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IDAHO PUBLIC UTILITIES COMMISSION

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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF FALLS WATER COMPANY'S APPLICATION FOR AN ORDER AUTHORIZING INCREASES IN THE COMPANY'S RATES AND CHARGES FOR WATER SERVICE IN THE STATE OF IDAHO	)))))	**CASE NO. FLS-W-20-03** **COMPANY'S REPLY TO CONFIDENTIAL COMMENTS OF THE COMMISSION STAFF**

Comes now Falls Water Co., Inc. ("Falls Water" or the "Company") and files the following Reply to the Confidential Comments ("Comments") of the Staff of the Idaho Public Utilities Commission ("Staff"), filed January 11, 2021.

Staff made the following recommendations:

1. Staff recommends an annual revenue requirement of $1,967,016, consisting of a rate base of $4,928,979, a return on equity ("ROE") of 9.9%, and a weighted average cost of capital ("WACC") of 6.91%.
2. Staff recommends a reduction to the Company's proposed employee salaries of $79,747, employee benefits of $3,872, and payroll taxes of $6,143.
3. Staff recommends a reduction in training expenses of $2,983.
4. Staff recommends the elimination of the $8,315 operational expense as well as the contribution into the special plant reserve account, as ordered by the Idaho Public Utilities Commission ("Commission") in Order No. 32663. Staff also recommends that the Company continue to fund the special plant reserve account with the depreciation expense associated with advanced meters.
5. Staff recommends a reduction to shared services expense of $39,655.
6. Staff recommends setting the Company's property tax expense at 1.16% of net plant in service and making adjustments to the Company's income tax expense based on proposed adjustments to the Company's expenses and rate base.
7. Staff recommends that the Company deplete the special plant reserve fund towards the infrastructure projects built since the last rate case. Staff also states that all of the existing funds should be treated as a contribution in aid of construction ("CIAC").
8. Staff recommends the Company collect its revenue through an increase in commodity charges as shown in Table No. 3 of the Staff Comments.
9. Staff notes that due to customer complaints regarding a boil advisory from April 20, 2020, the Company will be implementing a mass communications system to alert customers of problems in a more timely and modern method than that required by the Idaho Department of Environmental Quality.
10. Staff recommends removing the Company's bank service charge fee from the calculation of the gross up factor.

INTRODUCTION

Falls Water thanks Staff for its diligence and flexibility in the face of the difficulties caused by COVID-19. Staff's flexibility allowed this case to carry forward in spite of the challenges faced due to COVID-19.

However, Falls Water respectfully disagrees with some of the assertions and conclusions contained in the Staff Comments, as described in more detail below.

GENERAL COMMENTS

First, Staff notes in several instances that Falls Water was acquired by NW Natural Water, and that NW Natural Water indicated that customer rates would not increase by virtue of the acquisition. Staff Comments at 2 and 7. That statement was true, and remains true: Falls Water is not seeking any increase in rates caused by the acquisition. Falls Water and NW Natural Water have always indicated that any increase in rates would be based on prudent investments and recognized ratemaking principles.[1] In this general rate case, Falls Water seeks a rate increase resulting from its prudent investments and other ratemaking principles. Falls Water asks that its application be reviewed in accordance with the Commission's established ratemaking principles and procedures. The requested increases are not caused by the acquisition, but rather from prudent investments and related expenses as described in more detail in the specific comments below.

Second, in several instances Staff notes increased expenditures on items such as training, accounting, human resources ("HR"), and other functions previously undertaken by Falls Water employees. Staff Comments at 5 (training), 6 (accounting, corporate communications, HR/payroll, and information technology and services ["IT&S"]). Increased expenditures, in and of themselves, are not an indication that the increase was unwarranted. Improving the operation of small water companies requires investment in areas such as training and operations. The two go hand-in-hand; one cannot expect that small water companies operate better without allowing expenditures in the companies' operations. Of course, the expenditures must be reasonable and prudent. But it is not reasonable to view all increases in operational expense as inherently suspect.

Third, Staff references seeking prudency approval before engaging in significant capital improvements. Staff Comments at 2, 9. Falls Water takes exception to those statements. Falls Water has made specific efforts to improve the advanced communication regarding our capital investments, and has been very deliberate about seeking Staff review and engagement in our capital investment decision-making process. The Company has been transparent during meetings and discussions with Staff, including a meeting held on October 16, 2019, during which Falls Water and Staff discussed Falls Water's Drinking Water Capital Facilities Plan. On this point, Staff acknowledges that the Company's rate case application "include[s] several additions and replacements that were in the Company's Drinking Water Capital Facilities Plan." Staff Comments at 8. The Company sought prudency review on the expenditure for the new well (FLS-W-17-01), which appears to be consistent with prudency reviews sought by water companies in prior cases. Falls Water is happy to discuss with Staff its view on what types of expenditures require prudency review. But the Company submits that, at this time at least, there

[1] FLS-W-18-01, Application, page 3, paragraph 10.

is no clear line (beyond seeking prudency review for new wells) between investments that require prudency review and those that do not.[2]

Fourth, the Staff Comments refer to potential hardships caused by COVID-19. Staff Comments at 4 (noting that wage increases in 2020 and beyond "are excessive at a time when many of the Company's customers may be facing financial hardship due to the ongoing COVD-19 pandemic"). The Company is cognizant of COVID-19 and the hardships it has caused. The Company voluntarily ceased disconnections and collections activities, and established payment arrangement options for customers who have been unable to meet the current payment due date. In addition, the investments and expenditures that form the basis for the proposed increase were planned prior to COVID-19. Those investments and expenditures are based on regulatory principles set forth by the Commission, have provided benefits during the COVID-19 pandemic, and will continue to provide benefits after the pandemic is over. The Company respectfully submits that the COVID-19 pandemic should not be a driver of the long-term ratemaking decisions at issue in this case.

In addition to these general comments, the Company provides the following comments, which are more specific to Staff's particular recommendations listed above.

COMMENTS ON STAFF'S RECOMMENDATIONS

RESPONSE TO RECOMMENDATION NO. 1

Falls Water requested that the ROE of 10.5%, established in its prior rate case, be maintained. Further, Falls Water recognized that its business is financed almost entirely from equity, so it offered that the overall rate of return be based on a hypothetical capital structure of 45% debt and 55% equity.

Staff agreed that the overall rate of return should be based on a hypothetical capital structure, rather than the actual rate structure, but recommended an ROE of 9.9%. Staff bases this recommendation in part on "[o]ther NW Natural Holdings utilities hav[ing] ROE's lower than Falls Water" and on the Commission having awarded non-water utilities ROEs of 9.5%. Staff Comments at 10. Staff also asserts that the WACC of 6.91% that results from lowering the ROE to 9.9% is "comparable to NW Natural Holding's weighted cost of capital for its Oregon natural gas utility, which is 6.97%." Staff Comments at 10.

Falls Water respectfully disagrees with the methodology and conclusion used by Staff to determine a recommended ROE. First and foremost, Falls Water is a small water company in Idaho. The Commission has consistently determined that ROEs of between 11% and 12% are appropriate for these companies. *See* Case No. GPW-W-017-01, Order No. 33910 at 8 (Oct. 13, 2017) (approving 11% return

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[2] Staff also makes the comment, "The Company is proposing large plant additions in this case, again without seeking a prudency determination from the Commission prior to beginning work, aside from the new well." Staff Comments at 9. However, Staff does not suggest that these expenditures are imprudent. And they are not imprudent—these are important, prudent investments that should be made to serve the system's customers. In addition, it is Falls Water's understanding that prudency review is historically sought for investments such as a new well, while more routine infrastructure improvements have not historically been subject to advance review. To the extent the Commission requires or desires advance prudency review, some guidance regarding the types of projects for which review is desired may be helpful to avoid future misunderstandings.

on equity on the basis that it "reflects a fair return in line with similar utilities."); Case No. DIA-W-15-01, Order No. 33578 at 11 (Aug. 29, 2016) ("We find the agreed 12% rate of return to be fair and just and consistent with that which we have allowed in other small water company cases, and thus approve it."); Case No. SPL-W-13-01, Order No. 32904 at 8 (Oct. 11, 2013) ("The Commission finds that a 12% return on equity and 11.42% overall rate of return is fair, just and reasonable return for the Company. This ruling is entirely consistent with past Commission precedent for small water companies and particularly for water systems comparable to Spirit Lake." (citing Case TRH-W-10-01, Order No. 32152; BCS-W-09-02, Order No. 30970; and Case No. CCH-W-12-01, Order No. 32662)); Case No. TRH-W-13-01, Order No. 32958 at 4, 10 (Dec. 21, 2013) (authorizing 12% return on equity for small water company, based in part on Staff's recommendation that "the 12% return on equity (ROE) is consistent with the Commission-authorized ROE for many small water companies"). In these cases, the Commission approved the ROEs based on comparisons to other small water companies in Idaho, and neither the Commission nor Staff discussed or analyzed the ROEs approved in other states, ROEs of non-water utilities, ROEs for affiliated companies, or the other factors Staff discusses here.

Falls Water submits that it is unreasonable—potentially discriminatory[3]—to deviate from the Commission's typical practices regarding small water utilities on the basis that Falls Water's parent company has holdings in other states. Potential discrimination aside, Staff does not explain how comparison to non-water utilities, utilities in other states, and other utilities held by Falls Water's parent company's holding company is appropriate here, particularly against the longstanding background of recommending ROEs based on the ROEs approved for small water companies. *See*, e.g., Case No. TRH-W-13-01, Order No. 32958 at 4 ("Staff says that the 12% return on equity (ROE) is consistent with the Commission-authorized ROE for many small water companies.").

In addition, while Staff makes a variety of comparisons to other utilities, Staff does not explain how it settled upon a recommendation of 9.9%. Indeed, Staff's recommendation does not appear to be based on any particular methodology. Staff appears to simply settle upon a percentage, and then discuss similar (and not-so-similar) percentages for in-state and out-of-state non-water companies. Staff's analysis does not distinguish between the water sector, natural gas sector, and electric sector, each of which has different risk profiles; or between states, again, each of which has different risk profiles. Most strikingly, Staff's analysis entirely omits the ROEs of companies that are most closely analogous to Falls Water: small water companies in Idaho. Falls Water submits that Staff's comparisons do not provide a reasonable basis for the Commission to authorize an ROE of 9.9%.

As noted, Falls Water's actual capital structure was 15.4% debt and 84.6% equity as of December 31, 2019. Falls Water proposed to use a hypothetical capital structure as an accommodation to lower the total rate of return. However, if Staff's analysis is adopted and the Commission uses an ROE of 9.9%, Falls Water submits that it would be appropriate to calculate the overall rate of return using its actual capital structure, rather than a hypothetical.

[3] The Commission may not discriminate against utilities based on the ownership status of their parent companies. *See In re PacifiCorp*, Case No. PAC-E-99-1, Order No. 28213 (1999) (noting that the U.S. Constitution's Commerce Clause and treaties prohibit "discriminat[ion] against service providers who are citizens of other states or foreign countries").

Accordingly, the Company requests that Staff's 9.9% ROE be increased to the Company's proposed ROE of 10.5%. Given the prior Commission decisions authorizing ROEs of between 11% and 12% for small water utilities, the Company would have been justified to seek a higher ROE, but it decided to not do so. Instead, the Company's requested 10.5% ROE is the same percentage as the Commission approved in Falls Water's last rate case, FLS-W-12-01, Order No. 32663, dated October 12, 2012. This ROE falls on the low side of ROEs approved for other small water companies, as discussed above. Falls Water's position is that the 10.5% ROE continues to be fair to both the Company's investors and its customers and will enable the Company to successfully operate and attract capital. The Company also notes that Suez Water filed its most recent rate case on September 30, 2020, SUZ-W-20-02, and its expert consultant is recommending a 10.2% ROE (Walker, p. 62). Falls Water's 10.5% requested ROE is within the range of reasonableness, especially given its smaller size compared with Suez Water. The Company could have hired an expert ROE consultant for this rate case, but decided that it was more in the public interest to not incur such rate case expense to be amortized over a period of time and recovered from customers. A final consideration is that while Falls Water's actual capital structure as of December 31, 2019 was 84.6% equity / 15.4% debt, the Company is proposing a more balanced hypothetical capital structure of 55% equity / 45% debt, and that concession merits adopting the Company's requested 10.5% ROE.

RESPONSE TO RECOMMENDATION NO. 2

Historically, Falls Water employees have been paid significantly less than employees of competitors in the area, including both municipal and investor-owned utilities. In recent years, Eastern Idaho has seen significant growth in economic activity and, correspondingly, an increase in wages and competition for qualified employees. Indeed, recently Falls Water lost two employees to other employers due in part to the Company's uncompetitive wages. To address this issue, Falls Water proposed wage increases, phased in over a number of years. These increases are necessary to bring compensation to a level offered by local competitors, such as the City of Idaho Falls water system.

In Staff Comments Table No. 1 (annual salary increase comparisons), Staff's data for Falls Water are based on the Company's response to Staff data request ("DR") No. 57. In that DR, Staff requested a list of all Falls Water employees and their wage rates and percentage of wage increases for each year starting in 2012 and ending in 2020. The Company's DR No. 57 response showed the gross wage increase percentage for the Company's employees as requested (on a confidential basis). Not detailed in the response (because it was not requested in the DR) were the components of the wage increases. Looking at the non-redacted wage increase percentages for other similar companies, many of the percentages are 2% to 3% increases. These percentages are comparable to a cost-of-living increase which is customary in most businesses. A second component to wage increases is incentive-based compensation for an employee attaining licenses, certifications, and other training that enhances the employee's skill set to better serve the utility and bring added benefit to the customers by increasing the employee's knowledge to safeguard the public. A third component to wage increases is performance-based compensation. As the employee excels in his or her position and/or is given added responsibilities, the company will award a wage increase to recognize the employee's improved value to the company and its customers.

Importantly, all three components of compensation are embedded in the Falls Water wage rates and percentage of wage increases disclosed confidentially in the spreadsheet accompanying the Company's response to DR No. 57. It appears that the other companies' wage increase percentages shown in Staff Comments Table No. 1 are only cost of living increases and do not reflect any additional wage increases based on incentive-based or performance-based wage increases. (Falls Water cannot definitively confirm this, because the data are confidential and have not been provided to Falls Water or the data are disclosed without citations, but the percentage increases that can be seen appear to reflect cost-of-living increases only.)

The Company has submitted to Staff a supplemental response to DR No. 57 that provides a more detailed confidential spreadsheet to break out the components of the wage increases.[4] While the details of the comparison are confidential, the components of Falls Water's wage increases that reflect cost-of-living increases fall within the increases noted in Staff's Table No. 1. The remaining components of the increases do not appear to be reflected in Staff's Table, and the Table should not be used to disallow the other components of Falls Water's proposed increases.

Moreover, Staff acknowledged in its comments that "the Company's salaries have historically been lower than other water systems, both investor-owned and municipal systems." Staff Comments at 4. In late 2018 and in 2019, the Company lost one of its two Class 3 Distribution Operators to a neighboring water system. The employee's reason for leaving was in part due to the opportunity to earn a better wage than he received from the Company. Approximately six months later, an equipment operator for the Company resigned because the Company was not able to match the wages offered by a local excavation company. The Company is not losing employees to other parts of the State or to companies outside of Idaho but to local businesses that offer higher wages. This creates a situation that is not in the best interest of customers. Customers deserve to have well-trained, competent, and knowledgeable employees working for the utility. If the Company struggles to hire good employees and then to retain them because it is unable to offer a competitive wage when compared to other local water systems and businesses, customer service is ultimately harmed.

It also is worth noting that Staff's Table No. 1 of comparisons to other employers is problematic. First and foremost, the information regarding other utilities is redacted. After it filed its Comments, Staff informed the Company that it cannot share the redacted information. Accordingly, the Company does not even know what the numbers on the table actually are, and it cannot obtain and analyze the underlying information to determine (for example) what the actual wages are, as opposed to the percent increase, what components are included within the salary increase, or otherwise meaningfully respond. The Company respectfully submits that viewing blacked-out boxes on a page does not provide an appropriate basis for adjustments in a rate case. Second, the chart focuses exclusively on percentage increases, without regard to the starting point of wages. If a company starts with historically low

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[4] Falls Water has submitted this information to Staff as confidential under the Commission's rules and pursuant to the protective agreement in this proceeding. There appears to be some ambiguity as to whether this information is formally considered as part of the record in the case. This information is highly sensitive, particularly in the small, competitive marketplace of Idaho Falls. There does not appear to be a mechanism in the Commission's rules that would allow *in camera* review by the Commission without publicly disclosing the confidential information to the public. Falls Water would be happy to facilitate an *in camera* review or other procedure that would provide this information to the Commission confidentially so that it can formally be considered part of the record. (Falls Water notes that the same ambiguity would apply to Staff's redacted Table. If Staff intends to provide the Commission with an unredacted version of its comments for *in camera* review, Falls Water would consider a similar procedure for its salary information.)

wages—as Falls Water does—then the company must play catch up with larger increases to maintain the ability to compete in the environment. This comparison does not provide a basis to freeze wages; the company will then simply fall further behind, and either fail to attract or retain talent, request greater increases in the future, or both. Third, the chart draws a comparison between a small water company in eastern Idaho with large, multi-state and multi-national corporations with operations in different sectors and in different areas of the state. Drawing such a broad comparison, while focusing exclusively on the percentage of salary growth, does not provide a basis to freeze wages. Falls Water does not compete with an Avista employee in Sandpoint or an Intermountain Gas employee in Boise; it competes with the City of Idaho Falls Water and similar private-sector companies in the area. It also should be noted that public-sector employers are able to offer pensions and other benefits that can create a competitive challenge for private companies like Falls Water.

The Company is attempting to bring its wages to a competitive level with local utilities and businesses to prevent loss of trained employees. The strategy was implemented to do this over a three-year period for 2020, 2021, and 2022. Staff instead recommends freezing recovery at 2019 levels, which will exacerbate the existing wage disparity and put the Company in the position of falling further behind or requesting larger increases to catch up at a later time. Staff's approach might work if the wage difference were a small percentage, which is not the case for Falls Water: The wage differential between the Company and the City of Idaho Falls is an average of 26% lower for Falls Water.[5] This difference would take much longer than a few years to correct, during which the Company expects that it would continue to lose employees because of its lower wages. Customers may benefit temporarily with lower rates, but at the long-term expense of the Company failing to attract and retain experienced workers for the benefit of its customers. The recommendation from Staff to not include any of the 2020 or 2021 wage increases in rate recovery may also shorten the Company's timing between rate cases.

Northwest Natural Water is actively acquiring small water systems in the surrounding area of the Company. Between the natural growth in the Company's service area and new acquisitions, the total number of connections served by the Company has grown from 3,832 connections at the beginning of 2012 to 5,902 connections as of December 31, 2020. The number of full-time employees in 2012 was seven and the Company has nine full-time employees as of the end of 2020. The Company needs to offer competitive wages to attract and retain quality employees who can provide the expertise necessary to give customers the quality of service that is expected by customers, particularly as the number of customers continues to grow.

RESPONSE TO RECOMMENDATION NO. 3

The Company takes exception to Staff's recommendation to reduce training expenses by $2,983. Given recent vaccine developments, the COVID-19 pandemic should not be expected to last for the next two or three years. Business travel should resume and training expenses should return to pre-pandemic levels during the time that these rates are in effect. Not all training can be done via teleconference training sessions. It is not possible to network effectively with peers in the industry via teleconferencing, and venues like conferences enhance the training experience. The Company requests the Commission reject Staff's proposal to reduce the Company's training expense.

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[5] Source information from City of Idaho Falls job descriptions and wage chart for October 1, 2018 thru September 30, 2019.

RESPONSE TO RECOMMENDATION NO. 4

The Company accepts Staff's recommendation to eliminate the $8,315 operational expense as well as the annual savings contribution into the special plant reserve account, as ordered by the Commission in Order No. 32663. The Company also agrees with Staff's recommendation that the Company continue to fund the special plant reserve account with the depreciation expense associated with advanced meters, consistent with that Order.

RESPONSE TO RECOMMENDATION NO. 5

The Company included $79,225 in shared services allocated costs in its pro forma adjustments for NW Natural Water expenses allocated to Falls Water. In response, Staff comments that "some of the services provided do not directly benefit Falls Water customers" and recommends removing charges "that don't offset other Falls Water expenses, specifically accounting, corporate communications, HR/payroll, and information services." Staff Comments at 9. Staff states that these functions "were provided by Falls Water employees prior to the acquisition," and that including the expenses would "increase customer rates without providing any additional benefit." *Id.*

First, Falls Water respectfully disagrees that these services do not benefit customers, and that including the expenses would increase rates without providing a benefit. The services identified by staff—accounting, corporate communications, HR/payroll, and IT&S services—do benefit customers. These are back-office functions that, while perhaps not as visible or customer-facing as other aspects of a business, are critical to a business's success. Improving these functions, while allowing local employees to conduct the day-to-day functions, means that NW Natural Water can leverage its platform expertise to benefit Falls Water service to all its customers under a shared services model. Indeed, these services were offered and included in rates prior to the acquisition too, as explained in more detail below, but now those services are shared over multiple water companies with increased expertise in a more cost-effective manner. Falls Water respectfully submits that the value of these back-office functions, and the expertise that NW Natural Water provides in these areas, be recognized fully in this case.

Second, while Staff is correct that theses services were provided by Falls Water before its acquisition by NW Natural Water (specifically, by the prior owner who left the Company in 2019), the duties that the prior owner performed were transitioned to NW Natural Water as he prepared to depart. The Company adjusted the test year to exclude the prior owner's 2019 wages, benefits and payroll taxes. The duties of accounting, communications, HR/Payroll, IT&S services, treasury, and other functions are now being fulfilled by people at NW Natural. Falls Water's proposal of shared services costs represents a savings to Falls Water customers of $69,127, or 47%, when compared to the costs of the eliminated position that have been removed from our operating costs (table below). The Company requests that Staff's recommendation to reduce the shared services expense be rejected given that the employee previously providing those services is no longer with the Company and that NW Natural Water now is providing these services in a more cost-effective manner than the prior owner.

2021 Wages/Benefits Budget		Previous Owner & Employee
Base Salary		123,000
Payroll Taxes (10/5%)		12,915
Benefits		12,437
TOTAL	$	148,352
Proposed Shared Services	$	79,225
Savings	$	69,127
% Savings		47%

Additionally, it should be noted that Staff has proposed to reduce our ROE due to NW Natural's access to capital markets and being able to borrow at better rates. Staff Comments at 10. These benefits do not materialize without audited financial statements to provide to lending institutions. Increased and improved back office support is required to achieve these customer benefits. Assuming a benefit to customers by reducing the proposed ROE while also excluding the associated costs that provide those benefits is inconsistent.

In today's world, maintaining cyber security of our network and systems is a real concern. Yes, our current staff can carry out certain IT&S functions, but they do not have the high level of expertise needed to administer our network to safeguard the water system and customer data. If the IT&S costs within our proposed shared services allocation are removed, the Company will be forced to consider adding third-party contract labor and discontinuing or reducing the use of NW Natural Water, even though shared services costs are lower.

Since being acquired by NW Natural, the HR department has carried out the following tasks to the benefit of Falls Water and its customers:

1. Recruiting for open positions
2. Changed payroll and benefits provider
3. Managed and processed open enrollment for health, dental, life and short-term and long-term disability benefits
4. Assisted with employee relations issues
5. Advised management on performance issues
6. 401k annual meeting
7. Written job descriptions
8. Creating new policies such as paid-time-off
9. Working to create an employee handbook

We believe these to be value added to Falls Water and again would like to reference that many of these tasks would have been carried out by the previous owner whose costs have been removed from our operating costs to the net benefit of customers.

The costs of the "NW Natural Water new 2020 jobs" that Falls Water included in this rate case, and which Staff shows in Table No. 2 of its Comments, relate to a Finance & Accounting Manager, a General Ledger Accountant, and an HR/Payroll Specialist. It is more cost effective to hire specialized personnel at the parent company to perform accounting and HR tasks across the water companies, rather than trying to piece these services together at each individual water company.

These costs have been pooled at the water holding company and will be allocated out using the Massachusetts Formula. Staff offers no specific reason why the Company should recover only half of these prudently-incurred costs.

The "Indirect Common Allocation Costs" that Falls Water included in this rate case, and which Staff shows in Table No. 2 of its Comments, are the indirect labor of the following departments combined with the costs related to our publicly-traded company structure (e.g., Securities and Exchange Commission registrant and filing fees):

- Corporate Governance and Compliance
- Corporate Security
- Financial Planning & Budgeting
- Financial Reporting
- Internal Audit
- Investor Relations

These costs are allocated out across all NW Natural entities using the Massachusetts Formula. Staff fails to explain why the Company should not be able to recover any of these prudently-incurred costs.

The "Corporate 27.5% admin charge" that Falls Water included in this rate case, and which Staff shows in Table No. 2 of its Comments, reflects a percentage of labor cost added to cover the cost of rented space, office supplies, IT&S costs, utilities, furniture, fixtures and equipment and other administrative costs. Staff does not explain why Falls Water should not be able to recover any of these prudently-incurred costs.

There are many components to the shared services costs modeled to Falls Water, as there is a large infrastructure of knowledge, expertise, and public company structure from which Falls Water benefits. Again, the cost of these benefits is 47% lower than the previous owner's costs that have been removed from the Company's rate case application.

RESPONSE TO RECOMMENDATION NO. 6

The Company accepts Staff's proposal for a rate of 1.16% of net plant in service to calculate property taxes. The Company also agrees that the income tax expense should be adjusted to reflect expense and rate base adjustments to its application.

RESPONSE TO RECOMMENDATION NO. 7

The Company agrees that using the special plant reserve fund is appropriate. The Company does, however, take issue with Staff's recommendation that the entire amount of the fund be treated as CIAC. Consistent with Commission Order No. 32663 that established the special reserve fund and Commission Order No. 33863 that provided guidance as to the administration of the fund, the amount applicable for CIAC treatment as of December 31, 2020 is $28,134.04.

The Commission issued Order No. 32663 in the Company's 2012 rate case that initiated the special reserve fund. Regarding the application of the funds in the special reserve account, the Order states (at 11), "To the extent any investments from this special plant reserve account are approved by the Commission, they will be allowed in rate base and depreciated like any other prudent plant investment." The Order further states (at 11), "we also find it reasonable and appropriate for the Company to reinvest the MXU-related depreciation and the annual savings of $8,315 over 25 years into a special plant reserve fund." In other words, the special reserve fund consists of two components: 1) the depreciation of the MXUs installed, and 2) the meter reading labor savings of $8,315 annually. Regarding these two components, Staff acknowledges that the Company "properly funded the special plant reserve fund since the previous rate case." Staff Comments at 5.

Importantly, the Commission's rationale regarding the MXU investment did not support a disallowance, but provided a pre-financing of future capital projects. The Order (at 11) states, "the Company is a small water utility, and we are concerned that wholly disallowing the MXU investment could jeopardize the Company's financial integrity and ability to provide safe and reliable service to customers. And while the Company spent far too much too quickly to install its MXUs, we believe the Company's MXUs ultimately will benefit its customers. We thus find it reasonable and appropriate to allow the Company to also include in rate base its $674,024 in MXU investment." If the depreciation-based portion of the fund is treated as CIAC, as Staff proposes here, the effect of that treatment is actually a disallowance of the original project, in that the recovery of investment through depreciation expense would not be returned to the investors of the project, but would rather offset the cost of a new project. The Commission did not intend a disallowance of the project.

Contrary to Staff's assertion, its proposal is <u>not</u> "consistent with Commission Order No. 33863 in Case FLS-W-17-01." Staff Comments at 9. In Case No. FLS-W-17-01, Commission Order No. 33863 stated (at 2), "With regard to accounting treatment of funds associated with the special reserve fund — annual savings of $8,315, now approximately $39,000 — Staff recommended that such contributions be a reduction to rate base, explaining that funds from the special reserve fund are customer- and not investor-supplied capital." The Order sided with Staff in stating (at 5): "The contribution of $39,172 (annual savings) from the plant reserve fund shall be recorded as a contribution in aid of construction, and will be a reduction to rate base." The order did not address the depreciation-based component of the reserve account in its determination of CIAC, which was appropriate.

As of December 31, 2020, the special plant reserve fund included $112,753.33 (See Exhibit 1 of the Company's Reply Comments). The meter reading labor savings (CIAC) portion of the balance is $28,134.04 and the MXU depreciation portion of the balance is $84,619.29. Consistent with the original intent of the fund and subsequent guidance by the Commission, the Company proposes that only the labor savings portion of $28,134.04 of the $112,753.33 in the special plant reserve fund be treated as CIAC.

RESPONSE TO RECOMMENDATION NO. 8

Staff recommends the rate structure proposed by the Company be revised to move all of the rate increase to the commodity charges. Staff proposes a 20% increase to commodity charges. However, the Company has concerns that moving the entire amount to commodity charges could result in reduced usage by customers and result in the Company not achieving its authorized revenue requirement. Staff shares the Company's concern that a misbalanced rate design "significantly reduces the likelihood that the Company could recover the revenue requirement approved in this case" and "could result in more cash flow variance throughout the year." Staff Comments at 12.

The Company acknowledges that conservation is promoted raising only the commodity charge, but believes a reduction in the usage allowance amounts (e.g., lowering the 12,000 gallons/month allowed for customers with 5/8- or 3/4-inch meters) would help to compensate for potential lost revenue due to conservation. Splitting the increase between volumetric and fixed charges, coupled with a decrease in the usage allowance amounts, would balance the need for conservation with the revenue certainty provided by fixed charges and, consistent with Staff's objective, would further "temper[] the level of volumetric recovery in this case." Staff Comments at 12.

RESPONSE TO RECOMMENDATION NO. 9

While the Company did meet the required customer notification deadlines resulting from the low-pressure event on April 20, 2020, many customers were unhappy that they were not notified individually of the issue. Many customers stated that they do not watch local news outlets and were unaware of the issue until it had been resolved. Because of the concerns of the customers and with the advancement in technology that makes it possible to contact customers via devices readily available to most if not all customers, the Company has enlisted the services of a mass communication service. The Company expects that the mass communications system will be active by the end of February 2021. The contract negotiated by Northwest Natural Water will provide this service for all of its water systems. The savings achieved through the economies of scale will be passed along to customers. The costs for this service will be billed to the Company based on the number of customers and will not be a part of shared services provided by Northwest Natural Water. The cost of this service will appear in the next rate case.

RESPONSE TO RECOMMENDATION NO. 10

The Company does not agree with Staff's recommendation to remove the Company's bank service charge fee from the calculation of the gross up factor. Staff Comments at 10-11. Part of the gross up factor is related to billed revenues, and nowhere else in this case is the expense of the bank service charge fee associated with incremental revenue included in the revenue requirement.

Respectfully submitted this 25th Day of January 2021.

K. Scott Bruce

Falls Water Company

K. Scott Bruce, General Manager

Cc: Eric Nelsen
Senior Regulatory Attorney
NW Natural, representing Falls Water

Exhibit 1 to Company's Reply Comments in FLS-W-20-03

Falls Water Co., Inc.
Allocation of Funds in Special Plant Reserve Fund
as of December 31, 2020

	Meter Rdg Lbr Savings		Interest	MXU Depreciation
10/31/2012	368.28			
11/30/2012	692.92			
12/31/2012	692.92	1,754.12		
1/31/2013	692.92			
2/28/2013	692.92			
3/31/2013	692.92		0.06	4,245.88
4/30/2013	692.92			
5/31/2013	692.92			
6/30/2013	692.92		0.75	
7/31/2013	692.92			
8/31/2013	692.92			
9/30/2013	692.91		0.76	2,257.20
10/31/2013	692.91			26,282.28
11/30/2013	692.91			
12/31/2013	692.91	8,315.00	4.59	
1/31/2014	692.92			
2/28/2014	692.92			
3/31/2014	692.92		5.28	
4/30/2014	692.92			
5/31/2014	692.92			
6/30/2014	692.92		5.34	
7/31/2014	692.92			
8/31/2014	692.92			11,191.28
9/30/2014	692.91		6.66	
10/31/2014	692.91			
11/30/2014	692.91			9,121.00
12/31/2014	692.91	8,315.00	8.60	2,592.21
1/31/2015	692.92			2,925.15
2/28/2015	692.92			
3/31/2015	692.92		9.38	
4/30/2015	692.92			
5/31/2015	692.92			
6/30/2015	692.92		9.60	
7/31/2015	692.92			
8/31/2015	692.92			
9/30/2015	692.91		9.71	
10/31/2015	692.91			20,033.46
11/30/2015	692.91			

12/31/2015	692.91	8,315.00	12.09	4,279.11
1/31/2016	692.92			2,059.47
2/29/2016	692.92			2,059.47
3/31/2016	692.92		13.92	
4/30/2016	692.92			2,059.47
5/31/2016	692.92			
6/30/2016	692.92		14.53	
7/31/2016	692.92			
8/31/2016	692.92			
9/30/2016	692.91		15.08	10,912.83
10/31/2016	692.91			
11/30/2016	692.91			6,474.18
12/31/2016	692.91	8,315.00	17.03	
1/31/2017	692.92			6,315.90
2/28/2017	692.92			
3/31/2017	692.92		18.14	2,654.79
4/30/2017	692.92			2,201.37
5/31/2017	692.92		7.32	2,051.91
6/30/2017	692.92		12.00	
7/31/2017	692.92			4,544.64
8/31/2017	692.92			2,050.02
9/30/2017	692.91		20.76	2,924.10
10/31/2017	692.91			2,046.24
11/30/2017	692.91			2,190.66
12/31/2017	692.91	8,315.00	21.33	2,189.40
1/31/2018	692.92			2,044.98
2/28/2018	692.92			2,044.98
3/31/2018	692.92		1.81	4,089.96
4/30/2018	692.92			
5/31/2018	692.92			
6/30/2018	692.92		3.50	4,089.96
7/31/2018	692.92			2,463.12
8/31/2018	692.92			2,320.59
9/30/2018	692.91		5.31	2,041.83
10/31/2018	692.91			1,082.17
11/30/2018	692.91			3,014.13
12/31/2018	692.91	8,315.00		2,314.98
1/31/2019	692.92		11.32	2,040.57
2/28/2019	692.92			2,310.51
3/31/2019	692.92			2,173.65
4/30/2019	692.92		17.27	2,038.68
5/31/2019	692.92			2,171.76
6/30/2019	692.92		21.14	2,170.50
7/31/2019	692.92			2,432.88
8/31/2019	692.92			2,166.72
9/30/2019	692.91		22.47	2,034.90
10/31/2019	692.91			2,294.76

11/30/2019	692.91				2,033.64
12/31/2019	692.91	8,315.00		8.32	2,162.31
1/31/2020	692.92				2,033.01
2/29/2020	692.92				2,032.38
3/31/2020	692.92			7.55	2,032.38
4/30/2020	692.92				2,285.31
5/31/2020	692.92				2,031.75
6/30/2020	692.92			6.77	2,031.75
7/31/2020	692.92				2,031.75
8/31/2020	692.92				2,155.38
9/30/2020	692.91			7.39	2,031.12
10/31/2020	692.91				2,031.12
11/30/2020	692.91				2,031.12
12/31/2020	692.91	8,315.00		8.08	2,152.23
Dec 2020 Depr					2,030.49
Total CIAC		68,274.12		333.86	214,109.39

Labor Savings Total		68,274.12
Interest		333.86
Depreciation Total		214,109.39
Well 10 use Depr	(129,823.96)	
Well 10 Use Lbr Savings	(40,140.08)	(169,964.04)
Net Total		112,753.33
Balance in Acct 127.1		112,753.33
		0.00
Total of Labor Savings Deposits		68,274.12
Total Used of Labor Savings Deposits		(40,140.08)
Remaining Balance of Labor Savings		28,134.04
Remaining Balance of Depreciation		84,619.29