prior school tax year. The school tax for the next school tax
7 year, July 2012 through June 2013, is projected to increase an additional
8 9.15%.

9 The 2011 village taxes are based on the known tax for the period through
10 May 2011. The village taxes for the period June 2011 through May 2012 are
11 expected to increase 22.06% over the prior year. The village taxes for the
12 next village tax year through May 2013 are projected to increase another
13 25.57%. Please see Exhibit 12, Tab 28 and the supporting work papers for
14 further information on pro forma property taxes

15 **7. Q. How has Staff's projection of property taxes differed from the**
16 **Company's projection?**

17 A. Staff has applied a GDP inflation rate to the latest known property taxes for
18 the town, school and village taxes. Staff used the actual 2011 town tax and
19 2010/2011 school tax as in the Company's projections, however, staff used
20 the 2011/2012 village taxes. The 2011/2012 village taxes were not available
21 when the Company's projections were made.

22 **8. Q. Do you agree with Staff's adjustment and method of projecting property**
23 **tax expense in the rate year?**

1 A. I disagree with the adjustment and the methodology of projecting property
2 taxes in the rate year based on a GDP inflation rate. Underlying Staff's
3 adjustment is an assumption that the Company's property tax expense will
4 increase at a general inflation rate even though future taxes will be based on
5 future assessments times the tax rate. The New York Office of Real Property
6 Tax Services, ORPS, provides the assessments to Nassau County and the
7 villages for the Company's property in the public right of way. These special
8 franchise assessments are based on the reproduction cost new less
9 depreciation (RCNLD) value of the reported inventory of the public property
10 and when appropriate, an economic obsolescence factor is determined by
11 ORPS. As the Company makes improvements to its property through future
12 construction, the value will increase. A higher economic obsolescence factor
13 will result in a lower RCNLD value. Over time, the economic obsolescence
14 factors for LIAW approved have been decreasing. This is because the
15 Company's rate of return has been increasing. The rate of return is the key
16 component in the Economic Obsolescence calculation.

17 **9. Q. Did Staff consider the future value of the Company's property and**
18 **economic obsolescence in the projection of property tax expense in the**
19 **rate year?**

20 A. Yes. Staff has provided the property tax expense, Tentative Full Value, TFV,
21 of the Company's property as determined by ORPS and the values of the
22 Utility Plant and Service and Construction Work in Progress, UPIS and
23 CWIP, as shown in the response to IR-63 BLB-8 (see Staff Exhibit_(BLB-2)

1 page 8 of 74). Based on this, Staff has concluded that an increase in UPIS and
2 CWIP does not automatically increase TFV or property tax expense.
3 However, staff has not considered that Economic Obsolescence was also a
4 factor in determining TFV and the resulting property tax expense. The 2010
5 property tax expense of \$10,824,144 shown on that schedule was based on an
6 economic obsolescence factor of 32%. The economic obsolescence factors
7 approved by ORPS in subsequent years have fallen to 29%, 18% and 16% as
8 approved by ORPS in August 2011. As the Company's rate of return has
9 increased, the economic obsolescence factor has decreased which will
10 eventually increase assessments.

11 Also, there is a time lag between when construction costs are reported
12 to ORPS, ORPS issues special franchise assessments and advisory
13 appraisals, assets are put on the tax rolls, tax rates are reset and the tax bills
14 are issued. Moreover, an increase in the investment reported to ORPS will
15 result in higher special franchise assessments of property located in the public
16 right of way and higher values in the advisory appraisals for property located
17 on private property. The increase in these values makes it much more likely
18 that taxes will increase and given the current economic conditions and it is
19 hard to conceive that municipalities will be lowering taxes.

20 **10. Q. Staff states that between 2005 and 2010, property taxes decreased an**
21 **average of 5.6%; are there any other factors that caused this?**

22 A. Yes, as a result of the Company's court case settlement to the tax certiorari
23 challenge, Nassau County agreed to lower the assessment on the Company's

1 private and mass property because Nassau County came to realize that its
2 historic approach to valuing property was incorrect. Also, Nassau County
3 turned to using the ORPS advisory appraisals as the basis for valuing the
4 Company's mass property each year. There is no assurance that Nassau
5 County will continue to use ORPS advisory appraisals going forward and if
6 they depart from that approach it is unlikely that they will use an approach
7 that will result in lower assessments.

8 Staffs approach of using past history without consideration of future
9 construction and changes in economic obsolescence would penalize the
10 Company for its historic success in protesting its property tax assessments.
11 Past history is strongly influenced by the one time effect of the changes made
12 by Nassau County as a result of the Company's successful tax challenges.

13 **11. Q. Do you agree with Staff's recommendation that property taxes should not**
14 **be subject to a reconciliation clause.**

15 A. No. As stated previously and in my testimony, the Company proposes the
16 continuation of the Property Tax Reconciliation Clause ("PTC") with a
17 change in the clause that would allow the Company to recover or refund 100%
18 of the property tax variance through the PTC. Under the current clause, the
19 Company recovers 85% of the tax expense over the rate allowance and
20 refunds 100% of the tax expense under the rate allowance. As further stated
21 in my testimony, the Company has received tax refunds for years when the
22 Company had to absorb the difference between the rate recovery of property
23 taxes through the PTC clause and the actual higher property tax expense for

1 those years. For the period April 1999 through March 2005, the Company
2 funded \$1,017,944 (either 15% or 20%) of actual property tax paid in excess
3 of that provided in rates. Through its aggressive tax challenges, the Company
4 subsequently received refunds for the tax years that it had paid taxes in excess
5 of the PTC allowance. As stated in my testimony, the Company incurred over
6 \$1 million dollars in expense during this period above the PTC-authorized
7 level. Going forward, the Company should be made whole prior to any
8 refunds being returned to the customers.

9 **12. Q. Do you agree with Staff's recommendation that the school tax projections**
10 **be updated based on the 2011/2012 actual school tax bill.**

11 A. Yes. I agree that the Company should update its projection based on the
12 2011/2012 school tax bill and in addition should be increased based on the
13 Company's methodology. The Company has been in contact with the Nassau
14 County tax department. The 2011/2012 school tax bill should be received in
15 the second week of October. In past years, the taxes have been payable
16 without penalty on November 10th, so the tax bills should be received before
17 then.

18 **Amortization of Actuarial Study Costs**

19 **13. Q. Please summarize Staff's position on the amortization of actuarial costs.**

20 A. Staff is recommending that \$96,444 included in rate year O&M expense for
21 the amortization of actuarial costs be eliminated. The Company has incurred
22 \$289,334 in costs that it is proposing to amortize over three years.

23

1 **14. Q. Why were these costs incurred by the Company?**

2 A. These were costs incurred by the Company to have its actuary perform stand-
3 alone pension and OPEB calculations as requested by the Commission.

4 **15. Q. Why is the Staff recommending the disallowance of the amortization of
5 these actuarial costs?**

6 A. Staff has stated that the recovery of these costs was not addressed either in the
7 last rate case, Case 07-W-0508, or the pension OPEB case, Case 05-W-0339.
8 Because recovery of the cost was not authorized, in either case, Staff has
9 taken the position that the cost should not have been deferred by the
10 Company. Staff has also introduced three other conditions for an expense to
11 qualify for deferred accounting treatment. Those conditions are:

- 12 1) The expense is incremental to the amount allowed in rates:
13 2) The incremental amount is material and extraordinary in nature; and,
14 3) Earnings are below the authorized rate of return on common equity.

15 **16. Q. Did Staff address the deferral of the actuary's cost in their testimony in
16 Case 07-W-0508?**

17 A. Yes, Mr. Leary discussed this topic on page 7-8 of his testimony. In his
18 testimony he disallowed \$100,000 in costs related to the stand-alone reporting
19 for the Pension and OPEBs case, Case 05-W-0339.

20 **17. Q. Please elaborate on where Mr. Leary thought the expenses should be
21 recovered.**

22 A. Mr. Leary stated on page 8, lines 10-13 of his testimony the following:

1 Accordingly, I have removed this cost from the company's projection
2 because the recovery of those costs will be decided in the company's other
3 proceeding.

4 **18. Q. Did the Company recover these expenses in Case 05-W-0339?**

5 A. No, Case 05-W-0339 was rolled into the rate case and cost recovery was not
6 addressed.

7 **19. Q. Does the Company agree that there was no agreement that these costs be**
8 **given deferral treatment or that the costs do not meet the three conditions**
9 **to be considered for deferral treatment.**

10 A. No. As I stated in my response to IR-126 BLB-18 (see Exhibit_(JNC-1)) and
11 discussed above, the Company had requested recovery of this expense in Case
12 07-W-0508 in Rate Case Expense. Please see the responses to IR-118, IR-232
13 and IR-247 from that case, attached as Exhibit_(JNC-2). Mr. Leary's
14 testimony on page 8, lines 1 through 13 he removes these costs, as stated
15 above, as they are part of Case 05-W-0339 and recovery of those costs should
16 be decided in that case. The recovery of these costs would produce a revenue
17 requirement and therefore were not formally addressed in Case 05-W-0339
18 but instead were discussed between the Company and Staff to defer the costs
19 and seek recovery in the next rate case proceeding. These actuarial costs were
20 therefore deferred over the period 2007 through 2011.

21 There is no specific wording in either case recommending deferral
22 treatment; however, the Company was of the opinion that Staff was aware of

1 the costs being incurred and that deferral treatment would be allowed for
2 consideration in the next rate case.

3 With regard to the 3 conditions introduced in Staffs testimony, the expense
4 was incremental to that allowed in rates. This incremental amount was only
5 incurred because the Commission required that the Company obtain stand-
6 alone calculations from its actuary. These stand-alone calculations are not
7 necessary for the actuaries work on the parent company's pension and OPEB
8 plans. Also, as alluded to in Mr. Bailey's testimony, \$118,579 was spent on
9 these stand-alone calculations in 2007, an amount in excess of 5% of 2007 net
10 income and a year when the Company was in a loss position and earning
11 below it authorized rate of return.

12 **20. Q. What is the Company's recommendation regarding these costs?**

13 A. The Company believes that it should recover 100% of the deferred costs for
14 the stand-alone calculations that resulted from Staff's questions in its rate case
15 and Case 05-W-0339. The Company believes that it should be allowed to
16 defer all future costs related to the stand-alone calculations to be addressed in
17 the following rate case. In lieu of future deferred treatment the Company
18 believes it should be allowed to recover \$35,000 in annual expenses in this
19 case for the on-going stand-alone calculations that we are requested to
20 perform. Another alternative is to include the studies in the Internal Reserve
21 as an expense in order to flow through the actual costs associated with each
22 plan.

1 **Pension and Other Post Employment Benefits:**

2 **21. Q. Why isn't the Company filing for Pension and Other Post Employment**
3 **Benefits (OPEB) cost on a stand-alone basis as recommended by Staff?**

4 A. The Company is not seeking recovery of pension and OPEB cost on a stand
5 alone basis because it would be onerous to both the ratepayers and the
6 Company. The Company is seeking a waiver from this requirement within the
7 Commission's Pension and OPEB Policy Statement, Case 91-M-0890 and
8 requests permission to seek recovery of Pension and OPEB expenses based on
9 the allocation to the Company for its share of the Pension and OPEB cost of
10 the AWW consolidated plans that Long Island American Water's employees
11 and retirees are members of. It would be onerous to both the ratepayers and
12 LIAW if it were to seek recovery on a stand alone basis.

13 **22. Q. How is the recovery of pension and OPEB cost on a standalone basis**
14 **onerous to the ratepayers?**

15 A. LIAW is seeking recovery of combined pension and OPEB cost in the rate
16 year of \$1,333,450 as shown in Exhibit 9 page 21 of 46 of the original filing.
17 If the Company was to seek recovery based on a stand alone basis as
18 recommended by Staff, the combined pension and OPEB cost in the rate year
19 would be \$3,043,100 or an increase of \$1,659,650. This would be onerous to
20 the ratepayers for the obvious need to recover these increased costs through
21 higher rates with no known benefit.

22 **23. Q. How would the recovery of pension and OPEB cost on a standalone basis**
23 **be onerous to the Company?**

1 A. It would be onerous to the Company because it would increase the balance in
2 the internal reserve that the Company is currently accruing interest on at the
3 pre tax rate of return. The Company's share of the contributions in the
4 pension and OPEB trusts would not increase if the Company recovered an
5 additional \$1,659,650 for pension and OPEB expense through rates. In
6 addition, as also discussed within Cynthia King's testimony, the Company
7 would incur significant additional costs to manage and administer a
8 standalone plan for LIAW. If Staff was to agree that pension and OPEB costs
9 should be based on an allocated versus stand alone basis, it would eliminate
10 the need for the engaging the Company's actuary to perform stand alone
11 calculations. The cost of this service, discussed above in the Amortization of
12 Actuarial Study Cost could be avoided going forward. Please see Ms. King's
13 testimony for additional information on this issue.

14 **24. Q. Does this conclude your rebuttal testimony?**

15 A. Yes, it does.