

DW 99-057

HAMPTON WATER WORKS COMPANY

Petition for Rate Increase

Order Approving Settlement Agreement

O R D E R N O. 23,412

February 28, 2000

APPEARANCES: Ransmeier & Spellman, P.C. by Timothy S. Britain, Esq. for Hampton Water Works Co.; Shaines & McEachern, P.A. by John H. McEachern, Esq. for Town of Hampton; Casassa and Ryan by John J. Ryan, Esq. for Town of North Hampton; Henry Fuller for Town of North Hampton Water Commission; and Donald M. Kreis, Esq. for the Staff of the New Hampshire Public Utilities Commission.

I. PROCEDURAL HISTORY

On May 19, 1999, Hampton Water Works Company (Company) filed a petition for an increase in annual revenue of approximately \$978,500, representing a total annual increase of 28.9 percent. By Order No. 23,236 (June 17, 1999), the Commission suspended the proposed rates and scheduled a prehearing conference. At the prehearing conference, conducted on July 15, 1999, the Commission granted petitions to intervene filed by the Town of Hampton (Hampton), the Town of North Hampton (North Hampton) and the Town of North Hampton Water Commission (Water Commission). By Order No. 23,281 (August 12, 1999), the Commission issued its report of the prehearing conference and approved the procedural schedule as proposed by Staff and the parties.

The Commission conducted a hearing on temporary rates on August 4, 1999 and subsequently issued Order No. 23,294 (August 30, 1999) approving a proposed stipulation presented by the parties and Staff concerning temporary rates. The stipulation provided for setting temporary rates at their then-current level, effective with service rendered on or after August 4, 1999. The stipulation, as approved, expressly noted the Commission's authority to conduct a reconciliation of rates at the conclusion of the proceeding in the event the permanent rates ultimately determined by the Commission differ from the approved temporary rates.

The Commission convened a public hearing in Hampton on September 28, 1999 at which time numerous customers provided comment on the proposed rate increase. Thereafter, the parties and Staff conducted discovery and, on January 5 and 6, 2000, met for settlement discussions. These discussions yielded a comprehensive Settlement Agreement, which was subsequently reduced to writing and filed with the Commission on January 21, 2000. The Company also filed a letter dated February 4, 2000 requesting rate recovery of \$183,063.41 in rate case expenses pursuant to the terms of the Settlement Agreement.

The Commission conducted a hearing on February 8,

2000 at which time Rod P. Nevirauskas, director of rates and revenues for American Water Works Service Company, an affiliate of Hampton Water Works, testified in support of the Settlement Agreement.

II. SETTLEMENT AGREEMENT

The proposed Settlement Agreement is intended to resolve all outstanding issues in the Company's rate case filing.

It provides for a revenue requirement of \$3,931,918, representing an annual increase of \$544,593 effective on March 1, 2000. Under the proposal, which calls for the Company to continue charging rates that are a combination of metered and non-metered charges, residential rates would increase by 15.67 percent and commercial rates by 15.54 percent. Public fire protection rates would rise by 13.05 percent and private fire protection rates by 18.37 percent. Seasonal residential customers would see their rates increase by 34.89 percent and rates for seasonal commercial customers would increase by 23.94 percent.

The Settlement Agreement provides for a rate of return of 8.81 percent. The Company's capital structure consists of 57.52 percent debt with a cost of 8.37 under the Agreement, 1.46 percent preferred stock with a cost of 6.75

percent and 41.02 percent common equity with a cost of 9.50 percent.

Under the Agreement, this 8.81 percent rate of return would be applied to a stipulated rate base of \$12,933,422. The proposed rate base includes \$856,291 in unamortized balances of deferred expenses, which under the terms of the Agreement consist almost entirely of expenses related to tank painting, the preparation of depreciation and cost of service studies and amortization of office leasehold improvements. The Company's original filing had called for including an additional unamortized balance of \$320,079 in rate base, in connection with the Company's effort to develop the so-called Hobbs Well in North Hampton, also referred to in the rate filing as Well No. 15. The Company sought to develop this well as a source of needed water supply, but abandoned the effort in the face of local opposition to the project given the well's proximity to a landfill. In order to reach a compromise, Staff and the parties agreed to include \$157,649 of Hobbs Well development costs in rate base, thus disallowing more than half of the Company's expenses relating to this failed project.

The proposed rate base includes \$1,672,719 to reflect the Company's annualized investment in three recently

developed wells: Nos. 17, 18 and 19, which were placed in service in December 1998, and \$380,000 to cover mains that were installed as tie-ins to the new wells. The mains were placed into service as of June 30, 1999. Although these adjustments were beyond the test year, the parties agreed to include them in rate base rather than trigger what would almost certainly have been an immediate request by the Company for an additional rate increase to account for the earnings deficiency caused by the new plant-in-service.

The Company's Operation and Maintenance expenses were \$1,591,186 during the test year, which ended on December 31, 1998. The Company had proposed \$112,958 in pro forma adjustments to its test year figures. The Settlement Agreement calls for a pro forma amount of (\$3,127). The difference was due, primarily, to the capitalization of certain expenses (\$56,088). Over \$21,000 in expenses were properly allocated to the Salisbury Water Company, an affiliate with which the Company shares certain costs, and the Settlement Agreement also corrects an error of almost \$14,000 in the computation of the Company's insurance expenses and approximately \$27,000 in non-recurring expenses. The Company's original proposal included a pro forma adjustment of \$31,530 to reflect amortized expenses associated with the

Hobbs Well, based on a ten-year amortization period. The parties and Staff agreed to delete the amortization of this expense from the Company's operations and maintenance budget for the reasons described above.

Staff and the parties agreed that the depreciation rates for service lives of the Company's plant and equipment, as set forth in the Company's depreciation study, are reasonable. There was a downward adjustment of \$30,144 to the Company's proposed annual depreciation expense of \$275,373.

It was further agreed among the parties and Staff that a temporary rate surcharge, effective on March 1, 2000, will apply over a twelve-month period to allow the Company to recover the revenue deficiency created by the difference between the permanent and temporary rates as of August 4, 1999. The Settlement Agreement also calls for a step increase to cover costs associated with the Company's Route 1-Lafayette Road Reconstruction Project and its so-called Chemical Feed Project. This increase would become effective on March 1, 2001, to coincide with the end of the rate-reconciliation surcharge.

Finally, the Settlement Agreement calls for recovery of rate-case expenses through a surcharge to be effective for the two years commencing with the effective date of the new

permanent rates at issue in this proceeding. The amount of rate case expenses is not fixed by the Settlement Agreement and, as noted above, on February 4, 1999 the Company submitted an itemization requesting recovery of \$183,063.41. Staff determined that the Company submitted this itemization without sufficient documentation; the Company is still in the process of responding to Staff's requests for additional information.

III. COMMISSION ANALYSIS

Having considered the Settlement Agreement and the testimony offered in support of it, we conclude that the proposed resolution of this case is for the public good and we will approve it.

In particular, we believe the parties' compromise on the highly contentious issue of the Hobbs Well is an appropriate and reasonable resolution of the issues related to that project. This is a water company that continues to experience a significant supply deficit. It is thus necessary for the Company to pursue an aggressive effort to identify and develop new sources of water, along with exploration of options for assisting customers to make more efficient use of current water resources. However, as is implicit in the Settlement Agreement, even in the face of such pressing needs the Company should have determined earlier than it did that

expenses related to Hobbs Well were not going to lead to a successful addition of new supply to the Hampton Water Works system.

We additionally note that the rate design contained in the Settlement Agreement is consistent with the Company's cost-of-service study. The Company's original proposal had called for residential and commercial rates in excess of the service costs associated with these customers in order to permit the Company to recover costs associated with public fire protection service. Under the Settlement Agreement, all these rates are adjusted to reflect the actual cost of service for each customer class. We believe this resolution to be in the public interest.

With regard to rate case expenses, the Settlement Agreement provides for a two-year recovery period that "shall become effective with the new rates approved in this proceeding." It is of concern that Staff and the Company have not been able to complete the necessary discussions and exchanges of information so as to allow Staff to make a recommendation on the level of rate case expenses that is appropriate in this case. We further note that the requested sum of \$183,063.41 represents an unusually high figure for a proceeding that was resolved by agreement. However, because

we have determined that the Settlement Agreement is consistent with the public good, and because the Settlement Agreement at least implicitly contemplates that the two-year recovery period for rate case expenses would coincide with the first two years of the new rates, we will permit the Company to implement a tariff reflecting its full request. We will then issue a subsequent order making a final determination of the Company's approved rate case expenses, at which time it will be necessary for the Company to reconcile the surcharge accordingly.

Based upon the foregoing, it is hereby

ORDERED, that the Settlement Agreement entered into among the Parties and Staff, and the rates described therein are approved; and it is

FURTHER ORDERED, that the Company submit a properly annotated compliance tariff with the Commission on or before March 1, 2000; and it is

FURTHER ORDERED, that the two-year surcharge for rate case expenses, as contemplated by the Settlement Agreement, be subject to revision and reconciliation upon the completion of Staff's review of the Company's itemization of rate case expenses.

By order of the Public Utilities Commission of New
Hampshire this twenty-eighth day of February, 2000.

Douglas L. Patch
Chairman

Susan S. Geiger
Commissioner

Nancy Brockway
Commissioner

Attested by:

Thomas B. Getz
Executive Director and Secretary