

**STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION**

DW 17-118

HAMPSTEAD AREA WATER COMPANY, INC.

Petition for Change in Rates

Order Approving Return on Equity and Change in Rates

ORDER NO. 26,195

November 28, 2018

APPEARANCES: Robert C. Levine, Esq., on behalf of Hampstead Area Water Company, Inc.; the Office of the Consumer Advocate by D. Maurice Kreis, Esq., on behalf of residential rate payers; and Christopher R. Tuomala, Esq., and F. Anne Ross, Esq., on behalf of Commission Staff.

In this order, the Commission approves a return on equity of 9.95 percent for Hampstead Area Water Company, Inc. As a result, effective January 1, 2019, an average residential customer will experience a bill increase of approximately \$0.93 per month, or \$11.16 annually.

I. PROCEDURAL HISTORY

Hampstead Area Water Company, Inc. (HAWC or the Company), is a New Hampshire public utility serving approximately 3,700 customers in Hampstead, Atkinson, and other communities in Rockingham County.

On July 31, 2018, the Commission approved a Settlement Agreement on Permanent Rates in this proceeding. *Hampstead Area Water Company, Inc.*, Order No. 26,165. The Settlement Agreement on Permanent Rates provided for a rate increase and a step adjustment. Both the rate increase and the step adjustment were based on a revenue requirement derived, in part, using a 9.60 percent return on equity (ROE) as a placeholder. The Settlement Agreement on Permanent Rates provided that the revenue requirement, permanent rates, and first step

adjustment would be recalculated after a separate proceeding on ROE, and that HAWC's customer rates reflecting the new ROE would be implemented through a second step adjustment, effective January 1, 2019, on a service-rendered basis.

On September 19, 2018, Commission Staff (Staff) filed the testimony of its ROE expert, Dr. J. Randall Woolridge, followed by a Staff recommendation on October 8, 2018. On November 6, 2018, Staff filed a Settlement Agreement on the Return on Equity (ROE Settlement) and the resulting rates to be implemented with the second step adjustment. The ROE Settlement was agreed to by Staff, HAWC, and the Office of the Consumer Advocate (OCA). A hearing on the ROE Settlement was held on November 7, 2018.

HAWC's petition as well as other docket filings, other than any information for which confidential treatment has been requested of or granted by the Commission, are posted on the Commission's website at <http://www.puc.nh.gov/Regulatory/Docketbk/2017/17-118.html>.

II. SUMMARY OF THE ROE SETTLEMENT

The ROE Settlement provides for a 9.95 percent ROE for HAWC, which will replace the previous 9.60 percent ROE contained in the Settlement Agreement on Permanent Rates. The change in the Company's ROE requires recalculation of the permanent rate increase and first step adjustment.

A. ROE

The agreed upon 9.95 percent ROE is based on information contained in two surveys published by Regulatory Research Associates (RRA): the average of authorized ROEs for water utilities during the first six months of 2018; and the median of authorized ROEs for gas utilities during the first six months of 2018. The ROE Settlement averages those two amounts to derive a base ROE percentage and then adds an additional 50 basis points to recognize rate case expense

savings arising from the Company's agreement to settle rather than to litigate the ROE. The calculation of the stipulated ROE percentage is as follows:

Average (Mean) Authorized ROE – Water Utilities: 1 st Half, 2018 ¹	9.41%
Median Authorized ROE – Gas Utilities: 1 st Half, 2018 ²	<u>9.50%</u>
Average (rounded down)	9.45%
Add: ROE Litigation Replacement Premium	<u>0.50%</u>
Stipulated ROE	<u>9.95%</u>

B. Capital Structure

For purposes of calculating the second step adjustment, the ROE Settlement provides for a pro forma capital structure for HAWC of 55 percent debt and 45 percent equity. The calculation of the Rate of Return (ROR) used in the recalculation of HAWC's Permanent Rate increase is as follows:

	<u>Component Percentage</u>	<u>Cost Rate</u>	<u>Weighted Cost</u>
Common Equity	45.00%	9.95%	4.48%
Long-Term Debt	<u>55.00%</u>	3.45%	<u>1.90%</u>
Total	<u>100.00%</u>		<u>6.37%</u>

The calculation of the ROR used in the recalculation of HAWC's First Step Adjustment³ is as follows:

	<u>Component Percentage</u>	<u>Cost Rate</u>	<u>Weighted Cost</u>
Common Equity	45.00%	9.95%	4.48%
Long-Term Debt	<u>55.00%</u>	3.41%	<u>1.87%</u>
Total	<u>100.00%</u>		<u>6.35%</u>

¹ RRA Water Advisory: Major Rate Case Decisions, January-June 2018, at 4 (July 27, 2018). The mean authorized ROE for water utilities was used because a median authorized ROE percentage was not provided.

² RRA Regulatory Focus: Major Rate Case Decisions – January-June 2018, at 6 (July 17, 2018).

³ The difference in the ROR calculations between permanent rates and the first step adjustment is due to the addition of \$50,000 of debt at an interest rate of 0.00% relative to HAWC's acquisition of the Wells Village water system that was included in the first step adjustment.

C. Recalculated Revenue Requirement and Rate Increase

The ROE Settlement provides a second step adjustment effective January 1, 2019, resulting in an increase in annual revenue of \$40,851. The proposed second step adjustment for HAWC is based on the recalculation of the Company's revenue requirement, from \$1,965,342 per Order No. 26,165, to the new revenue requirement of \$2,006,193.⁴ The difference in the revenues earned with the prior 9.60 percent ROE and the revenues that would have been earned using the 9.95 percent ROE and the pro forma capital structure will not be recouped by HAWC.

D. Customer Rate Impact

The recalculated revenue requirement results in a new consumption rate of \$6.11 per 100 cubic feet (ccf) of water, a \$0.16, or 2.69 percent, increase over the present volumetric rate of \$5.95 per month. There is no change to HAWC's current fixed meter charges. For a residential customer using approximately 69.60 ccf of water per year, the average annual bill will increase from \$534.12 to \$545.28, or \$11.16, an additional \$0.93 per month.

E. Rate Case Expenses

The ROE Settlement allows HAWC to recover its prudently incurred expenses for this proceeding through a surcharge. HAWC will be required to file its final expenses no later than 30 days from the date of this order.

F. Commission Investigative Proceeding on ROE Rulemaking

The ROE Settlement provides for a docket to be opened by the Commission within 45 days from the date of this order to investigate rulemaking for establishing an ROE methodology for all "small-sized" water utilities similar to HAWC.

⁴ Order No. 26,165 approved a permanent rate revenue increase of \$217,755 and a first step adjustment resulting in additional revenues of \$26,420. When added to pro forma test year revenues of \$1,721,167, the resulting revenue requirement is \$1,965,342 (\$1,721,167 + \$217,755 + \$26,420).

III. POSITIONS ON THE SETTLEMENT AGREEMENT

A. HAWC

HAWC requested that the Commission approve the ROE Settlement, and expressed its endorsement of the ROE contained therein. Hearing Transcript of November 7, 2018, at 47-48, 75.

B. Staff

Staff recommended that the ROE Settlement be approved, as it results in just and reasonable rates. *Id.* at 15, 74. Staff further stated that it expected the rate increase, along with future equity infusions by HAWC's shareholder, to result in a more balanced capital structure. *Id.* at 23.

C. OCA

The OCA recommended that the ROE Settlement be approved. *Id.* at 74. The Assistant Consumer Advocate, Dr. Pradip Chattopadhyay, testified that the ROE falls within the range of reasonableness and that it results in just and reasonable rates. *Id.* at 26, 32.

IV. COMMISSION ANALYSIS

Unless precluded by law, informal disposition by stipulation may be made of any contested case at any time prior to the entry of a final decision or order. RSA 541-A:31, V(a). Pursuant to N.H. Code Admin. Rules Puc 203.20(b), the Commission shall approve the disposition of any contested case by stipulation "if it determines that the result is just and reasonable and serves the public interest." The Commission encourages parties to settle disagreements through negotiation and compromise because it is an opportunity for creative problem solving, allows parties to reach a result in line with their expectations, and is often a better alternative to litigation. *Pennichuck East Utility, Inc.*, Order No. 26,179 at 13 (October 4,

2018). Nonetheless, the Commission cannot approve a settlement, even when all parties agree, without independently determining that the result comports with applicable standards. *Id.* at 13-14.

RSA 378:28 provides the standards by which the Commission sets permanent rates. The overarching requirement is that a utility's rates be just and reasonable. As part of the rate-setting process, the statute requires the Commission to approve "a just and reasonable rate of return" on a utility's prudent investments in plant and equipment that are used and useful in the provision of its service. *Id.*

In determining whether rates are just and reasonable, the Commission must balance the customers' interest in paying no higher rates than are required against the investors' interest in obtaining a reasonable return on their investment. *Appeal of Eastman Sewer Company, Inc.*, 138 N.H. 221, 225 (1994). In this way, the Commission fulfills its duties as an arbiter between the interests of customers and those of a utility's owners. RSA 363:17-a. The Commission exercises its discretion and judgment in striking this balance. *Appeal of Conservation Law Foundation of New England, Inc.*, 127 N.H. 606, 634-36 (1986).

The proposed ROE and adjusted capital structure is the product of compromise among HAWC, Staff, and the OCA regarding a number of technical issues. The ROE Settlement strikes a balance between the interests of shareholders and ratepayers, and settles all issues among the parties. Noting Dr. Chattopadhyay's testimony, we find that the ROE of 9.95 percent falls within the range of reasonableness for the Company's earnings. *See id.* at 635 ("the commission is bound to set a rate of return that falls within a zone of reasonableness, neither so low as to result in a confiscation of company property, nor so high as to result in extortionate charges to customers").

Further, we find the stipulated pro forma capital structure of 55 percent debt and 45 percent equity represents a reasonable capital structure for HAWC. A balanced capital structure proves more stable and beneficial to both owner and ratepayer. We expect all utilities to strive for that capital balance. We expect that the increase in rates will enable HAWC to increase its equity investment, and move it closer to an actual 55 percent debt and 45 percent equity structure, before its next rate case filing. With that understanding, the Commission finds the proposed ROE and resulting revenue requirement and rates to be just and reasonable and approves them.

We also approve the request to open a docket to investigate rulemaking for establishing an ROE methodology for all “small-sized” water utilities similar to HAWC within 45 days of this order. We note, however, that this is specifically an investigation into rulemaking, not the beginning of the rulemaking process under RSA ch. 541-A.

Based upon the foregoing, it is hereby

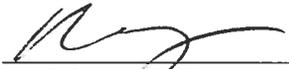
ORDERED, that the ROE Settlement is APPROVED, and HAWC shall commence collection of the resulting rates on a service rendered basis on January 1, 2019, subject to the terms of the ROE Settlement; and it is

FURTHER ORDERED, that HAWC shall submit properly annotated tariff pages consistent with the ROE Settlement with the Commission within 15 days of the date of this order; and it is

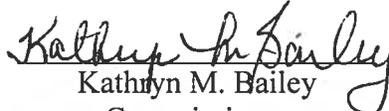
FURTHER ORDERED, that HAWC shall file its final rate case expense request pursuant to N.H. Code Admin. Rules Puc 1905.02, and the terms of the ROE Settlement, no later than 30 days from the date of this order; and it is

FURTHER ORDERED, that a Commission docket be opened to investigate rulemaking for establishing an ROE methodology for all “small-sized” water utilities, similar to HAWC, no later than 45 days from the date of this order.

By order of the Public Utilities Commission of New Hampshire this twenty-eighth day of November, 2018.



Martin P. Honigberg
Chairman

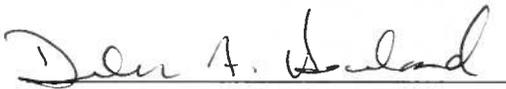


Kathryn M. Bailey
Commissioner



Michael S. Giaimo
Commissioner

Attested by:



Debra A. Howland
Executive Director