

**STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION**

**IN RE: KENT COUNTY WATER AUTHORITY'S) DOCKET NO. 3660
 ABBREVIATED RATE FILING)**

**POST-HEARING MEMORANDUM OF LAW OF THE DIVISION OF
PUBLIC UTILITIES AND CARRIERS**

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I. INTRODUCTION

The Kent County Water Authority (“KCWA”) filed its rate application with the Public Utilities Commission (“Commission”) in January of 2005. Subsequent to that filing, the Division of Public Utilities and Carriers (“Division”) retained Andrea C. Crane, a member of the Columbia Group, to review KCWA’s revenue requirements. After conducting an exhaustive investigation, the Division filed Direct and Surrebuttal Testimony of Ms. Crane, along with Direct Testimony of Alberico Mancini, with the Commission.

The Division and KCWA both agree that a rate increase of \$3,172,665 or approximately 25% over present rates is required. The parties, however, differ as to how \$841,763 of the \$3,172,665 should be allocated. The Division does not oppose KCWA’s requested increase up to and including \$2,330,902¹; however, any increase granted over this figure or \$841,763, the Division recommends, must be placed in KCWA’s restricted IFR account and utilized for additional IFR funding.

By contrast, KCWA contends that it should be entitled to use virtually the entire \$3,172,665 for the operation and maintenance of its business. The difference between the parties’ respective positions in terms of individual accounts can be broken down as follows: (A) Water Sales Revenues, (B) Customer Growth, (C) Incremental Variable Costs, *i.e.*, (1) Incremental Power Costs & Incremental Chemical Costs, (2) Chemical Inflation Adjustment, and (3) Purchased Water Expense, (D) Lobbying Costs, (E) Office Supplies and Expenses, (F) Maintenance of Mains, and (G) Operating Revenue Allowance.

¹ Note $\$841,763 + \$2,330,902 = \$3,172,665$.

The Commission heard the merits of this matter on May 20 and 23, 2005. Testimony adduced at hearing, along with the application of the appropriate legal and regulatory principles and policy, require findings that are in accordance with the position proffered by the Division at hearing. The Division respectfully requests that the Commission grant KCWA's rate application on such terms and conditions as are consistent with the testimony of Andrea C. Crane elicited at hearing as well as with her Direct and Surrebuttal Testimony. See ACC-1S (Revised 5/23/05), ACC 2S-6S, ACC 7S (Revised 5/23/05) and ACC 8S-11S.

II. THE DISPUTED ACCOUNTS

A. WATER SALES REVENUES - \$335,307 - ACC-2S

In order to determine KCWA's *pro forma* Water Sales Revenues, the Division recommends that the Commission base its calculation using an average of total sales over three years. The Division's recommendation in this regard conforms to the methodology that the Commission has utilized in countless numbers of rate cases, and accounts for wide variations that occur due to weather and other factors. See e.g., In Re: Kent County Water Authority Rate Application, Docket 3311, Order 17024, Settlement Schedule 1C (2001) (settlement using 3 year average); In Re Woonsocket Water Division Rate Application, Docket 3626 (2005) (3 year average; Order to be issued); In Re: Kent County Water Authority Application to Change Rate Schedule, Docket 2555, Order 15418 at 20 (1997) (4 year average).

By contrast, KCWA derives its projected revenues from water sales based solely on test year sales, adjusted to remove revenues from the loss of one large customer, On

Semiconductor. KCWA's logic supporting the adoption of this methodology is flawed for a number of reasons. First, KCWA's test year (the 12 months ending June 30, 2004) includes the summer (June, July and August) of 2003. Testimony elicited from KCWA's expert consultant upon cross-examination highlights the fact that the summer of 2003 was abnormally wet. June was the third wettest June in 105 reported years; August was 12th wettest August in 105 years; and only 34 of 105 Julys were wetter than July of 2003. All other things being equal, water sales tend to decrease substantially in very wet weather. Accordingly, KCWA's water sales were abnormally low in the test year. KCWA's test year sales, then, will not predict with any degree of accuracy a utility's water sales revenues in the rate year. See generally 5/20/2005 Transcript at 192-194.

KCWA sought to counter the Division's use of the three-year average methodology by introducing a graph (KCWA Exhibit 6) that purports to demonstrate significant variances between the actual water sales each year and estimated water sales based on a three-year average, as recommended by Ms. Crane. However, as noted by Ms. Crane during cross-examination, KCWA omitted three critical points with regard to this exhibit.

First, the variations between actual results and predictive results using a three-year average are both positive and negative, as would be expected. In some years, Ms. Crane's methodology would have resulted in estimated sales that were higher than actual results, while in some years her methodology would have predicted results that were lower than actual sales. 5/23/2005 Transcript at 18, lines 6-8. This conclusion was demonstrated by Division Exhibit 9, which replicated much of the data on KCWA Exhibit 6 but included the positive and negative signs to clearly show that in four of the

eight years for which data was available, Ms. Crane's methodology would have resulted in *pro forma* sales that were higher than actual results and in four of the eight years her methodology would have resulted in *pro forma* sales that were lower than actual results. (Data is only available for eight years since KCWA Exhibit 6 began with 1993 data and Ms. Crane's methodology uses a three-year average, with a two-year regulatory lag. Thus, her *pro forma* revenue was based on a three-year average of sales in fiscal years 2004, 2003, and 2002, while the rate year is fiscal year 2006.)

Even more importantly, Division Exhibit 9 expands upon KCWA Exhibit 6, by including the variation between predicted and actual results using KCWA's methodology, which is shown in the last column of Division Exhibit 9. The critical point is that for the eight years for which data is available, Ms. Crane's methodology was a better predictor of actual results in six of the eight years, or 75% of the time. KCWA's method was a better predictor in only two of the eight years. In addition, in one of the two years in which KCWA's methodology was a better predictor of actual results (1997), Ms. Crane's methodology would actually have provided more revenues to KCWA than the utility's own methodology. Thus, Division Exhibit 9 demonstrates that the use of a three-year average is a much better method of determining *pro forma* sales than the use of only one year's actual results, as recommended by the KCWA.

Lastly, KCWA Exhibit 6 shows that water sales fluctuate from year to year, but does not demonstrate a declining trend usage. Rather than a declining sales trend between 2002-2004, KCWA had greater sales than the twelve-year average in some years (*e.g.*, 2003, 2002, 2000, 1994 and 1993), and KCWA sold less water than the twelve-year average in some years (*e.g.*, 1997, 1998, 2001 and 2004). KCWA's contention that it

experienced declining sales between 2002 and 2004, therefore, is simply untrue. As Ms. Crane observed on behalf of the Division, "...there really is no significant persistent downward trend as would be suggested by the Authority." 5/23/2005 Transcript at 18, lines 6-8.

KCWA's projected operating revenues were based on abnormal test year data and in complete disregard of the methodology that the Commission has repeatedly ruled should be used for calculating a utility's projected water sales revenue. As shown above, this methodology provides a more accurate picture of KCWA's water sales revenue than the KCWA methodology. The Commission, therefore, should adopt the Division's recommendation regarding KCWA's Water Revenue Sales as reflected in ACC-2S.

B. CUSTOMER GROWTH - \$71,167 - ACC-3S

The Division and KCWA also disagree about KCWA's prospects for future customer growth. The Division has recommended an adjustment to KCWA's water sales revenues based on the projected growth of residential and industrial customers. Over the past five years, KCWA has reported the following growth in both residential and commercial customer categories:

	<u>2004²</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>
<u>Residential</u>	24,637	24,519	24,344	24,125	23,954
<u>Commercial</u>	1,458	1,440	1,415	1,396	1,389

KCWA Response to Division Data Request 1-20.

Between fiscal year 2000 and fiscal year 2004, KCWA's residential customers increased by an average of 171 per year. Therefore, "basing *pro forma* revenue on the

² As of June 30th.

number of customers as of June 30, 2004 is likely to understate the actual average number of customers in the rate year” (July 1, 2005 - June 30, 2006). Crane Direct Testimony at 12, lines 5-6. To correct this likely understatement, the Division recommends that the Commission adopt a revenue adjustment to reflect an additional 256 residential customers—*i.e.*, 18 months of growth from June 30 to January 1, 2006, the middle of the rate year. Crane Direct Testimony at 12, lines 9-12.

The Division’s adjustment is extremely conservative. The data produced by KCWA in response to Division Data Request 1-20 shows that KCWA has also experienced growth in its industrial customer class. “Since 2000, the number of industrial customers has increased from 1,389 to 1,458, or by approximately 17 customers per year.” Crane Direct Testimony at 12, lines 18-19. The Division, however, has *not* recommended an adjustment based on the growth of the industrial customer class since the usage among these customers varies much more than usage among residential customers. Nonetheless, given the increase in the number of industrial customers over the past five years, there may well be customers added between June 30, 2004 and the end of the rate year (June 30, 2006), which should be included within a projection of KCWA’s water revenue sales.

Public comment received at hearing supports this view. At least two projects—“Walmart” and the “Wingate Hotel” appear to be far enough developed so as to represent probable additions to KCWA’s industrial customer base in the foreseeable future. 5/20/2005 Transcript at 19-20. Furthermore, in her Direct Testimony at page 13, Ms. Crane observed that “Home Depot [was] in the process of building a new facility in Coventry and that this facility is expected to be operational shortly.”

Past Commission practice, the growth of KCWA's residential and industrial customer bases, as well as the likely addition of several large commercial customers support the Division's proposed adjustment for Customer Growth. The Commission, therefore, should adjust KCWA's Water Sales Revenue claim upward by \$71,167 as proposed by the Division.

C. INCREMENTAL VARIABLE COSTS

If the Commission accepts the Division's adjustment for Water Sales Revenues and Customer Growth, then the Commission must make further adjustments to KCWA's claim for Incremental Power Costs (ACC-4S - \$20,381) & Incremental Chemical Costs (ACC-5S - \$2,423). The Commission should also adjust KCWA's claims for Chemical Inflation (ACC-6S - (\$1,977)) and Purchased Water Expense (ACC-7S (Revised 5/23/2005) - (\$80,091)).

1. Incremental Power Costs (ACC-4S - \$20,381) & Incremental Chemical Costs (ACC-5S - \$2,423)

Of the four adjustments discussed above, the first two—Incremental Power and Chemical Costs—actually favor KCWA. KCWA has not contested their accuracy except to the extent that the utility contests the Division's recommendations with respect to Water Revenue Sales and Customer Growth. Accordingly, they will not be discussed in any further detail here.

2. Chemical Inflation Adjustment (ACC-6S - (\$1,977))

The third adjustment, Chemical Inflation, is a relatively minor adjustment and also was not contested by KCWA at the hearing. Nonetheless, KCWA's claim for a "4%

inflationary increase to chemical costs” suffers from the similar infirmity that affects its claims for Office Supplies and Expenses and Maintenance of Mains below. According to KCWA’s Rebuttal Testimony and Response to Division Data Request 1-14, the prices of chemicals are “heavily influenced” by energy costs. Further, on page 6 of his Rebuttal Testimony, Mr. Woodcock states that the chemical manufacturing industry is one of the six industries that consume three-quarters of all industrial energy and that chemical companies have been adding an energy or fuel surcharge on their bills.³

Mr. Woodcock, however, failed to demonstrate why either of these two facts supports his proposed inflation adjustment for chemicals. Mr. Woodcock did not know how industrial energy usage in the chemical industry compared with the usage in the other five industries. 5/20/2005 Transcript at 215. While Mr. Woodcock acknowledged that the “chemical industry” is very diverse, he did not provide any specifics about energy usage and the water purification chemical industry. Id.

In fact, Mr. Woodcock acknowledged that even though this case was filed in January 2005 and updated in February 2005, “the costs on June 30, 2004 were the most recent costs.” Woodcock Rebuttal Testimony at 6, lines 8-9. KCWA, however, failed to provide any data to support alleged cost increases that it has experienced since June 30, 2004. The generalizations presented by Mr. Woodcock do not provide new support for his chemical inflation adjustment; therefore, the Commission should adopt the Division’s recommendation to deny this adjustment.

³ It is interesting to note that Mr. Woodcock did not specify how much energy was used by the chemical industry relative to the other five industries in this group.

3. *Purchased Water Expense (ACC-7S (Revised 5/23/2005) - (\$80,091))*

KCWA's claim is based on its *pro forma* rate year sales projection. Moreover, KCWA assumes that its own internal production is limited to the amount pumped in the test year. Its rate year claim, therefore, in this case is based on the sale volumes of purchased water that were experienced in the test year, adjusted only to eliminate the water associated with its On Semiconductor revenue adjustment.

The Division is recommending two adjustments, both of which are incorporated at Schedule ACC-7S (Revised 5/23/05). First, the Division has made an adjustment to reflect incremental costs associated with incremental purchases of water that will be necessary as a result of increasing *pro forma* sales. Second, in order to develop a *pro forma* level of purchased water, the Division has reflected an unaccounted-for water percentage of 10%, rather than the 16% included in the KCWA's claim.

The Division's adjustment is based on a review of the actual unaccounted-for water percentage experienced over the past several years. As demonstrated below, KCWA's unaccounted-for water percentage has consistently been below 10%:

Unaccounted-for Water Percentage

FY 2004	8.4%
FY 2003	5.9%
FY 2002	5.2%
FY 2001	9.7%
FY 2000	3.1%
FY 1999	7.2%
FY 1998	7.4%

Crane Direct Testimony at 17.

However, in this case, KCWA has included a total supply of 4,748,309 Ccfs (or 3,551,735 mg) and sales of 3,984,152 Ccfs, for an unaccounted-for water percentage of 16.1%. This has the effect of inflating the purchased water requirements and therefore the associated costs. At Schedule ACC-7S (Revised 5/23/05), the Division made an adjustment to purchased water costs to reflect an unaccounted-for water percentage of 10%. This percentage is still greater than the KCWA's actual results over the past seven years, but is more reasonable than the 16.1% included in KCWA's claim.

KCWA contended that the data provided in the Annual Reports to the Commission was flawed. Moreover, KCWA would have the Commission believe that this data was flawed not just for the test year, but for each of the seven years reviewed by Ms. Crane. As a matter of law, KCWA should be held accountable for the accuracy of the data provided to the Commission each year. See In Re: Appeal of the Office of Consumer Advocate, 597 A.2d 528 (N.H. 1991) (a public utilities commission is entitled to rely on records, particularly annual reports, that utilities are required to file with the agency). It is perfectly reasonable, therefore, for the Commission to rely upon data contained in the annual reports filed by KCWA when determining a *pro forma* unaccounted-for water percentage.

Mr. Woodcock purports to demonstrate that the actual unaccounted-for-water percentage is closer to 18.0%, as shown on page 7 of his Rebuttal Testimony. His calculation is flawed, for several reasons. First, he has excluded sales to On Semiconductor in the sales figure, but he has included all of the water supply for On

Semiconductor in his supply figure. This overstates the actual unaccounted-for water percentage. 5/23/2005 Transcript at 12, lines 16-20.

Second, he excluded sales to Warwick as well as the supply to serve Warwick, but in doing so assumed no unaccounted-for water to Warwick. Thus, any water lost in the transmission to Warwick is implicitly allocated to other customers in his example. Mr. Woodcock acknowledged that it is reasonable to assume that there is some water lost in the transmission to Warwick. 5/23/2005 Transcript at 219, lines 5-8.

Third, Mr. Woodcock uses only one year of data in his analysis, and that one year of data is flawed as stated above. Since unaccounted-for water percentages can and do change from year to year, it is much more reasonable to use a multi-year average. In fact, Mr. Woodcock acknowledged that it was not unreasonable to assume an actual unaccounted-for water percentage of 10%. See 5/20/2005 Transcript at 250, lines 9-24.

For all of these reasons, KCWA has not met its burden of proof with respect to its claim for Purchased Water Expense. The Division, therefore, continues to recommend that the Commission reduce KCWA's claim for Purchased Water Expense by \$80,091 as set forth in ACC-1S and ACC-7S (both Revised 5/23/05).

D. LOBBYING COSTS - ACC-11S – (\$10,115)

On a number of previous occasions, the Commission has held that “it is a ratemaking principle that lobbying expenses are not legitimate ratepayer expenses.” In Re: New England Gas Company Distribution Adjustment Clause, Docket 3548, Order 17971 at 22 (2004); In Re: Tariff Filing by Narragansett Electric Co., Docket 1172, Order 9062 at 22 (1974); In Re: Tariff Filing by Valley Gas Co., Docket 1174, Order 9069 at 12 (1974).

In the last two cases, the electric and gas utilities sought to include \$11,390 and \$1,950 for lobbying activities “with respect to legislation before the Rhode Island General Assembly.” In Re: Tariff Filing by Narragansett Electric Co., Docket 1172, Order 9062 at 22. Although a portion of the activities was categorized as “legal research,” it was “connected solely to the utility’s lobbying effort.” Id. According to the Commission “[t]here [was] no excuse for its having been included in the first place.” In Re: Tariff Filing by Valley Gas Co., Docket 1174, Order 9069 at 12. The entire sum represents lobbying activity, and, therefore, should be disallowed. Id.

More recently, the Commission observed “[i]t is a ratemaking principle that lobbying expenses . . . are not legitimate ratepayer expenses. The Commission, therefore, disallowed \$67,551 of New England Gas Company’s fiscal year 2003 expenses related to lobbying and private membership dues.” In Re: New England Gas Company Distribution Adjustment Clause, Docket 3548, Order 17971 at 22. The Rhode Island Public Utilities Commission’s practice in this regard is not unique. Ms. Crane testified that of the “200 utility cases in approximately 18 states and the District of Columbia” in which she has testified, she has recommended “in virtually every one of those cases . . . against the inclusion of lobbying costs.” 11/23/2005 Transcript at 32-33.

At hearing, KCWA attempted to distinguish the aforementioned Rhode Island cases from the pending matter on the ground that KCWA is a non-investor owned utility. According to KCWA, the principle was more applicable to investor owned utilities because these entities could “take [these expenses] out of dividends.” 5/23/2005 Transcript at 26, line 16-17.

Commissioner Holbrook, however, observed that KCWA's board consists of five members that represent the communities that comprise KCWA's principal territories. The presence of these board members largely eliminates KCWA's need to incur lobbying expenses in the first place:

...the process causes us to have appointed [board members] to serve on the Kent County Water Authority board and oversee policy and planning and stuff like that...If I look at the eight communities that are served, there's significant representation of Kent County Water Authority there. I mean, if those people can't do it, I have a big problem thinking that a hired lobbyist, a hired gun can come in and make the difference between getting what is needed, justifying it versus not.

5/23/2005 Transcript at 43-44.

KCWA contends that R.I.G.L. § 42-139-1, *et seq.* bars its board members/employees from reviewing and commenting upon bills that may affect the utility's operations. 5/23/2005 Transcript at 35. The Division observes that in order to commit a violation of the statute, a person generally must have engaged in "lobbying activity" or have employed a "lobbyist" without having been properly registered. R.I.G.L. § 42-139-9. These terms, however, are limited by their respective statutory definitions or expressly carved-out exemptions.

A "lobbyist," for example, is defined as a person "who is employed and receives payment . . . for the purpose of lobbying . . . or is principally employed to lobby on behalf of that other person or governmental entity." R.I.G.L. § 42-139-2(a). Any employee of state or local government or of any public corporation "to the extent that he or she seeks only to influence or affect decisions or actions of other governmental entities and public corporations solely on its own behalf" is expressly excluded from the definition of "lobbyist." R.I.G.L. § 42-139-2(b)(iii).

The statute also excludes a number of activities from the definition of “lobbying.” The term “lobbying,” is restricted to “acting directly or soliciting others to act for the purpose of promoting, opposing or influencing (i) policy-making decisions of the executive branch of government or of public corporations,” or (ii) “decisions of the executive branch of government or any public corporation involving the sale, lease . . . of any real property owned or leased by the state or any public corporation.” “Participation in a governmental advisory committee or task force” is not considered a “lobbying activity.” R.I.G.L. § 42-139-(1)(b)(v). Nor is “disseminating any publication, including data, research or analysis on public policy issues . . . including any news media reports, editorials, commentary or advertisements” R.I.G.L. § 42-139-(1)(b)(iv). “Advocacy. . . involving the rights, duties or obligations of an individual” is not “lobbying.” R.I.G.L. § 42-139-(1)(b)(iii). Nor is “representation of one’s own, wholly-owned business entity.” R.I.G.L. § 42-139-(1)(b)(vi). Several other exemptions exist as well.

The Division does not express an opinion regarding the precise scope of § 42-139-1. Nonetheless, the foregoing discussion shows that far from constituting an absolute ban on every conceivable “lobbying activity,” R.I.G.L. § 42-139-1, *et seq.* is sufficiently narrow in scope so as to permit KCWA to proffer its views regarding legislation to the General Assembly that may impact its operations by ways that do not contravene the statute.

The Division continues to recommend that the Commission deny KCWA’s claim for \$10,115 in lobbying expenses. Any other result would be contrary to past Commission practice and the standard practice of public utility commissions in other jurisdictions. Further, allowing the recovery of such expenses would appear to have

minimal benefit given the ability of KCWA employees/Board members to represent the utility in the community.

E. OFFICE SUPPLIES AND EXPENSES - ACC-9S – (\$30,528)

Evidence presented at hearing by the Division convincingly showed that KCWA’s actual test year cost for Office Supplies and Expenses was “quite high relative to historic levels.” Crane Direct at 19, line 10. In FY 2004, the expense was \$136,477 while FY 2003 and FY 2002, the expense was \$88,801 and \$92,570, respectively. Id.

Based on this evidence, the Division recommended reducing KCWA’s *pro forma* claim for Office Supplies and Expenses by \$30,528. The Division calculated this adjustment by utilizing a three-year average of KCWA Office Supplies and Expenses—\$105,949—and subtracting the three-year average from KCWA’s claim of \$136,477.

At hearing, KCWA sought to justify its claim of \$136,477 in Office Supplies and Expenses because “we’ve added a newsletter to our company . . . [which is sent] out three times a year [for] about \$24,000.” 5/20/2005 Transcript at 65. KCWA’s effort in support of its “high” claim does not come close to satisfying the utility’s burden of proof with respect to this account item. 5/23/2005 Transcript at 53, lines 12-18. When the Division initially raised the issue in its Direct Testimony, KCWA did not provide any explanation in its Rebuttal Testimony that would justify the unusual increase. 5/23/2005 Transcript at 52, lines 7-23. Nor did KCWA ever produce documentary evidence to show how the newsletter resulted in \$24,000 of costs to the utility. 5/23/2005 Transcript at 53, lines 12-18.

Even at hearing, KCWA could not identify the composition of the incremental difference between its claim of \$136,477 in Office Supplies and Expenses and the far

lower expense figures that KCWA incurred for the same account in FY 2002 and FY 2003.

Q. Mr. Brown . . .What else can you tell us that accounts for the significant increase [in the Office Supplies and Expenses account] over the last three years?

A. I'd only be speculating. All I can say is that's what's booked to that account based on purchase of supplies and so forth. Outside of that, I can't answer the question. I don't know without a dissection of that account.

5/20/2005 Transcript at 98.

KCWA's claim for Office and Supplies expense over and above its historical norm is completely undocumented and unproven. Without any evidence to support KCWA's claim, the Division continues recommend a downward adjustment of \$30,528 as reflected in ACC-9S.

F. MAINTENANCE OF MAINS - ACC-8S – (\$55,338)

As with KCWA's claim for Office Supplies and Expenses, KCWA's claim for Maintenance of Mains is "abnormally high relative to prior year levels." Crane Direct Testimony at 18, lines 8-9. In FY 2002, KCWA's expense for this item was \$374,859; in FY 2003, it was \$395,163; in FY 2004, the expense rose to \$468,020. In the utility's rate application, KCWA seeks to recover \$497,024 for Maintenance of Mains.

Following the logic applied to the Office Supplies and Expenses account, the Division recommends using an average of the last three fiscal years (or \$412,682) in order to establish the *pro forma* level of main maintenance costs in this proceeding. The adjustment of \$55,338 is shown in ACC-8S.

KCWA has never explained with any precision why its claim deviated by such a material amount from FY 2002, FY 2003 or even FY 2004. Mr. Brown conceded that the issue was raised in the Division’s Direct Testimony and further conceded that KCWA had not filed Surrebuttal Testimony to resolve the issue. 5/20/2005 Transcript at 73, lines 9-10. Even at hearing, the best explanation KCWA could provide was that the Maintenance of Mains was a “labor category,” 5/20/20 Transcript at 65, lines 20-21 that “maintenance of mains is higher . . . because we’re doing a lot more of the maintenance of mains.” Id. at 66, lines 2-3.

Mr. Brown then stated the magnitude of these labor costs “depends upon ruptures, breaks and so forth that you have and nobody can predict...” Id., lines 13-14. If funds did not get applied to “maintenance of mains,” then “it would go into the maintenance of hydrants or something elsewhere the staff would be working.” Id., lines 16-18. When asked by his own attorney whether he “ha[d] any idea what that is? Mr. Brown replied, “Not off the top of my head. It fluctuates.” Id. at 66, lines 19-20.

Once again, KCWA has failed to satisfy its burden of proof with respect to its claim for Maintenance of Mains. Having produced absolutely no documentation or other concrete evidence that would remotely justify its *pro forma* claim of \$497,024, the Division continues to recommend reducing this amount by \$55,338, utilizing the methodology outlined in Ms. Crane’s Surrebuttal Testimony. See ACC-8S.

G. OPERATING REVENUE ALLOWANCE - ACC-10S – (\$118,524)

In In Re: Kent County Water Authority Rate Application, Docket 2098, Order 14364 (1993) and again in In Re: Kent County Water Authority Rate Application, Docket 3311, Order 17024 (2001) (settlement), the Commission did not permit KCWA to include

an Operating Revenue Allowance in rates when KCWA already possessed an Operating and Maintenance Reserve. The Commission has explained its rationale for this principle as follows:

The Commission finds that the Authority's inclusion of a proposed operating and maintenance reserve in this filing, a reserve which ostensibly makes KCWA bonds more appealing to potential bond purchasers, negates the need for a traditional operating reserve allowance

In Re: Kent County Water Authority Rate Application, Docket 2098, Order 14364 at 72-73. According to an expert witness proffered in Docket 2098, "the operating and maintenance reserve fund provides a source of funding for operations and maintenance expenses in the event that KCWA experiences a shortfall in receipts, such as that resulting from billing problems, temporary declines in sales or short-term service disruptions." Id. Based on this testimony, the Commission held: "*The operating and maintenance reserve serves an identical function to the operating reserve allowance, and therefore, denied KCWA's request for an additional \$61,815 operating reserve allowance.* Id. (emphasis added).

The Commission's reasoning in Docket 2098 is just as true today as it was in 1993, and was reaffirmed by Ms. Crane at hearing:

That's the whole purpose of the [operating and maintenance] reserve, should it be needed to meet unanticipated O & M expenses. That's why the bond holders require that the reserve be there because they want to make sure that the Authority does have funds if, for example, expenses are higher than anticipated. They want to make sure service won't suffer and those funds will be there. So they required a reserve . . . Rate payers have funded that by over \$2 million. Now you're saying let's ignore that, let's set that aside, let's forget there's a \$2 million reserve fund out there, let's hit the rate payers with another one and a half percent . . . rate payers have already provided that cushion through the funding of the O & M reserve.

5/23/2005 Transcript at 86-87, lines 9-24 & lines 1-3.

Even if the Operating and Maintenance Reserve account is viewed as simply “tied up” due to certain bond covenants, KCWA possesses ample funds to meet any of the utility’s *short-term* unanticipated cash requirements. Again, Ms. Crane testified at hearing:

The Authority currently has somewhere, I think it’s about either 3.4 or 3.6 million now in the IFR. They asked for slightly over 4 million in IFR. Under our recommendation, we give them over 4.9 million in IFR funding. I understand that basically, the IFR account is more or less the last to be funded. So potentially, there would be another source of funds available or potentially available to the Authority through the funding that we’ve given them for the IFR.

5/23/2005 Transcript at 87-88, lines 16-24 & lines 1-3.

KCWA contends that the Commission sanctioned the creation of an Operating Reserve Allowance when a utility already possesses an Operating and Maintenance Reserve. More specifically, KCWA seeks similar treatment to the Pawtucket Water Supply Board (“PWSB”), which currently receives funding in rates for these two reserves.

A review of the history of how the two accounts were established for PWSB shows KCWA’s contention is utterly meritless. In In Re: Pawtucket Water Supply Bd. Application to Change Rate Schedules, Docket 2674, Order 15664 at 73, the Commission “reestablished” PWSB’s Operating Reserve Allowance. At that time, PWSB did not possess an Operating and Maintenance Reserve. Subsequently, in In Re: Pawtucket Water Supply Bd. Application to Change Rate Schedules, Docket 3378, Order 17349 at 25, PWSB sought to establish an Operating and Maintenance Reserve “that will be

needed for treatment plant bonds.” At the time, the treatment plant, alone, had an estimated cost of \$55,000,000. Id. at 3.

Ultimately, PWSB and the Division reached a settlement in Docket 3378 that funded an Operating and Maintenance Reserve based on 25% of *pro forma* operating and maintenance expenses. Id. at 27. The Operating Reserve Allowance was simply incorporated into the settlement in the form previously approved by the Commission in Docket 2674. Id. at Exhibit A to Settlement. Docket 3378 was not litigated, and the Commission never addressed the issue of the propriety of duplicative reserve accounts. KCWA’s contention that PWSB’s history supports Commission approval of duplicative reserve accounts, therefore, is utterly erroneous. See Retirement Bd. of Employees’ Retirement System v. DiPrete, 845 A.2d 270, 282 (R.I. 2004) (where issue was not actually litigated in prior proceeding, issue was not deemed barred in subsequent matter).

The Commission should not now adopt an inappropriate utility practice—*i.e.*, allowing recovery in rates of duplicative reserve account expenses—that, contrary to KCWA’s position, has never received Commission approval. To do so would erroneously perpetuate an anomaly that exists due to the unique history of one utility—PWSB. Extending this anomaly to KCWA would be detrimental not only to KCWA’s ratepayers, but also to other Rhode Island ratepayers as their respective utilities would seek the creation of duplicative reserves as well.

III. CONCLUSION

For all of the above reasons, the Division recommends that the Commission approve the position reflected in the Division’s Surrebuttal, as amended, setting the Authority’s overall revenue requirement at \$15,703,730, provided that all amounts over

\$2,330,902 or \$841,763 are restricted and used for additional IFR funding, bringing the total IFR funding amount to \$4,921,763.

DIVISION OF PUBLIC UTILITIES AND
CARRIERS

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CERTIFICATE OF SERVICE

I certify that a copy of the within memorandum of law was forwarded by regular mail, postage prepaid, to the individuals designated on the Docket's Service List on the July __, 2005.
