

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

**BEFORE THE
RHODE ISLAND PUBLIC UTILITIES COMMISSION**

**IN RE:
CITY OF NEWPORT, UTILITIES DEPARTMENT,
WATER DIVISION APPLICATION TO CHANGE
RATE SCHEDULES**

Docket No. 4025

**INITIAL BRIEF OF THE
UNITED STATES DEPARTMENT OF THE NAVY**

Introduction

The United States Department of the Navy (Navy) herewith submits its Initial Brief in the above-captioned matter. Naval Station Newport, in Newport, Rhode Island, is the second-largest customer of the Newport Water Department (NWD). The Navy has participated in this proceeding through the submission of Direct Testimony, Surrebuttal Testimony, data requests and responses to data requests. This Brief will address certain aspects of the determination of revenue requirements that should be approved for the Newport Water Department and the design of rates to recover that level of revenues.

Revenue Requirements

1. Cost Allocation Manual

As a part of its direct filing in this proceeding, NWD offered a Cost Allocation Manual (CAM) that presents a methodology for allocating the costs of supporting services provided by the City of Newport to its various Enterprise Funds, including the Water Department (NWD Exhibit Nos. 1B and 1C). The CAM was presented in

response to the Commission's Order in NWD's most recent prior rate case, RIPUC Docket No. 3818. The Navy, Portsmouth Water and Fire District (PWFD) and the Division of Utilities and Carriers (Division) all presented testimony in opposition to certain NWD allocation methods (Navy Exhibit No. 1; PWFD Exhibit Nos. 1 and 2; Division Exhibit Nos. 1 and 2). In general, these parties testified that NWD's CAM over-allocated costs to the Enterprise Funds, including the Water Department.

The proper allocation of these costs between the Enterprise Funds on the one hand, and taxpayers in the City of Newport on the other, is a critical issue in this case. It is likely that the allocation methods approved by the Commission here will serve as a precedent in future NWD rate proceedings. The Navy testified through its witness Ernest Harwig, "[T]o the extent that these support costs are collected from Enterprise Fund customers, including Middletown retail water customers, PWFD and the Navy, property tax payers in Newport are relieved of this burden" (Navy Exhibit No. 1, Page 6).

In its Rebuttal Testimony, NWD has accepted some of the changes to its allocation methods offered by the other parties (NWD Exhibit Nos. 3 and 4). However, NWD still maintains that the School and Library budgets should be excluded from the total General Fund Budget when calculating the Water Department's share of City Manager and Finance Administration Costs. Both PWFD and the Division have argued for the inclusion of the School and Library budgets.

The Navy supports the position of PWFD and the Division for the inclusion of the School and Library budgets when calculating the total General Fund Budget. First, the exclusion of the School and Library budgets from the total General Fund Budget is contrary to the Compliance Filing in Docket No. 3818 (RFC Schedule A Final). Second, as Mr. Catlin testified on behalf of the Division, "...the fact that there is (at least) some involvement (by the City Council, City Manager and Finance Director) demonstrates that

it is not appropriate to simply exclude the School and Library budgets from the calculations” (Division Exhibit No. 2, Page 8, Lines 10 - 12).

2. Financing of Capital Improvement Projects

In its direct testimony, NWD proposed to finance \$553,199 of long-lived capital improvements with current revenues (Navy Exhibit No. 1, Page 6). The Navy argued that financing through current revenues instead of debt issuance places an undue burden on today’s ratepayers and creates intergenerational inequity, since future ratepayers will be subsidized by today’s customers. The witness for PWFD stated that he was philosophically in agreement with this approach (PWFD Exhibit No. 2, Page 3), as did the witness for NWD (NWD Exhibit No. 4, Page 5). Navy witness Harwig also noted that financing through current rates was economically burdensome to ratepayers, given that the most recently reported unemployment rate in NWD at the time of drafting his testimony was 11.2% (Navy Exhibit No. 1, Page 8, Line 14). The Navy urges the Commission to encourage NWD to finance its future capital improvement in a manner that places the least burden possible on NWD’s ratepayers, consistent with debt service coverage requirements imposed by NWD’s lenders.

3. Additional Revenue Requirement

NWD requested an additional revenue requirement equal to 3% of its operating expenses as a cushion against unexpected increases in operating expenses or decreases in revenues (NWD Exhibit No. 1C, Schedule 1). The Navy argued that a 1.5% additional revenue requirement would be consistent with the Compliance Filing in Docket No. 3818 (Navy Exhibit No. 1, Page 8). The Navy continues to maintain this position for the reason stated in its direct testimony, and additionally in light of the level of unemployment in Newport referenced above.

Cost of Service and Rate Design

NWD, PWFD, and the Division argue that any revenue increase granted to NWD in this case be implemented on an equal percent across-the-board basis. The Navy argued that such an approach could perpetuate or even exacerbate any disparities between the cost of serving individual customer classes and the revenues collected from them (Navy Exhibit No. 1, Page 9). The Navy recommended that the Commission order a Phase 2 Proceeding in the present case, upon the completion of the peak demand study now in progress and its incorporation in a cost of service study, to expeditiously address this important issue. The results of the study should form the basis for any adjustment in various customer class rates to make them conform more closely to the cost of providing service. NWD's witness, Harold Smith, agreed that a Cost of Service Study would allow for such an appropriate adjustment, which should be expeditiously implemented (Transcript, Page 217-218).