

To: Montana Energy and Telecommunications Interim Committee

From: Leroy Beeby, Independent Consultant for Water, Wastewater Utilities
1620 Townsend Ave, Helena MT 59601
Phone 406-431-9411; email – lebeeby@yahoo.com

Re: Small water and wastewater utility regulation by the Montana Public Service Commission

Date: September 25, 2017

I. Purpose

The purpose of this memorandum is to offer background information to the 2017 Energy and Telecommunications Interim Committee (“ETIC”) about the rate regulation of privately owned water and wastewater facilities in Montana by the Montana Public Service Commission (“PSC”) and my specific suggestions. The perspective offered is not reflective of the position or opinions of the Montana Consumer Counsel (“MCC”), the PSC nor of private industry. My perspective comes from 20 years in the industry, both on the regulated side and in the private sector.

II. Background

The PSC realized a number of years ago that the regulatory burden of its rules was simply too expensive for a small utility to endure and for many years ignored the problem of many non-complying companies and did not implement compliance efforts. Knowing that, the late Commissioner Bill Gallagher, Kate Whitney (the regulatory administrative supervisor) Chief Counsel Justin Kraske, and myself (I was the rate analyst for small water companies) designed the what is generally referred to as the “Small Water Rules”. Taking input from both the MCC and industry, the small water rules were established, standard rates were developed, and on paper it looked like a good solution to a problem that the Commission in the past had ignored.

The standard rates were developed and took into consideration a number of what can be termed as avoided costs. Those cost included but were not limited to attorney fees and consulting fees. For a small utility, those two costs alone can easily exceed \$25,000 to \$30,000. The intention of the standard rates was to allow a company to go through a checklist, file for standard rates, implement the standard rates and if requested by the PSC or by its own decision, phase them in over time to minimize rate shock to the customers. Given that, there was no anticipation in the standard rates for attorney and consultant fees. It’s interesting to note that the standard rates developed independently by the PSC are very close to the rates shown in the 2016 Department of

Natural Resources rate survey of water and wastewater companies with less than 500 customers.

The MCC apparently does not like the “one size fits all” rates for small water and wastewater utilities. It has made a point of exercising its constitutional right to intervene in the dockets that attempt to establish standard rates. The MCC has the constitutional right to intervene in municipal rate cases, but are limited to comments. The PSC, instead of just allowing the MCC to comment, through its action, has for all practical purposes initiated a contested case proceeding. It was not the intent of the small water rules to engage in that type proceeding. The PSC, by allowing discovery from both the MCC and PSC to the company, forces the company to retain an attorney to respond to the discovery and often times necessitates hiring a consultant to protect the company’s interest. The MCC engages at a minimum, both a staff attorney and a staff rate analyst in the development of its discovery requests and testimony. These highly trained MCC experts are provided at no cost to the customers as those costs are paid through the MCC fee and are not passed on to the customers. However, the costs that the MCC and PSC are forcing the company to incur are passed on in a contested case proceeding. A company walks a fine line between recovering its costs and keeping rates affordable to customers. Regardless of who actually causes the expenses, the company is blamed for it.

The PSC, in its comments, is referring to a specific investor-owned small utility and is challenging the company to file a standard rate case in order to recover its legally incurred costs. The PSC is implying that the costs caused by the PSC’s action are not recoverable in rates. It argues its point by stating that those costs were not specifically authorized in the simplified regulatory treatment rules. They fail to mention that those costs are not specifically disallowed either. It is a long established regulatory principle that cost recovery of expenses incurred in the establishment of rates is allowed. As stated earlier, those costs were perpetrated by the PSC and MCC in the first place. The end game of this approach will be that the company not only will be allowed its operating expenses, it will also recover all legal and consulting expenses incurred to establish rates. Those expenses will far exceed the standard rates that were originally requested by the company, accomplishing exactly the opposite of what the simplified small water rules were designed to do. The PSC and MCC through their actions have forced this specific company to seek legal recourse. I apologize for commenting on an ongoing legal case that really is outside the scope of ETIC, but feel ETIC should be aware that the issue is not as cut and dried as the PSC would lead you to believe.

Small utilities do not have large numbers or windfall profits. Most of these companies have less than 100 customers and have little, if any, opportunity to grow. The standard rate is \$50 a month. A 100 customer company grosses at best \$60,000. Purchase price on those systems is around \$1,000 a customer or about \$100,000. Costs of

running these sizes of systems are close to \$40,000 a year. Payments on \$100,000 system is a bit more than \$13,000 a year. That leaves the “opportunity” for profit at around \$7,000 or about 7% **before tax**. \$7,000 has to cover any unforeseen expenses and is less than a cost of a well pump.

III. In Summary

The PSC has for years ignored and continues to ignore small water and wastewater utilities. The only time it becomes involved in those utilities is when there is a customer complaint or a company tries to comply. Even companies the PSC are specifically aware of are not forced to comply. It is only when a company actually tries to comply, or there is a significant customer complaint does the onus of the full regulatory burden land with both feet. Given the present hostile regulatory climate, I cannot, with any conscience, suggest to a company that they should be in compliance, even though they are legally obligated to. The small water rules should be allowed to work as intended and not be the convoluted process that the MCC apparently desires and the PSC has encouraged. Neither the company, nor its customers can afford the additional regulatory burden being foisted on them by the PSC and MCC.

IV. Recommendation

I absolutely believe these small water and wastewater utilities need to be rate regulated, but they should not be forced to endure the same regulatory burden of a NorthWestern Energy or a Montana-Dakota Utilites. The rates could be capped and tied to an outside source such as the Department of Natural Resources rate survey. This survey is unfortunately not done on a consistent manner, so it may be more practical to take the latest survey (2016) and use that as a base rate and adjust with an inflationary factor each biennium. The other option would be to have PSC either do the survey themselves, or use a less desirable option of establishing standard rates through a hearing process where both the customers, and the companies are allowed input.

If the standard rates are tied to an external source, or were even allowed to work as designed and intended, there is no need for additional staff at the PSC. It would be easy for these small companies to become regulated and the compliance efforts would be well within the present workload of the PSC.