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BEFORE  THE  IDAHO  PUBLIC  UTILITIES  COMMISSION

IN THE MATTER OF THE APPLICATION)

OF FALLS WATER COMPANY, INC. FOR)CASE NO. FLS-W-97-1

AUTHORITY TO INCREASE ITS RATES)

AND CHARGES.)COMMENTS OF THE

 )COMMISSION STAFF

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COMES  NOW  the Staff of the Idaho Public Utilities Commission, by and through its attorney of record, Scott Woodbury, Deputy Attorney General, and in response to the Notices of Application and Modified Procedure in Case No. FLS-W-97-1, submits the following comments.

On May 19, 1997, Falls Water Company, Inc. (Falls Water, Company), an Idaho not for profit corporation and holder of Certificate of Public Convenience and Necessity No. 236 applied to the Idaho Public Utilities Commission for authorization to increase its charges for water service.

Falls Water requests authorization of a 34.9% increase in water rates as follows:

•Increase flat rate residential customer monthly charges from $8.80 plus $0.35 for DEQ fee to $11.65 plus $0.35 for DEQ fee for a total monthly rate of $12.00.

•Increase residential and commercial metered rates from $8.80 plus $0.35 (DEQ) for the first 40,000 gallons and $0.17 per thousand gallons in excess of 40,000 gallons to $11.65 plus $0.35 (DEQ) for the first 40,000 gallons and $0.30 per thousand gallons in excess of 40,000.

•Increase hook-up fees from $300 to $500.

•Institute a service charge for delinquent accounts in the amount of 1.5% per month with a $2 minimum.

Except for these changes, it is the Company’s intention that the tariffs on file with the Commission remain the same.

Staff’s comments on the Company’s Application are as follows:

REVENUE REQUIREMENT

Staff has reviewed the Company’s Application in this case and has conducted field audit work of the Company’s financial records.  Staff cannot support the revenue requested in the Company’s Application.  Based upon its analysis of the Company’s financial condition, Staff is willing to support an increase in the Company’s revenues of $31,133 (17.28%) to $38,994 (21.64%) as compared to the Company’s request for $62,922 (39.4%).  Attached to these comments is Exhibit No. 101 composed of three (3) financial schedules summarizing the results of the Staff’s analysis and audit.

Exhibit No. 101, Schedule A enumerates a number of exceptions to the way the Company has accounted for expenditures.  First, Staff has identified $10,695 of the Company’s reported operating expenses that are not properly chargeable to the water company operations.  Second, Staff takes exception to $17,127.76 of the Company’s reported operating expenses that should have been capitalized and recognized in the Company’s rate base.  Third, Staff has identified $8,988 of the Company’s reported plant in service accounts that should properly be included in the Company’s plant held for future use account.  Adjustments to the Company’s Application to recognize these exceptions requires adjustments to the Company’s reported depreciation expense and accumulated depreciation  accounts.

Exhibit No. 101, Schedule B presents the Company’s Results of Operations as filed by the Company and as adjusted by the Staff for the items detailed on Schedule A.  The Company reported a loss of $43,192 for the 1996 test year.  After making the adjustments proposed by Staff, the 1996 test year would still show a reported loss of $15,411.  Staff therefore believes that a rate increase is necessary to assure the viability of this Company.

Exhibit No. 101, Schedule C develops the Staff’salternative revenue increase amounts of $31,133 to $38,994.  These revenue increases represent increases of 17.28% to 21.64% of the revenues billed to customers in the 1996 test year and provide a return on rate base of 8% to 12%.  The capital structure of the Company for all practical purposes is composed entirely of owner’s equity and therefore is synonymous with rate base.  The Commission has for several years been using 12% as a reasonable return on equity for small water companies in recognition of the increased risk associated with a small customer base.  The Company’s Application included a return on rate base of 9.82% that was “backed into” from the Company’s desire to simplify the rate design and produce a return of 8% to 10% to provide a reserve to meet future improvements, repairs and replacements.

As a not-for-profit corporation, Falls Water cannot distribute earnings of the corporation to its shareholders.  Any profit realized from the operation must be used to either improve the water system or be held to meet unexpected repair and maintenance costs.  Despite its not-for-profit corporate status, Staff does not believe the Company will qualify for tax exemption under the Internal Revenue Code.  The Company filed a Federal corporate tax form 1120 and a State tax form 41 in 1996.  Staff has verified that the Company is not listed on the Internal Revenue Service’s list of exempt organizations.

Staff believes that the 8% return is adequate to build the reserve the Company desires and agrees that such a reserve is appropriate for this company.  The 12% benchmark return used by the Commission for profit making water companies would build the reserve faster and could provide funds for implementing a program to install meters for currently unmetered customers as discussed below under “Monthly Usage Allowance.”  Even with the 12% return, the revenue per customer required would still be among the lowest rates of any regulated water utility in Idaho.

MONTHLY USAGE ALLOWANCE

The Company’s current rate design for metered customers provides a monthly usage allowance of 40,000 gallons per month.  All usage below this amount is billed at a base rate, while usage above this amount is billed at a gallonage-based commodity rate.  Unmetered customers pay the same base rate as metered customers.

The monthly allowance of 40,000 gallons is very high compared to other regulated water companies in Idaho.  It is the highest allowance of any regulated company in the state, and is nearly four times the average monthly allowance of all other water companies.  Staff understands that the Company desires to have a high allowance so that its rate design functions as a flat rate most of the time.  With a high allowance, only those customers with very high usage will pay more than the base rate.  The 40,000 gallon/month allowance for metered customers appears to have been established to recognize consumption levels possible by small unmetered customers.

Staff has two objections to the Company’s 40,000 gal/month usage allowance.  First, such a high allowance creates a huge first block of customers who pay a base rate, and a very small second block who pay an additional amount for usage exceeding 40,000 gal/month.  With such a large first customer block, there is no distinction between minimal users and considerably heavier users.  For example, a customer who uses 4000 gal/month (a reasonable usage with no lawn watering) would be billed the same amount as a customer who uses 40,000 gal/month (a reasonable usage with lawn watering).  Staff’s analysis shows that during the course of the entire year, 88% of the monthly customer bills are billed at the minimum base rate for usage below the monthly allowance.  The remaining bills include the base charge plus a commodity charge for usage above the allowance.

Staff’s second objection is that little revenue is generated through sales billed at the commodity rate.  Few sales are billed at the commodity rate; furthermore, the commodity rate is so low that very little revenue is generated by those few sales.  The Company’s monthly revenues vary little from month to month, as shown in Exhibit No. 102.  Monthly revenues are higher in the metered summer months, but only by a small amount.  The portion of the Company’s annual revenue attributable to commodity rate sales for usage above 40,000 gal/month is approximately $13,300.  This represents less than 8% of the total annual revenue.  In fact, it is so low that it barely exceeds the Company’s annual metering cost.  The  portion of the Company’s revenue requirement attributable to metering, as estimated by Staff, is $10,400.  This includes meter reading labor costs, meter depreciation costs, and return on investment grossed up for taxes.

Staff recommends that the monthly usage allowance be reduced from 40,000 gal/month to 20,000 gal/month.  This would reduce the size of the customer block paying only the base rate, and would more fairly balance the revenue responsibility between small unmetered customers and larger metered customers.  This allowance, Staff believes, would still be high enough to not normally be exceeded by unmetered customers, but would be low enough that heavier users would pick up a greater share of the revenue requirement.  Staff analysis, as shown in Exhibit No. 103, indicates that metered customers’ usage exceeds 40,000 gal/month less than half of the time, even in the summer.  Unmetered customers, because of their small lot sizes, are even less likely to exceed this amount.  With an allowance of 20,000 gal/month, approximately 78% of the metered customers in the summer would pay more than the base rate as shown by

Exhibit No. 103.  This allowance, if reduced to 20,000 gal/month, would still be the second highest of the water companies regulated by the Commission.

A lower monthly allowance would also generate more revenue through commodity rate sales, further helping to justify the costs of metering.  Staff believes that one purpose of metering is to allocate costs more fairly between customers.  However, unless the extra revenue generated by metered sales exceeds the costs of metering, there is effectively no real difference in the net revenue from metered and unmetered customers.

Staff believes that the Company can more effectively utilize the meters it now has installed by lowering the monthly allowance and by implementing a more effective rate design that features a higher commodity rate.  Metering could be made still more effective if all customers were metered.  However, system-wide metering would not be recommended if current metered rates remain in place.

RATE DESIGN

There are an infinite number of combinations of base rates and commodity rates that could satisfy the Company’s revenue requirement.  The base and commodity rates however, are dependent on the monthly allowance.  Exhibit No. 104 illustrates, for specified monthly allowances, various combinations of base and commodity rates that would meet the Company’s revenue requirement with a 12% return.  The Company’s current rates are indicated on the exhibit, as are their proposed rates.

The Company’s proposed rate design, despite exceeding their revenue requirement as adjusted by Staff, has other weaknesses as well.  Aside from the monthly allowance which Staff believes is too high, the proposed rate design would recover the vast majority of revenue from base rate charges, and only a very small amount from commodity rate charges.  At the Company’s proposed rates, approximately 92% of annual revenues would come from base rate charges, while only 8% would come from commodity charges.  Since a substantial portion of the Company’s expenses are directly related to the quantity of water sold, Staff believes a greater portion of revenue should be recovered through commodity charges.

Staff proposes a rate design with only slightly higher base rate charges, but with a significantly higher commodity rate.  If the Commission chooses to lower the monthly allowance to 20,000, then Staff recommends a base rate of $10 per month and a commodity rate of $0.30 per thousand gallons.  These rates would achieve Staff’s recommended revenue requirement allowing for a 12% return.  This would represent an increase of 9% in the base rate, and an increase of 76% in the commodity rate.  This rate design recovers approximately 15% of the revenue requirement through commodity sales and 85% through base rates.  The Company’s monthly revenue stream would change as shown in Exhibit No. 105.  Greater revenue would be collected in the summer months, but these are also the months when expenses are higher due to labor, maintenance and repair, meter reading, and pumping costs.  Customers’ monthly bills under current rates, the Company’s proposed rates, and Staff’s proposed rates are presented in Exhibit No. 106 for various levels of monthly consumption.

  If the Commission chooses not to lower the monthly usage allowance, then Staff recommends the base rate be set at $10 per month, and the commodity rate be set at $0.52 per thousand gallons.  If the Commission chooses to abandon metering and charge all customers a flat monthly rate, then a rate of $11.78 per month would achieve the Company’s revenue requirement as recommended by Staff.

TARIFF REVISIONS

A review of the Company’s billing records for 1996 reveals that two large commercial customers are billed every month based upon meter readings by the Company.  All other customers, both residential and commercial, are billed a flat rate in all except the summer months of May through September.  The recorded usage of these two customers, one a car wash and the other a laundromat, far exceeds that of any other customers; consequently, Staff believes it is reasonable to bill these two customers monthly based on their recorded usage.  However, Staff recommends that the Company’s tariff be amended to reflect actual billing practice.  Staff suggests tariffs be revised to state that customers with monthly usage exceeding 100,000 gallons (or some other amount suggested by the Company) be assessed charges every month of the year based on actual recorded usage.

Four additional customers are billed monthly in multiples of the base rate.  For example, a 40-unit apartment building is billed an amount 40 times the base rate.  A mobile home park is billed an amount based upon the number of spaces filled during the month.  Two churches are billed based on the number of congregations that meet at each church.  None of these four customers are metered.  Staff recommends that the apartment building and the mobile home park be treated consistently.  Billing the apartment building based on the total number of units, occupied or not, while billing the mobile home park based on the number of occupied units is inconsistent.  Ideally, Staff would prefer that customers of this type be billed based on actual occupancy in each month.  This may be impractical, however, since the Company would have to keep track of occupancy rates, and prorate for partial month occupancy.  As an acceptable alternative, Staff recommends that both customers be billed based on the total number of units, and that tariffs be amended to state this treatment.

With regard to the two churches, Staff sees no reasonable rationale for the Company’s current billing practice.  Both presumably exceed a lot size of 6000 sq.ft., thus cannot qualify for a flat rate according to the Company’s tariffs.  If the churches have much turf to irrigate, their water requirements in the summer could be very substantial.  Because expected usage by the churches is unknown, Staff recommends that these two customers be metered and billed accordingly.  In those months when meters are not read, Staff recommends that a fair flat rate be established based upon  usage measured during a non-summer test period.

HOOKUP FEES

Staff has no objection to the Company’s proposal to increase its hookup fees from $300 to $500.  The Company has provided no basis for the increase, other than the proposed rate is more in line with the fees charged by nearby municipal water systems.  Staff however, believes that the proposed fee of $500 fairly represents today’s costs of installing a meter, meter base, and stub-out from the main line.  Cost estimates prepared by United Water Idaho, Inc. in 1995 show the cost of these items to be approximately $425.  Allowing for two years of inflation, a proposed hookup fee of $500 seems reasonable.

METER READING

The Company provided billing data for the test year in response to Staff production requests.  Examination of the data, along with corrections to the data as made by the Company, shows a fairly high rate of metering errors.  Over the course of the five-month metering season, approximately 6% of the recorded meter readings have been corrected by the Company.  In some months the error rate is nearly 8%.  Staff is uncertain about whether the errors are due to mechanical or human error; nonetheless, Staff believes this error rate is too high.  Staff recommends the Company be directed to work to improve the accuracy of its metering.  Metering errors inevitably lead to loss of revenue by the Company because the Company resorts to billing customers only the base rate in the event of metering errors or billing disputes.

In cases of mechanical metering errors, the Company is responsible for the maintenance of its metering equipment.  Meters are considered to be sufficiently accurate if tests indicate the accuracy is within plus or minus two percent of 100 percent accuracy.  If the meter is malfunctioning, it should be repaired or replaced at no cost to the customer.  Water bills should be adjusted as described in Rule 204 of the Utility Customer Relation Rules.  If a meter fails to register correctly, or loss of water occurs due to a leak on the customer’s service line, a measurement used for billing can be estimated on the basis of available data.  When a customer disputes a high billing, the Company should arrange to re-read the meter and make the necessary adjustments to the customer’s bill to reflect the correct meter reading.

DELINQUENT PAYMENT CHARGES

The Company is proposing a service charge for delinquent accounts in the amount of one and one-half percent (1.5%) per month on the unpaid balance with a $2.00 minimum late fee.  Staff finds the Company’s late fees to be excessive.

In response to Staff Production Request No. 12, the Company states that on    June 1, 1997, 54% of its delinquent accounts were more than 90 days past due, 10% were 60 to 89 days past due, and 36% were 30 to 59 days past due.  Having over half of those customers with delinquent accounts over 90 days past due is an unacceptable situation for the Company.  Late fees and interest charges, however, will not necessarily resolve the Company’s collection difficulties.  Late fees only increase the total amount the customer must pay and add to the financial burden of customers who may already be unable to pay their bills on time.  The Company should apply the Utility Consumer Rules and Regulations (UCRR) No. 302 to remedy its problems.  Customers wishing to avoid disconnection may make payment arrangements with the Company pursuant to UCRR No. 313.  However, they should not be allowed to postpone payment indefinitely.

The Commission has allowed collection of interest on unpaid balances in excess of 30 days in particular circumstances.  In the past, the Commission has approved a one percent (1%) interest fee for some regulated electric and water utilities.  Consideration is given to utilities that are unable to disconnect services during the winter months or to water companies that are not metered and fail to have shut-off valves.  Falls Water has individual shut-off valves on each metered and non-metered service connection, so there are no impediments to disconnecting service.

On a typical $20 past due amount, the proposed $2.00 minimum charge would equate to 10% per month, an effective annual rate of 120%.  If the Commission believes that the circumstances of the Company’s collection of payments warrants a late payment charge, Staff recommends that more a reasonable rate of 1% per month (12% annual) be adopted.

DATED at Boise, Idaho, this             day of July 1997.

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