

**FILED**  
January 6, 2017  
**INDIANA UTILITY  
REGULATORY COMMISSION**

**STATE OF INDIANA**

**INDIANA UTILITY REGULATORY COMMISSION**

**IN THE MATTER OF THE PETITION OF )  
BLOOMINGTON, INDIANA, FOR AUTHORITY TO )  
ISSUE BONDS, NOTES, OR OTHER OBLIGATIONS, )  
FOR AUTHORITY TO INCREASE ITS RATES AND )  
CHARGES FOR WATER SERVICE, AND FOR )  
APPROVAL OF A NEW SCHEDULE OF WATER )  
RATES AND CHARGES )**

**CAUSE NO. 44855**

**SETTLEMENT TESTIMONY OF**

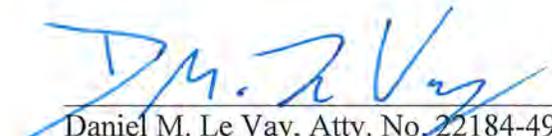
**EDWARD R. KAUFMAN – PUBLIC’S EXHIBIT NO. 3**

**ON BEHALF OF THE**

**INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR**

**JANUARY 6, 2017**

Respectfully submitted,

  
Daniel M. Le Vay, Atty. No. 22184-49  
Deputy Consumer Counselor

**TESTIMONY OF OUCC WITNESS EDWARD R. KAUFMAN, CRRA**  
**CAUSE NO. 44855**  
**BLOOMINGTON MUNICIPAL WATER**

**I. INTRODUCTION**

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

2 A: My name is Edward R. Kaufman, and my business address is 115 W. Washington  
3 St., Suite 1500 South, Indianapolis, IN 46204

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

5 A: I am employed by the Indiana Office of Utility Consumer Counselor (OUCC) as a  
6 Chief Technical Advisor with the Water-Wastewater Division. My Qualifications  
7 and experience are set forth in Appendix A.

8 **Q: What is the purpose of your testimony?**

9 A: My testimony supports the settlement agreement and recommends the Commission  
10 approve Bloomington's (Petitioner or Water Utility) proposed \$4,575,000 debt  
11 issuance, subject to certain adjustments and reporting requirement. I recommend  
12 placing restrictions on Petitioner's debt service reserve to ensure the funds are  
13 available if needed. My testimony also discusses the cost of capital leases that  
14 Petitioner included in its revenue requirements.

**II. ANNUAL DEBT SERVICE**

15 **Q: Please describe Petitioner's proposed debt issuance.**

16 A: Petitioner proposes to borrow \$4,575,000 for specified capital projects. The  
17 proposed annual debt service on Petitioner's combined debt is \$5,646,558.

1           Petitioner's proposed annual debt service assumes it will issue debt at the "AA"  
2           rate plus a spread of 100 basis points (as of March 4, 2016).

**A. Interest Rates**

3   **Q:    Do you accept Petitioner's proposed interest rates and the subsequent annual**  
4   **debt service on Petitioner's proposed debt?**

5   A:    While I would typically disagree with a 100 basis point as spread, such as that  
6        proposed by Mr. Skomp, because interest rates have trended upward since  
7        Petitioner filed its testimony, I accept the amortization schedule provided in its  
8        testimony.  Moreover, the parties agree that the annual debt service be subject to  
9        a true-up.  Thus to the extent the actual interest rates are different than those used  
10       to estimate Petitioner's annual debt service, Petitioner's rates will reflect the actual  
11       cost of its debt service.

**B. Debt Timing**

12   **Q:    Will there be a gap between the time Petitioner receives an order in this Cause**  
13   **and when it issues its proposed debt?**

14   A:    Petitioner cannot issue its proposed long-term debt until the Commission issues an  
15        order in this Cause, so there will necessarily be some amount of time between the  
16        date of the final order and the issuance of Petitioner's debt.  This gap in time only  
17        becomes a concern if Petitioner does not timely issue its proposed debt because, in  
18        the interim, it will receive revenues to pay a debt service expense that is not being  
19        incurred.  The parties agreed that if Petitioner does not issue its debt within four  
20        months of a final order in this Cause, Petitioner should temporarily reserve the  
21        funds collected in rates for its 2016 debt and use those funds to reduce the amount  
22        it needs to fund its debt service reserve.  For example, if Petitioner issued its

1 proposed debt four months after the final order in this Cause, over which period it  
2 collected \$25,000 per month for its 2016 debt, then it would use the \$100,000 (4 \*  
3 \$25,000) it collected to reduce the amount it needs to collect for its debt service  
4 reserve. This proposal matches revenues collected for Petitioner's proposed 2016  
5 bonds against its actual expense for its 2016 bonds. As such, this provision should  
6 be considered reasonable and in the public interest.

### **C. True-up and Other Issues**

7 **Q: Should reporting requirements be included as part of Petitioner's proposed**  
8 **debt issuance?**

9 A: Yes. The precise interest rates and annual debt service will not be known until  
10 Petitioner's debt is issued; therefore, Petitioner's rates should be trued-up to reflect  
11 the actual cost of the debt. The parties agreed Petitioner should file a report, within  
12 thirty (30) days of closing on its long term debt issuance with the Commission and  
13 serve a copy on the OUCC, explaining the terms of the new loan, including an  
14 amortization schedule, the amount of debt service reserve and an itemized account  
15 of all issuance costs. The report should include a revised tariff and also calculate  
16 the rate impact in a manner similar to the OUCC's schedules.

17 **Q: What other conditions will be placed on Petitioner's proposed debt issuance?**

18 A: The parties agreed that if Petitioner issues its debt for less than the amount  
19 authorized by the Commission, (unless otherwise agreed to by the parties) any  
20 unused financing authority should terminate.

### **D. Debt Service Reserve**

21 **Q: Is Petitioner seeking to recover funds for the debt service reserve on its**  
22 **proposed 2016 bonds through rates?**

1 A: No. Petitioner plans to prefund its debt service reserve and has included \$317,372  
2 (Skomp Exhibit E) in its proposed loan.

3 **Q: Will there be any restrictions on Petitioner's proposed debt service reserve?**

4 A: Yes. If Petitioner spends any funds from its debt service reserves for any reason  
5 other than to make the last payment on its proposed debt issuance, Petitioner should  
6 be required to provide a report to the Commission and the OUCC within five (5)  
7 business days of said transaction. The report should state how much Petitioner spent  
8 from its debt service reserve, explain why it spent funds from its debt service  
9 reserve, provide a cite to any applicable loan documents that allow it to spend funds  
10 from its debt service reserve, describe its plans to replenish its debt service reserve,  
11 and explain any cost-cutting activities Petitioner has implemented to forestall  
12 spending funds from its debt service reserve.

**E. Capital Leases**

13 **Q: Petitioner's proposed revenue requirement included \$82,061 for a 2013**  
14 **Capital Lease and \$76,537 for a 2014 Capital Lease. Does the Settlement use**  
15 **the amount Petitioner has included in revenue requirements for these leases?**

16 A: No. The Settlement Agreement establishes that each leases' remaining balance  
17 should be recovered over the anticipated life of Petitioner's rates. The annual  
18 revenue requirement for the 2013 Lease will be \$32,823 ( $\$164,115 / 5$ ) and the  
19 annual revenue requirement for the 2014 Lease will be \$53,549 ( $\$267,743 / 5$ ).

20 **Q: Why is this appropriate for settlement purposes?**

21 A: The 2013 Lease is set to expire in July 2018 and the 2014 Lease is set to expire  
22 January 1, 2020. Thus, assuming Petitioner's rates are in place for 5 years, it will  
23 over-collect on its leases. For example, the remaining payments on the 2013 Lease

1 are \$164,115.42<sup>1</sup>, yet as proposed Petitioner would collect \$413,005 over the  
2 anticipated life of its rates. Thus, without this settlement proposal, Petitioner would  
3 over collect more than \$248,000 on its 2013 Lease. While not as large the same  
4 situation occurs on Petitioner's 2014 Lease. The remaining payments on the 2014  
5 Lease are \$267,743<sup>2</sup>, yet Petitioner would have collected \$382,685 over the  
6 anticipated life of its rates.

### III. OUCC RECOMMENDATIONS

7 **Q: Please summarize your testimony.**

8 A: The Settlement includes the following related to Petitioner's proposed debt and its  
9 leases:

- 10 1) The Parties have agreed the Commission should authorize Petitioner to issue up  
11 to \$4,575,000, in long-term at a maximum interest rate of 7.0%.
- 12 2) Petitioner's revenue requirements include \$5,646,558 for the annual debt  
13 service on its current and proposed bonds.
- 14 3) If Petitioner does not issue its proposed debt within 4 months after it has filed  
15 a revised tariff with the Commission it should temporarily reserve the funds  
16 collected in rates for its 2016 debt and use those funds to offset the amount it  
17 borrows.
- 18 4) Within thirty (30) days of closing on its long term debt issuance, Petitioner shall  
19 file a report with the Commission and serve a copy on the OUCC, explaining  
20 the terms of the new loan, including an amortization schedule, the amount of  
21 debt service reserve and all issuance costs. The report should include a revised  
22 tariff and also calculate the rate impact in a manner similar to the OUCC's  
23 schedules. Petitioner's rates should be trued-up if necessary to match its actual  
24 cost of debt service.

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<sup>1</sup> This figure includes the \$41,030.17 payment that Petitioner will make on January 15, 2017.

<sup>2</sup> This figure includes the \$38,233.08 payment that Petitioner will make on January 1, 2017.

1           5) If Petitioner spends any of the funds from its debt service reserves for any  
2           reason other than to make the last payment on its proposed 2016 debt issuance;  
3           Petitioner shall provide a report (as described above) to the Commission and  
4           the OUCC within five (5) business days.

5           6) The remaining balance on Petitioner's 2013 and 2014 Capital Leases should be  
6           recovered over the anticipated life of Petitioner's rates. The annual revenue  
7           requirement for the 2013 Lease should be \$32,823 ( $\$164,115 / 5$ ) and the annual  
8           revenue requirement for the 2014 Lease should be \$53,549 ( $\$267,743 / 5$ ).

9    **Q: Does this conclude your testimony?**

10   A: Yes.

**IV. APPENDIX A**

1 **Q: Please describe your educational background and experience.**

2 A: I graduated from Bentley College in Waltham, Massachusetts with a Bachelors  
3 degree in Economics/Finance and an Associates degree in Accounting. Before  
4 attending graduate school, I worked as an escheatable property accountant at State  
5 Street Bank and Trust Company in Boston, Massachusetts. I was awarded a  
6 graduate fellowship to attend Purdue University where I earned a Masters of  
7 Science degree in Management with a concentration in finance.

8 I was hired as a Utility Analyst in the Economics and Finance Division of  
9 the OUCC in October 1990. My primary areas of responsibility have been in utility  
10 finance, utility cost of capital, and regulatory policy. I was promoted to Principal  
11 Utility Analyst in August 1993 and to Assistant Chief of Economics and Finance  
12 in July 1994. As part of an agency wide reorganization in July 1999, my position  
13 was reclassified as Lead Financial Analyst within the Rates/Water/Sewer Division.  
14 In October, 2005 I was promoted to Assistant Director of the Water/Wastewater  
15 Division. In October 2012, I was promoted to Chief Technical Advisor. I have  
16 participated in numerous conferences and seminars regarding utility regulation and  
17 financial issues. I was awarded the professional designation of Certified Rate of  
18 Return Analyst (CRRA) by the Society of Utility and Regulatory Financial  
19 Analysts (SURFA). This designation is awarded based upon experience and the

1 successful completion of a written examination. In April 2012, I was elected to  
2 SURFA's Board of Directors.

3 **Q: Have you previously testified before the Indiana Utility Regulatory**  
4 **Commission?**

5 A: Yes. I have testified before the Indiana Utility Regulatory Commission  
6 (Commission) in a number of different cases and issues. I have testified in water,  
7 wastewater, natural gas, telecommunication and electric utility cases. While my  
8 primary areas of responsibility have been in cost of equity, utility financing, fair  
9 value, utility valuation and regulatory policy, I have also provided testimony on  
10 trackers, guaranteed performance contracts, declining consumption adjustments,  
11 and other issues.

12 **Q: Please describe the review and analysis you conducted to prepare your**  
13 **testimony.**

14 A: I reviewed the Petition, testimony, and exhibits filed by Petitioner in this Cause. I  
15 participated in conducting discovery and reviewed Petitioner's responses. Finally,  
16 I reviewed publications such as Value Line which provide forecasted interest rates.

**AFFIRMATION**

I affirm, under the penalties for perjury, that the foregoing representations are true.

  
Edward R. Kaufman  
Indiana Office of Utility Consumer Counselor

January 6, 2017  
Date

Cause No. 44855  
City of Bloomington, IN  
Bloomington Municipal Water

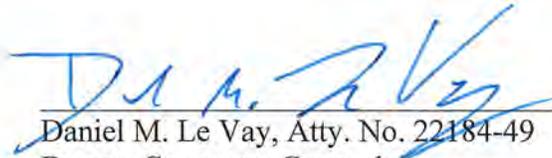
**CERTIFICATE OF SERVICE**

This is to certify that a copy of the foregoing *Settlement Testimony of Edward R. Kaufman: Public's Exhibit No. 3* has been served upon the following counsel of record in the captioned proceeding by electronic service on January 6, 2017.

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