

DW 05-112

HAMPSTEAD AREA WATER COMPANY

**Investigation into Permanent Rates and
Petition for Approval of Fire District and Fire Protection Rates**

Order Approving Step Adjustment for Local Property Taxes

ORDER NO. 24,734

March 23, 2007

I. PROCEDURAL HISTORY AND BACKGROUND

Hampstead Area Water Company (HAWC) is a regulated water utility with more than 2,500 customers in approximately a dozen communities throughout southeastern New Hampshire. On December 29, 2006, HAWC submitted correspondence and supporting schedules to the New Hampshire Public Utilities Commission (Commission) requesting approval of a step adjustment in rates to recover the cost of local property taxes. This filing was contemplated as part of the Commission's Order No. 24,626 (May 26, 2006), approving a settlement agreement calling for an increase in permanent rates for HAWC. A more complete description of the history of this docket can be found in Order No. 24,626.

Specifically, Section IV.4 of the settlement recognized that contributed plant added to HAWC's books would likely increase HAWC's local property tax liability and that local property taxes associated with that plant had not yet been assessed by the affected municipalities.¹ Section IV.4 allowed HAWC to petition the Commission for consideration of a

¹ "Contributed plant" in this context refers to assets on the books of the utility that it acquired without making an investment in them. Typically, this occurs when a developer builds a housing subdivision and installs the infrastructure necessary to bring utility service into the subdivision, presumably recovering the cost of the investment in the price of the housing units. In these circumstances, the utility does not recover on the value of these assets through rates, since that would amount to the homeowners paying twice, but notwithstanding the book value of zero for ratemaking purposes the assets are valuable property owned by the utility that is subject to real estate taxation.

step adjustment for local property taxes, no later than March 31, 2008. HAWC's December 29, 2006 filing was consistent with that stipulation provision and Order No. 24,626.

II. STAFF INVESTIGATION OF STEP ADJUSTMENT

HAWC proposed an increase in its local property tax expense of \$35,040. To recover this additional expense, HAWC proposed an increase of \$0.13 in its current consumption rate to \$3.70 per 100 cubic feet of water usage. HAWC's proposal for the step adjustment is based on the total local property taxes of \$73,310 that it was assessed during the year 2006. This amount is \$35,040 higher than the local property taxes of \$38,270 assessed to HAWC during 2005.

On March 9, 2007, Staff filed a letter with the Commission recommending the Commission approve HAWC's request, with modification. Staff conducted discovery relative to HAWC's proposal and attached copies of HAWC's responses to its letter. After reviewing the filing and data responses, Staff concluded HAWC was entitled to a \$36,116 increase in its annual local property expense, rather than HAWC's proposed \$35,040.

Staff explained that its recommendation was \$1,076 higher than HAWC's proposal because it used a different methodology than HAWC. According to Staff, HAWC based its calculations on the difference between the total local property tax assessments for the years 2005 and 2006, and therefore reflected the change in property tax expense resulting from the increases in property valuation on various parcels, and also reflected the changes in expense due to the differences in property tax rates applied to these parcels between 2005 and 2006. Staff believed the concern addressed by the settlement was limited to the anticipated increase in property valuations, as opposed to changes in the applicable tax rates. Staff deemed it inappropriate to use a subsequent year's tax rate in determining a step adjustment since the original revenue requirement was determined based upon the tax rates in effect during 2005. Staff arrived at the \$36,116 increase by first calculating the valuation differential between assessed values for the

years 2005 and 2006 on the various parcels and then applying the pertinent 2005 tax rates to these calculated differentials to derive the increase in property tax expense. After accounting for the increase in property tax expense, Staff proposed that the Commission approve a revenue requirement of \$1,273,792 for HAWC.

Staff recommended a \$0.14 increase in HAWC's current consumption rate to an amount of \$3.71 per 100 cubic feet of usage.² Staff stated that HAWC's customers will pay an average annual bill of approximately \$431.06, which is \$12.22, or 2.92 percent, higher than the current average annual bill of \$418.84.

Lastly, Staff indicated it had contacted the Office of the Consumer Advocate (OCA) to explain Staff's recommendation. Staff stated that OCA authorized Staff to represent to the Commission that OCA took no position on HAWC's filing.

III. COMMISSION ANALYSIS

RSA 378:7 authorizes the Commission to establish just and reasonable rates for a utility after conducting a hearing. In determining just and reasonable rates, the Commission must balance the consumers' interest in paying rates no higher than are required with the investors' interest in obtaining a reasonable return on investment. *Eastman Sewer Co.*, 138 N.H. 221, 225 (1994). In circumstances where a utility seeks to increase rates, the utility bears the burden of proving the necessity of the increase pursuant to RSA 378:8.

In Order No. 24,626 the Commission found Staff and the parties' stipulation agreement to be reasonable and for the public good and HAWC's overall consolidated revenue requirement

² For background, HAWC's consolidated rates as approved in Order No. 24,626 consisted of a \$100 annual fixed charge per customer and a \$3.15 per 100 cubic foot consumption charge. In Order No. 24,720 (December 28, 2006) in Docket No. DW 04-132, the Commission approved a step increase to recover the cost of a 500,000 gallon water storage tank as well as a tank level monitoring and telemetry system. This increased HAWC's consumption rate by \$0.42 to \$3.57 per 100 cubic feet. Staff's pending recommendation is to increase the consumption charge by another \$0.14 which will result in a total consumption rate of \$3.71 per 100 cubic feet.

to be just and reasonable. In approving HAWC's revenue requirement, the Commission approved then known annual operating expenses. In approving the stipulation, as stated earlier, a step adjustment was approved to offset the expected increase in property tax expense, once those taxes became known. We have reviewed HAWC's filing of updated property tax expense information as well as the Staff recommendation dated March 9, 2007, and we find that the proposal to increase HAWC's rates to account for its increased property tax expense due to the increase in assessed valuation is consistent with the stipulation agreement approved in Order No. 24,626.

We have employed step adjustments to rates as a means of ensuring that a regulated utility retains its ability to earn a reasonable rate of return after implementing large capital projects which increase its rate base. Specifically, we have employed step adjustments to avoid placing a utility in an earnings deficiency immediately after a rate case in which a revenue requirement was based on a historical test year. Additions to rate base are not the only factors that can affect a utility's rate of return. Consistent with the standards enunciated in *Federal Power Commission v. Hope Natural Gas Co.*, 320 US 592, 602 (1944) that rates be just and reasonable, we customarily determine a revenue requirement by multiplying rate base, which is plant in service minus accumulated depreciation, times an approved rate of return, plus expenses and taxes. In this case, HAWC has not increased its rate base; rather, it has incurred a substantial annual expense associated with increased local property taxes. This affects HAWC's revenue requirement. In light of the increase in HAWC's property tax expenses, we deem it reasonable and in the public interest to increase HAWC's revenue requirement.

We also find that granting HAWC's request for a step adjustment is in the public interest because it will help eliminate the need for an additional full rate proceeding on the heels of

HAWC’s most recent rate proceeding. This will avoid additional rate case costs to the utility and its customers.

Accordingly, we approve HAWC’s request for a step adjustment in revenues, as modified by Staff, in the amount of \$36,116, resulting in a new revenue requirement of \$1,273,792. We direct HAWC to submit revised tariff pages reflecting new customer rates as well as HAWC’s calculation of those rates from this revised revenue requirement.

Based upon the foregoing, it is hereby

ORDERED, that a step adjustment in the amount of \$36,116 to Hampstead Area Water Company Inc.’s revenue requirement is hereby approved; and it is

FURTHER ORDERED, that Hampstead Area Water Company is authorized to raise its consumption rate from \$3.57 per 100 cubic feet of water to \$3.71 per 100 cubic feet of water to reflect the approved increase in its revenue requirement; and it is

FURTHER ORDERED, that Hampstead Area Water Company, Inc. file a compliance tariff within fourteen (14) business days of the date of this order.

By order of the Public Utilities Commission of New Hampshire twenty-third day of March, 2007.

Thomas B. Getz
Chairman

Graham J. Morrison
Commissioner

Clifton C. Below
Commissioner

Attested by:

Debra A. Howland
Executive Director & Secretary