DECISION MEMORANDUM

TO:COMMISSIONER NELSON

COMMISSIONER SMITH

COMMISSIONER HANSEN

MYRNA WALTERS

TONYA CLARK

DON HOWELL

STEPHANIE MILLER

DAVE SCHUNKE

MADONNA FAUNCE

DON OLIASON

GARY RICHARDSON

WORKING FILE

FROM:SCOTT WOODBURY

DATE:AUGUST 21, 1996

RE:CASE NOS.  UWI-W-96-1/WSM-W-96-1

SALE/PURCHASE WARM SPRINGS MESA WATER SYSTEM

On March 28, 1996, United Water Idaho Inc. (UWI, United Water) and Warm Springs Mesa, Inc. (WSM, Warm Springs) collectively referred to as “Applicants,” filed an Application with the Idaho Public Utilities Commission (Commission) for an order approving the sale and transfer to United Water of Warm Springs’ water service properties located in Ada County, Idaho.  UWI also requests approval of certain related rate and ratemaking matters.

United Water is a public utility providing water service to more than 54,500 customers in Ada County, Idaho.  United Water is a regulated utility operating under Certificate of Public Convenience and Necessity No. 143 (as amended).  UWI is a subsidiary of United Water Works Inc., a Delaware corporation.

Warm Springs is a public utility providing metered water service to approximately 325 customers in and around Warm Springs Mesa subdivision in Ada County, Idaho.  Warm Springs is a regulated utility operating under Certificate of Public Convenience and Necessity No. 264 (as amended).

United Water, Warm Springs and J. H. Wise & Sons, Inc., an Idaho corporation (“Wise”) have negotiated and executed an Agreement for Purchase and Sale (Agreement) dated March 27, 1996 whereby Warm Springs and Wise will sell and transfer to United Water real property and water works facilities used in furnishing water service to the public in and around the Warm Springs Mesa subdivision.

The purchase price to be paid by United Water for all the land, improvements, personalty and intangible property used and useful in the furnishing of water service by Warm Springs is $550,000.  As per the stipulated results of Staff audit (Tr. p. 108 Staff; Tr. pp. 24, 42 UWI concurs), the purchase price consists of the following components and related valuation:

Depreciated cost of property (rate base)$277,248

Well No. 3    147,300

Land         63,150

Acquisition Adjustment    62,302

TOTAL$550,000

The purchase price by terms of the Agreement may be adjusted to reflect additional depreciation in the event regulatory approval is not received within six months of the Agreement date.

United Water proposes to provide water to Warm Springs customers at United Water’s approved tariff rates and in accordance with United Water’s rules and regulations governing the rendering of water service.  The average total bill of Warm Springs customers is not expected to be significantly different.

Although not required in the underlying Agreement, United Water proposes not to charge connection or hookup fees for new service in the Warms Springs area unless and until the Warm Springs system is interconnected to the United Water distribution system.  As reflected in the accompanying testimony there are approximately 215 undeveloped lots in the Warm Springs area.

Warm Springs states that it desires to convey its water company to United Water because it is unwilling to undertake the perceived risks of continued operations arising from increasingly stringent water quality regulations, increasingly complex utility regulation, and increasingly complex operational and technical requirements.  Because of its small size Warm Springs states that it has experienced, and in the absence of this sale, would continue to experience, difficulties in maintaining its system and in obtaining adequate financing for operations, maintenance and expansion.  Tr. pp. 49, 50.

United Water maintains that it possesses the technical, managerial and financial abilities to provide reliable and adequate service (e.g., engineering; hydrology; utility management; utility accounting; customer service; computer systems; water production, treatment & testing; and distribution system operation), and accordingly contends that the proposed transfer is in the public interest.  Tr. pp. 11, 12.

The Applicants request an order of the Commission:

1.Approving the sale of Warm Springs assets to United Water;

2.Confirming the right of United Water to include in rate base and future rate proceedings the net full purchase price of the assets subject to this transaction, and to recover reasonable costs of acquisition;

3.Confirming the right of United Water to provide water service in the area now served by Warm Springs at United Water’s currently and hereafter approved tariff rates with the exception of connection fees;

4.Confirming the right of Warm Springs to abandon service, cancellation of Warm Springs’ Certificate of Convenience and Necessity and amendment of United Water’s Certificate of Convenience and Necessity; and

5.Granting such other and further relief as the Commission deems appropriate.

The Application filed in Case Nos. UWI-W-96-1 and WSM-W-96-1 is accompanied by a service area map of United Water with boundary descriptions, the United Water/Warm Springs/Wise Agreement for Purchase and Sale, and the prefiled testimony of United Water.

Public hearing in Case Nos. UWI-W-96-1/WSM-W-96-1 was held in Boise, Idaho on July 16, 1996.  The following parties appeared and participated by and through their respective counsel:

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| United Water Idaho, Inc.  Warm Springs Mesa, Inc.  Commission Staff | Dean J.  Miller  Peter Boyd  Scott D. Woodbury |

Public testimony was taken in an evening hearing on the same date.

United Water and Warm Springs Mesa have presented for Commission approval an Agreement for the purchase and sale of the Warm Springs water system.  The purchase price is $550,000.  United Water agrees with the results of Staff audit and Staff’s valuation of the various components of the purchase price.  Tr. p. 24.  United Water also agrees with Staff’s description of the Warm Springs Mesa system.  Tr. p. 22.  Although Staff recommends approval of the transfer, Staff recommends that rate base decisions be deferred until the Company’s next rate case and that all UWI tariffs be implemented immediately, including UWI’s hookup fees for new connections.  The positions of the parties on the issues of difference can be described as follows:

Financial Considerations of the Agreement

United Water has approximately 54,500 customers.  The Company’s estimated 1995 year-end rate base stated in its current rate application (Case No. UWI-W-96-3) is $74,591,966.  Based on information furnished in this case, the Company’s estimated average rate base per customer is $1,346.00.  Tr. p. 35.

Warm Springs Mesa has approximately 325 customers.  Pursuant to Staff’s calculation,  the Warm Springs estimated average rate base per customer is $1,332.00 (w/o Well No. 3) and $1,692 (w/Well No. 3).  Tr. pp. 35, 81.

UWI estimates that in addition to the $550,000 cash purchase price, the Company will also incur the following costs ($53,000) for which it requests rate base treatment:

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| --- | --- |
| Telemetry (SCADA)  Meter box/meter setting modifications  Wells, pressure regulation vaults,        booster station modifications | $16,000  18,000  19,000 |

Tr. pp. 19, 20.

Staff agrees that plant and equipment should be brought up to reasonable construction standards and that unsafe conditions should be corrected.  Staff contends, however, that capitalization is perhaps only appropriate where the life of the facilities is extended, and must otherwise be expensed.  Tr. pp. 38, 39, 83.  Staff notes that the capacity of the Toluka booster station may also have to be increased in three to five years.  This is the type of investment, Staff states, that would normally be offset by connection fees.  Tr. p. 84.

Staff calculates that with Well No. 3 and the acquisition adjustment in rate base, UWI for the WSM system will have an annual revenue requirement of $114,852.  With the existing customer base (325 customers) UWI will realize an estimated revenue deficiency of $17,353.  Collecting or imputing hookup fees will reduce the revenue deficiency.  Tr. pp. 108, 109.  Deferring a rate base decision until a rate case will allow things to come in balance, e.g., additional revenue from new customers and depreciated investment.

Staff contends that the Warm Springs system should be accounted for in a manner that would allow all rate base, revenues and expenses, including allocated expenses, to be analyzed in a rate case.  This could be accomplished, Staff states, by using separate subaccounts, which could be later collapsed.  Tr. pp. 78, 110.  Regarding separate subaccounts, the Company contends that it is not necessary, justifiable or reasonable to keep separate books and records.  Tr. pp. 22, 23, 39, 40.  The Company contends through its counsel that it will be able to provide information with respect to this transaction within the context of its current accounting practices and as similarly ordered by the Commission in Case Nos. EUW-W-94-1 and UWI-W-95-2.  Tr. p. 130.

United Water assures the Commission that it is the Company’s intent by this purchase to hold existing customers harmless and to avoid any related subsidization by the Company’s existing customers.  The issue of subsidization it cautions, however, needs to be approached very carefully.  Tr. pp. 41, 42.

Acquisition Adjustment

As computed by Staff, the acquisition adjustment related to the purchase of the WSM water system by UWI is $62,302.  The figure represents the difference between WSM original cost of assets less depreciation and UWI purchase price.  Tr. p. 107.  Staff recommends that the amount be booked above the line with amortization beginning now.  Rate basing, Staff suggests, would occur later if Mesa customers are recovering their revenue requirement and if “quantifiable benefit” is demonstrated.  Tr. pp. 25, 26.

Hookup Fees

Hookup fees are assessed by UWI to recover system costs related to source of supply, storage and booster facilities.  Tr. pp. 45,78.  UWI recommends waiver of connection fees “until such time as new source of supply is required or until the two systems are connected.”  The current UWI hookup charge for standard residential meters is $465.  Tr. p. 37.  The Company justifies its waiver proposal based on its assessment that new customers on the Mesa (215 lots) won’t impose growth costs on the UWI system.  Tr. pp. 15, 16.  Noting that UWI rates and charges are based on average system costs and that the amount collected reduces rate base, Staff contends that all UWI customers would end up paying for any non-collection in their rates.  Staff recommends that all aspects of UWI’s tariffs, including hookup fees be implemented when UWI assumes ownership.  Tr. pp. 37, 78.  As further rationale for its position, Staff notes the statutory prohibition against unreasonable discrimination and preference.  (Idaho Code 61-315) Tr. pp. 78, 128, 129.  Should hookup fees not be collected by UWI, Staff recommends to avoid subsidization by existing customers, that the hookup fees be imputed in the Company’s next general rate case.  Tr. pp. 111, 124.

As an alternative, in the event the Commission disagrees with UWI’s primary proposal, United Water recommends that the 24 lots currently under construction be exempt from connection fees (anticipating that water facilities will be installed prior to closing); and that all lots connected from the date of closing be subject to connection fees.  Tr. pp. 27, 28.

Warm Springs maintains that waiving the connection fee until the WSM system is interconnected with the UWI system was part of the negotiated purchase price of $550,000.  Warm Springs therefore opposes the assessment and collection of any such fees.  Tr. pp. 62, 64.  Forgiveness of same, Warm Springs suggests, should perhaps be considered by the Commission as additional acquisition adjustment.

Well No. 3

The WSM system is comprised of three wells, the Toluka booster station (600 gpm), the Boulder Heights Reservoir (629,000 gal.), and the Boulder Heights Booster Station (300 gpm).  Tr. pp. 75, 76.  The total capacity of the three wells by WSM estimation is 1,195 gpm ((1) 125, (2) 400, (3) 670); by UWI estimation, 950 gpm.  Tr. pp. 75, 76.  Assuming a peak demand of 1.7 gpm/customer, Staff calculates that the three wells have sufficient capacity to handle existing (325 customers) and foreseeable customer growth (215), i.e., 918 gpm.  Staff Tr. pp. 76, 77; WSM Tr. p. 64; UWI Tr. 34.

Well No. 3 is not currently in WSM rate base.  United Water contends that Well No. 3 is currently “used and useful” and should be included in rate base.  Tr. p. 26.  Well No. 3, the Company contends, provides a redundant supply to Well Nos. 1 and 2, as is required by DEQ and by IDAPA 16.01.08.550.02.0.  Tr. pp. 27, 44.  Without Well No. 3, the Company contends, the system is marginally deficient.  Tr. p. 26.  Testimony also reflected that the pump in Well No. 2 is defective (producing only 150-190 gpm) and needs to be replaced.  Tr. pp. 54, 55, 66, 67.  Warm Springs has committed to replace the pump at no additional cost to United Water.  Tr. p. 70.

Staff recommends that the “used and useful” determination regarding rate base be delayed until the Company’s next rate case.  Tr. pp. 26, 83.  If a determination must be made now, Staff contends that Well No. 3 investment must be allocated between existing customers and future customers.  Exh. 104.  The ramifications of a generic determination of “used and useful” are different vis-á-vi WSM, an owner/developer system, and UWI.  The Company asks that UWI not be required to make a further showing of some unknown benefit at some time in the future.  Tr. p. 130.

Commission Decision

∙Should the sale of Warm Springs assets to United Water by WSM be approved?

∙re: Sale/Purchase Agreement

Stated purchase price    $550,000

Depreciated cost of property $277,248

Well No. 3    147,300

Land      63,150

Acquisition adjustment 62,302

Additional investment costs

Telemetry16,000

Meter modifications18,000

Wells, pressure regulation

vaults booster station

modifications19,000

∙re: rate base

Well No. 3       “Used and useful” determination—timing—now?  later?

Acquisition adjustment —demonstrated benefits?

Additional investment costs—capitalize vs. expense

∙re: hookup feeswaive vs.  collect vs. impute?

∙“hold harmless”

Estimated revenue deficiency$17,353

—collecting or imputing hookup fees will reduce rev. deficiency

Rate base per customer

UWI— $1346

WSM—$1332 (w/o Well No. 3)

             $1692 (w/Well No. 3)

∙re: tariffs/rates

∙re: meters—UWI recommends billing according to UWI tariffs—converted from hundreds of cubic feet to 1,000's of gal (Tr. pp. 14, 36).

∙Certificate of C&N—

cancel WSM

amend UWI

Scott Woodbury

vld/M:UWIW961.sw2