

Applicant's first application for a rate increase since its current rates were approved in Order No. 15985, filed on September 30, 1997, in Docket No. 7576.¹ Applicant states that since 1997, operating expenses have increased more quickly than operating revenues, such that Applicant's current revenues are insufficient to allow it to recover its operating and depreciation expenses.² If approved, Applicant's rates will increase by approximately 126.5 percent (126.5%) over existing rates.³

B.

Applicant's existing and proposed rates are as follows:

	<u>Present</u>	<u>Proposed</u>
Residential (single-family and condominiums) (monthly service charge per customer)	\$34.00	\$77.00
Industrial (monthly service charge per customer)	Minimum service charge of \$77.00, plus sewer consumption charge of \$3.25 per every 1,000 gallons of metered domestic water consumption.	Minimum service charge of \$174.39, plus sewer consumption charge of \$7.3606 per every 1,000 gallons of metered domestic water consumption.
Commercial (monthly service charge per customer)	Minimum service charge of \$105.00, plus sewer consumption charge of \$1.95 per every 1,000 gallons of metered domestic water consumption.	Minimum service charge of \$237.80, plus sewer consumption charge of \$4.4164 per every 1,000 gallons of metered domestic water consumption.
Golf Course Irrigation	\$0.50 per every 1,000 gallons of metered domestic water consumption	None.

¹Order No. 15985 amended Decision and Order No. 13304, filed on June 14, 1994, in the same proceeding. Decision and Order No. 13304 set forth permanent rates for Puhi's wastewater service.

²See Application at 2-3.

³See Application at 3.

II.

Applicant

Puhi is a Hawaii corporation which has its principal place of business in Lihue, Kauai. It is a public utility providing wastewater collection and treatment services to residential, commercial and industrial customers within its authorized service territory. Puhi is a wholly-owned subsidiary of Grove Farm Properties, Inc., which is a wholly-owned subsidiary of Grove Farm Company, Inc. Applicant was granted authority to operate as a public utility by the commission, pursuant to Interim Decision and Order No. 12654, filed on October 7, 1993, in Docket No. 7576.⁴

As of June 30, 2003, Applicant's customer base consisted of 758 residential customers, 41 commercial customers and 23 industrial customers.⁵ Applicant also provides effluent to the Puakea Golf Course ("Golf Course").^{6,7}

III.

Procedural History

By Statement of Position Regarding Completeness of Application, filed on November 14, 2003 ("Objection Statement"),

⁴The Interim Decision and Order set forth interim rates pending a final decision by the commission on permanent rates for Puhi's wastewater service.

⁵See Application at 2.

⁶Id.

⁷The Golf Course is owned by Applicant's affiliate. See Application at 10.

the Consumer Advocate stated that the Application was not complete, pursuant to the requirements of HRS § 269-16(d). In order for the Application to be deemed complete, the Consumer Advocate stated that Applicant must provide information regarding: (1) the amount of bonds authorized and issued, pursuant to HAR § 6-61-75(a)(4); (2) the rate and amount of dividends paid during the five (5) previous calendar years, pursuant to HAR § 6-61-75(a)(7); and (3) an audited balance sheet, pursuant to HAR § 6-61-75(b)(1).

On November 17, 2003, Puhi filed a response to the Consumer Advocate's Objection Statement in which it stated that it does not have any authorized or issued bonds, that no dividends have ever been paid out by Puhi, and that an audited financial statement from its parent company would be filed as soon as a protective order was issued for the instant docket.⁸

On November 18, 2003, the commission issued Protective Order No. 20642, setting forth the procedures for handling privileged and confidential information that may be requested and/or filed in the instant docket.

⁸Pursuant to HRS § 269-16(d), the commission has nine (9) months within which to issue a final decision on a public utility's rate application. The nine-month period begins only after a completed application has been filed with the commission, and a copy served upon the Consumer Advocate. In the instant case, Puhi's Application was deemed complete on November 17, 2003, the date on which amendments to its Application were filed with the commission in response to the Consumer Advocate's Objection Statement. Thus, the nine-month period in which the commission must make a determination on the Application ends on August 17, 2004.

On November 24, 2003, the Consumer Advocate filed a letter with the commission informing the commission that Puhi's Application was deemed to be in compliance with the requirements set forth in Subchapter 6 of Chapter 61, the Commission's Rules of Practice and Procedure, HAR.

On November 18, 2003, the Parties submitted a letter informing the commission that they have agreed to waive their right to an evidentiary hearing ("Stipulation to Waive Hearing"). By Order No. 20687, filed on November 26, 2003, in the instant docket, the commission granted the Parties' Stipulation to Waive Hearing, pursuant to HAR § 6-61-35. See also HRS § 91-9.

On January 15, 2004, the commission held a public hearing on the Application at the Kukui Grove Park and Pavilion, Lihue, Kauai, pursuant to HRS §§ 269-12(c) and 269-16(b).

On February 12, 2004, the commission issued Stipulated Prehearing Order No. 20800 ("Stipulated Prehearing Order"), which established the issues and the procedural schedule in this docket. Pursuant to the Stipulated Prehearing Order, the Parties submitted the following discovery: (1) on February 13, 2004, the Consumer Advocate filed its submission of information requests ("IR"s) to Puhi; (2) Puhi filed responses to the Consumer Advocate's IRs on March 12, 2004; (3) on April 2, 2004, the Consumer Advocate filed supplemental IRs to Puhi; (4) on April 23, 2004, Puhi filed responses to the supplemental IRs; and (5) on May 21, 2004, the Consumer Advocate submitted Direct Testimonies, Exhibits, and Workpapers.

On June 2, 2004, the Parties notified the commission that they were engaged in ongoing discussions regarding the disputed issues and that the Parties had agreed to modify the procedural schedule in the instant matter.

On August 3, 2004, the Parties jointly filed their Stipulation of Settlement Agreement in Lieu of Rebuttal Testimonies, Evidentiary Hearing and Briefs ("Stipulated Agreement"). By the Stipulated Agreement, among other things, the Parties agreed to: (1) an increase in Puhi's revenues of \$449,392 for the test year; and (2) a revenue requirement of \$1,100,275 for the test year.

IV.

Stipulated Issues

As set forth in the Stipulated Prehearing Order, the stipulated issues are as follows:

1. Is Puhi's proposed rate increase reasonable?
 - a. Are the proposed tariffs, rates and charges just and reasonable?
 - b. Are the revenue forecasts for the Test Year ending December 31, 2004 at present rates and proposed rates reasonable?
 - c. Are the projected operating expenses for the Test Year reasonable?
 - d. Is the projected rate base for the Test Year reasonable, and are the properties included

in the rate base used or useful for public utility purposes?

e. Is the requested rate of return fair?

V.

A.

Stipulated Agreement - in General

At the outset, we view the Stipulated Agreement as an attempt by the parties to resolve all issues in this docket without holding an evidentiary hearing, pursuant to HAR § 6-61-35. HAR § 6-61-35 provides that "[w]ith the approval of the commission, any procedure in a contested case may be modified or waived by stipulation of the parties and informal disposition may be made of any contested case by stipulation, agreed settlement, consent order, or default." See also, HRS § 91-9.

We also recognize the Stipulated Agreement to be comprised of proposed agreements of the parties, which constitute a formal confirmation by them of a resolution of all issues in this docket. Specifically, the Stipulated Agreement states, in relevant part, that:

The Parties agree that the provisions of this Stipulation are binding as between them with respect to the specific issues and matters to be resolved in the subject docket. In all respects, it is understood and agreed that the agreements evidenced in this Stipulation represent compromises by the Parties to fully and finally resolve all issues in the subject docket on which they had differences for the purpose of simplifying and expediting this proceeding, and are not meant to be an admission by either of the Parties as to the acceptability or permissibility of matters stipulated to herein. The Parties

reserve their respective rights to proffer, use and defend different positions, arguments, methodologies, or claims regarding the matters stipulated to herein in other dockets or proceedings. Furthermore, the Parties agree that nothing contained in this Stipulation shall be deemed to, nor be interpreted to, set any type of precedent, or be used as evidence of either Parties' position in any future regulatory proceeding, except as necessary to enforce this Stipulation.

The Stipulated Agreement also confirms the Parties' understanding and acknowledgment that the commission "is not bound by this [Stipulated Agreement] between the Parties, and that the settlement is subject to the review and approval of the [c]ommission".

In considering the Stipulated Agreement, the commission has the independent obligation, after reviewing it, to determine if the provisions of the Stipulated Agreement are reasonable and in the public interest. While we strive to respect the basic underlying agreements and conditions made by the Parties as expressed in the Stipulated Agreement, we must, given our statutory responsibilities, undertake an independent review to, among other things, ensure that the interests of the public (particularly Applicant's customers affected by the rate increase) are protected.

Upon our review, we find the proposed agreements and conditions set forth in the Parties' Stipulated Agreement to be reasonable and in the public interest. We also find that our approval of the Stipulated Agreement in its entirety will assist in expediting and facilitating the ratemaking process. Accordingly, we conclude that the proposed agreements and

conditions set forth in the Stipulated Agreement should be approved in their entirety and made a part of this decision and order.

The Parties should be advised, however, that commission review and approval of the Stipulated Agreement is based primarily on the Parties' representation that there are no remaining differences in this proceeding and that the Parties desire to resolve and dispose of the entire case by means of the Stipulated Agreement. Accordingly, our approval of the Stipulated Agreement in its entirety shall not be used or cited by any party or person as precedent in any other proceeding before the commission or before any court of law for any purpose, except in furtherance of the purposes and results of the Stipulated Agreement. As discussed below, we will from time to time state in this decision and order that the stipulated estimates are either reasonable or acceptable. Such statements shall not be read or construed as necessarily approving the methodology by which the stipulated estimates were derived, and the commission will, therefore, not be bound by the stipulated estimates in future rate cases.

B.

Summary of Proposed Agreements and Conditions of Stipulated Agreement

As shown in Exhibit A of the Application, the Stipulated Agreement results in a revenue requirement for Applicant of \$1,100,275 for the Test Year (consisting of \$867,967

in total operating expenses and \$232,308 in operating income), based upon a stipulated 8.85 percent (8.85%) rate of return on Applicant's stipulated rate base amount of \$2,624,959. This amounts to a revenue increase of \$449,392, or approximately 69 percent (69%). The result of the Stipulated Agreement allows Puhi an opportunity to recover its operating expenses and operating income under the settlement terms.

Once settlement was reached on the Test Year revenue requirement, the Parties settled on the issue of rate design. The agreed-upon rate design allows for a 3-year phase-in of the rate increase to address potential rate shock issues as they would affect Puhi's existing customers, while still providing a reasonable opportunity for Applicant to earn the Test Year revenue requirement of \$1,100,275 beginning in the last year of the phase-in period.

VI.

Revenues

In its Application, Applicant sought a Test Year revenue requirement of \$1,156,816. The Consumer Advocate proposed a Test Year requirement amount of \$659,303. The Parties agreed to a Test Year revenue requirement of \$1,100,275. To reach this agreement, the Parties first had to determine the Test Year revenues at present rates, and what, if any Test Year revenues should be attributed to Applicant's provision of effluent to the Golf Course.

A.

Revenues at Present Rates

Applicant originally began with a Test Year revenue amount at present rates of \$560,151. In response to discovery requests from the Consumer Advocate, Applicant adjusted this figure by updating its Test Year customer counts, water use figures and/or resulting wastewater revenue projections to arrive at a Test Year revenue amount at present rates of \$658,446. The Consumer Advocate reduced this amount by taking into account various factors, including eliminating the monthly customer fee that was expected to be received from five (5) new commercial establishments, reducing the number of hookups in the Test Year by three (3), and reducing the industrial customer account by one (1) to remove a duplicate counting. The result of the Consumer Advocate's proposed adjustments was a \$7,562 reduction to Applicant's Test Year forecast of \$658,446, resulting in a revised projection of \$650,884 to which the Parties have agreed.

The commission finds this Test Year estimate to be reasonable.

B.

Effluent Revenues

Applicant sought to remove from its tariff the rate for providing effluent to the Golf Course, noting that, because the owner of the Golf Course now has access at a minimal cost to irrigation water previously used by Lihue Plantation Company, Ltd. for its sugar cane operations, Applicant's effluent would

not be required to irrigate the Golf Course. Applicant would thus, be forced to seek other means of disposing the effluent.

The Consumer Advocate opposed Applicant's proposal for the following reasons:⁹ (1) Applicant's parent company, Grove Farm, received approval to develop the area by committing to provide wastewater collection services, including storage and disposal of the effluent; (2) use of the effluent is consistent with the State of Hawaii's policy to make use of reclaimed water; and (3) the users of effluent should be required to pay for the costs associated with producing and disposing the effluent.¹⁰ The Consumer Advocate states that, for rate setting purposes, the revenues associated with the delivery of effluent to the Golf Course must be imputed to prevent Applicant's customers from subsidizing the Golf Course operations by paying for the cost of Applicant producing and delivering the effluent to the Golf Course.

Applicant agreed to impute revenues from the effluent produced and delivered to the Golf Course in determining the Test Year requirements. The Parties, thus, stipulated to a Test Year projection of \$69,135 for the Golf Course.

The commission finds the Parties' stipulated amounts for effluent revenues to be reasonable.

⁹See Consumer Advocate's Direct Testimonies, Exhibits and Workpapers ("Direct Testimonies"), CA-T-2 at 19.

¹⁰See Stipulated Agreement at 12.

VII.

Operating Expenses

The Parties have agreed to total operating expenses of \$867,967 for the Test Year with each of the operating expense items as follows:

A.

Electricity Charges

Applicant sought a Test Year expense amount for electricity charges of \$158,387 in its Application. Applicant determined this amount by calculating electricity consumption and associated charges for a 12-month period ending June 30, 2003, and increasing that amount to reflect new customers through the Test Year.

The Consumer Advocate recommended an amount of \$138,912. In its Direct Testimonies, the Consumer Advocate recommended utilizing data for the 12-month period ending February 2004 as a more accurate reflection of Applicant's electricity usage. It concluded that Puhi's electricity usage forecast included a period of abnormal operating conditions in which a backup effluent pump was used.¹¹ The Consumer Advocate also did not include an adjustment to account for additional wastewater generated by the addition of customers during the Test Year saying that the actual data did not support a direct correlation between the consumption of electricity and any

¹¹The backup effluent pump was a 200 horse power pump; Applicant's normal operations utilize a 30 horse power effluent pump.

increase in the volume of wastewater requiring treatment due to additional customers.¹²

Applicant agreed to the Consumer Advocate's recommendation.

The commission finds this amount for electricity charges to be reasonable.

B.

Water Utility Charges

Applicant proposed a Test Year expense amount for water utility charges of \$10,155. The Consumer Advocate did not object to this amount, nor did it propose any adjustments to the amount. Accordingly, the Parties have stipulated to a Test Year expense amount for water utility charges of \$10,155. The commission finds this amount to be reasonable.

C.

Repair and Maintenance Expenses

Applicant utilizes the services of an outside company, Aqua Engineers, Inc. ("Aqua"), to perform its day-to-day operations. Applicant proposed a Test Year amount of \$146,689 for Aqua's professional fees, and an amount of \$50,500 to pay for Applicant's in-house repair and maintenance expenses. The Consumer Advocate proposed an upward revision of the professional

¹²See Direct Testimonies, CA-T-3 at 5-7.

expenses and a downward adjustment for the in-house repair and maintenance expenses.¹³

During settlement discussions, the Parties agreed to combine the professional and in-house repair and maintenance expenses to determine the Test Year expense. Because Applicant has experienced an increase in repair and maintenance costs due to the age of the plant, Applicant proposed a combined Test Year expense amount of \$182,899. The Consumer Advocate proposed an expense amount of \$170,727 which they arrived at by averaging expenses for the years 1997 to 1999 and 2001 to 2003.¹⁴ Applicant agreed to the Test Year amount, and as such, the Parties have stipulated to a total Test Year repair and maintenance expense amount \$170,727.

The commission finds the Test Year amount for repair and maintenance expenses to be reasonable.

D.

Insurance

Applicant proposed a Test Year expense amount of \$40,785 for insurance purposes, to which the Consumer Advocate did not object. Accordingly, the Parties have stipulated to \$40,785 as an expense amount for insurance.

¹³See Direct Testimonies, CA-T-3 at 8-20 for a discussion of the Consumer Advocate's reasons for these adjustments.

¹⁴The year 2000 was not included in the calculation because it represented an abnormally low year for repair and maintenance expenses. See Stipulated Agreement at 16.

The commission finds this expense amount to be reasonable.

E.

Management Fees

Applicant proposed a Test Year amount of \$34,375 for management fees. The Consumer Advocate did not object to this amount. Thus, the Parties have stipulated to a Test Year amount of \$34,375 for management fees.

The commission finds this stipulated expense for management fees to be reasonable.

F.

Allocated Charges

The Parties have stipulated to no expense amount for allocated charges. The Consumer Advocate noted that Applicant's parent company has not previously charged Applicant for various services delivered to Applicant. Additionally, Applicant was unable to provide documentation to support its proposed allocated amounts,¹⁵ making it impossible for the Consumer Advocate to independently support Applicant's numbers. As such, the Parties stipulated to no expense amount for allocated charges.

The commission finds this stipulation to be reasonable.

¹⁵Applicant proposed an amount of \$19,800 for allocated charges.

G.

Amortization of Rate Case Expenses

Applicant proposed a Test Year expense amount of \$31,000 to reflect the annual amortization of its estimated rate case expense of \$155,000 over a 5-year period. The Consumer Advocate proposed an amount of \$9,931, reflecting the elimination of hearing and briefing expenses, copying costs, travel, etc., in the amount of \$40,000 due to the settlement of issues in the instant proceeding between the Parties, and amortizing these expenses over an 11-year period. Applicant accepted the proposed reduction in expenses. The Consumer Advocate also accepted Applicant's proposal of a 5-year amortization period, thus resulting in a stipulated Test Year annual rate case expense of \$21,844.

The commission finds this stipulated amount to be reasonable.

H.

Bad Debt and Uncollectibles

Applicant proposed a Test Year expense amount of \$37,481 for bad debt and uncollectibles. Applicant utilized a bad debt factor average of 3.24 percent (3.24%) based on Applicant's bad debt average for the years 1997 through 2002.

The Consumer Advocate proposed a Test Year amount of \$1,989, using a bad debt factor of 0.31 percent (0.31%).¹⁶

¹⁶See Direct Testimonies, CA-T-3 at 27-30.

During discussions, the Parties agreed to utilize a bad debt factor of 2.0 percent (2.0%) in calculating Applicant's Test Year bad debt and uncollectible expense amount. Accordingly, the Parties have stipulated to a Test Year expense amount of \$22,174 for bad debt and uncollectibles.

The commission finds this stipulated amount to be reasonable.

I.

Depreciation

Applicant proposed a depreciation expense amount of \$534,726. The Consumer Advocate adjusted this amount to \$224,740, reducing the amount by what the Consumer Advocate believed to be excess capacity in Applicant's plant, as discussed, below.

The Parties agreed to the Test Year depreciation expense of \$226,516.

The commission finds this amount for a Test Year depreciation expense to be reasonable.

J.

Amortization of Contribution in Aid of Construction

Applicant did not propose any expense amount for the amortization of Contribution in Aid of Construction ("CIAC"). The Consumer Advocate proposed a Test Year expense for the amortization of CIAC of \$2,207. With a minor adjustment of \$17, as a result of rounding for excess capacity, to be discussed

below, the Parties agreed to a Test Year expense amount of \$2,225 for the amortization of CIAC.

The commission finds this Test Year amount to be reasonable.

VIII.

Taxes

A.

Taxes - Other Than Income

In its Application, Applicant sought a Test Year amount for taxes, other than income ("TOTIT") of \$71,470. The Consumer Advocate proposed an amount for TOTIT of \$42,097. The difference in the two amounts was due to the Parties' differing revenue requirement recommendations and the Consumer Advocate's determination that Applicant was not allowed, under the relevant laws, the deduction of bad debt/uncollectible expense in determining the taxable base to which revenue tax rates are to be applied.¹⁷

Applicant acknowledged the correctness of the Consumer Advocate's position that its bad debt/uncollectible expense should not be deducted in determining the applicable revenue tax base. The Parties thus stipulated to an amount of \$70,253 for TOTIT for the Test Year.

The commission finds the Parties' stipulated amount of \$70,253 for TOTIT for the Test Year to be reasonable.

¹⁷See Direct Testimonies, CA-T3 at 30-31.

B.

Income Taxes

In its Application, Applicant proposed an amount of \$8,179 for income taxes utilizing a federal income tax rate of 34 percent (34%) and a state income tax rate of 6.4 percent (6.4%). Applicant noted in its response to the Consumer Advocate's IRs that it used those rates because it was part of a consolidated tax return filing, and that it did not file its taxes on a stand-alone basis. See Consumer Advocate IR-33. The Consumer Advocate recommended the use of a lower tax rate, and asserted that Applicant should file its taxes as a stand-alone company. During discussions, the Consumer Advocate agreed to use the consolidated income tax rates for ease in determining the Test Year revenue requirements. The Parties thus settled on an income tax expense amount of \$139,194.

The commission finds the stipulated amount of \$139,194 for income tax expense to be reasonable.

C.

Amortization of Hawaii Capital Goods Excise Tax Credit

Applicant did not include as part of its Test Year expense an amount for the amortization of the Hawaii capital goods excise tax credit ("HCGETC"). Noting that the commission has recognized the HCGETC for ratemaking purposes by reducing the rate base by the unamortized balance of this credit and reducing income tax expense by the current year amortization of this

credit,¹⁸ the Consumer Advocate sought a Test Year amount for the current year amortization of the HCGETC of \$6,398. After settlement of the excess capacity issue, to be discussed below, and the income tax rate issue, discussed above, the parties agreed to a Test Year amortization of the HCGETC of \$4,913.

The commission finds this Test Year amount to be reasonable.

IX.

Rate Base

The Parties stipulated to a Test Year average rate base of \$2,624,959. In reaching the stipulated Test Year average rate base, the Parties negotiated the following items: (1) net plant in service; (2) accumulated deferred income taxes; (3) HCGETC; (4) net CIAC; and (5) working capital.

A.

Net Plant in Service

The Parties stipulated to an average Test Year net plant in service amount of \$3,365,649. The net plant in service amounts consists of two (2) components, plant in service and accumulated depreciation.

Applicant initially proposed an amount of \$12,681,142 for its plant in service; the Consumer Advocate proposed a plant

¹⁸See Direct Testimonies, CA-T-3 at 44.

in service amount of \$5,303,478. The Consumer Advocate's proposed amount adjusted Applicant's proposed amount by including the cost of certain assets purchased with Applicant's operating reserve and reducing Applicant's overall plant in service amount by 58.33 percent (58.33%), alleging that this amount of plant was excess capacity, which should not be included in the Test Year rate base.

During settlement discussions, Applicant agreed to the inclusion in its plant in service of the additional assets purchased with the operating reserve. Additionally, while Applicant did not agree completely with the excess capacity issues raised by the Consumer Advocate, in the interest of settlement, the Parties agreed to utilize the excess capacity percentage of 58 percent (58%).¹⁹ Accordingly, the Parties stipulated to a Test Year plant in service amount of \$5,345,387.

The Parties also stipulated to utilizing an accumulated depreciation amount of \$1,979,738 which includes the entire costs of the assets purchased with the operating reserve funds. Accordingly, the net plant in service, with the excess capacity settlement adjustment is \$3,365,649.

Given the net plant in service amount of \$3,365,649, the commission finds the accumulated depreciation amount of \$1,979,738 and the plant in service amount of \$5,345,387 to be reasonable.

¹⁹The Parties agreed to round the excess capacity percentage to the nearest percent. See Stipulated Agreement at 25.

B.

Accumulated Deferred Income Taxes

The Parties agreed to a Test Year amount of \$674,158 for accumulated deferred income taxes. The commission finds this amount to be reasonable.

C.

Hawaii Capital Goods Excise Tax Credit (HCGETC)

As noted above, the commission recognizes the HCGETC for ratemaking purposes. Also as noted, the Parties stipulated to a Test Year expense amount of \$4,913 for the current year amortization of this credit. After settlement of the excess capacity issue and the income tax rate issue, both discussed above, the Parties agreed to an unamortized HCGETC balance of \$60,971.

The commission finds this stipulated amount for HCGETC to be reasonable.

D.

Net CIAC

Applicant did not propose any CIAC amount in its Application. The Consumer Advocate proposed a Test Year net CIAC amount of \$5,518. After a slight adjustment of this figure by the Parties, the amount settled upon for net CIAC was \$5,562.

The commission finds this Test Year net CIAC amount to be reasonable.

E.

Working Capital

In the Application, Applicant proposed a Test Year amount of \$44,100 for working capital. The Consumer Advocate recommended that no working capital be allowed. It determined that because Applicant is allowed, pursuant to its rules and regulations, and has been, billing its customers in advance of providing service, Applicant has sufficient revenues in advance of providing service, such that any need for working capital is drastically reduced.²⁰ Applicant agreed to the Consumer Advocate's recommendation that no working capital be included in the Test Year rate base.

The commission finds this determination to be reasonable.

X.

Rate of Return

The Parties stipulated to a rate of return of 8.85 percent (8.85%). For reasons which will be discussed below, in rate design, the Parties agreed to a 3-year phase-in of Applicant's rates resulting from this stipulation. Thus, Applicant is not expected to earn the 8.85% of return until the final year of the phase-in period.

The commission finds the rate of return to be reasonable.

²⁰See Direct Testimonies, CA-T-3 at 48-49.

XI.

Rate Design

As discussed above, the Parties stipulated to a rate design that would provide Applicant a reasonable opportunity to earn the Test Year revenue requirement of \$1,100,275. This represents a revenue increase of \$449,392 or approximately 69 percent (69%). With regard to rate increases of 25 percent (25%) or more, the Consumer Advocate notes that its position in other proceedings before the commission has been that these increases should be phased in to prevent "rate shock" to the ratepayers.²¹ The Parties thus determined an appropriate phase-in period for the rate increase and the amount of increase appropriate for each period.

The Parties agreed to a 3-year phase-in period to give Applicant's customers time to adjust to the gradual rate increases, while also allowing Applicant the opportunity to recover its expenses and earn some return on its investment during the phase-in period. The Parties stipulated rate design is as follows:

²¹The Consumer Advocate describes "rate shock" as a sudden and dramatic increase in rates such that the ratepayer may suffer disruption to his service and undue hardship. A basic principle of ratemaking is "gradualism", wherein regulators seek gradual rate increases on the ratepayers. When large increases are deemed necessary, a phase-in of the rates and deferral of cost recovery are seen as ways to mitigate the impact upon the ratepayers. See Stipulated Agreement, n.19.

<u>Customer Class</u>	<u>Present</u>	<u>First Phase (1st 12-month period)</u>	<u>Second Phase (2nd 12-month period)</u>	<u>Third Phase (from expiration of 2nd 12-month period)</u>
Residential (Single Family and Condominiums) (monthly service charge per customer)	\$34.00	\$39.00	\$43.00	\$46.00
Industrial (monthly service charge per customer)	Minimum service charge of \$77.00, plus sewer consumption charge of \$3.25 per every 1,000 gallons of metered domestic water consumption	Minimum service charge of \$169.00, plus sewer consumption charge of \$4.85 per every 1,000 gallons of metered domestic water consumption	Minimum service charge of \$227.00, plus sewer consumption charge of \$5.86 per every 1,000 gallons of metered domestic water consumption	Minimum service charge of \$286.00, plus sewer consumption charge of \$6.88 per every 1,000 gallons of metered domestic water consumption
Commercial (monthly service charge per customer)	Minimum service charge of \$105.00, plus sewer consumption charge of \$1.95 per every 1,000 gallons of metered domestic water consumption	Minimum service charge of \$180.00, plus sewer consumption charge of \$2.84 per every 1,000 gallons of metered domestic water consumption	Minimum service charge of \$227.00, plus sewer consumption charge of \$3.41 per every 1,000 gallons of metered domestic water consumption	Minimum service charge of \$275.00, plus sewer consumption charge of \$3.98 per every 1,000 gallons of metered domestic water consumption
Effluent (Golf Course Irrigation)	\$0.50 per every 1,000 gallons of metered domestic water consumption			
Hookups	\$100.00	\$100.00	\$100.00	\$100.00

The Parties have stipulated that the first phase increase, amounting to 29.9 percent (29.9%) over existing rates, will become effective upon filing of the commission decision and

order approving the Stipulated Agreement.²² The second phase increase, approximately 15.6 percent (15.6%) over the first phase rates, would occur twelve (12) months following the effective date of the first phase rates. The third phase increase, approximately 12.6 percent (12.6%) above the second phase rates, would occur twelve (12) months following the effective date of the second phase rates.

The commission finds the Parties' proposed rate design to be reasonable.

XII.

Rules and Regulations

The Parties have agreed to the following changes to Applicant's Rules and Regulations:

1. The term "Consumer", as used throughout the Rules and Regulations is replaced with the term "Customer".
2. The following will be added to Rule 1 (Definitions):
 - 1.5 "Commercial" means a non-Residential area that is located outside of an area zoned Industrial.
 - 1.13 "Industrial" means an area zoned Industrial.
 - 1.16 "Residential" means an area that contains a single family or condominium unit where a Customer/tenant/person resides.

²²See Stipulated Agreement at 32.

3. Rule 3.2 (Interruption of Service) shall be amended to read as follows:

3.2 The Company reserves the right at any and all times to terminate service without notice for the purpose of making repairs, extensions, alterations, or for other reasons related to the operations of the sewage system. Repairs or improvements will be prosecuted as rapidly as practicable and, insofar as practicable, at such times as will cause the least inconvenience to the Customer. Except in the case of emergency repairs, the Company shall use reasonable efforts to give the Customer at least 24 hours notice before shutting off service.

4. The first full sentence of Rule 5.4.1 (Interest on Deposits) shall be amended by reducing the simple interest from 6 percent (6%) to 2 percent (2%) as follows:

Simple interest at the rate of two percent (2%) per annum shall be paid by the Company on standard Customer deposits described at Section 5.3 for the time it is held by the Company after credit is established.

5. Rule 6.3 (Service Connection) shall be amended to read as follows:

6.3 **Service Connection.** When the application has been approved, the Service Connection will be installed by the Company at the expense of the Applicant. All Service Connections shall become the property of the Company for its operation and maintenance after installation, and new connections or disconnections may be made thereto by the Company at any time. The Customer shall be responsible for the maintenance and repair of the lines located within the Customer's property, while the Company shall be responsible for the maintenance and repair of the lines located outside the Customer's property (including the Service Connection). Notwithstanding the above, the Customer shall be liable for damage to equipment, lines or other Company property, wherever located, if the damage is caused by the Customer. If the damage is caused by tree roots, the Company shall be responsible for initial tree root damage or blockage to sewer lines within the public right-of-way or within a utility easement along the Company's sewer main. If damage is caused by a tree on the Customer's property,

or which is the responsibility of the Customer to maintain, the Customer shall be responsible for the Company's costs to repair subsequent damage to the sewer lines.

6. The third full sentence of Rule 8.1 (Payment of Bills) shall be amended to read as follows:

Payment shall be made by personal check, cashier's check, money order, or cash at the office of the Company, through the U.S. mail or, at the Company's option, to duly authorized collectors of the Company.

The commission finds the Parties' stipulated revisions to the Applicant's Rules and Regulations to be reasonable.

XIII.

Other Changes

The Parties stipulated to other non-substantive changes to the Table of Contents and the Rules and Regulations. Specifically, the Parties agreed that Applicant should update the page numbering on the Table of Contents, revise the information on the footer of each page of the Rules and Regulations to update Applicant's contact information, and include a reference to the commission's final order in the subject docket when issued.

XIV.

Commission Approval

Upon our review of the Stipulated Agreement, the commission finds and concludes that the Parties' Stipulation achieves a resolution of all outstanding issues in this proceeding. This is Applicant's first rate increase since its rates were first approved in 1997. The Stipulation Agreement achieves a balance between the needs of Applicant to operate its business successfully, and the interests and views of its consumers, who have an interest in obtaining sufficient amounts of water for their varied uses at reasonable prices. As such, the commission concludes that the Stipulated Agreement should be adopted in its entirety. Specifically, the commission: (1) finds the Stipulated Agreement, taken as a whole, to be just and reasonable; and (2) approves the Parties' Stipulated Agreement.

XV.

Ultimate Findings and Conclusions

The commission finds and concludes:

1. The operating revenues and operating expenses for the Test Year, as set forth in Exhibit A, are reasonable.
2. The use of an average test year rate base is reasonable.
3. The Test Year average depreciated rate base under approved rates is \$2,624,959.
4. The stipulated rate of return for the Test Year is 8.85 percent (8.85%), which is fair.

5. Applicant is entitled to total operating revenues of \$1,100,275.

6. Applicant's new rate design and tariff revisions are reasonable.

XVI.

Orders

THE COMMISSION ORDERS:

1. The Parties' Stipulated Agreement, filed on August 3, 2004, is approved in its entirety and incorporated as part of this decision and order.

2. Puhi may increase its rates to produce a total annual revenue increase of \$449,392, as shown in Exhibit A, representing an increase in Puhi's revenue requirement to \$1,100,275, or a rate of return of 8.85 percent (8.85%) on its rate base for the Test Year.

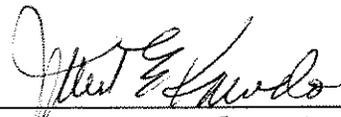
3. Puhi shall file with the commission revised tariff sheets and rate schedules reflecting the increases in rates and charges to its schedules and rules and regulations authorized by this decision and order. The revised tariff sheets and rate schedules shall be served on the Consumer Advocate and filed with the commission within three (3) days of the issuance of this decision and order. The rate increase for the first phase shall take effect on the date of this decision and order.

DONE at Honolulu, Hawaii AUG 17 2004.

PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

By 
Carlito P. Caliboso, Chairman

By 
Wayne H. Kimura, Commissioner

By 
Janet E. Kawelo, Commissioner

APPROVED AS TO FORM:


Benedyne S. Stone
Commission Counsel

03-0383.sl

CERTIFICATE OF SERVICE

I hereby certify that I have this date served a copy of the foregoing Decision and Order No. 21312 upon the following parties, by causing a copy hereof to be mailed, postage prepaid, and properly addressed to each such party.

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DIVISION OF CONSUMER ADVOCACY
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Karen Higashi

DATED: AUG 17 2004