

Exhibit No. \_\_\_\_\_  
Issue: Maintenance and Repair, Electrical  
Service Fee, Audit and Tax Preparation,  
Corporate Allocations, Bank Analysis Fees  
Witness: Phil Macias  
Type of Exhibit: Surrebuttal Testimony  
Sponsoring Party: Indian Hills  
Case No.: WR-2017-0259  
Date: November 13, 2017

**Missouri Public Service Commission**

**Surrebuttal Testimony**

**of**

**Phil Macias**

**On Behalf of**

**Indian Hills Utility Operating Company, Inc.**

**November 13<sup>th</sup>, 2017**

**AFFIDAVIT**

STATE OF MISSOURI     )  
                                  )  
COUNTY OF St. Louis    )     ss

I, Phil Macias, state that the answers to the questions posed in the attached Surrebuttal Testimony are true to the best of my knowledge, information and belief.



Subscribed and sworn to before me this 13<sup>th</sup> day of November, 2017.

  
Notary Public

My Commission Expires: 01/31/2021



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**SURREBUTTAL TESTIMONY OF  
PHIL MACIAS  
INDIAN HILLS UTILITY OPERATING COMPANY, INC.**

**WITNESS INTRODUCTION**

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**Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

A. My name is Phil Macias. My business address is 500 Northwest Plaza Drive  
Suite 500. St. Ann MO, 63074

**Q. ARE YOU THE SAME PHIL MACIAS THAT PROVIDED DIRECT AND  
REBUTTAL TESTIMONY IN THIS PROCEEDING?**

A. Yes.

**PURPOSE**

**Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

A. The purpose of my surrebuttal testimony is to respond to the rebuttal testimony of  
Ms. Ashley Sarver, witness for the Staff of the Missouri Public Service  
Commission, on Corporate Allocations, banking fees, and audit fees; Mr. John  
Robinett, witness for the Office of the Public Counsel (OPC), on the capitalization  
of leak repairs and categorization electrical investment; and, Ms. Keri Roth,  
witness for the OPC, on audit and tax fees.

**MAINTENANCE AND REPAIR EXPENSE**

1  
2 **Q. DOES INDIAN HILLS CONTINUE TO DISAGREE WITH THE COMMISSION**  
3 **STAFF AND OPC IN REGARD TO ITS PROPOSED TREATMENT OF**  
4 **MAINTENANCE AND REPAIR EXPENSE?**

5 A. Yes. We disagree with the Staff recommendations as to maintenance and repair  
6 expense as reflected in the Rebuttal Testimony of Staff Witness Jennifer  
7 Grisham. We disagree with the OPC recommendations as reflected in the  
8 rebuttal testimony of Mr. Robinett.

9 **Q. WHAT RECOMMENDATIONS DID THOSE WITNESSES MAKE?**

10 A. These witnesses recommend that instead of future repairs, the Company perform  
11 replacements of service lines and water mains, costs that are capital  
12 investments.

13 **Q. WHY DO YOU DISAGREE WITH THE RECOMMENDATIONS?**

14 A. As described in the testimony of Indian Hills witness Thomas and Staff Witness  
15 Spratt, the existing water system has been in a significant state of disrepair due  
16 to a lack of re-investment and substandard construction over the last 50 years.  
17 Ms. Grisham seems to suggest that replacement will solve repair issues at Indian  
18 Hills, but it is not practical to make a wholesale replacement of the distribution  
19 system in a short period of time and the Company cannot accurately predict  
20 where, how, or when repair issues will arise due to the severe state of disrepair  
21 of the existing water infrastructure. The repairs are going to be a continuing  
22 expense. As such, they are part of our on-going operational requirement to

1 provide safe, reliable service, and should be reflected in the Company's revenue  
2 requirement.

3 **Q. DO YOU AGREE WITH STAFF WITNESS STEPHEN MOILANEN'S**  
4 **CLASSIFICATION OF THE REPAIR EXPENSE?**

5 **A.** Yes. Mr. Moilanen correctly identifies why the Indian Hills work in question is  
6 repair expense as defined by the NARUC Uniform System of Accounts (1973).

7 **Q. DO YOU DISAGREE WITH OPC WITNESS ROTH'S CHARACTERIZATION OF**  
8 **YOUR DIRECT TESTIMONY ON REPAIR COSTS?**

9 **A.** Yes.

10 **Q. WHAT IS INCORRECT ABOUT MS. ROTH'S CHARACTERIZATION?**

11 **A.** Ms. Roth suggests that I am attempting bring future test year expenses into  
12 Indian Hills' current revenue requirement. I was not suggesting that those future  
13 amounts should be used in the revenue requirement to be established in this  
14 case. However, I do think those known amounts are relevant to an assessment  
15 of how to treat the past amounts in setting that revenue requirement given the  
16 positions of the parties. As I provided in my rebuttal testimony and the schedules  
17 submitted with my direct testimony, if the most recent Indian Hills repair expense  
18 was used, the resulting revenue requirement would be much higher than what  
19 the company is currently seeking. I have shown that our repair expenses have  
20 not dropped and will continue to trend higher going forward.

21 **Q. WHAT IS THE APPROPRIATE TREATMENT OF THIS ISSUE?**

22 **A.** The repair costs at Indian Hills were incurred inside the test year, they are  
23 known, measurable and, as the NARUC USOA states, the expenses clearly

1 qualify as “Work performed specifically for the purpose of preventing failure,  
2 restoring serviceability, or maintaining the life of the water systems.” In addition,  
3 the repair costs are clearly going to be reoccurring as I have shown using recent  
4 data. Amortization is inappropriate.

5 **Q. WHAT AMOUNT SHOULD THE COMMISSION INCLUDE IN INDIAN HILLS’  
6 REVENUE REQUIREMENT FOR MAINTENANCE AND REPAIR EXPENSE?**

7 A. \$99,303.

8 **ELECTRICAL SERVICE FEE**

9 **Q. STAFF WITNESS JENNIFER GRISHAM HAS TAKEN THE POSITION THAT  
10 THE COSTS ASSOCIATED WITH THE ELECTRIC SERVICE UPGRADE  
11 REQUIRED FOR THE BUILDING OF THE NEW WELL, BOOSTER PUMPS,  
12 GROUND STORAGE AND WELL HOUSE SHOULD BE TREATED AS RATE  
13 BASE. DOES THE COMPANY AGREE WITH STAFF’S PROPOSED  
14 TREATMENT OF THESE COSTS?**

15 A. Yes. We continue to agree with Staff that the cost associated with bringing  
16 power into the Indian Hills facility was an expenditure related to, and was  
17 reasonably and necessarily incurred as a part of, the Company’s (electrically  
18 powered) capital investment. The central issue is to identify the cost of both the  
19 goods and related scope of services that were necessarily incurred in the  
20 process of preparing the plant to be both “in use and usable.” Both the NARUC  
21 USOA and Generally Accepted Accounting Principles (GAAP) allow for the  
22 capitalization of costs associated with the construction of utility facilities.

23 **Q. WHAT DOES OPC PROPOSE IN REGARD TO THESE COSTS?**

1 A. OPC Witness Robinett continues to propose that these costs be treated as  
2 expenses and amortized over a five-year period.

3 **Q. WHAT IS FLAWED WITH OPC'S PROPOSAL?**

4 A. The total cost of any investment in capital equipment properly includes any of a  
5 number of other associated expenditures such as the cost of delivery, of labor  
6 expenses related to set-up, installation, testing & evaluation prior to placing the  
7 equipment in service, taxes, certain employee benefits, certain insurance costs  
8 and any additional special services and/or construction specifically related to the  
9 asset(s) and which are a functional necessity – i.e., required to ensure the  
10 equipment can operate and operate properly.

11 **Q. HOW SHOULD THE COST OF THE ELECTRICAL IMPROVEMENT BE**  
12 **TREATED?**

13 A. Both GAAP and the NARUC USOA allow Account 325 of the USOA to capture  
14 the cost of electrical pumping equipment, including installation. This includes the  
15 electrical facilities needed to bring power to the equipment, whether owned by  
16 Indian Hills or not. The initial service fee paid to Crawford County Electrical  
17 Cooperative was nonrefundable, was required for a permanent improvement to  
18 the water system, and was an ordinary and necessary cost directly associated  
19 with the building of the new well, booster pumps, ground storage, and well  
20 house. The electrical equipment associated with Indian Hills falls within the  
21 scope of USOA Account 325. Accordingly, this electrical line improvement  
22 should also be appropriately recorded in Account 325, as Staff Witness Ms.  
23 Grisham states.



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**AUDITING AND INCOME TAX PREPARATION FEES**

**Q. DOES THE COMPANY CONTINUE TO DISAGREE WITH THE COMMISSION STAFF IN REGARD TO AUDITING AND TAX PREPARATION FEES?**

**A.** No. Staff Witness Ashley Sarver has now included audit and tax preparation fees for Indian Hills and the pro-rata share of audit & tax preparation fees from First Round CSWR, LLC in her Rebuttal Testimony.

**Q. HOW IS THE OPC TREATING AUDITING AND TAX PREPARATION FEES?**

**A.** OPC Witness Roth excluded both the audit and tax preparation fees for Indian Hills and the pro-rata share of audit fees from First Round CSWR, LLC and allowed for a small portion of tax fees from First Round CSWR, LLC from 2015 in her Rebuttal Testimony.

**Q. WHY DOES OPC WITNESS ROTH ALLEGE THAT THESE FEES SHOULD BE EXCLUDED?**

**A.** Ms. Roth alleges they should be excluded because the Tax and Audit expense payment fell outside of the test year.

**Q. ARE THESE FEES A REASONABLE EXPENSE RELATED TO THE PUBLIC UTILITY OPERATIONS OF INDIAN HILLS?**

**A.** Yes. The 2016 Financial Audit and the 2016 Income Tax Returns are an integral component of the 2016 Indian Hills financial year, tax year, and test year. The audit and tax expenses are for the test year, the expense is known, measurable, and recurring, thus they should be part of Indian Hill's revenue requirement as both the Company and Staff have stated.

**CORPORATE ALLOCATIONS**

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**Q. STAFF WITNESS SARVER EXPLAINS IN HER REBUTTAL TESTIMONY STAFF’S APPROACH TO THE CORPORATE ALLOCATIONS. DO YOU AGREE WITH THE STAFF’S CORPORATE ALLOCATION APPROACH?**

A. No. The Staff continues to use a flawed methodology for the determination of corporate allocations.

**Q. WHAT IS FLAWED ABOUT THE STAFF ALLOCATION METHODOLOGY?**

A. I believe procedural errors in Staff’s execution of the model are compounded through the multi-step methodology and ultimately produce an answer that is incorrect.

**Q. WHAT IS INCORRECT ABOUT THE STAFF’S CORPORATE ALLOCATION MODEL?**

A. As discussed in my previous testimony, Staff’s allocation model is designed around five basic steps/calculations with each step being used as input for subsequent calculations. The Company does not have an issue with the overall design of the model, but does have concerns to the extent that Staff was not consistent is the use of the model for all employees and in some cases input data they acknowledged as being “assumed,” rather than using data available from the model.

**Q. WHAT ASSUMPTIONS DO YOU DISPUTE?**

A. To begin, Ms. Sarver notes that there was an increase in the number of employees at the parent company and asserts that an increase in the number of employees at the parent company should not equate to an increase in the

1 number of hours needed to complete required work related to Indian Hills. Ms.  
2 Sarver's calculation implies that additional personnel at the parent company  
3 automatically results in an increase in the labor hours required to effectively  
4 manage the required work at Indian Hills. There is a relationship between the  
5 required labor at Indian Hills and staffing at the parent company, but Ms. Sarver  
6 has reversed the case and effect. Parent company staffing did not drive  
7 additional required work at Indian Hills. It was the additional required work at  
8 Indian Hills that drove an increase in parent company staff.

9 For example, the Staff has reviewed timesheets that show a significant increase  
10 in overtime worked. This shows there are not too many team members but,  
11 based on the timesheet verified workload, there may be too few.

12 **Q. WHAT SPECIFIC PROBLEMS DOES THE STAFF'S CORPORATE**  
13 **ALLOCATION MODEL HAVE?**

14 A. The methodology Staff used to calculate allocations is a multistep process that  
15 has compounding errors.

16 **Q. PLEASE DESCRIBE STEP 1 OF THAT PROCESS AND YOUR THOUGHTS.**

17 A. Step 1 (IH Direct Assigned): Since employee labor hours are recorded by  
18 function (i.e., what company the employee was working for and (within general  
19 categories) what the employee was working on), it's only the portion of total  
20 hours associated with Indian Hills that drive the corporate allocation. It's  
21 because of this fact that the total number of parent company employees is  
22 irrelevant. As stated on Staff's Accounting Schedule "Allocation for Indian Hills"  
23 the total labor hours directly charged to Indian Hills was (1,056.3) for the test

1 year. By using this value in their analysis, Staff has accepted this number to be  
2 true and reliable. The number of people among whom these hours are divided is  
3 not relevant. In fact, since the required quantity of Indian Hills labor hours is now  
4 known and supported by Staff, from a purely mathematical perspective the  
5 greater the number of employees at the parent company, the lower the  
6 percentage of the corporate allocation. In short, the key to determining the  
7 correct corporate allocation percentage has nothing to do with the total number of  
8 parent company employees. It has everything to do with using a meaningful  
9 methodology in a correct and consistent manner.

10 Contrary to witness Sarver's assertion that the staff's method was consistent it, in  
11 fact, was not and this inconsistency was revealed in Sarver's rebuttal testimony  
12 (p.5).

13 In this step, Staff used actual recorded hours for the President, the SR Vice  
14 President and the Customer Service Manager. These were all full time positions  
15 and Staff was correct to use actual hours. However, Staff then chose not to use  
16 the actual hours for the 4th full time position (Chief Financial Officer), which  
17 existed and was filled for the entire test period. Failure to use actual hours for  
18 this position was inconsistent and incorrect. Likewise, actual hours for the two-  
19 remaining employee/positions were also available in staff's model but were not  
20 used. Rather, the hours for all three of these positions which had sharply  
21 different totals (85.3(IH)/699.45(total); 147.45(IH)/2,052.15(Total) &  
22 25.15(IH)/227.15(Total)) were blended together and the average was then  
23 applied to each position. This treatment was inconsistent and not reasonable.

1 **Q. PLEASE DESCRIBE STEP 2 OF THAT PROCESS AND YOUR THOUGHTS.**

2 A. Step 2 (Administrative Hours): This step is intended to capture the hours directly  
3 assigned to an Administrative category. As in step 1, Staff uses recorded hours  
4 for three of the positions but then uses a blended value for the remaining three,  
5 when actual hours are available for all six. The actual, recorded hours for all six  
6 positions should have been used in this step. This is important not just because  
7 of consistency, but also because the result of step 2 is then used as the  
8 numerator of a ratio (in step 3) that impacts the value of the corporate allocation.

9 **Q. PLEASE DESCRIBE STEP 3 OF THAT PROCESS AND YOUR THOUGHTS.**

10 A. Step 3 (Administrative Regulated): In step three, Staff again calculates a  
11 blended average for 3 employee/positions (but this time it is a different mix of  
12 employees than in the previous steps), which further distorts the results. Actual  
13 hours by individual were available and should have been used. However, Staff  
14 used the company-wide average (hours charged to regulated companies / hours  
15 charged to non-regulated companies) of all six positions and multiplied the  
16 quotient of that ratio to the step two results for only the 3 averaged employees.  
17 The resulting step three value is the product of that equation.

18 For two additional employees/positions (Macias and Thomas) staff used a  
19 different process. As provided in Ms. Sarver's rebuttal testimony (page 5), rather  
20 than rely on the data available from Staff's model, she used an "assumed" value  
21 of 66.6% as the percentage of non-admin hours allocated to regulated  
22 companies divided by total non-Admin labor hours. Not only is this method  
23 inconsistent with that used for the first three employees, it is relevant facts that

1 are readily available. For Macias, the fact-based model driven percentage was  
2 100%. For Thomas, the fact-based model driven percentage was 90.39%. For  
3 the final position (Cox), Staff again declines to use the percentage available from  
4 their data table. As with Macias and Thomas, Staff again assigned an “assumed”  
5 value to the calculation for Mr. Cox. In this case, the rate selected was 50%  
6 while the fact-based model driven value was 79.81%.

7 Staff declined to use fact based data available from their model and instead  
8 applied values they “assumed” to be reasonable for Cox, Thomas and Macias.  
9 Staff’s use of arbitrary and inaccurate percentages in lieu of their own fact-based  
10 model driven information is not reasonable.

11 **Q. PLEASE DESCRIBE STEP 4 OF THAT PROCESS AND YOUR THOUGHTS.**

12 A. Step 4 (Administrative IH): To obtain the value for step 4, Staff multiplies the  
13 results from step 3 and the ratio of company-wide Indian Hills hours to company-  
14 wide regulated company hours. While we have no concerns from a process  
15 perspective, it’s important to note that because staff’s step 3 results include  
16 compounded errors, the results of the step 4 calculation are also incorrect.

17 **Q. PLEASE DESCRIBE STEP 5 OF THAT PROCESS AND YOUR THOUGHTS.**

18 A. Step 5 (Total IH): The step five value is the sum of steps one and four. Because  
19 each of the preceding steps were calculated incorrectly, step five is also  
20 incorrect. With these five underlying steps in place, the total of the individual  
21 employee values are added together and used as the numerator in the ratio of  
22 total Indian Hills hours divided by total FR-CSWR hours. The result is the  
23 corporate allocation.

1 **Q. WHAT ALLOCATION PERCENTAGE DID STAFF DERIVE FROM THIS**  
2 **PROCESS?**

3 A. Staff's process resulted in an allocation percentage of 16.61%.

4 **Q. IF YOU CORRECT THE ERRONEOUS ASSUMPTIONS AND UTILIZE**  
5 **ACTUAL HOURS IN STAFF'S MODEL, WHAT ALLOCATION DO YOU**  
6 **CALCULATE?**

7 A. The corrected rate (using Staff's model and actual recorded hours) is 17.52%.

8 **BANK ANALYSIS FEES**

9 **Q. IN HER REBUTTAL TESTIMONY, STAFF WITNESS SARVER STATES THAT**  
10 **THE COMPANY SHOULD DO A COST BENEFIT OF THE BANK ANALYSIS**  
11 **FEES. WHAT IS THE COMPANY'S POSITION IN REGARD TO THAT**  
12 **SUGGESTION?**

13 A. Indian Hills has agreed to perform a cost benefit analysis of the bank service fees  
14 as part of the partial stipulation agreement. While Indian Hills is confident this  
15 future study will show how these fees are a net benefit to the customers in terms  
16 of overall final cost of service and level of service provided to the customer,  
17 Indian Hills continues to be agreeable to performing a new analysis for Staff's  
18 review

19 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

20 A. Yes, it does.