

ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF WATER SERVICE)
COMPANY OF INDIANA FOR)
AUTHORITY TO INCREASE ITS) CAUSE NO. 44104
WATER AND SEWER RATES AND)
CHARGES AND FOR APPROVAL OF A) APPROVED:
NEW SCHEDULE OF RATES AND) MAR 27 2013
CHARGES APPLICABLE THERETO)

ORDER OF THE COMMISSION

Presiding Officers:

Carolene Mays, Commissioner

Gregory R. Ellis, Administrative Law Judge

On October 28, 2011, Water Service Company of Indiana ("Petitioner," "WSC" or "Company") filed its petition with the Indiana Utility Regulatory Commission ("Commission") for authority to increase water and sewer rates and charges, and for approval of a new schedule of rates and charges.

Petitioner prefiled its testimony and exhibits constituting its case-in-chief on December 1, 2011. The Indiana Office of Utility Consumer Counselor ("OUCC") filed its responsive testimony and exhibits on May 23, 2012. On June 14, 2012, Petitioner filed its rebuttal testimony and exhibits.

On March 9, 2012, the OUCC requested that a field hearing be scheduled in this matter. The Commission granted the request. Pursuant to notice duly published as required by law, proof of which was incorporated into the record by reference and placed in the official files of the Commission, a public field hearing was held in the Lincoln Elementary School Gymnasium in Demotte, Indiana on May 2, 2012 at 6:00 p.m., at which the parties and members of the public appeared.

An evidentiary hearing was conducted in this Cause on July 10, 2012 at 9:30 a.m. in Room 224 of the PNC Center, 101 W. Washington St., Indianapolis, Indiana. At the hearing, the testimony and exhibits of the parties were admitted into the record and the respective witnesses were made available for cross-examination.

Based upon the applicable law and the evidence of record, the Commission now finds:

1. **Notice and Jurisdiction.** Notice of the filing of WSC's petition as well as each of this Commission's hearings in this Cause was given as required by law. WSC is a public utility as defined by Ind. Code § 8-1-2-1 and is subject to the jurisdiction of the Commission in the manner and to the extent provided by law. Accordingly, we have jurisdiction over both WSC and the subject matter of its petition.

2. **Petitioner's Characteristics.** WSCI owns, operates, manages and controls plant and equipment which are used and useful in the provision of water and sewer services in Jasper and Newton Counties. Petitioner is currently serving approximately 190 water and sewer customers within a rural area of Jasper and Newton Counties. Most of WSCI's customers are residential. WSCI also provides seasonal sewer-only service to one wholesale customer, the Yogi Bear Campground, which has approximately 692 tenants. Petitioner is a wholly-owned subsidiary of Utilities, Inc., which owns corporations that own over 70 systems providing utility service to approximately 270,000 customers in 15 states.

3. **Existing Rates and Relief Requested.** WSCI's current water rates and charges were approved by the Commission in Cause No. 42969 on August 30, 2006. WSCI's current sewer rates and charges were approved in Cause No. 41486 on January 19, 2000 for Petitioner's predecessor, Jasper-Newton Utility Company, Inc. In its Petition, WSCI states that since its rates and charges were last established it has made substantial capital investments to its system, including the construction of a new wastewater treatment plant. Petitioner further asserts that expenses and other costs have increased and, as a result, its existing rates and charges now, are, and will continue to be insufficient to provide revenues adequate to cover its necessary and reasonable operating expenses and provide the opportunity to earn the fair return to which Petitioner is lawfully entitled. In its initial testimonial filings, WSCI requested authorization to increase its existing water rates by \$130,087 or 179.11% from *pro forma* present revenues and its existing sewer rates by \$378,469 or 310.19% from *pro forma* present revenues. WSCI also requested recovery of certain expenses and approval of five new non-recurring charges for the water system and four non-recurring charges for the wastewater system.

4. **Test Year and Rate Base Cut-off.** The test year for determining Petitioner's actual and *pro forma* operating revenues, expenses and operating income under present and proposed rates shall be the twelve (12) months ended June 30, 2011, adjusted for changes that are fixed, known and measurable for ratemaking purposes and that occur within twelve (12) months following the end of the test year. The financial data for this test year, when adjusted for changes as provided in the Commission's December 15, 2011 docket entry, is a proper basis for fixing new rates for Petitioner and testing the effect thereof. As further provided in the docket entry, the rate base cut-off should reflect used and useful property as of June 30, 2011. The Commission finds that this test period is sufficiently representative of WSCI's normal operations to provide reliable data for ratemaking purposes.

5. **Evidence Presented.**

A. **Petitioners' Case-in-Chief.** Dmitry Neyzelman, Senior Regulatory Accountant for Utilities, Inc. and its subsidiaries, including WSCI, testified regarding Petitioner's requested change in water and sewer rates and charges. He also sponsored Petitioner's financial exhibits.

Mr. Neyzelman testified that WSCI is a wholly owned subsidiary of Utilities, Inc. WSCI provides both water and sewer service in Jasper and Newton Counties. Mr. Neyzelman indicated that Utilities, Inc. has over 70 systems that provide service to approximately 270,000 customers in 15 states and that WSCI's relationship with Utilities Inc. has many benefits for its customers. He noted that Utilities, Inc. provides managerial and professional services at a cost lower than is

available in the open market and that WSCI is able to pass these savings onto its customers through lower rates.

WSCI's current water rates were approved by Order entered by the Commission, August 30, 2006, in Cause No. 42969. WSCI's current sewer rates were last determined for WSCI's predecessor, the Jasper-Newton Utility Company, in an Order entered by the Commission on January 19, 2000, in Cause No. 41486. Mr. Neyzelman testified that WSCI is not able to cover its operating expenses and earn a reasonable return on its investment in the WSCI system under its current rates. Mr. Neyzelman also indicated that Petitioner's present rates do not reflect rising costs and the utility's need to make improvements to its systems. Petitioner had a test year net operating loss of \$28,233, for a return of -4.97% on an original cost rate base of \$568,091 for its water operations and earned a net operating income of \$5,949, for a 0.22% return on the original cost rate base of \$2,685,619 for its sewer utility. Mr. Neyzelman testified that WSCI is requesting an increase in the water division's revenue requirement in the amount of \$130,087 from *pro forma* present revenues and an increase in the sewer division's revenue requirement in the amount of \$378,469 from *pro forma* present revenues, which should allow WSCI to earn an 8.53% rate of return on the combined original cost rate base. He testified Petitioner is requesting rate relief so that it can continue to provide safe, reliable and efficient water and wastewater utility services to its customers.

Mr. Neyzelman testified adjustments were made to the test year revenues based on known, fixed and measurable changes through June 30, 2011. The adjustments resulted in an increase of \$1,772 to test year water revenues and \$7,883 to test year sewer revenues.

Mr. Neyzelman provided testimony concerning operating expenses. He explained all salary and wage costs are allocated to WSCI from the Water Services Corporation (the "Service Company"), a wholly-owned subsidiary of Utilities Inc., that provides support services to Utilities Inc.'s subsidiaries. No one works directly for WSCI. He further explained that other costs are allocated to WSCI from the Service Company. Costs incurred by the Service Company are allocated to its subsidiaries through direct allocation or the use of allocation factors. He indicated that costs not directly assignable to a specific subsidiary are allocated to all subsidiaries on a monthly basis. Mr. Neyzelman testified that an adjustment was made to salaries and wages to remove from operating expense the amount of labor that was capitalized during the test year.

Mr. Neyzelman summarized the various adjustments made by Petitioner to test year operating expenses. The test year level of regulatory expense was increased to reflect the anticipated costs of this proceeding, amortized over a three year period. Pensions and other benefits expense was increased to reflect the increased costs of pension and other benefits. Transportation expense was decreased by \$1,279 based on vehicles assigned to employees and their allocation percentages as of the end of the test year. He indicated depreciation expense was annualized based upon gross depreciable plant at the end of the test year plus *pro forma* projects. An adjustment was made to correct an over allocation of vehicle depreciation expense to WSCI during the test year. In addition, the Petitioner is proposing depreciation rates of 25% for utility vehicles and 12.5% for computer equipment and software systems to better reflect their typical useful lives. The result of these adjustments would be a decrease to depreciation expense of \$71,959. He explained that Taxes Other Than Income were adjusted for annualized payroll taxes, Utility Commission Taxes and Gross Receipts Taxes resulting in an increase of \$27. Federal and State income taxes were adjusted to reflect taxable income at current rates, which resulted in decreases of \$41,305 to Federal income taxes and \$25,895 to State income taxes.

Mr. Neyzelman testified that Petitioner's present rates net a pro-forma operating loss of \$28,233 for water operations and an operating income of \$5,949 for sewer operations. The proposed rates are calculated to provide the opportunity to earn an 8.53% return on net original cost rate base of \$568,091 for water operations and \$2,685,619 for sewer operations. The increased revenue requirement is calculated by determining the requested increase in operating income. The requested increase in net operating income is \$76,710 for water operations and \$223,257 for sewer operations. The increase in operating income is then grossed up for: (a) Federal income taxes, (b) State income taxes, (c) Taxes Other than Income, and (d) Uncollectibles. The resulting proposed increase in revenue requirements is \$130,087 for water operations and \$378,469 for sewer operations.

Mr. Neyzelman explained the rate base for Petitioner's water and sewer utilities reflect rate base as of June 30, 2011, net of accumulated depreciation reserve, with adjustments to annualize the allocation of vehicles and computers at the end of the test year. He stated all of the utility's property included in rate base, including plant adjustments, is used and useful and is currently providing service to WSCI's customers.

Mr. Neyzelman testified that rather than incur the costs associated with hiring a return on equity ("ROE") expert, WSCI proposes to use a cost of common equity of 10.44%. He provided a table of recent ROE granted to seventeen of Petitioner's sister companies and indicated that the average ROE was 10.44%. Based on a capital structure consisting of 49.69% long-term debt and 50.31% common equity, Mr. Neyzelman calculated a rate of return of 8.53% based on Petitioner's recommended cost of equity of 10.44%.

Mr. Neyzelman explained WSCI's proposed rate design would allocate water revenue requirements between the components that should be recovered from the fixed charge (the base facilities charge) and the components that should be recovered from the variable charge (the usage charge). The rate design would establish the base facilities charge based on the size of the customer's meter. The base facilities charges for both the water and sewer rates would be based on the equivalent meter factors as established by the American Water Works Association. He indicated that under the WSCI's proposed water rate design, approximately 33% of the water revenue requirement will be recovered in the base facilities charge.

Mr. Neyzelman also described proposed changes to WSCI's sewer rate design. He noted the Yogi Bear Campground ("Campground"), which represents a significant portion of the sewer user base, was not properly billed and therefore did not pay all of its sewer charges in periods prior to the test year. He explained that this under collection resulted in part because the Campground was supposed to be billed for seven months of service each year pursuant to an agreement approved in the utility's last sewer rate case, Cause No. 41486. In order to avoid this issue in the future, WSCI is proposing a billing change to move the Campground to monthly billing. The total annual amount billed to the Campground will be the same. He further indicated this rate design would address the fixed costs related to the Campground regardless of when the Campground is operational. Mr. Neyzelman indicated that WSCI lacks current flow information from the Campground. In determining its proposed rates, WSCI allocated a percentage of sewer revenues to the Campground based upon the annualized sewer revenue related to the Campground divided by the total sewer revenue.

Mr. Neyzelman also testified concerning WSCI's proposed water and sewer charges. The base facility charge for water customers is based upon the meter size and starts at \$26.07. Water customers will also be charged \$8.52 per 1,000 gallons consumed. For sewer customers, the base facility charge is based upon meter size and starts at \$39.98. Residential sewer customers will also be charged \$13.86 per 1,000 gallons consumed where commercial sewer customers will be charged \$21.11 per 1,000 gallons consumed.

Mr. Neyzelman testified the Petitioner is proposing to institute the following non-recurring charges for water service: Non-Sufficient Funds ("NSF") Charge, New Customer Charge, Meter Testing Fee (Outside Reader), Late Payment Charge and After-Hours Call Out Charge. In addition, the Company is proposing changes to the following current non-recurring charges: Reconnection Charge and Connection Charge. He indicated that Petitioner is proposing to institute the following non-recurring charges for sewer service: Non-Sufficient Funds ("NSF") Charge, New Customer Charge, Reconnection Charge and Late Payment Charge. In addition, the Company is proposing changes to the following current non-recurring charge: Connection Charge. He testified these charges are proposed to reflect the costs incurred from these services and to provide consistent rates across affiliated utilities. Finally, he explained that Petitioner is proposing various clarifying changes to its tariff language regarding billing and payment options and Petitioner's rules and regulations.

Bruce T. Haas, Regional Director of Operations for the Midwest Region of Utilities, Inc., testified regarding Petitioner's water and wastewater operations. Mr. Haas explained that Petitioner provides service to approximately 190 customers located in Jasper and Newton Counties. He indicated the WSCI water distribution system contains approximately 13,200 linear feet of water mains. According to Mr. Haas, Petitioner does not provide fire protection, but has flushing hydrants located throughout the system for seasonal flushing and maintenance purposes. He said the wastewater collection system is comprised of two lift stations and includes over 30,400 linear feet of gravity and pressure sewer mains. The sanitary sewage is treated at the 0.155 MGD Wastewater Treatment Plant ("WWTP").

Mr. Haas explained that WSCI staff collects and tests water samples at the point of entry and within the water distribution system on a daily basis. The staff also completes daily operations, equipment repairs and maintenance of assets. They are responsible for submitting complete and accurate monthly reports to the Indiana Department of Environmental Management ("IDEM") and maintaining compliance with all IDEM regulations. They maintain the distribution and collection systems, order and safely store and identify necessary chemicals, complete field activities and respond to customer inquiries as required. Finally, the staff is responsible for reading water meters on a monthly basis.

Mr. Haas testified that when the water and wastewater systems were acquired from Jasper-Newton Utility Company, Inc. in 2001, it became apparent that the existing plant was deteriorating and in need of extensive rehabilitation in order to be compliant with IDEM and other federal and state environmental and safety regulations. Addressing these issues while continuing to provide quality water and wastewater service required WSCI to undertake a number of capital improvement projects. He indicated that Petitioner has invested approximately \$400,000 in its water plant and has invested approximately \$2,550,000 in its sewer plant. He provided a summary of the capital improvements made by WSCI that were not previously reflected in WSCI's rate base, which include the following:

1. Add 13 Water Main Valves to system at a cost of \$27,311.
2. Water Quality and Security Monitoring at a cost of \$10,562.
3. Reline Well #2 and Clean Wells 1 & 2 at a cost of \$95,399.
4. Study for Water Infrastructure at a cost of \$13,685.
5. Remove grit from main & plant A surge tanks at a cost of \$12,870.
6. Install generators at the WWTP and lift station at a cost of \$36,925.
7. Install grating & hand railing at WWTP at a cost of \$9,201.
8. Rehab Liftstation B at WSC (MH Park) at a cost of \$19,458.
9. Replace Deteriorating WWTP – Engineering Evaluation at a cost of \$6,491.
10. Replace 420' of Sewer Main at a cost of \$24,517.
11. Engineering to rehab deteriorating WWTP at a cost of \$103,327.
12. Replace Deteriorating WWTP at a cost of \$2,235,053.
13. Emergency Sewer Main Repair at Yogi Bear Campground at a cost of \$33,888.
14. Lift Station Sewer Pipe Replacements at Yogi Bear Campground at a cost of \$17,164.
15. Emergency Lift Station Rehab at Yogi Bear Campground at a cost of \$42,866.

Mr. Haas provided further testimony regarding the WWTP. He stated that when WSCI acquired the wastewater system in 2001, the existing wastewater package plants were approximately 25 years old, while the equalization basin was approximately 35 years old. He noted that Petitioner's examination of the existing WWTP indicated that it suffered from significant physical deterioration and would not be able to meet the needs of Petitioner's customers and remain compliant with environmental regulations. In light of the condition of the old WWTP, Mr. Haas said an engineering study was conducted to determine whether the costs of continuing repairs to the existing WWTP would be lower than the cost of constructing a new WWTP.

Mr. Haas testified that the engineering study identified a number of problems with the old WWTP and ultimately recommended that Petitioner replace, rather than rehabilitate, the existing WWTP as the capital costs would be approximately equivalent. Mr. Haas discussed the study's findings regarding the extensive rusting and deteriorated physical state of the existing WWTP. He also discussed the problems with the old WWTP's treatment process, including issues with effluent quality, grit removal and chemical storage conditions. He also noted that at the old WWTP there was an "office" which was constructed out of a clear tarp and mobile home skirting. Paperwork was

completed and miscellaneous testing was conducted from this office. He testified that a water riser came up through the floor to supply staff with water as needed and there were no bathroom facilities available at the old WWTP. Employees had to use hand sanitizer to wash their hands above one of the basins while utilizing a garden hose, or forced to go to a local gas station to use restroom facilities.

Mr. Haas also testified regarding the new WWTP. He stated that in light of the substantial problems with nearly all of the components of the old WWTP, Petitioner engineered an entirely new WWTP that replaced the existing structures, with the exception of the secondary sludge tank. He said the old WWTP was entirely removed and replaced with new structures, including an influent zone, two activated sludge package treatment plants, an effluent zone, storage building, blowers, chemical room and scales. Petitioner also installed an actual office in which the plant operators are able to work and perform necessary process control testing, and which also includes proper restroom facilities. A separate room also houses the new blowers/aeration equipment, which greatly reduces the noise generated by the WWTP's blowers.

Mr. Haas testified regarding Petitioner's water and service quality. He said Petitioner does not currently have any issues with its water quality and is in compliance with all applicable water quality regulations and standards. He explained most of the intermittent instances of discolored water during the past twelve months occurred after a flushing or a main break situation. With respect to the sewer collection system, Mr. Haas explained that Petitioner at times, is finding extraordinary material in the collection system that has caused issues with the main lift station that serves the community. He added that these situations have been repaired prior to any customer being affected.

Finally, Mr. Haas testified briefly regarding the nature of the customer complaints received within the last twelve months. He stated the majority of the complaints within the past twelve months have been related to high water usage. He explained that almost all of the issues have been due to leaks in a customer's plumbing system, which causes excessive usage to occur through the water meter. He said that Petitioner has also received a few calls regarding discolored water, but these issues have been resolved by additional flushing in areas of the system.

B. OUCC's Case-in-Chief. Harold H. Riceman, Utility Analyst for the OUCC, discussed various proposed adjustments to WSCI's test year operating revenues and expenses. He also identified supporting schedules and attachments.

Mr. Riceman indicated that WSCI has requested an 8.5319% weighted cost of capital return on an original cost rate base of \$568,090 or rates that will yield an operating income of \$48,477 and a net revenue requirement of \$76,710 for water service. He explained that applying the Petitioner's proposed gross revenue conversion factor of 169.5818% results in a recommended revenue increase of \$130,087. Mr. Riceman further stated that per the Petitioner's case-in-chief, the average residential customer's water service bill will increase 216% over present rates. However, based on present rate water operating revenues subject to increase of \$72,629, Mr. Riceman calculated that the overall rate increase proposed by Petitioner is actually 179.11%. Mr. Riceman stated that Petitioner inadvertently misallocated purchased power costs between its water and sewer utilities, such that purchased power costs for its water utility should have been \$42,803 less than originally proposed. Removing this expense from Petitioner's revenue requirement yields a proposed overall rate increase of approximately 79%.

Mr. Riceman proposed a net operating income of \$38,755 which requires an overall operating revenue increase of \$45,673 per year or an overall increase of 62.05% to Petitioner's water rates. He recommended the Commission approve a Cost of Equity of 9.25% and a weighted cost of capital of 7.9332%. Mr. Riceman disagreed with Petitioner's calculation of rate base and recommended a water rate base of \$485,751.

With respect to Petitioner's sewer service, Mr. Riceman testified that the Petitioner has requested an 8.5319% weighted cost of capital return on an original cost rate base of \$2,685,618 or rates that will yield an operating income of \$229,126 and a net revenue requirement of \$223,176. He stated that applying the Petitioner's proposed gross revenue conversion factor of 169.5214% results in a recommended revenue increase of \$378,332. Mr. Riceman further stated that per the Petitioner's case-in-chief, the average residential customer's sewer service bill will increase 57% over present rates. However, based on present rate sewer operating revenues subject to increase of \$121,969, Mr. Riceman calculated Petitioner's overall rate increase to be 310.19%. In addition, Mr. Riceman explained Petitioner inadvertently misallocated purchased power costs between its water and sewer utilities, such that purchased power costs for its sewer utility should have been \$39,061 more than originally proposed. Including this expense in Petitioner's revenue requirement yields a proposed overall rate increase of approximately 364%.

Mr. Riceman recommended the Commission authorize an overall increase of 268.04% in Petitioner's sewer rates to produce an increase in revenues of \$334,034 per year. He also recommended that the Commission approve a Cost of Equity of 9.25% and a weighted cost of capital of 7.9332%. He stated that the OUCC disagreed with Petitioner's calculation of its rate base and recommended a sewer rate base of \$2,567,437.

Mr. Riceman also discussed the various adjustments the OUCC proposed to Petitioner's rate base, operating expense and revenues. The OUCC proposed a different working capital amount than Petitioner, based on the OUCC's proposed test year expense adjustments and the exclusion of purchased power costs. The OUCC accepted Petitioner's proposed billing determinant revenue adjustment and proposed an additional normalization adjustment to account for customer growth during the test year. The OUCC proposed to use the Commission's composite depreciation rates for Petitioner's vehicles and computers and removed land costs from Utility Plant in Service. Mr. Riceman proposed adjustments to Utility Receipts Tax and State and Federal income taxes.

Margaret Stull, Senior Utility Analyst for the OUCC, testified regarding Petitioner's proposed rate base. She also proposed an increase to water periodic maintenance expense to reflect the annual cost of well cleaning and other maintenance costs. She discussed the OUCC's recommendations regarding rate case expense. She also indicated the OUCC had concerns regarding certain non-recurring charges.

Ms. Stull noted WSCI's acquisition adjustment was approved in Cause No. 42969 and indicated that the OUCC agreed with the return on the acquisition adjustment included in Petitioner's rate base for its water utility. Ms. Stull's testimony indicated that the OUCC disagreed with Petitioner's inclusion in its revenue requirement of the "return of" or amortization of this acquisition adjustment. Ms. Stull explained that in Cause No. 42969, while an acquisition adjustment was approved, only a "return on" this acquisition adjustment was allowed, not a "return of." She added that Petitioner did not provide any support for a "return of" the acquisition on the

water utility in its case-in-chief. Consequently, Ms. Stull stated it was not appropriate to include this amortization expense in the revenue requirement.

She also indicated that the OUCC agreed with Petitioner's proposed adjustments for the vehicles and computers allocated from the Service Company. She proposed additional adjustments to Petitioner's rate base to remove certain items that appear to be operating expenses rather than capital. She also proposed to eliminate "double" capitalization of well pumps and motors installed in 2010.

Ms. Stull testified that she reviewed invoices provided by Petitioner and identified several items that were better described as maintenance costs rather than capital costs. This resulted in a total adjustment of (\$40,305) to rate base, with corresponding adjustments made to operating expenses for most of the items removed from rate base. She further proposed to remove from rate base costs associated with pumps and motors that were installed by Petitioner in 2010 when power interruptions caused its well pumps and motors to burn out. According to Ms. Stull, the costs incurred in 2010 were a result of an "accident" and should be covered by either the electric provider or Petitioner's insurance. She said it did not appear that the costs for the 2007 pumps and motors were removed from rate base when the 2010 replacement pumps and motors were installed, and thus it was appropriate to remove the 2010 expenditures from rate base. Finally, she made an adjustment to remove the appropriate amount of accumulated depreciation for each of the adjustments she proposed.

Ms. Stull noted that WSCI proposed a total rate case expense of \$201,508, including internal labor (Service Company Support Services) costs of \$109,305. She indicated that the OUCC proposed to eliminate all internal labor costs included in rate case expense. Ms. Stull expressed concern that the amount of rate case expense proposed by Petitioner was high given Petitioner's small customer base and noted that Petitioner's affiliate Twin Lakes Utilities, Inc. ("Twin Lakes") sought recovery of a lower level of rate case expense despite being a larger utility. She explained that \$14, or approximately 20%, of each residential customer's monthly bill, represents recovery of Petitioner's estimated rate case expense. She noted the amount of internal time that WSCI estimated would be spent on this case is unusually large. She explained that WSCI's main accounting or rate case expert alone estimated 700 hours, of which 339 hours was allocated to the water utility, for this relatively basic water utility rate case. She further noted that 339 hours equates to 42 business days or more than 8 weeks of work on a single small water utility rate case. Overall, WSCI estimates a total of 2,194 hours of internal employee time for this case for a total of \$109,305 of internal employee labor costs, of which, 1,063 hours were allocated to the water utility for a total of \$52,953. Ms. Stull testified that WSCI has provided no support for its estimated rate case expense and legal costs are no exception. She also expressed concern that the inclusion of internal labor costs in rate case expense could result in double recovery of such costs. Ms. Stull proposed to eliminate internal employee labor costs from Petitioner's rate case expense and to reduce legal fees included in rate case expense from \$85,000 to \$45,000, of which \$21,800 would be allocated to the water utility. She also removed \$4,500 of consultant costs included in rate case expense, noting that Petitioner did not present expert testimony or a rate of return study in this proceeding. Finally, Ms. Stull did not accept Petitioner's proposed three year amortization period for rate case expense. The OUCC proposed a five year amortization period stating that five years more closely reflects the anticipated life of the rates being set in this Cause.

Ms. Stull testified concerning the amortization of contributions-in-aid of construction (“CIAC”). She stated the OUCC disagreed with Petitioner’s proposal to exclude CIAC amortization from operating expenses in this Cause. She indicated that if a utility is going to amortize its CIAC and include accumulated CIAC amortization in its calculation of rate base, it must also include the annual amortization in its operating expenses. Ms. Stull noted the Commission has previously indicated that once a utility elects to amortize CIAC, it must also reduce its depreciation expense accordingly. Ms. Stull further noted that although it is not mentioned anywhere in its case in chief, Petitioner included in its calculation of wastewater rate base a net acquisition adjustment of \$114,157 for both a “return of” and “return on” this amount. Ms. Stull described the OUCC’s positions regarding acquisition adjustments noting that generally, a utility’s rate base should only include the net original cost incurred by the utility first devoting the property to public use. She explained that when a utility is allowed to earn a return on and of a purchase price that is above the property’s original cost, customers will be charged higher rates for the same utility property simply because the utility providing service was acquired by another company. Consequently, the OUCC believes requests for favorable ratemaking treatment on acquisition adjustments should be carefully considered and only granted if adequately supported. The OUCC opposed Petitioner’s inclusion of this acquisition adjustment for the wastewater utility.

Ms. Stull testified regarding Petitioner’s rate design, noting that WSCI did not prepare a cost of service study to support its proposed rate design. She indicated that Petitioner prepared a basic allocation of its revenue requirement between those costs that are “fixed” and best recovered through a flat monthly fee and those costs that are “variable” and are best recovered through a volumetric rate based on customer consumption. She indicated that although it would be preferable to have a cost of service study to support the cost of serving each customer class, the OUCC does not recommend one at this time as the preparation of a cost of service study would be unduly burdensome based on the size of this utility. Ms. Stull testified the OUCC accepted Petitioner’s methodology for this utility, and noted that the same methodology was used by Twin Lakes in Cause No. 43957 and by Indiana Water Service, Inc. in Cause No. 44097. She stated the OUCC accepted this rate design in both Causes and the Commission authorized this rate design in the Twin Lakes rate case.

Ms. Stull testified that Petitioner proposed to eliminate its current declining block water rate structure in favor of a rate design that includes a monthly base facility charge plus a volumetric consumption charge. She explained that the monthly base facility charge is designed to recover WSCI’s fixed costs and varies based on the customer’s meter size. The volumetric charge is a flat rate per thousand gallons based on a customer’s consumption during the billing period and is designed to recover Petitioner’s variable costs. The base facility charge and volumetric charge are the same for both residential and commercial customers. Ms. Stull recommended two changes to Petitioner’s proposed rate design. First, she proposed to allocate capitalized labor on a 50% fixed/50% variable basis, consistent with the allocation of salaries and wages. Second, she proposed to recover miscellaneous income equally through the fixed base facility charge and through the volumetric rate. Ms. Stull indicated the OUCC’s proposal equates to an across-the-board increase of 62.05%.

Ms. Stull next testified regarding Petitioner’s non-recurring charges. She indicated WSCI’s proposed increase to its reconnection fee from \$10.00 to \$37.50 should be considered reasonable, although she disagreed with some of the salary rates WSCI used to calculate its revised charges. Ms. Stull expressed concern with the proposed changes in the description of the reconnection charge

and in particular the language regarding rates to be charged to seasonal customers. She accepted WSCI's proposed NSF charge of \$25 as well as WSCI's proposed new customer charge of \$25. She testified that the OUCC accepted Petitioner's proposed late payment charge, noting that it follows the Commission's late payment rules.

Ms. Stull provided additional testimony concerning the wastewater utility. She noted the increase in rate base of \$2,273,247 since Petitioner's last rate case is the primary driver of the requested rate increase in this Cause. The increase is due primarily to the replacement of WSCI's wastewater treatment plant. She explained that WSCI proposes a rate base of \$2,685,618 including a net acquisition adjustment of \$114,157, working capital of \$10,778 and net CIAC of \$2,053. WSCI's proposed rate base also includes adjustments to vehicles and computers allocated from the Utilities, Inc. Finally, Petitioner's rate base is reduced by customer deposits and accumulated deferred income taxes.

Jeffrey Fish, Utility Analyst for the OUCC, testified regarding Petitioner's operations, recent system improvements and customer concerns and complaints received at the Commission's public field hearing on May 2, 2012. He also discussed cost-saving options that were available when Petitioner decided to rebuild its WWTP. He also provided testimony about his recommendation of the Commission approving certain non-recurring charges in Petitioner's proposed Schedule of Rates and Charges for Water Service.

Mr. Fish testified that Petitioner's water utility serves approximately 194 customers, which include 28 residential, 141 mobile homes, and 25 commercial customers. He stated that the water system consists of two wells, one treatment plant, a hydro-pneumatic pressure tank and distribution mains. He stated that because Petitioner only has the 2,200-gallon hydro-pneumatic pressure tank, it does not have a one-day storage supply of treated water and cannot supply fire protection. Mr. Fish also indicated that the well pumps must operate almost continuously to provide and maintain system pressure.

Mr. Fish testified that Petitioner completed a comprehensive study of its water system in October 2007. He indicated that the study looked at many aspects of the water system, but ultimately made recommendations that included: 1) acquiring another source of water supply for redundancy, 2) providing additional storage capacity (one-day supply tank), 3) purchasing a scale for weighing the sodium hypochlorite solution, and 4) installing a secondary containment system for the sodium hypochlorite solution. Although Petitioner has not implemented these recommendations, he believed each has good merit.

Mr. Fish testified that Petitioner indicated it had completed several capital projects in recent years. He said that Petitioner installed thirteen new water main isolation valves in the distribution system to minimize service outages. WSCI also installed water quality monitoring equipment to test for chlorine residuals and turbidity once it began providing disinfection treatment. He noted that WSCI also completed a major renovation of both wells in 2006, which work included cleaning both wells, relining both wells, and installing new pumping and electrical equipment in both wells and installing new piping and variable frequency drives for both wells.

Mr. Fish indicated that Petitioner experienced voltage fluctuations and power interruptions in its electrical service causing its well pumps and motors to burn out in 2010, which resulted in replacement of major components of both Well No.1 and Well No.2 within a period of four and one-

half years. He noted the well components should last much longer under normal circumstances. He provided additional testimony concerning the replacement costs, the frequency of replacements and Petitioner's improvements to prevent electrical damage by installing an emergency generator to provide electrical power for both wells and its water treatment plant. He stated that Petitioner's projects were reasonable and found all of the associated equipment to be used and useful. He recommended a 5-year interval for periodic well cleaning. He noted that Petitioner's meter change-out program is just beginning and that Petitioner plans to replace 10% of its manual read water meters each year with new Automatic Meter Reading ("AMR") water meters. He added that AMR water meters provide a valuable resource of information that can help resolve customer-billing issues and is reasonable.

Mr. Fish described how Petitioner constructed a new Class I, 0.155 MGD extended aeration WWTP consisting of flow equalization, secondary clarification, aerobic digestion, effluent chlorination/dechlorination, and effluent metering. He said Petitioner also operates and maintains two (2) lift stations that pump sewage to WWTP. He further added that the collection system is comprised of 100% sanitary sewers, which include approximately 30,400 linear feet of pipe, 650 feet of force main, 136 manholes, including the Campground sewage collection system. Mr. Fish noted that Petitioner's water utility and sewer utility serve a similar customer base of approximately 190 customers, but the sewer utility has a much larger user base when adjusting for the Campground, which has approximately 692 sewer-only customers.

Mr. Fish stated that the Petitioner's operation and maintenance duties include collecting wastewater samples, monitoring water quality and performing water quality tests as defined in its National Pollutant Discharge Elimination System ("NPDES") Permit No. IN0039101 issued by IDEM. He testified that based on his inspection of Petitioner's WWTP, collection system and analytical reports, Petitioner's operation and maintenance performance is acceptable at this time.

Mr. Fish noted that in 2004 Petitioner hired McMahon Associates, Inc. ("McMahon") to perform a comprehensive study of its sewer treatment plant. McMahon prepared a report, titled Wastewater Treatment Plant Evaluation ("2004 WWTP Evaluation"), which assessed the condition of the existing WWTP and recommended a plan to rehabilitate or replace Petitioner's WWTP. Mr. Fish advised the 2004 WWTP Evaluation indicated that the existing WWTP performance had been excellent and in substantial compliance with NPDES requirements. The 2004 WWTP Evaluation also indicated that Petitioner constructed the WWTP over a period of years ranging back to the 1960's with subsequent additions and expansions in the 1970's. The 2004 WWTP Evaluation also indicated that the sidewalls of the steel tanks, steel support brackets, steel framing, and steel air supply headers were all experiencing measurable signs of corrosion. The 2004 WWTP Evaluation indicated that the components showing signs of corrosion would need to be repaired to prevent tank failure. Mr. Fish also noted that the 2004 WWTP Evaluation recommended Petitioner retain and repair the existing package plants for an estimated cost of less than \$300,000, which would result in a minimum 15 year additional life.

Mr. Fish testified that Petitioner did not follow the 2004 WWTP Evaluation recommendations to repair to the WWTP. Mr. Fish noted Petitioner had another engineering report conducted with a purpose very similar to that of the 2004 WWTP Evaluation. The 2006 WSC Wastewater Treatment Plant Engineering Report ("2006 Engineering Report") was prepared by Strand Associates, Inc. The 2006 Engineering Report recommended replacement of the equalization tank, package plants, and chlorine contact tank with a new submersible influent

pumping station, new reinforced-concrete package plant, and new reinforced-concrete chlorine contact tank with new chlorination/dechlorination chemical feed systems. Mr. Fish noted the overall construction cost of the proposed new facilities was estimated to be \$1,558,000.

Mr. Fish testified that Petitioner was not compelled to construct the new WWTP by any regulatory agency and Petitioner was fully compliant with all NPDES permit limits when deciding to construct its new WWTP. Mr. Fish indicated that building a new WWTP was not a less costly option than repairing the existing WWTP. He noted Petitioner's lowest cost option would have been to repair the WWTP as outlined in the 2004 WWTP Evaluation, which would have extended its useful life for 15 years and the avoided the cost of constructing new facilities. Petitioner made the management decision to construct new facilities at an estimated cost of \$1,558,000. Mr. Fish cited the 2006 Engineering Report and testified that constructing a new WWTP was a reasonable, but more costly option given the condition of the WWTP in 2006. Mr. Fish noted that the return on and return of this new plant (the \$1.558 million cost of the new WWTP) is the major driver of Petitioner's proposed sewer rate increase. He added that based on the 2004 WWTP Evaluation, a significant portion of the rate base additions and the proposed rate increase could have been avoided if Petitioner had made the recommended WWTP repairs in 2004. Mr. Fish also noted that Petitioner completed several improvement projects to the original WWTP that included: removal of grit from Main and Plant A surge tanks, installation of generators at the WWTP and main lift station, installation of grates and handrails at the WWTP, renovation of Lift Station B at the Island Grove mobile home park and replacement of 420 feet of sewer main.

Mr. Fish testified that the customer comments that had been received indicated that a large water and sewer rate increase may have a devastating impact on many customers, with the Campground being particularly impacted by the increase. He explained that the Campground is Petitioner's largest commercial customer and uses sewer-only service for seven months of each year, during camping season. He raised a concern that Petitioner could be placing itself in a position to lose the Campground as a customer. He added that customers expressed concern about poor water quality and repeated service outages that led to boil orders. He explained that business owners expressed concern that the proposed rate increase, combined with added costs and lost revenues associated with water service outages, could cause them to close up their businesses. Mr. Fish added that although the improvements are beneficial, commercial and residential customers alike expressed concern that the proposal for increased water and sewer rates will be overwhelming to the community and the Petitioner may be facing a potential loss of customer base if its proposal for new rates and charges are approved as presented.

Mr. Fish next addressed certain of Petitioner's non-recurring charges. Mr. Fish considered Petitioner's Connection Charge as a typical "Tap Fee" and noted that Petitioner does not distinguish between residential and non-residential water connections. He testified that Petitioner's current water Connection Charge price ranges from \$150 for 5/8-inch & 3/4-inch water meters to \$300 for 2-inch and above water meter. He explained that Petitioner requested a new water Connection Charge based on an estimate from a local contractor and, according to Petitioner's estimate, customers will pay an additional \$1,600 for directional boring and an additional undefined amount for copper tubing provided beyond ten (10) feet. He testified that the current water Connection Charge ranging from \$150 to \$300 would typically not cover the cost of excavation, tapping, and installing a new water service line to a residential or non-residential customer, however, Petitioner's proposed \$1,800 water Connection Charge (for a 10-foot tap) and \$1,600 road boring fee seems excessive for water connections.

Mr. Fish's proposed alternative to the water Connection Charge would be that Petitioner could propose that customers hire a licensed and bonded contractor to install the tap and water line at the customer's expense and if Petitioner were so inclined, he would support an inspection fee to ensure the work meets its standards. He recommended that the Commission deny Petitioner's proposal for a new Connection Charge as presented based on (1) the insufficient estimates supporting this charge, and (2) the relatively high-proposed cost to customers.

Mr. Fish noted that Petitioner's current sewer connection fee is \$400 and Petitioner has proposed a sewer Connection Charge of \$2,010. Mr. Fish recommended the Commission deny Petitioner's proposed sewer Connection Charge as presented based on insufficient estimates supporting this charge and the relatively high-proposed cost to customers. However, he supported the idea of permitting customers to hire a licensed and bonded contractor to install the connection at the customer's expense.

Mr. Fish testified that after-hours call outs are manageable without discouraging customer calls with a charge. He explained that allowing Petitioner to impose this charge could discourage customers from calling after hours when emergency services do arise and opined that the charge was unreasonable. He also described how Petitioner's proposed Meter Testing Fee would work indicating that it was an acceptable and reasonable method for testing water meters and recommended Commission approval of the fee.

Mr. Edward Kaufman, Senior Utility Analyst for the OUCC, responded to Mr. Neyzelman's proposed 10.44% cost of equity. He testified that his analysis supported a range of cost of equity of 9.0% to 9.6% for Petitioner at this time and estimated Petitioner's authorized cost of equity for ratemaking purposes should be 9.25%. Mr. Kaufman raised concerns regarding WSCI's averaging the authorized costs of equity of seventeen (17) sister companies that received rate orders by state commissions during 2010 and early 2011 without demonstrating that each utility is reasonably comparable to Petitioner. He agreed with Petitioner's decision to avoid the cost of paying for a cost of equity witness, but testified that Petitioner's proposed cost of equity is unreasonably high and exceeds current investor expectations.

Mr. Kaufman testified that he did not complete a full cost of equity analysis, but relied upon the analysis provided by Petitioner and recent OUCC cost of equity estimates provided to the Commission. He explained that his cost analysis produced a range of cost of equity for the water industry of 7.71 % to 9.45%. He also indicated that he gave the most weight to methodologies that were most consistent with past Commission orders. These methodologies produced a range of estimates of 7.71 % to 8.44%. He testified that Indiana American Company Inc.'s ("Indiana American") risk in Cause No. 44022 was similar to the water industry and that the OUCC recommended a cost of equity of 8.6% in that case. He said that if he had performed a thorough cost of equity analysis in this case, it would be similar to the one he completed in the Indiana American rate case. He acknowledged that Indiana American is larger than Petitioner and that he would recognize Petitioner's specific risk by making a company specific risk adjustment, similar to the one made in an earlier Twin Lakes rate case, Cause No. 43128. Mr. Kaufman also testified that his analysis in this case would be different than what he filed in Indiana American because interest rates had started to decline and that decline was not fully reflected in his estimated cost of equity in that case.

Mr. Kaufman explained that he used the estimated cost of equity from the Indiana American rate case to establish the low end (8.6%) estimated cost of equity. He then used Petitioner's analysis (removing Sky Ranch) to determine the high end (10.4%) range of estimated cost of equity. However, he further stated that considering current market conditions and Petitioner's size, the low end of his range was unreasonably low and the high end was unreasonably high. He indicated that because Petitioner is smaller than Indiana American, it is appropriate to recognize Petitioner's smaller size and increased risk. Mr. Kaufman believed, based on his analysis, that a range of 9.0% to 9.6% is reasonable for Petitioner at this time and recommended the Commission authorize a cost of equity of 9.25%. Mr. Kaufman noted that Utilities, Inc.'s capital structure had a higher equity ratio in this case than in the Twin Lakes case. The higher equity ratio would result in lower financial risk. Mr. Kaufman also testified that his proposed company specific risk adjustment might be overstated because Petitioner is owned by a large multi-state utility holding company (Utilities, Inc.), which is held by an even larger multi-national company (Corix Utilities), who in turn is held by an even larger multi-national company (British Columbia INvestment Management Corporation or bcIMC).

Mr. Kaufman noted the potential in this Cause for rate shock, which he defined as the psychological and economic effects on customers of a sudden and drastic utility rate hike. He stated that rate shock is compounded when it is experienced by those who can least afford the increase in rates. Mr. Kaufman noted that Petitioner proposes to increase the average monthly sewer rates for customers in the Island Grove mobile home park by 383.19% (\$76.04 per month or \$912.48 per year). He added that commercial sewer customers could see increases of 369.78% to 554.79%. Mr. Kaufman explained that a commercial customer with a 5/8" connection using 10,420 gallons per month would see sewer rates increase from \$51.14 per month to \$259.95 per month. He noted that the Lake Holiday Campground could see an increase of 310.31%. Mr. Kaufman considered it foreseeable that increases of this magnitude would shock Petitioner's customers. Mr. Kaufman recommended the best way to reduce rate shock is to reduce the amount of the rate increase. He added that the proposed increase could also be phased-in over more than one year, but may ultimately be unaffordable.

Mr. Kaufman testified that Petitioner's proposed rate increase could negatively impact Petitioner's two largest customers ultimately distressing the community and harming Petitioner. Mr. Kaufman noted representatives of Autumn Hills Health and Rehab Center and Lake Holiday Enterprises, Inc. provided testimony at the field hearing which asserted that Petitioner's proposed rate increase is so large that their companies may cease to exist. Mr. Kaufman indicated the loss of jobs would be felt throughout the community. He also noted the Campground brings in thousands of visitors during the summer months that patronize local businesses. Mr. Kaufman asserted local businesses would see a decline in revenues while their water and wastewater expenses are increasing. Mr. Kaufman added that if either or both these businesses cease to exist and are not replaced by other businesses, WSCI would need to further increase its rates to make up for the lost revenues.

C. Petitioner's Rebuttal Evidence. Mr. Neyzelman provided rebuttal testimony in response to the testimony filed on behalf of the OUCC. He testified that WSCI accepted some of the OUCC's proposed adjustments while opposing others. Based on his rebuttal position, Mr. Neyzelman proposed that Petitioner's rates be increased by 91% for water and 311% for wastewater services.

Mr. Neyzelman testified that the OUCC accepted Petitioner's proposed billing determinant revenue adjustments. He indicated that the OUCC proposed an additional normalization adjustment to water revenues for customer growth during the test year and proposed to normalize wastewater revenues for customer growth during the test year. Mr. Neyzelman noted that for purposes of expediting this rate proceeding WSCI agreed with the OUCC's proposed adjustments related to test year customer growth.

Mr. Neyzelman provided testimony which indicated the OUCC accepted WSCI's adjustments to salaries and wages, capitalization of labor, pension and other benefits, transportation and payroll tax. He explained that for purposes of expediting this rate proceeding, WSCI had accepted the expense adjustments proposed by the OUCC regarding purchased power, utility receipts tax, periodic maintenance expense, depreciation, CIAC amortization, income tax and water Purchase Acquisition Adjustment ("PAA") amortization expense.

Mr. Neyzelman testified that the OUCC's proposed adjustment to salaries and wages inappropriately increases salaries and wages expense related to the proposed removal of internal labor costs from rate case expense. He explained that the OUCC's calculation of this adjustment uses WSCI's allocation methodology in allocating the internal labor costs specifically related to WSCI rate case expense, and then allocating only 0.14% to WSCI. He stated that this adjustment would mean that all Utilities, Inc. subsidiaries and their customers would share the burden of the costs related to WSCI's rate case. He believed it was appropriate to directly allocate these costs to WSCI and therefore included these costs in rate case expense.

Mr. Neyzelman also disagreed with the OUCC's adjustment to legal fees related to rate case expense and the adjustment to remove all Service Company employees' capitalized time related to rate case expense. He noted Ms. Stull's adjustment was to set legal fees related to rate case expense at \$45,000. He testified that Ms. Stull was incorrect when she testified that including WSCI's employees' capitalized time would result in the double recovery of labor costs. He opined that once the labor allocation methodology is understood, it is clear that the recovery of internal rate case expense does not produce a double recovery. He testified that all salary and wage costs are allocated to WSCI from the Service Company, either through a direct allocation or through the use of allocation factors. He indicated that when a WSCI Employee books their time to a rate case, the amount sits in a Construction Work in Progress ("CWIP") account just like any other project instead of being recorded to the salary and wage account. He further testified that once the project is completed or placed in service it then becomes a deferred rate case expense. Mr. Neyzelman testified that in the filing schedules included with the company's Case-in-Chief, WSCI did not include any deferred charges in rate base, nor did it seek recovery of the unamortized portion of rate case expense. He noted that the capitalized time amounts that are booked are offset in the salaries and wages expense. He stated that removal of the capitalized time from rate case expense would deny recovery of prudently incurred capitalized time spent preparing and supporting this rate case, and that this expense is not included anywhere else in the filing. Mr. Neyzelman indicated that WSCI disagreed with the OUCC's proposed amortization period of five (5) years. He noted that the Commission approved a four year amortization period in Twin Lakes Utilities, Inc.'s recent rate case, Cause No. 43197 and testified that for consistency and purposes of expediting this rate proceeding, a four (4) year amortization period is appropriate and should be approved.

Mr. Neyzelman stated that the OUCC accepted WSCI's rate base adjustments for the water PAA and rate base allocations from the Service Company. He testified that the OUCC proposed to

modify or reject some of WSCI's proposed rate base adjustments and proposed additional rate base adjustments. He agreed with most of the OUCC's rate base adjustments for purposes of expediting this rate proceeding and accepted the following adjustments proposed by the OUCC: working capital (to the extent that any changes to operating expense will flow through the working capital calculation), reclassification of capitalized expenses, removal of certain pump and motor capitalized items and the associated adjustment to accumulated depreciation.

Mr. Neyzelman testified that WSCI did not agree with the adjustments to wastewater PAA amortization expense that were proposed by the OUCC. He noted that WSCI has not filed a wastewater rate case since the system's acquisition and per books PAA amount is the appropriate amount booked at acquisition. He indicated that the OUCC incorrectly assumed that the PAA should be removed in its entirety and that to the extent the Commission was to approve the Company's requested PAA, an appropriate amount of PAA amortization expense should also be included.

Mr. Neyzelman testified that WSCI disagreed with the OUCC's recommended cost of equity of 9.25%. He believed that the Commission should approve a cost of equity of 10.2%, which he argued was consistent with the cost of equity recently proposed in the Twin Lakes rate case. Mr. Neyzelman also recognized that the Commission ultimately approved a lower cost of equity for Twin Lakes.

With respect to rate design, Mr. Neyzelman testified that Petitioner accepted the OUCC's recommendation to allocate capitalized labor and miscellaneous income equally through the fixed base facility charge and volumetric charge, for purposes to expedite this rate proceeding. He indicated that while he was sympathetic to the OUCC's desire to mitigate the impact of the proposed rate increase he did not agree with the OUCC's recommendation to phase in wastewater rates over a three year period, explaining that with the adjustments accepted on rebuttal, the rates can and should be implemented in a single phase. He testified that to the extent the Commission was to phase in rates, it should do so over a two year period and should include carrying costs based on the Company's weighted average cost of capital. He added that the carrying costs will be necessary since the Company will not be recovering sufficient revenues to cover the cost of providing safe and reliable service to its customers.

Mr. Neyzelman provided testimony concerning WSCI's proposed changes to its non-recurring charges and noted the OUCC accepted the inclusion of Petitioner's proposed NSF, New Customer, Meter Testing and Late Payment Charges. He indicated WSCI disagreed with the OUCC's recommendations to change WSCI's proposed language for the water reconnection charge. He further stated that WSCI's proposed language is reasonable because it ensures customers pay only the actual cost of reconnecting their wastewater service.

Mr. Neyzelman indicated that Petitioner agreed to accept the OUCC's recommendation regarding the company's proposed water and wastewater connection charge. He testified that WSCI is willing to adopt tariff language indicating that customers are responsible to hire a licensed and bonded contractor to install the tap and water or wastewater line at the customer's expense. He also recommended the Commission approve an inspection fee of \$50 to cover the Company's costs in reviewing the work to ensure that it meets applicable standards. Finally, he testified that the Company is willing to withdraw its request for an after-hours charge for purposes of expediting the relief sought in this proceeding.

6. **Commission Discussion and Findings.** An investor-owned utility calculates rates by first determining the return on rate base. Rate base is the amount of capital the utility needs to use to provide regulated services. The return on rate base calculation determines what the net operating income (“NOI”) should be in order to provide a reasonable return to the shareholders. Next, a determination is made as to the amount of the adjusted or *pro forma* operating income based on the utility’s current rates. The *pro forma* amounts are based upon the known test year revenues and expenses updated to include changes that are fixed within the time period, known to occur and are recurring, and are measurable in amount. By subtracting the NOI determined through the adjustment process from the NOI required by the return on rate base, the dollar amount of the increase needed to achieve the NOI that is expected to provide a reasonable return to the shareholders can be determined. The increase in NOI is then adjusted for taxes and fees related to the increased revenue and income.

In its Case-in-Chief, Petitioner proposed net revenue requirement increases of \$130,087 and \$378,332, for an overall rate increase of 179.11% and 310.19%, for its water and wastewater operations, respectively. The OUCC proposed net revenue requirement increases of \$45,672 and \$334,034, for an overall rate increase of 61.88% and 268.04%, for Petitioner’s water and wastewater operations, respectively. In rebuttal, Petitioner largely accepted the OUCC’s adjustments, resulting in proposed net revenue requirement increases of \$67,362 and \$388,253, for an overall rate increase of 91.26% and 311.55% for water and wastewater, respectively. The tables below summarize the revenue requirements as presented by both Petitioner and the OUCC:

Comparison of Petitioner’s and OUCC’s Revenue Requirements (Water)

Revenue Requirements:	<u>OUCC</u>	<u>WSOI Rebuttal</u>
Original Cost Rate Base	485,751	487,823
Times: Weighted Cost of Capital	7.94%	8.42%
Net Operating Income Required	38,555	41,051
Less: Adjusted Net Operating Income	10,236	(716)
Additional NOI Required	28,319	41,767
Times: Gross Revenue Conversion Factor	1.61278	1.61278
Recommended Revenue Increase	45,672	67,362
Calculated Percentage Increase	61.88%	91.26%

Comparison of Petitioner’s and OUCC’s Revenue Requirements (Wastewater)

Revenue Requirements:	<u>OUCC</u>	<u>WSOI Rebuttal</u>
Original Cost Rate Base	2,567,437	2,683,798
Times: Weighted Cost of Capital	7.93%	8.41%
Net Operating Income Required	203,723	225,739
Less: Adjusted Net Operating Income	(3,465)	(15,080)
Additional NOI Required	207,188	240,819
Times: Gross Revenue Conversion Factor	1.61222	1.61222
Recommended Revenue Increase	334,034	388,253
Calculated Percentage Increase	268.04%	311.55%

A. Rate Base and Rate of Return. The OUCC and Petitioner largely agreed on the calculation of Petitioner's rate base, the only differences being \$2,204 in working capital for wastewater, \$2,072 in working capital for water and Petitioner's proposed inclusion of a net acquisition adjustment of \$114,157 to its wastewater rate base. With respect to the amount of working capital, the OUCC's calculation reflected the OUCC's reduced level of rate case expense and its proposal to eliminate all internal labor costs included in rate case expense and to recover these costs through an increase in annual salaries and wage expense. Considering the evidence presented by the parties regarding *pro forma* operating expenses as discussed further below, the Commission finds proper working capital allowances for Petitioner's water and wastewater utilities should be \$5,104 and \$6,725, respectively.

1. Addition of New WWTP. WSCI provides water service to approximately 190 customers and wastewater service to approximately 882 customers when adjusted to include the seasonal campground customers. WSCI constructed a new WWTP in 2007 at a cost of \$2,125,042. Given the low number of wastewater customers, the inclusion in rate base of WSCI's new WWTP would create a significant increase in those customers' monthly rates.

The Commission notes that prior to constructing its new wastewater treatment plant in 2007, Petitioner had secured two engineering studies to assess the condition of its WWTP, which had been constructed over a number of years beginning in the 1960's with subsequent additions and expansions in the 1970's. The first of these studies was performed in 2004 by McMahon Associates, Inc. The 2004 WWTP Evaluation identified some deficiencies in the WWTP, but indicated Petitioner should retain and repair the existing package treatment plant for approximately \$300,000, which would result in extending the life of the plant by at least 15 years. The evidence shows that WSCI did not perform the repairs recommended in the 2004 WWTP Evaluation. WSCI subsequently had another engineering study performed on its WWTP. The 2006 Engineering Report was prepared by Strand Associates, Inc. The 2006 Engineering Report provided WSCI with several options including: renovation of existing extended air package plants at an estimated cost of \$589,600; installation of a mechanically aerated concrete package plant at an estimated cost of \$1,558,000; or installation of a steel package plant at an estimated cost of \$2,409,800. The 2006 Engineering Report did not suggest repairs that could extend the useful life of the plant by 15 years for less than \$300,000 as recommended in the 2004 WWTP Evaluation. The 2006 Engineering Report recommended the second option of installation of a mechanically aerated concrete package plant based on "significant risk that the smaller package plant is not adequately sized to treat the daily average flow into the plant and effluent NPDES permit violations could occur" noting that average daily treatment capacity would be reduced to one third of normal capacity during construction. OUCC's Ex. 3, Attachment 5 at page 13. The evidence demonstrates that Petitioner chose the second option, although the cost of replacing the plant exceeded the \$1,558,000 estimate by \$567,042.

At the evidentiary hearing, the Commission asked Petitioner's witness Mr. Haas to explain why one plan of action was chosen over the other. Mr. Haas testified that he was not involved in the operations of WSCI until June of 2010 and did not participate in the decisions made with respect to the 2004 and 2006 engineering reports. Mr. Haas did not know who at Utilities, Inc. or WSCI was involved in making the decision to invest in a new WWTP. In response to questions from the OUCC and the Presiding Officers, Mr. Haas testified that replacing the plant would ensure that all regulations and all NPDES permit requirements were met. Mr. Haas advised that, based on conversations with operations staff and his participation in a plant tour of the WWTP in 2005 or

2006, he understood the condition of the plant made repairing the plant imprudent. Mr. Haas also indicated he is not a professional engineer and therefore determining the relative cost of replacing plant, as opposed to repairing it, and the number of years that may be added by repairing the plant are not within his particular expertise.

At the evidentiary hearing, the Presiding Officers directed Petitioner to provide additional information regarding the decision to replace, rather than repair, the old WWTP. Petitioner submitted its Late-Filed Exhibit No.1 with attachments in response to that directive. Petitioner's brief response indicated repairing the old WWTP rather than replacing it would only serve as a temporary fix and that additional investment would be needed in the foreseeable future to repair more portions of the plant that would continually deteriorate.

As part of its response, Petitioner submitted a comparison of actual cost to build the WWTP versus the estimated costs. The comparison noted WSCI did not have sufficient detailed information to provide the requested comparison between the estimated cost of \$1,558,000 and actual cost of \$2,125,042 to build the WWTP. Petitioner indicated the primary driver of the cost difference is that the ultimate design of the WWTP differed significantly from the design assumed for purposes of the 2006 Engineering Report. The initial cost estimate assumed that a single circular structure package plant would be installed at WSCI to replace the two existing rectangular package plants. WSCI noted that during the design phase of the WWTP project it was determined that rather than having one large structure to serve this purpose it would be preferable to have two smaller structures of equal size to enable taking one half of the plant offline for servicing while still being able to serve the community with wastewater service. This design change increased the costs estimated in 2006 Engineering Report. It appears that Petitioner's design changes resulted in system redundancy of treatment processes that were neither reasonable nor necessary. These design changes increased the costs substantially and are not supported by the evidence. Petitioner did not provide any documentation or other information supporting its decision to replace rather than repair its WWTP. Petitioner failed to provide the Commission with information demonstrating the cost incurred to replace rather than repair the old WWTP was both prudent and necessary.

The Commission has taken into consideration the evidence presented, including both the 2004 WWTP Evaluation and the 2006 Engineering Report, in determining whether Petitioner's costs associated with construction of its new WWTP were reasonable and necessary. The reports made recommendations and provided several options WSCI could take to address its concerns with its WWTP. By making the decision to install a mechanically aerated concrete package plant that differed significantly from the design assumed for purposes of the 2006 Engineering Report and at increased costs, WSCI ultimately chose to pursue an option that was not recommended in either report. In light of the significant ratemaking effect such a decision would have on WSCI's small number of customers and these difficult economic times, it is particularly important that WSCI and its parent, Utilities, Inc., exercise prudence in its decision making with respect to major plant additions. The Commission finds the evidence of record insufficient to determine that WSCI's decision to construct the new WWTP at a cost of \$2,125,042 was necessary and reasonable. The Commission also notes that Petitioner had available the option to seek pre-approval of significant capital projects under Ind. Code § 8-1-2-23. Therefore, we cannot conclude in this Cause that the cost of \$2,125,042 for Petitioner's new WWTP should be included in Petitioner's rate base. However, because the evidence demonstrates that by the time the 2006 Engineering Report was made replacement of the existing plant would be more prudent due to the worsening condition of the plant, we find Petitioner's decision to replace the plant was reasonable. But, because Petitioner

failed to support its decision to build and design the plant that was ultimately constructed, we find that Petitioner's rate base addition for the WWTP should be limited to the \$1,558,000 estimated cost of replacing the plant design assumed and set out in the 2006 Engineering Report.

The OUCC requested that the Commission order a phase in of the proposed wastewater increase in order to mitigate the effects of the significant increase in rates. While we agree with the OUCC that Petitioner's proposed rate increase would likely create "rate shock" for its customers, the Commission recognizes the need to balance the public interest in just and reasonable rates while providing the utility the ability to produce a reasonable rate of return on its investment. In light of the Commission's decision to reduce the amount to be included in Petitioner's rate base, we find that a phasing in of the rate increase is unnecessary.

2. **Purchase Acquisition Adjustment.** The Commission notes that a return on purchase acquisition adjustment ("PAA") for the water utility was approved by the Commission Order in Cause No. 42969. We further note that Petitioner indicated in its evidence that for purposes of expediting this rate proceeding it had accepted the OUCC's proposed adjustment to exclude water PAA amortization expense. We agree with the OUCC that it is inappropriate to include the water PAA amortization expense in Petitioner's water revenue requirement.

Petitioner included in its calculation of wastewater rate base a net PAA of \$114,157 for both a "return of" and "return on" this amount. The OUCC recommended rejecting WSCI's proposed wastewater PAA of \$114,157 from rate base and that PAA amortization expense be excluded from the revenue requirements. In rebuttal testimony, Petitioner disagreed with the OUCC's proposed adjustments related to wastewater PAA and PAA amortization expense. The PAA and the PAA amortization expense in its revenue requirement for the WWTP has not been previously approved by the Commission and Petitioner offered no evidence to demonstrate the justification for PAA and the PAA amortization expense to be included in its revenue requirements here. Petitioner simply stated that it is appropriate to include its wastewater utility's PAA in rate base because it is the result of an arm's length transaction and was at a reasonable price. Petitioner has not shown it is entitled to an acquisition adjustment on its acquired wastewater system. We note that the property on which Petitioner seeks a PAA has largely been removed from service and replaced with a new WWTP.

The Commission finds that Petitioner's PAA amortization expense for water should not be included in Petitioner's water revenue requirement. We further find that Petitioner did not provide sufficient evidence to show inclusion of the wastewater PAA is reasonable and in the public interest. Therefore, Petitioner's inclusion of \$114,157 for wastewater PAA in its calculation of wastewater rate base should be denied. Accordingly, it is inappropriate to include any wastewater PAA amortization expense in Petitioner's wastewater revenue requirement.

Based on the above discussion, Petitioner's rate base is shown in the following table:

	<u>Water</u>	<u>Wastewater</u>
Utility Plant in Service at 06/30/11	\$ 725,307	\$ 3,077,357
Add: WWTP as Designed	-	1,558,000
Less: WWTP with Design Changes	-	(2,125,042)
Disallowed WWTP Costs	-	(567,042)
Less: Meter Costs	(7,375)	-
Wells & Springs	(32,930)	-
Pumps	(43,844)	-
Vehicle Allocation Adjustment	(6,919)	(7,363)
Computer Allocation Adjustment	(874)	(930)
Gross Utility Plant in Service	<u>633,365</u>	<u>2,502,022</u>
Accumulated Depreciation at 06/30/11	45,739	379,357
Less: Accum Depr - Meters (6 years)	(885)	-
Accum Depr - Wells & Springs (4.5 years)	(2,964)	-
Accum. Depr - Pumps (1 year)	(877)	-
Vehicle Allocation Adjustment	(6,149)	(6,543)
Computer Allocation Adjustment	(847)	(901)
Total Accumulated Depreciation	<u>34,017</u>	<u>371,913</u>
Net Utility Plant in Service	599,348	2,130,109
Add: Acquisition Adjustment, net of accumulated amortization	9,192	-
Working Capital	5,210	6,838
Less: Contributions-in-aid of Construction, net	1,355	2,053
Customer Deposits	1,729	1,840
Deferred Income Taxes	<u>124,836</u>	<u>132,575</u>
Total Original Cost Rate Base	<u>\$ 485,830</u>	<u>\$ 2,000,479</u>

B. Capital Structure and Weighted Cost of Capital. The cost of capital is comprised of three components: capital structure, cost of long-term debt and cost of equity. Both the Petitioner and the OUCC agreed that Petitioner's capital structure is 49.69% long-term debt and 50.31% equity. Furthermore, both parties agree that the cost of Petitioner's long-term debt is 6.60%. Petitioner's Case-in-Chief indicated the cost of Petitioner's long-term debt was derived from a collateral trust note at 6.58% for \$180,000,000 and annual interest payments of \$11,886,484.

The parties did not agree on cost of equity in the present Cause. We recognize the cost of equity, which is ultimately a measure of risk, cannot be precisely calculated and that it is normally offered based on a variety of factors. Given the size of WSCI and considering recent cases where the Commission has determined cost of equity using Capital Asset Pricing Model ("CAPM") and Discounted Cash Flow ("DCF") or has determined cost of equity for an affiliate of Petitioner, we agree with the parties that a complete cost of equity analysis is not warranted as substantial costs would have been incurred.

Petitioner proposed a cost of equity of 10.44% in its Case-in-Chief. Petitioner based its cost of equity on the average cost of equity determined by state public utility commissions for various affiliates. The OUCC based its recommendation, 9.25%, on its position taken in the most recent Indiana American rate case, Cause No. 44022, where CAPM and DCF analyses were used. In its analysis, the OUCC also factored in a 0.40% additive because Petitioner is a small utility. Petitioner proposed a cost of equity of 10.20% in its rebuttal testimony, which was the cost of equity the OUCC and Twin Lakes, an affiliate of Petitioner, agreed upon in Cause No. 43957. We reject Petitioner's position that the Commission should use the cost of equity from Cause No. 43957. The 10.20% was based on a settlement position between the OUCC and Twin Lakes and like all settlements cannot be the basis for future decisions. Moreover, 10.20% was not the cost of equity ultimately approved by the Commission. Finally, a complete cost of equity analysis using CAPM and DCF was not used by any party.

As neither party in this Cause submitted a cost of equity analysis, the Commission finds a reasonable starting point is the cost of equity determined in the Indiana American rate case, Cause No. 44022. In that case, a complete cost of equity analysis using CAPM and DCF was completed by four parties. The detailed analysis and the vetting of many positions yielded a 9.70% cost of equity that we found was appropriate. The Commission notes adjustments can be made for a variety of factors, including service quality issues, general economic and financial trends, and the size of the utility. There is no clear evidence in this case to demonstrate a need to make an adjustment for service quality issues. In Cause No. 44022, we indicated that while not an exact correlation, there is a positive relationship between cost of equity and interest rates. The OUCC presented evidence in this Cause showing the general trend of interest rates through May 2, 2012. For example, on May 2, 2012 30-Year Treasury Bonds were at 3.12% and published reports for yields on 30-Year Treasury Bonds show the rate remaining around 3.00% since May 2012.¹ Thus, we find no need to modify the cost of equity for changes in interest rates.

Based on the number of customers Petitioner serves, the Commission finds that a small company adjustment is warranted. The OUCC, recognizing Petitioner is smaller than Indiana American, proposed a small company adjustment of 0.40% similar to what it recommended in Cause No. 43128 for Twin Lakes. The OUCC also indicated that 0.40% might be overstated since Petitioner has a higher equity ratio than Twin Lakes, which would indicate a lower financial risk. We agree with the OUCC that a small company adjustment of 0.40% is too high in this case due to its relatively stronger financial position than Twin Lakes and its affiliation with a larger multi-national company. Therefore, the Commission finds the small company adjustment should be 0.30%. This adjustment, together with the cost of equity of 9.70%, yields a final cost of equity of 10.00%.

Combining the cost of equity, cost of long-term debt, and capital structure, the Commission finds that the cost of capital should be 8.31% based on the table below:

Description	Percent of Total	Cost Rate	Weighted Cost
Long-Term Debt	49.69%	6.60%	3.28%
Equity	50.31%	10.00%	5.03%
Total	100.00%		8.31%

¹ Yahoo Finance publishes yields on 30-Year Treasury bonds daily. See <http://finance.yahoo.com>

The authorized NOI is calculated by multiplying the rate base by the weighted cost of capital. Therefore, when the 8.31% rate of return is applied to the original cost rate base of \$485,830 for water and \$2,000,479 for wastewater, the result is a net operating income of \$40,375 and \$166,251 respectively.

C. Revenue Adjustments Under Present Rates. The OUCC accepted Petitioner's proposed billing determinant revenue adjustments and proposed customer growth adjustments to Petitioner's water and wastewater revenues, respectively. In rebuttal, Petitioner accepted these adjustments. WSCI and the OUCC agreed on the gross revenue conversion factor for both water and wastewater. The differences in the revenue requirements are driven by rate base, the cost of capital, rate case expense and PAA amortization. We find the proposed revenue adjustments to be reasonable and accordingly find Petitioner's *pro forma* revenue under present rates totals \$73,848 and \$124,680 for its water and wastewater utilities, respectively.

D. Operating Expense Adjustments. Both the OUCC and Petitioner proposed a number of adjustments to Petitioner's operating expenses. In rebuttal, Petitioner accepted many of the OUCC's proposed adjustments, including adjustments to purchased power, Utility Receipts Tax, periodic maintenance expense, depreciation, CIAC amortization, and income tax expense. The disputed adjustments are discussed below.

1. Salary and Wage Expense. In its Case-in-Chief, Petitioner proposed *pro forma* adjustments of \$655 and \$697 to its salary and wage expense for water and wastewater, respectively. The OUCC proposed to increase annual salaries and wage expense to include WSCI's share of internal labor costs included in rate case expense, resulting in additional operating expense adjustments of \$850 and \$903 for water and wastewater, respectively. We reject the OUCC's proposed changes to salaries and wage allocations between Petitioner and the Service Company in favor of simply limiting rate case expense to a reasonable amount. In order to comply with Ind. Code § 8-1-2-49 and provide the Commission with a better understanding of the relationship between Petitioner and the Service Company, Petitioner is directed to file its affiliated contracts with the Commission. Ind. Code § 8-1-2-49(g) sets out the following:

No management, construction, engineering or similar contract, hereafter made, with any affiliated interest, as hereinbefore defined, shall be effective unless it shall first have been filed with the commission. If it be found that any such contract is not in the public interest, the commission, after investigation and a hearing, is hereby authorized to disapprove such contract.

The Commission finds Petitioner's *pro forma* salary and wage expense should be \$13,276 and \$14,128 for its water and wastewater utilities, respectively. We further find that WSCI shall not implement its new rates until all affiliate agreements are filed with the Commission.

2. Rate Case Expense. In its Case-in-Chief, Petitioner estimated its total rate case expense, including both internal labor and outside legal expense, to be approximately \$201,508. Petitioner recommended that this amount be amortized over a three year period. The OUCC recommended the elimination of all internal labor costs included in rate case expense, a reduction in legal rate case expense from \$85,000 to \$45,000, and the elimination of \$4,500 of rate of return consultant fees. The OUCC further recommended the use of a five year amortization

period. In its rebuttal case, Petitioner reduced its proposed rate case expense to \$182,000, based on costs incurred to date along with an estimate of the remaining rate case expense. Petitioner also increased its proposed amortization period to four years. In the sections below, we discuss in more detail various components of Petitioner's proposed rate case expense.

Based on the evidence presented as discussed in further detail below, the level of rate case expense proposed by the Petitioner is neither prudent nor reasonable for the complexity of the issues presented in this Cause or for a utility with such a small customer base. WSCI serves 190 water customers and 190 wastewater customers; based on WSCI's proposed rate case expense, the average cost to each ratepayer would be approximately \$479 or \$958 for a ratepayer that receives both water and wastewater service. Not all expenditures are prudent and recoverable from ratepayers just because a utility claims to have incurred them. The utility has a responsibility to efficiently manage and control its costs. WSCI is strongly encouraged to investigate and explore possibilities for reducing its rate case expense in the future. For example, WSCI may be able to take advantage of the Commission's small utility filing procedure under Ind. Code § 8-1-2-61.5 and 170 IAC 14 for its next rate case. The table below shows Petitioner's proposed rate case expense and rate case expense approved by the Commission in recent cases involving utilities of similar size and complexity to that of WSCI.

Utility	Cause #	Rate Case Expense	Embedded Legal Fees	Number of Customers	Cost per Customer
Water Service Co. of Indiana	44104	\$ 182,000	32,000	380	\$ 478.95
Sani-Tech	43793-U	\$ 5,000	\$ -	113	\$ 44.25
Doe Creek Sewer	43530-U	\$ 16,404	\$ 1,404	382	\$ 42.94
Driftwood Utilites	43790-U	\$ 6,000	\$ -	1,451	\$ 4.14
Northern Richland Sewer	43791-U	\$ 15,000	\$ 5,000	239	\$ 62.76
Lakeland Lagoon	44115-U	\$ 2,400		120	\$ 20.00
Heir Industries	43949-U	\$ 13,588	5,000	99	\$ 137.25
Columbia City	44127-U	\$ 9,000		3,576	\$ 2.52
Prairie Utilities	44158	\$ 22,580	15,080	58	\$ 389.31

(a.) Internal Labor. Rate Case expense should represent a utility's incremental or additional costs incurred to execute its rate case. Rate case expense should not include costs that Petitioner will incur regardless of whether it is filing a rate case. Petitioner asserted this case will require 2,192 total hours by Petitioner's staff to complete. The Commission notes that a full-time employee that works 40 hours per week with two weeks of vacation works approximately 2,000 hours in a calendar year. The OUCC recommended \$0 in internal labor costs be included in Petitioner's rate case expense. In Late-Filed Exhibit No.1, Petitioner indicated that it had incurred approximately \$65,000 in internal labor rate case expense, but failed to provide supporting documentation justifying such a large amount of internal labor costs. Considering these

factors along with the small customer base of WSCI and expenses incurred by other similarly sized utilities, we find \$15,000 a prudent and reasonable amount for Petitioner's internal labor expenses devoted to rate case preparation.

(b.) **Legal Expenses.** Petitioner initially proposed to include \$85,000 of legal expenses in this Cause, but failed to offer support justifying such a large amount of legal expense. The OUCC recommended that amount be reduced to \$45,000. In Late-Filed Exhibit No.1, Petitioner indicated that it had incurred approximately \$32,000 in legal expense. Therefore, the Commission finds that for a utility of Petitioner's size, the complexity of this case, and consistent with prior Commission approved expense, Petitioner's legal expense shall be limited to \$32,000.

(c.) **Consultant Costs.** Petitioner proposed to include \$4,500 for a consultant in its estimate of rate case expense. This expense was for preparation of a rate of return study including a first draft of direct testimony. Petitioner indicated in its Case-in-Chief that, rather than incur the costs associated with hiring a return on equity expert, WSCI determined the best course of action was to use the average granted cost of equity from a list of seventeen companies. Accordingly, we find that it is inappropriate to include the cost of a consultant that was not retained, and the \$4,500 should be excluded from rate case expense.

(d.) **Other Associated Costs.** The Commission notes Petitioner's supporting documents filed with its Case-in-Chief warrant the award of other expenses that were not specifically addressed by the parties in testimony. Those expenses include: customer notice expense of \$681, mailing expense of \$923, and travel expense of \$1,768.

(e.) **Amortization Period.** Petitioner requested its total rate case expense be amortized over a three year period while the OUCC recommended a five year amortization period. Petitioner agreed to a four year amortization period in its rebuttal testimony. The Commission finds that a four year amortization period more closely reflects the anticipated life of the rates being set in this Cause and the appropriate period over which WSCI should be allowed to recover its rate case expense.

Based on the evidence presented and discussed herein, we find that Petitioner's rate case expense should be set at \$50,372 of which \$24,406 will be allocated to the water utility and \$25,966 will be allocated to the wastewater utility as illustrated by the table below.

Legal Fees	\$ 32,000
Rate Case Costs	15,000
Customer Notices	681
Overnight Mailings	923
Travel	1,768
Total Rate Case Expense	<u>\$ 50,372</u>
Amortized over 4 Years	<u>\$ 12,593</u>
Water 48.45%	<u>\$ 6,101</u>
Wastewater 51.55%	<u>\$ 6,492</u>

E. Net Operating Income at Present Rates. Based upon the evidence and the determinations made above, the Commission finds that Petitioner's *pro forma* revenue and expense amounts are shown as follows:

	<u>Water</u>	<u>Wastewater</u>
Operating Revenues		
Customer Revenues	\$ 72,629	\$ 121,969
Miscellaneous revenues	1,219	2,711
Total Operating Revenues	<u>73,848</u>	<u>124,680</u>
Operating Expenses		
Salaries & Wages	13,276	14,128
Capitalized Labor	(4,735)	(5,039)
Pensions & Other Benefits	2,806	2,987
Purchased Power	6,968	40,424
Maintenance	9,593	22,049
Chemicals	3,761	2,173
Transportation	1,088	1,157
Insurance Expense	1,439	1,532
Rate Case Expense	6,101	6,492
Other Miscellaneous	8,349	9,221
	<u>48,646</u>	<u>95,124</u>
Depreciaton Expense	12,638	62,415
Amortizaiton of CIAC	(32)	(48)
Taxes other than Income	5,511	6,493
Federal Income Taxes	(2,419)	(28,426)
State Income Taxes	(666)	(8,771)
Total Operating Expenses	<u>63,678</u>	<u>126,787</u>
Net Operating Income	<u>\$ 10,170</u>	<u>\$ (2,107)</u>

7. Authorized Rate Increase. Based upon the above findings, Petitioner's revenue requirement is calculated as follows:

Revenue Requirement

	<u>Water</u>	<u>Sewer</u>
Original Cost Rate Base	\$485,830	\$2,000,479
Times: Weighted Cost of Capital	8.31%	8.31%
Net Operating Income Required	40,375	166,251
Less: Adjusted Net Operating Income	10,170	(2,107)
Additional NOI Required	30,205	168,358
Gross Revenue Conversion Factor	1.591317013	1.59076123
Recommended Revenue Increase	\$48,066	\$267,819
Percent Increase	65.12%	214.81%

8. Rate Design.

A. Water Service. Petitioner proposed to eliminate its current declining block rate structure in favor of a rate design that includes a monthly fixed base facility charge plus a variable volumetric consumption charge. The rate design would establish the base facilities charge based on the size of the customer's meter. While the OUCC did not oppose this proposed change, it recommended that capitalized labor and miscellaneous income be allocated equally through the fixed base facility charge and volumetric charge. Petitioner accepted this recommendation on rebuttal. Accordingly, the Commission finds Petitioner's proposed water service rate design, as modified by the OUCC, is reasonable, appropriately allocates Petitioner's revenue requirements between fixed and variable charges and approved.

B. Wastewater Service. Petitioner's current rate structure is based on a volumetric charge with a minimum charge for each meter size, where residential and commercial customers pay the same volumetric charge and the Campground pays a rate per campsite. Petitioner proposed a new rate design that would include a monthly fixed base facility charge plus a variable volumetric consumption charge. The volumetric charge would vary for residential and commercial customers and would be a flat rate per thousand gallons consumed during the billing period. The Campground would continue to be billed based on the number of campsites. Similar to the water service rate design, the OUCC recommended that capitalized labor and miscellaneous income be allocated equally through the fixed base facility charge and volumetric charge. Petitioner accepted this recommendation on rebuttal.

Petitioner also noted that the Campground, which represents a significant portion of the sewer user base, was not properly billed and therefore did not pay all of its sewer charges in periods prior to the test year. Petitioner explained that this under collection resulted in part because the Campground was supposed to be billed for seven months of service each year pursuant to an agreement approved in the utility's last sewer rate case, Cause No. 41486. WSCI proposed moving the Campground to monthly billing in order to avoid this issue in the future. The total annual amount billed to the Campground would remain the same. Petitioner indicated this rate design would address the fixed costs related to the Campground regardless of when the Campground is operational. While we understand that Petitioner wants to avoid future billing errors that would result in the under collection of charges from the Campground, we also recognize the flow from the Campground during the winter months is minimal and the Campground has limited income during

this period. Therefore, we decline to approve Petitioner's request to move the Campground to a monthly billing cycle.

Finally, WSCI has proposed a differential on the wastewater rates between residential and general service customers of 25 percent to recognize the differences placed on the wastewater system by these different customers. In discussing the proposed volumetric charge, Petitioner indicated residential sewer customers would be charged \$13.86 per 1,000 gallons of water consumed where general service sewer customers would be charged \$21.11 per 1,000 gallons of water consumed. Petitioner indicated general service customers return a more significant portion of their water use to the wastewater system and that it is well recognized that residential customers use some water that is not returned to the wastewater collection system, citing activities such as lawn irrigation, car washing, and other normal uses. Mr. Neyzelman explained that the proposed 25 percent differential is one that has been used in other states and considered a normal regulatory practice. The Commission finds that Petitioner failed to provide any evidence, besides Mr. Neyzelman's limited testimony, that would support the higher usage rate for general service customers. Accordingly, Petitioner's proposal to charge general service customers a use differential of 25 percent more for their volumetric charge is denied.

Based on the evidence, the Commission approves, as modified herein, Petitioner's proposed wastewater service rate design, which includes a monthly fixed base facility charge plus a variable volumetric consumption charge.

9. Non-Recurring Fees and Charges. Petitioner proposed new non-recurring charges for the water system: NSF Charge, New Customer Charge, Meter Testing Fee, Late Payment Charge and After-Hours Call Out Charge. Petitioner also proposed new non-recurring charges for the wastewater system: NSF Charge, New Customer Charge, Reconnection Charge and Late Payment Charge. In addition, Petitioner proposed changes to its current Reconnection Charge for water service and Connection Charge for both water and wastewater services. The OUCC agreed with Petitioner's proposed NSF charge, New Customer Charge, Meter Testing Fee and Late Payment Charge, but opposed Petitioner's After-Hours Call Out Charge. Petitioner withdrew its request for approval of its proposed After-Hours Call Out Charge in its rebuttal testimony. Based on the evidence presented, we find the NSF charge, New Customer Charge and Late Payment Charge to be reasonable and are approved. The Commission further finds that Petitioner's request to charge a fee for meter testing is reasonable and should be approved, but directs Petitioner to submit language in its tariff that reflects the frequency of testing as outlined in 170 IAC 6-1-11.

With regards to connection fees, Petitioner proposed in its Case-in-Chief to increase its wastewater connection charge from \$400 to \$2,000. It also proposed water connection charges ranging from \$1,800 to \$2,500 or actual cost of the meter and its installation, whichever is greater. Petitioner's current water connection charge ranges from \$150 for 5/8-inch and 3/4-inch water meters to \$300 for 2-inch and above water meters. The OUCC opposed WSCI's proposed connection charges as excessive and unsupported by evidence. The OUCC recommended that Petitioner require customers hire a licensed and bonded contractor to install the tap and water or sewer line at the customer's expense. The Petitioner agreed to the OUCC's recommendation, adding a \$50 inspection fee. The Commission finds Petitioner's evidence demonstrates that its existing fees are not adequate to recover costs associated with making a connection to the respective systems. Therefore, we accept Petitioner's proposal, that in lieu of a defined charge, customers will be responsible to hire a licensed and bonded contractor to install the tap and water or wastewater

line at the customer's expense and to allow the Petitioner to charge the customer a \$50 inspection fee to recover the costs associated with WSCI's inspection of the connection.

Concerning reconnection fees, Petitioner proposed to increase its current charge for reconnection of water services following disconnection for failure to pay a bill from \$10 to \$37.50 and proposed to expand the coverage of this charge to include seasonal customers in order to cover actual costs being incurred. The OUCC indicated the proposed water reconnection charge is reasonable, but that it had concerns with Petitioner's proposed changes in the description of its reconnection charge and that the expanded use was unsupported by evidence, particularly the language regarding rates to be charged seasonal customers. The OUCC offered revised language concerning seasonal customers. Petitioner opposed the OUCC's revision indicating that WSCI's language would be consistent with Twin Lakes' approved water tariff language.

Petitioner does not currently charge a fee for reconnection of wastewater services following disconnection for failure to pay a bill. WSCI proposed to institute an actual cost for wastewater service reconnection, the estimated cost of which will be furnished to the customer with the cut-off notice. The OUCC recommended rejection of Petitioner's proposed wastewater reconnection charge indicating that Petitioner has not established the need for a wastewater reconnect charge or established why its water disconnection charge is not adequate to deal with late or non-paying customers. The OUCC noted that, with the exception of the Campground, all of Petitioner's wastewater customers are also water customers. Consequently, Petitioner can disconnect water service which will serve the same purpose as disconnecting wastewater service and there is no need to establish a wastewater reconnection charge or to disconnect wastewater service.

The Commission finds the amount of Petitioner's proposed increase in reconnection fees for water services is reasonable, supported by the evidence and should be approved. However, we find the Petitioner has failed to provide sufficient support for inclusion of its language regarding seasonal customers. We further find that the OUCC's proposed language concerning seasonal customers is reasonable and should be adopted. Regarding the wastewater reconnection fee, the Commission finds that for Petitioner's customers that receive both water and wastewater services, the need for reconnection charges is unsupported by the evidence and unnecessary because disconnecting water service will have the same effect as disconnecting wastewater service. However, we recognize the need for reconnection charges for Petitioner's customers that receive only wastewater service. Accordingly, Petitioner's proposed reconnection charges for wastewater service are approved with the modification that they shall apply only to customers not receiving water service.

IT IS, THEREFORE, ORDERED BY THE INDIANA UTILITY REGULATORY COMMISSION that:

1. Consistent with the above findings, Water Service Company of Indiana is hereby authorized to increase its rates and charges for water and wastewater utility service by 65.12% and 214.81% in order to produce total annual operating revenues of \$121,914 and \$392,499 respectively.
2. Water Service Company of Indiana's proposed water service and wastewater service rate designs, as modified by the above findings, are hereby approved.

3. Water Service Company of Indiana's non-recurring fees and charges as modified by Finding Paragraph 9, are approved.

4. Water Service Company of Indiana shall file with the Commission's Water/Sewer Division, within thirty (30) days of this Order and prior to placing into effect any rate increase, copies of any affiliated contracts as required by Ind. Code § 8-1-2-49.

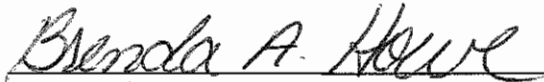
5. Prior to placing into effect the rates and charges approved herein, Water Service Company of Indiana shall file a schedule of rates and charges for the purpose of accomplishing the findings set forth above, with the Water/Sewer Division of the Commission. Water Service Company of Indiana shall also file revenue reconciliation schedules showing that forecast operating revenues equal those prescribed herein for each utility utilizing the rate design granted in this Order. Such rates and charges for water and wastewater service will become effective upon approval thereof by the Water/Wastewater Division of the Commission and shall supersede all prior rates and charges.

6. This Order shall be effective on and after the date of its approval.

ATTERHOLT, BENNETT, MAYS AND ZIEGNER CONCUR; LANDIS DISSENTS WITH SEPARATE OPINION:

APPROVED: MAR 27 2013

I hereby certify that the above is a true
and correct copy of the Order as approved.



Brenda A. Howe
Secretary to the Commission

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

**PETITION OF WATER SERVICE)
COMPANY OF INDIANA FOR)
AUTHORITY TO INCREASE ITS WATER) CAUSE NO. 44104
AND SEWER RATES AND CHARGES)
AND FOR APPROVAL OF A NEW) APPROVED:
SCHEDULE OF RATES AND CHARGES)
APPLICABLE THERETO)**

**DISSENTING OPINION OF
COMMISSIONER LARRY S. LANDIS**

One of the most challenging aspects in the preparation of this dissenting opinion is to know where to start in terms of identifying and outlining the egregious dysfunctionality reflected by the Petitioner in its pre-filed testimony and what appears to be an almost out right evasion of key questions raised in the course of the preceding.

Perhaps the best way in which to start is to suggest that as executed by Petitioner, their business model which posits no full-time staff present “on the ground,” coupled with an apparent disconnect from reality on the part of corporate management, has resulted in an almost total lack of meaningful communication between corporate executives and virtually any of Petitioner’s stakeholders, including the IURC; the OUCC; any state, county, or local officials; or any customers. This total lack of communication appears to extend from the time Utilities Inc. acquired the water and sewer properties early in the last decade.

There was a conference call in August of 2010 between representatives of utilities Inc. and several staff members of the Water/Sewer Division of the IURC, the majority of which was devoted to the Twin Lakes property. A year later, a manager from Water Service Company of Indiana (WSCI) called the director of the Water/Sewer Division to inform him that WSCI would be filing a rate case. The formal petition was filed on October 28, 2011. Staff has not been able to confirm any meeting with the OUCC other than contact directly related to the preparation of testimony on the part of OUCC. WSCI’s initial notice to customers did not properly reflect the rate increase in its initial filing and it wasn’t properly noticed until three months after the Case-in-Chief was filed. No mention was made of the exact percentage increase WSCI was seeking.

It appears that many of the decisions made in the ensuing years following acquisition of the property by Utilities Inc. were made in a total vacuum. Recommendations made by retained consultants with regard to appropriate steps which might need to be taken to upgrade the property and make it viable over the intermediate term were disregarded. The total evasion of any meaningful response to bench questions regarding why the company ignored recommendations of one consultant only to resort to a solution recommended by a second

consultant at five times the cost of the original recommendation, and then to fail to manage the project to the initial project budget is inexcusable.

Given the outrageous representation of the Petitioner with regard to the time purportedly invested and the costs allegedly involved in preparation for this rate case, all made without a semblance of meaningful support or justification, it is inconceivable that Petitioner's witnesses were so ill prepared and unresponsive to questions from the OUCC and from the bench. It is difficult to avoid the conclusion that Petitioner consciously avoided providing any witnesses that could shed light on certain of the decisions which could have such a crushing impact on ratepayers.

Mr. Neyzelman and Mr. Haas, in particular, goes on at great length with regard to certain aspects of the company's testimony, particularly when it supports the intent and/or convenience of Petitioner, but are almost totally uninformed on the stand when questioned about the decision process that led to the decision to totally rebuild the treatment facilities at a cost of \$1.5 million and then to incur additional expenses with a redesign that ran the cost up to over \$2 million. Paraphrasing, Mr. Haas makes it clear that he wasn't there when the decisions were made and construction took place in the 2007–2008 timeframe, and even the Late-Filed Exhibit is filled with ambiguities regarding the decision process, fails to identify the Respondent, and makes no attempt to describe by whom the decisions were made or, in any detail, on what basis. As this Order notes (at page 20), "...Making the decision to install him mechanically aerated concrete package plant that differed significantly from the design assumed for purposes of the 2006 [second] Engineering Report and at [significantly] increased costs, WSCI ultimately chose to pursue an option that was not recommended in either report [emphasis added]." Any attempt or representation by Petitioner which asserts that WSCI's decision is supported by either of the engineering reports is at the very least a stretch of even the sketchy response of Petitioner.

The record and this Order are replete with instances in which Petitioner failed to make its case, provided insufficient supporting evidence to sustain certain representations, and – in some instances – was simply flat-out nonresponsive.

Moreover, WSCI's perspective in certain matters is stunningly self-focused and with near-total disregard for the realities of certain "remedies" sought. For example, Mr. Neyzelman proposes that Petitioner be allowed to move billing to the Campground from seven months, the period of time in which the Campground is open, to 12 months in part because WSCI lacks current flow information from the Campground. In other words, it would be more convenient for WSCI to bill on a monthly basis, as opposed to during the seven months in which the Campground is active. This totally disregards any consideration of cash flow concerns on the part of Campground management. It doesn't take a rocket scientist to determine that when the Campground is closed, little revenue will be coming in, making cash flow management a major challenge for the Campground operator. I applaud my colleagues in this Order for standing fast and refusing to accommodate Petitioner's self-serving request motivated by its apparent utilities deficiencies in favor of a more customer-focused approach.

Petitioner's representations with regard to the cost incurred in the preparation of this Rate Case could take up an entire dissent in and of themselves. At the outset, it is outrageous that

apparently there was no one in charge of the case who was either capable or willing to manage the process as the stewards of the franchise granted by this Commission should be expected to do. In addition to the table (set forth on page 25 of this Order), the great expense per customer calculated by IURC staff results in a claimed great expense per customer of \$478.95, which tellingly is about 20 times the rate expense per customer associated with Cause 43957, the latest rate case of parent company Utilities Inc.'s Indiana affiliate, Twin Lakes, calculated at \$23.77. As this Order notes (at page 9) in quoting witness Ms. Stull of the OUCC, "...\$14, or approximately 20% of each resident's monthly bill, represents recovery of Petitioner's estimated Rate Case expense." This over the top, apparently totally unmanaged cost can only be said to be reflective of ignorance, arrogance or inept management.

In addition to other extreme outlying and/or poorly-or un-justified representations of Rate Case expenses, I note that Petitioner initially proposed to include \$85,000 of legal expenses in this Cause, but when pressed by the bench, in Late-Filed Exhibit #1, Petitioner acknowledged that in reality it had incurred approximately \$32,000 in legal expenses, or slightly above the one third that it initially proposed.

In closing, I return to the apparent total disconnect between the Petitioner and its stakeholders. Mr. Fish of the OUCC indicates (at page 11 of this Order) that 141 homes of the "...approximately 194 customers..." reside in mobile homes (manufactured housing) which is typically occupied by individuals of relatively modest means and/or fixed incomes. It should be apparent to the most casual observer that that Mr. Fish of the OUCC refers to customer comments received in this proceeding and to the fact that the dramatic "... water and sewer rate increase may have a devastating impact on many customers, with the Campground being particularly impacted by the increase. (this Order at p. I3)" While the record does not contain detailed information regarding the impact of the recent recession and slow-growth recovery, it is likely that the Campground would have already felt a disproportionate impact on revenues as middle-income and modest-income families sought to cut back on discretionary spending such as leisure activities and family vacations. Mr. Fish goes on to suggest that Petitioner could be placing itself in a position to lose the Campground as a customer, presumably either because the Campground might fail due to the added burden of significantly increased utility fees, or because the Campground might seek an alternative solution to its sewage disposal issue. Indeed, with the Campground constituting approximately 25 percent of the total revenues of the wastewater utility, if the utility were to lose that revenue it might as well launch the utility into a downward fiscal death spiral, quite possibly dragging the community's entire microeconomy down with it.

The OUCC proposed that action be taken to minimize the rate shock implications of the proposed increase, perhaps by phasing in the increase over a multi-year period. In response, Mister Neyzelman indicated that "...while he was sympathetic to the OUCC's desire to mitigate the impact of the proposed rate increase he did not agree with the OUCC's recommendation to phase in wastewater rates over a three-year period, explaining that with the adjustments accepted on rebuttal, the rates can and should be implemented in a single phase (this Order at page 17; emphasis added)."

Which leaves me to wonder why, if there was such urgency to the increase, there was at least a three-year lag between completion of the wastewater treatment plant and Petitioner's filing of

this case. Operating on essentially the same revenue structure and with virtually the same cost structure as reflected in the test year, why was there no urgency expressed during that three-year period, followed by great urgency in the summer of 2011? What other information does the commission not know that might be relevant to a decision in this context?

I fully appreciate the role of the Commission and its need to balance the interests of ratepayers and utilities in proceedings before it. I fully affirm the struggles my colleagues and staff have experienced in wrestling with this case. And I greatly respect my colleagues in their desire to find an acceptable and unanimous solution which minimizes the pain on the parties. Petitioner has done little to bolster its case, strengthen its credibility, or demonstrate that it honors in any respect what ought to be a covenant between a utility and its customers. While I fully appreciate the efforts of staff and my colleagues to hold Petitioner to a standard which it apparently does not share, and to expect Petitioner to make its case as well as its revenue target, I cannot in good conscience support a decision which does not make further allowances for the impact on the ratepayers which Petitioner has chosen to ignore and indeed, on the micro-economy of the entire community.

I respectfully dissent from the majority opinion in this cause.