STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: NARRAGANSETT BAY	:	
COMMISSION'S GENERAL	:	**DOCKET NO. 4364**
RATE FILING	:	

REPORT AND ORDER

On October 5, 2012, the Narragansett Bay Commission ("NBC") filed an application with the Rhode Island Public Utilities Commission ("Commission") seeking an increase in base rates for effect July 1, 2013. The proposed rates were designed to generate additional revenues of $12,483,704 and if approved as filed, would increase NBC's present revenues by 14.05 percent.

The present filing represents the fifth rate filing in the last three years all of which, with the exception of the instant matter, were needed to support debt service and debt service coverage associated with NBC's Capital Improvement Program ("CIP").[1]

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[1] In addition to applications to increase rates, the Commission in Docket No. 3483 allowed NBC expedited treatment when it files to increase rates solely for debt service and debt service coverage. NBC's primary source of funding for its capital program is in the form of borrowings from the State Revolving Loan Fund ("SRF") administered by the Rhode Island Clean Water Finance Agency ("RICWFA"). Since loan capacity is limited, the Variable Rate Debt Obligation in Tax Exempt Commercial Paper ("VRDO/TECP") program provides for short term financing with attractive variable rates that can be paid off as more State Revolving Loan Fund ("SRF") money comes available. VRDO/TECP is less costly than Open Market Bonds. The requirements for all compliance filings seeking a rate increase under the TECP/VRDO program are that they: 1) be filed no later than sixty days prior to its effective date, 2) be limited for debt service and debt service coverage for CIP projects, 3) contain a revised limited cost of service schedule reflecting the changes to the revenue and expense accounts affected by the VRDO/TECP program, 4) contain testimony and schedules in support of the debt service and debt service coverage proposed as well as a current and projected annual debt service payment schedule, 5) contain a summary of funds currently available for the CIP program and the projected funding needed for the rate year period, 6) contain a summary of funding received from Rhode Island Clean Water Finance Agency (RICWFA), including funds requested, received, the interest rate, and repayment schedules, 7) contain a summary of how prior years' debt service coverage funds were utilized, 8) contain a calculation of new rates based on a uniform percentage increase to rates, and 9) contain a showing of compliance with prior Commission orders and the requirements of Section 2.11 of the Commission's Rule of Practice and Procedure.

The following provides a history of recent rate increases:

DOCKET NO.	FILING DATE	INCREASE REQUESTED	INCREASE ALLOWED	AUTHORIZED REVENUE
4151	3/2/10	$ 2,111,330	$1,667,687	$78,604,366
4214	11/24/10	$ 2,521,655	$2,521,655	$81,126,021
4305	12/20/11	$ 1,763,306	$1,763,306	$82,889,327
4352	8/27/12	$ 5,877,586	$5,877,586	$88,766,913

In support of its application, NBC submitted the pre-filed testimony of its consultant, Walter Edge of B&E Consulting LLC, its financial advisor, William Fazioli, and its Combined Sewer Overflow ("CSO") Abatement Program Manager, Joseph Pratt.

I. NBC PRE-FILED DIRECT TESTIMONY

A. Testimony of Walter E. Edge, Jr.

In his pre-filed testimony, Mr. Edge noted that NBC has not filed for general rate relief since December of 2008. The major issue in NBC's last rate case, Docket No. 4026, was a revenue shortfall caused primarily by the over-estimation of rate year consumption resulting in consumption rates to be calculated lower than they should have been. In Docket No. 4026, NBC based rate year consumption on a downward trend which was supported by the Division of Public Utilities and Carriers ("Division") and approved by the Commission. Mr. Edge expressed that since that time, the decline in overall consumption has leveled off, so NBC based rate year consumption on test levels in the instant matter. Additionally, since the CSO Phase I facilities had not been operational at the time of the last general rate filing, the operating costs for those facilities were not included in the test year in Docket No. 4026. The current filing does include a full year of CSO Phase I Facilities operating costs for the fiscal year ending June 30, 2012. Mr. Edge also noted that in this proceeding, NBC was requesting an increase in its operating reserve from 1% to 1.5% which he identified as more in line with what other water utilities are allowed. Lastly, he listed a number of other items addressed in Docket No. 4026 that would also be addressed in the instant matter. Mr. Edge identified six major items driving NBC's need for additional revenues: 1) the need to update the base rates with respect to consumption, 2) the need to update the number of non-residential meters, 3) salaries and related fringe benefits, 4) utility increases, 5) debt service and 6) miscellaneous adjustments including biosolids disposal and management/audit services. He expressed that NBC is requesting $12,483,704 of additional revenue which amounts to a 14.50% rate increase over test year revenue or a uniform across-the-board increase of 14.98%.[2]

Mr. Edge used the fiscal year ending June 30, 2012 as the test year to which he made certain adjustments to revenues including the elimination of the Investment Income earned during the test year that was not available for operations, the elimination of Environmental Enforcement Fund revenues and related expenses, the removal of grant revenues and expenses and the elimination of capital contributions. He adjusted user fee accounts to reflect the approved and anticipated rate increases for debt service in Docket Nos. 4305 and 4352, respectively. Mr. Edge also made a number of adjustments to expenses: 1) removing a one-time dividend to worker's compensation insurance as it is non-recurring, 2) eliminating bond and note fees, removing depreciation and almost all of the annual amortization expense which he noted was for the Bucklin Point organization that was established a number of years ago by the Auditor General's office and needed because NBC is regulated on a cash basis, 3) increasing operating capital outlays that

[2] NBC Exhibit 1a, NBC Rate Application, Direct Testimony of Walter E. Edge, Jr. filed October 5, 2012 at 1-5.

were charged and note expenses which he reversed in the rate year because they are funded with the debt service coverage and carry-forward, 4) adding interest, principal and debt service coverage to reflect that amount requested in Docket No. 4352 and 5) calculating a 1.5% net operating reserve. Mr. Edge expressed that his adjusted test year represents a level of activity for a normalized year of the NBC.[3]

In organizing his testimony, Mr. Edge divided most accounts into four groups, revenue accounts, personnel service accounts, capital outlay accounts and accounts with balances in the test year of less than $200,000. For those accounts that did not fall within one of the four groups, he conducted a separate analysis. When discussing revenue accounts, Mr. Edge identified the use of test year consumption as the most significant issue regarding consumption projections. He noted how using test year consumption had adversely impacted NBC's ability to bill at the Commission approved revenue levels in the past and explained how the Commission had approved using a projected downward consumption trend method in the last general rate case. Although this resulted in a slight improvement over the use of test year consumption to project rate year consumption, it was not as successful as anticipated. Mr. Edge indicated that even with its revenue shortfalls, NBC finishes each year with significant net income because its approved rates are designed to generate 125% of principal and interest so that NBC is able to meet its debt coverage requirements. He provided that in the instant matter, he used the test year to project consumption, because the downward trend in consumption appears to have subsided.[4]

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[3] *Id.* at 6-9.
[4] *Id.* at 10-12.

Mr. Edge made a number of adjustments to expense accounts. First he discussed personnel services which he adjusted for salaries to reflect contracted step increases and Cost of Living Adjustments ("COLA") for union employees and merit increases for non-union employees. He calculated the two reimbursement accounts for capital salaries and fringe benefits and overtime in the same manner that he had increased the salaries for non-union employees. Then he increased FICA and Medicare expenses as they are a function of payroll expense. Retirement account expense, as well as the retirement health account for union employees, was calculated using values provided by the State of Rhode Island Budget Office for FY 2014, and non-union pension expense was calculated at 10% of non-union and limited rate year salaries as it had been in prior dockets. Mr. Edge adjusted for an increase in health and dental costs for the rate year by using a two year average percentage rate increase which he then reduced by a projected co-pay amount.[5]

In addition to personnel services, Mr. Edge adjusted the rate year cost of biosolids disposal to reflect contracted CPI increases for a total rate year expense of $4,300,094. Maintenance/Service Agreements expense was adjusted by $325,378 to reflect average percentage increase for the past two years as well as to reflect the cost of new equipment at Field's Point, new laboratory information management system software and laboratory instruments that did not previously have service contracts for a total expense of $1,060,552. Mr. Edge adjusted insurance expense by $63,995 which was the average of the two year annual percentage increase and also used a two year average to adjust therms in calculating $454,609 in natural gas expense. Electricity expense was also adjusted to reflect the projected electricity that will be generated by NBC's wind turbines once they become operational. The $129,788 adjustment in hypochlorite costs and

[5] *Id.* at 13-14.

$140,099 in bisulfite costs, the two chemicals NBC uses in its operations, were projected using the two year average for usage rate, and the costs of carbon feed and sodium hydroxide, new chemicals used at the Field's Point facility, were added as rate year expenses of $172,800 and $196,468, respectively. Mr. Edge adjusted the management/audit services account to reflect the contracted CPI increase. He deducted capital outlays from NBC's rate year revenue requirement as that expense is paid from the prior year restricted debt service coverage carry-forward. He also increased the debt service accounts to reflect borrowing expected during the rate year and requested that the Commission extend the current debt service compliance filing mechanism for an additional five years.[6]

Mr. Edge noted that in order to finance its Capital Improvement Program, NBC anticipates filing annually with the Commission. He requested that rate case expense be left at the test year level and that it not be amortized over any future period which is consistent with how the Commission has treated it in the previous docket. Lastly, he discussed NBC's net operating reserve and requested that the Commission increase this allowance from 1% to 1.5% in order to allow NBC the flexibility to meet operating costs should it experience an increase in operational costs in attaining permitting requirements. Mr. Edge requested that the proposed rates become effective July 1, 2013. Finally, he proposed that rates be increased equally across the board.

B. Testimony of William Fazioli

William Fazioli provided testimony regarding NBC's long term financing plans, debt issuance needs and in support of continuation of the debt relief compliance filing mechanism. He noted that as of August 31, 2012, NBC had $492.8 million in

[6] *Id.* at 14-17.

outstanding debt, $60 million of which is Variable Rate Demand Bonds ("VRDB") and $91.8 million of which is open market revenue bonds. He explained that most of NBC's borrowing and the lowest cost method of financing is through the Rhode Island Clean Water Finance Agency ("RICWFA") which has been supplemented by the issuance of variable rate debt. He pointed out that over the next three fiscal years, NBC's Capital Improvement Program has $310 million of programmed expenditures, $126 million of which are in FY 2013, and will have to issue debt of more than $280 million over the next five years.[7]

NBC's credit rating was upgraded by Standard and Poor's in 2008 to AA- which was recently affirmed in May of 2012. Mr. Fazioli noted that this rating is beneficial for ratepayers and will result in costs savings on future borrowings on interest rates and remarketing of its VRDBs which over the last year have been remarketed at an average rate of 0.14%. He expressed that both the Commission's allowance of rates that generate 125% of principal and interest in accordance with NBC's Trust Indenture as well as the Commission's approval of the debt service compliance filing mechanism have contributed to NBC's credit strength. Like Mr. Edge, Mr. Fazioli also requested that the Commission approve continuation of the debt service compliance filing mechanism.[8]

C. Testimony of Joseph Pratt

Mr. Pratt provided testimony to update the Commission on the status of NBC's Combined CSO Phase II Facilities. He indicated that the Louis Berger Group, Inc. has provided NBC with management services for the CSO Abatement Program since 1992. Mr. Pratt noted that pursuant to the terms of the Consent Agreement between NBC and

[7] NBC Exhibit 1b, NBC Rate Application, Direct Testimony of William Fazioli filed October 5, 2012 at 1-4.
[8] *Id.* at 4-7.

the Rhode Island Department of Environmental Management ("DEM"), NBC had completed and submitted final design plans for Phase II to DEM, which were approved and that NBC has four years to complete construction of the Phase II Facilities which began in 2012 and are 30% complete. The projects are scheduled to be complete in FY 2016[9]

D. Supplemental Testimony of Walter E. Edge

On March 7, 2013, Mr. Edge filed supplemental testimony for the purpose of correcting Schedule WEE-5 that he represented had understated the rate year adjustment and rate year expense for health and dental insurance by a total of approximately $169,000. With this supplemental testimony, he provided revised schedules.[10]

II. DIVISON PRE-FILED DIRECT TESTIMONY

Mr. Catlin testimony presented on behalf of the Division contained findings and recommendations regarding the requested revenue increase and the rate design proposed to recover that additional revenue. Based on his evaluation, he determined that NBC has a total revenue requirement of $93,377,869 which represents $5,192,022 less than the $12,483,704 NBC requested. He accepted NBC's rate design to recover the additional revenues through a uniform percentage increase in the flat fees and volumetric rates applicable to residential, commercial and industrial customers but suggested that a stormwater fee be implemented that would apply to more than just wastewater customers. He utilized a test year ending June 30, 2012 and a rate year ending June 30, 2014.[11]

Mr. Catlin reduced operating expenses by additional $4,247 that NBC acknowledged in a data request response should have been removed for grant related

[9] NBC Exhibit 1c, NBC Rate Application, Direct Testimony of Joseph Pratt, filed October 5, 2012 at 1-6.
[10] NBC Exhibit 7, Supplemental Direct Testimony of Walter E. Edge, Jr. filed March 7, 2013 at 1.
[11] Division Exhibit 1, Direct Testimony of Thomas S. Catlin filed March 22, 2013 at 1-6.

costs. He also proposed two adjustments to employee health insurance costs: revising the growth rate used to project medical and dental premiums for the FY 2014 rate year by using the average annual increase over a three year period instead of the single year percentage increase from FY 2012 to FY 2013 and correcting the understated rate year adjustment and rate year expense for health and dental insurance as Mr. Edge had in his Supplemental Direct Testimony. His total adjustment to Employee Health Insurance was an increase of $141,233. He reduced NBC's Workers' Compensation Old Claims to eliminate two claims that have been discontinued for a total reduction of $20,374.[12]

Regarding biosolids disposal costs, Mr. Catlin revised NBC's 2013 rate to reflect the actual increase in the CPI for the Boston area from November 2011 to November 2012 of 1.90% as opposed to the November 2010 to November 2011 rate of 3.12% that NBC had utilized and also revised the 2014 rate to reflect projected inflation from November 2012 to November 2013 based on financial indicators. His adjustment resulted in a biosolids disposal expense of $4,223,730 which is $76,364 less than the amount requested by NBC. Mr. Catlin disagreed with NBC's projected rate year maintenance and service costs asserting that the normal growth rate was overstated because NBC based it on the annual growth rate for the FY 2010 to FY 2012 period. He noted that in Docket No. 4205, NBC had represented that FY2011 costs were expected to increase by $106,867, because the costs associated with the two service agreements that had been previously charged to capital would be charged to expense prospectively. He provided that NBC's new Oracle accounting software does not provide for a breakdown of amounts spent on maintenance and service agreements by vendor/provider and because of this he was unable to determine if the reason that costs had increased from FY

[12] *Id.* at 4-9.

2010 to FY 2012 was the result of normal growth, new agreements or other causes. He recommended escalating the FY 2012 amount for inflation and adding in the cost of the two new agreements identified by NBC which resulted in a decrease of $161,230 of the amount requested by NBC.[13]

Mr. Catlin expressed that NBC had overestimated its natural gas costs by failing to recognize the decline in price that had occurred since FY 2010. He identified National Grid's primary GCR rate for the twenty-four month period beginning July 2010 through July 2012 and noted that based on National Grid's hedged volumes and prices for the year ending October 2014, those prices were expected to further decline. He adjusted the 2013 GCR rates to account for the decline in National Grid's hedged gas costs. Then he compared the average of the hedge purchases National Grid had made for the 2013 and 2014 GCR years and reduced its 2011 GCR rates by that amount to estimate the GCR rates that will be in effect for November 1, 2013 through October 2014. His calculations resulted in an estimated gas cost of $212,028 for gas supply costs for the rate year which was $95,937 less than NBC's request before gross earnings tax savings of $2,967. Mr. Catlin made three adjustments to NBC's estimated electric costs for the rate year: updating the Standard Offer rates to reflect National Grid's average rate for the most recent twelve month period, increasing the projected kWh that will be available from the three wind turbines that will be operational at Field's Point which will reduce the amount of electricity NBC must purchase at that facility, and recognizing revenues from the sales of renewable energy credits of $50 per MWh. His adjustment resulted in a reduction in NBC's electricity costs of $783,148.[14]

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[13] *Id.* at 9-12.
[14] *Id.* at 12-17.

NBC's Field's Point chemical costs were adjusted by Mr. Catlin to account for a calculation error that the Company identified in response to a data request accounting for a $68,136 reduction in that expense. Concerned that NBC's estimated chemical prices were overly conservative, Mr. Catlin requested that it attempt to obtain indicative prices for the chemicals from its suppliers. He noted that NBC was awaiting new bids for two chemicals and that he would update the Division's recommendation if new chemical prices became available.[15]

Mr. Catlin disagreed NBC's use of the test year as representative of bad debt expense since prior to FY 2012, NBC had not written off bad debt since FY 2008. He suggested that an average of the bad debt for FY 2011 and FY 2012 be utilized which resulted in a reduction to bad debt expense of $85,229. He adjusted NBC's debt service expense to reflect the reduction in the expected issuance of new debt in FY 2014 and concluded that the total amount required for debt service and coverage be $56,117,913 approximately $3.6 million less than NBC requested.[16]

Regarding the Operating Reserve allowance, Mr. Catlin made a downward adjustment to reflect 1 percent of total expenses excluding personnel services, debt service and debt coverage which resulted in a reduction of $414,269. He accepted the proposal that the revenue increase be recovered through uniform percentage increases in user fee rates. Lastly, he suggested that the Commission consider implementing a stormwater fee that applies to a broader base than only NBC's wastewater customers.[17]

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[15] *Id.* at 17-18.
[16] *Id.* at 18-21.
[17] *Id.* at 21-22.

III. NBC PRE-FILED REBUTTAL TESTIMONY

On April 24, 2013, NBC filed the rebuttal testimony of Mr. Edge. Addressing Mr. Catlin's proposed changes, he agreed with the adjustments to grant related expenses, workers compensation – old claims expense, and biosolid disposal costs. He explained that since the time of his initial filing, NBC obtained the actual renewal rates for health and dental insurance which resulted in a health insurance expense of $3,432,963 and a dental insurance expense of $253,195. Mr. Edge disagreed with Mr. Catlin's adjustment to maintenance and service agreements and noted that NBC will have a minimum expense of $1,007,802 in the rate year. He adjusted his schedule to reflect this minimum expense. He asserted that it was not reasonable to project a continued decline in natural gas costs noting also that NBC's customer charge had increased. This increase along with the current price of natural gas allowed for a reduction in his proposed rate year cost of $82,526. Mr. Edge accepted Mr. Catlin's adjustment for electricity produced by the wind turbines and for the projected revenues for the sale of RECs. He noted that this expense can vary significantly and that other adjustments or the operating reserve are not sufficient to accommodate such a variance. He made an adjustment to reflect NBC's three year contract price of $0.0641 per kWh.[18]

Mr. Edge agreed with Mr. Catlin's adjustments to Field's Point chemicals expense, bad debt expense, debt service and debt service coverage line items, conditioning his agreement on the Commission's approval of NBC's request to continue with the current debt service compliance filing mechanism as requested in Docket No. 4352. He disagreed continuing to only allow NBC to collect an operating reserve of 1.0% noting that it was inconsistent with the Commission's treatment of other utilities.

[18] NBC Exhibit No. 10 Rebuttal Testimony of Walter E. Edge, Jr. filed April 24, 2013 at 1-4.

He expressed that the 1.5% originally requested was conservative and amounts to less than 20% of one month's operating expenses or approximately $570,000. Lastly, he made two adjustments to revenue line items: eliminating BOD/TSS surcharges of $93,462[19] and increasing miscellaneous income by $355,650 to reflect Mr. Catlin's projection of revenue to be realized by the sale of RECs.[20]

VI. DIVISION PRE-FILED SURREBUTTAL TESTIMONY

Mr. Catlin provided surrebuttal testimony on May 8, 2013 to respond to Mr. Edge's rebuttal testimony and to update his recommendation on NBC's revenue requirement. Of the six items that were in dispute, employee health insurance, boisolids disposal costs, maintenance and service agreements, natural gas expense, electricity costs and the operating reserve, Mr. Catlin accepted all of Mr. Edges estimates and revisions except for the change to natural gas expense and NBC's rationale for increasing its operating reserve.[21]

Regarding NBC's natural gas expense, Mr. Catlin recommended that the Commission use the average of the National Grid GCR rate for the rate year instead of the 2013 GCR rate as proposed by NBC. He also noted that Mr. Edge had raised the issue of eliminating the BOD/TSS surcharges and assumed the Commission would approve this request to which he had no objection. His updated recommendation was that NBC be

[19] On March 20, 2013, NBC filed a tariff advise seeing to eliminate the BOD and TSS Surcharges. NBC requested the revision take effect January 1, 2013. In support of its request, NBC noted that it must install new and upgrade exiting Biological Nutrient Removal (BNR) facilities and that the BNR process will be helped by higher BOD levels reducing the need for NBC to supplement the process with chemicals. NBC further noted that as there is no correlation between higher TSS levels and NBC's wastewater treatment costs, the surcharge is no longer appropriate.
[20] NBC Exhibit No. 10 at 4-6.
[21] Division Exhibit No. 2 Surrebuttal Testimony of Thomas S. Catlin, filed May 8, 2013 at 1-3.

allowed additional revenue of $7,964,892 over present rates for an overall revenue requirement of $94,313,267.[22]

IV. HEARING

Following published notice, an evidentiary hearing was conducted at the offices of the Public Utilities Commission at 89 Jefferson Boulevard, Warwick, Rhode Island on May 15, 2013. The following appearances were entered:

FOR NBC:	Joseph A. Keough, Jr., Esq.
FOR THE DIVISION:	Christy Hetherington, Esq. Special Assistant Attorney General
FOR THE COMMISSION:	Patricia S. Lucarelli, Esq. Chief of Legal Services

Prior to the commencement of the evidentiary hearing, the Commission allowed for public comment where five individuals addressed the Commission and expressed concern over the impact of a revenue increase. Mr. Keough provided opening comments briefly describing NBC's filing and noting that NBC was amenable to the Division's reduction in its proposed cost for natural gas. He expressed that the only remaining issue was the amount of NBC's operating reserve. Mr. Edge, Mr. Fazioli and Mr. Pratt were presented as a panel to respond to questions regarding their testimonies and NBC's filing. Mr. Pratt adopted his pre-filed testimony noting, however, that since the filing, lower construction bids have resulted in NBC substantially reducing the costs of the 2014-2018 CIP. Mr. Fazioli also updated his testimony adding that since March of 2013, NBC has issued $75 million of debt at a rate of 4.04%. He recommended that NBC's debt filing mechanism be continued.[23]

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[22] *Id.* at 4-5.
[23] Transcript of Hearing ("T."), May 15, 2013 at 2-38.

After accepting Mr. Catlin's adjustments, one a true-up adjustment and the other a reduction in natural gas costs, Mr. Edge adopted his pre-filed testimony. Mr. Edge testified that the debt service compliance filing mechanism has significantly improved NBC's ability to borrow at the best rates which in turn benefits ratepayers. He expressed that with a 1.5% operating reserve, NBC's expenses are fair, reasonable and necessary to provide service to its ratepayers. In justifying NBC's request, he noted that the last matter in which NBC had requested additional revenue for operating expense was filed in 2008 for a 2010 rate year. He opined that NBC has been doing an excellent job of controlling operating expenses which is evidenced by the fact that it has not requested an increase for those expenses since 2010 and emphasized the small amount of the current request.[24]

When questioned about the operating reserve, Mr. Edge testified that he did not believe NBC has "ever even collect[ed] it." He noted that if NBC doesn't collect enough revenue, "the first thing that goes is the operating reserve…." He was unable to provide testimony as to the amount collected for the operating reserve. He further testified that NBC "never really get[s] the revenue that's authorized by [the] Commission, and, therefore, if you don't get the revenue, you have to pay all your bills first and the last thing that would be received would be the operating reserve." Continuing to address the operating reserve, Mr. Edge testified that there is "no fund for the operating reserve…and had there been an operating reserve fund, [he was] not sure there would have ever been enough revenue to fund it". He acknowledged that ratepayers have not suffered by this lack of funding and explained that the purpose of the operating reserve is to have money available should NBC's estimates made in a rate filing not be accurate. However, he

[24] *Id.* at 38-48.

alleged that because "NBC manages [its] money as well as anyone, and because of their good job, they're actually being penalized by having only the smallest net operating reserve [of] all the utilities regulated by the Public Utilities Commission."[25]

Mr. Edge was also questioned about the difference in the pay increase percentages between union and non-union employees to which he explained resulted from NBC's collective bargaining agreement with the union. He was unable to provide detail about merit increases given to non-union employees and acknowledged that he did not conduct a detailed review of the union employees' step increases. Karen Giebink, NBC's Director of Administration and Finance, testified in detail about the merit increase program available to non-union employees who are not entitled to receive longevity or step increases. She explained that the merit increases amount to an average of three percent but can be as much as five or six percent of an employee's salary. She described the extensive review that NBC had conducted of each employee's position and how job specifications were established and assigned a grade and an associated salary range. She responded that movement within the range is based on merit and that NBC has hired a third party to look at ranges. When questioned about the difference in the increase in health care expense between NBC and the state, Ms. Giebink pointed out that the state is self-insured which would account for part of the difference. Regarding overtime expense, Ms. Giebink testified that one of the reasons this expense has been so high is because of the construction at Field's Point and Bucklin Point and the fact that in order to bring a new facility on line, it requires that they take facilities off line which means employees are called in to work night shifts. In response to the question of whether these

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[25] *Id.* at 48-53.

costs would decrease, she provided that overtime is difficult to manage because of permit requirements.[26]

Ms. Giebink explained the sewer user rate as a composite charge consisting of a flat fee which is designed to recover fixed costs and a consumption charge based on usage and that each individual residential customer is charged a flat fee even if that customer lives in a multiunit dwelling of six or less units because the system has to have the capacity to handle discharge from each unit. Mr. Edge further explained that historically, the charge used to be only a customer charge to read a meter, send out bills, etc. However, this charge has changed substantially. He described how NBC's debt service fee remained fixed and was more significant each year and that the flat fee, which used to be called a customer charge is a recovery of fixed charges. Mr. Keough added that the new sewer connection fee and the customer charge per dwelling unit are not the same thing and that the flat fee includes more than only the customer charge.[27]

Ms. Giebink testified about NBC's wind turbines and how NBC has approval for the sale of Renewable Energy Certificates ("REC") in Massachusetts. She provided that the turbines are limited to instantaneously producing up to 900 kilowatts but should be able to be increased once some additional infrastructure is put in place. The anticipated revenue from the sale of the RECs she testified is $355,650 even though there are no contracts in place for such a sale. Mr. Catlin added how he had determined his estimated REC revenues. Mr. Edge noted that the generation provided by wind turbines resulted in an increase of revenue for NBC by the sale of RECs and a decrease of its electric expense. Mr. Pratt testified about how bid prices are below cost and the expectation that

[26] *Id.* at 53-63.
[27] *Id.* at 63-69.

change orders will be seven to nine percent of contract value in Phase 2. Of eleven contracts, he noted that nine were in-state bidders.[28]

Mr. Catlin, the Division's witness, reiterated that the adjustments made by the Division and NBC were reasonable. He described that there are high costs unrelated to wastewater treatment and collection requirements and suggested that the Commission conduct an investigation into the possibility of implementing a stormwater fee that would impose the cost of the CSO project on a broader base of people than just NBC's wastewater customers as it is that small group of non-customers that cause significant costs. As an example, he described how the stormwater runoff from a parking lot would collect in storm drains. When asked, he responded that these non-customers would be billed separately. Even though he suggested it in his direct testimony, he acknowledged that the issue of a stormwater fee was not an issue in the instant matter.[29]

When questioned about the 1% operating reserve, Mr. Catlin testified that he originally recommended that the Commission allow for an operating reserve of 1.5% but since the Commission had previously rejected this increase, he chose to recommend only the 1%. He opined that since NBC has not filed a rate case since 2008, it has been able to meet revenue requirements without a 1.5% operating reserve but was not able to provide testimony as to whether that higher amount was needed.[30]

V. DECISION

At its open meeting on June 13, 2013, the Commission deliberated on NBC's proposed revenue increase. Finding the adjustments made by the Division and accepted by NBC to be reasonable, the Commission discussed the sole remaining issue in dispute

[28] *Id.* 69-80.
[29] *Id.* at 85-92.
[30] *Id.* at 92-95.

between the parties, NBC's request for an increase in its operating reserve from 1.0% to 1.5%. Relying on Mr. Edge's testimony that NBC had not in the past collected sufficient revenues to actually fund this account and that other water utilities were afforded an amount greater than 1.0%, the Commission finds that the Company should be allowed an operating reserve of 1.5% consistent with the Commission's treatment of other water utilities. The Commission has previously stated that it is important for a utility to be able to manage unanticipated decreases in revenues or unexpected increases in expenses, which are beyond the control of the utility such as energy or chemical costs.[31] Because there are costs that NBC cannot control, the Company should be afforded some degree of security in the event that those costs exceed estimates so that it is able to continue to satisfy its financial obligations and maintain quality service to its ratepayers. As previously held, the Commission continues to believe that both personnel and debt service costs are within the control of the utility. In Docket No. 3797, the Commission considered a number of factors in setting an operating reserve including "significant revenue fluctuations, unanticipated increases in fuel costs, unexpected increases in expenses which are beyond the control of the utility and necessary to meet expenses approved in the cost of service."[32]

Understanding that each utility is unique in its fiscal management and needs, the Commission finds that even though NBC has agreed to accept the Division's adjustments, there continues to exist uncertainty in certain costs that justifies an increase in their operating reserve from 1.0% to 1.5%. Giving the magnitude of NBC's capital program and responsibilities of this operation relative to its peer water utilities, it is not

[31] Docket No. 3660, Order No. 18316 *citation omitted.*
[32] Docket No. 3739, Order No. 19062. The Commission reiterated these reasons in Docket No. 4026

unreasonable that NBC have the additional security of a 1.5% reserve to deal with unforeseen cash flow constrictions. The Commission approved the revenue increase agreed to by NBC and the Division for effect July 1, 2013 and accepted the Division's recommendation that the increase be recovered through a uniform increase to rates.[33] The Commission finds that this rate increase is reasonable, necessary and in the public's interest.

Accordingly, it is

(21132) ORDERED:

1. The Narragansett Bay Commission's rate application of October 5, 2012 is hereby denied.
2. A revenue increase of $8,049,145 resulting in a cost of service of $94,397,520 is hereby approved for usage on and after July 1, 2013. Said revenue increase shall be recovered through a uniform percentage increase to rates.
3. The Narragansett Bay Commission's request to fund its Operating Reserve at 1.5% of operating expenses, excluding Debt Service related costs and Personnel Expense, is approved.
4. The Narragansett Bay Commission's request to eliminate the BOD/TSS surcharges is approved.
5. The Narragansett Bay Commission shall comply with all other findings and instructions in this Report and Order.

[33] The approved cost of service schedule is attached to this Report and Order as Appendix A.

EFFECTIVE AT WARWICK, RHODE ISLAND ON JULY 1, 2013, PURSUANT TO AN OPEN MEETING DECISION ON JUNE 13, 2013. WRITTEN ORDER ISSUED AUGUST 9, 2013.

PUBLIC UTILITIES COMMISSION

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Elia Germani, Chairman*

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Mary E. Bray, Commissioner

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Paul J. Roberti, Commissioner

*Chairman Germani participated in the decision but was not available for signature.

Appendix A

	Docket 4352* Test Year	*Adjustment*	Rate Year
REVENUES			
User Fee Revenues	$ 83,337,501	*$8,049,145*	$ 91,386,646
Other Service Revenue	1,476,784		1,476,784
Miscellaneous	1,534,090		1,534,090
Total Revenue	**$86,348,375**	***$8,049,145***	**$ 94,397,520**
EXPENSES			
Personnel Services	19,475,384	*1,691,252*	21,166,636
Operating Supplies & Expenses	14,147,858	*(12,868)*	14,134,990
Professional Services	2,715,533		2,715,533
Capital Outlay	-		
-			
Amortization	9,690		9,690
Debt Service	44,894,330		44,894,330
Debt Coverage	11,223,583		11,223,583
Total Expenses	**$92,466,378**		**$94,144,762**
OPERATING RESERVE	$ 168,505	*$84,253*	$ 252,758
COST OF SERVICE	**$92,634,883**		**$94,397,520**
RATE YEAR REVENUES AT PRESENT RATES	$86,348,375		$86,348,375
REVENUE INCREASE	$ 6,286,508		$ 8,049,145

* Docket 4352 Rate Year approved by PUC. Most current debt service approved and included in rates.