

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: PAWTUCKET WATER SUPPLY :
BOARD GENERAL RATE FILING : DOCKET NO. 3497

REPORT AND ORDER

I. Background

On February 28, 2003, Pawtucket Water Supply Board (“PWSB”), a non-investor owned utility, filed with the Public Utilities Commission (“Commission”) an application for a general rate increase for effect April 1, 2003, pursuant to R.I.G.L. § 39-3-11. PWSB requested a total revenue increase of 27.3%, to collect an additional \$3,157,389 for operating revenues, for a total revenue requirement of \$14,708,719. The Commission suspended the effective date of PWSB’s requested rate increase in order to conduct a full investigation and to hold public hearings.

The instant general rate case filing represents PWSB’s fifth such filing in the last ten years. The following table provides a brief history:

Docket No.	Filing Date	Amount Requested	Amount Allowed
2158	12/7/93	\$1,460,486	\$ 624,876
2674	1/9/98	\$3,634,020	\$ 614,430
3164	6/30/00	\$2,289,601	\$1,820,799
3378	8/20/01	\$3,828,966	\$2,732,584

On April 14, 2003, PWSB filed a Motion and Memorandum for Interim Relief. Specifically, PWSB requested the Commission allow PWSB to utilize \$359,700 of the funds currently collected in its restricted Infrastructure Replacement Account (“IFR”) to undertake projects more appropriately classified as Operation and Maintenance (“O&M”)

expenses. On May 8, 2003, following a hearing, the Commission rendered a Bench decision approving PWSB's Motion to utilize IFR funds for certain O&M projects as filed.¹

II. PWSB's Pre-filed Direct Testimony

In support of its filing, PWSB submitted the pre-filed direct testimony of Pamela M. Marchand, P.E., PWSB's Chief Engineer, David G. Bebyn, a Consulting Department Supervisor with Bacon & Edge, P.C., Christopher P.N. Woodcock, President of Woodcock & Associates, Maureen Gurghigian, Senior Vice President at First Southwest Company, and Anthony Simeone, Executive Director of the CWFA.

Ms. Marchand testified that the request for a rate increase is designed to cover expenses related to the delay in construction of new water treatment facilities, unanticipated expenses and operations and maintenance ("O&M") expenses. Ms. Marchand indicated that PWSB must continue to operate the existing water treatment plant until the issues surrounding the construction of the new water treatment plant are resolved.²

According to Ms. Marchand, of the 28% requested increase, 15.7% is attributable to the delays associated with building the new treatment plant, 8.6% is to fund increases in taxes, medical insurance, property insurance and labor contract increases, 7% is to

¹ Order No. 17466 (issued May 21, 2003). The Commission specifically found that the circumstances surrounding the need for PWSB's request were caused by reasonably recent unforeseen events and that the unforeseen events were not caused by an error committed by PWSB. Furthermore, the Commission found that a denial of the interim relief "will interfere with the accommodation, convenience and welfare of the people." Finally, the Commission found, based upon the testimony of Ms. Marchand and Mr. Bell, that there was not a need to order an emergency interim rate increase.

² PWSB Exhibit 1 (Direct Pre-filed Testimony of Pamela M. Marchand), pp. 2-3. On April 23, 2003, the Pawtucket City Council reconsidered its decision not to ratify PWSB's choice of a vendor for the water treatment plant. On May 1, 2003, Ms. Marchand testified that discussions had commenced with the new vendor to negotiate a contract for construction and operation of the water treatment plant. See Order No.17515 (issued July 21, 2003).

cover O&M expenses, including the restricted O&M Reserve funds for bonding, operations reserve, chemical cost increases and operations expenses and a decrease of 3.3% represents the phase-out of payments to the Water Resource Board and to Central Falls in franchise fees.³ Ms. Marchand then summarized both the status of PWSB's accounts and the status of PWSB's compliance with the Commission's Order in Docket No. 3378. Ms. Marchand also discussed projects that need to be completed prior to the issuance of the Commission's Order in the instant docket.⁴

Turning to the "unanticipated expenses," Ms. Marchand explained that for tax year 2002-2003, the Town of Cumberland had increased taxes on the water system, valuing tangible property higher than in the past. Although PWSB has challenged the increase, it must continue paying the taxes in order to retain the right to challenge the Town of Cumberland's assessment. Additionally, in July 2002, PWSB's insurance costs for property, liability and health care increased significantly. Finally, in accordance with union contracts, salary costs have increased in FY 2003 and 2004.⁵

Addressing additional factors relative to PWSB's request in the instant docket, Ms. Marchand recommended the following: (1) \$20,000 for leak detection equipment, (2) the addition of a new position of a Leak Detector Crew Leader, a supervisor level position within the union who would be able to perform any task within the Transmission and Distribution ("T&D") Department, for \$55,000,⁶ (3) \$10,000 to Outside Professional Services to retain a consultant to set up a safety program, and (4) additional resources for

³ Id. at 3-4.

⁴ These issues are discussed in detail in PWSB's Motion for Interim Relief, Order No. 17466, (issued May 21, 2003).

⁵ PWSB Exhibit 1, pp. 8-9.

⁶ Ms. Marchand indicated that PWSB has eliminated the position of Assistant Maintenance Mechanic due to difficulty filling the position. She also noted that PWSB has replaced three clerks with two Customer

Outside Professional Services for the Cumberland tax issue and for management of delinquency accounts.⁷ Ms. Marchand recognized that many of the expenses requested appear to be one-time expenses in the test year, not normally retained in a pro-forma rate year. However, she maintained that any excess funds collected after satisfaction of the one-time expenses be deposited into PWSB's restricted debt service account for the payment of bond related debt.⁸

Finally, Ms. Marchand provided an update on the status of the unification of the PWSB and Central Falls distribution systems. She indicated that since the testimony in Docket No. 3378, she has been investigating the possibility of obtaining federal funds to assist PWSB in purchasing Central Falls' system. Senator Chafee announced that \$540,000 will likely be available to PWSB based on a 45% contribution by PWSB to purchase the system. Although PWSB and Central Falls differ on the proper methodology of valuing the system, Ms. Marchand testified that the money would be useful for purchasing the system. Neither party has moved from their respective positions with regard to the appropriate valuation. However, Ms. Marchand testified that the cost of renovating Central Falls' system to meet EPA requirements in 2010 is estimated at \$6 million. Despite this expense, Ms. Marchand indicated that PWSB would prefer to unite the systems rather than separating them further than they presently are. However, if the Central Falls system will pose a threat of EPA violations, PWSB is prepared to fully separate the systems.⁹

Service Agents who have additional responsibilities. Therefore, PWSB has eliminated two positions and is requesting creation of the new position. PWSB Exhibit 1, p. 10.

⁷ Id. at 8-11.

⁸ Id. at 11.

⁹ Id. at 12-15.

PWSB submitted the direct pre-filed testimony of David G. Bebyn, CPA. Mr. Bebyn is a Consulting Department Supervisor with the firm of Bacon & Edge, P.C. (B&E). In his testimony, he stated the test year was audited by B&E. Mr. Bebyn listed 13 adjustments he made to the audited test year prepared on a GAAP basis in order to present the test year on a normalized “rate making basis”. Finally, Mr. Bebyn presented a four year analysis (1999-2002) of audited revenue & expense.¹⁰

PWSB submitted the pre-filed direct testimony of Christopher P.N. Woodcock, President of Woodcock & Associates, Inc., in support of its pro forma revenue requirements and proposed rates and charges. Mr. Woodcock’s test year is FY July 1, 2001 through June 30, 2002. The proposed rate year is FY 2004. He quantified the costs that attribute to the rate increase as follows: (1) additional operating costs that would have otherwise been assumed by the DBO vendor of the new water treatment plant; (2) increases in the cost of salaries and benefits; (3) increases in insurance costs since September 11, 2001; (4) an increase in property taxes; and (5) an increase in operating costs resulting in an increase in the related operating reserves.¹¹ According to Mr. Woodcock, the resulting pro-forma revenue requirements necessitate an across-the-board increase of 28%, with a reduced allowance for operating income. He did note that 28% was the maximum authorized by the PWSB.¹² Therefore, he testified that “if the Commission [were to] find that any of the revenue requirements in this filing are overstated or there is disagreement, we hope to restore funding for [operating income] up to the normal 1.5% allowance.”¹³

¹⁰ PWSB Exhibit 5 (Pre-filed testimony of David Bebyn), pp. 2-4.

¹¹ PWSB Exhibit 2 (Pre-filed testimony of Christopher P.N. Woodcock), pp. 3-5.

¹² Id. at 5-6.

¹³ Id. at 6. Mr. Woodcock provided Schedules specifying each of his adjustments to the test year.

Although Mr. Woodcock noted that his analysis showed that PWSB requires an across-the-board increase in rates, he proposed an alternative rate design for Commission consideration. Specifically addressing the property tax impact on the revenue requirement, Mr. Woodcock stated:

Recently there had been a dramatic increase [in] the assessed value of the PWSB's real and tangible property located in the Town of Cumberland...Naturally, this has led to an increase in the PWSB's tax payments to Cumberland. I understand that they are the only community to propose this and obviously they reap the entire benefit. As such, the PWSB has asked that the Commission consider a surcharge to customers in Cumberland.¹⁴

PWSB's position was that it would be unfair to charge all ratepayers in other communities the increased taxes. The impact of the surcharge would be to increase non-Cumberland residents' rates by 25.4% and Cumberland residents' rates by 38.5%.¹⁵

PWSB submitted the pre-filed direct testimony of Maureen E. Gurghigian, Senior Vice President at First Southwestern Company to provide an update on the plan of finance and its impact upon proposed rates. She testified that PWSB's first plan is to defease the outstanding debt of the City of Pawtucket and the Public Building Authority and the second is to provide funds for the construction of a new water treatment plant and for PWSB Capital Improvements Plan ("CIP").¹⁶

She reviewed PWSB's financial structure, indicating that the Drinking Water State Revolving Fund ("SRF") will provide a significant portion of the capital funding for PWSB's capital program using federal capitalization grants and state matching fund to

¹⁴ Id. at 5.

¹⁵ Id., Schedule 7.0.

¹⁶ PWSB Exhibit 3 (Pre-filed testimony of Maureen E. Gurghigian), p. 2.

provide a subsidized loan at 25% below market rate.¹⁷ The finance plan requires the development of a new credit structure that is not entirely dependent upon the City of Pawtucket, but rather, upon rates. Under the plan, there would no longer be a general obligation support of the City of Pawtucket. However, in order to undertake PWSB's projects, the PWSB will be required to defease the current \$10 million PBA debt with the proceeds of new loans in order to make the required pledge to the Rhode Island Clean Water Finance Agency ("RICWFA") for the SRF loans.¹⁸ Overall, the current finance plan contemplates refunding or defeasance with \$5 million of new money in 2003, followed by the treatment plant financing as soon as a vendor is in place.¹⁹

Ms. Gurghigian explained that under PWSB's current debt structure, PWSB currently uses revenues to repay lease revenue bonds issued by PBA and general obligation bonds issued by the City of Pawtucket. The security provisions of the PBA bonds put any additional revenue bonds in a subordinate position to those of the outstanding PBA bonds. Therefore, in order to avoid the higher interest rates this situation creates and in order to obtain sufficient funds, PWSB needs to defease the PBA bonds.²⁰

According to Ms. Gurghigian, despite the activity to implement this finance plan, in the short run, there will be no major impact upon ratepayers that are directly related to the proposed debt structure. This is because initially, the bond payments will be structured to match the current bond payments. However, to the extent that additional

¹⁷ The subsidized interest rate produces an estimated savings of \$1.5 million on a typical \$10 million loan. For PWSB's anticipated borrowing of \$80 million over the next four borrowing cycles will save an estimated \$12 million over a 24-26 year period. *Id.* at 4.

¹⁸ *Id.* at 2-3.

¹⁹ *Id.* at 5.

²⁰ *Id.* at 3-4.

borrowing is required as a result of the modified finance plan, PWSB will have additional costs associated with issuance of the debt. She estimated the overall cost, exclusive of bond insurance will be 2.2% of the total loan amount. In addition, the delay on the treatment plant financing will extend the overall debt schedule into another fiscal year. Furthermore, interest rates cannot be fixed until the PWSB has a definite spending plan upon which to base a loan agreement with the RICWFA. Therefore, currently, Ms. Gurghigian only anticipates the possibility of the two series of defeasance or refunding bonds and a small amount of money for the 2003 construction season.²¹

She also noted that PWSB's finance plan uses IFR funding for approximately 50% of the distribution system projects in order to reduce reliance on long-term debt for projects that will have immediate benefits. Finally, she indicated that the SRF program requires that net revenues must equal or exceed 125% of annual debt service, but she also expected bond rating agencies' insurers to require at least that level, if not more. Therefore, prior to making debt service payments on the SRF loans, PWSB will direct all rate revenue approved for capital to reserves that will be required under the loan agreements and to the IFR program.²²

Finally, PWSB submitted the pre-filed direct testimony of Anthony B. Simeone, Executive Director of the RICWFA, to provide information regarding the SRF and other financing services that the RICWFA can make available to PWSB. Mr. Simeone explained that for qualified new money projects, the RICWFA can make subsidized loans with fixed interest at 25% below market rate. He also noted that for refinancing of prior debt or to finance projects that do not qualify under the SRF, the RICWFA can serve as a

²¹ Id. at 3-4.

²² Id. at 5-6.

conduit issuer, enabling PWSB to consolidate all of its financing under the RICWFA umbrella. Additionally, he indicated PWSB's proposed financing structure enables the City of Pawtucket and PWSB to establish a new revenue-based credit structure that is in line with the regional nature of the water system and which does not utilize the credit or debt capacity of the City of Pawtucket. He explained that loans under the SRF program are structured as "credit line" so that interest is not due until payments are made based upon invoices submitted by project vendors. Finally, he noted that Principal amortization normally begins within one year of the completion of construction.²³

III. Central Falls' Pre-filed Direct Testimony

Central Falls submitted the pre-filed testimony of Mayor Lee Matthews. He argues that because 15.7% of the increase is directly attributable to the costs associated with the delay in building a new treatment plant, Central Falls ratepayers should not have to pay any costs associated with the upkeep of the treatment plant. According to Mayor Matthews, "These expenditures would have been totally unnecessary but for the City of Pawtucket's interference with the orderly business of selecting a vendor."²⁴

Central Falls also argues that because it is no longer receiving a franchise fee from PWSB as the franchise agreement was terminated last year, it should now be allowed to collect a transport fee from PWSB. Finally, with regard to a potential sale of the system, Central Falls continues to argue that its system should be valued through the use of a "depreciation value" method which, in 1997, was \$2,950,424.²⁵

IV. Division's Pre-filed Direct Testimony

²³ Id. at 1-2.

²⁴ Pre-filed Direct Testimony of Mayor Lee Matthews, pp. 1-3.

²⁵ Id. at 3-4.

The Division presented the pre-filed direct testimony of its consultants, Andrea Crane, to provide recommendations regarding PWSB's revenue requirements and Mr. Thomas Catlin, to provide recommendations regarding PWSB's rate design. Ms. Crane recommended nineteen adjustments totaling \$2,041,810 to PWSB's proposed pro forma rate year revenue requirements resulting in a total revenue requirement of \$12,852,887. She concluded that, based on her recommendations, a rate increase of \$1,115,581, or a 9.5% increase over current rates is appropriate.²⁶

Beginning with consumption figures, Ms. Crane recommended using a five year average to derive the pro forma rate year retail consumption and a nine year average to derive the wholesale consumption. She maintained that the use of two different averages is not inconsistent, but rather, is entirely reasonable given her belief that her methodology produces the most accurate figures. Her total adjustment to consumption results in a \$184,748 increase to pro forma revenues.²⁷ These adjustments led to an adjustment in the State Surcharge Revenue level.²⁸

Addressing costs related to the treatment plant (\$1.77 million), Ms. Crane argued that there is no need for the Commission to require PWSB to reimburse the IFR account for the \$359,700 it was allowed to use for treatment plant related costs. She maintained that PWSB was originally planning on funding many of these costs through the IFR through 2005. Therefore, she recommended that the balance of the IFR costs be funded over two years indicating that it represents expenditures through 2005. While she recognized that PWSB had committed to depositing any incremental funds above those needed in later years for IFR projects into a restricted account, she suggested that it is

²⁶ Division Exhibit (Pre-filed testimony of Andrea C. Crane), pp. 5, 32.

²⁷ Id. at 9-12.

preferable to set rates lower now to mitigate the level of the necessary increase ratepayers are facing.²⁹

Next, addressing personnel costs, Ms. Crane began by recommending the Commission only approve funding for 65 positions rather than the requested 66 on the basis that PWSB has consistently had vacant positions. Because the one position is not vacant at any one time, she calculated her adjustment based on the average salary and wage expense for the PWSB's non-administrative employees. Ms. Crane made a corresponding payroll adjustment as well. Next, Ms. Crane recommended an adjustment to overtime costs, indicating that rather than increasing its actual test year overtime costs by 3% annually, it is more appropriate to use an average of actual overtime hours over a multi-year period to determine a reasonable level of pro forma overtime costs. The result was a reduction to PWSB's claim. Finally, Ms. Crane recommended the Commission deny PWSB's requested increase to employee benefits on the basis that PWSB did not provide sufficient support for the increase.³⁰

Turning to PWSB's adjustments to "Other Budgeted Items," Ms. Crane indicated that PWSB provided sufficient support for all but three items: Education and Training (Administration); Outside Services (Customer Service); and Postage (Customer Service). She indicated that the Education and Training costs were estimates that were not well supported, noting that in her opinion, there was no explanation why the costs are expected to increase by nearly 60%. With regard to the outside services, PWSB submitted documentation related to a lockbox, but for an amount below that which was being requested. Therefore, she recommended only funding the documented amount.

²⁸ Id. at 12.

²⁹ Id. at 13-14, 27-28.

With regard to the disputed postage costs, Ms. Crane indicated that PWSB did not provide any rationale for a 64% increase. Because the postal increase that occurred in the past year was approximately 8.8%, Ms. Crane recommended the test year postage costs be increased by only that amount. Finally, Ms. Crane made two corrections to PWSB's requested increases to Printing (Administration) and (Customer Service) as a result of PWSB's Responses to Division Data Requests.³¹

Addressing PWSB's claim for recovery through rates of the EPA penalty, Ms. Crane recommended denying the request on the basis that it is a penalty imposed on the PWSB as a result of its failure to comply with governmental regulations and it should be a non-recurring cost.³²

Moving to the property taxes, Ms. Crane made an adjustment to the claim to reflect a small reduction that Cumberland agreed to make after the initial filing. However, she stated, "[a]lthough the 5% increase for fiscal year 2004 is not supported with empirical evidence, a review of the actual taxes paid to date in the current fiscal year suggests that the Board's proposed proforma expense is not unreasonable."³³

Regarding chemical costs, Ms. Crane noted that PWSB's claim represented an increase of 63% over the test year costs. She maintained that although PWSB provided the support for its calculations, it has not explained the rationale for the significant cost increase. Therefore, she recommended the pro forma chemical expenses be determined

³⁰ Id. at 14-18.

³¹ Id. at 18-21.

³² Id. at 20-21.

³³ Id. at 22-23.

by pricing the actual test year quantities of chemicals, adjusted for her sales calculations, at the unit rates contained in Mr. Woodcock's testimony.³⁴

Addressing regulatory commission costs, Ms. Crane recommended that PWSB's regulatory commission expenses be based on the average actual costs PWSB incurred in its last three rate cases. Furthermore, Ms. Crane recommended PWSB be allowed to recover the costs over two years. This results in an average cost per rate case of \$106,318 or \$53,159 recovery per year.³⁵

Turning to leak detection costs, Ms. Crane recommended approval of \$15,495 rather than \$20,000 in order to more accurately reflect the cost of the equipment. Addressing PWSB's beeper stipend request, Ms. Crane made an adjustment to reflect discovery of a calculation error during discovery.³⁶ Regarding capital leases, Ms. Crane indicated that PWSB's documentation for the rate year showed a total lease amount of \$60,060, down from the test year level of \$110,689. Therefore, she adjusted the request down to reflect the termination of one of PWSB's leases in September 2002.³⁷

Addressing PWSB's O&M Reserve, Ms. Crane indicated that because she recommends a lower level of O&M expenses than those recommended by PWSB, her required reserve of 25% is correspondingly lower. Additionally, she reduced PWSB's claim to reflect the fact that a portion of the reserve has been funded through rates approved in Docket No. 3378.³⁸

Finally, turning to PWSB's Operating Reserve, Ms. Crane has noted that because PWSB is a non-investor owned utility which operates on a cash flow basis, the

³⁴ Id. at 23-24.

³⁵ Id. at 26.

³⁶ Id. at 24-25.

³⁷ Id. at 26-27.

Commission has traditionally allowed the municipal water utility to collect an operating reserve equal to 1.5% of total expenses. However, in this case, PWSB only included a request of \$57,321 in order to keep the requested increase below 28%. Therefore, Ms. Crane opined that PWSB believed that this amount was all that PWSB thought necessary as a reserve. However, in order to provide for some additional operating revenue allowance, Ms. Crane recommended that the Commission only permit the 1.5% to be applied to PWSB's O&M expenses rather than to overall expense. She stated, "I believe that this is a reasonable compromise between allowing the PWSB to recover an additional 1.5% of all costs and limiting the allowance to the \$57,321 included in the Company's request."³⁹

Mr. Catlin testified that it would be reasonable to increase rates by a uniform percentage. He recommended, however, that the Commission order PWSB to file an updated cost of service study with its next rate filing.⁴⁰ Specifically addressing PWSB's alternate rate design to impose a surcharge on Cumberland residents as a result of the increased property taxes, Mr. Catlin noted that Cumberland had not provided data responses regarding the calculation of the taxes. Therefore, he stated:

[T]he property subject to taxation is normally used for the benefit of all customers. Under such circumstances, it would be inappropriate to recover the property taxes assessed by a given municipality only from the customers located in that municipality. Instead, it is normally appropriate that all property taxes be recovered from all customers as part of base rates. In this proceeding, however, it is not clear: with what assets the taxes on tangible property in Cumberland are associated; what the bases for large increase in valuation and taxes are; or whether those taxes are associated with property which benefits all customers...Unless the Town of Cumberland provides information and documentation which address these concerns, it may be appropriate to make an exception in this case to allow

³⁸ *Id.* at 28-29.

³⁹ *Id.* at 29-31.

⁴⁰ Exhibit 2 (Pre-filed Direct Testimony of Thomas Catlin), p. 4.

recovery of the increase in property taxes on tangible property directly from customers in the Town of Cumberland.⁴¹

V. PWSB's Pre-filed Rebuttal Testimony

PWSB submitted the pre-filed rebuttal testimony of Pamela Marchand, David Bebyn and Christopher Woodcock. Ms. Marchand responded to the following Division recommendations: (1) projected wholesale sales; (2) IFR funding; (3) salary and wages; (4) overtime costs; (5) EPA penalty; (6) postage-customer service; (7) leak detection; and (8) capital leases.

With regard to projected wholesale sales, Ms. Marchand indicates that a five-year average produces a conservative level of usage for the rate year. She explained that the Town of Seekonk stopped purchasing water wholesale in 2001 when it developed its own system. Additionally, according to Ms. Marchand in FY 2001, because of problems with their wells and in FY 2002, because of the drought, wholesale sales to Cumberland were unusually high. Furthermore, Ms. Marchand indicated that because "FY 2004 has begun with full reservoirs and plenty of rain," she assumes Cumberland will minimize its wholesale purchases. Therefore, she does not believe it is appropriate to use a nine-year average.⁴²

Addressing IFR funding, Ms. Marchand maintains that Ms. Crane's position that the interim relief allowing PWSB to utilize IFR funds for treatment plant costs not be reimbursed to the IFR account and that the remaining request for treatment plant improvements be spread over two years contradicts the purpose for which the relief was sought. She noted that the Commission, in granting the request, recognized that transfers of funds could cause delays in projects for which the funds are earmarked and, she

⁴¹ Id. at 5-6.

argued, that if the IFR is not repaid, the main replacement projects will be delayed even further than previously anticipated, thus compounding the Commission's concern. Although she conceded that some of the treatment plant projects will not be completed immediately, under City rules, PWSB needs to collect the necessary funds prior to bidding projects. Therefore, she asserted, if PWSB is required to spread the collection of the funds over two years, it would most likely have to come back before the Commission to request additional interim relief in the meantime.⁴³

Turning to Ms. Crane's position on salaries, wages and overtime, Ms. Marchand testified that in the past that often times the vacancies existed due to lack of funding. In this case however, she stated that the positions are not truly vacant, but are being filled by temporary employees until the contract with the treatment plant vendor was signed. She noted that there is an agreement with the union that any permanent employee who is transferred to the payroll of the vendor will receive a bonus equal to 25% of salary & benefits. Having the positions filled by temporary employees should avoid having to pay the bonus for these two positions. Furthermore, the current vendor operation fee is based on the existing treatment plant staffing level of sixty-six employees. Therefore, if positions are eliminated, the vendor will not have to fill the positions when it takes over operations despite the fact that the operation fee is based on the current staffing level. For these reasons, Ms. Marchand argued against any reductions to salaries and benefits. Likewise, Ms. Marchand argued against any reduction to overtime. She agreed that overtime costs fluctuate from year to year, but maintained that, due to a shift in focus to address delinquent accounts, more customer service overtime has been necessary.

⁴² Pre-filed Rebuttal Testimony of Pamela Marchand, p. 2.

⁴³ Id. at 2-4.

Furthermore, she noted that the overtime costs for fiscal year 2003 is in excess of the requested rate year amount. Therefore, she maintained that there should be no reduction.⁴⁴

Addressing the one-time EPA fine, Ms. Marchand stated that PWSB had the required Spill Prevention Control and Countermeasure Plan for an above ground heating oil tank in place, but not separated out from its Emergency Plan. Additionally, the manufacturer/installer was unaware of the regulation and in fact, other utilities had been fined. Therefore, she indicated that because PWSB was not knowingly in violation of the EPA regulation, it should not be denied. Regarding Ms. Crane's concern that if the Commission approved the request for recovery during the rate year, PWSB would be overcollecting the funds in subsequent years, Ms. Marchand indicated that PWSB intends to apply for another rate filing in the next year for the treatment plant bond expense and that any additional revenues could be applied to debt expense.⁴⁵

Regarding the postage dispute, Ms. Marchand indicated that the postage charges listed in the test year were inaccurate and that the correct customer service postage number should have been \$26,776. Using Ms. Crane's suggested 8% increase the resulting rate year expense is \$29,918, which Ms. Marchand noted is consistent with PWSB's \$29,000 request. Additionally, the test year administration postage expense was inaccurate but the rate year includes postage costs for the Consumer Confidence report and two additional mailings. She concluded that although the test year numbers were in error, the request for rate year expenses are accurate. Finally, \$3,000 for customer service miscellaneous postage was inaccurately charged to Administration Miscellaneous

⁴⁴ Id. at 4-5.

⁴⁵ Id. at 5-6.

in both the test year and the rate year. Therefore, the rate year expenses should be reduced by \$3,000. However, Ms. Marchand requested that the Commission allow PWSB to retain the \$3,000 in rates to apply to any unexpected costs, such as higher insurance costs.⁴⁶

Regarding the leak detection equipment, Ms. Marchand indicated that at the time Ms. Crane provided her testimony, she did not have the additional information that PWSB had provided regarding the basis for the cost. Finally, regarding Ms. Crane's evaluation of the capital leases, Ms. Marchand indicated that PWSB did not include a lease for \$57,979. She indicated that the existing leases for Fiscal Year 2004, total \$73,069. Additionally, she noted that the PWSB is proposing to purchase an additional three vehicles on the lease program for Fiscal Year 2004 for an increase of \$37,500 to the annual payment, for a total lease program of \$110,600 in accordance with information she attached to her testimony.⁴⁷

Mr. Woodcock provided rebuttal testimony addressing the Division's position regarding employee benefits, training costs, chemical costs, IFR Funding, O&M Reserve Fund Deposit, and operating income allowance. With regard to employee benefits, Mr. Woodcock indicated that PWSB's initial figures were overstated, resulting in a reduction of \$16,000 to Ms. Crane's recommendation. However, with regard to training costs, Mr. Woodcock indicated that there should be no adjustment to the \$12,000 request, for two reasons, namely because the New England Water Works Association had raised its fees

⁴⁶ Id. at 6-7.

⁴⁷ Id. at 7-8.

and because PWSB would like to send at least one of its Board members to the conference in order to raise awareness on waterworks issues and programs.⁴⁸

Mr. Woodcock indicated that PWSB was no longer proposing to increase pro forma chemical costs through an inflationary adjustment because it now had bid prices. According to Mr. Woodcock, the chemical cost is \$402,208, based on Mr. Bebyn's projected sales.⁴⁹

Addressing the Division's position regarding IFR funding, Mr. Woodcock disagreed with Ms. Crane's recommendation of a two year recovery period for the \$638,000. He argued that because the IFR program is not a one-time expense, but an annual one, there should be no amortization or recovery period for the program. Furthermore, he maintained that PWSB needs full funding in place to adequately fund the main replacement projects and treatment plant upgrades. Mr. Woodcock recognized the Division's concern regarding the impact of the increase on ratepayers, but indicated that the funding has been phased in already and further reductions would only lead to rate shock in the future. Therefore, he continued to seek full annual funding of the IFR program at the requested level.⁵⁰

Turning to the Division's recommendations to reduce funding for the O&M Reserve Fund and to recover the remaining balance over an additional three years, Mr. Woodcock maintained that in Docket No. 3378, the Commission approved full funding of the fund over three years from the date of the Settlement in that docket, or by the end of 2004. Furthermore, according to Mr. Woodcock, the O&M Reserve of 25% of the pro forma operating costs should be higher than that which Ms. Crane recommended. He

⁴⁸ PWSB Exhibit (Pre-filed Rebuttal Testimony of Christopher Woodcock), pp. 1-2.

⁴⁹ Id. at 2-3.

argued that if the Commission were to accept Ms. Crane's proposals in full, the delay in funding the account together with what he termed "inadequate funding for increases sends a terrible signal to the investment community at a time when the PWSB needs all the support it can get for financing its capital improvement project."⁵¹

Finally, Mr. Woodcock addressed the difference in opinion regarding PWSB's Operating Reserve. He noted that Ms. Crane made the statement that "it is reasonable to assume that the Board considers \$57,321 to be sufficient." Mr. Woodcock indicated that this was a wrong assumption. He explained that the filing was made with a 1.5% operating reserve, but that subsequent to the filing, PWSB found that certain expense items needed to be adjusted upwards. However Pawtucket Water's Board had only authorized a filing seeking a 28% increase. Therefore, when PWSB adjusted certain expenses upward, it had to also reduce other expenses, namely the operating reserve. Mr. Woodcock argued that due to reductions proposed by the Division, to which PWSB agreed, it is now possible to restore the Operating Reserve to the full 1.5%. He attempted to justify the request by maintaining that PWSB has been careful with its expenditures and has found places to cut costs. He did not believe that the rates which the Commission had approved in the past, including a 1.5% Operating Reserve, were excessive.⁵²

Mr. Bebyn provided rebuttal testimony addressing the Division's position relating to PWSB's pro forma retail revenue, wholesale sales, surcharge revenue and regulatory expenses. Mr. Bebyn pointed out that Ms. Crane relied on unaudited annual reports rather than audited financial statements when developing her recommendations. He

⁵⁰ Id. at 3-4.

⁵¹ Id. at 5-6.

noted that the annual reports were overstated for Fiscal Years 2001 and 2002. Therefore, he indicated that these numbers skewed Ms. Crane's five year average causing her projected revenues to be overstated. He concluded that after correcting the data, no adjustments to PWSB's position regarding pro forma retail revenue is necessary.⁵³

Next Mr. Bebyn addressed the Division's adjustment to wholesale sales, indicating that PWSB's projection was a conservative estimate because the five year average included purchases from Seekonk, Massachusetts between 1999 and 2001 and abnormally high purchases from the Town of Cumberland during 2002. Additionally, Mr. Bebyn indicated that the close of Fiscal Year 2003 indicates that wholesale sales were less than 598,000 HCF. Therefore, because PWSB's pro forma average produced a higher level of sales than Fiscal Year 2003 actual sales, no adjustment should be made.⁵⁴

Regarding Ms. Crane's adjustment to the State Surcharge Revenue, Mr. Bebyn clarified application of the law to wholesale and retail sales. He indicated that wholesale sales are not subject to the surcharge and therefore, should have been excluded from Ms. Crane's adjustment. Additionally, the elderly are exempted from the surcharge by the law. Therefore, he indicated that it would be inappropriate to assume that 100% of any increase in consumption would be subject to the surcharge. Therefore, he made no additional adjustment to PWSB's calculation of the surcharge.⁵⁵

Finally, addressing the Division's recommendations regarding the funding of rate case expenses, Mr. Bebyn noted that Ms. Crane did not have the data for Docket No. 3193 in her calculations. He maintained that Docket No. 3164, an abbreviated filing,

⁵² Id. at 6-7.

⁵³ PWSB Exhibit (Pre-Filed Rebuttal Testimony of David Bebyn), pp. 1-2.

⁵⁴ Id. at 2-3.

⁵⁵ Id. at 3.

should be combined with Docket No. 3193, producing an additional \$33,000 in legal and witness costs. Furthermore, Ms. Crane's average of the past three filings included a docket which was filed six years ago, with no adjustment for the present value of the costs. Therefore, Mr. Bebyn believed that no additional adjustment needs to be made to PWSB's position regarding regulatory costs.⁵⁶

Responding to Central Falls' contention that its residents should not have to pay any costs associated with the delay of the treatment plant, Ms. Marchand filed additional Rebuttal Testimony. She argued that because the new plant will benefit all PWSB customers, including those in CF, all customers should bear the burden of the costs.⁵⁷

Turning to Central Falls' request for a transport fee, Ms. Marchand argues that there is no support in the record for such a fee. She indicates that when asked to provide a financial basis for this fee in Data Request 1-15, the City provided no substantive information.⁵⁸

PWSB continues to argue that the appropriate method is the original cost net of depreciation and net of contributions in aid of construction. Ms. Marchand indicates that the appropriate valuation made just before Docket No. 3378 is \$851,500. Central Falls owns the distribution system in the City, but has no responsibility for billing or collections as their residents are retail customers of PWSB. The only thing Central Falls has to do is maintain its system. However, even when it was receiving yearly franchise fees, it was not putting money into the system. In the last 10 years, Central Falls received approximately \$2 million from PWSB in franchise fees and expended between \$267,031 to \$426,395. Additionally, the same study upon which Central Falls bases its valuation

⁵⁶ Id. at 3-4.

⁵⁷ Pre-filed Rebuttal Testimony of Pamela Marchand to Central Falls, pp. 1-2.

called for replacement of hydrants and distribution pipe. Therefore, Ms. Marchand argues that because no preparations have been made to replace 53,060 feet of distribution pipe at a cost of \$4,217,750, PWSB should not have to pay a premium for the system. On June 30, 2003, counsel for PWSB, Central Falls and DPUC met regarding unification.⁵⁹

VI. Division's Pre-filed Surrebuttal Testimony

On July 24, 2003, the Division submitted the pre-filed surrebuttal testimony of Andrea Crane. Ms. Crane indicated that as a result of revisions in PWSB's rebuttal and updated information received from PWSB, she was accepting certain expenses of which she had previously recommended disallowing. Specifically, Ms. Crane noted that as a result of PWSB's rebuttal position, she no longer took issue with regard to Health Benefits Expense, Printing (Administration), Printing (Customer Service), Outside Services (Customer Service), Property Taxes, or Beeper Stipends. Additionally, as a result of new or updated information, Ms. Crane accepted PWSB's claims for Leak Detection Costs, Capital Leases, Overtime, Retail Revenues and Surcharge Revenues. Therefore, she recommends a \$1,362,967 increase, or 11.99% over PWSB's current rates.⁶⁰

Ms. Crane indicated that she continues to recommend adjustments to several of PWSB's expense claims. Specifically, she addresses Wholesale Revenue, Treatment Plant Related Costs, Salaries and Wages, Training and Education, Postage, Non-

⁵⁸ *Id.* at 2.

⁵⁹ *Id.* at 2-4.

⁶⁰ Pre-filed Surrebuttal Testimony of Andrea Crane, p. 4. Although Ms. Crane accepts PWSB's overtime cost claim, she believes that, due to annual fluctuations of overtime costs, the appropriate methodology is to base the expense on a three-year average and not the test year. Likewise, while Ms. Crane accepts PWSB's claim for retail revenue, she continues to recommend the use of average consumption over a period of time

Recurring Costs, Chemical Costs, Regulatory Commission Expense, Infrastructure Rehabilitation Funding, Operation and Maintenance Reserve, and Operating Reserve Allowance.⁶¹

With regard to the revenue related to wholesale sales, Ms. Crane indicated that PWSB's response to Division Data Request 4.9 differs from the testimony of Ms. Marchand. Therefore, Ms. Crane continues to recommend an adjustment to the wholesale sales claim, but has reduced the adjustment to reflect the FY 2003 results as reported by Ms. Marchand in her Rebuttal Testimony. This modification reduces the adjustment from \$115,884 to \$91,417.⁶²

Addressing PWSB's claim for Treatment Related Costs, Ms. Crane indicated that she continues to recommend that the Commission reduce PWSB's claim for amounts already transferred from the IFR as a result of its Interim Order in the instant docket in order to reduce the impact of a rate increase on ratepayers. She maintained that even with this adjustment, she is providing sufficient funds for IFR programs PWSB intends to undertake over the next few years. Furthermore, she continues to recommend recovery of treatment related costs over two years instead of one in order to avoid excessive rates in subsequent years.⁶³

With regard to PWSB's vacant position and request for Education and Training costs, Ms. Crane continued to recommend the Commission reduce PWSB's total salary and wage claim by at least \$40,174 because, she argued, Ms. Marchand did not provide a sufficient rationale for continuing to fund a position that has not been filled. Ms. Crane

rather than using the test year to determine a "normalized" level of consumption for ratemaking purposes. Id. at 6-7.

⁶¹ Id. at 9.

⁶² Id. at 9-10

also maintained that her adjustment to Education and Training costs will provide PWSB sufficient funds to cover PWSB's education and training costs.⁶⁴

Similarly, addressing the postage claim, Ms. Crane noted that in her Rebuttal Testimony, Ms. Marchand had provided an explanation for a portion of its requested increase. However, Ms. Marchand had also indicated that the costs had been overstated by \$3,000. She requested PWSB be allowed to include this amount in the revenue requirement for use in other areas. Ms. Crane urges the Commission to reject this argument as PWSB has not provided documentation of where the funds would be used.⁶⁵

Likewise, turning to the chemical costs, Ms. Crane asserts that PWSB has still failed to explain the reason for a 57% increase in chemical costs. Although PWSB has indicated that it plans to add a new chemical, it only accounts for \$75,000 of its requested increase. Ms. Crane recommends approval of chemical expenses as listed in PWSB's worksheet of actual 2003 bids plus \$8,138 for a new chemical to be added in 2004. This results in an allowed chemical expense claim of \$318,992.⁶⁶

Addressing rate case expenses, Ms. Crane indicates that she based her adjustment on the average of the last three rate cases that had been filed with the Commission, amortized over two years. She further noted that she agrees with Mr. Bebyn's claim that Docket No. 3193 (rate design) should be included as the pre-cursor to Docket No. 3194 (cost of service). Ms. Crane concluded that collecting the average of the last three rate cases over two years is much more reasonable than a one year recovery of \$158,983..⁶⁷

⁶³ Id. at 10-11.

⁶⁴ Id. at 11-12.

⁶⁵ Id. at 12-13.

⁶⁶ Id. at 14-15.

⁶⁷ Id. at 15-16.

Addressing IFR funding, Ms. Crane noted that her recommendations provide recovery for all projects included in the IFR budget. She maintains that she has not proposed any cut in the funding, but has targeted the incremental increase requested by PWSB. She notes that once treatment plant projects are completed, the annual IFR budget should drop from \$2.6 million to \$2 million. However, she is recommending a two-year recovery period as opposed to a one-year recovery period. She asserts that providing for full recovery of the incremental increase sought over one year will result in excessive rates being charged to ratepayers in subsequent years.⁶⁸

With regard to the O&M Reserve Account, Ms. Crane asserts that contrary to Mr. Woodcock's contention, it is not her recommendation that will delay full funding of the Account, but rather, the fact that, after fifteen months of the rate approved in Docket No. 3378, the reserve account has accrued less than one year's worth of funds. Therefore, she argues, the required increase is due, not only to the incremental revenue requirement in this case, but to the fact that funding of the reserve is not on schedule. She argues that it is unreasonable for PWSB to now request an accelerated schedule in order to catch up. Therefore, she still proposes funding the reserve over a three-year period, adjusted to the updated level of O&M expenses she is recommending.⁶⁹

Finally, with regard to the Operating Reserve Allowance, Ms. Crane continues to recommend that the Allowance only be applied to PWSB's O&M expenses because these costs are subject to greater variation and uncertainty than PWSB's capital costs. She

⁶⁸ Id. at 16-17.

⁶⁹ Id. at 17-18.

maintains that this methodology is consistent with the debt covenant reserve requirement, which is based on O&M expenses rather than overall costs.⁷⁰

VII. PWSB's Motion to Dismiss the Town of Cumberland from the Case

On April 24, 2003, PWSB issued data requests to Cumberland. Cumberland did not file any objection within 10 days or any responses within 21 days. The Commission issued a letter order compelling Cumberland's responses by June 9, 2003. Again, Cumberland did not respond to the Commission's letter. On June 19, 2003, at its open meeting, the Commission ordered Cumberland to respond no later than June 27, 2003. Commission counsel issued a second letter order indicating that failure to provide the responses could result in Cumberland losing the right to put forth testimony regarding any of the issues raised in the data requests. Counsel to Cumberland contacted Commission counsel indicating the responses would be provided. Cumberland filed its responses on June 27, 2003. On June 30, 2003, PWSB filed a Motion to Dismiss the Town of Cumberland as an intervenor and/or strike testimony, arguing that the information provided by Cumberland was not fully responsive. On July 17, 2003, Cumberland filed an objection indicating that it had provided all available information in response to PWSB's requests. On July 21, 2003, the Commission convened at its offices at 89 Jefferson Boulevard, Warwick, Rhode Island, to hear oral arguments by the parties.

The following appearances were entered:

FOR PWSB:	Joseph Keough, Jr, Esq.
FOR CUMBERLAND:	Richard Kirby, Esq.
FOR DIVISION:	Leo Wold, Esq. Special Assistant Attorney General

⁷⁰ Id. at 18-19.

FOR COMMISSION: Cynthia G. Wilson, Esq.
Senior Legal Counsel

PWSB argued that its Rebuttal Testimony was due on July 10, 2003 and it had no way to further address the Cumberland surcharge issue, beyond what had been contained in its initial filing. Counsel noted that the hearing was scheduled for August 21, 2003, one month from the arguments. He argued that even if the Commission were to issue another order compelling the responses, PWSB would not have enough time to adequately analyze the information and provide a response. Furthermore, counsel argued that what PWSB does not want is for Cumberland to suddenly show up at the hearing on August 21st with the information.⁷¹

Counsel for Cumberland argued that the Town had provided all of the information upon which the Tax Assessor had based the tax assessment. He stated that he had provided the Tax Assessor with every piece of correspondence he had received in this case. He assured the Commission that he would meet with the Mayor of Cumberland by the next day to assure he is fully apprised of the status of the case.⁷²

The Division argued that its witness needed the same information as PWSB in order to make a full recommendation to the Commission. However, rather than dismissing Cumberland from the case, the Division recommended granting the alternative relief sought in order to allow Cumberland to cross examine witnesses on other issues. Counsel to the Division noted that under the Commission's Rules of Practice and

⁷¹ Tr. 7/21/03, pp. 3-37. Counsel for PWSB stated, "I just want to make clear for the record that it's not been a contentions matter between Mr. Kirby and I. I think what's not being put forth is information from the Assessor's office..." Id. at 32.

⁷² Id. at 25-26, 33-44.

Procedure, Cumberland would not be permitted to present evidence anyway because they had missed the pre-filing deadlines.⁷³

At the close of the hearing, the Commission decided unanimously to grant the alternative relief requested, namely that Cumberland not be permitted to present any testimony at the hearing on the issue of taxation.⁷⁴

VIII. Hearings

The Commission held two hearings for the purpose of taking public comment, one in the City of Pawtucket on May 8, 2003 and one at the Commission on August 13, 2003. Additionally, members of the public were allowed to provide more comment at the evidentiary hearing held on September 10, 2003.

Duly noticed public evidentiary hearings were held at the Commission's offices at 89 Jefferson Boulevard, Warwick, Rhode Island on August 21, 2003,⁷⁵ September 10, 2003 and September 18, 2003 for the purpose of considering the evidence regarding PWSB's rate design and revenue requirements.

The following appearances were entered:

FOR PWSB: Joseph Keough, Jr., Esq.

⁷³ *Id.* at 45-47.

⁷⁴ *Id.* at 49-50.

⁷⁵ On August 21, 2003, Mr. Michael McElroy entered his appearance on behalf of the Town of Cumberland. He produced additional documentation regarding the property tax increase. The information was marked as Cumberland Exhibit 1 for identification only. Mr. McElroy made an oral motion for Relief from a Prior Commission Order under Commission Rule of Practice and Procedure 1.28(b)(3) which struck any testimony and evidence propounded by Cumberland regarding the tax and related surcharge issue for failure to comply with Commission discovery rules. After hearing argument from all parties, the Commission denied the Motion for Relief from a Prior Commission Order, specifically finding that if the Commission were to allow a party to a case to ignore its rules and then produce information at the last minute, there would be no incentive for parties to ever comply with the Commission's discovery rules. The Commission's rules require a showing of good cause for allowing a Motion to Reconsider a prior ruling. Mr. McElroy argued that Cumberland was unaware of the harsh penalty it could face for non-compliance with Commission discovery rules. However, the Commission pointed out that Cumberland was sent two letter orders, one specifically outlining that it could have its testimony stricken. Tr. 8/21/03, pp. 21-25, 39-45.

FOR CENTRAL FALLS: Matthew T. Oliverio, Esq.

FOR CUMBERLAND: Richard Kirby, Esq.
Michael McElroy, Esq.

FOR DIVISION: Leo Wold, Esq.
Special Assistant Attorney General

FOR COMMISSION: Cynthia G. Wilson, Esq.
Senior Legal Counsel

Steven Frias, Esq.
Executive Counsel

PWSB presented Ms. Marchand, Mr. Woodcock, Mr. Bebyn, Ms. Gurghigian, Mr. Simeone for cross-examination. The Division presented Mr. Catlin and Ms. Crane for cross examination.

A. Rate Design

PWSB presented Mr. Woodcock in support of its request for a surcharge to be paid for by Cumberland ratepayers as a result of the property tax increase. Mr. Woodcock testified that the surcharge is only for the additional \$300,000 of taxes. He also indicated that he did not know what the additional tax was based on, but believed that it included a tax on the pipes.⁷⁶

On cross examination by Cumberland, Mr. Woodcock testified that PWSB was only seeking the surcharge for the increase in taxes. He indicated that although other water utilities have been taxed for tangible property by other municipalities, Cumberland is the only community to include the pipes as tangible property. Additionally, Mr. Woodcock indicated that there was no information provided regarding the valuation of the pipes. Therefore, he stated that “the concern was that this was a unique situation with

⁷⁶ Tr. 9/10/03, pp. 206, 208, 217.

no explanation as to the basis for it, and because it was a unique situation that a surcharge would be appropriate.”⁷⁷

However, Mr. Woodcock also testified that even if the Superior Court were to find Cumberland’s valuation and related tax appropriate, the ratepayers of Cumberland should still have to pay the entire increase for the pipes taxed as tangibles on the basis that the distribution pipes serve the ratepayers of Cumberland. In response to a question regarding a tax assessment on Providence Water Supply Board by the Town of Scituate which was spread among all ratepayers, Mr. Woodcock distinguished that case by noting that the Scituate tax increase was on the reservoir and other land clearly benefiting all ratepayers. However, Mr. Woodcock conceded upon cross-examination by Commission counsel that he was not testifying that the PWSB system received no benefit from the distribution pipes located in Cumberland.⁷⁸

Under further cross-examination by Cumberland, Mr. Woodcock acknowledged that the proposed surcharge would apply to both Cumberland’s retail and wholesale customers and that the proposed surcharge would be reduced if the Commission adopted the Division’s recommendation on wholesale consumption. Also, Mr. Woodcock conceded that North Providence assesses taxes on Providence Water Supply Board for a pumping station that only serves North Providence customers and that this assessment is spread over the entire rate base.⁷⁹

⁷⁷ Tr. 8/21/03, pp. 47-49, 54, 60-63. Counsel for Cumberland attempted to circumvent the Commission’s order striking Cumberland’s previous data responses and limiting Cumberland’s additional data responses for identification purposes only by asking Mr. Woodcock to read the responses into the record. The objection to this method was sustained on the basis that Mr. Woodcock was presented as a witness for impeachment of his prior testimony and not as the proponent of Cumberland’s documents. *Id.* at 50-52.

⁷⁸ *Id.* at 54-59, 70-72.

⁷⁹ Tr. 9/10/03, pp. 174-75, 188-89.

The Division presented Mr. Catlin in support of its position regarding PWSB's rate design. Mr. Catlin indicated that although he agreed with PWSB that a new cost of service study was not necessary for the instant case, he recommended the Commission order PWSB to complete a new cost of service study in preparation for its next rate case.⁸⁰

On cross-examination regarding the surcharge issue, Mr. Catlin agreed that as a general rule, there is not normally a geographic distinction in rates based on where customers are located relative to where facilities are located.⁸¹ Additionally, Mr. Catlin agreed with his statement in his direct testimony that normally property taxes on property that benefits all ratepayers are spread over the entire rate base. He explained that in the instant case, he was not able to determine exactly how the property was valued and the tax calculated. However, he continued to maintain that the surcharge may be appropriate in the instant case because he believed the tax to be on facilities that benefit Cumberland residents. He opined that it would be up to the Commission to balance the policy between attempting to determine what portions of the system benefit which customers and attempting to dissuade municipalities from raising taxes on the water system in order to avoid raising property taxes among their own residents. According to Mr. Catlin, his recommendation was made in light of the fact that Cumberland had not provided the requested information during discovery and that there were no other municipalities assessing similar taxes on similar facilities by which to make a comparison. For example, he indicated that if each municipality were appropriately valuing and taxing the same facilities in the same manner, it may be appropriate to spread the taxes across the

⁸⁰ Tr. 8/21/03, pp. 87-88.

⁸¹ Id. at 90-92.

entire rate base without making a determination of how the facilities benefit specific ratepayers.⁸²

Mr. Catlin was also cross examined by counsel for Central Falls regarding the effect of the delay on rates and whether there should be a different rate for Pawtucket and Central Falls residents. Mr. Catlin testified that the delay in the treatment plant did not affect the cost of serving Central Falls residents in relation to serving Pawtucket residents. Therefore, it is appropriate to charge all ratepayers of Central Falls and Pawtucket the same rates.⁸³

B. Revenue Requirements - PWSB's Witnesses

i. Treatment Plant Issues

In support of its need for a rate increase, PWSB first presented Ms. Marchand for cross-examination. She indicated that she expected a contract with the DBO vendor, Earth Tech, would be executed within the month.⁸⁴ She stated that the next step in the process would be to obtain funding from CWFA and to obtain approval from the Pawtucket City Council for funding, with another review by the Division. The process with the CWFA could take up to 90 days to obtain the bonding. She explained that PWSB would be submitting a package of \$45 million for the treatment plant and facilities, \$12 million for the water main distribution system work and approximately \$2 million for watershed products.⁸⁵ Responding to questions from the Bench, Ms. Marchand noted that she had recently been advised of a change in the CWFA financing

⁸² Id. at 101-110.

⁸³ Id. at 127-134.

⁸⁴ Id. at 139-44. At the hearing on September 18, 2003, Mr. Keough notified the Commission that he had filed a copy of the contract with the Division that morning for its review.

⁸⁵ Tr. 8/21/03, pp. 144-146. As part of its financing plan, PWSB will use existing debt service to cover the defeasance of PPBA bonds. Id. at 147.

requirements whereby PWSB will have to have approval of rates sufficient to cover the bonds before the funding would be approved. She clarified that these rates are not the subject of the instant docket.⁸⁶

Ms. Marchand also responded to questions from counsel to Central Falls regarding the prior delays in the contracting for the new treatment plant and the fact that PWSB's current request is partly the result of critical upgrading needed to keep the old plant operational for a longer period of time than initially anticipated. Ms. Marchand testified that the costs should be spread over the entire rate base, despite the fact that the delay was not the result of any action or inaction by the ratepayers of the City of Central Falls, because these costs are necessary to keep the system operational.⁸⁷

Under cross-examination by Central Falls, PWSB's witness, Mr. Woodcock, admitted that Central Falls retail customers pay the same rate as other PWSB retail customers although Central Falls does not get the benefit of PWSB's personnel to maintain and repair Central Falls' pipes.⁸⁸

ii. Franchise Fee

Ms. Marchand indicated that PWSB has had several meetings with Central Falls to discuss the purchase of Central Falls' distribution system. She indicated that the final franchise payment would be made to Central Falls in FY 2004. She agreed that PWSB would continue to collect \$172,832 in rates annually thereafter absent another rate filing.⁸⁹

⁸⁶ Id. at 187.

⁸⁷ Id. at 168-181.

⁸⁸ 9/10/03, pp. 204-05. Central Falls owns its own distribution system, but does not provide billing or customer service services to its residents. Therefore, all Central Falls ratepayers are retail customers of PWSB.

⁸⁹ 8/21/03, pp. 148-51.

iii. IFR, O&M Reserve & Operating Reserve

Counsel for the Division led Ms. Marchand through each project for which PWSB was granted interim relief.⁹⁰ PWSB also presented Mr. Woodcock to address IFR requirements. Under cross-examination by the Division, Mr. Woodcock indicated that PWSB is requesting an additional \$638,000 for IFR to be recovered through rates annually. Also, Mr. Woodcock admitted that most of PWSB's CIP projects are to be completed over a two-year period.⁹¹ Mr. Woodcock admitted that PWSB reduced its claim for chemicals from \$418,000 to approximately \$364,000. In calculating PWSB's O&M reserve, Mr. Woodcock did not adjust for the \$552,263 currently in the account. Mr. Woodcock indicated that PWSB is seeking a 1.5% operating revenue allowance to be applied to total expenses including debt service instead of just the maintenance and operating expenses.⁹²

iv. Employee Funding

With regard to employee funding, Ms. Marchand testified that of the 66 funded positions, two have been kept deliberately vacant, but have been filled by temporary employees, specially retained for the positions through a temporary placement agency. She conceded that in previous years, PWSB has averaged 62 filled positions.⁹³ She explained that because PWSB expected to transfer operations shortly, the decision was made to fill the two permanent positions with temporary employees in order to avoid a 25% bonus payment to employees transferred to the vendor's operation. This way, the vendor would be responsible for paying all positions transferred but PWSB could avoid

⁹⁰ Id. at 151-63.

⁹¹ Tr. 9/10/03, pp. 133-34, 142-43.

⁹² Id. at 146, 153-55, 162.

⁹³ Tr. 8/21/03, pp. 163-68.

paying the bonus to the temporary employees. She noted that the vendor will be responsible for 17 employees less two that PWSB will keep, translating to a budget of 15 employees in the vendor fee.⁹⁴ She clarified that the vendor will be responsible for hiring permanent replacements for the two temporary employees.⁹⁵

v. Healthcare Costs

Ms. Marchand indicated that Blue Cross/Blue Shield costs had risen 21% over last year and 17% the year before. She noted that PWSB negotiates directly with the Teamsters and the City of Pawtucket negotiates with the city-wide union 1012, which represents the labor force. Members of the Teamsters have co-pays that have increased over the past few years. In the last round of negotiations, the City offered a choice between a health care co-pay and a raise. The union chose to forego a raise in order to avoid paying co-pays.⁹⁶

vi. Vehicles

Ms. Marchand testified that for each new vehicle PWSB plans to lease or purchase, one will be sold so that there will be no net gain in the total number of PWSB vehicles. She also agreed to consider the appropriateness of PWSB's policy allowing employees to bid on the vehicles which are sold through a public bidding process.⁹⁷

vii. Regulatory Expenses

On cross-examination by the Division, Mr. Bebyn, testified that although each separate rate case may have been below the amount being requested through rates, many

⁹⁴ Id. at 164, 195.

⁹⁵ Id. at 218.

⁹⁶ Id. at 204-06. PWSB has two unions, the management, with the exception of the General Manager, her assistant and the Assistant Chief Engineer, is represented by the Teamsters and the rest of the labor force are members of the City-wide union 1012.

⁹⁷ Id. at 201-03, 216-18.

cases interact during the same year, raising the level of rate case expenses. Additionally, the Regulatory Expenses include the Commission assessment against utilities each year. Finally, there are non-rate case dockets included in regulatory expenses.⁹⁸

viii. Wholesale Sales and Revenues

On direct by PWSB's counsel, Mr. Bebyn testified that the FY 2003 wholesale sales figures have been finalized. PWSB's wholesale sales for FY 2003 were 567,004 cubic feet, producing revenues of \$798,392. This is lower than the original forecast, based on a five year average, not including FY 2003, of 630,530 cubic feet.⁹⁹

On cross examination by counsel to Cumberland, Mr. Bebyn acknowledged that if the lower wholesale number were accepted as part of the rate year forecast, the Cumberland surcharge would rise.¹⁰⁰

ix. CWFA Financing, Related O&M Reserve and IFR Funding

In order to address the CWFA financing, PWSB presented Ms. Gurghigian and Mr. Simeone. Ms. Gurghigian noted that the instant case does not request any new debt service.¹⁰¹ However, she indicated that PWSB's borrowing needs will include approximately \$45 million (capped at \$56 million), \$10 to \$12 million per year for cleaning, lining and replacement of pipes, and \$30 million defeasance of the PPBA debt.¹⁰² She noted that funds for the defeasance of the PPBA debt are already in the rate base and PWSB has sufficient rates to commence the first phase of borrowing for the

⁹⁸ Tr. 9/10/03, pp. 109-12, 127-29. Mr. Bebyn also argued that the \$2,000 EPA fine was normalized out of the test year because it was included in regulatory expenses and the request for regulatory expenses is less than the actual test year expenses. Id. at 117.

⁹⁹ Id. at 102-03.

¹⁰⁰ Id. at 113-14.

¹⁰¹ Id. at 101. PWSB's debt service is ultimately projected to increase from approximately \$2.2 million to \$8.9 million. Id. at 60.

¹⁰² Id. at 46-47.

treatment plant.¹⁰³ She explained that “the current debt service allowance and funds available in the IFR which serve as [PWSB’s] coverage allowance will permit them to begin the treatment plant borrowing.”¹⁰⁴ With regard to the future, PWSB will have to file with the Commission a request for increased debt service as the construction proceeds, either asking the Commission to approve automatic increases or to approve increases on an annual basis. However, she stated that because the treatment plant has a 24-month construction time frame, she would not want to do that in more than two borrowings. Her preference would be for PWSB to make one request and to phase in the debt service over three years. She reiterated that while the funds do not have to be “in hand” in the first year after approval, the rates need to be approved in order to complete the second borrowing.¹⁰⁵

Mr. Simeone testified that before the CWFA can make a loan through the SRF, the project must be on the Department of Health’s project propriety list and the borrower must have a Department of Health certificate of approval of the project.¹⁰⁶ He indicated that currently, he expects the CWFA will be able to meet PWSB’s full borrowing needs through the SRF. However, he indicated that even if the CWFA were to make a loan outside of the SRF for lack of capacity, as long as the borrower had all of the necessary regulatory approvals, including the department of Health certificate, the borrower could take out that market rate debt at a subsidy in the future.¹⁰⁷ Furthermore, the CWFA will

¹⁰³ Id. at 47-48.

¹⁰⁴ Id. at 51-52.

¹⁰⁵ Id. at 83-84. Because PWSB’s debt service will increase significantly between FY 2006 and FY 2007, once the plant is completed and payments on the bond will commence, Ms. Gurghigian is working with PWSB to attempt to moderate the increase. Id. at 60.

¹⁰⁶ Id. at 76-77.

¹⁰⁷ Id. at 40-41.

not issue funds unless the PUC has provided approval of the debt service.¹⁰⁸ Mr. Simeone also noted that it usually takes approximately 90 days to take a bond issue to market once the CWFA has all of the documents and corroboration necessary to put a package together.¹⁰⁹

The CWFA provides an interest subsidy equal to 25% of the market rate. The market rate is considered to be the interest rate PWSB would receive if it attempted to borrow the money on its own. CWFA works with the PWSB financial advisor to determine the market rate.¹¹⁰ Therefore, Ms. Gurghigian explained that the role of the reserves, such as the O&M Reserve, is to strengthen the overall credit structure of PWSB, allowing it to obtain a better interest rate and lower its bond insurance premium.¹¹¹ Specifically addressing the timing of funding the O&M Reserve

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Finally, with regard to the timing of funding the IFR account, Ms. Gurghigian testified that the Commission's decision between the competing positions would more directly impact debt service. She indicated that the IFR is viewed as being available for debt service until the coverage requirement is met. Additionally, the IFR allows PWSB the ability to undertake more projects on a pay-as-you-go basis. She indicated that the IFR funding is important because if it is not funded in one year as requested by PWSB, the debt capacity, the amount that could be put toward the first loan, is reduced.¹¹³

C. Revenue Requirements - Division's Witness

i. Treatment Plant Issues and IFR Repayment

On cross examination, Ms. Crane testified that she recognized that borrowing money from IFR for O&M related expenses pushed the pipe project back by one year. However, while conceding that not repaying the IFR fund could "theoretically" delay the project further, Ms. Crane maintained that her recommendation would provide PWSB with sufficient funds through 2011 and would not actually delay the project.¹¹⁴

ii. IFR, O&M Reserve & Operating Reserve

With regard to PWSB's requested IFR increase, Ms. Crane agreed that the Division was in agreement with PWSB's requested \$638,000 increase, but argued that allowing collection in one year could result in excessive rates in subsequent years. She conceded that her recommendation was based on an assumption that PWSB's rates, as approved in the instant case, would be in effect for more than one year. However, she argued that if PWSB expects to be back before the Commission within a year, a more prudent course of action would be to approve a smaller increase that includes funding

¹¹³ Id. at 87-88.

¹¹⁴ Tr. 9/18/03, pp. 24-30.

over two years and revisit the issue in the next rate case rather than approving a larger increase and revisiting the issue.¹¹⁵

With regard to the effect on PWSB's ability to obtain a good credit rating and achieve a lower interest rate, Ms. Crane argued that the IFR funding level is not as significant as PWSB alleges because the bonds that are put out to investors are bundled by the financing agency. She maintained, therefore, that investors are more concerned with the financial integrity of the finance agency than with PWSB, which is only a small piece of the bundle.¹¹⁶

Similarly, with regard to the O&M reserve, Ms. Crane argued that while, as an investor, she would certainly want an O&M reserve funded at 100% immediately, that desire needs to be balanced against the impact on rates. She maintained that there is already a balance of \$560,000 in the account and as long as there is a good faith showing every month that deposits are being made, such a move should provide investors with adequate assurances.¹¹⁷

With regard to the Operating Reserve, when cross-examined by counsel for PWSB, Ms. Crane agreed that PWSB's actual insurance costs are \$20,000 higher than the amount requested in the filing. She further agreed that any variation in a revenue or expense item, such as the insurance costs, could deplete the reserve, but added that there is no evidence to show whether there were any other costs that are actually less than anticipated by the filing.¹¹⁸

¹¹⁵ Id. at 31-41.

¹¹⁶ Id. at 42-46.

¹¹⁷ Id. at 104-06. Ms. Crane also argued that she had used Mr. Woodcock's methodology when calculating the reserve, but her number differs because her overall O&M expenses are lower and she also reduced the reserve requirement by the amount already in the account. Ms. Crane's calculation provides full funding of the reserve by 2006. Id. at 18-21, 68-73.

¹¹⁸ Id. at 73-76.

iii. Employee Funding and Education

Addressing employee funding levels, Ms. Crane agreed that Ms. Marchand had provided solid reasons for not filling the two temporary positions with permanent employees, but argued that because PWSB has run the plant with an average of 62 employees over the past several years despite approval of funds for 66 employees, it is reasonable to eliminate one position.¹¹⁹

With regard to Education and Training Expenses, Ms. Crane maintained that PWSB did not provide sufficient support for its request for an increase. Ms. Crane indicated that she would have required an itemization of the estimate for each course and conference, the registration fee, hotel expenses, and other per unit costs.¹²⁰

iv. Regulatory Expenses

Ms. Crane conceded that regulatory expenses include more than just rate cases. She agreed that from time to time the utility is before the Commission on other types of dockets. She also agreed that consultant fees increase over time, but not at the rate of inflation. However, she also maintained that PWSB did not provide evidence for those types of expenses and therefore, her recommendation was based on the last three rate cases.¹²¹

v. Wholesale Sales and Revenues and Chemicals

With regard to her wholesale sales calculation, Ms. Crane continued to recommend using a nine-year average, but she updated her number to include the FY 2003 numbers that were provided during the hearings in this proceeding.¹²²

¹¹⁹ Id. at 90-103.

¹²⁰ Id. at 47-57.

¹²¹ Id. at 63-67.

¹²² Id. at 21-22.

Addressing the chemical costs, she recommended that the Commission base the rate year chemical allowance on the chemicals needed for the test year usage at the FY 2004 bid prices. She also made a volumetric adjustment of 1.12 percent over the test year to reflect the increased chemicals that would be needed for her forecasted usage levels.¹²³

IX. Post-Hearing Briefs

On September 29, 2003, the parties filed post-hearing briefs in support of their respective positions on the aspects of the case they believed more discussion would be helpful to the Commission.

In its brief, PWSB noted that a fully contested rate case of this nature has been more of the exception rather than the rule. However, PWSB argued that because it is about to embark on a crucial capital improvement program, its request must be viewed in light of the challenges facing the utility in its endeavor to modernize its treatment and distribution systems. PWSB argued that an increase must not be accepted or rejected simply because of the impact on customer bills, but rather, should be judged on the needs of the utility to provide safe water to its customers. Therefore, PWSB argued that the proposed 27% increase is necessary to achieve the PWSB's mandate to provide sufficient quantities of potable water and should be granted.¹²⁴ After reiterating arguments made in pre-filed and live testimony in support of its request, PWSB argued that the Division has done an excellent job representing the ratepayers in the instant docket, but in its attempt to keep the rates low, has spread certain funding over two years, stretching collection

¹²³ *Id.* at 16-18, 60-63.

¹²⁴ PWSB's Post-Hearing Brief, pp. 2-3.

over 30 months. PWSB believes that such methods will not be in the best interest of ratepayers.¹²⁵

In its brief, the City of Central Falls first argued that because PWSB does not own the Central Falls distribution system and does not maintain the system, Central Falls customers should not be paying the same rate as other retail customers. For this reason, Central Falls alleged that the rate design proposed by PWSB was discriminatory. With regard to the argument PWSB made at the hearing that Central Falls did not present the Commission with an alternate rate design, Central Falls argued that it is the responsibility of the utility and not its customers to propose non-discriminatory rates. Therefore, Central Falls requested the Commission order one of the following three options: (1) reduce the rate Central Falls ratepayers pay in an amount sufficient to offset costs paid by Central Falls to maintain its distribution system; (2) require PWSB to pay a wheeling fee; or (3) require the PWSB to maintain Central Falls' distribution system.¹²⁶

Central Falls also argued that the City of Central Falls and Town of Cumberland ratepayers should not have to pay any costs associated with repairs to the existing water treatment plant which resulted from the delay. Central Falls argued that the delay was caused by the City of Pawtucket and not by any members of the City of Central Falls or its elected officials. Therefore, Central Falls argued that only the constituents of Pawtucket's elected officials, or the PWSB ratepayers who live in Pawtucket, should pay for these costs.¹²⁷

In its brief, the Town of Cumberland focused almost entirely on the tax issue. The Town made six arguments against the imposition of a surcharge. First, Cumberland

¹²⁵ Id. at 24.

¹²⁶ Central Falls' Post-Hearing Brief, pp. 1-6.

argued that Cumberland residents receive the same water from PWSB as other ratepayers under substantially similar conditions.¹²⁸ Second, Cumberland argued that a tangible tax on a water utility's pipes by another municipality is not unique in the State of Rhode Island and that the Commission has not previously imposed a surcharge on a municipality's ratepayers to recover such a tax.¹²⁹ Third, PWSB never took a formal vote authorizing a surcharge as shown by the Board's January 14, 2003 minutes authorizing the filing of a rate case.¹³⁰ Fourth, PWSB did not provide a revised surcharge calculation as requested by the Commission.¹³¹ Fifth, it is up to the court to decide the tax dispute between the utility and the Town, not the Commission.¹³² Sixth, the Commission does not have adequate information in the record upon which to accurately calculate a surcharge.¹³³

In a footnote, Cumberland also argued that the Commission should have allowed the Town to submit its data responses in full on the first day of the hearing because the hearing process took four weeks. Cumberland relied on the fact that the Commission allowed the Division to present updated schedules on the last day of the hearing.¹³⁴

The Division reiterated its arguments as stated through pre-filed and live testimony regarding the items still in dispute.¹³⁵ Addressing the Cumberland rate differential, the Division indicated that it was not a concept easily embraced. However, the Division believed that if the Commission were to implement a rate differential, the

¹²⁷ *Id.* at 6-7.

¹²⁸ Cumberland's Post-Hearing Brief, pp. 3-4.

¹²⁹ *Id.* at 5-7.

¹³⁰ *Id.* at 8.

¹³¹ *Id.* at 8-9.

¹³² *Id.* at 10-11.

¹³³ *Id.* at 11-14.

¹³⁴ *Id.* at 9, n.6.

¹³⁵ Division's Post-Hearing Brief, pp. 1-12.

differential would be reasonable based on the belief that the new tax was on facilities that benefit only Cumberland residents.¹³⁶ The Division noted that without being able to obtain adequate information from Cumberland, it was unable to fulfill its statutory duty to make an appropriate recommendation to the Commission. The Division recognized that at the start of the hearings, Cumberland provided the requested information, but argued that “Cumberland’s compliance with the discovery process, however, came too late in the course of the proceedings for the Division’s expert consultant to properly evaluate the discovery materials.” The Division stated that whether the proposed rate differential has been rendered moot by the late compliance is best left to the sound discretion of the Commission.¹³⁷

X. Commission Findings

This case has been well advocated by the parties to the Docket. The PWSB has presented a strong case for the necessity of some increased need for additional revenue. The Division has done an excellent job advocating for the ratepayers. The other parties have made their specific issues well known to the Commission. Therefore, the Commission is left to determine which positions best serve the interests of the ratepayers. An important aspect of that analysis is balancing the needs of the utility to provide sufficient amounts of potable water to its ratepayers with the desire to set the rates as low as possible.

After a review of the evidence presented, the Commission finds that PWSB requires a revenue increase of 21.13%, to collect an additional \$2,382,459 for operating revenues, for a total revenue requirement of \$13,933,789. The revenue increase shall be

¹³⁶ *Id.* at 13, n. 5.

¹³⁷ *Id.* at 12-13.

applied across the board on all rate classes. The effect on a typical residential customer, a family of four using 100HCF per year will be an increase in the annual bill of \$47.69, from \$225.72 to \$273.41.¹³⁸

With regard to the items in dispute, the Commission finds as follows:

A. Wholesale Revenue

PWSB claims that the same 5 year average (1998-2002) used for retail sales is appropriate for wholesale sales, resulting in 630,530 HCF. The FY 2003 wholesale sales were 567,004 HCF. The Division claims that a nine year average of 692,013 HCF (including FY 2003) is appropriate. Ms. Crane argues that a 9 year average would better normalize the wholesale consumption. The monetary difference between the 2 positions is \$86,568. While it does appear that based on FY 2003 wholesale volumes, consumption is decreasing, in reality, future consumption is a best guess and both arguments are reasonable. The Commission accepts PWSB's position of 630,530 HCF. This is based on the average usage over the same time period as that used for retail usage. Also, due to the wet spring & summer, PWSB's sales were low in FY 2003 and have most likely continued to be low this year as opposed to prior years. As a result, PWSB's short term cash inflows will likely be reduced. Accepting the PWSB position will help to alleviate that problem.

B. Treatment Plant Costs

PWSB is requesting funding of \$1,137,700 in treatment plant costs for the current plant. There are two issues relating to treatment plant costs: (1) refunding the IFR money that was used for O&M expenses in accordance with the interim relief in the amount of

¹³⁸ A copy of the PUC Worksheet developed as a result of the Commission's decision is attached hereto as Appendix A.

\$359,700 and (2) funding future O&M expenses in the amount of \$778,000 annually. The Division recommends not funding the \$359,700 and allowing funding of \$778,000 over two years rather than one.

The Commission is disallowing the request to fund the repayment of the \$359,700. PWSB should still have sufficient IFR funds to complete its IFR projects through 2012.¹³⁹ With regard to the \$778,000, the funds should be collected through rates in one year because allowing it to be collected over two years would not collect the funding until 30 months from the effective date of the rates, or March 2006. This money is for repairs on the existing plant scheduled to be completed by FY 2005.

C. IFR

PWSB has requested an increase in IFR of \$638,000, from about \$2.033 million to \$2.671 million. The Division recommends funding this over 2 years at \$319,000 per year. The Commission believes that this would not be wise given that PWSB already struggles to fund IFR projects. Based on Division Exhibit 6, the IFR Requirements through 2012 are approximately \$18.9 million. IFR Funding at the level of \$2.671 million will provide approximately \$21.3 million. The Commission accepts PWSB's position to allow funding of \$638,000 over one year. To fund an increase in IFR over two years would only lead to further delays.

D. Employee Funding

Information provided through the discovery process indicated that PWSB had two vacancies. The Division recommends that funding for one position be eliminated as it is normal to have vacancies and throughout recent history, PWSB has operated with an average of 62 employees. The Division quantifies the amount of funding to eliminate by

taking the average of non-administrative salaries. They fix the amount at \$43,247 (salary plus taxes). PWSB has testified in the past that often times the vacancies existed due to lack of funding. In this case however, PWSB stated that the positions are not truly vacant, but are being filled by full time temporary employees.

PWSB has also argued that the vendor fee is based on the fact that PWSB has 66 funded positions and if there are fewer positions, the vendor will not have to staff all positions for which it is collecting a fee. The vendor is only required to employ as many employees as are actually transferred with the transfer of operations. Ms. Marchand explained that the vendor is expected to be responsible for 17 employees less two that PWSB will keep, translating to a budget of 15 employees in the vendor fee. She clarified that the vendor will be responsible for hiring permanent replacements for the two temporary employees and that those salaries are included in the vendor's fee.

The Commission is allowing funding for only 65 employees and is requiring PWSB to transfer the 17 employees Ms. Marchand testified will be transferred because to do otherwise, could allow the vendor an undue reduction in expenses – expenses covered through rates.

E. Training & Education

The test year training & education expense was \$7,519. PWSB requested \$12,000. The Division recommends \$10,000 which was the amount allowed in the prior rate case. Mr. Woodcock stated that the increased funding is required since the cost for NEWWA courses has increased and PWSB also plans to begin sending board members to training regarding water issues. After the hearings, PWSB provided several supporting documents to justify the increase, but has not provided documentation to support a claim

¹³⁹ See Division Exhibit 6 (DIV 1-3).

anywhere near \$12,000. Therefore, the Commission is denying PWSB's request for an additional \$2,000.

F. Postage

PWSB has requested \$32,000 for postage but has provided support for only \$29,000. PWSB has requested that they be allowed to keep the extra \$3,000 in case they need money somewhere else. The Division recommends approval of only the \$29,000. The Commission is denying \$3,000 of the request, allowing the \$29,000 as the additional \$3,000 does not satisfy the 'known & measurable' requirement.

G. EPA Fine

In the test year, PWSB was fined \$2,000 for not having a stand alone "Spill Prevention Control and Countermeasure" plan for an above ground heating oil tank. PWSB wishes to recover this amount in rates. The Division has recommended the Commission reject the request. As the fine was both the result of failure to comply with an EPA Regulation and a one time charge that should have been taken out when the test year was normalized, the Commission rejects funding for this item because rates are set prospectively.

H. Chemical Expense

PWSB is requesting \$363,961 for chemical expenses based on using FY 2003 chemical quantities at 2004 bid prices. The Division is recommending \$342,147 based on using 2004 bid prices on Test Year (FY 2002) quantities with an upward adjustment to account for new chemicals. The Commission finds that it is reasonable to use the 2004 bid prices and Test Year quantities and accept PWSB's request for new chemical expenses.

I. Regulatory Expense

PWSB requested funding of \$158,983 for rate case expense. The Division recommended funding of \$58,659 which is the average of the last 3 rate cases collected over 2 years. PWSB argued that Regulatory Expenses should not be based solely on rate case expenses but on the annual assessment, approximately \$20,000, by the Commission as well. PWSB's FY 2003 expenses were \$110,969, including the Commission/Division annual assessment, preparation for the instant case and participation in the interim hearing. FY 2003 also included all expenses from Docket No. 3452, the investigation of the treatment plant. FY 2004 will include portions of this docket and the request for debt service funding for the new plant. The Commission finds that the Division's position is reasonable to cover rate case expense and the PUC assessment. Therefore, the Commission allows \$117,318 to be recovered over two years for an annual collection of \$58,659.

J. O&M Reserve

In Docket No. 3378, it was envisioned that the O&M Reserve would be funded by December 31, 2004. It is expected that PWSB's request of one-third of 25% of its total operating and maintenance expense will provide full funding of the reserve by early 2005. It is expected that the Division's recommendation will provide full funding of the reserve by late 2006.

O&M Reserve equals 25% of the total O&M Expense collected over three years. Therefore, the actual number is driven by the allowed O&M Expense. The Commission accepts PWSB's calculation because Mr. Simeone testified that PWSB's CWFA interest rate is based on what PWSB would get on the market on its own. The sooner the account

is funded, the sooner PWSB will get a better rate. This method of funding is consistent with the Commission's Order in Docket No. 3378 and Ms. Gurghigian testified that any action that is viewed as a step back on commitment could adversely affect PWSB's interest rate.

K. Operating Revenue Allowance

PWSB is requesting the Operating Revenue Allowance be calculated on 1.5% of total expenses. The Division is recommending allowing 1.5% of operating expenses only. The actual number is driven by actual expenses. The Commission accepts the Division's method of calculation based on the fact that the Allowance is designed to address unexpected fluctuations in operating expenses. Ms. Crane testified that these costs fluctuate more than debt service. PWSB's debt service is expected to rise dramatically over the next few years. This method is consistent with the Commission's decision in Narragansett Bay Commission's ("NBC") most recent rate case. NBC is another utility whose debt service is rising quickly.

L. Central Falls

i. Treatment Plant

Central Falls argues that 15.7% of the increase is directly attributable to the costs associated with the delay in building a new treatment plant and therefore, Central Falls ratepayers should not have to pay any costs associated with the upkeep of the treatment plant. According to Mayor Matthews, "These expenditures would have been totally unnecessary but for the City of Pawtucket's interference with the orderly business of selecting a vendor." Ms. Marchand argues that because the new plant will benefit all PWSB customers, including those in Central Falls, all customers should bear the burden

of the costs. Mr. Catlin argues that there is no way to quantify what repairs to the existing treatment plant would have been necessary absent the delay.

The Commission finds that the expenses should be spread evenly. The delay was not caused by PWSB. The money being spent is to provide potable water to all ratepayers, including those in Central Falls. Central Falls did not specifically identify the costs of the delay in relation to costs that would have been incurred absent the delay.

ii. Rate Design

Central Falls argues that because it is no longer receiving a franchise fee from PWSB as the franchise agreement was terminated last year, it should now be allowed to either: collect a transport fee from PWSB; have its rates reduced by some currently uncertain amount; or have PWSB ordered to maintain a system it does not even own without any agreement between PWSB and Central Falls regarding maintenance.

Ms. Marchand argues that there is no support in the record for a transport fee. She indicates that when asked to provide a financial basis for this fee in Data Request 1-15, the City provided no substantive information. Furthermore, CF has not indicated how much a transport fee should be.

In its brief, Central Falls argued that it is the utility's burden to show that it is charging non-discriminatory rates. However, a party proposing an alternative to a utility's rate design has the burden of providing sufficient evidence to the other parties and to the Commission in order to determine whether the rates are unjustly discriminatory and, if they are, the appropriate calculation of the rates.

First, Central Falls customers are all retail customers – all billing, meter reading and collection is done by PWSB. With the exception of the maintenance issue, Central

Falls customers look just like other retail customers. Second, Central Falls was asked for a detailed accounting of its expenses in maintaining its system. What Central Falls provided in response was a generalized determination that 10% of its City maintenance fees go to maintaining the system. However, in order to come up with a dollar figure, several guesses and assumptions need to be made, rendering any figure unreliable. Furthermore, when questioned at the hearing regarding evidence, Mr. Oliverio stated that he was simply making legal argument and that his position was that the rates would be discriminatory. Legal argument and generalized numbers do not rise to the level of substantial evidence upon which the Commission can make a determination of any reasonable fee or rate reduction to Central Falls customers. Finally, Central Falls never made its data responses a part of the record and, therefore, they are not exhibits upon which the Commission can base its decision.

PWSB does not own the Central Falls System and has no right to maintain it. There was no agreement between the PWSB and Central Falls regarding maintenance of the system. The Commission will not order PWSB to enter into such a contract at this time. Furthermore, PWSB does not contract with the Central Falls' municipal employees. Therefore, requiring PWSB to maintain Central Falls' system would be requiring PWSB, first, to trespass on the system and second, possibly to contract with Central Falls' municipal employees for the work, adding further cost. Finally, Central Falls has another option; it can become a wholesale customer and do all of its own billing and maintenance.

In sum, the Commission finds that Central Falls retail customers have sufficient similarities to other retail customers to pay the same rates as other retail customers. The

Commission finds that the rates are not discriminatory. The Commission finds that Central Falls did not provide adequate information upon which the Commission could determine how much a reasonable rate differential or maintenance fee would be if Central Falls customers were substantially different than other retail customers of PWSB. The Commission orders PWSB to file a full cost of service study and rate design recommendation with its next full rate case, taking into account any differences between PWSB retail customers and Central Falls retail customers, including any avoided maintenance costs or any additional maintenance costs that may be required after a purchase of the system. PWSB shall evaluate and provide engineering reports and costs for separating the system if a purchase price is not agreed to and approved prior to its next full rate case.

M. Cumberland

PWSB and the Division agree that the Commission has the authority to set a different rate for different classes of customers. After reviewing the arguments of both parties, the Commission agrees that it may set a different rate for customers in different geographical areas. However, the Commission still has to have justification for the rate differential. In other words, the Commission cannot step into the shoes of a Superior Court judge and determine whether the valuation and related tax increase is appropriate. That is exactly what PWSB has asked the Commission to do. PWSB has asked the Commission to implement a rate differential to cover only the disputed valuation and related tax increase without looking at all property taxed by Cumberland.

PWSB has not made the argument that Cumberland ratepayers should be responsible for all taxes on real and tangible property assessed on PWSB by Cumberland.

In fact, PWSB has settled its real property tax dispute with Cumberland. PWSB has also not made the argument that the Commission should review all property in Cumberland and determine whether or not the property in question benefits all ratepayers.

Although arguing that the Commission does possess the authority to adjust the rate design, the Division quotes its witness, stating: “property subject to taxation is normally used for the benefit of all customers. Under such circumstances, it would be inappropriate to recover the property taxes assessed by a given municipality. Instead, it is normally appropriate that all property taxes be recovered from all customers as part of base rates.”

PWSB has one burden of proof in this rate case. It needs to show that its requested increase is based on the evidence. The evidence for the increase in taxes is the tax bill from the City of Cumberland. For PWSB to ask the Commission to impose a rate differential on only the increase because Cumberland has not provided PWSB with information that would support its appeal in state court is to ask the Commission to determine whether the valuation and subsequent tax is appropriate. The jurisdiction to make this determination lies with the Superior Court.

However, this finding is in no way intended to suggest that the Commission does not believe it could not impose a rate differential based on geographic boundaries if a cost of service study or other circumstances were to warrant. The Commission most certainly does have the authority to set different rates for different classes of customers so long as those rates are reasonable and not discriminatory.

In footnote six of its brief, Cumberland argued that the Commission erred in not allowing the last minute data responses because the final hearing was four weeks after the

first hearing. This case was supposed to be over in one day, two at the most. In reviewing the transcript, much of the delay was caused by Cumberland's participation at the hearings through extended arguments. Cumberland should not be able to benefit from this. Cumberland's second reason for arguing that the Commission should have allowed the last minute data responses was that the Commission allowed the Division to provide additional schedules on the final day of hearings when Ms. Crane testified. The difference here is that the Division submission of 9/18/03 was in direct response to updates received from PWSB during the hearings and was in response to testimony received during the hearings. Witnesses make adjustments at hearings all of the time. Cumberland filed no testimony throughout the entire case, did not comply with Commission discovery rules and should not be allowed to benefit from its inaction.

Normally, significant discovery issues do not arise in the Commission's dockets. The Commission's Rules of Practice and Procedure set forth the Commission's desire that each case include full and free disclosure of discovery. Statutorily, the Commission is allowed six months from the requested effective date to dispose of a rate case. Therefore, any procedural delay of a party has the potential to cause a substantive delay in the case and the potential to cause harm to the parties. Unfortunately, this case is indicative of what can occur when a party does not comply with the Commission's rules. Therefore, in the future, full intervention will only be allowed to a movant if that movant makes an affirmative showing that it will be filing pre-filed testimony. The Commission has allowed interested parties to be put on a service list in order to monitor a case.

O. Restricted Accounts

PWSB shall restrict the following accounts: Debt Service, IFR, Capital Lease Payments and O&M Reserve. PWSB shall notify the Commission immediately upon resolution of the Cumberland tax dispute. In the event PWSB receives a refund, it shall deposit said funds into a restricted account and provide the Commission with a recommendation regarding the disposition of said funds. For example, the money could be used for debt service rather than a direct refund to customers.

Accordingly, it is

(17574) ORDERED:

1. Pawtucket Water Supply Board's Application for a General Rate Increase, filed on February 28, 2003, is hereby denied and dismissed.
2. Pawtucket Water Supply Board is granted a revenue increase of \$2,382,459, for a total cost of service of \$13,933,789 to be applied to usage on and after October 4, 2003.
3. Pawtucket Water Supply Board shall comply with all other findings and instructions as contained in this Report and Order.

EFFECTIVE AT WARWICK, RHODE ISLAND PURSUANT TO AN OPEN MEETING DECISION ON OCTOBER 3, 2003. WRITTEN ORDER ISSUED OCTOBER 10, 2003.

PUBLIC UTILITIES COMMISSION

Elia Germani, Chairman

Kate F. Racine, Commissioner

Robert B. Holbrook, Commissioner

**PUC Worksheet
Docket 3497
Pawtucket Water Supply Board
Allowed Cost of Service**

	<u>PWSB Rebuttal (a)</u>	<u>Division Adjustments</u>	<u>Division Position</u>	<u>Commission Adjustments</u>	<u>Allowed by Commission</u>
1 Present Rate Revenue	11,277,415	86,568	11,363,983	(86,568) b	11,277,415
2 Miscellaneous Revenue	273,915		273,915		273,915
3 Total Proforma Revenue	11,551,330	86,568	11,637,898	(86,568)	11,551,330
Operating Expenses					
4 Administrative Expense	2,177,764	(147,571)	2,030,193	0	2,030,193
5 Customer Service Expense	223,428	(3,000)	220,428	0	220,428
6 Source of Supply Expense	827,686		827,686		827,686
7 Pumping Expense	651,329	(45,000)	606,329	45,000 c	651,329
8 Purification Expense	2,363,629 a	(596,314)	1,767,315	325,298 d	2,092,613
9 Transmission & Distribution	1,277,759		1,277,759		1,277,759
10 Engineering Expense	473,807		473,807		473,807
11 Meter Department Expense	430,145		430,145		430,145
Subtotal	8,425,547	(791,885)	7,633,662	370,298	8,003,960
Capital Costs					
12 RICWFA Expense	100,000	0	100,000	0	100,000
13 Bond Principal	930,000		930,000		930,000
14 Bond Interest	1,291,045		1,291,045		1,291,045
15 Lease Payments	110,689		110,689		110,689
16 IFR Rehab	2,671,039	(319,000)	2,352,039	319,000 e	2,671,039
17 Treatment/Pumping Storage	149,200	(129,200)		20,000 f	40,000
18 O&M Reserve	702,129	(250,078)	452,051	214,946 g	666,997 h
19 R&R Reserve	0		0		0
Subtotal	5,954,102	(698,278)	5,255,824	553,946	5,809,770
20 Total Expenses	14,379,649	(1,490,163)	12,889,486	924,244	13,813,730
21 Add: Operating Revenue Reserve	215,695	(101,190)	114,505	5,554	120,059 i
22 Rev Requirement (Cost of Service)	14,595,344	(1,591,353)	13,003,991	929,798	13,933,789
23 Increase Required	3,044,014	(1,677,921)	1,366,093	1,016,366	2,382,459
24 Increase - Rate Revenue	26.99%		12.02%		21.13%
25 Increase - Total Revenue	26.35%		11.74%		20.62%
Current bill (Residential 100 HCF)	225.72		225.72		225.72
Proposed Increase	60.93		27.13		47.69
Proposed New Bill	286.65		252.85		273.41

a PWSB rebuttal adjusted for revised chemical cost requested by PWSB

b adjust division position to accept PWSB wholesale revenue request (86,568)

c adjust division position to reflect 1 year funding of pumping facility expense 45,000

d adjust division position to reflect 1 year funding of purification facility expense 328,000
adjust division chemical expense to reflect PWSB wholesale position (2,702)
325,298

e adjust division position to reflect rate year IFR of \$2.67 million 319,000

f adjust division position to reflect 1 year funding intermin costs 20,000

g adjust division O&M reserve to accept PWSB request 214,946

h O&M reserve = (Total Operating expense x .25 x 1/3) (PWSB request)

i Operating Rev. Res = (Total Operating expense x 1.5%) (Div position)