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Addendum StartPage: 0

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APPLICATION OF MONARCH
UTILITIES I, L.P. FOR AUTHORITY
TO CHANGE RATES

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PUBLIC UTILITY COMMISSION
OF TEXAS

PRELIMINARY ORDER

Monarch Utilities I L.P., filed an application to change its water and sewer rates. This preliminary order identifies the issues that must be addressed in this proceeding.

I. Overview

On July 15, 2020, Monarch filed a class A application under Texas Water Code (TWC) § 13.187 to change its water and sewer rates based on a test year ending on December 31, 2019, adjusted for known and measurable changes.¹ Monarch provides water service within the service area of its water certificate of convenience and necessity (CCN) number 12983 and provides sewer service within the service area of its sewer CCN number 20899.²

In its application, Monarch states it provides utility service through its ownership and operation of 115 water utility systems with approximately 30,000 customers in 32 counties, and 12 sewer utility systems with approximately 4,400 customers in nine counties.³ The water and sewer rates proposed by Monarch include systems for which its acquisition have not been approved by the Commission. Monarch states that it has acquired seven water and sewer systems; several were purchased, the others were transferred from affiliates. Three applications to approve a transfer are currently pending.⁴

In this proceeding, Monarch seeks an increase in its annual revenue requirement of \$3,238,879 for water service and \$647,367 for sewer service.⁵ Monarch asserts that it has only one comprehensive customer class and has developed a comprehensive cost of service and revenue

¹ Application at 2 (Jul. 15, 2020).

² *Id.* at 3.

³ Application at 1.

⁴ Application at 000104–000105, Direct Testimony of George Freitag at 11–12.

⁵ *Id.* at 2.

requirement for providing water and sewer service for all of its customers. Monarch further asserts that consolidated rates were designed that will eventually be uniform for all of its customers.⁶

Phased-in rates are proposed for some of Monarch's newly acquired systems to moderate the rate increase. Monarch also proposes a consolidated tariff for its water systems and a consolidated tariff for its sewer systems.⁷ Monarch requests that all customers be subject to common service rules and common miscellaneous fees, including the meter-relocation fee, meter-conversion fee, seasonal reconnect fee, and supplemental emergency fee.⁸ To implement uniform tariffs, Monarch proposes that certain fees and charges be added, deleted, or modified from some individual system's current tariffs.

Monarch also requests changes to its pass-through mechanisms for purchased water and sewer service,⁹ increasing new-service tap fees for standard water and sewer residential taps,¹⁰ and the addition of a system-improvement-charge mechanism in both its water and sewer tariffs.¹¹ Monarch also proposes adding language to its sewer tariffs regarding the pretreatment of non-standard wastes, a change to its default winter average sewer usage from 5,000 gallons per month to 4,000 gallons per month, and clarifying ownership and responsibility for maintenance of on-site pressure wastewater units.

II. Procedural History

In Order No. 3 filed on August 18, 2020, the administrative law judge (ALJ) found Monarch's application and notice sufficient.¹² Additionally, the ALJ suspended the effective date for all proposed rates through the pendency of this proceeding.

Commission Staff requested referral of this proceeding to the State Office of Administrative Hearings (SOAH) under TWC § 13.187(f).¹³ In the order of referral to SOAH filed on August 31, 2020, Monarch was directed, and Commission Staff and other interested persons

⁶ Application at 000104, Direct Testimony of George Freitag at 10.

⁷ *Id.* at 000103, Direct Testimony of George Freitag at 9–10.

⁸ *Id.* at 000113, Direct Testimony of George Freitag at 19.

⁹ Application at 000090, Direct Testimony of Brian Bahr at 22–24.

¹⁰ Application at 000113, Direct Testimony of George Freitag at 19.

¹¹ Application at 000085, Direct Testimony of Brian Bahr at 17–21.

¹² Order No. 3 (Aug. 18, 2020).

¹³ Commission Staff's Comments on Administrative Completeness and Proposed Procedural Schedule (Aug. 14, 2020).

were allowed, to file by September 9, 2020 a list of issues to be addressed in this docket and also identify any issues not to be addressed and any threshold legal or policy issues that should be addressed. Monarch and Commission Staff each timely filed a list of issues.

III. Issues to be Addressed

The Commission must provide to the ALJ a list of issues or areas to be addressed in any proceeding referred to SOAH.¹⁴ After reviewing the pleadings submitted by the parties, the Commission identifies the following issues that must be addressed in this docket:

Applicant

1. What is the legal name and all assumed names, if any, of the applicant in this proceeding? If the utility has an assumed name, provide a currently valid certificate of assumed names.
2. What is the business form of the utility (e.g., corporation, partnership, sole proprietorship)? What is the charter or authorization number, the date the business was formed, and the dates any changes were made?
3. What is the proper legal name of the utility that currently holds CCN number 12983? In answering this issue, please identify who owns the equipment and facilities used to provide water service under CCN number 12983. Who operates such equipment and facilities?
4. If a combination of entities constitutes the entity seeking the water rate change, which entities should be joined in this proceeding in accordance with 16 TAC § 22.104(a)?
5. What is the proper legal name of the utility that currently holds CCN number 20899? In answering this issue, please identify who owns the equipment and facilities used to provide sewer service under CCN number 20899. Who operates such equipment and facilities?
6. If a combination of entities constitutes the entity seeking the sewer rate change, which entities should be joined in this proceeding in accordance with 16 TAC § 22.104(a)?
7. Did the utility seeking the rate increase file its annual report as required by TWC § 13.136 and 16 TAC § 24.129?

¹⁴ Tex. Gov't Code § 2003.049(e).

Notice of Intent

8. Did the utility provide proper notice of the proposed rate change to each customer or other interested party as required by TWC § 13.187(a-1) and (b) and 16 TAC § 24.27?

Revenue requirement

9. What revenue requirement will give the utility a reasonable opportunity to earn a reasonable return on its invested capital used and useful in providing service to the public in excess of its reasonable and necessary operating expenses while preserving the utility's financial integrity as required by TWC § 13.183(a)(1) and (2) and 16 TAC § 24.43(a)?
10. Does the revenue requirement properly offset from the utility's cost of service any revenue that is properly recognized for ratemaking purposes?
11. What is the appropriate portion of this revenue requirement that should be used to design the utility's water rates?
12. What is the appropriate portion of this revenue requirement that should be used to design the utility's sewer rates?

Cost of Service

13. What is the utility's cost of service for providing water service based on its test year?
14. What is the utility's cost of service for providing sewer service based on its test year?
15. What adjustments, if any, should be made to the utility's proposed test-year data in accordance with TWC § 13.185(d)(1) and 16 TAC § 24.41(b) and (c)(5)?
16. Are water or sewer systems included in this proceeding where the application to approve the transfer to Monarch has not been approved? If so, is it appropriate to include those systems in Monarch's cost of service in this proceeding?

Allowable Expenses

17. What are the reasonable and necessary allowable expenses for water service and for sewer service under 16 TAC § 24.41(b)? For issues 17 through 28, please specify the amount for water service and sewer service separately.
18. What is the utility's reasonable and necessary operations and maintenance expense?

19. What is the reasonable and necessary depreciation expense?
 - a. For each class of property, what are the proper and adequate depreciation rates and methods of depreciation, including service lives and salvage values?
 - b. Does this expense item contain any amounts related to property provided by explicit customer agreements or funded by customer contributions in aid of construction? If so, what are those amounts?
 - c. Does this expense item contain any amounts related to property contributed by a developer or governmental entity? If so, what are those amounts?
20. What is the reasonable and necessary expense for franchise fees, assessments, and taxes other than federal income taxes?
21. What is the reasonable and necessary amount for the utility's federal income tax expense?
 - a. Is the utility a member of an affiliated group that is eligible to file a consolidated income tax return under TWC § 13.185(f)?
 - b. If so, have income taxes been computed as though a consolidated return had been filed and the utility had realized its fair share of the savings resulting from the consolidated return as required by TWC § 13.185(f)?
 - c. If not, has the utility demonstrated that it was reasonable not to consolidate returns consistent with TWC § 13.185(f)?
22. Are any tax savings derived from liberalized depreciation and amortization, investment tax credits, or similar methods? If so, are such tax savings apportioned equitably between customers and the utility, and are the interests of present and future customers equitably balanced?
23. What is the reasonable and necessary amount for the utility's professional or trade association expense?
24. What is the reasonable and necessary amount for the utility's advertising expense, contributions, and donations?
25. If the utility has a self-insurance plan approved by the Commission or other regulatory authority, what is the approved target amount for the reserve account, and is it appropriate to change that amount? What is the amount of any shortage or surplus for the reserve account,

and what actions, if any, should be taken to return the reserve account to the approved target amount?

26. What are the utility's reasonable and necessary expenses, if any, for pension and other post-employment benefits?
27. Has the utility made any payments to affiliates for any expense item? If so, please address the following items.
 - a. Is the payment for each expense item reasonable and necessary?
 - b. What were the costs to the affiliate of each item or class of items in question?
 - c. Is the price to the utility for each item or class of items no higher than prices charged by the supplying affiliate to its other affiliates or divisions or unaffiliated entities for the same item or items?
 - d. If the payment to the utility is for an allocated expense, is the method used to allocate costs attributable to the utility and the utility's affiliates appropriate to ensure just and reasonable rates?
28. Are any requested expenses not allowed under 16 TAC § 24.41(b)(2)?

Capital Structure and Total Return

29. What is the appropriate debt-to-equity capital structure for the utility for the purpose of setting rates?
30. Does the utility have any debt? If so, what is the cost of that debt?
31. What is the appropriate overall rate of return (weighted cost of capital), including return on equity and cost of debt for the utility, consistent with 16 TAC § 24.41(c)(1)?

Rate Base (Invested Capital)

32. What are the reasonable and necessary components of the utility's rate base in accordance with 16 TAC § 24.41(c)? For issues 32 through 43, please specify the amount for water service and sewer service separately.
33. Has any rate-base item been acquired from an affiliated interest? If so, then address the following:
 - a. Is each such item used and useful in providing service to the utility's customers?

- b. Is the payment for each item reasonable and necessary?
 - c. What were the costs to the affiliate of each item or class of items in question?
 - d. Is the price to the utility for each item or class of items no higher than prices charged by the supplying affiliate to its other affiliates or divisions or unaffiliated entities for the same item or items?
 - e. If the payment to the utility is for an allocated share of the cost, is the method used to allocate costs attributable to the utility and the utility's affiliates appropriate to ensure just and reasonable rates?
34. What is the original cost of the property used and useful in providing service to the public at the time the property was dedicated to public use under TWC § 13.185(b) and 16 TAC § 24.41(c)(2)(A) and (B)?
35. What is the amount, if any, of accumulated depreciation on such property and the resulting net cost?
36. What is the amount for an allowance for funds used during construction, if any, that is being transferred to invested capital in this proceeding? If such amounts are being transferred, for what facilities and when was each facility placed into service. At what rate did the allowance for funds used during construction accrue?
37. Is the utility seeking inclusion of construction work in progress? If so, what is the amount sought and for what facilities? Additionally, has the utility proven that the inclusion is necessary to the financial integrity of the utility and that major projects under construction have been efficiently and prudently planned and managed as required by 16 TAC § 24.41(c)(4)?
38. What is the reasonable and necessary working capital allowance for the utility under 16 TAC § 24.41(c)(2)(C)?
39. Does the utility have any utility property that was acquired from an affiliate or a developer before September 1, 1976? If so, has such property been included by the utility in its rate base, and has it been included in all ratemaking formulas at the actual cost of the property rather than the price set between the entities as required by TWC § 13.185(i)?

40. Has the utility financed any of its plant with developer contributions? What is the amount, if any, of accumulated depreciation on that property?
41. Has the utility included any customer contributions or donations in invested capital? If so, what is the amount of those customer contributions or donations?
42. What is the reasonable and necessary amount of the utility's accumulated reserve for deferred federal income taxes, excess deferred federal income taxes, unamortized investment tax credits, contingency reserves, property insurance reserves, contributions in aid of construction, customer deposits, and other sources of cost-free capital? What other items should be deducted from the utility's rate base?
43. What regulatory assets, if any, are appropriately included in the utility's rate base? If such assets are included in rate base, what is the appropriate treatment of such assets?

Allocation and Rate Design

44. Has each component of cost of service been properly assigned or allocated between water and sewer services?
45. What is the appropriate allocation of costs and revenues among the utility's rate classes for water service and for sewer service?
46. What is the appropriate rate design for water service and for sewer service for each rate class consistent with 16 TAC § 24.43?
47. In designing rates for water and sewer service, should the utility use the current number of connections as of the date of the application or the number of test-year-end connections?

Consolidated Tariffs

48. Does TWC § 13.145 apply to Monarch? In how many counties did Monarch provide utility service on January 1, 2003?
49. If TWC § 13.145 applies to Monarch, then
 - a. Are the systems included in the proposed consolidated water tariff substantially similar in terms of facilities, quality of service, and cost of service?
 - b. Does the proposed consolidated water tariff include rates that promote water conservation for single-family residences and landscape irrigation?

Rates

50. What are the just and reasonable rates for water service and for sewer service that are sufficient, equitable, and consistent in application to each customer class and that are not unreasonably preferential, prejudicial, or discriminatory under TWC §§ 13.182 and 13.187(h) and 16 TAC § 24.35(d)? Do these rates recover the utility's revenue requirement for each type of service?
51. Are the proposed phased-in rates reasonable and appropriate? 16 TAC § 24.75(b).
52. What is the appropriate effective date of the rates fixed by the Commission in this proceeding?

Tariffs

53. Are the utility's proposed revisions to its tariffs and rate schedules appropriate?
54. For each proposed tariff, does the tariff include and identify all applicable systems?

Interim Rates

55. Did the utility request interim rates? If so, has the utility met the requirements for interim rates? If so, what are the appropriate levels of the interim rates under 16 TAC § 24.37?
56. If a refund or surcharge results from this proceeding, how and over what period of time should the refund or surcharge be made?

Rate Case Expenses

57. What are the utility's expenses incurred in this rate proceeding that are just, reasonable, necessary, and in the public interest under 16 TAC § 24.44? Does that amount include any prospective rate-case expenses to be incurred after the Commission's final order? Should the utility be able to recover its reasonable and necessary rate-case expenses from ratepayers? If so, how should such expenses, if any, be recovered by the utility?
58. Is the utility's proposal to implement a surcharge to recover rate-case expenses from Docket No. 47736 appropriate in this proceeding? If so, does the proposed tariff language regarding the rate-case expenses for Docket No. 47736 comply with the Commission's order in Docket No. 47736?
59. How should rate-case expenses be allocated between customers?

Pass-through rates

60. Has the utility requested to include costs in its pass-through rates for an entity for which it has also requested to recover costs through its base rates? If so, please identify the entity, the amount of costs, and what products or services the costs cover.
61. Do the utility's proposed pass-through rates include only the actual costs charged to the utility?
62. Do the proposed pass-through rates exclude any charges that are included in the utility's requested cost of service in this docket?
63. Does the utility's pass-through provision in its tariffs conform to Commission rules and is it appropriately worded?

Tax Cut and Jobs Act of 2017

64. Did the utility properly account for the effects of the Tax Cuts and Jobs Act of 2017? *Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018*, Pub. L. No. 115-97, 131 Stat. 2054 (Dec. 22, 2017).
65. Is Monarch's request to cease monthly refunds related to the Tax Cut and Jobs Act appropriate?

This list of issues is not intended to be exhaustive. The parties and the ALJ are free to raise and address any issues relevant in this docket that they deem necessary, subject to any limitations imposed by the ALJ, or by the Commission in future orders issued in this docket. The Commission may identify and provide to the ALJ in the future any additional issues or areas that must be addressed, as permitted under Tex. Gov't Code Ann. § 2003.049(e).

IV. Issues Not to be Addressed

The Commission identifies the following issue that need not be addressed in this proceeding for the reasons stated.

1. Monarch's request for a mechanism to implement a system improvement charge mechanism in its water and sewer tariffs.

TWC § 13.183 was recently amended to authorize the Commission to "adopt system improvement charges," including establishing a schedule by rule to require utilities to make periodic filings "to modify or review base rates charged by the utility." The Commission has opened Project No. 50322, *Alternative Ratemaking Mechanisms for Water and Sewer Utilities*, to

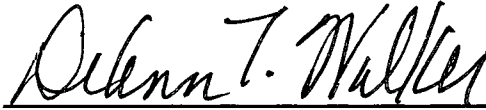
address system improvement charges, but has not yet proposed a rule. Adoption of a new rate mechanism should be in a rulemaking proceeding. This type of proceeding will allow input by all interested persons and will better inform the Commission of all concerns that should be addressed. Considering whether to adopt a mechanism for a single utility, Monarch, to implement a system improvement charge in this docket will not have that broad-based information. Such a mechanism is likely to differ from a mechanism adopted in a formal rulemaking. Thus, the mechanism would have to be conformed to the Commission's rule in a future proceeding. This would not be an efficient use of resources for anyone. Accordingly, Monarch's proposed tariff mechanism for a system improvement charge should not be addressed in this docket.

V. Effect of Preliminary Order

The Commission's discussion and conclusions in this Order regarding issues that are not to be addressed should be considered dispositive of those matters. Questions, if any, regarding issues that are not to be addressed may be certified to the Commission for clarification if the SOAH ALJ determines that such clarification is necessary. As to all other issues, this Order is preliminary in nature and is entered without prejudice to any party expressing views contrary to this Order before the SOAH ALJ at hearing. The SOAH ALJ, upon his or her own motion or upon the motion of any party, may deviate from the non-dispositive rulings of this Order when circumstances dictate that it is reasonable to do so. Any ruling by the SOAH ALJ that deviates from this Order may be appealed to the Commission. The Commission will not address whether this Order should be modified except upon its own motion or the appeal of a SOAH ALJ's order. Furthermore, this Order is not subject to motions for rehearing or reconsideration.

Signed at Austin, Texas the 24th day of September 2020.

PUBLIC UTILITY COMMISSION OF TEXAS



DEANN T. WALKER, CHAIRMAN



ARTHUR C. D'ANDREA, COMMISSIONER



SHELLY BOTKIN, COMMISSIONER