

**PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: December 18, 2007**

REGULAR X CONSENT _____ EFFECTIVE DATE _____ N/A _____

DATE: December 10, 2007

TO: Public Utility Commission

FROM: Michael Dougherty

THROUGH: Lee Sparling and Marc Hellman

SUBJECT: OREGON PUBLIC UTILITY COMMISSION STAFF: Request for the Commission to open an investigation into proposed sewer rates of Aegis Round Lake Sewer Company LLC and current water rates of RL Water LLC.

STAFF RECOMMENDATION:

Pursuant to ORS 756.515, Staff requests that the Commission open an investigation of the proposed sewer rates of Aegis Round Lake Sewer Company LLC (Aegis) and current water rates of RL Water LLC. In addition, the Commission should treat the proposed sewer rate of \$55 and water rate of \$25 as interim rates subject to refund based on the results of Staff's investigation.

DISCUSSION:

The owner of Aegis is also the owner of RL Water LLC (RL Water or Company). RL Water is a small investor-owned water utility located in the vicinity of Klamath Falls, Oregon. RL Water provides water to approximately 62 residential customers, one commercial customer (Recreational Vehicle (RV) Park), and one irrigation customer, Round Lake Golf Course. The current owner, Carol Lin, purchased the water system, sewer system, golf course, and RV Park on April 27, 2004.

Aegis is currently listed as an inactive entity by the Secretary of State (SOS). Additionally, the SOS's Business Registry lists Aegis as filing an administrative dissolution on August 31, 2007. When Staff contacted the owner of RL Water and Aegis, she was not aware of the inactive status.¹ This lack of knowledge of Aegis'

¹ Subsequent to Staff's notification to the Company of the Administrative Dissolution, the Company on November 28, 2007, filed a "Reinstatement Amended" with the Secretary of State (SOS). The SOS has

status may indicate that RL Water and Aegis are acting as one company and are only separated to avoid regulation and allow for cross subsidies. As such, Staff believes that the sewer rates of Aegis may be cross-subsidizing the water rates and may also be subject to the Commission's jurisdiction.

RL Water Regulation

RL Water was brought under PUC rate regulation by the customer petition process, Order No. 05-145 (WJ 1) dated March 25, 2005. The Company filed tariffs on October 31, 2005, (UW 111/Advice 05-39) requesting to increase annual revenues by \$106,143, or 79 percent above the Company's 12 month revenues ending May 31, 2005.² The Commission entered Order No. 05-1226 suspending the tariff sheets for six months. The Company's rate application was solely for its water rates as the Company had established a separate entity for sewer service, Aegis, on August 31, 2005.

During Staff's rate review, RL Water was unable to adequately provide test year documentation. As a result, in Commission Order No. 06-128, the tariff sheets were suspended for an additional three months on March 17, 2006. Even with the additional time granted by the Commission, the Company could not meet the requirements of Staff's data requests. On April 19, 2006, RL Water moved for an order closing UW 111 so that it could analyze and prepare the data necessary to support a future application for ratemaking and a rate increase. The Commission granted this request in Commission Order No. 06-212, dated May 2, 2006.

The Company never filed a subsequent rate application. Because RL Water's current flat residential rate of \$25 was lower than the Company's proposed rates and most likely lower than a rate that would have been proposed by Staff, Staff did not request the Commission to order RL Water to file a new rate application. Staff believed that the lower rate would continue to benefit customers. Additionally, Staff was hopeful that prudent utility management would result in RL Water filing an accurate rate application once the Company gathered quality information concerning its cost-of-service.

coded the Reinstatement as "NF", which states "Nonfilable. These transactions are not yet filed for various reasons." As a result, the Company will have to refile with SOS, pay a fee for refiling, and pay a fee for bringing the record to date.

² The Company appeared to have miscalculated its requested percentage increase. Staff's review calculated the percentage increase, based on the Company's test year and proposed revenues, as a 376 percent overall increase.

Aegis

As previously mentioned, the owner of RL Water separated the water system and sewer system into two distinct entities. Because Aegis was not a water utility as defined by ORS 757.061, Staff did not investigate the sewer system revenues, operating expenses, and plant during UW 111, with the exception to ensure that the water rates were not cross-subsidizing the sewer rates.

Because of Staff's concern over the two entities, Staff requested advice from the Attorney's General office concerning jurisdiction over wastewater utilities. On January 18, 2006, the assistant attorney general provided a memorandum concerning regulation of wastewater utilities. The memorandum concluded with the following:

"In conclusion, the Commission does not generally have authority over a wastewater company that does not also provide water service. Thus, the Commission does not have jurisdiction over separate wastewater companies unless it can demonstrate that the companies are not, in fact, separate but, instead, are one company and only separated to avoid regulation and allow for cross subsidies."

In a recent letter to customers, the Company sent 2008 payment coupon books to customers reflecting the continuation of the \$25 per month water rate, but an increase in the sewer rate from the current \$42 per month to a new rate of \$55 per month.

Staff believes Aegis and RL Water are operating as one entity

As previously discussed, the SOS Business registry on November 28, 2007, lists Aegis as inactive and administratively dissolved on August 31, 2007. When Staff contacted the owner of RL Water and Aegis, she was not aware of the inactive status. This lack of knowledge of Aegis' status appears to indicate that RL Water and Aegis are acting as one company and are only separated to avoid regulation and allow for cross subsidies.

The timing of the establishment of Aegis, after the jurisdiction order and prior to RL Water's rate filing, also suggests that the two companies were only separated to avoid regulation and allow for cross subsidization of water rates.

Additionally, RL Water experienced numerous outages and system quality problems during the summer and fall of 2007. These outages required amongst other things: the provision of bottled water, boiled water notices, installation of a continuous feed chlorinator, installation of a booster pump, installation of a pressure sustaining valve, repair of the well pump, repair of system leaks, increased chemical testing of the

system, and numerous system flushing. These numerous problems resulted in the coordinated efforts of Commission Staff, Drinking Water Program Staff, and the Klamath County Department of Public Health to bring the Company into compliance with water quality standards.

Being that all of the above improvements resulted in considerable costs to RL Water and RL Water has not filed for a rate increase, Staff believes the Company may be subsidizing the water improvements through the increased sewer rate.

On December 6, 2007, Staff separately met with both the Company and customers of RL Water in Klamath Falls, Oregon. Among other topics, the sewer rate and its potential relationship to the water rates and water system repairs were discussed. The Company and customers were made aware that Staff intended to request the Commission to open an investigation into the proposed sewer rates of Aegis and current water rates of RL Water. Although each group had differing views of the subject, no objections to Staff's intent were raised at the two meetings.

PROPOSED COMMISSION MOTION:

Pursuant to ORS 756.515, Staff requests that the Commission open an investigation of the proposed sewer rates of Aegis Round Lake Sewer Company LLC (Aegis) and current water rates of RL Water LLC. In addition, the Commission should treat the proposed sewer rate of \$55 and water rate of \$25 as interim rates subject to refund based on the results of Staff's investigation.