

Service Date: July 27, 1988

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

IN THE MATTER OF the Application) UTILITY DIVISION
of the BUTTE WATER COMPANY for)
Authority to Increase Rates and) DOCKET NO. 88.6.14
Charges for Water Services to its)
Butte, Montana Customers.) ORDER NO. 5349

INTERIM ORDER

BACKGROUND

1. On June 7, 1988, Butte Water Company (hereinafter BWC or Company) applied for a rate increase with the Montana Public Service Commission (hereinafter PSC or Commission). BWC seeks pre-approval of its proposal to lease the Silver Lake transmission system from Dennis Washington. Dennis Washington is the sole shareholder of BWC and the owner of the Silver Lake transmission system.

2. The proposed rate increase is \$1,560,000 -- approximately \$600,000 in standard rate making proposals and \$960,000 from leasing the Silver Lake transmission system. The lease terms include payment by BWC of an annual rental of \$854,839 plus 11/18th of the Silver Lake system's operating and maintenance expenses and property taxes. The lease also includes an option to purchase the property for \$6,905,000.

3. BWC proposes that the \$960,000 rate increase be approved by the Commission, but not charged to customers until the Silver Lake system is incorporated into the water system.

BWC's shareholder is willing to commit to using the lease payments as a source of funds for investing additional money in the Company's distribution system. As part of the lease plan Dennis Washington would seek to be exempt from utility status under 69-3-111, MCA.

4. After receiving the filing the Commission directed staff to send data requests for additional information on some matters contained in the filing. The requests were sent June 17, 1988 and responses were received July 1, 1988.

5. Under 38.5.184 Administrative Rules of Montana (hereinafter ARM) the Commission has 30 days from the date a rate application is filed to notify a utility that its application does not comply with Commission rules. At a work session held July 6, 1988, the PSC determined that BWC's rate application as filed does not comply with Montana statutes and cannot be considered by the Commission. The Commission issued a Notice of Commission Action informing BWC of the decision and stating what it could do to preserve the filing. The Notice of Commission action is attached.

6. At the request of BWC, the Commission is issuing this order stating the bases for its conclusion that it does not have the authority to approve BWC's rate application as filed.

FINDINGS OF FACT

7. Currently BWC has three systems of water supply: Big Hole River, Basin Creek and Moulton Reservoir. The combined system contains more than 111 miles of transmission lines. Four of the Company's transmission lines are wooden and BWC reports numerous leaks. (Workpaper 38.5.179, Statement N,

Rate application). The Silver Lake transmission system's water source is in the upper tributaries of Warm Springs Creek. Storm and Silver Lake water is diverted to a pipeline west of Anaconda. The water is transported to the Butte concentrator through a 34" steel pipe with the capacity of 18 million gallons per day. To include this in the BWC's system, a metered connection would be built and BWC would draw 11 million gallons per day. (Page 10 of Jim Chelini's prefiled testimony.)

8. BWC's application for a rate increase uses a historical test year ending December 31, 1987. (Page 3 of Don Cox's prefiled testimony.) Included in the requested rate increase are expenses of \$963,723 associated with leasing the Silver Lake system (Don Cox's Exhibits). BWC estimates that it would begin delivering water through the Silver Lake water system on September 1, 1989. (Page 15 of Jim Chelini's testimony.) This assumes that the Silver Lake water rights changes are accomplished by that date.

9. The water rights, which are currently in Atlantic Richfield Company's name, are identified in the Temporary Preliminary Decree, Basin 76 G as 76G-W-091503, 091504, 091505, 091506 and 091509 (BWC response to PSC data request 8). In response to PSC data request number 9 BWC stated:

Upon the Commission's acceptance of the Company's Application in this Docket, the owner of the water rights that would ultimately be transferred to the Company will file an Application with the Montana Department of Natural Resources and Conservation Water Rights Bureau for a change of appropriation water right covering the change in point of diversion, change in place of use, and change in purpose of use of the water rights identified in the Response to No. 8.

The proceedings are described in Section 85-2402, MCA, and will involve, in this case, the approval of the Montana Legislature.

The length and complexity of the proceedings will depend, to the greatest extent, upon the nature of any opposition to the proceedings. In any event, because legislative approval is required, the proceedings cannot be completed until after the Commission issues its final order in this Docket and must be completed before adjournment of the 51st Legislature.

DISCUSSION AND ANALYSIS

10. With this filing Butte Water Company asks the Commission to vary from its standard rate making practice of reviewing the reasonableness of a utility's expenses and acquisitions after the expense has been incurred. It seeks pre-approval of a transaction with an affiliated interest that may or may not go into effect in September, 1989. According to the Company, if the Commission does not accept certain provisions of the agreement or if the water rights cannot be changed, the transaction may never be finalized.

11. The Commission will not process the portion of the filing that seeks pre-approval of the lease. Butte Water Company has been notified of what it can do if it wishes to preserve its rate increase application (see attached Notice of Commission Action). The Commission is not accepting or rejecting the Silver Lake system as an option or preventing BWC from making any agreements it sees fit. The Commission's position is that BWC should proceed with improvements it believes are necessary to provide adequate service, then seek a fair rate of return on investment and recovery of reasonable expenses

according to the Commission's standard rate setting procedure.

12. The Public Service Commission is responsible for supervising and regulating Montana public utilities.

. 69-3-102, MCA. The Commission is governed by the provisions of Title 69, MCA. In addition, in 69-3-103, MCA, the legislature conferred on the Commission the authority to:

(P)rescribe rules of procedure and to do all things necessary and convenient in the exercise of the powers conferred by this chapter upon the commission; ...

(2) The Commission shall have the power to:

- (a) adopt reasonable and proper rules relative to all inspection, tests, audits and investigations;
- (b) adopt and publish reasonable and proper rules to govern its proceedings and
- (c) regulate the mode and manner of all investigations and hearings of public utilities and other parties before it.

The Commission has adopted administrative rules to implement Title 69. These rules, which are applied to all electric, gas and private water utilities, establish the procedures for filing a rate increase. These rules set forth what financial data is required and establish concepts such as the historical test year.

13. The Commission has two major reasons for not considering a pre-approval application: (1) the Commission does not have the legal authority to pre-approve utility investments or expenses; and (2) in this case water rights must be changed prior to the leasing of the system.

Statutory Authority to Pre-Approve

14. Pre-approving and valuing the Silver Lake transmission system, or any other utility plant, violates 69-3-109, MCA.

Ascertaining property values. The commission may, in its discretion, investigate and ascertain the value of the property of every public utility actually used and useful for the convenience of the public. The commission is not bound to accept or use any particular value in determining rates; provided, that if any value is used, such value may not exceed the original cost of the property. In making such investigation the commission may avail itself of all information contained in the assessment rolls of various counties, the public records of the various branches of the state government, or any other information obtainable, and the commission may at any time of its own initiative make a revaluation of such property.

15. The PSC sets utility rates, it is not responsible for managing utilities and is not involved in management decisions. It appears that 36 states may give limited pre-approval of utility investment activities. [Page 12. Commission Pre-approval of Utility Investments, the National Regulatory Research Institute (1987).] These states' utility statutes have either siting provisions or Certificates of Public Convenience and Necessity (PC&N) for utilities.

Montana utility statutes have neither siting provisions nor PC&N for utilities. (Montana does have PC&N for motor carriers.) States that give prior approval do so to a very limited extent; there is prior approval of the building activity, not the expenditure.

16. The PSC, as required by Montana law, uses the traditional regulatory procedure of reviewing the appropriateness of major utility investments after they have been made, when the utility seeks recovery of the costs in rates.

17. The Commission must comply with that portion of 69-3-109, MCA, which states "The Commission may, in its discretion, investigate and ascertain the value of the property of every public utility actually used and useful for the convenience of the public." The PSC does not have the authority to value property before it is used and useful.

18. Even if the Commission pre-approved an investment activity, a later Commission would not be bound to allow the recovery of the investment at the level pre-approved. One, an asset must be used and useful to be included in rate base -- if the Commission pre-approved expenditures that it later determined were not actually used and useful those expenses would not be recoverable. Section 69-3-109, MCA, states: "The commission is not bound to accept or use any particular value in determining rates.

19. Considering this request for pre-approval now could result in needless proceedings and expenses for all interested parties.

20. While the legal issues are not identical, it is worth noting that pre-approval was argued by the Montana Power

Company with Colstrip Units 3 and 4. MPC argued that the DNRC's certificate of environmental compatibility and public need for Colstrip Units 3 and 4, a type of "pre-approval," limited the application of 69-3-109, MCA. In MPC v. PSC, 692 P.2d 432 at 493 (1984) the Montana Supreme Court stated that under Montana's regulatory statutes "having constructed the plant, the utility requests rate base treatment for the new facility and the PSC then determines whether the facility is used and useful" (emphasis added).

Water Rights

21. Existing Silver Lake water rights are for industrial use. A BWC lease of the Silver Lake system would be useless until water rights are changed. The Department of Natural Resources (DNRC) is responsible for processing changes in appropriation right. ~ 85-2-402, MCA. It also will take legislative action under 85-2-402 (4)(b), MCA.

22. The Commission has no authority over water rights; it has no knowledge of who holds water rights or expertise concerning best use. A serious problem could occur if the Commission approved the Silver Lake system before it was used and useful, then DNRC denied the water rights. Obtaining water rights should be similar to any other property right such as access for transmission lines or condemning land for plant. The Commission is not involved in property ownership matters; a utility must resolve these issues on its own.

23. In addition to the problems of statutory authority and water rights, the Commission has other concerns with this filing. The certainty of the lease is questionable because the entire proposal depends, in part, on the Commission's willingness to exempt Dennis Washington from utility status under

. 69-3-111, MCA. The Commission has no knowledge of what entity owns the Silver Lake water rights. It appears to be Dennis Washington or Montana Resources, Inc. (MRI). The lease proposal hinges on exempting Dennis Washington or MRI from utility status which may not be possible. By furnishing water to BWC, however, Dennis Washington or MRI may not qualify to be exempt.

24. Section 65-3-111, MCA, allows the Commission the discretion to exempt entities that would not otherwise be utilities under 69-3-101, MCA, if that entity is a utility solely because it owns utility plant or water rights that are:

- 1) leased to a public utility, or
- 2) the operation and use is leased to a public utility, or
- 3) holds such plant for 90 day grace period after the above.

CONCLUSIONS OF LAW

1. The Applicant, Butte 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 authority to notify a utility that its filing is deficient and give it the opportunity to correct the filing. ARM 38.5.184 and 69-3-103, MCA.

ORDER

NOW THEREFORE, IT IS ORDERED that the Commission hereby notifies BWC that the filing is deficient. BWC seeks pre-

approval of the integration of the Silver Lake transmission system into its water system but the Commission does not have the jurisdiction to pre-approve utility management decisions. BWC may have until August 7, 1988, to correct its application by removing the pre-approval of the Silver Lake transmission system from its requested rate increase. If the correction is made within the time allowed, the date of the initial filing will be preserved.

Done and Dated this 25th day of July, 1988 by a vote of 5- 0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

CLYDE JARVIS, Chairman

JOHN B. DRISCOLL, Commissioner

HOWARD L. ELLIS, Commissioner

TOM MONAHAN, Commissioner

DANNY OBERG Commissioner

ATTEST:

Carol Frasier
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 ARM 38.2.4806.