

SUBJECT: Revising water utility rate and service regulations

COMMITTEE: Natural Resources — committee substitute recommended

VOTE: 8 ayes — Counts, T. King, Cook, Corte, Hope, R. Lewis, Puente, Walker

0 nays

1 absent — Hilderbran

WITNESSES: For — Jacqueline M. Croy, City of Houston; Danny R. Edwards, City of Ingram

Against — Jim Boyles, Tecon Water Cos.; James Lahtinen and Roy H. Moore, AquaSource; David L. Wallace, Diamond Water Co. and Water Services Inc.; Mark Zeppa

On — Janee Briesemeister, Consumers Union; Doug Holcomb and Irene Montelongo, Texas Natural Resource Conservation Commission

BACKGROUND: In the past few years, larger utilities have begun to acquire many small, privately owned water and sewer utilities. Most of the acquired utilities serve rural and unincorporated areas of Texas. In some cases, an acquiring utility has set uniform rates for customers of separate systems in the same region. Recently, a company has sought to consolidate all of the rate schedules for its systems across the state under a single uniform rate schedule or tariff.

Water Code, ch. 13 governs the regulation of water and sewer utilities. The Texas Natural Resource Conservation Commission (TNRCC) has the authority to regulate and supervise the business of every water and sewer utility within its jurisdiction. The governing body of a municipality has exclusive original jurisdiction over water and sewer services within the incorporated limits of the municipality.

The regulatory authority — TNRCC or the municipal governing board — can fix and regulate utility rates. Water Code, sec. 13.185 sets forth rules for

calculating utility rates on the basis of the utility's return on invested capital. Under sec. 13.183(c), to ensure that retail customers receive a higher quality or more reliable water or sewer service, the regulatory authority may develop ratemaking methodologies based on other factors than rate of return. Also, TNRCC rule 291.31(d) allows utilities to recover acquisition adjustments — costs incurred in purchasing a utility — for facilities acquired after September 1, 1997, through service rates under certain conditions.

DIGEST:

Payment location. CSHB 1281 would require every water utility to make available and notify customers of a location where they could make payments to prevent disconnection or to restore service in each county where the utility provided service or within 20 miles of any residential customer's residence. TNRCC could waive these requirements by rule for a utility that would have to impose a rate increase or otherwise harm or inconvenience customers to comply with the requirements. The rules would have to require a utility that received a waiver to give a customer an additional 14 days to pay before disconnecting service for late payment.

Multiple systems consolidated under tariff. A utility could consolidate multiple systems under a single tariff only if the systems were substantially similar in facilities, quality of service, and cost and if the schedule provided for rates that promoted water conservation for single-family residences and landscape irrigation.

TNRCC would have to establish by rule a preference that rates under a single schedule be consolidated by region. Regions under consolidated tariffs would have to be determined on a case-by-case basis.

Alternative ratemaking methodology. A regulatory authority could adopt an alternative ratemaking methodology by rule or ordinance to help make water or sewer service more affordable, in addition to the criteria in current law. The authority could not approve rates under an alternative methodology unless it adopted the methodology before the administrative completion of the rate application.

A municipal governing board could not approve an acquisition adjustment for a system purchased before the effective date of an ordinance authorizing such adjustments.

Statement of intent to change rates. CSHB 1281 would extend from 30 to 60 days the period that a utility would have to wait to implement new rates after filing a statement of intent to change rates. The utility also would have to deliver a statement of intent to each ratepayer that included:

- ! a billing comparison of the existing and new water rates for the use of 10,000 and 30,000 gallons of water, and
- ! a billing comparison of the existing and new sewer rates for the use of 10,000 gallons, unless the utility proposed a flat rate.

If a regulatory authority received a complaint from an affected municipality or from the lesser of 1,000 or 10 percent of the utility's ratepayers within 90 days (rather than 60 days) of the rate change, it would have to set the matter for hearing. Upon receiving sufficient complaints to set a hearing, the regulatory authority could suspend the effective date of the rate change. The change could not be suspended for longer than 90 days by the governing board of a municipality or longer than 150 days by TNRCC.

The regulatory authority could require a utility to refund money collected under a proposed rate before it was suspended or an interim rate was established, to the extent that the proposed rate exceeded the existing or interim rate. If a municipal governing body established interim rates or an escrow account, it would have to make a final determination on the rates within one year (rather than 335 days) of their effective date.

Wholesale water-supply contracts. An owner of a utility that supplied retail water service could not purchase wholesale service from an affiliated supplier unless:

- ! the wholesale service was provided for no more than 90 days to remedy an emergency situation, or
- ! the TNRCC executive director determined that the utility could not obtain wholesale service from another source at a lower cost than the affiliate.

The utility could not purchase groundwater if its source was located in a priority groundwater management area and a wholesale supply of surface water was available.

An entity providing wholesale water to a retail public utility would have to disclose to TNRCC any affiliated interest between the parties to the wholesale water-supply contract.

CSHB 1281 would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2001. It would apply only to proceedings in which TNRCC had not issued a final order before the bill's effective date. The requirements for wholesale water contracts between certain affiliates would not apply to contracts executed before the effective date.

**SUPPORTERS
SAY:**

CSHB 1281 would set needed limits on a water utility's ability to impose a statewide water rate. In rate cases before TNRCC, utilities have applied to impose a single tariff for thousands of customers of many systems in different regions. According to some estimates, one such case would raise rates by an average 29 percent for 35,000 customers across hundreds of systems, some of which would experience a 200 percent increase.

The bill would allow consolidation of similar systems and would encourage regional consolidation. Customers could benefit from consolidation without having to subsidize rates for customers on the other side of the state. For example, customers along the Gulf Coast would share costs of improvements to systems in their area but would not have to pay for improvements to systems in West Texas. Determining what systems were sufficiently similar to warrant consolidation would not burden small independent utilities, but it would require larger utilities to provide more research and information on a proposed consolidation during rate proceedings.

The bill would allow the regulatory authority to suspend implementation of a proposed rate change if enough complaints were received. If the proposed rate change was rejected, customers would not have to pay any part of the increase, as they would if an interim rate had been imposed.

CSHB 1281 would give municipalities and customers more time to protest rate increases. Under current law, a municipality has only 30 days from the date it receives a statement of intent to change rates to do everything required to act on the rate change, including hiring staff to research the proposed change, posting notice of and holding a public hearing, and convening city council meetings. This is especially difficult in municipalities where the city council meets only once a month. The bill would establish a more reasonable time frame for municipalities to study and act on proposed rate increases.

The bill also would require utilities to provide a reasonably close location where customers could make payments on their accounts. Many customers have been inconvenienced severely when their service was cut off and no location within a reasonable distance was available where they could make payment.

CSHB 1281 would require utilities to provide customers with a billing comparison for a proposed rate change. Currently, customers are notified only that their rates will change. A billing comparison would allow customers to know how much their utility bills would increase under a new rate.

Requiring systems to be interconnected or in contiguous areas in order to warrant consolidation would be too restrictive. It is extremely expensive to interconnect systems and would not be realistic for many small and isolated rural systems.

**OPPONENTS
SAY:**

CSHB 1281 would limit the benefits of consolidation encouraged under SB 1, Texas' landmark water legislation enacted in 1997. Statewide water rates allow utilities that operate multiple systems to spread the cost for single-system capital improvements among all their customers. Under the proposed bill, water utilities could not use these economies of scale to minimize the costs of capital improvements for individual system customers. Customers of smaller systems needing capital investment could see astronomical increases in their monthly water bills to finance improvements.

CSHB 1281 could require water utilities to establish separate tariffs for every system they operated. This would be especially burdensome and

inefficient for utilities that operate many systems, as they would have to file separate rate cases and maintain a separate set of books for each system. According to water utilities, more than half of all systems in Texas have fewer than 200 customers, and more than 80 percent have 2,000 customers or fewer.

The bill would add an administrative burden to rate proceedings and would create uncertainty for utilities. Determining what systems were sufficiently similar to warrant consolidation would require a lengthy hearing process at some point in the rate proceedings. Utilities would not know which of their systems they could consolidate until the proceeding was completed. Also, because most municipalities have not adopted acquisition-adjustment ordinances, the bill would virtually eliminate municipalities' ability to authorize rate adjustments for acquired facilities.

OTHER
OPPONENTS
SAY:

CSHB 1281 would not go far enough in establishing criteria for prohibiting the consolidation of multiple systems under a single tariff. The bill should allow consolidation only for systems that are interconnected or in contiguous areas, and it should set a maximum number of systems, such as 20, that could be consolidated under a single tariff. Approval of a single tariff for multiple systems should require that the rate promote conservation for all customer classes, not just for single-family residences and landscape irrigation.

NOTES:

The committee substitute made many changes to the original bill, including:

- ! requiring a utility to maintain a business location in each county where it provides service or within 20 miles of a residential customer;
- ! changing the requirements for consolidating multiple systems under a single tariff;
- ! requiring TNRCC to establish by rule a preference that rates under a consolidated tariff be consolidated by region;
- ! preventing a regulatory authority from approving an application for an alternative methodology to determine rates unless it had adopted the methodology before the end of the rate proceeding, instead of the beginning;
- ! eliminating a provision in the filed version that would prohibit a uniform rate across unconnected systems or alternative methodologies that

allowed revenues from customers of one system to subsidize improvements or service in others;

- ! eliminating the provision in the original version for determining costs under an alternative methodology;
- ! prohibiting a regulatory authority other than TNRCC from approving an acquisition adjustment for a system purchased before the effective date of an ordinance authorizing acquisition adjustments;
- ! requiring a statement of intent to change rates to be delivered at least 60 days before the effective date of the proposed change and to include a billing comparison of the existing and new rates;
- ! allowing a regulatory authority to suspend a proposed rate for certain periods if it received sufficient complaints and to require a utility to refund money collected under a proposed or interim rate before it was suspended;
- ! extending prohibitions in the original version on wholesale water contracts between certain affiliates to all utilities that supply retail water service; and
- ! prohibiting a utility from purchasing groundwater under certain conditions.