BEFORE THE

ARKANSAS PUBLIC SERVICE COMMISSION

IN THE MATTER OF THE
UNBUNDLING OF THE RATES OF
NORTH ARKANSAS ELECTRIC
COOPERATIVE CORPORATION

DOCKET NO. 99-260-U

PREPARED TESTIMONY

OF

DON MALONE
PUBLIC UTILITY AUDITOR

ON BEHALF OF THE STAFF OF THE

ARKANSAS PUBLIC SERVICE COMMISSION

AUGUST 08, 2000
1. Q. Please state your name and business address.

2. A. My name is Don Malone. My business address is P.O. Box 400, Little Rock, Arkansas 72203.

3. Q. By whom are you employed and what is your position?

4. A. I am employed by the Arkansas Public Service Commission as a staff public utility auditor.

TRAINING AND EXPERIENCE

5. Q. Please describe your educational background and professional experience.

6. A. I am a graduate of Arkansas State University with Bachelor of Science degrees in accounting and finance. I am a Certified Public Accountant licensed to practice in the State of Arkansas. To maintain my license I complete forty hours of continuing professional education annually of audit, tax, general accounting, and computer technology course work. Prior to joining the staff I held corporate, controller, cost analyst, and staff positions in manufacturing, cellular phone service, and public accounting companies.

PURPOSE OF TESTIMONY

7. Q. What is the purpose of your testimony in this docket?

8. A. I am presenting testimony in support of the operating expense adjustments made by Staff in this docket. These adjustments are shown in Staff Exhibit JH-5.
SUMMARY OF ADJUSTMENTS TO OPERATING EXPENSES

Q. Please explain the pro forma adjustments to wages and salaries expense.

A. The functionalized adjustments to the test year payroll expenses are shown in Exhibit JH-5, numbers IS-3(A), IS-4(A), IS-5(A), IS-6(A), IS-7(A), and IS-8(A). The total of these adjustments increased payroll expense by $171,228.

Payroll expense consists of wages, salaries, and bonuses paid to full and part time employees of the Company. Payroll expense was projected based on the employees' pro forma hourly wage rate or salary, annualized straight time hours, and a four year average of overtime earnings. The difference between actual test year 1998 payroll expense and the pro forma payroll expense equals the total payroll expense adjustment. Test year 1998 payroll expense distribution percentages by account were used to distribute the pro forma payroll expense adjustment to the functional classes and capital accounts.

Q. Did Staff use the same methods as the Company in calculating pro forma payroll expense?

A. Staff’s methodology differed from the Company’s payroll calculation in that Staff based the pro forma payroll on the 1999 straight time work hours per employee as opposed to the 1998 actual hours worked and a four year average was used to calculate overtime requirements as opposed to 1998 actual overtime hours. Staff and the Company used the same number of pro forma year employees and used the
same pay rates and salaries in the calculations of pro forma payroll expense.

2. Q. Please explain the adjustments to payroll tax expense.

3. A. The adjustments to payroll tax expenses are shown in Exhibit JH-5 numbers IS-3(C), IS-4(C), IS-5(C), IS-6(C), IS-7(C), and IS-8(C). The total adjustment amount is an increase of $22,476 to payroll tax expense. Payroll tax expense consists of FICA, medicare, federal unemployment insurance, and state unemployment insurance taxes levied upon the wages paid to employees of the Company. Payroll tax expense was calculated based on total pro forma payroll expense adjusted for the FICA wage base, FUTA wage base, and SUTA wage base before applying the appropriate payroll tax rates. The difference between actual test year 1998 payroll tax expense and the pro forma payroll tax expense equals the total payroll tax expense adjustment. Test year 1998 payroll expense distribution percentages by account were used to distribute the pro forma payroll tax expense adjustment to the functional classes and capital accounts.

4. Q. Please explain the adjustments to employee benefits expense.

5. A. The adjustments to employee benefits are shown in Exhibit JH-5 numbers IS-3(B), IS-4(B), IS-5(B), IS-6(B), IS-7(B), and IS-8(B). The total adjustment amount is an increase of $174,599 to expense. Employee benefits offered by the Company include medical insurance, long-term disability insurance, accidental death and dismemberment insurance, 401-(k) savings plan,
1. and a non-contributory retirement plan. Directors and attorneys of the Company
2. are offered medical insurance, life, AD&D, and accident insurance. The Company
3. provides the aforementioned benefits at zero cost to the employees, directors, and
4. attorney.
5. 401-(k) Savings Plan: The plan requires a Company contribution of 1% of the
6. employees base wages or salary for all employees with one year or more of
7. full time employment. The plan does not require the Company to match employee
8. contributions to the 401-(k) savings plan. A December 1999 employee participation
9. listing was used to calculate, by employee, the pro forma 401(k) savings plan
10. expense. The adjustment for the 401-(k) saving plan is an increase of $978 to
11. expense.
12. NRECA Retirement Pension Plan: The non-contributory retirement plan is fully
13. funded and has not required a full years contribution for the last five years. The
14. pro forma year actual contributions to the plan were used to calculate the retirement
15. plan expense. The actual pro forma year contributions to the plan ranged from
16. 9.7% to 12.9% of base wages or salaries and averaged 10.75% of the base amount
17. for the pro forma year. The average contribution rate of 10.75% was used to
18. calculate the pro forma retirement plan expense. The adjustment resulted in an
19. increase of $36,194 to expense. Staff’s methods differed from the Company’s in
20. that the Company used a 12.73% contribution rate which was the equivalent of
North Arkansas Electric Cooperative Corporation  
Docket No. 99-2604-U  
Prepared Testimony of Don Malone  

1. a full years 100% contribution level for the pro forma year adjustment.

2. **Group Insurance:** The Company provides each full time employee, director, and attorney medical, dental, & life insurance and provides each employee with long & short term disability insurance. A December 1999 group insurance vendor invoice was used to calculate, by employee, the total pro forma year group insurance benefits costs. The pro forma year group insurance benefit adjustment resulted in an increase of $137,427 to expenses.

3. The pro forma year employee benefits adjustments were distributed to the functional classes and capital accounts based on the test year 1998 payroll expense distribution.

4. **Q. Explain Staff's adjustments regarding property and liability insurance expense.**

5. A. Staff adjustments for property and liability insurance are based on the difference between test year 1998 and actual 1999 insurance premiums costs. Workers compensation insurance premiums decreased $5,960, the Electro Magnetic insurance premiums decreased $2,058, and the All Risk Blanket insurance premiums increased 6,464 for the pro forma year. The adjustments resulted in an increase of $1,336 to expenses as shown in Exhibit JH-5, numbers IS-3(E), IS-4(E), IS-5(E), IS-6(E), IS-7(E), and IS-8(E).

6. **Q. Did Staff make any adjustments with regard to regulatory expenses?**

7. A. Yes. The annual utility regulatory assessment adjustment proposed by the
1. Company was the difference between the amounts paid in the 1998 test year and the pro forma year. Adjustment number IS-8(H) increases the utility regulatory assessment $25,609 for the pro forma year.

4. **Q. Please explain the adjustment to post-retirement benefits (FAS 106) accrual.**

5. A. Adjustment numbers IS-3(D), IS-4(D), IS-5(D), IS-6(D), IS-7(D) and IS-8(D) are associated with the Company's accounting for post-retirement benefits other than pensions in accordance with the Statement of Financial Accounting Standards No. 106 (FAS 106). Briefly, the statement requires Companies to record a liability to recognize the future cost of insurance benefits offered to employees after they retire.

6. The amount of the liability is actuarially determined and is accrued annually by a Company. FAS 106 does not require a Company to fund the accrued cost of benefits and, accordingly, NAEC has not funded the obligation. However, in order to include those expenses in rates the Commission's Order No. 2 of Docket No. 92-265-U requires that a Company either externally fund the obligation or submit a proposed funding plan for Commission review and approval prior to including FAS 106 costs in rates. NAEC has not submitted such a plan and does not intend to externally fund the obligation. Therefore, Staff has excluded the $212,996 FAS 106 expense accrual for the pro forma year.

7. **Q. Please explain the adjustments concerning advertising, dues, donations, and certain other expenditures.**
1. A. Staff adjustment number IS-8(G), in the amount of $88,123, was made to remove dues, donations, certain other expenditures and Rural Arkansas Magazine from the pro forma year. The primary portion of this adjustment is attributable to Rural Arkansas Magazine in the amount of $68,591. Staff adjustment number IS-8(F), in the amount $32,849, was made to remove image, promotional, and political advertising that were identified during the audit process. Other expenditures consisted of payments to civic clubs, certain meals, chamber of commerce dues, and tickets to community functions.

9. **Q. Please explain the rate case expense adjustment.**

10. A. Adjustment number IS-8(I) increased pro forma year expenses $12,000 for the costs associated with preparing the Cost of Service Study and Unbundling Analysis. The total estimated cost of this study is $48,000. The Company proposed a four year cost amortization of $12,000 annually. Staff agrees with the amortization period and adjustment amount proposed by the Company.

15. **Q. Does this conclude your testimony at this time?**

16. A. Yes.
CERTIFICATE OF SERVICE

I, Jan Sanders, hereby certify that a copy of the foregoing Testimony has been served on all parties of record by forwarding the same by first-class mail, postage prepaid, this 8th day of August, 2000.

[Signature]
Jan Sanders
Secretary of the Commission