IN THE
COURT OF APPEALS OF INDIANA

No. 23A-EX-458

COMMUNITY UTILITIES of INDIANA, INC., *Appellant*, v. INDIANA UTILITY REGULATORY COMMISSION, et al., *Appellees*.	Appeal from the Indiana Utility Regulatory Commission, Cause No. 45651 Hon. James F. Huston, Chairman, Hon. Sarah E. Freeman, Commissioner, Hon. Stefanie Krevda, Commissioner, Hon. David E. Veleta, Commissioner, Hon. David E. Ziegner, Commissioner. Hon. Jennifer L. Schuster Senior Administrative Law Judge

BRIEF OF APPELLEE
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STATEMENT OF THE ISSUE

Whether the Indiana Utility Regulatory Committee's (IURC) decision—that, at this time, Community Utilities of Indiana, Inc. ("Community") could not recover, through a rate increase, engineering costs on proposed capital wastewater expansion projects that were denied pre-approval—was based on substantial evidence.

STATEMENT OF THE CASE

Community is a water and wastewater utility in northwestern Indiana that is regulated by the IURC. This appeal involves Community's most recent petition for general rate increase for water and wastewater services filed on December 7, 2021 (2 App. 11). The petition included a request for engineering costs for proposed wastewater improvement projects that were denied pre-approval because the IURC had found they were not necessary or used and useful (2 App. 73–74). The Indiana Office of Utility Consumer Counselor ("OUCC"), representing the public and ratepayers, and intervenors the Lakes of the Four Seasons Property Owners' Association ("Lakes of the Four Seasons") opposed Community's petition (2 App. 11).

After an evidentiary hearing on June 18, 2022, the IURC issued its final order on February 1, 2023. The final order denied recovery of the engineering costs for the previously denied wastewater upgrades but granted Community an increase in its rates in two phases for a total increase to annual authorized revenues of $2,321,863 (2 App. 7, 93–94). Community filed a petition for reconsideration with

the IURC on February 21, 2023, regarding certain denied costs, including the engineering costs (2 App. 98). Community filed a notice of appeal on March 1, 2023, but on its motion to stay pending reconsideration, the appeal was stayed on March 22, 2023 (2 App. 98). On May 3, 2023, the IURC granted, in part, Community's petition for reconsideration as to a portion of its prior legal cost but still disapproved the disputed engineering costs (2 App. 101–104). The stay of this appeal was lifted on May 9, 2023 (2 App. 98).

STATEMENT OF FACTS

Community was formed in 2015 as a merger of three smaller water and wastewater utilities in northwestern Indiana and serves approximately 5,300 residential water customers and 3,500 residential wastewater customers (II App. 11). Three main developments are relevant to this Court's resolution of the issue in this case; (A) Community's 2018 Rate Case and the required system improvement plan; (B) IURC's denial of pre-approval for Community's proposed capital project to expand its wastewater system capacity; and (C) IURC's denial of engineering costs for the projects denied in Community's 2021 Pre-Approval Case.

A. Community's 2018 Rate Case and the required System Improvement Plan

In 2018, as part of the final order in Community's previous rate case, the IURC ordered Community to create a master system improvement plan "to decrease total incidences of wastewater backups in homes and manhole overflows and to decrease total complaints about discoloration of drinking water" (Addend. 17; *see also* IURC Cause no. 44724, Addend. 3–21).

1. Required Content of the Plan

Community's system improvement plan had to be "well documented[,]" "include feedback from the OUCC and [Lake of Four Seasons,]" and be "implemented and [have] progress measured and reported" (Addend. 17). The IURC's 2018 final order required Community to develop "two primary components" of the plan to achieve the outlined goals: (1) a comprehensive inflow and infiltration ("I&I") reduction program; and (2) a multi-faceted program to decrease incidences of discolored water[1] (Addend. 17–18).

I&I is the term used to describe unintended water seeping into a wastewater system. I&I can occur from any unintended point of entry into a system's pipes. Common entryways of I&I into a wastewater system include: bent or corroded underground pipes, faulty manhole covers, improper sump pump usage (draining into a sewer pipe), and overflow water from stormy weather. Excessive I&I can overwhelm the installed collection and treatment system and thereby cause wastewater backups in customer homes and damage to utility infrastructure. By reducing the points of entry for I&I, a utility can reduce the volume of wastewater it needs to collect and treat. The 2018 final order required Community's I&I program to:

- "eliminate water inflow and ground water infiltration[;]"

[1] The discoloration issue is related to Community's water utility service, which is not relevant to this appeal.

- "decrease inflow of rain and storm water by working with [Lake of Four Seasons] to eliminate improperly installed residential sump pump and roof down spout and illegally connected drains[;]" and
- "Utilize [Community's] comprehensive asset program to decrease infiltration of groundwater into the wastewater system through leaky joints, cracked pipelines, and deteriorated manholes."

(Addend. 18).

After setting out the primary components—an I&I reduction program and a program to address water discoloration—the order directed Community to "propose capital investments that require [IURC] approvals and suggested timetables for the filings and approvals" (Addend. 17–18). And "[f]or proposed significant capital investments, Petitioner shall provide proper documentation of engineering studies and detailed competitive bids from contractors to support Petitioner's proposals" (Addend. 18).

2. Required Process for Development and Implementation of the Plan

The 2018 final order also set out the process for Community to develop and present its system improvement plan to the IURC (Addend. 18–19). Community was required to meet with IURC staff, OUCC staff, and Lake of Four Seasons in an initial technical conference within 90 days of the final order (Addend. 18). At least five days prior to this first technical conference, Community had to file an agenda and proposed system improvement plan with the IURC (Addend. 18). After the technical conference, IURC staff would provide written recommendations on the

proposed plan, and Community would revise the plan based on those recommendations (Addend. 18). Community was then required to file quarterly status reports with the IURC and hold quarterly technical conferences with the above-listed stakeholders to report on and update the plan (Addend. 18–19).

3. The Technical Conferences and Community's System Improvement Plan

As required, Community initiated the first technical conference (III App. 196-197). In response to Community's initial filings, IURC staff issued written recommendations (III App. 197–198). As to the I&I program, IURC staff concluded that "[Community] has not complied with the [IURC's] Order to develop a comprehensive I/I program" (III App. 197). Staff recommendations noted that Community had "completed the requisite flow monitoring of the system[,]" and, "[o]nce that data is finalized, [IURC] staff expects that [Community] will place more efforts into the appropriate SSO [Sanitary Sewer Overflow] program areas and that the results will drive the prioritization of capital improvements, focusing on rehabilitation/ replacement as opposed to conducting random spot repairs" (III App. 197).

For the next technical conference in August 2018, Community submitted a draft system improvement plan (II App. 129–142). Community's draft plan proposed to reduce wastewater basement backups and manhole overflows in two ways: (1) decreasing flow through developing an I&I reduction program; and (2) increasing capacity by expanding its collection system and upgrading its wastewater treatment plant (II App. 139). To develop an I&I reduction program, Community planned to

co-sponsor an ongoing home inspection program, initiate smoke and dye testing programs, and "[c]ontinue with [its] ongoing Sewer Capital Improvement Program to identify and repair defects in existing sewers and manholes" (II App. 139). Community's plan estimated it would spend approximately $705,000 on I&I reduction—$92,590 on sewer repairs and approximately $612,200 on a "smoke, dye, lateral televising, and manhole inspection project" (II App. 131, 139). In contrast, its plan estimated it would spend more than $30,000,000 on expanding its collection system and upgrading its wastewater treatment plant (II App. 131). In their written recommendations in response to Community's proposed system improvement plan, IURC staff suggested it should, "Continue to evolve [Community's] capital planning efforts as better information becomes available through [Community's] asset management program" (III App. 61).

In October 2018, Community's update system improvement plan showed modest goals for I&I reduction: (1) that 10% of the sewer system would be cleaned and televised in the next month and the remainder by the end of 2020; and (2) 2,715 linear feet of sewer would be lined by the end of November 2018 (III App. 74–75). The plan also reported that 20 manhole covers had been sealed and lined (III App. 75). Requests for proposals had been sent out to engineering companies for the projects to increase system capacity (III App. 76). The same distribution of estimated costs remained, which strongly favored capital improvements in expansion of the collection system and upgrading the wastewater treatment plant, instead of I&I remediation (III App. 66).

According to the agenda for the April 2019 technical conference, Community's only reported progress on the I&I program was: (1) that 101 home inspections had been completed; (2) an unspecified update on the sewer cleaning and televising project; and (3) information that 2,700 linear feet of pipe was lined in 2018 and another 6,000 linear feet were planned for 2019 (III. App. 90–91).

In the October 2019 technical conference agenda, Community reported the following progress on the I&I program: (1) 397 homes were inspected in 2019; (2) 100% of the homes had been smoke tested; and (3) an unspecified update on the lining process (Community's representative made comments on the cost of the process) (III App. 160–61).

B. Denial of Community's Request to Pre-Approve Wastewater Capital Projects for the Expansion of System Capacity

Indiana Code section 8-1-2-23 provides that a utility, like Community, may seek pre-approval of proposed wastewater utility capital investments. Seeking pre-approval is voluntary but provides certainty to the utility that the project costs will be included in the utility's rate base once they are completed and placed into service. Ind. Code § 8-1-2-23. In June 2020, Community sought preapproval for two major capital projects: one to expand its collection system, and one upgrade its wastewater treatment plant (together, the "Wastewater Capacity Projects") (IURC Cause No. 45389; Addend. 34). Community's request for expenditure pre-approval on these projects included capitalized labor and engineering costs that are the subject of the instant appeal. None of the proposed upgrades were targeted at reducing I&I (Addend. 34–44).

1. Collection System Improvement Projects

Community's proposed collection system expansion included projects to upgrade two lift (pumping) stations with more capacity, build a new lift station, build a new force (pumped) main from an existing lift station to the new lift station, and to build a new force main from the new lift station to the treatment plant (Addend. 42). These proposed projects were designed to "reduce the incidences of basement backups and manhole overflows" by increasing capacity instead of reducing I&I (Addend. 34). The estimated costs of the collection system improvements were $4,148,088 (Addend. 36).

2. Wastewater Treatment Plant Projects

Community's proposed wastewater treatment plant projects were designed to increase the capacity of Community's existing wastewater treatment plant from 1.1 million gallons per day to 1.6 million gallons per day by adding a new biological treatment process and upgrading auxiliary equipment and processes (Addend. 42). The estimated costs of the treatment plant upgrades were $19,712,491 (Addend. 36).

3. IURC's Denial of Pre-Approval for the Proposed Wastewater Projects

On May 5, 2021, the IURC issued a final order denying pre-approval of Community's proposed Wastewater Capacity Projects[2] (Addend. 44). For the

[2] In a separate case, IURC Cause No. 45342, Community also sought pre-approval for several water (not wastewater) service capital projects, all of which were approved by the IURC (*see* Addend. 22). The engineering costs at issue in this appeal are engineering costs attributable only to the denied wastewater projects.

collection system improvement projects, the IURC determined the capacity upgrades and new infrastructure were not needed because "hundreds of thousands of gallons of I&I per day could potentially be removed if [Community] addressed inflow in several specific locations identified by credible evidence presented by the OUCC and [Lake of the Four Seasons]" (Addend. 42). The IURC found that the areas specified by the OUUC "present opportunities for a successful I&I removal program to remove *more* than 30%[,]" disagreeing with Community's contention that it would be "unable to remove more than 30% of the I&I" (Addend. 42, emphasis added). The IURC characterized the approval of any collection system improvement projects as "premature" because "[Community] has not yet attempted to remediate, at a minimum, the inflow locations identified" (Addend. 42). Further, the IURC found that "[Community] should prioritize its I&I program so that we can assess the impact of the I&I removal on [Community's] request for pre-approval, rather than guess about what percentage of I&I could be removed, as it has done" (Addend. 42).

In a similar vein, the IURC concluded that the source of the I&I problem should be addressed before it pre-approved an increase in the wastewater treatment plant capacity: "[Community] should prioritize its I&I program so that we can assess the impact of the I&I removal on any need to expand its [wastewater treatment plant]" (Addend. 43). For the same reasons, the IURC also found that letters from the Indiana Department of Environmental Management (IDEM) regarding wastewater overflows did not necessitate the increases in treatment plant

capacity either, because Community's response of seeking projects to increase capacity were unreasonable "in light of [Community's] current situation and failure to work on I&I removal" (Addend. 43). Ultimately, the IURC denied Community's proposed non-I&I wastewater treatment plant upgrades and collection system improvements in their entirety because Community had not yet achieved meaningful I&I reduction (Addend. 44).

4. IURC's Denial of Community's Request for Reconsideration

After the IURC denied pre-approval of Community's proposed Wastewater Capacity Projects, Community filed a petition for reconsideration asserting that it had adequately addressed I&I removal (Addend. 45). The order denying reconsideration reiterated the IURC's finding that Community had not addressed its I&I problem to the point where pre-approval of the multi-million-dollar proposals was justified (Addend. 45). The IURC also reaffirmed that there was no evidence that Community could not continue providing reasonable and adequate service without the proposed upgrades (Addend. 45). Community did not appeal the IURC's decision denying pre-approval to its proposed wastewater projects.

C. Community's 2021 Request for a General Rate Increase

On December 7, 2021, Community filed a petition with the IURC to change Community's base rates and charges under Indiana Code sections 8-1-2-42.7 and -60 (II App. 11). The petition requested base rate increases for capitalized costs based on both water and wastewater services and improvements (II App. 13–94). After a public field hearing and evidentiary hearing, the IURC granted Community a rate increase in two phases for both its water and its wastewater utilities, with a

total wastewater utility increase to annual authorized revenues of $2,321,863 (II App. 7, 93–94). At issue here, the IURC denied, at this time through a rate increase, the recovery of $1,600,000 in engineering costs incurred for the planning of the Wastewater Capacity Projects that had been denied pre-approval (II App. 73–74).

1. The Engineering Costs

Community selected Baxter & Woodman as the engineering firm for the wastewater treatment plant upgrades (II App. 132). The $1,233,000 in accrued engineering costs for this project included payment for the design of: the wastewater treatment plant expansion, a new headworks, a new oxidation ditch, two new clarifiers, a new sludge building with equipment, a new operations building, and the design to repurpose several existing structures to support the new treatment processes (1 Exs. 42). The design work also included changes to the layout of office facilities at the treatment plant building and floorplans for the new expansion to the wastewater treatment plant building (13 Exs. 23–30). The office redesign proposal was later removed from the pre-approval request, but those costs are still included in the engineering costs Community seeks in this appeal.

The detailed information regarding the engineering costs was provided in the pre-approval case record, but Community did not submit it into evidence in this rate case. Owing to the lack of detailed records here, the OUCC argued "Community only provided a workpaper reflecting total 'engineering' costs incurred with no supporting detail or documentation provided" (11 Exs. 178). In response, Community stated it was unaware of an itemization requirement "that would

require CUII to attach engineering invoices in its original case in chief" (1 Exs. 137). Despite the denial in the pre-approval case, here Community "believes that these costs are presumed to be reasonable" until a party objects (1 Exs. 137). Regardless, Community did not provide any additional information or the details of the engineering costs in its rebuttal testimony submitted in this rate case, despite the OUCC and Lake of the Four Seasons challenging those costs (see II App. 71; 11 Exs. 178; 13 Exs. 97).

As to the engineering costs of the collection system upgrades, Community selected RHMG as the engineering firm (II App. 132). The $367,000 in accrued engineering costs for this project included payment for: locating the existing underground utility infrastructure and geotechnical engineering applicable to the collection system design efforts (1 Exs. at 41). These design costs included: permitting costs, the cost of plans and specifications, bidding costs, and the cost to design upgrades at three lift states and the new force mains at the lift stations (1 Exs. at 41).

2. Denial of Recovery for the Engineering Costs

The IURC denied recovery of the engineering costs at this time because "[Community] has made no meaningful attempt to date to achieve I&I removal as set forth in the 44724 [2018 Rate Case] Order" (Addend. 44). The IURC continued, "A robust I&I removal program is long overdue and could alter and help better determine the identity and scale of the improvements needed" (Addend. 44). As to the engineering costs directly, the IURC explained the "improvements proposed and

subsequently engineered under [Community's] direction and of which [Community] sought pre-approval in Cause No. 45389 are not directly related to any attempt to implement a comprehensive I&I program" (II App. 74). Instead, the IURC found that the engineering costs were incurred "without first making a substantive attempt to quantify and eliminate I&I as directed in the 44724 [2018 Rate Case] Order" (II App. 74). Concluding these engineering costs would result in a treatment plant, "that may be substantially overbuilt and not used and useful" the engineering costs were denied (II App. 74).

I&I capital costs incurred by Community, to the extent they were already placed into service, were included in Community's total rate base in this case (*see* II App. 13) and I&I operating and maintenance expenses were also recovered as with other expenses incurred by Community during the test year (*see* II App. 56).

Twenty days after the IURC's final order in this case, Community filed a Petition for Reconsideration requesting the IURC reconsider denial of the engineering costs and certain legal costs (II App. 98, 101–03). The IURC reaffirmed its denial of the engineering costs stating, "Those engineering costs were incurred with the intent of only replacing [Community's] aged [wastewater treatment plant] and investing in new capacity without first making a substantive attempt to quantify and recover previously lost capacity through the elimination of I&I as directed [in the 2018 Rate Case Order]" (II App. 101). The IURC concluded the Wastewater Capacity Projects and their associated engineering costs were not used and useful because they had not been put into service (II App. 101–02). The IURC

granted Community's request for reconsideration in part by approving recovery of $81,086.50 in attorney fees, but it again denied recovery of the engineering costs (II App. 104). Notably, the IURC did not permanently foreclose future recovery of the engineering costs, pointing out that Community could seek recovery of those engineering costs if it eventually built some or all of the Wastewater Capacity Projects and they become used and useful (II App. 103).

SUMMARY OF THE ARGUMENT

The IURC's decision that Community could not recover engineering costs for a multi-million-dollar capital project it has not started and for which it was denied preapproval is reasonable and supported by the evidence. The IURC properly found that the engineering costs cannot be recovered through ratemaking because the projects to which they are connected are not "used and useful." Community has not started, completed, or put into service the Wastewater Capacity Projects. And because it failed to meaningfully engage in I&I reduction, Community has not shown that the Wastewater Capacity Projects are necessary to the provision of utility service.

Furthermore, the IURC's conclusion that the engineering costs are not reasonable, necessary, or prudent is supported by unchallenged findings and conclusion and substantial evidence. In the preapproval case, the IURC found that expansion of its wastewater system capacity was unnecessary and unreasonable because Community has not first taken serious steps to reduce I&I. Community did not appeal that decision and does not challenge those findings and conclusion in

this appeal. Because the Wastewater Capacity Projects are unnecessary and unreasonable, the inextricably connected engineering costs planning those projects are also unnecessary and unreasonable and cannot be recovered through ratemaking at this time.

Community tries to excuse its decision to push ahead with new capital project while refusing to meaningful correct its I&I problem by claiming that: (1) the 2018 Rate Case Order requires it to pursue projects like the Wastewater Capacity Projects and (2) it assumed the Projects were reasonable based on IURC staff's implicit approval. But the 2018 Order explicitly requires Community to develop and implement a I&I reduction program as the only "primary" wastewater component of its system improvement plan. And any direction in the 2018 Order recommending wastewater capital projects should be, first, to further that I&I reduction program. Likewise, the IURC and its staff have continuously instructed Community to focus of I&I reduction. But because Community has not substantially improved its I&I problem, its proposed capital project to increase its systems capacity and the related engineering costs, are unnecessary and unreasonable at this time. Community is not foreclosed from every recovering these engineering costs in the future. If Community first addresses its I&I problems, and still ends up building the Wastewater Capacity Projects, it may be able to recover the engineering costs through ratemaking at that time.

STANDARD OF REVIEW

Recognizing the need for a fact-finding body with technical expertise to regulate utilities in Indiana, the General Assembly created the IURC. *Northern Indiana Pub. Serv. Co. v. U.S. Steel Corp.* ("*NIPSCO*"), 907 N.E.2d 1012, 1015 (Ind. 2009); *IPL Industrial Group v. Indianapolis Power & Light Co.,* 159 N.E.3d 617, 622 (Ind. Ct. App. 2020), *trans. denied*. Due to the General Assembly's delegation and the IURC's specialized expertise, an order from the IURC "is presumed valid unless the contrary is clearly apparent." *Citizens Action Coalition of Indiana, Inc. v. Northern Indiana Pub. Serv. Co.*, 485 N.E.2d 610, 612 (Ind. 1985); *see also Citizens Action Coalition of Indiana, Inc. v. Northern Indiana Pub. Serv. Co*., 76 N.E.3d 144, 151 (Ind. Ct. App. 2017).

This Court reviews IURC orders using a multi-tiered standard. *NIPSCO*, 907 N.E.2d at 1016; *Citizens Action Coalition of Indiana, Inc. v. Indianapolis Power & Light Co.,* 74 N.E.3d 554, 562 (Ind. Ct. App. 2017). First, the Court determines whether the IURC's findings of basic fact are supported by substantial evidence. *NIPSCO*, 907 N.E.2d at 1016. In substantial evidence review, "the appellate court neither reweighs the evidence nor assesses the credibility of witnesses and considers only the evidence most favorable to the Board's findings." *McClain v. Review Bd. of Ind. Dept. of Workforce Dev.,* 693 N.E.2d 1314, 1317–18 (Ind. 1998).

Second, the Court determines whether the IURC's order contains "specific findings on all the factual determinations material to its ultimate conclusions" and whether the IURC's conclusions of ultimate fact are reasonable. *Id*. (citation

omitted). This Court is tasked with "reviewing conclusions of ultimate facts for reasonableness, the deference of which is based on the amount of expertise exercised by the agency." *Citizens Action Coal. of Indiana, Inc. v. Indianapolis Power & Light Co.,* 74 N.E.3d 554, 563 (Ind. Ct. App. 2017). If the order involves a subject within the Commission's special competence, courts should give it greater deference. *McClain*, 693 N.E.2d at 1318. The Commission is afforded the authority decide each unique case before it without relying on past cases; however, it must explain its reasoning for the deviation to avoid arbitrary and capricious action. *Citizens Action Coal. of Indiana, Inc. v. S. Indiana Gas & Elec. Co.*, 120 N.E.3d 198, 208 (Ind. Ct. App. 2019).

In its ratemaking process, The IURC "balances the public's need for adequate, efficient, and reasonable service with the utility's need for sufficient revenue to meet the cost of furnishing serve and to earn a reasonable profit." *NIPSCO Indus. Group*, 100 N.E.3d 234, 238 (Ind. 2018). Ratemaking is a legislative rather than a judicial function. *Hamilton Southeastern Utils., Inc. v. Ind. Util. Regul. Comm'n*, 101 N.E.3d 229, 233 (Ind. 2018). And ratemaking "involves innumerable technical determinations which are particularly within [the IURC's] competence and expertise." *L.S. Ayres & Co. v. Indianapolis Power & Light Co.*, 351 N.E.2d 812, 822 (Ind. Ct. App. 1976).

ARGUMENT

I. Community's engineering costs for projects that are not completed, or even started, were properly excluded from ratemaking because the projects are not "used and useful."

Community's proposed Wastewater Capacity Projects, and their related engineering costs, are not "used and useful," and, therefore, the costs are not recoverable in ratemaking. Ordinarily, a utility cannot recover capital investments that have not been put into use to provide utility service. During ratemaking, the IURC "shall value all property of every public utility actually used and useful for the convenience of the public[.]" I.C. § 8-1-2-6(a). The "used and useful" standard requires: (1) that the utility plant be actually devoted to providing utility service, and (2) that the plant's utilization be reasonably necessary to the provision of utility service. *City of Evansville V. S. Ind. Gas & Elec. Co* 167 Ind. App. 472, 516, 339 N.E.2d 562, 589 (Ind. Ct. App. 1975). That is because "utility charges are based on service." *Citizens Action Coalition of Ind., Inc. v. N. Ind. Pub. Servo Co.,* 485 N.E.2d 610,613 (Ind. 1985). "Without 'used and useful' property there cannot be any service." *Id*. at 614. Community's proposed Wastewater Capacity Projects cannot meet either of the two necessary elements of "used and useful" standard.

First, it is undisputed that the projects are not built or actually devoted to providing services. And the engineering costs, a vital component of the projects as a whole, cannot be excised from the project and pushed through ratemaking when it is unclear whether the projects will ever be started or completed. To allow otherwise, would permit utility companies to fund portions of projects without any guarantee that they will ever be completed and put into service. This is precisely

what the statutorily-based "used and useful" standard is meant to prevent. Even if these projects had been preapproved (they were not), the pre-approval statute is not an exception to the rule that projects must be operational before they are included in ratemaking. The preapproval statute only allows a utility to have a *guarantee* of future rate base treatment before it expends significant money, but, even under pre-approval, the assets must be put into service before included in rates. *See* IC 8-1-2-23.

Second, Community has not shown that increasing the system's capacity through these Wastewater Capacity Projects is necessary. Because Community failing to fully engage in I&I remediation, it cannot show that the wastewater treatment plant upgrades and collection system improvements are necessary. This Court has found, "Unnecessary plant capacity is not used and useful for rate making purposes and should not be included [in the rate base.]" *L.S. Ayres & Co. v. Indianapolis Power and Light Co.*, 351 N.E.2d 814, 834 (Ind. Ct. App. 1976). The IURC ultimately concluded that the engineering costs could not be included in ratemaking because "[t]hose costs were incurred with the intent of replacing [Community's] aged [wastewater treatment plant] and increasing treatment capacity without first making a substantive attempt to quantify and eliminate I&I as directed in the [2018 Rate Case] Order, resulting in a [wastewater treatment plant] that may be substantially overbuild and not used and useful" (II App. 74). Because the projects are not in service or necessary, they are not used and useful,

and the inextricably connected engineering costs cannot be recovered through ratemaking.

This is not to say that Community is forever barred from obtaining recovery of the engineering costs. If Community later uses those plans for which it spent the engineering costs, builds the capital assets, and puts them into service, it can then seek rate base treatment and recovery of those engineering costs already incurred.

Community incorrectly claims that engineering costs for specific projects can be recovered through ratemaking even if the projects are not completed or put into service (Appellant's Br. 29). All but one of the cases cited by Community involve rate case expenses, or reimbursement for the cost of bringing a rate case, and are easily distinguishable from reimbursement for engineer costs for specific projects that were never started or completed (*see* Appellant's Br. 29–30).

The only case not involving rate case expenses, *PSI Energy, Inc.*, 2006 WL 2547054 (I.U.R.C. 2006), is also distinguishable from the present case. In *PSI Energy, Inc.*, the IURC approved a settlement agreement allowing Duke Energy "authority to defer and subsequently recover the feasibility study, engineering, and preconstruction costs associated with the consideration and exploration of constructing an integrated coal gasification combined cycle electric generating facility. *Id*. at *1. In that specific case, the IURC found approval of the settlement was appropriate because "[w]ith the current state of development of the [coal gasification] technology…additional study is clearly appropriate and could minimize future design change." *Id*. at *7. The study and development of this coal gasification

technology was also consistent with the General Assembly's explicit direction that the State should "…encourage the use of advanced clean coal technology, such as coal gasification." *Id*. at *7, quoting I.C. § 8-1-8.8-1(a)(5). In addition, the Commission approved the deferral of the study costs for recovery at such time the coal gasification project was approved and completed or only 50% of such costs if the project did not go forward. *Id*. at *8. All of these facts make *PSI Energy, Inc.* clearly distinguishable from the fact here, where Community seeks reimbursement for engineering costs for mundane (and unnecessary) capital projects it has not yet started or completed. Moreover, in *PSI Energy, Inc.* the IURC explicitly noted, "The parties agree that the Settlement Agreement should not be used as precedent in any other proceeding or for any other purpose, except to the extent necessary to implement and enforce its terms." *Id*. at *8.

None of the cases cited by Community support its assertion that it should be able to recover engineering costs for a project that it has not started, completed, or shown is necessary. Because Community's proposed Wastewater Capacity Projects are not used and useful, the inextricable connected engineering costs cannot be recovered through the current ratemaking. If Community constructs the projects, puts them into service, and shows they are reasonably necessary to the provision of utility service, it may seek to recover the engineering costs through ratemaking at that time.

II. The IURC's reasonable conclusion of ultimate fact—that Community's engineering costs were imprudent and unreasonable at this time—is supported by the evidence.

Even if Community could potentially recover engineering costs for an unstarted project, the IURC correctly found that those costs were imprudent, unreasonable, and not compensable through ratemaking at this time. The IURC made an ultimate conclusion of fact that Community's engineering costs for the proposed Wastewater Capacity Projects were unnecessary, imprudent, and unreasonable because those projects sought to negate the need for a comprehensive I&I program instead of implementing one as directed by the 2018 Rate Case Order (II App. 73–74). This conclusion is reasonable and supported by the evidence. When setting rates, the IURC has statutory authority to disapprove a utility's "unnecessary or excessive" expenditures. I.C. § 8-1-2-48. "While the utility may incur any amount of operating expenses it chooses, the [IURC] is invested with broad discretion to disallow for ratemaking purposes any excessive or imprudent expenditures." *Office of Util. Consumer Counselor v. Indiana Cities Water Corp.*, 440 N.E.2d 14, 15 (Ind. Ct. App. 1982), *trans. denied*. And when the IURC acts within its statutory authority, the courts give "great deference to the IURC's rate-making methodology." *Office of Util. Consumer Counselor v. Citizens Tel. Corp.*, 681 N.E.2d 252, 255 (Ind. Ct. App. 1997).

This Court does not reweigh the evidence and considers "only the evidence most favorable to the [IURC's] findings." *McClain v. Review Bd. of Indiana Dep't of Workforce Dev., 693 N.E.2d at 1318*. And this Court will only set aside the IURC's

findings if the Court determines, "that the agency's decision clearly lacks a reasonably sound basis of evidentiary support." *Nextel West Corp., et al. v. Ind. Utility Regulatory Comm., et al.*, 831 N.E.2d 134, 156–57 (Ind. Ct. App. 2005). "If there is substantial evidence to support the findings, and if the determination, decision and order is one which the Commission has the power to make, in view of the findings, courts must uphold it." *Davies-Martin Cnty. Rural Telephone Corp. v. PSC*, 174 N.E.2d 63, 68 (Ind. Ct. App. 1961). Community has the burden of showing that the IURC's findings are not supported by the evidence and cannot merely "cite to other evidence of record which would support a determination more favorable to their position." *Citizens Action Coalition of Indiana, Inc. v. Indianapolis Power & Light Company, 74 N.E.3d 554*, 564 (Ind. Ct. App. 2017).

Community has failed to meet its burden and cannot establish that the IURC findings and conclusion are unsupported. For purposes of this appeal, Community does not challenge that it has not sufficiently addressed its I&I problems. Instead, it seeks to justify its engineering costs by arguing: (1) the 2018 Rate Case Order directed Community to undertake capital projects like the Wastewater Capacity Projects; and (2) IURC staff somehow approved the engineering costs as reasonable (Appellant's Br. 31–44). Both of these contentions are incorrect. The 2018 Rate Case Order directs Community to develop and implement a comprehensive I&I reduction program, not to sweep its I&I problems under the rug by merely increasing the system's capacity. And IURC staff, who cannot bind the IURC as a body, consistently tried to redirect Community to fully address its I&I problems, not just

move forward with plans to mask them. Community does not challenge in this appeal the IURC's findings and conclusion that it has failed to make sufficient I&I remediation progress to justify that the Wastewater Capacity Projects are necessary and prudent, and the IURC's ultimate conclusion that the projects' engineering costs are not reasonable or recoverable through ratemaking at this time is supported by substantial evidence.

i. The IURC decision is correct under the unchallenged findings and conclusions that Community has not addressed its I&I problems sufficiently to make the proposed Wastewater Capacity Projects necessary or reasonable.

The IURC's unchallenged and unappealed findings and conclusion in the 2021 preapproval case alone support the IURC's ultimate conclusion in this case. The IURC denied preapproval to the Wastewater Capacity Projects because they were not necessary, reasonable, or prudent (Addend. 41–45). Community itself recognized that the engineering costs are inextricably connected to proposed construction of the Wastewater Capacity Projects, recognizing that the engineering costs were incurred for the purpose of bringing the pre-approval case (1 Exs. 41–42). It logically follows that the engineering costs planning the construction of those unnecessary projects are themselves unnecessary.

Moreover, the IURC's unchallenged reasoning for denying preapproval equally applies here. In the preapproval case, the IURC concluded that Community "has not addressed its problems with I&I to the point where preapproval of its multi-million-dollar proposals was justified" (Addend. 45). Community "does not challenge this conclusion in this appeal[,]" (Appellant's Br.

34), and emphasizes that "the Court is not being asked to review IURC's [2021] decision not to preapprove [Community's] proposed wastewater service capital projects[,]" (Appellant's Br. 30). This unchallenged conclusion alone—that Community has failed to sufficiently address its I&I problems—supports the IURC's reasonable ultimate finding that, as yet, Community's proposed Wastewater Capacity Projects, and their component engineering costs, are unnecessary and unreasonable. Indeed, the IURC quoted and relied on these unchallenged findings and conclusions when it concluded the engineering costs were unreasonable (II App. 73–74).

But even putting aside the unchallenged facts and conclusion in the 2021 preapproval case, the IURC's finding that the proposed Wastewater Capacity Projects are unnecessary and unreasonable is supported by substantial evidence in the record, included the following:

- Testimony of OUCC's Chief Technical Advisor that:
    - Community's engineering costs were not substantiated with supporting detail or documentation (11 Exs. 178).
    - Incurring the engineering costs was not responsive to the 2018 Rate Case Order's directive to develop a comprehensive I&I program and the IURC did not direct Community to incur these costs (11 Exs. 178–79).
    - There is no used and useful asset for these engineering expenditures (11 Exs. 179).

- Testimony of Lake of the Four Seasons's Director of Operations LOFS testimony that:
    - Community's wastewater system is old and in need of repair, and, if Community had had performed necessary maintenance and updates from the beginning, it would not have to spend as much money now (13 Exs. 97).
    - Ratepayer should not pay for engineering expenses for a non-preapproved upgrade to Community's wastewater treatment plant when Community should spend more time focusing on eliminating I&I (13 Exs. 97).
- In response to Community initial filings after the 2018 Rate Case Order, IURC staff concluded that "[Community] has not complied with the [IURC's] Order to develop a comprehensive I/I program" (III App. 197) and that "staff expects that [Community] will place more efforts into the appropriate SSO [Sanitary Sewer Overflow] program areas and that the results will drive the prioritization of capital improvements, focusing on rehabilitation/ replacement as opposed to conducting random spot repairs" (III App. 197).
- Community reported very modest I&I progress up until its request for preapproval of its Wastewater Capacity Projects in 2020. While Community outlines some plans for I&I progress, the record only establishes that: 20 manhole covers had been sealed and lined (III App.

75); 2,700 linear feet of pipe was lined in 2018 (III. App. 90–91); all the homes of Community's 3,500 residential customers had been smoke tested but only between 400 to 500 of the 3,500 homes had been inspected through 2019 (III App. 90–91, 160–61).

There is no evidence in the record of any efforts by Community to reduce I&I after preapproval for its proposed Wastewater Capacity Projects was denied in 2021. This evidence supports the IURC's finding that Community has not done enough I&I removal to show that the Wastewater Capacity Projects, or their engineering costs are reasonable or necessary.

ii. The 2018 Rate Case Order directs Community to develop and implement a comprehensive I&I remediation program, not to undertake projects like the Wastewater Capacity Projects.

The 2018 Rate Case Order explicitly directs Community to reduce its I&I problems, not to mask them by increasing system capacity. The 2018 Order requires Community to develop a system improvement plan that, relevant here, decreases wastewater backups in homes and manhole overflows (Addend. 17). The order is clear that this is not to be done by any means Community chooses but by implementing a "comprehensive inflow and infiltration ("I&I") program" (Addend. 17–18; *contra* CUII Br. at 31). This I&I reduction program is the only specified "*primary*" wastewater component that the system improvement plan *must* have (Addend. 17–18).

Community claims that the 2018 Order directs them to undertake capital projects like the Wastewater Capacity Projects, but it does not. Community takes

the Order's capital investment phrase out of context to try to justify a multi-million-dollar expansion of its wastewater treatment plant and collection system. In the same paragraph where the 2018 Order identifies the I&I program and the only necessary primary wastewater component of the system improvement plan, it directs Community to "propose capital investments that require [IURC] approvals and suggest timetables for the filings and approvals" (Addend. 17–18). In this obvious context, proposed capital projects were intended to be, at least initially, part of a the comprehensive I&I reduction program and not instead of it.

In Community's initial system improvement plan draft, it appeared Community understood that the 2018 Order intended it to first propose capital investments meant to directly accomplish I&I remediation. In its plan draft, Community stated that as one element of its I&I program it would "[c]ontinue with [its] ongoing Sewer Capital Improvement Program to identify and repair defects in existing sewers and manholes" (II App. 139). But as time went on, Community's plan to develop meaningful capital projects to repair its existing sewers (which is clearly in line with the 2018 Order's directive) fell by the wayside in favor of plans for multi-million-dollar expansions to of plant and system (*see* III App. 66 (Community's October 2018 draft system improvement plan estimating approximately $800,000 in I&I reduction activities and $30,400,000 in system capacity expansion projects). Despite the IURC's attempt to redirect Community to its I&I program to repair its existing system, Community insisted on moving forward with plans to expand its system capacity instead of making any meaningful

progress on its I&I problem. I&I reduction, not expansion of system capacity, has always been the only primary wastewater element of the required plan under the 2018 Order. And the 2018 Order does not guarantee recovery of engineering costs for *any* capital improvement project, let alone one that ignores the necessary primary elements of the system improvement plan.

iii. IURC staff continued to try to redirect Community to substantively address its I&I problems.

Since 2018, the IURC and its staff has consistently tried to get Community to fully address its I&I problems, and IURC staff repeatedly tried to redirect Community to I&I remediation. Here on appeal, Community argues that it relied on the IURC's actions and staff comments to assume that proceeding with the plans to increase its capacity were reasonable, relying on *Hamilton Southeastern Utils., Inc. v. Ind. Util. Regulatory Comm'n ("Hamilton Southeastern II")*, 115 N.E.3d 512 (Ind. Ct. App. 2018), and *Baliga v. Ind. Horse Racing Comm'n*, 112 N.E.3d 731 (Ind. Ct. App. 2018) (see Appellant's Br. 35–38). But the IURC and its staff repeatedly told Community to focus on I&I remediation and informed Community that staff communications were not preapproval to proceed with any specific projects.

In *Hamilton Southeastern II*, the utility company had contracted with a company, SAMCO, to manage its operations for approximately 25 years. 115 N.E.3d at 514. The utility had regularly filed SAMCO's billing contract with the IURC and recovery for SAMCO's rates and fees had been included in previous rate cases. *Id.* When the IURC denied the same costs in a subsequent rate case based on guidelines that had been presented in previous rate cases, this Court found the

utility had not been given sufficient notice of the IURC's changed position and that denial of the costs was unreasonable and arbitrary. *Id*. at 515. In *Hamiton Southeastern II*, the IURC had approved the exact same costs in previous rate cases and then changed course, while here, these engineering costs were never the subject of previous rate cases and the IURC has not preapproved the projects or costs.

Baliga is likewise inapposite to this case; there a veterinarian facing revocation of his license was given the impression by comments from the Horse Racing Commission's attorney that a hearing on the matter would be upcoming. 112 N.E.3d at 736. When the Horse Racing Commission defaulted Baliga and imposed a suspension without a hearing because he never formally requested one, Baliga appealed. *Id*. At 732–34. This Court reversed and remanded for a hearing because the Horse Racing Commission knew Baliga was actively challenging the suspension and had been given the distinct impression by the Horse Racing Commission that he would have a hearing. *Id*. At 737. Baliga does not apply here because Community knew the proper process to seek preapproval of potential projects and knew that communications from IURC staff was not preapproval of any projects.

In response to Community's initial filings in 2018, IURC staff issued written recommendations concluding "[Community] has not complied with the [IURC's] Order to develop a comprehensive I/I program" (III App. 197), and noting that "[IURC] staff expects that [Community] will place more efforts into the appropriate SSO [Sanitary Sewer Overflow] program areas and that the results will drive the prioritization of capital improvements, focusing on rehabilitation/ replacement as

opposed to conducting random spot repairs" (III App. 197). Later that year, when presented with Community's draft system improvement plan, IURC staff recommended that Community "[c]ontinue to evolve Petitioner's capital planning efforts as better information becomes available" (2 Exs. 62). In the docket entry for that recommendation the IURC forewarned Community that the "docket entry *is not pre-approval* by the Commission of Petitioner's proposed capital investments" (2 Exs. 61, emphasis added). In its denial in the preapproval case, the IURC continued to strongly recommend that Community "prioritize its I&I program so that we can assess the impact of the I&I removal on [Community's] request for preapproval, rather than guess about what percentage of I&I could be removed, as it has done" (Addend. 42).

Regardless, even if staff had encouraged Community to plan for these projects, it could not act as approval of those projects or associated costs for ratemaking purposes. Aside from the limited staff recommendation discussed above, Community participated in several technical conferences including IURC staff. Technical conference with stakeholders, including IURC staff, are required by the IURC from time to time. The purpose of technical meetings is to allow the utility to receive real time feedback from knowledgeable parties prior to seeking approval before the full IURC. *See e.g. In re: Petition of IPL*, 2016 WL 1118795 at *20 (I.U.R.C. 2016). They are a tool to assist the utilities, not to take control away from the utility as the ultimate responsible party for its investment decisions. While IURC staff may provide feedback during technical meeting to give the utilities real-

time feedback from experts, it is not an indication of how the Commissioners will vote and the utilities still ultimately bear the risk of their investment decisions.

Community implies that the technical conferences gave tacit "approval" to the Wastewater Capacity Projects (see Appellant's Br. 32–33). This misunderstands the purpose of the technical meetings and the authority of the IURC and its Commissioners. Commission staff do not speak for the Commission; not even a minority of Commissioners speak for the Commission. The IURC is made up of members appointed by the Governor, and only a majority of the Commissioners constitute a quorum to take any action, such as the approval of orders. I.C. § 8-1-1-2(a) and (b); I.C. § 8-1-1-3(d). Commission staff, an administrative law judge, or even a minority of appointed Commissioners cannot approve utility expenditures or set rates; only a quorum of the Commissioners can issue orders setting rates or make any other binding approvals or determinations. I.C. § 8-1-1-2(a) and (b); I.C. § 8-1-1-3(d). Moreover, the technical conferences here were not recorded or reported by court reporters; what was actually said at these technical conferences is not part of the evidence or record of this case. What the record of this case does show is that, from early on in the process, IURC staff expressed to Community that it was not in compliance with the 2018 Rate Case Order because it did not meaningfully address I&I reductions (Addend. 197-198).

In sum, there is no evidence that the IURC or its staffs made any comments that preapproved the Wastewater Capacity Projects or their engineering costs. And IURC orders are the only way it officially renders a decision. Here, the IURC found

the capital investments and their engineering costs were unreasonable in both the preapproval case and in this rate case.

Lastly, Community argues that the IURC improperly found that Community's proposed Wastewater Capacity Projects were not made in good faith (Appellant's Br. 44–48). The IURC's order does not depend on Community's good faith or bad faith (II App. 102). The IURC's denial of the engineering costs is based on the unchallenged fact that Community has failed to meaningfully address its I&I problems, despite repeated directions to do so (II App. 73–74, 102). And Community's willful insistence on proceeding with plans for capital project to expand capacity are in clear conflict with the obvious impetus of the 2018 Order and IURC's communications since—that Community needs to focus on correcting I&I problems by repairing its existing sewer system.

The IURC's ultimate conclusion that the engineering costs for the proposed Wastewater Capacity Project are not reasonable or necessary are supported by uncontested facts and substantial evidence. The IURC made all of the necessary findings on the relevant issues, and this Court should affirm because the IURC was acting reasonably within its statutory authority. *See Citizens Tel. Corp.*, 681 N.E.2d at 255.

CONCLUSION

Because the IURC's order and findings were supported by substantial evidence and correctly found the engineering costs were unreasonable, this Court should affirm the IURC's order.

Respectfully submitted,

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WORD COUNT CERTIFICATE

I verify that this Brief of Appellee contains no more than 14,000 words, not including those portions excluded by Indiana Appellate Rule 44(C).

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CERTIFICATE OF SERVICE

I certify that on October 30, 2023, I electronically filed the foregoing using the Indiana Filing System (IEFS), and that the foregoing document was served upon counsel via IEFS:

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