DECISION MEMORANDUM

TO:COMMISSIONER NELSON

COMMISSIONER SMITH

COMMISSIONER HANSEN

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WORKING FILE

FROM:SCOTT WOODBURY

DATE:SEPTEMBER 26, 1996

RE:CASE NO.  CAP-W-96-2

APPLICATION FOR TEMPORARY RATE INCREASE

On September 11, 1996, Capitol Water Corporation (Capitol Water; Company) filed an Application with the Idaho Public Utilities Commission (Commission) requesting authority to implement a temporary five-year 35% rate increase (approximately $100,000/year) to fund certain expenses and investments associated with improving the quality of water provided by Capitol Water to its customers.  The Company is experiencing the presence of secondary contaminants of iron and manganese in waters from several of its source wells.

Customer complaints regarding water quality have been received by the Company, the Commission (reference Case No. CAP-W-96-1: In the matter of the investigation of Capitol Water Company and its ability to provide adequate service and water quality) and the Idaho Division of Environmental Quality (DEQ).  The complaints describe water quality as “rusty or staining” water.  The Company states that the problem is localized depending on the season and the location of the individual customers on the Company’s system.  As represented by the Company, DEQ does not consider iron and manganese contamination to be a health hazard.  DEQ, the Company states, “has concluded that the current levels of iron and manganese in Capitol Water’s water supply does not constitute a health risk and does not constitute a basis for additional water treatment or the use of a different source of supply.”

Capitol Water serves approximately 2,228 residential customers and 147 commercial customers in an area of approximately four square miles in the near southwest part of Boise.  It is bounded roughly by Northview Street on the south, Ustick Road on the north, North Maple Grove on the west, and Curtis Road on the east.  The system has six wells.  There are no storage reservoirs.

Recognizing that high levels of iron and manganese are objectionable to some of its customers, Capitol Water has retained a consultant who has identified several remedies that the Company now desires to implement in its service area:

1.Phosphate Injection.  One method of mitigating the effect of iron naturally occurring in water, is to add conditioning chemicals that “sequester” the iron and manganese.  Capitol Water has already begun to add the sequestering chemicals  (phosphate) to Well Nos.  4 and 6.  Capital Water’s consultant recommends that eventually phosphate be injected into five of the Company’s six wells.

2.Rebuild Well No. 2.  Rebuilding Well No. 2 to a greater depth and installing a new casing would increase Well No. 2's capacity from the current 250 gallons per minute to 800 gallons per minute and would allow the Company to produce more water.  Having the ability to operate Well No. 2 would reduce the need to operate Well No. 6 thereby reducing the amount of lower quality water in the system.  Well No. 6 is the source of the highest levels of iron and manganese of all the wells on the Company’s system.  The Company’s consultants indicate this procedure could be effective in improving overall system water quality.  Rebuilding Well No. 2 would allow the Company to improve water quality and pressure and assure that Well No. 6 would only be required to provide adequate flows for fire protection and at times of summer irrigation system peak demand.  It is critical, the Company contends, that a rebuilt Well No. 2 be available in time for the 1997 irrigation season.

3.Drill a New Well at the Site of the Current Well No. 6.  In the Company’s judgment it is probably most cost-effective to drill another well at the existing Well No. 6 site rather than trying to redrill the existing Well No. 6.  Capitol Water’s consultant has advised the Company that drilling a new Well No. 6 to a better quality aquifer (600 to 800 feet) is likely to reduce the Company’s water quality problems.  The Company and its consultant recommend that Well No. 6 be redrilled in time to be available for the 1997 irrigation season.

The estimated costs of undertaking the above described water quality improvements are as follows:

1.Phosphate Injection.  The Company anticipates that any long-term program of phosphate injection will require an expenditure for chemicals of approximately $3,500 per month for seven months out of the year (on peak) and approximately $1,500 per month for five months (off peak).  This will cause an annual additional revenue requirement in the amount of $32,000 per year.

In addition to the required chemicals, the Company contends that the purchase of additional equipment to permit the efficient injection of phosphate is also necessary.  Acquisition of the injection equipment including the required liquid measurement instrumentations would require that the Company make a capital investment of approximately $10,550.

2.Rebuilding Well No. 2—$70,000.

3.Drilling new well at site of current Well No. 6—$170,000.

The Company therefore estimates that to obtain a long-term supply of higher quality water for the Capitol water system, it will be necessary for Capitol Water to make a capital investment of approximately $250,550.  Capitol Water contends that it does not have retained earnings sufficient to fund these capital improvements.  Capitol Water further contends that as a small water company its ability to borrow such an amount of money is very limited.  The amortization term of bank loans to small water companies, the Company states, is usually five to seven years.  Under traditional ratemaking practices, Capitol Water states that it would place the plant investment in rate base and recover the costs (plus a return) over a 20- to 30-year period.  This mismatch between the loan amortization term and the term for recovery of costs by way of depreciation would create a cash flow shortfall for Capitol Water so significant that Capitol Water contends it simply could not enter into such loan obligations at this time.

To obtain long-term water quality improvement, Capitol Water is proposing that the Commission approve an immediate temporary revenue increase of approximately $100,000 per year for five years.  The temporary rate increase is intended to allow the Company to recover the additional expenses of the phosphate injection chemicals and the loan amortization payments for the capital investment in well improvement.  Capitol Water also requests that the Commission allow the Company to place the costs incurred for phosphate chemicals incurred prior to the issuance of the Commission’s Order into a deferral account and allow the Company to amortize the deferred amount out of the proceeds of the proposed temporary rate increase.

Capital Water proposes that the proposed revenue increase be funded by means of a $3.01 per month charge added to the base monthly rate for customers under rate Schedule No. 1.  Schedule No. 1 is applicable to all non-metered customers for domestic use and lawn sprinkling.  The Company also requests a similar 35% increase in the rates for metered commercial customers taking service under the Company’s rate Schedule No. 2.  The Company proposes that the temporary rate increase remain in effect for five years or the length of the term of the loans undertaken to fund the capital investments, whichever is longer.  The Company also proposes that the proceeds of the temporary rate increase be segregated from the Company’s existing rates and charges previously approved by the Commission and dedicated to the payment of expenses and loan amortization costs directly related to the above described water quality improvements.  Having a dedicated account for loan amortization payments, the Company suggests, may act as an incentive to lenders to offer better loan terms.

Because Capitol Water is a small company, the Company contends that the cost of preparing and processing this Application will represent a significant extraordinary expense.  The Company estimates that the legal and accounting costs associated with this Application will be approximately $5,000.  Capitol Water requests that it be allowed to recover its actual expenses for processing this rate case out of the proceeds of the temporary rate increase.

Capitol Water represents that it is in the public interest that the Commission allow the Company to increase its revenues so as to permit the Company to address in a responsible fashion the need to improve water quality in its service area.  The Company requests that the requested temporary rate increase be allowed to go into effect as filed for water service rendered on and after November 1, 1996.

Commission Decision

The Company has requested a November 1, 1996, effective date.  Staff recommends that a Notice of Application, Intervention Deadline, Scheduling and Hearing be issued and that the proposed effective date be suspended.  How does the Commission wish to process this Application?  Should the proposed effective date be suspended?

Scott Woodbury

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