

**BEFORE THE STATE OF NEW JERSEY
BOARD OF PUBLIC UTILITIES
OFFICE OF ADMINISTRATIVE LAW**

IN THE MATTER OF THE :
PETITION OF SHORELANDS : **BPU Docket No. WR04040295**
WATER COMPANY, INC. FOR :
AN INCREASE IN BASE RATES : **OAL Docket No. PUCRA04214-2004S**
FOR WATER SERVICE, DEFERRED :
ACCOUNTING AND OTHER :
TARIFF MODIFICATIONS :

**DIRECT TESTIMONY OF ANDREA CRANE
REGARDING REVENUE REQUIREMENTS
AND COST OF CAPITAL
FILED ON BEHALF OF THE
NEW JERSEY DIVISION OF THE RATEPAYER ADVOCATE**

**SEEMA M. SINGH, ESQ.
RATEPAYER ADVOCATE**

Division of the Ratepayer Advocate
31 Clinton Street, 11th Floor
P. O. Box 46005
Newark, New Jersey 07101
(973) 648-2690 - Phone
(973) 624-1047 - Fax
www.rpa.state.nj.us
njratepayer@rpa.state.nj.us

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1 **I. STATEMENT OF QUALIFICATIONS**

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

3 A. My name is Andrea C. Crane and my business address is 1 North Main Street, PO Box 810,
4 Georgetown, Connecticut 06829.

5
6 **Q. By whom are you employed and in what capacity?**

7 A. I am Vice President of The Columbia Group, Inc., a financial consulting firm that specializes
8 in utility regulation. In this capacity, I analyze rate filings, prepare expert testimony, and
9 undertake various studies relating to utility rates and regulatory policy. I have held several
10 positions of increasing responsibility since I joined The Columbia Group, Inc. in January
11 1989.

12
13 **Q. Please summarize your professional experience in the utility industry.**

14 A. Prior to my association with The Columbia Group, Inc., I held the position of Economic
15 Policy and Analysis Staff Manager for GTE Service Corporation, from December 1987 to
16 January 1989. From June 1982 to September 1987, I was employed by various Bell Atlantic
17 (now Verizon) subsidiaries. While at Bell Atlantic, I held assignments in the Product
18 Management, Treasury, and Regulatory Departments.

19
20 **Q. Have you previously testified in regulatory proceedings?**

21 A. Yes, since joining The Columbia Group, Inc., I have testified in approximately 170
22 regulatory proceedings in the states of Arizona, Arkansas, Connecticut, Delaware, Hawaii,

1 Kansas, Maryland, New Jersey, New Mexico, New York, Oklahoma, Pennsylvania, Rhode
2 Island, South Carolina, Vermont, West Virginia and the District of Columbia. These
3 proceedings involved water, wastewater, gas, electric, telephone, solid waste, cable
4 television, and navigation utilities. A list of dockets in which I have filed testimony is
5 included in Appendix A.

6
7 **Q. What is your educational background?**

8 A. I received a Masters degree in Business Administration, with a concentration in Finance,
9 from Temple University in Philadelphia, Pennsylvania. My undergraduate degree is a B.A.
10 in Chemistry from Temple University.

11
12 **II. PURPOSE OF TESTIMONY**

13 **Q. What is the purpose of your testimony?**

14 A. On or about April 24, 2004, Shorelands Water Company ("Shorelands" or "Company")
15 filed a Petition with the State of New Jersey, Board of Public Utilities ("BPU" or "Board")
16 requesting a rate increase of \$1,642,583 or approximately 19.7% in its rates for water
17 service. The Columbia Group, Inc. was engaged by The State of New Jersey, Division of the
18 Ratepayer Advocate ("Ratepayer Advocate") to review the Company's Petition and to
19 provide recommendations to the Board regarding the Company's revenue requirement and
20 cost of capital claims.

1 **III. SUMMARY OF CONCLUSIONS**

2 **Q. What are your conclusions concerning the Company's revenue requirement and its**
3 **need for rate relief?**

4 **A. Based on my analysis of the Company's filing and other documentation in this case, my**
5 **conclusions are as follows:**

6 1. The Company's claim includes investment and expenses that extend too far past the
7 end of the test year selected by the Company, especially considering the litigation
8 schedule in this case.

9 2. The BPU should adopt a test year ending December 31, 2004, for purposes of
10 determining the Company's immediate need for rate relief.

11 3. The BPU should not include any post-test year adjustments when considering the
12 Company's need for immediate rate relief.

13 4. The Company has a test year pro forma rate base of \$9,281,191 (see Schedule ACC-
14 2).¹

15 5. The Company has a pro forma capital structure that consists of 42.34% common
16 equity, 20.62% existing long-term debt, and 37.05% new long-term debt (see
17 Schedule ACC-10).

18 6. The Company has a pro forma cost of equity of 9.47% (see Schedule ACC-11).

19 7. Based on my recommended capital structure and capital cost rates, I recommend that

1 Schedules ACC-1, ACC-28, and ACC-29 are summary schedules, ACC-2 to ACC-9 are rate base schedules, ACC-10 to ACC-15 are cost of capital schedules, and ACC-16 to ACC-26 are operating income schedules.

1 the Board adopt an overall cost of capital of 7.23% for Shorelands (see Schedule
2 ACC-10).

3 8. The Company has pro forma operating income at present rates of \$606,658 (see
4 Schedule ACC-16).

5 9. Shorelands has a test year, pro forma, revenue requirement deficiency of \$112,957
6 (see Schedule ACC-1). This is in contrast to the Company's claimed deficiency of
7 \$1,642,583.

8 10. Shorelands should not receive rate recognition for its new water treatment
9 replacement project until such time as the plant is completed and serving water
10 utility customers.

11 11. When the replacement plant is in-service, the Board should authorize a Phase II rate
12 increase for the Company of an additional \$958,013 (see Schedule ACC-27).

13
14 **IV. TEST YEAR**

15 **Q. What test year did the Company utilize in this case?**

16 A. Shorelands filed its case based on the test year ending December 31, 2004. Its revenue
17 claim is based on customers at January 1, 2005, effectively the end of the test year.
18 Shorelands' rate base claim includes plant-in-service and other rate base components
19 through December 31, 2005, a full year after the end of the Company's test year.

Schedule ACC-27 addresses the Company's Phase II increase.

1 Shorelands has also included expenses based on 2005 estimates. Thus, although the
2 Company states that its filing is based on a test year ending December 31, 2004, the
3 Company's Petition as filed effectively reflects a test year ending December 31, 2005 for its
4 rate base components and operating expenses.

5
6 **Q. Why has the Company included adjustments in its filing that extend so far beyond the**
7 **end of its stated 2004 test year?**

8 A. This Company's filing is being driven by its decision to replace one of its two treatment
9 plants. As stated in the Petition on page 1, Shorelands is proposing to "completely replace
10 the process equipment of one of its two water treatment plants which has been in-service for
11 approximately 50 years." The replacement plant will be a membrane filtration system
12 facility. The Company has estimated the cost of this replacement plant to be approximately
13 \$6.3 million. Shorelands is proposing to have this plant operating prior to the 2005 summer
14 season. Therefore, Shorelands' Petition is designed to include recovery for both capital and
15 operating costs associated with the membrane filtration replacement plant.

16
17 **Q. Has the BPU permitted certain post-test year adjustments to be reflected in rates in the**
18 **past?**

19 A. The BPU has permitted post-test year adjustments to be included under certain
20 circumstances. As discussed in the Board's Decision on Motion for Determination of Test
21 Year and Appropriate Time Period for Adjustments, Docket No. WR8504330, page 2, the

1 BPU stated that,

2 With regard to the second issue, that is, the appropriate time period
3 and standard to apply to out-of-period adjustments, the standard that
4 shall be applied and shall govern petitioner's filing and proofs is that
5 which the Board has consistently applied, the "known and
6 measurable" standard. Known and measurable changes to the test
7 year must be (1) prudent and major in nature and consequence, (2)
8 carefully quantified through proofs which (3) manifest convincing
9 reliable data. The Board recognizes that known and measurable
10 changes to the test year, by definition, reflect certain contingencies;
11 but in order to prevail, petitioner must quantify such adjustments by
12 reliable forecasting techniques reflected in the record.
13

14 However, in this case, the vast majority of the Company's plant-in-service additions
15 will not be in-service by the end of the test year. The Company's claim for utility plant-in-
16 service additions is approximately \$7.34 million, and Shorelands acknowledges that
17 approximately 95% of these additions will occur after the end of the test year in this case.
18 Moreover, the Petition in this case contains only three months of actual results. Even
19 though the Company intends to update its Petition during the litigation phase of this case, I
20 have only seven months of actual data available as of the preparation date of this testimony.
21 Of even greater concern is the fact that given the hearing schedule in this case, only eight
22 months of data will be available when this case goes to hearings in September. While I
23 recognize that utilities in New Jersey often include forecast data in their test year
24 projections, in my experience utilities generally have more than three months of actual data
25 included in their rate petitions. Moreover, projected data is usually updated for actual
26 results by the time that a case goes to hearings.

1 **Q. What do you recommend?**

2 A. Given the fact a) that this Petition was filed with only three months of actual data, 2) that
3 only eight months of data will be available by the time of hearings, and 3) that 95% of all
4 utility plant-in-service additions are projected to be in-service after the end of the test year, I
5 recommend that the Board eliminate all post-test year adjustments from the Company's
6 revenue requirement.

7

8 **Q. How do you recommend that the BPU handle the treatment plant replacement project**
9 **in evaluating the Company's need for rate relief?**

10 A. In order to determine the Company's immediate need for rate relief, I recommend that that
11 BPU eliminate all post-test year adjustments, including the treatment plant replacement
12 project, from the Company's claim. Therefore, the BPU should determine the Company's
13 need for rate relief based solely on the test year ending December 31, 2004.

14 However, in order to minimize regulatory costs, I am not opposed to the BPU
15 reviewing the prudence of the Company's plant upgrade as part of this proceeding and
16 approving a Phase II increase to take effect when the new treatment facility is on-line and
17 serving customers.

18

19 **Q. Please describe how a Phase II increase would be implemented.**

20 A. Based on the Company's Petition, the BPU can determine the revenue requirement
21 associated with the water treatment plant replacement project. This would include a return

1 on investment in the new plant, depreciation expense, and incremental operating and
2 maintenance expenses. The Phase II revenue requirement approved in this case would then
3 be implemented once the plant is completed, upon submission by the Company of a
4 certification that the plant replacement project is complete and that the plant is serving
5 customers. The Company should also provide documentation of its actual capital costs
6 relating to the project so that the Board can verify that the estimated costs contained in the
7 Company's filing are not over-stated. I have calculated a Phase II revenue requirement
8 associated with the water treatment plant replacement project in Section VIII of this
9 testimony.

10
11 **Q. Do you expect the Company to accept your recommendation that the increase**
12 **associated with the water treatment plant replacement project be implemented as a**
13 **Phase II increase after the replacement plant is completed and in-service?**

14 A. Yes, I do. The Company did not propose a Phase II in its filing. However, in its response to
15 RAR-59, the Company indicated that "it is the understanding of the Company that the
16 proposed increase would be implemented in two phases." Therefore, I expect the Company
17 to accept my recommendation that the revenue requirement increase associated with the
18 water treatment replacement project be delayed to a Phase II.

V. **COST OF CAPITAL AND CAPITAL STRUCTURE**

Q. What is the cost of capital and capital structure that the Company is requesting in this case?

A. The Company has utilized the following capital structure and cost of capital:

	<u>Percent</u>	<u>Cost</u>	<u>Weighted Cost</u>
Long Term Debt-Existing	16.86%	10.07%	1.70%
Long Term Debt-Existing	4.09%	8.94%	0.37%
Long Term Debt-New	3 6.02%	3.20%	1.15%
Common Equity	43.03%	11.00%	<u>4.73%</u>
Total			<u>7.95%</u>

Q. Are you recommending any adjustments to this capital structure or cost of capital?

A. Yes, I am recommending adjustments to the Company's capital structure and cost of equity.

A. **Capital Structure**

Q. What adjustments are you recommending to the Company's capital structure claim?

A. Earlier this year, Shorelands filed a Petition requesting authorization to issue up to \$5.0 million in additional debt. On April 15, 2004, the Company amended that Petition to increase the amount of borrowing from \$5.0 million to \$5.5 million. The Company included \$5.5 million of new debt in its capital structure and cost of capital claim in this case. However, the Company filed a subsequent letter, dated June 9, 2004, once again increasing

1 the amount of debt for which BPU approval was being sought, from \$5.5 million to \$5.75
2 million. Therefore, at Schedule ACC-10, I have made an adjustment to include \$5.75
3 million of new debt financing in the Company's pro forma capital structure.
4

5 **B. Cost of Equity**

6 **Q. What is the cost of equity that the Company is requesting in this case?**

7 A. Shorelands is requesting a cost of equity of 11.0%.
8

9 **Q. Are you recommending any adjustment to the Company's proposed cost of equity?**

10 A. Yes, I am recommending an adjustment to the Company's proposed cost of equity.
11 Specifically, I am recommending that the Commission adopt a cost of equity of 9.47% for
12 Shorelands.
13

14 **Q. How did you develop your cost of equity recommendation?**

15 A. To develop a recommended cost of equity in this case, I utilized both the Discounted Cash
16 Flow ("DCF") methodology as well as the Capital Asset Pricing Model ("CAPM"). It is my
17 understanding that the Board has traditionally relied upon the DCF methodology for
18 determining cost of equity for a regulated utility, and therefore I have given greater weight to
19 my DCF result.
20

1 Q. Please describe the DCF methodology.

2 A. The DCF methodology is the most frequently used method to determine an appropriate return
3 on equity for a regulated utility. The DCF methodology equates a utility's return on equity to
4 the expected dividend yield plus expected future growth for comparable investments.
5 Specifically, this methodology is based on the following formula:

$$\text{Return on Equity} = \frac{D_1}{P_0} + g$$

6
7
8
9 where "D₁" is the expected dividend, "P₀" is the current stock price, and "g" is the expected
10 growth in dividends.

11 In order to ensure that the return on equity determined for a particular utility is
12 representative of returns for comparable investments of similar risk, the DCF methodology
13 examines returns for similar companies through the use of a "comparable" or "proxy" group.
14 To determine a comparable group of companies, I utilized the water companies followed by
15 the Value Line Investment Survey. To determine an appropriate dividend yield for
16 comparable companies, i.e., the expected dividend divided by the current price, I calculated
17 the dividend yield of each of the comparable companies under two scenarios. First, I
18 calculated the dividend yield using the average of the stock prices for each company over the
19 past twelve months. The use of a dividend yield using a twelve-month average price
20 mitigates the effect of stock price volatility for any given day. Based on the average stock
1 prices over the past twelve-months, and the current dividend for each company, I determined

1 an average dividend yield for the comparable group of 3.06%, as shown in Schedule ACC-
2 13. I also calculated the current dividend yield at August 10, 2004, which showed an
3 average dividend yield for the comparable group of 3.27%, also shown in Schedule ACC-13.
4 Finally, I examined the average dividend yields for water utilities as reported in the August
5 2004, C.A. Turner Utilities Reports, which shows an average dividend yield for water
6 utilities of 3.3%. Based on all of this data, I recommend that a dividend yield of no greater
7 than 3.4% be used in the DCF calculation. This dividend yield of 3.4 % recognizes that the
8 DCF model is prospective and accounts for growth that may occur over the next 12 months
9 in the dividend yield.

11 **Q. What growth rate did you utilize?**

12 A. The actual growth rate used in the DCF analysis is the dividend growth rate. In spite of the
13 fact that the model is based on dividend growth, it is not uncommon for analysts to examine
14 several growth factors, including growth in earnings, dividends, and book value.

15 Following are the five-year historic growth rates for the companies included in my
16 comparable group, as well as projected growth rates over the next five years, based on
17 publicly available documents:
18

1

	Historic 5 Year Earnings	Historic 5 Year Dividends	Historic 5 Year Book Value	Projected 5 Year Earnings	Projected 5 Year Dividends	Project- ed 5 Year Book Value
American States Water Co.	1.5%	1.0%	4.0%	9.5%	1.5%	4.0%
Aqua America Water Co.	9.5%	6.0%	9.5%	9.5%	7.0%	11.5%
California Water Co.	(6.5%)	1.0%	1.0%	11.0%	1.0%	14.5%
Connecticut Water Co.	2.5%	1.0%	3.5%	NA	NA	NA
Middlesex Water Co.	0.5%	2.5%	3.5%	NA	NA	NA
SJW Corporation	-0.5%	4.0%	4.0%	NA	NA	NA
Southwest Water Corporation	15.5%	10.5%	11.5%	8.00%*	NA	NA
York Water Company	2.5%*	NA	NA	7.00%*	NA	NA
Average	3.1%	3.7%	5.3%	9.0%	3.2%	10.0%

2

3

Sources: Value Line Investment Survey unless otherwise indicated.

4

* Yahoo Finance.

5

NA - Not available

6

1 With regard to longer-term, historic, ten-year growth rates, Value Line only reports
2 these growth rates for American States Water Company, Aqua America, and California
3 Water Company. As shown below, the longer-term, ten-year, historic growth rates for
4 dividends and book value are generally below the five-year growth rates for the companies
5 followed by Value Line, while the historic ten-year earnings growth rate is slightly higher
6 than the five-year historic rate:

7	Ten Year Earnings Growth	4.0%
8	Ten Year Dividend Growth	2.8%
9	Ten Year Book Value Growth	5.0%

10
11 **Q. Why do you believe that it is reasonable to examine historic growth rates as well as
12 projected growth rates when evaluating a utility's cost of equity?**

13 A. I believe that historic growth rates should be considered because security analysts have been
14 notoriously optimistic in forecasting future growth in earnings. At least part of this problem
15 in the past has been the fact that firms that traditionally sell securities are the same firms that
16 provide investors with research on these securities, including forecasts of earnings growth.
17 This results in a direct conflict of interest since it has traditionally been in the best interest of
18 securities firms to provide optimistic earnings forecasts in the hope of selling more stock. As
19 a result of this practice, the Wall Street investment firms agreed to a \$1.4 billion settlement
20 with securities regulators in a settlement announced last year. Pursuant to that settlement, ten
21 major Wall Street law firms agreed to pay \$1.4 billion to investigating state regulators and

1 the United States Securities and Exchange Commission ("SEC"). Approximately \$900
2 million of this amount constituted fines. The remainder was earmarked for various education
3 and independent research activities. In addition, firms were required to sever the links
4 between their stock research activities and their investment banking activities. Therefore,
5 earnings growth forecasts should be analyzed cautiously by state regulatory commissions.
6

7 **Q. Based upon your review, what growth rate do you recommend be utilized in the DCF**
8 **calculation?**

9 A. Based on my review of this data, I believe that a growth rate of no greater than 5.5% should
10 be utilized. This growth rate is higher than the actual growth rates over the past five years in
11 earnings, dividends or book value. It is also higher than the ten-year growth rate in earnings,
12 dividends, or book value. Moreover, it is higher than the projected growth rate for
13 dividends, which is the growth rate that is reflected in the traditional DCF formula. While
14 the average projected growth rates in earnings and book value are higher than my
15 recommended growth rate, I have already discussed the fact that projected growth rates,
16 particularly in earnings, tend to be overly optimistic.
17

1 **Q. What are the results of your analysis?**

2 A. My analysis indicates a cost of equity using the DCF methodology of 8.90%, as shown
3 below:

4	Dividend Yield	3.40%
5	Expected Growth	<u>5.50%</u>
6	Total	8.90%

7
8 **Q. Did you also calculate a cost of equity based on the CAPM methodology?**

9 A. Yes, I did.

10
11 **Q. Please provide a brief description of the CAPM methodology.**

12 A. The CAPM methodology is based on the following formula:

13
14
$$\text{Cost of Equity} = \text{Risk Free Rate} + \text{Beta} (\text{Risk Premium})$$

15 or

16
$$\text{Cost of Equity} = R_f + B(R_m - R_f)$$

17
18 The CAPM methodology assumes that the cost of equity is equal to a risk-free rate
19 plus some market-adjusted risk premium. The risk premium is adjusted by Beta, which is a
20 measure of the extent to which an investor can diversify his market risk. The ability to
1 diversify market risk is a measure of the extent to which a particular stock's price changes

1 relative to changes in the overall stock market. Thus, a Beta of 1.00 means that changes in
2 the price of a particular stock can be fully explained by changes in the overall market. A
3 stock with a Beta of 0.60 will exhibit price changes that are only 60% as great as the price
4 changes experienced by the overall market. Utility stocks have traditionally been less volatile
5 than the overall market, i.e., their stock prices do not fluctuate as significantly as the market
6 as a whole.

7
8 **Q. How did you calculate the cost of equity using the CAPM?**

9 A. My CAPM analysis is shown in Schedule ACC-15. First, I used a risk-free rate of 5.06% for
10 the yield on long-term U.S. Government bonds, which was the rate at August 9, 2004, per the
11 Statistical Release by the Federal Reserve Board. Since January 1, 2004, this rate has ranged
12 from 4.65% to 5.56%. In addition, I used the average Beta for my proxy group, based on the
13 Beta for each company as reported by Value Line. This resulted in an average Beta of 0.625.
14 Finally, since I am using a long-term U.S. Government bond rate as the risk-free rate, the
15 risk premium that should be used is the historic risk premium of small company stocks over
16 the rates for long-term government bonds. According to the 2003 Ibbotson Associates'
17 publication, *2003 Handbook: Stocks, Bonds, Bills, and Inflation*, the geometric risk premium
18 of small company stocks relative to long-term risk-free rates using geometric mean returns is
19 6.6%. Accordingly, I have used 6.6% as the risk premium in the development of the cost of
20 equity based on the CAPM methodology.

1 **Q. What is the difference between a geometric and an arithmetic mean return?**

2 A. An arithmetic mean is a simple average of each year's percentage return. A geometric mean
3 takes compounding into effect. As a result, the arithmetic mean overstates the return to
4 investors. For example, suppose an investor starts with \$100. In year 1, he makes 100% or
5 \$100. He now has \$200. In year 2, he loses 50%, or \$100. He is now back to \$100.

6 The arithmetic mean of these transactions is $100\% - 50\%$ or $50\% / 2 = 25\%$ per year.
7 The geometric mean of these transactions is 0%. In this simple example, it is clear that the
8 geometric mean more appropriately reflects the real return to the investor, who started with
9 \$100 and who still has \$100 two years later. The use of the arithmetic mean would suggest
10 that the investor should have \$156.25 after two years ($\$100 \times 1.25 \times 1.25$), when in fact the
11 investor actually has considerably less. Therefore, a geometric mean return is a more
12 appropriate measure of the real return to an investor.

13
14 **Q. What is the Company's cost of equity using a CAPM approach?**

15 A. Given a long-term risk-free rate of 5.06%, a Beta of 0.625, and a risk premium of 6.6%, the
16 CAPM methodology produces a cost of equity of 9.19%, as shown on Schedule ACC-15.

17 Risk Free Rate + Beta (Risk Premium) = Cost of Equity

18 $5.06\% + (0.625 \times 6.6\%) = 9.19\%$

1 **Q. Based on your analysis of the DCF and CAPM results, what cost of equity are you**
2 **recommending in this case?**

3 A. The DCF methodology and the CAPM methodology suggest that a return on equity of 8.90%
4 to 9.19% would be appropriate. Since I recognize that the Board has generally relied
5 primarily upon the DCF, I have weighted my results with a 75% weighting for the DCF
6 methodology and a 25% weighting for the CAPM methodology. This results in a cost of
7 equity of 8.90%, as shown below:

8	DCF Result	$8.90\% \times 75\% = 6.67\%$
9	CAPM	$9.19\% \times 25\% = \underline{2.30\%}$
10	Total	8.97%

11

12 I have included one additional adjustment to the Company's cost of equity. Since Shorelands
13 is a much smaller company than the utilities in my comparable group, I have included a small
14 company premium of 50 basis points in my cost of equity recommendation.

15

1 **Q. What overall cost of equity that you are recommending for Shorelands?**

2 A. I am recommending a cost of equity of 9.47%, which includes a base award of 8.97% and a
3 small company premium of 50 basis points, as shown below:

5	Base Cost of Equity	8.97%
6	Small Company Premium	<u>0.50%</u>
7	Total Recommended Cost of Equity	<u>9.47%</u>

8

9 **C. Overall Cost of Capital**

10 **Q. What is the overall cost of capital that you are recommending for Shorelands?**

11 A. I am recommending an overall cost of capital for Shorelands of 7.23%, based on the
12 following capital structure and cost rates:

13

	Percent	Cost	Weighted Cost
Common Equity	42.34%	9.47%	4.01%
Long-Term Debt- Existing	20.62%	9.85%	2.03%
Long Term Debt - New	37.05%	3.20%	1.19%
Total Cost of Capital			7.23%

14

15

1 **VI. RATE BASE**

2 **Q. What adjustments are you recommending to the Company's rate base claim?**

3 A. I am recommending adjustments to the Company's claims for utility plant in service,
4 accumulated depreciation, inventory, prepayments, working capital allowance, customer
5 advances, and deferred income taxes.

6

7 **A. Utility Plant-in-Service**

8 **Q. How did the Company determine its utility plant-in-service claim in this case?**

9 A. As discussed earlier in my testimony, Shorelands' claim for utility plant includes the
10 Company's projected plant balance at December 31, 2005, one year past the end of the test
11 year selected by the Company. I am recommending that that the Board exclude all post-test
12 year plant from the Company's revenue requirement. Accordingly, at Schedule ACC-3, I
13 have made an adjustment to reflect only 2004 capital additions in rate base. To quantify my
14 adjustment, I began with the Company's utility plant-in-service balance at December 31,
15 2003, as reported in the 2003 Annual Report to the BPU. I added the projected 2004 plant
16 additions shown in the response to RAR-49 to develop my pro forma utility plant-in-service
17 balance at December 31, 2004.

18

1 **B. Accumulated Depreciation**

2 **Q. Are you recommending any adjustment to the Company's claim for accumulated**
3 **depreciation?**

4 **A. Yes, I have made an adjustment to the Company's accumulated depreciation reserve claim to**
5 be consistent with the plant-in-service recommendations discussed above with regard to the
6 projected test year plant additions. This adjustment is shown in Schedule ACC-4.
7 Specifically, I began with the reserve balance at December 31, 2003 of \$11,282,216 and
8 added depreciation taken during 2004 to develop the pro forma reserve balance at December
9 31, 2004.

10 As shown on Schedule ACC-4, I calculated an average 2004 plant balance, by taking
11 the average of the December 31, 2003 plant balance and my recommended pro forma balance
12 at December 31, 2004. Since these plant balances include plant that has been financed with
13 contributions in aid of construction ("CIAC") and customer advances, I deducted the CIAC
14 and customer advance balances from the December 31, 2003 and December 31, 2004 plant
15 balances. I then determined the average plant balance during 2004 for depreciable plant.

16 I applied the Company's composite depreciation rate of 2.5% to average utility plant-
17 in-service, net of CIAC and advances, to determine the pro forma 2004 annual depreciation
18 expense. I added that pro forma 2004 depreciation expense to the Company's reserve
19 balance at December 31, 2003 to determine the pro forma accumulated depreciation at the
20 end of the test year, December 31, 2004.

1 **C. Inventory**

2 **Q. Please describe your adjustment to the Company's rate base claim for inventory.**

3 A. Shorelands included a projected inventory balance at December 31, 2005 of \$185,000, while
4 I am recommending that a pro forma balance at December 31, 2004 be included in the
5 Company's claim. Moreover, since inventory balances can fluctuate from month-to-month,
6 it is customary to use an average over some period of time in order to develop a normalized
7 level to include in rate base. I reviewed the history of inventory balances and found that the
8 inventory balance has decreased in each of the past three years, as shown below²:

9

December 31, 2001	\$186,766
December 31, 2002	\$184,376
December 31, 2003	\$165,072
Average	\$178,738

10

11 Given these fluctuations, I recommend that a three-year average of Shorelands'
12 inventory balances be used to determine a normalized level for inclusion in pro forma rate
13 base in this case. My adjustment is shown in Schedule ACC-5.

14

2 Per Company Exhibit 2.

D. Prepayments

Q. Please describe your adjustment to the Company's rate base claim for prepayments.

A. My recommended adjustment is similar to the adjustment discussed above with regard to inventory. Following are the prepayment balances for each of the past three years³:

December 31, 2001	\$250,597
December 31, 2002	\$231,446
December 31, 2003	\$256,899
Average	\$246,314

The Company's three-year average historic balance is significantly less than the projected balance at December 31, 2005 of \$295,000. I have utilized this three-year average in my recommended adjustment, which is shown in Schedule ACC-6.

E. Cash Working Capital

Q. What is cash working capital?

A. Cash working capital is the amount of cash that is required by a utility in order to cover cash outflows between the time that revenues are received from customers and the time that expenses must be paid. For example, assume that a utility bills its customers monthly and that it receives monthly revenues approximately 30 days after the midpoint of the date that

1 service is provided. If the Company pays its employees weekly, it will have a need for cash
2 prior to receiving the monthly revenue stream. If, on the other hand, the Company pays its
3 management service fees quarterly, it will receive these revenues well in advance of needing
4 the funds to pay its management service fee expense.

5
6 **Q. Do companies always have a positive cash working capital requirement?**

7 A. No, they do not. The actual amount and timing of cash flows dictate whether or not a utility
8 requires a cash working capital allowance. Therefore, one should examine actual cash flows
9 through a lead/lag study in order to accurately measure a utility's need for cash working
10 capital.

11
12 **Q. How did the Company determine its cash working capital claim?**

13 A. The Company used a formula method, i.e., its cash working capital claim is based on 1/8th of
14 its operating expenses. This 1/8th formula method is based on the assumption that a utility
15 requires 45 days of cash working capital, i.e., that it will receive its revenues, on average, 45
16 days after it pays its expenses.

1 **Q. Do you believe that the formula method provides an accurate calculation of a utility's**
2 **cash working capital requirement?**

3 A. No, I do not. The problem with the formula method is that it will always result in a positive
4 cash working capital requirement. The formula method gives no consideration to the actual
5 timing and pattern of cash flows. Therefore, this method can never accurately measure a
6 utility's need for cash working capital. For example, I understand that in a recent base rate
7 case, Middlesex Water Company reported a negative cash working capital requirement. So a
8 utility's cash working capital requirement is not always positive, even though the formula
9 method will always yield a positive result.

10
11 **Q. What other methods can be used to determine a utility's cash working capital**
12 **requirement?**

13 A. The most accurate method, and one that is commonly used, is the lead/lag method. This
14 methodology examines the actual timing and pattern of cash flows by comparing the average
15 revenue lag, which determines how soon after the midpoint of the service period the
16 Company receives its revenues, with the expense lag, which determines how soon after
17 incurring a particular expense, payment on that expense is required to be made. Shorelands
18 did not provide a lead/lag study in this case.

19

1 **Q. What do you recommend?**

2 A. I recommend that the Company's cash working capital claim be denied. As was recently
3 demonstrated in the Middlesex Water Company case, it is entirely possible for a utility to
4 have a negative cash working capital requirement. Since the Company did not provide a
5 lead/lag study, it has not supported its request for a cash working capital allowance.
6 Accordingly, I recommend that its cash working capital claim be denied. My adjustment is
7 shown in Schedule ACC-7.

8

9 **F. Customer Advances**

10 **Q. What is a customer advance?**

11 A. A customer advance may include cash, services, or property received from developers,
12 individuals, municipalities, or other parties for the purpose of constructing utility assets.
13 Customer advances are similar to CIAC. However, contributed plant is a permanent transfer
14 of assets to the utility while advances more closely resemble a partial loan, since at least a
15 portion of the value of the advanced property may be refunded at some point, in whole or in
16 part, to customers or developers depending upon specific factors, such as the amount of
17 annual revenues generated as a result of extending service. To the extent that customer
18 advances are refunded more quickly than new advances are received, the amount of customer
19 advances on a utility's balance sheet will decline over time.

20 Customer advances are deducted from rate base, since customer advances represent
plant that has not been funded by the utility's investors. Since investors did not finance this

1 plant, they should not be permitted to earn a return upon it, hence, customer advances are
2 excluded from a utility's rate base.

3
4 **Q. How did the Company determine its claim for customer advances?**

5 A. As shown in Exhibit 2, page 18, of the Company's filing, Shorelands included customer
6 advances of \$450,130, which is the projected balance at December 31, 2005. Since I am
7 recommending that all post-test year adjustments be eliminated, I have included a pro forma
8 balance for customer advances at December 31, 2004.

9
10 **Q. How did you determine the pro forma balance of customer advances at December 31,**
11 **2004 to include in rate base?**

12 A. I began with the balance for customer advances at December 31, 2003 of \$950,130. In order
13 to determine a pro forma balance at the end of the Test Year, I reviewed information on net
14 advances over the past several years. From December 31, 2001 to December 31, 2002, net
15 customer advances decreased by \$285,481, as shown in Exhibit 2, page 21 of the Company's
16 filing. From December 31, 2002 to December 31, 2003, net customer advances declined by
17 \$213,122. I used the average of these amounts, or \$249,302, as the pro forma decrease
18 expected from December 31, 2003 to December 31, 2004, the end of the test year in this
19 case. My adjustment therefore results in a balance for customer advances of \$700,829, as
20 shown in Schedule ACC-8.

1 **Q. Did you also make an adjustment to the Company's claim for CIAC?**

2 A. No. The Company's CIAC balance has remained the same over the past few years and the
3 Company is not projecting any change in its CIAC balance in 2004 or 2005. Therefore, I
4 made no adjustment to the CIAC amount included by the Company in its rate base claim.
5

6 **G. Deferred Tax Reserve**

7 **Q. How did the Company determine its claim for deferred taxes?**

8 A. Shorelands included a deferred tax reserve balance of \$850,000, which is the projected
9 balance at December 31, 2005.

10
11 **Q. What adjustment are you recommending to the Company's deferred income tax
12 reserve claim?**

13 A. I am recommending that a pro forma balance at December 31, 2004 be included in rate base.
14 In order to determine a pro forma deferred tax reserve balance at December 31, 2004, I began
15 with the balance at December 31, 2003, in the amount of \$707,915. I then reduced this
16 reserve balance to reflect the annual amortization of deferred investment tax credits, in the
17 amount of \$12,000. This amortization is shown in Exhibit 2, page 21 of the Company's
18 filing. I did not make any other adjustment to the Company's deferred tax reserve balance.
19 Deferred tax reserves generally increase over time, as new plant is added by the utility. Thus,
20 my recommendation is likely to overstate the Company's rate base and therefore to overstate
its need for rate relief. My adjustment is shown in Schedule ACC-9. If the Company

1 provides an updated deferred income tax balance, I will revise my recommendation
2 accordingly.

3
4 **H. Summary of Rate Base Issues**

5 **Q. What is the impact of all of your rate base adjustments?**

6 A. My recommended adjustments reduce the Company's rate base claim from \$16,200,880 as
7 reflected in its filing, to \$9,281,191, as summarized on Schedule ACC-2.

8
9 **VII. OPERATING INCOME ISSUES**

10 **A. Salaries and Wages**

11 **Q. Are you recommending any adjustment to the Company's salary and wage claim?**

12 A. Yes, I am recommending that the Company's post test year adjustments be denied.

13
14 **Q. How did the Company determine its salary and wage claim in this case?**

15 A. As shown in the response to RAR-18, Shorelands began with its projection of 2004 labor
16 costs. The Company then added an increase of 4% to reflect projected 2005 labor increases.
17 In addition, the Company included costs for one open engineering position in the amount of
18 \$75,000.

1 **Q. What do you recommend?**

2 A. Since I am recommending that the Board deny any post test year adjustments, I have
3 eliminated the 2005 labor increase and the costs for the new employee position. My
4 adjustment is shown in Schedule ACC-17. In addition, at Schedule ACC-18, I have made an
5 adjustment to eliminate the payroll taxes associated with the labor costs that I have
6 eliminated.

7

8 **B. Pension Costs**

9 **Q. Please describe the Company's pension cost claim.**

10 A. Shorelands has included a pension cost claim of \$166,000 in its filing. The Company stated
11 in Exhibit 2, page 11, that it "has been advised...that an increased contribution will be
12 required in the rate year to meet the plan's funding requirements...The Company's consultant
13 has forecast rate year FASB [Financial Accounting Standards Board] 87 pension cost to be
14 no lower than 141,777 (sic)." Thus, the Company's claim in this case is based on its
15 projected funding requirements, not on its actuarial FASB 87 requirement.

16

17 **Q. Please explain the difference between the FASB 87 pension expense and the amount
18 funded.**

19 A. Companies are required to calculate their pension expense for financial reporting purposes on
20 an accrual basis pursuant to FASB 87. The minimum amount that must be contributed to a
1 company's pension plan is determined each year pursuant to the Employee Retirement

1 Income Security Act ("ERISA") while Internal Revenue Service ("IRS") regulations dictate
2 the maximum contribution that is tax deductible. Over the long term, a company's pension
3 requirements pursuant to FASB 87 should match its funding requirements.

4 Some regulatory commissions utilize FASB 87 for ratemaking purposes while other
5 commissions use the amount of annual contributions to determine the pension cost to be
6 recovered from ratepayers. Both methods have some merit. The important point is that
7 regulatory commissions should be consistent in their approach and should not fluctuate
8 between the use of the FASB 87 method and the cash funding method.

9
10 **Q. Can you provide an example of the annual differences between the FASB 87 pension**
11 **cost and the contributions made to a pension fund?**

12 **A.** Yes, this difference is illustrated in the Company's response to RAR-37. According to that
13 response, Shorelands incurred the following FASB 87 pension costs over the past five years:

2003	\$141,777
2002	\$ 44,798
2001	(\$26,986)
2000	(\$43,841)
1999	(\$45,569)

14

15

1 As demonstrated above, a company's pension costs pursuant to FASB 87 may be positive or
2 negative. For example, from 1999-2001, Shorelands actually booked a negative expense or
3 credit pursuant to FASB 87. However, RAR-37 shows that Shorelands has not made any
4 cash contribution to its pension plan over the past five years. One of the reasons why the
5 Company projects that it will have to make a cash contribution for 2004 is because no cash
6 contributions have been made over the past five years.

7 The differences between the annual FASB 87 pension cost and the annual amount of
8 pension funding demonstrate why it is important for regulatory commissions to be consistent
9 from rate case to rate case. If a regulatory commission switched its ratemaking methodology
10 for pension costs periodically, utility companies and other parties could advocate the
11 methodology that gave them the best result, i.e., utility companies could promote the
12 methodology that resulted in the largest revenue increases, and consumer advocates could
13 promote the methodology that resulted in the smallest increases. Therefore, regulatory
14 commissions are consistent in their ratemaking approach in order to remove any incentive for
15 such gaming.

16
17 **Q. What methodology has traditionally been used by the Board?**

18 **A.** In New Jersey, the Board has traditionally used the FASB 87 methodology to set rates. I
19 recommend that it continue to utilize this methodology in this case.
20

1 **Q. What is the impact of using the FASB 87 methodology to set rates in this case?**

2 A. Use of the FASB 87 methodology will result in a pension cost of \$141,777, which is the
3 pension cost determined by the Company's most recent actuarial report. This report, which
4 was supplied by the Company in response to RAR-36, was prepared by the Company's
5 actuaries in May 2004. At Schedule ACC-19, I have made an adjustment to reflect the
6 FASB 87 pension cost of \$141,777 in my revenue requirement recommendation.
7

8 **C. Deferred Purchased Water Costs**

9 **Q. Please describe the Company's claim for deferred purchased water costs.**

10 A. Shorelands has included a purchased water expense claim in its filing for normal, prospective
11 water purchases, based on projected volumes and current rates for purchased water. In
12 addition, Shorelands is requesting deferred accounting treatment in this case for increased
13 purchased water costs from the New Jersey Water Supply Authority ("NJWSA").
14 Specifically, the Company is requesting of \$45,000 for increased costs incurred from July 1,
15 2004 to December 31, 2004. In addition, Shorelands is requesting recovery of costs in the
16 amount of \$32,560 relating to negotiations for water diversion rights from Keansburg
17 Municipal Utility Authority ("Keansburg"). The Company is proposing that both the
18 deferred purchased water costs and the costs relating to the water diversion rights be
19 recovered over a two year period.
20

1 **Q. Do you believe that the Company's claim is reasonable?**

2 A. No, I do not. I recommend that the Board reject both the Company's claim relating to
3 deferred purchased water costs and its claim with regard to costs for water diversion rights
4 from Keansburg.

5

6 **Q. What is the basis for your recommendation?**

7 A. Shorelands had the opportunity to file for a purchased water adjustment clause ("PWAC")
8 within three years of its last base rate case. Prior to that case, the Company did have a
9 PWAC in place. The PWAC is the mechanism adopted by the Board in order to provide for
10 dollar-for-dollar recovery of purchased water costs. The Company did not request
11 implementation of a PWAC and it should not now be permitted to pass through these
12 additional costs to ratepayers. Under a PWAC mechanism, water utilities have the ability to
13 pass through to ratepayers all purchased water costs on a dollar-for-dollar basis, but in return
14 they must file periodically with the Board and they must flow back to ratepayers any over-
15 recovery for purchased water costs. Shorelands apparently made the decision that it would
16 take the risk of absorbing purchased water costs and that it would retain any benefits if actual
17 purchased water costs were less than the amounts included in base rates. There is no
18 rationale for now permitting the Company to defer increased costs for future recovery. My
19 adjustment is shown in Schedule ACC-20.

20

1 **Q. In determining the Company's prospective purchased water costs, have you considered**
2 **the higher NJWSA rates that are now being charged to Shorelands?**

3 A. Yes, I have. I am not recommending any adjustment to the Company's claim for prospective
4 purchased water costs, which reflects new rates implemented by the water providers in 2004.
5 My recommendation is solely to disallow the past costs that have been incurred by
6 Shorelands, since the Company chose not to utilize the PWAC mechanism that it had
7 available for purchased water costs.

8
9 **Q. Why are you recommending disallowance of the costs associated with the water**
10 **diversion rights from Keansburg?**

11 A. The costs associated with negotiation of the water diversion rights from Keansburg were
12 booked to Account 301 - Land and Land Rights.⁴ According to the Company, it sought
13 approval from the New Jersey Department of Environmental Protection ("NJDEP") for this
14 transfer of water diversion rights and this approval is still pending. However, Keansburg has
15 now demonstrated a renewed need for these water division rights and I understand that these
16 water division rights will not be transferred to Shorelands. Therefore, the investment booked
17 by the Company has not been used to provide utility service and will not be used to provide
18 utility service in the future. Accordingly, there is no rationale for charging ratepayers for
19 these costs. The Company is compensated for various business and financial risks through
20 an appropriate return on equity award. One of the risks for which shareholders are

1 compensated is the risk that they will make investments in assets that are not used and useful
2 in the provision of regulated utility service and that they will not be able to recover these
3 investments from ratepayers. Ratepayers received no benefit from these water diversion
4 rights costs and they will not receive any benefit from them in the future. Therefore, I
5 recommend that recovery of such costs be denied. My adjustment is shown in Schedule
6 ACC-20.

7
8 **D. Regulatory Commission Costs**

9 **Q. Please describe the Company's claim for regulatory commission costs.**

10 A. Shorelands is requesting recovery of rate case costs for the current case of \$100,000. These
11 costs are composed of the following:

12	Legal	\$ 75,000
13	Financial (Rate of Return)	\$ 20,000
14	Accounting	<u>\$ 5,000</u>
15	Total	<u>\$100,000</u>

16
17 Shorelands has used a two-year amortization period for recovery of these costs.
18

1 **Q. Are you recommending any adjustment to the Company's claim.**

2 A. Yes, I am recommending two adjustments to the Company's claim. First, I am
3 recommending that the Company's rate case costs be amortized over a four-year period. The
4 Company's last three base rate case proceedings had rates effective July 1990, July 1994, and
5 June 1998.⁵ Rates in this case will not be effective until late in 2004. Therefore, on average,
6 there has been at least four years between each of the Company's base rate case proceedings
7 since 1990. Accordingly, I am recommending a four-year amortization period in this case.
8 My adjustment is shown in Schedule ACC-21.

9
10 **Q. What is your second adjustment?**

11 A. The Board has a longstanding policy of requiring a 50/50 sharing of rate case costs between
12 ratepayers and shareholders. Such a sharing has not been reflected in the Company's filing.
13 Therefore, I recommend that rate case expenditures be subject to this 50/50 sharing,
14 consistent with the Board's policy.

15
16 **Q. Hasn't the Board previously allowed this Company to collect 100% of rate case costs
17 from ratepayers?**

18 A. The Board did permit West Keansburg Water Company, a predecessor to Shorelands, to
19 forego a 50/50 sharing with ratepayers.⁶ This decision was made over twenty years ago.

5 Response to RAR-42.

6 In the Matter of West Keansburg Water Company, BPU Docket No. 838-737, OAL Docket No. PUC 7175 (April

1 Furthermore, the Board's Decision in that case stated the following,

2 In the recent past proceedings involving the State's major
3 utility companies, the Board has shared rate case expenses,
4 including Rate Counsel fees, equally between the
5 shareholders and the ratepayers. While we continue to
6 consider this issue on a case by case basis, we are of the
7 opinion that the sharing of rate case expenses by a company
8 the size of Petitioner is inappropriate. It is our belief that the
9 sharing of rate case expenses would have a greater negative
10 effect on companies such as Petitioner as opposed to major
11 utilities. This is so because rate case expenses make up a
12 substantially higher percentage of operating expenses for such
13 companies and the resultant reduction in the earned rate of
14 return would be greater.

15 The Board will continue to closely scrutinize and review all
16 rate case expenses incurred by the Petitioner in the future in
17 order to assess their reasonableness. As such, the Company is
18 urged to use its utmost discretion and best efforts in order to
19 minimize such expenses to the greatest extent possible.

20
21 I believe that the facts in the Shorelands case are substantially different than in the
22 West Keansburg case for several reasons. First, it is my understanding that the rate case
23 costs being claimed in the West Keansburg case amounted to over 4% of total revenue, while
24 the Company's claim in this case amounts to 1.2%. On an annual basis, assuming a four-
25 year amortization, the shareholders' portion of these rate case costs will amount to less than
26 two-tenths of one percent (0.2%) of Shorelands 2004 revenue. In addition, while still a
27 relatively small company, Shorelands has grown significantly relative to the West Keansburg
28 system that was the subject of the Board's order. Therefore, the impact of absorbing 50% of
29 these expenses will be much less on Shorelands today than it would have been on West
30

1 Keansburg in 1984. Furthermore, while the Board noted in its Order that "Rate Counsel"
2 fees were included in rate case costs in 1984, fees for the Ratepayer Advocate, the successor
3 agency to Rate Counsel, are not included in the Company's rate case costs and are not subject
4 to this 50/50 sharing. For all these reasons, I recommend a 50/50 sharing of rate case costs in
5 this case. My adjustment is shown in Schedule ACC-21.

6
7 **E. Inflation Adjustment**

8 **Q. Did the Company use an inflation adjustment to determine its pro forma claim for any**
9 **cost categories?**

10 A. Yes, Shorelands developed its 2005 claim by applying a 5% inflation adjustment to its
11 projected 2004 test year costs for water treatment, transmission and distribution, customer
12 accounting, all other A&G, and general plant expenses. In addition, the Company used a 5%
13 inflation adjustment to develop a portion of its claim for pumping expenses. While the
14 Company indicated that its claims for these costs were based on "management's estimate,"
15 according to its discovery responses the Company generally utilized a 5% inflation factor.

16
17 **Q. Are you recommending any adjustment to the Company's claim for these costs?**

18 A. Yes, I am recommending that the Company's proposed inflation adjustments be rejected, for
19 two reasons. First, inflation adjustments do not meet the standard for known and measurable
20 changes. The Company has not demonstrated that these costs vary in proportion to inflation,
1 nor has the Company provided any support for the use of a 5% inflation factor. Second, as

1 previously discussed, I am recommending that all post-test year adjustments be eliminated,
2 on the basis that the Company's test year does not end until December 31, 2004, well after
3 the hearings in this case. Therefore, speculative 2005 cost increases for these cost categories
4 should be eliminated from the Company's revenue requirement claim. My adjustment is
5 shown in Schedule ACC-22.

6 It should be noted that the Company's claim for an adjustment in 2005 for pumping
7 expenses included both an inflation adjustment and an adjustment related to increased power
8 costs resulting from the water treatment plant replacement program. Both of these Company
9 adjustments are eliminated from my revenue requirement in Schedule ACC-22, since my
10 recommendation is to disallow all post-test year adjustments. However, I have included
11 incremental power costs in the Phase II revenue increase that I propose be implemented once
12 the water treatment replacement plant is complete, as discussed in Section VIII of this
13 testimony.

14
15 **F. Depreciation Expense**

16 **Q. Are you recommending any adjustment to the Company's depreciation expense claim?**

17 **A.** Yes, I am recommending an adjustment to revise the Company's depreciation expense claim
18 consistent with my recommended utility plant-in-service adjustment. Since I am
19 recommending that the Company's rate base include plant balances at the end of the 2004
20 test year, it is necessary to make a corresponding adjustment to eliminate the annual
depreciation expense on plant that will not be in-service by December 31, 2003. At

1 Schedule ACC-23, I have calculated a pro forma depreciation expense based on my utility
2 plant-in-service balance at December 31, 2004. I have utilized the Company's composite
3 depreciation rate of 2.5% to develop my adjustment. In quantifying my adjustment, I have
4 excluded all depreciation expense on contributed and advanced plant.
5

6 **Q. Is the Company taking depreciation on its contributed plant?**

7 A. It appears that Shorelands may be including depreciation expense on contributed and
8 advanced plant in its claim. Depreciation expense on both advances and contributions should
9 be excluded from a utility's revenue requirement. Contributed and advanced plant that is not
10 refunded are, by definition, non-investor supplied capital. Investors are entitled to a return on
11 their investment, and to a return of their investment through depreciation charges. However,
12 it is inappropriate to return contributed or advanced capital to investors through depreciation
13 charges, since investors never funded this investment. Depreciation expense on contributed
14 or advanced plant represents a return of capital to shareholders which the shareholders never
15 supplied, and therefore it should be eliminated from the Company's claim.
16

17 **G. Income Tax Expense at Present Rates**

18 **Q. Are you recommending any adjustment to the Company's income tax expense claim?**

19 A. Yes, I am, although it is more of an adjustment in presentation than in substance. In
20 calculating a utility's need for rate relief, I first calculate its pro forma income at present rates
1 by making various operating income adjustments to its claim for operating income at present

1 rates. I then compare its pro forma income at present rates with its required operating
2 income, which is based upon my recommended rate base and cost of capital. The difference
3 between the Company's income at present rates and its required income is its income
4 deficiency or surplus. This surplus or deficiency is then grossed-up for taxes to an operating
5 revenue amount.

6 In its filing, the Company calculated that it has a taxable loss at present rates (once its
7 interest expense is taken into account), and therefore it included no income tax liability in its
8 pro forma income statement at present rates. However, because of this tax loss, the Company
9 can increase its operating revenue up to a point without incurring any positive income tax
10 liability. This is a benefit to the Company that is not fully reflected in its pro forma income
11 calculation at present rates. Therefore, at Schedule ACC-24, I have made an adjustment to
12 the Company's income tax claim, at present rates, to reflect this tax benefit. Related to this
13 adjustment is the fact that the revenue multiplier that I use to gross-up the Company's
14 income is much higher than the revenue multiplier that is implicit in the Company's Petition.
15 Therefore, my reduction in income taxes at present rates is largely offset by my use of a
16 higher revenue multiplier.

17
18 **H. Interest Synchronization and Taxes**

19 **Q. Have you adjusted the pro forma interest expense for income tax purposes?**

20 **A.** Yes, I have made this adjustment at Schedule ACC-25. It is consistent (synchronized) with
21 my recommended rate base, capital structure, and cost of capital recommendations. I am

1 recommending a lower rate base than the rate base included in the Company's filing. My
2 recommendations, therefore, result in lower pro forma interest expense for the Company.
3 This lower interest expense, which is an income tax deduction for state and federal tax
4 purposes, will result in an increase to the Company's income tax liability under my
5 recommendations. Therefore, my recommendations result in an interest synchronization
6 adjustment that reflects a higher income tax burden for the Company, and a decrease to pro
7 forma income at present rates.
8

9 **I. Revenue Multiplier**

10 **Q. What revenue multiplier have you used for your adjustments?**

11 A. My revenue multiplier includes gross receipts taxes of 7.50%, franchise taxes of 5.00%,
12 excise taxes of 1.56%, and a BPU assessment of .17%. resulting in total revenue taxes of
13 14.23%, as shown on Schedule ACC-26. In addition, I have utilized a federal income tax rate
14 of 34%. These tax rates are the same rates used by Shorelands in its filing.
15

16 **VIII. PHASE II INCREASE**

17 **Q. Once the water treatment replacement project is complete, what level of additional rate
18 increase would you recommend?**

19 A. Once the project is complete, I recommend that the Company implement a Phase II increase
20 based on the direct incremental costs of the facility. These costs include incremental power
1 costs, incremental chemical costs, and incremental sludge disposal costs. These were the

1 incremental operating expenses identified by Shorelands. In addition, I have included
2 Shorelands' claim for incremental depreciation expense, based on its composite rate of 2.5%.

3 In addition to these incremental expenses, I have also included in my Phase II
4 recommendation the additional operating income that Shorelands will require on the
5 replacement plant, based on my overall recommended rate of return of 7.23%. Finally, I have
6 reduced the Company's incremental revenue requirement to reflect interest synchronization
7 associated with the new facility. Since the water treatment replacement facility will increase
8 the Company's interest expense, there will be a corresponding adjustment in its income tax
9 liability.

10 As shown on Schedule ACC-27, I am recommending a Phase II increase of \$958,013
11 for Shorelands. The Phase II increase should not be implemented until the Company provides
12 the appropriate documentation certifying that the water treatment replacement plant is
13 complete and in-service. The Company should also provide documentation of its actual
14 capital costs relating to the project so that the Board can ensure that the estimated costs
15 contained in the Company's filing are not over-stated.

16
17 **Q. Should the Board include other increases in Phase II, such as salary and wage increases?**

18 **A.** No, it should not. As stated earlier, the Board should reject any post-test year adjustments,
19 given the litigation schedule in this case. While I am recommending a Phase II increase
20 associated with one construction project, that does not change my recommendation that the
21 Company's post-test year adjustments are too speculative in this case. If the Company wants

1 to delay the hearings in this case and the implementation of any rate increase until it has actual
2 results for the twelve months ending December 31, 2004, then the Board may want to
3 consider certain post-test year adjustments. However, given the current schedule in this case
4 and the Company's selection of the 2004 test year, no post-test year adjustments should be
5 included in Phase II except for direct incremental costs of the water treatment replacement
6 project.

7
8 **IX. REVENUE REQUIREMENT SUMMARY**

9 **Q. What is the result of the recommendations contained in this testimony?**

10 A. My adjustments result in a revenue requirement deficiency at present rates of \$112,957, as
11 summarized on Schedule ACC-1. This recommendation reflects revenue requirement
12 adjustments of \$1,529,626 to the Company's requested revenue requirement increase of
13 \$1,642,583. In addition, I am recommending a Phase II increase of \$958,013 (Schedule ACC-
14 27) once the water treatment plant replacement project is complete and the plant is in-service.

15
16 **Q. Have you quantified the revenue requirement impact of each of your recommendations?**

17 A. Yes, at Schedule ACC-28, I have quantified the revenue requirement impact of the rate of
18 return, rate base, revenue and expense recommendations contained in this testimony.

1 **Q. Have you developed a pro forma income statement?**

2 A. Yes, Schedule ACC-29 contains a pro forma income statement, showing utility operating
3 income under several scenarios, including the Company's claimed operating income at present
4 rates, my recommended operating income at present rates, and operating income under my
5 proposed rate increase. My recommendations will result in an overall return on rate base of
6 7.23%.

7
8 **Q. How do you recommend that any rate increase be allocated among Shorelands'**
9 **customer classes?**

10 A. I recommend that both the Phase I and Phase II rate increases be allocated on an across-the-
11 board basis. Shorelands has not provided an allocated cost of service study and therefore
12 there is no documentation that supports any other revenue allocation.

13
14 **Q. Does this conclude your testimony?**

15 A. Yes, it does.

APPENDIX A

The Columbia Group, Inc., Testimonies of Andrea C. Crane

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Artesian Water Company	W	Delaware	04-42	8/04	Revenue Requirements Cost of Capital	Division of the Public Advocate
Long Neck Water Company	W	Delaware	04-31	7/04	Cost of Equity	Division of the Public Advocate
Tidewater Utilities, Inc.	W	Delaware	04-152	7/04	Cost of Capital	Division of the Public Advocate
Cablevision	C	New Jersey	CR03100850, et al.	6/04	Cable Rates	Division of the Ratepayer Advocate
Montague Water and Sewer Companies	W/WW	New Jersey	WR03121034 (W) WR03121035 (S)	5/04	Revenue Requirements	Division of the Ratepayer Advocate
Comcast of South Jersey, Inc.	C	New Jersey	CR03100876,77,79,80	5/04	Form 1240 Cable Rates	Division of the Ratepayer Advocate
Comcast of Central New Jersey, et al.	C	New Jersey	CR03100749-750 CR03100759-762	4/04	Cable Rates	Division of the Ratepayer Advocate
Time Warner	C	New Jersey	CR03100763-764	4/04	Cable Rates	Division of the Ratepayer Advocate
Interstate Navigation Company	N	Rhode Island	3573	3/04	Revenue Requirements	Division of Public Utilities and Carriers
Aqua Pennsylvania, Inc.	W	Pennsylvania	R-00038805	2/04	Revenue Requirements	Pennsylvania Office of Consumer Advocate
Comcast of Jersey City, et al.	C	New Jersey	CR03080598-601	2/04	Cable Rates	Division of the Ratepayer Advocate
Delmarva Power and Light Company	G	Delaware	03-378F	2/04	Fuel Clause	Division of the Public Advocate
Atmos Energy Corp.	G	Kansas	03-ATMG-1036-RTS	11/03	Revenue Requirements	Citizens' Utility Ratepayer Board
Aquila, Inc. (UCU)	G	Kansas	02-UTCG-701-GIG	10/03	Using utility assets as collateral	Citizens' Utility Ratepayer Board
CenturyTel of Northwest Arkansas, LLC	T	Arkansas	03-041-U	10/03	Affiliated Interests	The Arkansas Public Service Commission General Staff
Borough of Butler Electric Utility	E	New Jersey	CR03010049/63	9/03	Revenue Requirements	Division of the Ratepayer Advocate
Comcast Cablevision of Avalon Comcast Cable Communications	C	New Jersey	CR03020131-132	9/03	Cable Rates	Division of the Ratepayer Advocate
Delmarva Power and Light Company d/b/a Conectiv Power Delivery	E	Delaware	03-127	8/03	Revenue Requirements	Division of the Public Advocate
Kansas Gas Service	G	Kansas	03-KGSG-602-RTS	7/03	Revenue Requirements	Citizens' Utility Ratepayer Board
Washington Gas Light Company	G	Maryland	8959	6/03	Cost of Capital Incentive Rate Plan	U.S. DOD/FEA
Pawtucket Water Supply Board	W	Rhode Island	3497	6/03	Revenue Requirements	Division of Public Utilities and Carriers
Atlantic City Electric Company	E	New Jersey	EO03020091	5/03	Stranded Costs	Division of the Ratepayer Advocate

The Columbia Group, Inc., Testimonies of Andrea C. Crane

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Public Service Company of New Mexico	G	New Mexico	03-000-17 UT	5/03	Cost of Capital Cost Allocations	Office of the New Mexico Attorney General
Comcast - Hopewell, et al.	C	New Jersey	CR02110818 CR02110823-825	5/03	Cable Rates	Division of the Ratepayer Advocate
Cablevision Systems Corporation	C	New Jersey	CR02110838, 43-50	4/03	Cable Rates	Division of the Ratepayer Advocate
Comcast-Garden State / Northwest	C	New Jersey	CR02100715 CR02100719	4/03	Cable Rates	Division of the Ratepayer Advocate
Midwest Energy, Inc. and Westar Energy, Inc.	E	Kansas	03-MDWE-421-ACQ	4/03	Acquisition	Citizens' Utility Ratepayer Board
Time Warner Cable	C	New Jersey	CR02100722 CR02100723	4/03	Cable Rates	Division of the Ratepayer Advocate
Westar Energy, Inc.	E	Kansas	01-WSRE-949-GIE	3/03	Restructuring Plan	Citizens' Utility Ratepayer Board
Public Service Electric and Gas Company	E	New Jersey	ER02080604 PUC 7983-02	1/03	Deferred Balance	Division of the Ratepayer Advocate
Atlantic City Electric Company d/b/a Conectiv Power Delivery	E	New Jersey	ER02080510 PUC 6917-02S	1/03	Deferred Balance	Division of the Ratepayer Advocate
Wallkill Sewer Company	WW	New Jersey	WR02030193 WR02030194	12/02	Revenue Requirements Purchased Sewage Treatment Adj. (PSTAC)	Division of the Ratepayer Advocate
Midwest Energy, Inc.	E	Kansas	03-MDWE-001-RTS	12/02	Revenue Requirements	Citizens' Utility Ratepayer Board
Comcast-LBI Crestwood	C	New Jersey	CR02050272 CR02050270	11/02	Cable Rates	Division of the Ratepayer Advocate
Reliant Energy Arkla	G	Oklahoma	PUD200200166	10/02	Affiliated Interest Transactions	Oklahoma Corporation Commission, Public Utility Division Staff
Midwest Energy, Inc.	G	Kansas	02-MDWG-922-RTS	10/02	Gas Rates	Citizens' Utility Ratepayer Board
Comcast Cablevision of Avalon	C	New Jersey	CR02030134 CR02030137	7/02	Cable Rates	Division of the Ratepayer Advocate
RCN Telecom Services, Inc., and Home Link Communications	C	New Jersey	CR02010044, CR02010047	7/02	Cable Rates	Division of the Ratepayer Advocate
Washington Gas Light Company	G	Maryland	8920	7/02	Rate of Return Rate Design (Rebuttal)	General Services Administration (GSA)
Chesapeake Utilities Corporation	G	Delaware	01-307, Phase II	7/02	Rate Design Tariff Issues	Division of the Public Advocate
Washington Gas Light Company	G	Maryland	8920	6/02	Rate of Return Rate Design	General Services Administration (GSA)
Tidewater Utilities, Inc.	W	Delaware	02-28 38	6/02	Revenue Requirements	Division of the Public Advocate
Western Resources, Inc.	E	Kansas	01-WSRE-949-GIE	5/02	Financial Plan	Citizens' Utility Ratepayer Board
Empire District Electric Company	E	Kansas	02-EPDE-488-RTS	5/02	Revenue Requirements	Citizens' Utility Ratepayer Board

The Columbia Group, Inc., Testimonies of Andrea C. Crane

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Southwestern Public Service Company	E	New Mexico	3709	4/02	Fuel Costs	Office of the New Mexico Attorney General
Cablevision Systems	C	New Jersey	CR01110706, et al	4/02	Cable Rates	Division of the Ratepayer Advocate
Potomac Electric Power Company	E	District of Columbia	945, Phase II	4/02	Divestiture Procedures	General Services Administration (GSA)
Vermont Yankee Nuclear Power Corp.	E	Vermont	6545	3/02	Sale of VY to Entergy Corp. (Supplemental)	Department of Public Service
Delmarva Power and Light Company	G	Delaware	01-348F	1/02	Gas Cost Adjustment	Division of the Public Advocate
Vermont Yankee Nuclear Power Corp.	E	Vermont	6545	1/02	Sale of VY to Entergy Corp.	Department of Public Service
Pawtucket Water Supply Company	W	Rhode Island	3378	12/01	Revenue Requirements	Division of Public Utilities and Carriers
Chesapeake Utilities Corporation	G	Delaware	01-307, Phase I	12/01	Revenue Requirements	Division of the Public Advocate
Potomac Electric Power Company	E	Maryland	8796	12/01	Divestiture Procedures	General Services Administration (GSA)
Kansas Electric Power Cooperative	E	Kansas	01-KEPE-1106-RTS	11/01	Depreciation Methodology (Cross Answering)	Citizens' Utility Ratepayer Board
Wellsboro Electric Company	E	Pennsylvania	R-00016356	11/01	Revenue Requirements	Office of Consumer Advocate
Kent County Water Authority	W	Rhode Island	3311	10/01	Revenue Requirements (Surrebuttal)	Division of Public Utilities and Carriers
Pepco and New RC, Inc.	E	District of Columbia	1002	10/01	Merger Issues and Performance Standards	General Services Administration (GSA)
Potomac Electric Power Co. & Delmarva Power	E	Delaware	01-194	10/01	Merger Issues and Performance Standards	Division of the Public Advocate
Yankee Gas Company	G	Connecticut	01-05-19PH01	9/01	Affiliated Transactions	Office of Consumer Counsel
Hope Gas, Inc., d/b/a Dominion Hope	G	West Virginia	01-0330-G-42T 01-0331-G-30C 01-1842-GT-T 01-0685-G-PC	9/01	Revenue Requirements (Rebuttal)	The Consumer Advocate Division of the PSC
Pennsylvania-American Water Company	W	Pennsylvania	R-00016339	9/01	Revenue Requirements (Surrebuttal)	Office of Consumer Advocate
Potomac Electric Power Co. & Delmarva Power	E	Maryland	8890	9/01	Merger Issues and Performance Standards	General Services Administration (GSA)
Comcast Cablevision of Long Beach Island, et al	C	New Jersey	CR01030149-50 CR01050285	9/01	Cable Rates	Division of the Ratepayer Advocate
Kent County Water Authority	W	Rhode Island	3311	8/01	Revenue Requirements	Division of Public Utilities and Carriers
Pennsylvania-American Water Company	W	Pennsylvania	R-00016339	8/01	Revenue Requirements	Office of Consumer Advocate

The Columbia Group, Inc., Testimonies of Andrea C. Crane

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Roxiticus Water Company	W	New Jersey	WR01030194	8/01	Revenue Requirements Cost of Capital Rate Design	Division of the Ratepayer Advocate
Hope Gas, Inc., d/b/a Dominion Hope	G	West Virginia	01-0330-G-42T 01-0331-G-30C 01-1842-GT-T 01-0685-G-PC	8/01	Revenue Requirements	Consumer Advocate Division of the PSC
Western Resources, Inc.	E	Kansas	01-WSRE-949-GIE	6/01	Restructuring Financial Integrity (Rebuttal)	Citizens' Utility Ratepayer Board
Western Resources, Inc. --	E	Kansas	01-WSRE-949-GIE	6/01	Restructuring Financial Integrity	Citizens' Utility Ratepayer Board
Cablevision of Allamuchy, et al	C	New Jersey	CR00100824, etc.	4/01	Cable Rates	Division of the Ratepayer Advocate
Public Service Company of New Mexico	E	New Mexico	3137, Holding Co.	4/01	Holding Company	Office of the Attorney General
Keauhou Community Services, Inc.	W	Hawaii	00-0094	4/01	Rate Design	Division of Consumer Advocacy
Western Resources, Inc.	E	Kansas	01-WSRE-436-RTS	4/01	Revenue Requirements Affiliated Interests (Motion for Suppl. Changes)	Citizens' Utility Ratepayer Board
Western Resources, Inc.	E	Kansas	01-WSRE-436-RTS	4/01	Revenue Requirements Affiliated Interests	Citizens' Utility Ratepayer Board
Public Service Company of New Mexico	E	New Mexico	3137, Part III	4/01	Standard Offer Service (Additional Direct)	Office of the Attorney General
Chem-Nuclear Systems, LLC	SW	South Carolina	2000-366-A	03/01	Allowable Costs	Department of Consumer Affairs
Southern Connecticut Gas Company	G	Connecticut	00-12-08	03/01	Affiliated Interest Transactions	Office of Consumer Counsel
Atlantic City Sewerage Corporation	S	New Jersey	WR00080575	3/01	Revenue Requirements Cost of Capital Rate Design	Division of the Ratepayer Advocate
Delmarva Power and Light Company d/b/a Conectiv Power Delivery	G	Delaware	00-314	3/01	Margin Sharing	Division of the Public Advocate
Senate Bill 190 Re: Performance Based Ratemaking	G	Kansas	Senate Bill 190	2/01	Performance-Based Ratemaking Mechanisms	Citizens' Utility Ratepayer Board
Delmarva Power and Light Company	G	Delaware	00-463-F	2/01	Gas Cost Rates	Division of the Public Advocate
Waitsfield Fayston Telephone Company	T	Vermont	6417	12/00	Revenue Requirements	Department of Public Service
Delaware Electric Cooperative	E	Delaware	00-365	11/00	Code of Conduct Cost Allocation Manual	Division of the Public Advocate
Commission Inquiry into Performance-Based Ratemaking	G	Kansas	00-GIMG-425-GIG	10/00	Performance-Based Ratemaking Mechanisms	Citizens' Utility Ratepayer Board
Pawtucket Water Supply Board	W	Rhode Island	3164 Separation Plan	10/00	Revenue Requirements	Division of Public Utilities and Carriers
Public Service Company of New Mexico	E	New Mexico	3137, Part III	9/00	Standard Offer Service	Office of the Attorney General

The Columbia Group, Inc., Testimonies of Andrea C. Crane

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Laie Water Company	W	Hawaii	00-0017 Separation Plan	8/00	Rate Design	Division of Consumer Advocacy
El Paso Electric Company	E	New Mexico	3170, Part II, Ph. 1	7/00	Electric Restructuring	Office of the Attorney General
Public Service Company of New Mexico	E	New Mexico	3137 - Part II Separation Plan	7/00	Electric Restructuring	Office of the Attorney General
PG Energy	G	Pennsylvania	R-00005119	6/00	Revenue Requirements	Office of Consumer Advocate
Consolidated Edison, Inc. and Northeast Utilities	E/G	Connecticut	00-01-11	4/00	Merger Issues (Additional Supplemental)	Office of Consumer Counsel
Sussex Shores Water Company	W	Delaware	99-576	4/00	Revenue Requirements	Division of the Public Advocate
Utilicorp United, Inc.	G	Kansas	00-UTCG-336-RTS	4/00	Revenue Requirements	Citizens' Utility Ratepayer Board
TCI Cablevision	C	Missouri	9972-9146	4/00	Late Fees (Affidavit)	Honora Eppert, et al
Oklahoma Natural Gas Company	G	Oklahoma	PUD 990000166 PUD 980000683 PUD 990000570	3/00	Pro Forma Revenue Affiliated Transactions (Rebuttal)	Oklahoma Corporation Commission, Public Utility Division Staff
Tidewater Utilities, Inc. Public Water Supply Co.	W	Delaware	99-466	3/00	Revenue Requirements	Division of the Public Advocate
Delmarva Power and Light Company	G/E	Delaware	99-582	3/00	Cost Accounting Manual Code of Conduct	Division of the Public Advocate
Philadelphia Suburban Water Company	W	Pennsylvania	R-00994868 R-00994877 R-00994878 R-00994879	3/00	Revenue Requirements (Surrebuttal)	Office of Consumer Advocate
Philadelphia Suburban Water Company	W	Pennsylvania	R-00994868 R-00994877 R-00994878 R-00994879	2/00	Revenue Requirements	Office of Consumer Advocate
Consolidated Edison, Inc. and Northeast Utilities	E/G	Connecticut	00-01-11	2/00	Merger Issues	Office of Consumer Counsel
Oklahoma Natural Gas Company	G	Oklahoma	PUD 990000166 PUD 980000683 PUD 990000570	1/00	Pro Forma Revenue Affiliated Transactions	Oklahoma Corporation Commission, Public Utility Division Staff
Connecticut Natural Gas Company	G	Connecticut	99-09-03	1/00	Affiliated Transactions	Office of Consumer Counsel
Time Warner Entertainment Company, L.P.	C	Indiana	48D06-9803-CP-423	1999	Late Fees (Affidavit)	Kelly J. Whiteman, et al
TCI Communications, Inc., et al	C	Indiana	55D01-9709-CP-00415	1999	Late Fees (Affidavit)	Franklin E. Littell, et al
Southwestern Public Service Company	E	New Mexico	3116	12/99	Merger Approval	Office of the Attorney General
New England Electric System Eastern Utility Associates	E	Rhode Island	2930	11/99	Merger Policy	Department of Attorney General
Delaware Electric Cooperative	E	Delaware	99-457	11/99	Electric Restructuring	Division of the Public Advocate

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Jones Intercable, Inc.	C	Maryland	CAL98-00283	10/99	Cable Rates (Affidavit)	Cynthia Maisonette and Ola Renee Chatman, et al
Texas-New Mexico Power Company	E	New Mexico	3103	10/99	Acquisition Issues	Office of Attorney General
Southern Connecticut Gas Company	G	Connecticut	99-04-18	9/99	Affiliated Interest	Office of Consumer Counsel
TCI Cable Company	C	New Jersey	CR99020079 et al	9/99	Cable Rates Forms 1240/1205	Division of the Ratepayer Advocate
All Regulated Companies	E/G/W	Delaware	Reg. No. 4	8/99	Filing Requirements (Position Statement)	Division of the Public Advocate
Mile High Cable Partners	C	Colorado	95-CV-5195	7/99	Cable Rates (Affidavit)	Brett Marshall, an individual, et al
Electric Restructuring Comments	E	Delaware	Reg. 49	7/99	Regulatory Policy (Supplemental)	Division of the Public Advocate
Long Neck Water Company	W	Delaware	99-31	6/99	Revenue Requirements	Division of the Public Advocate
Delmarva Power and Light Company	E	Delaware	99-163	6/99	Electric Restructuring	Division of the Public Advocate
Potomac Electric Power Company	E	District of Columbia	945	6/99	Divestiture of Generation Assets	U.S. GSA - Public Utilities
Comcast	C	Indiana	49C01-9802-CP-000386	6/99	Late Fees (Affidavit)	Ken Hecht, et al
Petitions of BA-NJ and NJPA re: Payphone Ops	T	New Jersey	TO97100792 PUCOT 11269-97N	6/99	Economic Subsidy Issues (Surrebuttal)	Division of the Ratepayer Advocate
Montague Water and Sewer Companies	W/WW	New Jersey	WR98101161 WR98101162 PUCRS 11514-98N	5/99	Revenue Requirements Rate Design (Supplemental)	Division of the Ratepayer Advocate
Cablevision of Bergen, Bayonne, Newark	C	New Jersey	CR98111197-199 CR98111190	5/99	Cable Rates Forms 1240/1205	Division of the Ratepayer Advocate
Cablevision of Bergen, Hudson, Monmouth	C	New Jersey	CR97090624-626 CTV 1697-98N	5/99	Cable Rates - Form 1235 (Rebuttal)	Division of the Ratepayer Advocate
Kent County Water Authority	W	Rhode Island	2860	4/99	Revenue Requirements	Division of Public Utilities & Carriers
Montague Water and Sewer Companies	W/WW	New Jersey	WR98101161 WR98101162	4/99	Revenue Requirements Rate Design	Division of the Ratepayer Advocate
PEPCO	E	District of Columbia	945	4/99	Divestiture of Assets	U.S. GSA - Public Utilities
Western Resources, Inc. and Kansas City Power & Light	E	Kansas	97-WSRE-676-MER	4/99	Merger Approval (Surrebuttal)	Citizens' Utility Ratepayer Board
Delmarva Power and Light Company	E	Delaware	98-479F	3/99	Fuel Costs	Division of the Public Advocate
Lenfest Atlantic d/b/a Suburban Cable	C	New Jersey	CR97070479 et al	3/99	Cable Rates	Division of the Ratepayer Advocate
Electric Restructuring Comments	E	District of Columbia	945	3/99	Regulatory Policy	U.S. GSA - Public Utilities

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Petitions of BA-NJ and NJPA re: Payphone Ops	T	New Jersey	TO97100792 PUCOT 11269-97N	3/99	Tariff Revision Payphone Subsidies FCC Services Test (Rebuttal)	Division of the Ratepayer Advocate
Western Resources, Inc. and Kansas City Power & Light	E	Kansas	97-WSRE-676-MER	3/99	Merger Approval (Answering)	Citizens' Utility Ratepayer Board
Western Resources, Inc. and Kansas City Power & Light	E	Kansas	97-WSRE-676-MER	2/99	Merger Approval	Citizens' Utility Ratepayer Board
Adelphia Cable Communications	C	Vermont	6117-6119	1/99	Late Fees (Additional Direct Supplemental)	Department of Public Service
Adelphia Cable Communications	C	Vermont	6117-6119	12/98	Cable Rates (Forms 1240, 1205, 1235) and Late Fees (Direct Supplemental)	Department of Public Service
Adelphia Cable Communications	C	Vermont	6117-6119	12/98	Cable Rates (Forms 1240, 1205, 1235) and Late Fees	Department of Public Service
Orange and Rockland/ Consolidated Edison	E	New Jersey	EM98070433	11/98	Merger Approval	Division of the Ratepayer Advocate
Cablevision	C	New Jersey	CR97090624 CR97090625 CR97090626	11/98	Cable Rates - Form 1235	Division of the Ratepayer Advocate
Petitions of BA-NJ and NJPA re: Payphone Ops.	T	New Jersey	TO97100792 PUCOT 11269-97N	10/98	Payphone Subsidies FCC New Services Test	Division of the Ratepayer Advocate
United Water Delaware	W	Delaware	Docket No. 98-98	8/98	Revenue Requirements	Division of the Public Advocate
Cablevision	C	New Jersey	CR97100719, 726 730, 732	8/98	Cable Rates (Oral Testimony)	Division of the Ratepayer Advocate
Potomac Electric Power Company	E	Maryland	Case No. 8791	8/98	Revenue Requirements Rate Design	U.S. GSA - Public Utilities
Investigation of BA-NJ IntraLATA Calling Plans	T	New Jersey	TO97100808 PUCOT 11326-97N	8/98	Anti-Competitive Practices (Rebuttal)	Division of the Ratepayer Advocate
Investigation of BA-NJ IntraLATA Calling Plans	T	New Jersey	TO97100808 PUCOT 11326-97N	7/98	Anti-Competitive Practices	Division of the Ratepayer Advocate
TCI Cable Company/ Cablevision	C	New Jersey	CTV 03264-03268 and CTV 05061	7/98	Cable Rates	Division of the Ratepayer Advocate
Mount Holly Water Company	W	New Jersey	WR98020058 PUC 03131-98N	7/98	Revenue Requirements	Division of the Ratepayer Advocate
Pawtucket Water Supply Board	W	Rhode Island	2674	5/98	Revenue Requirements (Surrebuttal)	Division of Public Utilities & Carriers
Pawtucket Water Supply Board	W	Rhode Island	2674	4/98	Revenue Requirements	Division of Public Utilities and Carriers
Energy Master Plan Phase II Proceeding - Restructuring	E	New Jersey	EX94120585U, EO97070457,60,63,66	4/98	Electric Restructuring Issues (Supplemental Surrebuttal)	Division of the Ratepayer Advocate
Energy Master Plan Phase I Proceeding - Restructuring	E	New Jersey	EX94120585U, EO97070457,60,63,66	3/98	Electric Restructuring Issues	Division of the Ratepayer Advocate

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Shorelands Water Company	W	New Jersey	WR97110835 PUC 11324-97	2/98	Revenue Requirements	Division of the Ratepayer Advocate
TCI Communications, Inc.	C	New Jersey	CR97030141 and others	11/97	Cable Rates (Oral Testimony)	Division of the Ratepayer Advocate
Citizens Telephone Co. of Kecksburg	T	Pennsylvania	R-00971229	11/97	Alternative Regulation Network Modernization	Office of Consumer Advocate
Consumers Pennsylvania Water Co. - Shenango Valley Division	W	Pennsylvania	R-00973972	10/97	Revenue Requirements (Surrebuttal)	Office of Consumer Advocate
Universal Service Funding	T	New Jersey	TX95120631	10/97	Schools and Libraries Funding (Rebuttal)	Division of the Ratepayer Advocate
Universal Service Funding	T	New Jersey	TX95120631	9/97	Low Income Fund High Cost Fund	Division of the Ratepayer Advocate
Consumers Pennsylvania Water Co. - Shenango Valley Division	W	Pennsylvania	R-00973972	9/97	Revenue Requirements	Office of Consumer Advocate
Delmarva Power and Light Company	G/E	Delaware	97-65	9/97	Cost Accounting Manual Code of Conduct	Office of the Public Advocate
Western Resources, Oneok, and WAI	G	Kansas	WSRG-486-MER	9/97	Transfer of Gas Assets	Citizens' Utility Ratepayer Board
Universal Service Funding	T	New Jersey	TX95120631	9/97	Schools and Libraries Funding (Rebuttal)	Division of the Ratepayer Advocate
Universal Service Funding	T	New Jersey	TX95120631	8/97	Schools and Libraries Funding	Division of the Ratepayer Advocate
Kent County Water Authority	W	Rhode Island	2555	8/97	Revenue Requirements (Surrebuttal)	Division of Public Utilities and Carriers
Ironton Telephone Company	T	Pennsylvania	R-00971182	8/97	Alternative Regulation Network Modernization (Surrebuttal)	Office of Consumer Advocate
Ironton Telephone Company	T	Pennsylvania	R-00971182	7/97	Alternative Regulation Network Modernization	Office of Consumer Advocate
Comcast Cablevision	C	New Jersey	Various	7/97	Cable Rates (Oral Testimony)	Division of the Ratepayer Advocate
Maxim Sewerage Corporation	WW	New Jersey	WR97010052 PUCRA 3154-97N	7/97	Revenue Requirements	Division of the Ratepayer Advocate
Kent County Water Authority	W	Rhode Island	2555	6/97	Revenue Requirements	Division of Public Utilities and Carriers
Consumers Pennsylvania Water Co. - Roaring Creek	W	Pennsylvania	R-00973869	6/97	Revenue Requirements (Surrebuttal)	Office of Consumer Advocate
Consumers Pennsylvania Water Co. - Roaring Creek	W	Pennsylvania	R-00973869	5/97	Revenue Requirements	Office of Consumer Advocate
Delmarva Power and Light Company	E	Delaware	97-58	5/97	Merger Policy	Office of the Public Advocate
Middlesex Water Company	W	New Jersey	WR96110818 PUCRL 11663-96N	4/97	Revenue Requirements	Division of the Ratepayer Advocate

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
Maxim Sewerage Corporation	WW	New Jersey	WR96080628 PUCRA 09374-96N	3/97	Purchased Sewerage Adjustment	Division of the Ratepayer Advocate
Interstate Navigation Company	N	Rhode Island	2484	3/97	Revenue Requirements Cost of Capital (Surrebuttal)	Division of Public Utilities & Carriers
Interstate Navigation Company	N	Rhode Island	2484	2/97	Revenue Requirements Cost of Capital	Division of Public Utilities & Carriers
Electric Restructuring Comments	E	District of Columbia	945	1/97	Regulatory Policy	U.S. GSA - Public Utilities
United Water Delaware --	W	Delaware	96-194	1/97	Revenue Requirements	Office of the Public Advocate
PEPCO/ BGE/ Merger Application	E/G	District of Columbia	951	10/96	Regulatory Policy Cost of Capital (Rebuttal)	GSA
Western Resources, Inc.	E	Kansas	193.306-U 193.307-U	10/96	Revenue Requirements Cost of Capital (Supplemental)	Citizens' Utility Ratepayer Board
PEPCO and BGE Merger Application	E/G	District of Columbia	951	9/96	Regulatory Policy, Cost of Capital	U.S. GSA - Public Utilities
Utilicorp United, Inc.	G	Kansas	193,787-U	8/96	Revenue Requirements	Citizens' Utility Ratepayer Board
TKR Cable Company of Gloucester	C	New Jersey	CTV07030-95N	7/96	Cable Rates (Oral Testimony)	Division of the Ratepayer Advocate
TKR Cable Company of Warwick	C	New Jersey	CTV057537-95N	7/96	Cable Rates (Oral Testimony)	Division of the Ratepayer Advocate
Delmarva Power and Light Company	E	Delaware	95-196F	5/96	Fuel Cost Recovery	Office of the Public Advocate
Western Resources, Inc.	E	Kansas	193.306-U 193.307-U	5/96	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Princeville Utilities Company, Inc.	W/WW	Hawaii	95-0172 95-0168	1/96	Revenue Requirements Rate Design	Princeville at Hanalei Community Association
Western Resources, Inc.	G	Kansas	193,305-U	1/96	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Environmental Disposal Corporation	WW	New Jersey	WR94070319 (Remand Hearing)	11/95	Revenue Requirements Rate Design (Supplemental)	Division of the Ratepayer Advocate
Environmental Disposal Corporation	WW	New Jersey	WR94070319 (Remand Hearing)	11/95	Revenue Requirements	Division of the Ratepayer Advocate
Lanai Water Company	W	Hawaii	94-0366	10/95	Revenue Requirements Rate Design	Division of Consumer Advocacy
Cablevision of New Jersey, Inc.	C	New Jersey	CTV01382-95N	8/95	Basic Service Rates (Oral Testimony)	Division of the Ratepayer Advocate
Cablevision of New Jersey, Inc.	C	New Jersey	CTV01381-95N	8/95	Basic Service Rates (Oral Testimony)	Division of the Ratepayer Advocate
Chesapeake Utilities Corporation	G	Delaware	95-73	7/95	Revenue Requirements	Office of the Public Advocate

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
East Honolulu Community Services, Inc.	WW	Hawaii	7718	6/95	Revenue Requirements	Division of Consumer Advocacy
Wilmington Suburban Water Corporation	W	Delaware	94-149	3/95	Revenue Requirements	Office of the Public Advocate
Environmental Disposal Corporation	WW	New Jersey	WR94070319	1/95	Revenue Requirements (Supplemental)	Division of the Ratepayer Advocate
Roaring Creek Water Company	W	Pennsylvania	R-00943177	1/95	Revenue Requirements (Surrebuttal)	Office of Consumer Advocate
Roaring Creek Water Company	W	Pennsylvania	R-00943177	12/94	Revenue Requirements	Office of Consumer Advocate
Environmental Disposal Corporation	WW	New Jersey	WR94070319	12/94	Revenue Requirements	Division of the Ratepayer Advocate
Delmarva Power and Light Company	E	Delaware	94-84	11/94	Revenue Requirements	Office of the Public Advocate
Delmarva Power and Light Company	G	Delaware	94-22	8/94	Revenue Requirements	Office of the Public Advocate
Empire District Electric Company	E	Kansas	190,360-U	8/94	Revenue Requirements	Citizens' Utility Ratepayer Board
Morris County Municipal Utility Authority	SW	New Jersey	MM10930027 ESW 1426-94	6/94	Revenue Requirements	Rate Counsel
US West Communications	T	Arizona	E-1051-93-183	5/94	Revenue Requirements (Surrebuttal)	Residential Utility Consumer Office
Pawtucket Water Supply Board	W	Rhode Island	2158	5/94	Revenue Requirements (Surrebuttal)	Division of Public Utilities & Carriers
US West Communications	T	Arizona	E-1051-93-183	3/94	Revenue Requirements	Residential Utility Consumer Office
Pawtucket Water Supply Board	W	Rhode Island	2158	3/94	Revenue Requirements	Division of Public Utilities & Carriers
Pollution Control Financing Authority of Camden County	SW	New Jersey	SR91111718J	2/94	Revenue Requirements (Supplemental)	Rate Counsel
Roaring Creek Water Company	W	Pennsylvania	R-00932665	9/93	Revenue Requirements (Supplemental)	Office of Consumer Advocate
Roaring Creek Water Company	W	Pennsylvania	R-00932665	9/93	Revenue Requirements	Office of Consumer Advocate
Kent County Water Authority	W	Rhode Island	2098	8/93	Revenue Requirements (Surrebuttal)	Division of Public Utilities and Carriers
Wilmington Suburban Water Company	W	Delaware	93-28	7/93	Revenue Requirements	Office of Public Advocate
Kent County Water Authority	W	Rhode Island	2098	7/93	Revenue Requirements	Division of Public Utilities & Carriers
Camden County Energy Recovery Associates, Inc.	SW	New Jersey	SR91111718J ESW1263-92	4/93	Revenue Requirements	Rate Counsel
Pollution Control Financing Authority of Camden County	SW	New Jersey	SR91111718J ESW 1263-92	4/93	Revenue Requirements	Rate Counsel
Jamaica Water Supply Company	W	New York	92-W-0583	3/93	Revenue Requirements	County of Nassau Town of Hempstead

<u>Company</u>	<u>Utility</u>	<u>State</u>	<u>Docket</u>	<u>Date</u>	<u>Topic</u>	<u>On Behalf Of</u>
New Jersey-American Water Company	W/WW	New Jersey	WR92090908J PUC 7266-92S	2/93	Revenue Requirements	Rate Counsel
Passaic County Utilities Authority	SW	New Jersey	SR91121816J ESW0671-92N	9/92	Revenue Requirements	Rate Counsel
East Honolulu Community Services, Inc.	WW	Hawaii	7064	8/92	Revenue Requirements	Division of Consumer Advocacy
The Jersey Central Power and Light Company	E	New Jersey	PUC00661-92 ER91121820J	7/92	Revenue Requirements	Rate Counsel
Mercer County Improvement Authority	SW	New Jersey	EWS11261-91S SR91111682J	5/92	Revenue Requirements	Rate Counsel
Garden State Water Company	W	New Jersey	WR9109-1483 PUC 09118-91S	2/92	Revenue Requirements	Rate Counsel
Elizabethtown Water Company	W	New Jersey	WR9108-1293J PUC 08057-91N	1/92	Revenue Requirements	Rate Counsel
New Jersey American Water Company	W/WW	New Jersey	WR9108-1399J PUC 8246-91	12/91	Revenue Requirements	Rate Counsel
Pennsylvania-American Water Company	W	Pennsylvania	R-911909	10/91	Revenue Requirements	Office of Consumer Advocate
Mercer County Improvement Authority	SW	New Jersey	SR9004-0264J PUC 3389-90	10/90	Revenue Requirements	Rate Counsel
Kent County Water Authority	W	Rhode Island	1952	8/90	Revenue Requirements Regulatory Policy (Surrebuttal)	Division of Public Utilities & Carriers
New York Telephone	T	New York	90-C-0191	7/90	Revenue Requirements Affiliated Interests (Supplemental)	NY State Consumer Protection Board
New York Telephone	T	New York	90-C-0191	7/90	Revenue Requirements Affiliated Interests	NY State Consumer Protection Board
Kent County Water Authority	W	Rhode Island	1952	6/90	Revenue Requirements Regulatory Policy	Division of Public Utilities & Carriers
Ellesor Transfer Station	SW	New Jersey	SO8712-1407 PUC 1768-88	11/89	Regulatory Policy	Rate Counsel
Interstate Navigation Co.	N	Rhode Island	D-89-7	8/89	Revenue Requirements Regulatory Policy	Division of Public Utilities & Carriers
Automated Modular Systems, Inc.	SW	New Jersey	PUC1769-88	5/89	Revenue Requirements Schedules	Rate Counsel
SNET Cellular, Inc.	T	Connecticut	-	2/89	Regulatory Policy	First Selectman Town of Redding

APPENDIX B

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

REVENUE REQUIREMENT SUMMARY

	Company Claim (A)	Recommended Adjustment	Recommended Position	
1. Pro Forma Rate Base	\$16,200,880	(\$6,919,689)	\$9,281,191	(B)
2. Required Cost of Capital	7.95%	-0.72%	7.23%	(C)
3. Required Return	\$1,287,905	(\$617,304)	\$670,601	
4. Operating Income @ Present Rates	113,336	493,322	606,658	(D)
5. Operating Income Deficiency	\$1,174,569	(\$1,110,625)	\$63,944	
6. Revenue Multiplier	1.3985		1.7665	(E)
7. Revenue Requirement Increase	<u>\$1,642,583</u>	<u>(\$1,529,626)</u>	<u>\$112,957</u>	

Sources:

- (A) Company Exhibit 2, page 1.
- (B) Schedule ACC-2.
- (C) Schedule ACC-10.
- (D) Schedule ACC-16.
- (E) Schedule ACC-26.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

RATE BASE SUMMARY

	Company Claim (A)	Recommended Adjustment		Recommended Position
1. Utility Plant in Service	\$34,242,718	(\$6,986,165)	(B)	\$27,256,553
Less:				
2. Accumulated Depreciation	(\$12,789,716)	\$978,357	(C)	(\$11,811,359)
3. Contributions in Aid of Construction	(5,090,725)	0		(5,090,725)
4. Net Utility Plant	\$16,362,277	(\$6,007,808)		\$10,354,469
Plus:				
5. Inventory	\$185,000	(\$6,262)	(D)	\$178,738
6. Prepayments	295,000	(48,686)	(E)	246,314
7. Working Capital Allowance	760,320	(760,320)	(F)	0
Less:				
8. Customer Advances	(\$450,139)	(\$250,699)	(G)	(\$700,838)
9. Customer Deposits	(101,578)	0		(101,578)
10. Deferred Taxes	(850,000)	154,085	(H)	(695,915)
11. Total Rate Base	<u>\$16,200,880</u>	<u>(\$6,919,689)</u>		<u>\$9,281,191</u>

Sources:

- (A) Company Exhibit 2, page 18.
- (B) Schedule ACC-3.
- (C) Schedule ACC-4.
- (D) Schedule ACC-5.
- (E) Schedule ACC-6.
- (F) Schedule ACC-7.
- (G) Schedule ACC-8.
- (H) Schedule ACC-9.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

UTILITY PLANT IN SERVICE

1. Utility Plant in Service @ 12/31/03	\$26,907,284	(A)
2. 2004 Utility Plant Additions	<u>349,269</u>	(B)
3. Pro Forma 2004 Plant	\$27,256,553	
4. Company Claim	<u>34,242,718</u>	(C)
5. Recommended Adjustment	<u>\$6,986,165</u>	

Sources:

(A) Response to RAR-48, 2003 Annual Report to the BPU, page 11.

(B) Response to RAR-49.

(C) Company Exhibit 2, page 18.

Schedule ACC-4

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

ACCUMULATED DEPRECIATION

1. Utility Plant @12/31/03	\$26,907,284	(A)
2. Less Contributions and Advances	<u>(6,040,864)</u>	(B)
3. Depreciable Plant @ 12/31/03	\$20,866,420	
4. Pro Forma Plant @ 12/31/04	\$27,256,553	(C)
5. Less Contributions and Advances	<u>(5,791,563)</u>	(D)
6. Depreciable Plant @ 12/31/04	\$21,464,991	
7. Average 2004 Depreciable Plant	\$21,165,705	
8. Composite Depreciation Rate	<u>2.50%</u>	(E)
9. Pro Forma Depreciation Expense	\$529,143	
10. Accumulated Depreciation @ 12/31/03	<u>11,282,216</u>	(A)
11. Pro Forma Accumulated Dep. @ 12/31/04	\$11,811,359	
12. Company Claim	<u>12,789,716</u>	(F)
13. Recommended Adjustment	<u>\$978,357</u>	

Sources:

- (A) Response to RAR-48, 2003 Annual Report to the BPU, page 11.
- (B) Response to RAR-48, 2003 Annual Report to the BPU, page 12.
- (C) Schedule ACC-3.
- (D) CIAC per response to RAR-48, 2003 Annual Report to the BPU, page 12 and advances per Schedule ACC-8.
- (E) Depreciation Rate per Company Exhibit 2, page 10.
- (F) Company Exhibit 2, page 18.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

INVENTORY

1. Balance at 12/31/01	\$186,766	(A)
2. Balance at 12/31/02	184,376	(A)
3. Balance at 12/31/03	<u>165,072</u>	(A)
4. Average Three Year Balance	\$178,738	
5. Company Claim	<u>185,000</u>	(B)
6. Recommended Adjustment	<u>\$6,262</u>	

Sources:

(A) Company Exhibit 2, page 21.

(B) Company Exhibit 2, page 18.

Schedule ACC-6

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

PREPAYMENTS

1. Balance at 12/31/01	\$250,597	(A)
2. Balance at 12/31/02	231,446	(A)
3. Balance at 12/31/03	<u>256,899</u>	(A)
4. Average Three Year Balance	\$246,314	
5. Company Claim	<u>295,000</u>	(B)
6. Recommended Adjustment	<u>\$48,686</u>	

Sources:

(A) Company Exhibit 2, page 21.

(B) Company Exhibit 2, page 18.

Schedule ACC-7

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

CASH WORKING CAPITAL

1. Company Claim	\$760,320	(A)
2. Recommended Adjustment	<u>\$760,320</u>	

Sources:

(A) Company Exhibit 2, page 18.

SHORELANDS WATER COMPANY**TEST YEAR ENDING DECEMBER 31, 2004****CUSTOMER ADVANCES**

1. Decrease from 2001 to 2002	\$285,481	(A)
2. Decrease from 2002 to 2003	<u>213,122</u>	(A)
3. Average Annual Decrease	\$249,302	
4. Balance @ 12/31/03	<u>950,139</u>	(A)
5. Pro Forma Customer Advances	\$700,838	
6. Company Claim	<u>450,139</u>	(B)
7. Recommended Adjustments	<u>\$250,699</u>	

Sources:

(A) Company Exhibit 2, page 21.

(B) Company Exhibit 2, page 18.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

DEFERRED INCOME TAXES

1. Balance at 12/31/03	\$707,915	(A)
2. Amortization of ITC	<u>12,000</u>	(A)
3. Pro Forma Deferred Taxes	\$695,915	
4. Company Claim	<u>850,000</u>	(B)
5. Recommended Adjustment	<u>\$154,085</u>	

Sources:

(A) Response to RAR-48, 2003 Annual Report to the BPU,
page 32.

(B) Company Exhibit 2, page 18.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

REQUIRED COST OF CAPITAL

	Amount	Capital Structure	Cost Rate	Weighted Cost
	(A)			
1. Common Equity	\$6,570,865	42.34%	9.47% (C)	4.01%
2. Long Term Debt -Existing	3,200,000	20.62%	9.85% (A)	2.03%
3. Long Term Debt - New (B)	5,750,000	37.05%	3.20% (A)	1.19%
4. Total Cost of Capital	15,520,865	100.00%		<u>7.23%</u>

Sources:

(A) Company Exhibit 2, page 20.

(B) Reflects amount per Amended Financing Petition.

(C) Schedule ACC-11.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

RECOMMENDED COST OF EQUITY

1. Discounted Cash Flow Result (A)	8.90%	
2. Discounted Cash Flow Weighting (B)	<u>0.75</u>	6.67%
3. CAPM Result (C)	9.19%	
4. CAPM Weighting (B)	<u>0.25</u>	2.30%
5. Small Company Premium		<u>0.50%</u>
6. Recommended Return on Equity		<u>9.47%</u>

Sources:

(A) Schedule ACC-12.

(B) Based upon the Board's traditional reliance upon the DCF model.

(C) Schedule ACC-15.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

DISCOUNTED CASH FLOW RESULT

1. Dividend Yield	3.40%	(A)
2. Growth Rate	<u>5.50%</u>	(B)
3. Total Cost of Equity	<u>8.90%</u>	

Sources:

(A) Derived from Schedule ACC-13.

(B) Derived from Schedule ACC-14.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

AVERAGE DIVIDENDS

Company	Dividend	Closing Price	Current Dividend Yield
American States Water	\$0.88	\$22.10	4.00%
Aqua America	0.48	19.70	2.44%
California Water	1.13	27.25	4.15%
Connecticut Water Services	0.83	24.06	3.45%
Middlesex Water Company	0.66	17.31	3.81%
SJW Corporation	1.02	32.00	3.19%
Southwest Water Company	0.21	12.09	1.74%
York Water Company	0.58	17.15	3.38%
Average			<u>3.27%</u>

Company	Dividend	52 Week Low	52 Week High	52 Week Average	Dividend Yield
American States Water	\$0.88	\$20.82	\$26.80	\$23.81	3.71%
Aqua America	0.48	18.28	22.85	20.57	2.33%
California Water	1.13	25.11	30.15	27.63	4.09%
Connecticut Water Services	0.83	24.05	30.41	27.23	3.05%
Middlesex Water Company	0.66	16.65	21.81	19.23	3.43%
SJW Corporation	1.02	27.32	38.25	32.79	3.11%
Southwest Water Company	0.21	9.95	15.79	12.87	1.63%
York Water Company	0.58	16.50	21.04	18.77	3.09%
Average					<u>3.06%</u>

Source: Yahoo Finance, August 10, 2004 (Closing prices August 9, 2004).

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

GROWTH IN EARNINGS, DIVIDENDS, BOOK VALUE

	Five Year Historic Earnings	Five Year Historic Dividends	Five Year Historic Bk. Value
American States Water	1.50%	1.00%	4.00%
Aqua America	9.50%	6.00%	9.50%
California Water	-6.50%	1.00%	1.00%
Connecticut Water Services	2.50%	1.00%	3.50%
Middlesex Water Company	0.50%	2.50%	3.50%
SJW Corporation	-0.50%	4.00%	4.00%
Southwest Water Company	15.50%	10.50%	11.50%
York Water Company (*)	2.50%	NA	NA
Average	<u>3.13%</u>	<u>3.71%</u>	<u>5.29%</u>

	Ten Year Historic Earnings	Ten Year Historic Dividends	Ten Year Historic Bk. Value
American States Water	NA	1.50%	4.50%
Aqua America	8.50%	5.00%	8.00%
California Water	-0.50%	2.00%	2.50%
Average	<u>4.00%</u>	<u>2.83%</u>	<u>5.00%</u>

	Five Year Projected Earnings	Five Year Projected Dividends	Five Year Projected Bk. Value
American States Water	9.50%	1.50%	4.00%
Aqua America	9.50%	7.00%	11.50%
California Water	11.00%	1.00%	14.50%
Connecticut Water Services	NA	NA	NA
Middlesex Water Company	NA	NA	NA
SJW Corporation	NA	NA	NA
Southwest Water Company	8.00%	NA	NA
York Water Company	7.00%	NA	NA
Average	<u>9.00%</u>	<u>3.17%</u>	<u>10.00%</u>

Sources:

Value Line - April 30, 2004, except where otherwise noted.

* Yahoo Finance, July 7, 2004.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

CAPITAL ASSET PRICING MODEL RESULT

Risk Free Rate + (Beta X Market Premium)

$$5.06\% + (.625 \times 6.6\%) = \underline{9.19\%}$$

Sources:

Risk Free Rate = 20 Year Constant Maturity Treasury at August 9, 2004.

Betas per Value Line Investment Survey, April 30, 2004.

Market Premium per 2003 Yearbook (Stocks, Bonds, Bills, and Inflation), Ibbotson Associates, Table 2-1.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

OPERATING INCOME SUMMARY

		Schedule No.
1. Company Claim	\$113,336	1
Recommended Adjustments:		
2. Salaries and Wages	85,488	17
3. Payroll Taxes	6,540	18
4. Pension Costs	15,987	19
5. Deferred Purchased Water Costs	25,595	20
6. Regulatory Commission Expense	24,750	21
7. Inflation Adjustments	63,408	22
8. Depreciation Expense	196,598	23
9. Income Taxes @ Present Rates	133,096	24
10. Interest Synchronization	<u>(58,140)</u>	25
11. Net Operating Income	<u>\$606,658</u>	

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

SALARIES AND WAGES

1. 2004 Pro Forma Test Year	\$1,363,163	(A)
2. Company Claim	<u>1,492,690</u>	(A)
3. Recommended Adjustment	\$129,527	
4. Income Taxes @	34.00% <u>44,039</u>	
5. Operating Income Impact	<u>\$85,488</u>	

Sources:

(A) Response to RAR-18.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

PAYROLL TAXES

1. Recommended Salary and Wage Adjustments		\$129,527	(A)
2. Payroll Taxes @ 7.65%		9,909	(B)
3. Income Taxes @	34.00%	<u>3,369</u>	
4. Operating Income Impact		<u>\$6,540</u>	

Sources:

(A) Schedule ACC-17.

(B) Based on statutory rate.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

PENSION COSTS

1. FASB 87 Costs Per Actuarial Report	\$141,777	(A)
2. Company Claim	<u>166,000</u>	(B)
3. Recommended Adjustment	24,223	
4. Income Taxes @ 34.00%	<u>8,236</u>	
5. Operating Income Impact	<u>\$15,987</u>	

Sources:

(A) Response to RAR-36.

(B) Company Exhibit 2, page 11.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

DEFERRED PURCHASED WATER COSTS

1. Annual Claim for Deferred NJWSA Increase		\$22,500	(A)
2. Annual Claim for Keansburg Water Rights		<u>16,280</u>	(A)
3. Recommended Adjustment		\$38,780	
4. Income Taxes @	34.00%	<u>13,185</u>	
5. Operating Income Impact		<u>\$25,595</u>	

Sources:

(A) Company Exhibit 2, page 16.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

REGULATORY COMMISSION EXPENSES

1. Company Claim	\$100,000	(A)
2. Amortization Period (C)	<u>4</u>	(B)
3. Annual Amortization	\$25,000	
4. Sharing Between Ratepayers and Shareholders	<u>50.00%</u>	(B)
5. Recommended Annual Cost	\$12,500	
6. Company Claim	<u>50,000</u>	(A)
7. Recommended Adjustment	\$37,500	
8. Income Taxes @ 34.00%	<u>12,750</u>	
9. Operating Income Impact	<u>\$24,750</u>	

Sources:

(A) Company Exhibit 2, page 14.

(B) Recommendation of Ms. Crane.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

INFLATION ADJUSTMENT

	Operation	Maintenance	
	(A)	(B)	
1. Pumping (C)	22,718		
2. Water Treatment	\$10,549	\$3,670	
3. Transmission & Distribution	4,200	\$7,351	
4. Customer Accounting	6,966		
5. All Other A&G	38,929		
6. General Plant		1,690	
7. Subtotals	\$83,362	\$12,711	
8. Total 2005 Inflation Adjustment		\$96,073	(D)
9. Income Taxes @	34.00%	32,665	
10. Operating Income Impact		<u>\$63,408</u>	

Sources:

(A) Company Exhibit 2, page 8.

(B) Company Exhibit 2, page 9.

(C) Includes inflation and impact of new plant.

(D) Sum of Operation and Maintenance adjustments.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

DEPRECIATION EXPENSES

1. Pro Forma Utility Plant	\$27,256,553	(A)
2. Less Contributions and Advances	<u>(5,791,563)</u>	(A)
3. Depreciable Plant	\$21,464,991	
4. Composite Depreciation Rate	<u>2.50%</u>	(B)
5. Pro Forma Depreciation Expense	\$536,625	
6. Company Claim	<u>834,500</u>	(C)
7. Recommended Adjustment	297,875	
8. Income Taxes @	34.00% <u>101,278</u>	
9. Operating Income Impact	<u>\$196,598</u>	

Sources:

(A) Schedule ACC-2.

(B) Depreciation Rate per Company Exhibit 2, page 10.

(C) Company Exhibit 2, page 10.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

INCOME TAXES AT PRESENT RATES

1. Operating Revenue		\$8,328,264	(A)
2. Total Operating Expenses		<u>8,214,929</u>	(A)
3. Net Operating Revenue		\$113,335	
4. Interest Expense		<u>469,500</u>	(B)
5. Taxable Income		(\$356,165)	
6. Income Taxes @	34.00%	(121,096)	
7. Tax Credits - ITC Amortization		<u>(12,000)</u>	(C)
8. Total Income Taxes		(\$133,096)	
9. Company Claim		<u>0</u>	
10. Recommended Adjustment		<u>\$133,096</u>	

Sources:

(A) Company Exhibit 2, page 1.

(B) Response to RAR-56.

(C) Company Exhibit 2, page 19.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

INTEREST SYNCHRONIZATION

1. Pro Forma Rate Base	\$9,281,191	(A)
2. Weighted Cost of Debt	<u>3.22%</u>	(B)
3. Pro Forma Interest Expense	\$298,501	
4. Company Claim	<u>469,500</u>	(C)
5. Increase in Taxable Income	\$170,999	
6. Income Taxes @ 34.00%	<u>\$58,140</u>	

Sources:

- (A) Schedule ACC-2.
- (B) Schedule ACC-10.
- (C) Response to RAR-56.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

REVENUE MULTIPLIER

1. Revenue	1.0000	
2. Revenue Taxes @ 14.2292%	<u>0.1423</u>	(A)
3. Federal Taxable Income	0.8577	
4. Income Taxes @ 34%	<u>0.2916</u>	(B)
5. Operating Income	0.5661	
6. Revenue Multiplier	<u>1.7665</u>	(C)

Sources:

(A) Company Exhibit 2, page 17.

(B) Rate per Company Exhibit 2, page 19.

(C) Line 1 / Line 5.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

IMPACT OF NEW FACILITY-PHASE II INCREASE

1. Incremental Power Costs		\$31,500	(A)
2. Incremental Chemical Costs		46,600	(A)
3. Incremental Sludge Disposal Costs		780	(A)
4. Depreciation Expense		<u>157,500</u>	(B)
5. Total Incremental Costs		\$236,380	
6. Income Taxes @	34.00%	<u>80,369</u>	
7. Operating Income Impact		\$156,011	
8. Capital Costs	\$6,300,000		(B)
9. Return @	<u>7.23%</u>		(C)
10. Return Requirement		\$455,199	
11. Interest Synchronization		<u>(68,891)</u>	(D)
12. Total Operating Income Impact		\$542,319	
13. Revenue Multiplier		<u>1.76651</u>	(E)
14. Phase II Increase		<u>\$958,013</u>	

Sources:

(A) Response to RAR-51.

(B) Company Exhibit 2, page 10.

(C) Schedule ACC-10.

(D) Weighted cost of debt times capital cost times income tax rate.

(E) Schedule ACC-26.

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

REVENUE REQUIREMENT IMPACT OF ADJUSTMENTS

1. Rate of Return	(\$164,081)
2. Utility Plant in Service	(705,908)
3. Accumulated Depreciation	98,857
4. Inventory	(633)
5. Prepayments	(4,919)
6. Working Capital Allowance	(76,826)
7. Customer Advances	(25,332)
8. Deferred Taxes	15,569
9. Salaries and Wages	(119,551)
10. Payroll Taxes	(9,146)
11. Pension Costs	(22,357)
12. Deferred Purchased Water Costs	(35,793)
13. Regulatory Commission Expense	(34,612)
14. Inflation Adjustments	(88,674)
15. Depreciation Expense	(274,933)
16. Income Taxes @ Present Rates	(186,129)
17. Interest Synchronization	81,306
18. Revenue Multiplier	23,535
19. Total Recommended Adjustments	<u>(\$1,529,626)</u>
20. Company Claim	<u>1,642,583</u>
21. Recommended Revenue Requirement Deficiency	<u>\$112,957</u>

SHORELANDS WATER COMPANY

TEST YEAR ENDING DECEMBER 31, 2004

PRO FORMA INCOME STATEMENT

	Per Company	Recommended Adjustments	Pro Forma Present Rates	Recommended Rate Adjustment	Pro Forma Proposed Rates
1. Operating Revenues	\$8,328,264	\$0	\$8,328,264	\$112,957	\$8,441,221
2. Operating Expenses	6,082,563	(326,103)	5,756,460	0	5,756,460
3. Depreciation	834,500	(297,875)	536,625	0	536,625
4. Taxes Other Than Income	1,297,865	(9,909)	1,287,956	16,073	1,304,029
5. Taxable Income Before Interest Expenses	\$113,336	\$633,887	\$747,223	\$96,884	\$844,107
6. Interest Expense	469,500	(170,999)	298,501	0	298,501
7. Taxable Income	(\$356,164)	\$804,886	\$448,722	\$96,884	\$545,606
8. Income Taxes @ 34.00%	0	140,565	140,565	32,941	173,506
9. Operating Income	\$113,336	\$493,322	\$606,658	\$63,944	\$670,601
10. Rate Base	\$16,200,880		\$9,281,191		\$9,281,191
11. Rate of Return	0.70%		6.54%		7.23%

APPENDIX C

Referenced Data Requests

RAR-18

RAR-36

RAR-37

RAR-42

RAR-48 (partial)

RAR-49

RAR-51

RAR-56

RAR-59

Bruce S. Edington, Esq.
June 9, 2004
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RAR-18. Please provide full and complete copies of any and all supporting workpapers and calculations for the Company's labor cost claim.

	<u>Test Year 2004</u>	<u>Estimated 4% Increase</u>	<u>Open Eng. Position</u>	<u>Rate Year 2005</u>
Operation Labor	984,375	39,375	75,000	1,098,750
Maintenance Labor	<u>378,788</u>	<u>15,152</u>	<u>0</u>	<u>393,940</u>
	1,363,163	54,527	75,000	1,492,690

Bruce S. Edington, Esq.
June 9, 2004
Page 38

RAR-36. Please provide the most recent actuarial studies for the Company's pension plan and, if applicable, other post-retirement benefit plan. (see attached)

RAR-36

**SIEGEL
BENEFIT
CONSULTANTS, INC.**

71 UNION AVENUE
RUTHERFORD, NJ 07070

ACTUARIES & ADMINISTRATORS

(201) 896-9616
FAX: (201) 896-0560
customerservice@sbcbenefit.com

May 20, 2004

Mr. Michael Walsh
Shorelands Water Co., Inc.
1709 Union Avenue
Hazlet, NJ 07730

Re: Shorelands Water Co., Inc. Pension Plan
Financial Accounting Standards Board Statement No. 87
(FASB-87) **Reconciliation** for the Year Ending **December 31, 2003**

Dear Mr. Walsh:

In accordance with your request, we are pleased to present the results of our FASB-87 reconciliation report for the plan year ending December 31, 2003.

The calculations are based on a specific funding method used to produce a projected and accrued liability, namely, the projected unit credit method. Pension obligations are required to be measured and disclosed on the books of the Company in conformity with the FASB Statement 87. That Statement deals with the obligations of an on-going pension plan.

The 2003 Net Periodic Pension Cost of \$141,777 includes the following:

- a) The Service Cost is the present value of benefits attributed by the benefit formula to service during the valuation year.
- b) The Interest Cost is the increase in the value of projected benefits due to the passage of time.
- c) The Amortization of Unrecognized Net Asset Existing at Date of Initial Application of Statement 87 is being amortized on a straight-line basis over 17 years.
- d) The Actual Return on Plan Assets is based on the fair value of plan assets at the beginning and end of the valuation year, adjusted for contributions and benefit payments.

- e) There was no **Amortization of Prior Service Cost** reported on the 1996 FASB '87 report prepared by the prior third party administrative firm and any modifications since that report are only intended to be clarifications or corrections.
- f) The **Amortization of Unrecognized Net Gain** is the cumulative gain that has yet to be recognized as part of the Net Periodic Pension Cost. A gain is a change in the value of either the Projected Benefit Obligation or the plan assets resulting from experience more favorable than that assumed, or from a change in actuarial assumptions. This amount is amortized on a straight-line basis over the average remaining service of employees expected to receive benefits under the plan - for 2003, a period of 18.10 years.
- g) **Net Asset Gain during the period deferred for later recognition** is the actual investment experience for 2003 compared to what was expected at the beginning of the year.

There are three basic assumptions which are required to be applied explicitly and not modified by the effect of other assumptions. Those assumptions are:

- 1) Discount Rate - The rate used to arrive at the current value of certain future benefit obligations, i.e., the Projected Benefit Obligation, current Service Cost, and Accumulated Benefit Obligation. This is the expected rate at which pension benefits could be effectively settled on an annuity basis. It should be the best estimate of the interest rate for the settlement of the accrued benefits (adjusted for the effect of future compensation) whereby those benefits would be distributed over the life expectancy of the participants or over the joint life expectancy of participants and their beneficiaries.

The interest rate may be based on current prices of annuity contracts that could be used to settle the pension obligations. It may also be based on either Pension Benefit Guaranty Corporation rates or rates of return on high-quality fixed-income investments currently available and expected to be available during the period to maturity of the pension benefits. For 2003, Shorelands Water Co., Inc. chose 7.75%.

2) Salary Scale Assumption (Benefit Increase Assumption) - The Projected Benefit Obligation (PBO) reflects future compensation levels to the extent that the pension benefit formula defines pension benefits wholly or partially as a function of future compensation levels. Assumed compensation levels reflect an estimate of the actual future compensation levels of the individual employees involved, including future changes attributed to general price levels, productivity, seniority, promotion and other factors. All assumptions shall be consistent to the extent that each reflects expectations of the same future economic conditions such as future rates of inflation. There are limitations such as those currently imposed by Section 415 of the Internal Revenue Code that affect benefits provided by the Plan. For 2003, Shorelands Water Co., Inc. chose 4.50%

3) Asset Earnings Rate - The expected long-term rate of return on plan assets should reflect the average rate of earnings expected on the funds invested to provide for the benefits included in the Projected Benefit Obligation. In estimating the rate, appropriate consideration was given to the returns being earned by the plan assets in the fund and the rates of return expected to be available for reinvestment, but not the expected return on future years' contributions. For 2003, Shorelands Water Co., Inc. has determined 8% as the long-term interest rate.

The following are general items which apply to the FASB-87 valuation:

- a) All participants and their benefits have been included in our calculations.
- b) The plan sponsor's funding policy has been to meet contributions as they accrue.
- c) The amortization of the original transitional asset is over a period of 17 years.
- d) There have been no 2003 amendments affecting the benefit structure of the Plan.
- e) There are no insurance or annuity contracts for active, retired or deferred participants included in our calculations. Benefits provided by annuity purchases cease to be plan obligations.
- f) There are no 5% or greater liabilities, such as legal or accounting fees.
- g) The plan sponsor provided census and asset data as of 12/31/02 and 12/31/03.

Michael Walsh

- b) The economic assumptions used for this valuation are shown in Attachment J; other actuarial assumptions are shown in Attachment K.
- i) We are not aware of any events during the year that might represent settlements or curtailments.
- j) Our relationship with the plan or the plan sponsor does not impair or appear to impair the objectivity of our work.
- k) There were no events that eliminated for a significant number of employees the accrual of benefits for some or all of their future service.

The following Attachments are included in this Report.

Attachment A	-	Reconciliation of Net Periodic Cost
Attachment B	-	Amortization of Transition Amount
Attachment C	-	Projected Benefit and Accumulated Benefit Obligations
Attachment D	-	Asset (Gain) or Loss
Attachment E	-	(Accrued) or Prepaid Pension Expense and Pension Liability
Attachment F	-	Additional Liability and Intangible Asset & Charge to Equity
Attachment G	-	Summary of Prior Service Cost Amortization Schedules
Attachment H	-	Amortization of Gain
Attachment I	-	Reconciliation of Net Gain
Attachment J	-	Assumptions and Data Provided by the Plan Sponsor
Attachment K	-	Other Assumptions Used by the Actuary
Attachment L	-	Reconciliation of Plan Participants
Attachment M	-	Summary of Principal Plan Provisions

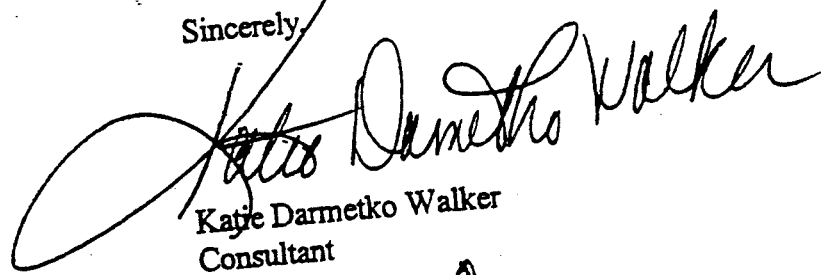
May 20, 2004

5

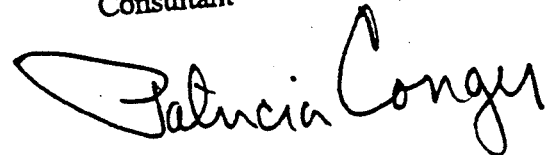
Mr. Michael Walsh

To the best of our knowledge, the information contained in this report was determined in accordance with FASB Statement No. 87 (including the FASB's booklet entitled "A Guide to Implementation of Statement 87 on Employers' Accounting for Pensions: Questions and Answers" and the Actuarial Standards Board's booklet entitled, "An Actuarial Compliance Guideline for Statement of Financial Accounting Standards No. 87"). We do not believe any additional disclosure is required pursuant to FASB Statement No. 132. If you require additional information pursuant to Statement 132, please contact our office.

Sincerely,



Katie Darmetko Walker
Consultant



Patricia Conger
Actuary

KDW/PC/cv
Enclosures

cc: John Morro, CPA

SHORELANDS WATER CO., INC. PENSION PLAN
 FINANCIAL ACCOUNTING STANDARDS BOARD #87

ATTACHMENT A

RECONCILIATION OF NET PERIODIC PENSION COSTS

For the period ending December 31, 2003

1.	SERVICE COST		
	a. Normal Cost at beginning of year	\$ 101,546	
	b. Interest at 7.75% for full year	<u>7,870</u>	\$ 109,416
	c. Total service cost (a) + (b)		
2.	PROJECTED BENEFIT OBLIGATION		
	a. Projected Benefit Obligation	\$ 2,719,500	
	b. Expected distributions, weighted for timing	<u>(24,677)</u>	
	c. Average expected PBO (a) + (b)	\$ 2,694,823	
	d. Discount rate	7.75%	\$ 208,849
	e. Interest cost (c) x (d)		
3.	Amortization of Transition(Asset) (See ATTACHMENT B, Item 5)		\$ (14,624)
4.	Actual Return on Assets (See ATTACHMENT D, Item 5)		\$ 593,608
5.	Amortization of Prior Service Cost (See ATTACHMENT G, Column 2)		\$ 0
6.	Amortization of Loss [See ATTACHMENT H, Item 13]		\$ 17,944
7.	Net Asset Gain (Loss) during the period deferred for later recognition (See ATTACHMENT D, Item 7)		\$ 413,800
8.	Net Periodic Pension Cost (1c)+(2e)+(3)-(4)+(5)+(6)+(7)		<u>\$ 141,777</u>

Bruce S. Edington, Esq.
June 9, 2004
Page 39

RAR-37. Please provide, for each of the past five years: a) the Company's SFAS 87 pension cost; and b) the actual amount of any contributions to the pension fund.

	<u>SFAS 87 Pension Cost</u>	<u>Contributions to Pension Fund</u>
2003	141,777	0
2002	44,798	0
2001	(26,986)	0
2000	(43,841)	0
1999	(45,569)	0

Bruce S. Edington, Esq.
June 9, 2004
Page 44

RAR-42. Please provide, for each of the past three base rate case proceedings: a) the total rate case costs incurred by the Company; and b) the effective date of new rates.

Shorelands past 3 rate case proceedings

	<u>Total Rate Case Costs Incurred</u>	<u>Effective Date of New Rates</u>
1998	102,479	June 10, 1998
1994	*75,000	July 1, 1994
1990	*85,000	July 1, 1990

* Represents amount allowed for recovery in rates.

Bruce S. Edington, Esq.
June 9, 2004
Page 50

RAR-48. Please provide a full and complete copy of the most recent Annual Report to the BPU. (see attached)

ANNUAL REPORT

OF

Shorelands Water Company Inc.
(NAME OF RESPONDENT)

1709 Union Ave., PO Box 158, Hazlet, NJ 07730
(ADDRESS OF RESPONDENT)

TO THE

BOARD OF PUBLIC UTILITIES STATE OF NEW JERSEY

YEAR ENDED DECEMBER 31, 2003

Name, title, and address of Officer or other person to whom any communication should be addressed concerning this report.

Michael P. Walsh, P.E., P.P./President

Shorelands Water Co., Inc. 1709 Union Ave. Hazlet, NJ 07730

DO NOT ROLL OR FOLD

YEAR: 2003

NAME OF UTILITY: SHORELANDS WATER CO., INC.

COMPARATIVE BALANCE SHEET

(Include for use Class A and B)

ASSETS AND OTHER DEBITS

NUMBERS AND TITLES OF ACCOUNTS		SCHED. PAGE NO.	BALANCE END OF YEAR	BALANCE BEGINNING OF YEAR	INCREASE OR (DECREASE)
(a)		(b)	(c)	(d)	(e)
UTILITY PLANT					
101-06	Utility Plant	15	26,907,284	25,961,989	945,295
107	Construction Work In Progress	18	320,612	485,591	(164,979)
111-13	Accum. Prov. For Depreciation (Cr.)	20	(11,282,216)	(10,627,033)	(655,183)
114-16	Accum. Prov. For Amort. Of Ut. Ptl. (Cr.)	-			
117-19	Utility Plant Adjustments	-	15,945,681	15,820,547	125,134
Net Utility Plant					
OTHER PROPERTY AND INVESTMENTS					
121	Nonutility Property	-			
122	Accum. Prov. For Depn. And Amort. of Nonutility Property (Cr.)	22			
123	Investment In Assoc. Companies	22			
124	Other Investments	-			
125	Sinking Funds	-			
126	Depreciation Fund	-			
128	Other Special Funds	-			
Total Other Prop. And Invest.					
CURRENT AND ACCRUED ASSETS					
131	Cash	-	535,760	750,877	(215,117)
132-4	Special Deposits	-			
135	Working Funds	22			
136	Temporary Cash Investments	-			
141	Notes Receivable	-	785,647	802,972	(17,325)
142	Customer Accounts Receivable	-			
143	Other Accounts Receivable	22			
144	Accum. Prov. For Uncollect. Accts. (Cr.)	-			
145	Notes Rec. From Assoc. Companies	-	165,072	184,376	(19,304)
146	Accts. Rec. From Assoc. Companies	-	256,899	231,446	25,453
151-163	Materials And Supplies	23			
165	Prepayments	-			
171	Interest And Dividends Receivable	-			
172	Rents Receivable	-			
173	Accrued Utility Revenue	23			
174	Misc. Current And Accrued Assets	-	1,743,378	1,969,670	(226,292)
Total Current And Accrued Assets					
DEFERRED DEBITS					
181	Unamort. Debt Disc. And Expense	24	58,013	63,269	(5,256)
182	Extraordinary Property Losses	25	0	0	0
183-186	Other Deferred Debits	25	58,013	63,269	(5,256)
Total Deferred Debits					
Total Assets And Other Debits			17,747,072	17,853,486	(106,414)

**COMPARATIVE BALANCE SHEET
LIABILITIES AND OTHER CREDITS**

NUMBERS AND TITLES OF ACCOUNTS (a)	SCHED. PAGE NO. (b)	BALANCE END OF YEAR (c)	BALANCE BEGINNING OF YEAR (d)	INCREASE OR (DECREASE) (e)
PROPRIETARY CAPITAL				
201-3 Common Capital Stock	26	1,075,200	1,070,200	5,000
204-6 Preferred Capital Stock	27	172,531	165,561	6,970
207-11 Other Paid-in Capital	-			
212 Installments Rec. On Cap. Stock	-			
214 Capital Stock Expense (Dr.)	28	3,925,840	3,888,643	37,197
215 Appropriated Earned Surplus	28			
216 Unappropriated Earned Surplus	26			
217 Reacquired Capital Stock (Dr.)	-	5,173,571	5,124,404	49,167
Total Proprietary Capital				
LONG-TERM DEBT				
221-22 Bonds	29	3,400,000	3,500,000	(100,000)
223 Advances From Assoc. Companies	29			
224 Other Long Term Debt	-	3,400,000	3,500,000	(100,000)
Total Long-Term Debt				
CURRENT AND ACCRUED LIABILITIES				
231 Notes Payable	30	368,981	419,920	(50,939)
232 Accounts Payable	30			
233 Notes Payable To Assoc. Companies	-			
234 Accts. Payable To Assoc. Companies	-	101,178	98,558	2,620
235 Customer Deposits	31	1,158,274	1,126,696	31,578
236 Taxes Accrued	-	147,269	152,008	(4,739)
237 Interest Accrued	-			
238 Dividends Declared	-			
239 Matured Long Term Debt	-			
240 Matured Interest	-			
241 Tax Collections Payable	32	489,812	392,123	97,689
242 Misc. Cur. And Accrued Liabilities	-	2,265,515	2,189,305	76,210
Total Current And Accrued Liabilities				
DEFERRED CREDITS				
251 Unamortized Premium On Debt	24	950,139	1,163,261	(213,122)
252 Customer Advances For Construction	32	867,122	785,792	81,330
253 Other Deferred Credits	-	1,817,261	1,949,053	(131,792)
Total Deferred Credits				
OPERATING RESERVES				
261 Property Insurance Reserve	33			
262 Injuries And Damages Reserve	33			
263 Pensions And Benefits Reserve	33			
265 Miscellaneous Operating Reserves	-			
Total Operating Reserves		5,090,725	5,090,725	0
CONTRIBUTIONS IN AID OF CONSTRUCTION				
271				
Total Liab. And Other Credits		17,747,072	17,853,486	(106,414)

YEAR: 2003

NAME OF UTILITY: SHORELANDS WATER CO., INC.

MISCELLANEOUS CURRENT AND ACCRUED LIABILITIES

- 1. Report amount and description of other current and accrued liabilities at end of year.
- 2. Minor items may be grouped under appropriate titles.

LINE NO.	ITEM (a)	BALANCE END OF YEAR (b)
1	Accrued Payroll	18,020
2	Accrued Vacation	78,417
3	Accrued Pension Funding	110,115
4	Accrued Legal	10,824
5	Accrued Other	20,292
6	Accrued Tank Painting	68,081
7	Accrued Tank Painting	111,527
8	Accrued Purchased Water	12,708
9	Accrued Sludge Removal	16,505
10	Accrued Manasquan User's Group	43,323
11	Unearned Revenue	
12		
13		
14		
16		
18	TOTAL	489,812

OTHER DEFERRED CREDITS

- 1. Report information called for concerning other Deferred Credits.
- 2. Minor items may be grouped by classes.

LINE NO.	DESCRIPTION (a)	BALANCE BEGINNING OF YEAR (b)	DEBITS		CREDITS (e)	BALANCE END OF YEAR (f)
			ACCOUNT CREDITED (c)	AMOUNT (d)		
1	Accrued Deferred Investment					182,533
2	Tax Credit	194,533	253.1	12,000		525,382
3	Deferred Taxes	525,382	253.2			
4						
5						
6						
7						
8						
9						
10						
11						
12						
13						
14						
15				12,000		707,915
16	Total	719,915				

RAR-49. Please identify all capital projects anticipated to be completed between January 1, 2004 and December 31, 2005. For each project, please provide: a) a description of the project; b) the estimated cost; c) the actual cost incurred to date; d) the projected (or actual) start date; and e) the projected (or actual) in-service date.

2004 Capital Budget

Start Date	Projected In-Service Date	Estimated Cost	Actual Incurred To Date 6/04	<u>2004 Capital Budget - Field Services</u>		Project Number
Sept	Nov	\$10,000	\$0	Geographic Information System / Hyd Model Software		1
Feb	Jun	\$10,000	\$9,575	T&D and Meter Shop Computer Equipment		2
Jan	Mar	\$20,000	\$20,000	MXU Installations along Route 35 and 36		3
Sept	Oct	\$25,000	\$0	6" Main - Franklin and Compton		4
Oct	Nov	\$26,000	\$0	6" Main - Sidney and Woody		5
Sept	Sept	\$10,000	\$0	Field Services Locker Room		6
Mar	Mar	\$5,300	\$5,780	Meter Shop Floor		7
Mar	Mar	\$10,000	\$9,500	Valve Excersizing Equipment		8
Nov	Nov	\$1,000	\$0	Sensus Autogun		9
Sept	Sept	\$5,000	\$0	Paving under Pipe Fittings		10
Aug	Aug	\$3,500	\$0	3" Mud Pump		11
		\$4,500	\$4,700	Misc		12
		<u>\$130,300</u>	<u>\$49,555</u>			

Date of Completion	Projected In-Service Date	Estimated Cost	Actual Incurred To Date 6/04	<u>2004 Capital Budget - Production</u>		Project Number
June	June	\$128,500	\$135,292	Plant 2 - 600kw Generator		1
Mar	Apr	\$48,000	\$50,570	Well # 3 - Column Pipe and Pump		2
May	Jun	\$6,000	\$4,948	Replace Plant#2 and Joe P Computer		3
April	April	\$4,000	\$2,997	(4) Faciliworks V6 License		4
Mar	Mar	\$4,300	\$4,300	Concrete Lagoons Plant# 2		5
May	June	\$6,334	\$4,250	Plant 2 - Mezzanine		6
Mar	April	\$9,000	\$8,700	Fiberglass Stop Planks Plant #2 Lagoon		7
Feb	Mar	\$12,835	\$12,835	SCADA Upgrade and Graphics		8
		\$0	\$0	Misc		9
		<u>\$218,969</u>	<u>\$223,892</u>			

\$349,269 Total 2004 Capital Budget

RAR-49 (Continued)

Please identify all capital projects anticipated to be completed between January 1, 2004 and December 31, 2005. For each project, please provide: a) a description of the project; b) the estimated cost; c) the actual cost incurred to date; d) the projected (or actual) start date; and e) the projected (or actual) in-service date.

2005 Capital Budget

6/23/2004

Start Date	Projected In-Service Date	Estimated Cost	<u>2005 Capital Budget - Field Services</u>	<u>Project Number</u>
Feb	Jul	\$30,000	GIS / Hyd Model Software & Consultant	1
Jan	Mar	\$10,000	T&D and Meter Shop Computer Equipment	2
Jul	Jul	\$25,000	VXU Software and Laptop	3
Jun	Aug	\$30,000	6" Main - Thorne, Olive, Trumen and Byrne	4
Aug	Aug	\$125,000	Front End Loader	5
Sept	Sept	\$75,000	Replace Dump Truck #4	6
April	April	\$5,000	Fiber Optic Network Cable between Buildings	7
<u>\$300,000</u>				

Start Date	Projected In-Service Date	Estimated Cost	<u>2005 Capital Budget - Plants</u>	<u>Project Number</u>
May 04	May	\$6,300,000	Reconstruction of Plant 1	1
March	April	\$200,000	Roof Structure over Plant 1 Lagoons	2
May	May	\$140,000	Plant 1 - 600kw Generator	3
Jan	Mar	\$36,000	Water Quality Monitoring for NJA Chambers 1 & 2	4
Feb	Mar	\$35,000	HS Station Relocation of Plant# 1 Generator	5
Jul	Jul	\$15,000	Plant#2 Fence around Plant	6
Mar	May	\$35,000	Plant# 2 TV Monitoring Equipment	7
Mar	Mar	\$5,500	Plant# 2 Influent Meter	8
Mar	Mar	\$6,000	Well# 3 Level Monitor	9
Feb	Feb	\$7,500	Plant# 2 Electric Gate	10
May	Oct	\$10,000	Plant # 1 & 2 IT Replacement	11
Mar	Mar	\$10,350	Plant #2 Lagoon 1 Concrete	12
<u>\$6,800,350</u>				

\$7,100,350 Total 2005 Capital Budget

Note: None of the above projects have incurred actual capital costs to date

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RAR-51. Please quantify all expense increases/decreases anticipated as a result of the new treatment plant.

	<u>Existing Plant #1</u>	<u>New Plant #1</u>	<u>Inc. / (Dec.)</u>
Labor Costs - Unchanged			
Power Costs	56,000	87,500	31,500
Chemical Costs	41,800	88,400	46,600
Sludge Disposal	2,568	3,348	780
Change in Operation expenses			78,880

See also RAR's 27 & 28 regarding the increased operating costs for the new plant #1.

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RAR-56. Regarding page 19 of Exhibit 2, please identify how much of the "Interest and Other Charges" in the amount of \$484,756 is interest and how much is other charges, and identify all other charges.

Interest and Other Charges - Proforma Rate Year

427	Interest on Long Term Debt	469,500
428	Amortization Debt Discounts	5,256
431	Other Interest Expense	<u>10,000</u>
		484,756

RAR-59. Regarding the response to SRR-13, is the Company proposing to implement its proposed increase in two phases? If so, please explain fully which part of the increase would be implemented in Phase II.

Michael P. Walsh, President

Yes. Based upon the comments at the pre-filing conference held at Newark, it is the understanding of the Company that the proposed increase would be implemented in two phases. Phase II would include the Operating Expenses associated with the new Plant (i.e. electric, chemical, sludge, etc.), the final Construction cost, the final Cost of Debt and any Capitalized Interest accumulated when the Plant was placed in service, as well as the value of the Capital Improvements for the Lagoon Roof Structure which is an associated project, however, not included in the Northeast Remsco contract. It is further anticipated that the wage and salary increases effective April 1, 2005 would be included in Phase II.