

Service Date: December 22, 1989

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 MOUNTAIN WATER COMPANY for ) UTILITY DIVISION  
Authority to Increase Rates and ) DOCKET NO. 89.6.23  
Charges for Water Service in the ) ORDER NO. 5449  
Missoula, Montana Service Area. )

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APPEARANCES

FOR THE APPLICANT:

John Alke, Attorney at Law, Hughes, Kellner, Sullivan &  
Alke, P.O. Box 1166, Helena, Montana 59624

FOR THE INTERVENORS:

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

FOR THE COMMISSION:

Robin McHugh, Staff Attorney, 2701 Prospect Avenue, Helena,  
Montana 59620

BEFORE:

Clyde Jarvis, Chairman  
Howard Ellis, Commissioner  
Danny Oberg, Commissioner  
Wally Mercer, Commissioner

FINDINGS OF FACT

1. On June 29, 1989, Mountain Water Company (Applicant or MWC) filed an application with this Commission for authority to increase water rates and charges for its Missoula, Montana customers on a permanent basis by approximately 17.68 percent. If granted, this would constitute a revenue increase of approximately \$804,241.

2. Concurrent with its filing for a permanent increase in rates MWC filed an application for an interim increase in rates of approximately 11.75 percent, equalling a revenue increase of approximately \$534,329 or 66.4 percent of the proposed permanent increase.

3. On September 27, 1989 MWC and the Montana Consumer Counsel (MCC) entered into a stipulation that, for purposes of this rate case, a reasonable cost of equity would be 12.5 percent and a reasonable hypothetical capital structure would be 55 percent equity and 45 percent debt. The stipulation also provided that the debt component of the capital structure would be divided into two parts, 25.5 percent being the actual debt of the Company and 19.5 percent representing hypothetical debt.

4. The stipulation filed with the Commission contained a motion requesting that the Commission issue an order adopting the stipulation entered into by the Applicant and MCC. Before the Commission will accept a stipulation disposing of a contested issue in a rate case it requires, 1) that the parties to the stipulation provide sufficient information for the Commission to conclude that the stipulation is reasonable, and 2) that all parties have an opportunity to comment on the stipulation.

5. On November 27, 1989 following notice to all parties in this Docket, a meeting was held in the Commission offices to discuss the reasonableness of the proposed stipulation. Representatives of MWC and the MCC, were present at the meeting. The only other intervenor, the City of Missoula, was not represented. The purpose of this meeting

was to allow the Applicant and the MCC to provide the Commission with additional background information in support of the reasonableness of their stipulation and to receive comments from all parties.

6. The Commission, having considered all of the information presented on the reasonableness of the proposed stipulation, adopts the stipulation entered into by the Applicant and the MCC. Although the Commission adopts the proposed stipulation, it would be remiss if it did not discuss certain concerns regarding the stipulation.

#### Discussion

7. The information presented at the stipulation meeting, and in various supporting documentation indicates that the cost assigned to the hypothetical debt component of the capital structure does not accurately portray MWC's actual incremental cost of attracting additional debt capital. The premise of the stipulation is that any potential debt issuance would obligate MWC and would be placed with a local financial institution. The testimony and exhibits of MWC in this Docket indicates that any future debt issuance by MWC would be through local placement. However, the Commission has reason to believe that this would not be the case.

8. Mountain Water Company is a wholly owned subsidiary of Park Water Company (Park Water). Park Water provides certain support services to MWC through its main office in Downey, California. One of the services provided to MWC, by Park Water, is financial management assistance. The main office financial management assistance includes the handling of any potential debt placement for Mountain and all other subsidiaries under Park's corporate umbrella.

9. During the stipulation meeting, Mr. John Alke, MWC's attorney, represented that none of Park Water Company's subsidiaries actually holds debt in its name. Mr. Alke explained that all current outstanding debt obligations of Park Water Company, and its subsidiaries, are held in the name of Park. Under this arrangement debt is acquired by the parent, then the debt is allocated, for financial reporting and ratemaking purposes, to the

corporate entity receiving benefit from the debt proceeds. (Such is the case with the Montana Power Company debt obligation assigned to MWC.)

10. There is a logical reason behind Park Water being the originator and obligated party in debt financing. Park Water, as the parent, uses consolidated financial statements giving it a greater borrowing capacity and affording the company the opportunity to acquire debt at a rate lower than its individual subsidiaries. Historically, and at the present time, debt capital attraction is a function of the parent.

11. Mr. Alke in his presentation to the Commission stated that MWC should be viewed on a stand alone basis and that this view should form the basis for Commission acceptance of the interest rate quoted in the testimony, and accepted by the parties to the stipulation. He made this assertion, even though his own statements regarding existing conditions and Park's corporate policies on debt financing, contradict the view that MWC stands alone.

12. The parent/subsidiary debt financing arrangement has an impact on the cost of capital employed by MWC in providing service to its customers. It is the current policy of Park Water that all debt obligations will be initiated at the corporate level, be in the name of the parent, and the debt cost will be recovered from the subsidiary receiving beneficial use from the debt obligation. Given this policy, the Commission finds that a more appropriate basis for determining the cost of incremental debt to MWC would be to determine the rate at which Park Water Company can attract debt capital.

13. Although it does not appear that the proposed stipulation represents the facts and circumstances as they actually exist, the Commission will accept the stipulation as filed. Rejection of the stipulation would necessitate the hiring of expert witnesses to address the issue of capital structure and cost of capital. The cost of retaining expert witnesses would exceed any potential revenue requirement reduction associated with a reduced cost of the hypothetical debt. Since the cost of having the parties address the issue would exceed any potential benefit to be derived by the ratepayer it is prudent in this case to accept the stipulation. However, the Applicant is cautioned that any stipulations

filed in future proceedings regarding this issue will be scrutinized by the Commission to insure that they accurately portray the conditions under which capital will be attracted.

14. Having disposed of the cost of capital and capital structure issues, which could significantly impact the Applicant's need for additional revenues, it is now appropriate for the Commission to address the issue of the Applicant's request for interim rate relief. The Commission's interim rules and guidelines call for a clear showing that the petitioning utility is suffering an obvious income deficiency before the Commission will authorize the grant of interim rate relief.

15. As provided for in the procedural schedule in this Docket the deadline for the filing of intervenor testimony has passed. The only intervenor to file testimony was the MCC. In that testimony the MCC supports the granting of a revenue increase in the amount of \$374,516. Authorizing an increase in this amount, therefore, should be uncontested by any party participating in this proceeding.

16. The Commission finds that additional annual revenues in the amount of \$374,516 are reasonable as a level for interim rate relief to the Applicant.

17. The annual revenue increase shall be spread to all services provided by the Applicant, other than private fire protection, on the basis of a uniform percentage increase.

#### CONCLUSIONS OF LAW

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

2. Section 69-3-304, MCA, provides in part, "The Commission may in its discretion, temporarily approve increases pending a hearing or final decision.

3. The Commission concludes that the grant of an interim rate increase in the manner set forth herein is just, reasonable and within the discretion granted by Section 69-3-304, MCA.

4. The increase granted herein is subject to rebate, with interest at the rate of 12.5 percent annually, should the final order in this Docket determine that a lesser revenue increase is warranted. Section 69-3-304, MCA.

5. The Commission afforded all parties to this proceeding notice and the opportunity to participate in the stipulation presentation. The Commission acted at all times in conformance with its rule on voluntary settlement. ARM 38.2.3001.

6. The stipulation adopted herein is declared to be reasonable, just and proper.

ORDER

NOW, THEREFORE, IT IS ORDERED THAT:

1. Mountain Water Company shall file rate schedules which reflect an increase in annual revenues of \$374,516 for its Missoula, Montana service area. The increased revenues shall be generated by increasing rates and charges to all customer classifications as provided herein.

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

3. The stipulation entered into between Mountain Water Company and Montana Consumer Counsel on September 27, 1989, establishing the cost of capital for Mountain Water Company and establishing a reasonable hypothetical capital structure in this case is adopted. Cost of capital and hypothetical capital structure will henceforth not be contested issues in this Docket.

4. DONE IN OPEN SESSION at Helena, Montana, this 20th day of December, 1989, by a 4 - 0 vote.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

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CLYDE JARVIS, Chairman

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HOWARD L. ELLIS, Commissioner

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WALLACE W. "WALLY" MERCER, Commissioner

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DANNY OBERG, 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.