

**STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION**

DW 08-052

PITTSFIELD AQUEDUCT COMPANY, INC.

Permanent Rate Proceeding

Order Approving Temporary Rates

ORDER NO. 24,929

December 31, 2008

APPEARANCES: McLane, Graf, Raulerson & Middleton, P.A., by Sarah B. Knowlton, Esq. for Pittsfield Aqueduct Company, Inc.; Locke Lake Colony Association by Michael Ranaldi and Deana Cowen; Mitchell Municipal Group, P.A., by Laura A. Spector, Esq. for Town of Pittsfield; Birch Hill Water District by Kirk W. Smith; Office of the Consumer Advocate by Rorie E. P. Hollenberg, Esq. on behalf of residential utility ratepayers; and Staff of the Public Utilities Commission by Marcia A. B. Thunberg, Esq.

I. PROCEDURAL HISTORY

Pittsfield Aqueduct Company (PAC) provides water service to customers in the Town of Pittsfield and to customers in Birch Hill, Sunrise Lake Estates, and Locke Lake Colony (together, North Country systems). PAC is a wholly owned subsidiary of Pennichuck Corporation.

On May 2, 2008, PAC filed a petition for temporary rates and an increase in permanent rates. PAC seeks, on a permanent basis, to increase its gross annual revenues by \$957,641. PAC requests recovery of this revenue increase from its customers as follows: \$200,503 from general metered and fire protection customers in Pittsfield (a 44.01% increase) and \$757,138 from North Country customers (a 239.52% increase). PAC also requests a step increase in the rates of its North Country customers to cover capital improvements planned for completion by November

2008. This proposed step increase would generate \$228,836 in additional revenues and represents an increase of 72.39% over test year revenues.

The proposed permanent rate and step increase would result in an increase of \$181.76 to the average annual residential bill for Pittsfield customers and an increase of \$682.72 to the average annual residential bill for North Country customers. If approved, the new average annual residential bill would be \$593.58 for Pittsfield customers and \$1,159.92 for North Country customers.

In addition to the proposed permanent rate and step increase, PAC requests the Commission to approve a temporary increase in its revenue requirement while the Commission conducts its investigation of PAC's permanent rate request. Specifically, PAC proposes a \$150,377 increase in revenues collected from customers in Pittsfield, which corresponds to a 33.01% rate increase compared to current rates and a \$567,854 increase in revenues collected from North Country customers, which corresponds to a 179.64% rate increase compared to current rates. PAC requested the temporary rates to take effect on June 1, 2008 on a service-rendered basis, or the date on which customers are notified, whichever is sooner. In support of its request, PAC filed schedules and the testimony of Bonalyn J. Hartley.

PAC also requested a waiver of the Commission's administrative rules requiring the filing of internal financial reports, balance sheets and income statements, and information on PAC's parent company. In support of the request, PAC stated that it had previously filed this information with the Commission and that filing it in this docket would be duplicative. In a letter filed on July 17, 2008, Staff concurred with PAC's waiver request, stating that PAC had filed the subject information previously with the Commission and that the information was

publicly available to members of the public and intervenors. The Commission approved PAC's waiver request by secretarial letter dated July 28, 2008.

On May 7, 2008, the Office of the Consumer Advocate (OCA) filed its notice of intent to participate in this docket. On May 12, 2008, PAC filed a cost of service study. On May 23, 2008, the Commission issued Order No. 24,857 suspending the taking effect of PAC's proposed permanent rates and setting a prehearing conference and technical session for July 16, 2008.

On June 30, 2008, Sunrise Lake Estates Association (Sunrise) filed a petition to intervene. Sunrise is a residential community of approximately 83 customers in the Town of Middleton. On July 1, 2008, the Locke Lake Colony Association (LLCA) filed a petition to intervene. LLCA is comprised of approximately 755 residential customers in the Town of Barnstead. Also on July 1, 2008, the Town of Pittsfield (Pittsfield) filed a petition to intervene. PAC provides residential and commercial water service to approximately 650 customers in Pittsfield. On July 7, 2008, the Birch Hill Water District (BHWD) filed a petition to intervene. BHWD is comprised of approximately 207 residential customers, some of whom are seasonal, in the Town of Conway.

On July 16, 2008, the Commission conducted a prehearing conference and Staff and the parties met in a technical session thereafter. On the same day, Staff filed a proposed procedural schedule developed by it and the parties. The Commission approved the procedural schedule by secretarial letter dated July 25, 2008.

On July 25, 2008, the Commission issued a secretarial letter setting public statement hearings for August 7, 13, and 27, 2008, in North Conway, Alton, and Pittsfield, respectively. The Pittsfield public statement hearing was later rescheduled to August 25, 2008, in a secretarial letter dated August 8, 2008.

On September 18, 2008, LLCA filed the testimony of Michael Ranaldi and Staff filed the testimony of James L. Lenihan. On September 26, 2008, Staff filed revised testimony of Mr. Lenihan. The Commission held a hearing on the issue of temporary rates on October 7, 2008.

II. POSITIONS OF THE PARTIES AND STAFF

A. Pittsfield Aqueduct Company, Inc.

According to its temporary rate petition and supporting testimony at hearing, PAC is earning 12.42% less than its allowed rate of return based on the books and records on file with the Commission. PAC's presently allowed rate of return is 8.42%. PAC attributed the decline in earnings to significant improvements in its North Country systems, which it acquired in 2006. Under PAC's current rate design, all customers are charged the same rates. PAC proposed to change this by placing Birch Hill, Locke Lake, and Sunrise Estates into one rate group and by placing Pittsfield into another rate group.

PAC's proposed temporary rate increase is 75% of its permanent rate increase, which represents a 33.01% increase for Pittsfield customers and a 179.64% increase for North Country customers. PAC stated that under the proposed temporary rates, bills for the average residential customer in Pittsfield would rise from \$412 to \$549 annually while bills for North Country customers would rise from \$282 to \$788 annually. Exh. 1 at 7 and 10.

At hearing, PAC testified that separating the customers into two rate groups is justified by the fact that the groups have different profiles. Pittsfield customers have surface water treatment, are both commercial and residential customers, are primarily full time customers, and have public and private fire protection. Hearing Transcript of October 7, 2008, (10/07/08 Tr.) at 17 lines 15-23. By comparison, Locke Lake has a residential customer base that is 42% seasonal. 10/07/08 Tr. at 62 lines 5-18. When PAC acquired the North Country systems, its

expected revenues were based on an average customer use of seven and one half to eight units per month, which is Pittsfield's average usage. After meters were installed in the North Country systems, however, PAC realized that the North Country systems' usage was much different than Pittsfield's and averaged only two units per month. 10/07/08 Tr. at 64 lines 13-24 and at 65 lines 1-11. PAC requests temporary rates to take effect June 6, 2008, which is the last date customers were notified. 10/07/08 Tr. at 31 lines 1-5.

B. Locke Lake Colony Association

In its pre-filed testimony, LLCA stated that PAC's temporary rate increase should cover only the operational costs until all parties can come to agreement on the breakdown of the capital expenditures. Exh. 6 at 1. LLCA acknowledged that PAC's net plant in the North Country systems increased by \$2,662,640, or 377%, over a span of 21 months. Exh. 6 at 2. LLCA stated that PAC's costs associated with its capital expenditures should be separated from PAC's operational costs and be spread out over 20 years at a fixed cost base for all customers. As an example, LLCA said that spreading \$5 million out over 20 years and over 2,700 customers would produce a monthly payment associated with capital expenditures of \$8.00 per customer. Exh. 6 at 2. LLCA opposed PAC's proposal to allocate the increased revenue requirement among North Country customers differently than among Pittsfield customers. LLCA argued that there is safety in numbers and it is difficult to predict when one or any of the systems will require major improvements. LLCA requested the Commission to consider the impact of these rates during these troubled economic times.

C. Town of Pittsfield

The Town of Pittsfield did not present witnesses at the temporary rate hearing but stated in closing that it is concerned with the level at which Pittsfield customers subsidize the North

Country customers. According to Pittsfield, if there is a blended rate, Pittsfield would see a 94% rate increase on a temporary basis, rather than the proposed 33% increase. For this reason, Pittsfield supports PAC's proposal to separate Pittsfield customers from the other systems and set separate rates. Pittsfield requested that, if the Commission approves temporary rates, the Commission approve separate rates as proposed.

D. Birch Hill Water District

BHWD did not present witnesses at the temporary rate hearing. In closing, however, it stated that PAC had done a good job in trying to maintain and improve the water system at Birch Hill. BHWD agreed that PAC is entitled to some temporary increase to its revenue requirement. BHWD stated that it is mostly concerned with the allocation of the increase between the fixed and volumetric charges to address the issue of part-time residents.

E. Sunrise Lake Estates

Sunrise did not participate in the temporary rate hearing but articulated its position at the prehearing conference. Sunrise recommended that the Commission consider spreading the costs of all the water systems owned by PAC and its affiliates among their approximately 31,000 customers, similar to the practice of electric utilities. Sunrise contended that \$4.3 million would be a drop in the bucket if spread out over more customers. Sunrise expressed concern that PAC's rate increase would be the last straw for struggling families living in Sunrise.

F. Office of the Consumer Advocate

OCA did not present witnesses at the temporary rate hearing. In closing, however, it objected to PAC's proposal to depart from consolidated rates and charge different rates in Pittsfield and in the North Country systems. OCA stated that RSA 378:27 allows the Commission to set reasonable temporary rates sufficient to yield a reasonable return on the costs

of property used and useful in the public service. According to OCA, the New Hampshire Supreme Court has recognized that setting temporary rates involves less stringent standards and is a more expeditious process than that required for the determination of permanent rates. OCA pointed to Staff's testimony that it has not yet analyzed PAC's cost of service study and stated that RSA 378:27 contains no provision for making changes to the way temporary revenue increases are collected. OCA stated the proposed separate rate increases will create a hardship to customers given their financial circumstances, the high cost of living, and the anticipated high costs of energy for this coming winter. OCA maintained that PAC's proposal for separate rates conflicts with the Commission's standing practice and policy of consolidating small water systems and rates to mitigate the impact of costly investments required to provide safe and adequate service. OCA contended that the temporary rate phase is an inappropriate time for the Commission to make drastic changes to customer rates and that Staff and PAC have not sustained their burden of proving the separate rates are just and reasonable. OCA also cited recent cases where parties or the Commission deferred making changes to rate design for purposes of temporary rates. OCA urged the Commission to maintain PAC's present rate design until PAC's permanent rate filing is fully investigated. OCA stated that the reconciliation mechanism contained in RSA 378:29 adequately protects PAC and customers while PAC's rate design is investigated in this docket.

G. Staff

Staff concurred with PAC's request for temporary rates. Through testimony of James L. Lenihan, Staff stated it had reviewed the books and reports on file with the Commission and agreed that PAC is earning a negative rate of return. According to Staff, PAC's proposed temporary rates would provide PAC with a reasonable rate of return while Staff and the parties

investigate the permanent rate request. Staff agreed with PAC that June 6, 2008, was the date that notice to all customers was complete and testified that making temporary rates effective June 6, 2008, was reasonable. 10/07/08 Tr. at 81 lines 1-12. Staff also agreed with PAC's proposal to separate customers into two rate groups for purposes of temporary rates. Staff stated that it was cognizant of the adverse impact such a large rate increase would cause to customers and that during the remainder of the docket it would be reviewing ways to mitigate the final rate increase.

III. COMMISSION ANALYSIS

Pursuant to RSA 378:27, the Commission may approve reasonable temporary rates for the duration of the proceeding if, in its opinion, the public interest so requires and the reports of the public utility on file with the Commission indicate it is not earning a reasonable return on its property used and useful in the public service. The standard for approval of temporary rates is less stringent than that for permanent rates. *Appeal of Office of Consumer Advocate*, 134 N.H. 651, 660 (1991). RSA 378:27 also contemplates that in fixing temporary rates, the necessary allocation of costs shall be made by reasonably practical and expeditious means, without such investigation as might be deemed necessary to a determination of permanent rates. *New England Telephone & Telegraph Co. v. State*, 95 N.H. 515, 518 (1949). Neither the method of allocation nor its result needs to be adopted in the final establishment of permanent rates. *Id.*

The temporary rate request before us includes a proposal for an increase in PAC's revenue requirement by a total of \$718,231 that PAC and Staff indicate would allow a reasonable rate of return until permanent rates are set. PAC's last authorized rate of return on net plant in service was 8.42%. Using the last authorized return on equity of 9.75% and with pro forma adjustments to the cost of capital from the issuance of new debt, PAC calculated their pro forma test year allowed overall rate of return to be 7.03%. Exh. 1 at 3-4. PAC's requested permanent

rates are designed to yield a 7.03% overall rate of return. Their proposed temporary rates are set at 75% of their requested permanent rates (excluding the separate requested step increase), and should yield an approximate 5.1% rate of return based on the pro forma test year, during the temporary rate period, subject to reconciliation to permanent rates. PAC's proposed increase in revenue would be allocated to customers as follows: \$150,377, a 33.01% increase, would be collected from Pittsfield customers and \$567,854, a 179.64% increase, would be collected from North Country customers. If approved, bills for the average residential customer in Pittsfield would rise from \$412 to \$549 annually; bills for North Country customers would rise from \$282 to \$788 annually. Exh. 1 at 7 and 10. PAC proposes, and Staff agrees, that the rates ought to become effective for service taken on or after June 6, 2008.

Agreement as to PAC's proposal is not unanimous. In particular, LLCA would prefer that a temporary increase in PAC's revenue requirement only cover operational costs and not include costs relating to capital expenditures until such costs can be fully reviewed in the rate case. LLAC especially opposes PAC's proposal to place Pittsfield customers in a separate rate category. As stated above, a separate rate for Pittsfield would result in the North Country customers paying a majority of the proposed temporary revenue requirement. Sunrise also expresses concern that PAC's rate increase would adversely impact customers at Sunrise. The OCA, while not opposing an increase to PAC's revenue requirement, contends that any changes to how the revenue requirement is collected from customers should wait until after the issue has been fully investigated. BHWD does not oppose an increase to PAC's revenue requirement but is more concerned with the allocation of the revenue requirement among the fixed and volumetric charges and the impact of seasonal customers on those rates.

Having reviewed the proposed revenue requirement and positions of the parties relative to that issue, we find a temporary increase to PAC's revenue requirement to be warranted. The record demonstrates that PAC is not earning a reasonable return on its property that is presumptively used and useful in the public service. Specifically, PAC's rate of return is currently at negative 4.0%, 12.42% less than its last allowed rate of return of 8.42% and 11.03% less than PAC's calculated pro forma test year rate of return of 7.03%. Exh. 1 at 3-4. We understand that much of the decline in the rate of return is due to PAC's increase in net plant in service of approximately 377% over the past 21 months. This negative rate of return could adversely impact PAC's financial capability and it could adversely affect the provision of safe and adequate service to customers. Thus, we find it in the public interest to approve, on a temporary basis for the course of this proceeding, an increase in PAC's overall revenue requirement and rates to bring their rate of return into reasonable positive territory. PAC and its customers are protected because, pursuant to RSA 378:29, the temporary and final revenue requirements and rates will be fully reconcilable upon final disposition of the issues involved in this proceeding. This reconciliation provision protects both PAC and its customers in that PAC will only recover the revenue requirement as finally determined and customers will pay net rates no higher than those authorized.

We next consider the issue of what rates to impose in order to generate increased revenues. Staff and the parties have recommended allocations that range from preserving the present consolidated rate design to implementing separate rate groups. With the former, Pittsfield states customers could see a rate increase of 94%. With the latter, North Country customer rates could rise 179.64%, although we note that this percentage increase does not reflect the fact that the North Country customers' existing average annual residential bill is \$282

while Pittsfield customers' average annual residential bill is \$412. Regardless, the disparity between the different rate recommendations is significant.

Having carefully reviewed the competing proposals, we find that neither maintaining the present rate design nor adopting PAC's proposal is appropriate. If the present rate design is maintained for temporary rates but the final disposition of this proceeding results in two rate groups, then North Country customers may face extreme rate shock, especially when recoupment of the difference between temporary rates and permanent rates is taken into account, while Pittsfield customers may receive refunds. On the other hand, if we adopt PAC's proposed rate design for temporary rates, but the final disposition of this proceeding results in one rate group, then North Country customers may be due a refund while Pittsfield customers may be subject to rate shock. In order to moderate the impacts from these possible outcomes, we strike a middle course, increasing the revenue requirement percentage that Pittsfield customers will bear under temporary rates and decreasing the revenue requirement from North Country customers below PAC's temporary rate request.

We believe it is appropriate to increase Pittsfield customers' rates by 40%, rather than PAC's proposed 33%. This amount is closer to but still less than PAC's requested permanent rate increase of 44% for Pittsfield customers and much less than the 94% increase that would result from LLAC and OCA's suggestion to maintain fully combined rates. This will raise, on a temporary basis for Pittsfield customers, the average annual residential bill to \$577, which is more than the \$549 proposed by PAC but is much less than the \$788 anticipated by PAC for North Country customers.

We take a middle ground on separate rates between Pittsfield and North Country customers, recognizing that there has been disproportionate investment in North Country water

systems compared with Pittsfield, but not in any way prejudging the ultimate outcome of this case. We find that temporary rates for North Country customers that result in average annual residential bills that are only 25% greater than for Pittsfield customers is a reasonable middle ground that will mitigate the risk of rate shock for any one customer group regardless of the permanent rates that may be approved, while allowing PAC to begin to earn a reasonable return on their investments. On a temporary basis for North Country customers, the average annual residential bill will increase to \$722, which is lower than PAC's proposed \$788 but still high enough that if under permanent rates North Country customers are indeed separated into their own rate group, the potential rate shock and recoupment is mitigated. We find that moderating the proposed temporary rate bills for Pittsfield and North Country customers in this way will result in just and reasonable rates.

The revenue requirement resulting from these rate increases will also allow PAC to earn a positive rate of return on a combined basis, as well as on an individual basis. The 40% temporary rate increase for Pittsfield customers will generate an additional \$182,226 in revenues and will allow PAC to earn a 6.98% rate of return on that system. Increasing the Pittsfield customer's average annual residential bill by 25% to \$722, and applying that to North Country customers will generate an additional \$484,101 in revenues and, importantly, will allow PAC to earn a positive 2.43% rate of return on those systems on a proforma basis. On an overall basis, the revenue increase we are approving will allow PAC to earn a 4.17% rate of return on a proforma test year basis until permanent rates are determined. Such rates will allow PAC to generate an additional \$666,327 in revenues, which is 69.6% of the permanent rates requested by PAC, excluding the requested step increase. This is less than the 75% requested, but we find that it is still within a range of reasonableness for temporary rates.

If we were to keep parity between the Pittsfield and North Country average annual residential bills such that North Country customers had the same average annual residential bill of \$549 that PAC requested for temporary rates for Pittsfield customers, then PAC would earn a negative rate of return on the North Country systems and would only be projected to earn a 0.02% overall rate of return on a pro forma test year basis. If we were to maintain such parity to the end that North Country customers had the same average annual residential bill of \$577 that we are approving on a temporary basis for Pittsfield customers, then PAC would still have a negative rate of return on the North Country systems and would still only have an overall projected rate or return of about 1%. According to PAC and Staff, most of the cause for PAC's negative rate of return has been the recent increase in new plant investment. "The majority of the investments, according to PAC witnesses, have been necessary to bring the systems in compliance with the provisions of the Safe Drinking Water Act combined with system repairs and upgrades." Exh. 5 at 5. The extent to which such investments are deemed prudent, used and useful in the public service, and thus are allowed into rate base for determining revenue requirements and reasonable rates, will be fully examined as part of our review of permanent rates. In the meantime, temporary rates must yield not less than a reasonable rate of return. *See Appeal of Pennichuck Water Works, 120 N.H. 562 (1980)*. We do not believe that a rate of return on the order of 1% or less is reasonable under the circumstances where there is no evidence before us to indicate that the new plant in service is not used and useful at this present time.

For the foregoing reasons, we will approve a temporary increase in PAC's revenue requirement of \$666,327, for a total test year revenue requirement of \$1,438,000. We will approve a temporary rate increase to Pittsfield customers' bills of 40%, or \$577 for the average

annual residential customer. We approve a temporary rate increase to PAC's North Country customers of an additional 25% over Pittsfield customer's average annual residential bill, or \$722. We will approve these changes in customer rates effective for service taken on or after June 6, 2008, the date notice to all customers was completed. Pursuant to RSA 378:29, these rates will be fully reconciled with the rates as finally determined in this proceeding.

Additionally, the method we have chosen for reasonably allocating the temporary increase in PAC's revenue requirement in rates need not be adopted in the final establishment of permanent rates and reflects no prejudgment of the final outcome. *See New England Telephone & Telegraph Co. v. State*, 95 N.H. 515, 518 (1949). In light of the amount of the increase, especially for North Country customers, and the difficult economic times, we urge PAC to be understanding of customers who may have difficulty paying the increase and to work with those customers to schedule a feasible payment plan.

Based upon the foregoing, it is hereby

ORDERED, that Pittsfield Aqueduct Company, Inc.'s request for a temporary increase to its revenue requirement, as discussed and modified above, is GRANTED; and it is

FURTHER ORDERED, that Pittsfield Aqueduct Company, Inc. is authorized to raise the rates it charges its Pittsfield customers by 40% on a temporary, service rendered basis effective June 6, 2008; and it is

FURTHER ORDERED, that Pittsfield Aqueduct Company, Inc. is authorized to raise the rates it charges its North Country customers by an additional 25% over the new average annual residential customer bill authorized for Pittsfield, as discussed above, on a temporary, service rendered basis effective June 6, 2008; and it is

FURTHER ORDERED, that Pittsfield Aqueduct Company, Inc. shall submit tariff pages in compliance with this order within 14 days of the date of this order.

By order of the Public Utilities Commission of New Hampshire this thirty-first day of December, 2008.

Graham J. Morrison
Commissioner

Clifton C. Below
Commissioner

Attested by:

Lori Davis
Assistant Secretary

DW 08-052, PITTSFIELD ACQUEDUCT COMPANY
TEMPORARY RATES
DISSENTING OPINION OF CHAIRMAN GETZ

I agree with my colleagues that it is in the public interest to fix temporary rates for PAC for the duration of this proceeding. I disagree, however, with granting rate increases of 40% for the Town of Pittsfield customers and 150% for North Country customers. I would set the temporary rate increase for customers in the Town of Pittsfield at the 33% level proposed at the hearing on October 7, 2008, which would result in an average annual bill of \$549 for those customers. I would limit the increase for the North Country customers to the same average

annual bill of \$549, which would equate to a 93% increase for such customers, as opposed to the 179% increase that was proposed at hearing.

In my view, this result is reasonable inasmuch as it yields a positive return on investment for PAC, albeit barely, even if it were assumed that all of the Company's construction activities were prudent and that the plant is used and useful in the public service. It is premature, however, to conclude that all of the Company's construction activities were, in fact, prudent. Therefore, there are reasonable grounds to fix a temporary rate lower than that proposed by the Company. This approach has the advantage of mitigating the rate impact on customers in the Town of Pittsfield and the North Country and it comports with the ratemaking principle of gradualism.