

Service Date: April 26, 1988

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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| IN THE MATTER of The Application of) | |
| MIDVALE WATER COMPANY for Authority) | UTILITY DIVISION |
| to Increase Rates and Charges for) | DOCKET NO. 87.5.24 |
| Water Service in its Eureka, Montana) | ORDER NO. 5292b |
| Service Area.) | |
| _____) | |

APPEARANCES

FOR THE APPLICANT:

Marshall Myers, Attorney at Law, P.O. Box 1287, Eureka,
Montana 59917.

FOR THE INTERVENORS:

Mary Wright, Staff Attorney, Montana Consumer Counsel, 34
West Sixth Avenue, Helena, Montana 59620.

FOR THE COMMISSION:

Geralyn Driscoll, Staff Attorney, 2701 Prospect Avenue,
Helena, Montana 59601.

Ronald Woods, Rate Analyst, 2701 Prospect Avenue, Helena,
Montana 59620.

BEFORE:

Howard Ellis, Commissioner and Hearing Examiner

BACKGROUND

1. On May 22, 1987, Midvale Water Company (Applicant or MWC) filed an application with this Commission for authority to increase water rates and charges for its Eureka, Montana customers on a permanent basis by approximately 99.0%. This constitutes a revenue increase of approximately \$12,360.

2. On August 5, 1987, following a notice of public hearing, a hearing was held in the County Annex Building, Eureka, Montana. For the convenience of the consuming public there was also a night session, held in the Lincoln Electric Coop, Meeting Room, Eureka, Montana. The public hearing was to consider the merits of the Applicant's proposed water rate increase. At the close of the public hearing, all parties stipulated to a final order in this docket.

3. At the close of the public hearing the Applicant made a motion for interim rate relief. The Applicant's motion did not specify an amount of interim rate relief.

4. On September 9, 1987, the Commission having considered the merits of the Applicant's interim request, issued Order No. 5292 authorizing the Applicant interim rate relief. Order No. 5292 authorized the Applicant to obtain \$15,000, for construction funding and payment of engineering fees, from loan proceeds administered by the Montana Department of Natural Resources and Conservation (DNRC).

5. On October 21, 1987, this Commission received a letter from O. C. Thatcher, principal owner of Midvale Water, requesting authorization to obtain an additional \$8,000 in construction funds from DNRC. Giving the Applicant authority to obtain additional construction funds would require the Commission to grant of additional interim rate relief to service the increased debt obligation.

6. On November 10, 1987, the Commission, after reviewing the information submitted in support of the Applicant's request for additional construction funding, issued Order No. 5292a. Order No. 5292a authorized the Applicant to borrow an additional \$8,000 in construction funding, bringing total authorized construction funding to \$23,000.

FINDINGS OF FACT

7. At the public hearing the Applicant presented the testimony and exhibits of Marshall Myers, partner in MWC, in support of its proposed water rate increase. The Montana Consumer Counsel presented the testimony of seventeen public witnesses.

8. It is the Commission's policy to evaluate the need for increased rates to private utilities through an analysis of rate base, operating revenues and expenses, depreciation, taxes, capital structure and rate of return. This policy, developed over many years applies to all privately-owned public utilities under its jurisdiction.

9. MWC is a privately-owned public utility, but the Applicant has requested that the Commission evaluate the need for increased rates on a cost basis, similar to the treatment afforded municipal utilities. Specifically, the Applicant has requested that the

Commission treat principal and interest payments on the proposed DNRC loan as an operating revenue deduction and grant sufficient revenues to cover this cost as an "above the line" item.

10. The Applicant's request for a deviation from general ratemaking principles stems, in part, from the fact that it has received approval from DNRC's, Water Development Program for a loan to construct needed capital improvements to its system. One of the DNRC loan requirements is that MWC have rates sufficient to service the debt costs associated with the loan.

The Applicant's analysis of traditional ratemaking principles indicated that, given its rate base, it would not generate sufficient net operating income to meet the principal and interest payments on this debt obligation, as required by DNRC. The fact that traditional ratemaking principles would not allow the Applicant to generate sufficient net operating income to cover the DNRC debt cost coupled with the terms of a Consent Decree (further discussion of the Decree will appear later in this order), in the Applicant's view, warrants deviation from general principles.

11. The Commission, in this instance, agrees with the Applicant that a deviation from general ratemaking principles is warranted. The Applicant is cautioned, however, that if at a future date a sale and transfer of the assets and operating responsibility occurs, all assets acquired from the loan proceeds found reasonable in this order should be excluded from consideration in negotiating an equitable sales figure. The Commission includes this caution because the ratepayer rather than the equity investor is assuming direct responsibility for repayment of the debt obligation and because testimony from consumers

indicated there was public interest in the Town of Eureka, or a water association, acquiring the system.

CAPITAL IMPROVEMENT PROGRAM

12. On January 23, 1987, the State Department of Health and Environmental Science (DHES) filed a complaint in state district court seeking an order that Midvale Water Service bring its water system up to the standards set by that Department. Under the terms of a Consent Decree, Midvale Water Company must bring its entire system up to the standards detailed in the Ten States Water Compact by July 1, 1988.

13. In response to the Consent Decree, MWC commissioned an engineering firm to undertake a system evaluation to determine what system improvements were necessary to bring the utility into compliance with the standards set forth in the Consent Decree. The engineering study determined that MWC needed to make improvements to its water system costing \$82,214.75 to bring the system into compliance with the "Ten State Standard."

The system improvements outlined in the study include:

1. Construction of improvements to the distribution system; that would include looping and installation of gate valves.
2. Upgrade of reservoir booster pump station (serving upper Midvale system) and reservoir.
3. Upgrade pumphouse for Well #4.
4. Installation of new tank level control system.
5. Conversion of Wells #1 and #2 to standby operation. Pump start shall be on falling pressure resulting from drop in reservoir level.

14. The Applicant's witness testified that these improvements satisfied the Consent Decree provision requiring the utility facilities to comply with the "Ten States Standard." The statement is supported by the fact that the DHES has approved the plans and specifications.

15. The Consent Decree obligates the Midvale Water Company to improve its water utility facilities. This Commission does not have the authority to supersede the conditions and requirements imposed on MWC in that order. Therefore, the Commission's role in examining the need for proposed capital improvements in this docket is limited to assuring that the improvements comply with the requirements contained in the court order. Since the district court action against MWC was brought by the DHES, the Commission's assurance that the requirements of the court order are met is provided by the fact that the DHES approved MWC's plans and specifications. The Commission based upon the testimony in this Docket finds the proposed capital improvement program and estimated construction costs outlined by MWC to be reasonable and prudent.

DEBT SERVICE

16. MWC proposes to finance the capital improvement program outlined in the preceding Findings of Fact through a loan from DNRC. MWC applied to DNRC's, Water Development Bureau, pursuant to 85-1-608, MCA, for a loan of approximately \$95,500 to finance the system improvements required by the DHES. The loan amount exceeds the construction costs because it includes interim financing charges and an additional 10% contingency fee for unexpected costs (the additional 10% is a DNRC loan requirement).

17. DNRC has approved MWC's loan application for \$95,524. The loan will be repaid over a 15 year period and carry an interest rate of 7.33%. The annual principal and interest payment, as calculated by the Applicant, is \$11,626.80.

18. DNRC has approved loans for municipal water utilities in the past, but this loan represents the first loan to a private water utility. DNRC imposed a condition on the Applicant that it also imposes on municipal water utilities -- the utility's rates must be sufficient to service the principal and interest payments of the loan.

19. The loan approved by DNRC for construction of the required capital improvements represents a least cost alternative for the

Applicant, and ratepayer, when compared to the cost of capital associated with either equity capital or commercial financing. The Commission finds the financing proposal outlined by the Applicant, executing a loan with DNRC in the amount of \$95,524 to be repaid over 15 years, and carrying an interest rate of 7.33%, to be reasonable.

OPERATION AND MAINTENANCE EXPENSE

20. In its application MWC proposed operation and maintenance expenses totalling \$13,234. The proposed operation and maintenance expenses were not challenged by any party participating in this proceeding and are accepted by the Commission.

REVENUE NEED

21. MWC testified that, under present rates, user charges would generate approximately \$12,500 in annual revenues. The test period revenues are not a contested issue in this case and are accepted by the Commission.

22. The Commission, based upon Findings of Fact contained herein, finds that the Applicant should be allowed to increase annual revenues by \$12,360. This requirement is calculated as follows:

| | |
|--------------------|----------|
| Operating Revenues | \$12,500 |
|--------------------|----------|

| | |
|---------------------------|---------------|
| Less: | |
| Operating Expenses | \$13,234 |
| Debt Service | <u>11,626</u> |
| Total Revenue Requirement | \$24,860 |
| REVENUE DEFICIENCY | \$12,360 |

RATE DESIGN

23. The Applicant testified that the proposed rate structure is designed to generate total annual revenues of \$24,860 and represents an annual revenue increase totalling \$12,360. In its application, the Applicant proposes to perpetuate an unmetered rate structure (monthly flat rate) for all customer classifications. The Applicant's rate proposal also, seeks Commission approval of a metered rate structure to be implemented, at some future date, if metering of the system occurs.

24. During cross-examination of the Applicant's witness the Commission developed concerns relative to the amount of revenue that would be generated if the proposed "metered rates" were implemented. The Applicant's proposed metered rate structure proposes assessment of a minimum monthly charge equal to the monthly flat rate assessment and allows 5,000 gallons of consumption in the minimum block. Consumption in excess of the minimum monthly allowance would be assessed at the rate of \$2.00 per

thousand for the next 5,000 gallons and all consumption in excess of 10,000 gallons would be charged at the rate of \$1.00 per thousand.

25. The Applicant, in constructing the metered rate to generate the revenue requirement recognized in this order, has assumed that the average residential connection would consume 5,000 gallons per month and that minimal consumption would occur in the two block declining commodity charge. The Commission, given its general knowledge and expertise in the area of water consumption patterns of residential consumers, believes these assumptions are wrong. In general the Commission has found that the average residential consumer uses approximately 8 to 10 thousand gallons of water during nonirrigating months and substantially more than that amount during irrigating months (average consumption during irrigating months depends on lot size). Since the Commission's general knowledge in the area of residential consumption patterns does not coincide with the Applicant's assumptions, no substantive supporting data is available, and metering does not currently exist, the Commission feels strongly that metered rates should not be approved in this application. In the Commission's opinion, if

approved, the proposed metered rates would generate significantly more revenue than calculated by the Applicant and exceed the revenue requirement recognized in this order.

26. At the present time MWC has no connections on its system that are metered. If MWC is serious about implementing a metered rate structure it should meter several representative connections and maintain consumption information for a minimum of one (1) year. After the consumption information for the representative connections has been gathered an appropriate metered rate could be determined.

27. The Applicant in its proposed flat rate water schedule attempted to recognize cost differentials associated with provision of service to various locations within its service area and to introduce some equity in its sprinkling rate. However, the some rate structure modifications proposed by the Applicant are not supported by the record.

28. During his presentation Mr. Myers indicated that MWC had three (3) pressure zones within its service area. Because three pressure zones exist on the system (Midvale area, Eureka Heights and the Hruby property) the Applicant proposed three different

monthly flat rates. In the opinion of Applicant the proposed rates fairly reflect the cost differential in providing service to the different zones. The Commission, based upon the evidence, was concerned that the rate differential proposed by the Applicant for the Hruby property was not fully supported by the record. The issue is moot, however, because on March 13, 1988, the Commission was informed that the Hruby property had requested disconnection from the system, and had alternative service available (presumably a well).

29. Under its present rate schedule MWC assesses its sprinkling customers a monthly charge of \$5.00 per month, for a four month period, to recover its cost of providing sprinkling water.

In the rate application, under consideration by the Commission, the Applicant is proposing to modify its method of assessing sprinkling charges. The Applicant proposes to convert to an annual sprinkling assessment that would be calculated by applying a usage rate to the square footage of irrigable area.

The proposed method of assessing irrigation charges would be more equitable than the present method employed by the Applicant, which assumes that all consumers have the same irrigation

requirements. Assessment of the charge based on square footage of irrigable area would recognize the fact that in general, the larger the irrigable area the higher the demand for irrigation water.

30. The Applicant has calculated that the charge per hundred square feet of irrigable area should be \$1.25 per season. In calculating this charge the Applicant assumed that the average consumer in the MWC service area irrigated 3,000 square feet. The testimony in this docket indicates that the average lot size in the service area of the Applicant is 1/3 of an acre which is equal to 14,520 square feet. This average lot size indicates to the Commission that the average sprinkling consumer would have substantially more irrigable area than 3,000 square feet. The Commission requested that the Applicant file a late-filed exhibit providing the Commission with the actual square footage of irrigable area so that an accurate irrigation charge could be calculated. The Applicant as of the date of this order has not provide the Commission that information. The Commission has no alternative, at this time, but to deny the Applicant's request to modify its method of assessing irrigation charges. If, however, the Applicant, prior to Commission approval of rates, files

sufficient information to calculate the appropriate irrigation charge the Commission will approve the proposed modification.

31. The Applicant in its filing indicated that it wished to generate \$1,300 annually from proposed irrigation charges. Under present rates the Applicant's irrigation charge generates \$800 annually. Since the Commission has found the Applicant's proposed revenue requirement to be reasonable it must authorize an increase in irrigation charges. The Commission finds, unless the requirements of the preceding Finding of Fact are satisfied, that the Applicant should increase its monthly sprinkling charge from its current level of \$5.00/per month to \$8.15/per month, for the four month period.

32. The Commission finds the rate structure as modified in this order to be reasonable. The Commission further finds, with the exception of the modifications contained herein, that the rate structure contained in the application should be approved.

RULES

33. The Applicant proposed the implementation of seven (7) special rules of service. The proposed rules were reviewed by the MCC and the Commission staff to determine if they were in conflict

with this Commission's "General Rules for Privately Owned Water Utilities." The examination did not reveal any conflict, therefore, the Commission finds the rules should be approved.

CONCLUSIONS OF LAW

1. The Applicant, Midvale Water Company, is a public utility as defined in Section 69-3-101, MCA. The Montana Public Service Commission properly exercises jurisdiction over the Applicant's rates and service pursuant to Section 69-3-102, MCA.

2. The Commission has provided adequate public notice and an opportunity to be heard as required by Section 69-3-303, MCA, and Title 2, Chapter 4, MCA.

3. The rates and rate structure approved in this order are just and reasonable. Sections 69-3-201, and 69-3-330, MCA.

ORDER

NOW THEREFORE, IT IS ORDERED THAT:

1. Midvale Water Company shall file rate schedules which reflect an increase in annual revenues of \$12,360 for its Eureka, Montana service area. The increased revenues shall be generated by increasing rates and charges as provided herein.

2. The rates approved herein shall become effective upon Commission approval, which will occur once the Applicant has provided the Commission with signed copies of the loan agreement between itself and the Department of Natural Resources and Conservation.

3. The Applicant is authorized to implement rules as provided herein.

DONE IN OPEN SESSION at Helena, Montana this 25th day of April, 1988, by a 5 - 0 vote.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

CLYDE JARVIS, Chairman

HOWARD L. ELLIS, Commissioner

TOM MONAHAN, Commissioner

DANNY OBERG, Commissioner

JOHN B. DRISCOLL, Commissioner

ATTEST:

Ann Purcell
Commission Secretary

(SEAL)

NOTE: Any interested party may request that the Commission reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.