

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: PAWTUCKET WATER SUPPLY :
BOARD ABBREVIATED RATE FILING : DOCKET NO. 3593

REPORT AND ORDER

I. Introduction

On February 23, 2004, Pawtucket Water Supply Board (“PWSB”), a non-investor owned utility, filed with the Public Utilities Commission (“Commission”) an abbreviated rate application filing. PWSB requested a rate increase of 25% for the collection of \$3,414,969 in additional operating revenues for a total cost of service of \$17,348,757. PWSB requested an effective date of April 1, 2005. On May 3, 2004, the City of Central Falls filed a Motion to Intervene. No party objected to the Motion. Therefore, the Motion was granted pursuant to Commission Rule of Practice and Procedure (“Procedural Rule”) 1.13.

The instant general rate case filing represents PWSB’s fifth rate filing in the last six years. The following table provides a brief history:

Docket No.	Filing Date	Amount Requested	Amount Allowed
2674	1/9/98	\$3,634,020	\$ 614,430
3164	6/30/00	\$2,289,601	\$1,820,799
3378	8/20/01	\$3,828,966	\$2,732,584
3497	2/28/03	\$3,157,389	\$2,382,459
3578	2/23/04	\$3,414,969	

II. Motion for Exemption

On March 5, 2004, PWSB filed a Motion for Exemption from certain filing requirements. No party objected. At its open meeting on March 18, 2004, the Commission considered PWSB's requests and approved the request to the extent a waiver is necessary, finding that the filing requirements are essentially satisfied by the information provided in the instant filing and in Docket No. 3497. The following details the request and findings:

PWSB requested an exemption from Procedural Rule 2.6 (a) relating to the Test Year. Rather than using an actual historic test year, PWSB requested use of the rate year figures approved in Docket No. 3497, approved on October 3, 2004.¹ The Commission determined that the approved rate year is substantially accurate and should be allowed as the Test Year. Similarly, PWSB sought to use the cost of service schedules approved in Docket No. 3497 to comply with Procedural Rule 2.10 (d)(1) and the comparative statement of revenues and expenditures for the past three years provided in Docket No. 3497 to comply with Procedural Rule 2.10 (d)(3). The Commission approved these requests.

PWSB requested that the rate year begin on April 1, 2005 and requested a waiver from Procedural Rule 2.6 (b). While the rate year will begin more than a year from the filing date, it is still a twelve month period which shall commence no later than six months after the proposed effective date of the new tariffs. The proposed effective date is April 1, 2005, the same date the rate year is expected to commence. Such a request does not appear to violate any of the Procedural Rules or Rhode Island law. Therefore, a waiver is unnecessary.

¹ See Order No. 17574 (issued October 10, 2003).

PWSB requested a waiver from providing workpapers detailing the test year revenues by source, tariff, rate class, etc. As part of its instant filing, PWSB has provided a proof of revenues and bill impact analysis, thus providing essentially the same information as required under Procedural Rule 2.10 (d)(4). The Commission approved the request.

Finally, PWSB requested a waiver from Procedural Rule 2.10 (d)(8), which requires a summary on the status of compliance and reporting required by prior Commission Orders. At the time of filing, PWSB was current with its compliance and reporting requirements of an Order that had only been in effect for four months. Because of its compliance, a waiver is unnecessary.

III. PWSB's Direct Testimony

PWSB submitted the Pre-Filed Testimony of Maureen E. Gurghigian, Senior Vice President at First Southwest Company. She provides financial advisory services to issuers of municipal debt, primarily in the State of Rhode Island. Ms. Gurghigian indicated that PWSB needs to borrow approximately \$74 million to construct the new water treatment plant and complete other significant capital improvement programs.² She explained that in order to accomplish its goals, PWSB has undertaken, and will undertake several significant borrowings. She noted that as a result of Order No. 17574, PWSB was able to defease the Pawtucket Building Authority ("PBA") Bonds, the first step in its financing plan.³ In December 2003, PWSB borrowed approximately \$30 million from

² PWSB Exhibit 2 (Pre-Filed Testimony of Maureen Gurghigian), p. 2.

³ Id. The PWSB system and all of its assets were previously pledged to the PBA Bonds, the security provisions of which put all other revenue bonds in a subordinate position. Such a structure causes higher interest rates. In addition, the capacity of the PBA was limited to approximately \$60 million, with an annual issuance limit of \$20 million. With these restrictions, PWSB would not have been able to finance its capital program through the PBA. Therefore, this debt had to be defeased. Id. at 2-3. The Commission approved rates for the defeasance in Order No. 17349 (issued January 23, 2003).

the Rhode Island Clean Water Financing Agency (“RICWFA”) for this purpose (“December 2003 bonds”), successfully defeasing the PBA bonds.⁴

Ms. Gurghigian indicated that because PWSB was able to receive a favorable interest rate on the December 2003 bonds, the payments on these plus the existing City of Pawtucket general obligation bonds are approximately \$1.75 million per year. The annual debt allowance of \$2,221,045 allowed in Order No. 17574 minus the \$1.75 million payments provide for an annual increment for debt service of approximately \$470,000. According to Ms. Gurghigian, these funds, in conjunction with the PWSB’s IFR allowance, will allow PWSB to issue bonds of approximately \$43,450,000 (“2004 borrowing”). She noted that this is not sufficient to cover the entire treatment plant and the main cleaning/lining projects, but rather, is the maximum amount PWSB can currently borrow from RICWFA given the present debt service allowed through rates.⁵

Therefore, in order to take advantage of low interest rates, Ms. Gurghigian indicated that PWSB applied to the Division of Public Utilities and Carriers (“Division”) for approval of its 2004 borrowing, to be priced on or about March 4, 2004 in order to close by the end of the month and have funds available for PWSB in April 2004.⁶ She explained that the PWSB needed to dedicate its IFR allowance to debt service, but if granted the rate increase requested in this docket, will not need to use the funds for the debt service.⁷

The next borrowing, Ms. Gurghigian explained, will be in FY 2005, to provide an additional \$32 million to complete the new water treatment plant and finance additional

⁴ PWSB Exhibit 2, p. 3.

⁵ Id. at 3.

⁶ Id. at 4. The Division approved PWSB’s Application. See Division Order No. 17764 (issued February 27, 2004).

⁷ PWSB Exhibit 2, p. 4.

capital improvements (“2005 borrowing”). She maintained that in order to undertake the 2005 borrowing, it will be necessary to demonstrate to investors, prior to the issuance of those bonds, that the PWSB has approved rates sufficient to pay the annual principal and interest on the bonds. Therefore, the PWSB requires an order from the Commission authorizing an increase before the 2005 borrowing in order to assure investors that PWSB has the authority to increase its debt service when necessary and to free up the IFR allowance for IFR projects.⁸

With regard to the timing of the rate increase, Ms. Gurghigian explained that PWSB does not need to start collecting rates for the 2005 borrowing until April 2005, but requires an Order authorizing the collection of sufficient rates as soon as possible to satisfy RICWFA requirements and requirements of the Pawtucket Trust Indenture. One of the requirements of the Pawtucket Trust Indenture is that a consulting engineer provide a certificate demonstrating debt service coverage for the first three fiscal years following the issuance of the debt. In order for the projection to occur, rate increases must already be adopted by the City and approved by the Commission for the first full fiscal year following the issuance. Therefore, Ms. Gurghigian asserted, unless the rate increase is approved in FY 2004 or very early in FY 2005, PWSB will be unable to undertake the 2005 borrowing, thus increasing risks associated with delay.⁹

Discussing the projected schedule of debt and debt service, Ms. Gurghigian indicated that PWSB expects the total debt service to increase from approximately \$2 million annually to approximately \$7 million annual by FY 2008. She explained that the increases will be moderated through the use of capitalized interest in the first two years of

⁸ Id.

⁹ Id. at 5.

each of the loans and the fact that the PWSB has been able to dedicate IFR funds to debt service. As a result, PWSB has been able to fund more than 50% of the cost of the new water treatment plant at historically low rates in the 2004 borrowing.¹⁰

Turning to the mechanics of the financings, Ms. Gurghigian explained that the RICWA fund uses federal capitalization grants and state matching funds to provide subsidized (25% below market rate) loans to water suppliers for qualifying projects that are listed on the Project Priority List maintained by the Department of Health. The RICWFA sells bonds in the public market and loans the proceeds to its drinking water borrowers pursuant to loan agreements.¹¹

With regard to costs associated with the borrowings, Ms. Gurghigian explained that all out of pocket closing costs will be paid by PWSB. She indicated that, as permitted by federal guidelines, PWSB will use loan proceeds to fund transaction expenses. These costs will include an origination fee for each loan to RICWFA to pay a portion of the expenses related to the issuance of the Agency's bonds. The issuance costs will include Borrower Bond Counsel and Disclosure Counsel, Financial Advisory, Engineering Consulting, Accounting, Trustee and other related services. According to Ms. Gurghigian, the overall cost of issuance, exclusive of municipal bond insurance, is estimated at 2% of the total loan amount. The premium for municipal bond insurance, based on recent experience with Rhode Island municipal utilities, is expected to range from 1% to 1.5% of the par value. She noted that the insurance significantly reduces the interest cost and results in appreciable net savings.¹²

¹⁰ Id. at 5.

¹¹ Id. at 6.

¹² Id. at 6-7.

PWSB also submitted the Pre-Filed Testimony of Christopher P.N. Woodcock, a consultant. Mr. Woodcock reiterated each point made by Ms. Gurghigian with respect to the debt service requirement and the process and timing of financing.¹³ Mr. Woodcock indicated that PWSB is also seeking Commission approval to apply the restricted amounts for the O&M reserve and for the water treatment plant O&M to debt service once they are no longer needed. He noted that the O&M reserve was initially funded to be built up over three years to the amount required in the Trust Indenture. Thereafter, the O&M reserve deposits should be less than what was approved. Therefore, PWSB is requesting that once the initial funding is completed in FY 2006, the remainder plus the treatment plant account deposits be redirected or restricted to cover a debt service shortfall that is expected in FY 2007.¹⁴

Addressing the effect of using the IFR allowance for the 2004 bond issue on the plans to rehabilitate and replace distribution mains, Mr. Woodcock noted that there would be a delay, but indicated that interest rates have been so favorable that “it is essential to move forward as quickly as possible.”¹⁵

With regard to the timing of approval and of the effective date, Mr. Woodcock reiterated Ms. Gurghigian’s position that it is necessary to have revenues approved by the Commission that are sufficient to pay the annual debt service in order to undertake the 2005 bond issue. He indicated that it is estimated that payment on the 2005 bonds will begin in September 2006. Therefore, due to billing cycles, it takes close to eighteen months from the effective date to collect a full year’s worth of revenues from rates. Accordingly, with an effective date of April 2005, PWSB will have sufficient revenues

¹³ PWSB Exhibit 3 (Pre-Filed Testimony of Christopher Woodcock), pp. 2-7.

¹⁴ Id. at 5-6.

¹⁵ Id. at 6.

by September 2006 to make payments on the 2005 bonds. Furthermore, Mr. Woodcock explained that the Trust Indenture requires PWSB to make monthly deposits to the Debt Service Account so that there will be sufficient funds to make the semi-annual interest payments and the annual principal payments. In effect, he stated, PWSB must pre-pay the debt service and thus needs rates in place to make these “pre-payments.”¹⁶

According to Mr. Woodcock, if approved, the impact on a typical residential customer, a family of four using 100 HCF per year will be an increase in the annual bill of \$68.32, from \$273.42 to \$341.74.¹⁷

IV. Settlement

On May 18, 2004, in lieu of any additional pre-filed testimony, PWSB and the Division filed a Settlement Agreement (“Settlement”).¹⁸ The City of Central Falls did not join in the Settlement.

The Settlement provided for an adjustment of rates effective April 1, 2005 to obtain an additional \$3,414,969 of revenues, or 24.99% of test year revenues. The purpose of the additional revenues will be utilized to service approximately \$32,000,000 of anticipated debt (2005 bonds). The 2005 bonds will be issued to finance the completion of construction of the projects in PWSB’s Capital Improvement Program (“CIP”).

The Settlement retained all previously restricted accounts (Debt Service, O&M Reserve, IFR, and Water Treatment Plant O&M). The Settlement provided that PWSB be able to apply the restricted amounts designated for the O&M Reserve and for the Water Treatment Plant O&M to debt service once they are funded at required levels. The

¹⁶ Id. at 7.

¹⁷ Id. at Schedule 4.0.

¹⁸ A copy of the Settlement is attached hereto as Exhibit A.

Settlement noted that the requested levels of debts service plus available amounts designated to fund the O&M Reserve and Water Treatment Plant O&M could result in a surplus by the end of FY 2010. Accordingly, the parties agreed to reexamine the need to permit the PWSB to use the amount currently designated for the O&M Reserve and Water Treatment Plant O&M to meet its debt service requirements under the Trust Indenture when PWSB files its next base rate case. At that time, the parties agreed to take positions on whether the amounts designated to fund the O&M Reserve and Water Treatment Plant O&M requirements should be reduced or eliminated from the PWSB's revenue requirement.

Finally, the Settlement noted that in the event PWSB files another base rate case in which rates are approved for effect April 1, 2005 or prior, the rates approved in this case will not go into effect, but rather, will be superseded by any rates approved in the Commission subsequent to this filing, but prior to April 1, 2005.

V. Hearing

Following public notice, a hearing was conducted at the Commission's offices, 89 Jefferson Boulevard, Warwick, Rhode Island on June 22, 2004. The following parties entered appearances:

FOR PWSB:	Joseph A. Keough, Jr., Esq.
FOR DIVISION:	Leo Wold, Esq. Special Assistant Attorney General
FOR COMMISSION:	Cynthia Wilson, Esq. Senior Legal Counsel

In his opening statement, Mr. Keough noted that although the rates are proposed to take effect April 1, 2005, PWSB is seeking rate approval currently in order to

demonstrate to investors, before the issuance of the bonds, that PWSB has approved rates which are sufficient to pay annual principal and interest on the bonds.¹⁹

PWSB presented Maureen Gurghigian, Christopher Woodcock and Pamela Marchand, P.E., PWSB's Chief Engineer in support of its request and of the Settlement. The Division presented John Bell, a Rate Analyst V in support of the Settlement. Mr. Woodcock explained that it takes approximately fifteen to sixteen months to collect a full year's worth of revenue once a rate change is effective. Therefore, an effective date of April 1, 2005 will allow PWSB to collect sufficient funds to meet the due date on the first payment on the 2005 borrowing in September 2006.²⁰ He indicated that, assuming no other rate change is allowed before April 1, 2005, the result of the Settlement will be an across-the-board increase of 25% on all rate classes. A typical residential customer using 100 hcf per year will experience an increase of approximately \$68.00 or \$17.00 per quarter.²¹

Ms. Gurghigian and Ms. Marchand explained that although the funds in the IFR account were pledged to secure the 2004 borrowing, approval of the rates proposed in this case will obviate the need to actually expend those funds. Therefore, no IFR projects currently scheduled to occur over the next several years will be delayed as a result of the 2004 borrowing.²²

¹⁹ Tr. 6/22/04, p. 7.

²⁰ Id. at 11-12.

²¹ Id. at 13-14.

²² Id. at 15-17.

Mr. Bell testified that a rate increase of approximately 25% is necessary for PWSB to be able to undertake the 2005 borrowing. He believed PWSB's request and the resulting Settlement is in the best interest of PWSB's ratepayers.²³

VI. Open Meeting

On June 29, 2004, at an open meeting, the Commission approved the Settlement entered into between PWSB and the Division, finding it to be necessary for the continued construction of the new water treatment plant and in the best interest of PWSB's ratepayers.

Accordingly, it is

(17930) ORDERED:

1. Pawtucket Water Supply Board's Application for an Abbreviated Rate Increase, filed on February 23, 2004, is hereby denied and dismissed.
2. The Settlement entered into between the Pawtucket Water Supply Board and the Division of Public Utilities and Carriers, filed on June 18, 2004, is hereby approved effective on usage on and after April 1, 2005.
3. Pawtucket Water Supply Board is allowed an increase in revenues of \$3,414,969, for a total cost of service of \$17,348,757.
4. Pawtucket Water Supply Board shall comply with all other findings and instructions as contained in this Report and Order.

²³ Id. at 35-36.

EFFECTIVE AT WARWICK, RHODE ISLAND PURSUANT TO AN OPEN MEETING DECISION ON JUNE 29, 2004. WRITTEN ORDER ISSUED JULY 29, 2004.

PUBLIC UTILITIES COMMISSION

Elia Germani, Chairman

Kate F. Racine, Commissioner

Robert B. Holbrook, Commissioner