ORIGINAL

Commissioner	Yes	No	Not Participating
Huston			√
Bennett	√		
Freeman	√		
Veleta	√		
Ziegner	√		

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF INDIANA-AMERICAN WATER COMPANY, INC. FOR (1) AUTHORITY TO INCREASE ITS RATES AND CHARGES FOR WATER AND WASTEWATER UTILITY SERVICE THROUGH A THREE-STEP RATE IMPLEMENTATION, (2) APPROVAL OF NEW SCHEDULES OF RATES AND CHARGES APPLICABLE TO WATER AND WASTEWATER UTILITY SERVICE, INCLUDING A NEW UNIVERSAL AFFORDABILITY RATE, (3) APPROVAL OF REVISED DEPRECIATION RATES APPLICABLE TO WATER AND WASTEWATER PLANT IN SERVICE, (4) APPROVAL OF NECESSARY AND APPROPRIATE ACCOUNTING RELIEF, (5) APPROVAL OF THE EXTENSION OF SERVICE TO AN INFRASTRUCTURE DEVELOPMENT ZONE IN MONTGOMERY COUNTY, INDIANA AND AUTHORITY TO IMPLEMENT A SURCHARGE UNDER IND. CODE § 8-1-2-46.2, AND (6) APPROVAL OF PETITIONER'S PLANS TO DEVELOP FUTURE WATER SOURCES OF SUPPLY UNDER IND. CODE § 8-1-2-23.5.

CAUSE NO. 45870

APPROVED: FEB 14 2024

ORDER OF THE COMMISSION

Presiding Officers:
James F. Huston, Chairman
Sarah E. Freeman, Commissioner
Loraine L. Seyfried, Chief Administrative Law Judge

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On March 31, 2023, Indiana-American Water Company, Inc. ("Petitioner," "Indiana American," or "INAWC") filed its Petition for General Rate Increase and Associated Relief under Ind. Code § 8-1-2-42.7, Surcharge Under Ind. Code § 8-1-2-46.2, and Approval of Plans to Develop Future Water Sources under Ind. Code § 8-1-2-23.5 and Notice of Provision of Information in Accordance with the Minimum Standard Filing Requirements with the Indiana Utility Regulatory Commission ("Commission"), seeking: (i) authority to increase its rates and charges for water and wastewater through a three-step rate implementation, (ii) approval of new schedules of rates and charges, (iii) approval of revised depreciation rates applicable to its water and wastewater plant in service, (iv) approval of the regulatory accounting treatment, (v) approval of Petitioner's extension of service to a Montgomery County Infrastructure Development Zone and authority to implement a surcharge under Ind. Code § 8-1-2-46.2, and (vi) approval of Petitioner's plans to develop future sources of water supply. That same day Indiana American also filed testimony and exhibits from the following witnesses[1]:

- Matthew Prine, President of Indiana American
- Gregory D. Shimansky, Director, Rates & Regulatory for American Water Works Service Company, Inc. ("Service Company")
- Matthew H. Hobbs, Director of Engineering at Indiana American
- Kari C. Britto, Vice President, Operations at Indiana American
- Charles B. Rea, Senior Director, Regulatory Pricing and Affordability for the Service Company
- Nicholas Furia, Assistant Treasurer for the Service Company
- Ann E. Bulkley, Principal at The Brattle Group
- Jennifer M.B. Grisham, Senior Manager of Regulatory Services for the Service Company
- Manuel Cifuentes, Jr., Senior Principal Regulatory Analyst for the Service Company
- Thomas G. O'Drain, Director of National Categories and Corporate Procurement for the Service Company
- Patrick Baryenbruch, President, Baryenbruch & Company LLC
- Larry E. Kennedy, Senior Vice President, Concentric Energy Advisors, Inc.

Petitions to Intervene were filed on April 5, 2023, by Citizens Action Coalition of Indiana, Inc. ("CAC"); on April 11, 2023, by the City of Crown Point ("Crown Point"); on April 17, 2023, by the Town of Schererville ("Schererville") and Sullivan-Vigo Rural Water Corporation ("Sullivan-Vigo"); on April 26, 2023 by a group of industrial customers of Indiana American[2] ("Industrial Group"); on May 4, 2023, by the Town of Whiteland ("Whiteland"); on May 19, 2023, by Borden Tri-County Regional Water District, Jackson County Water Utility, Inc., and the Town

[1] On April 28, 2023, Indiana American filed corrections to witnesses Shimansky and Rea testimony. On June 6, 2023, Indiana American filed its second submission of corrections to witnesses Shimansky, Britto, Bulkley, and Cifuentes and updates to certain of its financial exhibits. On August 29, 2023, Indiana American filed its third submission of corrections to witness Shimansky's direct testimony. All corrections were included in the evidence submitted at the hearing.

[2] The ad hoc group at time of intervention included, Cleveland Cliffs Steel LLC, Linda, General Motors, Haynes International, Inc., and United States Steel Corporation.

of Greenville, Indiana; and on July 13, 2023, by Hamilton County Regional Utility District ("District"), (collectively, the "Intervenors"). The Commission issued Docket Entries in which each of said petitions to intervene were granted; thus, all of the entities requesting intervention were made parties to this Cause. The Indiana Office of Utility Consumer Counselor ("OUCC") also participated.

A Stipulation as to Procedural Matters setting forth certain procedural matters that had been agreed upon with the OUCC, and Intervenors CAC, Crown Point, Schererville, Sullivan Vigo, and the Industrial Group was filed on April 21, 2023. By Docket Entry issued May 3, 2023, the Presiding Officers established certain procedural requirements, scheduling, and other matters. By Docket Entry dated June 23, 2023, the Presiding Officers modified the date by which the OUCC and all Intervenors were to file their respective cases.

Pursuant to Ind. Code § 8-1-2-61(b), a public field hearing was conducted on June 29, 2023, in Fishers, Indiana, which is the largest municipality in Petitioner's service area. Pursuant to the Commission's June 19, 2023 Docket Entry granting the OUCC's request for a second field hearing, a second field hearing was conducted on July 6, 2023, in the City of Gary. During the public field hearings, members of the public provided oral and/or written testimony in this Cause.

On July 21, 2023, the OUCC and Intervenors filed their respective cases-in-chief. The OUCC's case-in-chief included testimony and attachments from the following witnesses[3]:

- Scott Bell, Director of the Water/Wastewater Division
- Carla Sullivan, Utility Analyst in the Water/Wastewater Division
- Margaret Stull, Chief Technical Advisor in the Water/Wastewater Division
- Thomas Malan, Utility Analyst in the Water/Wastewater Division
- Jason Compton, Utility Analyst in the Water/Wastewater Division
- Shawn Dellinger, Senior Utility Analyst in the Water/Wastewater Division
- David Garrett, Resolve Utility Consulting, PLLC
- Jerome Mierzwa, Principal and Vice President, Exeter Associates, Inc.
- James Parks, Senior Utility Analyst in the Water/Wastewater Division
- Carl Seals, Assistant Director of the Water/Wastewater Division
- Kristen Willoughby, Utility Analyst in the Water/Wastewater Division

The OUCC also filed the written consumer comments pertaining to this docket and the relief requested as Public's Exhibit 12.

A group of sale-for-resale ("SFR") customers ("Wholesale Customers") filed the testimony of Eric Callocchia, Partner of NewGen Strategies & Solutions, LLC's Environmental Practice.[4]

[3] On August 2, 2023, the OUCC filed corrections to the testimony of Scott A. Bell, Carla F. Sullivan, and Thomas W. Malan and redlined schedules. On August 30, 2023, the OUCC filed additional corrections to Ms. Sullivan's testimony. All corrections were included in the evidence submitted at the hearing.

[4] The Wholesale Customers include the Towns of Schererville, Greenville, and Whiteland, the City of Crown Point, Borden Tri-County Regional Water District, Jackson County Water Utility, Inc., Hamilton County Regional Utility District, and the Sullivan-Vigo Water Corporation.

The District filed the testimony and attachments of Martin A. Wessler, CEO of Wessler Engineering.

The Industrial Group's case-in-chief included testimony and attachments from the following witnesses[5]:

- Michael Gorman, Managing Principal, Brubaker & Associates, Inc.
- Jessica York, Consultant, Public Utility Regulation, Brubaker & Associates, Inc.

Crown Point filed testimony from Gregory Guerrettaz, President, Financial Solutions Group, Inc.

Whiteland filed testimony and attachments of Carmen Young, Director of Administration for Whiteland.

CAC filed testimony and attachments from Benjamin Inskeep, CAC's Program Director.

On August 8, 2023, Indiana American filed rebuttal testimony, exhibits, and workpapers for witnesses Shimansky, Hobbs, Britto, Rea, Bulkley, Grisham, Cifuentes, and Kennedy.[6] Indiana American also filed rebuttal testimony for Melissa Ciullo, Vice President of Tax, and Michael Farrell, Senior Director with Willis Towers Watson. On the same day, the OUCC filed cross-answering testimony and exhibits of witnesses Stull and Mierzwa; the Industrial Group filed cross-answering testimony and exhibits of witness York; the Wholesale Customers filed the cross-answering testimony and exhibits of witness Callocchia; the District filed the cross-answering testimony of Wessler; and CAC filed cross-answering testimony of Benjamin Inskeep.

The Presiding Officers caused to be issued Docket Entries requesting additional information from Indiana American on June 12, 2023, August 4, 2023, August 17, 2023, August 25, 2023, August 30, 2023, and August 31, 2023, to which Indiana American filed its responses on June 13, 2023 (Pet. Ex. 25), August 8, 2023 (Pet. Ex. 26), August 21, 2023 (Pet. Ex. 27), August 30, 2023 (Pet. Ex. 28), August 31, 2023 (Pet. Ex. 29), and September 1, 2023 (Pet. Ex. 30).

The Commission held an evidentiary hearing in this Cause starting on August 31, 2023, at 9:30 a.m. and continuing on September 5, 2023, in Room 222 of the PNC Center, 101 West Washington Street, Indianapolis, Indiana. Indiana American, the OUCC, and Intervenors were present and participated through counsel. The testimony and exhibits of the parties were admitted into the record without objection.

Having considered the evidence presented and based on the applicable law, the Commission now finds:

1. **Notice and Jurisdiction.** Notice of the petition filed in this Cause was given and

[5] The Industrial Group filed corrections to its witnesses' testimony on July 24, 2023.

[6] On August 31, 2023, Petitioner filed a corrected Attachment CBR-7R to Mr. Rea's rebuttal testimony.

published by Petitioner as required by law, and Petitioner provided notice to its customers summarizing the nature and extent of the proposed changes in its rates and charges for water service. Pet. Ex. 1, Attachments MP-1 and MP-2.

Due, legal, and timely notices of the public hearings in this Cause were given and published as required by law. Petitioner is a "public utility" within the meaning of that term in Ind. Code § 8-1-2-1(a)(2) and is subject to the jurisdiction of the Commission in the manner and to the extent provided by the laws of the State of Indiana. Under Ind. Code §§ 8-1-2-42 and 42.7, the Commission has jurisdiction over Petitioner's rates and charges. The Commission also has jurisdiction over Petitioner's extensions of water and wastewater service to rural areas under Ind. Code § 8-1-2-46.2 and the development of future water sources under Ind. Code § 8-1-2-23.5. Accordingly, the Commission has jurisdiction over Petitioner and the subject matter of this proceeding.

2. Petitioner's Organization and Business. Indiana American is a public utility with its principal place of business located at 153 North Emerson Ave., Greenwood, Indiana. Indiana American provides water utility service to approximately 328,000 customers located in and around numerous communities throughout the State of Indiana. Indiana American also provides sewer utility service to approximately 2,400 customers located in Clark, Delaware, Hamilton, Wabash, and Vigo Counties.

Indiana American renders such water and wastewater utility service by means of utility plant, property, equipment, and related facilities owned, leased, operated, managed, and controlled by it which are used and useful for the convenience of the public in the production, treatment, transmission, distribution, and sale of water for residential, commercial, industrial, public authority, and sale for resale purposes, for the provision of public and private fire service, and for the provision of wastewater service.

3. Existing Rates. Petitioner's existing basic rates and charges for water and wastewater utility service were established pursuant to the Commission's Order in *Indiana-American Water Co.*, Cause No. 45142 (IURC June 26, 2019) (the "2019 Rate Order") and adjusted downward through a Settlement in Cause No. 45032 S4 (Petitioner's subdocket for addressing certain impacts of the Tax Cuts and Jobs Act of 2017) and also to reflect the removal of Utility Receipts Tax ("URT"). Since the 2019 Rate Order, Petitioner has also implemented a Distribution System Improvement Charge ("DSIC") pursuant to the Commission's Orders in Cause Nos. 42351 DSIC 12, issued March 17, 2021, 42351 DSIC 13, issued March 21, 2022, and 42351 DSIC 14, issued March 22, 2023. A Service Enhancement Improvement ("SEI") charge was authorized by the Commission's Orders in Cause Nos. 45609 SEI 1, issued February 22, 2023, and 45609 SEI S1, issued March 8, 2023.

4. Test Year. As authorized by Ind. Code § 8-1-2-42.7(d)(1), Petitioner proposed a forward-looking test period using projected data. As provided in the Commission's May 3, 2023 Docket Entry, the test year to be used for determining Petitioner's projected operating revenues, expenses and operating income shall be the 12-month period ending April 30, 2025. The historical base period is the 12-month period ending September 30, 2022.

5. **Indiana American's Requested Relief.** In its Petition, Indiana American sought Commission approval of an overall increase in rates and charges for water and wastewater service that would produce additional revenues in three steps of approximately $86.7 million, which would reflect an overall revenue increase of 31.1%. This overall revenue increase comprises a Step 1 increase of 15.49%, a Step 2 increase of 5.63% from Step 1, and a Step 3 increase of 7.45% from Step 2. As a rate mitigation effort, Petitioner requested to recover 65% of its total wastewater revenue requirement ($4,658,471 at Step 3) through wastewater rates. After reallocating $1,630,465 of the wastewater revenue requirement to water, the projected wastewater revenue requirement is $3,028,006.[7] Increases to industrial and SFR classes were to be capped at 1.5 times the overall water revenue increase. No increase to public and private fire service was requested. The remainder of the increase was to be allocated to residential and commercial classes in proportion to present rate revenues. Rates for Areas 1, 2, and 3 will be fully consolidated, phased in over the three steps.

As detailed in Indiana American's case-in-chief, Petitioner also requested Commission approval of a new schedule of rates and charges applicable to water and wastewater utility service, as well as approval of a new Universal Affordability Tariff for water service. Indiana American also requested approval of revised depreciation rates applicable to its water and wastewater plant in service, approval of regulatory accounting treatment, approval of Petitioner's extension of service to an Infrastructure Development Zone in Montgomery County and authority to implement a surcharge under Ind. Code § 8-1-2-46.2, and approval of Petitioner's plans to develop future sources of water supply.

6. **Overview of the Evidence.**

A. **INAWC Case-in-Chief.** Mr. Prine addressed Indiana American's provision of water and wastewater services in Indiana. He discussed the major drivers of Petitioner's request for rate relief in this proceeding, primarily the significant capital investments and other expenditures that Petitioner has made and plans to make through April 2025. He explained how Petitioner's ratemaking proposals are intended to support the more efficient use of water, investment in Indiana American's system, and the long-term interests of customers. Finally, he discussed Petitioner's corporate citizenship and community outreach efforts.

Mr. Shimansky testified on the test period used in this case and Petitioner's overall revenue requirement, rate base, depreciation, amortization, pension costs, and other post-employment benefit ("OPEB") costs, including Petitioner's request for regulatory accounting treatment of pension/OPEB costs, production costs, and certain costs associated with the proposed new

[7] On June 6, 2023, Petitioner filed a Second Submission of Corrections to Direct Testimony and Exhibits updating several financial exhibits reflecting an overall revenue increase of 31.77% or approximately $88.6 million. Petitioner explained that a re-run of its model would be done at rebuttal but offered to provide an updated CD of the model upon request of the Commission. At the Commission's request, Petitioner filed its updated full financial model on June 13, 2023. Subsequent to this filing, Petitioner indicated in an August 31, 2023 Docket Entry response that it did not increase its rate request when it filed its June 6, 2023 update. However, Petitioner compared its rebuttal position to the full financial model filed on June 13, 2023, noting that although it was accepting certain positions of other parties, the changes did not fully offset the net increase in revenue requirement filed on June 13, 2023. Pet.'s Ex. 29. Therefore, the Commission's determination of the issues identified in this Order uses the full financial model filed on June 13, 2023.

Universal Affordability Tariff. He also presented Petitioner's proposals related to: (1) an over-collection associated with the repeal of the URT, and (2) a surcharge related to an Infrastructure Development Zone established in Montgomery County.

Mr. Hobbs testified on the used and useful nature of the utility plant in service ("UPIS"), explained Petitioner's overall approach to capital management, and described the significant capital investments Petitioner has made and plans to make. He also described Petitioner's plans for future source of supply investments.

Ms. Britto described Petitioner's water and wastewater operations, commitment to water quality and safety, ongoing efforts to improve water and wastewater efficiency, and employee staffing levels and compensation.

Mr. Rea sponsored Petitioner's cost of service analysis and rate design proposals, affordability analyses, and revenue projections including adjustments to Indiana American's historical billing determinants.

Mr. Furia testified on the projected capital structure to be used for computing the weighted average cost of capital ("WACC") for Indiana American. The WACC is used as the authorized overall rate of return on rate base in this Cause.

Ms. Bulkley testified on the reasonableness of Petitioner's requested cost of common equity, capital structure, and requested authorized net operating income as compared to a fair return on the fair value of Petitioner's assets.

Ms. Grisham discussed and supported the level of operations and maintenance ("O&M") expense as it relates to: (1) labor and labor-related costs, (2) pension/benefits, (3) support services, (4) contract services, and (5) taxes other than income, with the exception of property taxes which was covered by Mr. Cifuentes.

Mr. Cifuentes discussed and provided support for the level of O&M expense as it relates to: (1) production costs, (2) other operating expenses not covered by Ms. Grisham, and (3) property taxes.

Mr. O'Drain testified in support of current and projected chemical pricing.

Mr. Baryenbruch offered support for the necessity and reasonable cost of services provided by the Service Company as shown by Petitioner's Service Company Market Cost Comparison.

Mr. Kennedy testified on the comprehensive depreciation study for water and wastewater plant in service.

Petitioner also provided its Financial Exhibit in support of its requested relief in this proceeding in Excel and PDF formats.

B. <u>OUCC and Intervenors' Cases-in-Chief</u>. The OUCC and Intervenors proposed a number of adjustments to Petitioner's proposed revenue requirements and took issue with numerous other components of Indiana American's case-in-chief and proposed rate increase.

For instance, the OUCC proposed a return on equity ("ROE") of 9.0% versus Petitioner's proposed ROE of 10.6% and recommended certain operating revenue and expense adjustments. The OUCC recommended seven changes to Indiana American's proposed water operations rate base, including changes to UPIS, cost of removal, retirements, and accumulated depreciation, all summarized in Table 7 of OUCC Exhibit 3. Specifically, the OUCC recommended adjustments related to the following: (1) Sheridan – Land for future wellfield, (2) Sheridan Water Treatment Plant, (3) & (4) Sheridan Main Extensions, (5) Winchester Water Treatment Plant, (6) Lake Station Wells and Treatment Plant, and (7) BT SOP 98-01 Costs. OUCC witness Parks recommended denial of Petitioner's two major projects, as well as disallowance of the $9.3 million transmission main Indiana American proposed from its Sheridan treatment plant to serve the District. Further, OUCC witness Seals discussed Indiana American's levels of non-revenue water and made recommendations regarding non-revenue water and other Indiana American operational issues. OUCC witness Willoughby recommended adjustments to non-construction costs for one of Petitioner's lift station projects, denial of another lift station project, and denial of Petitioner's proposed acquisition of property in Sheridan for new wellfields.

Industrial Group witness Mr. Gorman recommended adjustments to Petitioner's overall rate of return, return on common equity and capital structure, and other revenue requirement adjustments reflecting a reduction to total company revenue requirement from approximately $92.1 million over three steps to approximately $60.6 million. His recommended return on equity is 9.10%, which produces an overall return of 6.00% for 2023, 5.97% for 2024, and 6.08% for 2025. Mr. Gorman also proposed a three-year amortization period to return Indiana excess accumulated deferred income tax ("EADIT"), an adjustment to Petitioner's offset to its revenue requirement based on URT over-collection to include carrying charges at an 8% interest rate, an adjustment to projected O&M expense based on his proposed inflationary factors, and adjustment to projected residential sales to reflect a slowing in reduced use per customer, a reduction to projected contractor expense, and an adjustment to salaries and wages expense to address employee attrition. He also objected to the inclusion of the prepaid pension asset and the OPEB asset in Petitioner's capital structure.

Industrial Group witness Ms. York recommended adjustments to Petitioner's class cost of service study ("COSS") and its proposed spread of the requested revenue change across rate classes. Specifically, Ms. York recommended that any rate increase approved by the Commission be implemented in the form of an across-the-board rate, system average increase. In addition, Ms. York recommended that the Commission direct Indiana American to make meaningful movement toward cost of service for its wastewater customers to reduce the non-cost-based subsidy that is currently being provided by water customers. She also recommended that Petitioner be required to move toward class-specific rates, beginning with developing and implementing a separate rate schedule for the industrial class at the conclusion of this case. Lastly, Ms. York recommended that the revenue requirements associated with the DSIC and the SEI charge that are being rolled into base rates continue to be recovered from customers on a per meter basis, rather than a combination of meter charges and volumetric charges.

The Wholesale Customers witness Callocchia recommended the Commission reject Petitioner's COSS and require any increase to be implemented across-the-board to each customer class, make changes to Petitioner's proposed rate design to recover DSIC and SEI costs via meter charges, and require Petitioner properly calculate a transmission rate for Wholesale Customers.

CAC witness Inskeep and Crown Point witness Guerrettaz argued for a lower ROE and Mr. Inskeep made recommendations with respect to URT over-collection and certain existing fees and charges that would affect the overall revenue requirement.

C. <u>INAWC Rebuttal</u>. Mr. Shimansky rebutted positions taken by the CAC, Crown Point, Industrial Group, and OUCC, with respect to overall revenue requirements, rate base forecasts, specific projects included in the case, the Hamilton County Bakers Corner transmission main, the Montgomery County surcharge, Indiana State EADIT, prepaid pension and OPEB assets, proposed new regulatory accounts, depreciation and amortization, amortization lives, acquisition related expenses, recovery of deferred expenses, URT repeal impacts to revenues, operating revenues and associated adjustments, future test year filings, long-term planning, fees and charges, and Petitioner's tariffs. Mr. Shimansky testified that Petitioner is accepting certain Intervenor positions, including their position on Montgomery County and customer-side lead line property tax issues, the removal of certain expenses from the revenue requirement, and the update to the current IURC Fee.

Mr. Hobbs responded to criticisms raised by OUCC witnesses Bell, Parks, and Willoughby regarding Petitioner's proposed capital investments. Mr. Hobbs rebutted positions taken by the OUCC on the Winchester and Sheridan Major Projects, as well as other capital projects, and explained why these projects are necessary for Indiana American to continue providing safe and reliable service. Ms. Britto responded to OUCC witness Parks' recommendation that the Lake Station Water Treatment Plant ("WTP") should be removed from Petitioner's rate base, as well as to OUCC witness Seals' positions on non-revenue water and other Indiana American operations. She also addressed issues raised by Industrial Group witness Gorman and OUCC witness Malan regarding Petitioner's proposed headcount and line locate expense. Finally, she responded to issues raised by CAC witness Inskeep regarding Petitioner's disconnect process.

Mr. Rea responded to OUCC witnesses Bell, Sullivan, Compton, Dellinger, and Mierzwa, CAC witness Inskeep, Crown Point witness Guerrettaz, Wholesale Customers witness Callocchia, Whiteland witness Young, Industrial Group witnesses Gorman and York regarding issues related to: (1) affordability, (2) Universal Affordability Tariff, (3) cost of service, (4) water rate design, (5) revenue allocations, (6) wastewater revenue requirement reallocation, (7) Indiana American residential water usage analysis, (8) bill comparisons, and (9) revenue calculations.

Ms. Bulkley responded to the issues raised in the testimonies of OUCC witness Dellinger, Industrial Group witness Gorman, CAC witness Inskeep, and Crown Point witness Guerrettaz regarding a just and reasonable ROE and the appropriate capital structure for Petitioner in this proceeding.

Ms. Grisham addressed issues raised by the OUCC and the Industrial Group regarding labor and labor-related contract services, support services, and uncollectible expenses. Mr. Cifuentes responded to recommendations made by the OUCC concerning the proposed updates to the gross revenue conversion factor, proposed changes to the late payment fee percentage, removal of annualization adjustments as it pertains to Building Maintenance & Supplies, Telecommunications, Postage Printing & Stationery, Office Supplies & Services, Employee Related Expense Travel & Entertainment, Miscellaneous Expense, and Maintenance Supplies & Services. He also addressed the Industrial Group's proposed adjustment related to the application of certain inflationary adjustments. Mr. Kennedy responded to the changes recommended by OUCC witness Garrett to the average service life and Iowa curve estimates. Ms. Ciullo supported Petitioner's method of calculating and including income tax expense and accumulated deferred income taxes ("ADIT") and addressed the proposal by OUCC witness Stull to change the tax accounting regulatory treatment of the tax repairs deduction, its impact on income tax expense and ADIT and her adjusted calculation for the Average Rate Assumption Method ("ARAM") component of EADIT giveback. Mr. Farrell responded to Industrial Group witness Gorman's recommendation that the prepaid pension asset and OPEB asset be removed from Petitioner's capital structure for ratemaking purposes.

D. Cross-Answering Testimony. The OUCC and Intervenors filed cross-answering testimony on various topics. For example, OUCC witness Stull responded to rate design issues associated with Indiana American's DSIC and SEI capital trackers raised by Crown Point witness Guerrettaz, Wholesale Customers witness Callocchia, and Industrial Group witness York. OUCC witness Mierzwa responded to various witness testimony concerning their positions on the water COSS, revenue allocations, and rate design proposals presented by Indiana American. Industrial Group witness York responded to the positions taken by OUCC witness Mierzwa regarding COSS and revenue allocation and to Wholesale Customers witness Callocchia's COSS recommendations.

CAC witness Inskeep provided cross-answering testimony regarding other parties' positions regarding the Universal Affordability Tariff. Wholesale Customers witness Callocchia responded to testimonies submitted by the OUCC, Industrial Group, and CAC related to their positions regarding Petitioner's COSS, rate design, and affordability. District witness Wessler addressed certain concerns or questions raised by OUCC witness Parks regarding the anticipated water needs in Hamilton County, Indiana, by discussing the anticipated development plans and overall need for potable water and fire protection service in the District's service territory.

7. Petitioner's Rate Base.

A. Utility Plant Forecast.

1. Major Projects. Indiana American proposed to include two major projects in this Cause—the Winchester Major Project and the Sheridan Major Project. Both projects consist of replacing existing an WTP with a new, higher capacity WTP. The Winchester Major Project's projected in-service date is April 30, 2025, with an estimated cost of approximately $25 million. The Sheridan Major Project's projected in-service date is August 31, 2024, with an estimated cost of approximately $29.82 million.[8]

[8] Based on Petitioner's December 27, 2023 Submission of Monthly Update, the estimated cost of the Sheridan WTP is $30,584,508 and the Winchester WTP is $24,191,828.

a. Winchester Major Project.

i. INAWC Case-in-Chief. Mr. Hobbs testified Petitioner is proposing to replace the Winchester WTP because the existing plant has capacity issues, structural issues, as well as safety and water quality/quantity concerns. With respect to capacity, Mr. Hobbs testified the existing aeralator/filtration system at Winchester was constructed in 2001 and does not provide adequate filtration capacity to reliably treat the maximum daily demands for the system. He further testified a December 2020 TIC Aeralator Evaluation report indicated the Aeralator system is in poor condition and the Winchester system is not able to deliver 3,500 gallons per minute ("gpm") for three-hour durations to meet fire flow recommendations. Based on the Structural Assessment Summary, there are also structural concerns with the existing chemical building. Additionally, Mr. Hobbs testified that there are safety concerns present with the existing chemical transport process, as well as chemical system deficiencies identified at the existing chemical feed building. He further testified no clearwell storage exists at the existing facility and the Winchester WTP does not provide chlorine contact time to meet 4-Log inactivation of viruses.

Mr. Hobbs sponsored relevant portions of the Winchester Comprehensive Planning Study ("CPS"), which discusses the recommended solution for each project as well as alternatives Petitioner identified for each portion of the project. While the TIC Aeralator Evaluation report identifies rehabilitation of the Aeralator unit as a potential alternative, Mr. Hobbs testified that attempting to improve the existing facilities is not recommended for several reasons, including the condition of the existing facilities and inadequate capacity of the existing facilities. He testified replacement of the facility is therefore recommended. Mr. Hobbs sponsored Attachments MHH-7 through MHH-13 of Petitioner's Exhibits 3 and 3-C providing additional support for the Winchester Major Project.

ii. OUCC. Mr. Parks recommended the Commission disallow including the Winchester Major Project in rate base because Indiana American failed to support the need for the project at the $25 million cost. Mr. Parks testified the proposed replacement plant is oversized, there is no Life Cycle Cost-Benefit Analysis ("LCCBA") of alternatives as required by Ind. Code § 13-18-26-3, and it is too expensive at $25 million or $12.68 million per MG of rated capacity, which exceeds costs paid by other utilities for groundwater treatment plants. In addition, Mr. Parks testified Indiana American has not supported the total replacement of the existing plant with a much larger plant, and that its requested project costs are prudent and in the best interest of customers. Mr. Parks further testified there are substantial cost discrepancies in Indiana American's cost estimates that Petitioner has not mentioned or explained.

Mr. Parks testified Indiana American did not evaluate any alternatives for the Winchester Major Project and did not perform a LCCBA. Mr. Parks testified a LCCBA analysis is required under Indiana law to receive an Indiana Department of Environmental Management ("IDEM") construction permit for water treatment plant modifications or expansions. Indiana American must prepare and certify with its permit application that it has completed a LCCBA in accordance with Ind. Code § 13-18-26-3. Mr. Parks recommended that Indiana American be required to identify alternatives as part of its standard capital planning efforts and comply with Ind. Code § 13-18-26-3.

With respect to his contention that Indiana American did not support the total replacement of the existing plant, Mr. Parks testified Indiana American should have evaluated other alternatives, including the rehabilitation and repainting of the Unilator as an alternative to replacement. Mr. Parks cited to the Winchester CPS portions, which indicates the life expectancy of the existing Unilator can range from 25 to 35 years. Mr. Parks testified Indiana American has not provided evidence that the Unilator cannot be rehabilitated and repainted. Mr. Parks further testified that despite Petitioner's claims that it cannot meet maximum day demand (0.85 MGD in 2023) when only two of the four filter cells are in service providing a 0.72 MGD firm capacity based on 3.0 gpm/ft, Indiana American can currently meet peak demand in its Winchester system. Additionally, Mr. Parks testified Petitioner does not need to increase the Winchester WTP's firm and rated capacities because the Winchester CPS indicates decreasing maximum day demand through 2035. Further, with respect to Petitioner's decision to construct a new clearwell as part of the Winchester Major Project, Mr. Parks testified Petitioner has not demonstrated that it is required by IDEM under the Groundwater Rule to meet a 4-Log virus inactivation.

As to the proposed $25 million cost of the Winchester Major Project, Mr. Parks calculated a capital cost of $12.68 million per MG of capacity and testified this capital cost is significantly above two other similar WTP projects. He compared the Winchester Major Project to the Eastern Bartholomew Water Corporation WTP[9] and the Batesville Water & Gas Utility WTP.[10] Mr. Parks updated the costs to 2023 and estimated total project costs of $11.12 million and $9.1 million for the Eastern Bartholomew plant and the Batesville plant, respectively. Mr. Parks estimated the new Winchester plant without the maintenance garage should cost $6.65 million. Mr. Parks also testified Indiana American's estimated costs for the new Winchester facilities have varied and increased substantially since 2021. Mr. Parks also testified the proposed design and site layout of the water treatment plant are oversized, overly lavish, expensive, and unwarranted.

iii. <u>INAWC Rebuttal</u>. Mr. Hobbs disagreed with Mr. Parks' recommendation to disallow the Winchester Major Project because it fails to recognize the age, capacity, condition, or process challenges associated with the current facility. Mr. Hobbs explained that while the age and condition of the Aeralator unit is one of the primary reasons Indiana American determined to replace the Winchester treatment plant, there are a number of other critical areas of treatment and resiliency that need to be addressed as part of the overall project. He explained these challenges include capacity concerns, structural concerns, and process challenges, in addition to the Aeralator unit, that need to be addressed at the plant.

Regarding Mr. Parks' contention that Indiana American did not consider rehabilitating the Aeralator unit and other alternatives for the plant, Mr. Hobbs testified Petitioner considered three alternatives for the Aeralator unit, including rehabilitation, as identified and discussed in the Winchester CPS. As to Mr. Parks' claim that Indiana American did not perform a LCCBA, Mr. Hobbs walked through the relevant provisions of Ind. Code ch. 13-18-26 and explained why he believes the statute is unclear about what is required. Mr. Hobbs further noted the statute is

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[9] A 3.5 MGD rated capacity (all filters in service) groundwater treatment plant, office, lab, and clearwell placed in service on August 15, 2019 for a total project cost of $7.412 million, or $2.12 million per MG. Pub. Ex. 9 at 7-8.

[10] A 3.0 MGD rated capacity ion exchange groundwater softening plant that was placed in service in 2021. The total loan amount for the softening plant in 2019 was $6,053,911, or $2.02 million per MG as calculated by Mr. Parks. Pub. Ex. 9 at 8.

enforced by IDEM, and IDEM has not promulgated any regulations regarding what a life-cycle cost benefit analysis should include. He also testified that while IDEM has issued one guidance document, the document does not provide much additional insight into what is specifically required. Mr. Hobbs testified Indiana American followed the statutory language and compared the costs and benefits (not limited to monetized costs and benefits) of the proposed improvements to one or more alternatives.

Mr. Hobbs explained why Indiana American determined to replace the Aeralator unit instead of rehabilitating the unit as Mr. Parks suggests. He testified Winchester is the only district in Indiana American's system that is solely dependent on a single combination style unit or Aeralator for source of treatment, which adds operational complexity and maintenance challenges. He stated Petitioner's proposed separated process layout will allow the system's individual components (such as an individual filter) to be taken offline for maintenance and repair while maintaining treatment. Whereas, in contrast, Aeralators do not have the flexibility to take individual units offline for maintenance or repairs, and instead the entire unit must be taken out of service. Mr. Hobbs testified that the current Aeralator unit can only be taken out of service for approximately one-half day and rehabilitating the Aeralator unit is anticipated to take 4-5 months, which would require full temporary treatment during that time.

Further, Mr. Hobbs testified rehabilitation of the Aeralator does not consider the age and deteriorated condition of the existing Aeralator unit. He testified that at 22 years of service, the Aeralator is nearing its anticipated end of life. Mr. Hobbs explained that rehabilitating the existing Aeralator would also not address the issues of the existing Aeralator not being able to meet the maximum day demand of the system when two filters are out of service. Mr. Hobbs also disagreed that Indiana American does not need to increase the firm and rated capacity of the plant. He testified Mr. Parks' claim is based on his belief that it is acceptable for system demand to exceed firm capacity, which is not in alignment with water industry standards, Indiana Code, or the Ten State Standards. Mr. Hobbs reiterated that the existing Winchester plant does not have sufficient capacity to meet the current or projected maximum day demands of the system. Citing to the Winchester CPS, Mr. Hobbs testified Winchester had annual average day demands ranging from 0.508 MGD to 0.636 MGD and annual maximum day demands ranging from 0.724 MGD to 0.970, and these demands are projected to be 0.877 MGD, 0.859 MGD and 0.847 MGD for years 2025, 2030, and 2023.

Mr. Hobbs reiterated that addressing the Aeralator unit issues will not address the other challenges at the plant, including the lack of onsite clearwell storage, structural failures associated with the chemical building and the backwash holding tank, and the other challenges outlined in the Winchester CPS. Mr. Hobbs discussed each of these challenges and explained they need to be addressed in addition to the Aeralator unit. Mr. Hobbs testified that the new clearwell is needed to provide adequate fire flow protection in the system. He explained that the capacity from the current WTP is only adequate for meeting a fire flow demand of up to 2,500 gpm for the recommended 2-hour duration, and higher fire flows of 3,000 gpm to 3,500 gpm could not be sustained for the recommended 3-hour duration as needed for a significant number of commercial and industrial sites around the system. Mr. Hobbs also testified that one of the ancillary benefits of the added clearwell capacity is the achievement of 4-Log virus inactivation, which is an added benefit to Indiana American's customers and adds to system resiliency.

Regarding the cost of the Winchester Major Project and the cost estimates, Mr. Hobbs explained why Mr. Parks' comparisons to the Eastern Bartholomew Water Corporation and Batesville Water & Gas Utility water treatment plants are not appropriate. He testified that a more appropriate cost comparison would be to the Mooresville WTP that was completed more recently for a total cost of $21,708,452. Further, with respect to Mr. Parks' criticisms of Petitioner for providing varying cost estimates, Mr. Hobbs identified the various sources of the costs estimates Indiana American included in this Cause. He testified it is very rare that a cost estimate will remain the same from the preliminary identification and planning phase of a project to final design and construction of a project. Mr. Hobbs disagreed with Mr. Parks' contention the Winchester treatment plant is oversized and overly lavish, explaining recent water treatment plants constructed by Indiana American included similar amenities.

Mr. Hobbs reiterated that the Winchester Major Project is being competitively procured through a design-build proposal process and subsequent competitive sub-package bidding. He testified that Indiana American's estimated cost is therefore based on actual pricing. Further, Mr. Hobbs testified that only final, actual costs of the projects will be reflected in rate base.

iv. **Discussion and Findings.** With respect to the Winchester Major Project, the crux of the issue between Petitioner and the OUCC is whether Indiana American considered alternatives, such as rehabilitation of the existing plant, before making the decision to build a new water treatment plant. The OUCC contends Indiana American did not identify and consider alternatives for the plant and did not perform a LCCBA of these alternatives as required by Ind. Code § 13-18-26-3. Further, the OUCC contends Indiana American has not supported that total replacement of the plant is warranted and the plant is too expensive at $25 million.

As noted by Petitioner's witness Hobbs, Ind. Code § 13-18-26-3 is a statute enforced by IDEM. Ind. Code ch. 13-18-26 establishes conditions for receipt of an IDEM permit for water and wastewater treatment plants, one of which is for the applicant to certify that it has prepared and completed a LCCBA. *See* Ind. Code § 13-18-26-2. Whether Indiana American has complied with Ind. Code §§ 13-18-26-2 and -3 to prepare and complete a LCCBA for purposes of obtaining an IDEM permit is a decision to be made by IDEM, and not the Commission.[11] However, we agree with the OUCC that performing a life cycle cost analysis when determining whether to undertake a project, like construction of a new WTP, is generally a reasonable and appropriate first step because it can readily provide the necessary evidentiary support that the chosen project is reasonable, and that cost recovery should be authorized.

Although Indiana American argued that Ind. Code § 13-18-26-3 is unclear and that IDEM has not issued any specific guidance regarding a LCCBA, a life cycle cost analysis, which is a generally understood term in the engineering world, considers the total cost of building, as well as owning and operating, a particular asset and then compares that estimate to other alternative

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[11] In the future, the Commission will request copies of the LCCBA for which a utility has certified to IDEM that it has performed.

assets.[12] This type of analysis, which considers the estimated costs of owning and operating an asset along with the cost of construction, is generally favored because it will identify and favor solutions that may have slightly higher, one-time construction costs but provide greater value through reduced day-to-day operating costs over years.

Although Indiana American did not provide such a full life cycle cost analysis, Mr. Hobbs provided Attachment MHH-7 of Petitioner's Exhibit 3C (the relevant portions of the Winchester CPS), which identifies and discusses the alternatives Petitioner considered for the Aeralator unit and other portions of the project. Mr. Hobbs explained that while Indiana American did consider rehabilitating the existing Aeralator unit, horizontal or vertical pressure filters for treatment as Petitioner is proposing with the Winchester Major Project will provide much greater flexibility for future operations. He also explained that the downtime associated with the rehabilitation work is anticipated to take four to five months and, during that time, full temporary treatment would be required. Mr. Hobbs also addressed the issues with rehabilitating the existing Aeralator and explained why the current unit, if rehabilitated, would still not be capable of meeting maximum day demands or address the other operational and structural challenges at the plant.

Ultimately, the record shows that the current Winchester WTP is not capable of meeting current or projected maximum day demands for the Winchester system and is not capable of meeting the recommended fire flows. The record further shows that the Aeralator treatment unit is the only source of treatment in the Winchester district, and Winchester is Indiana American's only system that is solely dependent on a single combination style unit or Aeralator for source of treatment. No evidence was offered to show that replacing or rehabilitating the Aeralator unit would produce any savings in the overall project cost, or that replacing the Aeralator unit would address any of the other challenges currently present at the plant.

As for the estimated cost of the Winchester Major Project, the OUCC took issue with the estimated $25 million cost, comparing it to two other treatment plants—Eastern Bartholomew Water Corporation and Batesville Water & Gas Utility. However, Mr. Hobbs explained why those plants were not good comparisons and presented evidence of the cost of the Mooresville WTP, which was completed more recently, of a similar scope, and reflects the price escalation for capital projects seen in recent years due to the COVID pandemic. The evidence further reflects that the project was procured through a design-build proposal process and subsequent competitive sub-package bidding. Thus, Indiana American's estimated cost is based on actual pricing.

Based on the evidence presented, we find that the Winchester Major Project is reasonable and necessary to address the challenges identified at the existing Winchester WTP and provide safe and reliable service to Petitioner's customers. We also find that the $25 million estimated cost of the project reflects the market price for this project. Once the project is complete and placed in service, Indiana American is authorized to true-up this cost to the actual cost of the project, subject to the compliance filing process discussed below.

Finally, regardless of any IDEM requirement concerning the performance of an LCCBA,

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[12] *See e.g.*, American Water Works Association ("AWWA") Asset Management Definitions Guidebook at 18-19, and the Life-Cycle Costs Analysis by the National Institute of Standards and Technology (https://www.wbdg.org/resources/life-cycle-cost-analysis-lcca).

we encourage Indiana American to undertake a life cycle cost analysis that estimates the overall costs (planning, design, construction, commissioning, operations, maintenance, and retirement) of project alternatives when considering and evaluating future projects to demonstrate more easily that its chosen project is reasonable.

b. Sheridan Major Project.

i. INAWC Case-in-Chief. Mr. Hobbs explained Petitioner is proposing to build the new Sheridan Water Treatment Plant to help address challenges meeting maximum day demands, to help serve growth in the service area, and to address other operational challenges. With respect to the plant's capacity challenges, Mr. Hobbs testified the existing Sheridan WTP has a firm capacity of 0.4 MGD, has experienced maximum day demands that have exceeded the plant firm capacity, and is not designed for expansion. Mr. Hobbs further testified that much of the existing facility and equipment dates back to the 1960s and has limited remaining life. He also testified the existing facility uses chlorine gas, which can pose a safety hazard to both employees and customers, and does not have an ammonia feed system, which can present challenges for maintaining a stable chloramine level.

Mr. Hobbs sponsored relevant portions of the Sheridan CPS, which identified the alternative of rehabilitation and expansion of the existing plant to the Sheridan Major Project. Mr. Hobbs testified that while Petitioner considered continuing to use the existing facility, doing so was not the recommended solution for several reasons. He testified continuing to use the existing plant would require major facility upgrades and replacements, or essentially a rebuild of the existing facilities, along with requiring construction of new plant facilities for adequate capacity expansion, for conversion from gaseous chlorine to liquid sodium hypochlorite, and for addition of liquid ammonium sulfate. Mr. Hobbs testified that maintaining the existing facility would also require additional cost for providing treatment while it is rebuilt. Mr. Hobbs further testified that by constructing one new expandable facility, Petitioner can maintain safe and reliable service while the new facility is being completed. Mr. Hobbs sponsored Attachments MHH-14 through MHH-23 providing additional support for the Sheridan Major Project.

ii. OUCC. Mr. Parks recommended the Commission disallow the Sheridan Major Project because Indiana American failed to support the need for the project at the $29.82 million cost and did not support that a total replacement of the existing plant with a much larger plant, is prudent, reasonable, or in the best interest of customers. Like the Winchester Major Project, Mr. Parks testified the proposed replacement plant is oversized, has no LCCBA of alternatives as required by Ind. Code § 13-18-26-3, and is too expensive at $29.82 million or $15.38 per MG of rated capacity.

Mr. Parks testified Indiana American did not evaluate any alternatives besides replacement of the water treatment plant and did not conduct a LCCBA. Mr. Parks testified that Indiana American provided no testimony that a condition assessment was conducted to evaluate the equipment and treatment building to determine whether the existing facility could be expanded as an alternative to replacement. He testified there is no evidence that Petitioner considered the rebuild/expansion/upgrade alternative in any way other than in a perfunctory manner. Mr. Parks further testified that Petitioner does not need to increase Sheridan's firm and rated capacities and claimed that expansion in the near term (five years) does not appear to be needed and could be delayed further if a fourth vertical pressure filter is added. Mr. Parks also testified that Indiana American should perform a regionalization study as identified in the Sheridan CPS and pause its plan to replace the Sheridan WTP until the study has been completed. He also took issue with the fact that Sheridan's new plant capacity does not include water demand for the new wholesale customer, the District.

Like the Winchester Major Project, Mr. Parks compared the Sheridan Major Project to the Eastern Bartholomew Water Corp. and Batesville plants and testified Sheridan's capital cost is significantly more expensive than these plants. Mr. Parks estimated the new Sheridan Water Treatment Plant to cost $7.0 million instead of the $29.82 million requested by Petitioner.

iii. <u>INAWC Rebuttal</u>. Mr. Hobbs disagreed with Mr. Parks' opinion and recommendation, testifying that Mr. Parks fails to recognize the age, capacity concerns, condition, operation, and process challenges of the Sheridan facility. Mr. Hobbs explained that Indiana American needs to replace the existing Sheridan treatment plant due to capacity concerns, the age of the facility, operational challenges, the need to switch from chlorine gas to liquid sodium hypochlorite, and to add an ammonia feed, among other issues.

Regarding the capacity challenges, Mr. Hobbs testified Petitioner already has challenges meeting maximum day demands and the near future potential growth in the service area will only exacerbate these concerns. He explained that between 2018 and 2021, the Sheridan system had annual average day demands ranging from 0.18 MGD to 0.22 MGD and annual maximum day demands ranging from 0.38 MGD to 0.41 MGD. Mr. Hobbs testified that maximum day demand of the low, base, and high scenarios is projected to increase to 0.53 MGD, 1.07 MGD, and 1.48 MGD respectively, by 2035. He explained that the existing Sheridan WTP has a total filtration capacity of 0.65 MGD and a firm filtration capacity of 0.43 MGD with one of the three filters out of service. Thus, the current firm filtration capacity is inadequate to meet the projected maximum day demands for all three scenarios. Mr. Hobbs testified the proposed water treatment plant is sized with a firm treatment capacity to meet the projected maximum day demands and can expand as additional capacity is needed. He also noted the Sheridan system is located in Hamilton County, which is one of the state's fastest growing counties, and therefore he anticipates the system demand to grow beyond the 15-year projected demand.

Mr. Hobbs responded to Mr. Parks' recommendation that Indiana American wait to construct the new Sheridan WTP until it completes a regionalization study and the relationship of the study to the District. He explained the purpose of the regionalization study is to determine the optimal means of providing water service to the District and all other regionalization areas between Sheridan and Noblesville, as well as to evaluate the impact and benefits of connecting Sheridan to Noblesville and the possibility of supplying water to Sheridan from Noblesville. He explained that Indiana American has not sized the new Sheridan WTP to serve a fully developed Bakers Corner, and the design of the plant at initial completion is intended to serve growth in Sheridan (the area proposed to be served by the District). Mr. Hobbs testified that the plant is being built so it can readily be expanded in the future and explained that if Indiana American determines to ultimately serve Hamilton County from the Sheridan WTP, Petitioner would expand the plant and add additional source of supply to do so.

Mr. Hobbs disagreed with Mr. Parks' recommendation that Indiana American should wait to construct the plant until completion of the regionalization study. He testified the Sheridan Major Project is to help address the current and projected water challenges in the system and the design of the plant at initial completion is intended to serve the growth in Sheridan. Mr. Hobbs testified that while the regionalization study will be helpful for determining how to serve the undeveloped areas in Northern Hamilton County in the long-term, as well as future growth in the service area, this study does not change that Indiana American cannot reliably meet Sheridan's maximum day demands today.

As to Indiana American's evaluation of alternatives for the Sheridan WTP, Mr. Hobbs testified the Sheridan CPS identified the following two alternatives: (1) constructing a new water treatment facility; and (2) conducting a facility assessment for complete rehabilitation/expansion of the current facility. Mr. Hobbs testified Petitioner determined Option 2 (rehabilitation/expansion of the existing plant) was not feasible because much of the existing facility and equipment dates back to the 1960s and has limited remaining service life. He explained Petitioner does not believe it would be a prudent investment to make costly repairs and updates to a 60-plus year-old facility that is already approaching the end of its useful life. He also identified the challenges associated with attempting to expand the plant, and questioned whether the current plant could be expanded. With respect to the LCCBA, Mr. Hobbs again explained that Indiana American followed the statutory language and compared the costs and benefits of the proposed improvements to one or more alternatives.

As for the cost of the Sheridan Major Project, Mr. Hobbs reiterated why Mr. Parks' comparisons to the Eastern Bartholomew Water Corporation and Batesville Water & Gas Utility water treatment plants are not appropriate comparisons. He testified the Sheridan Major Project was competitively procured through a design-build proposal process and subsequent competitive sub-package bidding, and therefore, Indiana American's cost is based on actual pricing. He again testified that a more appropriate cost comparison would be to the Mooresville WTP, which was completed more recently for a total cost of $21,708,452.

iv. <u>Discussion and Findings</u>. Like the Winchester Project, the major dispute between the parties with respect to the Sheridan Major Project is whether Indiana American considered alternatives to total replacement of the WTP and whether Indiana American evaluated these alternatives as part of a LCCBA. Here, the OUCC argued that Indiana American did not perform a condition assessment to evaluate the equipment and treatment building to determine whether the existing facility could be expanded as an alternative to replacement. Further, the OUCC argued Indiana American should pause its plan to replace the Sheridan WTP until a regionalization study is completed.

We again concur with the OUCC about the benefits of performing a life cycle cost analysis that compares the costs of construction and operation of an asset over its useful life with the costs of various alternative assets before embarking on a significant project. While Indiana American did not undertake such an analysis here, we find, in this instance, that Petitioner has sufficiently demonstrated the reasonableness and necessity for the Sheridan Major Project. Mr. Hobbs explained that Indiana American did consider rehabilitating and expanding the plant, but such option is not feasible or recommended because much of the existing facility and equipment dates back to the 1960s and is at the end of its useful life. Petitioner expanded on this issue in its response to the Commission's August 25, 2023 Docket Entry, where it included pictures of the existing Sheridan WTP showing existing building deterioration, building footprint limitations for expansion, current use of gas chlorination, and the space for a fourth filter installation being occupied by laboratory and chemical use.

The evidence also demonstrates that Petitioner currently has challenges meeting maximum day demands and that potential growth in the service area in the near future will only exacerbate these concerns. Mr. Hobbs explained that even if the current plant could be rehabilitated, it would still need to be expanded to address these capacity challenges. He also explained why it is questionable whether the current plant could even be expanded, including the closeness of the wells and filter capacity limitations. Mr. Hobbs identified multiple challenges that would need to be addressed to expand the existing facility, and identified a number of other operational and structural issues that need to be addressed as part of the project.

With respect to the need for the new Sheridan WTP, Mr. Hobbs testified that the Sheridan system is located in Hamilton County, which is one of the fastest growing areas in the State. The record shows that Indiana American already has challenges meeting maximum day demands in the service area as the recent historical maximum day demand of 0.41 MGD is already nearly equal to the firm capacity (0.43 MGD) of the current 60-year old plant, without any consideration for growth. Given the likelihood for significant future growth in this area, these capacity challenges are likely to only get worse in the near future.

The OUCC argues that Indiana American should put a pause on the project until it has had the opportunity to conduct a regionalization study to determine how service should be provided in the service territory. However, as Mr. Hobbs explained in his rebuttal testimony, the design of the Sheridan Major Project at initial completion is intended to serve growth in Sheridan, and Indiana American cannot reliably meet Sheridan's maximum day demands today. Further, the record shows that the sizing of the WTP excludes the District's demand, so if it is determined through the regionalization study or other means that the Sheridan WTP will be used to serve this new customer, this will only exacerbate the capacity challenges Indiana American is experiencing in the Sheridan service area. We agree that while the regionalization study will be useful for helping Petitioner determine how to serve northern Hamilton County in the long-term, it will not address the current system capacity challenges or the other operational and structural concerns at the plant.

Like the Winchester WTP, the OUCC also took issue with Petitioner's estimated cost for the Sheridan Major Project of $29,817,795. Mr. Parks compared the Sheridan Major Project cost to the Eastern Bartholomew and Batesville plants and used this comparison to argue the cost of the project is too high. Mr. Hobbs disagreed with Mr. Parks that the Eastern Bartholomew and Batesville plants provided an appropriate comparison, and again pointed to the Mooresville plant as a more appropriate comparison.

For the reasons discussed previously for the Winchester Major Project, we do not need to address the issue of which cost comparison is more appropriate. The record shows that the Sheridan Major Project was bid and the estimate included in Indiana American's case-in-chief reflects the actual pricing received. We therefore find that the $29,817,795 estimated cost of the project reflects the market price for this project. Once the project is complete and placed in service, Indiana

American is authorized to true-up this cost to the actual cost of the project, subject to the compliance filing process discussed below.

2. **Other Disputed Rate Base Items**.

a. **Main Extension to Hamilton County Regional Utility District**.

i. INAWC Case-in-Chief. As part of its capital additions in this Cause, Indiana American proposed to extend 11,400 feet of 20-inch transmission main for Phase 1, and 7,700 feet of 16-inch transmission main for Phase 2, east from Sheridan to connect to the future District's water system at Springmill Road & 236th Street, more commonly known as Bakers Corner.[13] Indiana American proposed the project for inclusion because it entered into a SFR agreement to provide drinking water for the District located between Sheridan and Noblesville, and interconnection with an existing Indiana American Water system was required to serve District.

ii. OUCC. Mr. Parks took issue with the project and argued that the project is a main extension subject to the Commission's main extension rules under 170 IAC 6-1.5. Mr. Parks testified Petitioner should have developed a main extension agreement and developed the estimated costs to design and construct the main extension. He further testified that all costs, except a three-year revenue allowance, are the responsibility of the District and should be paid to Indiana American. Mr. Parks testified that the project costs should not be added to rates without a main extension payment by the District reflecting its contribution in aid of construction. Mr. Parks further testified that because it appears Petitioner has not properly characterized the project as a main extension, he recommended disallowing recovery of the capital costs in rate base.

iii. INAWC Rebuttal. Mr. Hobbs disagreed with Mr. Parks' contention that the new transmission main to connect Indiana American's system with the newly formed District is a main extension subject to the Commission's rules under 170 IAC 6-1.5. Mr. Hobbs testified the Indiana General Assembly enacted Ind. Code § 8-1-2-46.2(b) which provides:

> (b) Notwithstanding any law or rule governing extension of service, a water or wastewater utility may, on a nondiscriminatory basis, extend service:
> (1) for economic development purposes;
> (2) to rural areas; or
> (3) to developed but underserved areas;
> without a deposit or other adequate assurance of performance from the customer, to the extent that the extension of service results in a positive contribution to the utility's overall cost of service over a twenty (20) year period. For the purposes of this subsection, a water or wastewater utility's extension of service to a developed but underserved area will be considered as resulting in a positive contribution to the utility's overall cost of service over a twenty (20) year period to the extent that

[13] *See* Petitioner's Exhibit 3, Attachment MHH-4 at 1-2.

> rates to be paid by fifty percent (50%) or more of the customers who could be served by the extension of service would enable the utility to fully recover the weighted cost of debt and depreciation expense attributable to the cost of the main extension for the extension of service.

Mr. Hobbs testified that this is a unique main extension in one of the (if not the) fastest growing areas in the State.

Indiana American witness Shimansky sponsored the calculation showing Indiana American satisfied the 20-year test set forth in Ind. Code § 8-1-2-46.2(b). Mr. Shimansky explained how the test would be applied and sponsored Attachment GDS-2R, which showed the extension will result in a positive contribution of service in year 13. Mr. Hobbs testified that because the extension of service will result in a positive contribution to Indiana American's overall cost of service over a 20-year period, no deposit from the District was required and the Commission's main extension rules did not apply. Mr. Hobbs testified that Mr. Parks' testimony about a three-year revenue allowance and a requirement that Hamilton County fund a portion of the cost is therefore incorrect.

Mr. Hobbs reiterated why the new transmission main to the District is a unique main extension. He said it is well understood that Hamilton County has long been one of the fastest growing areas in the State. He testified that in a matter of a few years, much of the County has grown from towns and small cities surrounded by farmland into a densely populated and largely urban area. He further testified that growth has continued north in the County and has reached the point that only the northern portion of the County remains undeveloped.

Mr. Hobbs expanded on the purpose of the regionalization study, the relationship of the study to serving the District, and Indiana American's overall regionalization strategy for serving the new growth in northern Hamilton County. Mr. Hobbs explained that Indiana American has not sized the new Sheridan WTP to serve a fully developed Bakers Corner, but the plant is being built so that it can be readily expanded in the future if needed. Mr. Hobbs explained that a regional approach will be needed to meet this need so that development in Hamilton County is not hindered due to lack of capacity to serve new growth. Mr. Hobbs testified that Petitioner is in the process of conducting a regionalization study, and once the study is completed and Petitioner has a more complete understanding of the best way to bring water to the entirety of the undeveloped area in northern Hamilton County, Indiana American will be in a position to know whether the full buildout of Bakers Corner should be served by a further expansion of the Sheridan Plant, interconnection to a future expansion of the Noblesville Plant, a combination of the two, or some other option that has not yet been identified.

iv. __Discussion and Findings__. The crux of the issue between the parties with respect to this project is who should be responsible to pay for the transmission main to interconnect and serve the District. The OUCC argues this is a main extension that should be subject to the Commission's main extension rules at 170 IAC 6-1.5, and thus should be primarily funded by the District. In contrast, Indiana American argues this is a unique main extension that falls under Ind. Code § 8-1-2-46.2(b), which allows a water utility to, among other things, extend service for economic development purposes or to rural areas, without a deposit from the customer if the extension of service results in a positive contribution to the utility's overall cost of service over a 20-year period.

Ind. Code § 8-1-2-46.2(b) authorizes a utility to extend service: (1) for economic development purposes; (2) to rural areas; *or* (3) to developed but underserved areas. (emphasis added). While Indiana American argues that the main extension is for economic development purposes, this does not appear to be supported in the record. Mr. Hobbs testified as to the expected growth in the area but did not specify the type of growth expected. Our review of the area reveals, except with some minor exceptions along U.S. 31, the main extension will likely be dominated by residential growth. However, the statute also authorizes the extension of service to rural areas and no party disputed that this main extension would extend service to a rural area of the State.[14]

Mr. Shimansky sponsored Attachment GDS-2R to Petitioner's Exhibit 15 showing the extension will result in a positive contribution of service in year 13. Mr. Shimansky assumes that the District's water use will increase to its projected usage of 2.45 MGD over a 20-year period by adding approximately 900 customers a year. However, this assumption has no foundation in the record and contradicts the District's own projections. In response to an OUCC discovery request, the District states there is no study that supports adding approximately 900 customers a year. Pub. Ex. CS-7, Part 1 at 2 of 335. The District goes on to note that for cash flow purposes, it has assumed growth of only 150 customers per year. *Id.* Further, the District projections show growth of approximately 150 customers per year for years one through ten and only 75 customers per year for years 11 through 20. Pub. Ex. CX-7, Part 2 at 151 and 154 of 252. Using the District's projections, the proposed extension will not result in a positive contribution of service until approximately year 33.

Based on the evidence presented, we find Indiana American has not satisfied the requirements of Ind. Code § 8-1-2-46.2(b) to demonstrate that the main extension will result in a positive contribution to the utility's overall cost of service over a 20-year period. As such, the Commission's main extension rules apply. Therefore, the estimated $9,238,302 project costs should not be added to rate base without a main extension payment by the District reflecting its contribution in aid of construction. If Indiana American proceeds with the project under the Commission's main extension rules, it is authorized to reflect its portion of the main extension cost in rate base, which is generally the revenue allowances provided by the main extension rules.

We further agree that a regional approach is needed to ensure the provision of water service keeps pace with development in Hamilton County. We believe the regionalization study Indiana American is in the process of conducting is a critical tool in determining how to serve these rural, undeveloped areas in northern Hamilton County in the long-term, as well as future growth in the service area. As such, we encourage Indiana American to complete the regionalization study to determine how best to regionalize service in Hamilton County in the future.

[14] Ind. Code § 8-1-2-46.2 does not define "rural area." The Mirriam-Webster Online dictionary defines "rural" as "relating to the country," which is consistent with the definition of "rural area" in other sections of Title 8 (i.e., Ind. Code §§ 8-1-2-87 and 89) as areas in Indiana but outside municipal corporate limits.

b. Future Source of Supply.

i. INAWC Case-in-Chief. Petitioner included four future sources of supply projects in this Cause: (1) Project I10-100020 – KOK Sheridan Property Acquisition for New Well or Wells ("Sheridan Property"); (2) Project I10-500003 – CRW SOS Test and Property Acquisition; (3) I10-600024 – NOB Hamilton Co SOS Property Purchase; and (4) Project I10-600010-03 – NOB WRCC SOS Property. Mr. Hobbs testified Petitioner prepared plans to develop each of these future sources of supply and is seeking approval of those plans and to add the actual costs of these sources of supply to the value of Petitioner's property pursuant to Ind. Code § 8-1-2-23.5.

Mr. Hobbs sponsored Petitioner's plans to develop each of these future sources of supply as Attachment MHH-24 to Petitioner's Exhibit 3, and testified the information required by Section 23.5 is included in Petitioner's plans for each of the future sources of supply. Mr. Hobbs testified that Indiana American's future source of supply plans are reasonable and prudent for the provision of safe and reliable service.

ii. OUCC. Ms. Willoughby challenged the Sheridan Property project. She recommended the Commission reject the $779,566 Indiana American requested to include in rate base for the proposed acquisition of property for the new well(s) in Sheridan because it is not currently necessary and prudent for Petitioner to acquire property for a future wellfield in Sheridan. She testified that the rates set in this case are intended for projects through April 2025, and population growth estimates through 2040 show that Sheridan will not be utilizing even half of its current wellfield capacity before the addition of proposed new Well No. 7. Therefore, she recommended the Commission deny the $779,566 requested for the acquisition of land for new well(s) in Sheridan.

iii. INAWC Rebuttal. Mr. Hobbs testified that he believes Ms. Willoughby's objection is actually to Ind. Code § 8-1-2-23.5, which allows a water utility to acquire vacant ground for a future well field before that land has been developed and becomes unavailable. Mr. Hobbs explained that the rate of growth and development in Sheridan creates the present need to obtain property rights for future sources of supply, and Indiana American is competing for property rights with development firms that intend to develop property for other purposes. Mr. Hobbs testified that if Indiana American's future source of supply plan is approved and the additional source of supply is captured in rate base, but not placed in service by the date identified in the timetable, then the statute sets forth a refund procedure to restore customers.

iv. Discussion and Findings. Ind. Code § 8-1-2-23.5 allows a public utility to seek Commission approval of a plan to develop a future source of water supply. Section 23.5(a) requires the utility's plan to include: (1) the timetable for placement in service of the future source of supply; (2) the cost of the source of supply; (3) the need for a new source of supply within the public utility's timetable; (4) the availability of alternatives to the proposed source of supply; and (5) the need to secure property rights to preserve and protect the planned future source of supply.

The only future source of supply project challenged was the Sheridan Property project. The

OUCC argues that this project should not be allowed in rate base because additional wellfield capacity is not currently needed in Sheridan and will not be needed by April 2025, the period rates are to be set for this Cause.

We agree with Indiana American that Ind. Code § 8-1-2-23.5 allows a water utility to acquire vacant ground for a future well field before that land has been developed and becomes unavailable, even if the completion date extends beyond the test year. However, we find Petitioner has failed to satisfy Ind. Code § 8-1-2-23.5(a)(4) with respect to the Sheridan Property project. Petitioner's Exhibit 3, Attachment MHH-24, which contains Petitioner's plan for each of the source of supply projects, provides the following for the Sheridan Project:

> Indiana American Water has initiated a preliminary hydrogeologic study to evaluate potential locations for development of ground water source of supply in the area. Ground water source of supply is preferred and anticipated to be available for the projected demands. *Alternatively, development of a surface water source of supply could be evaluated.* The development of surface water requires additional challenges and time that may not be available depending on rate of drinking water demand growth.

Id. at 67, emphasis added. No specific surface water source was identified, no analysis was provided, and no conclusions were rendered concerning possible alternatives to the proposed project.[15] Instead, Petitioner's plan simply indicates that development of a surface source of supply *could be* evaluated. Accordingly, because Petitioner failed to sufficiently address the availability of alternatives to the proposed Sheridan Property project, we cannot find Petitioner's plan for that project is reasonable and prudent for the provision of safe and reliable service at this time.

As for the other three source of supply projects, we find Indiana American has included the information required under Ind. Code § 8-1-2-23.5(a) and the plans for those three projects are reasonable and prudent for the provision of safe and reliable service for the reasons set forth in Mr. Hobbs' direct testimony and Attachment MHH-24. Accordingly, we find Petitioner may reflect the costs of developing the following in rate base as set forth in Ind. Code § 8-1-2-23.5(b): (1) Project I10-500003 – CRW SOS Test and Property Acquisition; (2) I10-600024 – NOB Hamilton Co SOS Property Purchase; and (3) Project I10-600010-03 – NOB WRCC SOS Property.

c. <u>Lake Station Water Treatment Plant</u>.

i. <u>INAWC Case-in-Chief</u>. Indiana American did not discuss the Lake Station WTP and wells in its case-in-chief testimony.

ii. <u>OUCC</u>. Mr. Parks recommended the Lake Station WTP and wells be removed from Indiana American's rate base because they are not needed from a technical, operational, or economic standpoint. Mr. Parks testified that the WTP and wells have been continually out of service since February 5, 2019, and have not produced any finished water for over four years. Mr. Parks explained that while Indiana American provided testimony in Cause No. 45041 that it would maintain and regularly place the plant into operation to ensure rapid

[15] Petitioner's response to our August 17, 2023 Docket Entry provided no additional information. Pet. Ex. 27.

reliability to use during peak demand days, or as emergency supply, Indiana American has not restarted the wells and treatment plant nor produced any water since closing on the acquisition. Mr. Parks further testified that Indiana American was not able to show it is incurring O&M costs to keep the Lake Station WTP in a state of ready availability if needed during peak day demands or emergencies.

Mr. Parks testified that the Lake Station WTP is not needed during peak demand days or emergencies. He explained that Indiana American meets peak demand in its Northwest Indiana District without operating the Lake Station treatment plant and has also met demand in Northwest Indiana during voluntary shutdowns of the Ogden Dunes WTP without the Lake Station WTP on-line. Mr. Parks also testified that reopening the existing East Chicago interconnection and purchasing water would serve as a lower marginal cost alternative than restarting the Lake Station wells and WTP in response to an emergency. Finally, Mr. Parks testified that Indiana American did not propose any "ratemaking options that might mitigate the impact of the purchase price" of the wells and WTP as suggested by the Commission in its Order in Cause No. 45041.

OUCC witness Stull sponsored Petitioner's adjustment to remove $6,539,385 from rate base for the Lake Station wells and WTP. *See* Pub. Ex. 3, Attachment MAS-1 at 3.

iii. <u>INAWC Rebuttal</u>. Indiana American witness Britto testified that contrary to Mr. Parks' testimony, the Lake Station WTP is fully operational and is maintained day-to-day in standby status. Ms. Britto testified that the WTP maintains an active WT3 Operator License through IDEM and has all of the necessary equipment (including chemicals and chemical feed equipment) to produce potable, finished water. Ms. Britto further testified that maintenance is regularly performed, and Indiana American personnel operate the wells and pumps on a monthly basis to ensure the plant remains fully operational. She also testified that at least one employee is on-site at the WTP each day to do visual inspections and confirm there are no issues at the plant. The WTP also maintains its own chemicals inventory and disinfection chemicals are kept on-site in the event treatment is needed.

Ms. Britto further explained the WTP is maintained in standby status to minimize the day-to-day operations and maintenance expense associated with operating the plant. She testified the WTP can be transitioned out of standby status to produce potable finished water within 24 hours. Ms. Britto testified that this is how Indiana American intended to operate the Lake Station WTP when it acquired the system in Cause No. 45041.

Ms. Britto disagreed with Mr. Parks' contention that the Lake Station WTP is not needed during peak day demands or emergencies and explained why the Lake Station WTP is needed in an emergency situation to serve the Northwest District.

Finally, Ms. Britto disagreed that reopening the East Chicago interconnection would serve as a lower cost alternative compared to operating the Lake Station WTP in standby status as Indiana American currently does. Ms. Britto testified that Indiana American cannot simply open a valve and obtain water from the interconnection, and that in order to take East Chicago water into the Northwest Operations Distribution system, Petitioner would need to overcome the East Chicago Free Chlorine water with high quantities of chlorine injected at the connection site of the two systems. Ms. Britto explained that Indiana American does not currently have this equipment installed and the system is not equipped to do this. She said treating the water at the point of entry would require the construction of a structure to house the chlorine, chlorine inventory onsite, flow control equipment, chemical feed equipment and monitoring equipment. In addition to these capital investments, Ms. Britto testified there would be additional O&M costs associated with operating this equipment, including maintenance costs, security costs, and labor costs to maintain the site. She testified that this is just one example of why providing water via the East Chicago interconnect would not provide a lower cost marginal alternative in an emergency situation.

Indiana American witness Shimansky responded to Mr. Parks' contention that Indiana American did not propose "ratemaking options that might mitigate the impact of the purchase price" of the wells and treatment plant. Mr. Shimansky testified Petitioner has greatly reduced the level of O&M expense at the plant to minimize the impact of purchasing the plant. He provided Petitioner's Exhibit 15, Attachment GDS-1R, which showed the customer bill impact from having the Lake Station plant ready to activate in an emergency is 12 cents per month.

iv. <u>Discussion and Findings</u>. Before addressing the parties' dispute over whether the Lake Station WTP should continue to be maintained as an emergency backup source of water supply, we must address an error in the OUCC's proposed accounting for its recommendation. In Cause No. 45041, the Commission found the Lake Station WTP to be used and useful.[16] The Commission's Order was affirmed on appeal on this specific question. *Ind. Off. of Util. Consumer Counselor v. Indiana-American Water Co., Inc.*, 129 N.E.3d 833 (table), 2019 WL 2608488 (Ind. Ct. App. 2019) (unpublished opinion).[17] We also approved in that same Order, the journal entry to record the acquisition of the Lake Station WTP as used and useful utility plant. The OUCC's position is that used and useful plant is no longer needed and is therefore no longer used and useful, which is essentially an argument that the plant should be retired. As Mr. Shimansky testified on rebuttal, the retirement of depreciable utility plant is recorded by debiting Account 108 (Accumulated Depreciation) and crediting UPIS for the original cost of the asset reflected on the utility's books. 170 IAC 6-2-2(a) and 1996 Uniform System of Accounts, Instruction 27(B)(2). The effect of these entries is offsetting—there is zero impact on net original cost rate base. *See,* e.g., *Ind. Mich. Power Co.*, Cause No. 44182 at 59 (IURC July 17, 2013). As such, even if we were to accept the OUCC's position, the effect of doing so would not produce the result that the OUCC seeks. There would be no reduction to net original cost rate base.

With the understanding that we are not addressing an issue that affects net original cost rate base, we now address the main dispute between the parties—whether the Lake Station WTP and wells are currently in operation and used and useful to Indiana American. This same issue was raised in the Lake Station acquisition case, where the parties disputed whether the Lake Station WTP assets would be used and useful following the acquisition.

While the OUCC asserted that the Lake Station WTP has remained out of service since February 5, 2019, and is not currently in operation, Indiana American provided evidence that it is

[16] Jt. Pet. of Indiana-American Water Co., Inc. and the City of Lake Station, Indiana, Cause No. 45041 at 32 (IURC Aug. 15, 2018).

[17] Ind. Off. of Util. Consumer Counselor, Town of Schererville v. Indiana-American Water Co., Inc., 137 N.E.3d 922 (Ind. 2019), transf. denied.

in operation and being maintained in standby status in the event of an emergency. Ms. Britto testified that the plant maintains an active WT3 Operator License through IDEM, it has all of the necessary equipment to produce potable, finished water, maintenance is performed regularly at the plant, and Indiana American personnel operate the wells and pumps on a monthly basis to ensure the plant remains fully operational. The evidence further demonstrates that the WTP can be transitioned out of standby status to produce potable finished water within 24 hours in the event of a chemical spill in Lake Michigan or another emergency requiring the plant to provide emergency capacity to the Northwest Indiana District.

The OUCC also questioned whether Indiana American needs the plant to serve the Northwest District in emergency situations, noting that Indiana American has met demand in Northwest Indiana during shutdowns of the Ogden Dunes WTP without the Lake Station plant online. On rebuttal, Indiana American explained why, and under what circumstances, Indiana American would need the Lake Station plant to serve the Northwest District in the event of an emergency. Pet. Ex. 17-C at 12. While Indiana American has not yet been required to activate the Lake Station WTP in an emergency situation, Ms. Britto's testimony demonstrates probable scenarios where this situation could become a reality.

The OUCC also argued that reopening the East Chicago interconnect would provide the lowest marginal cost alternative compared to the Lake Station WTP to provide service in response to an emergency. However, Ms. Britto explained why reopening the East Chicago interconnect is not feasible and would not provide a lower cost alternative to maintaining the plant in standby status. The evidence demonstrates that Indiana American cannot simply open a valve from the interconnect and the two water systems are incompatible because East Chicago is a free chlorine system whereas the Northwest District is a total chlorine system.

Finally, the OUCC argued that Indiana American has not proposed ratemaking options to mitigate the cost of the Lake Station WTP and wells. The language from our Order in Cause No. 45041 (at 32) encouraged Indiana American to propose ratemaking options that might mitigate the impact of the purchase price in future cases "*if it does in fact turn out the WTP and wells are not used and useful to Indiana American following the acquisition*." The evidence demonstrates that Indiana American has reduced O&M expenses at the plant to only those required to maintain the plant in standby status. Mr. Shimansky calculated a customer bill impact of 12 cents per month from having the Lake Station plant ready to be activated in an emergency.

Accordingly, based on the evidence presented, we find that the Lake Station WTP and wells are currently used and useful to Indiana American to provide service in the event of an emergency in the Northwest District. Indiana American has also taken steps to minimize the plant's O&M expense to mitigate costs to customers while still ensuring the plant's availability in the event of an emergency. As such, we find that the assets are appropriately included in rate base in this Cause.

d. <u>Lift Station Replacement Projects</u>.

i. <u>INAWC Case-in-Chief</u>. Indiana American proposed Project I10-110002 – Kokomo Wastewater Sheridan 6th Street Lift Station Replacement

(“6th Street Project”).[18] The project would replace the existing lift station that is past its useful life and currently cannot handle peak flows associated with the sanitary basin. While significant customer growth is not anticipated in the basins, increased inflow and infiltration (“I&I”) present capacity concerns in these areas. Petitioner noted overflows downstream of the lift station as well as flooding of the wet well during wet weather conditions. The current lift station mechanical and electrical components are in poor condition and at the end of their useful life. Additionally, the lift station is located within the State Road 38 right-of-way and the location and lack of safe access poses a safety risk to personnel during regular maintenance and operation.

Petitioner also proposed Project I10-110003 – Kokomo Wastewater Sheridan Maple Run Lift Station (“Maple Run Project”).[19] The project includes improvements to the existing Maple Run Lift Station pumping and electrical, as well as the addition of a metering vault structure. Improvements are needed to provide necessary pumping capacity for the South drainage sub-basin. The Maple Run lift station capacity is limited by a number of factors such as wet well size, pump capacity, force main size, and downstream discharge location capacity.

ii. OUCC. With respect to the 6th Street Project, Ms. Willoughby recommended the Commission disallow the inclusion in rate base of $1,791,005 because Indiana American did not provide sufficient evidence to support replacing the lift station or the cost estimate. She testified it is an imprudent use of ratepayer funds to install larger equipment to handle I&I without addressing the underlying cause for the I&I. Further, Ms. Willoughby testified Petitioner has not provided documentation to support replacement of the lift station based on its condition, or to support the cited safety concerns for relocating the lift station. She testified that having a lift station in the right of way is not unusual and does not necessarily make the location unsafe. Ms. Willoughby also took issue with Indiana American’s cost estimates and testified that Petitioner needed to provide documentation and calculations to support how the cost estimate was assembled.

With respect to the Maple Run Project, Ms. Willoughby recommended the Commission deny a portion (the final amount is confidential) of the proposed costs for overestimation of labor, contingency, and indirect overhead costs. She testified that Indiana American provided conflicting cost estimates for the project, and Petitioner’s cost estimates include errors.

iii. INAWC Rebuttal. Regarding the OUCC’s recommendation to disallow the 6th Street Project, Mr. Hobbs explained that addressing I&I in the basin as Ms. Willoughby suggests will help the entire system with a reduction in eventual treatment but will not address the issue that the station is undersized for the number of customers it serves, or address the other significant project drivers, such as the condition of the lift station, lack of current pumping capacity, site access, safety, and security. Mr. Hobbs testified Indiana American has attempted to address the I&I issues in the basins but addressing I&I will not obviate the need for replacement of the lift station. With respect to the current capacity concerns at the lift station, Mr. Hobbs testified that equivalent dwelling unit estimates coupled with a peaking factor of four indicate that the station needs to be sized at a minimum for a peak flow of approximately 370 gpm.

[18] Petitioner’s Exhibit 3, Attachment MHH-4 at p. 3.

[19] *Id.* at p. 5.

Mr. Hobbs testified that during a 2019 draw down test, the current pumps were not able to achieve the estimated 370 gpm flow rate needed, where pump 1 at 196-gpm and pump 2 at 122-gpm pumped a combined 270-gpm.

With respect to the condition issues, Mr. Hobbs sponsored photos of the lift station at Attachment MHH-10R of Petitioner's Exhibit 16 to show the heavily corroded discharge piping without protective coating, control panel structural supports with excessive corrosion, surface deteriorating of concrete, access hatches without secondary safety protection, wetwell exhaust vent located between the sidewalk and road, and a 230-volt control panel in poor condition. With respect to the safety issues, Mr. Hobbs testified there is currently no dedicated access for employees to safely park and maintain the station, and they are currently using an undeveloped lot at the corner of State Road 38/6th and Main Street for wetwell maintenance. Mr. Hobbs explained that if the lot becomes inaccessible in the future, it will require employees to park vehicles and equipment along State Road 38, and this could result in safety issues for employees and traffic flow disruptions for the public.

Regarding Petitioner's cost estimates for the Maple Run Project, Mr. Hobbs testified that Petitioner provided two cost estimates for the lift station project that were prepared at different times, which is why the cost estimates Petitioner provided for the project differ. As to the errors Ms. Willoughby identified, Mr. Hobbs stated that the cost estimates Indiana American provided are just that, estimates. He explained that as costs mature through the implementation process, the estimates will be updated through monthly reforecasting where any potential overestimating of labor in the estimate will be corrected when the actual costs of the project go into rate base. Mr. Hobbs testified the cost estimate issues raised by the OUCC are generally not relevant, because it is the actual costs of the project that will be reflected in rate base.

iv. **<u>Discussion and Findings</u>.** With respect to the 6th Street Project, the OUCC argues the capacity issues at the lift station are the result of I&I in the system, which should be addressed before installing larger equipment. While we agree larger equipment should not be the first solution to I&I, the evidence demonstrates that Indiana American conducted a system wide collection system evaluation that included an assessment of I&I issues. Pet. Ex. 16, Attachment MHH-1R. It shows Indiana American has attempted to address specific I&I issues associated with infrastructure upstream of the 6th Street lift station, but the station is still undersized.

The record also shows that capacity issues are not the only driver of the project, as components of the lift station are in poor condition and the location of the lift station in the public right-of-way poses security and safety concerns to Indiana American's employees and the public. Pet. Ex. 16, Attachment MHH-10R. Petitioner identified several issues related to age and system deterioration that need to be addressed, including piping restrictions and electrical issues. These issues indicate that replacement of the lift station is needed to maintain operation. In addition, while site safety does not appear to be a concern today, the evidence demonstrates that future planned road improvements are likely to create safety and security concerns.

Accordingly, we find that replacement of the 6th Street lift station is necessary to address the capacity, condition, safety, and security concerns identified by Petitioner, and is required for

Indiana American to provide safe, adequate, and reliable service to its customers. For those reasons, we find the 6th Street Project should be approved.

With respect to the Maple Run Project, the OUCC did not take issue with the project itself, but rather raised concerns about the cost estimates Indiana American provided to support the project. While Petitioner's cost estimate is a planning-level estimate, we find such estimate to be sufficient at this time. As Mr. Hobbs explained on rebuttal, it is the actual cost of the project and not the estimates that will be reflected in rate base. For this reason, we find the Maple Run Project should be approved and the amount that should be reflected in rate base for the project is the actual cost of the project upon completion.

e. BT SOP 98-01.

i. INAWC Case-in-Chief. Indiana American sought to include its Business Transformation costs (referred to as "BT SOP 98-01") in rate base in this Cause. As part of its total company rate base, Indiana American proposed to include $7,170,944 of BT SOP 98-01 costs as UPIS, as well as $6,619,332 of accumulated depreciation associated with the BT SOP 98-01 project.

ii. OUCC. Ms. Stull recommended Indiana American's request to include these costs in rate base be denied. She explained that the BT SOP 98-01 costs refers to expenditures associated with implementation of American Water's customized SAP software system. She said SOP 98-01 provides guidance on accounting for the costs of computer software developed or obtained for internal use and requires training and data conversion costs be expensed as incurred.[20] Ms. Stull noted that, in Cause Nos. 44450 and 45142, Indiana American sought to capitalize these costs for ratemaking purposes, which the OUCC opposed but did not object to the recovery of the costs over time through amortization. She noted that in settlements, these costs were excluded from rate base but amortized over 13 years, which has effectively allowed Indiana American a "return of" but not a "return on" the expenditures.

Ms. Stull clarified that the OUCC does not oppose Indiana American's continued ability to earn a return of the expenditures. However, she said Indiana American should not be authorized to earn a return on the expenditures because they are not construction costs used to produce plant that is used and useful in the provision of utility service under Ind. Code § 8-1-2-6. She further testified that Petitioner neither supported why these costs should be included in rate base nor why the treatment of these costs should deviate from prior Commission rate orders for Indiana American.

iii. INAWC Rebuttal. Mr. Shimansky disagreed with Ms. Stull's recommendation that the BT SOP 98-01 costs be disallowed. With respect to Ms. Stull's contention that these costs do not qualify for inclusion in rate base because they are not construction costs under Ind. Code § 8-1-2-6, Mr. Shimansky testified that capital dollars spent do not have to be related to "construction" to be recovered in rate base. He testified that capital dollars, or any asset, represents money spent today that creates a benefit for future periods. He further

[20] SOP is a Statement of Position issued by the American Institute of Certified Public Accountants, which is considered to be a source of generally accepted accounting principles.

testified that Ind. Code § 8-1-2-6 also provides that rate base includes "the cost of bringing property to its then state of efficiency," which is precisely what the BT SOP 98-01 asset represents. Mr. Shimansky explained that the planning, data conversion, training deployment, and stabilization costs invested in the Business Transformation program and recorded as SOP 98-01 assets were critical to bringing the Business Transformation investment to its current state of efficiency. He testified that the OUCC is not opposed to the collection of the BT SOP 98-01 asset, and if the asset is eligible to be collected in rates, it should also be included in rate base.

As for the costs not being included in rate base in prior rate cases, Mr. Shimansky testified the treatment of the BT SOP 98-01 costs in Indiana American's prior rate case was pursuant to a settlement and for the purpose of reaching a resolution in that case. Mr. Shimansky explained Petitioner did not agree to remove it permanently from rate base nor did it agree not to include it in the rate calculations in its next rate case.

iv. <u>Discussion and Findings</u>. In Cause No. 44059, Indiana American sought approval of expenditures for the design, development, and implementation of its Business Transformation program, which was to replace and upgrade its information technology systems. In that Cause, the Commission approved an agreement by the parties that Indiana American could defer for future recovery the estimated $6,800,000 of associated costs and that the deferred costs should be amortized over ten years. In a settlement approved by the Commission in Cause No. 44450, the parties agreed that all BT SOP 98-01-related assets should be depreciated, or amortized, over 13 years rather than the ten years approved in Cause No. 44059.

As an initial matter, we agree with the OUCC that given Petitioner's decision to request authorization to include the BT SOP 98-01 costs in its base rates after such costs were previously excluded, Indiana American should have included a discussion to support the reasonableness of its request in its case-in-chief. Nonetheless, we find the evidence supports including these costs in rate base.

We recently addressed the inclusion of these types of software costs in rate base in *Aqua Indiana, Inc.*, Cause No. 45675 (IURC Jan. 18, 2023). There, the utility sought preapproval of design, implementation, and development costs associated with improvements to its information technology systems and software under Ind. Code § 8-1-2-23. The OUCC argued that the software costs were not appropriate for pre-approval under Ind. Code § 8-1-2-23 because they did not qualify as an extension, construction, addition or improvement to plant and equipment. *Id.* at 9. The OUCC also argued that these costs, which generally accepted accounting principles ("GAAP") require to be expensed, should not be capitalized in rate base because they did not result in utility assets. *Id.* at 5-6. We disagreed and found that the software qualified for pre-approval and authorized the costs to be included in rate base.

We are dealing with the same type of costs here. These deferred expenses are linked to software and associated with an asset includable in utility plant. Therefore, the unamortized balance of the deferred costs can be included in rate base. Whether the costs received preapproval under Ind. Code § 8-1-2-23 does not affect, or alter, the manner in which such costs are treated for ratemaking purposes. We also disagree with the OUCC's argument that the treatment of these costs in the 2019 Rate Order should dictate how these costs are treated in this Cause. As Mr.

Shimansky explained on rebuttal, the agreement to exclude these costs from rate base in Cause No. 45142 was done for purposes of reaching a settlement. Nothing in the settlement reflects Petitioner's agreement that these costs should be excluded from rate base.

Accordingly, we find that the BT SOP 98-01 cost Petitioner proposes to include in rate base in this Cause is eligible to earn a return on as part of its rate base. As such, we find these costs were appropriately included in rate base in this Cause and should be approved.

f. Acquisition Related Costs.

i. OUCC. Ms. Stull noted that INAWC has been authorized to include in its rate base legal fees incurred by the utility related to its acquisition of water and wastewater utilities. She expressed concern with Indiana American's practice of embedding into rate base legal expenses based on fixed fee agreements. Ms. Stull explained in Cause No. 45461, the Commission found that such fees could properly be included in rate base pursuant to Ind. Code ch. 8-1-30.3, but that such expenses must be reasonable and the appropriate time to challenge the reasonableness of such costs was in the utility's next rate case. She noted the Commission also expressed an expectation that, in the future, Indiana American should provide a more accurate and detailed estimate of incidental expenses and other costs of acquisition. Ms. Stull noted the Commission made similar findings in Cause No. 45550 involving Petitioner's acquisition of the Town of Lowell's system.

Ms. Stull raised concern that Indiana American is not adequately incented to control its acquisition costs because it is permitted to include its legal expense in rate base, where it will earn a return as if it is an investment. She noted that acquisition cases have become less controversial and involved and argued that Indiana American's fixed fee arrangements present a significantly large expense for a simple case (*e.g.*, $120,000 for the Claypool case) but does not afford protection for the ratepayer in the case of protracted acquisition cases.

Ms. Stull suggested Indiana American is not monitoring these fixed fee arrangements to determine if they are a good deal for customers. She recommended that Indiana American be required to present support for the reasonableness of legal costs with the case-in-chief testimony in its rate case and keep track of the hours spent by outside counsel for evaluation. She did not, however, propose any adjustment in this case to Petitioner's rate base.

ii. INAWC Rebuttal. Mr. Shimansky responded to Ms. Stull's concerns by stating that "hours" are not the only factor in considering the value of legal representation. He testified that Indiana American's lawyers have actively negotiated and revised the "fixed" fees to match the reasonable reality of a case. He gave the example of the fixed fee for the Claypool acquisition which, as Petitioner told the OUCC in discovery, was reduced at the request of general counsel for Indiana American after it became apparent that the OUCC was not going to engage in the more litigious approach it has taken in other acquisition cases. He testified this disproves Ms. Stull's theory that Indiana American has no incentive to monitor the fees in relation to the level of work required.

iii. Discussion and Findings. Through our prior acquisition orders, we have made it clear that the reasonableness of legal expense incurred by

Petitioner in acquisition cases under Ind. Code ch. 8-1-30.3 is an issue to be addressed in Petitioner's next rate case. *See e.g., Indiana-American Water Co., Inc. and Wastewater One, LLC*, Cause No. 45461, at 13, (IURC June 2, 2021). As the party seeking cost recovery of such expenses, Indiana American bears the burden of demonstrating the reasonableness of such costs.

While the OUCC expressed concern with Petitioner's use of fixed fee arrangements for legal fees and the lack of information provided by Petitioner that would allow it to easily determine whether such arrangements would produce lower outside counsel fees, the OUCC did not offer any evidence disputing the reasonableness of the legal expenses requested by Petitioner or request that we disallow any expense. Rather, the evidence of record reflects that INAWC takes steps, even after executing fixed fee arrangements with outside counsel, to monitor and mitigate legal fees incurred in connection with INAWC's acquisitions. Pet. Ex. 15 at 37-38.

We do, however, agree that Indiana American could have provided testimony or other evidence in its case-in-chief to support the reasonableness of its legal expenses. While the OUCC urges us to order Petitioner to require its outside counsel to documents its hours when using a fixed fee arrangement, we decline to do so. As we have encouraged Indiana American to provide more detailed estimates of its expenses and costs of acquisition in its case-in-chief filings under Ind. Code ch. 8-1-30.3, we encourage Indiana American to provide additional detail in its base rate case-in-chief filings concerning the reasonableness of its acquisition legal expenses for which it seeks recovery, including an explanation for why its chosen legal fee arrangement was appropriate and resulted in reasonable costs and the reason(s) any expenses were not within the range of estimated costs identified in the acquisition case.

Accordingly, we accept the amount of legal expense Petitioner has proposed for each of its acquisitions that are to be included in rate base in this case.

B. <u>Quantification of Original Cost Rate Base</u>. Based upon our findings above, we find that Petitioner's net original cost rate base projected as of Step 1 is as follows:

Utility Plant:	Total Company	Water	Wastewater
Plant in service	$2,491,462,490	$ 2,470,774,861	$ 20,687,629
BT SOP 98-01	7,170,944	7,119,313	51,631
Deferred depreciation	8,311,140	8,277,794	33,346
Post-in-service AFUDC	7,137,440	7,123,318	14,122
Total Utility Plant	2,514,082,014	2,493,295,286	20,786,728
Accumulated Depreciation:			
Plant in service	618,690,066	616,302,719	2,387,347
BT SOP 98-01	5,364,418	5,325,794	38,624
Deferred depreciation	4,791,904	4,770,447	21,457
Post-in-service AFUDC	4,206,403	4,197,650	8,754
Total Accum. Depreciation	633,052,791	630,596,610	2,456,182
Net Utility Plant	1,881,029,223	1,862,698,676	18,330,546
Deductions:			
Contributions in aid of construction	210,713,116	210,528,039	185,076
Customer advances for construction	62,267,845	61,809,736	458,109
Capacity Adjustment - Somerset	309,000	182,091	126,909
Total Deductions:	273,289,961	272,519,866	770,094
Additions:			
Acquisition Adjustment (net)	8,524	-	8,524
SEI Deferred Depr, Property Taxes & PISCC	4,364,489	4,364,489	-
	2,241,938	2,227,653	14,285
Total Additions:	6,614,951	6,592,142	22,809
Total Rate Base	$ 1,614,354,213	$ 1,596,770,952	$ 17,583,261

We further find, for purposes of Step 2 rates, that Petitioner's net original cost rate base forecasted as of April 30, 2024 (the beginning of the test year) to be $1,679,732,875 as follows:

Utility Plant:	Total Company	Water	Wastewater
Plant in service	$2,602,876,784	$ 2,579,745,204	$ 23,131,580
BT SOP 98-01	7,170,944	7,119,313	51,631
Deferred depreciation	8,311,140	8,277,794	33,346
Post-in-service AFUDC	7,137,440	7,123,318	14,122
Total Utility Plant:	2,625,496,308	2,602,265,629	23,230,679
Accumulated Depreciation:			
Plant in service	655,519,019	652,533,660	2,985,359
BT SOP 98-01	5,902,238	5,859,742	42,496
Deferred depreciation	5,103,400	5,080,176	23,224
Post-in-service AFUDC	4,378,467	4,369,116	9,351
Total Accum. Depreciation	670,903,124	667,842,694	3,060,430
Net Utility Plant:	1,954,593,184	1,934,422,935	20,170,249
Deductions:			
Contributions in aid of construction	211,940,701	211,759,216	181,485
Customer advances for construction	69,151,383	68,693,274	458,109
Capacity Adjustment - Somerset	305,305	181,380	123,925
Total Deductions:	281,397,389	280,633,870	763,519
Additions:			
Acquisition Adjustment (net)	7,757	-	7,757
SEI Deferred Depr, Property Taxes & PISCC	4,287,385	4,287,385	-
	2,241,938	2,227,653	14,285
Total Additions:	6,537,080	6,515,038	22,042
Total Rate Base	$ 1,679,732,875	$ 1,660,304,103	$ 19,428,772

As explained herein, Step 3 rates will be based upon the actual utility plant in service as of that date, provided that the April 30, 2025 net original cost rate base we have found as shown below shall serve as a cap on the total net original cost rate base throughout all steps.

Utility Plant:	Total Company	Water	Wastewater
Plant in service	$ 2,827,527,524	$ 2,802,385,362	$ 25,142,162
BT SOP 98-01	7,170,944	7,119,313	51,631
Deferred depreciation	8,311,140	8,277,794	33,346
Post-in-service AFUDC	7,137,440	7,123,318	14,122
Total Utility Plant:	2,850,147,048	2,824,905,787	25,241,261
Accumulated Depreciation:			
Plant in service	711,792,718	707,859,896	3,932,822
BT SOP 98-01	6,619,332	6,571,673	47,659
Deferred depreciation	5,515,957	5,490,377	25,580
Post-in-service AFUDC	4,600,670	4,590,524	10,147
Total Accum. Depreciation	728,528,677	724,512,470	4,016,208
Net Utility Plant:	2,121,618,371	2,100,393,317	21,225,053
Deductions:			
Contributions in aid of construction	213,576,985	213,400,179	176,805
Customer advances for construction	78,573,679	78,115,570	458,109
Capacity Adjustment - Somerset	313,011	194,631	118,380
Total Deductions:	292,463,675	291,710,380	753,294
Additions:			
Acquisition Adjustment (net)	6,734	-	6,734
SEI Deferred Depr, Property Taxes & PISCC	4,150,345	4,150,346	-
	2,241,938	2,227,653	14,285
Total Additions:	6,399,017	6,377,999	21,019
Total Rate Base	$ 1,835,553,713	$ 1,815,060,936	$ 20,492,778

C. **Fair Value of INAWC's Rate Base.**

1. INAWC Case-in-Chief. Ms. Bulkley performed an analysis to estimate the fair value of INAWC's rate base. She testified that the methodology that she relied on is generally consistent with the methodology that has been used by the Commission to establish the fair value of INAWC's assets in prior rate proceedings. This methodology begins with the fair value rate base that was established in the last rate proceeding. The historical fair value rate base is trended to current dollars using an inflation index, CPI-U, to establish the current value of the fair value rate base from the prior case. She stated that because INAWC's last general rate case resulted in a settlement that did not specify a fair value rate base, she relied on the fair value rate base that was estimated as of the conclusion of the test year in Cause No. 44450 of $1,222,819,707. She then escalated the fair value rate base from January 28, 2015 (the end of the test year in Cause No. 44450) to the end of each of the projected periods in this case, using the average inflation factor for the period from January 2015 through the end of each of the periods proposed by Petitioner to be utilized as rate base cutoffs for the three-step implementation of rates in this Cause. Ms. Bulkley noted that this methodology is consistent with the methodology that was relied upon in Cause No. 44022, the most recent fair value determination made by the Commission for

Petitioner.

The net investor supplied additions used in Ms. Bulkley's fair value analysis are the difference between the original cost rate base in Cause No. 44450 and the pro forma net investor supplied additions through the periods ending July 31, 2023, April 30, 2024, and April 30, 2025. Her resulting fair value rate base was $2,372,363,444 at July 31, 2023, $2,474,101,830 at April 30, 2024, and $2,667,265,966 at April 30, 2025. Ms. Bulkley compared the fair value rate base for each of the periods to a reproduction cost new less depreciation study that was prepared by Petitioner using the Handy-Whitman Index and included in her workpapers. After comparison, Ms. Bulkley concluded the methodology previously used continues to be a reasonable method for determining fair value.

Ms. Bulkley then calculated the return on the fair value rate base using the same approaches that were applied in Cause No. 44022. Each of these approaches makes an adjustment to the WACC to remove inflation from the fair value rate base where inflation has been applied. She walked through the methodologies and results of each. She clarified that the first component of the fair value rate base is the value as estimated in Cause No. 44450, which is escalated by inflation. The second component is net investor supplied capital since the last rate proceeding, which does not include inflation. The fair value increment is determined by comparing the operating income from the fair value rate base to the operating income derived by applying the original cost return to the original cost rate base for each period, ending July 31, 2023, April 30, 2024 and April 30, 2025. This resulted in a fair value increment of $33,861,953 at July 31, 2023, $35,673,678 at April 30, 2024 and $38,990,129 at April 30, 2025. Pet. Ex. 7 at 63 and Attachment AEB-10.

Ms. Bulkley explained that while each of the methodologies is a reasonable approach to estimating the fair value operating income, Petitioner is not proposing to rely on the fair value increment that results from the methodologies described above. Rather, Petitioner proposes to include only the return on the Indiana Cities Acquisition Adjustment that has been authorized by the Commission in other proceedings through informed fair value ratemaking. Below is the resulting Return on Indiana Cities Acquisition Adjustment presented by Ms. Bulkley:

Return on Indiana Cities Acquisition Adjustment

Date	Indiana Cities Acquisition Adjustment	Return on Indiana Cities Acquisition Adjustment
July 31, 2023	$4,713,294	$319,090
April 30, 2024	$4,362,716	$294,483
April 30, 2025	$3,895,280	$267,995

2. <u>Industrial Group</u>. Mr. Gorman testified that the fair value increment as proposed by Ms. Bulkley is not appropriate and inflates the compensation provided to the utility above a fair and reasonable level. He stated her fair value increment proposal is severely flawed and he recommends it be rejected and not relied upon by the Commission for any purpose in setting rates in this proceeding. As an example, he noted the starting point for her fair value rate base was the estimate provided in Cause No. 44450, which was never approved as reasonable by the Commission, and therefore, is not a reasonable de facto estimate of Petitioner's fair value rate base.

3. INAWC Rebuttal. In response to Mr. Gorman's concerns with her calculation of the fair value increment, Ms. Bulkley testified that the basis of her analysis was not the findings from the settled case. Instead, her estimate of the fair value rate base builds on what Petitioner presented in its evidence in the settled case, which is based on the last fair value finding from a litigated case. Moreover, Ms. Bulkley pointed out that the methodology she relied on in developing the fair value rate base has been relied on by the Commission in several prior cases. Ms. Bulkley explained that in these cases, the Commission methodology begins with the fair value rate base from Petitioner's last fair value finding in a rate case and trends the rate base using a cost inflation index. The Commission then adds net plant additions to determine the updated fair value of the plant. She reiterated that Petitioner is proposing to recover the return on the acquisition adjustment for the Indiana Cities acquisition, not the fair value increment on the entire rate base.

4. Discussion and Findings. Although Indiana-American appears to request that we make a finding of the fair value of Petitioner's rate base, Ms. Bulkley testified that Petitioner is not asking the Commission to rely on, or otherwise use, the fair value of its rate base as calculated through her fair value methodology for any ratemaking purpose except for the calculation of a specific fair value increment to the return on the Indiana Cities Acquisition Adjustment. Pet. Ex. 7 at 64. No party objected to the inclusion of an adjustment for the Indiana Cities acquisition, and as discussed below, when calculating a fair rate of return for INAWC, we will reflect that specific adjustment.

In addition, rather than rely on Ms. Bulkley's calculation of the fair value of its rate base to serve as the statutory "fair value" of its rate base under Ind. Code § 8-1-2-6 for ratemaking purposes, Petitioner proposed the use of its net original cost rate base as of the close of its test year to calculate its fair rate of return. No party objected to the use of net original cost as the basis for a fair value finding. Accordingly, we find a determination of the fair value of Petitioner's rate base to be unnecessary and conclude that Petitioner's net original cost of its rate base, adjusted by our other findings contained in this Order, is the appropriate and proper statutory fair value of its used and useful plant and equipment. Based on our findings herein, we find the resulting return on Indiana Cities Acquisition Adjustment as follows:

Date		Indiana Cities Acquisition Adjustment		Return on Indiana Cities Acquisition Adjustment
July 31, 2023		$4,713,294		$319,090
April 30, 2024		$4,401,669		$297,113
April 30, 2025		$3,934,233		$270,675

8. Fair Rate of Return.

A. ROE.

1. INAWC Case-in-Chief. Ms. Bulkley supported Petitioner's proposed ROE and testified in support of INAWC's projected capital structure. She recommended an ROE of 10.60% as reasonable and appropriate for this proceeding.

In determining her recommended ROE, Ms. Bulkley first developed a proxy group of utility companies that face similar risk as INAWC. To that proxy group, she applied the Constant Growth Form of the Discounted Cash Flow ("DCF") model, the Capital Asset Pricing Model ("CAPM"), and the Empirical Capital Asset Pricing Model ("ECAPM"). Her recommended ROE also takes into consideration the following factors: (1) INAWC's capital expenditure program relative to the proxy group companies; (2) the test year convention mechanism used to set rates for INAWC; (3) the risk associated with variations in volume/demand and the resulting effect on INAWC's revenues and cash flows; and (4) INAWC's proposed capital structure as compared to the capital structures of the proxy group companies. She stated that while she did not make specific adjustments to her recommended ROE for these factors, she did consider them in the aggregate when determining where her recommended ROE falls within the range of the analytical results.

Ms. Bulkley testified that she considered the following key factors in her cost of equity analyses and recommended ROE: (1) the standards established by the U.S. Supreme Court's *Hope* and *Bluefield* decisions for determining a fair and reasonable authorized ROE for public utilities; (2) the effect of current and prospective capital market conditions on the cost of equity estimation models and on investors' return requirements; (3) the results of several analytical approaches that provide estimates of Petitioner's cost of equity; and (4) Petitioner's regulatory, business, and financial risks relative to the proxy group of comparable companies in determining where Petitioner's ROE should fall within the reasonable range of analytical results to appropriately account for any residual differences in risk.

Ms. Bulkley presented the results of her Constant Growth DCF, CAPM and ECAPM analyses, ultimately leading to a range from 10.00% to 11.00% as reasonable.

Ms. Bulkley explained that utilities compete directly for capital with other investments of similar risk, which include other water, natural gas, and electric utilities. Therefore, the ROE authorized for a utility sends an important signal to investors regarding whether there is regulatory support for financial integrity, dividends, growth, and fair compensation for business and financial risk. She testified that the regulatory framework is one of the most important factors in debt and equity investors' assessments of risk and that credit rating agencies consider the authorized ROE and equity ratio for regulated utilities to be important for two reasons: (1) they help determine the cash flows and credit metrics of the regulated utility; and (2) they provide an indication of the degree of regulatory support for credit quality in the jurisdiction. She stated not only do credit ratings affect the overall cost of borrowing, they also act as a signal to equity investors about the risk of investing in the equity of a company. She testified that providing the opportunity to earn a market-based cost of capital supports the financial integrity of Petitioner, which is in the interest of both customers and shareholders.

Ms. Bulkley walked through the effect current and prospective market conditions have on the cost of equity for Petitioner, stating that the combination of persistently high inflation, and the Federal Reserve's changes in monetary policy contribute to an expectation of increased market risk, and an increase in the cost of the investor-required ROE. She explained that because the share prices of utilities are inversely correlated to interest rates, and government bond yields are already substantially greater than utility stock dividend yields, the share prices of utilities will likely decline, which is the reason a number of equity analysts have classified the utility sector as either underperforming or underweight. She said the expected underperformance of utilities means that DCF models using recent historical data likely underestimate investors' required return over the period that rates will be in effect. In addition, Ms. Bulkley testified that prospective market conditions warrant consideration of forward-looking cost of equity estimation models such as the CAPM and ECAPM, which may better reflect expected market conditions.

Ms. Bulkley described her process of selecting a group of proxy companies to estimate the cost of equity for INAWC. She then walked through her use of the Constant Growth DCF model, the CAPM, and the ECAPM methods for estimating the cost of equity. The mean and median DCF results using the average growth rates ranged from 9.65% to 9.97%, and the mean and median results using the maximum growth rates ranged from 10.76% to 11.04%. Her traditional CAPM analyses produced a range of returns from 10.19% to 10.88% and her ECAPM analysis results ranged from 10.77% to 11.29%. Ms. Bulkley performed a flotation cost calculation and used it to identify a recommended ROE within the range of ROE estimates from her various models. Ms. Bulkley also explained that from a credit perspective, the additional pressure on cash flows associated with high levels of capital expenditures exerts corresponding pressure on credit metrics and, therefore, credit ratings. She noted that Petitioner's capital expenditure requirements as a percentage of net utility plant are significant and will continue over the next few years. Additionally, similar to a number of the operating subsidiaries of the proxy group, Ms. Bulkley noted that INAWC does have a capital tracking mechanism to recover some of Petitioner's projected capital expenditures.

2. <u>OUCC and Intervenors</u>. OUCC witness Dellinger recommended an ROE of 9.00%. He derived this recommendation from an analysis of the Constant Growth DCF model, the Two-Stage DCF model, the CAPM and the ECAPM. Mr. Dellinger discussed his approach to these models and how they differed from Ms. Bulkley's approach. As to the appropriate proxy group, Mr. Dellinger explained why he included some additional companies and excluded others from those used by Ms. Bulkley.

Mr. Dellinger described the DCF model, his results, and how his results compared with Ms. Bulkley's results. His Constant Growth DCF analysis produced a 9.0% ROE for the mean calculation and a 9.32% ROE for the median. Mr. Dellinger discussed how the limitations and weaknesses of the Constant Growth DCF model are addressed by using a two-stage model. His Two-Stage DCF model resulted in a 7.61% ROE for the Mean calculation and an 7.16% ROE for the median calculation.

Mr. Dellinger described the CAPM, his preferred metric for interest rates (the 7-day yield of the 30-year treasury), and the calculation of Beta. He also discussed the equity risk premium component and the issues with Ms. Bulkley's calculation. He also discussed a logical inconsistency in Ms. Bulkley's DCF used for her CAPM due to a mismatch between the inputs Ms. Bulkley's used in her model. Mr. Dellinger ultimately recommended a CAPM ROE of 7.39% calculated on the Mean and 7.38% calculated on the Median. He also ran an ECAPM, which then resulted in an ROE of 7.59% calculated on the Mean and 7.54% calculated on the Median. He did not recommend reliance on the ECAPM, because he did not believe it to be a compelling model.

Mr. Dellinger explained why his results, which were lower than those of Ms. Bulkley, were appropriate and reasonable. He discussed the historic spread between U.S. Treasury rates and Indiana American's awarded ROEs over time. Mr. Dellinger testified that flotation costs should not be reflected in a higher cost of equity, as investors adjust a stock's market price to account for the fact that a portion of the proceeds they pay for shares does not go to Petitioner issuing equity.

Industrial Group witness Gorman recommended an ROE of 9.10%, which was 30 basis points less than the midpoint of his recommended range to "offset some of the excessive cost to ratepayers created by INAWC's unreasonable equity-thick ratemaking capital structure and mitigate, in part, its cost of service increase and related adjustment to tariff rate charges" in the proceeding. IG Ex. 1 at 5. Mr. Gorman also recommended that the Commission not adjust the ROE for the recovery of flotation costs because it is not based on the recovery of reasonable flotation expenses for Petitioner.

Mr. Gorman reviewed market evidence concerning how regulatory decisions and authorized returns on equity for regulated utility companies have supported utilities' access to capital, financial integrity, and credit standing. He testified the industry authorized returns on equity for water utilities have ranged from 9.04% to 9.76% for the period of 2014-2022. He also noted that in the only rate case for a water utility to date in 2023 that identified an equity return, the approved return on equity was 8.70%. Based on these authorized ROEs, he said credit rating agencies have rated the credit standing of regulated utilities as "stable" and the credit quality of the industry has increased over the last few years.

Mr. Gorman also testified regarding the investment risk of INAWC and its proposed capital structure. He explained that INAWC's capital structure has a far greater common equity ratio in comparison to authorized rate-setting capital structures allowed for electric, natural gas, and water utilities over the last several years. He testified that INAWC's equity thick capital structure has the effect of increasing charges to customers, relative to the industry average ratemaking capital structure, with a revenue impact that is comparable to a 120 basis point differential in the return on equity. Mr. Gorman's recommended ROE represents a movement of a little over half of this 120 basis point difference from the high end of his recommended range of 9.0% to 9.8%.

Mr. Gorman explained the methods he used to estimate INAWC's cost of common equity including several variations of the DCF model, the risk premium model, and the CAPM and the inputs he used in applying these models. His DCF recommendation was 9.00%. His CAPM analysis resulted in 10.10% and his Risk Premium analysis resulted in 9.55%.

Crown Point witness Guerrettaz did not perform any quantitative analyses regarding the cost of equity for Petitioner. Mr. Guerrettaz instead estimated that a reasonable authorized ROE for Petitioner is 9.00% based on his understanding of the financial markets and Petitioner's business characteristics. He testified that Petitioner has extremely low business risk because it: (1) sells an essential service, (2) enjoys traditional rate regulated revenue pricing without competition, and (3) grows rate base, revenues, and profits through utility acquisitions and risk-reducing tracking mechanisms. Mr. Guerrettaz stated that the business risk of Petitioner and its parent company is nominal based on stock prices and dividend growth.

CAC witness Inskeep recommended the Commission reject Petitioner's proposed ROE to mitigate the rate impact of an "extraordinary utility unaffordability crisis." CAC Ex. 1 at 36. He noted the Commission has approved ROEs for Indiana American of 9.70% (Cause No. 44022), 9.75% (Cause No. 44450), and 9.80% (Cause No. 45142) as compared to Indiana American's proposal in this case of 10.6%. He stated that customers do not derive a tangible benefit from an increased ROE, rather a higher ROE reflects a higher profit margin for Indiana American's shareholders at the cost of higher rates for its customers.

3. <u>INAWC Rebuttal</u>. Responding to the issues raised by the OUCC and Intervenors, Ms. Bulkley testified the primary factors that should be considered are: (i) the importance of investors' actual return requirements and the critical role of judgment in selecting the appropriate ROE; (ii) the importance of providing a return that is comparable to returns on alternative investments with commensurate risk; and (iii) the need for a return that supports a utility's ability to attract needed capital at reasonable terms. She also considered the effect of current and expected capital market conditions on these factors.

Ms. Bulkley asserted that the OUCC and Industrial Group ROE are inconsistent with recent changes in market conditions and do not reflect the current cost of equity. She noted that interest rates have increased since Petitioner's last rate proceeding, and authorized ROEs have increased from 2021 through 2023, which demonstrates that borrowing costs and the cost of equity have increased. She testified that Mr. Gorman's and Mr. Dellinger's proposals that the Commission reduce Petitioner's currently authorized ROE are directionally inconsistent with market conditions and the investor required ROE. She stated that a comparison of Mr. Gorman's ROE recommendations in various rate proceedings in Indiana since 2019 demonstrates that his recommended ROE in this proceeding is inconsistent with the increase in the cost of equity reflected in his model results and that his proposed risk adjustment reduction to the ROE of 30 basis points is arbitrary and asymmetric given his past testimony.

Ms. Bulkley testified that making reasonable adjustments to the OUCC's cost of equity analyses of Mr. Dellinger results in a range of returns from 9.53% to 10.82%, which demonstrates that Petitioner's requested ROE is reasonable and appropriate. She disagreed with the composition of his proposed proxy group and the application of his constant growth DCF model. Ms. Bulkley also explained her disagreement with Mr. Dellinger's criticisms of her DCF, CAPM and ECAPM analyses.

Ms. Bulkley testified that while Mr. Gorman states that he relies on the midpoint of his DCF results, as well as the midpoint of the results of all his cost of equity analyses as his overall ROE recommendation, he incorrectly states the midpoint of his DCF results and the results of his overall cost of equity analyses. She said simply correcting these two errors produces a midpoint ROE of 9.60% instead of the 9.40% stated in Mr. Gorman's testimony.

When Mr. Gorman's risk premium analysis is adjusted to reflect the inverse relationship between interest rates and the equity risk premium, Ms. Bulkley showed the cost of equity is 10.86%. She stated this change increases Mr. Gorman's cost of equity range of 9.10% to 10.86%. Thus, the midpoint, which is the central tendency that forms the basis for Mr. Gorman's market cost of equity recommendation, would be 9.98%.

Ms. Bulkley defended her use of flotation costs by stating that such costs, just like rate base investments, are part of the invested costs of the utility, and the need to reimburse shareholders for the lost returns associated with equity issuance costs has been recognized by the academic and financial communities. Ms. Bulkley did not address Mr. Guerrettaz's and Mr. Inskeep's ROE recommendations other than to recommend they be dismissed summarily because neither provided an independent analysis.

4. **Discussion and Findings.** In setting the rate of return, the Commission's decision must be framed by *Bluefield Waterworks & Improvements Co. v. Pub. Serv. Comm'n*, 262 U.S. 679, 43 S.Ct. 675 (1923) and *Fed. Power Comm'n v. Hope Natural Gas, Co.*, 320 U.S. 591, 64 S.Ct. 281 (1944).[21] The general standards these cases established require a cost of common equity set by the Commission to be sufficient to establish a rate of return that will maintain the utility's financial integrity, attract capital under reasonable terms, and be commensurate with the returns of other businesses of comparable risk.

The Commission is also mindful that "the cost of common equity cannot be precisely calculated and estimating it requires the use of judgment." *Indiana-American Water Co.*, Cause No. 44022, at 35 (June 6, 2012). Due to this lack of precision, the use of multiple methods is desirable, in part, because no one method will produce reasonable results under all conditions and in all circumstances. The Commission is also mindful of the strengths and weaknesses of the various models typically used to estimate a utility's cost of common equity, and we find that with appropriate and reasonable inputs, models such as the DCF and other methods can produce reasonable estimates of a utility's cost of common equity. Consistent with the standards in *Hope* and *Bluefield*, as well as under Indiana law, INAWC's authorized return on equity should be reasonable given the totality of the circumstances.

The parties proposed various returns using the DCF model and other methods as bases for their positions. Ms. Bulkley's analysis of INAWC's cost of equity produced a range of 10.00% to 11.00% with the recommendation that the Commission adopt an ROE of 10.60%. The OUCC's analysis produced a range of 7.16% to 9.32% with a recommended ROE of 9.00%. Mr. Gorman's analysis for the Industrial Group produced a range of 9.00% to 9.80% with a recommended ROE of 9.10%, adjusted downward 0.30% from 9.40% due to Petitioner's capital structure. Accordingly, the overall recommendations provided by the witnesses would place the approved return on equity between 9.0% to 10.6%.

In addition to the recommendations of these experts and while not determinative of the ROE in this case, we note the ROE awarded Indiana's vertically-integrated electric utilities outside of settled cases has been trending lower over time. *See, e.g.,* Indiana Michigan Power Company, 10.2% in Cause No. 44075 (2013); Indianapolis Power and Light Company, 9.85% in Cause No. 44576 (2016); Northern Indiana Public Service Company LLC, 9.75% in Cause No. 45159 (2019); Indiana Michigan Power Company, 9.70% in Cause No. 45235 (2020); and Duke Energy Indiana, LLC, 9.70% in Cause No. 45253 (2020). We also note that Petitioner's current ROE of 9.80% was approved in 2019 pursuant to a settlement reached in Cause No. 45142. While we find the overall

[21] *See also, Indianapolis Power & Light Co.*, Cause No. 44576 at.41 (IURC March 16, 2016).

downward trend instructive, we also recognize the change in general economic factors, like the increase in interest rates, since these orders were issued.

Our determination should also appropriately consider Petitioner's specific risk characteristics, such as the mitigation of risk associated with Petitioner's use of regulatory mechanisms, including a forecasted test year in this proceeding and the trackers approved for INAWC. In addition to the DSIC and SEI trackers, the Commission also approved in Cause No. 45043, a lead service line replacement program under Ind. Code ch. 8-1-31.6. The effect of these tracking mechanisms is to reduce the uncertainty of the earnings that an investor can expect. *See Ind. Mich. Power Co.,* Cause No. 44075 at 42-43 (IURC Feb. 13, 2013). Moreover, in this case, INAWC is adding two major projects into rate base, along with substantial costs associated with its acquisition of Lake Station, which removes even more risk from Petitioner.

Having taken into consideration the observable market data reflected in the record, and a general assessment of the investment risk characteristics of the water and wastewater utility industry, combined with a thorough understanding of the Indiana jurisdiction and its risk mitigation ratemaking mechanisms, and INAWC in particular, and the expert witness recommended range identified above, the Commission finds a reasonable range for Petitioner's ROE is 9.3% to 9.9%. The resulting midpoint of this range is 9.60%. Taking into consideration all the evidence presented and based on the rising capital cost environment, the Commission finds that an ROE of 9.65% would represent a fair and reasonable rate.

B. <u>Cost of Debt</u>. Petitioner's projected cost of long-term debt as of July 31, 2023 is 4.73%, and 4.71% as of April 30, 2024 and as of April 30, 2025 is 4.71%. The computation of these costs is shown on INAWC Financial Exhibit CC, Schedule CC1, Workpaper 2 contained within Petitioner's Exhibit 29. No party disputed these costs.

C. <u>Capital Structure</u>.

1. <u>INAWC Case-in-Chief</u>. Mr. Furia presented Petitioner's projected capital structures as of July 31, 2023, April 30, 2024, and April 30, 2025 to be used for computing Petitioner's WACC at each of the three steps proposed for rate implementation. These dates match the dates used to calculate the proposed rate base for each of Step 1, Step 2, and Step 3. Mr. Furia explained that the revenue requirement for each proposed increase will use Petitioner's actual capital structure as of these dates when rates go into effect. He used Indiana American's actual capital structure as of September 30, 2022 and adjusted the component balances in that capital structure to reflect all changes expected to occur by July 31, 2023, April 30, 2024 and April 30, 2025. He reflected expected long-term debt maturities on January 1, 2024 and May 1, 2024, a common equity infusion that occurred in March of 2023, new long-term debt issuances planned for November 2023 and May 2024, and a common equity infusion planned for May 2024, as adjustments to arrive at the capitalization for the forecasted test year.

The total projected capitalization of Indiana American as of April 30, 2025 is $1,731,127,386, and the overall WACC is 6.88%. This WACC reflected Petitioner's proposed cost of common equity of 10.60%. The total projected capitalization of Indiana American as of April 30, 2024 is $1,545,974,304, and the overall WACC is 6.75%, and also reflects a cost of common equity of 10.60%. The total projected capitalization of Indiana American as of July 31, 2023 as filed in Petitioner's case-in-chief was $1,511,522,316, and the overall WACC was 6.77%, and also reflected a cost of common equity of 10.60%.[22] Mr. Furia described the bases for various components on Schedule CC1, including accumulated depreciation on contributed utility plant for Muncie Sewer, OPEBs, the prepaid pension asset, all included at zero cost. With respect to OPEBs and the prepaid pension asset, because the balance for the relevant time periods represented asset positions, they were included in the capital structure as negative values.

Mr. Furia described adjustments to INAWC's long-term debt balance to reflect: (1) maturity of the 6.990% first mortgage series B on January 1, 2024; (2) maturity of the 2.300% tax-exempt bonds on January 1, 2024; (3) maturity of the 7.110% taxable series general mortgage bonds on May 1, 2024; (4) the new taxable debt issuance in the amount of $23,000,000 planned for November 2023; and (5) the new taxable debt issuance in the amount of $96,658,000 planned for May 2024. He described the new long-term debt Petitioner plans to issue in November 2023 and March 2024. Indiana American's projected cost of long-term debt as of July 31, 2023 was 4.73% and the projected cost of long-term debt as of April 30, 2024 and as of April 30, 2025 is 4.71%. Pet. Ex. 13 and 14, Financial Exhibit CC, Schedule CC1.

Mr. Furia described adjustments to INAWC's common equity component of its capital structure to reflect: (1) a common equity infusion of $53,000,000 on March 15, 2023, (2) a common equity infusion of $73,600,000 planned for May 2024, and (3) changes to the retained earnings balance that are expected to occur between September 30, 2022 and April 30, 2025. He stated these adjustments reflect Petitioner's projections for the 2023-2025 period and are based on Petitioner's projected capital requirements and the need to maintain appropriate capital structure ratios.

INAWC witness Bulkley testified that comparing Petitioner's projected equity ratio as of April 30, 2025 of 56.15% (excluding the adjustments for zero cost capital items) demonstrates that Petitioner's requested equity ratio is within the range of equity ratios for the proxy group. She further stated Petitioner's proposed equity ratio is reasonable considering that credit rating agencies have identified the outlook for the utility sector as "negative" due to the negative effect on the cash flows and credit metrics associated with increasing interest rates, inflation and commodity costs, and the pressure that those factors place on customer affordability and utilities' prompt rate recovery.

2. <u>OUCC and Industrial Group</u>. OUCC witness Dellinger did not disagree with the Petitioner's proposed capital structure for purposes of determining the WACC. However, Mr. Dellinger did testify about how Petitioner's capital structure has changed over time, becoming more weighted toward equity and more expensive for customers and implicating affordability.

He stated that customers benefit from having an optimal capital structure (meaning the lowest reasonable WACC), but gross profitability declines as more debt is included in the capital structure, because in a regulated environment profits come from the return on equity. Mr. Dellinger stated that in the present case, Indiana American's cost of debt is 4.71% and its after-tax cost of

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[22] This was updated in Petitioner's Response to Request No. 2 to the Commission's August 30, 2023 Docket Entry (Pet. Ex. 29) to $1,527,028,439 and an overall WACC of 6.73%.

equity is 14.13%, so the cost of equity is three times the cost of debt. He showed that in each case since 2010, the percentage of equity in the capital structure has increased. Mr. Dellinger also noted that in Petitioner's last financing case (Cause No. 45660), the final order for which was issued less than one year prior to this case, INAWC projected that this ratio would start to decrease. But instead, it has increased again and is now projected to be 56.15%. He testified that if the capital structure had the same equity percentage in this case as it did in 2012 (48.98%), the step 3 annual revenue requirement would be $6.2 million lower.

OUCC witness Ms. Stull recommended adjustments to Petitioner's projected balance of ADIT to account for adjustments she proposed to the amortization of EDIT and the calculation of income tax expense but otherwise accepted Petitioner's proposed capital structure components. She recommended two adjustments that affected the amount of ADIT to be included in Petitioner's capital structure: (1) a reduction to income tax expense to incorporate the repairs deduction for ratemaking purposes and (2) an adjustment to the amortization of EDIT. Ms. Stull explained that because she proposed to include the repairs deduction in the determination of income tax expenses for ratemaking purposes, there would be no difference between book and tax on a going forward basis and, therefore, no additional ADIT (related to the repairs deduction) should be projected for Steps 1, 2, or 3. She further explained that, due to the way Petitioner projected and presented its ADIT balances, the effect on ADIT as a result of this adjustment was not readily transparent. She estimated the effect to ADIT by multiplying the repair deduction by 25% and reducing ADIT accordingly. Ms. Stull's adjustment was a $2,927,966 reduction to ADIT in Step 2 and a $9,439,895 reduction to ADIT in Step 3.

Industrial Group witness Gorman testified that Indiana American's projected capital structure is not reasonable because it imposes excessive cost on its retail customers. He testified that Petitioner's equity ratio is excessive relative to its bond rating, and the capital structure largely attributes credit benefits to support its parent company's bond rating, rather than being structured to support a regulated Indiana utility capital structure. Mr. Gorman acknowledged that the Commission has historically declined to make pro forma adjustments to utilities' capital structures but recommended the Commission consider the excessive cost INAWC imposes through its "equity rich capital structure" in determining a reasonable ROE that reflects Petitioner's actual financial risk to ensure that the overall rate of return and the resulting costs imposed on customers are just and reasonable. He presented a comparison of Petitioner's projected capital structure to those used to set rates in the utility industry, concluding that INAWC's capital structure "has a far greater common equity ratio in comparison to authorized rate-setting capital structures allowed for electric, natural gas and water utilities over the last several years." IG Ex. 1 at 65.

Mr. Gorman also objected to the inclusion of the prepaid pension and OPEB assets in INAWC's capital structure. Mr. Gorman testified that the prepaid pension asset reflects funds provided by customers through rate revenue, which Petitioner has been able to use to offset its actual pension expense. As the prepaid pension asset was funded by collections from customers, rather than shareholder contributions, Indiana American is not entitled to a return of that sum by including the asset in its capital structure or cost of service. He stated Petitioner did not show that the amount of pension expense included in cost of service and recovered in customer rates during the time the prepaid pension asset was accumulated was limited to Petitioner's annual pension expense. Specifically, he presented a table comparing actual pension expense to the amount reflected in rates and testified that, since 2020, there has been an overcollection that has fully compensated for most of the current prepaid pension asset. He proposed a similar adjustment to the OPEB asset included in the capital structure.

3. <u>INAWC Rebuttal</u>. Ms. Bulkley explained that Mr. Gorman's analysis of recent authorized equity ratios for water and natural gas utilities was flawed because he included limited-issue rider cases in his benchmarking analysis, relied on the mean and median authorized equity ratios for water and natural gas utilities in each year since 2013, and incorrectly asserted that Petitioner's projected equity ratio is higher than the maximum authorized equity ratios of the water and natural gas utilities since 2013. She explained that the "maximum" authorized equity ratio that Mr. Gorman reflects in his testimony is the highest average or median result over that time period, not the highest overall authorized equity ratio over that period. She testified that from 2013 through 2023, the range of authorized equity ratios was 42.01% to 60.59%, meaning Petitioner's projected equity ratio of 56.16% is well within the range of the authorized equity ratios for natural gas utilities over this period.

She also explained Mr. Gorman's comparison of Petitioner's projected capital structure to the capital structures of the holding companies in the proxy group is flawed because it is not appropriate to compare the projected equity ratio of Petitioner to the average equity ratio of the proxy group at the holding company level. Additionally, she stated, if the capital structures at the holding company level are considered, the market value of debt and equity must be used to estimate the percentage of debt and equity in the capital structure, not the book value of debt and equity as Mr. Gorman has done. She stated that relying on a cost of equity estimate based on market values but a capital structure based on book values, results in the incorrect conclusion that a return reflecting the financial risk of the market value equity ratio would be sufficient to compensate investors for a much more highly levered capital structure based on book value. She testified that Petitioner's projected ratemaking capital structure of 56.16% is consistent with the actual capital structures of the operating utility subsidiaries of the proxy group of 56.09%.

INAWC witness Farrell responded to Mr. Gorman's recommendation to remove the prepaid pension and OPEB assets from the capital structure for ratemaking purposes. He explained that Petitioner has followed GAAP to record its annual pension costs and cash pension plan contributions, which has resulted in a prepaid pension asset on Petitioner's balance sheet. Mr. Farrell stated that any asset on Petitioner's balance sheet is inherently financed through Petitioner's capital structure until it is recognized as expense on Petitioner's income statement. Mr. Farrell said it is those cash contributions that have resulted in the existence of the prepaid pension asset in the first place and the substantial benefits to customers include lowering pension costs and providing a source of ADIT.

INAWC witness Ciullo presented the ADIT associated with Petitioner's prepaid pension asset and prepaid OPEB asset is $1,687,610 and $1,647,921 respectively. Mr. Farrell testified that the lower pension and OPEB expense and accelerated income tax deductions directly lower costs to customers. He explained that the cash pension plan contributions reduce pension expense. In addition, Mr. Farrell explained that the economic benefit of the tax deductibility of Petitioner's pension plan occurs when Petitioner contributes cash to the plan—not when it books (and reflects in regulatory accounting) its pension expense. As with other circumstances where the timing of tax deductions is different from the timing of book expense (e.g., utility plant depreciation), the financing value of the income tax benefits should accrue to the benefit of customers. He also noted that to the extent that a prepaid pension asset is excluded from the calculation, it would be inequitable to include the ADIT balance related to prepaid pension in rate base because it is a well-known regulatory principle that the inclusion in the capital structure of ADIT should only include ADIT for book-tax differences included elsewhere in the revenue requirement determination.

Mr. Farrell testified that the prepaid pension asset represents the cumulative difference between Indiana American's contributions to the pension trust and cumulative pension expense. He said the entire balance represents investor supplied funding and, as a result, is entitled to a return, which supports Petitioner's position of including the prepaid pension asset as a negative zero cost component of the capital structure. The same is true of the OPEB asset. Mr. Farrell explained that in a situation where the pension or OPEB expense is negative, the "other side of the pension credit entry" is to a prepaid pension asset (or OPEB as the case may be). He said typical reasons for a negative pension expense are expected return on plan assets in excess of other components of pension cost and positive plan experience (e.g., lower than expected health care cost increases or participation rates). He pointed out that Petitioner cannot access these pension assets because employers are not permitted to access funds from an ongoing pension or OPEB plan other than for the payment of benefits under that plan.

Mr. Shimansky responded to Mr. Gorman's comparison of actual pension expense to the amount used to set the revenue requirement for calculating rates. He testified that, absent deferred accounting, Mr. Gorman's attempt to compare pension expense in later years to pension expense included in the revenue requirement to deny proper recovery of costs in a rate case would be prohibited retroactive ratemaking. Further, he noted that customers pay rates and have no claim to variances between the level of expense in rates and actual expenses in later years. Finally, he presented analyses showing that throughout the period of Mr. Gorman's analysis, Indiana American had not earned its authorized rate of return.

4. <u>Discussion and Findings</u>. Addressing Mr. Gorman's Prepaid Pension and OPEB asset position first, the inclusion of a prepaid pension asset in either the utility's rate base or capital structure has been previously addressed in other Indiana utility rate cases. For example, in *Indiana Michigan Power Co.*, Cause No. 44075 at 10 (IURC Feb. 13, 2023), we found that:

> [T]he record reflects that the prepaid pension asset was recorded on the Company's books in accordance with governing accounting standards. The record also reflects that the prepaid pension asset has reduced the pension cost reflected in the revenue requirement in this case and preserves the integrity of the pension fund. Petitioner made a discretionary management decision to make use of available cash to secure its pension funds and reduce the liquidity risk of future payments. In addition, the prepayment benefits ratepayers by reducing total pension costs in the Company's revenue requirement. Therefore, we find that the prepaid pension asset should be included in Petitioner's rate base.

These findings were upheld on appeal. *Ind. Office of Util. Consumer Counselor v. Ind. Mich. Power Co.*, 7 N.E.3d 1025 (Ind. Ct. App. 2014) (transfer denied); *see also Duke Energy Indiana, LLC*, Cause No. 45253 at 26-27 (IURC June 29, 2020). For OPEBs, this treatment has been confirmed for more than thirty years. *Ind. Bell Tel. Co., Inc., et al*, Cause No. 39348 (IURC Dec. 30, 1992).

Petitioner has demonstrated a projected prepaid pension asset of $10,463,716 and an OPEB asset of $11,254,406 in Step 3, and the prepaid pension and OPEB assets have been recorded on Petitioner's books in accordance with applicable accounting standards. The record also reflects that the prepaid pension asset has reduced the pension cost reflected in the revenue requirement in this case, and the asset serves to preserve the integrity of the pension fund. The prepayment benefits customers by reducing total pension costs in Petitioner's revenue requirement. The record also reflects that the entire balance of the prepaid pension asset represents investor supplied funding and, as a result, is entitled to a return, which supports Petitioner's position of including the prepaid pension asset as a negative zero cost component of the capital structure. The same is true of the OPEB asset. Petitioner's evidence showed that it does not have access to funds from the ongoing pension or OPEB plan other than for the payment of benefits under the plan. Therefore, we find that the prepaid pension and OPEB assets should be included in Petitioner's capital structure as offsets to zero cost capital as proposed by Petitioner.[23]

As to Mr. Gorman's reliance on comparisons of past amounts reflected in rates to actual expense to disallow the prepaid pension asset, we agree with Mr. Shimansky that this would constitute prohibited retroactive ratemaking. *Office of Util. Cons. Couns. v. Duke Energy of Ind.*, 183 N.E.2d 266 (Ind. 2022).

Turning now to the appropriate equity component to use in the capital structure for setting rates for Petitioner, we find that Petitioner's forecasted capital structures at each of the relevant cutoff dates for the implementation of rates in three steps are reasonable. Longstanding Indiana precedent requires the use of a utility's actual, not hypothetical, capital structure when setting rates. Hypothetical capital structures are contrary to Indiana law. *See Public Service Comm'n of Ind. v. Ind. Bell Tel. Co.*, 235 Ind. 1, 130, N.E.2d 467 (Ind. 1955). Although we are dealing with a future test period and using forecasted capital structures at this point in the process, Petitioner's proposal will incorporate its actual capital structure, not a forecasted capital structure, when implementing its Step 1, 2, and 3 rate increases. We find the proposed equity and debt components to be comparable to those of similarly situated utilities and in line with this Commission's prior findings on what constitutes a reasonable capital structure to satisfy the *Bluefield* and *Hope* standards and our charge under Indiana law to ensure that rates are just and reasonable while affording the utility an opportunity to earn a fair return. Accordingly, as referenced above, we reject Mr. Gorman's invitation to adjust the ROE based on the projected capital structure. We accept Petitioner's projected capital structures in this case.

Finally, the OUCC proposed changes to the regulatory treatment of the repairs deduction for federal income tax purposes and raised issues concerning the appropriate amortization of EADIT. Industrial witness Gorman has proposed to accelerate the amortization of Indiana EADIT. All of these issues, to the extent they were to be accepted, would have an impact on ADIT reflected

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[23] Because we reject the Industrial Group's recommendation to remove the prepaid pension and OPEB assets from Petitioner's capital structure, we need not make the adjustments, correctly recommended by Petitioner, to the ADIT balances included in the capital structure were those assets to be removed.

in the capital structure. Later herein, we reject Ms. Stull's and Mr. Gorman's proposals and so there is no need to adjust ADIT flowing from these positions for purposes of the capital structure.

D. Overall WACC. Petitioner's projected capital structure and WACC were included in Financial Exhibit CC, Schedule CC1 of Petitioner's Exhibit 13 and its supporting workpapers. The overall WACC was calculated by summing the component costs of the capital structure, with each component weighted by its respective proportion to total capitalization. Based on the projected capital component balances and component costs described in Mr. Furia's direct testimony, and as updated for July 31, 2023 actuals, Indiana American's projected WACC is 6.88% as of April 30, 2025, 6.75% as of April 30, 2024, and 6.73% as of July 31, 2023 as shown on the financial exhibits provided with Petitioner's response to the Commission's August 30, 2023 Docket Entry.

Based upon the foregoing findings and after giving effect to the ROE we authorize above, we find that Petitioner's forecasted capital structure and weighted cost of capital as indicated below is reasonable and should be adopted for purposes of setting rates in this proceeding:

	Step 1			
	As of 7/31/23	Percent of Total	Cost	Weighted Cost
Common Equity	$ 716,559,651	47.41%	9.65%	4.58%
Long Term Debt	557,418,248	36.88%	4.73%	1.74%
Accumulated Deferred Income Taxes	253,164,451	16.75%	0.00%	0.00%
Accumulated Depr on Contr Utility Plant for Muncie Sewer	98,742	0.01%	0.00%	0.00%
Prepaid OPEBs (Other Post Retirement Employee Benefits)	(8,264,162)	-0.55%	0.00%	0.00%
Accumulated Deferred Investment Tax Credits - Pre 1971	-	0.00%	0.00%	0.00%
Job Development Investment Tax Credits (JDITC) - Post 1970	607,436	0.04%	7.47%	0.00%
Prepaid Pension	(8,062,051)	-0.53%	0.00%	0.00%
Total Capital Structure	$ 1,511,522,315	100.0%		6.32%

	Step 2			
	As of 4/30/24	Percent of Total	Cost	Weighted Cost
Common Equity	$ 731,237,765	47.30%	9.65%	4.56%
Long Term Debt	570,746,268	36.92%	4.71%	1.74%
Accumulated Deferred Income Taxes	261,928,953	16.94%	0.00%	0.00%
Accumulated Depr on Contr Utility Plant for Muncie Sewer	100,471	0.01%	0.00%	0.00%
Prepaid OPEBs (Other Post Retirement Employee Benefits)	(9,545,695)	-0.62%	0.00%	0.00%
Accumulated Deferred Investment Tax Credits - Pre 1971	-	0.00%	0.00%	0.00%
Job Development Investment Tax Credits (JDITC) - Post 1970	597,878	0.04%	7.47%	0.00%
Prepaid Pension	(9,091,336)	-0.59%	0.00%	0.00%
Total Capital Structure	$ 1,545,974,304	100.0%		6.30%

	Step 3			
	As of 4/30/25	Percent of Total	Cost	Weighted Cost
Common Equity	$ 834,238,915	48.19%	9.65%	4.65%
Long Term Debt	651,443,865	37.63%	4.71%	1.77%
Accumulated Deferred Income Taxes	266,474,818	15.39%	0.00%	0.00%
Accumulated Depr on Contr Utility Plant for Muncie Sewer	102,776	0.01%	0.00%	0.00%
Prepaid OPEBs (Other Post Retirement Employee Benefits)	(11,254,406)	-0.65%	0.00%	0.00%
Accumulated Deferred Investment Tax Credits - Pre 1971	-	0.00%	0.00%	0.00%
Job Development Investment Tax Credits (JDITC) - Post 1970	585,133	0.03%	7.47%	0.00%
Prepaid Pension	(10,463,716)	-0.60%	0.00%	0.00%
Total Capital Structure	$ 1,731,127,385	100.0%		6.42%

We find that these respective WACCs, adjusted to reflect Petitioner's actual capital structure at the time and applied to Petitioner's actual net original cost rate base per our previous findings plus the remaining unamortized balance of the Indiana Cities acquisition adjusted as of the same applicable date, represents a fair return on the fair value of Petitioner's used and useful property.

9. <u>Disputed Test Year Revenues</u>. The tables below are summaries of Step 1 and Step 2 pro forma present rate adjustments. The adjustments in bold were disputed and are discussed below.

Step 1	Water			Wastewater		
Description	Base Year Ended '9/30/22	Adjustments	Present Rates Step 1	Base Year Ended '9/30/22	Adjustments	Present Rates Step 1
Operating Revenue	$ 247,037,067		$ 247,037,067	$ 1,734,039		$ 1,734,039
Late Fee Revenue	1,261,837	$ 146,275	1,408,112	8,275	$ 285	8,560
Miscellaneous Revenue	2,964,225		2,964,225	570		570
						-
URT Tax Impact		(3,221,822)	(3,221,822)		(19,277)	(19,277)
Normalization of Billings - Usage		**(1,584,569)**	**(1,584,569)**		12,831	12,831
Annualization of Lowell		700,661	700,661		-	-
Customer Normalization		**3,039,147**	**3,039,147**		60,752	60,752
DSIC Revenue Adjustment		**24,035,317**	**24,035,317**		-	-
SEI Revenue Adjustment		5,150,494	5,150,494		-	-
Yankee Surcharge		-	-		-	-
Miscellaneous Adjustments		**411,538**	**411,538**		4,899	4,899
Acquisition Adjustment		95,807	95,807		-	-
Eliminate 50% of LIPP		**10,262**	**10,262**		**-**	**-**
Rate Increase OOR		-	-		-	-
Normalize Misc. Billing Units		11,835	11,835		-	-
			-			-
Total Operating Revenues	$ 251,263,129	$ 28,794,945	$ 280,058,074	$ 1,742,884	$ 59,490	$ 1,802,374

Step 2	Water			Wastewater		
Description	Step 1 Pro forma Proposed Rates	Adjustments	Present Rates Step 2	Step 1 Pro forma Proposed Rates	Adjustments	Present Rates Step 2
Operating Revenue	$ 269,759,541		$ 269,759,541	$ 3,811,799		$ 3,811,799
Late Fee Revenue	1,537,630	$ 10,382	1,548,012	18,817	$ 632	19,449
Miscellaneous Revenue	2,964,225		2,964,225	570		570
						-
URT Tax Impact	(3,221,822)	-	(3,221,822)	(19,277)	-	(19,277)
Normalization of Billings - Usage	**(1,584,569)**	**(1,390,474)**	**(2,975,043)**	12,831	(660)	12,171
Annualization of Lowell	700,661	-	700,661		-	-
Customer Normalization	**3,039,147**	**3,434,062**	**6,473,209**	60,752	88,399	149,151
DSIC Revenue Adjustment	24,035,317	-	24,035,317		-	-
SEI Revenue Adjustment	5,150,494	-	5,150,494		-	-
Yankee Surcharge	-	(76,056)	(76,056)		-	-
Miscellaneous Adjustments	411,538	-	411,538	4,899	-	4,899
Acquisition Adjustment	95,807	75,826	171,633		-	-
Eliminate 50% of LIPP	10,262	-	10,262		-	-
Rate Increase OOR	-	206,594	206,594		10,555	10,555
Normalize Misc. Billing Units	11,835	19,024	30,859		-	-
			-			-
Total Operating Revenues	$ 302,910,066	$ 2,279,358	$ 305,189,424	$ 3,890,391	$ 98,926	$ 3,989,317

A. <u>Normalization of Billings – Declining Use</u>.

1. <u>INAWC Case-in-Chief</u>. Mr. Rea presented a quantitative analysis of water consumption by INAWC's customers. He explained the modeling used to develop the revenue forecasts for the residential customer class and the development of the revenue projections for all customer classes (residential, commercial, industrial, public authorities, and sales for resale). He testified that the parameters and relationships necessary to analyze declining water use, weather impacts on water consumption, and the impact of COVID on water consumption for customers were estimated using statistical linear regression modeling. Mr. Rea testified his regression models show a trend of declining use identified for residential customers of approximately 585 gallons per year per customer. He stated several factors drive the decline in residential customers' usage, including the incremental introduction of low-flow fixtures and appliances, new regulations that lead to further reductions in fixture flow rates, conservation programs, and public initiatives that have led to greater consumer water conservation awareness. Mr. Rea testified that INAWC's modeling normalizes for weather and COVID and shows that there is a pervasive decline in residential usage over the past ten years, a trend expected to continue in the future.

2. <u>OUCC and Intervenors</u>. While both OUCC and Industrial Group recognized the impact of declining residential water usage per customers, OUCC witness Dellinger and Industrial Group witness Gorman provided testimony proposing different estimated levels of forecasted use per customer than Petitioner using different methodologies than INAWC to arrive at those estimates. Mr. Gorman proposed a 1.1% decline from Year End 2022 use per customer to yield 3,941 gallons per customer per month for the 12-months ended December 2023 and 3,897 gallons per customer per month for the 12-month period ending December 2024. Mr. Dellinger proposed a 0.89% decline from the 12-month period ended September 2022 to yield a projection of 4,019 gallons per customer per month for 12-months ended December 2023 and 3,971 gallons per month for the 12-month period ended April 2025. Mr. Gorman's estimates were higher than Petitioner's by approximately 40 gallons per month and Mr. Dellinger's estimates were higher than Petitioner's by approximately 100 gallons per month.

OUCC witness Dellinger testified that INAWC's declining use projections are not consistent with other information Petitioner has produced regarding general average declines in usage of 2% per year, and target reductions in water usage presented in American Water's investment literature. He testified that advances in water saving technology drives enhanced efficiency and that this trend should, over time, reduce the need for larger water and wastewater treatment plants, allow for lower storage and pumping requirements, and generally provide savings and benefits to society at large.

Mr. Dellinger testified Petitioner is not requesting a percentage reduction from actual usage but instead proposes to use the output of a regression analysis, which results in a much steeper decline for the period between the base period and calendar year 2023, to estimate future usage. Rather than producing a "trendline," he said Petitioner produced a future monthly projection of estimated flows based on estimated precipitation, estimated cooling degree days, monthly adjustments, and an estimated 585-gallon annual decline. Mr. Dellinger pointed to inconsistencies in Petitioner's monthly model between forecasted maximum monthly usage values and the historical data. He testified the means to capture the decline in customer use is via an annual trendline applied to actual usage, and not a monthly model with significant and unnecessary complexity.

Mr. Dellinger conducted his own analysis using annual data instead of monthly data with no weather variables and a single COVID impact variable to measure the impact on usage due to the COVID pandemic in 2020 and 2021. He acknowledged that weather affects usage, but the effects are more pronounced on a monthly basis, and for declining usage what is important is the underlying trend of lower use on an annualized basis. He stated he did run regression models on an annualized basis incorporating weather adjustments, but weather adjustments did not have statistical significance or relevance to the annualized analysis.

Industrial Group witness Gorman testified that Petitioner's projected use per forecasted level of customers over the forecast period understates a reasonable estimate of residential sales throughout the forecasted test period. He testified that Petitioner's use of declining use per customer based on ten years of historical trends does not reflect actual, recent, historical data. It fails to acknowledge that declining use per customer will slow over time as customers continue to replace old less water-efficient appliances with new more efficient ones—a factor Petitioner notes as among those driving customer declining use over the historical time period. Further, Mr. Gorman testified that a review of INAWC data shows that declining use per customer has begun to slow and thus, assuming the trend continues, Petitioner has understated customer use through the forecast period, understated revenue at current rates, and inflated the claimed revenue deficiency. Mr. Gorman presented an analysis to show that there is an obvious change in use per customer on a normalized sales basis but that the relative change is not linear from year to year. Mr. Gorman concluded that on an annual basis, the declining use per customer has changed from approximately 1.5% per year decline over the period 2013-2017, slowing to approximately a 1% per year decline over the period 2019-2022, which forms the basis for his proposal.

3. <u>INAWC Rebuttal</u>. Mr. Rea disagreed with Mr. Dellinger's approach to modeling residential usage without reflecting weather effects and his approach of using less data to forecast usage. In response to Mr. Dellinger's modeling that input both cooling degree days and precipitation on an annualized basis, he stated the results were not surprising because using fewer data points doesn't make the weather impacts go away, it just makes it harder to identify the impacts. Mr. Rea took exception to Mr. Dellinger's approach of ignoring the impacts of weather on water consumption. He testified it makes no sense to argue that it is better to model annual data to get an annual answer and ignore weather impacts than to model monthly data, understand weather impacts, normalize for them, and sum monthly normalized results to get an annual answer. He performed a comparison of the results of Mr. Dellinger's modeling approach using actual (non-normalized) annual usage compared to weather-normalized data and testified the weather-normalized model shows more declining usage. He testified the results of his comparison validate the results from the monthly model.

In response to Mr. Gorman's analysis, Mr. Rea did not dispute that the percentage change in residential usage is smaller in the latter half of the ten-year historical period than the first half. However, without a finding that the change in trend is statistically significant, Mr. Rea testified it is impossible to know whether the change in trend is real or simply by happenstance. He therefore disagreed with Mr. Gorman's conclusion that there has been a significant and lasting reduction in the rate of declining residential usage use per customer.

4. <u>Discussion and Findings</u>. All parties who offered testimony on the level of declining use by INAWC's residential customers recognized some level of expected annual reduction per customer. Mr. Rea, on behalf of the Petitioner, estimated a reduction of 585 gallons per customer, per year based on a linear regression model. Pet. Ex. 5 at 68. Mr. Gorman calculated a reduction of approximately 520 gallons per customer per year using the ten-year average from the results of Petitioner's linear regression model. IG Ex. 1 at 28, Table 5. The OUCC calculated a decline of 436 gallons per customer, per year based on a linear regression model. OUCC Ex. 6 at 3-4. The difference in the parties' positions, as explained above, is in how the amount of annual per customer declining use was calculated.

The results of the parties' regression models or average of a model are shown below. A negative number implies a decline in usage whereas a positive number implies an increase.

Year	INAW normalized use (weather and Covid) per customer	% change year-to-year	OUCC normalized use (Covid) per customer	% change year-to-year	Industrial Group (INAW 10-Year Average	% change year-to-year
2013	4.422		4.346		4.422	
2014	4.343	-1.787%	4.310	-0.836%	4.343	-1.787%
2015	4.279	-1.474%	4.273	-0.844%	4.279	-1.474%
2016	4.210	-1.613%	4.237	-0.851%	4.210	-1.613%
2017	4.191	-0.451%	4.200	-0.858%	4.191	-0.451%
2018	4.093	-2.338%	4.164	-0.865%	4.093	-2.338%
2019	4.134	1.002%	4.128	-0.873%	4.134	1.002%
2020	4.144	0.242%	4.270	3.449%	4.144	0.242%
2021	3.898	-5.936%	4.144	-2.944%	3.898	-5.936%
2022	3.984	2.206%	4.019	-3.033%	3.984	2.206%
2023	3.901	-2.078%	3.982	-0.905%	3.939	-1.128%
2024	3.852	-1.252%	3.946	-0.913%	3.895	-1.128%
2025	3.804	-1.268%	3.910	-0.921%	3.851	-1.128%
INAW Average 2013 - 2022				-1.128%		
OUCC Average 2013 - 2022				-0.851%		
Average INAW and OUCC 2013 - 2022				-0.989%		

The Commission believes the output of regression analysis can provide important data to determine future residential usage per customer, but reviewing the results both in the periods from where the original data came from (2013-2022) and the forecast period (2023-2025) provide an important reasonableness check.

Simply looking at the data above raises concern with the reliability of INAWC's and the OUCC's model. Mr. Rea used ten years of monthly data, which was normalized for weather and COVID. The results showed there is a year-to-year decrease from 2013 to 2018, which appears logical, particularly as we agree that usage per customer has decreased over time with water saving appliances. However, in 2019 and 2020, usage per customer increases. Then, in 2021 there is a significant decline (-5.94%), which is twice the next largest decline and over five times the ten-year average of -1.128%. Finally, in 2022, it increases 2.206%. Thus, in those four years, the model predicted three years of increase and one relatively large decrease, indicating a random, rather than a "pervasive," decline over the past ten years as Mr. Rea suggests. The forecast results from Petitioner's model also raises concern. Petitioner's regression model declined by -2.078% in 2023, which is above any decline until 2018, but drops to -1.252% in 2024, and -1.268% in 2025. We also reject Mr. Rea's proposition that the Commission should focus on the Adjusted R-Squared, which is a measure of how well the regression line or model approximates actual data. The Commission does not view this as a competition and the winner has the highest Adjusted R-Squared. In fact, Mr. Rea's original model only has an Adjusted R-Squared of 84.7%, while Mr. Dellinger's model has an Adjusted R-Squared of 87.5%.

The OUCC's model used ten years of annual data, which was normalized only for COVID. The model showed that weather was not a statistically significant variable. The results show a steady decline from 2013-2019, but 2020 has a relatively large increase, and 2021 and 2022, a relatively large decrease, which is unexplainable based on the previous years. The forecast results from the OUCC's model are more consistent for 2023, 2024, and 2025, showing -0.905%, -0.913%, and -0.921%, respectively. We are also not sufficiently concerned to eliminate the OUCC's model, as Mr. Rea argues, because it used annual data instead of monthly data, since there was no evidence showing that one year in the ten-year data set was an outlier when considering weather or that there is a trend in weather, such as hotter and/or dryer, over the past ten years.

The Industrial Group used the ten-year average from the results of Petitioner's linear regression model because he argued the period 2013-2017 is different from 2019-2022. However, because of our concerns with Petitioner's results, we reject Mr. Gorman's declining usage of 1.128% per year as our ultimate determination.

As indicated above, the output of regression models is informative but given our concerns over the results of the regression models, we believe Mr. Gorman's method of taking an average has merit. As shown above, INAWC's ten-year average is -1.128% and the OUCC's ten-year average is -0.851%. Because we do not believe one regression model to be superior to another, we find the average of INAWC's and the OUCC's (-0.989%) is a reasonable approximation of the yearly decline in residential usage per customer. This percentage reduction will be applied to the monthly average actual usage per customer beginning with the 12 months ending December 2022 of 4.058, which results in the following table.

	Usage Per Month	Gallons Per Year	Decline in Gallons Per Year
For the 12 Months Ended 12. 31. 2022	4.058	48,702	
For the 12 Months Ended 12. 31. 2023	4.018	48,220	-482
For the 12 Months Ended 12. 31. 2024	3.979	47,743	-477
For the 12 Months Ended 12. 31. 2025	3.939	47,271	-472

Using Petitioner's model, which multiplies the forecasted adjusted volume by the appropriate rate block to calculate the adjustment, we find appropriate to use a pro forma declining usage adjustment of ($1,584,569) for Step 1 and ($1,390,474) for Step 2, which results in total pro forma declining usage of ($2,975,043).

B. <u>Customer Normalization</u>.

1. <u>INAWC Case-in-Chief</u>. Mr. Rea explained the development of INAWC's pro forma revenue in this case. A summary of pro forma revenues for Indiana American's water and sewer operations under present and proposed rates is provided in Petitioner's Exhibit 14, Schedules REV1 W and REV1 WW, which show operating revenues by customer class for the base year under present rates (12-months ended September 30, 2022) and for the Step 1 (12-months ended December 31, 2023) and Step 2 and Step 3 (12-months ended

April 30, 2025) forecast periods. He testified that base year revenues for the 12 months ended September 30, 2022 were based on actual billing determinants for the base year period and were annualized using the rates that became effective November 2022 that reflect the impact of removing the URT from revenue requirements. Revenues for future test year at present rates for Step 1 were based on current rates and projected billing determinants by customer class for the 12-month period ending December 31, 2023, as well as projections for other miscellaneous revenues.

These projections of revenues for the Step 1 period at present rates compared to the calculated revenue requirement for the same period is the basis for the requested increase in this case for Step 1. For Step 2, revenues at present rates were based on proposed rates from Step 1 and projected billing determinants by customer class for the 12-month period ending April 30, 2025. For Step 3, revenues at present rates were based on proposed rates from Step 2 and projected billing determinants by customer class for the 12-month period ending April 30, 2025.

Mr. Rea testified that for each class, forecasted sales were determined by multiplying forecasted customer counts for each class by forecasted use per customer. Metering billing determinants were developed by applying forecasted customer counts to the base year pattern of meter sizes in each class. Usage billing determinants were determined by applying forecasted sales to the base year pattern of usage by rate block in each class. Forecasted billing units for both monthly meter charges and usage were multiplied by current rates to get forecast revenue at present rates for Step 1 and were multiplied by Step 1 proposed rates to get forecast revenue at present rates for Step 2 and then multiplied by Step 2 proposed rates to get forecast revenue at present rates for Step 3.

Mr. Rea detailed the specific factors for forecasting customer and usage by customer class components for organic growth for each class. He explained how the various components of Other Revenues were developed. He also explained the calculation of revenues under proposed rates utilized the following billing determinants: billing determinants for Step 1 are based on forecasted usage and customer count information for the 12-month period ending December 2023. Billing determinants for Step 2 and Step 3 are identical and are based on forecasted usage and customer count information for the 12-month period ending April 2025.

2. <u>OUCC</u>. OUCC witness Sullivan raised issues with respect to certain elements of Petitioner's revenue calculations. Regarding INAWC's proposed adjustment for non-residential declining use, Ms. Sullivan testified that using a three-year average consumption rate (October 1, 2019 through September 30, 2022) is not appropriate because consumption levels between April 2020 and December 2021 were affected by COVID. Although Indiana American considered this in its residential consumption analysis, it was not given consideration in Mr. Rea's non-residential customer consumption analysis. For her analysis, Ms. Sullivan instead calculated a ten-year median value from the ten years of historical data provided by Petitioner to forecast future non-residential consumption. She testified using a median value of the ten years of data would eliminate the high and low values from non-typical years, like years with droughts and pandemics.

Ms. Sullivan also testified regarding INAWC's proposed adjustment for organic growth. She said Petitioner did not project any growth for its non-residential customer classes after December 31, 2023, but non-residential growth should be recognized through the end of the future test year, April 30, 2025. She also calculated a different Step 1 organic customer growth adjustment by using the OUCC's average customer consumption values instead of Petitioner's values and calculated a different Step 2 adjustment by including non-residential customer class growth through April 30, 2025.

3. **INAWC Rebuttal.** Mr. Rea did not take issue with the OUCC's adjustment for residential customer counts, which were nearly identical to Petitioner's. However, because he disagreed with the OUCC's forecast of residential use per customer, he disagreed with Ms. Sullivan's residential class revenue adjustments. Similarly, he disagreed with Ms. Sullivan's commercial class adjustment that was based on the OUCC's use per customer projection for 2023, which is a reduction from 2022 but was well above any level seen in the 2017-2021 timeframe. Mr. Rea stated Petitioner's projections for use per customer for commercial customers are more in line with recent history and should be used instead of the OUCC's projections. He further disagreed with OUCC industrial usage forecasts showing increases in 2024 and 2025 that are higher than any year in the historical period. He stated this is not a realistic result for a class that has shown flat or even slightly declining usage over time. He testified that Petitioner's forecast of usage is more realistic and reflective of current usage levels in both 2021 and 2022.

With respect to Ms. Sullivan's adjustment for the Public Authorities class, Mr. Rea testified that the combination of the ten-year median use per customer for the Public Authorities class and the customer growth function employed by Ms. Sullivan results in total usage for the class that is higher than any annual usage for this class would suggest. He said that this results from using a use per customer data point in the historical data that is not consistent with the customer counts that serve as the base for the forecast which come from a different year, producing what he described as a gross mismatch in this class between projections and historical reality.

4. **Discussion and Findings.** INAWC and the OUCC used the same general methodology for forecasting residential customer count with the only difference being when to begin the forecast period. Petitioner begins the forecast period October 2022, while the OUCC begins the forecast period January 2023. In rebuttal, Mr. Rea did not take issue with the OUCC's customer count adjustment. The Commission believes that when actual data is available, it should be used. Thus, we find the OUCC's residential customer count should be adopted, which is shown in the table below.

3 months ending 12.2022	12 months ending 12.2023	12 months ending 12.2024	12 months ending 12.2025
289,845	292,295	294,672	296,930

The non-residential customer total usage is customer count multiplied by the usage per customer. INAWC did not model non-residential usage per customer using regression analysis, but instead used, in many cases, an average based on the three-year average for the 12 months ending September 2020 through September 2022, which includes the COVID years of 2020-2021. In addition, customer counts for several non-residential customer classes were based on the count as of September 2022. Mr. Rea argued that using a consistent methodology across all customer classes is preferable, such that all classes are treated equitably and no bias is built into the forecast process.

For usage per customer, OUCC witness Sullivan used the ten-year median (2012-2021) because it eliminates the high and low values for non-typical years (i.e., droughts and pandemics). Generally, for customer count the OUCC used actual customer count for October through December 2022 and customer growth was based on the methodology used for residential customers.

The Commission is not persuaded that the median over the past ten years is a good predictor of future water usage per customer for the non-residential class and finds it preferable to use an average of more recent years. The Commission also questions the reasonableness of reaching back to 2012 for the start of the ten years when, for residential usage per customer, both the OUCC and INAWC start in 2013. We agree with Petitioner that for certain non-residential customer classes the OUCC's methodology results in abnormally high total billed usage. However, while we agree a three-year average is a better predictor, we do not agree that in all cases the years 2020, 2021, and 2022 should be used to calculate the average. The use of the same methodology across the non-residential customer classes may produce an unrealistic forecast. Thus, the Commission examined INAWC's data from 2018 through 2022, attempting to avoid the COVID years and years that appeared to be an outlier, and determined, based on its review, which of the five years should be used to determine the three-year average and a reasonable predictor of future usage per customer.

For customer counts, the parties generally differed on whether to use actual figures for the three months October through December 2022. As with residential customer growth, the Commission believes that when actual data is available, it should be used.

Accordingly, our findings on customer count and usage per customer for the Commercial Class, Industrial Class, Public Authority Class, and Sale-for-Resale Class are shown in the table below.

Class of Customer	3 Months Ending 12.2022 Customer Count	3 Months Ending 12.2022 Avg. Usage Per Customer	12 Months Ending 12.2023 Customer Count	12 Months Ending 12.2023 Avg. Usage Per Customer	12 Months Ending 12.2024 Customer Count	12 Months Ending 12.2024 Avg. Usage Per Customer	12 Months Ending 12.2025 Customer Count	12 Months Ending 12.2025 Avg. Usage Per Customer
Commercial[1]	28,552	26.598	28,733	26.181	28,860	26.183	28,994	26.184
Industrial[2]	654	564.140	653	609.972	653	609.972	653	609.972
Public Authority[3]	2,185	54.150	2,244	66.386	2,367	66.449	2,514	66.517
Sale-for-Resale[4]	24	N/A	24	N/A	24	N/A	24	N/A

1. Only difference in count was use of actual data.; Year 2020 usage/customer is outlier, used average of 2019, 2021, and 2022.
2. INAWC count is more accurate.; Years 2018 and 2020 usage/customer are outliers, used average of 2019, 2021, and 2022.
3. OUCC count is more accurate.; Years 2018 and 2019 usage/customer are outliers, used average of 2020, 2021, and 2022.
4. There is no disagreement on count.; used INAWC billed usage per customer.

These figures were entered into Petitioner's model, which multiplies the forecasted adjusted volume by the appropriate rate block to calculate the adjustment. Using this methodology results in a pro forma customer growth adjustment of $3,039,147 for Step 1 and $3,434,062 for Step 2.

		IURC
Step 1 - Customer Growth Adjustment:		
Residential	$	1,308,578
Commercial		313,836
Industrial		189,475
Public Authority		881,020
Miscellaneous		-
Sale for Resale		-
Fire		346,238
Step 1 Adjustment -- Increase (Decrease)	**$**	**3,039,147**
Step 2 - Customer Growth Adjustment:		
Residential	$	1,873,505
Commercial		398,463
Industrial		-
Public Authority		789,235
Miscellaneous		-
Sale for Resale		-
Fire		372,859
Step 2 Adjustment -- Increase (Decrease)	**$**	**3,434,062**

C. Low-Income Pilot Program ("LIPP") Discount Adjustment.

1. OUCC. Ms. Sullivan recommended an additional $15,259 in revenues related to the LIPP, for a $25,521 increase to operating revenue to eliminate the discounts provided under Petitioner's low-income pilot program during the base period based on the amount recorded to its general ledger during the base year.

2. INAWC Rebuttal. Mr. Shimansky explained that under the settlement approved in Cause No. 45142, a regulatory asset was established for the customer-funded portion of the total program costs. The total amount of discounts provided under the LIPP is recorded as a debit to revenues (having the effect of decreasing revenues) but then the customer-funded portion is credited to revenues (having the effect of making the revenues whole for that portion) and debited to the regulatory asset. Petitioner only added back $10,262 to adjust for the LIPP because that is the portion (the non-deferred company contributions to the LIPP) by which the revenues were decreased.

3. Discussion and Findings. The evidence reflects that the portion of the discount that represents the customer-funded portion of the LIPP discounts and is recorded to the regulatory asset to be collected at a later date was already added back to revenues. The revenues for this portion of the discount that is attributable to the customer obligation does not need to be added back a second time. Accordingly, we find Petitioner's adjustment should be accepted.

D. **<u>DSIC Revenue Adjustment</u>.**

1. <u>OUCC</u>. Ms. Sullivan also proposed an adjustment to forecasted operating revenues related to Cause No. 42351 DSIC 14 ("DSIC 14"). She testified that INAWC's forecasted DSIC revenues were overstated by $85,983, because to include anything other than the approved amount of DSIC revenues could result in INAWC's revenues being adjusted twice—once in this case and again when the reconciliation is calculated. From the amount authorized in DSIC 14 ($35,316,103), she subtracted DSIC revenue included in the base year operating revenues ($11,366,769). As a result, she recommends a $23,949,334 increase to base year operating revenue to reflect total authorized DSIC revenues based on total DSIC revenues authorized by the Commission in DSIC 14**.**

2. <u>INAWC Rebuttal</u>. Mr. Shimansky responded by explaining that Ms. Sullivan's adjustment was based upon a figure from the DSIC 14 Order before it was adjusted as called for in that order. He said the DSIC 14 Order required INAWC to revise its DSIC factor to adjust the property tax expense for accrued depreciation when submitting its tariff. After giving effect to this language, he said the final total DSIC revenues is $35,316,103.

3. <u>Discussion and Findings</u>. Both Indiana American and the OUCC agree that Petitioner's forecasted DSIC revenues equal $35,316,103, the amount authorized in DSIC 14. However, they have different pro forma DSIC revenue adjustments because they each used different base year amounts. Ms. Sullivan determined that base year DSIC revenues total $11,366,769, resulting in a pro forma increase of $23,949,334. Mr. Shimansky, however, determined base year revenues of $11,280,786, resulting in a pro forma increase of $24,035,317. Although the OUCC's lower pro forma adjustment amount would result in a higher rate increase, Mr. Shimansky recommended the OUCC's proposed adjustment be denied. Accordingly, we accept Petitioner's pro forma DSIC revenue adjustment.

E. **<u>Late Fee Adjustments</u>.**

1. <u>OUCC</u>. OUCC witness Sullivan also recommended an increase to operating revenues for late fees based on application of the late fee ratio (using the same methodology as Petitioner) to the OUCC's recommended operating revenues. She testified the late fee ratio reflected in Petitioner's late fee adjustment was 0.5108%

2. <u>INAWC Rebuttal</u>. Mr. Shimansky testified that because Indiana American disagreed with the OUCC's proposed adjustment to operating revenues, no adjustment to late fees is necessary.

3. <u>Discussion and Findings</u>. We find Petitioner's proposed water late fee ratio of 0.5108% for Step 1 and 0.5081% for Step 2 should be applied to the level of pro forma water operating revenues at present rates found in this Order.

10. <u>Disputed Test Year Expenses</u>. The tables below summarize Step 1 and Step 2 pro forma present rate adjustments. The adjustments in bold were disputed and are discussed below.

Step 1		Water			Wastewater	
	Base Year Ended		Present Rates	Base Year Ended		Present Rates
Operating and Maintenance Expenses	'9/30/22	Adjustments	Step 1	'9/30/22	Adjustments	Step 1
Purchased Water	$ 381,079	$ (20,137)	$ 360,942	$ (856)		$ (856)
Production - Fuel & Power	**9,061,988**	**485,255**	**9,547,243**	**47,778**	**(3,893)**	**43,885**
Production - Chemicals	**3,693,252**	**3,039,732**	**6,732,984**	25,860	6,880	32,740
Waste Disposal	1,497,670	168,744	1,666,414	717,122	(125,001)	592,121
Salaries and Wages	**17,644,123**	**2,925,321**	**20,569,444**	**200,371**	**(185,487)**	**14,884**
Pension	(1,292,968)	1,923,563	630,595	(5,391)	9,964	4,573
OPEB	(2,645,262)	907,428	(1,737,834)	(18,743)	6,140	(12,603)
Group Insurance	**3,760,373**	**843,973**	**4,604,346**	**48,937**	**(45,943)**	**2,994**
Other Benefits	**1,276,876**	**423,681**	**1,700,557**	**13,445**	**(13,118)**	**327**
Support Services	**25,462,958**	**1,511,404**	**26,974,362**	**184,660**	**10,961**	**195,621**
Contract Services	**1,888,539**	**1,300,789**	**3,189,328**	57,136	1,256	58,392
Bldg. Maintenance & Services	**1,637,996**	**(2,756)**	**1,635,240**	**53,715**	**(18,387)**	**35,328**
Telecommunications	**695,038**	**45,170**	**740,208**	**3,625**	**179**	**3,804**
Postage, Printing, & Stationary	**51,951**	**265**	**52,216**	183	13	196
Office Supplies & Services	**539,343**	**42,241**	**581,584**	**2,835**	**215**	**3,050**
Advertising & Marketing	300	(300)	-	-	-	-
Employee Related Expense	**331,016**	**(30,609)**	**300,407**	**1,705**	**111**	**1,816**
Miscellaneous Expense	**2,459,435**	**(105,743)**	**2,353,692**	**32,421**	**1,730**	**34,151**
Rents	353,197	(49,757)	303,440	1,024	274	1,298
Transportation	**1,225,890**	**117,849**	**1,343,739**	**(962)**	**962**	**-**
Uncollectible Accounts	**2,103,281**	**404,071**	**2,507,352**	**15,254**	**1,030**	**16,284**
Customer Accounting	**290,355**	**13,791**	**304,146**	2,103	(5)	2,098
Regulatory Expense	**649,640**	**(301,095)**	**348,545**	**4,712**	**(2,184)**	**2,528**
Insurance Other Than Group	3,009,272	858,474	3,867,746	22,177	5,873	28,050
Maint. Supplies & Services	**4,343,548**	**1,661,096**	**6,004,644**	**60,994**	**13,354**	**74,348**
Capital movements	3	(3)	-	2	(2)	-
Total O&M Expenses	78,418,893	16,162,447	94,581,340	1,470,107	(335,078)	1,135,029
Other Expenses						
Depreciation	**53,265,802**	**13,128,974**	**66,394,776**	**1,350,810**	**(426,974)**	**923,836**
Amortization	**285,871**	**65,831**	**351,702**	**2,315**	**309**	**2,624**
Federal income taxes	**13,131,316**	**(832,412)**	**12,298,904**	**95,230**	**(325,455)**	**(230,225)**
State income taxes	**3,702,083**	**(144,535)**	**3,557,548**	**26,848**	**(77,105)**	**(50,257)**
Investment tax credits	(39,816)		(39,816)	(289)		(289)
Property Taxes	**13,137,584**	**3,290,514**	**16,428,098**	**296**	**458,492**	**458,788**
Payroll Taxes	**1,312,165**	**228,461**	**1,540,626**	**14,673**	**(14,082)**	**591**
Environmental Tax	312,173	7,939	320,112	2,263	(913)	1,350
URT	2,423,546	(2,423,546)	-	17,576	(17,576)	-
IURC Fee	273,469	127,448	400,917	1,983	75	2,058
Total Expenses	$ 166,223,086	$ 29,611,121	$ 195,834,207	$ 2,981,812	$ (738,307)	$ 2,243,505

Step 2	Water			Wastewater		
Operating and Maintenance Expenses	Step 1 Pro forma Proposed Rates	Adjustments	Present Rates Step 2	Step 1 Pro forma Proposed Rates	Adjustments	Present Rates Step 2
Purchased Water	$ 360,942	$ -	$ 360,942	$ (856)		$ (856)
Production - Fuel & Power	**9,547,243**	**60,058**	**9,607,301**	**43,885**	**197**	**44,082**
Production - Chemicals	**6,732,984**	**2,442,281**	**9,175,265**	32,740	7,818	40,558
Waste Disposal	1,666,414	109,109	1,775,523	592,121	38,768	630,889
Salaries and Wages	**20,569,444**	**919,019**	**21,488,463**	**14,884**	**(187)**	**14,697**
Pension	630,595	-	630,595	4,573	-	4,573
OPEB	(1,737,834)	-	(1,737,834)	(12,603)	-	(12,603)
Group Insurance	**4,604,346**	**242,792**	**4,847,138**	**2,994**	**(37)**	**2,957**
Other Benefits	**1,700,557**	**70,273**	**1,770,830**	**327**	**(12)**	**315**
Support Services	**26,974,362**	**1,226,865**	**28,201,227**	**195,621**	**8,898**	**204,519**
Contract Services	**3,189,328**	**173,204**	**3,362,532**	58,392	2,175	60,567
Bldg. Maintenance & Services	**1,635,240**	**53,866**	**1,689,106**	**35,328**	**1,135**	**36,463**
Telecommunications	**740,208**	**33,421**	**773,629**	**3,804**	**126**	**3,930**
Postage, Printing, & Stationary	**52,216**	**500**	**52,716**	196	-	196
Office Supplies & Services	**581,584**	**35,474**	**617,058**	**3,050**	**183**	**3,233**
Advertising & Marketing	-	-	-	-	-	-
Employee Related Expense	**300,407**	**14,501**	**314,908**	**1,816**	**82**	**1,898**
Miscellaneous Expense	**2,353,692**	**76,247**	**2,429,939**	**34,151**	**1,277**	**35,428**
Rents	303,440	6,950	310,390	1,298	16	1,314
Transportation	**1,343,739**	**54,979**	**1,398,718**	-	-	-
Uncollectible Accounts	**2,711,763**	**23,334**	**2,735,097**	**34,961**	**1,141**	**36,102**
Customer Accounting	**304,146**	**7,482**	**311,628**	2,098	-	2,098
Regulatory Expense	**348,545**	**-**	**348,545**	**2,528**	**-**	**2,528**
Insurance Other Than Group	3,867,746	679,323	4,547,069	28,050	4,927	32,977
Maint. Supplies & Services	**6,004,644**	**198,730**	**6,203,374**	**74,348**	**2,449**	**76,797**
Capital movements	-	-	-	-	-	-
Total O&M Expenses	94,785,751	6,428,408	101,214,159	1,153,706	68,956	1,222,662
Other Expenses						
Depreciation	**66,394,776**	**4,801,739**	**71,196,515**	**923,836**	**137,907**	**1,061,743**
Amortization	**351,702**	**637,408**	**989,110**	**2,624**	**827**	**3,451**
Federal income taxes	**16,815,212**	**(2,628,751)**	**14,186,460**	**182,436**	**(42,563)**	**139,873**
State income taxes	**4,665,641**	**(646,283)**	**4,019,358**	**50,991**	**(10,162)**	**40,829**
Investment tax credits	(39,816)	-	(39,816)	(289)	-	(289)
Property Taxes	**16,428,098**	**2,398,303**	**18,826,401**	**458,788**	**65,893**	**524,681**
Payroll Taxes	**1,540,626**	**92,931**	**1,633,557**	**591**	**(14)**	**577**
Environmental Tax	**320,112**	1,949	**322,061**	1,350	-	1,350
URT	-	-	**-**	-	-	-
IURC Fee	434,155	2,803	436,958	5,095	647	5,742
Total Expenses	$ 201,696,257	$ 11,088,507	$ 212,784,763	$ 2,779,128	$ 221,491	$ 3,000,619

A. Production Expenses.

1. INAWC Case-in-Chief. Mr. Cifuentes explained that production costs are expenses that vary according to the amount of water provided or wastewater processed. The costs include purchased water, fuel and power, chemicals, and waste disposal. System delivery is the amount of treated water that Petitioner's treatment plants produce. Water sales and other factors impact the amount of water produced by the plants, which in turn impact expenses associated with treating and distributing that water. Mr. Rea proposed pro forma revenue adjustments related to declining usage and customer growth and calculated associated pro forma system delivery. INAWC used the same level of system delivery in its pro forma fuel and power and chemical production related expenses.

With respect to fuel and power expense, Petitioner proposed a total company Step 1 increase of $310,160 to base period fuel and power expense of $9,109,766 yielding Step 1 pro forma fuel and power expense of $9,419,926. Petitioner proposed a Step 2 decrease of $479 yielding Step 2 pro forma fuel and power expense of $9,419,447. Pet.'s Ex. 13, OPER Sch. OM2.

Regarding chemicals expense, Petitioner proposed, in its updated June 6, 2023 filing, a total company Step 1 increase of $2,981,484 to base period chemical expense of $3,719,112 yielding Step 1 pro forma chemical expense of $6,700,596. Petitioner proposed a Step 2 increase of $2,426,941 yielding Step 2 pro forma chemical expense of $9,127,537. Pet.'s Ex. 13, OPER Sch. OM3. Petitioner's update corrected a conversion error in the calculation of historic base period usage (quantity) and forecasted usage in light of a transition from gaseous chlorine to liquid chlorine (sodium hypochlorite) and the difference in the amount of chemical utilized in the treatment process. OUCC Ex. 4 at 23.

2. <u>OUCC</u>. The OUCC accepted Petitioner's pro forma adjustments for purchased water, fuel and power, chemicals, and waste disposal.

3. <u>Discussion and Findings</u>. No party disputed Petitioner's pro forma purchased water and waste disposal expenses. Because the Commission's determination on declining usage and customer growth revenue adjustments do not impact these two expenses, we find they should be approved.

While the OUCC recommended declining usage and customer growth revenue adjustments that would have increased INAWC's pro forma revenues, the OUCC did not propose a corresponding increase in production expense. However, with increased revenues, we find that an associated increase in fuel and power and chemical expense should be recognized. Therefore, in conjunction with the increase in system delivery associated with the Commission's pro forma declining usage and customer growth revenue adjustments determined herein, we approve the following pro forma production costs:

Fuel and Power Expense

Line		Total Company	Water	Wastewater
1	Base Year Fuel and Power Expense as of 9/30/2022:	$9,109,766	$9,061,988	$47,778
	Detail of adjustments to Fuel & Power Expense:			
	System Delivery	(85,434)	(86,155)	721
	Billing adjustments and annualization of New Locations	280,813	280,813	-
	2023 Rate Changes	273,878	278,492	(4,614)
	Acquisitions	5,550	5,550	-
	Production Change Improvements	6,555	6,555	-
	2023-2025 Inflation Adjustments	-	-	-
2	Step 1 Pro forma Adjustment	$481,362	485,255	(3,893)
3	**Fuel and Power Expense as of 12/31/2023 (Line 1 + Line 2)**	$9,591,128	$9,547,243	$43,885
	Detail of adjustments to Fuel & Power Expense:			
	System Delivery	43,114	42,917	197
	Billing adjustments and annualization of New Locations	-	-	-
	2023 Rate Changes	-	-	-
	Acquisitions	1,786	1,786	-
	Production Change Improvements	15,355	15,355	-
	2023-2025 Inflation Adjustments	-	-	-
4	Step 2 Pro forma Adjustment	60,255	60,058	197
	Pro Forma Fuel and Power Expense as of 4/30/2025 Test Year (Line 3 + Line 4)	$9,651,383	$9,607,301	$44,082

Chemicals Expense

Line		Total Company	Water	Wastewater
1	Base Year Chemicals Expense as of 9/30/2022:	$3,719,112	$3,693,252	$25,860
	Detail of adjustments to Chemical Expense:			
	Change in System Delivery	45,008	45,008	-
	Change in Chemical Pricing and Usages	3,000,574	2,993,694	6880
	Acquisitions	1,030	1,030	-
2	Step 1 Pro forma Adjustment	$3,046,612	$3,039,732	$6,880
3	**Chemicals Expense as of 12/31/2023 (Line 1 + Line 2)**	$6,765,724	$6,732,984	$32,740
	Detail of adjustments to Chemical Expense:			
	Change in System Delivery	16,602	16,602	-
	Change in Chemical Pricing and Usages	2,433,441	2,425,623	7,818
	Acquisitions	56	56	-
4	Step 2 Pro forma Adjustment	2,450,099	2,442,281	7,818
	Pro Forma Chemicals Expense as of 4/30/2025 Test Year (Line 3 + Line 4)	$9,215,823	$9,175,265	$40,558

B. **Labor and Labor-Related Expenses**.

1. INAWC Case-in-Chief. In its updated filing dated June 6, 2023, Petitioner proposed a Step 1 increase of $3,252,490 to base period salaries and wages expense of $17,844,494 yielding Step 1 pro forma salaries and wages expense of $21,096,984. Petitioner proposed a Step 2 increase of $1,223,089 to Step 1 pro forma salaries and wages expense of $21,096,984 yielding Step 2 pro forma salaries and wages expense of $22,320,073. In Step 1 Petitioner proposed a $709,640 increase for existing positions, an increase of $267,509 for its annual performance plan, an increase of $82,541 for its long-term performance plan, an increase of $598,117 for overtime expense, and an increase of $1,594,683 to add new positions. In Step 2 Petitioner proposed a $724,564 increase for existing positions, an increase of $91,878 for its annual performance plan, an increase of $7,636 for its long-term performance plan, an increase of $109,879 for overtime expense, and an increase of $289,132 to add new positions. As explained by INAWC witness Grisham, pro forma salaries and wages expense was calculated on a position-by-position basis, based on 408 full-time positions.

INAWC witness Britto explained that Petitioner is projecting an increase in staffing levels to support the increased investment and maintenance for aging infrastructure, systems added through acquisitions, and compliance with increasing water quality and wastewater regulations as well as to improve levels of service, quality, reliability, and efficiency for customers and the community. She stated Petitioner's operations are widely dispersed throughout the state and INAWC operates distinct public water systems providing service to approximately 78 communities. She explained Petitioner continues to look to improve efficiency, enhance compliance, and better serve customers by evaluating areas of operations and identifying the positions that fit best in a regional approach and can function optimally at a centralized location. She testified Petitioner has slowly added support staff to ensure it is adding the right positions in the right areas to support its customers and maintain compliance.

Ms. Britto provided a summary of the positions INAWC has added and plans to add from 2019 through the Test Year. She testified 13 positions were added as a result of the Sheridan and Lowell acquisitions. In 2021 and 2022, five positions were added to provide more effective oversight and operations support, including two Director of Operations positions, an Information Technology Specialist and two Business Operations Specialists. Ms. Britto stated Petitioner is adding four positions in 2023 to provide more effective oversight and support of operations throughout the state, including a state-wide water quality and environmental compliance supervisor, two staff engineers, and a state-wide training coordinator. She said Petitioner added three senior manager roles to operations in the East, Central, and West regions (for a total of six managers across the state, one per region) in 2022. Petitioner also added six new pipe mechanics to create two crews for replacing lead service lines that fall outside of Petitioner's scheduled engineering projects. Ms. Britto stated Petitioner plans to add three water treatment plant operators for the East, Central and South regions in 2023. Thus, by 2024, Petitioner will have added six water quality and environmental compliance positions to better support its regional structures and improve its focus on water quality and environmental compliance. Ms. Britto stated these additional employees will support compliance with more stringent regulations that require additional tracking, monitoring, and reporting and will enhance Petitioner's cross connection control program, which is a critical component to protect the distribution system and customer health and safety. She further testified Petitioner plans to add four health and safety specialists: two in 2023 (one Northern region, one Southern region) and two more in 2024 (one Central region, one Western region) to align with and support Petitioner's regional structure and further strengthen Petitioner's commitment to safety.

Ms. Britto also explained how Petitioner proposes to address its current and future staffing needs given existing workforce demographics. She said Petitioner is no exception to the challenge faced by water utilities across the country with the loss of significant knowledge and expertise over the next five to ten years due to retirements. Ms. Britto testified that currently 28% of Indiana American's front-line employees are over the age of 55, and 16% are over 60 years of age. She explained these tenured employees have familiarity with Indiana American's operations and processes, along with the necessary licenses required by state and federal regulations, that cannot be easily supplemented with new employees. Ms. Britto testified Indiana American believes the most logical solution is to hire employees before the wave of retirements hit so the new hires can learn side-by-side with the soon to be retirees. She stated this approach will also provide the new hires with the on-the-job experience required for a license and provide ample time for the new hires to prepare for and pass applicable exams.

For water payroll taxes, Petitioner proposed a Step 1 increase adjustment of $267,597 yielding a Step 1 pro forma payroll taxes expense of $1,579,762 and a Step 2 increase adjustment of $116,192 yielding Step 2 pro forma payroll taxes expense of $1,695,954. For wastewater payroll taxes, Petitioner proposed a Step 1 decrease adjustment of $14,000 yielding a Step 1 pro forma payroll taxes expense of $673 and a Step 2 pro forma payroll taxes expense of $673.

For water group insurance, Petitioner proposed a Step 1 increase adjustment of $958,645 yielding a Step 1 pro forma group insurance expense of $4,719,018 and proposed a Step 2 increase adjustment of $312,265 yielding a Step 2 pro forma group insurance expense of $5,031,283. For wastewater group insurance, Petitioner proposed a Step 1decrease adjustment of $45,868 yielding a Step 1 pro forma group insurance expense of $3,069 and proposed a Step 2 pro forma group insurance expense of 3,069.

2. **<u>OUCC</u>.** Mr. Malan disagreed with Petitioner's increase to salaries and wages expense. He testified that INAWC made no adjustment for perpetual vacant positions and explained that, through the normal course of business, INAWC will continue to have vacancies. He noted that a level of positions has historically remained vacant, and Petitioner did not have full employment through the base period or the verifiable link period. Mr. Malan also asserted that customers should not have to bear the cost of an expense Petitioner is not likely to incur.

Mr. Malan testified that while the OUCC accepts Petitioner's adjustments to salaries and wages expense for Step 1 and Step 2 and the increase resulting from the addition of 46 new employees proposed in this Cause, the OUCC disagrees with Petitioner's proposed increase to salaries and wages expense due to historic vacancies. He testified that 100% staffing is not realistic and therefore it would be imprudent to include the full salaries and wages for all positions as INAWC requested.

To determine a rate for vacant positions based on INAWC historic vacancy levels, Mr. Malan used Petitioner's vacancies and number of full-time equivalents ("FTEs") on December 31 for the years 2013 through 2022. He then averaged the vacancy percentage for years 2013-2022 to arrive at an average vacancy rate of 3.66% and adjusted Step 1 downward by 1.23% to 2.43% to account for Petitioner's acknowledged five vacant positions less the historic vacancy rate. He adjusted Step 2 by the full 3.66% vacancy rate. He applied this historic vacancy rate in determining appropriate adjustments for salaries and wages expense, payroll taxes, group insurance, and other benefits.

Based on this historic vacancy rate, Mr. Malan recommends a Step 1 increase of $2,739,833 to base period salaries and wages expense of $17,844,494 yielding Step 1 pro forma salaries and wages expense of $20,584,327. Mr. Malan further recommends a Step 2 increase of $918,832 to Step 1 pro forma salaries and wages expense of $20,584,327 yielding Step 2 pro forma salaries and wages expense of $21,503,159.

For payroll taxes, Mr. Malan recommends a Step 1 increase of $214,379 to base period payroll taxes expense of $1,326,960 yielding Step 1 pro forma payroll taxes expense of $1,541,339. He further recommends a Step 2 increase of $92,917 to Step 1 pro forma payroll taxes expense of $1,541,339 yielding Step 2 pro forma payroll taxes expense of $1,634,256.

For group insurance, Mr. Malan testified that in conjunction with his proposed reduction to salaries and wages expense, a corresponding reduction to group insurance expense is also necessary to adjust for the historic vacant positions at the calculated rate. Mr. Malan testified OUCC recommends a Step 1 increase of $798,030 to base period group insurance expense of $3,809,308 yielding Step 1 pro forma group insurance expense of $4,607,338. He also states the OUCC recommends a Step 2 increase of $242,755 to Step 1 pro forma group insurance expense of $4,607,338 yielding Step 2 pro forma group insurance expense of $4,850,093.

3. **Industrial Group.** Mr. Gorman testified that INAWC has set its cost of service to include both the costs of new employees and employees who are expected to retire during the timeframe in which rates set in this proceeding are likely to be in effect. He testified that an adjustment should be made for employee attrition due to retirements, transfers, or other factors. Mr. Gorman stated employee attrition can offset increases in Petitioner's employee count and labor expense as a result of hiring employees for new positions, leaving the number of positions unchanged and potentially reducing wage expense as new hires start at lower wage rates than those employees who have left. He stated failing to make an adjustment for employee attrition, will result in customer rates that include excessive labor costs. Mr. Gorman further testified that it is unreasonable for Petitioner to include increases for new employees and increases in contractor expenses in addition to an increase in overtime expense instead of assuming that the new hires will alleviate overtime pressures on existing employees or that the cost of overtime for new hires might be less than that of existing employees. Mr. Gorman proposed an adjustment of 16% for employee attrition spread over the rate increase period. He did not make an adjustment to overtime expense ($1.9 million in the base period), stating these expenses (along with the proposed increases in overtime expense) can be used by Petitioner for any required overtime it may need as employees retire.

4. **INAWC Rebuttal.** Ms. Britto acknowledged it is reasonable to assume that occasionally there will be vacant positions. She agreed that Mr. Malan's use of a historical average vacancy rate compared to budget could represent a reasonable estimate of vacancies at any point in time but contended that there are other reasonable representations as well. She explained that using the actual head count over the last ten years as compared to the head count assumed in rate cases (and thus built into rates), Indiana American averages 3.47% more employees than what was used to set rates.

With respect to Mr. Gorman's proposed reduction based upon a 16% attrition rate spread equally over Steps 1 and 2, Ms. Britto asserted such an adjustment is speculative and not grounded in any evidence. Ms. Britto further testified there is also no evidence that an employee who actually retires will leave a position open that will remain unfilled. Further, Ms. Britto stated that Mr. Gorman's position is unsupported by the fact that Indiana American has hired above the level of employees assumed in its rate cases during the last ten years.

As to Mr. Gorman's criticism that Petitioner did not propose an adjustment to overtime expense, Ms. Britto explained that because water utilities operate 24/7 to provide essential service to customers, overtime is often a business requirement to provide clean, reliable service. She stated a large part of overtime work includes emergency call out service work and W5 operators that need to be on site, which will continue to be performed and cannot be replaced by the FTEs proposed in this case.

5. <u>Discussion and Findings</u>. No party disputed Petitioner's proposed new positions. Instead, the parties took issue with INAWC's proposed FTEs due to the potential for vacancies and the possibility for new employees and the proposed increased use of contractors to offset the need for overtime. While the OUCC recommended approval of Petitioner's proposed FTEs, denial of the proposed increase to contractor expense and a new proposed vacancy rate adjustment (Step 1 – 2.43% and Step 2 – 3.66%), the Industrial Group recommended approval of Petitioner's proposed increase to contractor expense (with minor adjustments) and a reduction to the proposed FTEs.

The parties seem to agree that it is reasonable to assume a certain level of vacancies within Petitioner's forecasted headcount. The purpose of a future test year process is to forecast expenses a utility expects to incur during the year in which rates are in effect. Thus, it is reasonable to expect that vacancies will exist prior to the start of the test period.

Petitioner also provided testimony supporting its need to continue a certain level of overtime consistent with its forecast, particularly because the utility operates on a 24/7 basis. However, while we agree that a certain level of overtime will always be necessary due to emergencies and availability of qualified personnel, we also expect that Petitioner's proposed use of contractors will free up its staff for other projects. Accordingly, with our adjustment to the vacancy rate (Step 1 – 2.43% and Step 2 – 3.66%) and Petitioner's contract expense as discussed below, we find Petitioner's proposed overall labor expense level, including the overtime expense adjustment, to be reasonable. We find Petitioner's pro forma salaries and wages expense should be $20,584,328 for Step 1 and $21,503,160 for Step 2.

For payroll taxes, with our adjustment to the vacancy rate (Step 1 – 2.43% and Step 2 – 3.66%), we find Petitioner's Step 1 to be $1,541,217 and Step 2 to be $1,634,134 based on the pro forma level of salaries and wages approved herein.

For group insurance, with our adjustment to the vacancy rate (we find Petitioner's Step 1 – 2.43% and Step 2 – 3.66%), we find Petitioner's Step 1 to be $4,607,340 and Step 2 to be $4,850,095.

C. <u>Other Benefits Expense</u>.

1. <u>INAWC Case-in-Chief</u>. In Step 1 Petitioner proposed a $30,071 increase to 401(k) expense, a $270,441 increase to defined contribution plan expense, a reduction of $7,156 to employee stock purchase plan expense ("ESPP"), a $21,499 increase to Voluntary Employee Benefits Association expense, a $928 increase for additional miscellaneous benefits for existing positions, and a $136,665 increase for additional miscellaneous benefits for new positions. In Step 2 Petitioner proposes a $92,229 increase to 401(k) expense, a $97,197 increase to defined contribution plan expense, a $14,301 increase to ESPP expense, a $9,820 increase to Voluntary Employee Benefits Association expense, a $97 decrease to existing positions, and a $118,633 decrease to new positions.

2. <u>OUCC</u>. The OUCC did not accept Petitioner's Step 1 and Step 2 adjustments for new employee 401(k) and ESPP expense. Mr. Malan testified that Petitioner overstated its new employee 401(k) expense by assuming a 100% participation rate and that Petitioner's five-year average 401(k) participation rate is 86%. Accordingly, he recommended Step 1 new employee 401(k) expense of $81,826, which is $13,319 less than that requested by Petitioner. He proposed Step 2 new employee 401(k) expense of $16,131, which is $2,626 less than Petitioner's request. Mr. Malan further took exception with Petitioner's calculation of its proposed new employee ESPP expense, which also assumed 100% participation. He testified that Petitioner's five-year average ESPP participation rate is 37%. Thus, he recommended a $5,452 reduction to Petitioner's proposed Step 1 new employee ESPP expense and a $1,072 reduction to Petitioner's proposed Step 2 new employee ESPP.

3. <u>INAWC Rebuttal</u>. Ms. Grisham responded to OUCC witness Malan's arguments that Petitioner's 401(k) and ESPP programs are not fully enrolled, acknowledging they are not, but rejecting Mr. Malan's proposed five-year average participation rate. She explained that rather than assuming a participation rate, Petitioner's calculation to determine the average expense per employee is based on actual costs and includes $0 line items for the 41 and 226 employees that are not currently participating in the 401(k) and ESPP program, respectively. Ms. Grisham pointed out that Mr. Malan's use of the five-year average 401 (k) participation rate ignores the fact that participation rates over the past five years have been increasing as the number of pension-eligible employees decreases. She presented actual annual participation rates for Petitioner's 401(k) for the most recent three years, which is higher than the five-year average of 86%.

4. <u>Discussion and Findings</u>. With respect to the OUCC's proposed reductions to other benefits expense, we find that Petitioner's methodology already accounts for non-participating employees and therefore provides a more accurate and realistic preview of the dollars Petitioner will spend on both 401(k) and ESPP expenses than the five-year average participation rate recommended by the OUCC. With respect to the 401(k) participation rate in particular, Petitioner's evidence shows the five-year average participation rate likely underestimates future participation rates. *See* Pet. Ex. 20 at 5, Table 1. Accordingly, we find that the evidence in this case supports Petitioner's forecasted level of other benefits expense with an adjustment for vacant positions, and we decline to make the OUCC's recommended new employee benefit adjustments. We find Petitioner's pro forma other benefits expense to be $1,700,884 for Step 1 and $1,771,145 for Step 2.

D. Support Services Expense.

1. INAWC Case-in-Chief. Petitioner proposed forecasted total support services expense of $27,411,536 in Step 1 and $28,657,034 in Step 2. Mr. Grisham testified the services provided by the Service Company include, among others, customer service, water quality testing, innovation and environmental stewardship, human resources, communications, information technology and cyber security, finance, accounting, payroll, tax, legal, engineering, accounts payable, supply chain, and risk management.

2. OUCC. Ms. Stull testified that Petitioner's proposed forecasted total support services expense is a 44.44% increase over the revenue requirement in the 2019 Rate Order. She accepted Indiana American's forecasted adjustments to support services expenses. However, she recommended removal of all business development department costs, which Petitioner forecasted to be $241,552 in Step 1 and $251,285 in Step 2. Ms. Stull testified she recommended removal of all business development department costs for the same reasons expressed by the Commission in Cause No. 44022, wherein it found no evidence that the business development activities provided a benefit to customers. Therefore, Ms. Stull proposed to eliminate all operating expenses included in service company expenses for the business development department.

3. INAWC Rebuttal. Ms. Grisham disagreed with Ms. Stull's recommended adjustment to remove business development costs from support services expense. She testified the evidentiary record in Cause No. 44022 does not control the Commission in this proceeding, and business development does more in communities than facilitate acquisitions. Ms. Grisham testified that American Water's business development activities help build relations with community businesses and leaders and benefit customers of Indiana American by mitigating the costs to be recovered per customer, enhancing purchasing power, and spurring activities that contribute to their local economies.

Ms. Grisham explained business development activities that grow Indiana American's customer base enable system investment costs and operating expenses to be spread across a larger customer group. She testified despite Petitioner's operating expenses increasing by approximately $9 million from 2013 through 2022, due in part to the customer base expanding by approximately 37,000 customers during that time period, operating expense per customer actually decreased slightly, from $255 per customer in 2013 to $253 per customer in 2022. Ms. Grisham further testified that business development activities also benefit many of the communities served by Petitioner. As an example, needed investment allowed a soft sewer ban to be lifted in Sheridan, allowing growth in a community that had been stifled by lack of treatment capacity.

Finally, Ms. Grisham testified that through operation improvements of acquired wastewater and water utilities, business development activities achieve public policy objectives of improving the quality of the water consumed by customers and of the public bodies of water into which wastewater effluent is discharged.

4. <u>Discussion and Findings</u>. The OUCC accepted Indiana American's forecasted adjustments to support services expenses but recommended removal of all business development department costs from the expense totals. Pub. Ex. 3 at 29. The OUCC recommended disallowance of these costs for the same reasons the Commission cited in *Indiana-American Water Co*., Cause No. 44022, 2012 WL 2154248, (IURC 6/6/2012), where the Commission found no evidence that Petitioner's business development activities provided a benefit to customers.

Petitioner asserts that its business development activities help build community relations, achieve public policy objectives, and benefit customers by enhancing purchasing power and spreading costs across a larger customer group from acquisitions and economic development. However, we agree with the OUCC that although Petitioner claims it has lowered customer operating expenses and other costs, Indiana American has not sufficiently tied those reductions to its business development activities. Although Petitioner may be achieving economies of scale and enhancing its purchase power, it is doing so in part through its acquisitions. Also, while acquisitions may facilitate economies of scale as measured by operating expense per customer, this metric does not consider the initial investment to acquire the customers or subsequent investments in the acquired utilities. And, as the OUCC pointed out, this may not necessarily be a benefit to Indiana American's customer base, particularly given the fact that Ind. Code § 8-1-30.3-5 provides for favorable ratemaking treatment on acquisitions. Thus, the Commission remains concerned that customers may be subsidizing INAWC's business development with limited offsetting customer benefits and Petitioner's evidence does nothing to alleviate those concerns.

As for improving community relations and achieving public policy objectives, we note that Petitioner has included approximately $593,312 in its forecasted expenses for "external affairs and public policy," which could cover those anticipated expenses. Therefore, we accept the OUCC's recommended adjustment to remove business development costs of $241,552 in Step 1 and $251,285 in Step 2. We find Petitioner's pro forma support services to be $27,169,983 for Step 1 and $28,405,746 for Step 2.

E. <u>Contract Services – Line Locates</u>.

1. <u>INAWC Case-in-Chief</u>. Ms. Britto testified that Petitioner continues to see a significant increase in Indiana 811 notices to locate and mark its facilities since Petitioner's last general rate case and projects this trend will continue through the test year in this Cause. She presented Petitioner's projected volume of notices to locate and mark its facilities based on the average increase in notices from 2020 to 2022. She explained that non-essential frontline service work was deferred from March 2020 through December 2021 to help protect the safety of employees and customers during the pandemic and, consequently, Petitioner did not contract out work such as locates during this time. Ms. Britto testified that with the continuing increases in the volume of notices to locate and mark facilities, as well as frontline service work no longer being deferred, Petitioner has frequently reassigned employees from completing customer service orders and other crucial (although less time sensitive) tasks such as hydrant maintenance, valve maintenance, leak detection, fire service inspections, cross-connection inspections, contractor site inspection, cross training/development activities, and a variety of other water distribution tasks to stay current with the 811 work demands. She stated Petitioner proposes to address the continued increasing demand to locate and mark its facilities by utilizing contractors to do most of this work. The proposed increase in contract services expense (Pet. Ex. 13, OPER Schedule OM 11 in the file INAWC 2023 Rate Case – Contract Services) is based on the costs of bid responses received from contractors to complete the current and the projected level of notices requiring Petitioner to locate and mark its facilities. She said shifting to contractors for line locates will limit the number of new hires included in this case to address this work and repurpose employees back to maintenance activities.

INAWC witness Grisham explained that the level of contract services operating expense for the test year was determined beginning with the expense level from the base period and then adding a projected monthly level of work to locate and mark facilities as discussed by Ms. Britto. A monthly inflation factor of 0.23% was then applied through the end of the future test year.

2. **OUCC.** The OUCC recommended denial of Petitioner's proposed Step 1 and Step 2 adjustments for contracted line locates. Mr. Malan testified that Petitioner made no reduction to any other expense to offset the $4.2 million total increase to contract services expense for additional contracted services to perform line locates, including no adjustments to reduce overtime or wages that would not be needed for those line locates which would be performed through contract services. He testified that Petitioner did not incur any base period expense for contracted line locates nor any time since and has made no effort to outsource line locates since Petitioner's deferral of non-essential frontline service work had ended in December of 2021. He noted that in its last rate case, Petitioner had received approval for $507,528 for additional contracted line locates, yet no locates were performed by outside vendors. Mr. Malan contended that Petitioner has not sufficiently justified its failure to implement its prior proposal and request to use additional contract services for performance of line locates. He testified that Petitioner also failed to provide sufficient justification for its proposed adjustment. He stated it is also unclear to what extent line locates will be performed by contractors, instead of employees, or whether these costs have been double counted in Petitioner's proposals.

In addition, OUCC witness Seals testified that the number of Petitioner's service orders show a decreasing trend and that the transition to advanced metering infrastructure ("AMI") meters should further improve the efficiency of local field service employees. Because these AMI meters will be able to be read remotely by Indiana American staff without manual contact, meter-reading functions will be largely eliminated. He said the combination of decreased service orders and decreased meter reads would free employees to complete additional tasks, including line locates, that would foster a reduced need for contract services, which is not otherwise subject to adjustment.

3. **Industrial Group.** Mr. Gorman proposed to cap Petitioner's projected levels of contractor expenses at its Step 1 request because he said Petitioner has not proven the projected number of line locates it proposes to outsource is reasonable nor that it will actually incur its projected cost. Mr. Gorman took issue with Petitioner's forecasted increase in line locates in excess of the historical increase and said Petitioner did not offer evidence that the increase experienced in 2022 is representative of a sustained acceleration in the number of calls to

Indiana 811 rather than simply an outlier, nor has it shown the line locates are expected to increase at the same rate going forward. He noted that Petitioner did not use previously requested funds in its prior rate case on contractors for line locates. He recommended the contractor expense tied to outsourcing line locates be capped at the 2024 increase, which would allow Petitioner to increase contractor expense by $3.9 million for line locates. He said capping these costs achieves a balance of Petitioner's desire to outsource line locates to reduce the workload on internal employees while protecting customers from cost increases that he says Petitioner is unlikely to incur in the rate effective period.

4. <u>INAWC Rebuttal</u>. Regarding Petitioner's employment of outside vendors to perform line locates, Ms. Britto explained that the COVID pandemic commenced shortly after Petitioner's last rate case and as a result non-essential frontline service work was deferred. During the pandemic, Ms. Britto said existing staff could be redeployed from completing customer service orders and other maintenance activities to remain current with the locate work demands. She testified Petitioner is no longer operating in the same conditions, and conditions existing during the pandemic do not serve as a reasonable basis to doubt that Petitioner will use contract labor to complete the forecasted line locates. She noted that the OUCC did not dispute Petitioner's projection of locate requests or the cost per locate, nor did he propose any other method or cost for addressing locate requests. As to Mr. Gorman's dispute of the forecasted growth in locates, she said that Indiana American had actually reduced the projection from the 8% increase seen in 2021-2022 to project a 6% increase in line locates. Ms. Britto testified that Mr. Gorman's proposal to cap contractor expense for line locates at the 2024 increase of $3.9 million, while more reasonable than Mr. Malan's recommendation, would still leave Petitioner short of recovery for costs it expects to incur while rates are in effect. She stated Mr. Gorman's use of a seven-year average of forecasted growth is driven down by pandemic years and opined that the 6% growth rate is more reflective of what is expected for the future.

5. <u>Discussion and Findings</u>. INAWC requests a substantial increase to its contract services expense to perform line locates. Specifically, Petitioner requests a two-step adjustment, allowing it to increase its contractor expenses by approximately $3.9 million for the year ending December 31, 2023 and an additional $303,771 increase over Step 1 for the year ending April 31, 2025. Petitioner's forecasted expense is based on one of three bids it received for such contract services. Based on the evidence presented, we find Petitioner has failed to support its proposed increase in contractor expense.

INAWC has previously requested and received approval to outsource its line locates to contractors, as opposed to using internal employees, and not followed through with the approved outsourcing. In the 2019 Rate Order, Petitioner received approval of approximately $500,000 for additional contract service for line locates. However, the evidence shows no line locates have been performed by outside vendors and Petitioner instead has reassigned employees from completing customer service orders and a variety of other tasks to perform the line locates. We understand the impact from the COVID pandemic, but Petitioner has failed to sufficiently explain its delay since that impact was alleviated, particularly given Petitioner's assertion that the amount of line locates increased in 2022 and are expected to continue.

Despite Petitioner's purported intention to utilize contract labor for line locates, it has not done so, and this failure gives us reason to doubt the extent to which Petitioner will actually use the requested increase to outsource labor for line locates going forward. This uncertainty is further heightened by the fact that INAWC has yet to execute a contract securing outside labor for line locates, is negotiating the use of outside contractors with its union employees, and thus, its proposed level of spend is based solely on bids it has received and not on a firm contract. We also note that the bid relied upon by Petitioner for its forecasted expense is significantly higher than the lowest bid and Petitioner offered no explanation for its choice to rely on that bid other than to indicate it was the middle bid.

Furthermore, INAWC has made no reduction to any other expense to offset its proposed increase to contract services expense for additional contracted services to perform line locates, including no adjustments to reduce overtime or wages for its own employees that would not be needed if those line locates would be performed under contract service agreements. Thus, it is unclear to what extent line locates will be performed by contractors, instead of employees, or whether these costs have been double counted in Petitioner's proposals.

Petitioner's proposed increase in contractor expense is also based on its assumption that line locates will increase by 6% in 2024 and 2025, despite the fact that since 2016, line locates have, on average, increased by just 4% each year. Pet. Ex. 4 at 31. INAWC attempts to justify this assumption by pointing to the 8% increase in line locates in 2022. However, it offered no evidence demonstrating that the increase in 2022 is representative of a sustained acceleration in the number of line locates requested rather than simply an outlier.

Petitioner is seeking a substantial increase in staff (both employee and contractor) in this case. As noted earlier, Petitioner is adding 46 new positions at a cost of $1,883,816 while also proposing to outsource all line locates at a cost of $4,194,530. These two increases result in an additional $6,078,346, a 34% increase in labor costs from Petitioner's base period salaries and wages of $17,884,494.

Based on the evidence presented, we find that Petitioner's contract services expense should be based on the lower bid received. However, given our finding above regarding Petitioner's proposed labor expense and in recognition that at least some outsourcing of its line locates will allow Petitioner to meet its goal of developing a pool of skilled workers, we find that Petitioner should be authorized to outsource half of its line locates, resulting in a contract services Step 1 water adjustment of $1,300,789, which includes the two undisputed adjustments for removal of lobbying expense and inflation. The total company Step 1 contract services adjustment is $1,302,045 after including the $1,256 wastewater adjustment. The contract services Step 2 water adjustment is $173,204, which includes the inflation adjustment of $69,147. The total company Step 2 contract services adjustment is $175,379 after including the $2,175 wastewater adjustment. We find contract service for Step 1 to be $3,247,720 and for Step 2 to be $3,423,099.

F. Inflation/Annualization.

1. INAWC Case-in-Chief. Mr. Cifuentes described Petitioner's methodology used to calculate its pro forma expense levels that are based on an inflation factor for the verifiable link period and then trended through the future test year. Petitioner used unique and specific inflation factors developed for each O&M category that aligns with the U.S. Bureau of Labor Statistics by specific measure category and type of cost to recognize the impact of inflation on Petitioner's expenses for the verifiable link period and through the future test year. Petitioner also proposed to annualize or normalize the following expense accounts: building maintenance & supplies (OM12); telecommunications expense (OM13); postage, printing & stationery (OM14); office supplies and services (OM15); employee related expense (OM17); maintenance supplies & services (OM18); and miscellaneous expense (OM25). To calculate the annualization, Petitioner selected the last month of 2023 within each respective workpaper and multiplied the monthly expense by 12 to get the yearly expense.

2. **OUCC.** Mr. Compton recommended the adjustments to annualize these expense accounts be denied, because he disagreed with how Petitioner normalized (i.e., annualized) these expenses for inflation. Mr. Compton explained that Petitioner calculated the annualization of each expense by multiplying the expense in the last month of 2023 by twelve, essentially projecting each expense for inflation. Petitioner's pro forma adjustment was then calculated by subtracting each month's expense in 2023 (January through December) from the monthly annualization Petitioner had calculated. Mr. Compton testified that by adjusting for inflation and then annualizing the expense based on the year-end's inflationary adjusted expense, Petitioner double counted inflation in Step 1.

Mr. Compton explained that annualizing is appropriate and necessary when there is less than a full year of information, but because Petitioner's base year and future projections are based on a full year's worth of data, there was no need to annualize the expense accounts and doing so has the effect of double counting inflation.[24] Mr. Compton testified Petitioner's annualization adjustment should be removed from each Step 1 expense projection for each respective expense account.

3. **Industrial Group.** Mr. Gorman objected to Petitioner's use of the historical three-year average of inflation rather than economists' projected prospective inflation rate through the close of the forecasted test year (April 2025). He explained that relying on a historical three-year average that ends at the start of the base period (September 2022), as INAWC proposes, does not adjust historical O&M costs for the inflation outlook expected from the base period through the forecasted test year. He testified that the prospective inflation outlooks by independent economists from October 2022, through the end of the forecasted test year, April 2025, are significantly lower than the actual inflation rate that occurred for the three-year period ending in September 2022. In other words, inflation has decreased significantly from the level that is reflected in INAWC's historical average. Thus, Mr. Gorman explained that relying on escalation factors based on historical data is not a reasonable basis for projecting increases in O&M expenses over the link period and future test year and inaccurately inflates INAWC's actual O&M expense from the historical base year through the forecasted test year.

To account for the disparity between the historical rate of inflation leading up to the base period and the independent inflation outlook from the base period through the close of the test year, Mr. Gorman recommend adjusting the forecasted test year O&M expense to reflect inflation outlooks from the historical base period through the forecasted test year. Mr. Gorman testified that this effectively lowers the inflation rate used by Petitioner from 5.05% to 2.97%. Mr. Gorman

[24] Mr. Compton noted the only annualization he would consider acceptable by these standards would be an annualization of expenses for Lowell but considered annualizing expenses for all communities to be unreasonable.

testified that adopting his approach and adjusting the various inflation factors that INAWC uses to the consensus economists' forecasts for future inflation would lower the claimed revenue deficiency by approximately $698,000 for water and $30,000 for wastewater.

4. <u>INAWC Rebuttal</u>. Responding to Mr. Compton's recommendation to remove annualization for the identified O&M expenses, Mr. Cifuentes testified that the purpose of the annualization is to adjust the Step 1 expenses to a level predictive of what INAWC will experience going forward. Mr. Compton's recommendation, however, bases the Step 1 level of these expenses on the projected levels for calendar year 2023, which fails to reflect the inflation projected to occur during most of 2023 and understates the level projected to be occurring at the anticipated date of the order in this Cause.

Mr. Cifuentes explained there is no double counting of inflation in the adjustment. The monthly amount for December 2023 within each of the relevant expense accounts is multiplied by 12, which represents 12 months to arrive at the pro forma level of expense for 2023 on an annualized basis. The annualized amount (based on the last month in 2023) captures the inflation adjustment and does not compound, nor is it calculated in excess of its intended value.

In response to Mr. Gorman's proposed adjustment to use consensus analysts' reports to forecast inflation, Mr. Cifuentes responded that Mr. Gorman's recommendation is flawed in assuming that analysts' and/or economists' reports provide projected inflation rates that would consistently be useful and relevant to the expenses to which they are applied. He stated accuracy is enhanced when specific inflationary rates are applied to each category of expenses when available and Mr. Gorman's proposal would use one across-the-board rate of 2.97%, which is an average of the general consumer price index forecasted to occur from 2022 through 2024, or a general inflationary factor. Mr. Cifuentes stated this rate does not contemplate for, adjust, or target each expense category presented in this Cause.

5. <u>Discussion and Findings</u>. We find the evidence shows that Petitioner has not already adjusted for inflation the relevant expense accounts in developing its forecast for calendar year 2023 prior to annualizing such expenses. As a result, without the step of annualizing these amounts based on the last month in 2023, the full effect of inflation at the time this Order is issued would not be captured. We find that Petitioner's method of annualizing these expenses better matches the amount to be included in rates to the amount projected to be incurred at Step 1. We therefore reject the OUCC's proposed removal of annualization for these expense accounts.

INAWC witness Cifuentes chose specific inflationary factors for the applicable industry, which he used in his adjustment. We find that the use of more specifically tailored inflationary factors for each of the O&M categories as sourced from the U.S. Bureau of Labor Statistics provides a more reliable forecast of inflation with respect to each category of expense to which those inflationary factors were applied than the use of generic inflation economist outlooks. Accordingly, we reject the Industrial Group's recommended blanket inflationary factor.

G. <u>Miscellaneous Expense</u>.

1. <u>INAWC Case-in-Chief</u>. INAWC proposed an overall $57,089 decrease to base year miscellaneous expense of $2,491,856 yielding pro forma miscellaneous expense of $2,434,767 for Step 1 expenditures. In addition, Petitioner proposed an overall $20,435 increase to base year miscellaneous expense to yield a pro forma expense of $2,512,291 for Step 2 expenditures.

2. <u>OUCC</u>. Mr. Compton explained that Petitioner proposed eight adjustments to base year miscellaneous expense. Petitioner also proposed adjustments to remove $124,760 of charitable contributions, a total of $23,000 of lobbying expenses, and $42,000 of penalties from base year expenditures. In addition, Petitioner proposed to add in $300 of adjustments from OM16, $27,594 of adjustments from OM17, $65,767 of adjustments for inflation, and $39,010 of adjustments for annualization to base year expenditures for Step 1 expenditures. Mr. Compton explained that Petitioner proposes the same adjustments for Step 2 expenditures as it did in Step 1; however, Petitioner does not adjust for annualization and proposes an inflation adjustment for an increase of $179,255 to base year expenditures. All other adjustments remained the same.

Except for Petitioner's adjustments for the annualization of the expense account, Mr. Compton accepted Petitioner's proposed miscellaneous expense adjustments. However, Mr. Compton proposed other adjustments. Mr. Compton removed $38,023.12 from the Community Relations for a full season plan of courtside tickets for Pacer games at Gainbridge Fieldhouse, explaining this expense is of no benefit to customers and should not be included in rates. He also removed from the base year $8,900 from the 2022 Environmental Grant Program because its function is charitable and image-building. He noted Petitioner's pamphlet provides, "All grants will be funded either by the American Water Charitable Foundation upon the advice or recommendation of personnel from American Water and its state subsidiaries or directly by such American Water subsidiary." OUCC Ex. 5, Attachment JTC-5. Mr. Compton testified that as the program can be funded by the charitable foundation, it should be treated as such and therefore should not be treated as a recoverable expense. Lastly, rather than removing from the base year only a portion of the National Association of Water Companies ("NAWC") bill (13%), which Petitioner acknowledged is involved in lobbying on behalf of public utilities, Mr. Compton recommended the full amount for the NAWC invoice of $188,932.91 be removed from the base year as NAWC activities substantially benefit shareholders' interests rather than customers.

Based on the foregoing, Mr. Compton recommended a decrease of $309,001 to base year miscellaneous expense of $2,491,856, resulting in a pro forma miscellaneous expense of $2,182,855 for Step 1 expenditures. Additionally, he recommended a decrease of $192,468 to base year miscellaneous expense to resulting in a pro forma miscellaneous expense of $2,299,388 for Step 2 expenditures.

3. <u>INAWC Rebuttal</u>. Mr. Shimansky accepted removal of the Indiana Pacers expenses.

INAWC witness Cifuentes explained the Environmental Grant Program focuses on projects that address watershed and/or source water protection in INAWC's service areas and is therefore beneficial to customers. He stated the costs to administer the program include the cost of preparing, printing, and mailing of Environmental Grant Brochures plus associated costs, including time spent by staff to evaluate the applications and to choose recipients. Mr. Cifuentes provided an example of an Environmental Grant Program project that benefited INAWC customers called the Riverview Park Bioswale & Prairie Planting Improvements project where the funds will be used to improve water quality by installing a vegetated bioswale to capture runoff at Riverview Park that currently discharges to Holt Ditch within 50 feet of convergence with the White River. He testified the project will reduce flooding and storm water runoff and associated pollution into the White River, a water source for INAWC. He stated the removal of invasive species and installation of native plants will help to filter pollutants and sediment from water exiting the site.

Mr. Cifuentes disagreed with the OUCC that all NAWC activities benefit the interest of shareholders rather than customers. The NAWC is a professional association that provides a forum for its members to collaborate, share best practices, and leverage their strengths to benefit the communities they serve. Indiana American's utilization of tools offered by its NAWC membership benefit customers through professional development for INAWC employees, which provides more efficient and effective service through knowledge of the latest trends and techniques.

4. <u>Discussion and Findings</u>. On rebuttal, Petitioner accepted the OUCC's position that Indiana Pacers tickets should be removed from miscellaneous expense and employee-related expense. We agree and find such expense should be removed.

As for the Environmental Grant Program, we agree with the OUCC and find that this program is primarily charitable in nature and for the purpose of building Petitioner's image in its communities. The evidence shows that the program can be funded by the American Water Works' charitable foundation or its state subsidiary, supporting the primarily charitable nature of the program. Expenses identified as charitable contributions are considered non-recoverable expenses and should not be included in the revenue requirement of the requesting utility. Therefore, we find this expense should be removed.

With respect to Petitioner's NAWC expense, Indiana American properly excluded the portion of the expense related to lobbying and we find the remainder of the expense to be properly included. As Mr. Cifuentes explained on rebuttal, NAWC is professional association that provides a forum for its members to collaborate and share best practices and grow through professional development, which benefits customers through more efficient and effective utility service.

Accordingly, we find Petitioner's forecasted miscellaneous expense for the total company is $2,387,843 for Step 1 and $2,465,367 for Step 2.

H. <u>Transportation Expense</u>.

1. <u>OUCC</u>. Mr. Compton accepted Petitioner's proposed pro forma level of transportation expense with one exception. He testified that the proposed level of transportation expense included a "salvage value reclass inflation" and that salvage value is not a transportation expense. Citing to the National Association of Regulatory Utility Commissions Uniform System of Accounts for Class A Water Utilities, Mr. Compton testified that salvage value should be accounted for through accumulated depreciation and not as a transportation expense. Mr. Compton recommended all salvage value reclass be removed from base year transportation expense, producing a reduction of $99,421.

2. INAWC Rebuttal. Mr. Cifuentes explained that the reclassification that Mr. Compton was referencing was a credit received from a vendor during the base period for vehicles that had been retired from plant records. As such, it was a credit against the bill (which was booked as transportation expense), and the credit needed to be reclassified to salvage value (which Mr. Cifuentes agreed is not an expense). As such, reclassifying the credit must be done to properly state the amount to be booked to expense.

3. Discussion and Findings. We find that Mr. Cifuentes has adequately explained why the credit must be reclassified so as to properly reflect transportation expense. As such, we reject Mr. Compton's recommendation.

I. Bad Debt Expense.

1. INAWC Case-in-Chief. Petitioner proposed pro forma bad debt expense of $3,295,142, which includes the incremental increases to bad debt expense associated with each step of Petitioner's pro forma present rate revenue increases, using a factor of 0.9062% and a factor of 0.8945% for each step's proposed revenue increase.

2. OUCC. Ms. Sullivan proposed bad debt expense adjustments to base year bad debt expense totaling $629,201 yielding pro forma bad debt expense of $2,734,586 utilizing the same factors used by Petitioner.

3. Discussion and Findings. We agree with the factors used by the parties to compute Petitioner's forecasted bad debt expense. We find, based on the methodology used by the parties and our pro forma operating revenues proposed in this case, Petitioner's bad debt expense is $3,141,034.

J. Customer Accounting - Credit Card Fees and Disconnection Process.

1. INAWC Case-in-Chief. Petitioner proposed to include $1,163,647 in the revenue requirement attributed specifically to its proposal to waive the credit card processing fees applied to individual customers and include those fees in the cost of service within Customer Accounting expense (OM22). Pet. Ex. 2 at 35-36. Mr. Shimansky testified that charging a credit card fee on top of the customer bill adds friction to the process of paying a bill. He stated that eliminating the direct payment of the fee will help more customers pay their bill on time and avoid late fees and potential disconnections and is also expected to improve timely collections.

2. OUCC. Mr. Compton recommended the Commission deny Petitioner's proposal because such costs should not be socialized but remain with the cost causer. He argued it should not be the burden of all customers to pay the costs being generated by a subset of customers. Mr. Compton disagreed with the suggestion that customers will be saving money. While he acknowledged that customers paying their bills with credit or debit cards will save money, the customers who don't pay their bill with a card will see an increase in their bills. He stated there is no evidence that Petitioner's proposal will generate any value in customer satisfaction, on-time payment, and disconnection avoidance. Mr. Compton suggested that any increase in timely collections that might result will accrue to Petitioner's benefit as it would make more money in the long run. Mr. Compton argued the net benefit to customers as a whole is neutral as some customers would be receiving assistance at the expense of other customers. He noted that customers who have been paying through methods other than credit or debit card to avoid paying a fee will no longer be able to save that money because they will have to pay for the benefit whether they take advantage of it or not. He also indicated his recommendation is consistent with the Commission's Order in Cause No. 45253, wherein a similar request was denied.

3. <u>CAC</u>. Mr. Inskeep testified that the CAC supports INAWC's proposal and believes it is beneficial to consumers. He testified consumers should not be charged extra fees for paying their monthly bill in the manner most convenient to them, within reason. He noted that payment by credit card is a popular payment method among consumers in Indiana. Mr. Inskeep testified that the support given by Petitioner to stop assessing per-transaction charges for payment by credit card would also apply to other per-transaction fees for payment by phone, debit card, or other reasonable method. He recommended the Commission approve Indiana American's proposal to remove the $1.95-per-transaction charge on credit card transactions and also direct Indiana American to discontinue any other per-transaction charges assessed on residential customers for paying a water and/or wastewater bill, including, but not limited to, payment by phone or debit card. Mr. Inskeep also expressed concern with Petitioner's disconnection policies for customers with medical conditions, reconnection procedures, and its use of internal credit scores that are used to apply discriminatory treatment in its collection activities.

4. <u>INAWC Rebuttal</u>. Responding to the OUCC, Mr. Shimansky testified that when the cost to pay by credit and debit card is removed from the individual customer, those bills become easier to pay leading to more timely payments and lower uncollectible expenses. When this happens, all customers benefit as uncollectible expenses are a part of the revenue requirement. Mr. Shimansky demonstrated the impact on other rates is relatively minor (0.3% of total Operating Revenues) in comparison to making it easier to pay bills. With respect to customer satisfaction, Mr. Shimansky stated the use of a credit card may help customers avoid late payment fees and the discontinuation of water service for non-payment and associated reconnection fees, each of which contribute to customer satisfaction, as does avoiding the incurrence of additional costs associated with mailing in payments or traveling to make in person payments.

With respect to CAC's recommendation that all fees associated with any customer bill payments should be removed, Mr. Shimansky responded that Petitioner has not done the analysis or determined the increased revenue requirement associated with removing such other fees. He testified that Petitioner is not opposed to doing an analysis and corresponding proposal in the next rate case if the Commission finds it necessary. Ms. Britto denied the use of internal credit scores in Petitioner's collection process and testified that Petitioner applies its procedures and policies uniformly to all customers, which are consistent with Commission rules.

5. <u>Discussion and Findings</u>. The Commission addressed a similar proposal to socialize the cost of providing a fee-free payment option in *Duke Energy Indiana, Inc.* Cause No. 45253 at 105-106 (IURC June 29, 2020), wherein it found the proposal unreasonable because it had not been shown to provide value to non-participating customers. While Petitioner asserted in this case that all customers would benefit from more timely payments by those customers who use credit or debit cards for payments and the resulting lower uncollectible expense that results from more timely payments, Petitioner provided no evidence or cost/benefit analysis to support those assertions. Instead, the only analysis performed was to calculate the estimated amount of fees that would be generated from a small subset of customers using a credit or debit card to pay their water bill that it proposed to allocate to all customers. Therefore, we reject Indiana American's proposal to shift its credit card processing fees to all customers.

We also find that Indiana American adequately explained the use of an internal credit metric, which is not used in its collection process. Additionally, Indiana American's disconnection, reconnection, and collection policies and procedures are consistent with the Commission's rules, and we decline to require any modifications based on the CAC's recommendations. However, we encourage Petitioner to continue discussions with CAC and others about additional options for decreasing the number of residential disconnections and improving the reconnection process, particularly for the more vulnerable residential customers.

K. Regulatory Expense - Rate Case.

1. INAWC Case-in-Chief. INAWC forecasted $1,404,295 for rate case expense to be amortized in rates over 3 years, or $468,098 per year. INAWC Financial Exhibits OPER Schedule OM23 within the INAWC 2023 Rate Case – Regulatory Expense file of Petitioner's Exhibit 13.

2. OUCC. Ms. Sullivan testified that the OUCC does not oppose the rate case costs forecasted by Petitioner but disagreed with the total costs to be amortized as well as the amortization period to be used. She stated Petitioner was authorized to recover $1,941,165 in the 2019 Rate Order amortized over three years but not removed from rates. Thus, Petitioner will have collected $647,055 per year for approximately 4.58 years by the time the rates in this case are implemented (July 2019 through approximately February 2024), or $2,965,669, resulting in what she described as an over-collection of at least $1,024,504. Ms. Sullivan testified that because the OUCC has agreed to include under recovered rate case costs in prior cases, it is only equitable that any over collection of rate case costs should be credited against rate case costs to be incurred in this case. She recommended the $1,404,295 of forecasted rate case costs be reduced by the "over collection" of rate case costs from Cause No. 45142, resulting in net rate case costs of $379,791. She recommended this amount be recovered during Step 2 and then removed from Step 3 rates to avoid any future over collection of rate case costs. She also recommended all rate case expense be removed from Step 1 resulting in no rate case expense recovery in Step 1, stating that Step 1 may be of indefinite length and therefore removing rate case expense from Step 1 removes the potential for additional over, or under, recovery of OUCC's recommended net rate case expense.

Ms. Sullivan also recommended a five-year amortization period should the Commission not accept her recommendation. She testified this period is more appropriate than Petitioner's proposed shorter three-year period because the time between rate case filings has been approximately five years for the last three rate case filings. She stated INAWC has been able to extend the period between rate case filings due to its use of DSIC and SEI trackers. Ms. Sullivan further recommended that if the Commission orders a three-year amortization of rate case expense, the Commission order rate case expense should be removed by a tariff filing at the completion of the amortization period.

3. INAWC Rebuttal. Mr. Shimansky disagreed that rate case expense from Cause No. 45142 was over-collected. Citing to a term of the settlement in the prior rate case, he testified that the parties agreed to an annual regulatory expense amortization of $647,055, which included a $50,000 reduction to the annual forecast proposed by Petitioner, driven by reduced projected levels of expense associated with settling the case rather than fully litigating it. Mr. Shimansky testified there was no agreement as to the time over which to amortize the rate case expense. He also noted that there was no term in the settlement that required a filing of new tariffs following expiration of any amortization period. He testified there was no agreement to stop amortizing rate case expense and the balance in the regulatory account for those expenses was never fully amortized to a zero level.

4. Discussion and Findings. The Commission's Order in INAWC's prior rate case approved a settlement among the parties that authorized an annual regulatory expense amortization amount. *See* 2019 Rate Order at 14 and Appendix A of the approved settlement at 4. While the OUCC asserts that the settlement established a total rate case expense amount of $1,941,165 to be amortized over three years, there is no indication in the Commission's Order, or the settlement attached thereto, that anything other than an annual regulatory expense amortization amount was agreed upon or approved. Therefore, we decline to modify the settlement or our Order approving it through the OUCC's recommended offset.

Accordingly, we approve Petitioner's proposed rate case expense. However, we find that such expense should be amortized over four years based on Petitioner's historical average of time between rate cases.[25] Petitioner shall also file revised tariffs upon the end of the amortization period to remove the annual amortization expense from its rates if the four-year period adopted herein expires before new rates are approved.

L. Amortization - COVID Deferral.

1. INAWC Case-in-Chief. INAWC is seeking recovery of $383,817 of COVID related costs. Mr. Shimansky testified that the amortization amount includes balances from both the regulatory asset and the regulatory liability that was set up and charged since March 6, 2020 through December 31, 2021. INAWC proposed to amortize this net balance over three years. These costs include foregone late fees, disconnect/reconnect expenses, uncollectible/bad debt expense, other direct costs, debt carrying costs, and Service Company expenses, offset by savings realized by Petitioner on forgone Travel and Conference expenses.

2. OUCC. Ms. Stull accepted Petitioner's basic methodology for calculating COVD-19 costs but disagreed with Petitioner's "conclusions." She testified that the methodology should include recognition of the line locate costs not incurred during the pandemic but recovered through rates. She calculated an avoided cost of $916,667. As a result, she recommended a deferred COVID regulatory liability of $532,850 (Petitioner's net regulatory asset of $383,817 reduced by avoided line locate costs of $916,667). She also disagreed with INAWC's proposal to amortize deferred COVID costs over three years, positing that five years is a more appropriate amortization period as that is the time between rate case filings for INAWC's last three rate cases. Ms. Stull recommended a deferred COVID regulatory liability of $532,850 be

[25] Petitioner's prior rate case filings include Cause No. 44022 on May 2, 2011, Cause No. 44450 on January 24, 2014, Cause No. 45152 on September 14, 2018, and Cause No. 45870 on March 31, 2023.

amortized over a five-year period as a reduction of $106,570 to INAWC's annual total company operating expenses.

3. INAWC Rebuttal. Mr. Shimansky opposed Ms. Stull's recommendation, noting that Petitioner voluntarily deferred avoided travel and conference expense savings when it was not required to do so. He cited to the June 29, 2020 Order in the Commission's COVID investigation, Consolidated Cause Nos. 45377/45380 (at 9-10) ("45380 Order"), which provided: "All jurisdictional Indiana utilities are authorized to use regulatory accounting for COVID related impacts directly associated with any prohibition on utility disconnections, collection of certain utility fees (i.e., late fees, convenience fees, deposits, and reconnection fees), and the use of expanded payment arrangements, as well as COVID related uncollectible and incremental bad debt expense." Mr. Shimansky noted this was precisely the deferred accounting authority sought by the OUCC and, in fact, the OUCC actively opposed further deferred accounting authority. He stated there is no deferred accounting authority for the avoided line locate expense. He also acknowledged that there is no deferred accounting authority for the avoided transportation and conference expense, and Petitioner did not to have offset those savings against the deferred expenses that were specifically authorized.

With respect to Ms. Stull's proposal to lengthen the amortization period for the COVID deferred costs, Mr. Shimansky responded that the costs in this regulatory asset were paid for by Petitioner over a period of around 22 months and Petitioner is not asking to recover interest on these accounts. Mr. Shimansky testified that to recover these costs over five years means Petitioner will be waiting almost nine years (COVID expense began in June 2020 versus end of amortization period of January 2029) with no interest compensation.

4. Discussion and Findings. The 45380 Order authorized regulatory accounting for COVID impacts associated with prohibitions on utility disconnections, waiver or exclusion of certain utility fees (i.e., late fees, convenience fees, deposits, and reconnection fees), and the use of expanded payment arrangements. In that same order, we declined to approve a request for deferral of O&M costs but found utilities could seek cost recovery or other related rate relief through future filings, such as a base rate case. While we recognize that Petitioner deferred certain O&M savings as offsets to the costs authorized to be deferred, we decline the OUCC's invitation to require additional offsets simply because Petitioner voluntarily included some offsets. Consistent with our decision above concerning the amortization of rate case expense, we find these costs should also be amortized over the four-year expected life of Petitioner's approved rates. Therefore, we authorize Petitioner to amortize $383,817 over four years, a figure that includes COVID costs, bad debt expense, and an offset for travel and conference expenses not incurred. Additionally, if the four-year amortization period expires before new rates are approved, Petitioner shall file a new tariff to remove the amortization from rates upon expiration.

M. Amortization - LIPP Expense.

1. OUCC. OUCC witness Stull proposed to amortize deferred costs related to Petitioner's LIPP over five years instead of three. She proposed to amortize the deferred low-income program costs of $77,127 over five years, for a $10,279 decrease to Indiana American's proposed amortization expense of $25,704.

2. <u>INAWC Rebuttal</u>. Mr. Shimansky responded that based on the period over which the discounts for customers through the LIPP program were captured in the regulatory asset and the fact that Petitioner has not sought carrying charges with respect to the deferred amounts, Petitioner's proposed three-year amortization period is appropriate. He also pointed out that it is inconsistent for the OUCC to suggest that the over-collection of the URT repeal revenues be returned immediately with interest but the expenses for LIPP are to be returned over five years with no interest.

3. <u>Discussion and Findings</u>. For the reasons stated above with respect to the amortization period for the deferred COVID costs, we find a four-year amortization period should be adopted. We further find INAWC should file a new tariff to remove the amortization from rates upon expiration if the four-year period adopted herein expires before new rates are approved.

N. <u>Property Tax Expense</u>.

1. <u>INAWC Case-in-Chief</u>. Mr. Cifuentes presented pro forma property tax expense. To calculate the forecasted property tax, he calculated the five-year weighted average of assessed values for 2017-2021 adjusted for the granted personal property assessment obsolescence claims, divided by the UPIS basis amounts for 2016-2020. This quotient provided the ratio of assessment value to UPIS value for real and personal property. The tax rate was calculated by dividing property taxes paid in 2022 by the 2021 assessed values. While property taxes are expensed in the year of assessment, they are paid in arrears. The five-year weighted average ratio of assessed value to UPIS was then multiplied by the December 31, 2024 UPIS to determine 2025 property tax expense. The monthly 2025 property tax expense was then annualized to arrive at the test year pro forma property tax expense (water and wastewater).

2. <u>OUCC</u>. Ms. Stull accepted generally Petitioner's method for forecasting property tax expense. However, Ms. Stull disagreed with Indiana American's use of its estimated property tax assessment as of December 31, 2024 to establish Step 2 property tax expense. She testified that property taxes are based on an assessment conducted on December 31 each year, and the December 31, 2023 assessment will have been the latest assessment as of the beginning of Petitioner's forward-looking test year (Step 2 – May 1, 2024). Ms. Stull testified that Step 2 rates should be based on the assessed value of the property as of the beginning of the test year (the December 31, 2023 assessment). She explained further that only Step 3 rates should be based on the December 31, 2024 assessment.

Ms. Stull noted that Petitioner included utility plant that is not subject to property tax in its property tax expense calculation. She noted the main extension to the Montgomery County Development Zone will be exempt from property taxes and Petitioner only included its net investment of $2,777,506 rather than its total investment of $18,000,000. Ms. Stull explained that property taxes are based on what was constructed and taxing entities do not consider whether plant was contributed in establishing what value is to be taxed. Ms. Stull also noted that while Petitioner is allowed to recover a return on and of its investment in customer-owned lead service line replacements, it does not actually own these assets and therefore does not owe property taxes on this investment. Therefore, Ms. Stull excluded$18,000,000 for the Montgomery County main extension and $22,565,208 for lead service line replacements from her recommended property tax expense.

Ms. Stull also made several recommendations for the computation of property tax expense in future SEI and DSIC cases. She stated Petitioner should use its rate case methodology for purposes of calculating property taxes in these trackers.

3. INAWC Rebuttal. Mr. Shimansky agreed with Ms. Stull that the Montgomery County surcharge assets and customer-owned lead service line replacements should be excluded. He disagreed, however, with her recommendation that Step 2 rates should be based upon the December 31, 2023 assessment. He explained that the test year is the 12 months ending April 30, 2025, and that basing the Step 2 rates on the 2023 assessment will understate the pro forma test year expense. He agreed to her recommendations regarding the calculation of property tax in future SEI and DSIC cases.

4. Discussion and Findings. The primary dispute between the parties is whether to include property tax expense on plant that will be assessed on December 31, 2024 in Step 2 rates as proposed by Petitioner or in Step 3 rates as proposed by the OUCC.

In *Indiana-American Water Co., Inc.,* Cause No. 44022 at 93-94 (IURC June 6, 2012), we addressed a similar issue and referenced our decision in *Ind. Cities Water Corp.*, Cause No. 39166 (IURC July 8, 1992) wherein the utility sought to include an adjustment for plant added between December 31,1990 and May 31,1991. The test year in that case ended June 30, 1990, with a one-year adjustment period and the new plant was assessed for tax purposes on March 1, 1991, even though the tax rate would not be set until 1992 and taxes would not be due until 1993. Because the utility's accrual accounting system recorded property taxes as a liability in the year of assessment (*i.e.*, during the adjustment period), the utility estimated the property tax expense based on the most current tax rate. The Commission included the utility's proposed expense for new plant, finding that estimating the property tax using the most-current tax rate and an assessment made during the adjustment period resulted in a sufficiently fixed, known, and measurable expense.

Although this case is not based on a historical test year and the fixed, known, and measurable standard does not apply, we find it appropriate to consider the tax assessment date and the timing of when the utility's accrual accounting system records the property taxes as a liability. We find it is reasonable to permit recovery of property taxes on assessed plant in the period when the utility accrues the tax in its accounting records. In response to the Commission's August 25, 2023 Docket Entry, Petitioner stated that it will record property tax expense on 2024 investments in January 2025. Because the cutoff date for Step 2 revenues and O&M expenses are through April 30, 2025, we find the amount of property tax expense should be based on plant that will be assessed on December 31, 2024. Accordingly, we find Petitioner's forecasted property tax expense adjustment is $3,749,006 for Step 1 and $2,464,196 for Step 2. Further, we find the OUCC's recommendations regarding the calculation of property tax in future SEI and DSIC cases should be approved.

O. IURC Fee and Gross Revenue Conversion Factor.

1. OUCC. Ms. Sullivan calculated an updated gross revenue conversion factor to reflect the IURC fee that went into effect on July 1, 2023. She also proposed a $134,693 increase to base year IURC fee expense of $275,452 for a total pro forma IURC fee expense of $410,145 utilizing the current 2022-2023 IURC fee of 0.1467603% and applying the fee to the OUCC's proposed operating revenue.[26]

2. __INAWC Rebuttal__. Mr. Cifuentes testified that Petitioner agrees with application of the current IURC fee rate for 2022-2023, but that percentage should be applied to the level of revenue ultimately adopted in this Cause.

3. __Discussion and Findings__. There is no dispute between the parties as to the appropriate IURC fee to use in calculating the gross revenue conversion factor, only in the appropriate level of revenues to which the percentage representing the fee for 2023-2024 should be applied. We find that the IURC fee of 0.1467603% should be applied to the level of pro forma operating revenues at present rates found in this Order. Further, we find the gross revenue conversion factor of 134.5031%, which includes the IURC fee of 0.1467603%, should be applied to the net increase required before gross-up for each phase as found in this Order.

P. __Income Tax Expense__. There were only two disputed issues concerning federal and state income tax expense: (1) the regulatory treatment of the timing difference associated with the repairs deduction, and (2) the appropriate amortization period for EADIT.

1. __Repairs Deduction__.

a. __OUCC__. Ms. Stull recommended a reduction to income tax expense to include Petitioner's repairs deduction in the determination of income tax expense for ratemaking purposes. She explained the repairs deduction represents costs that have been capitalized and included in rate base for book and ratemaking purposes but expensed for tax purposes as allowed by the Internal Revenue Code. Ms. Stull further explained that the adjustment she proposes is only for determining income tax expense for ratemaking purposes and has no effect on the operating expense or rate base.

Ms. Stull testified the tax normalization rules do not prohibit the inclusion of a repairs deduction for purposes of determining income tax expense for ratemaking purposes. Rather, normalization rules pertain to differences in depreciation methodologies and depreciation rates used for book and tax purposes, which are "protected" under the normalization rules. However, she explained, the repairs deduction creates a basis difference which is not protected under the normalization rules. She concluded it is unnecessary for customers to pay rates that include income taxes related to the repair deduction. She did not split the repairs deduction between water and wastewater operations because the amount for wastewater was immaterial and Petitioner's proposed subsidy to wastewater operations is significant.

Ms. Stull stated the ADIT balance at September 30, 2022 includes an amount related to the additional repairs deduction included in American Water's federal income tax return. This historical balance should continue to be included in ADIT. However, Ms. Stull explained that because she proposes to flow through the repairs deduction in the determination of income tax

[26] We note the 0.1467603% is the IURC Fee for the fiscal year 2023-2024.

expense for ratemaking purposes, there will be no difference between book value and tax value (at least for ratemaking purposes) on a going forward basis. Therefore, no additional ADIT should be projected for Petitioner's capital structure in Steps 1, 2, or 3.

Finally, Ms. Stull acknowledged a reduction to the ADIT balance included in Indiana American's capital structure should result from her recommendation. She estimated the effect to ADIT by multiplying her repair deduction by 25% and reducing ADIT accordingly. The effect of her proposed adjustment is a $2,927,966 reduction to ADIT in the Step 2 capital structure and a $9,439,895 reduction to ADIT in the Step 3 capital structure.

b. INAWC Rebuttal. Ms. Ciullo explained the Internal Revenue Service ("IRS") allows an immediate deduction for certain expenditures as repairs which, for regulatory accounting purposes, are capitalized rather than expensed. This creates a timing difference, which Petitioner proposes to normalize over the life of the capitalized asset. The effect of that timing difference is reflected in lower customer rates through the recognition of ADIT, consistent with the Muncie Remand Method as outlined in *Muncie Water Works Co.*, Cause No. 34571, 44 PUR4th 331 (Ind. Pub. Serv. Comm'n Sept. 16, 1981). Ms. Ciullo explained that Ms. Stull's proposal is to instead flow through the tax impacts of the tax repairs deductions because the rates paid by customers include income taxes INAWC will not pay until some future period, which she says unnecessarily increases rates for customers today. Ms. Ciullo explained that Petitioner's current approach of continuing to normalize tax repairs provides stability in customer rates by not having large fluctuations in bills when taxes come due. For the utility, Ms. Ciullo explained, normalization allows the utility to recover costs more evenly over time. She testified that current and future customers benefit from normalization because the timing difference is reflected as a zero-cost source of capital over the life of the underlying asset, which results in a lower authorized net operating income. In contrast, Ms. Ciullo stated, flow-through captures 100% of the benefit of the tax deduction for current customers, leaving none of the benefit for future customers.

Ms. Ciullo testified it is still necessary due to a timing difference to compute ADIT on the tax repairs adjustment under Ms. Stull's approach, since the costs associated with the tax repairs deduction are capitalized for book purposes. Under Ms. Stull's approach, however, a regulatory asset for the ADIT (and gross-up) for income taxes to be paid in the future would be created. Ms. Ciullo testified that changing certain tax expenses from normalization to flow-through adds unnecessary complexity to an already complex tax calculation and could add complexities with other filings, such as the DSIC. Ms. Ciullo stated that, if the capital expenditure qualifies for tax repairs for tax purposes and is treated as a flow through, then as the capital expenditure is depreciated for book purposes, the corresponding book depreciation also needs to be treated as flow-through. Thus, Petitioner would need to separately track any book activity, including retirements associated with the underlying capital, to ensure the full reversal of the regulatory asset created as a result of the flow-through treatment. She also indicated that if the treatment to flow-through was to be changed retrospectively, other considerations would also need to be made.

c. Discussion and Findings. Even though the repairs deduction timing difference has existed for several years, this is the first case where a party has proposed that its effects should be flowed through to customer rates rather than be normalized. While we have not faced this specific proposal with respect to the repairs deduction, Indiana long ago decided that temporary tax timing differences (like the repairs deduction) are to be normalized:

> It has been a long standing practice of this commission to permit utilities, subject to our jurisdiction for rate-making purposes, to utilize normalization accounting principles in regard to timing difference adjustments and investment tax credits.

Muncie Water Works Co., 44 PUR4th 331, 337-38 (quoting *Boone County REMC v. Ind. Pub. Serv. Comm'n,* 239 Ind. 525, 536, 29 PUR3d 409, 159 N.E.2d 121 (1959). The use of normalization accounting principles permits an entity to equalize the tax consequences resulting from timing difference adjustments, such as accelerated depreciation, to taxable income and investment tax credits associated with capital assets over the useful life of the asset. Consequently, when such normalization is utilized for rate-making purposes, the present and future utility customers share such tax consequences equally over the life of the assets that are used to provide the utility service.

Timing differences have been normalized as standard ratemaking practice, in part, because other timing differences in the tax calculation, such as depreciation, would violate IRS normalization rules if flowed through to the ratepayers. Even though the repairs deduction could be flowed through to ratepayers without violating those rules, the additional complexities do not warrant the change proposed by the OUCC. As Ms. Ciullo noted, the corresponding book depreciation would need to be treated as a flow-through if the capital expenditure qualifies for tax repairs and is treated as flow-through. For consistency, the DSIC and other filings would need to be modified as well. Also, while the current method requires ratepayers to pay more income taxes through rates than the utility is required to remit to the IRS immediately, these funds are available to invest in rate base. Thus, the funds represented by deferred income taxes are a source of capital, like debt or equity, for which the utility is not required to pay interest or dividends. Thus, the deferred income taxes are included in the capital structure at zero cost, providing a benefit to the ratepayers.

Normalization relating to timing differences of deductions in tax calculations is a long-standing ratemaking practice. We do not believe a change is warranted due to the additional complexities that will result and because ratepayers receive benefits from the normalization practice. Accordingly, we reject the OUCC's proposal.

2. <u>EADIT</u>.

a. <u>INAWC Case-in-Chief</u>. Mr. Shimansky testified that pursuant to the settlement agreement in Cause No. 45032 S4, EADIT from the Tax Cuts and Jobs Act of 2017 is being returned as an offset against income tax expense using ARAM. Mr. Shimansky explained that the Workpapers for Deferred Income Tax were compiled by the American Water's Tax Department using PowerTax.

b. <u>OUCC</u>. Ms. Stull disagreed with Indiana American's proposed EADIT amortization. She testified that the ARAM used at the time of settlement was approximately 41 years. She objected to INAWC's calculation of ARAM of approximately 74 years, 63 years, and 65 years for Steps 1, 2, and 3, respectively. She asserted that while ARAM will vary from one period to the next, an increase of this magnitude is not reasonable. She stated that Petitioner's workpapers do not provide any useful support for its calculation of EDIT amortization or its calculation of ARAM. While she understands Petitioner used PowerTax to perform the detailed calculations, she said it is incumbent upon Petitioner to provide basic information about the calculation, such as the ARAM used, along with an explanation of why it differs significantly from that used in prior cases.

Ms. Stull stated that while Petitioner cannot amortize EADIT any faster than ARAM without violating normalization rules, she considered the ARAM calculated in this case to be an error. Due to the absence of support in Petitioner's case-in-chief regarding its calculation of ARAM, Ms. Stull based her recommended ARAM on the results of the OUCC's depreciation study, which calculated remaining lives for water plant of 48.99 years, wastewater plant of 28.15 years, and total plant of 48.70 years. Ms. Stull considered an amortization period of 41 years to be a reasonable basis on which to calculate the EDIT amortization.

c. **<u>Industrial Group</u>.** Mr. Gorman proposed that the amortization period to return Indiana EADIT to customers be reduced to three years; and that the full balance of the refund be credited to Petitioner's water customers. He stated that the Indiana General Assembly gradually lowered the Indiana corporate income tax rates beginning in 2012. The current tax rate is 4.90% and the tax rate used in Petitioner's last rate case, Cause No. 45142, was 5.5416%. Mr. Gorman testified this results in Indiana EADIT balances that represent over-collections of deferred tax payments from customers that will no longer be remitted to government taxing authorities due to the change in Indiana tax law. Mr. Gorman proposed the Indiana EADIT credit to customers should be accelerated. He stated the Indiana EADIT can be amortized in accordance with the Commission's discretion and is not required to be refunded using ARAM. He urged the refunding of these deferred tax over-collections to customers as quickly as possible. Mr. Gorman stated the faster the refund to customers means a greater reduction to cost of service that can offset a portion of Petitioner's current proposed rate increase. He also contended that a faster amortization period will result in a more balanced treatment to the current generation of customers, most of whom would have been paying rates that reflect the old tax rate, without creating any detriment to INAWC or its future customers who did not contribute to the EADIT balance. Mr. Gorman proposed a faster amortization of three years, consistent with the proposed three step rate increase. Accelerating the amortization to three years increases the Indiana EADIT amortization expense from $136,087 to $1,508,393, or an increase of $1,372,306.

d. **<u>INAWC Rebuttal</u>.** Regarding the OUCC's disagreement with the portion of Petitioner's EADIT calculation using ARAM, Ms. Ciullo explained that while ARAM is supposed to mimic the average remaining life, it is not intended to be a straight-line calculation. She also noted that the 41 years Ms. Stull uses is based on an estimated calculation that was utilized in the prior rate case, at a time when Petitioner had not completed the implementation of the PowerTax system. Ms. Ciullo explained that PowerTax is the industry software used to compute the full ARAM calculation using detailed records for a more accurate calculation than can be done in Excel. She stated the ARAM calculation is more complex than using a straight-line method and using that method is only appropriate if a utility does not have the appropriate books and records to calculate ARAM. Ms. Ciullo testified that Ms. Stull is comparing an estimate of ARAM calculated prior to PowerTax to the ARAM result produced by PowerTax and the fact that the number has grown materially does not make it unreasonable. It is instead likely the result of using a far more detailed and accurate calculation than was available to Petitioner at the time of the last case. Ms. Ciullo further testified that Ms. Stull's proposal to flow back protected EADIT over a 41-year period even though ARAM is more than 20 years longer unnecessarily risks a normalization violation by giving back the EADIT quicker than under ARAM. This could result in Petitioner no longer being able to utilize accelerated tax depreciation, which would be a severe detriment to both Petitioner and customers.

Mr. Shimansky acknowledged that unlike federal EADIT, the amortization period for Indiana EADIT rests entirely within the Commission's discretion. However, he disagreed with the highly expedited proposal from Mr. Gorman. First, Mr. Shimansky stated the underlying assets that set up this EADIT will continue to depreciate over the life of the assets. In other words, if the EADIT is flowed back over three years but the underlying asset is depreciated over its remaining life, there is a mismatch that contradicts Mr. Gorman's desire to provide more balanced treatment to current customers. Mr. Shimansky urged that if the Commission decides to accept Mr. Gorman's three-year proposal or other expedited proposal, then the order should also include language to change the tariff rate at the end of the amortization. This should include not only the income tax expense but also the capital structure, as fully amortized state EADIT (reflected as zero-cost financing in the capital structure) will increase the overall WACC.

e. <u>Discussion and Findings</u>. We note at the outset that the amortization for both federal and state EADIT were established in the settlement approved by the Commission in its June 24, 2020 Order in Cause No. 45032 S4. The record in that Cause and in the current proceeding reflects that federal protected EADIT could not be amortized using any shorter period than that established using ARAM without risking a normalization violation for federal income taxation purposes. It was understood on a going forward basis that the estimated pass back to customers established in that Cause was always intended to be updated through PowerTax to arrive at the actual ARAM calculation. Any other result would risk a normalization violation for purposes of the Internal Revenue Code. That update has occurred, and the resulting calculation of Petitioner's federal EADIT follows the method established in Cause No. 45032 S4 to avoid a possible normalization violation. The OUCC has made no showing that the ARAM calculation produced by PowerTax is in error. Therefore, we decline to adjust the calculation based on the OUCC's recommendation.

With respect to Indiana EADIT, our conclusion is the same as for the repairs deduction. While the question is one for our discretion, we long ago exercised that discretion and determined that temporary timing differences would be normalized because any other approach would be "out of touch with reality." *Muncie Water Works*, 44 PUR4th at 338. Accordingly, we reject Mr. Gorman's proposal to accelerate the pass back of Indiana EADIT.

11. <u>Net Operating Income at Present Rates</u>. Based on the evidence and determinations made above, we find Petitioner's adjusted test year operating results under its present rates are:

Operating Revenues		$ 284,238,732
Less: Deductions		
Operating and Maintenance		102,213,733
Depreciation & Cost of Removal		81,372,636
Amortization		992,561
General Taxes		21,715,052
Federal Income Taxes		6,889,379
State Income Taxes		2,244,414
Total Deductions		215,427,775
Present Rate Net Operating Income		$ 68,810,957

We find that with appropriate adjustment for ratemaking purposes, Petitioner's annual net operating income under its present rates for water/wastewater service would be $68,810,957. We have previously found that Petitioner's net original cost rate base as of the end of the test year is forecasted to be $1,835,553,713, that Petitioner's WACC is 6.42%, which would produce a return on net original cost rate base of $117,842,548. To this return we add the fair value increment for the Indiana Cities Water Corporation acquisition adjustment of $250,077, calculated pursuant to the methodology that has been utilized in numerous rate cases over the course of the more than twenty years, producing a total fair return on fair value of $118,092,625. Petitioner's current return of $68,810,957 will be insufficient to represent a fair return on the fair value of its rate base. We therefore find that Petitioner's present rates are unreasonable and confiscatory.

12. Authorized Rate Increase and Rate Implementation.

A. INAWC Case-in-Chief. Mr. Shimansky described Petitioner's proposed rate implementation in three steps. INAWC has chosen a test year that will commence a few months after the date of this Order. The first step will take effect upon the issuance of this Order. It will incorporate rate base, capital structure, depreciation, and grossed up return as of a rate base cutoff of July 31, 2023. The first step will also incorporate the annualized level of revenues, uncollectible expense, operating and maintenance expense, amortizations and taxes projected in the link period through December 31, 2023. The second step will incorporate the level of revenues, uncollectible expense, operating and maintenance expenses, amortizations and taxes projected through the test year, combined with rate base, capital structure, depreciation expense, and grossed up return as of the beginning of the test year (April 30, 2024). The third and final step will adjust revenues, uncollectible expense, and certain taxes (IURC fee and state and federal income tax), based upon rate base, capital structure and depreciation as of the end of the test year (April 30, 2025). At each step, INAWC will submit a rate base and capital structure compliance filing to certify that all utility plant reflected in that submission is in service as of that date.

B. OUCC. The OUCC did not object to Petitioner's proposed three-step process. However, Ms. Stull testified that the parties should have an opportunity to review Indiana American's update filings, conduct any necessary discovery, and be afforded meaningful opportunity to respond to the update filings. She said for all steps, Petitioner should certify the plant in service and verify construction costs paid. She also recommended a number of additional submissions be made as part of the rate implementation: (1) filings should compare actual amounts to authorized amounts, with an explanation of variances greater than 5%; (2) rate base should be capped at each step at the amount in the forecast; (3) INAWC should file detailed general ledger information with each step; (4) for Steps 1 and 2, detailed schedules showing comparisons between actuals and "approved" amounts, by account and project number, along with detailed general ledger transactions, which would be followed by a 30-day period for review; and (5) for Step 3, the same as Steps 1 and 2, except that information supporting UPIS as of December 31, 2024 would be submitted by February 1, 2025. The remainder of the test year additions would be submitted by May 31, 2025, with parties having until July 30, 2025 for review. She testified that rates should take effect for all steps upon filing on an interim subject to refund basis.

C. Industrial Group. Mr. Gorman did not oppose the three-step process; however, he testified that multi-step processes are not needed and recommended that rate base be capped at the level approved in this Order.

D. INAWC Rebuttal. Mr. Shimansky testified that the OUCC's recommendations that rate base be capped at the amount authorized in this Order, that rates be put in effect upon submission on an interim basis subject to refund, and that a hearing be scheduled to resolve any disputes are consistent with past practice and is acceptable. He also testified that the 30-day period to submit objections is also acceptable. He agreed to an earlier submission of calendar year end data but stated that with year-end close it would be difficult to meet the proposed February 1 date and March 1 would be more realistic. He otherwise objected to the new additional requirements proposed by Ms. Stull. He testified that the Commission should not impose any reporting obligations different than those imposed in any other future test year case. He testified that no compelling reason has been offered for the additional layers of reporting she has requested and that it would be inefficient.

E. Discussion and Findings. The Commission approves Petitioner's unopposed three-step increase, with Step 1 taking effect as soon as possible after the issuance of this Order for service rendered after approval of the tariffs by the Commission's Water/Wastewater Division and based upon actual rate base and capital structure as of July 31, 2023. Step 2 rates will take effect on or about the beginning of the test year, based upon the rate base and capital structure as of May 1, 2024. Step 3 rates will take effect on or about the end of the test year, April 30, 2025, and based upon the end of test year rate base and capital structure. Step 3 rate base will be capped at the net original cost rate base we have found herein to be appropriate, with any amounts in excess of the cap being eligible for inclusion in other rate or tracker proceedings. All three steps will take effect on an interim subject to refund basis upon submission of the compliance filing described herein. The parties to this proceeding will have 30 days to submit any objections to the compliance filings for Steps 1 or 2 and 60 days for Step 3.

The OUCC took issue with the date for submission of rate base update as of December 31, 2024, and recommended capping the Steps 1 and 2 rate base figures and including specific additional information with the compliance filing. We agree with INAWC witness Shimansky that year-end closing may pose problems for a February 1 submission, and so we find a March 1 submission to be satisfactory. As to the other information the OUCC requests be submitted with its compliance filing, this case presented complex issues involving rates, cost of service, and rate design. Thus, to verify and ensure adherence to the Commission's findings herein, a technical conference may be convened as needed for Petitioner to explain its compliance filing.

Accordingly, we find that at each of the three steps, Indiana American shall submit a certification of its actual utility plant in service and actual capital structure as part of its compliance filing broken out between water, wastewater, and corporate. The compliance filing will calculate rates for the applicable step based upon these certifications for water and wastewater, subject to the approved rate base at the conclusion of the test year found herein. All supporting schedules should be provided in Excel format with formulas intact. The rates shall take effect upon submission subject to the rights of parties to submit an objection to the compliance filing as previously found herein. If necessary to resolve any objections, we will schedule a hearing. However, within a week of Petitioner's compliance filing, a technical conference may be held at the request of either a party or Commission staff to allow for further discussion in determining whether Petitioner's filing complies with this Order and to determine what additional information, if any, should be provided for Step 2 and Step 3's compliance filings. We find this process is reasonable and consistent with the process that has been used and worked well in our other future test year cases.

Based on the evidence presented and subject to the approved compliance filing process, we find that Petitioner should be authorized to increase its rates and charges in three steps, calculated to produce combined additional operating revenue of $66,285,371 at the conclusion of the test year, resulting in total operating revenue of $350,524,090. This revenue is reasonably estimated to afford Petitioner the opportunity to earn net operating income that is no more than the fair return of $118,092,625 that we have found to be appropriate, based upon projected test year end rate base and capital structure. The rate increase shall take place over the three steps we have described and, subject to the compliance filings, shall be calculated to produce total company operating revenues and net operating income at each step as follows:

Step 1	
Operating Revenues	$ 306,800,457
Less: Deductions	
Operating and Maintenance	95,939,457
Depreciation & Cost of Removal	67,318,612
Amortization	354,326
General Taxes	19,188,815
Federal Income Taxes	16,957,543
State Income Taxes	4,716,632
Total Deductions	204,475,385
Net Operating Income	$ 102,325,072

Step 1	
Original Cost rate Base	$ 1,614,354,213
Times: Weighted Cost of Capital	6.32%
Net Operating Income Required for	
Return on Rate base	102,027,186
Add: Fair Value Increment - Indiana Cities	297,880
Net Operating Income Required	102,325,066
Less: Adjusted Net Operating income	83,782,736
Net Revenue Increase Required before Gross-up	18,542,330
Gross Revenue Conversion Factor	134.5031%
Recommended Revenue Increase	$ 24,940,009
Divided By: Revenues Subject to Increase	$ 278,883,818
Recommended Percentage Increase	8.94%

Step 2		
Operating Revenues	$	326,266,908
Less: Deductions		
Operating and Maintenance		102,589,675
Depreciation & Cost of Removal		72,258,258
Amortization		992,561
General Taxes		21,776,181
Federal Income Taxes		17,663,414
State Income Taxes		4,888,792
Total Deductions		220,168,881
Net Operating Income	$	106,098,026

Step 2

Original Cost rate Base	$ 1,679,732,875
Times: Weighted Cost of Capital	6.30%
Net Operating Income Required for	
Return on Rate base	105,823,171
Add: Fair Value Increment - Indiana Cities	274,851
Net Operating Income Required	106,098,022
Less: Adjusted Net Operating income	93,393,359
Net Revenue Increase Required before Gross-up	12,704,663
Gross Revenue Conversion Factor	134.5031%
Recommended Revenue Increase	$ 17,088,166
Divided By: Revenues Subject to Increase	$ 305,965,938
Recommended Percentage Increase	5.58%

Step 3

Operating Revenues	$ 350,524,090
Less: Deductions	
Operating and Maintenance	102,806,656
Depreciation & Cost of Removal	81,372,636
Amortization	992,561
General Taxes	21,811,463
Federal Income Taxes	19,989,553
State Income Taxes	5,458,591
Total Deductions	232,431,459
Net Operating Income	$ 118,092,631

Step 3	
Original Cost rate Base	$ 1,835,553,714
Times: Weighted Cost of Capital	6.42%
Net Operating Income Required for	
Return on Rate base	117,842,548
Add: Fair Value Increment - Indiana Cities	250,077
Net Operating Income Required	118,092,625
Less: Adjusted Net Operating income	100,057,961
Net Revenue Increase Required before Gross-up	18,034,664
Gross Revenue Conversion Factor	134.5031%
Recommended Revenue Increase	$ 24,257,183
Divided By: Revenues Subject to Increase	$ 323,054,105
Recommended Percentage Increase	7.51%

13. Depreciation Study.

A. INAWC Case-in-Chief. Mr. Kennedy presented full and comprehensive depreciation studies of Petitioner's water and wastewater plant in service as of December 31, 2022. Pet. Ex. 12, Attachments LEK-2 and LEK-3. Mr. Kennedy concluded that INAWC's requested depreciation rates, resulting in a composite depreciation rate related to water of 2.88% and related to wastewater of 4.53%, reasonably reflect the annual consumption of the undepreciated service value of the utility plant in service. The new rates would take effect upon approval of Step 1 rates in this Cause and thus would affect net original cost rate base at Steps 2 and 3.

The water depreciation study results in a depreciation rate related to Structures and Improvements of 1.94%, Transmission and Distribution plant of 2.59%, and a depreciation rate related to General Plant of 9.34%. Mr. Kennedy compared these rates to the current rates for each functional group. He testified that one significant cause of the change in depreciation rates is the change in average service life of many of the accounts. The average service life was shortened for 13 accounts and lengthened for 16 accounts, based on the detailed analysis presented in Mr. Kenney's report. In addition, Concentric completed a review of the net salvage requirements related to the water assets. He presented a summary of the proposed net salvage estimates compared to the currently used estimates, demonstrating the more negative net salvage requirements in 7 accounts and the less negative net salvage requirements in 17 accounts.

The wastewater depreciation study results in a depreciation rate related to Structures and Improvements of 4.97% and Collecting, Treatment and General Plant of 4.43%. Again, he noted one of the significant causes of the change in wastewater depreciation rates was the change in average service life of many of the accounts, with the shortening of the average service life of 2 accounts and the lengthening of the average service lives in 5 accounts. A more negative net salvage requirement was estimated for 3 accounts.

Mr. Kennedy testified that the average service life of many asset classes is lengthening throughout North America due in part to the increased focus of utilities in maintaining and life extending the infrastructure. However, at the same time as there has been a trend toward lengthening average service lives for some asset classes, Mr. Kennedy stated it has become common for there to be a shortening in other asset class, due in part to the quickening pace of technological change. For example, the pace of technological change in metering assets has resulted in the life of metering classes to be shortened industry wide.

Mr. Kennedy explained that his study calculates the annual and accrued depreciation using the Straight-Line Method and Average Life Group Procedure for most accounts. For certain general plant accounts, the annual and accrued depreciation are based on amortization accounting. Both types of calculations were based on original cost, attained ages, and estimates of service lives. Mr. Kennedy testified that the depreciation rates calculated in this study were calculated in the same manner as used in the prior full depreciation study—however, the calculation of the composite remaining life for the account as a whole has been slightly modified in this depreciation study.

B. OUCC. Mr. Garrett recommended several adjustments to Petitioner's proposed depreciation rates based on different service life estimates for several of Petitioner's water transmission and distribution accounts. His proposed depreciation rate adjustments would result in a $6.9 million decrease to Petitioner's proposed total annual depreciation accrual of $69.3 million. Mr. Garrett described the processes he employed to determine his proposed adjustments to Petitioner's depreciation rates. He explained the "curve-fitting process" in which the best Iowa curve is selected to fit the observed life table curve through a combination of visual and mathematical curve-fitting techniques, as well as professional judgment. He testified that mathematical fitting is an important part of the curve-fitting process because it promotes objective, unbiased results, particularly when there is sufficient data available. Mr. Garrett stated that for each of the accounts to which he proposed adjustments, Petitioner's proposed average service life, as estimated through an Iowa curve, is too short to provide the most reasonable mortality characteristics of the account. He asserted his proposal is generally based on the objective approach of choosing an Iowa curve that provides a better mathematical fit to the observed historical retirement pattern derived from Petitioner's plant data, in addition to applying judgment to the analysis. The eight accounts to which Mr. Garrett proposed adjustments include: Account 306.000 – Lake, River, and Other Intakes; Account 320.200 – Water Treatment Equipment – Filter Media; Account 333.000 – Services; Account 334.100 – Meters; Account 334.110 – Meters – Bronze Case; Account 334.130 – Meters – Other; Account 334.131 – Meter Reading Units; and Account 334.200 – Meter Installations.

C. INAWC Rebuttal. Mr. Kennedy explained that in his study, he followed a process of estimating service lives which starts with compiling historical data for the plant accounts or depreciable groups and analyzing this history using a similar process to that used by Mr. Garrett. However, rather than stopping at that point, Mr. Kennedy further considered additional information, including that gained from operational staff interviews, which provides critical information related to the reasons for past retirements and the expected future causes of retirement. For example, in addition to the on-going retirement of plant due to physical forces, Mr. Kennedy testified that significant future retirements may be caused by obsolescence resulting from the introduction of increased technology into some asset accounts and due to changing economic considerations. The combination of the historical experience and the estimated future considerations yield survivor curves from which Mr. Kennedy's average service lives were derived. His average service life estimates were then tested against the approved average service life estimates of similar water utilities.

Mr. Kennedy walked through the bases for his selection of the Iowa curve estimates for each of the eight accounts where he and OUCC witness Garrett disagreed on the average service life or Iowa curve dispersion estimate.

D. <u>Discussion and Findings</u>. Ind. Code § 8-1-2-19(b) and (c) provide that:

> (b) The Commission, from time to time, shall ascertain and determine the proper and adequate rates of depreciation of the several classes of property of each public utility. Depreciation rates under this subsection shall be calculated to recover a reasonable estimate of the future cost of removing retired assets of the public utility.
>
> (c) A public utility's rates, tolls and charges shall be such as will provide the amounts required over and above the reasonable and necessary operating expenses, to maintain such property in an operating state of efficiency corresponding to the progress of the industry. . . .

Both Petitioner's witness Kennedy and OUCC's witness Garrett cited the foundational text, *Depreciation Systems*, which cautions against removal of judgment from the fitting process and blind acceptance of mechanical fitting processes. The cited material goes on to state that "the results of the mathematical fitting should be checked visually and the final determination of the best fit determined by the analyst." Pet. Ex. 22 at 4 (internal citations omitted). Based on the evidence presented, we find the process used in Mr. Kennedy's average service life estimates was more rigorous and complete than that employed by the OUCC. Furthermore, of the eight accounts for which Mr. Garrett recommends a change, three are for meters: Account 334.100 – Meters, Account 334.110 – Meters – Bronze Case, Account 334.130 – Meters – Other. We agree with Mr. Kennedy that the pace of technological change in metering assets has resulted in the life of metering classes to be shortened. We find Petitioner's requested depreciation rates reasonably reflect the annual consumption of the undepreciated service value of the utility plant in service. We find the use of the depreciation rates as presented in INAWC witness Kennedy's report, by account, will provide for an appropriate amount of depreciation expense in Petitioner's revenue requirement. Therefore, we find that the proposed depreciation rates set forth in the Petitioner's depreciation study should be adopted by the Commission for regulatory purposes as well as by Petitioner for financial reporting purposes.

14. <u>Affordability</u>.

A. <u>INAWC Case-in-Chief</u>. Mr. Prine testified Petitioner's proposed rate increase is primarily driven by the need to make expenditures necessary to keep water and wastewater service safe and reliable. He stated such expenditures cannot be avoided indefinitely and are in the long-term best interests of customers to avoid the possibility of even more increased costs. Mr. Prine stated, as an example, where mains are not replaced in a timely fashion or equipment is neglected, costs rise as unanticipated main breaks can create water quality issues, unexpected expenses, and disruption to the communities served. He testified that because of the importance for service to remain affordable, Petitioner evaluated the customer impact of the proposed rate increase and performed an affordability analysis under the proposed rates. Mr. Prine described ways in which INAWC maintains the affordability of its water service, including continuously seeking to improve business processes and making investments that improve operational efficiencies. He stated Petitioner leverages the power of its organization to share learning on best practices and purchase equipment and supplies at advantageous terms.

Mr. Prine identified two proposed changes to Petitioner's water service rate design for customers who might face affordability issues: (1) an allowance-based rate for all water service customers, and (2) a Universal Affordability Tariff to further address the affordability of water service for vulnerable customers. He explained that an allowance-based rate will enhance the affordability of Basic Water Service, especially for the more economically vulnerable customers, without the need for these customers to directly apply for assistance. He stated an allowance-based rate design improves the affordability by reducing monthly bills for lower monthly usage amounts (which tend to equate more to Basic Water Service) and increasing monthly bills for higher monthly usage amounts (which tend to equate more to discretionary seasonal water use). Even with an allowance-based rate design, Mr. Prine acknowledged that affordability of service may still be an issue for the most vulnerable customers. Therefore, Petitioner is proposing a Universal Affordability Tariff to help the estimated 54,000 residential water service customers with household incomes at or below 150% of the federal poverty level. He stated the discount offered under this tariff would reduce a typical Basic Water Service bill for a three-person household from $58 per month to $40 per month, which is a discount of 30% on the total bill and is less than what these customers would pay for Basic Water Service under current rates.

INAWC witness Rea stated Petitioner's affordability analyses shows that INAWC's investment practices and management of its water and wastewater systems are in the long-term best interest of its customers; and Petitioner's affordability analysis also is a direct measure of the benefits that customers gain from Petitioner's prudent management of the system. Mr. Rea explained that Petitioner assesses affordability of water and wastewater service by comparing annual bills for water and/or wastewater service to household income. He stated that for the broader residential customer base, the most commonly available household income measure is Median Household Income ("MHI"), which can be measured at a community level and is paired with a data set that provides the number of customers served in each community to arrive at a weighted number that represents MHI for Petitioner's entire service territory. At a more detailed level, individual household income is considered, and affordability can then be assessed across a range of households based on their income levels and bills for water and/or wastewater service. Mr. Rea explained that a variety of household income data is available from the U.S. Census Bureau through the American Community Survey ("ACS") at the state, county, and community levels. He presented Petitioner's affordability study for water service and the affordability study for wastewater service in Petitioner's Exhibit 5, Attachments CBR-1 and CBR-2, respectively. He explained that for water service, Petitioner performed an Enterprise-Level Analysis and a Community-Level Analysis. For wastewater, only a Community-Level Analysis was provided, as there is not enough historical data.

Mr. Rea described the Enterprise-Level Analysis, which is a historical comparison of average monthly bills to MHI for Petitioner's residential customers over the last ten years. The metric used to describe affordability is the Bill-to-Income ("BTI") Ratio, which is defined as annual water bills divided by estimated annual household income. The MHI for Petitioner's service territory is a weighted average of the number of customers Petitioner serves in each community in the service territory and the median household income in each of those communities for owner-occupied and single-unit renter occupied homes as reported by data in the ACS based on the most recent year's available data (2021). The relationship between this service territory specific figure and the MHI for the State of Indiana for 2021 (also provided at the community level through the ACS) was then applied to historical MHI data for the State of Indiana to arrive at historical MHI data for the INAWC service territory. Mr. Rea testified that a benchmark for affordability expressed as a total bill's percentage of MHI is a policy decision; however, bills less than 2.0% or 2.5% of MHI for water service and 4.0% to 4.5% of MHI for combined water/wastewater service are considered "affordable" by some. He said the overall BTI Ratios for water service have improved over the last decade and is expected to be 0.76% under Petitioner's proposed Step 3 rates in this case, which is below the thresholds considered to be the high-end limit of affordability for residential customers at the system wide level.

Mr. Rea described the Community-Level Analysis as a deeper dive into affordability at a local level across different customer demographics and proposed rates for each community that Petitioner serves. For purposes of the affordability analyses, Mr. Rea said Petitioner used the concept of Basic Water Service to represent a water usage level that reflects water consumption provided for basic human services (cooking, cleaning, sanitation, and general health requirements), which is then assumed to be constant from month-to-month and not subject to significant seasonality or weather condition. Mr. Rea stated Petitioner defined Basic Water Service for purposes of the affordability analysis to be 40 gallons of water per household member per day based upon relevant literature and a review of residential billing data in months with minimum levels of discretionary water usage. The Community-Level Analysis showed that 84% of residential customers can expect to see bills for Basic Water Service less than 2% of their household income. Petitioner estimated there are approximately 47,500 residential water customers that will see bills for Basic Water Service above 2% of their household income, which is approximately 16% of the total customer population.

Mr. Rea testified that affordability of service is not uniform across Petitioner's service territory because household income can vary significantly across its service territory. He said Indiana American has diverse service territories and serves customers in urban, suburban, and rural communities. He explained that assessing affordability information for the entire residential customer population can demonstrate whether customers in general are having or would have difficulty paying their water bills under Petitioner's current or proposed tariff structure and inform decision-makers about the size and scope of efforts that may be needed to help these vulnerable customers better afford water and wastewater service.

Mr. Rea concluded that Petitioner's water service has been, is, and is expected to continue to be affordable for the majority of its residential customers, including under the proposed rates, but also that there are groups of customers for whom affordability of water service may be challenging.

B. **<u>OUCC</u>.** Mr. Bell expressed concern about the immediate financial impacts of Indiana American's requested rate increase. Mr. Bell advised the Commission that state policy for investment in infrastructure also requires decision-makers to recognize how infrastructure projects affect the affordability of utility services for present and future generations of Indiana citizens. He noted that Indiana American seeks approval of water rates that are 55% higher overall than the rates approved in 2019 and the requested wastewater rates are 106% higher. Mr. Bell noted that through DSIC and SEI trackers Petitioner has already increased rates to water customers by approximately 17.69%. Mr. Bell recommended the Commission consider the affordability of Indiana American's existing and proposed rates.

Mr. Bell stated that safe and reliable water and wastewater systems are critical to basic human needs but noted customers are faced with increasing utility costs and other cost of living increases due to inflation. He suggested that in recognition of the importance of affordability, Indiana American could seek a lower and more reasonable ROE, lower the equity portion its capital structure to establish a more reasonable 50/50 debt to equity ratio, moderate the growing level of capital expenditures, and reduce the corporate overhead costs being allocated to Indiana American. He explained that these actions could lower the proposed rate increase and lessen the financial impact to customers.

Mr. Bell believed Indiana American's affordability analysis recognizes Petitioner's rates have risen to the point where a significant number of its customers can no longer be expected to afford its water services without financial assistance, which it proposes come from its own residential customer base. Mr. Bell compared Indiana American's rates with various other water utilities in the state and concluded that Indiana American has the most unaffordable rates when compared to those other water utilities.

Mr. Compton stated that the OUCC does not consider 2% of household income to be an appropriate threshold to measure affordability. He also disagreed that Indiana American's water customers have a higher MHI than the statewide MHI. Mr. Compton stated the inputs Petitioner chose to calculate its customers' MHI understate the number of customers that will have a higher BTI than 2%. He identified three reasons for his disagreement with Petitioner's methodology. First, Petitioner's disregard of the ACS data is based on the faulty premise that we should ignore the effect of rate increases on indirect customers (i.e., customers that receive and pay for water service but do not have a direct relationship with the utility, such as renters). Second, in the absence of reliable data, further assumptions that mutate the integrity of the data should not be made. And third, excluding indirect customers naturally skews the results of affordability making Petitioner's water appear more affordable because statistically, households who rent generally have lower income.

Mr. Compton testified that Petitioner did not appropriately calculate for the BTI ratios. Mr. Compton explained Petitioner calculated the average bill by taking each year's revenue amounts and dividing by each year's respective customer count. However, in its calculation of revenues, Petitioner only included revenue generated from metered and unmetered sales to calculate the average bill. Petitioner did not include revenues generated by public or private fire protection charges. Mr. Compton presented his own calculation of the MHI for water customers using

Petitioner's methodology but including indirect customers. Mr. Compton calculated an overall MHI of $62,650 as compared to Petitioner's calculation of $69,151.

Mr. Compton noted that Petitioner's analysis for the wastewater model is identical to the water model other than using different ACS data. Using the same methodology Mr. Compton used to calculate the MHI for Petitioner's water customers, he calculated a MHI for Petitioner's wastewater customers of $65,504 as compared to Petitioner's calculation of $70,323.

Mr. Compton criticized Petitioner's use of a five-year estimate of household income data from the ACS, stating that to evaluate future affordability, a historical affordability analysis is not appropriate and the comparative data, if possible, should be more current. Mr. Compton testified that since the ACS does not provide current estimates for some communities in which Petitioner serves, it calls into question the usefulness of performing this kind of affordability analysis.

C. **Crown Point.** Mr. Guerrettaz opposed the proposed rates for Crown Point and SFR customers in general, stating the proposed rates and charges would be excessive and unreasonable.

D. **CAC.** Mr. Inskeep testified that Petitioner's analysis shows that its proposed rates will not be affordable for customers. He challenged Petitioner's proposed definition of Basic Water Service at 40 gallons per household member per day, instead urging that it be replaced with the total average bill (4,050 gallons per month). He recommended that the Commission take note of the sizeable population of Hoosier families who will not be able to afford Petitioner's proposed rate increase. Mr. Inskeep recommended the Commission act to significantly reduce the overall requested revenue requirement and approve proposals that will increase the affordability of essential water and wastewater service, like the Universal Affordability Tariff.

E. **INAWC Rebuttal.** Mr. Rea testified that the question of affordability of service is not simply a yes or no question but a continuum, as shown by Petitioner's Community-Level analysis. He stated there will always be customers for whom water service is more affordable than for others depending on demographics and income levels. Petitioner's Community-Level analysis shows that for a large majority of customers, Basic Water Service is expected to be less than 2% of household income (the benchmark Petitioner is using at the individual customer level) at Petitioner's proposed rates, but there are customers for whom Basic Water Service is expected to be more than 2% of household income. This is the target population that Petitioner's Universal Affordability Tariff is intended to address.

Mr. Rea disagreed with OUCC witness Bell that INAWC rates have reached a tipping point where a significant number of its customers can no longer be expected to afford water services. He stated the percentage of household income taken up by Petitioner's average water bills over time has gone down, not up and the BTI Ratio measured at the MHI level under Petitioner's proposed rates is consistent with levels seen historically. Mr. Rea testified that under Petitioner's proposed rates, Basic Water Service is expected to take up less than 2% of household income for 84% of Petitioner's residential customers. Basic water service is expected to take up more than 3% of household income for approximately 9% of Petitioner's residential customers before applying any discounts associated with the proposed Universal Affordability Tariff.

Mr. Rea testified that the terms household income and median household income are not interchangeable. He explained that Petitioner's Enterprise-Level analysis used MHI as the income component of the affordability comparison because it is broad based, easily available, and is available for multiple years of history, which lends itself well to a consistent longer-term historical analysis. Mr. Rea stated Petitioner's Community-Level analysis is not based on MHI, but instead on household income measured at the individual household level, using 2% of household income (not median household income) as a benchmark to estimate the numbers of customers where Basic Water Service is expected to take up differing percentages of household income. Petitioner proposed the Universal Affordability Tariff to address those customers.

Responding to the OUCC's criticisms of his affordability analysis, Mr. Rea stated that it is appropriate for the analysis to concentrate on direct customers because: (1) the use of an MHI statistic, which best estimates household income for Petitioner's direct customers, is consistent with the calculation of the average bill, which is also based on direct customers; and (2) for Petitioner's indirect customers (e.g., renters in multi-family buildings) it is impossible to know what these households pay in rent for water service. He further stated that even if, as Mr. Compton asserts, calculations of MHI for the communities that Petitioner serves would be lower if all rental households were included, then water consumption and total bills for rental households would also be lower than the average bills and consumption for the residential class in total. He said this is true because (1) households that rent are smaller than households that own their home, meaning consumption is likely to be lower, and (2) where there are multiple households within a single building behind a single meter, each individual customer's share of the total meter charge would be less than it would be if they were in the home where water service was only serving them.

With respect to the average bill calculation not including revenues associated with public and private fire protection charges, Mr. Rea responded that private fire service charges are not charged to residential customers. As for public fire protection, Mr. Rea explained that it is only when the unit of local government so elects that the costs of public fire service are recovered directly from water customers through public fire surcharges. Mr. Rea also stated the charges are not large enough to fundamentally change the trend of improving affordability over time that Petitioner's Enterprise-Level analysis shows.

Mr. Rea agreed with Mr. Compton that there are differences between the ACS five-year data set and one-year data sets, but he rejected the suggestion that the five-year data is somehow biased because it is older. Mr. Rea presented a comparison of household income estimates from the ACS one-year and five-year data sets, which showed that there is no significant difference between the two data sets regarding estimates of household income. Mr. Rea testified that use of the ACS five-year data set is appropriate because it provides current estimates of household income and provides that information for all communities in Indiana, which is important in developing a comprehensive affordability analysis across the entire service territory.

Mr. Rea disagreed with Mr. Bell's bill comparison and conclusions. He testified the comparison is of little practical use due to fundamental differences in water utility structure, ownership, operations, and customer bases. He stated there are significant differences that can help to explain in part the differences between Indiana American's typical bills and typical bills for other service providers, such as the existence of natural subsidies for customer rates of municipal utilities through tax and other policies. Mr. Rea also listed a number of operational differences between Indiana American and other service providers that can lead to significant differences in bills, including the nature of Petitioner's service territory, significant differences in investment levels and strategies, and rate structures.

F. Discussion and Findings. Affordability is always an important consideration for the Commission when establishing just and reasonable rates. Affordability is an ongoing concern for all consumers in the State of Indiana. However, our role in addressing this concern is not to reach a conclusion as to whether the rates approved herein are "affordable" for each and every customer, particularly given the difficulty in defining affordability in general and for the many diverse customers and communities Indiana American serves.

Pursuant to Ind. Code § 8-1-2-46(c), Petitioner has proposed rate design solutions utilizing an allowance-based rate and a proposed Universal Affordability Tariff to address the issue of affordability of utility service for customers. While the OUCC took issue with various data and assumptions in Petitioner's affordability analysis, such as the appropriate affordability benchmark and INAWC's consideration of indirect utility customers, Petitioner's analysis does provide us with information in considering its proposals (each of which is discussed in greater detail below). Additionally, we note that despite the parties' disagreement with Petitioner's affordability analysis, the evidence also shows general agreement among the parties that Indiana American provides water service to customers for whom affordability of service is an issue. *See* Pub. Ex. 5 at 12; CAC Ex. 1 at 18-20, 25.

We also recognize that the OUCC and several Intervenors expressed concern with the general affordability of Indiana American's proposed rates and offered alternatives for lowering rates for certain classes of customers, low-income customers, and all customers. To the extent those suggestions include aspects of Petitioner's proposed rates, such as rate design, cost of service, and ROE, those suggestions are addressed in other sections of this Order.

15. Cost of Service Study and Rate Design.

A. Cost of Service Study.

1. INAWC Case-in-Chief. Mr. Rea presented Petitioner's COSS for water service. He testified Petitioner used the Base/Extra Capacity method outlined in the AWWA M1 Manual titled "Principles of Water Rates, Fees, and Charges" to allocate production and distribution costs to customer classes. The revenue requirement for various cost categories was allocated to the following customer classes: residential, commercial, industrial, public authorities, sales for resale, private fire service, and public fire service. Different cost categories were allocated to customer classes using a class allocation factor that differs depending on the nature of the costs. The cost categories Petitioner used to group individual accounts were variable cost, capacity cost (including source of supply, water pumping, water treatment, transmission mains, distribution mains, and storage), metering cost, service line costs, customer service costs, and fire hydrants.

2. OUCC. Mr. Mierzwa addressed Petitioner's water COSS. While he generally agreed with Petitioner's use of the Base/Extra Capacity methodology, he recommended adjustments to the maximum hour extra capacity factors developed for the industrial and SFR customer class. He also recommended modifications to Petitioner's assignment of main costs to the transmission and distribution functions. Mr. Mierzwa presented a revised COSS for water that reflects his recommended adjustments and modifications. Mr. Mierzwa testified the extra capacity factors proposed by Petitioner for the industrial and SFR classes unrealistically assume that the usage of each of these classes is exactly the same in every hour of every day of the maximum month of usage. He stated it is unclear why Petitioner is able to use its AMI system to determine maximum hour extra capacity factors for the residential, commercial, and public authority classes but not for the industrial or SFR classes. Mr. Mierzwa recommended application of the AWWA M1 Manual estimated hourly ratios to the maximum day capacity factor developed by Petitioner for the industrial and SFR customers. This would increase the maximum hour capacity factor for the industrial class from the 1.20 to 1.60 and would result in a SFR maximum hour capacity factor of 2.32.

Mr. Mierzwa testified it is unreasonable to assign mains costs to the transmission and distribution functions based on mileage as Petitioner has done because it fails to recognize that the costs of purchasing and installing mains generally increase as the main diameter increases. He recommended that mains be assigned to the transmission and distribution functions based on the weighted installed costs of those mains.

3. **<u>Industrial Group</u>.** Ms. York identified numerous issues regarding Petitioner's COSS model, which led her to conclude that the COSS model is inaccurate and should not be relied on to guide revenue apportionment. Ms. York stated that INAWC has not conducted a reasonable comparison of the results of its new, pared down COSS model to the more detailed model that has been used in prior rate cases. She testified the new COSS model includes significant changes regarding the functionalization, classification, and allocation of costs, relative to how those steps were taken in the prior model, and that these changes have not been adequately explained or justified by INAWC. Specifically, Ms. York stated that INAWC's new COSS model fails to demonstrate the details of how each cost is classified before it is allocated across customer classes. Furthermore, she stated that regulators in other jurisdictions, such as Illinois and Missouri, have criticized similar COSS models set forth by American Water affiliates in those jurisdictions. Ms. York identified certain adjustments to the proposed COSS in an attempt to improve the accuracy of Petitioner's measurement of each class's cost of service. However, Ms. York stated that given that INAWC's COSS model obscures important information, even with her adjustments, there may be other functionalization, classification, and allocation issues that are not readily identifiable and could alter the outcome of the COSS. Because the COSS model cannot be adequately validated, Ms. York recommended the use of an across-the-board rate increase.

Ms. York further testified that even if INAWC's COSS model were found to be reliable, she has other concerns with the bases used to functionalize certain costs. For example, Ms. York emphasized Petitioner's failure to accurately functionalize transmission and distribution costs. She testified there is no evidence to support Petitioner's projected test year split of length of mains between transmission and distribution, or the associated split of costs to those functions in its COSS. She cited a lack of accurate information about the actual level of investment since the last rate case in support of her proposal that the split in calendar year 2022 as being the most reliable historical data available. Even then, without determinative evidence that the length of main is an accurate proxy for the allocation of transmission and distribution costs between the transmission function and distribution function, Ms. York characterized this split is, at best, an approximation.

Ms. York also objected to the manner in which certain costs were allocated to customer classes within Mr. Rea's COSS. In particular, she disagreed with Petitioner's use of Factor 1 to allocate purchased power expenses associated with source of supply and water treatment. She stated that purchased power costs are incurred to pump water to meet both the base and extra capacity demands of the rate classes. Therefore, Ms. York stated, Factor 1 does not accurately allocate purchased power costs to the customer classes that drive the electric demands for pumping, which in turn causes Petitioner to incur the purchased power costs. She stated Factor 2 is a more appropriate allocator because it reflects both average flow and maximum-day demand requirements.

Ms. York objected to the distribution multiplier for the industrial class of 0.50, recommending that INAWC should consider the length of distribution mains serving the industrial customers (in addition to the usage served by distribution mains), as it may only represent a small fraction of the total length of distribution mains on the system. Thus, she recommended an adjustment to the distribution multiplier to reflect the actual portion of industrial class usage that is served by distribution mains based on Petitioner's evidence.

Ms. York objected to Petitioner's approach of not allocating any source of supply or water treatment costs to private fire or public fire classes, which differs from INAWC's approach in its prior rate case COSS model. She recommended that a portion of source of supply and water treatment costs be allocated to the public and private fire classes, consistent with the methodology used in the prior rate case, because production capacity is in part based on the need to maintain adequate fire protection. As noted in the AWWA M-1 Manual, a significant portion of extra capacity costs can be allocated to fire protection when distributing costs to customer classes. Ms. York explained the service provided is principally of a standby nature—that is, readiness to deliver relatively large quantities of water for short periods of time at any of a large number of points in the water distribution system. In the absence of better estimates of test year annual usage for private and public fire service, Ms. York recommended using the same usage data for fire classes as was used in the COSS model in Cause No. 45142.

4. Wholesale Customers. Mr. Callocchia recommended rejection of INAWC's COSS based on a lack of justification or explanation for the change in methodology from INAWC's previous rate case and the inadequacy of supporting data for certain cost allocations. Mr. Callocchia stated the two-step COSS approach was significantly different from the single-step COSS approach used in Petitioner's previous rate case and produces radically different results without justification or explanation. He referenced challenges to the two-step COSS approach in cases brought by INAWC affiliates Illinois American Water and Missouri American Water. He testified that an alternative approach to cost allocation in this case would be to implement any approved increase in revenue requirements across-the-board to each customer class.

Mr. Callocchia also contended that the COSS does not properly recognize the unique characteristics and service demands of the SFR class and inappropriately allocates costs to SFR customers that are not incurred in the provision of service to SFR customers. Specifically, it does not adjust for system wide water loss, lacks proper justification for the allocation of transmission costs to SFR customers, and assigns revenue requirements to SFR customers that are not caused by or provide any benefit to SFR customers. He contended that it costs INAWC significantly less to serve SFR customers because service to SFR customers involves delivering treated water to master meters connected to INAWC's transmission main and INAWC is not involved with, or responsible for, costs related to the distribution systems of SFR customers.

He raised issues related to how Petitioner distinguished between transmission and distribution costs in the COSS, which included $858,906,753 of costs listed as "TD Mains Not Classified." He stated all costs related to transmission and distribution that cannot be properly identified as either transmission or distribution are allocated 26.2% to transmission and 73.8% to distribution. He said, shockingly, 98.8% of Petitioner's transmission and distribution revenue requirement and 98.3% of its transmission and distribution plant in service is assigned based on this allocator. Mr. Callocchia testified the methodology used by Mr. Rea does not properly identify Petitioner's investment in the system's transmission and distribution facilities because the proper identification of system investments in transmission and distribution would be the result of an analysis of actual investment by pipe diameter.

Mr. Callocchia objected to recovery of costs related to COVID, the low-income program and credit card fees through SFR rates, stating these costs were neither caused by, nor provide any benefits to, the SFR class. He stated COVID related costs include foregone late fees, disconnect/reconnect expenses, uncollectible/bad debt expense, other direct costs, debt carrying costs, and Service Company expenses, offset by savings realized by Petitioner on forgone travel and conference expenses. Mr. Callocchia asserted that none of these costs should be allocated to the SFR class. In addition, he testified that under the proposed COSS methodology the SFR class would be unfairly subsidizing Petitioner's low-income program without their own low-income customers receiving the benefits. He stated members of the SFR class have customer assistance programs of their own and should not pay for costs of INAWC's low-income program, from which they receive no benefit. Finally, he contended that because SFR customers do not pay by credit card, they should not share in any costs absorbed by Petitioner related to credit card fees.

Mr. Callocchia also took issue with the COSS as not correctly reflecting the SFR class's average demand, specifically in Class Allocation Factor 1 (based on each class's projected average day demand on the system), which then flows through to other allocation factors based on Factor 1. He said Petitioner did not properly recognize distribution-level water losses in its system when developing Factor 1. He disagreed with Petitioner treating metered data from different service levels the same in the allocation of costs. Mr. Callocchia stated that the majority of water loss occurs within Petitioner's distribution system; because almost 74% of all water mains are categorized as distribution and given the vast size of the distribution system and the number of valves and connections within this system, the chances of line breaks, water leaks, and unauthorized usage are much more substantial at this service level. If metering data at the smaller, distribution-level is used in the same manner as transmission-level metering data in the allocation of costs for SFR classes, Mr. Callocchia stated it inappropriately allocates more cost to the SFR class in favor of the non-SFR classes. He stated all customer data would need to be adjusted back to the same service level, namely the transmission level of service, prior to the allocation of costs. After making this adjustment, he calculated a level of loss to be recognized for non-SFR customers to correct for what he deemed an over-allocation of demand to SFR customers in Factor 1. He then calculated average day demand factors that he said would result in a properly calculated Class Allocation Factor 1.

5. **Crown Point.** Mr. Guerrettaz objected to Petitioner's use of a COSS method different from what it used in its prior rate case. As described in detail by Mr. Callocchia, the new INAWC COSS method has been disallowed in Illinois and avoided within a settlement in the Missouri American Water Works rate cases. He recommended INAWC's proposed COSS be disallowed and accordingly any increase approved be applied across-the-board.

6. **Whiteland.** Ms. Young testified that Petitioner did not adequately consider the lower cost of providing wholesale water to SFR customers like Whiteland. She stated that the cost to serve SFR customers is lower than the cost of serving direct retail customers because SFR customers bear the burden of all costs related to the distribution of the water downstream from Petitioner's point of delivery of its wholesale water to the SFR customers. She also stated that Petitioner does not account for SFR customers having their own low-income customers and that Whiteland's customers, including those that are low-income customers, will have to subsidize Indiana American's low-income customers but will not receive any of the benefits under Petitioner's low-income proposal.

7. **INAWC Rebuttal.** Mr. Rea testified that his cost of service analysis, even as modified for changes upon which Petitioner agrees with other parties, indicates that an increase for industrial and SFR customers that is a significant multiple above the overall system average increase is appropriate. He noted that when Indiana American was asked in discovery whether it did any benchmarking to compare the results of the study prepared in Cause No. 45142, Petitioner responded that it had compared the subsidy analysis from that Cause to the subsidy analysis in this Cause. Every class that was subsidizing in Cause No. 45142 is subsidizing in the current Cause, and every class that was being subsidized in Cause No. 45142 is still being subsidized today. Moreover, Mr. Rea testified the subsidies for industrial and SFR customers have grown. Mr. Rea testified that there have been five different COSS prepared by three different cost of service professionals over a 14-year period and every one of those studies show that rates for industrial and SFR customers are being significantly subsidized.

With respect to the two-step COSS model, Mr. Rea explained that this approach simplifies the cost of service analysis and makes the resulting allocation to customer class more intuitive by unbundling the revenue requirement into business functions and allowing stakeholders to see what the cost of service is for each customer class by business function. He testified he has used this approach successfully and without objection for Iowa-American Water Company, West Virginia-American Water Company, and New Jersey-American Water Company. Mr. Rea provided Attachment CBR-4R, a one-step version of the cost of service analysis that has previously been used in Indiana American rate cases, the purpose of which is to compare results against the two-step model. Mr. Rea explained the only difference between the two models is the functionalization approach. All other cost allocators to function and customer class are the same. Mr. Rea concluded that the two approaches yield virtually identical results assuming the same allocators and allocation methodologies. From a cost allocation perspective, he characterized the two modeling approaches as identical.

Mr. Rea testified that Petitioner's cost of service analysis recognizes the unique circumstances SFR customers face. For example, SFR customers are allocated no costs associated with distribution mains (mains with less than 10" diameters). In addition, the SFR class is allocated only a minimal amount of customer service-related expenses. Mr. Rea presented the volumetric rates for each major customer class coming from Petitioner's cost of service analysis for cost categories that are typically charged volumetric rates (all costs except for metering costs, service line costs, and customer service expenses), which shows that the SFR class has the lowest volumetric rate for any major customer class in the cost of service analysis.

With respect to the split between transmission and distribution, Mr. Rea accepted OUCC witness Mierzwa's proposal that mains be assigned to the transmission and distribution functions based on the weighted installed costs of those mains. The split between transmission costs and distribution costs under his proposal is 32.4% and 67.6% respectively.

While Mr. Rea generally agreed with Mr. Callocchia that it would be reasonable to account for water losses differently for different customer classes depending on how much of the transmission and distribution system they use, he disagreed with Mr. Callocchia's calculation for how losses should be accounted for.

Mr. Rea accepted OUCC witness Mierzwa's approach with respect to hourly capacity factors for industrial and SFR classes.

Mr. Rea testified that Ms. York has not provided any evidence to suggest that cost per kilowatt-hour ("kWh") that Petitioner incurs is significantly higher during periods of high demand than during periods of low demand. If the cost per kWh is roughly the same regardless of when Petitioner uses electricity, then there is no reason to allocate costs disproportionately to certain customer classes. Mr. Rea testified that given there has been no demonstration that the cost per kWh is different during different times of the year, allocating purchase power costs based on total consumption (Factor 1) is appropriate.

Mr. Rea disagreed that the distribution multiplier for the industrial class should be a product of both the usage served at the distribution level and the mileage associated with those customers. According to Mr. Rea, it is plausible to say that the allocator should be based on one or the other, but not a combination of both. He stated it is reasonable to allocate the cost of mains to customers based on a usage-based allocator like the Base/Extra allocator. It would also be reasonable, in Mr. Rea's opinion, to allocate the cost of mains to customers based on a direct assignment of assets to customers assuming that can be done for all customer groups. He testified it would not be reasonable, however, to carve out a set of assets to be allocated to the industrial class based on exclusive use but then allocate a portion of that cost to other classes using a general usage-based allocator.

Mr. Rea agreed with Ms. York that an allocation of source of supply and water treatment costs to private and public fire classes is appropriate. He did not agree that an allocation of meter costs to fire protection services is appropriate because fire protection service is generally not metered.

Mr. Rea agreed with Mr. Callocchia that the SFR class should not be allocated the $6,889 related to the COVID-related and low-income costs included in Other Amortization Expense.

8. **<u>Discussion and Findings</u>.** Petitioner's COSS is a significant source of disagreement among the parties, particularly regarding the methodology used and the assumptions made by Indiana American. As an initial matter, it is important to note that Petitioner has not designed its rates based upon its COSS. Petitioner's COSS showed the industrial and SFR customers are being heavily subsidized by residential customers. However, because of the significant subsidization, INAWC witness Rea proposed the increases for these two classes be held at 150% of the overall system average. In contrast, witnesses for the industrial and SFR customers ask for Mr. Rea's study to be ignored and that rates be increased in an across-the-board fashion. Thus, to the extent Mr. Rea's study meaningfully presents the costs of serving different customer classes, the industrial and SFR customers' position would leave that subsidy in place.

The subsidy identified by Mr. Rea is not new. We find compelling Mr. Rea's summary on rebuttal of the COSS results presented in Petitioner's prior four general rate cases. Five different studies prepared by three different professionals all reach the same conclusion: that industrial and SFR customers are being significantly subsidized. We understand that simply because a prior COSS identified a subsidy, it does not mean that the subsidy continues to exist today. However, Petitioner's evidence on rebuttal demonstrates that there is no material difference between the results of the COSS under the prior one-step method or the two-step model used in this case. Further, none of the industrial or SFR intervenors presented their own study proving otherwise. Thus, we decline to find Indiana American's COSS model to be inappropriate simply because it has not been accepted by other state utility commissions.

Accordingly, we find that, while a departure from past COSS models utilized by Petitioner, the two-step COSS used in this case is appropriate and is not flawed in the various ways suggested by some Intervenors. We accept the COSS set forth by Petitioner, as modified on rebuttal and find Petitioner has adequately addressed the concerns raised by the parties, described in more detail below.

Sale for Resale. The Wholesale Customers suggested that it is cheaper to serve their class than any other customer class. This suggestion is supported by Petitioner's cost of service analysis.

Transmission and Distribution Costs. In the COSS, as agreed by Petitioner and the OUCC, the total net plant split for mains between the transmission and distribution function is 32.4% for transmission and 67.6% for distribution. Allocation of costs based on line length is not appropriate because investment varies with line size, potentially under-allocating costs to large users. Petitioner's and the OUCC's approach eliminates the need to normalize pipe length by allocating based on original cost. In this rate case, more of the costs associated with mains is assigned to the distribution function than in the previous rate case. The growth in the distribution allocation appears reasonable based on the nature of investments made since the last rate case, which has been reflected in the DSIC mechanism. As a result, a bigger share of the total main investments is allocated to residential and commercial customers and away from industrial and SFR customers.

Losses. INAWC's rebuttal cost of service analysis incorporates a calculation for water losses which accounts for both the amount of mains (by footage or mileage) at different capacities and the relative capacities associated with each type of main.

Capacity Factors. INAWC's rebuttal cost of service analysis incorporates hourly capacity factors determined using OUCC witness Mierzwa's recommended approach of applying the AWWA M1 Manual estimated hourly ratios to the maximum day capacity factor developed by Petitioner for the industrial and SFR classes. We agree with Mr. Rea that the use of actual AMI data for the industrial and SFR classes is inappropriate because the classes are not sufficiently homogenous to provide a reasonable reflection of actual customer usage. In addition, while we also understand, and generally agree, that using examples from the AWWA M1 Manual is not ideal, we find it to be the most reasonable surrogate for the lack of actual data for these classes in this instance.

Purchased Power Costs. While we agree Petitioner will incur more costs to pump water at times when demands are higher than at times when demands are lower, the record is devoid of evidence that the cost per kilowatt-hour that Petitioner incurs is significantly higher during periods of high demand than during periods of low demand. Accordingly, we find that no change to the allocation factor for purchased power is warranted.

Distribution Multiplier. INAWC's rebuttal cost of service analysis incorporates updated distribution multipliers based upon data provided in discovery. We decline to adopt the Industrial Group's recommendation to base the distribution multiplier on both the usage served at the distribution level and the mileage associated with those customers for the reasons stated in Mr. Rea's rebuttal.

Fire Protection Costs. An allocation of source of supply and water treatment costs to private fire and public fire classes was incorporated into INAWC's rebuttal cost of service analysis, which we find to be reasonable and appropriate.

Low-Income and COVID Costs. On rebuttal, INAWC removed the allocation of these expenses to the SFR class from its COSS analysis, which we find to be appropriate.

In sum, we find that Mr. Rea's COSS, as modified on rebuttal, is reasonable and useful for purposes of reviewing Petitioner's proposed rate increase allocation.

B. <u>Rate Design</u>.

1. <u>INAWC Case-in-Chief</u>. Mr. Rea also sponsored Petitioner's proposed rate design. He discussed a number of important guiding principles associated with sound rate design, including cost causation, revenue stability, efficiency of use, gradualism, avoidance of discrimination, simplicity and feasibility, and affordability. He explained that Petitioner's current rate design for general service and SFR water service is a two-area declining block rate design with the separate rate designs for Area 1 (Statewide) and Area 2 (Mooresville & Winchester) for general service customers. Volumetric rates for general service are differentiated for Area 1 and Area 2 and both are declining block rate structures. Mr. Rea testified that all customers regardless of customer class (residential, commercial, industrial, public authorities) take service on the same rate structure. Monthly meter charges are differentiated between general service and SFR. Meter charges are not differentiated between Area 1 and Area 2. Mr. Rea explained that DSIC and SEI charges, while not a part of base rates, are collected on a fixed charge basis by meter size and will be rolled into base rates in this proceeding. Volumetric rates for SFR are separate from general service rates and are also on a declining block rate structure. Volumetric rates for SFR are not differentiated between Area 1 and Area 2. Mr. Rea explained that private fire rates are on a monthly charge basis based on meter size and are the same for Area 1 and Area 2. Public fire surcharges are on a monthly charge basis based on meter size and are the same for Area 1 and Area 2, but separate rates apply to West Lafayette, Seymour, Summitville, and Lowell. Additional tariffs are in place to provide service to two newly acquired service territories, River's Edge and Lowell.

Mr. Rea testified that Petitioner is proposing a change to its water service rate design to include an allowance-based rate for all customers in Area 1 and Area 2. In addition, Petitioner is proposing to consolidate volumetric rates for Area 1 and Area 2 customers. He explained that an allowance-based rate is a rate design that features a level of usage offered to all customers at no additional charge above the fixed monthly meter service charge. Under Petitioner's proposal, instead of a volumetric rate that applies to all usage, there would be a level of usage provided to all customers (1,500 gallons of usage per month) at no additional charge beyond the monthly meter service charge. Mr. Rea testified that Petitioner is proposing an allowance-based rate to enhance affordability of Basic Water Service, especially for Petitioner's more economically vulnerable customers, without the need for these customers to directly apply for assistance through a discount tariff or some other type of customer-assistance program. He stated an allowance-based rate design reduces monthly bills for lower monthly usage amounts and increasing monthly bills for higher monthly usage amounts. He presented data from the National U.S. Census Bureau on the average size of household by income level, which shows a correlation between household income and the size of the household, with higher income households tending to have more occupants than lower income households.

Mr. Rea presented a comparison of bills under proposed rates for Basic Water Service for different household sizes under Indiana American's proposed allowance-based rate versus the current rate design. This comparison showed that the majority of Petitioner's customer base that may have issues of affordability of service would do better under the allowance-based rate than under Petitioner's standard rate design. He testified that from a cost causation perspective, it is cheaper on a per unit basis to provide Basic Water Service than it is to provide peakier seasonal service, and therefore appropriate from a cost of service perspective that Basic Water Service should be priced at a lower rate than seasonal water service. In addition, he stated data across the American Water footprint shows that there is a positive correlation between household income and the seasonal use of water. Mr. Rea stated that if: (1) seasonal water service is more expensive on a per unit basis to serve than Basic Water Service from a cost of service and cost causation perspective, (2) higher income customers are more likely to have significantly higher seasonal water use than lower income customers, and (3) a single volumetric rate applies to all service for all customers, the result is that lower income customers are actually subsidizing higher income customers under Petitioner's current rate design. He testified the biggest impact of the allowance-based rate will be seen by lower use residential customers regardless of their household income. He stated that while bills for Basic Water Service will increase for households of three or more (3,600 gallons per month or more), bills for two-person households (2,400 gallons per month) will be almost exactly the same as under present rates and bills for one-person households (1,200 gallons per month) will drop by more than $10 per month under Petitioner's proposed rates.

Mr. Rea further testified that Petitioner proposes to consolidate Area 1 and Area 2 rates and to increase the base rate monthly meter charge. He also described the treatment of recently acquired systems within Petitioner's proposed rate design.

Mr. Rea testified that Petitioner used the following general guidelines in allocating the proposed Step 3 revenue increase to customer classes as follows: (1) increases to industrial and SFR classes will be capped at 1.5 times the overall water service revenue increase requested in this case for Step 3 rates, (2) no increases are assigned to private and public fire, as cost of service indicates that decreases are in order for these classes, and (3) the remainder of the increase is allocated to residential and commercial classes in proportion to present rate revenues. With respect to industrial and SFR customers, Mr. Rea again noted that cost of service continues to indicate significant increases for those customers. While he recommended these subsidies be reduced, he also noted the need to mitigate the impact to these customers. Therefore, Mr. Rea concluded, it is appropriate to cap increases for these classes at 1.5 times the system average to maintain a gradual approach.

Mr. Rea also presented Petitioner's proposal to consolidate wastewater rates for all of its customers into a single rate design as well as to collect 65% of the proposed wastewater revenue requirement (Step 3) from its wastewater customers and to move 35% of the proposed wastewater revenue requirement (Step 3) to water service customers to be collected through water service rates. He explained this proposal was intended to dampen the impact on wastewater service customers, consistent with what has occurred in several recent cases but is even more necessary now. Without some movement of wastewater revenue requirement to water service customers, Mr. Rea stated wastewater service customers would generally see rate increases of 100% or more. Petitioner's objective with this proposal is to assist with the affordability of its wastewater service and keep wastewater bills for typical residential customers at approximately $100 per month. He noted the impacts on water service customers of this proposal is minimal, representing approximately $0.07 per hundred gallons for Petitioner's residential water service customers or a bill impact of approximately $0.27 per month for a residential customer with average usage. He said without this proposal, the average wastewater service bill would be approximately $150 per month.

2. **<u>OUCC</u>**. Mr. Mierzwa recommended a separate schedule of volumetric charges be established for the public authority class that would result in a Step 1 increase comparable to 2.0 times the system average increase proposed by Petitioner for the industrial and SFR classes. He also recommended the additional revenues realized in Step 1 from increasing the rates of the public authority customer class should be utilized to reduce the rate block 2 volumetric rate.

For Steps 2 and 3, Mr. Mierzwa recommended SFR rates should be proportionately increased to provide for an increase that is 2.0 times the system average increase. For the industrial and public authority classes, he recommended that the volumetric rates for these customers be proportionally increased until the increase assigned to one of these classes reaches 2.0 times the system average increase. The additional revenues realized in Steps 2 and 3 from increasing the rates of the SFR, industrial, and public authority customer class should be utilized to reduce the rate block 2 volumetric rate. He also recommended that any reduction to Petitioner's requested wastewater revenue requirement first be applied to reducing the wastewater revenue requirement to be recovered from water service customers.

Mr. Mierzwa testified that at the conclusion of Step 3, under Petitioner's proposed revenue distribution, the residential and commercial customer classes will be contributing revenues in excess of the indicated cost of service, and the industrial, public authority, and SFR classes will be contributing revenues less than the indicated cost of service. He recommended reducing these differences to the extent possible while maintaining gradualism.

In cross-answering testimony, Mr. Mierzwa disagreed with Industrial Group witness York's proposal to recover the DSIC and SEI revenue requirement through monthly customer charges. He said such proposal would eventually result in recovery of all fixed costs through fixed monthly charges and only the recovery of variable costs through usage charges. He noted Crown Point witness Guerrettaz proposed a similar recommendation, referred to as a straight fixed variable rate design, which he said is inconsistent with cost causation principles. He said such a rate design would increase Petitioner's cost of providing service and is not in the best interest of customers.

3. Industrial Group. Ms. York objected to the proposed non-cost-based wastewater subsidy that INAWC recommends be assigned to water customers. Ms. York testified that INAWC's proposal to shift nearly $1.63 million of the cost of providing wastewater service to water service customers, who are already facing a sizable rate increase, is at odds with sound cost-causation and rate design principles. Ms. York also noted that INAWC's proposed subsidy is nearly 500% greater than the wastewater subsidy identified in its prior case and will continue to grow unless INAWC takes steps to bring wastewater customers toward cost of service. Thus, Ms. York recommended that the proposed wastewater subsidy be reduced by the greater of either 25% of Petitioner's proposed subsidy of $1.6 million, or by the amount of reduction in wastewater revenue requirement Mr. Gorman recommends, plus $100,000. Under Ms. York's proposal, wastewater rates would be set equal to those proposed by Petitioner, with any reduction to the wastewater utility's revenue requirement being reflected as a reduction in the amount of wastewater revenue requirement Petitioner has proposed to collect from water customers.

Ms. York also recommended that the Commission direct INAWC to move toward class-specific rates, rather than continue to apply a single rate structure to all customer classes except the SFR class. This will make it easier to develop rates to recover individual classes' cost of service, as well as improve the accuracy of cost allocation within classes. She recommended Petitioner begin this process by implementing an industrial rate schedule at the conclusion of this case. She testified that a separate industrial rate would allow INAWC to more accurately allocate costs within the class to reflect the distinction in infrastructure used to provide service. She stated it would also allow INAWC to recover costs from industrial customers in a manner consistent with cost of service principles, without materially impacting other rate classes.

Ms. York also recommended that the revenue requirements that are being rolled to base rates associated with the DSIC and the SEI charge continue to be recovered from customers on a per meter basis.

4. Wholesale Customers. Mr. Callocchia objected to the recovery of

DSIC and SEI costs in part from volumetric charges, which he stated is inconsistent with the plain language of Ind. Code § 8-1-31-8, Petitioner's previous testimony, and cost causation principles. He stated Petitioner is proposing to collect DSIC 12, 13, and 14 and SEI revenue requirements as part of base rates through both meter charges and volumetric rates in a proportion of approximately 50% each. Mr. Callocchia recommended Petitioner collect DSIC and SEI revenue requirements related to the currently effective charges 100% via meter charges.

Mr. Callocchia also recommended that INAWC be directed to develop a transmission tariff so SFR customers have the option to secure alternative potable water supply and pay a transmission tariff to Petitioner to wheel water through Petitioner's system.

In cross-answering testimony, Mr. Callocchia agreed with Industrial Group witness York that DSIC and SEI revenue requirements should be recovered through fixed monthly meter charges because it is consistent with cost of service principles.

5. **<u>Crown Point</u>.** Mr. Guerrettaz testified that INAWC's rate design in this case attempts, in part, to charge Crown Point for the renovation costs of distant unrelated acquired utilities by "arbitrarily rolling 50% of DSIC and SEI charges into volumetric rates." He testified that applying DSIC and SEI charges to volumetric rates is contrary to statute and INAWC's testimony in prior cases. He advocated for a transportation rate as an alternative for Crown Point to obtain Lake Michigan water at a more affordable cost.

6. **<u>CAC</u>.** Mr. Inskeep agreed with Indiana American that the proposed allowance-based rate design can help enhance affordability and is consistent with the rate design principle of simplicity and feasibility. He testified that a key benefit of this proposal is that there is no need for customers to take any action to benefit from the rate design change, unlike a utility program that requires customer enrollment. He also agreed that this rate design will help better align rate design with cost causation. He stated that although this rate design change will tend to benefit lower-income residential customers, it is being applied uniformly to all customers in a non-discriminatory manner.

Mr. Inskeep disagreed, however, with Indiana American's proposal to increase the base rate monthly meter charge. He testified that high residential fixed charges reduce customer control, disproportionately impact low-usage customers and low-income customers, reduce the financial viability of deploying water efficiency measures, and result in higher water system costs. He also recommended Petitioner use the total average bill (4,050 gallons per month) for defining Basic Water Service.

7. **<u>INAWC Rebuttal</u>.** Mr. Rea opposed the CAC's recommendation to use a total average bill for the community-level or customer level analysis of affordability, explaining that total average bill is a static calculation that applies equally to everyone. He stated that the definition of Basic Water Service needs to be flexible enough to accommodate households of different sizes and recognize the high degree of correlation between household water usage and the number of persons in the household. In addition, Mr. Rea testified that approximately 10% of the water that Petitioner sells to residential customers (and therefore approximately 10% of total average use) is for discretionary summertime usage, which is not appropriate to use as a basis for an affordability analysis specifically targeted at individual customers or lower income customers.

Moreover, lower income households tend to have fewer people in them which means that, all other things considered, lower income households will tend to have lower levels of water consumption than the residential population in total. Using an average water bill, as Mr. Inskeep suggests, therefore overstates the amount of water that lower income customers will use and overstates, on average, the total bill for these customers.

Mr. Rea testified that the proposed $20.00 meter charge is supported by Petitioner's cost of service analysis and results from a standard method for calculating meter charges based on the revenue requirements associated with meters and meter reading, service lines, and customer service functions. The calculated meter rate for a 5/8" meter in the cost of service analysis is $20.17 per month. Petitioner's proposed $20.00 charge is just under that calculated value.

With respect to DSIC and SEI related costs, Mr. Rea explained that DSIC and SEI related investments are not accounted for separately in Petitioner's revenue requirements and cost of service analysis. They are allocated to customer class not based on how they used to be recovered through the DSIC and SEI recovery clauses, but instead on how they would normally be allocated to customer class in a COSS.

Mr. Rea was generally supportive of the concept of separate volumetric rates for each customer class but did not support the piecemeal implementation of this type of rate design or a transition to this rate design as suggested by Ms. York or implied in part by Mr. Mierzwa. If it is to be done, Mr. Rea advised it is most efficient and appropriate to all customers to move to this type of rate design in one complete step once all the impacts to customers are well understood. He did, however, point out disadvantages to this type of rate design, namely that the definition of what constitutes a residential, commercial, industrial, and public authorities customer becomes much more important and the ability to assign and track customers to each class becomes much more important. He stated there will always be winners and losers in the process of changing rate design and these impacts need to be well understood.

Mr. Rea opposed the Wholesale Customers' recommendation to develop a transmission-only rate, citing lack of evidence that it would be in the public interest and that it would not be detrimental to non-transmission customers. He cited various other considerations if such a rate were to be adopted, including the application of appropriate exit fees or other charges attributable to those sunk costs that would need to be calculated to avoid harming the non-transportation customers. Mr. Rea stated that if the transportation customers desired Petitioner to serve as a back-up source of supply, then an appropriate back-up rate would need to be calculated.

Mr. Rea opposed the recommendations by the Industrial Group and SFR customers to increase rates on an across-the-board basis for the same reason already addressed regarding cost of service—that these classes are being heavily subsidized and that has been true for some time. That said, he disagreed with Mr. Mierzwa that these classes should receive an increase of two times the system average on the grounds that it was too extreme. As to the wastewater reallocation to water, he disagreed with both Ms. York's and Mr. Mierzwa's alternative proposals. He indicated that, in the event of a reduction to the wastewater revenue requirement, wastewater customers should receive some benefit. He proposed that a reasonable compromise would be to reduce the reallocation amount by double the percentage of any wastewater revenue requirement reduction. He testified that Ms. York's proposal was unacceptable because it would, in many cases, result in higher wastewater bills and run counter to Petitioner's goal of keeping the average residential wastewater bill below $100 per month.

8. **<u>Discussion and Findings</u>.** We find that Petitioner's rate design proposals, as modified on rebuttal, satisfy the guiding principles of cost causation, revenue stability, efficiency of use, gradualism, avoidance of discrimination, simplicity and feasibility, and affordability. As the Commission has authorized an increase in water rates that is less than the requested increase, Petitioner shall reduce water service volumetric rates on a pro rata basis until the difference between the authorized increase and the requested increase is met. We further find that Petitioner's proposals achieve a rate design that is consistent with statute for all customer groups and is just and reasonable. Additionally, we find Petitioner's proposed allowance-based rate to be a reasonable means to address affordability issues for all customers while adhering to the other guiding principles noted above.

Single Tariff Pricing. We note that no party opposed Petitioner's proposal to consolidate the volumetric charges for Areas 1 and 2 over the three steps of the increase in this Cause and so we find it should be approved.

Revenue Allocation. The only difference among the parties concerning allocation of the revenue increase relates to the allocation to the SFR and industrial classes. Petitioner proposes that these classes receive an allocation of 150% of the overall system average. The OUCC proposes that they receive an increase of 200% of the overall system average. The industrial and SFR customers propose an across-the-board increase. Based on our prior findings regarding cost of service and the subsidies currently being provided to industrial and SFR customers, we decline to impose an across-the-board increase. As to the OUCC's proposed 200% allocation, we find approving an increase for a class so high in relation to the overall system average would be too aggressive of a move towards cost of service. Accordingly, we find Mr. Rea's proposal that the allocation to these classes should be 150% of the overall system average strikes the appropriate balance of moving these classes closer to cost of service, consistent with the need for gradualism. With its tariff filing, Petitioner shall provide the revenue proofs demonstrating the adjusted revenue allocations will recover the adjusted cost of service.

Wastewater Reallocation. It is generally undisputed that subsidies are contrary to cost causation principles and that utility rates should reflect the costs incurred to provide service, as reflected in our decision above concerning the allocation of costs to the industrial and SFR customers. However, we also recognize the role that reasonable and temporary subsidies can provide when necessary to address issues that arise, such as avoiding rate shock for a particular class of customers.

No party disputed that, absent a reallocation of wastewater costs to be recovered through water rates, the increase in wastewater rates would be significant. Given the relative sizes of the water utility and the wastewater utility, a reallocation such as that proposed by Petitioner can produce significant relief for the wastewater customers while having a minor impact on the overall water rates. While we remain concerned with allocating costs caused by one set of Petitioner's customers to another set of customers that are not receiving the same utility service (i.e., allocating wastewater costs to customers that do not receive wastewater service), we also recognize the

Indiana General Assembly's recent directive in Ind. Code § 8-1-30.3-6.5 concerning similar allocations. Accordingly, we find that a reallocation in this instance should be approved. However, we agree with the Industrial Group that movement towards cost of service for Petitioner's wastewater customers is essential and we encourage Petitioner to increase its efforts to move in that direction.

The only dispute among the parties that we must resolve centers on how the reallocation should change based upon any changes by the Commission in this Order to Petitioner's proposed revenue requirement. We agree with Mr. Rea that Ms. York's proposed modification to the reallocation could produce wastewater rates that are higher than those proposed by Petitioner and should therefore be rejected. We also agree that the OUCC's proposal that any reduction in the wastewater revenue requirement first being applied to the reallocation would provide wastewater customers no benefit from such reduction. As such, we approve Mr. Rea's proposal on rebuttal that the reduction be applied by reducing the reallocation amount by doubling the percentage of wastewater revenue requirement reduction as shown in Petitioner's Exhibit 18 at 66-70.

Meter Charge/Allowance Rate. No party opposed Petitioner's proposed Allowance Rate, whereby there would be no additional volumetric charge for consumption below 1,500 gallons per month. We find persuasive Mr. Rea's presentation of the usage characteristics of customers with different income levels. We further find that the use of this allowance rate will provide cost stability that will ameliorate affordability concerns in a fashion that adheres to cost of service concepts. We therefore find it should be approved.

The Industrial Group and SFR customers proposed that costs previously being recovered through the DSIC and SEI continue to be recovered through a fixed charge. We disagree with the suggestion by these customers that the General Assembly intended these costs to be recovered through a fixed charge in perpetuity. The statute is clear that the DSIC and SEI charges are to be a fixed charge by meter size while being recovered in the tracker but that these charges are reset in the context of a general rate case. Neither the DSIC nor the SEI statute indicate or require that the costs must continue to be recovered through a fixed charge when approved in base rates. Recovery of the entire DSIC and SEI revenue requirement through a fixed charge would eliminate all risk to Petitioner of under-recovery and remove any incentive for customers to better manage their water use. We recognize that the change in meter charge results in what equates to an approximate 50% consolidation of DSIC and SEI revenue and is not the result of any specific allocation of DSIC and SEI costs within the rate design. Accordingly, we find the DSIC and SEI costs, which are being rolled into base rates and allocated to customer class based on how they would normally be allocated through a COSS, is reasonable.

With respect to the allocation of source of supply and water treatment cost to private fire and public fire classes, the Commission agrees that fire protection service is generally not metered. Thus, we agree that a portion of the source of supply and water treatment costs should be allocated to the public fire and private fire protection classes but reject any allocation of meter costs to fire protection services as explained by Petitioner on rebuttal.

The CAC also objected to increasing the base rate monthly meter charge for 5/8 inch meters from $15.25 to $20.00 per month because of the disproportionate impact it will have on low-usage and low-income customers. Based on the evidence, we find that Petitioner's proposal is consistent with the results of the COSS and the resulting monthly meter charge represents the cost to serve those customers.

Separate Rate Structures By Class. We find Petitioner has expressed sufficient interest in examining the potential impacts of a change in rate design to develop separate volumetric rates by customer class that a study of these impacts is warranted, and we authorize the costs of such analysis to be deferred for recovery in Petitioner's next general rate case.

Transportation Rate. The SFR customers did not cite to any prior occasion when the Commission has approved a transportation rate for a water utility. Nor do we believe the SFR customers provided evidence demonstrating such a rate would be in the public interest or that it would not harm other customer classes. Unlike the natural gas industry, where a federal policy exists to unbundle the sales of natural gas, in the water industry, there can be a multitude of reasons for why water from different suppliers cannot be comingled in the manner urged by the SFR customers. We are not persuaded that a transportation or transmission-only rate such as that proposed by the Wholesale Customers would be in the public interest. Because we lack sufficient evidence concerning the Wholesale Customers' proposal as to the potential impacts on non-transportation customers, we decline to require Petitioner to develop a transportation rate.

C. <u>Universal Affordability Tariff</u>.

1. <u>INAWC Case-in-Chief</u>. INAWC proposed a Universal Affordability Tariff for water service that includes multiple tiers of discounts based on different levels of household income stated as multiples of the federal poverty level. The tariff offers discounts on both the basic 5/8" meter charge and the volumetric charges for water service. Mr. Rea explained that the driving principle behind Petitioner's proposed Universal Affordability Tariff is to provide all participating customers discounts such that the expected bill for Basic Water Service (40 gallons of water per household member per day) will be no more than 2% of their annual household income. The impetus behind the proposal was a recognition that there will always be groups of customers that will have issues with the affordability of water and wastewater service. Mr. Rea stated Petitioner's proposed tiered discounts are designed to provide customers at each interval of the federal poverty level the opportunity to have Basic Water Service bills in the 1% to 2% range of household income.

2. <u>OUCC</u>. Mr. Bell recommended the Commission reject the proposed Universal Affordability Tariff because it is not in the public interest. He asserted it does not protect the affordability of utility services for present and future generations of Indiana citizens as required by Ind. Code § 8-1-2-0.5. Mr. Bell explained that neither Indiana American nor its parent company proposes to contribute any funds to providing bill discounts through the proposed Tariff. Rather, the bill discounts are to be funded solely and involuntarily by captive ratepayers. Additionally, Mr. Bell testified Indiana American has not shown it is able to administer a program of its own design, noting the lack of success in its administration of bill discounts to qualifying low-income customers in the Terre Haute, Muncie, and Northwest/Gary districts.

Mr. Bell explained Indiana American proposes to roll back into base rates the estimated total amount of discounts provided through the Universal Affordability Tariff (i.e., $1,274,901 for

Step 2 rates and $1,371,677 for Step 3 rates). He said because Petitioner's program includes regulatory accounting treatment to address under-recovery, the cost of the program to captive ratepayers may be even higher than Petitioner's proposed recovery. Mr. Bell stated that Indiana American may benefit by receiving more timely payments, reducing bad debt expense, and increasing customer retention at no expense to shareholders, reducing Indiana American's overall risk.

Mr. Bell explained that Ind. Code § 8-1-2-46(c) allows utilities to establish programs to charge customers lower rates or provide discounts based on something other than customer usage characteristics. He stated that while a lower rate or discount for certain customers is no longer considered discriminatory, it remains unreasonable to make captive customers pay higher rates to fund a customer assistance program with no utility contribution. Mr. Bell noted that nothing in the statute prohibits Indiana American from establishing a program relying on voluntary contributions or sources other than a revenue requirement included in rates, such as soliciting voluntary customer contributions through an opt-in roundup program or from an opt-in contribution. He also indicated that Indiana American is a for-profit company and is a wholly owned subsidiary of American Water Works Company, Inc., which has a market capitalization of over $27 billion. He concluded that Indiana American has significant resources that it could draw from to fund the proposed low-income rate if it chooses.

Mr. Bell asserted that Petitioner's proposed 10% level of customer participation in the bill discounts is unsupported by the evidence. Mr. Bell testified that this level of customer participation is not consistent with the extremely low level of low-income customer participation in the current LIPP, which was only 0.5%. Mr. Bell also pointed out that in Cause No. 45142, Mr. Rea testified that one of the reasons Indiana American was proposing its LIPP was to gauge low-income customer interest in such a program.

Mr. Bell also testified that Indiana American has administered only $90,885 out of $1.2 million of available assistance in the current LIPP to qualifying low-income customers. He said, in total, Indiana American administered only 7.6% of the available funds, leaving $1,109,115 or 92.4% of the available funds undistributed to its customers who qualify for LIPP assistance.

Mr. Bell recommended the Commission reject Petitioner's proposed Universal Affordability Tariff and remove $1,274,901 from Step 2 rates and $1,371,677 from Step 3 rates, which amounts he said were embedded in the proposed rate design.

3. **<u>CAC</u>.** Mr. Inskeep urged the Commission to approve the proposed Universal Affordability Tariff and to expand the discounts to the total bill (inclusive of public fire protection surcharge and other separate surcharges) and expand proposed eligibility and discounts under the tariff.

4. **<u>INAWC Rebuttal</u>.** Mr. Rea testified that more households and families in Indiana will have access to affordable water and wastewater service with Petitioner's proposed Universal Affordability Tariff than without it. In his opinion, this meets the definition of protecting the affordability of utility service for present and future generations of Indiana citizens. Mr. Rea stated that even after implementation of INAWC's proposed allowance-based rate, lower income customers will still be subsidizing higher income customers (albeit to a lesser extent).

Given that, Mr. Rea opined it does not make sense to ask Petitioner's shareholders to forego recovery of its cost of providing service to fund discounts for lower income customers and leave higher income customers still being subsidized. Mr. Rea explained that the LIPP and Universal Affordability Tariff are designed differently. He also noted the LIPP launched just prior to the COVID emergency, and therefore, the challenges of the LIPP should not be used to deny the Universal Affordability Tariff proposed here.

Mr. Rea disagreed with the CAC's recommendation to expand eligibility for the Universal Affordability Tariff. While Mr. Rea recognized that many Indiana families live every day under financial hardships, he stated there does need to be a balance between reducing bills in order to make them more affordable and the costs of the discounts that must be borne by others.

5. <u>Discussion and Findings</u>. For a water or wastewater utility, there is specific statutory authorization for the Commission to approve assistance for income-qualified water or wastewater customers. Ind. Code § 8-1-2-46(c) provides:

> Upon request by a water or wastewater utility in a general rate case, the [C]ommission may allow, but may not require, a water or wastewater utility to establish a customer assistance program that:
>
> (1) uses state or federal infrastructure funds; or
>
> (2) provides financial relief to residential customers who qualify for income related assistance.
>
> A customer assistance program established under this subsection that affects rates and charges for service is not discriminatory for purposes of this chapter or any other law regulating rates and charges for service. In considering whether to approve a water or wastewater utility's proposed customer assistance program, the commission shall determine that a customer assistance program established under this subsection furthers the interests set forth in [Ind. Code § 8-1-2-0.5] and is in the public interest.

Ind. Code § 8-1-2-0.5 provides:

> . . . it is the continuing policy of the state . . . to use all practicable means and measures . . . in a manner calculated to create and maintain conditions under which utilities plan for and invest in infrastructure necessary for operation and maintenance while protecting the affordability of utility services for present and future generations of Indiana citizens.

Ind. Code § 8-1-2-46(c) provides that the Commission *may* approve requests by water or wastewater utilities to establish customer assistance programs that provide rate relief, such as through reduced rates or rate discounts, for utility service. And while this statute provides that a lower rate or discount for certain customers is not considered discriminatory, it does not address the cost recovery associated with such programs.

The Commission has previously approved two low-income customer assistance programs, both were pilot programs and approved as part of settlements. In *CWA Authority, Inc.,* Cause No. 45151 (IURC July 29, 2019), the Commission approved a customer assistance program wherein the utility's residential wastewater customers that qualified for assistance through Indiana's Energy Assistance Program received varying degrees of bill discounts and infrastructure investment assistance based on customer income level. The program was funded via a $0.45 monthly charge per residential customer and a $200,000 annual utility contribution. The second approved customer assistance program was for Indiana American in its last base rate case, Cause No. 45142, wherein the Commission approved the three-year LIPP, which provided bill discounts to residential customers that qualified for assistance through Indiana's Energy Assistance Program. The LIPP was funded through both customer rates and matched contributions from the utility.

Since the approval of both of these programs, the Commission has also declined approval of a water and wastewater customer assistance program in *Community Utilities of Indiana, Inc.*, Cause No. 45651 (IURC Feb. 1, 2023). In that case, the utility proposed to provide discounts of $2.80 (water) and $2.90 (wastewater) per month for certain qualifying low-income residential customers using 5,000 gallons of water or wastewater, which was to be funded 100% by other residential customers and without any utility contribution. The Commission declined approval of the program, finding the proposed discounts to be paid by the other residential customers to be more than "minimal" and expressing disagreement with the utility that it would be confiscatory for it or its shareholders to voluntarily fund a portion of Petitioner's low-income program. *Id.* at 81-82.

As a general matter, the programs approved by the Commission shared common features, such as utility contributions and eligibility requirements tied to qualifying for Indiana's Energy Assistance Program. The customer assistance program most recently rejected by the Commission included neither of these attributes and imposed more than minimal cost on the funding ratepayers.

The Universal Affordability Tariff before us today includes no utility contributions and requires customers to submit documentation that is largely duplicative of documentation required for other assistance programs, such as Indiana's Energy Assistance Program. Petitioner also seeks regulatory accounting deferral treatment, without carrying costs, for expenses related to the implementation of the Universal Affordability Tariff. The design of the program, as well as the failure of Petitioner's LIPP, lead us to agree with the OUCC that the Universal Affordability Tariff is not in the public interest. We also agree with CAC witness Inskeep that there are simpler and more efficient ways to determine eligibility for a program like the Universal Affordability Tariff. We disagree with Indiana American witness Rea's assertion that the challenges of the LIPP, which was implemented immediately prior to and during the COVID pandemic, should not be used to deny the Universal Affordability Tariff. Additionally, Indiana American argued that lower income customers are subsidizing higher income customers because higher income customers use water differently and cost more to serve. However, the Universal Affordability Tariff does not address the cause of the subsidization, i.e., lower volume customers subsidizing higher volume customers, because *all* residential customers are charged the same rate and would be allocated the costs of the low-income program.

For these reasons, and as discussed further below, we deny approval of the Universal Affordability Tariff and encourage Petitioner to return to the drawing board and design a new Universal Affordability Tariff based on the following framework. However, Petitioner is also encouraged to consider other additional options that build upon this identified framework.

First, Indiana American should base eligibility for the Universal Affordability Tariff on enrollment in or qualification for one or more of the following assistance programs:

- Indiana Energy Assistance Program
- Low Income Water Assistance Program
- Supplemental Nutrition Assistance Program
- Other assistance programs identified by Indiana American that base eligibility on a percentage of the federal income poverty level

A combination of two or more programs likely would yield a larger pool of applicants and potentially result in increased participation by Petitioner's customers.

Second, Indiana American should evaluate the cost-effectiveness of using a third-party administrator to implement the Universal Affordability Tariff in comparison to implementing the program using its existing resources. Petitioner's administration of the LIPP was abysmal in many respects. Given this underperformance, combined with the fact that other American Water affiliates appear to be using a consultant to administer similar types of low-income programs, we agree that Petitioner's consideration, at least initially, to use a third-party administrator may be reasonable. Should Indiana American determine it is cost-effective to use a third-party administrator, the Commission strongly encourages Petitioner to learn from that third-party administrator, as well as from its peer utilities in Indiana and throughout the American Water enterprise, in order to remove this cost from future iterations of its low-income programs. A company of the caliber of Indiana American, particularly with its access to the shared services of its parent company American Water, should be capable of administering a program of this limited scope and size.

Next, the application for the Universal Affordability Tariff should be designed to be completed to the greatest extent practicable on a mobile device. Petitioner should evaluate the costs and benefits of such an application design and select the application design that provides the greatest access and ease of use to applicants at the most reasonable cost.

In addition, Indiana American should market the Universal Affordability Tariff to its customers by all means practicable and cost effective, including on bill and other direct communications and through community action agencies and Indiana 211. The Commission encourages Indiana American to consult with the OUCC and CAC in identifying the means of communication that best reaches Indiana American's customers.

As a final matter, the Commission is aware that it cannot mandate utility shareholder contribution to a low-income program such as the Universal Affordability Tariff. Nevertheless, as Indiana American redesigns and resubmits it Universal Affordability Tariff, the Commission recommends that Indiana American identify and keep track of recurring expenses that are reduced over time through the successful implementation of the Universal Affordability Tariff, such as receiving more timely payments, reducing bad debt expense, and increasing customer retention. As noted by OUCC witness Bell, these benefits accrue to Indiana American at no expense to its shareholders and reduce Indiana American's overall risk. The Commission further notes that if, in its redesigned Universal Affordability Tariff, Indiana American again seeks regulatory deferred accounting treatment for expenses related to implementation of the Universal Affordability Tariff, any eventual review of those expenses will evaluate the prudence of those expenses, including their direct and indirect maximization of positive impacts and mitigation of adverse impacts.[27]

Accordingly, after consideration of the evidence and for the foregoing reasons, we find that approval of Indiana American's proposed Universal Affordability Tariff is not in the public interest and is denied.

D. <u>Montgomery County Surcharge</u>.

1. <u>INAWC Case-in-Chief</u>. Petitioner proposed a new surcharge that would apply to operations in Montgomery County based upon an ordinance adopted by the Montgomery County Board of Commissioners establishing an "Infrastructure Zone" and requesting Petitioner extend water mains pursuant to Ind. Code § 8-1-2-46.2.

Mr. Shimansky described Petitioner's investment project in Montgomery County where Phase 1 consisted of installation of water main to extend service east towards I-74 and Phase 2 consisted of installation of main, a booster station, and a water tower. Mr. Shimansky testified that this project supports the economic development efforts of Montgomery County and provides service to an industrial park and its first manufacturer. He explained that after completion of final punch list items in spring 2023, the total cost of Phase 1 and 2 is expected to be approximately $18,000,000 (before netting the contribution), and the primary funding is being provided by Montgomery County.

Mr. Shimansky further testified that $2,777,506 is included in the rate base actuals through September 2022 for this project. He explained that these costs are to be recovered through a surcharge on Montgomery County customers in the Crawfordsville District only. He testified there are 6,339 customers, not counting private fire protection meters, and, in order for these customers to reimburse Petitioner for these costs in compliance with the ordinance, Petitioner proposes to charge $3.54 per meter per month on their regular water bill. Mr. Shimansky testified this number has been reduced for revenues received from a large customer in the area. Mr. Shimansky sponsored a copy of the Montgomery County Ordinance and a workpaper calculating the per-meter monthly charge. Pet. Ex. 2, Attachment GDS-3 and GDS-4.

Mr. Shimansky testified that the extension satisfies Ind. Code § 8-1-2-46.2(c). He testified, however, that if the request under subsections (d) and (e) of that statute were denied, without the surcharge, Indiana American would recover Petitioner's costs of its portion of the investment from all customers across the State.

2. <u>OUCC</u>. Ms. Stull opposed Indiana American's proposed Montgomery County surcharge because: (1) Petitioner did not request approval of the project before completing it; (2) application of the surcharge throughout Montgomery County is contrary to Petitioner's agreement with the County and the County Redevelopment Commission; and (3) concerns with the overall calculation of the surcharge. Ms. Stull proposed that Petitioner include project costs in its rate base with cost recovery through its cost of service allocation to the

[27] We also expect any future request for regulatory accounting deferral treatment would continue to not include a request for carrying costs.

appropriate customer classes.

3. **INAWC Rebuttal**. Mr. Shimansky noted that Ms. Stull did not oppose the project underlying the proposed surcharge; instead, she only opposes the surcharge and proposes that Petitioner include the costs of the project in rate base and recover those costs through its cost of service allocation to the appropriate customer classes. In response to Ms. Stull's contention that project preapproval is needed, Mr. Shimansky testified that the statute only requires approval of the project and there is no objection to the underlying project. Mr. Shimansky testified that the question is one of rate design, which he believes the Commission can approve with or without a statute specifically directing it. Mr. Shimansky further testified that the Montgomery County Board of Commissioners specifically requested a main extension to support an economic development project, and they did so with full understanding that it would result in a surcharge imposed on the constituents who are customers of Indiana American. Mr. Shimansky did not understand why the OUCC would oppose the surcharge and instead request that the costs of the project be rolled into the calculation of the rates of all customers.

In response to Ms. Stull's contention that imposition of the surcharge is contrary to the agreement between Petitioner and the County and its Redevelopment Commission by imposing surcharges throughout the County (rather than just in the infrastructure zone), Mr. Shimansky explained that the County Commissioners adopted an ordinance after the agreement, which clearly states that the surcharge would be payable "by customers located in the geographic area within the jurisdiction of the Commissioners, including the geographic area established as an Infrastructure Development Zone." Pet. Ex. 2, Attachment GDS-3. Mr. Shimansky testified that between signing the agreement and adopting the ordinance, the County concluded it would be better for the surcharge to apply throughout Montgomery County.

Mr. Shimansky also responded to the OUCC's concerns regarding how the surcharge was calculated to show that the surcharge was correctly calculated. Mr. Shimansky testified Petitioner is accepting the OUCC's position that Petitioner's investment is exempt from property tax, and, as such, he recalculated the surcharge to reflect this issue and the revised calculation is set forth on Petitioner's Exhibit 15, Attachment GDS-3R.

4. **Discussion and Findings.** Ind. Code § 8-1-2-46.2(d) and (e) provides, in summary, that upon a county executive or municipal legislative body (in this case, Montgomery County Board of Commissioners) establishing an infrastructure development zone and requesting a utility (in this case, Indiana American) to extend service, the utility (again, Indiana American) may file a petition with the Commission seeking approval of the requested extension. If such request is approved, the Commission shall approve rate schedules that include a surcharge payable only by customers located in the geographic area within the jurisdiction of the requesting governmental entity, including the geographic area established as an infrastructure development zone. In accordance with Ind. Code ch. 6-1.1-12.5, Montgomery County executives adopted an ordinance designating a geographic territory as an Infrastructure Development Zone.

As summarized above, OUCC witness Stull opposed Indiana American's proposed surcharge for three reasons. She also raised questions about the overall calculation. Ultimately, the OUCC recommended that Indiana American instead include the costs of the project in rate base and recover these costs through its cost of service allocation to the appropriate customer classes.

In response to Ms. Stull's first contention that request for approval of the project should have been made prior to installation for Ind. Code § 8-1-2-42.6 to apply, Mr. Shimansky testified that the statute only requires approval of the project. The plain language of Ind. Code § 8-1-2-42.6(e) does state that a utility that "receives a request" for extension of service "may file a petition with the [C]ommission seeking approval of the requested extension of service." However, the OUCC did not take issue with the underlying project or the extension of service; rather, the OUCC took issue with the surcharge and how it was to be applied to Montgomery County customers. Thus, we agree with Indiana American that this is not an issue regarding the reasonableness of the underlying project, but rather an issue of rate design that the Commission has authority to approve with or without a statute. Nonetheless, we do believe the intent of the statute is for utilities to come in and seek approval of the extension of service project prior to filing for approval of a surcharge in a general rate case, and we would encourage utilities to follow this process in future cases.

In response to Ms. Stull's second contention that the application of the surcharge throughout Montgomery County is contrary to Petitioner's agreement with the County and the County Redevelopment Commission, we agree with Indiana American that it is the Montgomery County Commissioners' ordinance—not the agreement—that should control in this situation. *See* Pet. Ex. 2, Attachment GDS-3. This ordinance provides that the surcharge would be payable "by customers located in the geographic area within the jurisdiction of the Commissioners, including the geographic area established as an Infrastructure Development Zone." *Id.* at 2. The Commissioners adopted this ordinance after signing the agreement and we believe this ordinance represents the Commissioners' final word on the subject and their ultimate decision for the surcharge to apply throughout Montgomery County, which is consistent with Petitioner's filing in this Cause.

Finally, we disagree with the OUCC's third contention that the costs of this project should be reflected in Petitioner's rate base and recovered through Petitioner's cost of service allocation to the appropriate customer classes. Petitioner's Exhibit 2, Attachment GDS-3 clearly demonstrates the Montgomery County Board of Commissioners' desire for this main extension to support an economic development project for Montgomery County. Further, the ordinance clearly demonstrates that the Commissioners intended for this extension to be payable only by customers located within the jurisdiction of the Commissioners, including the geographic area established as an Infrastructure Development Zone. This extension of service is an economic development project that will create economic benefits for the County and benefit the health, safety, and welfare of Montgomery County citizens. Thus, this project will only directly benefit Montgomery County and its citizens, and we disagree with the OUCC that it is appropriate for Indiana American to recover these costs from all customers. Further, we believe that recovering the costs of this project via the surcharge as Petitioner has proposed, is consistent with the Montgomery County Commissioners' ordinance and will benefit all of Indiana American's customers, because it will only be recovered from those Indiana American customers in Montgomery County that are positioned to directly benefit from the project. As such, we find that the Montgomery County extension of service and surcharge are appropriate and should be approved.

With respect to the issues Ms. Stull raised regarding Indiana American's calculation, we find Indiana American appropriately calculated the surcharge. We also agree that it is appropriate for Petitioner to accept the OUCC's position that Petitioner's investment is exempt from property tax, and thus we find the revised calculation of the surcharge set forth on Petitioner's Exhibit 15, Attachment GDS-3R to be appropriate and should be approved.

16. URT Repeal.

A. INAWC Case-in-Chief. Mr. Shimansky explained the URT over-collection. He described the repeal of the URT through House Enrolled Act 1002 effective May 1, 2022 and Petitioner's 30-Day filing to remove the URT from its revenue requirement effective July 1, 2022. Mr. Shimansky stated the OUCC filed an objection to that 30-Day filing leading to a subdocket being created in Cause No. 45734 S1. Indiana American filed its revised tariff on October 20, 2022 and on November 23, 2022, the new tariff was approved removing the URT. Mr. Shimansky explained that during the period of time from July 1, 2022 through November 23, 2022, the URT remained in the revenue requirement and was collected in rates, producing an over-collection of $1,356,008 that needs to be returned to customers. INAWC proposed returning this over-collected balance to customers during the Step 1 rate change on a special tariff that expires after four months. Mr. Shimansky stated this would mean the balance would be returned over approximately the same time frame it was collected. He stated that because the over-collection was collected through both volumetric and fixed rates for both water and wastewater customers, the correction should happen the same way.

B. OUCC. Ms. Sullivan testified that the OUCC recommends a direct refund of all URT revenue collected after June 30, 2022, including carrying costs, as a separate line-item credit on the customer bill. Ms. Sullivan proposed that Petitioner should pay customers for the use of the over-collected funds at Petitioner's WACC. She stated there is no reason for Petitioner to wait to refund the over-collection. She contended that Petitioner's proposed revenue adjustment would only incorporate URT collected through September 30, 2022 despite URT being included in rates through November 23, 2022.

C. Industrial Group. Mr. Gorman expressed concern that under INAWC's proposal, Petitioner will not have fully refunded customers until June 2024, roughly two years after it should have ceased collecting the URT from customers. Mr. Gorman testified that throughout that period of time Petitioner has had access to, and been able to use, those funds for its benefit. He testified that customers should be compensated for the use of these customer funds by Petitioner. Accordingly, Mr. Gorman recommended the URT balance be adjusted to include a carrying charge on the funds INAWC collected from customers, which should be included as part of the refund to customers. In support of his recommendation that the Commission include simple interest at a rate of 8% as a component of the refund calculated in this proceeding, Mr. Gorman cited the Indiana Supreme Court's holding in *N. Ind. Pub. Serv. Co. v. Citizens Action Coalition of Ind., Inc.*, 548 N.E.2d 153 (Ind. 1989), that customers were entitled to simple interest at the statutory rate of 8% in the context of a utility refund. He stated that similar to a customer deposit, the utility has had the use of those funds since it began collecting them. Therefore, according to Mr. Gorman, just as customer deposits carry interest, these funds should carry interest to properly compensate customers for Petitioner's ability to utilize the over-collection of the URT. He proposed to include a carrying charge on the customer held funds from the time the excess tax was collected until the refunds are completed in June 2024. He calculated this would increase the URT refund amount by approximately $184,000.

D. **CAC.** Mr. Inskeep testified Petitioner failed to follow directives and suggests Petitioner has held onto ill-gotten revenues. He recommended the entire balance in the over-collection along with an 8% interest be returned at once to customers. He further suggested that the approved ROE be reduced as a penalty for Petitioner not following state law.

E. **INAWC Rebuttal.** Mr. Shimansky opposed the OUCC's and intervenors' proposal to include carrying costs on a simple over-collecting, stating it is inconsistent with the other regulatory accounts included in the case, including the recovery of deferred COVID costs, Comprehensive Planning Studies, and Universal Affordability Tariff costs. In addition, Mr. Shimansky contended that if this over-collection is to be treated as a loan from customers that are due an 8% interest, it should be included in the capital structure with an 8% cost of financing.

Mr. Shimansky testified that Mr. Gorman's calculation of the additional refund amount to account for interest was incorrect. He said Mr. Gorman's proposed adjustment assumes the entire over-collection that has the 8% interest applied to it occurred on July 1, 2022. Mr. Shimansky clarified that it did not. Instead, it was a build-up of rates collected over time from July 1, 2022 while the URT calculation was being contested, until late November 2022 when rates were finally approved and implemented. Mr. Shimansky further stated that if carrying charges were to be applied, they should be no higher than the WACC approved in this case, because there was no wrongdoing on the part of Petitioner.

In response to the OUCC, Mr. Shimansky explained that the point of a revenue adjustment to the September 2022 revenue number is to "normalize" the revenues in the base year. Adjusting the revenues to reflect the URT repeal is one such adjustment. He stated the amount of refund Petitioner will put in rates is the actual over-collection from July 1, 2022 through the time period when the URT repeal was actually put into rates, which is beyond September 30, 2022. Mr. Shimansky also opined that a separate line item on the bill would only create confusion as the URT is no longer in rates and add unnecessary complexity to the bill.

Mr. Shimansky disagreed that Petitioner somehow acted improperly and should be penalized through the ROE as a result. He relayed how Petitioner followed the statute and Commission procedure. He stated it is clear from the copies of Petitioner's URT repeal submissions that Petitioner did nothing incorrectly and followed the established regulatory process.

F. **Discussion and Findings.** As noted by Petitioner, House Enrolled Act 1002 repealed the collection of URT in rates effective July 1, 2022. *See* Ind. Code § 8-1-2-4.2. On June 20, 2022, the Commission opened Cause No. 45734 to address compliance by jurisdictional utilities who were to remove the URT from their rates through the Commission's 30-Day filing process. Further any utilities continuing to collect the utility receipts tax on July 1, 2022, was required to apply regulatory accounting treatment, such as the use of regulatory liabilities, to account for the unlawful collection of the URT. Indiana American was the only jurisdictional utility with fixed monthly and volumetric charges to file a 30-Day filing that did not include a proposal to reduce both charges to remove the URT, resulting in an objection and requiring a subdocket.

The disagreement among the parties now concerns how the URT overcollection should be returned and whether interest should be included. We agree with the OUCC and Intervenors that customers are entitled to interest on the over-collected URT amount. Once removal of the URT from Petitioner's rates was approved, Petitioner could have made another 30-Day filing to refund the overcollection of the URT, but it chose not to do so. *See* 170 IAC 1-6-3(7). Thus, because Indiana American has had use of the entirety of the URT overcollection (funds which belong to the customer) since at least November 23, 2022, we find it appropriate that the refund of the over-collected URT include interest from that date until the over-collection is refunded. Contrary to the Petitioner's assertions, interest is not a penalty. As explained in *N. Ind. Public Serv. Co. v. Citizens Action Coalition*, 548 N.E.2d 153, 159 (Ind. 1989), in reversing a Commission order that did not apply interest to a customer refund, "denying interest on the sum [would amount] to a double wrong by depriving the person owed of the increase to which he was justly entitled and by allowing the one holding the funds to profit from the use of funds that did not rightly belong to him."

Having determined interest is appropriate from November 23, 2022 until the refund is completed, we must now determine the appropriate interest rate. Because Indiana American had the choice to refund the over-collected URT earlier and chose not to do so, we find the statutory interest rate of 8% to be reasonable. Petitioner may refund the URT over-collection at one time or may refund it over four months following implementation of Step 1 rates as proposed.

The OUCC also recommended that the refund occur as a separate line-item credit on the customer bill. While we decline to require Indiana American include the credit as a separate line-item, we do require Petitioner to provide notice to its customers that the bill reflects a credit due to the repeal of the URT, consistent with the requirements of Ind. Code § 8-1-2-4.2(e).

Within 30 days of the issuance of this Order, Petitioner shall make a compliance filing under this Cause with the supporting calculation of the URT refund amount and applicable interest to be computed from November 23, 2022 through the anticipated refund date of the URT over-collection. Included in the compliance filing should be the methodology used to compute the interest, the total amount to be refunded by class and Group, a draft customer notice, and the proposed billing cycle(s) the over-collection will be returned. The other parties in this Cause shall have five business days to file any objection to Petitioner's calculation.

17. Non-Recurring Charges.

A. INAWC Case-in-Chief. Mr. Shimansky presented the proposed tariffs as Attachments GDS-1 and GDS-2 to Petitioner's Exhibit 2. Indiana American did not propose any changes to its non-recurring fees, including its reconnection charge, insufficient funds charge, and after hours service charge. Mr. Rea explained how revenue projections for these fees were developed. He said revenue projections for returned check charges, reconnect fees, after hours charges, and miscellaneous service revenues are all based on a three-year average for the calendar years 2018, 2019, and 2021. He added that revenue projections for late payment fees are based on the actual ratio of late payment fees to total revenue for the 12 months ended September 2022 base year projected to forecast test year revenue amounts.

B. OUCC. Ms. Sullivan explained that reconnection fees were last updated in 30-Day filing #3097, approved by the Commission on July 17, 2013. She said insufficient funds and after-hours service charges were last updated in Cause No. 43680 (May 2010). She opined that Petitioner's non-recurring charges are out-of-date. She said that the costs of these services have certainly increased over the past ten to 13 years. She explained that the OUCC recommends Indiana American include a proposal to adjust its non-recurring charges in its next general rate case or submit a 30-Day filing just prior to its next general rate case to prevent over collection.

C. **CAC.** Mr. Inskeep recommended denying the continuation of Indiana American's late fees, reconnection fees, after-hours charges, and insufficient funds charges, asserting that they disproportionately harm vulnerable customers and significantly exacerbate affordability concerns, running counter to Petitioner's stated goals underlying its Utility Affordability Tariff.

D. **INAWC Rebuttal.** Mr. Shimansky explained he did not agree that all late fees, reconnection fees, after-hour charges, and insufficient fund charges should be eliminated. He said these charges have been approved by the Commission as part of Petitioner's tariff and there was no forecast created in this case to change those fees. He said the miscellaneous revenues created by those fees were used in the revenue determination. Mr. Shimansky explained that eliminating those fees would create a need to reassess the expenses forecasted for these programs as well as the revenue allocation amongst all customers. He said a proper study would need to be done before they were to be changed. He explained that Petitioner is not opposed to updating these rates prior to the next rate case, but because these fees and charges recover costs incurred by Petitioner, he concluded outright elimination of the fees would not be appropriate.

E. **Discussion and Findings.** As evidenced by Petitioner's case-in-chief filing and explained by Indiana American witness Shimansky, Petitioner is not proposing to change the non-recurring fees established in 30-Day filing #3097 or Cause No. 43680. Pet. Ex. 2, Attachment GDS-1, at 30, and GDS-2 at 12, Pet. Ex. 15 at 62, and Pub. Ex. 2 at 27. It is the OUCC and CAC that seek a change to what the Commission has previously approved.

The Commission is not persuaded that elimination of these fees is reasonable or appropriate at this time. While the Commission has suspended the collection of these fees in extenuating circumstances, providing these services comes at a cost to Petitioner and as such, should be reflected in rates. Further, without a study, which no party put forth, we lack evidence showing whether costs to provide these services have increased or decreased and what the effect on Petitioner's expenses might be if there were an elimination of these fees. As Mr. Shimansky explained, eliminating all non-recurring fees would need to be considered in the expense forecast and could affect the revenue allocation among all customers. The Commission, in this instance, declines to make a change that affects cost allocation without further information. However, based on Mr. Shimansky's rebuttal, it appears Petitioner is not opposed to the OUCC's recommendation to update these fees prior to or in its next rate case. Accordingly, we encourage Petitioner to evaluate whether the costs of these services have changed and as appropriate, adjust its non-recurring fees.

18. **Tariff Matters.**

A. **INAWC Case-in-Chief.** Mr. Shimansky presented the proposed tariffs as Attachments GDS-1 and GDS-2 to Petitioner's Exhibit 2, inclusive of redlined changes.

B. **OUCC.** Ms. Sullivan claimed Petitioner's current tariff is difficult to understand. She said moving Area 2 and Area 3 customers to Area 1 will eliminate some confusion. She further stated that the OUCC urges Indiana American to publish a tariff that is easier for a customer to understand so they can quickly discern how their bills are calculated.

C. **CAC.** Mr. Inskeep requested Indiana American be required to publish its entire tariffs, rules, and regulations on its website in an accessible manner. Mr. Inskeep states the lack of text-search functionality on some pages makes finding information not only difficult, but an accessibility issue. He said the public and all of Indiana American's customers, including individuals with disabilities, should be able to access all of Petitioner's tariffs.

D. **INAWC Rebuttal.** Mr. Shimansky testified that Petitioner appreciates the feedback on its tariffs and has since ensured that the tariffs and rules on Petitioner's website are fully searchable. Mr. Shimansky explained that Petitioner hopes this helps provide customers easier access to its tariffs.

E. **Discussion and Findings.** The OUCC and CAC expressed concern with Indiana American's tariff language and accessibility of the tariffs but made no specific recommendations for change other than those concerning tariff publication on Petitioner's website. As Mr. Shimansky testified, Indiana American has taken action to ensure that the tariffs and rules on its website are fully searchable. We encourage Indiana American to periodically review and revise its tariffs to be clearer and more understandable and to continue to be responsive to customer and stakeholder feedback about improving the presentation of, and ability to understand, Petitioner's tariff.

19. **Customer Service.**

A. **Lowell Service Area.** OUCC witness Seals highlighted and discussed certain of the customer comments received by the OUCC, with emphasis on comments received regarding the Lowell system, which Indiana American acquired in 2021. Mr. Seals noted that, based upon IDEM records, for the first six months of 2023, the Lowell operation experienced 28 boil advisories, with 12 caused by main breaks. He compared this level of boil advisories to Petitioner's larger Wabash operation, which experienced three boil advisories during the same period. Mr. Seals recommended Indiana American be required to evaluate the repeated main failures and resultant boil water orders in the Lowell district and provide the Commission with a report as to proposed solutions within 90 days.

Indiana American witness Britto, responding to Mr. Seals' concerns, stated "[s]ince acquiring the Lowell System, we have encountered a number of broken valves. Undertaking system improvements in such an environment will at times cause pressures to drop throughout the system. Pursuant to IDEM guidance regarding Boil Water Procedures, Indiana-American issued boil water advisories for each of these instances as required." Pet. Ex. 17 at 19. Ms. Britto disagreed with Mr. Seals' recommendation, stating Petitioner "is already evaluating the system and making capital investment to address the aging infrastructure." *Id.* at 20. We find Mr. Seals raises an important concern about the Lowell system. As it appears from Ms. Britto's rebuttal testimony that Petitioner is aware of the problems and is already evaluating the system, we find Indiana American should prepare a report outlining the issues seen in the Lowell system and its proposed solutions within 90 days of the issuance of this Order.

B. Gary/Northwest Indiana Service Area. At the public field hearing held in Gary, Indiana, we heard from many customers expressing frustration because of Indiana American's lack of local corporate presence, ever increasing rates, operations resulting in basement flooding from lines being cut, and the closure of Indiana American's in-person payment center, which has been a hardship. At the evidentiary hearing, the Presiding Officers asked INAWC witness Britto about locations where customers can make in-person payments or ask questions in the Gary area. Hrg. Tr. at B-22 to B-25. INAWC witness Shimansky was able to provide some information at the hearing about the 12 payment locations in and around the Gary area (around zip code 46401). Hrg. Tr. at E-17. Mr. Shimansky testified that "more than half are Speedy Check cashiers, and there is a City of Hobart location where bills can be paid." *Id*. He said the hours are different at each location, with some open until 11:00 p.m. and others closing at 4:30 p.m. *Id*. We find it is important for customers to have access to locations where they can make payments, preferably without additional fees, and get questions about their accounts answered. We approved almost 30 years ago INAWC's decision to consolidate to a central location all customer service activities, and we did so due in part to the resulting efficiencies and cost savings. *Indiana-American Water Co.*, Cause No. 39595 at 19-21 (IURC Feb. 2, 1994). However, consolidation should not result in the loss of important customer services, including access to Petitioner within the communities it serves. Accordingly, we encourage INAWC to review the feasibility of offering in-person customer service option in light of financial, operational, and customer convenience cost-benefits. We also encourage Petitioner to ensure that each of its payment locations are provided with INAWC customer service contact information that can be provided to customers who may have questions or need additional information about their bills.

20. Non-Revenue Water.

A. INAWC Case-in-Chief. Ms. Britto testified regarding the steps Petitioner is taking to improve water and wastewater efficiency. She testified that Petitioner's efforts include supply side practices, such as improved pump efficiency, meter reading, leak detection, and repair programs, as well as demand-side strategies, such as customer efficiency and public education programs. From an operations perspective, Ms. Britto explained that improving water and wastewater efficiency requires achieving a cost-effective mix of prudent investments and improved O&M management capabilities targeting safety, customer satisfaction, sustainability, and system efficiency. She further testified Petitioner is planning to expand its efforts in improving apparent losses through large meter testing and profiling, conducting fire service audits, and improving Petitioner's billing process.

B. OUCC. Mr. Seals discussed the impact of non-revenue water, pointing out that total company non-revenue water has risen during the past five years, from 18.5% in 2018 to 21.2% in 2022. He stated that four districts experienced greater than 30% non-revenue water during the five-year period, causing IDEM to identify a significant deficiency for these districts. While noting that Indiana American has begun some effective first steps towards reducing non-revenue water, Mr. Seals recommended Petitioner place increased emphasis and resources on addressing the issue through leak detection, fire service audits, and consideration of district metering.

Mr. Seals testified that only 36% of Indiana American's private fire services are metered, making this problematic for non-revenue water. He said unmetered water may pass through the private fire system due to usage for testing, potential leaks on the internal system, or unintentional connections by the customer for non-fire purposes. Mr. Seals testified this potential source of non-revenue water can be mitigated and recommended that Indiana American begin a program to meter all private fire services over the next five years and perform inspections of private fire services once every five years.

C. <u>INAWC Rebuttal</u>. Ms. Britto testified that Petitioner is continuously analyzing and evaluating the amount of non-revenue water in its system to determine what cost-effective steps can be taken to reduce the amount even further. With respect to Mr. Seals' recommendation that Indiana American: (1) increase the emphasis and resources utilized on addressing non-revenue water, especially on leak detection and on fire service audits; (2) investigate other means of measuring and reducing non-revenue water, such as establishing district-metered areas, especially as Petitioner transitions towards AMI; and (3) act on the recommendations contained within the water audits for improvements to be achieved, Ms. Britto testified that Indiana American is doing these things and others to help reduce non-revenue water. She testified that Petitioner is also addressing any metering issues and analyzing its accounted for water losses, as well as analyzing already installed meters to ensure the right size of meters are installed and are representative of current services. She testified these steps will allow Indiana American to capture the flows more accurately for these services. Ms. Britto noted, however, that these activities have costs associated with them, and Petitioner cannot do everything without the increased dollars/headcount to do so.

As to Mr. Seals' recommendations regarding private fire services, Ms. Britto testified that what Mr. Seals recommends will be an expensive investment. She testified that for many customers this cost could run as much as $200,000, since the customer frequently owns the vault. She further testified there would also be significant impact in larger meters being added to these vaults. Ms. Britto testified that should the Commission order Indiana American to make these investments, Petitioner would commence doing so and would include the costs in future DSIC cases.

D. <u>Discussion and Findings</u>. The record shows that Indiana American has taken numerous significant steps to address non-revenue water in its system. The record further shows that the OUCC agrees with the steps Indiana American has taken to reduce non-revenue water and acknowledges that these steps are effective first steps. However, the OUCC also recommends that Indiana American place an increased emphasis on, and dedicate more resources to, addressing non-revenue water, in particular on leak detection and fire service audits.

Ms. Britto testified that Indiana American is already engaging in each of the activities the OUCC recommended to help reduce non-revenue water. However, the OUCC presented evidence that Indiana American's total company non-revenue water increased slightly over the five-year period from 2018-2022, from 18.5% in 2018 to 21.2% in 2022. Additionally, four districts experienced greater than 30% non-revenue water during the five-year period, causing IDEM to identify a significant deficiency for these districts. We note that three of these four districts are recent acquisitions and hence raise concern with the sufficiency of O&M prior to acquisition.

We believe the evidence shows that Indiana American is taking adequate first steps to manage water loss and address non-revenue water within its system. Ms. Britto testified regarding all the steps Petitioner is taking to reduce non-revenue water, explaining Indiana American is continuously analyzing and evaluating the amount of non-revenue water in its system to determine what cost-effective steps can be taken to reduce the amount even further.

Accordingly, we find Indiana American is taking appropriate steps to address non-revenue water within its system and the evidence shows Indiana American will continue engaging in these activities moving forward. While we decline, at this time, to require additional steps or resources beyond those already identified by Petitioner, we encourage Petitioner to continue its efforts to identify and implement cost-effective solutions for addressing its rising non-revenue water.

21. Regulatory Accounting Treatment.

A. INAWC Case-in-Chief. Mr. Shimansky described three proposals for regulatory accounting treatment. The first relates to pension and OPEB expense, the second relates to production expenses and the third relates to the proposed Universal Affordability Tariff. As to pension and OPEB expense, INAWC requests authority to record as a regulatory asset or liability amounts above or below the amount reflected in rates. He described the pension/OPEB balancing account that was proposed by Petitioner in Cause No. 43680, which was denied, and how, if it had been approved, pension and OPEB costs that had gone down in the subsequent years would have been returned to customers.

The production cost regulatory accounting would capture changes in chemical cost, purchased fuel and power, waste disposal, and purchased water. Production costs above and below the amount used to set rates would similarly be deferred to a regulatory asset or liability.

As to the Universal Affordability Tariff, which will provide discounts to participating and qualified customers, INAWC proposes an assumption that 10% will participate, and projected the level of discounts that would be provided as $1.3 million for Step 2 and $1.4 million for Step 3. To the extent the actual discounts vary from these amounts, the difference would be deferred as a regulatory asset or liability.

B. OUCC. Ms. Stull responded to Indiana American's proposed regulatory accounting deferral treatment for production costs and costs related to the Universal Affordability Tariff. As to production costs, she testified the OUCC opposes the proposal because it would remove any incentive for Petitioner to efficiently manage and operate its utility operations and otherwise negates basic regulatory principles. She explained that when a utility's rates are set, the utility is given the opportunity to earn its authorized return, which is not a guarantee. She noted that neither is a utility prevented from exceeding its authorized return. She explained this system promotes efficiency because it incents utilities to hone their operations through good management so it may retain more of its earnings. She said allowing a utility to track costs and recover the difference between the amount included in rates and the actual expense discourages efficient management and negates a basic principle of ratemaking.

Ms. Stull testified that Indiana American intends to track any and all differences between actual and projected production costs included in its revenue requirement without differentiating between production cost increases due to increased demand versus increases in price, which she viewed as problematic. She testified Indiana American has not allowed for the fact there could be offsetting changes to operating revenues that would already compensate Indiana American for certain types of changes in production costs, such as higher than projected customer growth or customer consumption, which can be caused by such things as a drought. She explained both of these factors would create increased production costs that would be recovered through increased operating revenues and would allow Petitioner to potentially over-recover these cost increases. Moreover, Ms. Stull testified Indiana American already has the ability to track increases to its purchased water expense, noting that if an unprojected cost increase occurs, Indiana American has the option of submitting a purchased water tracker under 170 IAC 1-6 to recover the increased expense. Thus, she concluded, there is no need to provide another mechanism for Indiana American to recover these cost increases.

As for the Universal Affordability Tariff, Ms. Stull stated the OUCC recommends Petitioner's proposed tariff be rejected and therefore, no deferred accounting treatment would be warranted on that basis.

C. Industrial Group. Mr. Gorman recommended the Commission reject INAWC's three proposals to defer in regulatory assets. He testified that the three deferral mechanisms place too much risk on customers and do not include significant protections to customers from paying rates that are no more than a just and reasonable level. He testified that Petitioner has not shown these expenses limit the ability to earn its authorized return under the revenues generated during rate-effective periods in the past or are largely outside its control or more variable than they have been in the past.

D. INAWC Rebuttal. Mr. Shimansky testified that these accounts are not being proposed to provide a rate of return but to protect both customers and Petitioner from volatility. He testified that the variances in these costs are almost entirely outside the INAWC's control. For instance, variations in pension expense are driven by market pressures. In response to Ms. Stull's testimony that regulatory accounting would remove incentives to manage production costs, he indicated that since the deferred amounts would not bear carrying charges, there is still an incentive for Petitioner to do all it can do to manage costs.

E. Discussion and Findings. Indiana American requests regulatory accounting deferral treatment for: (1) pension and OPEB expense, (2) production costs, and (3) Universal Affordability Tariff discounts. Based on our decision above, we need not address Petitioner's request for regulatory accounting deferral treatment for the Universal Affordability Tariff discounts.

When determining whether costs should be tracked, we have generally considered whether the expenses are "collectively or potentially significant, whether they are potentially variable or volatile, and whether they are largely outside the utility's control." *Indianapolis Power & Light Co.*, Cause No. 44602 at 79 (IURC March 16, 2016). We also consider the utility's request from a broader perspective by reviewing "the utility's risks related to its operating costs and the other tracking mechanisms it has in place." *S. Ind. Gas and Elec. Co.*, Cause No. 43839 at 94 (IURC Apr. 27, 2011). We have generally found that revenue or cost trackers tend to make utilities less accountable for their actions and thus, should remain limited to ensure the utility is properly incented to manage its overall operating costs. *Id.* at 94-95. Because, if utilities can "recover the majority of their variable costs through trackers, they have no incentive to come before the Commission and account for other, non-tracked, decreasing costs or increasing revenues." *Id.*

In 2010, the Commission rejected a proposal by Petitioner to create a "Pension and OPEB Balancing Account" that would have allowed the utility to "defer under- or over-recovery in Pension/OPEB expense as a regulatory asset/liability for future recovery or refund to customers." *Indiana-American Water Co.*, Cause No. 43680 at 111-112 (IURC April 30, 2010). In that case, we rejected the requested relief determining that if we were to authorize the creation of the balancing account and related regulatory accounting treatment, we would be shifting risks inherent to the prudent operation of the utility to ratepayers, thereby lessening the utility's incentive to manage its business properly and effectively. Accordingly, we ultimately concluded that it was "not in the public interest to require ratepayers to bear this risk." *Id.*

In the present case, Indiana American again seeks approval of balancing accounts and regulatory accounting treatment. This time, however, it seeks that treatment not just for its pension and OPEB expense, but also for its production costs. These three separate regulatory accounts would operate in the same manner. Specifically, beginning with the effective date of new rates established in this case, Indiana American would begin comparing its actual expenses in each of these categories to the amount approved for recovery and embedded in base rates with the total difference being treated as a regulatory asset or liability in the next rate case.

Petitioner requests this extraordinary relief because it claims the relief will protect itself, and customers, from volatility in those expenses. The proposed deferred regulatory treatment differs little, if at all, from the relief we denied in Cause No. 43680, which was based on substantially the same justification offered in this proceeding. Seeing the same problems with Petitioner's current proposal as we saw with its past proposal, we see no reason to alter or deviate from our prior decision.

We agree with the OUCC and other Intervenors that what Petitioner requests is to be shielded from volatility inherent to the operation of a utility. Some risk of volatility or uncertainty as to the performance of the market or, for example, as to the actual cost of chemicals, is not justification to authorize deferred accounting. While Petitioner speculated about the potential impact of market fluctuations and price volatility, the evidence does not show that the variability in costs will expose Petitioner to the risk of not meeting its service obligations or shareholders to not earning a reasonable return, or that the requested relief will fundamentally benefit ratepayers.

Our ability to balance those interests is essential as it lies at the heart of the regulatory compact. As part of that compact, in exchange for the dedication of its plant and equipment to the service of the public, a utility is given the opportunity to earn its authorized return, recovering both its reasonable and prudent costs and a reasonable return on its investment. As Ms. Stull points out, however, the opportunity for Indiana American to earn its authorized return is not a guarantee. The opportunity to earn its authorized return provides the incentive for the utility to operate efficiently, an incentive which we have previously found to be put at risk through risk shifting proposals, such as balancing accounts proposed by Petitioner. We also note that Petitioner has access to, and uses, several tracking mechanisms to recover costs associated with a range of investments. There is also an established rule and standard practice in place that allows utilities to quickly amend their rates to cover increases in purchased water costs—one of the costs INAWC seeks to include in the balancing account.

In conclusion, we find Indiana American has failed to show that the balance struck between the utility and its ratepayers as a result of its proposed balancing accounts is in the public interest. Accordingly, we decline to approve Petitioner's requested accounting deferral treatment.

22. Future DSIC and SEI Cases. The only remaining dispute regarding future DSIC and SEI cases relates to how cost of removal is accounted for in the DSIC and SEI calculations. OUCC witness Stull explained cost of removal is recovered from customers before these costs are actually incurred by Petitioner because the cost is built into Indiana American's authorized depreciation rates. Indiana American continues to recover these costs because (a) it is embedded in the depreciation rates used to calculate depreciation and (b) DSIC and SEI additions are not reduced by the increase in applicable accumulated depreciation since the last rate case. She argued this treatment results in a level of double recovery that inequitably benefits shareholders at the expense of ratepayers. While recovery of the cost of removal results in a reduction to rate base, Ms. Stull stated she does not believe that the quid pro quo of this arrangement is evenly balanced between ratepayers and shareholders because the reduction in rate base only occurs when Indiana American files a rate case. Between rate case filings, Indiana American recovers additional costs of removal but there is no corresponding reduction to rate base that benefits ratepayers until Indiana American receives its next rate order.

As Mr. Shimansky noted in rebuttal, the Commission previously addressed this issue in its February 22, 2023 Order (at p. 8) in Cause No. 45609 SEI 1, wherein the Commission authorized the inclusion of costs of removal in the SEI calculation because it was consistent with the approach used in DSIC cases.[28] Although, Ms. Stull is correct about the costs of removal being embedded in depreciation rates, in the context of a tracker, it is necessary to include the costs of removal in the pretax return because the accounting entries to retire the assets are recorded on the utility's books and records, but these entries are not reflected in the tracker amounts. Thus, the costs of removal associated with retired assets must be included in the pretax return calculation of a tracker case.

When assets in a tracker filing are retired, the accounting entries to retire the assets will be recorded on the utility's books and records, including a debit to accumulated depreciation for the associated cost to remove the retired asset. When a debit entry is recorded to accumulated depreciation to account for the cost of removal, the effect is to increase rate base by the same amount. However, the effect of these accounting entries will not be reflected in base rates until the utility's next base rate case. Until that time, the utility's rate base is understated by the amount of removal cost recovered through depreciation expense and reflected in the accumulated depreciation account. Essentially, accumulated depreciation is overstated by the cost of removal which has not yet been incurred reducing rate base until the cost of removal takes place. In a tracker filing, the base rates do not include the debit to accumulated depreciation until the next base rate case. Thus, it is reasonable to provide a return on the cost of removal in a tracker filing to offset

[28] *See also*, *Indiana American Water*, Cause No. 45609 SEI 1 S1 at 9 (IURC March 8, 2023).

the lower rate base generated by the cost of removal reflected in accumulated depreciation on the utility's books and records. This permits the utility to earn a return on cost of removal associated with retired assets in a tracker, which will end when new rates are established. The cost of removal will be reflected in base rates and the tracker will be reset to zero. This issue is a matter of timing.

23. **<u>Confidentiality</u>.** On March 31, 2023, August 4, 2023, and August 8, 2023, Indiana American filed Motions for Protection and Nondisclosure of Confidential and Proprietary Information in this Cause, which were supported by affidavits showing that certain information to be submitted to the Commission was trade secret information as defined in Ind. Code § 24-2-3-2 and should be treated as confidential in accordance with Ind. Code §§ 5-14-3-4 and 8-1-2-29. On July 21, 2023, and July 25, 2023, the Industrial Group also filed Motions for Protection and Nondisclosure of Confidential and Proprietary Information in this Cause. In Docket Entries dated April 13, 2023, August 8, 2023, and August 14, 2023, the Presiding Officers found the information should be held confidential on a preliminary basis. After review of the information and consideration of the affidavits, we find the information is trade secret information as defined in Ind. Code § 24-2-3-2, is exempt from public access and disclosure pursuant to Ind. Code §§ 5-14-3-4 and 8-1-2-29, and shall be held as confidential and protected from public access and disclosure by the Commission.

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

1. Petitioner is authorized to adjust and increase its rates and charges for water and wastewater service in three steps approved herein, ultimately calculated to produce total operating revenues of $350,524,090, which are calculated to provide the opportunity to earn net operating income of $118,092,625. Such rates and charges for each step shall take effect immediately upon submission, on an interim subject to refund basis subject to the process for review by the parties we have approved.

2. Petitioner shall file new schedules of rates and charges in three steps on the basis set forth in Finding Paragraph 12, which schedules shall be effective for water and wastewater service rendered upon submission on an interim subject to refund basis subject to the compliance filing process described in that same finding paragraph.

3. Within 30 days of the issuance of this Order, Petitioner shall make a compliance filing under this Cause concerning the URT refund consistent with Finding Paragraph 16.

4. Petitioner's proposed depreciation accrual rates are approved upon the submission of Step 1 rates.

5. Petitioner's requests for deferred accounting authority described in Finding Paragraph 21 are denied.

6. Petitioner's proposed Montgomery County surcharge is approved.

7. Petitioner's proposed Universal Affordability Tariff is denied.

8. Petitioner's plans to develop future water sources of supply are approved as set forth in Finding Paragraph 7.A.2.b.

9. The information filed by Petitioner, OUCC, and Intervenors in this Cause pursuant to the Motions for Protective Orders is deemed confidential pursuant to Ind. Code § 5-14-3-4, exempt from public access and disclosure by Indiana law, and shall be held confidential and protected from public access and disclosure by the Commission.

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

BENNETT, FREEMAN, VELETA, AND ZIEGNER CONCUR; HUSTON ABSENT:

APPROVED: FEB 14 2024

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

Dana Kosco
Digitally signed by Dana Kosco
Date: 2024.02.14 10:11:11
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Dana Kosco
Secretary of the Commission

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF INDIANA-AMERICAN WATER COMPANY, INC. FOR (1) AUTHORITY TO INCREASE ITS RATES AND CHARGES FOR WATER AND WASTEWATER UTILITY SERVICE THROUGH A THREE-STEP RATE IMPLEMENTATION, (2) APPROVAL OF NEW SCHEDULES OF RATES AND CHARGES APPLICABLE TO WATER AND WASTEWATER UTILITY SERVICE, INCLUDING A NEW UNIVERSAL AFFORDABILITY RATE, (3) APPROVAL OF REVISED DEPRECIATION RATES APPLICABLE TO WATER AND WASTEWATER PLANT IN SERVICE, (4) APPROVAL OF NECESSARY AND APPROPRIATE ACCOUNTING RELIEF, (5) APPROVAL OF THE EXTENSION OF SERVICE TO AN INFRASTRUCTURE DEVELOPMENT ZONE IN MONTGOMERY COUNTY, INDIANA AND AUTHORITY TO IMPLEMENT A SURCHARGE UNDER IND. CODE § 8-1-2-46.2, AND (6) APPROVAL OF PETITIONER'S PLANS TO DEVELOP FUTURE WATER SOURCES OF SUPPLY UNDER IND. CODE § 8-1-2-23.5.	)	**CAUSE NO. 45870** **APPROVED: FEB 14 2024**

<u>CONCURRING OPINION OF COMMISSIONER SARAH E. FREEMAN</u>

I concur in today's order and write separately to emphasize three issues of importance.

First, by encouraging and providing guidance to Petitioner to submit a redesigned Universal Affordability Tariff — rather than ordering and dictating the contents of a redesigned tariff — we acknowledge the permissive language enacted by the Indiana General Assembly in its authorization of customer assistance programs under Ind. Code § 8-1-2-46(c). I firmly believe that Petitioner is invested in improving affordability for its ratepayers and will be beyond shocked if Petitioner, in cooperation with the OUCC and CAC, does not submit a redesigned Universal Affordability Tariff in short order, and I eagerly await the opportunity to review.

Next, I write to amplify the concerns underlying our decision in Section 19.B. related to the dwindling opportunities for Indiana American ratepayers to engage in face-to-face communications with Indiana American customer service representatives. The original authority to consolidate in-person service locations and instead rely on robust shared services was logical and supported by evidence of efficiencies and cost savings. However, this particular end game — with no in-person interactions between utility and ratepayer — was not an inevitable outcome; it was a choice. Many communities, with Gary being a leading example, suffer disproportionately when the opportunity for in-person engagement is removed. Petitioner regularly asserts its desire to be a model corporate citizen, yet it repeatedly squanders its chances to do so. As a first step, perhaps Indiana American could access the shared services of American Water to identify and develop creative uses of existing technology to connect ratepayers paying in person in physical locations directly with Indiana American customer service representatives to respond to immediate questions and concerns. A solution need not be overly complicated or require excessive resources to succeed.

Finally, I commend the relevant and useful testimony presented at the July 6, 2023 field hearing in Gary, Indiana. This field hearing stands out because the witnesses conveyed the reality of their situations within the framework of the issues presented in this proceeding and because of the constructive and practical solutions they offered Petitioner to increase and improve its presence and reputation as a corporate citizen. Of note was testimony highlighting apprenticeships as a way for Petitioner to demonstrate its commitment to its individual ratepayers and the larger community as well as a particularly elegant suggestion that Petitioner provide rain barrels to interested customers, simultaneously promoting conservation and the Indiana American brand.

STATE OF INDIANA

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<u>CONCURRING OPINION OF COMMISSIONER DAVID E. ZIEGNER</u>

I concur in the Order but write to emphasize a concern I have regarding the absence of the availability for customers to have face to face communications with utility personnel. Indiana American should explore innovative ways to enhance direct communications with customers who have billing and service issues.

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

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<u>CONCURRING OPINION OF COMMISSIONER WESLEY R. BENNETT</u>

I concur in today's Order and the Concurring Opinion of Commissioner Freeman. In addition, I write separately to express my concern with Indiana American's compliance with Ind. Code § 13-18-26-2. This statute requires a utility applying for a wastewater treatment plant permit to certify that it has prepared and completed a LCCBA. However, the evidence demonstrates that Petitioner did not complete a full life cycle cost benefit analysis, as that term is generally understood in the engineering world. Therefore, it appears to me that Indiana American has not complied with Indiana law.

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