

**STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION**

DW 08-065

HAMPSTEAD AREA WATER COMPANY

Notice of Intent to File Rate Schedules

Order Granting Rate Increase

ORDER NO. 25,000

August 4, 2009

APPEARANCES: Hampstead Area Water Company, Inc. by Robert C. Levine, Esq.; Office of the Consumer Advocate on behalf of residential ratepayers by Rorie E.P. Hollenberg, Esq.; and Staff of the Public Utilities Commission by Marcia A.B. Thunberg, Esq.

I. PROCEDURAL HISTORY

Hampstead Area Water Company, Inc. (HAWC) is a regulated public utility as defined by RSA 362:2 and 362:4 and currently serves approximately 2,900 customers in various communities throughout southeastern New Hampshire. On April 28, 2008, HAWC filed a notice of intent to file rate schedules and, on June 25, 2008, HAWC filed schedules and materials, pursuant to N.H. Code Admin. Rules Puc 1600, supporting its request to increase its annual revenues by \$167,193, or 13.77%. The procedural history is more fully described in Order No. 24,932 (January 16, 2009) in which the Commission approved HAWC's current rates as temporary rates, effective for service provided on or after September 1, 2008.

Staff and the parties conducted discovery and, on April 22, 2009, the OCA filed direct testimony of Utility Analyst Stephen R. Eckberg. On May 27, 2009, Staff filed a stipulation entered into by all of the participants in the docket: HAWC, Staff, and the OCA. The settling parties presented the stipulation at the hearing held on June 3, 2009.

II. STIPULATION AGREEMENT

A. Revenue Requirement

The settling parties propose a revenue requirement of \$1,310,082 based on HAWC's 2007 test year. The settling parties also recommend the test year revenues be based on 2,909 customers, the number of customers served by HAWC as of the end of 2008.

The settling parties recommend HAWC receive two step adjustments to its revenue requirement. The first would allow: 1) a return on \$61,249 in plant additions installed during 2008 as well as the annual operating expenses associated with these assets; 2) a return on costs of drilling a new well at Dearborn Ridge, \$21,927, which proved to be unproductive, in addition to the annual amortization expense of these drilling costs based on a 20-year recovery period; 3) a return on the costs associated with the December 2008 Ice Storm in the amount of \$22,877 in addition to the annual amortization expense of the Ice Storm Costs based on a three-year recovery period; 4) the incremental annual operating expenses HAWC will incur from converting from a quarterly to monthly billing cycle and a reduction in the cash working capital component of rate base associated with this conversion. Step 1 would increase HAWC's annual revenues by \$61,757, or 5.24%. The settling parties recommend Step 1 become effective as of the date of the Commission's final order in this docket, on the condition that the Commission also approve HAWC's proposed debt financings discussed below. The settling parties also recommend that Step 1 not be reconciled with temporary rates.

The second step concerns HAWC's Interconnection Project. The settling parties recommend the Commission allow HAWC to recover capital costs of approximately \$800,000 associated with this project, the financing for which the Commission approved in Docket No. DW 08-088. The project is expected to begin during the summer of 2009 but the settling parties recognize that there is a possibility the project could be delayed until 2010. Together with a return on this rate base, depreciation, and property taxes, the settling parties expect Step 2 to increase HAWC's annual revenues by approximately \$61,061 or about 5.18% over test year revenues. HAWC agrees, upon completion of the interconnection project, to submit a filing to the Commission with its request for this step adjustment, along with supporting documentation. Staff and OCA will review the filing and the Commission's Audit Staff will audit the plant records. Staff and OCA will then submit their recommendations for consideration. The settling parties recommend that Step 2 not be reconciled with temporary rates.

B. Rate Impact

The recommended revenue requirement and Step 1 will raise HAWC's base rate to \$10 per month for 5/8 inch meter customers and raise the consumption rate to \$4.29 per 100 cubic feet. Based upon these rates, an average residential customer using 7,853 cubic feet of water per year will pay approximately \$457 on an annual basis. This represents an annual increase of \$66 over present rates.

C. Rate Case Expenses

The settling parties recommend the Commission allow HAWC to recover rate case expenses and to that end, HWAC agrees to submit, within fifteen days from the date of a final order in this docket, documentation of its rate case expenses and a proposed surcharge to recover these expenses. Staff and OCA state that they will review HAWC's rate case expense filing and will offer recommendations.

D. Financings

On May 15, 2009, HAWC filed a petition for approval of long-term debt from its affiliate, Lewis Builders Development, Inc. The Staff and HAWC agree that it is just and reasonable for HAWC to borrow \$94,232 from Lewis Builders Development, Inc. and recommend the financing be approved. The OCA takes no position on the amount or terms of this financing. The revenue impact of this financing has been incorporated into the revenue impact reflected in Step 1.

HAWC proposes to refinance with TD Bank, N.A. \$1,450,000 of its long-term debt owed to Lewis Builders, Inc. and Lewis Builders Development, Inc. Staff and HAWC agree that refinancing this debt is consistent with the public good and recommend the Commission approve it. The terms include a five-year maturity, twenty-year amortization period and an interest rate that is 300 basis points above the 5 year Federal Home Loan Bank Classic Advance Rate, which resulted in an interest rate of 6.46% as of June 2009. The proposed refinancing is expected to reduce interest costs associated with the long-term debt by approximately \$33,917. This will lower HAWC's weighted average cost of debt. The settling parties have incorporated the revenue impact of the refinancing into the revenue requirement reflected in Step 1.

E. Conversion of Debt to Equity

HAWC agrees to convert \$990,353 of its accounts payable due to Lewis Builders Development, Inc. to Additional Paid-in Capital, an equity account. The accounts payable balance remaining after this debt-to-equity conversion will be approximately \$200,000 as of June 30, 2009. Going forward, HAWC agrees to make payments on the \$200,000 balance so as to keep the existing payables within a range permissible without prior Commission review and approval as required by RSA 369 and Puc 608.05 (i.e., no more than 12 months past due and no more than 10% of HAWC's net fixed plant). The revenue impact of this debt conversion has been incorporated into the revenue impact reflected in Step 1.

F. Reporting Requirements

1. Affiliate Agreements — HAWC agrees to file revised affiliate agreements with LBDI, Lewis Equipment Co., and Atkinson Resort & Country Club within 90 days of the Commission's final order in this docket for Commission review and approval. HAWC agrees to provide copies of these filings to the OCA.

2. Fire Protection Governed Solely by Tariff — HAWC agrees to discontinue its practice of individual fire protection contracts with municipalities and agrees to provide such fire protection service by tariff.

3. Internal Controls – HAWC agrees to implement internal controls recommended in Audit Issues 18, 19, and 20 of the Final Audit Report dated March 25, 2009 concerning the calculation of overhead and labor burden rates as well as the approval of employee time records. HAWC agrees to file, within 90 days from the date of the Commission's final order, evidence of its revised internal control procedures.

4. Hydrology Study Note – HAWC agrees to reduce the interest rate on the promissory note approved in Docket DW 06-104 from 10.5% to the prime rate as of March 31, 2009 (3.25%) plus 2.25%, or 5.50%. HAWC agrees to file an updated promissory note within 90 days to the Commission for review and approval.

5. Production and Consumption Data – HAWC agrees to include in its Annual Report to the Commission a report of production and consumption, tabulated monthly by system, once the conversion to monthly billing is fully implemented. Such reporting will begin in 2010 for HAWC's 2009 Annual Report. HAWC agrees to collect and report data such that the time periods for production and consumption data correspond.

III. COMMISSION ANALYSIS

RSA 378:7 authorizes the Commission to fix rates after a hearing upon determining that the rates, fares, and charges are just and reasonable. In determining whether rates are just and reasonable 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 their 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. Pursuant to RSA 541-A:31, V(a), informal disposition may be made of any contested case at any time prior to the entry of a final decision or order, by stipulation, agreed settlement, consent order or default. N.H. Code Admin. Rules Puc 203.20 (b) requires the Commission to determine, prior to approving disposition of a contested case by settlement, that the settlement results are just and reasonable and serve the public interest.

A. Revenue Requirement

The settling parties propose a revenue requirement of \$1,310,082 based on a 2007 test year, a rate base of \$3,704,979 and a rate of return of 6.05%. This represents an increase of 11.22% over HAWC's 2007 test year revenues. The revenue requirement is calculated by performing test year revenues using an updated customer count as of the end of 2008, and reflects the results of HAWC's efforts to refinance a substantial amount of its debt, which is the subject of Docket No. DW 09-112. HAWC's refinancing would lower its weighted average cost of debt and that lower cost of debt has been used in the calculation of the proposed revenue requirement.

The settling parties also recommend a step increase to HAWC's revenue requirement. This step increase includes \$61,249 in additional plant installed by HAWC in 2008 after its test year and represents an additional 5.24% of the increase to HAWC's revenue requirement. The settling parties believe this plant is a reasonable addition to HAWC's rate base. It includes costs HAWC incurred during the 2008 Ice Storm when HAWC lost all external power to its systems. HAWC testified that it rented two large generators from its affiliate, Lewis Builders Developer, and five additional generators from three other contractors. Hearing Transcript of June 3, 2009 (6/3/09 Tr.) at 20, lines 18-24. The settling parties agreed that recovery of the costs of the generators was appropriate and recommended the Commission allow these costs to be recovered over a three-year period.

The step increase also includes costs relating to HAWC's conversion from quarterly to monthly billing. We find this to be a reasonable adjustment since it provides more frequent billing, which will send more accurate price signals to customers and reduce HAWC's cash working capital requirements. The step includes HAWC costs relating to securing additional source capacity at Dearborn Ridge. HAWC testified that, at the behest of the Department of

Environmental Services (DES), it drilled a new well costing \$21,927 but that the well was ultimately unproductive. 6/3/09 Tr. at 23, lines 17-23. HAWC asserted that, had the well been productive, it would likely have been allowed in rate base. Id. at 23, line 24 and at 24, lines 1-4. The settling parties recommend a 20-year recovery period for the \$21,927 to coincide with the term of a 20-year loan from LBDI used to finance the cost of the well. Id. at 25 lines 11-19. Staff testified that it had audited the components of the proposed step increase and Staff concluded that the plant was prudent, used, and useful in the provision of utility service. See, Exh. 6. Staff also testified that if the amounts were not allowed in the Company's rate base there would be a detrimental impact on the company's rate of return. 6/3/09 Tr. at 27, lines 21-24.

Step adjustments to rates are employed as a means of ensuring that a regulated utility retains its ability to earn a reasonable rate of return after implementing large capital projects, and 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, which in this case was 2007. We find that the capital improvements and expenses recommended in the step increase are used and useful and should be included in rate base. Traditional rate-of-return principles permit a utility to have "the opportunity to make a profit on its investment, in an amount equal to its rate base multiplied by a specified rate of return." *Appeal of Conservation Law Foundation*, 127 N.H. 606, 634 (1986). Having reviewed the record and testimony presented at hearing, we approve the proposed step increase, effective as of the date of this order on a service rendered basis, to cover the costs and expenses identified above. This step increase shall not be considered part of permanent rates and shall not be subject to reconciliation pursuant to RSA 378:29. Lastly, with respect to the overall revenue requirement, we find that the plant included in the proposed

revenue requirement is prudent, used, and useful and that the revenue requirement is appropriate and will produce just and reasonable rates.

B. Rate Impact

According to the proposal offered by the settling parties, the increase in HAWC's revenue requirement will raise HAWC's base rate for 5/8 inch metered service to \$10 per month and its consumption rate to \$4.29 per 100 cubic feet. The settling parties estimate that an average residential customer using 7,853 cubic feet of water per year will pay approximately \$457 annually; an increase of \$66. We note that HAWC has agreed to discontinue charging its fire protection customers pursuant to individual contracts and will now charge customers pursuant to a uniform tariff.¹ The increase in HAWC's revenue requirement and its institution of tariff rates will result in municipal fire protection customers in the Town of Atkinson and Town of Hampstead being charged an annual hydrant charge of \$200 per hydrant as well as an availability fee of \$2,000 per year; private fire protection customers will be charged a graduated rate ranging from \$100 to \$1,500 depending on the size of the service. Exh. 5 at 28. Customers with 1-inch service will be charged an annual rate of \$100 and customers with a 6-inch service will be charged an annual rate of \$1,500. *Id.* Having considered these proposed rates, we find that they are an appropriate way of collecting the revenue requirement from customers and we find them to be just and reasonable pursuant to RSA 378:7.

C. Second Step Adjustment

The settling parties recommend that we approve a second step increase to account for approximately \$800,000 in net additional rate base anticipated from HAWC's interconnection project. The interconnection project involves approximately \$1.1 million in plant additions, but

¹ The tariff rates agreed to by the settling parties were first approved in *Hampstead Area Water Company, Inc.*, Order No. 24,747, 92 NH PUC 115 (2007).

the interconnection grant from DES in the amount of \$270,000 lowers the cost to approximately \$800,000. In Order No. 24,937 (February 6, 2009) the Commission approved HAWC's request to finance the interconnection project, but deferred the issue of how the financing would impact rates to the instant docket. HAWC stated that the project is estimated to be completed in November of 2009, assuming the project receives Governor and Council approval in June 2009.² 6/3/09 Tr. at 30-31. At the conclusion of the project, HAWC will submit documentation of its costs relating to the project for Staff and the OCA's review and then for Commission review and approval. At present, the settling parties calculate that the second step will result in a \$61,061 increase to HAWC's revenue requirement. This translates to an additional 5.18% increase in rates.

As noted with regard to step one, the Commission allows step adjustments to rates as a means of ensuring that a regulated utility retains its ability to earn a reasonable rate of return even after implementing large capital projects. In HAWC's context we consider \$800,000 in additional plant to be a large capital project and we will allow HAWC to submit its documentation of costs incurred relating to the interconnection project for our review at the completion of the project.

D. Reporting and Other Obligations

HAWC agrees to update its affiliate agreements pursuant to RSA 366:3. Pursuant to RSA 374:4, the Commission has the duty to keep informed of the operations and management of public utilities. Having updated affiliate agreements on file with the Commission is a necessary prerequisite for the Commission's oversight of HAWC. HAWC also commits to implementing internal controls. At hearing, HAWC testified that such internal controls include: the calculation of overhead relating to LBDI; how employee rates are being charged to HAWC; and the signing

² HAWC received approval of Governor and Council on June 17, 2009.

of time cards. 6/3/09 Tr. at 41, lines 23-24 and at 42, lines 1-6. These changes were recommended by Staff in its audit report. We find the implementation of internal controls to ensure that only prudent expenses associated with the provision of water service are passed along to ratepayers is reasonable and we will approve them.

HAWC also commits to reducing the interest rate on an existing loan with LBDI which had an original loan amount of \$267,299. The proceeds of the loan were used to conduct a hydrology study. At the time the Commission approved the loan, the interest rate was 10.5% and, since that time, interest rates have fallen to the point where HAWC is able to commit to an interest rate of 5.5%. Lowering the cost of financed debt is beneficial to ratepayers, thus, we will approve this portion of the stipulation and await HAWC's updated promissory note as called for in the stipulation.

The stipulation contains a requirement that HAWC report production and consumption data, by month and by system, and that the data be reported annually, commencing with its 2009 Annual Report to the Commission. In *Investigation into Water Conservation*, Order No. 24,243, 88 NH PUC 603 (December 5, 2003), the Commission required all regulated water utilities to submit annual accounting of lost water, tabulated monthly, with their annual reports. In the past, HAWC has been unable to report such data because it read meters quarterly, rather than monthly. As stated earlier, HAWC now commits to reading customer meters monthly. The expense associated with monthly meter reading has been included in HAWC's new revenue requirement. Conversion to monthly meter reading and monthly billing should have occurred in June 2009 and thus HAWC should be able to come into compliance with the lost water reporting requirement. Given these developments, we find it reasonable to discontinue the Commission's waiver of

HAWC's lost water reporting obligation and we will require the Company to file the production and consumption data commencing with its 2009 Annual Report.

Having reviewed the record in this proceeding, including the stipulation and supporting testimony presented at the June 3, 2009 hearing, we find the terms of the stipulation to be reasonable and for the public good. We find that the terms will result in just and reasonable rates and that they represent an appropriate balancing of ratepayer interests and the interests of HAWC's investors under current economic circumstances. Accordingly, we approve the stipulation.

Based upon the foregoing, it is hereby

ORDERED, that the stipulation entered into among the parties to this proceeding and Staff is adopted and approved as discussed herein; and it is

FURTHER ORDERED, that Hampstead Area Water Company, Inc.'s request for a revenue requirement of \$1,310,082 is approved and Hampstead Area Water Company, Inc. is authorized to collect from customers the permanent rates necessary to recover this revenue requirement, as described herein, for service rendered on or after September 1, 2008; and it is

FURTHER ORDERED, that Hampstead Area Water Company, Inc.'s request to increase its revenue requirement by \$61,757 for a combined revenue requirement of \$1,371,839 is hereby approved, for service rendered on or after the date of this order, and Hampstead Area Water Company, Inc. is authorized to collect from customers the rates described herein to recover this revenue requirement; and it is

FURTHER ORDERED, that Hampstead Area Water Company, Inc. file within fifteen days from the date of this order documentation of its calculation of the difference between

temporary and permanent rates as well as a proposed surcharge for recovering the difference from customers; and it is

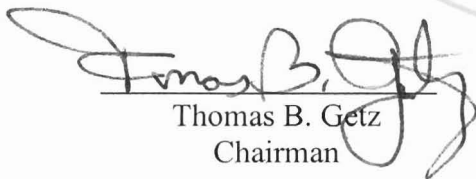
FURTHER ORDERED, that Hampstead Area Water Company, Inc. file documentation of its rate case expenses as well as a proposed surcharge for recovery of these expenses within fifteen days from the date of this order; and it is

FURTHER ORDERED, that Hampstead Area Water Company, Inc. include in its Annual Report, beginning with year 2009, a report of its production and consumption data from the time it converted to monthly billing forward and that this data be tabulated monthly by system; and it is

FURTHER ORDERED, that within 90 days of the date of this order Hampstead Area Water Company, Inc. file updated affiliate contracts and an amended promissory note as discussed herein; and it is

FURTHER ORDERED, that Hampstead Area Water Company file a compliance tariff within ten days of the date of this order.

By order of the Public Utilities Commission of New Hampshire this fourth day of August, 2009.


Thomas B. Getz
Chairman


Clifton C. Below (KNS)
Commissioner

Attested by:


Debra A. Howland
Executive Director