

Service Date: February 21, 1990

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

* * * * *

IN THE MATTER of the Application)	
of the BUTTE WATER COMPANY for)	UTILITY DIVISION
Authority to Increase Rates and)	DOCKET NO. 88.9.29
Charges for Water Service to its)	ORDER NO. 5382c
Butte, Montana Customers.)	
_____)	

APPEARANCES

FOR THE APPLICANT:

Milton Datsopoulos and Richard M. Basket, Datsopoulos,
MacDonald & Lind, 201 West Main Street, Missoula, Montana
59802.

FOR THE INTERVENORS:

Mary Wright, Staff Attorney, Montana Consumer Counsel, 34
West 6th Avenue, Helena, Montana 59620.

FOR THE COMMISSION:

Denise Peterson, Staff Attorney, 2701 Prospect Avenue,
Helena, Montana 59620.

Ron Woods, Rate Analyst, 2701 Prospect Avenue, Helena,
Montana.

BEFORE:

JOHN DRISCOLL, Commissioner & Hearing Examiner
CLYDE JARVIS, Chairman
HOWARD ELLIS, Commissioner
DANNY OBERG, Commissioner
WALLY MERCER, Commissioner

BACKGROUND

1. On September 26, 1988, Butte Water Company (Applicant or
BWC) filed an application with this Commission for authority to
increase water rates and charges to its Butte, Montana customers

on a permanent basis by approximately 18.4%. This constitutes an annual revenue increase of approximately \$685,356 (See Exhibit E, Schedule DC-1).

2. Concurrent with its filing for a permanent increase in rates, BWC filed an application for an interim increase in rates. BWC's requested interim rate increase would have increased annual revenues by approximately \$489,484.

3. On November 21, 1988, after proper notice, a hearing was held in the City Council Chambers, Butte, Montana. For the convenience of the consuming public there was also a night session that commenced at 7:00 p.m. on November 21, 1988, at the same location. The public hearing was bifurcated to consider the merits of the Applicant's proposed water rate adjustment and to consider the adequacy of service provided to water subscribers in BWC's Butte, Montana service area.

4. On December 2, 1988, the Commission, having considered the testimony and supporting exhibits submitted at the public hearing in support of the Applicant's interim application, issued Order No. 5382 granting the Applicant interim relief in the amount of \$460,166.

5. On March 16, 1989, after completing responses to data requests and meeting with the staff of the Montana Consumer Counsel (MCC) and the Commission, BWC filed revised interim tariff tables for its Butte Division. Revised interim tariffs incorporated a reduction of flat rate charges, other than sprin-

klings, of 8.23% from the interim rates authorized in Order 5382. The proposed reduction in rates represented an annual revenue reduction in the amount of \$138,913. BWC filed the revised tariffs because it could not support an annual revenue increase in the amount authorized in the original interim order. (See BWC letter of application, March 16, 1989.)

6. On March 27, 1989, the Commission, after reviewing BWC's proposal to reduce interim rates, issued Order No. 5382a. This order provided that BWC was authorized to decrease rates by the 8.23% requested. The order also provided that BWC would, over a four month period, return to the ratepayers \$38,601 in overcollected revenues.

7. On April 18, 1989, after proper notice, an additional hearing was held in the City Council Chambers, Butte, Montana. For the convenience of the consuming public a night session was held commencing at 7:00 p.m. at the same location. The purpose of this public hearing was to receive additional testimony so that the Commission could make a final determination regarding the application for increased rates.

8. On August 17, 1989, this Commission issued Order No. 5382b denying BWC's request for increased rates and charges in its Butte service area. This order also provided that all monies collected under the interim rates approved in Order No. 5382a be rebated to consumers.

9. On August 28, 1989, BWC, filed a Motion for Reconsideration of Order No. 5382b, alleging that the denial of BWC's request for increased rates was incorrectly premised on the Applicant's failure to discharge its public utility obligation.

10. On December 1, 1989, the Applicant filed a Notice of Filing of Capital Improvement Plan and an Amended Motion for Reconsideration. BWC notified the Commission that the proposed capital improvement plan was submitted in compliance with Commission Order Nos. 5387 and 5387a, subject of litigation between the Commission and the Applicant. The Amended Motion for Reconsideration alleged that "there had been a change of facts since the date of the Commission's Order No. 5382b and the Applicant's initial Motion for Reconsideration that provides additional grounds for the Commission to reconsider Order No. 5382b."

11. After review of the Amended Motion for Reconsideration and the supporting brief, the Commission on its own initiative reopened the Docket for the taking of additional evidence. The Docket was reopened for the express purpose of receiving additional testimony on the alleged changed circumstances of BWC since the date of issuance of Order No. 5382b.

12. On January 11, 1990, after proper notice, the Commission held hearings in the Public Library Meeting Room and the Senior Citizens Center, Butte, Montana. The purpose of these hearings was to receive testimony on alleged changed circumstances that in the Applicant's opinion provided additional grounds

for the Commission to reconsider Order No. 5382b, and testimony from the public.

FINDINGS OF FACT

13. During the various public hearings in this docket on the Applicant's proposed rate adjustment and on adequacy of service, the Applicant presented the testimony and exhibits of:

James Chelini, President & General Manager, BWC
Mike Patterson, Vice President & Operations Manager, BWC
Patrick White, Consulting Engineer
Don Cox, Certified Public Accountant and Controller, BWC

14. At the various public hearings the MCC presented the testimony and exhibits of one expert witness, Frank Buckley, Rate Analyst, Montana Consumer Counsel, and 24 public witnesses.

15. In Order No. 5382b issued August 17, 1989, the Commission did not address the one remaining issue in dispute between the MCC and the Applicant, that is, the matter of interest synchronization. Interest synchronization is a ratemaking procedure used in many regulatory jurisdictions to compute tax deductible interest expense when a hypothetical capital structure is used to establish a reasonable rate of return. This issue was not testified to during the January 11 public hearing and is not one of the changed circumstances alleged by the Applicant. Therefore, for purposes of this order no reconsideration is

being given to the merits of the previous arguments presented by the parties on this issue.

16. In Order No. 5382b the Commission found that the testimony received to the date of the order established that BWC was not discharging two of its primary public utility obligations. The Commission stated the following:

"As a public utility BWC is required to satisfy a three part equation in the discharge of its public utility obligation. The components of this three part equation are reasonably adequate service plus reasonably adequate facilities plus just and reasonable rates equals discharge of public utility obligation (Section 69-3-201, MCA). BWC is not providing its customers with reasonably adequate service and facilities; BWC's failure to discharge these relevant regulatory requirements impact the Commission's revenue need deliberations."

17. The Commission found in Order No. 5382b that it would not be just and reasonable to authorize a rate increase which would allow a recovery from ratepayers for escalating operation and maintenance expenses in excess of a level reasonably expected if the facilities were adequate. Further finding that the rates should reflect the inadequacy of service and facilities, the Commission denied the rate increase application.

18. The Commission takes administrative notice of the hearing held by the Montana Legislative Consumer Committee on October 13, 1989, in which representatives of BWC, MCC, Montana Department of Health and Environmental Sciences (DHES), Butte-Sil-

ver Bow and the Commission appeared and testified. At this hearing BWC expressed its willingness to work toward correcting the water service and facility problems in Butte. BWC expressed the commitment of Dennis Washington, BWC's sole corporate owner, to participate appropriately in this matter through BWC's new counsel, Milton Datsopoulos. Mr. Datsopoulos stated that Mr. Washington was willing to invest in the system with the understanding that he would have an opportunity to earn a reasonable rate of return on his investment.

19. At the Commission hearing held on January 11, 1990, the Applicant admitted that no changed circumstance existed in the adequacy of facilities, but stated that it was taking positive steps to correct the inadequacies.

20. The changed circumstances that the Applicant addressed at the public hearing on January 11, 1990, included progress made toward identifying system deficiencies; its contacts with the financial community in an attempt to attract debt capital; the willingness of the equity investor to invest capital to upgrade service and facilities; and the cooperative effort between BWC and various governmental agencies to develop a capital improvement program that represents low cost production, while still meeting the required standards of the agencies and BWC's cash flow requirements.

21. Don Cox, Controller for BWC, testified that BWC had engaged the services of an engineering firm. The firm was direct-

ed by BWC to determine what corrective actions needed to be taken by the company to comply with the facility mandates of this Commission and DHES. Mr. Cox indicated that the direction given the firm was limited to an examination of the existing facilities and sources of supply owned and controlled by BWC. BWC directed the consulting engineers to examine only existing facilities because of the time constraints imposed on BWC to upgrade service and facilities.

22. Patrick White, engineer from the consulting firm of James M. Montgomery, testified that his firm had been engaged by BWC to update the water master plan and to assist the company in addressing the health advisory issued by the DHES. Mr. White provided an update regarding the progress of the consulting engineers in completing BWC's charge to examine existing facilities and recommend corrective actions.

23. Mr. White indicated that his firm had prepared a disinfection study to address part of the health concerns of the DHES which had been finalized and sent to BWC on January 8, 1990. Mr. White also testified that his staff had completed the preliminary water master plan update requested by BWC, but that he had not, as of the hearing, had an opportunity to review the plan. He indicated that upon his return to his office he would review the draft prepared by his staff and submit the plan to BWC for its review during the week of January 15, 1990.

24. BWC is attempting to obtain debt to generate part of the monies needed to construct capital improvements to the water system. Mr. Cox indicated that in order to use debt financing as a resource for implementing its capital improvement program BWC has been in contact with experts in the financial community. These experts were contacted by the company to determine the minimum acceptable financial criteria that would be imposed on BWC in connection with a proposed debt issue.

25. Mr. Cox testified that the financial experts had indicated that at a minimum BWC would be required to produce current financial statements showing that BWC was being given the opportunity to earn a fair return on its existing rate base. He further testified that without the increase under consideration in this proceeding BWC would incur an operating loss of approximately \$200,000. Without Commission authorization to increase rates and charges, BWC will not meet the minimum expectations of the financial community in regard to any possible debt issue.

26. The engineering firm estimates in the current water master plan that BWC has a capital investment requirement of approximately \$30,000,000 over the next five years, in order to comply with the orders of this Commission to upgrade facilities and service and satisfy the requirements of the Safe Drinking Water Act enforced by the DHES.

27. With the time constraints and magnitude of capital investment requirement, BWC cannot rely on its ability to generate

capital internally or expect the debt market to take the entire risk of funding the capital requirement. The debt market's unwillingness to accept the entire risk for funding the capital improvements will necessitate some investment from BWC's equity investor in construction of capital improvements. In previous proceedings before this Commission, BWC has indicated that its equity investor is unwilling to invest additional capital in this enterprise (Docket No. 87.6.30, Prefiled testimony of J. W. Chelini, Page 9). Agents of BWC have since represented that if debt financing can be obtained to partially fund the improvement program the equity investor is willing to invest additional monies in this enterprise.

28. The representation that the equity investor is willing to participate in the funding of the capital improvement program is a significant change in light of the historic position represented to the Commission by BWC. Without participation of the equity investor there would be no reasonable expectation that BWC would attract sufficient monies from the financial community to accomplish the task of funding the necessary capital improvements.

29. Testimony from Don Cox at the January 11 hearing indicated that there was an ongoing, coordinated and cooperative effort among various entities (the Company, the MCC, Butte-Silver Bow, DHES, the PSC staff, and other representatives) interested in resolving the problems confronting BWC and its subscribers. In

his testimony Mr. Cox indicated that the concerned groups participated in several meetings to discuss possible resolutions to the problems of inadequacy of service, poor water quality, financing and low cost production alternatives.

30. This new spirit of cooperation exhibited by all of the interested participants represents a significant change from the recent past. Since 1985, there has been a highly contentious atmosphere surrounding relationships between BWC, the Commission, MCC and others. The change in attitude and cooperative tone has resulted in the establishment of round table discussions which will hopefully resolve BWC's facility and financial problems.

31. Don Cox also testified that BWC needed the increase in rates in order to have sufficient funds to complete the necessary engineering studies to construct the required facilities. BWC also needed the increase to generate sufficient capital internally to construct some of the less expensive capital improvements contemplated for this construction season, such as the modifications to the disinfection system. It was BWC's position that without these internally generated funds it could not proceed along the time line established for the construction of various facilities or attain the ultimate goal of providing consumers with a safe reliable supply of water.

32. Progress made toward identifying system deficiencies, contacts with the financial community, the apparent willingness

of the equity investor to invest capital, the cooperative effort between BWC and various governmental agencies, and cash flow requirements are the issues on which BWC wishes the Commission to premise its reconsideration and grant a rate increase.

33. The vast majority of the consumers presenting testimony at the hearing expressed opposition to the Applicant's proposal that the Commission reconsider and authorize an increase. These consumers pointed to the fact that the Commission had originally denied BWC's request for increased rates on the grounds that the company was failing to discharge its public utility obligation to provide reasonably adequate service and facilities. These consumers testified that since the date of the Commission's original order no improvement in service or facilities had occurred. Subsequent to the Commission's denial of the rate increase consumers within BWC's service territory were placed under a health advisory from DHES to boil their water. As a result of the advisory, consumers were being forced to purchase potable bottled water or obtain potable water from other sources at their own expense. BWC had expended no monies on capital improvements to show good faith in alleviating the existing problems and therefore, according to public testimony, the public interest is not served by the granting of an increase at this time.

34. A minority of the consumers testifying at the hearing supported the increase for various reasons. There was testimony

that further economic development in Butte is contingent upon Butte having an adequate and safe supply of water. This minority of the public testified that absent adequate revenues the utility would be unable to upgrade facilities and provide reasonably adequate service and that health concerns require that the facilities be upgraded.

DISCUSSION, FURTHER FINDINGS AND ANALYSIS

35. All of the parties put forth convincing reasons why the Commission should adopt their position to grant or deny the motion for reconsideration. The validity of the opinions expressed by both sides on the issue of reconsideration places the Commission in the position of having to rely on its best judgment regarding the long term best interests of the ratepayers and BWC. Any decision of the Commission necessarily conflicts with either those in support of or in opposition to the rate increase.

36. The Commission recognizes that the consumers are presently paying for a product that is less than adequate. The Commission further recognizes that the consumers do not think they should pay more for the product without some improvement in service or facilities. As the consumers point out in their testimony, no improvement has occurred in the quality of the product or the service since the issuance of the last order.

37. Although there has been no change in the service provided consumers, there has been a significant change in attitude on the part of the Applicant. The Applicant has now demonstrated a good faith effort toward addressing and resolving the current system deficiencies. BWC has engaged an engineering firm, contacted the financial community, filed an improvement plan with the Commission and made a cooperative effort with all interested parties.

38. In the current proceeding BWC has shown that without the Commission's reconsideration of its previous decision, BWC will not have available the basic financial resources necessary to start improving service to its consumers. BWC presented testimony that it needed sufficient cash flows in order to continue with its planning for major improvements. BWC also established that if it is to gain access to the debt market or attract equity capital in order to construct capital improvements, it must demonstrate to potential investors that on a current basis it is generating a reasonable return on its current rate base.

39. At this juncture the main objective of the Commission is to compel BWC, by whatever means are at its disposal, to improve service and facilities in its Butte service area. To achieve the goal of improving service, the Commission in the exercise of its regulatory powers will support BWC in its efforts to obtain the necessary resources to accomplish the task. The Commission in this order demonstrates to potential debt holders and/or equi-

ty investors that the goal of improved service is a cooperative venture and further, that the regulatory process does not represent an impediment to improving service and facilities.

40. The Commission based upon the evidence presented in this Docket finds that it should reconsider its Order No. 5382b and authorize the Applicant an annual revenue increase in the amount of \$321,253. The Commission finds that the Applicant should generate the increased revenues authorized herein by increasing rates and charges to all customer classes except metered customers.

41. As part of the January 11, 1990, public hearing the Applicant presented testimony on a request to modify its existing Butte, Montana service area. The Applicant indicated that the service area map filed with the Commission on July 5, 1989 represented a reduction in its service area, but included within the service area all properties currently adjacent to its water mains. The Commission, with the understanding that the July 5, service area map includes all properties adjacent to company mains, approves the request to modify the service area.

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 69-3-102, MCA.

2. The Commission has provided adequate 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. Section 69-3-201, MCA.

ORDER

NOW, THEREFORE, IT IS ORDERED THAT:

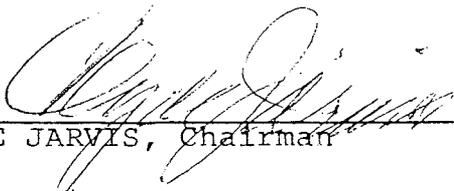
1. Butte Water Company shall file rate schedules which reflect an increase in annual revenues of \$321,253 for its Butte, Montana service area. The increased revenues shall be generated by increasing rates and charges as provided herein.

2. The rates approved herein shall not become effective until approved by the Commission.

3. Butte Water Company's request to modify its service area is approved.

DONE IN OPEN SESSION at Helena, Montana this 20th day of February, 1990 by a 5 - 0 vote.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION



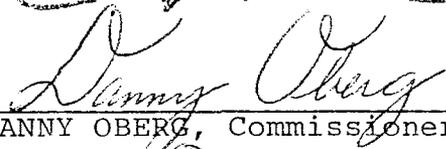
CLYDE JARVIS, Chairman



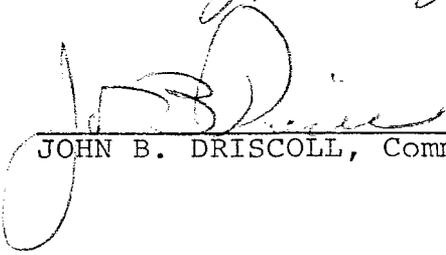
HOWARD L. ELLIS, Commissioner



WALLACE W. "WALLY" MERCER, Commissioner



DANNY OBERG, Commissioner



JOHN B. DRISCOLL, Commissioner

ATTEST:


Ann Peck
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.