Service Date: June 17, 1988

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

* * * * *

IN THE MATTER of the Application of the TOWN OF CASCADE for Authority to Increase Rates and Charges for Water Service in its Cascade, Montana Service Area.	UTILITY DIVISION DOCKET NO. 87.9.48 ORDER NO. 5329a

APPEARANCES

FOR THE APPLICANT:

John Doubek, Attorney at Law, Small, Hatch, Doubek and Pyfer, Livery Square, Helena, Montana 59601.

FOR THE INTERVENORS:

Arthur Kountz, Utility Subscriber, 117 Front St., Cascade, Montana 59421.

Carl Cordeiro, Utility Subscriber, South Russell, Cascade, Montana 59421.

Tom Klock, Utility Subscriber, 211 3rd South, Cascade, Montana 59421.

Lucy Pettapiece, Utility Subscriber, South Russell, Cascade, Montana 59421.

FOR THE COMMISSION:

Robin McHugh, Staff Attorney, 2701 Prospect Avenue, Helena, Montana 59620.

Ron Woods, Rate Analyst, 2701 Prospect Avenue, Helena, Montana 59620.

BEFORE:

Clyde Jarvis, Commissioner and Chairman
Howard Ellis, Commissioner
Tom Monahan, Commissioner

BACKGROUND

1. On September 11, 1987, the Town of Cascade (Applicant or Town) filed an application with this Commission for authority to increase rates and charges for water service to its customers in its Cascade, Montana service area. The Applicant requested an average increase of approximately 188%, which constitutes an increase of approximately $85,720 in annual revenues.

2. On November 24, 1987, following issuance of proper notice, a hearing was held in the Wedsworth Hall, Cascade, Montana. For the convenience of the consuming public there was also a night session, held at the same location. The purpose of the public hearing was to consider the merits of the Applicant's proposed water rate adjustment.

3. On February 18, 1988, the Commission, having considered the evidence presented at the hearing, issued Order No. 5329. this Order granted the Applicant authorization to file increased rates recognizing operation and maintenance costs and costs associated with a proposed $725,000 revenue bond issue.

4. Following public protest of Order No. 5329, the MCC, a party to this Docket, moved that the Commission extend the deadline for reconsideration of its order from February 29, 1988, to March 11, 1988. The Motion was granted.

5. On March 7, 1988, the MCC filed a Motion requesting special party status be granted certain residents of Cascade disaffected by Order No. 5329. In addition, the MCC requested that the record in Docket No. 87.9.48 be reopened for certain limited purposes.

6. On March 17, 1988, at a scheduled work session, the Commission voted on its own Motion, pursuant to ARM Section 38.2.4805, to reopen the record for the limited purpose of allowing intervenors an opportunity to present a case in opposition to the original proposal of the Town of Cascade.

7. As part of the Procedural Order issued on March 23, 1988, the Commission included a stay of Order No. 5329. The order was stayed pending consideration of the record established pursuant to that Procedural Order, or until it was determined that no additional record would be established.

8. On May 26, 1988, following issuance of proper notice a hearing was held in the Wedsworth Hall, Cascade, Montana. For the convenience of the consuming public there was also a night session, held at the same location. The public hearing was for the purpose of receiving evidence and testimony from special intervenors in opposition to the original application. The MCC did not participate in this phase of the proceeding.

ANALYSIS AND FINDINGS OF FACT

9. At the public hearing the Applicant presented the testimony and exhibits of the following witnesses:

Raymond Young, Certified Public Accountant
Jim Cummings, Consulting Engineer

These witnesses provided rebuttal testimony to some of the assertions made by the special intervenors and testified relative to the financing of proposed capital improvements, debt service obligations, and rate structure.

10. The appointed spokesman for the intervenors, Arthur "Lucky" Kountz, presented the testimony and exhibits of the group. Mr.

Kountz provided testimony and exhibits that, in the opinion of the group, brought into question the validity and reasonableness of the Applicant's engineering analysis, proposed capital improvement program, and financing proposal.

11. During the course of the public hearing 36 public witnesses appeared and offered testimony. The public testimony received during this proceeding was divided between supporters and critics of the increase. In general those subscribers voicing dissatisfaction with the increase predicated their opposition to the Town's proposal on the Town Council's decision to eliminate the spring source of supply from the water utility's operating configuration. Generally those consumers supporting the Town's proposal cited an awareness of a need for capital improvements to the system and/or confidence in the wisdom of the Town Council to make informed decisions regarding the operation of the utility.

CAPITAL IMPROVEMENT PROGRAM

12. For purposes of this reopened docket the intervenors were charged with the responsibility of making a clear showing that the Town's proposed capital improvement program was ill conceived. The intervenors prefiled direct testimony in support of their position that the Town's proposed capital improvement program was

unnecessary, and titled this testimony "Report of the Intervenors."

In this report the intervenors provide the Commission with their "needs" analysis for the water system and their critique of certain aspects of the engineering report prepared by Thomas, Dean and Hoskins (TDH). The TDH report is the source document used by the Town to establish its capital improvement program for the water system. The intervenors, based upon their financial and engineering analysis, find that current operating deficiencies on the system can be corrected through prudent expenditure of net revenues, generated by currently effective rates. The intervenors also find that the capital improvement priorities established in the TDH report are improper.

13. The first intervenor assertion that the Commission will address is the allegation that the existing water rates will generate sufficient net operating revenues to allow the utility to rebuild the system. On page 7 of their testimony the Intervenors state the following:

> ...We the intervenors contend that the present distribution system can be repaired and upgraded with the revenue generated by the Water Utility at the present rate charged, provided the Town of Cascade spends the funds,

> for maintenance and replacement, instead of financial advisors, lawyers and engineers...

At the request of the PSC staff Ray Young prepared a schedule summarizing the costs of water system projects and the source of revenue for funding of that project. This schedule provided information for fiscal years 1985 through 1988 to date. The schedule indicates that during this period the the Town expended a total of $100,985 on various water system projects. The schedule further indicates that of this total expenditure $49,477 of the funding was provided by the water fund. In other words, the monies available in the water utility fell $51,508 short of covering the full cost of water utility obligations incurred during this time frame.

The Town, having to obtain $51,508, or more than half, of the funding for water utility projects from other revenue sources, specifically the General Fund and Revenue Sharing monies, in the Commission's view gives a clear indication that the present rates are not sufficient for the water utility to discharge all of its current obligations. The evidence in this Docket does not support the intervenor statement regarding the adequacy of current rates to generate sufficient net revenues to support water system operations.

14. The intervenors strongly object to the Town's proposal to eliminate the spring water source of supply from the utility's operating configuration. The intervenors assert that the spring source has been and will continue to be a reliable and quality source of supply. The intervenors, while not providing any substantive data, maintained that rehabilitation of the spring boxes could be accomplished for substantially less money than the $100,000 to $200,000 cost estimate provided by TDH.

15. The Commission does not believe that the Town's presentation represents that the spring source of supply is anything other than a reliable, quality source of water for the Town's utility. It has been the Commission's perception from the outset of this proceeding that the general consensus of all parties is that the spring source of supply is an attractive source because its operating costs are minimal, due to the fact that it is gravity flow, and provides a substantial amount of the Town's winter daily demand.

In this application the concern expressed by the Town regarding the spring source was economic in nature, not operational. The indications from both the consulting engineer and the Montana Department of Health were that substantial rehabilitation of this source will be required for it to meet the requirements of the Safe

Drinking Water Act, with significant costs being incurred by the Town to continue use of this supply source. Both of the Department of Health and TDH testified that in their opinion it was not economically feasible to rehabilitate this source of supply and they recommended elimination of this source from the operating configuration of the utility.

16. There was no substantive evidence such as, construction bids, engineering cost estimates, or unit price comparisons, presented by intervenors during this phase of the hearing that contradicted the assessment of the consulting engineer or the Department of Health that this source be eliminated. In the Commission's view it would be irresponsible for the Town to expend an estimated $100,000 rehabilitating the spring source, which produces 30-40 gallons per minute, when it has alternatives to develop a source with greater production capabilities at less cost. The alternative sources include development of a new well on the east or west side of the river, insulating the existing transmission main under the bridge so that utilization of the wells on the other side of the river can occur year round, or possibly increase the pumping capacity at one of its existing sources.

17. The next major item in dispute between the Town and the intervenors is the consulting engineer's calculation of total water

introduced into the distribution system and the percentage of lost and unaccounted for water calculated by the engineer. The Town of Cascade does not have measuring devices on its sources of water supply or on the majority of its end user connections; therefore, in order to ascertain total water delivered to the distribution system, and the amount consumed by subscribers, a calculation must be employed.

18. In his study the engineer states that his calculation of total water discharged to the distribution system was accomplished by monitoring the draw down of the water level in the storage facility and measuring the capacity of the spring flow. Simply stated this means that, by employing a mathematical volume calculation for each foot of water draw down in the storage facility and adding the inflow of water from the springs which feed the facility, the engineer calculated that total water introduced into the distribution system to be 136,700 gallons per day.

19. The intervenors did not directly attack the method employed by the engineer to calculate the water discharged to the water system, nor did they point out specific errors contained in the the calculation. Instead of attacking the engineer's method they proposed their own calculation of water production which they asserted was more accurate. In their calculation of water produced

the intervenors accepted that the spring source of supply produces 41,760 gallons per day. The intervenors then conducted field tests to determine the production capability of the spring well west of Town. The information gathered by the intervenors during their field test resulted in them calculating that the production capability of this well is 45,321 gallons per day. The intervenors state that the maximum amount of water that can be introduced into the system from these two sources on a daily basis is, 87,081 gallons which is substantially less than the 136,700 gallons calculated by the engineers.

20. The engineer and the intervenors both assert that their calculation of the water entering the distribution system is reasonably accurate. The two production calculations are subjective and require a certain degree of personal interpretation to develop the numbers presented. Irrespective of which calculation is the most accurate both support the fact that a substantial amount of lost and unaccounted for water is being experienced on the system.

Accepting the engineer's forecast that per capita winter daily consumption is approximately 65 gallons, winter domestic use for the Town of Cascade totals 52,000 gallons. Lost and unaccounted for water on the system totals 40.3% or 61.9%, depending on whether

the calculated production of the intervenors or the engineer, is used.

21. Typically with small utilities the Commission is presented with lost and unaccounted for percentages in the range of 20 to 25 percent. Clearly under either calculation just discussed the lost and unaccounted for amounts are substantially above that norm. This indicates to the Commission that there is a significant problem with lost and unaccounted for water on the distribution system of the Town. Whether that loss is being experienced on facilities that are the responsibility of the Town or on facilities that are the responsibility of the consumer, is unknown. In finding the Town's proposal to upgrade the distribution system reasonable, lost and unaccounted for water was not the Commission's only consideration. The Commission also considered the Town's testimony relative to inadequate fire flows, inadequate pressures, number of pipeline breaks not confined to a specific area, and inoperable valves.

22. The intervenors took issue with the Town's proposal to construct approximately $80,000 of water system improvements on property that the Town of Cascade has no formal agreement to assure continued use of, or even possible future purchase of, the private property that, the two east wells are located on. This subject was

addressed during this proceeding and the intervenors statement was found to be erroneous. The Town produced an easement entered into between the property owners and the Town granting the Town a utility easement on this property.

23. In their testimony the intervenors established that sections of the currently existing water service area will not receive substantial benefit from the proposed upgrade to water facilities. The intervenors argued that due to fire flow requirements these areas should be included in the area to receive proposed upgraded facilities. The Town admits that the sections of Town alluded to in the intervenor testimony will not receive substantial benefit and it further admits that upgrades in the area are warranted. But the Town maintains that the priorities established in the improvement program represent a management decision of placing monies where the majority of consumers will receive the most benefit.

The Commission agrees with the intervenors that the Town should endeavor to provide quality service to all consumers in its service area. But as long as the management decision represents a reasonable expenditure of funds the Commission cannot overrule that decision because the management of the utility is not vested with this Commission. The Commission would however, urge the Town to

examine its proposed capital improvement program and available funding, and if at all possible provide upgrades to the facilities in these areas.

24. The intervenor testimony in this Docket brings into question the prudence of one of the Applicant's proposed improvements. The intervenors in their field testing of the spring well indicated that the pump at that well was cycling on and off due to draw down of the well. One of the Town's proposals is to install a second pump on this source of supply to increase production. This proposal should be reviewed before any action is taken committing the Town to this improvement.

25. The Commission finds, based upon the testimony received during both hearings in this Docket, that the capital improvement program as proposed by the Town is reasonably prudent and therefore accepts the Town's assertion the improvements outlined in the filing need to be constructed.

DEBT SERVICE

26. The Commission in the prior Order in this Docket provided findings relative to the Town's proposed financing package and will not reiterate those findings in this Order. The Commission still finds the Applicant's proposed financing as outlined in that Order to be reasonable; however, the Applicant has submitted an

alternative financing proposal that needs to be addressed in this Order.

27. As provided in the Procedural Order the Applicant, at its option, submitted to the Commission an alternative financing proposal for the water system improvements. The Applicant has submitted a pre-application with the Farmers Home Administration (FHA) requesting that FHA provide funding for the Town's proposed capital improvement program. The Town proposes to issue revenue bonds in the amount of $785,000, to be purchased by the FHA. If the FHA accepts the Town's proposal the bonds would be repaid over a period of 40 years and carry an interest rate of 6.125%. If the FHA purchases the bonds it will require that the town accumulate over a 10 year period a bond reserve equal to the principal and interest payment on the bond and provide a debt service coverage of 110%.

28. Contingent upon FHA approval, the Commission finds the Applicant's proposal to issue $785,000 in revenue bonds with a maximum term of 40 years and a maximum interest rate of 6.125% to be acceptable. The Commission further finds the requirements that the Town establish a bond reserve and provide a debt service coverage of 110% to be appropriate.

29. If the Town completes the sale of the proposed revenue bonds to FHA it will incur a principal and interest payment on the outstanding bonds of approximately $52,658. It will also incur the obligation to have a net operating income of at least $5,266 to meet the requirement that it achieve a 110% coverage ratio. The required net income is calculated by multiplying the principal and interest payment on the outstanding bonds by 10% ($52,658 x .10 = $5265.80).

OPERATION AND MAINTENANCE EXPENSE

30. In a revised submission the Town indicated that it would incur test year operation and maintenance expenses totalling $36,000. In its original submission the Town has indicated and the Commission accepted total test year operation and maintenance of $35,000. The Applicant explained that the additional $1,000 in expense proposed in this phase of the hearing was to cover the cost of meter reading and billing. For reasons that will become apparent later in this Order the Commission finds the Applicant's request to increase operation and maintenance expenses by $1,000 should be denied. The Commission further finds test year operation and maintenance expenses to be $35,000.

31. The Commission finds the following test year operating revenue deductions to be reasonable if the FHA purchases the revenue bonds:

Operating Expense	$35,000
Debt Service	52,658
Debt Coverage Ratio	5,266
TOTAL	$92,924

The test year expense assumes full annualized costs for the proposed FHA revenue bond issue. The Commission chooses to calcu late expenses in this manner, as it is the most reasonable way of accounting for the effect of the proposed bond issue on the operating statement of the utility.

REVENUE NEED

32. The Town indicated that, under present rates annual revenue generation would be approximately $45,656. The Applicant also indicated that the water utility would generate approximately $3,798 in interest earnings, resulting in total revenues of $49,454. The test period operating revenues were not a contested issue in this case and are accepted by the Commission.

33. The Commission, based upon the Findings of Fact contained in this Order and the previous order, finds that the Applicant should be allowed to increase revenues by either $84,866 or $43,470. These requirements are calculated as follows:

	Original Proposal	FHA Proposal
Operating Revenue	$49,454	$49,454
Less:		
Operating Expense	$35,000	$35,000
Debt Service	$79,456	$52,658
Debt Service Coverage	$19,864	$ 5,266
Total Revenue Requirement	$134,320	$92,924
REVENUE DEFICIENCY	$84,866	$43,470

34. The Commission is providing authorization for two revenue increase levels because the Applicant is only in the pre-application stage of it financing request with FHA, and therefore has no assurance that the application filed with that agency will be approved. The Commission anticipates that the FHA application will ultimately be approved and that the Town will require only an increase of $43,470. In the event the FHA application is disapproved, the Town will need authorization to implement rates that are sufficient to cover the cost of the original financing proposal.

RATE DESIGN

35. The Commission in its previous order fully discussed its concerns regarding the Applicant's proposed flat rate structure for provision of water service. The Commission in that order also provided the Applicant with recommendations that would improve the

equity in its rate design. The Commission will not reiterate that discussion in this Order but incorporates that discussion by reference.

36. If the FHA agrees to purchase the Town's proposed revenue bond issue one of the bonding requirements will be that the Town's water system be fully metered. In anticipation of that requirement the Town in this phase of the proceeding provided the Commission with a proposed metered water rate structure. The consumption information provided the Commission for purposes of establishing the metered rates is an estimated figure, because, for the most part the Town presently provides water service on an unmetered basis.

37. While the Applicant's calculated consumption may be a reasonable estimate of the actual consumptions that will be experienced by the water utility, the Commission finds that the estimate should not be used for purposes of determining metered rates. Critical in the calculation of the applicable usage rate is actual water consumption information, because absent this actual information the reliability of the calculated rate is suspect and could result in an over-collection or under-collection of the revenue requirement to the detriment of the consumer or the utility respectively.

38. The Commission finds that, absent actual water consumption information, the Applicant's request to implement metered rates should be denied.

39. Since the Commission has denied the Applicant's proposed metered water rate structure it is incumbent upon the Commission to specify a rate structure that will allow the Applicant the opportunity to generate the revenue requirement recognized in this Order. The Commission finds that the Applicant should implement the flat water rate structure authorized in the previous order, including the recommendations to improve equity in the structure.

40. The intervenors in their testimony indicated that it was their opinion that the cost of proposed water utility improvements to enhance the fire protection at the school should be recovered from all residents of the school district and not be subsidized by the water utility subscribers. The Commission agrees with the intervenors on this point. The fire hydrant rental charge that is assessed the school should recover, over the life of the assets, the costs associate with the enhanced fire protection. Assessment of a cost based fire hydrant rental charge against the school will result in all residents of the school district contributing toward the cost, since the hydrant rental charge will be recovered through the tax authority.

41. Once the Applicant has one year's actual consumption data available, it can convene a hearing under the provisions of Title 69, Chapter 7, MCA, and implement a metered rate structure to comply with the requirements of the FHA. The Commission would encourage the Applicant to convene such a hearing because usage based rates create equity in billing, causing the user receiving the service to pay for the service received.

MISCELLANEOUS

42. During their presentation the intervenors presented numerous photographs showing the condition of existing utility facilities. These photographs, in the opinion of the Commission, demonstrate that historically there has been a failure on the part of the Town to provide for the necessary daily maintenance requirements of the water utility. The Town through this Order is being authorized to implement a substantial capital improvement program, at significant cost to the ratepayer. The least the ratepayer and the Commission can expect, on a prospective basis, is that the Town will fulfill its statutory obligation to maintain reasonably adequate water facilities. It is only rea sonable for the consumer and the Commission to expect utility management to provide for the necessary day-to-day system maintenance

requirements, to ensure quality service and longevity of the capital assets paid for by the consumer.

COMMENT

During the course of this proceeding there were numerous issues brought before this Commission that were and are not within this Commission's jurisdiction. There were numerous attempts on the record to involve this Commission in the local administrative and decision making process. Throughout the proceeding protestants directed allegations at the local government, such as failure to provide for open meetings, withholding of information, inability of consumers to comment on proposals, violation of local government statutes, conspiracy to contrive water system deficiencies, and others. The citizens have the option of seeking a remedy for these allegations through the judicial process or the election process. A rate case before the Commission is an administrative procedure; therefore, these allegations, while presenting a concern to the Commission, are beyond the scope of this Commission's authority. The Commission, on the record in this proceeding, declined to get involved or rule on the validity of the allegations, and it does so again in this Order.

CONCLUSIONS OF LAW

1. The Applicant, the Town of Cascade, is a public utility as defined in Section 69-3-101, MCA. The Montana Public Service Commission properly exercises jurisdiction over the Applicant's rates. Title 69, Chapter 7, MCA.

2. The Commission has provided adequate public notice and an opportunity to be heard as required by Section 69-3-303, MCA, and Title 2, Chapter 4, MCA.

3. The rates and rate structure approved in this Order are just and reasonable. Sections 69-3-201, and 69-3-330, MCA.

ORDER

NOW, THEREFORE, IT IS ORDERED THAT:

1. The Town of Cascade shall file rate schedules, consistent with the Findings of Fact herein, for its Cascade, Montana service area.

2. The Town of Cascade is authorized to issue revenue bonds in the amount of $785,000 with the requirements as outlined in Finding Fact No. 28.

3. If the Town of Cascade is unsuccessful in its attempt to obtain financing from the Farmers Home Administration the provisions of Order No. 5329, regarding the issuance of revenue bonds shall be authorized.

4. The Town of Cascade is authorized to file increased rates recognizing operation and maintenance costs and costs associated with the proposed revenue bonds. The rates shall become effective upon Commission approval subsequent to the issuance of the revenue bonds.

5. The rates approved herein shall not become effective until the tariffs, revenue bond ordinance(s), and necessary calculations relating to debt costs have been submitted for review by the Commission.

DONE IN OPEN SESSION at Helena, Montana, this 16th day of June, 1988, by a 3 - 0 vote.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

_____
CLYDE JARVIS, Chairman

_____
HOWARD L. ELLIS, Commissioner

_____
TOM MONAHAN, Commissioner

ATTEST:

Ann Purcell
Acting Secretary

(SEAL)

NOTE: Any interested party may request that the Commission reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.