

**BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND)	
TRANSPORTATION COMMISSION,)	DOCKET NO. UW-030410
)	
Complainant,)	ORDER NO. 03
)	
v.)	
)	ORDER APPROVING AND
TIMBERLINE VILLAGE WATER)	ADOPTING SETTLEMENT
COMPANY, INC.,)	AGREEMENT; CANCELING
)	PROCEDURAL SCHEDULE
Respondent.)	
.....)	

1 **Synopsis.** *The Commission approves and adopts the Settlement Agreement as a reasonable resolution of the issues in the Timberline Village rate case, and finds that the rates proposed in the Settlement Agreement are fair, just and reasonable. The Commission cancels the procedural schedule for the proceeding set forth in Order No. 02.*

I. INTRODUCTION

2 **Proceeding:** This proceeding involves a request by Timberline Village Water Company, Inc. (Timberline Village or the Company) to increase its monthly rates, and other rates and charges, to establish a mandatory ready-to-serve charge for all properties not currently served by the water system, and to establish a facilities charge that applies to vacant lots in the company’s service area that may request water service in the future.

3 **Procedural History:** On March 26, 2003, Timberline Village filed with the Commission a request to revise its currently effective tariff. The Commission suspended the Company’s filing during its April 30, 2003 open meeting, and entered Order No. 01, Complaint and Order Suspending Tariff Revisions.

- 4 The Commission convened a prehearing conference in this docket in Olympia, Washington on August 8, 2003, before Administrative Law Judge (ALJ) Ann E. Rendahl. The Timberline Community Association (Association) filed a Petition to Intervene in the proceeding. The Association's petition was granted during the conference.
- 5 During the prehearing conference, Timberline Village and Commission Staff announced that they were close to filing a settlement agreement with the Commission. The parties agreed to a procedural schedule for the proceeding, however, in the event that the parties did not reach a settlement, or the Commission did not accept the settlement the parties intended to file.
- 6 On the afternoon of August 8, 2003, Timberline Village and Commission Staff filed a Settlement Agreement with the Commission, requesting that the Commission schedule a settlement hearing to allow the rates to become effective by September 1, 2003.
- 7 On August 11, 2003, ALJ Rendahl entered a Prehearing Conference Order, Order No. 02, establishing the procedural schedule for the proceeding.
- 8 Pursuant to notice issued on August 8, 2003, the Commission convened a settlement hearing before ALJ Rendahl, in Olympia, Washington, to explore the terms and conditions of the proposed settlement agreement, to consider whether the proposal is consistent with the public interest, and to determine whether the rates proposed in the settlement are fair, just and reasonable.
- 9 James A. Ward, Regulatory Analyst for the Commission, testified on behalf of Commission Staff. Stephen L. Harrington, President of Timberline Village, testified on behalf of the Company. The Association did not present a witness, stating that the Board of Directors of the Association had voted against

contesting the Settlement Agreement. The parties waived the entry of an initial order by the ALJ, and requested that the Commission enter a final order.

10 In the evening of August 20, 2003, the Commission convened a public hearing on the proposed settlement agreement in Olympia, Washington, before ALJ Rendahl. As the Association's Board had voted against contesting the Settlement Agreement, no members of the association or other members of the public appeared to give testimony.

11 **Appearances.** Stephen L. Harrington, President, Tumwater, WA, represents Timberline Village. Mary M. Tennyson, Senior Assistant Attorney General, Olympia, represents Commission Staff. Glenna Malanca, Gig Harbor, WA, and William H. Griffies, Tacoma, WA, represent the intervenor, Timberline Community Association.

II. MEMORANDUM

12 **Timberline's Original Tariff Filing.** On March 26, 2003, Timberline Village filed with the Commission a request to revise its currently effective tariff. Timberline Village serves approximately 213 customers east of Packwood, in Lewis County. The Company proposed a 119 percent increase in rates, through an increase in the monthly flat rate, as well as the establishment of monthly metered rates, other ancillary rates and charges, a mandatory ready-to-serve charge for all properties not currently served by the water system, and a facilities charge.

13 **Settlement Agreement.** The August 8, 2003, Settlement Agreement between Timberline Village and Commission Staff would resolve the issues in the current rate case. The Settlement Agreement was admitted in the proceeding as Exhibit 1. Two attachments to the Settlement Agreement, spreadsheets labeled Results of Operations Statement and Revenue and Rate Calculations, were admitted as Exhibits 2 and 3, respectively. The Results of Operation Statement sets forth the company's revenues and expenses, with company and staff adjustments known

as restating adjustments, per book adjustments, and proforma adjustments. The Revenue and Rate Calculation sets forth the basis of the residential rate design. The Settlement Agreement and attachments are attached to this Order, collectively, as Appendix A.

- 14 The Settlement Agreement results in a 69.94 percent annual revenue increase to Timberline Village, a revenue increase of \$32,181, based upon a revenue requirement (not including taxes and other ancillary charges) of \$75,838 and an authorized overall rate of return of 7.04 percent. *Ex. 1, para. 13, 14; See also Ex. 2, 3.* The calculation of the revenue requirement and rate of return are discussed in more detail below.
- 15 Under the terms of the Settlement Agreement, the monthly flat rate for unmetered service will increase from \$16.80 to \$27.60 per month. The monthly residential metered service will be \$22.80 per month, with a rate of \$0.012 per cubic foot of water consumed up to 400 cubic feet, and \$0.0175 per cubic foot of water consumed over 400 cubic feet. The calculations used for determining the residential rate design are set forth in Exhibit 3.
- 16 Under the Settlement Agreement, the ready to serve charge will be \$7.55 instead of \$15.62 per month as proposed in the company's tariff filing. The ready to serve charge was reduced to reflect the fixed costs associated with ready to serve customers. *Tr. 70-71.*
- 17 The Settlement Agreement does not provide for a facilities charge. Mr. Ward explained that the facilities charge was removed "as an inappropriate funding mechanism." *Tr. 46.* Mr. Ward explained that a facilities charge is a means to allow a water company to grow by providing a source of funds for future improvements. *Id.* Timberline Village has an established service area with capacity remaining in its service area, although the Company has been approached for service by adjacent property owners. *Tr. 46, 88.*

- 18 The NSF check charge proposed in the company’s tariff was reduced from \$25.00 to \$15.00. All other ancillary charges proposed in Timberline’s original filing remain the same.
- 19 During the settlement hearing, Mr. Harrington agreed that Timberline will use the Commission Staff-proposed rates for larger-than-residential rate design, *i.e.*, larger than a ¾ inch meter, set forth in Exhibit 3. *Tr. 86, 89.*
- 20 The following table sets out the Company’s existing rates and charges and compares them to the proposed tariff rates and the rates and charges agreed in the Settlement Agreement and during the hearing. The figures in bold reflect changes from the Company’s original proposal.

RATE ELEMENT	EXISTING RATE	PROPOSED RATE	SETTLEMENT RATE
Unmetered Service/mo.	\$16.80/mo.	\$34.19	\$27.60
Metered Service (¾" base)	None	\$32.50	\$22.80
Cons. Charge = 400 cf	None	\$0.012	\$0.012
Cons. Charge > 400 cf	None	\$0.0175	\$0.0175
1 inch metered service	None	\$54.27	\$38.76
1 ½ inch metered service	None	\$108.22	\$75.24
2 inch metered service	None	\$173.22	\$120.84
3 inch metered service	None		\$228.00
4 inch metered service	None		\$380.76
Ready to Serve Charge	None	\$15.62	\$7.55
Service Connection Charge	\$250.00	\$550.00	\$550.00
Facilities Charge	None	\$1850.00	None
Late Payment Fee	None	\$3.50	\$3.50
Account Set Up Charge	None	\$15.00	\$15.00
NSF Check Charge	None	\$25.00	\$15.00
Special Meter Read	None	\$25.00	\$25.00

- 21 **Revenue Requirement.** In reaching the operating revenue of \$80,049 for the Company, the Company and Commission Staff made several adjustments to the Company's actual per-book accounts using a historical 12-month test period. *Ex. 1, para. 7; Ex. 2.* The primary issue in determining the appropriate level of cost, and therefore, revenue, for Timberline Village was the proper allocation of the cost for services provided by an affiliated interest, Utility Management Services (UMS).
- 22 UMS is a Satellite Management Agency (SMA) licensed by Department of Health to manage and operate community water systems by providing meter reading, testing, routine maintenance, and billing services, and addressing customer concerns and complaints. *Ex. 1, para. 10; Tr. 28, 80.* UMS is an affiliated interest of Timberline Village through its shared ownership and by providing services under contract to Timberline Village. Mr. Harrington is the owner of UMS, as well as the owner of Timberline Village. *Tr. 28.* UMS provides SMA services to six regulated water companies owned by Mr. Harrington: H & R Waterworks, Inc.; Meadows Water System, LLC; Quail Run Water Company, Tall Timber Water Systems, LLC, Timberline Village, and WACOWA (The Water Company of Washington, LLC). *Ex. 1, para. 10.* UMS also provides SMA services to non-regulated water companies, construction services to affiliated and non-affiliated, regulated and non-regulated water companies, and to non-water companies, as well as other services. *Id.*
- 23 Mr. Ward testified that the Commission reviews charges from an affiliated interest to a regulated company to ensure that the affiliated interest charges a regulated company no more than the cost incurred by the affiliated interest. *Tr. 28-29.* The concern is the close relationship between the two entities and the possibility of self dealing. *Id.*
- 24 Under the Settlement Agreement, the costs for officer salary, UMS property and liability insurance, and UMS costs were excluded from Timberline Village's

costs, and added back in to the revenue requirement after making adjustments and allocating the costs to each of the affiliated, regulated water companies. *Ex. 1, paras. 6, 7.*

25 **Allocation of Officer Salary.** Mr. Harrington is the owner and President of six regulated water companies and owner and President of UMS. Commission Staff determined an appropriate salary for an officer of all six regulated water companies, included benefits and taxes and then allocated an amount back to each water company on a proportional basis, based upon the number of customers served by each company. *Ex. 1, para. 8; Tr. 30-31.*

26 **Allocation of Insurance Costs.** UMS's insurance policy includes coverage for Automobiles, Property, and Liability (General and Umbrella). *Ex. 1, para. 9.* Under the Settlement Agreement, the parties agreed that the automobile insurance premium would be included in UMS' general and administrative costs. *Id.; Tr. 33.* A portion of these costs was removed as unrelated to the regulated companies. The remainder was allocated equally among regulated and non-regulated services as described below. *Ex. 1, para. 9; Tr. 33-34.*

27 The parties also agreed that a portion of the property insurance premium would be allocated to UMS using a ratio of UMS net assets to total net assets (3.44%). *Ex. 1, para. 9.* This portion is included in UMS' general and administrative costs, similar to the automobile insurance premium. The remainder is allocated directly to the affiliated, regulated water companies based on the number of customers served by each company. The liability insurance premium is allocated directly to the six affiliated, regulated water companies, UMS' non-regulated services and other services based on the number of customers. *Ex. 1, para. 9.* The direct allocations for property and liability insurance are reflected in Exhibit 2 on the line labeled Insurance under the column labeled Revised Rates. *See Ex. 2.*

28 **Allocation of UMS Costs.** Commission Staff and Timberline Village propose an allocation method that would allocate UMS' costs among the six, affiliated regulated water companies for which UMS provides SMA and construction services, the non-regulated water companies for which UMS provides SMA and construction services, and the other services UMS provides, including construction services to non-water companies. *Tr. 35-36.* Section D. 3. of the Settlement Agreement describes the allocation method, which is based upon four separate work functions and allocation factors using direct hours from timesheets as well as standardized and estimated times to allocate costs for the work function. *Ex. 1, para. 10.*

29 While Commission Staff asserts that direct or actual costs are a better basis for allocating costs than standard or estimated costs, Staff agreed to use standard costs for allocation factors in the absence of an accurate method of calculating direct costs. *Ex. 1, para. 11.* Under the Settlement Agreement, UMS will allocate costs based on the method described above for the purpose of setting rates in this case and for other affiliated, regulated water companies until May 1, 2004. *Ex. 1, para. 12.* After that date, UMS will assign direct costs using time sheet information instead of estimated allocation factors. *Id.* The Company then will review UMS's actual costs and determine whether the allocation model can accommodate the new data or should be revised. *Tr. 75-76.*

30 **Rate of Return.** The rate of return was determined using a weighted cost of capital, calculated on a rate base of \$83,178, using a 12 percent rate of return on equity, the actual cost of third party debt (i.e., traditional bank loans), the 6.75 percent rate of a loan from UMS to Timberline Village, plus 200 points to avoid the concern of self-dealing, and actual capital structure. *Ex. 1, para. 13; Tr. 40, 63.*

31 **Rate Design.** In determining the rates and charges for the company, Commission Staff looked at how the Company's costs are incurred and the customers who cause those costs. *Tr. 41.* Based on this information and the

Company's revenue requirement, Commission Staff determined the appropriate rates for the flat monthly rate, metered rates, and the ready to serve charge. *Tr. 41; see Ex. 3.*

32 **Discussion and Decision.** The ultimate determination to be made by the Commission in this proceeding is whether the Settlement Agreement is appropriate and consistent with the public interest, and whether the rates proposed in the Settlement Agreement are fair, just and reasonable, pursuant to RCW 80.28.020. We resolve these questions by reviewing the Settlement Agreement and the record developed in this proceeding to assess whether the proposal appears fair in

- determining the Company's adjusted results of operations during the test year;
- establishing fair and reasonable costs incurred by the affiliated interest UMS to be allocated to Timberline Village and other affiliated regulated water companies;
- determining the proper rate of return permitted the Company on its property in service; and
- establishing the appropriate spread of rates charged customers to recover that return.

33 The Commission is charged by statute, RCW 80.28.020, to ensure that public service companies, including water companies, provide services at fair, just, reasonable and sufficient rates. The Settlement Agreement, and the Results of Operations Statement (attached Exhibit 2) and the testimony of Mr. Ward and Mr. Harrington explain the adjustments made to the company's books to reach the appropriate operating expenses and operating revenue. This record adequately demonstrates the process used to reach a settlement among the parties and that the adjustments made were appropriate and reasonable.

- 34 **Allocation Method for Affiliated Interest Costs.** Under Chapter 80.16 RCW, the Commission has authority to review the contracts and arrangements between affiliated interests and a regulated company for the purpose of determining whether the contract or arrangement is reasonable or in the public interest. *RCW 80.16.020.* Public service companies must file with the Commission copies of a contract or arrangement with an affiliated interest. *Id.* While the Commission may disallow the contract or arrangement, the statute does not require that the Commission approve the contract or arrangement.
- 35 UMS is an affiliated interest of Timberline Village under RCW 80.16.010. UMS has a management or service contract with Timberline Village and Mr. Harrington is the owner of both UMS and Timberline Village. Timberline has filed its contract with UMS with the Commission for review, as required by statute and Commission rules. *Tr. 61.*
- 36 The allocation of officer salary and insurance costs among UMS and regulated and non-regulated customers is a fair and reasonable allocation of costs resulting in fair, just, and reasonable rates for customers.
- 37 The allocation method agreed to in the Settlement Agreement for UMS costs also results in appropriate costs for Timberline Village. The method has been subject to several years of discussion and evaluation by the Company and Commission Staff. *Tr. 38, 80.* The allocation method uses the most accurate data available, including a combination of actual and standardized or estimated costs. *Tr. 38-39, 60.* After May 1, 2004, the Company will use actual direct costs in the allocation model. *Ex. 1, para. 12.* The allocation model is appropriate and will create consistency in accounting for all six affiliated, regulated water companies owned by Mr. Harrington, as well as consistent treatment during rate cases involving these companies. *Tr. 38.*

38 **Rate of Return.** The 7.04 percent rate of return for the Company was calculated based on a weighted cost of capital. *Tr. 39.* The use of actual cost of third party debt and a 200 basis point premium over the prime lending rate for owner-held debt is consistent with the Commission's decision in the American Water Resources rate case. *Sixth Supp. Order, WUTC v. American Water Resources, Inc., Docket Nos. UW-980072, UW-980258, UW-980265, and UT-980076, at 6; see also Tr. 40.* The rate of return in the Settlement Agreement was developed consistent with ratemaking principles adopted by the Commission and appears reasonable.

39 **Rate Design.** The Revenue and Rate Calculations (attached Exhibit 3) together with the testimony of Mr. Ward and Mr. Harrington, demonstrate how Commission Staff determined the appropriate residential rate design for Timberline Village. The monthly flat and metered rates, as well as the ready to serve charge, will generate an appropriate level of revenue to cover the reasonable and appropriate costs incurred by the Company.

40 We commend Commission Staff and the Company for their efforts to resolve the issues presented by this rate case. The parties negotiated a substantial reduction of the original requested annual revenue requirement amount. The agreement results in lower monthly customer bills as compared to the original filing and allows the Company to recover appropriate costs incurred due to services provided by the affiliated interest UMS.

41 Based on the record, we find the issues are adequately addressed and resolved by the terms of the Settlement Agreement and attached Exhibits. Under these circumstances, we are satisfied that the rates proposed in the Settlement Agreement and attached Exhibits are fair, just, reasonable and sufficient, that the Settlement Agreement, as modified during the hearing by the attached Exhibits, is appropriate and consistent with the public interest, and that the Settlement Agreement should be approved and adopted as a full and final resolution of all issues pending in Docket UW-030410. The Commission determines that it is

appropriate that Timberline Village be authorized to file compliance tariffs by noon on August 28, 2003 to become effective on September 1, 2003.

III. FINDINGS OF FACT

42 Having discussed in detail both the oral and documentary evidence concerning
all material matters inquired into, and having previously stated findings and
conclusions based thereon, the following summary of the facts is now made. The
portions of the proceeding detailing findings and discussion pertaining to the
ultimate facts are incorporated by this reference.

- 43 (1) The Washington Utilities and Transportation Commission is an agency of
the State of Washington vested by statute with the authority to regulate
rates, rules, regulations, practices, and accounts of public service
companies, including water companies.
- 44 (2) Timberline Village Water Company, Inc. operates a water system in
Washington State that serves approximately 213 customers.
- 45 (3) On March 26, 2003, Timberline Village filed with the Commission certain
tariff revisions designed to effect an increase in its rates for water service.
- 46 (4) On August 8, 2003, Timberline Village and Commission Staff filed with
the Commission a Settlement Agreement intended to resolve all issues in
this proceeding.
- 47 (5) During the hearing on August 20, 2003, the parties agreed to rates for the
larger than residential rate metered service included in Exhibit 3.

IV. CONCLUSIONS OF LAW

48 Having discussed above in detail all matters material to this decision, and having
stated general findings and conclusions, the following provides summary
conclusions of law. Those portions of the preceding detailed discussion that
state conclusions pertaining to the ultimate decisions of the Order are
incorporated by this reference.

49 (1) The Washington Utilities and Transportation Commission has jurisdiction
over the subject matter of, and the parties to, this proceeding. *RCW*
80.01.040, Chapter 80.04 RCW, Chapter 80.28 RCW.

50 (2) Timberline Village Water Company, Inc. is a public service company as
defined in RCW 80.04.010.

51 (3) UMS is an affiliated interest, as defined in RCW 80.16.010, of Timberline
Village and five other regulated water companies.

52 (4) The allocation method set forth in the Settlement Agreement used to
allocation costs from UMS to affiliated regulated water companies is
reasonable and appropriate for use in this proceeding and other
proceedings before this Commission involving H & R Waterworks, Inc.;
Meadows Water System, LLC; Quail Run Water Company, Tall Timber
Water Systems, LLC, Timberline Village, and WACOWA.

53 (5) The Settlement Agreement (Appendix A to this Order), as modified
during the hearing by Exhibits attached 2 and 3, fully and fairly resolves
the issues pending in this proceeding, is consistent with the public
interest, and should be approved. *RCW 80.01.040, WAC 480-09-466.*

- 54 (6) The Settlement Agreement (Appendix A to this Order), as modified during the hearing by attached Exhibits 2 and 3, results in rates for prospective application that are just, reasonable, and compensatory; and that are neither unjustly discriminatory nor unduly preferential. *RCW 80.28.010, RCW 80.28.020, RCW 80.28.090, RCW 80.28.100.*
- 55 (7) The Commission should retain jurisdiction over the subject matter of and the parties to this proceeding to effectuate the provisions of the Order.

V. ORDER

THE COMMISSION ORDERS That:

- 56 (1) The proposed tariff revisions filed by Timberline Village on March 26, 2003, and suspended by prior Commission order, are rejected.
- 57 (2) The Settlement Agreement (Appendix A to this Order), as modified during the hearing by attached Exhibits 2 and 3, is approved, adopted, and made part of this Order.
- 58 (3) Timberline Village Water Company, Inc. is authorized to file compliance tariffs no later than the close of business on August 28, 2003, to effectuate the terms of the Settlement Agreement and this Order.
- 59 (4) The Commission Secretary may approve by letter the compliance filing.
- 60 (5) The procedural schedule established in Order No. 02 in this proceeding is canceled.
- 61 (6) The Commission retains jurisdiction over the subject matter and the parties to effectuate the provisions of this Order.

Dated at Olympia, Washington and effective this 27th day of August 2003.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

RICHARD HEMSTAD, Commissioner

PATRICK J. OSHIE, Commissioner

NOTICE TO PARTIES: This is a final order of the Commission. In addition to judicial review, administrative relief may be available through a petition for reconsideration, filed within 10 days of the service of this order pursuant to RCW 34.05.470 and WAC 480-09-810, or a petition for rehearing pursuant to RCW 80.04.200 or RCW 81.04.200 and WAC 480-09-820(1).

[Service Date August 27,2003]

Appendix A