

DW 04-117

HANOVER WATER WORKS COMPANY, INC.

Petition For Authority To Issue Securities And To Increase Rates

Order Approving Stipulation For Financing And Rate Recovery

ORDER NO. 24,393

October 29, 2004

Appearances: McLane, Graf, Raulerson & Middleton, P.A., Sarah B. Knowlton, Esq. on behalf of Hanover Water Works Company, Inc.; F. Anne Ross, Esq., Office of Consumer Advocate; and Suzanne Amidon, Esq., on behalf of the Staff of the New Hampshire Public Utilities Commission.

I. BACKGROUND AND PROCEDURAL HISTORY

On July 9, 2004, Hanover Water Works Company, Inc. (Hanover) filed with the New Hampshire Public Utilities Commission (Commission) a Petition for Authority to Issue Securities and to Increase Rates. Hanover supplies water to approximately 1,800 customers in the Town of Hanover.

Hanover petitioned for authority pursuant to RSA 369 to borrow up to \$6,500,000 to construct a new water filtration and treatment system, and to build a 1,000,000 gallon water storage tank (Projects). Hanover stated that these Projects are necessary to comply with the new requirements of the Safe Drinking Water Act (SDWA) and address customer complaints regarding taste, odor and color. Hanover also requested authority to increase customer rates to a level that will enable Hanover to pay the debt service on the loan and to earn a reasonable return on its invested capital. In its Petition, Hanover estimated that the rate increase would be approximately 66%.

The Commission issued an Order of Notice on July 23, 2004, scheduling a Prehearing Conference for August 19, 2004, and ordering the publication of the Order of Notice

pursuant to N.H. Admin. Rule, Puc 203.01. The Commission further ordered that any party seeking to intervene in the proceeding file a Petition to Intervene with the Commission no later than August 16, 2004.

On July 23, 2004, the Office of Consumer Advocate (OCA) notified that Commission that it would participate in the Docket on behalf of residential ratepayers. The Prehearing Conference was held on August 19, 2004. Following the Prehearing Conference, Hanover, the OCA and Commission Staff (Staff) met in a technical session and established a Procedural Schedule. The Commission approved the Procedural Schedule by Secretarial Letter dated August 26, 2004. Discovery was conducted as provided by the Procedural Schedule.

On September 22, 2004, the Commission held a Public Hearing in Hanover to permit Hanover customers to comment on Hanover's Petition. Following the Public Hearing, Hanover, the OCA and Staff negotiated a Stipulation which was filed with the Commission on October 8, 2004. The Stipulation is entitled "Stipulation Between Hanover Water Works Company, the Staff of the New Hampshire Public Utilities Commission and the Office of the Consumer Advocate." The Stipulation includes two attachments: A, "Calculation of Revenue Requirement" and B, "Estimated Impact on Average Residential Customers."

On October 20, 2004, the Commission held a duly noticed hearing and received the Parties and Staff's testimony in support of the Stipulation.

II. SUMMARY OF THE STIPULATION

The Stipulation contains a recitation of the facts which prompted Hanover to seek authority to finance the construction of a water filtration system. A summary of those facts follows.

Hanover has provided water service to its customers for over 100 years. Hanover's water supply is an unfiltered surface water source for which it has been granted a Waiver of Filtration from the New Hampshire Department of Environmental Services (NHDES). The Waiver remains in effect as long as Hanover meets certain "avoidance" criteria which provide strict controls on the watershed and the water.

In recent years, Hanover has found it increasingly difficult to comply with the avoidance criteria. In addition, the remedial efforts used by Hanover to achieve compliance have had the secondary effects of creating significant taste, color and odor complaints from its customers. Hanover retained the engineering firm of Provan and Lorber, Inc. to evaluate methods to improve its water quality and address its need for additional water capacity. After reviewing the Provan and Lorber study, Hanover retained Wright-Pierce to conduct a safe yield analysis. Wright-Pierce recommended that Hanover construct a Membrane Filtration Facility to treat its water and help achieve compliance with state and federal drinking water requirements. Wright-Pierce also recommended the construction of a new water storage facility. Hanover estimates the Projects will cost \$6,500,000 and will be completed in the second quarter of 2006.

Hanover intends to finance the Projects through the use of the Drinking Water State Revolving Funds (DWSRF), which is administered by NHDES. Initially, NHDES approved Hanover for DWSRF funding for the amount of \$700,000 for the design and

construction of the Membrane Filtration Facility and the purchase and installation of the additional water storage tank. This initial loan would bear an interest rate of no greater than 3.728% for a term of 20 years. On August 4, 2004, NHDES approved Hanover to borrow an additional \$5,800,000 million for construction, thus providing for complete funding of improvements through DWSRF at interest rates of less than 4%. As a result, Hanover amended its estimate of rate increases needed to service the debt to 53.07%, down from the 66% rate increase anticipated in its Petition. Hanover stated that NHDES requires that Hanover receive the Commission's approval no later than November 1, 2004, to retain eligibility to borrow DWSRF funds.

The Stipulation states the agreement of the Parties that the construction of the Projects is a prudent means of providing adequate, safe and reliable water service under all conditions to the customers of Hanover. In addition, the Parties agreed that funding the Projects through the DSWRF is in the public good. Under the Stipulation, Hanover agrees to submit the final terms of the financing to the Commission as soon as they are available. Furthermore, Hanover agrees that if the terms and conditions of the financing vary materially from the description it provided, the new or modified terms and conditions would be subject to Commission approval.

The Stipulation recognizes that rate increases will be required to provide Hanover with a sufficient cash flow to repay the issued securities. The Stipulation requires that such rate increase would be based only on the construction of the Projects. In requesting an increase, Hanover agrees to submit a filing to the Commission detailing the actual costs of the Projects,

the return on the capital assets of the Projects, the depreciation expense, and the direct expenses to be recovered through the rate increase.

Hanover further agrees, as stated in the Stipulation, that the rate increase would be effective on a service rendered basis on or after the date on which the relevant capital additions first provide service to the public. Attachments A and B to the Stipulation establish the methodology for calculating the rate increase, using the cost of debt capital for the financing for the Projects that are the subject of the petition. The Stipulation states that a rate increase shall be subject to the Commission's review and approval of the costs actually incurred for each Project to confirm that such costs are consistent with Hanover's petition in this case or that any costs in excess thereof were prudently incurred.

To assure that Hanover's customers are not billed for construction work in progress, the Stipulation requires Hanover to obtain meter readings that ensure customers are not billed for service rendered prior to the provision of service from the new capital additions. In addition, the Stipulation requires Hanover to proportionately assess the rate increase anticipated from the capital improvements across all customer classes.

The Stipulation does not prevent Hanover from filing a full rate proceeding at any time. Under the Stipulation, if Hanover requests a full rate proceeding, it may request that the adjustment to its rates resulting from the Projects be implemented in conjunction with the full rate proceeding, if administratively efficient. In such a case, the Projects must be in service as of the date of the final resolution of such a rate proceeding, and the methodology for calculating the rate adjustment shall be consistent with the Stipulation. Further, the Stipulation acknowledges that the Commission retains the right to review the prudence of the amounts actually expended in

constructing the Projects. However, in such an event, the Stipulation states that the issue of prudence of the Projects themselves as a means of addressing water quality, storage, and filtration issues as noted in the Petition shall not be subject to review.

III. COMMISSION ANALYSIS

Pursuant to the provisions of RSA 369:1, public utilities engaged in business in this State may issue evidences of indebtedness payable more than 12 months after the date thereof only if the Commission finds the proposed issuance to be “consistent with the public good.” The New Hampshire Supreme Court has further provided that the public good consideration involves looking beyond actual terms of the proposed financing to the use of the proceeds of those funds and the effect on rates to insure the public good is protected. See *Appeal of Easton*, 125 N.H. 205 (1984). We conduct our review of Hanover’s Petition in light of these authorities.

In the case at hand, Hanover has requested authorization to borrow up to \$6,500,000 from the DWSRF in order to finance the construction of a water treatment plant and a water storage tank. After reviewing the Petition and the Stipulation submitted by Hanover, Staff, and the OCA, we are satisfied that Hanover has substantiated the need for the Projects and we find that they are in the public good.

With respect to the request for a rate increase, we note that, we are not approving the proposed percent rate increase at this time; rather, we are approving the method by which Hanover may request an increase in rates to recover the costs of the Projects as set forth in the Stipulation, using the methodology identified in Attachment B. The Stipulation requires Hanover to file with the Commission documentation containing detailed actual costs of the

Projects, the allowed return on the capital assets of the Projects, the depreciation expense, and the direct expenses proposed to be recovered through the rate increase. Our review of this information will assure pursuant to RSA 378:28 that before the Projects can go into the rate base, the expenses proposed for recovery are prudent and the Projects are used and useful for the provision of utility service. These are appropriate measures to ensure customers are not charged for construction work in progress, which is prohibited by RSA 378:30-a. Hanover's agreement to read meters at the time the step adjustment is to take effect will also assure that any increase will only take effect on a service rendered basis. In addition, Hanover has proposed to institute the rate increase proportionately across all customer classes. For these reasons, we approve the method Hanover intends to pursue to request the step increase and we will review the proposed step increase and make our final determination as to the justness and reasonableness of the rate at that time.

With respect to the terms of the DWSRF financing, we find the proposed terms to be reasonable and in the public good. We will approve the proposed terms on the condition that the final terms be substantially similar to those stated in the Stipulation. Hanover must submit the final financing terms to the Commission for final review, any terms which vary substantially from the proposed terms will require a further proceeding.

Finally, we find that the financing is consistent with the public good. We will approve the Stipulation as a reasonable means of disposing of the matters raised in Hanover's petition in this docket.

Based upon the foregoing, it is hereby

ORDERED, that the Stipulation between Hanover Water Works Company, Inc., the Office of Consumer Advocate and the Commission Staff is **APPROVED**.

By order of the Public Utilities Commission of New Hampshire this twenty-ninth day of October, 2004.

Thomas B. Getz
Chairman

Graham J. Morrison
Commissioner

Attested by:

Michelle A. Caraway
Assistant Executive Director