

**BEFORE THE PUBLIC UTILITY COMMISSION  
OF OREGON**

UI 260

In the Matter of	)	
	)	
AVION WATER COMPANY, INC.	)	ORDER
	)	
Affiliated Interest Application with	)	
Jan M. Wick.	)	

**DISPOSITION: APPLICATION APPROVED WITH CONDITIONS**

On January 23, 2007, Avion Water Company, Inc. (Avion) filed an application with the Public Utility Commission of Oregon (Commission) pursuant to ORS 757.495 and OAR 860-036-0730, requesting approval of a compensation agreement between Avion and its Principal Shareholder and President, affiliated interests. A description of the filing and its procedural history is contained in the Staff Report, attached as Appendix A, and incorporated by reference.

Based on a review of the application and the Commission’s records, the Commission finds that the application satisfies applicable statutes and administrative rules. At its public meeting on February 27, 2007, the Commission adopted Staff’s recommendation.

**OPINION**

**Affiliation**

An affiliated interest relationship exists under ORS 757.015.

**Applicable Law**

ORS 757.495 requires a public utility to seek approval of contracts with affiliated interests within 90 days after execution of the contract.

ORS 757.495(3) requires the Commission to approve the contract if the Commission finds that the contract is fair and reasonable and not contrary to the public interest. However, the Commission need not determine the reasonableness of all the financial aspects of the contract for ratemaking purposes. The Commission reserves that issue for a subsequent proceeding.

**CONCLUSIONS**

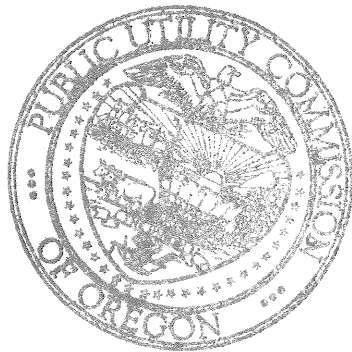
1. An affiliated interest relationship exists.
2. The agreement is fair, reasonable, and not contrary to the public interest.
3. The application should be granted, as modified herein, including certain conditions and reporting requirements.

**ORDER**

IT IS ORDERED that the application of Avion Water Company, Inc. for approval of the compensation agreement between Avion Water Company Inc. and its Principal Shareholder and President is approved, subject to the conditions stated in the Staff Report attached as Appendix A.

Made, entered, and effective MAR 05 2007.

BY THE COMMISSION:



*Becky L. Beier*  
\_\_\_\_\_  
**Becky L. Beier**  
Commission Secretary

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-014-0095. A copy of any such request must also be served on each party to the proceeding as provided by OAR 860-013-0070(2). A party may appeal this order by filing a petition for review with the Court of Appeals in compliance with ORS 183.480-183.484.

PUBLIC UTILITY COMMISSION OF OREGON  
STAFF REPORT  
PUBLIC MEETING DATE: February 27, 2007

REGULAR \_\_\_\_\_ CONSENT X EFFECTIVE DATE \_\_\_\_\_ NA \_\_\_\_\_

DATE: February 12, 2007

TO: Public Utility Commission

FROM: Michael Dougherty *MD*

THROUGH: *LS* Lee Sparling and *MH* Marc Hellman

SUBJECT: AVION WATER COMPANY, INC.: (Docket No. UI 260) Application Requesting Approval of an Affiliated Interest Agreement between Avion Water Company and the Principal Shareholder and President of Avion Water Company.

**STAFF RECOMMENDATION:**

The Commission should approve Avion Water Company's (Avion or Company) affiliated interest agreement with the Principal Shareholder and President of Avion Water Company, Jan Wick, subject to the following conditions:

1. The Company shall provide the Commission access to all books of account, as well as all documents, data, and records that pertain to any payments to Jan Wick.
2. The Commission reserves the right to review, for reasonableness, all financial aspects of this transaction in any rate proceeding or alternative form of regulation.
3. Avion shall notify the Commission in advance of any substantive changes to the contract, including any material change in price over ten percent of the levels in the original application. Any such change shall be submitted in an application for a supplemental order (or other appropriate format) in this docket.

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**DISCUSSION:**

Avion filed this application on January 23, 2007, pursuant to ORS 757.495 and OAR 860-036-0730. Jan Wick owns 46.75 percent of the common stock of Avion and therefore, Jan Wick and Avion are affiliated interests pursuant to ORS 757.015.

In Commission Order No. 06-627 (UW 117), dated December 4, 2006, the Commission clarified the requirements relating to situations where owners of water utilities were also employed by the utility. Staff had historically not requested an affiliated interest filing in such circumstances and instead rigorously reviewed the compensation expense during general rate reviews. In Order No. 06-627, the Commission found that the plain, natural, and ordinary meaning of the affiliated interest statute mandates that payments of wages and benefits of an owner of a utility requires an affiliated interest filing, pursuant to ORS 757.495(1).

Jan Wick, as President of the Company, is receiving wages and benefits from the Company. The last time staff reviewed the terms of compensation as an expense in rates was UW 93. Commission Order No. 04-051, dated January 31, 2004, adopted rates that included \$110,000 for officer wages and \$301,832 for company-wide pensions and benefits.

In the affiliated interest filing, Avion requests the Commission to approve the compensation agreement between Avion Water Company and the Principal Shareholder and President of Avion Water Company as follows:

1. Salary - \$150,000/year;
2. Retirement Contribution - \$15,000/year; and
3. Health and Dental Insurance - \$13,350/year.

Jan Wick, as President of Avion, will provide management and engineering services as an employee of Avion Water Company, Inc. According to the Company's application, Avion believes that by retaining the services of Jan Wick, the Company will be able to maintain the high level of service provided to Avion's customers, particularly during the rapid growth that the Company is currently experiencing.

The President of Avion is responsible for all aspects of Avion Water Company's operations and management. The duties include, but are not limited to, long range tax and financial planning and cash management, engineering of new facilities, negotiating with developers, maintaining banking relations, regulatory communications with the Commission, and public relations with Avion customers and the Central Oregon area.

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Avion is the largest investor-owned water utility regulated by the Commission. As previously mentioned, the Company is experiencing phenomenal growth. The following table highlights the growth Avion has experienced over the past five years.

**Table 1 – Avion Growth 2002 Through 2006**

	2002	2003	2004	2005	Preliminary 2006	Percent Change 2002 - 2006
Total Customers	8,609	9,109	9,724	10,596	11,618	35%
Number of Employees	22	23	26	27	30	36%
Total Revenue	\$3,782,706	\$4,216,622	\$4,645,757	\$5,035,903	\$5,507,740	46%
Total Operating Expenses	\$2,330,537	\$2,380,391	\$2,637,454	\$2,986,072	\$3,336,037	43%
Total Other Deductions	\$1,062,266	\$409,038	\$808,079	\$990,963	\$951,687	-10%
Net Income	\$389,903	\$1,427,193	\$1,200,224	\$1,058,868	\$1,220,016	213%
Total Rate Base <sup>1</sup>	\$9,133,213	\$11,483,512	\$11,077,352	\$11,109,638	\$12,980,682	42%
Calculated Rate of Return <sup>2</sup>	4.27%	12.43%	10.83%	9.53%	9.40%	-

As can be seen from the above table, the operations of Avion have increased significantly over the past five years. In addition, according to Avion's 2006 Master Plan, the Company has been experiencing annual growth in customer accounts ranging from 10 percent to 15 percent. To finance this growth, Avion received approval from the Commission in Commission Order No. 07-031 (UF 4234), dated January 29, 2007, to enter into a loan agreement to borrow \$2.6 million for system upgrades.

This growth in Avion's service territories is consistent with projected growth in the two counties served by Avion: Deschutes and Crook.<sup>3</sup>

<sup>1</sup> The total rate base does not include contributed plant which was \$13,206,737, net book value, as of December 31, 2005.

<sup>2</sup> Authorized rate of return, UW 93, is 8.16 percent.

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Although revenues, customers, and rate base have increased significantly, the total compensation package for the President of Avion has not kept pace and increased 13 percent over the same time period. The Consumer Price Index for all Urban Consumers (CPI-U)<sup>4</sup> increased 13.5 percent for the same time period while the Employment Cost Index<sup>5</sup>, total compensation, increased 18.2 percent over the five-year period 2001 through 2005. Additionally, a five-year percent increase for compensation of the President is significantly lower than Avion's total payroll increase of 57.7 percent for the same time period.

### Issues

Staff investigated the following issues:

1. Transfer Pricing
2. Public Interest Compliance
3. Records Availability, Audit Provisions and Reporting Requirements

### Transfer Pricing

Pursuant to OAR 860-036-0739, Allocation of Costs by a Water Utility, the amount paid by a utility to an affiliated interest is required to be at cost or the market rate, whichever is lower. Given the nature of the proposed contract - between the Company and its President, Staff's review will focus on analyzing the market rate since in this case the terms "market" and "cost" are the same given the uniqueness of this affiliated interest relationship and its human capital services.

Since Avion is the only current Class A Water Company<sup>6</sup> in the state, Staff used the American Water Works Association (AWWA) Water Utility Compensation Survey as a proxy to determine the market rate.

In the AWWA survey, the average pay for "Top Operations and Maintenance Executives" was \$138,298. The average pay for "Top Engineering Executive" was \$100,647. The average pay for "Top Finance Executive" was \$127,357.

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<sup>3</sup> Per information from the Oregon Employment Department, Deschutes County grew by 6.4 percent and Crook County 7.7 percent from 2005 to 2006. [www.olmis.org](http://www.olmis.org)

<sup>4</sup> The CPI-U includes expenditures by urban wage earners and clerical workers, professional, managerial, and technical workers, the self-employed, short-term workers, the unemployed, retirees and others not in the labor force. CPI is sometimes referred to as "headline inflation."

<sup>5</sup> The ECI is the Employment Cost Index measured by the Bureau of Labor Statistics. The ECI is a measure of the change in the cost of labor, free from the influence of employment shifts among occupations and industries. The series measures changes in compensation costs (wages and salaries and employer costs for employee benefits).

<sup>6</sup> Class A water companies are water utilities with over \$1,000,000 in revenue.

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Although the pay requested by Avion is higher than the average pay for the above positions, the amount seems reasonable given Avion's significant growth and cost pressures, and the fact that Avion's President entails responsibilities for all three of the above positions.

Staff did not note any issues concerning benefit and retirement costs in the agreement given that it is the same comparable terms as those offered to all employees of Avion.

Public Interest Compliance

As previously mentioned, Avion is the largest and fastest growing investor-owned water utility in Oregon. Even with this high-growth, Avion has continued to achieve excellent customer service, and low operating cost per customer.

Records Availability, Audit Provisions, and Reporting Requirements

Order Condition Number 1, listed above in the Staff recommendation, affords the necessary Commission examination of Avion's records concerning this application.

Based on the review of this application, Staff concludes the following:

1. The application involves an affiliated interest transaction that is fair and reasonable and not contrary to the public interest, with the inclusion of the proposed ordering conditions.
2. Necessary records are available.

**PROPOSED COMMISSION MOTION:**

Avion Water Company's application be approved subject to the three recommended conditions.

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