KRISTINE A. SASSER
DEPUTY ATTORNEY GENERAL
IDAHO PUBLIC UTILITIES COMMISSION
PO BOX 83720
BOISE, IDAHO 83720-0074
(208) 334-0357
BAR NO. 6618

Street Address for Express mail
472 W. WASHINGTON
BOISE, IDAHO 83702-5918

RECEIVED
2010 FEB 11 PM 4:49
IDAHO PUBLIC
UTILITIES COMMISSION

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF FALLS WATER COMPANY FOR AUTHORITY TO INCREASE ITS RATES AND CHARGES.

CASE NO. FLS-W-09-01

COMMENTS OF THE COMMISSION STAFF

The Staff of the Idaho Public Utilities Commission, by and through its attorney of record, Kristine A. Sasser, Deputy Attorney General, in response to the Notice of Scheduling and Notice of Telephonic Hearing (Order No. 30994) submits the following comments.

BACKGROUND

On August 4, 2009, Falls Water Company filed an Application for authority to increase its total revenue requirement by $143,497, or 14.39%. The Company is proposing to increase its metered customer charge from $14.00 to $18.00 (29%) to improve cash flows to meet minimum fixed costs during winter months and decrease it's commodity rate from $0.667 to $0.601 per thousand gallons (-10%). The Company proposes to delete its obsolete current flat rate Schedule R-2. The Company is also proposing to add certain non-recurring charges to the Company's Schedule M. The Company requested that the Application be processed by Modified Procedure and that the tariff changes become effective September 10, 2009.

On September 2, 2009, the Commission issued a Notice of Application and Notice of Intervention Deadline that suspended the Company's proposed effective date of September 10,

2009. Order No. 30893. No parties petitioned to intervene. On September 16, 2009, a Notice of Public Workshop and Notice of Modified Procedure was issued setting a deadline for comments to be filed no later than October 7, 2009. Order No. 30899. On September 30, 2009, Commission Staff filed a Motion to Suspend the Deadline for Filing Comments. The Commission granted Staff's Motion to Suspend and directed Staff to present a feasible schedule to the Commission for approval after meeting with the parties to discuss the processing of this case. Order No. 30927. Pursuant to the directive given by the Commission, the parties agreed to a schedule which was adopted by the Commission. Order No. 30994.

STAFF ANALYSIS

System Condition

As part of the evaluation process, Staff conducted a field tour of the water system on October 8, 2009, accompanied by Tony Wise, Operations Manager and certified water operator of Falls Water Company. The tour involved inspecting the various components of the water supply and distribution system and focusing on project components that were recently completed or are in the process of being completed.

Falls Water currently has seven production wells (Well Nos. 1, 2, 4, 5, 6, 8 & 9) as sources of water supply. Well No. 9 located at North Deborah Drive and close to the Company's office is the newest well developed and put into service in May 2009. Well No. 9 is a 16-inch well equipped with 450-hp vertical turbine pump, the largest pumping unit in the Falls Water system with a design capacity of approximately 3,000 gpm. Well No. 9 is also equipped with a variable frequency drive and a 514 kW backup power generating unit. Although pump No. 9 was not operating during the tour, Staff observed the pressure reading at the discharge line (mainline pressure) past the gate valve was 64 psi. The system does not have storage reservoirs although some of the pumping units are equipped with hydro-pneumatic tanks to supply water during low demand. The facility does not have any booster pumps. The well pumps are also equipped with totalizing flow meters to record water production on a monthly basis. The total rated pumping capacity of all the production pumps is approximately 9,100 gpm.

The distribution network is comprised of various pipe sizes ranging from 2-inch to 12-inch PVC pipes. Water is delivered to various residential and commercial customers using a combination of manual-read (11% of total), touch-read (70%) and radio-read (19%) service meters with sizes ranging from 5/8-inch to 4-inch meters. Approximately 86% of all customers have 3/4-inch service meters. In response to Staff Production Request No. 43, the Company indicated that the conversion of unmetered customers to metered customers was substantially completed at the end of 2008. The few remaining unmetered service lines were converted to metered lines in the spring of 2009. Currently, the Company provides water service to over 3,600 residential and commercial customers. Application at 2.

Revenue Requirement

Test Year, Revenues, Capital Structure, and Overall Rate of Return

The Company proposes using 2008 as its test year. The operating revenues for Falls Water are being properly billed under the existing tariffs on file with the Commission. The accounting for operating revenues is consistent with the requirements of the Uniform System of Accounts, as adopted by this Commission. The major source of revenue for Falls Water is the sale of water to residential, commercial and industrial customers. There is also revenue from hook-up fees. In 2008, actual operating revenues totaled $997,043.

The Company proposes a capital structure of 84.44% Long Term Debt and 15.56% Common Equity. The Company proposes to use the actual cost of the long term debt and a 12% return on common equity. The capital structure proposed, along with the weighted actual cost of debt of 2.88% and 12% return on common equity produces a 4.74% overall rate of return. Staff agrees with the calculation of the capital structure and accepts the return on equity of 12% as being reasonable (Company Exhibit 3). This return on equity is consistent with prior Commission orders for small water companies.

Staff proposes to accept the Company's requested test year, capital structure, and overall rate of return.

Staff proposes to include in test year revenues the revenue from a rental located on Company property. This property was originally used by the water company, remains in rate base, and is held for a future reservoir site. The Company is currently recording this income in non-utility income, and excludes this revenue in its Application. Staff proposes to include this revenue because the property is included in plant in service and the customers are paying a return on this property. The property that has the rental has a revenue requirement of $2,771. The annual income from the rental, at $400 per month, totals $4,800 (Attachment A, line 48) and including this revenue in the test year revenues provides a benefit to customers of $2,029. Incorporating the adjustments, Staff proposes test year revenues of $1,001,843.

Expenses

The Company makes adjustments to seven expense categories, as shown on Company Exhibit No. 2. The expense adjustments are:

1. Adjustment for Non-Recurring Items
2. Increased Labor Costs
3. Increased Office Rent Costs
4. Increased Liability Insurance
5. Increased Source of Supply Costs
6. Increased Miscellaneous Operating Costs
7. Decreased Depreciation Costs

Except for Item 3, Increased Office Rent Costs, Staff accepts the Company's proposed adjustments. Staff also proposes additional adjustments for Water Testing Expense and Depreciation Expense. Staff's adjustment to Depreciation Expense is discussed in the Rate Base section, as it flows from Staff's adjustments to plant in service. Staff's other adjustments are discussed below and shown on Staff Attachment A.

Increased Office Rent Expense

The Company's adjustment for office rent expense reflects the move, during 2008, from the previous office to the current office and warehouse. The Company's adjustment reflects the average amount of the yearly rental expenses for years 2, 3, and 4 of the current lease. The Company's calculated average monthly office and warehouse rent expense is $3,640.

The lease is a four-year lease, beginning on September 1, 2008 and ending on September 1, 2012. The terms of the lease include a base rent of $2,700 per month, increasing by $100 per month in each successive year over the term of the lease. For the year beginning September 1, 2008 through August 30, 2009, the base rent was $2,700 per month. The monthly base rent increases to $2,800 for the second year, $2,900 per month for the third year, and $3,000 per month for the final year of the lease.

The lease also provides for operating costs in addition to the base rent. For the first year of the lease, the additional rent payment for the operating costs totaled $610 per month, and covered property taxes, electricity & natural gas, security system, exterior maintenance, and insurance. The lease terms include an escalator in these costs of 10% per year. For the first year the additional rent was $610 per month, and increases to $811.91 per month for the fourth year of the lease.

The lease was signed with Rockwell Development, Inc., on September 10, 2008. Rockwell Development is an affiliate of Falls Water Company. Both Rockwell Development and Falls Water share the same owners. For Falls Water Company, Inc., Brent Johnson is the President, Jay Johnson is the Vice President, and Paul Johnson is the Secretary/Treasurer. They are also listed as Directors of Falls Water Company on the annual report to the Secretary of State. For Rockwell Development, Inc., Brent Johnson is the Secretary, Paul Johnson is the President, and Jay Johnson is the registered agent.

Staff is concerned about the affiliate/interlocking relationship of the owners and officers between Falls Water Company and Rockwell Development, Inc. The potential for abuse arises because the Company management could inflate expenses charged to the regulated utility, essentially moving the profit from the regulated utility to an unregulated affiliate. Regulated utilities by law receive recovery of costs incurred in the service of providing an essential service; therefore, if the Company inflates utility expenses, the requested recovery from customers for those inflated expenses in rates could be excessive.

Staff notes that affiliate transactions are subject to close scrutiny and the regulated utility has an increased burden of proving the reasonableness of its affiliate transactions. The Company cannot simply rely upon the fact that expenditures were incurred. For expenses to be justified, there needs to be evidence of arm's length bargaining between the Company and the source of the expense. The burden of proof is on the Company to show that the costs incurred in the affiliate transaction are reasonable and beneficial to customers.

In Response to Production Request Nos. 7, 8, and 9, the Company provided information about the Company's need for a larger office and warehouse and a market analysis for the current office and warehouse rental. The Company provided the following reasons for moving to a new office with a warehouse:

1. The lease at the old location was complete and the Company did not want to sign another long term lease agreement for the location because the location no longer met its needs.
2. The Company wants to improve efficiencies in communication and travel by having all managerial offices at one location.
3. The parking for customers and employees was insufficient at the old location.
4. The old location was located outside the Company's service area and the Company was looking to locate within its service area for the convenience of

its customers and to improve efficiency of travel time for field employees to bring information to the office.

5. The old location did not have sufficient room for storage of customer files and other filing that office staff needed to access routinely.
6. A new location would need warehouse space. The warehouse space would be used to store chemicals, equipment, and other items that DEQ states are possible contaminates to the water supply and to comply with wellhead protection rules are not to be stored on site at the wells.

Staff finds the rationale provided by the Company to be reasonable. The new office provides Company personnel with adequate space to perform the functions necessary to provide service to the customers. Staff is aware that the Company had outgrown the previous location and that more space was needed. Staff notes that the new location is not extravagant, nor is there office space that the Company is not utilizing.

Staff reviewed the market analysis provided by the Company. The market analysis provided seven different comparisons for office space with and without a warehouse. Based on the square footage rates for comparable office space of $1.00 per square foot and warehouse space at $0.50 per square foot, the market analysis found the fair market value of the current office and warehouse to be $2,800 per month.

Staff also made inquires as to the rental rates for office space and warehouse space in the Idaho Falls area, and found the market analysis to be reasonable. However, Staff is concerned with the level of due diligence the Company has undertaken in order to prove that the lease terms are reasonable and representative of an arm's length transaction. The market analysis was prepared by Ben Winder of Winstar Realty, yet it was not on Winstar Realty letterhead, nor was it signed by Ben Winder. Furthermore, Staff believes that Ben Winder has a conflict of interest. Ben Winder is listed as the Treasurer of Rockwell Development in the 2009 Annual Report to the Secretary of State. Therefore this market analysis is also an affiliate activity and does not independently verify the market value of the current lease. Staff is not comfortable basing any recommendations upon this market analysis. If Staff had not also made inquires as to the rental rates for office space and warehouse space in the Idaho Falls area, it would be inclined to remove all costs associated with the new office and warehouse. However, based on its own inquiry, Staff finds that the initial lease terms are within a reasonable range.

However, Staff is unable to accept all the terms of the lease, especially the escalators. Staff therefore recommends that only the base amount of the lease be included in rates for recovery from customers. Staff recommends that the total rental expense included in rates be the base rent of $2,700 per month and the base additional rent in the amount of $610 per month.

Staff proposes that the office and warehouse rent costs to be included for recovery from customers is $39,720. The Company included a cost of $43,684 for Office Rent Costs. Staff's adjustment is a decrease in expenses of $3,964, as shown on Attachment A, line 34.

Cash Flow Issues

In the Application the Company states that "The Company's current monthly winter billings create a revenue shortfall of approximately $9,000 each month." Application at 5. This is typical of cash flow problems experienced by many small water companies. In the winter months, revenues are reduced, while in the summer months revenues are increased. Staff has done a cash flow analysis and finds this also to be true for Falls Water Company. However, the cash flow problems are, in part, exacerbated by the owners of the Company. The Company continues to pay the previous owner $2,000 per month for consulting. In the previous rate case, FLS-W-07-01, the Commission disallowed this expense for ratemaking purposes, and while it has not been included in this Application for recovery from customers, it does impact the cash available to the Company, especially during the winter months. In addition to this expense, the Company President charged over $35,000 in personal expenses to the Company credit card. While these expenses were also excluded from the Application for recovery from customers, this too contributes to the cash flow problems experienced by the Company. Staff notes that the owners of the Company do not draw a salary from the Company, and in turn, it is Staff's understanding that the owners are not involved in the daily operations of the Company, therefore a salary would not be appropriate. Staff finds that although these expenditures are not included in the revenue requirement, it is the revenue and cash flow from customers that is funding these activities, and will have an impact on customers to the extent that the Company is unable to pay for maintenance and upkeep necessary to maintain the water system.

Staff notes that the Company's last pay increases were effective in December of 2008. The Company, in response to the downturn in the economy, did not give pay raises in 2009 and, during the onsite audit, indicated that it has no plans to give pay raises in 2010. During the audit, Staff found the Company's costs to be well contained, to the extent that the Company management had control over those costs, and that the Company management strives to keep the costs as low as possible, without negatively impacting service to the customers.

Electric Power Costs

Staff reviewed the adjustment made by the Company to recognize increases in electric power costs. The power cost model developed by the Company initially calculates the normalized kWh usage per customer using the actual kWh usage for nine years (2000-2008) and applying the current electric power rates. The model then computes the annual power cost by using the nine-year average yearly demand and energy charges and multiplied by the total number of year-end customers during the test year (3,594). The result is a normalized annual power cost of $126,622. Staff believes the methodology used by the Company is appropriate. The normalized amount compares favorably with the actual 2009 power expense of $126,022. Staff, therefore, accepts the power cost adjustment proposed by the Company in the amount of $30,028 resulting in a pro forma cost of power in the amount of $126,622. (Attachment A, line 15).

Water Testing Cost

The Company claims that the cost for water testing during the test year is $9,866. The Company did not propose any adjustments to its water testing expenses. Because of different testing cycles required for various water contaminants, Staff believes it is necessary to make appropriate adjustments to normalize water testing costs. The Company provided Staff an annualized cost for a nine-year cycle for water testing in the amount of $5,473 (Response to Staff Production Request No. 2). The Company assumes that for Well No. 9 testing for primary inorganics, synthetic organics, volatile organics, sodium, arsenic and the radiological contaminants (Gross Alpha, Radium 226, Radium 228 and uranium) would be done annually instead of once every nine years (9-year cycle) because Well No. 9 is still a new source. Staff contacted IDEQ and verified that while additional tests may be necessary, they will not be required on a yearly basis for the nine-year cycle. Consequently, Staff made adjustments for the cost of water testing in Well No. 9. These adjustments are presented in Attachment B. The difference between water testing costs for Well No. 9 proposed by the Company ($2,155) and that recommended by Staff ($677) is $1,478. Subtracting $1,478 from the total normalized water testing cost of $5,473 proposed by the Company results in an annual testing cost of $3,995. Staff's adjustment removes $5,871 from the $9,866 water testing cost. (Attachment A, line 27).

Rate Base

The Company proposes a total rate base of $1,856.449 (also shown on Staff Attachment C, line 21), which includes completion of Well No. 9, land and water rights acquisition, pump facility building and a back-up generator. In addition, the Company has included the cost to complete the planned installation of a SCADA system for Well No. 9, and the planned acquisition and installation of additional service meters and MXU transmitters as part of its long-term asset replacement and upgrade program. The meter replacement will consist of upgrading old manual read meters to touch read meters.

As part of the Company's Application, Falls Water proposes to recover the capital expenditures for the various completed and planned system improvements as previously discussed by including them in rate base.

Rate Base Adjustments

Staff has reviewed the Company's request and makes several adjustments to Plant in Service. These include adjustments to Account 303 – Land and Land Rights, Account 304 – Well Structures and Improvements, Account 307 – Wells, Account 311 – Pumps and Accessories, Account 334 – Meters, and Account 340 – Office Equipment. Staff also makes the appropriate adjustments to depreciation expense and accumulated depreciation as they relate to the various plant adjustments proposed by Staff. Staff's rate base adjustments are summarized on Attachment C. The depreciation expense adjustment is summarized on Attachment A, line 51.

Account 307 – Wells

Staff makes an adjustment to Account 307 – Wells, to include a chlorinator pump for Well No. 9. In the course of the audit, Staff was able to evaluate the pro forma adjustments to plant in service proposed by the Company. This adjustment includes the additional investment in Well No. 9 that was not included in the Company's pro forma estimate for the new well. This adjustment increases plant in service by $2,810 as shown on Attachment C, line 3.

Account 311 – Pumps and Accessories

Staff makes an adjustment to Account 311 – Pumps and Accessories to include new controls for the Variable Frequency Drive for the pump located at Well No. 1. In the course of the audit, Staff was able to evaluate the pro forma adjustments to plant in service proposed by the

Company. This adjustment includes the additional investment in Well No. 1 that was not included in the Company's pro forma plant in service adjustment. This adjustment increases plant in service by $2,668 as shown on Attachment C, line 5.

Account 340 – Office Equipment

Staff makes an adjustment to Account 340 – Office Equipment to include 2 new laptop computers. In the course of the audit, Staff was able to evaluate the pro forma adjustments to plant in service proposed by the Company. This adjustment includes the additional investment in office equipment that was not included in the Company's pro forma plant in service adjustment. This adjustment increases plant in service by $1,100 as shown on Attachment C, line 10.

Well No. 9

As discussed previously, one major project that the Company has undertaken was the development and construction of Well No. 9. An engineering study completed by Schiess & Associates Consulting Engineers for Falls Water in 2004 revealed that the Company's water system was experiencing tremendous growth during the decade and it was imperative that a new well be planned immediately to supply peak flow and fire flow demands to the Summit Park and Calico subdivisions. Although Schiess & Associates Engineering Report initially recommended to build the Iona Road Well and Crowley Road Well to improve system pressures and keep supply in pace with demand, Well No. 9 was eventually built by the Company at Deborah Drive. The Company contends that the mainline infrastructure in place around the Deborah Drive lot provides a much better distribution of the well's production into the water system with little or no additional mainline installations other than main line tie-in for the well itself. The Deborah well site can also provide space for future water storage infrastructure.

Staff believes it was appropriate for the Company to undertake the construction of Well No. 9 at the chosen location. The Company also provided Staff a copy of a letter from the Idaho Department of Environmental Quality dated February 27, 2006, indicating that IDEQ supported the project and concured that the proposed water system improvements would be beneficial for public health. The Company put Well No. 9 into service in May 2009. Although the well was not operating during the Staff visit on October 8, 2009, this specific project is considered by Staff as "used and useful."

Cost of Developing Well No. 9

In response to Staff Production Request No. 9, the Company provided a breakdown of the total cost of developing and constructing Well No. 9:

Project Component	**Cost**
Land acquisition	$ 160,000.00
Well drilling	282,843.63
Pump and motor	100,394.35
Electrical controls	90,363.72
Variable frequency drive	30,805.65
Appurtenances	17,251.60
Pump facility building	144,851.00
Back-up generator	98,252.00
Mainline tie-in	54,269.00
Engineering & Miscellaneous	147,115.00
TOTAL COST	**$1,126,145.95**

Staff reviewed the cost of various work elements required to construct Well No. 9 to determine it they were reasonable. Staff also asked the Company to explain cost control efforts applied in contracting and/or paying for project elements. The Company explained that construction of Well No. 9 was funded with State Revolving Loan Fund monies. As with any state funded project, a competitive bid process was followed and the low bidder was selected to build the project. The project was bid in two parts: 1) drilling of the well which was awarded to Andrews Well Drilling and b) construction of the well house, mainline tie-ins, pumps, motors controls, back-up generators, VSD, and appurtenances which was awarded to Vern Clark & Sons. Staff believes that the costs of various project elements were reasonable and comparable with similar projects built by other water utilities. However, Staff takes exception to some of the engineering/professional consulting fees as discussed below.

Engineering Consulting Fees

Staff questions the two payments made by the Company for bid assistance services. As part of the cost for the development and construction of Well No. 9, the Company contracted the services of Schiess & Associates Consulting Engineers and the East-Central Idaho Planning & Development Association, Inc. The specific services provided by Schiess & Associates was specified as follows:

Bid Assistance Services:

Provide bid documents to bidders (1 for well, 1 for building)	$1,200
Answer contractor questions (2 bid periods)	1,680
Issue addendums (2 bid periods)	2,020
Evaluate bids & prepare recommendations (1 for well, 1 for well house)	1,740
Prepare contracts and Notice of Awards (1 for well, 1 for well house)	1,520
Meetings with FWC (2 meetings)	400
Schedule Subtotal	$8,560

(Exhibit A-Description of Engineering Services, Professional Services Contract between Falls Water Company and Schiess & Associates Consulting Engineers, February 22, 2006.)

The Company also confirmed with Staff (response to Staff Production Request No. 50) that the bid documents and project specification for construction of the major components of Well No. 9, which included well construction and development and construction of the well house, mainline, pumps, etc. were prepared by Schiess & Associates and that such documents were approved by the IDEQ, through whom the financing for the project was obtained.

However, another payment was made to East-Central Idaho Planning & Development Association (ECIPDA) for doing similar tasks for the same project. One of the specific services provided by ECIPDA is as follows:

> 3. The Falls Water will pay the Contractor $8,000 for working with the engineer/architect to prepare bid package, to oversee the bid opening and bid award, to help with the execution of construction contract, and to conduct the pre-construction conference. Payment will occur upon execution of the construction contract and completion of the pre-construction conference.
> (Attachment A, Scope of Services, Professional Services Contract, Falls Water and ECIPDA, February 22, 2006.)

Staff believes that this service provided by ECIPDA is a duplication of a similar service already provided by Schiess & Associates as discussed above. Staff recommends that the cost of $8,000 paid to ECIPDA be excluded from the rate base as shown on Attachment C, line 2.

Land Acquisition Cost

The land acquisition cost for Well No. 9 was $160,000. The lot was purchased by the Company from Rockwell Development, an affiliated company of Falls Water. In Order No. 30484 (Case No. FLS-W-07-01), the Commission said:

> We find there is substantial and competent evidence that the property for Well No. 9 was purchased from an affiliate Falls Water. For affiliate expense to be justified, the utility needs to provide compelling evidence of arm's length bargaining when incurring costs between the utility and affiliate. In addition, it appears that the water rights were acquired from a company affiliated with Falls Water's vice president.

Staff asked the Company to provide the necessary information to demonstrate the reasonableness of the lot purchase price because there appeared to be no arm's length negotiation that took place between Falls Water and its affiliated company. In response to Staff Production Request No. 28, the Company explained that it conducted a market analysis by comparing the sale price of the property obtained from Rockwell Development to sale prices of other real estate properties similar in size and zoning. The Company found that the price of the lot for Well No. 9 is within the sale values of other comparable properties. Staff reviewed the results of the market analysis conducted by the Company and believes that the price of the lot was reasonable.

However, Staff was informed by the Company that the lot was purchased with the dual intent of locating the well and as a future site for a water storage reservoir. The well and well house site plan provided to Staff by the Company shows a future site for a two million gallon water storage tank. Although there is no acreage specified for the reservoir site, it appears that only one-half of the lot is needed for the new well and the remainder is devoted to future storage. Therefore, Staff recommends only $80,000 of the purchase price be allocated to the cost of developing Well No. 9 and allowed in rate base (one-half of the total cost of $160,000) and the other half ($80,000) be booked as "Plant Held for Future Use." The Staff adjustment to remove $80,000 from Land is part of the adjustment shown on Attachment C, line 1.

Cost of Additional Water Rights

As a result of the engineering study conducted by Schiess & Associates in June 2004, it was found that water rights for the Company were deficient and that additional water rights were needed to serve existing peak demand during summer and to serve new subdivisions. Following the recommendations of the engineering study, the Company commenced the acquisition of additional water rights through application of new water rights/permits and purchase of existing water rights. Staff verified that the Company's new permit to appropriate water was approved on October 11, 2005. The Company must still submit proof of putting the water to beneficial use on or before October 1, 2010 to complete the licensing process.

Staff believes that it was necessary and prudent for the Company to increase its water rights by applying for new rights/permits and acquiring existing water rights from private parties. Staff notes the total water rights that the Company owns and purchased is 35.21 cfs (17.37 cfs under decreed rights/permit plus 17.84 cfs purchased from private parties). The 35.21 cfs of Company water rights currently exceeds the present flow rates for all Company well pumps totaling 20.28 cfs (9,100 gpm per Company response to Staff Production Request No. 38).

Two of the purchased water rights were acquired by the Company from Idaho Sod Farm, an affiliate company, for $492,000 (492 AF, $1,000/AF) and $750,000 (1,000 AF, $750/AF). Again, Staff asked the Company to provide information demonstrating the reasonableness of the costs for the purchase of the above water rights. The Company explained that unlike the real estate and rental markets, data regarding the sales of similar ground water rights is not readily available. Private sale prices of ground water rights are not recorded by the Idaho Department of Water Resources and the Company is unaware of other agencies where records could be obtained. The Company further contends that unlike surface water rights, ground water rights are not as frequently sold or rented. Surface water prices can be obtained from sales of shares in reservoirs. Staff attempted to research ground water rights sales data in Idaho for comparison but was unable to find any. Idaho is a non-disclosure state and it is difficult to get water rights sales data from public records. Some entities hire professionals (*e.g.*, WestWater Research, Inc., Boise and LeMoyne Realty and Appraisal, Inc., Twin Falls) that offer water rights evaluation and appraisal services and use the appraised value as a base for negotiating prices. The Company, however, did not use such services. Staff notes that performing an appraisal/evaluation of water rights by appropriate professionals would add to the total cost of water rights acquisitions.

Additional research conducted by Staff revealed that during the City of Shelley Council Meeting on March 10, 2009, Mr. Del Kunz, Idaho Water Company, responded to a question posed by Council Member John Lent concerning cost of water rights in the area. Idaho Water Company based in Eden, Idaho provides services for obtaining, selling or transferring water rights. Mr. Kunz explained to the Council that he bought, sold, and transferred water rights and he had water rights with early priority dates such as 1952 that might be beneficial to the city. He said usually the cost of water rights is $900 to $1,000 per acre-foot (AF). Given the location and early priority dates, Staff believes that the amount paid by the Company to Idaho Sod, Inc., is reasonable.

The Company also acquired water rights from Idaho Water Company (Water Rights Nos. 35-12915 and 35-13316) for $502,875 (1004 AF @ $500.8715 per AF). Staff believes that the price paid by the Company to Idaho Water Company is also reasonable.

Staff was apprised by the Company that all the water rights purchased by the Company as discussed above have not yet been officially transferred and approved by the Idaho Department of Water Resources. This means that the Company cannot use these water rights and pump water exceeding its decreed and permitted water rights of 17.37 cfs. Nevertheless, Staff believes advance purchase of water rights when available, with cost recovery, is justified given the risk of future ground water curtailment and the obligation of the Company to serve growing demand. Prior Commission decisions are also consistent with this approach:

> It is undisputed that United Water has experienced steady growth in the number of customers in recent years, and that demand for potable water is increasing. The only method available to the Company to increase its water supply is to obtain, strengthen and consolidate water rights in both surface and groundwater. We believe the Company has acted responsibly in taking action to increase its water rights, even if it has enough water to supply current demands. Accordingly, the Commission accepts the Company's water rights costs to be included in the rate base.

Order No. 29838

In the Response to Staff Production Request No. 3, the Company provided updated numbers for rate base. Included in the response was an actual amount expended for water rights of $306,192, rather than the estimated Pro Forma amount of $591,306 that was included in the Application. The Company has contracted for a total of $1,744,875 for the water rights, but has not completed the transactions. Staff reduces the rate base amount in Account 303 – Land and Land Rights by $285,114 to include only the actual amount expended for water rights. This adjustment to rate base does not have a corresponding depreciation adjustment as this account is not depreciated. This adjustment is included in the adjustment amount shown on Attachment C, line 1.

Meter Installations

The Company planned to purchase and proposes to include the cost for 300 new meters and 300 MXU transmitters in the rate base. The total estimated cost to complete the planned meter project is $85,536. The actual number of service meters installed as of October 31, 2009 was only 81 meters and 81 MXU's. The actual cost for purchasing 81 meters and 81MXU's, with