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October 20, 2023
INDIANA UTILITY
REGULATORY 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**

<u>OUCC's PROPOSED ORDER</u>

The Indiana Office of Utility Consumer Counselor ("OUCC"), by counsel, hereby submits its proposed order.

Respectfully submitted,

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ORDER OF THE COMMISSION

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

On March 31, 2023, Indiana-American Water Company, Inc. ("Petitioner," "Indiana American," "INAWC" or "Company") 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 ("Petition") 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 described herein and in Petitioner's case-in-chief, (v) 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 (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

[1] On April 28, 2023, Indiana American prefiled corrections to witnesses Shimansky and Rea testimony. On June 6, 2023, Indiana American prefiled 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 prefiled its third submission of corrections to witness Shimansky's direct testimony. All corrections were included in the evidence submitted at the hearing.

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 a group of wholesale customers of Indiana American[3], ("Wholesale Customers"), and on July 13, 2023, by Hamilton County Regional Utility District ("HCRUD" or "District"), (collectively, the "Intervenors"). The Commission issued Docket Entries granting each of said petitions to intervene; 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 ("Stipulation") 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 Commission set forth procedural, scheduling and other matters. By Docket Entry dated June 23, 2023, the Commission 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.

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[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.

[3] At the time of intervention, the Wholesale Customers included the Town of Whiteland ("Whiteland"); and on May 19, 2023 Borden Tri-County Regional Water District ("Borden Tri-County"), Jackson County Water Utility, Inc. ("Jackson County Water"), and the Town of Greenville, Indiana, by and through its municipal water utility ("Greenville").

On July 21, 2023, the OUCC and intervenors prefiled their respective cases-in-chief. The OUCC's prefiled case-in-chief included testimony and attachments from the following witnesses[4]:

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, Utility Analyst in the Water/Wastewater Division

David Garrett, Resolve Utility Consulting, PLLC

Jerome Mierzwa, Principal and Vice President, Exeter Associates, Inc.

James Parks, 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 prefiled the written consumer comments pertaining to this docket and the relief requested as Public's Exhibit No. 12.

Wholesale Customers prefiled the testimony of Eric Callocchia, Partner of NewGen Strategies & Solutions, LLC's Environmental Practice.[5]

HCRUD prefiled the testimony and attachments of Martin A. Wessler, CEO of Wessler Engineering.

The Industrial Group's prefiled case-in-chief included testimony and attachments from the following witnesses[6]:

- Michael Gorman, Managing Principal, Brubaker & Associates, Inc.

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

[5] Whiteland indicated Mr. Callocchia's testimony was filed separately in collaboration with 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.

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

- Jessica York, Consultant, Public Utility Regulation, Brubaker & Associates, Inc.

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

Whiteland prefiled testimony and attachments of Carmen Young, Director of Administration for the Town of Whiteland.

CAC prefiled testimony and attachments from Benjamin Inskeep, Program Director, Citizens Action Coalition of Indiana, Inc.

On August 8, 2023, Indiana American prefiled rebuttal testimony, exhibits, and workpapers for witnesses Shimansky, Hobbs, Britto, Rea, Bulkley, Grisham, Cifuentes, and Kennedy.[7] Indiana American also prefiled 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; HCRUD prefiled the cross-answering testimony of witness Wessler; and CAC prefiled cross-answering testimony of Benjamin Inskeep.

The Presiding Officers 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),[8] 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 all of the parties were admitted into the record without objection.

Having considered all of the evidence presented in this proceeding, based on the applicable law and evidence, the Commission now finds:

1. <u>Notice and Jurisdiction</u>. Due, legal and timely notice of the Petition filed in this Cause was given and published by Petitioner as required by law. Proper and timely notice was given by Petitioner to its customers summarizing the nature and extent of the proposed changes

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[7] On August 31, 2023, Petitioner prefiled a corrected Attachment CBR-7R to Mr. Rea's Rebuttal Testimony.

[8] Petitioner's Response to Request No. 2 in the Commission's Docket Entry dated August 30, 2023 stated that Petitioner's submission on August 30, 2023 of an updated *pro forma* revenue requirement and *pro forma* income statement reflecting actual rate base as of July 31, 2023, actual capital structure as of July 31, 2023 and updates to incorporate items accepted in Petitioner's rebuttal, along with a summary of rebuttal updates was "submitted so as to provide the parties and the Commission as soon as it became available the actual July 31 rate base and capital structure that would be filed after the issuance of the Commission Order in support of Step 1 rates. The submission is not intended to limit the compliance filing review process that would be set forth in the Commission's Order." Pet. Ex. 29 at 2.

in its rates and charges for water service. 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. Accordingly, this 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 6/26/2019)[9] (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 ("TCJA")) 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) ("Section 42.7"), 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

[9] *Indiana-American Water Co*., Cause No. 45142, 2019 WL 2903633, (IURC 6/26/2019).

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.[10] Increases to industrial and sales for resale 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. As further described below and in Indiana American's case-in-chief, 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 the Company'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 described the contributions that Indiana American makes to the State of Indiana in providing water and wastewater services. Pet. Ex. 1 at 3-4. He discussed the major drivers of the Company's request for rate relief in this proceeding, primarily the significant capital investments and other expenditures that the Company has made and plans to make through April 2025. *Id.* He explained how Petitioner's ratemaking proposals in this case 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 the Company's corporate citizenship and community outreach efforts, which are emblematic of who Indiana American is as a Company.

Mr. Shimansky testified on the test period used in this case and the Company's overall revenue requirement, rate base, depreciation, amortization, pension costs, and other post-employment benefit ("OPEB") costs, including the Company's request for regulatory accounting treatment of pension/OPEB costs, production costs, and certain costs associated with the proposed new Universal Affordability tariff. Pet. Ex. 2. He also presented the Company'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. *Id.* at 44-46.

Mr. Hobbs testified on the used and useful nature of the utility plant in service ("UPIS"), explained the Company's overall approach to capital management, and described the significant capital investments made by the Company and those the Company plans to make. Pet. Ex. 3. He also described the Company's plans for future source of supply investments. *Id.* at 29-30.

[10] This was updated in the model files provided with Petitioner's Response to the Commission's August 30, 2023 docket entry (Pet. Ex. 29) to total wastewater revenue requirement of $4,668,605 and $3,034,567 after reallocation.

Ms. Britto described the Company's water and wastewater operations, commitment to water quality and safety, ongoing efforts to improve water and wastewater efficiency, and employee levels and compensation. Pet. Ex. 4.

Mr. Rea sponsored the Company's cost of service analysis and rate design proposals, affordability analyses, and revenue projections including adjustments to INAWC's historical billing determinants. Pet. Ex. 5.

Mr. Furia testified on the projected capital structure to be used for computing the weighted average cost of capital ("WACC") for Indiana American. Pet. Ex. 6. The WACC is used as the authorized overall rate of return on rate base in this Cause. *Id.* at 2.

Ms. Bulkley testified on the reasonableness of the Company'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 the Company's assets. Pet. Ex. 7.

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. Pet. Ex. 8.

Mr. Cifuentes discussed and supported the level of O&M expense as it relates to: (1) production costs, (2) other operating expenses that are not covered by Ms. Grisham, and (3) property taxes. Pet. Ex. 9.

Mr. O'Drain testified in support of current and projected chemical pricing. Pet. Ex. 10.

Mr. Baryenbruch, supported the necessity and reasonable cost of services provided by Service Company as shown by the Company's Service Company Market Cost Comparison. Pet. Ex. 11.

Mr. Kennedy testified on the comprehensive depreciation study for water and wastewater plant in service. Pet. Ex. 12.

Petitioner also provided its Financial Exhibit in support of its requested relief in this proceeding in Excel (Pet. Ex. 13) and PDF formats (Pet. Ex. 14).

B. <u>OUCC and Intervenors' Cases-in-Chief</u>. The OUCC and intervenors proposed a number of adjustments to the Company'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 a Company proposed ROE of 10.6%, and recommended certain operating revenue and expense adjustments. Pub. Ex. 6 at 3; *see, e.g.*, testimonies of OUCC witnesses Stull (Pub. Ex. 3) and Malan (Pub. Ex. 4). The OUCC recommended seven changes to Indiana American's proposed water operations rate base, including, changes to UPIS, cost of removal ("COR"), retirements, and accumulated depreciation, all summarized in Table 7 of Ms. Stull's testimony. Pub. Ex. 3 at 10-11.

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. Pub. Ex. 3 at 11. OUCC witness Parks recommended denial of the Company'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 HCRUD. Pub. Ex. 9 at 59-60. 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. Pub. Ex. 10. OUCC witness Willoughby recommended adjustments to non-construction costs of one of the Company's lift station projects and denial of one of the Company's lift station projects, as well as denial of the Company's proposed acquisition of property in Sheridan for new wellfields. Pub. Ex. 11.

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. IG Ex. 1. 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. *Id.* at 5. Mr. Gorman also proposed a shorter amortization period to return Indiana excess accumulated deferred income tax ("EADIT"), an adjustment to INAWC's offset to its revenue requirement based on URT over-collection to include carrying charges, 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. *Id.* at 14, 7, 8. He also rejected the inclusion of the prepaid pension asset and the OPEB asset in the Company's capital structure. *Id.* at 8.

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. INAWC Rebuttal. 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 the Company's tariffs. Pet. Ex. 15. Mr. Shimansky testified that the Company is accepting certain Intervenor positions on Rebuttal, 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. *Id.* at 65.

Mr. Hobbs responded to criticisms raised by OUCC witnesses Bell, Parks, and Willoughby regarding the Company's proposed capital investments. Pet. Ex. 16. Mr. Hobbs rebutted the positions taken by the OUCC on the Company's 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. *Id.* Ms. Britto responded to OUCC witness Parks' recommendation that the Lake Station Water Treatment Plant ("WTP") should be removed from the Company's rate base, as well as to OUCC witness Seals' positions on non-revenue water and other Indiana American operations. Pet. Ex. 17 at 2-14; 14-20. She also addressed issues raised by Industrial Group witness Gorman and OUCC witness Malan regarding the Company's proposed headcount and line locate expense. *Id.* at 20-25. Finally, she responded to issues raised by CAC witness Inskeep regarding the Company's disconnect process. *Id.* at 26-30.

Mr. Rea responded to OUCC witness Bell, OUCC witness Sullivan, OUCC witness Compton, OUCC witness Dellinger, OUCC witness 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. Pet. Ex. 18.

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 the just and reasonable ROE and the appropriate capital structure for the Company in this proceeding. Pet. Ex. 19.

Ms. Grisham addressed issues raised by the OUCC and the Industrial Group regarding labor and labor related, contract services, support services and uncollectible expenses. Pet. Ex. 20. Mr. Cifuentes responded to recommendations made by the OUCC concerning the proposed updates to the Gross Revenue Conversion Factor ("GRCF"), 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. Pet. Ex. 21. He also addressed the Industrial Group's proposed adjustment related to the application of certain inflationary adjustments. *Id.* at 8-9. Mr. Kennedy responded to the changes recommended by OUCC witness Garrett to the average service life and Iowa curve estimates. Pet. Ex. 22. Ms. Ciullo supported the Company'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. Pet. Ex. 23. Mr. Farrell responded to Industrial Group witness Gorman's recommendation that the prepaid pension asset and other post-retirement employee benefits ("OPEB") asset be removed from the Company's capital structure for ratemaking purposes. Pet. Ex. 24.

D. <u>Cross-Answering Testimony</u>. The intervening parties 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. Pub. Ex. 13. OUCC witness Mierzwa responded to various witness testimony concerning their positions on water COSS, revenue allocations, and rate design proposals presented by Indiana American in this proceeding. Pub. Ex. 14. 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. IG Ex. 3 at 15.

CAC witness Inskeep provided cross-answering testimony regarding other parties' positions regarding the Universal Affordability Tariff. CAC Ex. 2. Wholesale Customers witness Callocchia responded to testimonies submitted by the OUCC, the Industrial Group, and the CAC related to their positions regarding the Company's COSS, rate design, and affordability. Wholesale Customers' ("WC") Ex. 2 at 2-13. HCRUD witness Mr. Wessler addressed certain concerns or questions raised by OUCC witness Parks regarding the anticipated water needs in Hamilton County, Indiana. HCRUD Ex. 2 at 2-11. He specifically discussed the anticipated development plans and overall need for potable water and fire protection service in the District's service territory. *Id.*

7. <u>Petitioner's Rate Base</u>.

A. <u>Utility Plant Forecast</u>.

1. <u>Major Projects</u>. Indiana American proposed to include two Major Projects in this Cause: the Winchester Major Project, which replaces the existing Winchester Water Treatment plant with a new, higher capacity WTP, and the Sheridan Major Project, which replaces the existing Sheridan WTP with a new, higher capacity WTP. Pet. Ex. 3 at 23-27. The Winchester Major Project has a projected in-service date is April 30, 2025, with an estimated cost of $25,000,000. *Id.* at 24-5. The Sheridan Major Project has a projected in-service date is August 31, 2024, with an estimated cost of $29,817,795. *Id.*

a. <u>Winchester Major Project</u>.

i. <u>INAWC Case-in-Chief</u>. Mr. Hobbs testified the Company 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. *Id.* at 23-25. 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. *Id.* at 23; Attachment MHH-7, at 1. He further testified a December 2020 inspection report indicated the aeralator system is in poor condition (Winchester Aeralator Evaluation, TIC, 2020 attached as MHH-8), the Winchester system is not able to deliver 3,500 gpm for 3-hour duration to meet fire flow recommendations, and there are structural concerns with the existing chemical building (Structural Assessment Summary, INAW, 2020 attached as MHH-9). *Id.* at 23. Mr. Hobbs also 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. *Id.* at 23-34. 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. *Id.* at 24.

Mr. Hobbs sponsored relevant portions of the Winchester Comprehensive Planning Study ("CPS") as confidential Attachment MHH-7 to his direct testimony. The Attachment discusses the recommended solution for each project, as well as alternatives the Company identified for each portion of the project. While the TIC Aeralator Evaluation report (Attachment MHH-8) identifies rehabilitation of the Aeralator unit as a potential alternative, Mr. Hobbs testified on direct 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. *Id.* at 24. He testified replacement of the facility is therefore recommended. *Id.* Mr. Hobbs sponsored Attachments MHH-7 through MHH-13 providing additional support for the Winchester Major Project. *Id.*

ii. <u>OUCC</u>. Mr. Parks recommended the Commission disallow including the Winchester project in rate base because Indiana American failed to support the need for the project at the $25 million cost. Pub. Ex. 9 at 25. Mr. Parks testified the proposed replacement plant is oversized, there is no Life Cycle Cost-Benefit Analysis 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 that its preferred project, a 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 ratepayers. Mr. Parks further testified there are substantial cost discrepancies in Indiana American's cost estimates that Petitioner has not mentioned or explained. *Id.* at 25.

Mr. Parks testified that Petitioner previously replaced the Winchester plant in 2001 after the Winchester system acquisition in 2000. *Id.* at 14. Mr. Parks described the existing facilities which includes four wells, aeration, detention, a steel Unilator 4 cell package filtration plant, disinfection, and fluoridation. There is no separate clearwell. He noted Petitioner added lead and copper corrosion control in 2019. Filter backwash drains to a 40,000-gallon concrete holding tank. He testified the plant has a 0.72 MGD firm capacity with two of four filter cells in service and a 1.44 MGD rated capacity with all filters in service (normal operation). The distribution system includes one 400,000-gallon elevated storage tank. *Id.* at 5-6. He testified Petitioner's projected 2035 maximum day demand is 0.85 MGD. *Id.* at 13. Mr. Parks testified Petitioner proposes to demolish the existing plant and chemical building and replace them with a new, larger capacity, and fully automated groundwater plant capable of unattended operation, that will include aeration, a detention tank, four vertical pressure filters, a new 50,000-gallon backwash holding tank, a new 450,000-gallon clearwell, backwash pumps, a new chemical/maintenance/office building, a new high service pump station with higher capacity pumps, and 16" discharge piping. He testified the proposed plant will have a higher 1.25 MGD firm capacity with three of the four new filters in service and a 1.90 MGD rated capacity with all filters in service. *Id.* at 5-7.

Based on Petitioner's proposed $25 million cost of the Winchester Major Project, Mr. Parks calculated a unit cost of $12.68 million per MG of rated capacity and testified this capital cost is significantly above two similar WTP Projects. *Id.* at 7. He compared the Winchester Major Project to Eastern Bartholomew Water Corporation's ("EBWC") groundwater treatment

plant[11] and Batesville Water & Gas Utility's groundwater softening plant.[12] Mr. Parks updated their 2019 costs to 2023 by an assumed 50% increase to $11.118 million and $9.081 million equivalent to $3.18 million per MG and $3.03 million per MG of rated capacity respectively. Mr. Parks testified that Petitioner's $12.68 million per MG cost is quadruple the EBWC and Batesville unit costs. *Id.* at 7-9. Using a slightly higher $3.50 million per MG unit cost than he calculated for EBWC and Batesville, Mr. Parks estimated the new Winchester plant without the maintenance garage should cost $6.65 million which is close to the $6.8 million project cost in Petitioner's CPS. *Id.* at 12.

Mr. Parks testified Petitioner selected Bowen's Design-Build team from two proposals received. He also testified Indiana American's estimated costs for Winchester's new facilities have varied and increased substantially since 2021. *Id.* at 9. He summarized the cost variations in Petitioner's annual five-year Strategic Capital Expenditure Plans ("SCEP"), the 2020 Winchester Comprehensive Planning Study ("CPS"), Mr. Hobbs' Direct testimony and attachments, and in the Monthly Major Project Updates. The initial estimated cost at $1,435,774 in 2019 for the WIN Chemical Building and Residuals Improvements, rose to $6,801,198 in 2021 for the RIC WIN Plant Improvements (A1, A2, A3, B1, B2, B4) which included additional improvements. These costs jumped nearly 175% in only one year to reach $18.6 million in 2022 and then rose to $25 million in March 2023 which implies a 34% annual inflation rate. Mr. Parks testified the Priority A and B projects appear to be what Petitioner is proposing to build. He testified the CPS estimate more closely aligns with EBWC and Batesville's 2023 updated costs. *Id.* at 9-12.

Mr. Parks testified Petitioner has not kept the IURC informed about the Winchester plant's problems that would justify building a completely new plant and improperly characterized the project as "Future" in its 2021 and 2022 IURC Annual Reports rather than current. He criticized Petitioner's minimal description of "Winchester Plant Improvements" that identified location only but without costs and some project description that would inform the Commission and others that this major project constitutes a total replacement of the existing Winchester plant. *Id.* at 12-14. Mr. Parks summarized the 2020 CPS Priority A and B projects in Table 3, whose combined costs are well below Petitioner's proposed $25 million project cost. *Id.* at 16.

Mr. Parks testified Indiana American did not evaluate any alternatives for the Winchester Major Project and did not perform a life cycle cost-benefit analyses ("LCCBA") that establishes each alternative's capital costs, annual operation and maintenance costs and present worth over a period. He testified it appears Petitioner did not actually prepare the required life cycle cost-benefit analyses for the completed Charlestown and Mooresville WTPs and the proposed Sheridan and Winchester projects. He testified that while Mr. Hobbs states alternatives identified in the CPS will be evaluated during Design-Build proposal selection and preliminary design to determine the detailed project scope, it appears Petitioner already selected what it wants to build

[11] 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 was $7.412 million, or $2.12 million per MG in 2019. *See* Pub. Ex. 9 at 7-8.

[12] 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. *See* Pub. Ex. 9 at 8.

as shown in the Design Concept document listing specific design elements the Design-Build teams must provide. *Id.* at 17-18. As part of standard capital planning efforts, especially for higher cost projects, including Major Projects, Mr. Parks recommended that Indiana American identify alternatives rather than just selecting its preferred alternative. *Id.* at 19. He further recommended Petitioner prepare and complete bona fide and required LCCBAs in order to comply with Ind. Code § 13-18-26-3. *Id.*

Mr. Parks testified the Winchester system has always met peak demand, but Petitioner claims it cannot meet the 2035 forecasted 0.85 MGD maximum day demand if two of four filter cells are in service at a 0.72 MGD firm capacity based on 3.0 gpm/ft^2. Mr. Parks analyzed Winchester's Monthly Reports of Operation from 2018 to 2022 which showed water production below 0.72 MGD over 94% of the time that is often sustained for greater than 14 days. He testified with half of the filter cells offline for painting, Petitioner could meet maximum day demands in several ways. He referenced Petitioner's discussion in CPS Project A-1, where it indicates it could temporarily filter at a higher 3.75 gpm/ ft^2 rate (within the 2.0 to 4.0 gpm/ ft^2 standard). *Id.* at 21-22. Other options include: a) schedule repainting in lower water demand periods; b) coordinate painting when large users may have reduced demand; and c) use temporary filtration units that Petitioner used for its Charlestown system in 2021. He also testified Petitioner could enlist customer help to limit usage for lawn watering, car washing, etc. *Id.*

Mr. Parks testified Petitioner does not need to increase Winchester's firm and rated capacities. He referenced Winchester's CPS indicating decreasing maximum day demand through the 2035 planning horizon. *Id.* at 22. He testified Indiana Business Research Center data showed decreasing Randolph County and Winchester population over many decades that is forecasted to continue decreasing. He reported Petitioner testified declining water usage will also continue. Mr. Parks testified usage is further restrained by Petitioner's increased rates that signal customers to wisely use water, not waste it, and repair leaky toilets and fixtures. He testified Petitioner's plan to replace the existing plant with an expanded 1.90 MGD plant at a very high $25 million cost is unsupported by Petitioner's 2020 Comprehensive Planning Study, is unwarranted, is not prudent or reasonable, and is not in the ratepayers' interest. *Id.* at 22.

Mr. Parks testified a clearwell may be beneficial to help assure disinfection contact time and to provide water for sustained high demand periods during fires. He testified Petitioner has not demonstrated that IDEM requires 4-Log virus inactivation under the Groundwater Rule and absent a documented IDEM requirement for additional disinfection facilities including a larger clearwell, Petitioner's current disinfection system should be viewed as adequate to meet all regulatory disinfection standards. Mr. Parks criticized Bowen's design concept and Indiana American's overly conservative design assumptions that oversize the clearwell and make it more expensive than it needs to be. He testified clearwell oversizing is linked to Petitioner's design criteria for providing 3,500 gpm fire flows. He recommended Petitioner refine clearwell sizing and seek lower cost LCCBA options for tank construction such as alternate materials besides welded steel that will incur substantial lifetime interior and exterior repainting costs. Such options could include bolted glass lined steel tanks and prestressed concrete tanks. *Id.* at 23-24.

Mr. Parks testified Winchester's design and layout are oversized, overly lavish, expensive, and unwarranted. He described the size, features, and high cost per foot of the new

treatment building which includes two offices, two restrooms, a lobby, a conference room for 12 people, a break room, an operator/lab area, brick exterior, a 4-bay garage area with overhead doors, parking for seven passenger vehicles and four utility trucks and other building features Petitioner claimed are confidential. Mr. Parks testified the building size and site requirements appear to be excessive when compared to the existing plant that has provided acceptable service over the last two decades. *Id.* at 24. Mr. Parks testified that all the other reasons Petitioner gave to support replacing the Winchester plant again should be addressed individually such as repairing the spalling concrete on the backwash tank, installing backup metering pumps, repairing the structural deficiencies in the chemical building, adding secondary containment, etc. Combined, these deficiencies do not warrant replacing the existing treatment plant with a completely new, larger capacity, and far more expensive plant. *Id.* at 25.

iii. INAWC Rebuttal. On rebuttal, Mr. Hobbs testified that he disagreed with Mr. Parks' recommendation with respect to the Winchester Major Project because the recommendation fails to recognize the age, capacity, condition, or process challenges associated with the current Winchester facility. Pet. Ex. 16 at 12. 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. *Id.* at 13-14. Mr. Hobbs explained these challenges include capacity concerns, structural concerns, and process challenges, and all of these challenges, in addition to the Aeralator unit, also need to be addressed at the plant. *Id.* at 21.

Mr. Hobbs responded to Mr. Parks' contention that Indiana American did not consider rehabilitating the Aeralator unit and other alternatives for the plant. *Id.* at 15. Mr. Hobbs testified the Company considered three alternatives for the aeralator unit, including rehabilitation, as identified and discussed in the Winchester CPS (Attachment MHH-7). *Id.* Mr. Hobbs also responded to Mr. Parks' claim that Indiana American did not perform a LCCBA as required under Indiana law. Mr. Hobbs walked through the relevant provisions of the statute at issue (IC ch. 13-18-26) and explained the statutes are unclear for the following reasons: (1) Section 1 states that it is establishing a precondition for receipt of a "a permit required under IC 13-18-16 for the operation of a public water system" even though IC 13-18-16 establishes permit requirements for the "construction, installation, or modification" of public water systems (i.e., not permits for "operation"); and (2) the definition of "life cycle cost-benefit analysis" is unclear because the terms "costs" and "benefits" are undefined. *Id.* at 19. Mr. Hobbs further testified the statute is enforced by IDEM, and IDEM has not promulgated any regulations regarding what a life-cycle cost benefit analysis should include. *Id.* at 20. He also testified that while IDEM has issued one guidance document, the document does not provide much additional insight into the specific requirements for IC 13-18-26-3 and the link that the document provides to see a sample is broken. *Id.* at 20. 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. *Id.*

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. *Id.* at 15-16. He explained that due to Aeralators combined

treatment components (aeration, detention, and filtration) there is added operational complexity and maintenance challenges associated with the combined unit. *Id.* at 16. Mr. Hobbs explained that a separated process layout like the Company is proposing as part of the Winchester Major Project will allow the system's individual components (such as an individual filter) to be taken offline for maintenance and repair while maintaining treatment. *Id.* at 16. In contrast, Mr. Hobbs explained that as combined units, 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. *Id.* Further, 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. He testified that during the 4-5 month period full temporary treatment would be required. *Id.* at 16-17.

Further, Mr. Hobbs testified rehabilitation of the Aeralator does not consider the age and deteriorated condition of the existing Aeralator unit. *Id.* at 17. He testified that at 22 years of service the Aeralator is already nearing its anticipated end of life. *Id.* 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. *Id.* Mr. Hobbs further testified he disagreed with Mr. Parks' statement 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 it is acceptable for the system demand to exceed the firm capacity of the existing water treatment facility, which is not in alignment with water industry standards, Indiana Code, or the Ten State Standards. *Id.* at 22-23. 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. *Id.* at 22. Mr. Hobbs cited to the Company's Winchester CPS and 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. *Id.*

Further, Mr. Hobbs reiterated that addressing the issues with the Aeralator unit will not address the other plantwide 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 CPS. *Id.* at 15. Mr. Hobbs discussed each of these challenges in his rebuttal testimony and explained that these challenges also need to be addressed in addition to the Aeralator unit. *Id.* at 23-25. Mr. Hobbs testified that the new clearwell is needed to provide adequate fire flow protection in the system. *Id.* at 27. He explained that the current capacity from the current WTP is only adequate for meeting a fire flow demand of up to 2,500 gallons per minute ("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. *Id.* at 25. Mr. Hobbs testified there exists a significant number of commercial and industrial sites around the system that have an ISO fire flow guideline of 3,500 gpm for a 3-hour duration. *Id.* 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. *Id.* at 26-27.

Mr. Hobbs also responded to Mr. Parks' criticisms of 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, and testified that a more appropriate cost comparison would be to the Mooresville water treatment plant which was completed more recently for a total cost of $21,708,452. *Id.* at 33-36. Further, with respect to Mr. Parks' criticisms of the Company for providing varying cost estimates, Mr. Hobbs identified the various sources of the costs estimates Indiana American included in this Cause and testified that he would expect cost estimates to vary for an individual capital project. *Id.* at 8. 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. *Id.* Mr. Hobbs also testified that he disagreed with Mr. Parks' contention the Winchester treatment plant is oversized and overly lavish, and explained recent water treatment plants constructed by Indiana American included similar amenities. *Id.* at 28-29.

In response to Mr. Parks' criticisms of the Winchester Major Project cost, Mr. Hobbs reiterated that the Winchester Major Project is being competitively procured through a design-build proposal process and subsequent competitive sub-package bidding. *Id.* at 34. Mr. Hobbs testified that Indiana American's estimated cost is therefore based on actual pricing. *Id.* Mr. Hobbs testified further that only final, actual costs of the projects will be reflected in rate base. *Id.* at 32.

iv. Discussion and Findings. With respect to the Winchester Major Project, the crux of the issue between Petitioner and the OUCC is the high cost of the replacement plant that is significantly higher than the cost of treatment plants constructed by other utilities, the larger capacity of the proposed Winchester plant, and 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 argues Indiana American did not identify and consider alternatives for the plant and did not perform a LCCBA of these alternatives as required by IC § 13-18-26-3. Pub. Ex. 9 at 17. Further, the OUCC testified Indiana American has not supported that total replacement of the plant is warranted and the plant is too expensive at $25 million. *Id.* at 25.

Mr. Hobbs disagreed with Mr. Parks that Indiana American failed to evaluate alternatives for the plant and perform a LCCBA. Pet. Ex. 16 at 15, 18. Mr. Hobbs cited to confidential Attachment MHH-7 (the relevant portions of the Winchester CPS) provided with his direct testimony which identifies and discusses the alternatives the Company considered for the Aeralator unit and other portions of the project. *See* Attachment MHH-7 (Redacted) at 1-20. Further, with respect to the OUCC's argument that Indiana American did not perform a LCCBA under Ind. Code § 13-18-26-3, Mr. Hobbs explained in his rebuttal testimony the uncertainty of Ind. Code § 13-18-26-3 and lack of guidance from IDEM. Pet. Ex. 16 at 18-20.

While Mr. Hobbs explained that Indiana American did consider rehabilitating the existing Aeralator unit, Mr. Parks identified evidence that a field inspection in 2020 had recommended rehabilitation within the next two years, which was not done by Indiana American. Pub. Ex. 9 at 19-21.

Regarding the dispute between the parties on whether Indiana American identified alternatives for the Winchester Major Project, we find that Indiana American did not sufficiently

identify alternatives for the project and did not include cost information on the alternatives. While Confidential Attachment MHH-7 identifies and discusses the individual alternatives that were identified for each portion of the Winchester Major Project, this discussion notes that additional information is needed. For example, discussing the rehabilitation of the Aeralator unit, the CPS states "It is recommended to perform a life cycle cost comparison of this alternative with the primary recommendation to install new filtration capacity prior to proceeding with the project." Pet. Ex. 3, Attachment MHH-7 at 4. Therefore, we agree with the OUCC that Petitioner did not identify alternatives for the project and agree with the OUCC that Indiana American did not evaluate these alternatives as part of a LCCBA as required under IC § 13-18-26-3, despite the uncertainties of the statute.

Ultimately, the record shows that the current Winchester Water Treatment plant is capable of meeting current and projected maximum day demands for the Winchester system. Mr. Parks raised the issue of declining population in Randolph County and Winchester, which was unrebutted by Mr. Hobbs. Indiana American did not present sufficient evidence on replacing or rehabilitating the Aeralator unit, so it is unknown whether it would produce any savings in the overall project cost.

The only remaining issue we need to address is the estimated cost of the Winchester Major Project. The OUCC took issue with the $25 million cost Indiana American estimated for the project and Mr. Parks estimated that the new Winchester Plant without the maintenance garage should cost $6.65 million. Pub. Ex. 9 at 12. Mr. Parks estimated this amount based on his comparison to two other treatment plants - Eastern Bartholomew Water Corporation plant and the Batesville Water & Gas Utility water treatment plant. On rebuttal, while Mr. Hobbs pointed out that the Eastern Bartholomew and Batesville plants are not good comparisons, because the projects were completed many years ago, the project were only completed in 2019. Pet. Ex. 16 at 34-35. We believe it is appropriate to evaluate the cost of the proposed Winchester facility in comparison with other, similar facilities. In this case, both facilities referenced by Mr. Parks have larger rated capacities than the proposed Winchester facility but are priced significantly lower.

Based on the lack of an adequate alternative analysis including the required LCCBA, the lack of immediate need for the new facility, and excessive cost compared to similar facilities, we cannot find the $25 million estimated cost of the project is appropriate.

b. <u>Sheridan Major Project</u>.

i. <u>INAWC Case-in-Chief</u>. Mr. Hobbs explained the Company 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. Pet. Ex. 3 at 26. With respect to the plant's capacity challenges, Mr. Hobbs testified the existing Sheridan Water Treatment facility 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. *Id.* Mr. Hobbs further testified much of the existing facility and equipment dates back to the 1960s and has limited remaining life. *Id.* 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. *Id.*

Mr. Hobbs testified that while the Company considered continuing to use the existing facility, doing so was not the recommended solution for a variety of reasons. Pet. Ex. 3 at 27. Mr. Hobbs sponsored relevant portions of the Sheridan CPS as confidential Attachment MHH-15 to his direct testimony. Attachment MHH-15 identified the alternative the Company considered for the project, which is rehabilitation and expansion of the existing plant. Attachment MHH-15 at 5. 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. *Id.* Mr. Hobbs testified that maintaining the existing facility would also require additional cost for providing treatment while it is rebuilt. *Id.* Mr. Hobbs further testified that by constructing one new expandable facility, the Company 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. *Id.*

ii. <u>OUCC</u>. Mr. Parks recommended the Commission disallow the Sheridan project because Indiana American failed to support the need for the project at the excessively high $29.82 million cost and did not support that its preferred project, a total replacement of the existing plant with a much larger plant, is prudent, reasonable, or in the best interest of ratepayers. Pub. Ex. 9 at 8-9, 43-44. Mr. Parks testified the proposed Sheridan replacement plant is oversized, has no Life Cycle Cost-Benefit Analysis of alternatives as required by IC§ 13-18-26-3, and is too expensive at $29.82 million or $15.38 per MG of rated capacity, which exceeds costs paid by other utilities for groundwater treatment plants. *Id.* at 44.

Mr. Parks testified that Sheridan's water production averaged 212,000 gallons per day (0.212 MGD) for 2019 to 2022. He reported Sheridan's treatment facilities include a 2.16 MGD well field with all three wells in service and a groundwater treatment plant that has a 0.65 MGD rated capacity with all filters in service (normal operation) and a 0.43 MGD firm capacity with two of three filters in service. He reported Petitioner replaced the filter media and both high service pumps in 2019. He testified there is no WTP clearwell, but the system includes a 0.5 MG elevated water tank installed in 2007. *Id.* at 26-27. Mr. Parks reported Petitioner has added an average of 45 new customers annually to its Sheridan system, which it acquired in 2018, and now serves 1,350 residential customers with an estimated population of 3,429 people. *Id.* at 28.

Mr. Parks summarized Petitioner's proposed Sheridan Major Project to demolish and replace the existing plant with a new larger capacity, fully automated plant capable of unattended operation with firm and rated capacities of 1.5 MGD and 2.0 MGD respectively but with several components sized for future expansion to 4.0 MGD. He testified Petitioner reported in Monthly Update No. 3, that costs increased to $30,761,981 for the proposed WTP, which equates to $15.38 million per MG of rated capacity. *Id.* at 28-29. Mr. Parks compared the capital cost and cost per MG of capacity for Sheridan to costs, updated to 2023 prices, from two similar 2019 WTP projects that were competitively bid at Eastern Bartholomew Water Corp. and Batesville. He testified Sheridan's capital cost is significantly more expensive than these plants and is also higher than Petitioner's proposed Winchester WTP. Mr. Parks increased the updated 2023 costs further for Batesville and Eastern Bartholomew to $3.5 million per MG of rated capacity and estimated the new 2.0 MGD Sheridan plant should cost $7.0 million instead of the $29.82 million requested by Petitioner. *Id.* at 30-33.

Mr. Parks reported that from three invited Design-Build teams, Petitioner selected Reynolds to build the new Sheridan WTP but that he understood selection was not based on lowest construction cost or lowest total project costs but rather on the Lump Sum Price Proposal for design fees, Design/Builder's fee, construction superintendence, and bond costs and on evaluation criteria identified by the Petitioner in the RFP. He testified the contractor was not selected through an open, competitive public bid in which all contractors wanting to complete the work can submit a bid. Mr. Parks testified Petitioner has had varying project cost estimates and summarized the varying 2021 to 2023 costs. He noted Sheridan's project was not listed on Petitioner's annual five-year Strategic Capital Expenditure Plan ("SCEP") until 2022 for the 2023-2027 SCEP. *Id.*

Mr. Parks testified he did not see evidence in Petitioner's Case-in-Chief that it has not met customer demands. He noted the existing WTP's firm and rated capacities met the 0.41 MGD maximum day flow over the last four years and that Petitioner's 500,000-gallon storage tank has over two days average storage to help meet maximum day demand and fire flows. *Id.* at 35. Mr. Parks refuted Mr. Hobbs' claim the Sheridan WTP was not designed for expansion by referencing the Sheridan Waterworks Improvement drawings in Mr. Hobbs Attachment MHH-16. The drawings show space reserved for a fourth filter that would increase firm and rated capacities to 0.65 MGD and 0.86 MGD. Mr. Parks recommended Petitioner evaluate costs to add the fourth filter and a third high service pump. Mr. Parks testified that the draft Sheridan CPS states an alternate solution is that in lieu of constructing a new WTP, the existing facility could be expanded but a condition-based assessment of the WTP building would be needed. Mr. Parks testified Mr. Hobbs did not indicate a condition assessment was conducted. Mr. Parks interpreted the lack of a condition assessment to indicate Petitioner has not developed and evaluated any alternatives that could meet near term water demands and delay a complete WTP replacement with its high cost to ratepayers. *Id.* at 36

Mr. Parks testified Indiana American has not kept the Commission informed about the need to demolish and replace the Sheridan WTP, noting Petitioner first listed the WTP and Source of Supply projects in the 2022 IURC Annual Report submitted in April 2023. He testified Petitioner did not finalize the Sheridan Comprehensive Planning Study but listed four Priority A projects in the draft CPS, presented single line cost estimates with no details, and that Appendix B which was to include detailed costs was empty. *Id.* at 36-37. Mr. Parks summarized the Priority A projects in Table 9.[13] Mr. Parks testified he included Project A-1, Regionalization Study because in its CPS, Indiana-American recommended a Regionalization Study to determine how best to serve the Hamilton County Regional Utility District ("HCRUD") including providing service from Sheridan or from Noblesville via an eight-mile cross-county transmission main. He agreed such a study would be advisable and that ratepayers would benefit if Petitioner paused its plan to replace the Sheridan WTP until the study was completed. *Id.* at 38-39.

Mr. Parks testified Indiana American did not evaluate any alternatives besides its preferred $29.82 million Sheridan WTP replacement project and provided no evidence that the Company considered the rebuild/expansion/upgrade alternative in more than a perfunctory manner. *Id.* at 39. He testified Petitioner has not provided any evidence that its existing filters

[13] The Sheridan Priority A Projects include A-1, Regionalization Study; A-2, Additional Source of Supply; A-3, New Sheridan WTP, and A-4, Distribution System Main Upgrade for New WTP.

cannot continue to operate and stated value to ratepayers will be enhanced if the rebuild/expansion/upgrade alternative can postpone the high-cost replacement WTP until the Regionalization Study is completed, supply chain/inflation issues subside, and construction markets return to normal. *Id.* Mr. Parks testified there is a total absence of any attachment, evaluation, cost estimate, or Life Cycle Cost-Benefit Analysis examining any alternative. He noted that Indiana law requires a life cycle cost-benefit analysis of the WTP options under Ind. Code § 13-18-26-3. *Id.* at 40.

Mr. Parks testified Petitioner's proposed flows are overestimated, replacement in the near term (five years) appears unneeded and could be delayed by adding the fourth filter. *Id.* at 41. He also testified that remarkably, Petitioner states new plant capacity does not include HCRUD water demand. He testified Petitioner's growth assumptions and demand forecasts appear aggressive, and that forecasting maximum day demand at a 95% confidence interval, representing a level not exceeded more than once every 20 years, is overly conservative and causes oversized excess capacity facilities with higher costs. He testified Petitioner assumed new residential customer usage much higher than the existing 108 gallons per day usage despite water efficient plumbing fixtures being required in new homes. *Id.* at 40-42.

Mr. Parks testified replacing the existing plant at a very high $29.82 million is unsupported by the Draft Comprehensive Planning Study, is unwarranted, and is not prudent, reasonable, or in ratepayers' interest. The new treatment building is much bigger than the existing building with an extensive footprint despite the proposed plant being fully automated and capable of unattended operations. He testified Petitioner needs to explain why it needs to build facilities that are so drastically oversized and expensive and, why they must be built now. He testified Petitioner should individually address treatment plant issues and that combined, these deficiencies do not warrant replacing the existing treatment plant with a completely new, larger capacity, and far more expensive plant. *Id.* at 42-43.

iii. <u>INAWC Rebuttal</u>. On rebuttal, Mr. Hobbs testified he disagreed with Mr. Parks' opinion and recommendation to disallow the Sheridan Major Project because it is too expensive, oversized and has no Life Cycle Cost Benefit Analysis of alternatives as required by IC § 13-18-26-3, among other criticisms. Pet. Ex. No. 16 at 36. Mr. Hobbs testified that Mr. Parks fails to recognize the age, capacity concerns, condition, operation and process challenges of the Sheridan facility. *Id.* Mr. Hobbs referenced his direct testimony and explained that Indiana American needs to replace the existing Sheridan treatment plant due to capacity concerns, the age of the facility and not being easily expandable, operational challenges, including the need to add a new well, to switch from chlorine gas to liquid sodium hypochlorite, and to add an ammonia feed. *Id.* at 37-38.

Mr. Hobbs testified regarding the capacity challenges at the current plant. Mr. Hobbs testified the Company already has challenges meeting maximum day demands and potential growth in the service area in the near future will only exacerbate these concerns. *Id.* at 37. Mr. Hobbs 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. *Id.* at 39. 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. *Id.* He explained that the existing Sheridan water treatment plant 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. *Id.* Thus, the current firm filtration capacity is inadequate to meet the projected maximum day demands for all three scenarios. *Id.* 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. *Id.* at 39. Further, Mr. Hobbs testified 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 fifteen-year projected demand. *Id.* at 41.

Mr. Hobbs disagreed with Mr. Parks' recommendation that Indiana American wait to construct the new Sheridan WTP until it completes a regionalization study.[14]. Mr. Hobbs testified HCRUD's projected full build-out demand exceeds Sheridan's current supply and production capacity. He testified the Sheridan WTP project is to address current and projected water demands challenges. He further testified that Indiana-American cannot reliably meet Sheridan's maximum day demands today and the projected maximum day demands used in the sizing of the water treatment plant excludes HCRUD's demand. *Id.* at 42. Mr. Hobbs explained the purpose of the regionalization study and the relationship of the study to HCRUD is to determine the optimal means of providing water service to HCRUD 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. *Id.* Mr. Hobbs testified that while the regionalization study will be helpful for determining how to serve the vast 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. *Id.*

Mr. Hobbs testified that Mr. Parks is correct that the Sheridan Major Project will not, upon completion, produce enough water to serve the County at full build-out. *Id.* at 61. He explained that Indiana American has not sized the new Sheridan Water Treatment Plant to serve a fully developed Bakers Corner, and the design of the plant at initial completion is intended to serve growth in Sheridan. *Id.* 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 the County from the Sheridan WTP, the Company would expand the plant and add additional source of supply to do so. *Id.*

Mr. Hobbs explained Petitioner's "regionalization strategy" for the entire northern portion of Hamilton County, which is about much more than Bakers Corner. He testified Petitioner is conducting a regionalization study and that one likely outcome is interconnection of the Sheridan and Noblesville Operations, similar to what the Company has done with Johnson County and Shelbyville. With the main that Petitioner plans to construct to serve Bakers Corner, the distance separating those two operations will be cut by about one-third. He testified that once that regionalization study is completed, Petitioner will have a more complete understanding of the best way to bring water to the entirety of this undeveloped area, and Petitioner will be in a

[14] Mr. Parks testified that in Sheridan's draft CPS, Petitioner recommended a Regionalization Study to determine how best to serve the HCRUD including service from Sheridan or Noblesville via an eight-mile cross-county transmission main. Mr. Parks agreed the study was advisable and ratepayers would benefit if Petitioner paused its plan to replace the Sheridan WTP until the study was completed. Pub. Ex. 9 at 38-39.

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 Petitioner has not yet identified. *Id.* at 62.

Mr. Hobbs also responded to Mr. Parks' contention that Indiana American did not evaluate alternatives for the Sheridan Water Treatment Plant and did not complete a LCCBA. Mr. Hobbs testified the draft 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 aging facility. *Id.* at 45. Mr. Hobbs testified the Company 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. *Id.* at 44. Mr. Hobbs explained the Company 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. *Id.* at 45. He also explained that there are several challenges associated with attempting to expand the plant, and it is questionable whether the current plant could be expanded. *Id.* at 44-45. Mr. Hobbs identified the numerous challenges that would need to be addressed in order to expand the existing facility at pages 47-49 of his rebuttal testimony. With respect to the LCCBA, Mr. Hobbs once again explained that Indiana American followed the statutory language and compared the costs and benefits of the proposed improvements to one or more alternatives. *Id.* at 49-50.

Mr. Hobbs also responded to Mr. Parks' criticisms of 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. *Id.* at 57. Mr. Hobbs testified the Sheridan 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. *Id.* at 57. Mr. Hobbs again testified that a more appropriate cost comparison would be to Indiana-American's Mooresville water treatment plant which was completed more recently for a total cost of $21,708,452. *Id.* at 57-58.

iv. Discussion and Findings. The OUCC recommended disallowing Petitioner's Sheridan Major Project, because Indiana American failed to support that its preferred $29.82 million total replacement of the existing plant with a larger plant, is prudent, reasonable, or in the best interest of ratepayers. Pub. Ex. 9 at 43-44. Mr. Parks testified the proposed Sheridan replacement plant is oversized, there was no Life Cycle Cost-Benefit Analysis of alternatives as required by IC§ 13-18-26-3, and the project is too expensive at $29.82 million or $15.38 per MG of rated capacity, which exceeds costs paid by other utilities for groundwater treatment plants. *Id.* at 42-44. Petitioner posits that the major dispute between the parties about the Sheridan Major Project is whether Indiana American developed and evaluated alternatives to total WTP replacement as part of the required LCCBA. Here, the OUCC argues Indiana American did not conduct a condition-based assessment of Sheridan's plant as recommended in its draft CPS[15] and that Petitioner provided no evidence the Company considered the rebuild/expansion/upgrade alternative in any other way than a perfunctory manner, stating there is a total absence of any attachment, evaluation, cost estimate, or Life Cycle Cost-Benefit Analysis examining any alternative. Pub. Ex. 9 at 36, 39. The OUCC agreed

[15] Pet. Ex. 3, Attachment MHH-15

Petitioner should complete a regionalization study, as recommended by Petitioner in its draft CPS, and recommended Indiana American pause its plan to replace the Sheridan WTP until the study is complete. *Id.*

On rebuttal, Mr. Hobbs testified that Indiana American did consider rehabilitating and expanding the plant. Pet. Ex. 16 at 45 Many different components to an expansion were presented in the draft CPS provided as Attachment MHH-15 to Mr. Hobb's testimony. However, Mr. Hobbs claims that the rehabilitation/expansion option was 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. Pet. Ex. 16 at 45. The Company expanded on this issue in its Response to the Commission's Docket Entry dated August 25, 2023, where it included pictures of the existing Sheridan Water Treatment Plant which show existing building deterioration, building footprint limitations for expansion because the space reserved for the fourth filter is being occupied by laboratory and chemical use, and current use of gas chlorination. Pet. Ex. 28, IURC 03-06 Attachment 02. Mr. Hobbs testified on rebuttal and Petitioner reiterated in its docket entry response that the Company does not view conducting a more in-depth condition assessment of the existing WTP as a prudent use of resources and 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. Pet. Ex. 28, at 4; Pet. Ex. 16 at 45. Petitioner stated it "knows that rehabilitating the existing plant will not provide the needed capacity or operational flexibility needed to serve the needs of the Sheridan and Hamilton County communities." Pet. Ex. 28 at 4. Therefore, cost estimates and a comparison of the alternatives that were requested in the Docket Entry dated August 25, 2023 were not provided. Additionally, while an LCCBA was not provided, Mr. Hobbs defends this by citing the uncertainty of the statute, the lack of guidance from IDEM regarding what a life-cycle cost benefit analysis should include, and concluding that the comparison of the cost and benefits was done in the DRAFT CPS, which compares the proposed new treatment plant to the alternative of expanding the facility. Pet. Ex. 16 at 18-20, 50.

Mr. Hobbs also testified regarding the capacity challenges at the current plant. He cited to the current and projected future demands of the system in his rebuttal testimony, and testified the Company already has challenges meeting maximum day demands and potential growth in the service area in the near future will only exacerbate these concerns. *Id.* at 37, 39.

With respect to the need for the new Sheridan water treatment plant, Mr. Hobbs testified that the Sheridan system is located in Hamilton County, which is one of the fastest growing areas in the State. *Id.* at 60. However, Petitioner has not prepared any population growth and water demands studies for Hamilton County or HCRUD and such studies are not in the record. OUCC Cross Exhibit CX-3, DR 56-24, DR 63-6, DR 63-7, DR 64-2, and DR 64-3. There is no evidence that the same pace of growth experienced by Hamilton County in recent years will be sustained uninterrupted for the next twenty years or what percentage of the growth will occur in Sheridan's, Noblesville, or HCRUD's system.

The OUCC agreed with Indiana American's recommendation in the draft Sheridan CPS that a Regionalization Study should be conducted to determine how best to serve HCRUD, including providing service from Sheridan or from Noblesville via an eight-mile cross-county transmission main. The OUCC suggested ratepayers would benefit if Petitioner paused on its

plan to replace the Sheridan WTP until the Regionalization Study was completed. Public Ex. 9 at 39. The OUCC also noted Sheridan's WTP was designed with space reserved for a fourth filter, that if installed, would increase firm and rated capacities to 0.65 MGD and 0.86 MGD. The OUCC suggested Petitioner evaluate costs to add the fourth filter and a third high service pump. *Id.* at 36. The OUCC stated there is value to ratepayers if the rebuild/expansion/upgrade alternative can postpone the need for the high-cost replacement WTP until the Regionalization Study is completed, supply chain/inflation issues subside, and construction markets return to normal. *Id.* at 39. Further, surprisingly, Petitioner's testimony shows that the sizing of the water treatment plant excludes HCRUD'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.

The OUCC argues that Indiana American should have considered rebuilding and expanding the current plant for the five-year near-term period until the Regionalization Study is completed as an alternative to the costly total replacement of Sheridan's plant now. Pub. Ex. 9 at 39. While Indiana American stated in rebuttal and in its docket entry response that it did consider rehabilitation of the existing plant, but that due to the age of the plant (approximately 60 years old) and due to the fact that expansion of the existing plant is likely not feasible, it determined without a more in depth condition assessment of the existing WTP that this alternative is not a viable or feasible alternative to total replacement.

The OUCC also took issue with Petitioner's estimated cost for the Sheridan Major Project of $29,817,795. Pub. Ex. 9 at 44. Like the Winchester Major Project, 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. *Id.* at 30. Both the Eastern Bartholomew and Batesville plants are rated at higher capacities than the Sheridan WTP, yet both cost far less, at $7.4 million and $6.1 million, respectively, versus $30 million for the Sheridan WTP. *Id.*

Mr. Hobbs disputed the comparison, stating there is no additional information on the Eastern Bartholomew and Batesville plants to correlate the specific components to the Sheridan facility, but then suggests that comparing costs to costs for the Indiana-American Mooresville facility is appropriate. Pet. Ex. 16 at 57-58. The OUCC's point is that costs for Petitioner's proposed Major Projects are quadruple the cost for comparable groundwater treatment plants. Limiting cost comparisons only between Indiana-American plants would hide this cost difference. While Mr. Hobbs testified on both direct and rebuttal that the Sheridan Major Project was competitively procured through a design-build proposal process it is appropriate to evaluate the cost of the project in comparison to other, similar facilities. Pet. Ex. 3 at 27; Pet. Ex. 16 at 57.

Based on the lack of an adequate alternative analysis, the lack of immediate need for the new facility, and excessive cost compared to similar facilities, we cannot find the $29,817,795 estimated cost of the project is appropriate.

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

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

i. INAWC Case-in-Chief. While not discussed directly in the body of his testimony, Indiana American witness Hobbs included, as part of the capital additions in this Cause, Project I10-100019, "Kokomo Sheridan Interconnect-EST to Springmill," 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 HCRUD water system at Springmill Road & 236th Street, more commonly known as Bakers Corner. Pet. Ex. 3, Attachment MHH-4 at 1-2. Indiana American estimates the total project cost is $9,278,301. Indiana American proposed the project for inclusion in this Cause because the Company entered into a sale-for-resale agreement to provide drinking water for HCRUD located between Sheridan and Noblesville, and interconnection with an existing Indiana American Water system was required to serve the district. *Id.*, and Workpaper MHH-10, Wholesale Water Supply Agreement with HCRUD, dated December 12, 2022.

ii. OUCC. Mr. Parks described the proposed $9.3 million project to extend 11,400 feet of 20-inch (Phase 1) and 7,700 feet of 16-inch (Phase 2) transmission main east from Sheridan to HCRUD to be completed September 30, 2024. Pub. Ex. 9 at 44. He explained the project name, Kokomo Sheridan Interconnect – EST to Springmill is a misnomer. The project will be in the Kokomo District but will not interconnect Sheridan with Kokomo. Rather it will connect Sheridan with the yet to be developed HCRUD, a new Regional Water and Sewer District formed to spur development within the US 31 Corridor project area near Baker's Corner in Hamilton County. He testified Petitioner has excess water production capacity in Noblesville's system that could provide water to HCRUD via an eight-mile transmission main across Hamilton County, but Petitioner decided to construct a new shorter main from Sheridan. *Id.* at 44-45. He testified Petitioner's Sheridan groundwater wells and water treatment facilities cannot meet HCRUD's long-term demand and would require additional treatment and pumping facilities. *Id.* at 46. Mr. Parks testified the years for the initial and long-term demand are not listed and Petitioner did not discuss or specify a timeframe for meeting the long-term demand. He noted the Water Supply Agreement term is twenty years, renewable every ten years. *Id.* at 45-46.

Mr. Parks stated that WTP capacity for Sheridan "does not include near or long-term demand from the area referred to as 'Baker's Corner.' Service to the Baker's Corner area would require significant additional supply and a hydrogeological study to determine supply location and feasibility." *Id.*, quoting Pet. Ex. 3, Attachment MHH-3 at 2. Mr. Parks testified he agreed with Petitioner that a Regionalization Study to determine how best to serve HCRUD, including providing service from Sheridan or Noblesville, would be advisable. He stated ratepayers would benefit if Petitioner paused on the plan to replace the Sheridan WTP until the study was completed. *Id.* at 38-39.

Mr. Parks testified Mr. Hobbs did not mention the main extension rules nor did HCRUD's Water Supply Agreement call out the new transmission main as a "main extension" subject to 170 IAC 6-1.5 – Extension of Water Mains. *Id.* Mr. Parks testified Indiana-American appears obligated under Section 2 of the Water Supply Agreement for design, construction, and

easement acquisition costs. *Id.* at 48. Mr. Parks testified the project is clearly a main extension subject to the Commission's main extension rules. He testified Petitioner should have developed a main extension agreement and developed estimated costs for design and construction. He further testified all main extension costs except a three-year revenue allowance are HCRUD's responsibility to be paid to Petitioner. *Id.* He testified the estimated $9,278,301 project costs should not be added to rate base without a main extension payment by HCRUD reflecting its contribution in aid of construction. Because Petitioner has not properly characterized the project as a main extension Mr. Parks recommended the Commission disallow recovery of the capital costs in rate base. *Id.* at 49.

Finally, to minimize the future risk that Indiana-American ratepayers will have to pay to relocate the transmission main due to road widening, Mr. Parks recommended obtaining permanent easements and building the new transmission main away from 236th Street, a transportation primary arterial in favor a route along agricultural fields and county roads that are not likely to be widened in the future. *Id.* at 50.

iii. **Rebuttal**. On rebuttal, Mr. Hobbs testified he disagreed with Mr. Parks' contention that the new transmission main to connect Indiana American's system with the newly formed HCRUD is a main extension that is subject to the Commission's rules under 170 IAC 6-1.5. Pet. Ex. No. 16 at 59. 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 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 which showed Indiana American satisfied the 20-year test set forth in Indiana Code 8-1-2-46.2(b). Pet. Ex. 15 at 16-17. 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. *Id.* 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 HCRUD was required and the Commission's main extension rules did not apply. Pet. Ex. 16 at 60. Mr. Hobbs testified that Mr. Parks' testimony about a three-year revenue allowance and a requirement that the County fund a portion of the cost is therefore incorrect. *Id.*

Mr. Hobbs reiterated why the new transmission main to HCRUD is a unique main extension. Mr. Hobbs testified that it is well understood that Hamilton County has long been one of the fastest growing areas in the State. *Id.* 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. *Id.* He further testified that growth has continued north in the County and has reached the point that the northern portion of the County is the only area that remains undeveloped. *Id.*

Mr. Hobbs expanded on the purpose of the regionalization study, the relationship of the study to serving HCRUD, 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 Water Treatment Plant 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. Pet. Ex. 16 at 61. 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. *Id.* at 62. Mr. Hobbs testified that the Company is in the process of conducting a regionalization study, and once the study is completed and the Company 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. *Id.* at 62.

iv. <u>Discussion and Findings</u>. 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 HCRUD. 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 HCRUD. Pub. Ex. 9 at 48. In contrast, Indiana American argues this is a unique main extension that falls under Indiana Code 8-1-2-46.2(b), which allows, among others, a water utility to 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 twenty (20) year period. Pet. Ex. 16 at 59-60. Mr. Shimansky sponsored Attachment GDS-2R which purportedly showed the extension will result in a positive contribution of service in year 13. Pet. Ex. 15 at 17. Mr. Shimansky assumes that HCRUD's water use ramps up to its projected usage of 2.45 MGD over a 20-year period by adding approximately 900 customers a year. *Id.* However, this assumption has no foundation in the record, and even goes against HCRUD's own projections. HCRUD states there is no study

which supports adding approximately 900 customers a year. Pub. Ex. CX-7, Part 1, p. 2 of 335. HCRUD goes on to note that for cash flow purposes, it has assumed growth of only 150 customers per year, a small fraction of what Mr. Shimansky assumes. *Id.* HCRUD projections actually show growth of approximately 150 customers per year for years 1-10, Pub. Ex. CX-7, Part 2, p. 151 of 172, and only 75 customers per year for years 11-20. Pub. Ex. CX-7, Part 2, p. 154 of 252. Using HCRUD's projections, and not Mr. Shimansky's "conservative assumption," will not result in a positive contribution of service over a 20-year period. We therefore find that the requirements of Ind. Code § 8-1-2-46.2(b) are not met. As such, the main extension rules apply. As such, the estimated $9,278,301 project costs should not be added to rate base without a main extension payment by HCRUD reflecting its contribution in aid of construction.

b. Future Source of Supply.

i. INAWC Case-in-Chief. The Company included four future sources of supply projects in this Cause: (1) Project I10-100020 – KOK Sheridan Property Acquisition for New Well or Wells; (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. Pet. Ex. 3 at 29. Mr. Hobbs testified the Company 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 the Company's property pursuant to Ind. Code § 8-1-2-23.5. *Id.*

Section 23.5 requires the public utility's plan to include: (1) the public utility's 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. *Id.* at 30. Mr. Hobbs sponsored the Company's plans to develop each of these future sources of supply as Attachment MHH-24, and testified the information required by Section 23.5 is included in the Company's plans for each of the future sources of supply. *Id.* Mr. Hobbs testified that Indiana American's future source of supply plans are reasonable and prudent for the provision of safe and reliable service. *Id.*

ii. OUCC. OUCC witness Ms. Willoughby challenged the KOK Sheridan Property Acquisition for New Well or Wells project. Pub. Ex. 11 at 10. Ms. Willoughby 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 INAW to acquire property for a future wellfield in Sheridan. *Id.* 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. *Id.* Therefore, she recommended the Commission deny the $779,566 requested for the acquisition of land for new well(s) in Sheridan. *Id.* at 13.

iii. Rebuttal. On rebuttal, Mr. Hobbs responded to Ms. Willoughby's recommendation that the Sheridan future source of supply project be disallowed from rate base. Pet. Ex. 16 at 70. 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. *Id.* 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. *Id.* 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 Indiana Code sets forth a refund procedure to restore to ratepayers. *Id.*

iv. Discussion and Findings. The future source of supply project challenged in this Cause is Project I10-100020 – KOK Sheridan Property Acquisition for New Well or Wells. To be clear, this request is only for the acquisition of land for future source of supply. The OUCC argues that the Sheridan Source of Supply project should be disallowed from rate base because additional wellfield capacity is not currently needed in Sheridan and will not be needed through 2040, fifteen years after the land acquisition in this Cause. Pub. Ex. 11 at 10. On rebuttal, Mr. Hobbs explained that Ind. Code § 8-1-2-23.5 allows for a water utility to acquire vacant ground for a future well field before that land has been developed and becomes unavailable.[16] Pet. Ex. 16 at 70. Mr. Hobbs explained that if the 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 set forth in Petitioner's plan, Ind. Code § 8-1-2-23.5 sets forth a refund procedure to restore ratepayers.[17] *Id.*

We agree with Indiana American that Ind. Code § 8-1-2-23.5 allows a utility to seek approval of a future source of supply project. However, we must still determine whether Indiana American's plans to develop the Sheridan future source of supply project proposed in this Cause satisfies the requirements of Ind. Code § 8-1-2-23.5. Under Ind. Code § 8-1-2-23.5(a), the public utility must seek approval of its plan to develop a future source of supply and the plan must include: (1) the public utility's 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.[18] The statute requires the Commission to approve the public utility's plan "if the Commission finds that the plan is reasonable and prudent for the provision of safe and reliable service."[19]

Mr. Hobbs sponsored Indiana American's plans to develop the Sheridan future source of supply project included in this Cause as Attachment MHH-24. Mr. Hobbs testified that the information required by Ind. Code § 8-1-2-23.5(a) is included in the Company's plans for the Sheridan source of supply project. Pet. Ex. 3 at 29-30. In our Docket Entry Request dated August

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[16] See Ind. Code § 8-1-2-23.5(a) which provides: "a public utility that provides water utility service may file petition with the commission to seek approval of a plan to develop a future source of water supply. Any plan submitted must include a completion date by which the public utility will place the future source of supply into service. The completion date may not be later than fifteen (15) years after the date on which the plan is submitted. . . ."

[17] Ind. Code § 8-1-2-23.5(c).

[18] Ind. Code § 8-1-2-23.5(a).

[19] *Id*.

17, 2023, we asked Petitioner to identify where the availability of alternatives to the proposed source of supply is addressed in Attachment MHH-24. In the Company's response to our docket entry request, Petitioner explained that the information could be found in the last paragraph of page 67 for the combined Noblesville and Sheridan Plan. Pet. Ex. 27 at 3. The OUCC took issue with the Sheridan future source of supply project because based on population growth estimates an additional source of supply will not be needed through 2040, fifteen years after the end of the future test year in this Cause.

Having reviewed Attachment MHH-24 and Petitioner's docket entry response, we find Indiana American has not meet the requirement to include the information required under Ind. Code § 8-1-2-23.5(a) for the Sheridan future source of supply. Based on Indiana American's own well analysis, the additional land is not needed. The existing Sheridan wellfield, according to Attachment MHH-14, has a safe yield of 1.15 MGD and a reliable pumping capacity of 1.05 MGD, with base projected maximum day demands for the Sheridan system of 1.07 MGD. Additionally, Indiana American proposes to construct Well No. 7 on land it already owns, which would provide firm capacity of 1.152 MGD. Pub. Ex. 11 at 8, citing Attachment MHH-24 (Part 6), p. 153 of 173. Therefore, Indiana American has existing capacity to meet its projected demand and does need to purchase additional land for water supply.

For these reasons, we find Petitioner's plans to develop future sources of supply as set forth in Attachment MHH-24 do not satisfy the requirements of Ind. Code § 8-1-2-23.5 Accordingly, we reject Petitioner's plans.

c. Lake Station Water Treatment Plant.

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

ii. OUCC. Mr. Parks reviewed Petitioner's acquisition of the Lake Station water system for $20.68 million in 2019. He testified that on January 9, 2020, IDEM inactivated Lake Station's WTP and water system because it was connected to Indiana American's - Northwest system, received treated Lake Michigan water and no longer produced water. Public's. Ex. 9 at 55. IDEM added Lake Station as an inactive point or entry. Pub. Ex. 9, Attachment JTP-17. Mr. Parks recommended removing Lake Station's wells and treatment plant from rate base, because they are not needed from a technical, operational, or economic standpoint. Public's. Ex. 9 at 57. OUCC witness Stull sponsored the Company's adjustment to remove $6,539,385 from rate base for Lake Station's wells and WTP. Pub. Ex. 3, Attachment MAS-1 at 3. Mr. Parks recommended salvaging the pumps, tanks, motors, generator, etc. and returning the building to productive use by selling it to a third party. He stated this will avoid operations and maintenance expenses and capital costs, reduce Indiana American's property taxes and insurance, and reduce future removal costs by transferring the assets to a third party. *Id.* at 57-58. Mr. Parks testified that a lower marginal cost alternative to restarting the Lake Station plant in an emergency is to reopen the existing East Chicago interconnection and purchase water. He doubted Lake Station assets could be brought back on-line quickly but testified the East Chicago emergency connection could be quickly available. *Id.* at 58-59.

Mr. Parks testified the City of Lake Station, due to brown tap water complaints in late 2018 and treatment plant equipment "glitches", began supplying its customers with purchased water from Indiana-American after the City shut down its WTP on February 5, 2019. *Id.* at 52. He reported Petitioner acquired Lake Station's system on October 22, 2019. *Id.* at 51. However, Indiana-American did not rectify the treatment problems nor restart the WTP which has been continually out of service for 4-1/2 years. Through his review of Monthly Reports of Operation, Mr. Parks confirmed the WTP did not produce any finished water under City ownership from February 5, 2019 to October 21, 2019 and has not produced any water under Indiana-American ownership since the October 22, 2019 acquisition. *Id*. at 53 and 55-56.

Mr. Parks reported that Mr. Prine, in Cause No. 45041, testified the WTP would be regularly placed in operation to ensure rapid reliability during peak demand or as emergency supply. However, contrary to Mr. Prine's testimony, Petitioner has not placed the plant in operation to produce any water. *Id*. at 53-54. Mr. Parks testified the OUCC requested the annual power, labor, chemicals, and well cleaning costs. Petitioner tabulated November 2019 to May 2023 electrical costs at approximately $155,000 but provided no other costs, stating plant labor is not tracked and it incurred no chemical or well cleaning costs. Mr. Parks interpreted the absence of these costs to confirm Petitioner has not operated the Lake Station wells and WTP. *Id*. at 54.

Mr. Parks testified the Lake Station WTP is not needed during peak demand days or emergencies. *Id*. at 54. He testified peak demand for Petitioner's Northwest Indiana District was readily supplied by the Borman Park and Ogden Dunes WTPs without operating Lake Station. He reported Indiana-American met demand in the last five years without the Lake Station WTP on-line during several precautionary (voluntary) shutdowns of the Ogden Dunes WTP lasting up to eight days. *Id*. at 56. Mr. Parks testified that on May 8, 2023, Petitioner's personnel indicated to IDEM inspectors that the Lake Station WTP "is an unmanned public drinking water plant" that "Indiana American Water bought . . .for use as an emergency pumping station. Indiana American Water made the decision to discontinue the use of the water softening process and abandoned the tanks in place." *Id.* at 55.

Mr. Parks testified Indiana-American did not mention Lake Station in this Cause, 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, and seeks to continue recovering the full return of and return on the wells and WTP. *Id.* at 58. Mr. Parks testified that in the acquisition case, Cause No. 45041, Mr. Prine addressed the issue of keeping the Lake Station plant in service, stating in rebuttal:

> If the deal is approved, that cost is sunk. Decisions in the future about whether that plant should reasonably be kept in service should be based upon the marginal costs of doing so. In other words, the plant adds value to our system as explained by Mr. Hoffman. Only upon finding of a lower marginal cost alternative should retirement of the plant be evaluated. *Id*. at 58.

Mr. Parks testified that the lowest marginal cost alternative to restarting the Lake Station wells and plant in response to an emergency is to reopen the existing East Chicago interconnection and purchasing water. *Id*. at 58.

iii. <u>INAWC Rebuttal</u>. Indiana American witness Britto responded to Mr. Parks' recommendation that the Lake Station WTP and wells should be removed from service. Ms. Britto explained that contrary to Mr. Parks' testimony, the Lake Station WTP is fully operational and is maintained day-to-day in standby status. Pub. Ex. 17 at 3. 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. *Id*. Ms. Britto further testified that maintenance is performed regularly at the required maintenance intervals and Indiana American personnel operate the wells and pumps on a monthly basis to ensure the plant remains fully operational. *Id*. Ms. Britto also testified that at least one Company employee is on-site at the WTP each day to do visual inspections and confirm there are no issues at the plant, and the WTP maintains its own chemicals inventory and disinfection chemicals are kept on-site in the event treatment is needed. *Id*.

Ms. Britto further explained that the WTP is maintained in standby status in order to minimize the day-to-day operations and maintenance expense associated with operating the plant. *Id*. She testified that the plant is fully operational and stands ready to serve in the event of a chemical spill in Lake Michigan or another emergency requires it to provide emergency capacity to the Northwest Indiana District. *Id*. She further testified the WTP can be transitioned out of standby status to produce potable finished water within 24 hours. *Id*. Ms. Britto testified that this is how Indiana American intended to operate the Lake Station Water Treatment Plant when it acquired the system in Cause No. 45041. *Id*. at 4.

Ms. Britto testified that she fundamentally disagreed with Mr. Parks' contention that the Lake Station WTP is not needed during peak day demands or emergencies. *Id*. at 10-11. While the specifics under which the Lake Station WTP would be needed in an emergency are confidential, Ms. Britto explained in her confidential testimony why the Lake Station WTP is needed in an emergency situation to serve the Northwest District. Pet. Ex. 17-C at 12.

Finally, Ms. Britto testified she disagreed with Mr. Parks 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. Pet. Ex. 17 at 12-13. Ms. Britto explained 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, the Company would need to overcome the East Chicago Free Chlorine water with high quantities of chlorine injected at the connection site of the two systems. *Id*. Ms. Britto explained that Indiana American does not currently have this equipment installed and the system is not equipped to do this. 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. *Id*. 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. *Id*. Ms. Britto further 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. Pet. Ex. 15 at 11-12. Mr. Shimansky testified that he disagreed with Mr. Parks, as the Company has greatly reduced the level of operation and maintenance expense at the plant in order to minimize the impact of purchasing the plant. *Id*. Mr. Shimansky further testified that the ratemaking impact of the purchase price is minimal, and sponsored 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. *Id*.

iv. <u>Discussion and Findings</u>. The main dispute between the parties in this Cause with respect to the Lake Station water treatment plant is whether the Lake Station WTP and wells are currently in operation and used and useful to Indiana American. Despite Indiana American's attempt to conflate the OUCC's arguments with our decision in Cause No. 45041, this is not the same issue as 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.[20]

In this Cause, OUCC witness Parks states the Lake Station water treatment plant has remained out of service since February 5, 2019 and has not produced finished water since eight and a half months before its acquisition by Indiana American. Pet. Ex 9 at 53. Indiana American confirmed that it has never produced water for public consumption from the Lake Station WTP. Pub. Ex. CX-3, DR 56-21. For this reason, Mr. Parks recommends the costs related to the wells and WTP be removed from rate base. *Id*. at 59. In contrast, on rebuttal, Indiana American provided evidence that the Lake Station water treatment plant is currently in operation and being maintained in standby status in the event of an emergency. Pet. Ex. 17 at 3. While 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, she did not dispute that the plant has not produced finished water since its acquisition. *Id*. at 3.

The OUCC also disputed that Indiana American needs the plant to serve the Northwest District in emergency situations. Mr. Parks testified that Indiana American met demand in Northwest Indiana during shutdowns of the Ogden Dunes WTP without the Lake Station plant online. Pub. Ex. 9 at 56. Mr. Parks also testified 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. *Id.* at 58-59. Ms. Britto responded to the OUCC's claims that the Lake Station plant is not needed during an emergency in the confidential portions of her rebuttal testimony and 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. We find Ms. Brittos' description of how Northwest Indiana customers would benefit from Lake Station in an emergency to be impractical and of limited use. Pet. Ex. 17 at 12, lines 8-10. Also, while Ms. Britto explained the difficulties in reopening the East Chicago connection,

[20] Jt. Pet. of Indiana-Am. Water Co., Inc. and the City of Lake Station, Indiana, Cause No. 45041, 2018 WL 4006723, (IURC 8/15/2018) at 32.

these concerns would not be an issue in emergency situations, as noted by the "Ten States" standards. Pub. Ex. No. Ad. Nts. 1, Exhibit B at 3, § 4.4.5.8.

Indiana American witness Shimansky responded to the OUCC's contention that Indiana American did not provide ratemaking options to mitigate the impact of the purchase price in this Cause. Pet. Ex. 15 at 11. He testified the Company's expenses to keep the plant in standby status are minimal so that the plant can be quickly activated, and he calculated the bill impact from having the Lake Station plant ready to be activated in an emergency situation, and testified the bill impact is 12 cents per month. *Id*. at 11-12; Attachment GDS-1R. However, under cross examination, Mr. Shimansky admitted that other costs were not included in his calculation, thus increasing the impact on ratepayers. Tr. (D) at 36-37.

Regarding the dispute between the parties whether the Lake Station WTP and wells are used and useful to Indiana American, the record shows that IDEM recognizes the Lake Station WTP as a plant that is being held in standby status in the event of an emergency, (Pet. Ex. 17, Attachment KCB-1R) and that Indiana American operates and maintains the plant in such a fashion as to allow the plant to be transitioned out of standby status to produce finished water within 24 hours. Pet. Ex. 17 at 3. However, the record also shows that the plant has not produced finished water since its acquisition by Indiana American.

As noted specifically in the confidential portion of Ms. Britto's testimony, we do not believe the Lake Station WTP provides a critical need in the event of an emergency. Indiana American has not yet been required to activate the Lake Station Plant in an emergency situation, and has an easier and less expensive option to obtain water in emergency situations with the connection to East Chicago. Indiana American has purchased water from East Chicago in amounts greater than that produced by the Lake Station WTP. Pub. Ex. CX-2, DR 56-23a. On cross examination, Petitioner's witness, Mr. Shimansky confirmed that based on East Chicago' current Tariff, the cost per million gallons to purchase water from East Chicago would be somewhere between $1,740 based on the lowest rate of $1.74 per 1,000 gallons and $1,820 based on the highest rate of 1.82 per 1,000 gallons. Hrg. Transcript pp. D-39-D-40.

For the reasons set forth herein, we find that the Lake Station WTP and wells are not currently used and useful to Indiana American. The facility has not produced water for public consumption since its acquisition, and Indiana American can obtain water in a more cost-effective manner in emergency situations. As such, we find that the assets are appropriately excluded from rate base in this Cause.

We must also address the OUCC's argument that Indiana American has not proposed ratemaking options to mitigate the cost of the Lake Station WTP and wells in this Cause. The language from our Order 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*."[21] Because we have made the determination that the Lake Station WTP and wells are not used and useful to Indiana American, and as Indiana American has not proposed ratemaking options to mitigate the impact

[21] Cause No. 45041 Order at 25 (emphasis added).

of the cost of the plant, we accept the OUCC's recommendation to remove this facility from rate base.

Finally, it is important for us to address how Indiana American characterizes the OUCC's proposed accounting for the result that it seeks. Indiana American incorrectly argues that the OUCC's position is that the plant should be retired. This is not the OUCC's position. Rather, the OUCC argues that the plant should be removed from rate base, not retired, as it is not used and useful in the provision of water utility service. Therefore, the OUCC's proposed accounting adjustment removing Lake Station utility plant from rate base is appropriate and Mr. Shimansky's rebuttal discussion is not relevant.

d. Lift Station Replacement Projects.

i. INAWC Case-in-Chief. In its case-in-chief, Indiana American proposed Project I10-110002 – Kokomo Wastewater Sheridan 6th Street Lift Station Replacement.[22] 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 in not anticipated in the basins, increased inflow and infiltration ("I&I" or "I/I") present capacity concerns in these areas. INAW has noted overflows downstream 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 Company personnel during regular maintenance and operation.[23]

The Company also proposed Project I10-110003 – Kokomo Wastewater Sheridan Maple Run Lift Station.[24] 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.[25]

ii. OUCC. With respect to the Sheridan 6th Street Lift Station Replacement project, OUCC witness Willoughby recommended the Commission disallow the inclusion in rate base of $1,791,005 as requested by Petitioner. Pub. Ex. 11 at 8. Ms. Willoughby testified Indiana American has not provided sufficient testimony to support replacing the lift station and has not provided adequate justification for the cost estimate. *Id*. Ms. Willoughby testified it is imprudent use of taxpayer funds to install larger equipment to handle I&I without addressing the underlying cause of the I&I. *Id*. at 4. Further, Ms. Willoughby testified Petitioner has not provided documentation to support replacement of the lift station based on its condition, but Petitioner did list rehabilitation as an option on page 3 of Attachment MHH-4 *Id*. at 4-5. Ms.

[22] Attachment MHH-4 at p. 3.

[23] *Id*.

[24] Attachment MHH-4 at p. 5.

[25] *Id*.

Willoughby testified Petitioner has not provided documentation to support the safety concerns Petitioner cited as support for relocating the lift station. *Id*. at 4-5. Ms. Willoughby testified that having a lift station in the right of way is not unusual for a wastewater utility and does not necessarily make the location unsafe. *Id*. at 5. Ms. Willoughby also took issue with Indiana American's cost estimates and testified that Petitioner needed to provide documentation and calculations to support how a cost estimate was assembled. *Id*. at 7.

With respect to the Sheridan Maple Run Lift Station, Ms. Willoughby recommended the Commission deny a portion of the proposed costs for overestimation of labor, contingency, and indirect overhead costs. *Id*. at 13. Ms. Willoughby testified that Indiana American provided conflicting cost estimates for the project, and the cost estimates provided by Petitioner include errors. *Id*. at 12.

iii. <u>INAWC Rebuttal</u>. On rebuttal, Mr. Hobbs responded to Ms. Willoughby's recommendation that the $1,791,005 Petitioner requested for the Sheridan 6th Street Lift Station be disallowed. 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. Pet. Ex. 16 at 64. Mr. Hobbs testified Indiana American has attempted to address the I/I issues in the basins as evidenced by the Company's response to OUCC 09-049 and Supplemental (Attachment MHH-1R), but addressing I/I will not obviate the need for replacement of the lift station. *Id*. at 64-65. With respect to the current capacity concerns at the lift station, Mr. Hobbs testified that equivalent dwelling unit (EDU) estimates coupled with a peaking factor of 4 indicate that the station needs to be sized at a minimum for a peak flow of approximately 370 gpm. *Id*. at 66. Mr. Hobbs testified the 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. *Id*.

With respect to the condition issues, Mr. Hobbs sponsored photos of the lift station as Attachment MHH-10R which show the heavily corroded discharge piping without protective coating, control panel structural supports showing excessive corrosion, surface deteriorating of concrete, access hatches without secondary safety protection, wetwell exhaust vent located between the sidewalk and road, and 230v control panel in poor condition. *Id*. at 65. With respect to the safety issues, Mr. Hobbs testified there is currently no dedicated access for Indiana American employees to safely park and maintain the station, and they are currently using an undeveloped lot at the corner of SR 38/6th and Main Street for wetwell maintenance. *Id*. at 65. Mr. Hobbs explained that if the lot becomes inaccessible in the future, it will require employees to park vehicles and equipment along SR 38, and this could result in safety issues for Indiana American's employees as well as traffic flow disruptions for the public. *Id*.

With respect to the issues Ms. Willoughby raised regarding the cost estimates Indiana American provided for the Sheridan Maple Run Lift Station, Mr. Hobbs explained that the Company provided cost estimates from both MHH-4 and its SCEP for the lift station project and these estimates were prepared at different times, and this is why the cost estimates the Company provided for the project differ. *Id*. at 71. Further, with respect to the errors Ms. Willoughby

identified, Mr. Hobbs explained that the cost estimates Indiana American provided are just that, estimates. *Id*. at 72. Mr. Hobbs explained that as these costs mature through the implementation process, the cost 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. *Id*. Mr. Hobbs explained that the issues Ms. Willoughby raised regarding the cost estimates are generally not relevant, because it is the actual costs of the project that will be reflected in rate base, not the estimate from the SCEP or Attachment MHH-4. *Id*. at 73.

iv. <u>Discussion and Findings</u>. With respect to the 6th Lift Station, the OUCC argues the capacity issues at the lift station are the result of I/I in the system, and Indiana American should be required to address the underlying I/I issue instead of installing larger equipment to handle the I/I. Pub. Ex. 11 at 4. Indiana American argues it has attempted to address I/I in the system but addressing I/I alone will not obviate the need for replacement of the lift station because the capacity issues are not the only reason the lift station needs replaced. Pet. Ex. 16 at 65. However, based on response to their response to DR 09-049, supplemental response b, Indiana American made the determination to replace the lift station based on the safety and security of its employees and the public. Only once the decision to replace was made, did Indiana American propose to increase the capacity of the lift station. Pub. Ex. 11, Attachment KW-02 at 3-4. While Indiana American also states in the supplemental DR response, based on their preliminary investigation, that the lift station is undersized, this contradicts its earlier response in the same DR that there have been no documented overflows at the lift station during the last three years, indicating that the lift station is not undersized. *Id*. at 2. Additionally, the calculation to determine the peak flow of 370 gpm was only done in Mr. Hobbs' rebuttal testimony, after the determination was made to replace the lift station, and was not provided earlier in response to discovery.

Mr. Hobbs sponsored Attachment MHH-1R (Indiana American's responses to OUCC 09-049 Supplemental) which shows Indiana American's attempt to address specific I/I issues associated with infrastructure upstream of the 6th Street Lift Station was limited to a manhole repair and grouting. Additionally, Indiana American did not complete its hydraulic model of the Sheridan collection system, nor was Indiana American able to provide workpapers supporting the cost determination for lift station. Pet. Ex. 16, Attachment MHH-1R, pages 3-4 of 14.

Based on the uncertainty in the determination of the capacity of the lift station, the and the lack of cost support, we find that replacement of the 6th Street Lift Station is not necessary at this time. Once the hydraulic model is complete, the proper capacity of the lift station can be determined. Additionally, Indiana American should develop a detailed cost estimate with supporting documentation, especially once the proper capacity is determined. For those reasons, we find the 6th Street Lift Station project should be denied.

With respect to the Maple Run Street Lift Station, the OUCC took issue with the Petitioner including a higher amount for the project in rates than Indiana American estimates it will cost. While it is true the actual cost of the project will be reflected in rate base, Indiana American is requesting customers to pay rates based on old estimates that were only partially updated by the Petitioner before filing this case. Pub. Ex. 11 at 12. We understand project estimates change over time, but rates should be based on the best available information. By only updating a portion of the costs for this project, Indiana American is overstating the cost of this

project leading to higher rates and possible over recovery in rates. For this reason, we deny the cost overestimations as reflected in Ms. Willoughby's testimony for the Maple Run Street Lift Station project.

e. <u>BT SOP 98-01</u>.

i. <u>INAWC Case-in-Chief</u>. 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 Utility Plant in Service, as well as $6,619,332 of accumulated depreciation associated with the BT SOP 98-01 project. Pet. Ex. 14 at 12-13.

ii. <u>OUCC</u>. OUCC witness Margaret Stull explained that the "BT Project SOP 98-01" costs Indiana American proposes to include in rate base in this Cause, refers to some expenditures associated with Indiana American's Business Transformation ("BT") project, which included implementation of American Water's customized SAP software system, which was added to Indiana American's rate base in Cause No. 44450. Ms. Stull explained that SOP stands for "Statement of Position" issued by the American Institute of Certified Public Accountants, which is considered to be one of the sources of generally accepted accounting principles. Public's Exhibit No. 3 Page 12. Ms. Stull noted that SOP 98-01 provides guidance on accounting for the costs of computer software developed or obtained for internal use, and, Specifically, this SOP requires that training and data conversion costs, as well as costs incurred in a project's preliminary stage, should be expensed as incurred. Ms. Stull pointed out that, nonetheless, in Cause Nos. 44450 and 45142 Indiana American sought to capitalize these costs for ratemaking purposes to be included in rate base, which the OUCC opposed, though it did not object to the recovery of these costs over time through amortization. Ms. Stull added that in a settlement in that cause, those costs were excluded from rate base but amortized over thirteen (13) years, which was the then current 7.69% depreciation rate for computer software. She testified this effectively allowed Indiana American a "return of" these expenditures but not a "return on" them.

Ms. Stull clarified that the OUCC does not in this case oppose Indiana American's continued ability to a return *of* the expenditures as Indiana American was authorized to do in Cause Nos. 44450 and 45142. But she Indiana American should not be authorized to earn a return *on* the expenditures because the SOP 98-01 costs do not qualify to be included in rate base as they are not construction costs used to produce plant that is used and useful in the provision of utility service under I.C. § 8-1-2-6. She stated Indiana American should not earn a return on these expenditures. Public's Exhibit No. 3 Page 13. Ms. Stull noted Indiana American did not explain in this rate case why it believes this subcategory of BT Project costs should be included in rate base, the only discussion being Mr. Shimansky's testimony merely stating where in the workpapers the entry could be found.[26] Ms. Stull said Mr. Shimansky's testimony neither supported including these costs in rate base nor explained why the treatment of these costs

[26] Mr. Shimansky merely testified "The accumulated amortization balances for BT SOP 98-01, Deferred Depreciation, and Post In-Service AFUDC are included on lines 11 – 13, the supporting schedules are Schedule RB3, RB4 and RB5, respectively. The amortization schedules are continued through April 2025." (Shimansky Direct at page 20, lines 12 – 15.)

should deviate from the Commission's findings made in Cause Nos. 44059, 44450 and 45142. Ms. Stull explained that none of those orders authorized Indiana American to capitalize its BT SOP 98-01 costs and include them in rate base. Ms. Stull reiterated Indiana American was only authorized to amortize these costs as an expense to receive a return "of" not earn a return "on." Ms. Stull recommended Indiana American's request to be denied.

iii. <u>INAWC Rebuttal</u>. OUCC witness Shimansky testified he disagreed with Ms. Stull's recommendation that the BT SOP 98-01 costs be disallowed from rate base in this Cause. Pet. Ex. 15 at 10-11. 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 he disagreed and explained that capital dollars spent do not have to be related to "construction" in order 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 testified that the statute that Ms. Stull cites (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 asserted 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. *Id*. He argued that the OUCC is not opposed to the collection of the BT SOP 98-01 asset, in other the words, the return "of" the asset, and if the asset is eligible to be collected in rates and the asset is doing work for the customers' benefit, it should also be included in rate base and be compensated with a return "on" as well. *Id*.

Mr. Shimansky characterized Ms. Stull's testimony to argue that the costs should not be included in rate base in this Cause because they were not included in prior cases, Mr. Shimansky testified he also disagreed with this contention. *Id*. Mr. Shimansky testified the treatment of the BT SOP 98-01 costs in Indiana American's prior rate case was pursuant to a Settlement Agreement for the purpose of reaching a resolution in that case, and the costs were removed "for the purposes of settlement" and "Indiana American agree[d] not to include them in rate base when calculating Step 1 and Step 2 rates."[27] Mr. Shimansky explained the Company did not agree to remove it permanently from rate base nor did it agree not to include it in the next rate case for inclusion in the calculation of future rates. Mr. Shimansky testified Indiana American did not accept Ms. Stull's arguments in arriving at the stipulation in Cause No. 45142, and it does not accept the arguments in this case for excluding the asset from rate base. *Id*.

iv. <u>Discussion and Findings</u>. In Cause No. 44059, Indiana American sought an order approving expenditures pursuant to Ind. Code § 8-1-2-23 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 OUCC, the Industrial Group and Indiana American agreed the Commission should issue an order authorizing the deferral for future recovery of an estimated $6,800,000 of costs associated with Business Transformation that would be recorded as expense pursuant to Generally Accepted Accounting Principles, and specifically Statement of Position ("SOP") 98-01. It was agreed the deferred costs should be amortized over ten (10) years. In a Settlement in Cause No. 44450, the Settling Parties agreed that all BT-related assets (including plant in service, deferred depreciation, post-in-

[27] Cause No. 45142 Order, p. 10.

service AFUDC, the BT CPS, and BT SOP 98-01 costs) should be depreciated or amortized, as the case may be, over 13 years and not the 10-year amortization rate approved in Cause No. 44059.

The approved settlement in Cause No. 44059 established that the "question of recovery of a *return on* the unamortized balance is reserved for a future rate case." (Order, Cause No. 44059 p. 9, Stipulation and Settlement, p. 3. Emphasis added.) More precisely, the Settlement Agreement in Cause No. 44059 established that future rate case was to be the first general rate case after Petitioner had completed the Business Transformation Project. Following a provision addressing Allowance for Funds Used During Construction in Cause No. 44230, the settlement agreement provided what BT costs were to be in rate base was an issue for the *first* general rate case after implementation:

> All other issues related to Business Transformation shall be reserved for the <u>first general rate case</u> filed by Indiana American after Business Transformation is placed in-service[, noting t]he list of such issues includes but is not necessarily limited to Business Transformation costs, cost recovery, prudence review, cost allocation, and inclusion of Business Transformation in rate base."

Settlement Agreement, p. 3, Final Order, Cause No. 44059) (emphasis added.).

Petitioner's witness in Cause No. 44059, Mr. Gregory Roach testified that "the Parties have stipulated that all other issues raised in this Cause, including, without limitation, prudence, cost allocation, and inclusion in rate base, will be reserved for the <u>first general rate case</u> filed by Indiana-American after Business Transformation is placed in-service." Cause No. 44059, Order, p. 9.

That first general rate case after the implementation of the BT Project was Cause No. 44450, a case that was ultimately settled and more importantly resulted in a final order that did not establish that the Business Transformation expenditures now at issue in this case should be added to Indiana American's Rate Base. Since Cause No. 44450, Indiana American also brought forth Cause No. 45142, So that there have been two intervening rate cases between this Cause and the Commission's order in Cause No. 44059. Arguably, pursuant to the agreement in Cause No. 44059, which specified the issue of what could be included in rate base was for the next general rate case after implementation Cause No. 44450 was Indiana one and only opportunity to establish these Business Transportation expenses should be included in rate base. The OUCC's Ms. Stull did not argue that position in her testimony, though Petitioner ascribed to her something like that argument in its rebuttal case.[28]

[28] Mr. Shimansky indicates in his testimony and Petitioner indicates in its proposed order that Ms. Stull argued the costs should not be included in rate base in this Cause **simply** because they were not included in prior cases. In fact, While Ms. Stull pointed out that none of orders in Cause Nos. 44059, 44450 and 45142.authorized Indiana American to capitalize its BT SOP 98-01 costs and include them in rate base, she more precisely focused on a lack of evidence to support the inclusion of the cost in rate base. She noted that "Mr. Shimansky's testimony neither supported including these costs in rate base nor explained why the treatment of these costs should deviate from the Commission's findings made in Cause Nos. 44059, 44450 and 45142."

But we need not address whether Indiana American is precluded by the Settlement Agreement approved in Cause No. 44059 from reasserting at this late juncture that its unamortized BT SOP 98-1 costs should be added to its rate base. Whether Cause No. 45540 was Indiana American's only opportunity to do put these costs in rate base is neither here nor there. For purposes of the discussion that follows, we will assume Indiana American was not precluded by the Settlement Agreement from making a case that its unamortized BT expense should be added to rate base. We find for the reasons stated below that Indiana American's request should be denied because Indiana American's case did not support converting the unamortized portion of its BT SOP 98-1 expenses into rate base.

First, we note that Indiana American did not explain in its case why it believes this subcategory of BT Project costs should be included in rate base, the only discussion being Mr. Shimansky's testimony merely stating where in the workpapers the entry could be found.[29] In the two preceding rate cases, Indiana American continued to maintain the status quo of these expenses not being included in rate base and receiving a return of those expenditures through amortization. As such, if Indiana American proposed to change the status quo in this case, it had the obligation to submit evidence in its case-in-chief to support including the unamortized portion of the expense into rate base. It did not do so. We do not agree under the circumstance of this issue that it is appropriate for Petitioner to place the cost in its accounting schedules with any testimonial support. Petitioner has the burden of proving what should go into its rate base. It is not properly the burden of the consumer parties to make a prima facie case why this unsupported change should not be authorized.

Second, even if it were proper for Petitioner to make its prima facie case in its rebuttal case, Petitioner has not done so. In this regard, Petitioner's testimony is general and does not explain why the guidance under SOP 98-1 should not be considered to apply. In response to Ms. Stull's argument about IC 8-1-2-6, without specifics Mr. Shimansky simply asserted the expenses at issue were critical to bringing the Business Transformation investment to its current state of efficiency. While Mr. Shimansky testified that "capital dollars," or any asset, represents money spent today that creates a benefit for future periods, he did not counter Ms. Stull's testimony that under SOP 98-1 these costs are not capital costs, but they are to be expensed when incurred.

Indiana American argued in its proposed order that our final order in Cause No. 45675[30] dispenses with the OUCC's position with respect to these costs. It does not. Importantly, the issue in that case was the application of the pre-approval statute IC 8-1-2-23, and whether Aqua Indiana's SIP software costs were appropriate for pre-approval under Ind. Code 8-1-2-23 because the expenditures addressed in Ind. Code § 8-1-2-23 are for an "extension, construction, addition or improvement of [a public utility's] plant and equipment. While we disagreed with the OUCC position on whether relief could be afforded under that statute and approved Petitioner's request for preapproval of the $2,517,593 in allocated SIP costs, we did not in our discussion and findings dispense with the arguments raised by the OUCC on this matter. While we noted in our

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[29] Mr. Shimansky merely testified "The accumulated amortization balances for BT SOP 98-01, Deferred Depreciation, and Post In-Service AFUDC are included on lines 11 – 13, the supporting schedules are Schedule RB3, RB4 and RB5, respectively. The amortization schedules are continued through April 2025." (Shimansky Direct at page 20, lines 12 – 15.)

[30] *Aqua Indiana, Inc.*, Cause No. 45675, 2023 WL 371882, (IURC 1/18/2023).

summary of Margaret Stull's testimony in that case about rules under GAAP governing capitalization of software costs, the terms "GAAP," "generally accepted accounting principles," and "SOP 98-1" appear nowhere in our discussions and findings. Consequently, we reject Indiana American's proposal that we construe our final order in Cause No. 45675 as making broad precedent setting pronouncements with respect to GAAP's SOP 98-1. Finally, our determination on what should be preapproved for rate base purposes in that case was based on the facts submitted into evidence in that case. Our determination in that case does not relieve Petitioner in this case of proving why its unamortized portion of BT SOP 98-1 expenses should be converted to rate base.

Petitioner also argued that because the OUCC is not opposed to the collection of the BT SOP 98-01 "asset" through amortization (i.e., a return "of") the expenditure, it should also be included in rate base and be compensated with a return "on" as well. *Id*. This argument includes several faulty assumptions. First, by using the word "asset," in its argument, Petitioner has engaged in a tautology. The issue is not whether an "asset" qualifies under GAAP's SOP 98-1 but whether an expense qualifies. Second, if expenditure creates a benefit for customers, that does not necessarily make it a rate base item. For instance, employing individuals to interact with and assist customers may be a benefit to customers, but the cost of doing so is clearly and O&M expense. To that end, expending money to train employees to use the Company's software should not be considered creating used and useful plant. Last, we recall that the underlying amortization of the expensed BT costs was authorized by an order approving a Settlement Agreement. Settlements are typically not to be construed as an admission by any party, and the Stipulation and Settlement approved by the Commission in its final order in Cause No. 44059 included just such a stipulation. For the foregoing reasons, we reject this argument.

We find that Petitioner has not made a case adequate to support transferring its unamortized BT expense into rate base.

f. <u>Acquisition Related Costs</u>.

i. <u>OUCC.</u> Ms. Stull noted that INAWC has been authorized to include in its rate base legal fees incurred by the utility to apply for relief under IC 8-1-30.3-1 et al related to the acquisition of water and wastewater utilities. Ms. Stull expressed concern with Indiana American's practice of embedding into rate base legal expenses based on fixed fee agreements. Ms. Stull asserted that Indiana American has not shown that the legal expenses associated with those fixed fee arrangements are reasonable. Public's Exhibit No. 3, Page 54.

Ms. Stull explained in Cause No. 45461, the Commission found that such fees could properly be included in rate base as "incidental expenses and other costs of acquisition." under IC 8-1-30.3. But the Commission also found that such expenses must be reasonable, and the next rate case was the appropriate time to challenge the reasonableness of such costs. Tshe noted the Commission found in that case "when Indiana American files its next general rate case, the amount actually recorded on its books and records pursuant to the authority granted here will be subject to review for reasonableness." (Order in Cause No. 45461, June 2, 2021, 9 p. 13) She noted the Commission also expressed an expectation about the transparency of legal expenses and other costs of acquisition finding that Indiana American should do a better job of supporting that expense and provide a more accurate and detailed estimate of incidental expenses and other

costs of acquisition in their cases-in-chief. It found that in future cases, Indiana American should provide a breakout of the expenses (e.g., legal expenses, appraisal expenses, environmental expenses, and expenses charged to any affiliate such as American Water Works Service Company, Inc.). For each category of expense, Indiana American should provide the current actual expenses and estimated future expenses. Order in Cause No. 45461, June 2, 2021, pp. 13-14. Ms. Stull noted that later in Cause No. 45550 involving Petitioner's acquisition of the Town of Lowell's system, the Commission again found that the next general rate case was the time to evaluate the reasonableness of incidental expenses and other costs of acquisition. including a breakout of the expenses (e.g., legal expenses, appraisal expenses, environmental expenses, and expenses charged to any affiliate such as American Water Works Service Company, Inc.), including current actual expenses and estimated 6 future expenses. Public's Exhibit No. 3 Pages 54 and 55.

Ms. Stull discussed what amount of legal expense Petitioner has proposed to rate base for each of its acquisitions in this case. She explained that Petitioner did not in its case identify the amount of legal expense for each of these acquisitions but based on Petitioner's response to discovery (OUCC Attachment MAS-14), Petitioner has requested incidental expenses for each of the following acquisitions: 1) Lake Station - $232,773 - Cause No. 450410) of which $228,606 are legal expense; 2) Riley Wastewater - $172,640 (Cause No. 45290) all of which are legal expense; 3) River's Edge - $131,292 (Cause No. 45461) of which $102,006 is legal; and 4) Town of Lowell - $156,336.66 (Cause No. 45550) of which $120,000 2 is legal. Public's Exhibit No. 3, Page 56.

Ms. Stull noted that some of the acquisition cases involved fixed fee arrangements in which INAWC agreed to pay Barnes and Thornburg a predetermined amount for each of four phases of the case: (1) Case Assessment/Preliminary Investigation; (2) Discovery; (3) Rebuttal & Hearing/Hearing Preparation; and (4) Post Hearing. Ms. Stull pointed out that Indiana American has a lack of incentive to control its incidental expenses and other costs of acquisition. She added that Indiana American acknowledged the only financial incentive it has to procure lower incidental expenses is the risk of disapproval by the Commission. In other words, the risk is that Indiana American will incur an expense that the Commission does not allow it to include in rate base. (OUCC Attachment MAS-15) Public's Exhibit No. 3, Page 56. Ms. Stull asserted Indiana American is not adequately incented to control its acquisition costs because Indiana American is permitted to include its legal expense in rate base, where it will earn a return as if it is an investment. Ms. Stull testified that, Indiana American is not financially incented to manage these costs or engage in settlement talks and thereby avoid the costs of a contested final hearing.

Ms. Stull asserted acquisition cases have become less controversial and involved, noting that the last two acquisition cases filed by Indiana American under IC 8-1-30.3 had limited discovery, no filing of testimony by the OUCC, no cross-examination by the OUCC, and agreement on the form of the final order.

Ms. Stull explained 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. She explained that more than four sets of discovery are outside the scope of services as are depositions, appeals, and petitions for reconsideration. Ms. Stull indicated in her experience, a case involving any degree

of real controversy typically will well exceed four discovery sets. As such, she questioned whether these fixed fee arrangements protect the customers from having higher legal costs in rate base. (See OUCC Attachment MAS-22.)

Ms. Stull explained that Indiana American did not justify the use of a fixed fee arrangement. She noted that Indiana American was asked in this case to explain and provide what it relied on to determine whether the flat fee arrangement was appropriate (OUCC 22 Attachment MAS-16) She noted Indiana American's response included no information and its explanation consisted only of the statement "Flat fee negotiations were performed by counsel for INAWC and were based on the experience of counsel, the experience of INAWC with the OUCC and Intervenors, and the legal market." Public's Exhibit No. 3 Page 57. Ms. Stull asserted that vague response does not provide assurances that the fixed fee, on which the customers will be paying a return on and return of the fee, is reasonable. Ms. Stull suggested Indiana American is not monitoring these fixed fee arrangements to determine if they are a good deal for ratepayers. She noted Indiana American was asked to explain what the legal expense would have been for each of its acquisitions without the fixed fee arrangement and show its calculations and state its assumptions, and Indiana American responded by stating simply that "INAW has not performed calculations but assumes competent counsel avoids the expense of fixing incompetent counsel." 15 (OUCC Attachment MAS-17.) She noted Indiana American acknowledged it does track the actual number of hours expended by its counsel under fixed fee arrangements. (OUCC Attachment MAS-18). She noted that the terms of Fixed Fee Arrangement are negotiated and asserted there is no reason such arrangements could not require Counsel to keep track of time spent on the various matters so that Indiana American could evaluate whether continuing such fixed fee arrangements is in the best interest of its customers who ultimately pay those fees through a higher return and higher depreciation expense. Public's Exhibit No. 3 Page 58. Ms. Stull said that based on the very limited information in Petitioner's case-in-chief and in its responses to discovery in this case, she was unable to form an opinion as to whether the legal fees portion of the incidental expenses and other costs of acquisition to be included in rate base are in fact reasonable. She asserted that if Petitioner has the burden of proof in this case, it has not met it. Ms. Stull testified that if evaluating the reasonableness of such costs is an issue for the next general rate case, when actual costs will already have been incurred, Indiana American should present its support for the reasonableness of those costs in case-in-chief. Secondly, she recommended that if Indiana American is going to persist in securing these legal services with fixed fee arrangements, it should require its counsel to keep track and communicate hours expended so Indiana American's management can evaluate whether it should continue to enter into such agreements and so the Public may evaluate whether the costs incurred are reasonable.

ii. INAWC Rebuttal. INAWC witness Shimansky responded to Ms. Stull's concerns and recommendations with respect to legal fees for acquisitions. He testified that Ms. Stull has not established that she possesses any educational or professional background or experience in legal oversight and negotiation. Pet. Ex. 15 at 36. Mr. Shimansky stated that "hours" are not the only factor in considering the value of legal representation and Ms. Stull gives no authority for suggesting that is the only way to know if the legal representation is valuable. When asked by Indiana American for information from the OUCC on how it establishes its own 'value', including number of hours and the value of each hour worked, the OUCC objected and provided only a response that "OUCC staff does not record their time in the manner in which the question is phrased, which is more closely aligned with a law firm

"billing" concept." *Id*. Despite the OUCC's assertions in discovery that it does not seek rate recovery for its efforts, Mr. Shimansky pointed out that the OUCC is funded through the collection of fees paid by utilities, which fees are recovered (as in this case) through rates charged to ratepayers. *Id*. at 36-37. He stated it is hard to reconcile the inherent inconsistency in the OUCC's position, asserting that private lawyers be treated differently than ratepayer funded state lawyers who have significant impact on the required expenditure of time from company lawyers. *Id*. at 37.

Mr. Shimansky offered testimony illustrating 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 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 several other acquisition cases. *Id*. at 37; Attachment GDS-6R. 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. *Id*. at 37.

iii. Discussion and Findings. Through our prior acquisition orders, we have made it clear that the reasonableness of outside counsel legal fees incurred by Indiana American in its acquisition cases under IC 8-1-30.3 is an issue to be addressed in the next rate case. These pronouncements came in response to concerns expressed by the OUCC to a lack of transparency and support for the fixed fee arrangements for legal fees Indiana American proposed as a basis for its favorable ratemaking treatment in acquisition cases. Yet in this rate case, Indiana American provided no evidence in its case-in-chief to support the reasonableness of its rate base additions based on the flat fee arrangements in its acquisition cases. Moreover, in its response to discovery from the OUCC on this issue, Indiana American provided nothing that could reasonably assure the OUCC that the fixed fee arrangements were reasonable or allow the OUCC to establish with evidence that they may result in higher legal fees at greater cost to the ratepayers.

Petitioner proposed we find that "While Ms. Stull proposes that the Company effectively change the terms of its arrangement with outside counsel in future cases, the OUCC offers no evidence or argument that such changes would produce lower outside counsel fees." This is a specious argument. The OUCC's recommendation is that we require Indiana American to acquire and present the information that will allow the OUCC and this Commission to make that evaluation. This recommendation is in response to Indiana American's inability through its case and through responses to discovery to provide meaningful support to show that its fixed fee arrangements are reasonable and that they do not result in higher rate base than would occur through standard hourly billing.

While we have found that legal fees prosecuting cases under IC 8-1-30.3-5 may properly be included in rate base as part of the cost differential, we also found such costs must be reasonable, and the next rate after the actual costs have been incurred is the time to address the reasonableness of the cost. It is Petitioner's burden in a rate case where this issue must be addressed to provide evidence to support such a conclusion. It is not the OUCC's burden to prove that the legal expenses associated with prosecuting relief under IC 8-1-30.3-5 was not reasonable.

Petitioner argued "the OUCC's position on this issue has not been shown to be based upon anything more than mere supposition." And the "OUCC has provided no evidence that a fixed fee arrangement like that which Indiana American has negotiated with its outside counsel produces an unreasonable fee or that some other arrangement would actually produce a lower total fee." The foregoing statement suggests Indiana American has no burden to support the reasonableness of its rate base additions. Moreover, it underscores the lack of meaningful support Petitioner provided in response to discovery. For instance, in OUCC DR 48-06(d), Petitioner was asked to "explain and provide what Indiana American relied upon to determine whether the flat fee agreement was appropriate." Petitioner responded, "Flat fee negotiations were performed by counsel for INAWC and were based on the experience of counsel, the experience of INAWC with the OUCC and Intervenors, and the legal market." This response suggests no careful study or evaluative analysis was performed.

Notwithstanding the lack of support for the reasonableness of the expense through discovery or its case, the OUCC has only asked us to require Indiana American to require its counsel under a fixed fee arrangement to document the number of hours its outside counsel expends on these matters so that both Petitioner and the OUCC may evaluate whether the fixed fee arrangements are reasonable or whether they have the effect of unnecessarily increasing acquisition costs. The effect of higher than necessary acquisition costs is that Indiana American will have a larger rate base value on which to base its rates. Allowing the Commission and the OUCC to evaluate whether a fixed fee arrangement results in lower or higher rate base than a standard hourly agreement is reasonable. Importantly, it also allows Indiana American to make its own comparison and determine which method of paying for counsel should tend to lower its rate based acquisition costs and thereby reduce the risk of legal complications. (The OUCC asked Indiana American to describe every financial incentive to avoid or reduce legal expense associated with incidental expenses to be included in a cost differential under I.C. § 8-1-30.3-1. Although it purported to answer the question, Petitioner did not truly identify any financial incentive to reduce the legal expense it incurs in acquisition cases.[31])

Petitioner argued that the OUCC position on this issue has not been shown to be based upon anything more than mere supposition and stated the OUCC has provided no evidence that a fixed fee arrangement like that which Indiana American has negotiated with its outside counsel produces an unreasonable fee or that some other arrangement would actually produce a lower total fee. Petitioner's proposed order, pp. 37-38. This argument does not fairly or accurately characterize the OUCC's position. While it questions whether a fixed fee arrangement is reasonable, the OUCC has not asked us to find any particular fixed fee arrangement was unreasonable. Rather it has asked us to require a means of determining whether it is reasonable. Petitioner's own rebuttal evidence suggests fixed fee arrangements may result in higher costs than a simple hourly rate. The evidence of record reflects that in one case INAWC itself recognized that the rates charged under a fixed fee arrangement with outside counsel required

[31] Petitioner responded that the "incentive" is efficiency in reducing risk of legal complications. Merriam-Webster defines "incentive" as something that incites or has a tendency to incite to determination or action. In common practice, fewer legal complications generally means a reduced legal expense, so INAW has incentive to receive competent legal counsel to avoid such complications. In addition, the structure of the fixed fee arrangements is such as to incent all parties (including the OUCC and any intervenors) to reduce legal expense by eliminating issues that have previously been decided and issues that do not have a material effect. OUCC Attachment MAS-14.

mitigation. *See* Pet. Ex. 15 at 37-38. Whether that mitigation was sufficient can only be a matter of speculation or supposition.

For the foregoing reasons, we agree that is a reasonable and modest step for Indiana American to require its outside counsel to document the number of hours it spends providing legal services through a fixed fee or flat fee arrangement and so order. If Petitioner intends to rely on a fixed fee arrangement in any future acquisition cases under IC 8-1-30.3-5, it must require counsel to track as incurred the hours expended on the matter so that Indiana American, the OUCC and this Commission can form an opinion as to whether a fixed fee arrangement truly benefits Indiana American's customers as Petitioner has suggested.

B. <u>Depreciation</u>.

i. <u>INAWC Case in Chief</u>. Mr. Kennedy presented full and comprehensive depreciation studies of the water and wastewater plant in service of the Company 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. Pet. Ex. 12 at 18. 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 deprecation 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%. *Id.* at 6. 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. *Id*. The average service life was shortened for 13 accounts and was lengthened for 16 accounts, based on the detailed analysis presented in Mr. Kenney's report. *Id.* at 8. 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. *Id. at 9.*

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, 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. *Id.* at 11. A more negative net salvage requirement was estimated for 3 accounts. *Id.* at 12.

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. *Id.* 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 throughout North America for there to be a shortening in other asset class, due in part to the quickening pace of technological change. *Id.* at 13. For example, the pace of technological

change in metering assets has resulted in the life of metering classes to be shortened industry wide. *Id.*

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. *Id.* at 15-16. 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. *Id.* at 16.

ii. <u>OUCC</u>. OUCC witness Garrett recommended several adjustments to the Company's proposed depreciation rates based on different service life estimates for several of the Company's water transmission and distribution accounts. His proposed depreciation rate adjustments would result in a $6.9 million decrease to the Company's proposed total annual depreciation accrual of $69.3 million. Pub. Ex. 7 at 3. 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 ("OLT") curve through a combination of visual and mathematical curve-fitting techniques, as well as professional judgment. *Id.* at 9. 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. *Id.* at 9-10. Mr. Garrett stated that for each of the accounts to which he proposed adjustments, the Company's proposed average service life, as estimated through an Iowa curve, is too short to provide the most reasonable mortality characteristics of the account. *Id.* at 11. He asserts 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 the Company's plant data, in addition to applying judgment to the analysis. *Id.* 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.

iii. <u>INAWC Rebuttal</u>. On 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 provide critical information related to the reasons for past retirements and the expected future causes of retirement. Pet. Ex. 22 at 3. 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. *Id.*

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. *Id.* at 6-12.

iv. Discussion and Findings. Ind. Code § 8-1-2-19(b) and (c) place an affirmative obligation on the Commission:

> (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). This type of analysis is noted by Mr. Garrett. In noting that the mathematically best-fitting curve is not always selected, he stated; "Mathematical fitting is an important part of the curve-fitting process because it promotes objective, unbiased results. While mathematical curve-fitting is important, however, it may not always yield the optimum result." Pub. Ex. 7 at 9. Mr. Garrett proposed modifications to several accounts, noting that his analysis provides a better fit to the full and truncated historical data for each account. Additionally, for Account 334.100 – Meters, Account 334.110 – Meters – Bronze Case, and Account 334.130 – Meters – Other, it is Mr. Kennedy's understanding that regulations require the testing of meters after 15 years, which is inconsistent with Commission rule 160 TAC 6-1-10(b), which requires testing of 5/8 inch meters every 10 years, and more frequent testing for larger meters. Mr. Kennedy states it is "more cost effective to simply remove the meter at the end of the testing period rather the [sic] remove the meter, test it and then reinstall it following the testing," and this "has a significant life shortening impact on the assets within this account." Pet. ex. 22 at 9. However, when examining the OLT curves in Mr. Garrett's testimony for these accounts, there is no significant change in the curves after 10 years. We agree with OUCC witness Mr. Garrett's positions regarding his proposed service life adjustments on these accounts. The Iowa curves selected by Mr. Garrett are based on objective analysis, and the evidence shows that the Iowa curves he selected for these accounts result in better mathematical fits to the historical retirement patters in these accounts. Therefore, we find that the proposed depreciation rates should be modified by the Company for financial reporting purposes.

C. Quantification of Original Cost Rate Base.

Based upon our findings above and our approval of the OUCC's proposed depreciation accrual rates, we find that Petitioner's net original cost rate base projected is as follows (*see* OUCC Schedules 8TC, 8W, and 8S)

Table 1: Step 1 Rate Base as of July 31, 2023

	Total	Water	Wastewater
Utility Plant:			
Plant in service	############	############	##########
BT SOP 98-01	-	-	-
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:	2,500,371,685	2,479,636,588	20,735,097
Accumulated Depreciation:			
Plant in service	618,069,270	615,681,923	2,387,347
BT SOP 98-01	-	-	-
Deferred depreciation	4,791,904	4,770,447	21,457
Post-in-service AFUDC	4,206,404	4,197,650	8,754
Total Accum. Depreciation	627,067,578	624,650,020	2,417,558
Net Utility Plant:	############	############	##########
Deductions:			
Contributions in aid of construction	210,713,115	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:	273,289,960	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	-
Material & Supplies	2,241,938	2,227,653	14,285
Total Additions:	6,614,951	6,592,142	22,809
Total Rate Base	############	############	##########

Table 2: Step 2 Rate Base as of April 30, 2024

	Total	Water	Wastewater
Utility Plant:			
Plant in service	$ 2,595,807,004	$ 2,573,205,819	$ 22,601,185
BT SOP 98-01	-	-	-
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:	2,611,255,584	2,588,606,931	22,648,653
Accumulated Depreciation:			
Plant in service	654,483,978	651,513,735	2,970,243
BT SOP 98-01	-	-	-
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	663,965,845	660,963,027	3,002,818
Net Utility Plant:	$ 1,947,289,739	$ 1,927,643,904	$ 19,645,835
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	-
Material & Supplies	2,241,938	2,227,653	14,285
Total Additions:	6,537,080	6,515,038	22,042
Total Rate Base	$ 1,672,429,430	$ 1,653,525,072	$ 18,904,358

Table 3: <u>Step 3 Rate Base as of April 30, 2025</u>

	Total	Water	Wastewater
Utility Plant:			
Plant in service	$2,768,745,303	$2,745,916,360	$22,828,943
BT SOP 98-01	-	-	-
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:	2,784,193,883	2,761,317,472	22,876,411
Accumulated Depreciation:			
Plant in service	713,048,559	709,102,905	3,945,654
BT SOP 98-01	-	-	-
Deferred depreciation	5,515,957	5,490,377	25,580
Post-in-service AFUDC	4,600,671	4,590,524	10,147
Total Accum. Depreciation	723,165,186	719,183,806	3,981,381
Net Utility Plant:	$2,061,028,697	$2,042,133,666	$18,895,030
Deductions:			
Contributions in aid of construction	213,576,983	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:	292,463,673	291,710,380	753,294
Additions:			
Acquisition Adjustment (net)	6,734	-	6,734
SEI Deferred Depr, Property Taxes & PISCC	4,150,345	4,150,345	-
Material & Supplies	2,241,938	2,227,653	14,285
Total Additions:	6,399,017	6,377,998	21,019
Total Rate Base	$1,774,964,040	$1,756,801,284	$18,162,756

D. Fair Value of INAWC's Rate Base.

i. <u>INAWC Case-in-Chief</u>. 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 (the "IURC Methodology"). The IURC Methodology begins with the Fair Value Rate Base ("FVRB") that was established in the last rate proceeding. The historical FVRB is trended to current dollars using an inflation index, CPI-U, to establish the current value of the FVRB from the prior case. Pet. Ex. 7 at 56. She stated that since Cause No. 45142 (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. *Id.* at 56-57. 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 pointed out that this methodology is consistent with the methodology that was relied upon by the IURC in Cause No. 44022, the most recent fair value determination made by the IURC for the Company. *Id.* 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. *Id.* at 58. 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. *Id.* at 59. Ms. Bulkley compared the FVRB for each of the periods to a reproduction cost new less depreciation ("RCNLD") study that was prepared by the Company using the Handy-Whitman Index and which was included in her workpapers. After comparing to the RCNLD, Ms. Bulkley concluded the IURC Methodology continues to be a reasonable method for determining fair value. *Id.*

Ms. Bulkley then calculated the return on the FVRB using the same approaches that were applied in INAWC's 2011 rate case. Each of these approaches makes an adjustment to the weighted average cost of capital ("WACC") to remove inflation from the FVRB where inflation has been applied. She walked through the methodologies and results of each. *Id.* at 60-61. She clarified that the first component of the fair value rate base is the fair value rate base 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. *Id.* at 62. 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. However, Ms. Bulkley explained that while each of these methodologies is a reasonable approach to estimating the fair value operating income for INAWC, the Company is not proposing to rely on the fair value increment that results from the methodologies described above. Rather, INAWC is proposing to include only the return on the Indiana Cities acquisition adjustment that has been authorized by the IURC in other proceedings through informed fair value ratemaking. Below is the resulting Return on Indiana Cities Acquisition Adjustment presented by Ms. Bulkley:

Table 4: <u>Return on Indiana Cities Acquisition Adjustment</u>

	As of 7/31/2023	**As of 12/31/2024**	**As of 12/31/2025**
Acquisition Adjustment			
1993 Purchase of Indiana Cities	$ 17,412,009	$ 17,412,009	$ 17,412,009
Less: Indiana Cities Accumulated Amort	12,698,715	13,049,293	13,516,729
Acquisition Adjustment Net of Amort	$ 4,713,294	$ 4,362,716	$ 3,895,280
Times: Rate of Return	5.950%	5.930%	6.070%
Return on Indiana Cities	$ 280,441	$ 258,709	$ 236,443

ii. <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. IG Ex. 1 at 7 and 130-138.

iii. 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 the Company presented in its evidence in the settled case, which is based on the last fair value finding from a litigated case. Pet. Ex. 19 at 92. 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 including: Cause Nos. 42359 and 40003 - Duke/PSI; Cause No. 44075 – Indiana Michigan Power Company; Cause Nos. 44022, 43680, 42520 and 40703 – Indiana American Water Company; and Cause No. 40418 – Indiana Utilities. Ms. Bulkley explained that in these cases, the Commission methodology begins with the fair value rate base from the Company's last fair value finding in a rate case and trends the rate base using a cost inflation index, consumer price index ("CPI"). The Commission then adds net plant additions to determine the updated fair value of the plant. *Id.* at 92-93. She reiterated that the Company 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. *Id.* at 94.

iv. Discussion and Findings. Indiana-American requests that we make a finding of the fair value of the Company's rate base based on the testimony of, and the fair value methodology employed by, Ms. Bulkley. We decline to do so for several reasons.

First, it is unnecessary. The Company's own testimony states that it is not asking this Commission to rely on, or otherwise use, the fair value of its rate base as calculated through Ms. Bulkley' fair value methodology for any ratemaking purpose except insofar as she calculates a specific fair value increment to the return on the Indiana Cities acquisition adjustment. Pet. Ex. 7 at 64 ln. 4-12. 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 the Company, we will reflect that specific adjustment.

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 Indiana Code §8-1-2-6 for ratemaking purposes; the Company itself 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.

Second, we are not persuaded that Ms. Bulkley's calculation is an accurate representation of the fair value of the utility's plant in service. As pointed out by Mr. Gorman, Ms. Bulkely's methodology simply inflates the Company's own, prior, fair value estimate upon which we did not make a finding, to which she added plant additions. Pet. Ex. 7 at Attachment AEB-11. She makes no adjustment for retirements, depreciation, or obsolescence, all of which would impact the "fair value" of Petitioner's rate base. Finally, as noted by Mr. Gorman, a properly calculated "fair value" rate base should produce roughly the same net operating as an original cost rate base, but Ms. Bulkley's methodology does not. In fact, her analysis suggests an NOI approximately $38.99 million more than the Petitioner's net original cost rate base would yield. Given these analytical flaws we cannot find Ms. Bulkley's analysis produced a reasonable

estimate of the fair value of the utility's rate base. We therefore do not adopt Petitioner's fair value calculation.

Contrary to any implication by Petitioner, Indiana Code §8-1-2-6 does not require this Commission to use a "fair value methodology" to determine a utility's fair value rate base. It was, long ago, made plain that this Commission is not limited to any "one or more methodologies of valuation, be it prudent investment, original cost, present value, or cost of reproduction" to ascertain the fair value of the utility's rate base. *Pub. Serv. Comm'n v. City of Indianapolis*, 131 N.E.2d 308, 318 (Ind. 1956). Indiana's courts have also made clear that the term "fair value" as used in the statute is "in reference to the Commission's duty to value the used and useful property" and constitutes a "conclusion or final figure, drawn from all the various values or factors" that this Commission weighs in ascertaining the value of the utility's rate base. *OUCC v. Gary-Hobart Water Corp.*, 650 N.E.3d 1201, 1203 (Ind. Ct. App. 1995) quoting in part *Indianapolis Water v. Pub. Serv. Comm'n.*, 484 N.E.2d 635 (Ind. Ct. App. 1985).

Accordingly, so long as we make a finding as to the fair value of the Petitioner's rate base which considers valuation methodologies presented to us and allows us to arrive at "a figure that is fair and equitable to both investor and consumer" we have fulfilled our statutory obligation under Section 6. *Capital Improvement Bd. of Managers v. Pub. Serv. Comm'n*, 375 N.E.2d 616, 631 (Ind. Ct. App. 1978). Weighing the evidence and the valuation methods before us, we 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.

8. Fair Rate of Return.

A. ROE.

i. INAWC Case in Chief. Ms. Bulkley supported Petitioner's proposed ROE and testified in support of the reasonableness of INAWC's projected capital structure. She recommended an ROE of 10.60 percent as reasonable and appropriate for this proceeding. Pet. Ex. 7 at 8.

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. Pet. Ex. 7 at 3.

Ms. Bulkley testified that she considered the following key factors in her cost of equity analyses and recommended ROE for the Company in this proceeding: (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 the Company's cost of equity. Because the Company's authorized ROE should be a forward-looking estimate over the period during which the rates will be in effect, these analyses rely on forward-looking inputs and assumptions (*e.g*., projected analyst growth rates in the DCF model, forecasted risk-free rate and market risk premium in the CAPM analysis); and (4) the Company's regulatory, business, and financial risks relative to the proxy group of comparable companies in determining where the Company's ROE should fall within the reasonable range of analytical results to appropriately account for any residual differences in risk. Pet. Ex. 7 at 4-5.

Ms. Bulkley presented the results of her Constant Growth DCF, CAPM and ECAPM analyses, ultimately leading to a range from 10.00 percent to 11.00 percent as reasonable. *Id.* at 8.

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. *Id.* at 10. 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 very 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. *Id.* at 10-11. 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. *Id.* at 11. She testified that providing the opportunity to earn a market-based cost of capital supports the financial integrity of the Company, which is in the interest of both customers and shareholders. *Id.*

Ms. Bulkley walked through the effect current and prospective market conditions have on the cost of equity for the Company, 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 return on equity. *Id.* at 13. 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 underperform or underweight. 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. *Id.* at 26.

Ms. Bulkley described her process of selecting a group of proxy companies to estimate the cost of equity for INAWC. *Id.* at 26-32. She then walked through her use of the Constant Growth DCF model, the CAPM, and the ECAPM methods for estimating the cost of equity. *Id.* at 33-43. The mean and median DCF results using the average growth rates ranged from 9.65 percent to 9.97 percent; the mean and median results using the maximum growth rates ranged from 10.76 percent to 11.04 percent; and the mean and median results using the minimum growth rates ranged from 8.50 to 8.65 percent. *Id.* at 37-38. Her traditional CAPM analyses produced a range of returns from 10.19 percent to 10.88 percent and her ECAPM analysis results ranged from 10.77 percent to 11.29 percent. *Id.* at 43. 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. *Id.* at 47. 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. *Id.* at 48. She noted that the Company'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 the Company's projected capital expenditures. *Id.* at 49-50.

ii. <u>OUCC and Intervenors</u>. OUCC witness Dellinger recommended an ROE of 9.00%. Mr. Dellinger derived this recommendation from an analysis of the Constant Growth DCF model, the Two-Stage DCF model, the CAPM and the ECAPM. Pub. Ex. 6 at 3. Mr. Dellinger discussed his approach to these models and how they differed from Ms. Bulkley. *Id.* at 4. Mr. Dellinger began his analysis by determining the appropriate proxy group, starting with the appropriate water utilities and including some gas utilities by necessity. Id at 7-10. He explained why he included some additional companies compared to Ms. Bulkley's proxy group and why he excluded some companies that were in Ms. Bulley's proxy group. *Id.* at 8-11. He discussed the higher ROE's that resulted from the inclusion of the gas utilities in this proxy group, but discussed why, in this case, this inclusion was necessary and appropriate. *Id.* at 11.

Mr. Dellinger then proceeded to describe the DCF model, express his results, and present how his results compared with Ms. Bulkley. He explored the areas of disagreement between himself and Ms. Bulkley (e.g., different proxy groups, different resources for the growth estimates, and his inclusion of historical growth estimates), and he expounded on his preferred inputs. *Id.* at 13-14. The results of his Constant Growth DCF were a 9.0% ROE for the Mean calculation and a 9.32% ROE for the Median. *Id.* Mr. Dellinger then discussed the limitations and weaknesses of the constant growth DCF model, and how he addressed those limitations and weaknesses by using a two-stage model. *Id.* at 14-15. His two-stage model resulted in a 7.61% ROE for the Mean calculation and an 7.16% ROE for the Median calculation. *Id.* at 15.

Mr. Dellinger then proceeded to describe the CAPM; he discussed his preferred metric for interest rates (the 7-day yield of the 30-year treasury); and he discussed the calculation of Beta. *Id.* at 17. He used six different sources for Beta for the model and discussed that Ms. Bulkley's Beta results from her two sources were approximately 35% higher than the average from the four additional sources he used. *Id*. at 17-18. He next discussed the equity risk premium ("ERP") component. First, he addressed issues with Ms. Bulkley's calculation of the ERP, and why her results were problematic. He pointed out that Ms. Bulkley testified the DCF cannot be

fully trusted because utility stocks are overvalued, however, Ms. Bulkley then used the disparaged DCF model to calculate a generous ERP for use in the CAPM; the ERP, being a critical input of the CAPM. *Id.* at 19.

To further demonstrate the issues with Ms. Bulkley's CAPM methodology, Mr. Dellinger used a two-stage DCF model using Ms. Bulkley's inputs, which then generated a market return of 7.28%-7.92%. He stated this difference was 522 basis points lower than the expected market return derived by Ms. Buckley's methodology. *Id.* 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 highlighted that Ms. Bulkley had used different component companies in developing her market dividend rates compared to her market growth estimates. *Id.* He further pointed out that the growth estimate for just the dividend paying companies that she had used was nearly 170 basis points less than what Ms. Bulkley used as the input in her CAPM. *Id.*

With respect to the CAPM components, Mr. Dellinger also discussed that there are readily available estimates of long-term market returns from several reputable, national sources. *Id.* at 19-20. He stated he used twelve sources and the average of twelve sources resulted in a long-term market return estimate of 7.02%. *Id.* at 21. These twelve sources for long-term market return estimates included Indiana American's pension fund and the Indiana State Public Retirement System pension funds. *Id.* He also stated that Equity Risk Premiums are also directly calculated by informed third parties, and the average result of these estimates is 5.42%. *Id.* at 22.

Mr. Dellinger ultimately recommended a CAPM ROE of 7.39% calculated on the Mean and 7.38% calculated on the Median. *Id.* at 22. He also ran an ECAPM for only using non-adjusted Betas, 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 it is not a compelling model. *Id.* at 22-23.

Mr. Dellinger then discussed the reasons his results were lower than Ms. Bulkley, and why his results are appropriate and reasonable. He discussed the historic spread between Treasury rates and Indiana American's awarded ROE's over time; stated that the linkage between Treasury rates and the awarded ROE was not strong after interest rates declined after 2010; and stated that a return based on the average spread between 2002-2010 would result in an ROE of 8.95%. *Id*. at 24-25. Mr. Dellinger also discussed the market-to-book ratio of the proxy group, which was a ratio of 2.301 (the market-to-book-ratio was 2.88 for the water utilities in the proxy group and was 3.02 for American Water Works, itself). Mr. Dellinger pointed out that the market-to-book ratios strongly imply that the risk-adjusted returns being enjoyed by the average water utility are certainly higher than necessary to compensate the investor for the risk they are incurring. *Id.* at 26-27.

Mr. Dellinger then explained his reasoning for recommending a 9.0% ROE, and why he was recommending a result which was higher than the average result of the models he used. *Id.* at 27.

With respect to Ms. Bulkely's testimony regarding flotation costs, Mr. Dellinger testified that flotation costs should be disregarded; flotation costs should not be reflected in a higher cost

of equity. *Id*. at 31-34. Mr. Dellinger explained that 1) INAWC's equity consists of retained earnings which would not have incurred any flotation costs, and that retained earning balances for INAWC do not accurately reflect the full amount of INAWC's retained earnings; 2) The hypothetical adjustment by Ms. Bulkley of 4 basis points is overstated (the total amount of equity issued by American Water amounts to 8.2% of its Market Cap, which would only result in a value of 0.3 basis points, not 4 basis points); 3) INAWC has not incurred any flotation costs (American Water, not INAWC, would have issuances; and most of the approximately 97.5% of costs for issuance are underwriter discounts); and 4) The market already accounts for flotation costs. *Id.* at 32-34.

Intervenors, the Industrial Group, Crown Point, and CAC also provided testimony regarding the recommended ROE.

Industrial Group witness Gorman recommended an ROE of 9.40% less 30 basis points 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. His DCF recommendation was 9.00%. His CAPM analysis resulted in 10.10% and his Risk Premium analysis resulted in 9.55%. Mr. Gorman recommends that the Commission not adjust the ROE for the recovery of flotation costs, because he said Ms. Bulkley's flotation cost adjustment is "not based on the recovery of prudent and reasonable flotation expenses." IG Ex. 1 at 114.

Crown Point witness Guerrettaz did not perform any quantitative analyses regarding the cost of equity for the Company. Mr. Guerrettaz instead provided a "holistic" estimate that a reasonable authorized ROE for the Company is 9.00 percent based on his "understanding of the financial markets" and the "characteristics" of the Company's business. He characterized the Company as having extremely low business risk. Crown Point Ex. 1 at 21. In support of his ROE recommendation, Mr. Guerrettaz stated that INAWC has beneficial regulatory mechanisms that he claimed provide revenue stability between rate proceedings and is now proposing a future test year for ratemaking purposes.

CAC witness Inskeep recommended the Commission reject the Company's proposed ROE to mitigate the rate impact of what he calls an "extraordinary utility unaffordability crisis." CAC Ex. 1 at 36.

iii. <u>INAWC Rebuttal</u>. INAWC witness Bulkley responded to the issues raised in the OUCC and intervenors' testimony regarding the recommended ROE and the appropriate capital structure for the Company in this proceeding. She 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. Pet. Ex. 19 at 2-3. Ms. Bulkley also considered the effect of current and expected capital market conditions on these factors. *Id.* at 3.

Ms. Bulkley concluded that the ROE recommendations of Mr. Dellinger and Mr. Gorman in this proceeding are inconsistent with recent changes in market conditions and do not reflect

the current cost of equity. In support of this conclusion, Ms. Bulkley explained that interest rates have increased since the Company's last rate proceeding, and authorized ROEs have been increasing over the period from 2021 through 2023, which demonstrates that borrowing costs and the cost of equity have increased. *Id.* She testified that Mr. Gorman's and Mr. Dellinger's proposals that the Commission reduce the Company's currently authorized ROE by 70 and 80 basis points, respectively, are directionally inconsistent with market conditions and the investor required return on equity. Pet. Ex. 19 at 4 and 7-9. She stated that in fact, 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. *Id.* at 4 and 46-47. Ms. Bulkley responded to Mr. Gorman's proposed risk adjustment reduction to the ROE of 30 basis points, contending it is also arbitrary and asymmetric given his past testimony, and thus should be rejected. *Id.* at 4 and 48-49.

Ms. Bulkley evaluated the reasonableness of the ROE recommendations of Mr. Dellinger and Mr. Gorman relative to the comparable return standard that must be satisfied under the *Hope* and *Bluefield* decisions. *Id.* at 6. She discussed changes in market conditions since the Company's last rate proceeding which indicate an increase in the cost of equity, including increasing interest rates – both short-term and long-term. *Id.* at 6-7. She testified that credit rating agencies have recognized that the increases in interest rates may lead to increases in authorized ROEs, citing statements by Moody's Investors Service. *Id.* at 7 (internal citations omitted). Ms. Bulkley testified that Mr. Gorman's recommended ROE from within his range of DCF results does not appear to be responsive to market conditions. *Id.* at 48.

Ms. Bulkley testified on rebuttal that making reasonable adjustments to the cost of equity analyses of Mr. Dellinger results in a range of returns from 9.53 percent to 10.82 percent, which she states demonstrates that the Company's requested ROE is reasonable and appropriate. *Id.* at 4 and 44. She disagreed with the composition of his proposed proxy group. *Id.* at 11-14. With respect to the application of his constant growth DCF model, Ms. Bulkley had three additional primary concerns: (1) his use of the mean as opposed to the median as the measure of central tendency for the results of his analysis; (2) his inconsistent approach of relying on historical growth rates to estimate his mean DCF result but not his low and high-end DCF results; and (3) the relevance of the results produced by the DCF model under current market conditions. Pet. Ex. 19 at 15-19. In addition, Ms. Bulkley disagreed with Mr. Dellinger's criticisms of her DCF, CAPM and ECAPM analyses. *Id.* at 20-25; 38-43.

Ms. Bulkley recommended the following adjustments to Mr. Dellinger's constant growth DCF model: (1) Remove AWK and add both NI and ES to his proxy group, which results in a proxy group that is more risk comparable to INAWC; (2) Apply an outlier screen, which results in the exclusion of the constant growth DCF results for MSEX from the low and mean DCF scenarios; (3) Modify the methodology used to estimate the low- and high-end DCF results so that it is consistent with the methodology used to estimate the mean DCF results. She stated that making these reasonable changes to Mr. Dellinger's constant growth DCF analysis, the mean ROE result increases by 53 basis points from 9.00 percent to 9.53 percent, while this range of 7.47 percent to 9.77 percent shifts higher to 7.96 percent to 11.29 percent. *Id.* at 19; Attachment AEB-R-3.

With respect to Mr. Dellinger's two-stage DCF model, Ms. Bulkley testified that the results of his analysis are well below any ROE authorized for a water distribution company since 2012, and states that they are not reflective of the cost of equity for INAWC. *Id.* at 30. In addition, Ms. Bulkley testified that Mr. Dellinger's two-stage DCF result is below any comparable authorized ROE for an electric utility or natural gas utility in the U.S. since at least 1980. *Id.* (internal citations omitted). Ms. Bulkley testified that the two-stage DCF results clearly violate the *Hope* and *Bluefield* standards, which require the authorized return to be just and reasonable, as well as comparable to other returns available to investors in companies with similar risk. Pet. Ex. 19 at 30. Ms. Bulkley described her other specific concerns with Mr. Dellinger's two-stage DCF analysis. *Id.* at 31-32.

Ms. Bulkley testified that Mr. Dellinger's CAPM analysis did not produce reliable results and should not be used to inform the cost of equity estimate for Petitioner in this proceeding. *Id.* at 33. She described her primary areas of disagreement with Mr. Dellinger's CAPM analysis. *Id.* at 34-38. Ms. Bulkley adjusted Mr. Dellinger's CAPM analysis to: (1) remove AWK and add both NI and ES to his proxy group to result in a proxy group that is more risk comparable to INAWC; (2) exclude the beta coefficients from Yahoo! Finance and NYSE since they rely on the same methodology as Zacks; (3) apply the Blume adjustment to the betas from Zacks and S&P; and (4) rely on her forward-looking market return of 12.50 percent. Ms. Bulkley stated that by making these modifications, which she characterized as reasonable, to Mr. Dellinger's CAPM analysis, the mean ROE result increases by 287 basis points from 7.39 percent to 10.26 percent, and the median ROE result increases 292 basis points from 7.38 percent to 10.29 percent. *Id.* at 42, Attachment AEB-R-4.

Ms. Bulkley showed that if the results of Mr. Dellinger's two-stage DCF model are excluded and her adjustments are made to Mr. Dellinger's constant growth DCF, CAPM and ECAPM, the cost of equity range for his mean results is 9.53 percent to 10.82 percent, which is significantly higher than the range supported by Mr. Dellinger of 7.39 percent to 9.00 percent. Furthermore, Ms. Bulkley's recommended ROE for INAWC of 10.60 percent falls within this adjusted range. In contrast, Mr. Dellinger's ROE recommendation of 9.00 percent is significantly below the adjusted results. *Id.* at 44.

Ms. Bulkley disagreed with the assumptions relied upon in Mr. Gorman's constant growth DCF model using sustainable growth rates and his multi-stage DCF model. She testified that Mr. Gorman's reliance on the sustainable growth rates in the constant growth DCF model is not appropriate. *Id.* at 49-52. She stated Mr. Gorman's assumed long-term growth rates in his constant growth and multi-stage DCF are internally inconsistent and that the long-term growth rate in his multi-stage DCF is also inconsistent with the analyst literature he cites in his testimony. *Id.* at 53. She rejected Mr. Gorman's recommended "corrections" to her DCF model, which would convert a constant growth DCF model to a multi-stage model. *Id.* at 55-57.

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 of 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. Simply correcting these two errors produces a midpoint ROE of 9.60 percent instead of the 9.40 percent stated in Mr. Gorman's testimony. *Id.* at 4 and 79-80.

Ms. Bulkley testified 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 percent. She stated this change increases Mr. Gorman's cost of equity range of 9.10 percent to 10.86 percent. The midpoint, which is the central tendency that forms the basis for Mr. Gorman's market cost of equity recommendation would then be 9.98 percent. *Id.* at 4 and 60-63.

Ms. Bulkley disagreed with the manner in which Mr. Gorman has calculated the market return for purposes of his CAPM analyses, stating that simply applying a projected inflation rate to a long-term historical average does not produce a "forward-looking" market return. *Id.* at 65. She disagreed with Mr. Gorman's criticisms of her CAPM analyses. *Id.* at 65-69. She testified that Mr. Gorman's market return is inconsistent with his own multi-stage DCF analysis, and his historically based market return does not reflect investors' forward-looking return requirements in the current market. In addition, Ms. Bulkley testified there is no basis for dismissing the results of her scenarios relying on the longer-term projected risk-free rate given that Mr. Gorman also relies on a near-term projected risk-free rate in his CAPM that is reasonably consistent with the level of the long term projected risk-free rate in her analysis. Furthermore, Ms. Bulkley testified Mr. Gorman's position that his "revised" versions of her CAPM that rely on the historical average betas of the proxy group are the appropriate CAPM result is undermined by the fact that, in his own CAPM analyses, he recommends the scenario that relies on the current betas of his proxy group for purposes of his ROE recommendation. *Id.* at 69.

Ms. Bulkley rejected Mr. Gorman's objection to the use of adjusted betas in the ECAPM. She testified that the purpose of the ECAPM is to account for the fact that the risk-return relationship is flatter than what is estimated by the CAPM, even when using adjusted betas. While beta is not observable and must be estimated, the theory behind the ECAPM is that even if the true value of a stock's beta were observable, the CAPM would understate the results for stocks with betas less than 1.00 and overstate the results for stocks with betas greater than 1.00. Therefore, contrary to Mr. Gorman's assertion, the purpose of each adjustment is different and thus applying both adjustments in the ECAPM is not duplicative. *Id.* at 70-79.

With respect to the Company's business risks, Ms. Bulkley rejected the notion set forth by Mr. Gorman that INAWC faces risks that are comparable to the proxy group because the business risks that she has evaluated are already considered by the credit rating agencies, and that the credit rating of INAWC's parent, American Water, is consistent with the credit ratings of the proxy group companies. She disagreed with Mr. Gorman's comparison of credit ratings as being dispositive of INAWC's relative risk to the proxy group, because credit ratings are assessments of the likelihood a company could default on its *debt*, whereas the topic of her testimony is to determine the riskiness and cost of the Company's *equity*. In addition, Ms. Bulkley asserted that while credit rating agencies consider the business risks of an individual company, when establishing its debt credit rating, they do not conduct a comparative analysis of business risks relative to the proxy group. *Id.* at 81.

Ms. Bulkley did not address further Mr. Guerrettaz's and Mr. Inskeep's ROE recommendations other than to recommend they be dismissed summarily, and to provide a response to Mr. Guerrettaz's testimony as it relates to the Company's business risk and its impact on the cost of equity. *Id.* at 4-5. She responded to Mr. Guerrettaz's claims that the Company's

regulatory paradigm provides "full cost recovery," stating that is simply not the case, as the Company does not have guaranteed full cost recovery as he suggests. *Id.* at 82. Moreover, Ms. Bulkley pointed out that while Mr. Guerrettaz supports his ROE recommendation on the basis that the Company has low business risk and the Company's proposed future test year reduces its risk, he has not conducted any analysis of the *relative* risks of the Company as compared to the proxy group. *Id.* at 82.

Ms. Bulkley defended her use of flotation costs as a consideration when establishing the appropriate ROE. She stated that just as rate base investments, flotation costs are also 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. *Id.* at 85.

iv. <u>Discussion and Findings</u>. We note that the water companies in the proxy group (and significantly, American Water, which is included) have extremely elevated market-to-book ratios, which would demonstrate that the existing ROE is greater than necessary, because if that were not the case the market-to-book ratios would be much closer to 1.0. The evidence demonstrating the market-to-book ratios in the record is undisputed.

The United States Supreme Court's *Hope* and *Bluefield* decisions established the standards for determining a fair and reasonable authorized ROE for public utilities, including consistency of the allowed return with the returns of other businesses having similar risk, adequacy of the return to provide access to capital and support credit quality, and the requirement that the result lead to just and reasonable rates. *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) ("*Hope*"); *Bluefield Waterworks & Improvement Co., v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923) ("*Bluefield*"). As the Court noted in Bluefield, a proper rate of return should be reasonably sufficient to assure "confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, 262 US at 693. As the Court went on to explain in *Hop*e, "[t]the rate-making process … involves balancing of the investor and consumer interests." Hope, 320 US at 603.

The fact that the water company proxies, and notably, American Water, trade at such a high premium, certainly demonstrates that current awarded ROEs are *higher* than *reasonably sufficient* to enable INAWC to raise the money necessary and maintain and support its credit for the proper discharge of its duties, *assuming efficient and economical* management (e.g., efficient and economical "economies of scale").

As demonstrated through the testimony of Mr. Dellinger, interest rate decreases of the past decade, or more, have not been fully reflected in reduced awarded ROE's. Therefore, we do not find that awarded ROEs must now be correlated, or closely correlated, with interest rates, as interest rates return to more historically normal levels. It is also compelling to note that returning to the same spread as was in effect for INAWC from 2000-2012 would result in a ROE below 9.0%. We further find it compelling that this historical spread would result in an ROE very close to that recommended by the OUCC.

We find the use of a two-stage DCF, with the second stage having the theoretical ceiling of long-term growth to be appropriate and reasonable, and that this is a model that the Commission includes, and will continue to include, in its consideration. We further find that the utilization of unadjusted betas in the CAPM model is appropriate and reasonable.

We find that Mr. Dellinger's proxy group is reasonable and agree that including gas utilities in a proxy group for a water utility requires close scrutiny that is appropriately reflected in Mr. Dellinger's testimony and proxy group.

There is not a cost of equity estimation model that will produce the actual cost of equity for a utility; each model we consider and upon which we rely may be used to estimate the cost of equity. However, each such model has limiting assumptions that make it incorrect to conclude that any one model produces the actual cost of equity for INAWC.

This Commission has remained 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, 2012 WL 2154248, (IURC 6/6/2012) at 35; *see also Duke Energy Indiana, LLC*, Cause No. 45253, 2020 WL 3630515, (IURC 6/29/2020), at 57-58. In Cause No. 45253, the Commission reiterated:

> 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.

However, we also reiterate that the Commission appreciates the incorporation of historical data into the projected growth forecasts for the DCF models. This was stated in the order for Cause No. 43680, and we reiterate that here.

A return that is adequate to attract capital upon reasonable terms enables INAWC to continue providing safe, reliable water and wastewater service at reasonable and affordable rates, in comparison to an excessive ROE.

Having taken into consideration the observable market data reflected in the record, and a general assessment of the investment risk characteristics of the similarly situated utilities in the industry, combined with a thorough understanding of the Indiana regulatory environment, and INAWC in particular, and the recommended range identified above by the parties' expert witnesses, the Commission finds a reasonable range for Petitioner's cost of equity is 8.50% to 9.50%. Taking into consideration all of the evidence presented, the Commission finds that an ROE of 9.00% represents a fair and reasonable rate.

Furthermore, we find that the evidence of record shows that an ROE of 9.00% is well within the range of reasonableness and sufficiency and is significantly higher than the outputs of many of the models upon which we have historically placed reliance.

B. **Cost of Debt**.

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 Pet. Ex. 29. No party disputed these costs.

C. **Capital Structure**.

i. INAWC Case-in-Chief. INAWC witness Furia presented the Company's projected capital structures as of July 31, 2023, April 30, 2024 and April 30, 2025 to be used for computing the weighted average cost of capital ("WACC") for Indiana American at each of the three steps proposed for rate implementation in this case. These dates match the dates used to calculate proposed rate base for each of Step 1, Step 2 and Step 3. Mr. Furia explained that the revenue requirement for each proposed increase in Step 1, Step 2 and Step 3 will use the Company's actual capital structure as of these dates when rates go into effect. Pet. Ex. 6 at 4. Mr. Furia 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. *Id.*

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 a cost of common equity of 10.60%, as recommended by Indiana American's cost of equity expert witness, Ann E. Bulkley. 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%. *Id.* at 5; Pet. Ex. 13 at Schedule CC1.[32] Mr. Furia described the bases for various components on Schedule CC1, including Accumulated Depreciation on Contributed Utility Plant for Muncie Sewer, Other Post-Retirement Employee Benefits ("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 have been included in the capital structure as negative values. *Id.* at 6-7.

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. *Id.* at 8. He described the new long-term debt the Company plans to issue in

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[32] 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%.

November 2023 and March 2024. *Id.* at 8-9. 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. *Id.* at 9-10. He stated these adjustments reflect the Company's projections for the 2023-2025 period and are based on the Company's projected capital requirements and the need to maintain appropriate capital structure ratios. *Id.* at 10.

INAWC witness Bulkley testified that comparing the Company's projected equity ratio as of April 30, 2025 of 56.15 percent (excluding the adjustments for zero cost capital items) demonstrates that the Company's requested equity ratio is well within the range of equity ratios for the proxy group. Pet. Ex. 7 at 7. She further stated the Company'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. *Id.* at 7 and 50-54.

ii. <u>OUCC and Industrial Group</u>. OUCC witness Dellinger did not disagree with the Petitioner's capital structure as proposed, for purposes of the determination of the WACC. However, Mr. Dellinger did testify detailing how the capital structure has changed over time becoming more weighted toward equity and becoming more expensive for ratepayers and implicating affordability. Pub. Ex. 6 at 28.

He stated that ratepayers would benefit from having an optimal capital structure (meaning the lowest reasonable weighted average cost of capital), 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. *Id.* at 29. Mr. Dellinger stated that in the present case, Indiana American's cost of debt is 4.71%, and, as he explained, the after-tax cost of equity is 14.13%, so the cost of equity is three times the cost of debt. *Id.* at 29. He showed that in each case since 2010, the percentage of equity in the capital structure has increased. Mr. Dellinger also showed that in the 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 now increased again. The percent equity projected for 2025 was estimated to be 53.69% according to Cause 45660 estimates, but is now projected to be 56.15%. *Id.* at 29-31. 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. *Id.* at 31.

OUCC Witness Ms. Stull recommended adjustments to Petitioner's projected balance of accumulated deferred income taxes 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. Pub. Ex. 3 at 46. 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. *Id.* 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 stated that 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 (OUCC Attachment MAS-8). *Id.* at 47.

Industrial Group witness Gorman testified that INAWC's projected capital structure is not reasonable because it imposes excessive cost on its retail customers. He testified that INAWC's equity ratio is far too 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 utility capital structure in the state of Indiana. IG Ex. 1 at 63. Mr. Gorman noted that the IURC has historically declined to make *pro forma* adjustments to utilities' capital structures. Still, he recommended the Commission consider the excessive cost INAWC imposes through its equity rich capital structure in determining a reasonable return on equity that reflects the Company's actual financial risk, and ensuring that the overall rate of return and the resulting costs imposed on INAWC's customers are just and reasonable. *Id.* at 64. He presented a comparison of the Company'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." *Id.* at 65.

Mr. Gorman also objected to the inclusion of a prepaid pension asset and an OPEB asset in INAWC's capital structure. Mr. Gorman testified that the prepaid pension asset reflects funds provided by ratepayers through rate revenue, which INAWC 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, INAWC is not entitled to a return of that sum by including the asset in its capital structure or cost of service. IG Ex. 1 at 8-9, 38-40. He stated the Company did not show that the amount of pension expense included in cost of service and recovered in customer rates during the time the PPA was accumulated was limited to the Company's annual GAAP pension expense. Specifically, he presented a table comparing the amount of pension expense that IAWC has collected in rates to the and testified that, since 2020, there has been an overcollection of recorded pension expense that has fully compensated for the vast majority of INAWC's current prepaid pension asset. *Id.* at 38-40. He proposed a similar adjustment to the OPEB asset included in the capital structure. *Id.* at 40-41.

iii. **INAWC Rebuttal**. Ms. Bulkley explained that Mr. Gorman's analysis of recent authorized equity ratios for water and natural gas utilities was flawed because (1) he included limited-issue rider cases in his benchmarking analysis and (2) he relied on the mean and median authorized equity ratios for water and natural gas utilities in each year since 2013, but he also incorrectly asserted that the Company'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. Pet. Ex. 19 at 86-87. She testified that from 2013 through 2023, the range of authorized equity ratios was 42.01 percent to 60.59 percent, meaning the Company's projected equity ratio of 56.16 percent is well within the range of the authorized equity ratios for natural gas utilities over this period. *Id.* at 87.

She also explained Mr. Gorman's comparison of the Company's projected capital structure to the capital structures of the holding companies in the proxy group is flawed because (1) it is not appropriate to compare the projected equity ratio of the Company to the average equity ratio of the proxy group at the holding company level and (2) while it is not appropriate, 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. *Id.* at 87-91. 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. *Id.* at 91. She testified that the Company's projected ratemaking capital structure of 56.16 percent is consistent with the actual capital structures of the operating utility subsidiaries of the proxy group of 56.09 percent. *Id.* at 88; Pet. Ex. 7, Attachment AEB-9.

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 Mr. Gorman ignores the fact that the Company has followed GAAP to record its annual pension costs and cash pension plan contributions. This accounting has resulted in a prepaid pension asset on the Company's balance sheet. Mr. Farrell stated that any asset on the Company's balance sheet is inherently financed through the Company's capital structure until it is recognized as expense on the Company's income statement. Pet. Ex. 24 at 3. He testified that Mr. Gorman does not address the clear economic benefits to customers resulting from the Company's pension plan contributions and OPEB asset. Mr. Farrell stated it is those cash contributions that have resulted in the existence of the prepaid pension asset in the first place. He explained the benefits are substantial — lowering pension costs and providing a source of accumulated deferred income tax ("ADIT"). *Id.* at 3. INAWC witness Ciullo presented the ADIT associated with the Company's prepaid pension asset and prepaid OPEB asset is $1,687,610 and $1,647,921 respectively. Pet. Ex. 23 at 10. Mr. Farrell testified that the lower pension and OPEB expense and accelerated income tax deductions directly lower costs to customers. Pet. Ex. 24 at 3. He explained that the cash pension plan contributions reduce pension expense. *Id.* at 10. In addition, Mr. Farrell explained that the economic benefit of the tax deductibility of the Company's pension plan occurs when the Company 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. *Id.* at 11. 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. 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. *Id.* at 3-4.

Mr. Farrell testified that the entire prepaid pension asset represents the cumulative difference between Company contributions to the pension trust and cumulative pension expense. The entire balance represents investor supplied funding and, as a result, is entitled to a return, which supports the Company'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. *Id.* at 13. 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). *Id.* at 14. He pointed out that the Company cannot access these pension assets. ERISA requirements do not permit employers to access funds from an ongoing pension or OPEB plan other than for the payment of benefits under that plan. *Id.*

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. Pet. Ex. 15 at 22-25.

iv. <u>Discussion and Findings</u>. The inclusion of a prepaid pension asset in either the utility's rate base has been previously addressed in other Indiana utility rate cases. In Cause Nos. 44576/44602, the Commission stated that with respect to the treatment of a prepaid pension asset in rate base, we "must address two issues," specifically (1) whether the asset is used and useful property under Ind. Code § 8-1-2-6, and (2) what amount of any prepaid asset should be "recognized as investor capital on which a return should be provided." *Indianapolis Power & Light*, Cause Nos. 44576/44602 at 23-24 (IURC March 16, 2016). In that case, we disallowed a portion of a utility's prepaid asset to the extent the funds represented the ERISA-minimum amount that was outside the discretion of investor-supplied capital. *Id.* at 24. As we noted in Cause No. 43526, it is the utility's burden to demonstrate that the prepaid pension asset is discretionary capital made available by investors. *NIPSCO*, Cause No. 43526 at 9.

Our decision in *Indianapolis Power & Light* is consistent with the holding of the Indiana Court of Appeals in *City of Evansville v. Southern Indiana Gas & Electric, Co.*, 167 Ind. App. 472, 339 N.W.2d 562 (1975). In that case, the Court concluded that we have established unjust and unreasonable rates in part because we authorized the utility to "obtain a return on funds contributed by customers." 167 Ind. App. at 512, 339 N.E.2d at 587. The Court did not go so far as to require "the exclusion of all customer contributed capital from rate base in all cases," but did hold that it would be unreasonable to establish "rates which permit the Petitioner to obtain a return on capital not advanced by investors." *Id*.

In this case, INAWC proposed to reflect the prepaid pension asset in its capital structure, which results in an increase to the weighted cost of capital calculation. However, IAWC has not demonstrated whether the prepaid pension asset was funded by either investor capital or

collections of pension-related costs from retail customers. IG Ex. 1, at 38. In the direct testimony of INAWC witness Shimansky, INAWC provided data on the authorized pension expense and the actual pension expense incurred for the years 2010 through 2022. (Testimony pg. 28, line 4). This data demonstrates that, since 2020, the amount of pension expense in rates has greatly exceeded INAWC's actual pension expense. IG Ex. 1, at 39. Furthermore, data provided by INAWC showing the calculation of its prepaid pension asset from 2018 to 2022 shows that the increase of the prepaid pension asset over the period 2018 to 2022 is equal to the difference between pension trust contributions less the recorded pension expense over that period. *Id.* In other words, the growth of the prepaid pension asset over this period was funded by collections from customers, not investor capital. Furthermore, over the period 2020 and 2022, the pension expense that IAWC has collected in rates was $7.9 million greater than the pension expense it recorded while the rates were in effect. *Id.* Thus, INAWC's over collection of recorded pension expense has fully compensated INAWC for the vast majority of its current prepaid pension asset which sits at a value of $8.1 million in 2023. *Id*. In sum, it is clear that collections from customers are a source of the prepaid pension asset. As a source of the prepaid pension asset is ratepayer funds, INAWC is not entitled to a return of that sum, as it is not contributed by investors. The prepaid pension asset reflects funds provided by ratepayers through rate revenue which INAWC has been able to use to offset its actual pension expense. The same is true of the OPEB asset. Thus, we reject the inclusion of the prepaid pension asset and the OPEB asset in INAWC's capital structure.[33] With the exclusion of those two items from the capital structure, we otherwise accept the proposed Step 3 capital structure as set for below in subsection (C).

D. <u>Overall WACC</u>.

The Company'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. Pet. Ex. 29, Financial Exhibit CC, Schedule CC1.

The OUCC's recommended capital structure and WACC were included in OUCC Schedule 9TC. Based on the OUTCC's recommended capital structure components and component costs, the OUCC recommended a 6.14% WACC as of April 30, 2025, 6.01% as of April 30, 2024, and 6.01% as of July 31, 2023.

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[33] Mr. Shimansky, in his rebuttal testimony, asserted Mr. Gorman's reliance on comparisons of past amounts reflected in rates to actual expense to disallow the prepaid pension asset would constitute prohibited retroactive ratemaking. However, during the evidentiary hearing, Mr. Shimansky conceded that Mr. Gorman did not make any adjustments to INAWC's pension or OBED expense to be recovered in rates. Tr. at D-22. As noted above, the utility has the burden to demonstrate its historic funding of the prepaid pension asset was made with voluntary investor contributions. Removing the prepaid pension asset from Petitioner's capital structure based on evidence that the historic funding was sourced from ratepayers does not constitute retroactive ratemaking.

The Industrial Group's recommended capital structure and WACC were included in Attachment MPF-1. Based on the Industrial Group's recommended capital structure components and component costs, the Industrial Group recommended a 6.08% WACC as of April 30, 2025, 5.97% as of April 30, 2024, and 6.0% as of July 31, 2023.

Based upon the foregoing findings and after giving effect to the ROE we authorized above, we find that, based on our other findings herein and the evidence of the parties, the forecasted capital structure and weighted cost of capital, as indicated in the table below, is reasonable and should be adopted for purposes of setting rates in this proceeding:

Table 5: <u>Capital Structure as of July 31, 2023</u>

	Amount	Percent of Total	Cost	Weighted Cost
Capital Structure as of 7/31/2023				
Common Equity	$ 716,559,651	46.90%	9.00%	4.22%
Long Term Debt	557,418,248	36.48%	4.73%	1.73%
Accumulated Deferred Income Taxes	253,164,451	16.57%	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)	-	0.00%	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	-	0.00%	0.00%	0.00%
Total Capital Structure	############	100.00%		5.95%

Table 6: <u>Capital Structure as of April 30, 2024</u>

	Amount	Percent of Total	Cost	Weighted Cost
Capital Structure as of 4/30/2024				
Common Equity	$ 731,237,765	46.83%	9.00%	4.21%
Long Term Debt	570,746,268	36.55%	4.71%	1.72%
Accumulated Deferred Income Taxes	258,787,249	16.57%	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)	-	0.00%	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%	8.01%	0.00%
Prepaid Pension	-	0.00%	0.00%	0.00%
Total Capital Structure	############	100.00%		5.93%

Table 7: <u>Capital Structure as of April 30, 2025</u>

	Amount	Percent of Total	Cost	Weighted Cost
Capital Structure as of 4/30/2025				
Common Equity	$ 834,238,915	47.88%	9.00%	4.31%
Long Term Debt	651,443,865	37.39%	4.71%	1.76%
Accumulated Deferred Income Taxes	256,136,559	14.70%	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)	-	0.00%	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%	8.02%	0.00%
Prepaid Pension	-	0.00%	0.00%	0.00%
Total Capital Structure	############	100.00%		6.07%

9. Disputed Test Year Revenues.

A. Declining Use (Residential).

i. INAWC Case-in-Chief. INAWC witness Rea presented the Company's 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). For residential customers, he testified that the parameters and relationships necessary to analyze declining water use, weather impacts on water consumption, and the impact of COVID-19 on water consumption for INAWC's customers were estimated using statistical linear regression modeling. Pet. Ex. 5 at 56-73. Mr. Rea testified his regression models show a trend of declining use identified for residential customers of approximately 585 gallons per year per customer. *Id.* at 68. 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. *Id.* at 69. Mr. Rea testified that INAWC's modeling normalizes for weather and COVID-19 and shows that there is a pervasive decline in residential usage over the past ten years. *Id.* at 72-73. He stated he expects the trend of declining usage to continue in the future. *Id.* at 71.

ii. OUCC and Intervenors. 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 the Company 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. IG Ex. 1 at 28. 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. Pub. Ex. 6 at 44. Mr. Gorman's estimates were higher than the Company's by approximately 40 gallons per month and Mr. Dellinger's estimates were higher than the Company's by approximately 100 gallons per month. Pet. Ex. 18 at 71.

Mr. Dellinger testified that INAWC's declining use projections are not consistent with other information the Company 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. Pub. Ex. 6 at 35. He testified that declining use is typically based on a trend calculated over time. *Id.* He testified 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 many savings and benefits to society at large. *Id.* He testified the average decline over the period of 2015 through 2020 has been approximately 1.0% a year, and going forward it is expected to decline by a lower 0.67% per year. *Id.*

Mr. Dellinger testified the output of the regression analysis results in a much steeper decline for the period between the base period and calendar year 2023. Mr. Rea did not produce a "trendline"; rather, he produced a future monthly projection of estimated flows based on estimated precipitation, estimated cooling degree days, monthly adjustments and his estimated 585-gallon annual decline. His 2023 forecast based on these estimates is significantly lower than the actual 2022 volumes, as well as the base period ending September 2022. *Id.* at 37. He pointed out the inconsistencies in the Company's monthly model between forecasted maximum monthly usage values and the historical data, and he testified the means to capture this decline is via an annual trendline applied to actual usage, and not a monthly model with significant and unnecessary complexity. *Id.* at 38-39. Mr. Dellinger utilized a modeling approach that uses annual data instead of monthly data (10 data points instead of 120 data points) with no weather variables and a single COVID impact variable to measure the impact on usage due to the COVID-19 pandemic in 2020 and 2021. *Id.* at 40.

For instance, Mr. Dellinger testified that based on actual usage, Mr. Rea's forecasted decline from 2022-2023 is 3.87%. (Id at 36-37). Mr. Rea stated that the average decline has been 2.0 % per year since 2013, and that Mr. Rea forecasted a declining use of 3.06% in 2023, 1.25% in 2024 and 1.27% in 2025. However, based on actual usage, Mr. Rea's decline from 2022-2023 is 3.87%; the output of the regression analysis results in a much steeper decline for the period between the base period and calendar year 2023. Id at 36-37. Mr. Rea's 2023 forecast based on these estimates is significantly lower than the actual 2022 volumes. *Id.* at 37.

Mr. Dellinger presented maximum forecasted usage in the highest month of the year from 2013 through 2025, which showed that the forecasted period had drastically lower maximum use months than in the past. *Id.* at 37-39. He stated this forecasted period represents years in which the outputs of the model are based on forecasted or estimated inputs only. Id at 38.

Mr. Dellinger then walked through various steps and visual presentations of the actual data involved. *Id.* 39-41. He stated he used annual inputs, and included a Covid adjustment that was in full effect in 2020 and half effect in 2021. *Id.* 40-41. He acknowledged that weather affects usage, but that these effects are much more pronounced on a monthly basis, and for declining usage what is important is the underlying trend of lower use on an annualized basis. *Id.* at 42-44. 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. *Id.* Mr. Dellinger testified that the results of his final model had a higher R squared value (a measure of the "fit of the model") than Mr. Rea's model. *Id.* at 42-43 and note 51.

Ultimately, Mr. Dellinger's analysis and modeling resulted in his demonstrated decline of 436 gallons per year from actual usage from the base period, which results in projected monthly usage of 4,019 gallons in calendar year 2023 and 3,971 gallons per year in the test year ending April 2025. He stated that Petitioner's proposal to use the numbers predicted by its model for future periods, fundamentally means that for Petitioner's proposal the actual usage in the base period does not matter significantly. *Id.* at 44.

Industrial Group witness Gorman testified that the Company'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 the use of declining use per customer based on ten years of historical trends does not reflect actual, recent, historical data and fails to acknowledge that declining use per customer will slow over time. IG Ex. 1 at 24-25. 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. *Id.* at 25; Table 4. 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. *Id.* at 26.

iii. <u>INAWC Rebuttal</u>. Mr. Rea disagreed with Mr. Dellinger's approach to modeling residential usage without reflecting weather effects and generally his approach of using less data to forecast usage. Pet. Ex. 18 at 73. Mr. Rea responded to the results of Mr. Dellinger's modeling wherein he input both cooling degree days and precipitation on an annualized basis, explaining that the resulting t-Stat Value or P-value were not surprising because "watering down the data from a monthly data stream to an annual data stream doesn't make the weather impacts go away. It just makes it harder to identify them." *Id.* at 74. Mr. Rea took exception to Mr. Dellinger's approach of ignoring the impacts of weather on water consumption even if you know they exist. He testified it makes no sense to argue that it is better to model annual data to get an annual answer and be ignorant of weather impacts than to model monthly data, understand weather impacts, normalize for them, and sum monthly normalized results to get an annual answer. *Id.* He performed a comparison of the results of Mr. Dellinger's modeling approach using actual (non-normalized) annual usage compared to weather-normalized data. *Id.* at 75. He concluded that the Adjusted R-Square statistics for the weather normalized model is 93.4% versus 87.5% for Mr. Dellinger's model. He testified the weather-normalized model shows more declining usage. He testified the results of his comparison validate the results from the monthly model presented in Mr. Rea's Direct Testimony.

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. *Id.* at 77.

iv. <u>Discussion and Findings</u>. We find that fundamentally, the biggest difference in models involves the question of whether the usage in future periods should be determined by an annual adjustment to the actual usage, or the results of a model, with all inputs being estimates. We find that adjustments must be fixed, known, and measurable, and should be based on actual data from the base period and that any declining use adjustment must, likewise, be based fundamentally on actual usage in the base period (4,065 gallons per month). Once this determination is made, the difference between Mr. Rea's results of an adjustment of 585 gallons per year and Mr. Dellinger's of 436 gallons per year are not as significant. However, we find that the result of Mr. Dellinger's model of 436 gallons per year is accurate and reasonable, as it gives an annual reduction in usage with high certainty, with a minimum of future estimates that will affect the results.

B. **Revenue Calculations**.

i. INAWC Case-in-Chief. Mr. Rea explained, generally, 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 Schedules REV1 W and REV1 WW, which show operating revenues by customer class for the base year under present rates (twelve 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. Pet. Ex. 5 at 73 and Pet. Ex. 14 at 57-58. Mr. Rea also sponsored Schedule Rev2, which includes the *pro forma* revenue adjustments, and sponsored the supporting workpapers. Pet. Ex. 5 at 4, 73, 77, and see Pet. Ex. 14 at 59-62. 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. *Id.* at 74. 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. *Id.* at 74. 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. *Id.* at 74-75. Mr. Rea detailed the specific factors he used for forecasting customer and usage by customer class components for organic growth for each class. *Id.* at 75-76. He explained how the various components of Other Revenues were developed. *Id.* at 76. Mr. Rea 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. *Id.* at 77.

ii. OUCC. OUCC witness Sullivan presented the overall results of the OUCC's analysis of INAWC's proposed overall operating revenue increase and its proposed revenue adjustments. Ms. Sullivan also recommended certain adjustments applicable to the Company's operating revenue (base year revenue or revenue requirements in a Step, as applicable), including changes in average customer consumption, customer growth, capital trackers, Utility Receipts Tax Repeal, and other revenue adjustments. Pub. Ex. 2 at 1, 2, 8-10.

Ms. Sullivan testified regarding INAWC's proposed adjustment for non-residential declining use. Pub. Ex. 2 at 11-14. Ms. Sullivan testified that Mr. Rea used a three-year average to project future average consumption for the non-residential customer classes, as a whole. *Id.* at 11. Ms. Sullivan did not dispute Mr. Rea's method of analyzing all non-residential customer classes, as a whole. However, Ms. Sullivan testified that using a three-year average consumption rate (October 1, 2019 through September 30, 2022) for the non-residential customers is not appropriate because consumption levels between April 2020 and December 2021 were affected by COVID-19. *Id.* at 12. Ms. Sullivan also noted that Mr. Rea had taken this effect into consideration in his analysis for residential consumption but had not given consideration in his non-residential customer consumption analysis. *Id.* For her analysis, Ms. Sullivan instead calculated a 10-year median value from the 10 years of historical data provided by the Company to forecast future non-residential consumption. *Id.* at 12-13. 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. Pub. Ex. 2 at 12.

Ms. Sullivan also testified regarding INAWC's proposed adjustment for organic growth. Pub. Ex. 2 at 14-15. Petitioner did not project any growth for its non-residential customer classes after December 31, 2023 and non-residential growth should be recognized through the end of the future test year, April 30, 2025. *Id.* at 15. She also calculated a different Step 1 organic customer growth adjustment from the Company by using the OUCC's average customer consumption values instead of the Company's values. *Id.* at 14. She calculated a different Step 2 adjustment by including non-residential customer class growth through April 30, 2025. *Id.* at 15.

iii. <u>INAWC Rebuttal</u>. INAWC witness Rea disagreed with Ms. Sullivan's revenue adjustment for the residential class. He did not take issue with her adjustment for residential customer counts, which were nearly identical to the Company's. Pet. Ex. 18 at 80-81. However, because he disagreed with the OUCC's forecast of residential use per customer, he did not accept Ms. Sullivan's residential class revenue adjustments. *Id.* Similarly, he disagreed with Ms. Sullivan's commercial class adjustment which 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 the Company'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. Pet. Ex. 18 at 81. He further disagreed with OUCC industrial usage forecasts which show 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 the Company's forecast of usage is more realistic and reflective of current usage levels in both 2021 and 2022 and should be adopted. *Id.* at 82. With respect to Ms. Sullivan's adjustment for the Public Authorities class, Mr. Rea testified that the combination of the 10-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 far and away higher than any annual usage for this class would suggest. Mr. Rea testified 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. Mr. Rea stated the Company's forecast for both customer counts and usage for the Public Authorities class should be adopted by the Commission. *Id.*at 83.

iv. <u>Discussion and Findings</u>. We find that the forecasts developed using Petitioner's methodology are not more reliable than the OUCC's. INAWC presented revenue adjustments based on two different methodologies. Consumption for residential customers was based on a regression analysis using 10-years of data but, non-residential consumption was based on a simple 3-year average. Ms. Sullivan correctly pointed out the 3-year average used to calculate non-residential average consumption included years affected by COVID-19 when businesses, industries, and schools were closed due to stay at home orders. We find non-residential consumption data between April 2020 and December 2021 to be unreliable for the purpose of forecasting future consumption. Therefore, we find the OUCC's 10-year mean methodology is more reliable.

Additionally, Petitioner forecasted and incorporated residential customer growth through the end of the test year, April 30, 2025, but did not forecast and incorporate non-residential customer growth beyond December 31, 2023. Petitioner's workpapers do not support Mr. Rea's testimony that Step 2 and Step 3 adjustments are based on forecasted usage and customer count information for non-residential customers for the periods ending April 2025.

While different methodologies may be used for different classes, we find it more appropriate to use a consistent methodology across all classes to avoid the potential for bias in the forecast process in attempt to achieve a certain outcome. We therefore reject the Petitioner's methodology for forecasting non-residential usage and customer counts and find that the OUCC's forecast should be adopted for this proceeding.

C. <u>Low-Income Pilot Program ("LIPP") Discount Adjustment</u>.

i. <u>INAWC Case-in-Chief</u>. INAWC made a *pro forma* revenue adjustment of $10,262 titled "Eliminate 50% of LIPP" to its base year revenues. Pet. Ex. 14 at 59. This adjustment was not accompanied by explanatory testimony**.**

ii. <u>OUCC</u>. OUCC witness Sullivan recommended the actual amount of LIPP discounts provided during the base year be added back to operating revenues due to the discontinuance of the program. Pub. Ex. 2 at 19-20. Ms. Sullivan testified according to INAWC's general ledger, INAWC had recorded $25,521 to its general ledger account 40111001 – Residential Sales Billed – Discount. *Id.* Therefore, Ms. Sullivan recommended an adjustment of $25,521 to INAWC's base year revenues to include the entire general ledger balance for the discontinued LIPP program discounts**.** Id**.**

iii. <u>INAWC Rebuttal</u>. In response to Ms. Sullivan's LIPP Discount adjustment, Mr. Shimansky testified that under the settlement approved in Cause No. 45142, a regulatory asset was established for the customer-funded portion of the total program costs. Pet. Ex. 15 at 49. He testified 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. *Id.* Mr. Shimanski then testified the Company 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. Mr. Shimanski did not, however, offer testimony referencing the accounting entries or ledger balances, nor offer

testimony explaining the derivation of the Company's "Eliminate 50% LIPP" adjustment (which does not represent 50% of the ledger balance for the Residential Sales Billed – Discount account).

iv. Discussion and Findings. The evidence reflects that the ledger balance for the LIPP discount during the base year was $25,521. INAWC offered insufficient evidence for the Commission to determine the complete bases for INAWC's proposed adjustment in the amount of $10,262. Therefore, we find the OUCC adjustment should be accepted, and the Company adjustment should be denied.

D. DSIC Revenue Adjustment.

i. INAWC. INAWC made a *pro forma* revenue adjustment of $24,035,317 titled "DSIC Revenue Adjustment" to its base year revenues. Pet. Ex. 14 at 59. This adjustment was not accompanied by explanatory testimony.

ii. OUCC. OUCC witness Sullivan proposed an adjustment to forecasted operating revenues related to 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. Pub. Ex. 2 at 17. From the amount authorized in Cause No. 42351-DSIC14 ($35,316,103), she subtracted DSIC revenue included in the base year operating revenues ($11,366,769). *Id.* at 17-18. 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 Cause No. 42351 DSIC-14. *Id.*

iii. INAWC Rebuttal. INAWC witness Shimansky testified that 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 in the order, the final total DSIC revenues per the order is $35,316,103. Pet. Ex. 15 at 48-49.

iv. Discussion and Findings. Ms. Sullivan's *pro forma* adjustment is supported by the evidence and establishes that INAWC's *pro forma* adjustment to increase its revenues was overstated (and, thus, the OUCC's adjustment favors INAWC). Accordingly, we find the OUCC's proposed DSIC revenue adjustment should be accepted.

E. Other Operating Revenue Adjustments.

i. OUCC. 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. Pub. Ex. 2 at 20. Ms. Sullivan testified that the late fee ratio reflected in INAWC's late fee adjustment was 0.5108%. *Id.*

ii. INAWC Rebuttal. 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. Pub. Ex. 2 at 20. Ms. Sullivan testified that the late fee ratio reflected in INAWC's late fee adjustment was 0.5108%. *Id.*

iii. Discussion and Findings. The evidence establishes the late fee ratio to be 0.5108% and there is no dispute between the parties as to the late fee ratio to use in calculating a late fee adjustment, based on revenue adjustments. We have accepted the OUCC's revenue adjustments as discussed herein, and, accordingly, we find that the late fee ratio of 0.5108% should be used to calculate the late fee revenue adjustment based on all other revenue adjustments.

Table 8: Operating Revenue Adjustments

	Step 1	Step 2	Total
URT Tax Impact	$(3,241,099)	$ -	$ (3,241,099)
Normalization of Billings - Usage	845,954	(1,298,242)	(452,288)
Annualization of Lowell	685,485	-	685,485
Customer Normalization	3,415,200	3,926,504	7,341,704
DSIC Revenue Adjustment	23,949,334	-	23,949,334
SEI Revenue Adjustment	5,150,494	-	5,150,494
Yankee Surcharge	-	(76,056)	(76,056)
Miscellaneous Adjustments	(329,333)	-	(329,333)
Acquisition Adjustment	95,807	75,826	171,633
Eliminate 50% of LIPP	25,521	-	25,521
Rate Increase OOR	-	217,149	217,149
Normalize Misc. Billing Units	11,835	19,024	30,859
Late Fees	156,273	13,604	169,877
	##########	#########	$ 33,643,280

10. Disputed Test Year Expenses.

A. Labor and Labor-Related Expenses.

i. 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. *See* Pub. Ex. 4 at 2-3. As explained in the Direct Testimony of INAWC witness Grisham, *pro forma* salaries and wages expense was calculated on a position-by-position basis, based on 408 full-time positions. Pet. Ex. 8 at 4.

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. Pet. Ex. 4 at 27. She stated the Company's operations are widely dispersed throughout the state. INAWC operates distinct public water systems providing service to approximately 78 communities throughout Indiana. Pet. Ex. 4 at 27. She explained that one way INAWC continues to look to improve efficiency, enhance compliance, and better serve customers is by consistently evaluating all areas of operations and identifying the positions that fit best in a regional approach and which positions can function optimally at a centralized location. She testified that INAWC has slowly added support staff to ensure it is adding the right positions in the right areas of the state to support its customers and maintain compliance. *Id.* at 28-29.

Ms. Britto provided a summary of the positions INAWC has added and plans to add from 2019 through the Test Year in this case. 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 support of operations throughout the state, including two Director of Operations positions, an Information Technology Specialist and two Business Operations Specialists. *Id.* at 29. In 2023, Ms. Britto stated the Company 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. In 2022, Ms. Britto testified, the Company 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). The Company also added six new pipe mechanics to create two crews for replacing lead service lines that fall outside of the Company's scheduled engineering projects, these include service line leaks and turning on service to homes that have existing lead. In 2023, Ms. Britto testified, the Company plans to add three water treatment plant operators for the East, Central and South regions. By 2024, Ms. Britto testified, the Company 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 – one in 2021, one in 2022, two in 2023, and two in 2024. *Id.* at 30. Ms. Britto stated these additional employees will support compliance with more stringent regulations that require additional tracking, monitoring, and reporting and will enhance the Company's cross connection control program, which is a critical component to protect the distribution system and the health and safety of customers. She further testified the Company plans to add four health and safety specialists (one Northern region, one Southern region in 2023), and two more in 2024 (one Central region, one Western region in 2024) to align with and support the Company's regional structure and further strengthen the Company's commitment to safety. *Id.* at 30-31.

Ms. Britto also explained how the Company proposes to address its current and future staffing needs given the demographics of the Company's existing workforce. She acknowledged that the Company is no exception to the challenge faced by water utilities across the country with the inevitable loss of significant knowledge and expertise over the next 5 to 10 years due to retirements. Pet. Ex. 4 at 34. Ms. Britto testified that currently 28% of the front-line employees at Indiana American are over the age of 55, and 16% of the front-line employees are over 60 years of age. She explained these tenured employees have familiarity with the Company's operations, processes and the local knowledge of the Company's systems, and many have the necessary licenses required by state and federal regulations. Supplementing the loss of a retiree cannot be

achieved simply by filling a vacancy as the freshman class of front-line employees do not come with a wealth of knowledge of the water and wastewater industry. *Id.* at 33-34. 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 the applicable exams. Pet. Ex. 4 at 34.

ii. <u>OUCC</u>. OUCC witness Malan testified that the OUCC does not accept Petitioner's increase to salaries and wages expense. Pub. Ex. 4 at 4. Mr. Malan 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. *Id.* Mr. Malan testified that a level of positions have historically remained vacant for INAWC. *Id.* He pointed out that INAWC did not have full employment through the base period or the verifiable link period. Mr. Malan also made the point that ratepayers should not have to bear the cost of an expense that Petitioner is not likely to incur. *Id.*

For salaries and wages expense, 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 does not accept Petitioner's proposed increase to salaries and wages expense, due to the historic vacancies as stated. *Id.* 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 had requested. *Id.*

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 all years 2013-2022 to arrive at an average vacancy rate of 3.66%. *Id*. at 5-6. Mr. Malan 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. Mr. Malan's adjustments include the reasonable reduction for the average vacancy rate of 3.66%. *Id.* at 5-6.

For payroll taxes, Mr. Malan recommends a Step 1 increase of $214,379 to base period payroll taxes expense of $1,326,838 yielding Step 1 *pro forma* payroll taxes expense of $1,541,217, which is $39,218 less than that proposed by Petitioner. He further recommends a Step 2 increase of $92,916 to Step 1 *pro forma* payroll taxes expense of $1,541,217 yielding Step 2 *pro forma* payroll taxes expense of $1,634,133, which is $23,276 less than that proposed by Petitioner. Mr. Malan's payroll taxes adjustments include the reduction for historic vacant positions of 3.66%. *Id.* at 8-9.

For group insurance, Mr. Malan testified that in conjunction with the reduction to salaries and wages expense proposed in his testimony, a corresponding reduction to group insurance expense is also necessary to adjust for the historic vacant positions at the calculated rate. *Id*. at 10-11.

Mr. Malan testified OUCC recommends a Step 1 increase of $798,030 to base period group insurance expense of $3,809,310 yielding Step 1 *pro forma* group insurance expense of $4,607,340. He also states the OUCC recommends a Step 2 increase of $242,755 to Step 1 *pro forma* group insurance expense of $4,607,340 yielding Step 2 *pro forma* group insurance expense of $4,850,095. *Id*.

iii. 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 the Company'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 the Company. He stated failing to make an adjustment for employee attrition as the Company proposes, will result in customer rates that include excessive labor costs. IG Ex. 1 at 36. 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. *Id.* at 36-37. Mr. Gorman proposed an adjustment of 16% for employee attrition spread over the rate increase period. IG Ex. 1 at 37 and Attachment MPG-6. He did not make an adjustment to overtime expense ($1.9 million in the base period), stating these expenses (along with the increases in overtime expense proposed by INAWC) can be used by the Company for any required overtime it may need as employees retire. IG Ex. 1 at 38.

iv. INAWC Rebuttal. Ms. Britto acknowledged on rebuttal that it is reasonable to assume that from time to time 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 and comparing 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. Pet. Ex. 17 at 21.

With respect to Mr. Gorman's proposed reduction based upon a 16% attrition rate spread equally over Steps 1 and 2, Ms. Britto responded that the adjustment is speculative and not grounded in any evidence that the number of employees who are eligible to retire will in fact retire during the test year. *Id.* at 22. Ms. Britto further testified there is also no evidence that an employee who actually retires will leave a position open that will remain unfilled. *Id.* Further, Ms. Britto pointed out that Mr. Gorman's position is not supported by the facts in her rebuttal

demonstrating that Indiana American has hired above the level of employees assumed in its rate cases during the last 10 years (2013-2022). *Id.*

In response to Mr. Gorman's criticism that the Company 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. *Id.* at 22. She stated a large part of overtime work includes emergency call out service work and W5 operators that need to be on site 24/7, which will continue to be performed and cannot be replaced by the FTEs proposed in this case. *Id.*

v. Discussion and Findings. No parties disputed Petitioner's proposed new positions. All parties seem to agree that it is reasonable to assume a certain level of vacancies within Petitioner's forecasted headcount. We find the OUCC's proposed adjustments to be compelling and supported by historical, empirical data. We, therefore, accept the OUCC's proposed adjustments as set forth above.

B. Other Benefits Expense.

i. INAWC Case-in-Chief. In Step 1 Petitioner proposed a $30,071 increase to 401(k) expense, a $270,441 increase to defined contribution plan (DCP) expense, a reduction of $7,156 to employee stock purchase plan expense (ESPP), a $21,499 increase to Voluntary Employee Benefits Association (VEBA) 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 DCP expense, a $14,301 increase to ESPP expense, a $9,820 increase to VEBA expense, a $97 decrease to existing positions, and a $118,633 decrease to new positions. Pet. Ex. 8 at 11-12.

ii. OUCC. Mr. Malan testified the OUCC recommends a Step 1 increase of $391,792 to base period other benefits expense of $1,290,321 yielding Step 1 *pro forma* other benefits expense of $1,682,113 and a Step 2 increase of $66,575 to Step 1 *pro forma* other benefits expense of $1,682,113 yielding Step 2 *pro forma* other benefits expense of $1,748,688. Pub. Ex. 4 at 11-17.

The OUCC did not accept Petitioner's Step 1 and Step 2 adjustments for new employee 401(k) and ESPP expense. OUCC witness Malan testified that Petitioner overstated its new employee 401(k) expense by assuming a 100% participation rate. Pub. Ex. 4 at 15. Mr. Malan testified Petitioner's five-year average 401(k) participation rate is 86%. *Id.* 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%. *Id.* at 16. 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. *Id.* at 17.

iii. INAWC Rebuttal. Ms. Grisham responded to OUCC witness Malan's arguments that the Company's 401(k) and ESPP programs are not fully enrolled, acknowledging that it is correct they are not, but rejecting Mr. Malan's proposed five-year average participation rate. Pet. Ex. 20 at 4. She explained that rather than assuming a participation rate, the Company'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. *Id.* at 4. Ms. Grisham pointed out that Mr. Malan's use of the 5-year average participation rate for 401(k) participation ignores the fact that participation rates over the past five years have been increasing as the number of pension-eligible employees decreases. *Id.* at 5. She presented actual annual participation rates for the Company's 401(k) for the most recent three years, which is higher than the 5-year average of 86%.

iv. Discussion and Findings. With respect to the OUCC's proposed reductions to other benefits expense, we find that historic participation rates are relevant and provide objective evidence that demonstrates the level of adjustment that is fixed, known, and measurable for the other benefits expenses. Accordingly, we find that the evidence in this case supports OUCC's adjustments for other benefits expense and Petitioner's adjustments should be denied.

C. Support Services Expense.

i. INAWC Case-in-Chief. The Company proposed forecasted total support services expense of $27,411,536 in Step One and $28,657,034 in Step Two in this Cause. Indiana American witness 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. Pet. Ex. 8 at 15.

ii. OUCC. OUCC witness Margaret Stull testified that Indiana American proposes forecasted total support services expense of $27,411,536 in Step One and $28,657,034 in Step Two, which is a 44.44% increase over the revenue requirement established in Cause No. Cause No. 45142. Ms. Stull accepted Indiana American's forecasted adjustments to support services expenses, but she also proposed her own adjustment to remove all business development department costs, which Indiana American forecasted to be $241,552 in Step One and $251,285 in Step Two. Ms. Stull explained she made this recommendation for the same reasons the Commission gave in Cause No. 44022, when it found "no evidence that the business development activities provide a benefit to ratepayers" and further expressed concern that "ratepayers may be subsidizing business development with limited offsetting benefits." (Commission Order, Cause No. 44022, page 70.) Ms. Stull eliminated from the OUCC's proposed revenue requirement all operating expenses for the business development department. (Ms. Stull showed her calculation of this adjustment for water service in her OUCC 2 Schedule 6W, Adjustment No. 5 and for wastewater services in OUCC Schedule 6S, Adjustment No. 5. Pub. Ex. 3 at 29-30.

iii. INAWC Rebuttal. Ms. Grisham testified she disagreed with Ms. Stull's recommended adjustment to remove business development costs from support services expense. Pet. Ex. 20 at 7. Ms. Grisham asserted that Witness Stull's stated reason for removal of Business Development costs is that in Cause No. 44022, the Commission found no evidence that the business development activities provide a benefit to ratepayers and argued that the evidentiary record in Cause No. 44022 does not control the Commission in this proceeding and testified that Business Development does more in communities than facilitate acquisitions. *Id*. at 7-8. Ms. Grisham testified that American Water's Business Development activities help the Company build relations with community businesses and leaders and also help benefit customers of Indiana American, directly and indirectly, by mitigating the costs to be recovered per customer, enhancing purchasing power, and spurring activities that contribute to their local economies. *Id*. at 8.

Ms. Grisham stated that business development activities which grow Petitioner's customer base, enable the Company to spread system investment costs and operating expenses across a larger customer group, thereby mitigating the costs to be recovered per customer. *Id*. She argued that despite the Company's operating expenses increasing by approximately $9 million over the 10 year period 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. *Id*. Ms. Grisham asserted that the Company's Business Development activities also benefit many of the communities served by the Company and, for example, needed investment allowed a soft sewer ban to be lifted in Sheridan, allowing growth in the community which had been stifled by lack of treatment capacity. *Id*. at 8-9. Ms. Grisham also testified that planning efficient uses and development of new sources of supply benefit drinking water customers in a similar way, and that through the improvements in the operations of the wastewater and water utilities that the Company acquires, business development activities achieve public policy objectives of improving the quality of the water consumed by customers and the quality of the public bodies of water into which wastewater effluent is discharged.

iv. Discussion and Findings. The OUCC accepted Indiana American's forecasted adjustments to support services expenses but removed all business development department costs from the expense totals. Pub. Ex. 3 at 29. In support of its recommendation, the OUCC's Ms. Stull explained she was recommending disallowance of those costs for the same reasons we relied upon in our order in *Indiana-American Water Co*., Cause No. 44022, 2012 WL 2154248, (IURC 6/6/2012) to wit, we found there was no evidence that the

business development activities provided a benefit to ratepayers. We make a similar finding here.[34]

Petitioner asserts we should find there is evidence that its "business development activities" are providing a benefit to Indiana American's rate payers without actually explaining how its business development activities accomplish this or describing what its business development activities actually comprise. Rather, Petitioner claims lowered per customer operating expenses and other costs without tying those results to any activities of its business development department. In this manner, Petitioner seems to be confusing achieving economies of scale through natural synergies with customer benefits shown to be secured through its business development department. The achievement of economies of scale may be indicates through isolated and discrete examples, but as to what the business development department has actually achieved and how it functions, the evidence is lacking.

The only function of the business development department that was clearly identified by Petitioner was the acquisition of other utilities. But we cannot assume that acquisitions are necessarily a benefit to Indiana American's customer base. IC 8-1-30.3-5, under which Indiana American secures favorable ratemaking treatment on its acquisitions, acknowledges that these acquisitions may result in some, albeit statutorily acceptable, level of rate subsidization by Indiana American's ratepayers.

Finally, in support of allowing its business development activities in rates, Ms. Grisham testified that American Water's Business Development activities help the Company build relations with community businesses and leaders. Grisham rebuttal, p. 8. This explanation of the business development department's function equates to image building, which is not a proper cost to allocate to ratepayers.

We find the evidence presented in this case does not support introducing the cost of Indiana American's business development activities into customers' rates.

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

i. <u>INAWC Case-in-Chief</u>. Ms. Britto testified that the Company continues to see a significant increase in Indiana 811 notices to locate and mark its facilities since the Company's last general rate case (Cause No. 45142) and projects this trend will continue through the test year in this Cause. She presented the Company's projected volume of notices to locate and mark its facilities based on the average increase in notices from 2020 to 2022. Pet. Ex. 4 at 32. She explained that non-essential frontline service work was deferred from

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[34] Petitioner suggests Ms. Stull asks us to rely on evidence presented in Cause No. 44022. Ms. Grisham asserted that Witness Stull's stated reason for removal of Business Development costs is that in Cause No. 44022, the Commission found no evidence that the business development activities provide a benefit to ratepayers and argued that the evidentiary record in Cause No. 44022 does not control the Commission in this proceeding. This is a misreading of Ms. Stull's testimony, wherein she said she was recommending removal of all business development department costs "[f]or the same reasons the Commission stated in Cause No. 44022, the at 29-30. Citing Commission Final Order in Cause No. 44022, page 70.) Ms. Stull merely indicated we should apply the Commission's reasoning in that case to the facts of this case. Commission 'found no evidence that the business development activities provide a benefit to ratepayers.'" Pub. Ex. 3

March 2020 through December 2021 to help protect the safety of employees and customers during the pandemic and, consequently, the Company did not contract out work such as locates during this time. *Id.* 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, the Company 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 in order to stay current with the 811 work demands. *Id.* She stated the Company is proposing to address the continued increasing demand to locate and mark its facilities in this Cause by utilizing contractors to do most of this work across the state. The proposed increase in contract services expense in this Cause (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 the Company to locate and mark its facilities. Ms. Britto stated that shifting to contractors for line locates will limit the number of new hires included in this Cause to address this work. *Id.* Ms. Britto testified that using contract labor to locate and mark our facilities and repurposing our employees back to maintenance activities will allow for building a more robust team of employees that can focus on the critical, yet fundamental, elements of adequately operating a water distribution system. *Id.* at 33.

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 .23% was then applied through the end of the future test year. Pet. Ex. 8 at 17; Pet. Ex. 13, OPER Schedule OM11.

ii. 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. Pub. Ex. 4 at 19-20. Mr. Malan testified that Petitioner did not incur any base period expense for contracted line locates nor any time since. He stated Petitioner made no effort to outsource line locates since Petitioner's self-imposed deferral of non-essential frontline service work had ended in December of 2021. *Id.* at 20. Mr. Malan stated that there is no assurance the funds will be used for the intended purpose. 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. *Id.* Mr. Malan states that Petitioner was the only party in control of the funds received through rates and further 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 the proposed adjustment in this case. He stated it is unclear from INAWC's testimony and supporting schedules 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. *Id.* Accordingly, Mr. Malan recommended the Commission reject the adjustment for contract services line locates. *Id.* at 21.

In addition, OUCC witness Seals testified that the number of Petitioner's service orders show a decreasing trend. Pub. Ex. 10 at 8-9. Further, Mr. Seals testified that the transition to 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. *Id.* at 9-10. The combination of decreased service orders and decreased meter reads would free INAWC staff to complete additional tasks, including line locates, that would foster a reduced need for contract services, which is not otherwise subject to adjustment.

iii. <u>Industrial Group</u>. Mr. Gorman proposed to cap the Company's projected levels of contractor expenses at its Step 1 request, because he said the Company has not proven the projected number of line locates it proposes to outsource is reasonable nor that it will actually incur its projected cost. IG Ex. 1 at 9. Mr. Gorman took issue with the Company's forecast of an increase in line locates in excess of the historical increase and said the Company 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. *Id.* at 32. He noted that Petitioner did not use previously requested funds in the prior rate case (Cause No. 45142) on contractors for line locates. *Id.* at 33. He recommended the contractor expense tied to outsourcing line locates be capped at the 2024 increase, which would allow the Company to increase contractor expense by $3.9 million for line locates. He opined that capping these costs achieves a balance of the Company's desire to outsource line locates in order to reduce the workload on internal employees while protecting ratepayers from cost increases he says the Company is unlikely to incur in the rate effective period. *Id.* at 34.

iv. <u>INAWC Rebuttal</u>. Ms. Britto responded in rebuttal to Mr. Malan's and Mr. Gorman's testimony citing to the last rate case where the Company indicated it required additional contract services to complete line locate requests but did not employ outside vendors to perform line locates. She explained that the COVID pandemic commenced shortly after the last rate case and as a result non-essential frontline service work was deferred. Pet. Ex. 17 at 24. During the pandemic, Ms. Britto explained existing staff could be redeployed from completing customer service orders and other maintenance activities in order to remain current with the locate work demands. *Id.* at 25. She testified the Company is no longer operating in the same conditions, and conditions existing during the pandemic do not serve as a reasonable basis to doubt that the Company will use contract labor to complete the forecasted line locates. *Id.* at 25. She noted that OUCC witness Malan 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. *Id.* at 24. She responded to Mr. Gorman's dispute of the forecasted growth in locates by explaining that Indiana American had actually reduced the projection from the 8% increase seen in 2021-2022 to project a 6% increase in line locates. *Id.* 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 the Company short of recovery for costs it expects to incur while rates are in effect. She stated Mr. Gorman's use of a 7-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. *Id.* at 25.

v. Discussion and Findings. In its last rate case, Petitioner had received approval for $507,528 for additional contract service for contracted line locates, however, the evidence establishes that no locates were performed by outside vendors, and that the portion of the expense adjustment in that case for contracted line locates was neither needed, nor used by INAWC. We recognize the impact resulting from the COVID-19 pandemic, however, INAWC has not sufficiently explained its delays since those impacts were alleviated, even with its response to our Docket Entry questions dated August 17, 2023, in which we invited INAWC to fully explain the lack of any use of funds for contracted line locates. We cannot now determine that the adjustment for contracted line locates is reasonable or necessary. Given the absence of any expense in the base year or link period, and given the specific request in the last rate case for a need that was not met, we find there is not a sufficient basis in the evidence to determine that this expense is necessary. Or would be considered fixed, known, and measurable. We, therefore, find that the evidence in this case does not support Petitioner's proposed adjustment.

E. Inflation/Annualization.

i. INAWC Case-in-Chief. Mr. Cifuentes described the methodology the Company used to calculate those *pro forma* expense levels that are based on an inflation factor for the verifiable link period and then trended through the future test year. Pet. Ex. 9 at 3-4. He said the Company used unique and specific inflation factors developed for each O&M category that aligns with the United States (U.S.) Bureau of Labor Statistics ("BLS") by specific measure category and type of cost to recognize the impact of inflation on the Company's expenses for the verifiable link period and through the future test year. *Id.* at 4. Petitioner also proposed to annualize or normalize the inflation adjustment for 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. *See* Pub. Ex. 5 at 13.

ii. OUCC. OUCC Witness Jason Compton did not accept Petitioner's methodology for annualizing or normalizing building maintenance & supplies expense, employee related expenses, maintenance supplies & services expense, miscellaneous expense, office supplies and services, postage, printing & stationary, and telecommunication expense. More specifically, Mr. Compton did not agree 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 said that method should be rejected and the resulting adjustment denied. [35] Mr. Compton asserted that by adjusting for

[35] With respect to building maintenance & supplies, maintenance supplies & services, office supplies & services, postage, printing, & stationary, and telecommunication expense, Mr. Compton testified that except for the adjustment for annualization, the underlying adjustments should be approved.

inflation and then annualizing the expense based on the year-end's inflationary adjusted expense, Petitioner double counted inflation in Step 1. Duplicating the effect of inflation will not adjust forecasts to a "more predictive level."[36] Public's Ex. 5 at 13-14.

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 in this case has the effect of double counting inflation.[37] Mr. Compton explained that by annualizing data that does not need to be annualized and double counting inflationary factors, Petitioner overstated the amount of expense INAWC is likely to incur. Mr. Compton testified Petitioner's annualization adjustment should be removed from each Step One expense projection for each respective expense account.

iii. <u>Industrial Group</u>. 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). IG Ex. 1 at 21. He expressed this is particularly a concern because 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. *Id*. He recommended adjusting the forecasted test year O&M expense to reflect inflation outlooks from the historical base period through the forecasted test year, and rejected the Company's assumption that the inflation rates that took place over the three-year period ending September, 2022, will be repeated over what the Company calls the "Link Period" through the close of the forecasted test year. Mr. Gorman testified that this effectively lowers the inflation rate used by the Company from 5.05% to 2.97%. Adopting Mr. Gorman's suggestion and changing the various inflation factors that INAWC uses to the consensus economists' forecasts for future inflation would lower the Company's claimed revenue deficiency by approximately $698,000 for water and $30,000 for wastewater. *Id.* at 23.

iv. <u>INAWC Rebuttal</u>. Mr. Cifuentes responded to Mr. Compton's recommendation to remove annualization for the identified O&M expenses. He explained that the Company has taken the forecasted level of expense in the month before the anticipated Order date (December 2023) and multiplied by twelve to annualize that month. *Id.* He 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 bases the Step 1 level of these expenses on the projected levels for calendar year 2023, thereby failing to reflect the inflation projected to occur during most of 2023 and understating the level projected to be occurring at the anticipated date of the Order. Pet. Ex. 21 at 4.

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[36] Mr. Compton noted that Petitioner claims it conducted the annualization because it adjusts the forecasted expenses to a "more predictive level." (Petitioner's 10 Response to OUCC data request 33-29, OUCC Attachment JTC-4.) Mr. Compton explained, however, that Petitioner had already adjusted for future predictive levels by adjusting its base year expenses for inflation in future steps.

[37] Mr. Compton testified that 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.

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 twelve (12), which represents twelve 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. Pet. Ex. 21 at 4.

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. Pet. Ex. 21 at 8. He explained that accuracy is enhanced when specific inflationary rates are applied to each category of expenses when available and that Mr. Gorman's proposal would use one across the board rate of 2.97% which is an average of the general CPI forecasted to occur from 2022 through 2024, or a general inflationary factor. *Id.* at 9. Mr. Cifuentes stated this rate does not contemplate for, adjust, or target each expense category presented in this Cause. *Id.*

v. Discussion and Findings. Petitioner asserted in its proposed order that "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" and that annualizing these amounts based on the last month in 2023 is necessary to capture the full effect of inflation. This is simply not accurate. Petitioner's workpapers filed with its case-in-chief show that Petitioner's 2023 calendar year expenses are projections based on a level of inflation. INAWC's Financial Exhibit OM25 Maintenance Supplies & Services Expense, for instance, shows that Petitioner calculated an inflation factor for the expense and projected the expense from October 31, 2022 through April 30, 2025.

The issue is whether Petitioner's adjustment is consistent with the test year methodology it has chosen for its Step 1 period rates. Petitioner's methodology for its Step 1 proposal is essentially the methodology used to make adjustments to historic test year expenses. However, 2023, which Petitioner used to calculate its Step 1 revenue requirement, is not a historic test year. Instead, for purposes of Step 1, 2023 is essentially a forward-looking test period as the expenses calculated in 2023 are not actual expenses, but projections. As such, it is inappropriate to use the annualization adjustment methodology used for historic test years for its future test year adjustment calculation for Step 1. Petitioner's case-in-chief workpapers show that Petitioner has not followed an annualization methodology appropriate for use with projected data. Moreover, it has not followed the methodology it declared in its case for Step 1. Through the testimony of Mr. Greg Shimansky, Petitioner indicated in its case-in-chief that its Step 1 increase was to be based on the twelve months ending December 31, 2023:

> The first step will also incorporate the annualized level of revenues, uncollectible expense, operating and maintenance expenses, amortizations and taxes projected in a portion of the link period through December 31, 2023.
>
> Pet. Ex. 2, p. 9, lines 1-3.

As Mr. Compton explained, Petitioner did not follow that method but instead used the last month in 2023 as the only factor to annualize each expense. To be consistent with its stated methodology, Petitioner should have added the 12 months leading up to and through December 31, 2023. As the only difference between each month projected in the linking period was the amount of inflation attributed, Petitioner's use of only the last month had the effect of overstating the amount of inflation that should be used to calculate Petitioner's revenue requirement for those expenses.

For these reasons we reject Petitioner's annualization adjustment for these expense items.[38]

F. Miscellaneous Expense.

i. INAWC Case-in-Chief. 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 One 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 Two expenditures. Pet. Ex. 9 at 14, Pet. Ex. 13 and 14, OPER Schedule OM18.

ii. OUCC. 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 One expenditures. Mr. Compton explained that Petitioner proposes the same adjustments for Step Two expenditures as it did in Step One; 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 (Response to OUCC DR 33-20, OUCC Attachment JTC-5). Mr. Compton explained that this expense is of no benefit to ratepayers and cannot be attributed to providing safe and reliable water to customers; therefore, it 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 and not sufficiently related to providing utility service. He noted a pamphlet Petitioner provided in response to discovery indicating "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." (Response to OUCC DR 33-20, OUCC Attachment JTC-5.) Mr. Compton testified that as the program can be funded by the charitable foundation, it should be treated as such and

[38] Building Maintenance & Supplies Expense, Employee Related Expenses, Maintenance Supplies & Services Expense, Miscellaneous Expense, Office Supplies and Services, Postage, Printing & Stationary, and Telecommunication Expense.

therefore should not be treated as a recoverable expense. Lastly, rather than removing from the base year only a portion of the 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 ratepayers and therefore should not be included in rates. 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 One 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 Two expenditures.

iii. <u>INAWC Rebuttal</u>. Mr. Shimansky noted in his rebuttal that Petitioner accepted the OUCC's position that Indiana Pacers tickets should be removed. However, Mr. Shimansky explained that the Company is not resubmitting the Revenue Requirement and Rates at this time because Petitioner believed these changes to be immaterial and incorporating them should not materially change Petitioner's position from that presented in its case-in-chief. Pet. Ex. 15 at 65.

INAWC witness Cifuentes explained that 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 INAWC customers. Pet. Ex. 21 at 5. He explained that 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. *Id.* 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. *Id.* at 6.

Mr. Cifuentes disagreed with OUCC witness Compton that all NAWC activities benefit the interest of shareholders rather than customers. He asserted 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. INAWC's utilization of tools offered by its NAWC membership benefit INAWC customers through professional development for INAWC employees, which provides more efficient and effective service through knowledge of the latest trends and techniques. Pet. Ex. 21 at 6.

iv. <u>Discussion and Findings</u>. While Petitioner's witness Mr. Shimansky agreed with the OUCC that Petitioner's expense of Indiana Pacers tickets should be removed miscellaneous expense, he explained the Company is not resubmitting the Revenue Requirement and Rates at this juncture because doing so should not materially change Petitioner's position from that presented in its case-in-chief. Pet. Ex. 15 at 65. Thus, Petitioner acknowledged it should not have included courtside Indiana Pacer tickets in its revenue requirement. Whether the expenses are material or immaterial to the case plays no role in its

exclusion from the revenue requirement. While correcting the failure to remove this expense from Petitioner's base period and its revenue requirement may not have a significant reduction in rates, it is an exercise we insist should be done. Ratepayers should not be required to bear that cost no matter how insignificant its effects may be on rates. Indiana ratepayers require assurances that the rates they pay are only for expenses reasonably necessary for the treatment, production, transmission, distribution, and sale to them of water and wastewater service. The Indiana Administrative Code (170 IAC 6-2-2(a)) requires Class A utilities to follow the guidance set forth by the National Association of Utility Regulatory Commissions' ("NARUC") Uniform System of Accounts ("USoA"):

> Sec. 2. (a) The rules governing the classification of accounts for Classes A, B, and C water utilities operating within the state of Indiana shall be the 1996 edition of the Uniform System of Accounts as approved, prescribed, and promulgated by the National Association of Regulatory Utility Commissioners, which:
>
> (1) are hereby incorporated into this rule by reference; and
>
> (2) do not include any later amendments or editions.
>
> (b) Copies of the 1996 edition of the Uniform System of Accounts prescribed for Classes A, B, and C water utilities, as approved, prescribed, and promulgated by the National Association of Regulatory Utility Commissioners are available for purchase from the National Association of Regulatory Commissioners, 1101 Vermont Avenue NW, Suite 200, Washington, D.C. 20005.

Furthermore, although Mr. Cifuentes explains how the Environmental Grant Program Petitioner participates in and funds how benefits to a small subset of its customers, Mr. Compton is correct in his assertion that the program is charitable in nature and for the purposes of building Petitioner's image in its communities. The pamphlet Mr. Compton included in his testimony as provided by Petitioner indicates that the program can be funded by the American Water Works' charitable foundation. Ultimately, this coincides with Mr. Compton's description of the program. That the program can be funded by a charitable organization indicates the program functions as a charity. Expenses identified as charitable contributions are considered non-recoverable expenses and should not be included in the revenue requirement of the requesting utility. Charitable contributions by the company are a below the line expenditure to be paid for by the company's shareholders and not the Company's customers.

With respect to Petitioner's $188,932.91 NAWC expense, Mr. Compton asserted NAWC's activities substantially benefit shareholders rather than ratepayers, and therefore, they should not be an expense included in the revenue requirement and ultimately billed to ratepayers. Mr. Cifuentes countered Mr. Compton's testimony indicating the opposite, stating that NAWC is a forum for utilities to communicate and share knowledge and information that helps participating utilities provide a more efficient and effective service. However, Mr. Cifuentes failed to provide any specific evidence or examples of such activities in neither his case-in-chief or rebuttal testimonies. In fact, while Mr. Cifuentes was perfectly capable of providing real

examples of how a $8,900 Environmental Grant Program was beneficial to ratepayers[39], Mr. Cifuentes did not provide any specific examples of a collaborative benefit of the $188,932.91 NAWC expense. Through discovery, Petitioner was asked to identify the benefits ratepayers receive from its participation in NAWC (OUCC DR 33-19 b. and OUCC DR-58-2) and list instances where Petitioner acquired knowledge or practices from its membership in NAWC that it otherwise would not have without it (OUCC DR-58-3). (OUCC CX Exhibit-2.) Petitioner provided no such examples or instances repeating the vague assertion that "The Customers benefit from this organization through professional development it offers to the employees servicing the Indiana communities as well as more efficient and effective service through knowledge of latest trends and techniques." (OUCC CX Exhibit-2.) Hr. Tr., B-3 – B11. It is not disputed that the National Association of Water Companies engages in lobbying, which is not a recoverable above the line expense. As such, it behooved Petitioner to provide examples that support its contention that the organization provides direct or indirect benefits to Indiana American's customers. When asked through discovery, Mr. Cifuentes and Indiana American did not do so. As such, Petitioner failed to establish that its NAWC membership expense should be included in rates as an above the line expense.

For the above reasons, we accept Mr. Compton's proposed adjustments to remove the Environmental Grant Program and NAWC expenses from Petitioner's revenue requirement. We also order Petitioner to update its schedules to include the removal of the Indiana Pacer tickets of which Petitioner has already accepted Mr. Compton's proposal.

G. Transportation Expense.

i. INAWC Case-in-Chief. Petitioner proposed an overall $118,812 increase to base year transportation expense of $1,224,928 yielding *pro forma* transportation expense of $1,343,740 for Step One expenditures. For Step Two expenditures, Petitioner proposed an overall $173,790 increase to base year transportation expense to yield a *pro forma* of $1,398,718. Petitioner's made adjustments to the base year transportation expense including an increase of $13,986 for Holman/ARI charges for going level vehicles, an increase of $16,418 for inflated miscellaneous transportation purchases, an increase of $3,957 for inflated employee business mileage reimbursement, an increase of $5,903 for inflated salvage value reclass, a decrease of $186 for capitalization, and an increase of $78,733 for an accrual offset for Step One expenditures. Petitioner proposed the same adjustments for Step Two expenditures as it did in Step One. However, Petitioner proposed an increase in base year expenditures for Holman/ARI charges of $89,629, inflated miscellaneous transportation purchases of $27,897, inflated employee business mileage reimbursement of $6,876, inflated salvage value reclass of $10,259, and the same increase for an accrual offset. Petitioner also proposed a decrease in base year expenditures for capitalization of $39,604.

ii. OUCC. OUCC Witness Jason Compton did not accept the Company's proposed *pro forma* level of transportation expense because he disagreed with including salvage value. Mr. Compton explained that salvage value is not a transportation expense and therefore adjustments for inflation should not be attributed to transportation expense. Mr. Compton noted that the NARUC Uniform System of Accounts for Class A Water

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[39] Cifuentes Rebuttal Pg 6. Lines 1-11

Utilities instructs that "At the time of retirement of depreciable utility plant, this account shall be charged with the book cost of the property retired and the cost of removal and shall be credited with the salvage value and any other amounts recovered, such as insurance."[40] Mr. Compton testified that, therefore, salvage value should be accounted for through accumulated depreciation and not as a transportation expense. Mr. Compton recommended that all salvage value reclass be removed from base year transportation expense of $99,421 because salvage value is not an expense which should be attributed to transportation and instead should be accounted for through accumulated depreciation. Mr. Compton recommended an increase of $13,487 to base year transportation expense of $1,224,928, resulting in a *pro forma* transportation expense of $1,238,415 for Step One expenditures. Mr. Compton recommend an increase of $64,110 to base year transportation expense resulting in a *pro forma* miscellaneous expense of $1,289,038 for Step Two expenditures. Pub. Ex. 5 at 21.

iii. <u>INAWC Rebuttal</u>. INAWC witness Cifuentes responded to Mr. Compton's testimony 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. Pet. Ex. 21 at 7.

iv. <u>Discussion and Findings</u>. Mr. Cifuentes did not adequately explain why the credit must be reclassified to properly reflect transportation expense. The NARUC instruction Mr. Compton quoted is applicable. Mr. Cifuentes refers to the credit as salvage value throughout his Excel documents in his case-in-chief, and he acknowledges the credit is for salvage value in his rebuttal. In addition, Mr. Cifuentes position as stated in his rebuttal would create an illogical result as it would have the effect of salvage value, which accrues to the benefit of the Company, ultimately increasing operating expenses for ratemaking purposes. As such, we accept Mr. Compton's recommendation to remove $99,421 of salvage value from Transportation Expense and netted against accumulated depreciation.

H. <u>Bad Debt Expense</u>.

i. <u>INAWC Case-in-Chief</u>. INAWC proposed *pro forma* bad debt expense in its initial case in chief of $2,888,841 as shown on INAWC Financial Exhibits OPER Schedule OM21 within the INAWC 2023 Rate Case INAWC 2023 Rate Case – Uncollectibles file in Pet. Ex. 13 and Pet. Ex. 14.

ii. <u>OUCC</u>. Ms. Sullivan proposed a bad debt expense adjustment to base year bad debt expense of $2,118,534 yielding *pro forma* bad debt expense of $2,542,202 after applying Petitioner's proposed bad debt rate of 0.9062% to the OUCC's recommended *pro forma* operating revenue of $280,528,047. Pub. Ex. 2 at 23-24.

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[40] NARUC Uniform System of Accounts for Class A Water Utilities, Balance Sheet Accounts, Account 108.1. Accumulated Depreciation of Utility Plant Service, Part B.

iii. Discussion and Findings. There is no dispute between the parties as to the appropriate bad debt ratio to use in calculating the bad debt adjustment, only in the appropriate level of revenues to which the percentage should be applied. We find that the bad debt ratio of 0.9062% should be applied to the level of *pro forma* operating revenues at present rates found in this Order.

I. Credit Card Fees.

i. 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. INAWC witness 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. Pet. Ex. 2 at 35.

ii. OUCC. OUCC witness Jason Compton recommend the Commission deny Petitioner's proposal to recover in rates the $1,163,647 cost created by those customers who pay their monthly bill with a credit card or debit card. Mr. Compton argued that cost should not be socialized but should remain with the cost causer. It should not be the burden of all customers to pay the costs being generated by a subset of customers. Mr. Compton rejected the suggestion that customers will be saving money. He acknowledged that customers paying their bills with credit cards or debit cards will save money overall, the customers who don't pay their bill with a card will see an increase in their bills. Pub. Ex. 5 at 23-24. Mr. Compton also noted the lack of evidence to support Petitioner's argument that Petitioner's proposal will generate any value including, but not limited to, customer satisfaction, on-time payment, and disconnection avoidance. Mr. Compton suggested that any increase in timely collections that might result will accrue to the benefit of Petitioner 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 card 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. Mr. Compton concluded by stating his recommendation of denial is consistent with the Commission's order in Cause No. 45253, wherein a similar request was denied. Pub. Ex. 5 at 24.

iii. CAC. 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. CAC Ex. 1 at 42. He noted that payment by credit card is a popular payment method among consumers in Indiana. *Id.* at 42-43. He 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. *Id.* at 43. He recommended that the Commission approve Indiana American's proposal to remove the $1.95-per-transaction charge on credit card transactions. However, he also recommended that the Commission 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. *Id.* at 44.

iv. __INAWC Rebuttal__. In response to OUCC witness Compton's recommendation to deny Petitioner's proposal with respect to credit card fees, INAWC witness 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. Pet. Ex. 15 at 64. Mr. Shimansky demonstrated that the impact on other rates is relatively minor (0.3% of total Operating Revenues) in comparison to making it easier to pay bills. *Id.* 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 satisfaction with doing business with the Company, as does avoiding the incurrence of additional costs associated with mailing in payments or traveling to make in person payments. *Id.*

With respect to CAC witness Inskeep's recommendation that all fees associated with any payments of customer monthly bills should be removed, Mr. Shimansky responded that the Company has not done the analysis or determined the increase revenue requirement associated with removing such other fees. He testified that the Company is not opposed to doing an analysis and corresponding proposal in the next rate case if the Commission finds it necessary. Pet. Ex. 15 at 63.

v. __Discussion and Findings__. . Indiana American's customers who chose to pay their water or wastewater bills by credit card or debit card are responsible for paying a processing fee ultimately charged by the credit card companies and banks. Indiana American proposes to remove the cost of such payments from customers. Accordingly, Indiana American proposes a $1,163,647 *pro forma* revenue requirement shifting the cost of these transaction fees to all customers. Pet. Ex. 2 at 35-36. INAWC witness Shimansky testified that charging a credit card fee on top of the customer bill adds friction to the process of paying a bill and eliminating the direct payment of the transaction 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. Pet. Ex. 2 at 35.

The transaction fee is an example of a cost that can be and has been directly ascribed to the cost causer, which are those customers who elect to pay their bills by credit card or debit card. Consequently, subsidization by other customers is clearly the consequence of this change and should only be approved if there is a compelling reason. The OUCC opposed this change, while Intervenor CAC was in favor of it and suggested an elimination of fees that affect other customers. In our Order in Cause No. 45253, we rejected a similar proposal by Duke Energy Indiana to provide a fee-free payment option, finding that the proposal had not been shown to provide value to non-participating customers. *Duke Energy Indiana, Inc.* Cause No. 45253 (IURC 6/29/2020) at 106. Through Mr. Shimansky, Petitioner asserted there were benefits such as timelier payments by those customers who do use credit cards and the resulting lower uncollectible expense that results from more timely payments. Mr. Shimansky asserted these benefits would inure to all customers, not strictly those who use credit cards for their payments.

Through Mr. Compton's testimony, the OUCC rejected the suggestion that all customers will receive a net benefit from this change. Pub. Ex. 5 at 23-24. Mr. Compton noted the lack of evidence to support Petitioner's argument that Petitioner's proposal will generate any value. Indeed, Petitioner has not quantified the financial benefit of foregoing the transaction fee. Consequently, we are doubtful that the benefit to Petitioner's operations will exceed the more than $1 million dollar cost it proposes to collect from its customers through a higher rate. Mr. Compton also suggested that any increase in timely collections that might result will only accrue to the benefit of Petitioner. If Petitioner can expect to avoid any costs associated with avoiding late payments, encouraging earlier payments, or avoiding uncollectable expenses, Petitioner has not shown how this would actually result in a benefit its customers may enjoy. Petitioner has not made any other offsetting adjustment to rates, through a lower bad debt expense for instance. Petitioner's argument that there is a benefit to customers is illusory. Moreover, customers who may have been paying through methods other than credit card or debit card to avoid paying a transaction fee will no longer have any incentive to do so increasing the cost to Indiana American of providing this service. Such a higher operating cost would increase Indiana American's base year expenses in its next rate case. If, as Indiana American implies, it believes waiving these transaction fees will result in a net benefit in the form of decreasing its other operating expenses and improving its bottom line, it may elect to do so, but it should not be at any cost to its ratepayers. Based on the foregoing, we decline to approve Petitioner's proposed $1,163,647 *pro forma* revenue requirement.

J. <u>Rate Case Expense</u>.

i. <u>INAWC Case-in-Chief</u>. . INAWC forecasted $1,404,295 for rate case expense to be amortized in rates over 3 years, or $468,098 per year. See INAWC Financial Exhibits OPER Schedule OM23 within the INAWC 2023 Rate Case – Regulatory Expense file of Petitioner's Exhibit No. 13.

ii. <u>OUCC</u>. OUCC witness Sullivan testified that the OUCC does not oppose the rate case costs forecasted by the Company, but she disagreed with the total costs to be amortized as well as the amortization period to be used. Pub. Ex. 2 at 24. She explained that Petitioner was authorized to recover $1,941,165 in rate case costs in Cause No. 45142 amortized over three years but not removed from rates. She stated that 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. *Id.* 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. *Id.* at 25. She recommended the $1,404,295 of rate case costs forecasted in this case 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. *Id.*

Ms. Sullivan recommended a five-year amortization period should the Commission not accept her recommendation. She testified this period is more appropriate than the shorter three-year period proposed by Indiana American because the time between rate case filings has been approximately five years for the last three rate case filings. *Id.* at 25-26. Ms. Sullivan explained that INAWC has been able to extend the period between its rate case filings due to its use of DSIC and SEI trackers under I.C. ch. 8-1-31 and I.C. 8 ch. 8-1-31.7. Ms. Sullivan recommended that if the Commission orders a 3-year amortization of rate case expense, the Commission order rate case expense be removed by a tariff filing at the completion of the amortization period. *Id.* at 26.

iii. INAWC Rebuttal. Mr. Shimansky testified on rebuttal that he disagrees that rate case expense from Cause No. 45142 was over-collected. He recited the term of the settlement in the prior rate case related to annual regulatory expense. He explained 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 the Company, driven by reduced projected levels of expense associated with settling the case rather than fully litigating it. Pet. Ex. 15 at 42. 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. *Id.* 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. *Id.* at 43. During cross-examination, Mr. Shimansky reiterated multiple times that the regulatory account for rate case expense from Cause No. 45142 never reached a zero balance. Tr. at D-57, 58, 60-61.

iv. Discussion and Findings. In his rebuttal testimony, Mr. Shimansky testified that in the settlement in Cause No. 45142, the parties agreed to an annual regulatory expense amortization of $647,055, which included a $50,000 reduction to the annual forecast proposed by the Company, which was driven by reduced projected levels of expense associated with settling the case rather than fully litigating it. But in its proposed order, Petitioner asked us to find that there is no mention of (1) a total amount of rate expense, or (2) an amortization period of 3 years in the final order in Cause No. 45142 and "decline the invitation to modify the settlement or our Order approving it through the offset recommended by the OUCC in this case." Petitioner's proposed order, pp. 78 -79. While the Order in Cause No.45142 and the Stipulation and Settlement approved by that order does not explicitly state the amortization period or the amount being amortized, the fact that an annual regulatory expense amortization of $647,055 was included in rates was not only uncontested by the evidence in this case but was acknowledged by Petitioner's own accounting witness in his rebuttal testimony.

Mr. Shimansky argued in his rebuttal testimony that there was no agreement as to the time over which it would amortize rate case expense and that even if there had been, the parties included no term in the Settlement that required us to file new tariffs following the expiration of that amortization period. Mr. Shimansky asserted customers do not require rights in specific levels of expense that are included in a revenue requirement, and Ms. Sullivan's argument to offset current rate expense with her perceived "overcollection" of rate case expense in the past is retroactive ratemaking. In essence, Mr. Shimansky asserted that Ms. Sullivan advocated both a modification of the settlement agreement and retroactive ratemaking. We address these related issues one at a time.

We first address the suggestion that Ms. Sullivan is advocating for retroactive ratemaking. Importantly, the issue is what prospective level of rate case expense this order should authorize be recovered. Retroactive ratemaking is typically considered recovering a past cost through prospective rates. Further, the function of a test year and rate setting more generally is to establish a level of rates that will allow a utility to meet its prospective operating expenses and provide an opportunity for the utility to earn an authorized return. Any rate case expense Petitioner has experienced and seeks to recover has largely already been incurred. Furthermore, it is not a recurring expense. Affording amortized rate case expense is an accepted and well developed exception to the principle that a utility cannot recover a past expense through prospective rates.

It is an established practice that utilities have been permitted to amortize in rates the unamortized portion of rate case expense from the preceding rate case. Indiana American has itself benefited from this practice. During Cross-examination by the OUCC, Mr. Shimansky acknowledged that in Cause No. 42520 Indian American appears to have been permitted to recover unamortized rate case expense from the prior rate case. Hr. Tr. p. E-7, E-1 – E-7. Indiana American has been the beneficiary of this practice of addressing under-amortization of rate case expense, and it is only equitable to address over amortization of rate case expense in the same manner.

In seeking to address the over amortization in rate case expense in this case, Indiana American argued that the OUCC seeks a modification of the settlement agreement. Petitioner stated in its proposed order that "there is no indication in the Cause No. 45142 Order or the settlement attached thereto that anything other than an annual regulatory expense amortization amount was agreed upon[, and t]here is no mention of (1) a total amount of rate expense, or (2) an amortization period of 3 years." Petitioner's proposed order, p. 79. This does not dispense with the OUCC's position that over amortization of rate case expense can and should be addressed in this case. Nothing in the settlement or the final order in Cause No. 45124 prohibits the Commission in its next rate case addressing over collection or under collection of rate case expense as it has done in Cause No. 42520. We note that in our final order in Cause No. 42029, Indiana American's rate case prior to Cause No. 42520, we established an amortization period resulting in a *pro forma* regulatory expense, but we made no pronouncement in that case about whether unamortized rate case expense or over amortized rate case expense should be addressed in the next rate case. Order, Cause No. 42029, pp. 54-55 Yet we did precisely that, presumably accepting Indiana American's proposal to add the unamortized portion of rate case expense from Cause No. 42029 to the rate case expense for Cause No. 42520. (See Book 3 of 5 of the MSFR workpapers in Cause No. 42520 – Administrative Notice 2) Nothing in our final order in Cause No. 42520 reveals any controversy about that proposal.

We find that Petitioner's over amortization of rate case expense should be reflected in the amortization of rate case expense authorized in this case.

As to the amortization period in which the expense is to be collected, we agree with the OUCC that these costs should be recovered during Step 2 and then removed from Step 3 rates to avoid any future over collection of rate case costs. No rate case expense should be included in Step 1 rates.

K. COVID-19 Deferral.

i. INAWC Case-in-Chief. INAWC seeks recovery of $383,817 of COVID-19 related costs. Pet. Ex. 2 at 37, Pet. Ex. 13, Amortization Expense. INAWC witness 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 the Company on forgone Travel and Conference expenses. *Id.* at 39.

ii. OUCC. Ms. Stull testified that she accepted the basic methodology the Company used to calculate COVID-19 costs, but she disagreed with the Company's "conclusions." She testified that the methodology should include recognition of the line locate costs not incurred during the pandemic but recovered through rates. Pub. Ex. 3 at 26. Ms. Stull explained that in Petitioner's last rate case, Cause No. 45142, Indiana American was authorized $500,000 *pro forma* annual contract service expense to outsource a portion of its line locates. She explained that Petitioner's witness Kari C. Britto explained that "Non-essential frontline service work was deferred from March 2 2020 through December 2021 to help protect the safety of our employees and customers, consequently, we did not contract out work such as locates during the pandemic." (Britto Testimony, page 32.). Ms. Stull added that in response to discovery, INAWC 5 confirmed it did not outsource any line locates from 2016 through 2022 (OUCC 6 Attachment MAS-4). Thus, this cost avoidance is directly related to the pandemic. Ms. Stull calculated an avoided cost of $916,667. *Id.* at 27. As a result, she recommended a deferred COVID-19 regulatory *liability* of $532,850 (the Company's net regulatory asset of $383,817 reduced by avoided line locate costs of $916,667). *Id.* at 28.

Ms. Stull also disagreed with INAWC's proposal to amortize deferred COVID-19 costs over three years, arguing 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. *Id.* Ms. Stull recommended a deferred COVID-19 regulatory liability of $532,850 be amortized over a five-year period as a *reduction* of $106,570 to INAWC's annual total company operating expenses. *Id*.

iii. INAWC Rebuttal. Mr. Shimansky opposed Ms. Stull's recommendation on deferred COVID-19 cost recovery, noting that the Company voluntarily deferred avoided travel and conference expense savings when it was not required to do so. Pet. Ex. 15 at 39. He cited the Commission's June 29, 2020 Order in Cause No. 45380, which provided: "All jurisdictional Indiana utilities are authorized to use regulatory accounting for COVID-19 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-19 related uncollectible and incremental bad debt expense." *Id.* (citing Cause No. 45380 Order dated June 29, 2020 at 9-10.) 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 explained there is no deferred accounting authority for the avoided line locate expense. He acknowledged that there is no deferred accounting authority for the avoided transportation and

conference expense, and the Company would have been perfectly within its rights not to have offset those savings against the deferred expenses that were specifically authorized. *Id.*

With respect to Ms. Stull's proposal to lengthen the amortization period for the COVID-19 deferred costs to five years, Mr. Shimansky responded that the costs in this regulatory asset were paid for by the Company over a period of around 22 months and the Company is not asking to recover interest on these accounts. Pet. Ex. 15 at 33. Mr. Shimansky testified that to recover these costs over five years means the Company will be waiting almost nine years (COVID-19 expense began in June 2020 versus end of amortization period of January 2029) with no interest compensation. *Id.*

iv. <u>Discussion and Findings</u>. On June 29, 2020, this Commission issued an order in 45380 Phase 1[41] allowing "regulatory accounting for any impacts associated with any prohibition 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 to aid customers. Such regulatory accounting authority may include costs incurred beginning on March 6, 2020." *Id.* at 9-10. In that same order, we declined to approve the request for deferral of O&M costs, but found utilities could seek "cost recovery or other related rate relief at any time in the future through existing regulatory avenues, such as through the filing of a base rate case." *Id.* While we recognize that Petitioner deferred certain O&M savings as offsets to the costs authorized to be deferred under our 45380 Phase I Order, we decline the OUCC's invitation to retroactively impose requirements for additional offsets merely because Petitioner voluntarily included some offsets. We reject Ms. Stull's addition and authorize the Company's request to amortize $383,817 over three years, a figure that includes COVID-19 costs, bad debt expense and the wholly voluntary offset for travel and conference expenses not incurred. Moreover, we decline to order a longer amortization period for the COVID-19 costs, given the period over which the costs were incurred and the fact that Petitioner has not sought carrying charges with respect to the regulatory asset. We do, however, find it is appropriate that if the three-year amortization period expires before new On June 29, 2020, this Commission issued an order in 45380 Phase 1 allowing "regulatory accounting for any impacts associated with any prohibition 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 to aid customers. Such regulatory accounting authority may include costs incurred beginning on March 6, 2020." *Id.* at 9-10. In that same order, we declined to approve the request for deferral of O&M costs but found utilities could seek "cost recovery or other related rate relief at any time in the future through existing regulatory avenues, such as through the filing of a base rate case." *Id*

The regulatory accounting Petitioner seeks in this case is extraordinary relief, and when considering it we must be mindful of the factors involved and what the authorizing order intended to accomplish. Petitioner's position is based on the premise that we must only consider

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[41] Verified Jt. Pet. of Duke Energy Indiana, LLC, Indiana Gas Co. d/b/a Vectren Energy Delivery of Indiana, Inc., Indiana Michigan Power Co., Indiana Nat. Gas Corp., Indianapolis Power & Light Co., Midwest Nat. Gas Corp., N. Indiana Pub. Serv. Co., LLC, Ohio Valley Gas Corp. and Ohio Valley Gas, Inc., S. Indiana Gas & Electric Co. d/b/a Vectren Energy Delivery of Indiana, Inc., and Sycamore Gas Co., Cause No. 45377, 2020 WL 3630517 (IURC 6/29/2020).

cost increases to the utility without recognizing in rates any cost savings or offsets. But when we addressed deferral of Covid related expenses in our June 29, 2020 order in Cause No. 45380, we acknowledged that there could be offsetting savings, and those savings should be considered at some juncture:

> Without knowing the extent of the financial impact, it is difficult to balance the interests of the utility and its customers. And because deferred regulatory accounting carries with it a presumption of cost recovery, if reasonable and prudent, we must be cautious in authorizing utilities that extraordinary relief. Consequently, we find this request is better addressed in Phase 2 and/or through an individual utility's request for a subdocket wherein evidence of the impact of any costs or offsetting savings can be presented and considered in an evidentiary hearing.
>
> June 29, 2020 Order, Cause No. 45380, p. 8, (emphasis added.)

A purpose of our investigation in Cause No. 45380 was to mitigate hardship and preserve the long term functioning of utilities in response to an extraordinary event, but also to balance the best interest of customers and utilities. Where we could, we delayed affording relief to utilities until the full impact of the pandemic could be better known. For a utility seeking relief from Covid related costs, we appropriately must look at the larger picture, recognizing costs avoided because of Covid alongside costs incurred. Clearly, the $500,000 per annum revenue requirement we put in rates to procure line locates on a contract basis was avoided because of Covid. Petitioner's witness Kari C. Britto explained that "Non-essential frontline service work was deferred from March 2 2020 through December 2021 to help protect the safety of our employees and customers, consequently, we did not contract out work such as locates during the pandemic." (Britto Testimony, page 32).

We agree with the OUCC that in assessing Indiana American's request for Covid recovery we should consider the net effect of costs avoided by Covid and consider that in our calculation. We find Indiana American has a deferred COVID-19 regulatory *liability* of $532,850 (the Company's net regulatory asset of $383,817 reduced by avoided line locate costs of $916,667). We also agree that the liability should be amortized over five years as proposed by the OUCC and that at the end of five years, Indiana American should amend its schedule of rates and charges to remove that amortization from rates.

L. <u>LIPP Amortization Expense</u>.

i. <u>OUCC</u>. 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. Pub. Ex. 3 at 34.

ii. <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. Pet. Ex. 15 at 33. He argued 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 5 years with no interest. *Id.*

iii. Discussion and Findings. We have generally timed amortization of expenses and credits to conform to a five year period based in part on our expectation as to the life of the rates. As a matter of administrative efficiency, it makes sense that to the extent possible and consistent with our findings in this order that amortizations end in fewer filings of revised schedules of rates and charges. Accordingly, with respect to the amortization period for the deferred LIPP, we find the five-year amortization period proposed by the OUCC should be adopted. We further find INAWC should file a new tariff to remove the amortization from rates upon expiration of the five year period.

M. Property Tax Expense.

i. INAWC Case-in-Chief. INAWC witness Mr. Cifuentes presented *pro forma* property tax expense. To calculate the forecasted property tax, he calculated the five (5) 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). Pet. Ex. 9, at 19-20, Pet. Ex. 13 and 14, OPER Schedule OTX1.

ii. OUCC. Ms. Stull accepted Indiana American's methodology for calculating its property tax expense as it is appropriate to consider the tax basis of its utility plant in service. However, Ms. Stull disagreed with Indiana American's use of its estimated property tax assessment as of December 31, 2024 to establish Indiana American's Step 2 property tax expense. Ms. Stull explained 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. Pub. Ex. No. 3 at 37.

Ms. Stull noted that in its calculation of property tax expense Petitioner included utility plant that is not subject to property tax. She noted that the main extension to the Montgomery County Development Zone will be exempt from property taxes. She also noted that 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 both the

Montgomery County main extension and the lead service line replacements from her recommended property tax expense.

For Step 2, Ms. Stull calculated Property Tax expense of $17,265,073 for water operations and $505,321 for wastewater operations. Ms. Stull noted that INAWC did not make any change to property tax expense for Step three Rates, but she recommends Step Three property tax expense of $18,518,224 for water operations and $513,003 for wastewater operations. Pub. Ex. No. 3 at 38-39.

iii. INAWC Rebuttal. Petitioner's witness, Mr. Shimansky agreed with Ms. Stull that the Montgomery County surcharge assets and customer owned lead service line replacements should be excluded from Property tax expense. But he disagreed that the Step 2 rates should be based upon the December 31, 2023 assessment. He explained that the test year is the twelve months ending April 30, 2025, and that basing the Step 2 rates on the 2023 assessment will understate the *pro forma* test year expense. Pet. Ex. 15 at 61. He agreed to her recommendations regarding the calculation of property tax in future SEI and DSIC cases.

iv. Discussion and Findings. The only issues in dispute regarding *pro forma* property tax expense is what annual assessments should be used for Steps 2 and 3. The foremost issue raised by the OUCC is whether it is appropriate to collect property tax from Indiana American's ratepayers (i.e., include in rates) property taxes on an assessment a full eight months before the actual assessment has even been made.

Mr. Shimansky argued that basing the Step 2 rates on the December 31, 2023 assessment will *understate* the *pro forma* test year expense. Pet. Ex. 15 at 61. By application of the same logic, Mr. Shimansky's proposed use of the December 31, 2024 assessment to base property tax expense in Step 2 would *overstate* test year expense. One of the primary reasons the assessment on 12/31/24 will be different from the assessment on 12/31/23 is that Petitioner will have added new plant between those two dates. Thus, Petitioner is proposing to impose on its ratepayers a higher rate to collect an expense on plant that will not yet exist or be in service when Step 2 begins. If property tax liability begins *after* the assessment, Petitioner's property tax liability on a December 31, 2024 would not begin to accrue any earlier than January 1, 2025. Petitioner should not be permitted to collect an expense from ratepayers before that expense has even been incurred. The test year in this case was Petitioner's choice. It could have chosen a test year beginning on January 1, 2024, the effective date of the December 31, 2023 assessment. That would have been the only assessment completed during the test year. Petitioner should not be permitted to fast-forward twelve months to an increased estimated assessment effective on January 1, 2025.

Moreover, there is no evidence Petitioner will pay in the test year any property taxes on plant added between 12/31/23 and 12/31/24. If property taxes are paid in arrears, payment on new plant does not immediately follow the assessment adding that new plant. And yet we note that the OUCC's proposal still would permit Indiana American to include a level of property tax expense in rates without regard to when Indiana American will actually *pay* the level of property tax expense it proposes be included in test year and proposed rates. In the next rate case, we may visit the issue of whether property tax expense should be based on accrued property tax liability or actual test year expenditures. Meanwhile, we agree with the OUCC that Petitioner should not

be permitted to include in Step 1 rates, which begin on May 1, 2024, property tax expense based on the December 31, 2024 assessment. We also agree with the OUCC's proposal to use the December 31, 2024 assessment as the basis for property taxes in Step 3.

N. IURC Fee and Gross Revenue Conversion Factor.

i. OUCC. Ms. Sullivan calculated an updated gross revenue conversion factor to reflect the IURC fee that went into effect on July 1, 2023. Pub. Ex. 2 at 8. She also proposed a $130,462 increase to base year IURC fee expense of $275,452 for a total *pro forma* IURC fee expense of $405,914 utilizing the current 2022-2023 IURC fee of 0.1467603% and applying the fee to the OUCC's proposed operating revenue. Pub. Ex. 2 at 26.

ii. INAWC Rebuttal. Mr. Cifuentes testified on rebuttal 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. Pet. Ex. 21 at 2.

iii. 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 2022-2023 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.

O. Income Tax Expense. There were two disputed issues concerning federal and state income tax expense: (1) the inclusion of the repairs deduction in the determination of income tax expense or ratemaking purposes and (2) the appropriate amortization period for state and federal EADIT.

1. Repairs Deduction.

i. 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 that 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. Pub. Ex. 3 at 40. Ms. Stull further explained that the adjustment she proposes is only for the purposes of determining income tax expense for ratemaking purposes and has no effect on the operating expense or rate base (included in Petitioner's revenue requirement). *Id.*

Ms. Stull explained the IRS normalization rules do not prohibit the inclusion of a repairs deduction for purposes of determining income tax expense for ratemaking purposes. The IRS 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 IRS normalization rules. She concluded that it is not necessary for ratepayers to pay rates that include income taxes related to the repair deduction. *Id.* at 40 -41. Ms. Stull included $35,135,595 in Step One, $43,007,543 in Step Two, and $46,525,494 in Step Three as adjustments to the calculation of water operations *pro forma* income tax expense. These

adjustments are based on information included in INAWC Financial Exhibit OPER, Schedule TX1. She did not split the repairs deduction between water and wastewater operations because the amount for wastewater was immaterial and Petitioner was already proposing a significant subsidy to wastewater operations in this case. *Id.*

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 this repairs deduction in the determination of income tax 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 One, Two, or Three. Pub. Ex. 3 at 47.

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 Two capital structure and a $9,439,895 reduction to ADIT in the Step Three capital structure (OUCC Attachment MAS-8). Pub. Ex. 3 at 47.

ii. INAWC Rebuttal. INAWC witness Melissa Ciullo explained on rebuttal that the Internal Revenue Service allows an immediate deduction for certain expenditures as repairs which, for regulatory accounting purposes, are capitalized rather than expensed. Pet. Ex. 23 at 5. This creates a timing difference, which the Company 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 accumulated deferred income taxes ("ADIT"), consistent with the Muncie Remand Method as outlined in *Muncie Water Works Co.*, Cause No. 34571, 44 PUR4th 331 (PSCI 9/16/81). Ms. Ciullo testified this is consistent with past practice. Pet. Ex. 23 at 5. 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. *Id.* at 5-6. Ms. Ciullo explained that the Company'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 today's and tomorrow's customer will 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 for the Company. In contrast, Ms. Ciullo stated, flow-through captures 100% of the benefit of the tax deduction for today's customer, leaving none of the benefit for tomorrow's customer. *Id.* at 6.

Ms. Ciullo testified that it is still necessary 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, so there is still a timing difference. *Id.* at 6. Under Ms. Stull's approach, however, a regulatory asset for the ADIT (and gross-up) for income taxes to be paid 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. In addition, further complexities could arise with other filings such as the DSIC. Pet. Ex. 23 at 7. Ms. Ciullo said another layer of complexity would be tracking the underlying capital expenditures. Ms. Ciullo explained, 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. Therefore, the Company 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. If the treatment to flow-through was to be changed retrospectively, other considerations would need to be made, such as creating a large regulatory asset to offset the accumulated deferred income tax in cost of capital calculation as well as re-evaluating excess accumulated deferred income tax already given back. *Id.* at 8.

iii. Discussion and Findings. Historically Indiana has normalized temporary tax timing differences and the net impact of those temporary tax differences have been relatively immaterial. As such, our decision to normalize these temporary tax differences balanced ratepayer interests (i.e., lower rate impacts) with those of the utility (i.e., avoided burden and expense of tracking these differences). However, the Internal Revenue Code has been changed to allow utilities to *expense* certain costs as operating expenses *for tax purposes* but *capitalize* these same costs *for book purposes*. Therefore, we agree with the OUCC that the treatment of temporary tax differences warrants an updated review and analysis to avoid inequitable or unbalanced results.

In this instance, the temporary difference that is created by Petitioner's repairs deduction is significant, representing a $35,135,595 deduction in Step One, $43,007,543 in Step Two, and $46,525,494 in Step 3 based on Petitioner's own estimates. Normalizing this temporary difference increases the income tax expense included in customer rates by $8.8 million in Step 1 to $11.6 million in Step 3, assuming a 25% overall effective tax rate. This is a significant burden for Indiana American's ratepayers, a burden which can be avoided. Normalizing this temporary difference created by the repairs deduction is not required because it is unprotected, making the treatment of this temporary tax difference within our discretion.

In support of continuing the practice of normalization, Petitioner asserted normalizing temporary timing differences will be reflected in lower customer rates through the recognition of accumulated deferred income taxes in Petitioner's capital structure. Petitioner provided no support or evidence for this assertion. And while we agree that the inclusion of ADIT in the capital structure does somewhat reduce the required net income, we disagree this reduction materially offsets the increase in annual income tax expense included in a utility's revenue requirement because of the normalization of the repairs deduction. Normalizing temporary timing differences results in customers providing funds to a utility for income taxes the utility will not pay for years to come. This would be in essence an interest free loan from ratepayers to the utility that will be paid back over decades. While this treatment may be appropriate when applied to temporary differences related to *depreciation expense*, primarily resulting from accelerated depreciation rates, it is less clear that this treatment is appropriate when applied to the *repairs deduction*. That is because *accelerated depreciation expense*, the protected timing difference, was authorized by Congress and protected to ensure the purpose of the deduction was preserved. However, the *repairs deduction* is the result of a tax court ruling regarding the

determination of a "unit of property." We also reject Petitioner's argument that normalization provides stability in customer rates and allows the utility to recover costs more evenly over time. Again, while this may be true when applied to temporary differences related to depreciation expense, it is less clear that normalization is necessary to provide these same benefits for the repairs deduction. Further, Petitioner provided no support or corroborating evidence to substantiate its assertions about the impact on customer rates of normalizing all temporary timing differences.

We also reject Petitioner's argument that changing the treatment of certain tax expenses from normalization to flow-through would add unnecessary complexity to an already complex tax calculation and would require the creation of a regulatory asset or liability. We likewise reject Petitioner's argument that tracking the underlying capital expenditures adds another layer of complexity that should be avoided. Petitioner's current policy of treating certain "repair" costs differently for book (expense) and tax (capital) purposes has already added that level of complexity to the determination of income tax expense and tracking of accumulated deferred income tax assets and liabilities. Likewise, Petitioner must already track the underlying "repair" expenditures in order to properly account for its accumulated deferred income taxes and, more importantly, comply with the IRS normalization rules.

Because the effect the repairs deduction has on the determination of income tax expense is material, affecting customer rates, we find for ratemaking purposes Petitioner must flow-through the repairs deduction in the determination of its income tax expense.

2. EADIT.

i. INAWC Case-in-Chief. INAWC witness Shimansky testified that pursuant to the settlement agreement in Cause No. 45032 S4, excess accumulated deferred income tax ("EADIT") from the Tax Cuts and Jobs Act of 2017 is being returned as an offset against income tax expense using the Average Rate Assumption Method ("ARAM"). Pet. Ex. 2 at 42; Pet. Ex. 13, Exhibit OPER TX1, Line 23 and supporting Workpapers for Deferred Income Tax. Mr. Shimansky explained that the Workpapers for Deferred Income Tax were compiled by American Water's Tax Department using PowerTax. *Id.*

ii. OUCC. 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 One, Two and Three, respectively. She asserted that while ARAM will vary from one period to the next, an increase of this magnitude (41.7 years compared to 65 to 74 years) is not reasonable. She further explained that Petitioner's workpapers do not provide any useful support for its calculation of EDIT amortization or its calculation of ARAM. She stated the source of the data included in Petitioner's workpapers used to calculate ARAM was not provided nor any information as to how ARAM was calculated or even what ARAM was used. Ms. Stull explained that it is understandable that Petitioner used PowerTax to perform the detailed calculations for ARAM but it is incumbent upon Petitioner to provide basic information about the calculation, such as the ARAM used in the calculation along with an explanation of why it differs significantly from that used in prior cases. Pub. Ex. 3 at 42-43.

Ms. Stull stated that while Petitioner cannot amortize EADIT any faster than ARAM without violating the IRS normalization rules, she considered the ARAM it had calculated in this case to be an error. *Id.* at 44. 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 48.7 years. Ms. Stull considered an amortization period of 41 years to be a reasonable basis on which to calculate the EDIT amortization in this case. *Id.*

iii. <u>Industrial Group</u>. Mr. Gorman proposed that the amortization period to return Indiana EADIT to customers be reduced from the 33.5 years proposed by the Company to 3 years; and that the full balance of the refund be credited to the Company's water customers. IG Ex. 1 at 7. 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 the Company'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 IURC's discretion and is not required to be refunded using ARAM. He urged that these deferred tax over-collections should be refunded 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 the Company'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 ratepayers, most of whom would have been paying rates which reflect the old tax rate, without creating any detriment to INAWC or its future customers who did not contribute to the EADIT balance. IG Ex. 1 at 14. Mr. Gorman proposed a faster amortization of 3 years, consistent with the three step rate increase proposed in this case. Accelerating the amortization to 3 years increases the Indiana EADIT amortization expense from $136,087 to $1,508,393, or an increase of $1,372,306. *Id.* at 15.

iv. <u>INAWC Rebuttal</u>. Ms. Ciullo responded to Ms. Stull's disagreement with the portion of Petitioner's EADIT calculation computed using ARAM. She explained that while ARAM is supposed to mimic the average remaining life, it is not intended to be a straight-line calculation. Pet. Ex. 23 at 8. Moreover, the 41 years Ms. Stull uses is based on an estimated calculation that was utilized in the prior rate case, at a time when the Company had not completed the implementation of the PowerTax system. *Id.* Ms. Ciullo explained that PowerTax is the industry software which is used to compute the full ARAM calculation using detailed records for a vastly more accurate calculation than can be done in Excel. She stated the ARAM calculation is much more complex than using straight line and using a straight line method is only appropriate if a utility does not have the appropriate books and records to calculate ARAM. *Id.* at 9. Ms. Ciullo pointed out that the Company had made these points clear in the prior rate case (IURC Cause No. 45142) in both the direct and rebuttal testimony of the tax witness John R. Wilde. Ms. Ciullo testified that Ms. Stull is comparing an estimate of ARAM calculated prior to PowerTax to the ARAM result produced by PowerTax. Accordingly, 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 the Company at the time

of the last case. *Id.* at 9. Ms. Ciullo 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 the Company no longer being able to utilize accelerated tax depreciation, which would be a severe detriment to both the Company and the customers.

Mr. Shimansky acknowledged on rebuttal that unlike Federal EADIT, the amortization period for Indiana EADIT rests entirely within the Commission's discretion. Pet. Ex. 15 at 20. 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 3 years but the underlying asset is depreciated over its remaining life, there is a mismatch that contradicts Mr. Gorman's desire to "result in a more balanced treatment to the current generation of ratepayers." *Id.* at 21. Mr. Shimansky urged that if the IURC decides to accept Mr. Gorman's 3-year proposal or other expedited proposal, then the final order in this Cause 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 Weighted Average Cost of Capital. *Id.*

v. <u>Discussion and Findings</u>. With respect to the amortization of Federal EADIT, we note that the current amortization period of 41.49 years was established in the settlement approved by our June 24, 2020 Order in Cause No. 45032 S4.[42] The record in that Cause and in the current proceeding reflects that Federal protected EADIT cannot be amortized using any shorter period than that established using ARAM without risking a normalization violation. In Cause No. 45032-S4, it was understood that, on a going forward basis, the EADIT amortization period would be based on the actual ARAM calculation (through PowerTax) and would be updated as necessary in subsequent rate cases. In this Cause, Petitioner updated its Federal EADIT amortization period to reflect its asserted ARAM calculation. The OUCC raised concerns about the results of Petitioner's ARAM calculation regarding whether the result is reasonable and accurate. While we agree it may be appropriate and necessary to use computer software such as PowerTax to calculate ARAM, the software is still programmed by human beings and relies on inputs from human beings. Errors are possible, and it would be a mistake not to question the results when they appear to be inaccurate or unreasonable. The OUCC also raised concerns about the support Petitioner provided for its proposed Federal EADIT amortization period and the determination of ARAM.

We find that Petitioner's proposed ARAM period should be used to amortize Federal EADIT to avoid any potential normalization violations. However, the reasonableness and accuracy of the purported result of Petitioner's ARAM calculation cannot be assumed. In this regard, we are concerned with the lack of support and transparency provided in Petitioner's case-in-chief. Therefore, we also find Petitioner should submit a compliance filing within 60 days of the issuance of this order, providing details of the ARAM calculation and explaining why ARAM increased so dramatically since Cause No. 45032-S4 concluded. If errors or other issues

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[42] *Re Indiana Util. Reg. Commissions Investigation into the Impacts of the Tax Cuts and Jobs Act of 2017 and Possible Rate Implications Under Phase 1 and Phase 2 for Indiana Am. Water Co., Inc.,* 45032 S4, 2020 WL 3489487 *5 (IURC 6/24/2020), at 6.

with the calculation are identified in the compliance, filing Petitioner should include an updated calculation of the adjusted Federal EADIT amortization and calculate a customer refund if applicable. Petitioner should provide any applicable refund to customers in the next billing period occurring after the submission of the required compliance filing. The OUCC and other Intervenors in this case shall have 30 days to review and submit any objection to this compliance filing.

[The Indiana American Industrial Group submitted testimony regarding the amortization of State EADIT. The OUCC provided no testimony on this issue. The OUCC recommends the Commission adopt the Industrial Group's discussion and findings with respect to the amortization of Indiana State EADIT]

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

Table 9: Net Operating Income at Present Rates

	Present Rates Step 1	Present Rates Step 2	Present Rates Step 3
Total Operating Revenues	$ 283,771,484	$ 282,463,751	$ 287,212,003
Operating Expenses			
Operations and Maintainenance	93,320,301	100,178,213	100,220,686
Depreciation and Amortization	64,476,074	62,367,670	68,460,820
Taxes Other than Income	19,110,320	20,132,129	21,399,868
Federal Income Taxes	5,710,529	2,494,834	719,744
State Income Taxes	2,167,532	1,387,349	950,890
Total Expenses	184,784,756	186,560,195	191,752,008
Net Operating Income	$ 98,986,728	$ 95,903,556	$ 95,459,995

In summary, we find that with appropriate adjustment for ratemaking purposes, Petitioner's annual net operating income under its present rates as of July 31, 2023 for water/wastewater service would be $98,986,728. We found that Petitioner's net original cost rate base as of the end of the test year (April 30, 2025) is forecasted to be $1,747,964,040, that Petitioner's WACC is 6.07%, which would produce a return on net original cost rate base of $107,740,317. To this return we add the fair value increment for the Indiana Cities Water Corp. acquisition adjustment of $236,443, 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 $107,976,760. Petitioner's current return of $98,986,728 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.

Table 10: Net Operating Income at Proposed Rates

	Proposed Rates Step 1	Proposed Rates Step 2	Proposed Rates Step 3
Total Operating Revenues	$ 279,585,941	$ 287,212,003	$ 304,047,437
Operating Expenses			
Operations and Maintainenance	93,282,861	100,220,686	100,371,279
Depreciation and Amortization	64,476,074	62,367,670	68,460,820
Taxes Other than Income	19,104,232	20,139,035	21,424,355
Federal Income Taxes	4,883,328	3,433,246	4,046,981
State Income Taxes	1,964,575	1,617,592	1,767,240
Total Expenses	183,711,070	187,778,229	196,070,675
Net Operating Income	$ 95,874,871	$ 99,433,774	$ 107,976,762

12. Authorized Rate Increase and Rate Implementation.

A. INAWC Case-in-Chief. Mr. Shimansky described Petitioner's proposed rate implementation in three steps, which is based at least in part on the rate implementation approved by this Commission in *City of Evansville*, Cause No. 45545 (IURC 3/2/2022). INAWC has chosen a test year that will commence a few months after the date of this Order. INAWC proposes to implement the rate increase in three steps. The first step would take effect upon the issuance of this Order. It would incorporate rate base, capital structure, depreciation, and grossed up return as of a cutoff of July 31, 2023. The first step would 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 would 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 would adjust revenues, uncollectible expense and certain taxes (IURC, SIT and FIT), based upon rate base, capital structure and depreciation as of the end of the test year (April 30, 2025). At each step, INAWC would 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. Pet. Ex. 2 at 8-9.

B. OUCC. The OUCC did not offer testimony in opposition to the to Petitioner's proposed three-step process. Ms. Stull explained that OUCC and other parties should have an opportunity to review Indiana American's update filings, conduct discovery as necessary, and be afforded a meaningful opportunity to respond to Indiana American's update to assure adherence to the Commission's findings. Indiana American should be allotted adequate time to put together its compliance filing and the OUCC and other parties should be allotted adequate time to conduct their review and respond as necessary. For all Steps, Ms. Stull stated Indiana American should also provide a certification that the plant is in service and verification that the construction costs have been incurred and paid. The OUCC and intervenors should have 30 days to raise any issues or concerns or otherwise object to Indiana American's Step One

compliance filing. Any finding resulting in a decrease in rate base from the amount used to implement Step One rates should result in a refund 12 to customers.

Ms. Stull testified the process she proposed is consistent with the process the Commission has approved in other cases involving updates to rate base in forward-looking test year cases. Ms. Stull explained that I.C. § 8-1-2-42.7 and I.C. § 8-1-2-6 apply to this proceeding, which means Petitioner may increase its rate base to the end of its forward-looking test year, but a return cannot be earned on the rate base additions until they are in service and the plant has been determined to be both used and useful for the provision of water service or wastewater service. This requires an additional process wherein each component of rate base and capital structure should be updated to actual costs at July 31, 2023 (Step One), April 30, 2024 (Step Two), and April 30, 2025 (Step 2 Three). She asserted these updates should compare the actual amounts to the amounts approved 3 by the Commission in its final order in this case, with an explanation for any variance of 5% or greater. Petitioner's rate base updates should be subject to review to determine whether identified projects have been completed and placed in service by the end of the test year and whether the costs authorized to be added to rate base have actually been incurred and paid by the end of the test year.

Ms. Stull testified that in each phase, or step, total rate base should not exceed the value of rate base approved by the Commission in the final order. To the extent the total value of rate base components at July 31, 2023, April 30, 2024 or April 30, 2025 exceed approved rate base, the difference should be removed from utility plant in service. Any asset additions excluded from Step One or Step Two rate base may properly be included in a subsequent step - provided the inclusion does not cause 22 the rate base in the next step to exceed the amount approved for that step. Any asset addition cost excluded from Step Three rate base because it was not completed and in service by the end of the test year or because it would cause rate base to exceed the cap or any other reason, would presumably be considered in the next rate case 3 or, if eligible, presented in a subsequent distribution system improvement charge 4 ("DSIC") or system enhancement improvement ("SEI") charge.

Ms. Stull recommended Indiana American be required to provide: (1) account number, (2) account name; (3) transaction date; (4) 9 transaction description; (5) transaction number or other identifying information; (6) 10 project number; (7) project description; (8) vendor name (where applicable); (9) transaction amount; (10) cost center number; and (11) cost center description. Further, she said Indiana American should be prepared to provide invoices and other supporting documentation of the costs incurred and paid.

For Step One rates, Ms. Stull recommended Indiana American be required to provide the information pertaining to actual rate base, capital structure, and depreciation expense as of July 31, 2023, once the Commission issues its final order in this case: (1) Comparisons between actual rate base achieved as of July 31, 2023 and approved rate base. (2) Comparisons between actual and approved capital structure components. (3) Updated revenue requirement calculation. (4) Updated tariff. (5) Updated utility plant in service listing by asset account, clearly identifying any disallowed plant or other adjustments, and separately identifying those accounts that are water, wastewater, or corporate (6) Updated utility plant in service listing by project number, including updated in-service dates and actual expenditures, that ties to the actual additions to utility plant in service. (7) Detailed general ledger transaction listing supporting utility plant

additions. (8) Updated accumulated depreciation by asset account, clearly identifying any disallowed plant or other adjustments, and separately identifying 30 those accounts that are water, wastewater, or corporate. (9) Updated contributions in aid of construction and customer advances for construction by asset account. (10) updated depreciation expense calculation in the same format as Schedule. She added that all these supporting schedules should be provided in Excel format with formulas intact except the updated tariff.

Ms. Stull proposed a Step two, which is to begin on May 1, 2024. Within 30 days of the implementation of Step rates, Indiana American should provide for actual rate base, capital structure, and depreciation expense as of April 30, 2024 (1) Updated utility plant in service listing by asset account, clearly identifying any disallowed plant or other adjustments, and separately identifying those accounts that are water, wastewater, or corporate.(2) Updated utility plant in service listing by project number, including updated in-service dates and actual expenditures, that ties to the actual additions to utility plant in service. (3) Detailed general ledger transaction listing supporting utility plant additions. (4) Updated accumulated depreciation by asset account, clearly identifying any disallowed plant or other adjustments, and separately identifying those accounts that are water, wastewater, or corporate. (5) Updated contributions-in-aid of construction and advances for construction by asset account. (6) Updated capital structure in the same format as Schedule CC1. (7) Updated depreciation expense calculation. (8) Updated revenue requirement. (9) Revised tariff if applicable. All these supporting schedules should be provided in Excel format with formulas intact. Indiana American should also provide a certification that the Step Two plant is in service and verification that the construction costs have been incurred and paid as of April 30, 2024. OUCC and intervenors would have 30 days to raise any issues or concerns with Indiana American's Step Two compliance filing. Any finding 16 resulting in a decrease in rate base from the amount used to implement Step Two rates should result in a refund to customers.

For Step 3, Ms. Stull explained that in order to expedite the update process, there should be two filings to allow adequate time for the OUCC and intervenors to review actual asset additions while at the same time reducing any delay in the implementation of Step Three rates. Ms. Stull recommend Indiana American file all supporting documentation for Step Three utility plant additions as of December 31, 2024. This filing would include the following: (1) Updated utility plant in service listing by asset account, clearly identifying any disallowed plant or other adjustments, and separately identifying those accounts that are water, wastewater, or corporate. (2) Updated utility plant in service listing by project number, including 5 updated in-service dates and actual expenditures. (3) Detailed general ledger transaction listing supporting utility plant additions. (4) Updated accumulated depreciation by asset account, clearly identifying 9 any disallowed plant or other adjustments, and separately identifying 10 those accounts that are water, wastewater, or corporate. (5) Updated contributions-in-aid of construction and customer advances for construction by asset account. All these supporting schedules should be provided in Excel format with formulas intact. This compliance filing should be provided to the OUCC and other intervenors by February 1, 2025.

Ms. Stull stated that in the second Step 3 filing Indiana American should provide for asset additions from January 1, 2025 through April 30, 2025: (1) Updated utility plant in service listing by asset account, clearly identifying any disallowed plant or other adjustments, and separately 21 identifying those accounts that are water, wastewater, or corporate. (2) Updated

utility plant in service listing by project number, including 23 updated in-service dates and actual expenditures. (3) Detailed general ledger transaction listing supporting utility plant additions. (4) Updated accumulated depreciation by asset account, clearly identifying any disallowed plant or other adjustments, and separately identifying 28 those accounts that are water, wastewater, or corporate. (5) Updated contributions-in-aid of construction and customer advances for construction by asset account. (6) Following information for actual rate base, capital structure, and depreciation expense as of April 30, 2024: Updated capital structure in the same format as Schedule CC1. a. Updated depreciation expense calculation b. Updated revenue requirement, if applicable. c. Updated tariff, if applicable. Ms. Stull identified additional informational 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; (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. Pub. Ex. 3 at 16-22. She testified that rates should take effect for all steps upon filing on an interim subject to refund basis. *Id*., at 18-19.

C. <u>Industrial Group</u>. Industrial Group Witness Gorman did not offer testimony in opposition to 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. IG Ex. No. 1, 10-11.

D. <u>INAWC Rebuttal</u>. Mr. Shimansky testified on rebuttal that the recommendations that rate base be capped at the amount authorized by the final 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 thirty day period to submit objections is also acceptable. He agreed to an earlier submission of calendar year end data, but 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 new reporting obligations different than those imposed in any other prior rate orders in future test year cases. He testified that no compelling reason has been offered for the additional layers of reporting she has requested and that it would be inefficient. Pet. Ex. No. 15, 53-55.

E. <u>Discussion and Findings</u>. We begin our findings with the issues that are not in dispute. We approve Petitioner's proposed three-step increase, with Step 1 taking effect as soon as possible after the issuance of this Order 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. This three-step process is consistent with the multi-step process we approved for the City of Evansville in Cause No. 45545. There, the petition was filed 24

months before the test year; here it was filed 13 months before the test year beginning. In both cases, Step 1 would take effect upon order issuance, before the beginning of the test year and based upon the extent of the projected data at that time. 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 rider proceedings. All three steps will take effect on an interim subject to refund basis upon submission of the compliance filing described herein. Parties to this proceeding will have thirty days to submit any objections to the compliance filings for Steps 1 or 2 and 60 days for Step 3.

The issues in dispute are the date for submission of rate base update as of December 31, 2024, the OUCC's proposal to cap the Steps 1 and 2 rate base figures and the OUCC's request to include specific information with the compliance filing. We accept Mr. Shimansky representations 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 information Ms. Stull proposed Indiana American be required to file for each Step, Ms. Stull began her discussion by explaining that OUCC and other parties should have an opportunity to review Indiana American's update filings, conduct discovery as necessary, and be afforded a meaningful opportunity to respond to Indiana American's update to assure adherence to the Commission's findings. She acknowledged that Indiana American should be allotted adequate time to put together its compliance filing but that the OUCC and other parties should also be allotted adequate time to conduct their review and respond as necessary. Ms. Stull's credentials are set forth as an attachment to her testimony, and she has been testifying in rate cases before this Commission for more than two decades. As such, we are inclined to accept Ms. Stull's representations as to what information should be provided to the OUCC so it can conduct an appropriate review and meet its statutory obligation to protect rate payers. Moreover, requiring the information at the outset of each Step will avoid the necessity of consumer parties asking Indiana American to provide the information thorough discovery. Indiana American is adding approximately $430.0 million of UPIS additions to its rate base in the three steps following this order, and it is not unreasonable for Indiana American to provide the information set forth above in Ms. Stull's testimony summary and we so find. However, to the extent Ms. Stull recommended a cap in Steps 1 and 2, we find the cap shall only apply to Step 3. However, in no event may the rate base in Steps 1 and 2 exceed the cap for Set 3.

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. The compliance filing will calculate rates for the applicable step based upon these certifications, subject to the approved rate base at the conclusion of the test year found herein. The rates shall take effect upon submission subject to refund and the rights of parties to submit an objection to the compliance filing as previously found herein. Petitioner shall provide the information set forth in Ms. Stull's testimony summary above. If necessary to resolve any objections, we will schedule a hearing. We find this process is consistent with the process used in our other future test year cases.

On the basis of the evidence presented in these proceedings and subject to this compliance filing process we have found to be appropriate, we find that Petitioner should be authorized to increase its rates and charges in three steps, calculated to produce combined

additional operating revenue of $17,398,148 at the conclusion of the test year, resulting in total operating revenue of $304,047,437. This revenue is reasonably estimated to afford Petitioner the opportunity to earn net operating income that is no more than the fair return of $107,976,760 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 the total operating revenues and net operating income at each step as follows:

Table 9: Revenue Requirement

	Step 1	Step 2	Step 3
Original Cost rate Base	############	############	############
Times: Weighted Cost of Capital	5.95%	5.93%	6.07%
Net Operating Income Required for Return on Rate base	95,594,431	99,175,065	107,740,317
Add: Fair Value Increment	280,441	258,709	236,443
Net Operating Income Required	95,874,872	99,433,774	107,976,760
Less: Adjusted Net Operating income	98,986,728	95,903,556	95,459,997
Net Revenue Increase Required Requirement	(3,111,856)	3,530,218	12,516,763
Gross Revenue Conversion Factor	134.5031%	134.5031%	134.5031%
Recommended Revenue Increase	(4,185,542)	4,748,253	16,835,434
Revenues Subject to Increase	280,794,383	279,250,948	283,999,201
Recommended Percentage Increase	-1.49%	1.70%	5.93%

13. <u>Affordability</u>.

A. <u>INAWC Case-in-Chief</u>. Mr. Prine testified in his case-in-chief why the proposed rate increase should be considered reasonable and appropriate. He stated that a significant driver of the rate case is INAWC's ongoing infrastructure investment, which he said accounts for one-third of the Company's total requested rate increase. Pet. Ex. 1 at 7. Mr. Prine said the Company is also requesting a moderate increase to O&M expenses, saying that the increase is largely driven by an increased demand on Company resources associated with the acquisition of seven water and wastewater systems and organic customer growth (more than 13,000 new customers) since the companies last rate case. Pet. Ex. at 7-8. Mr. Prine stated the increase in O&M expenses is caused by increased regulatory requirements. *Id. at 8.* Finally, he said increased O&M is driven by "improved organizational structure and enhanced business processes. *Id.*

Mr. Prine testified he recognized how important it is for service to remain affordable and that Petitioner has evaluated the impact of the proposed rate increase on its customers and performed an analysis of the affordability of service under the proposed rates, as described by INAWC witness Rea. *Id.* at 9. Further referencing the testimony of Mr. Hobbs and Ms. Britto, Mr. Prine described ways in which he said INAWC maintains the affordability of its water service, including continuously seeking to improve business processes and making investments that improve operational efficiencies. He stated the Company leverages the power of its organization to share learning on best practices and purchase equipment and supplies at advantageous terms. *Id.* at 10.

Mr. Prine also introduced two proposed changes to the Company's water service rate design for customers (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. *Id.* Mr. Prine noted that INAWC witness Mr. Rea discussed those changes in more detail. Mr. Prine asserted an allowance-based rate will enhance the affordability of Basic Water Service, especially for the Company's more economically vulnerable customers, without the need for these customers to directly apply for assistance. *Id.* He stated an allowance-based rate design improves the affordability of Basic Water Service 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). *Id.* at 11. Mr. Prine indicated that even with an allowance-based rate design, affordability of service may still be an issue for the most vulnerable customers. Mr. Prine testified the Company proposed the 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 ("FPL"). He stated the discount offered under this tariff would reduce typical Basic Water Service bill for a three-person household from $58 per month under proposed rates 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 the Company's current rates. *Id.* 11-12.

INAWC witness Rea testified that the Company knows that its water and wastewater service is essential and knows how important it is for that service to remain affordable. He asserted the affordability analyses done by the Company shows that INAWC's investment practices and management of and investment in its water and wastewater systems are in the long-term best interest of its customers; and the Company's affordability analysis also is a direct measure of the benefits that the Company's customers gain from the Company's prudent management of the system. Pet. Ex. 5 at 5. Mr. Rea explained that the Company assesses affordability of water and wastewater service by comparing annual bills for water and/or wastewater service to household income in the communities the Company serves. 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 the Company's entire service territory. At a more detailed level, individual household income is considered, and affordability can then be assessed across a full range of households based on their various income levels and bills for water and/or wastewater service. Mr. Rea explained that a variety of household income data is readily and publicly available from the U.S. Census Bureau through the American Community Survey ("ACS") at the state, county, and community levels. *Id.* He presented the Company's affordability study for water service (Attachment CBR-1) and the affordability study for wastewater service (Attachment CBR-2). He explained that for water service, the Company 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 from which to develop an Enterprise-Level affordability analysis for wastewater service. *Id.* at 6.

Mr. Rea described the Company's Enterprise-Level Analysis of affordability of service, which is a historical comparison of average monthly bills for INAWC residential customers to MHI for the Company'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 the Company's service territory is a weighted average of the number of customers the Company 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 in this proceeding). 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. *Id.* 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. *Id.* at 8. The overall BTI Ratios for water service for Indiana American customers have improved over the last decade and is expected to be 0.76% under the Company's proposed Step 3 rates in this case, which is well below the thresholds considered to be the high-end limit of affordability for residential customers at the system wide level. *Id.*

The Community-Level Analysis takes a deeper dive into affordability of water and wastewater service at a local level across different customer demographics and proposed rates for each community that the Company serves. *Id.* at 9. For purposes of the Company's affordability analyses, Mr. Rea the Company 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. *Id.* at 10. Mr. Rea stated the Company 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 on the subject and a review of Company billing data for residential customers in months with minimum levels of discretionary water usage. *Id.* 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. The Company estimated that 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. *Id.* at 12.

Mr. Rea testified that affordability of service is not uniform across the Company's service territory because household income can vary significantly across the Company's service territory and Indiana American has very diverse service territories and serves customers in urban, suburban, and rural communities. *Id.* at 13. He explained that assessing affordability information of water and wastewater service for the entire residential customer population can demonstrate whether customers in general are having or would have difficulty paying their water bills under the Company's current or proposed tariff structure. These assessments can 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, both in terms of general rate design proposals that can reduce the cost of Basic Water Service for all customers, including lower-income customers, and customer assistance programs that may include customer grants, tariff discounts, levelized billing, and outreach programs. *Id.* at 16.

Mr. Rea concluded that the affordability of the Company's water service from 2012 through the forecast test period indicates that the way the Company has invested in and managed

its water and wastewater systems in the INAWC service territory has indeed been for the long-term benefit of our customers. He opined that the Company's water service has been, is, and is expected to continue to be affordable for the vast majority of its residential customers, including under the rates proposed in this case, but also that there are groups of customers for whom affordability of water service may be challenging. *Id.* at 16-17. The two proposed rate design changes were proposed to address such challenges.

B. <u>OUCC</u>. OUCC witness Scott 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 explained that if approved, Indiana American's capital investment requests will likely realize significant returns on a proposed $875 million increase in rate base by 2025. Mr. Bell stated that in his 35 years of experience with utility ratemaking and IURC proceedings, Indiana American's case is perhaps the most complicated and issue-loaded base rate case this utility has ever presented.

Mr. Bell noted that Indiana American asks the Commission to approve water rates that are 55% higher overall than the rates approved in its last rate case set in 2019 and the requested wastewater rates are 106% higher. Mr. Bell noted that through DSIC and SEI trackers Indiana American has already increased rates to water customers by approximately 17.69%. In addition to the proposed rate increase, Mr. Bell stated that Indiana American is expected to seek future rate increases for its water customers through DSIC and SEI infrastructure cost recovery mechanisms, which raises issues of affordability.

Mr. Bell explained that water and wastewater utilities in Indiana are monopolies whose customers have no choice in their service providers and that these customers depend on the Commission to apply traditional ratemaking principles to ensure that a water or wastewater utility's costs and returns are reasonable so that customers are not paying for unreasonable expenses, imprudent investments, or excessive returns through higher rates. Mr. Bell explained that the Commission is charged with the task of balancing the interests of the utilities with ratepayers and consistent with the General Assembly's stated policy, the Commission should take steps to moderate the imposition of higher rates over time and only approve necessary and reasonable requests for Indiana American to provide affordable water and wastewater service. He recommended that the Commission consider the affordability of Indiana American's existing and proposed rates when examining the various components of the utility's requests.

Mr. Bell stated that safe and reliable water and wastewater systems are critical to basic human needs. However, he added that at the same time customers are faced with increasing utility costs, they must also contend with other cost of living increases due to inflation. He suggested that this combination of price pressure is unsustainable and that these hardships are only worsened during periods of widespread economic turmoil. He suggested that in recognition of the importance of affordability, Indiana American could seek a lower and more reasonable ROE than the 10.6% it requests in this docket, lower the equity portion of the 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 the Company has reached a tipping point, explaining that its rates have risen to the point where a significant number of its customers can no longer be expected to afford its increasingly expensive water services without financial assistance, which it proposes come from Indiana American's own residential customer base. He explained that Indiana American's response to the increasing unaffordability of its water service, which it proposes to increase by 55% since its last rate order, is to place a further burden entirely on its customers, to assist those customers to pay the balance of what Indiana American acknowledges is a rate a significant number of its customers cannot afford.

Mr. Bell compared Indiana American's rates with various other water utilities in the state. Mr. Bell noted that Indiana American, which is the largest investor-owned water utility in the state by customer count, has the highest water rates in the State when compared to Citizens Water (the largest water utility in the state by customer count), Citizens Water of Westfield, LLC (the second largest investor-owned water utility in the state by customer count), and the next eight largest municipal water utilities. He concluded that Indiana American has by far the most unaffordable rates when compared to those ten water utilities.

Mr. Bell compared the rates of Indiana American to Citizens Water, the largest water utility in the state by customer count (i.e., Citizens Water serves approximately 341,597 customers). He indicated a bill for a Citizens Water customer that uses 5,000 gallons of water in a month, including its $8.56 service charge and $0.72 DSIC charge, is $33.43, while an Indiana American residential customer using 5,000 gallons of water during a month (subject to current Area 1 rates) pays $54.90, a difference of $21.47 or 64.2% more than a Citizens Water residential customer, for basically the same level of service. He added that if Indiana American's proposed rate increase is approved, a residential customer using 5,000 gallons of water during a month (subject to Area 1 rates) would pay $79.85, a difference of $46.42, or 139% more than a Citizens Water residential customer. Mr. Bell explained that bill differences are similar if a comparison is based on usage of only 4,000 gallons per month, where a Citizens Water residential customer would pay $28.60, compared to an Indiana American residential customer who would pay $49.75 a month – a difference of $21.15 or 74% more. He added that if the entire rate increase is approved as proposed, an Indiana American residential customer will pay $64.10 for 4,000 gallons compared to only $28.60 for a Citizens Water residential customer - a difference of $35.50 or 124% more.

Mr. Bell also compared the rates of Indiana American, the largest investor-owned water utility in the state by customer count to Citizens Water of Westfield LLC, the second largest investor-owned water utility in the state by customer count. He indicated that Citizen Water of Westfield, LLC serves approximately 18,895 metered customers and that a bill for a Citizens Water of Westfield customer that uses 5,000 gallons of water in a month is $32.96, which includes a $10.47 base charge and a $3.39 fire protection charge service fee. He compared that to an Indiana American residential customer using 5,000 gallons of water during a month (subject to Area 1 rates) currently pays $54.90, a difference of $21.94 or 66.6% more than a Citizens Water of Westfield residential customer for basically the same level of service. He added that if

Indiana American's proposed rate increase is approved, a residential customer using 5,000 gallons of water during a month (subject to Area 1 rates) will pay $79.85, or 142% more than a Citizens Water of Westfield residential customer. Mr. Bell explained that the bill differences are similar if based on usage of only 4,000 gallons per month. He added that a Citizens Water of Westfield residential customer would pay $29.14 compared to an Indiana American residential customer who would pay $49.75 a month, a difference of $20.61 or 71% more. He added that if the entire rate increase is approved as proposed, an Indiana American residential customer will pay $64.10 for 4,000 gallons versus $29.14 for a Citizens Water of Westfield residential customer, a difference of $34.96 or 120% more.

Finally, Mr. Bell compared Indiana American's rates to the state's eight largest regulated municipal water utilities (Ft. Wayne, Evansville, South Bend, Lafayette, Bloomington, Anderson, Elkhart, and Columbus). When compared to those eight municipal utilities, Indiana American customers pay the highest water bills in the State. He included Table 1 in his testimony to graphically compare Indiana American's current water bill for 5,000 gallons of usage to the eight largest regulated municipal water utilities.

Mr. Bell concluded that based on his comparison of Indiana American's rates to Citizens Water, Citizens Water of Westfield, LLC and the eight largest regulated municipal water utilities, Indiana American currently has the highest and most unaffordable rates in the State. He added that if the proposed excessive rate increase is approved, Indiana American will continue, by an even larger margin, to have the highest, most expensive, and most unaffordable rates in the State. He explained that not only will Indiana American's rates be an increasing financial burden to its captive residential customers, but it may also be problematic for businesses and could hinder economic development. Mr. Bell indicated that affordability is not just an issue of a customer's ability to pay, but it may also speak to how a utility's rates compare to the rates of other utilities in the state providing the same service. He added that the Indiana General Assembly has recently acknowledged that the comparison of prices has a place when considering affordability of utility service. He testified that HEA 1007 (2023), states that decisions concerning Indiana's electric generation resource mix, energy infrastructure, and electric service ratemaking constructs must consider, among other things, "(2) Affordability, including ratemaking constructs that result in retail electric utility service that is affordable and competitive across residential, commercial, and industrial customer classes." (Emphasis added.) Mr. Bell concluded that Indiana American's very high rates (current and proposed) when compared to other utilities in the state should be considered when discussing whether its rates are affordable.

OUCC witness Jason Compton noted Petitioner's water affordability analysis indicated a bill was affordable if it was less than or equal to 2% of the customer's household income. Furthermore, Mr. Compton explained Petitioner conducted its study by examining the financial characteristics and various demographics of communities it serves using American Community Survey ("ACS") data. Mr. Compton states that using that data, Petitioner developed affordability indices to assert a level of affordability of its proposed rates by community and across the state. Pub. Ex. 5 at 2-3. Mr. Compton explained that Petitioner compared the median household income ("MHI") of its customers across the state against the statewide MHI. Mr. Compton testified that Petitioner did not determine the actual household income of all its customers and determined a proxy for its communities (i.e., zip code) that Petitioner then used to determine a MHI for each community it serves. Mr. Compton explained that its necessary to use a proxy

because the ACS compiles the MHI separately for homeowners and renters and therefore it is necessary to consider the number of households that rent and the number that own in each community. *Id.* at 3. In discussing whether a 2% Bill-to-Income ratio ("BTI") is an acceptable threshold, Mr. Compton -noted the OUCC does not consider 2% of household income to be an appropriate threshold to measure affordability.

Mr. Compton did not agree with Petitioner that Indiana American's water customers have a higher MHI than the statewide MHI. Mr. Compton testified that Indiana American's water customers have a lower MHI than the statewide MHI. Furthermore, Mr. Compton stated the inputs Petitioner's chose to calculate its customers' MHI *understated* the number of customers that will have a higher BTI than 2%. Mr. Compton indicated Petitioner did not correctly and consistently rely on the ACS data to estimate its customers MHI. He explained that this was done to accommodate Petitioner's approach to not consider the incomes of households that use Indiana American's water when that water it procured through indirect means (e.g., sub-billing and supplied by landlords). *Id.* at 4. Mr. Compton asserted this approach caused Petitioner to make unsupported assumptions about the household income of those it excluded from its analysis. Mr. Compton testified that any meaningful analysis must consider all households that are ultimately using and paying for Petitioner's water service. He indicated an affordability analysis should consider all households using Petitioner's service because the proposed rate increases ultimately effects *all* households receiving Petitioner's produced water.[43] *Id.* at 4. Mr. Compton pointed out that Petitioner's annual reports to the Commission categorizes revenues generated by customers in attached and multi-family housing as residential revenues. *Id.* at 5.

Mr. Compton explained three reasons why he disagreed with Petitioner's methodology. First, Petitioner's underlying need to disregard the ACS data is based on the faulty premise that we should ignore the effect of rate increases on households that use and pay for Petitioner's service but do not have a direct customer relationship. Second, even if the first were true, it required Petitioner to guess in the absence of reliable data, in which, it should not be a researcher's practice to make further assumptions that mutate the integrity of the data. Third, excluding indirect customers naturally skews the results of affordability making Petitioner's water appear more affordable because statistically, households who rent their residences generally have lower levels of income. *Id.* at 6-7.

Mr. Compton testified that Petitioner's calculation of a statewide MHI of $64,251 is not representative of the entire community of the customers Petitioner serves and therefore mutated the ACS data again. Moreover, Mr. Compton testified that Petitioner did not appropriately calculate for the Bill-to-Income ratios. As 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. Thus, Petitioner's

[43] Mr. Compton explained that Petitioner's exclusion of all attached housing from the proxies is flawed. Petitioner only considers direct customers in its analysis and assumed that "attached" housing as described by the ACS were indirect customers. However, attached housing includes townhouses, duplexes, and other single-family homes connected through a shared wall that may be direct metered customers. Pub. Ex. 5 at 4.

calculation of the average bill was faulty and understated the true average bill and BTI, ultimately resulting in a lower BTI ratio. *Id.* at 7-8.

Mr. Compton presented his own calculation of the MHI for Petitioner's water customers using the methodology Petitioner used, but unlike Petitioner, he did not exclude customers considered to have an indirect relationship with Indiana American. Mr. Compton calculated an overall Indiana American user MHI of $62,650 as compared to Petitioner's calculation of $69,151. *Id.* at 8. Mr. Compton explained that his calculation of the MHI showcased Petitioner's customers' MHI is 2.3% less than the statewide MHI as compared to Petitioner's calculation that its customers are making 7.63% more than the statewide MHI. *Id.* at 9.

Mr. Compton addressed that Petitioner conducted a wastewater affordability analysis as well, however, the only difference is that Petitioner did not explore a historical affordability analysis for its wastewater customers. Petitioner's analysis for the wastewater model is identical to the water model besides the fact that it used different ACS data to represent its wastewater customers. 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. *Id.* at 10. Mr. Compton explained that Petitioner's calculation for its customers' MHI showed that its customers made 9.45% more than the statewide MHI, whereas Mr. Compton's calculation showed Petitioner's customers only made 2.11% more. *Id.* at 10-11.

Finally, Mr. Compton noted Petitioner used a five-year estimate from the ACS. Mr. Compton criticized the five-year estimate because as it was used in Mr. Rea's models, it looked at what affordability was like in the past rather than the present and future. Mr. Compton continued by 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 that Petitioner performed. *Id.* at 11-12.

Mr. Compton reiterated that the study overstates affordability because Petitioner's rate increases affect not just direct customers but also households that use and ultimately pay for its services directly. Mr. Compton presented that his corrections for Petitioner's calculations would suggest that Petitioner's overall water affordability index is not 84%, but 80%. Mr. Compton also presented that Petitioner's over wastewater affordability index is not 66%, but 62% under its 2% affordability standard. *Id.* at 12.

C. Crown Point. Mr. Guerrettaz testified in opposition to the proposed rates for Crown Point and Sale for Resale ("SFR") customers in general, stating the proposed rates and charges would be excessive and unreasonable. Crown Point Ex. 1 at 6.

D. CAC. Mr. Inskeep testified that the Company's analysis shows that its proposed rates will not be affordable for customers. CAC Ex. 1 at 20. He challenged the Company'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) used in the Company's Enterprise-Level Analysis. CAC Ex. 1 at 17-18. He recommended that the

Commission take note of the sizeable population of Hoosier families who will not be able to afford the Company's proposed rate increase. *Id.* at 21. Mr. Inskeep recommended the Commission take action in this proceeding 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 and allowance-based rate that can further help mitigate the bill vulnerable populations. *Id.*

E. <u>INAWC Rebuttal</u>. Mr. Rea testified on rebuttal that the question of affordability of service is not simply a yes or no question – one cannot state simply that water service is either affordable or not affordable. Instead, affordability of service is a continuum, as shown by the Company'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. This is true across the communities that Indiana American serves and is true even within the wealthiest communities that the Company serves. The Company'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 the Company is using at the individual customer level) at the Company'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 the Company's Universal Affordability Tariff is intended to address. Pet. Ex. 18 at 7.

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 the Company's "increasingly expensive" water services. He referred to Chart 2 from his Direct Testimony showing that the percentage of household income taken up by the Company's average water bills over time has gone down, not up. Pet. Ex. 18 at 8. He stated the BTI Ratio measured at the MHI level under the Company's proposed rates is consistent with levels seen historically. *Id.* Mr. Rea testified that the Company's affordability analysis is necessarily detailed in order to provide a complete, comprehensive, and unbiased view of the affordability of the Company's service across all different customer groups. *Id.* at 9. He explained that the Company's affordability analysis is an objective, data-driven analysis made up of an Enterprise-Level analysis and a Community-Level analysis with two different but complementary objectives. Mr. Rea testified that under the Company's proposed rates, Basic Water Service is expected to take up less than 2% of household income for 84% of the Company's residential customers. Basic Water Service is expected to take up more than 3% of household income for approximately 9% of the Company's residential customers before applying any discounts associated with the Company's proposed Universal Affordability Tariff. *Id.* at 9.

Mr. Rea testified that the terms household income and median household income are not interchangeable, despite OUCC witnesses Bell and Compton using them interchangeably. *Id.* at 10. 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. *Id.* 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. The Company has proposed a Universal Affordability Tariff to address those customers identified

through the use of this 2% benchmark as likely to benefit from this additional customer assistance. Pet. Ex. 18 at 10.

Mr. Rea responded to OUCC witness Compton's criticisms of his affordability analysis, stating that it is appropriate for the analysis to concentrate on customers that are direct customers of the Company because (1) the use of an MHI statistic which best estimates household income for direct customers of the Company is consistent with the calculation of the average bill which is also based on direct customers, and (2) for indirect customers of the Company (e.g., renters in multi-family buildings) it is impossible to know what these households pay in rent for water service. Pet. Ex. 18 at 17. He further stated that even if, as Mr. Compton asserts, calculations of MHI for the communities that the Company 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. This is true because (1) household sizes for households that rent are smaller than for 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. *Id.* at 18.

With respect to Mr. Compton's argument that the average bill for the Company's customers was not accurately calculated because it did not include revenues associated with public and private fire protection charges, Mr. Rea responded that Private fire service charges are not charged to residential customers. They are charged to non-residential customers who directly use private fire service. *Id.* at 18. 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. *Id.* at 19. As a policy matter, he stated he would expect the local government officials making this election understand the affordability implications of such a decision. *Id.* Mr. Rea also stated the charges are not large enough to fundamentally change the trend of improving affordability over time that the Company's Enterprise-Level analysis shows. *Id.*

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. *Id* at 19. 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. *Id.* at 20. Mr. Rea testified that the ACS five-year data set is, in fact, the appropriate data set to use for the affordability analysis that the Company is conducting because it provides current estimates of household income and provides that information for all communities in Indiana, both urban and rural, which is important in developing a comprehensive affordability analysis across the entire service territory and the entire state. *Id.*

Mr. Rea disagreed with Mr. Bell's bill comparison and conclusions drawn therefrom. He testified that Mr. Bell's comparison is of little practical use due to fundamental differences in structure, ownership, operations, and customer bases of the relevant water operations being compared. Pet. Ex. 18 at 11-12. 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. The most significant of these is the existence of natural subsidies for the rates of customers of municipal utilities through tax and other policies. Municipal utilities do not pay income tax and their obligation to pay other types of taxes may be eliminated or reduced. The cost of municipal debt is lower because holders of that debt are exempt from income tax. Municipal utilities are eligible for grant funding and government-funded subsidized interest programs that are not so readily available to investor-owned utilities. *Id.* at 13. In addition, Mr. Rea listed a number of operational differences between Indiana American and other service providers in Indiana that can lead to significant differences in bills, including the nature of the Company's service territory, significant differences in investment levels and investment strategies and rate structures. *Id.* at 13-14. Mr. Rea concluded that there is nothing in the data to suggest that Indiana America's rates are out of line with water service rates for other providers in the state, especially when significant financial and operational differences between service providers exists. *Id.* at 14. Mr. Rea further noted that none of this comparison relates to the affordability of Indiana-American's rates for Indiana-American's customers, which is demonstrated by the Enterprise-Level and Community-Level affordability analysis presented by Mr. Rea in his direct testimony. *Id.*at 14-15.

F. <u>Discussion and Findings</u>. We are charged by statute with the task of balancing the interests of the utilities with ratepayers. Consistent with the General Assembly's stated policy, the Commission should take steps to moderate the imposition of higher rates over time and only approve necessary and reasonable requests for Indiana American to provide affordable water and wastewater service. Water and wastewater utilities in Indiana are monopolies whose customers have no choice in their service providers and that these customers depend on the Commission to apply traditional ratemaking principles to ensure that a water or wastewater utility's costs and returns are reasonable so that customers are not paying for unreasonable expenses, imprudent investments, or excessive returns through higher rates. Through a study performed, Indiana American has asserted its rates should be considered affordable and its requested rate increases both reasonable and appropriate. The OUCC has disagreed. OUCC witness Scott Bell recommended the Commission consider the affordability of Indiana American's existing and proposed rates when examining the various components of the utility's requests. Each individual revenue requirement issue must be decided based on the evidence, law, and policy in effect for that issue. We do not directly address any of the utility's *pro forma* revenue requirement in this section, and the merits of Indiana American's specific revenue requirements will be addressed elsewhere in this order. Nonetheless, the parties have focused on the affordability of Indiana American's rates, and we will speak to that issue.

Indiana American's president, Mr. Prine testified that the 55% increase in water rates since its last case and 31% increase over current rates should be considered reasonable and appropriate. Mr. Prine testified that the proposed rate increase is reasonable and appropriate because 'it is driven primarily by the need to make the expenditures necessary to keep our water and wastewater service safe and reliable." Pet. Ex. 1 at 8. Mr. Prine asserted that a significant driver of the rate case is INAWC's ongoing infrastructure investment, which he said accounts for one-third of the Company's total requested rate increase. Pet. Ex. 1 at 7. Mr. Prine said the Company is also requesting a moderate increase to O&M expenses, saying that the increase is largely driven by an increased demand on Company resources associated with the acquisition of seven water and wastewater systems and organic customer growth (more than 13,000 new customers) since the companies last rate case. Pet. Ex. at 7-8. Mr. Prine stated the increase in

O&M expenses is caused by increased regulatory requirements. *Id. at 8.* Finally, he said increased O&M is driven by "improved organizational structure and enhanced business processes." *Id.* Mr. Prine also testified he recognized how important it is for service to remain affordable *Id.* at 9. And referencing the testimony of Mr. Hobbs and Ms. Britto, Mr. Prine indicated INAWC maintains the affordability of its water service by continuously seeking to improve business processes and making investments that improve operational efficiencies. *Id.* at 10.

In describing both what is driving Indiana American's request to increase its rates and what Indiana American does to keep rates affordable, Mr. Prine seems to contradict himself. Where Mr. Prine asserted that "improving business processes" and "making investments that improve operational efficiencies" is done to make sure Indiana American's rates "remain affordable," he also asserted that "improved organizational structure and enhanced business processes" is one of the drivers of the increase to its O&M revenue requirement. *Id.* at 8. Thus, what makes its rates "remain affordable" is also what makes its rates increase. Mr. Prine asserted that Indiana American has been "very successful" in maintaining its affordability "by continuously seeking to improve Indiana American's business process and make investments that improve operational efficiencies." *Id.* at 9.

We question whether Indiana American can truly claim to have been "very successful" in its efforts to maintain the affordability of its water and wastewater services. We share the concern expressed by OUCC witness Scott Bell about the immediate and ongoing financial impacts of Indiana American's requested rate increase. Mr. Bell noted that Indiana American asks the Commission to approve water rates that are 55% higher overall than the rates approved in its last rate case set in 2019 and wastewater rates that are 106% higher. Mr. Bell pointed out that through DSIC and SEI trackers Indiana American has already increased rates to water customers by approximately 17.69%. In addition to the proposed rate increase, Mr. Bell stated that Indiana American is expected to seek future rate increases for its water customers through DSIC and SEI infrastructure cost recovery mechanisms.

To support the assertion that Petitioner's rate increase is reasonable and appropriate he discussed the need to make expenditures necessary to keep Indiana American's water and wastewater service safe and reliable. Mr. Prine gave as an example the need to replace mains. Importantly, Mr. Prine acknowledges that infrastructure improvement is only $25 million of its $86.7 million (31% increase). Another cause of the increase was an increase in O&M "largely driven by an increased demand on Company resources associated with the acquisition of seven water and wastewater systems and organic customer growth (more than 13,000 new customers) since the companies last rate case. Pet. Ex. at 7-8. It is somewhat troubling that the addition of ratepayers through new connections and acquisitions, should serve to increase per customer costs rather decrease them. The principles of economies of scale would suggest new customers should enhance affordability, not cause customers to pay more per month. Likewise, "improved organizational structure and enhanced business processes" intuitively should also serve to bring per customer costs down, not serve as a driver of a significant rate increase.

As to whether Petitioner's rates should be considered affordable at the outset, we refer to Mr. Bell's comparison with the rates of other utilities. Mr. Bell noted that Indiana American, which is the largest investor-owned water utility in the state by customer count but it has the

highest rates in the State when compared to Citizens Water (the largest water utility in the state by customer count), Citizens Water of Westfield, LLC (the second largest investor-owned water utility in the state by customer count), and the next eight largest municipal water utilities. He concluded that Indiana American has by far the most unaffordable rates when compared to those ten water utilities. Mr. Bell compared the rates of Indiana American to Citizens Water noting that a Citizens Water customer that uses 5,000 gallons of water in a month pays $33.43, while an Indiana American residential customer using 5,000 gallons of water during a month (subject to current Area 1 rates) pays $54.90, a difference of $21.47 or 64.2% more for basically the same level of service. Mr. Bell noted that if Indiana American's proposed rate increase is approved, a residential customer using 5,000 gallons of water during a month (subject to Area 1 rates) would pay $79.85, a difference of $46.42, or 139% more than a Citizens Water residential customer. Mr. Bell noted a customer of Citizens Water of Westfield LLC, the second largest investor-owned water utility in the state by customer count that uses 5,000 gallons of water in a month pays $32.96, compared to Indiana American's current rate of $54.90.

During Cross examination by the OUCC, of Petitioner's witness Mr. Rea, the OUCC asked Mr. Rea questions about the Commission's 2023 Annual Water Bill Analysis, which compares the average bill for 5,000 gallons of 83 water utilities. (OUCC CX-5.) Where Mr. Rea considered Indiana American (Area 1 rates) to have the sixth highest rates among twenty-three investor owned water utilities, it shows two of those utilities with higher rates are Indiana American operations (IAWC Area 3 - Lowell and IAWC Area 3 - Rivers Edge). Further, the document did not reflect the more recent DSIC 14 and SEI surcharges that made Indiana American Area 1 rates nearly $6 higher than what is indicated on the Bill analysis. With the exception of Granger Water Utility, LLC, the three IAWC utilities have the highest water IOU rates in the state. Hr. Tr. C-27 – C-35

We also address Petitioner's affordability study. Mr. Rea's Affordability study indicated that Indiana American's water rates are affordable to 84% of its water customers. Using the same basic methodology but including "indirect customers" as defined broadly by Petitioner, Mr. Compton determined that Indiana Americans rates were affordable to 80% of its water customers. Mr. Bell disagreed that 2% is an appropriate threshold for affordability and noted that the AWWA journal article Mr. Rea noted in his testimony called the 2% MHI affordability flawed and stated that it does not measure affordability at the household level. Pub. Ex 1 at 19.

We agree with Mr. Compton that affordability should be considered for customers that have an indirect relationship with the utility. Whether a customer owns their home, rents their home or lives in an apartment, they will be using Indiana American's water and ultimately paying the rates Indiana American is authorized to charge. Petitioner's proposed rate increase effects both direct and indirect customers. In fact, Mr. Rea admitted in his cross-examination that, statistically on average, customers who rent their properties make less than those who own their properties. Hr. Tr. C-22. This would suggest that the concept of affordability matters even more for customers who Petitioner defines as indirect and excluded from its analysis of affordability. Importantly, Petitioner excluded indirect customers who are multi-family households (renters) from its calculation of its customers' median household income, which as Mr. Rea admitted during his cross-examination, would drive up the median household income when he calculated customer incomes. Hr. Tr. C-22, lines 5-9.

Mr. Rea also admitted that he calculated the bill-to-income ratios on his historical affordability analysis using revenues generated by both indirect and direct customers as defined by Petitioner. Hr. Tr. C- 23-25. Considering, that an analysis that excludes indirect customers plays a role in calculating the bill-to-income ratio that includes those same customers, it makes us question the reliability of Petitioner's model and whether its genuine in its effort to promote affordability. Further, Mr. Rea admitted in cross-examination that indirect customers have less water consumption than indirect customers, which would inherently imply that the bill of an indirect customer would, on average, be less than direct customers. Hr. Tr. C-19-20.

Increasing its customers' median household income by excluding indirect customers and understating its average bill by using those same lower income customers to calculate the average bill, Petitioner's affordability index is flawed. For that reason, Petitioner's affordability models cannot be relied upon in its discussion of affordability. We also must disregard the Affordability analyses to the extent they are based on a threshold of 2% of MHI, which the article Mr. Rea cited in his case-in-chief testimony stated was seriously flawed. Pet. Ex. 5 at 8. Pub. Ex. 1 at 19.

We have great concern about the affordability of Indiana American's rates. We decline to conclude Indiana American's rates are affordable.

14. Cost of Service Study and Rate Design.

A. Cost of Service Study.

i. INAWC Case-in-Chief. Mr. Rea presented the Company's cost of service study ("COSS") for water service. He testified the Company 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. Pet. Ex. 5 at 43. The revenue requirement for various cost categories was allocated to the following customer classes INAWC serves: 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. *Id.* The cost categories the Company 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. *Id.* at 46-47.

ii. OUCC. Mr. Mierzwa addressed the Company's water cost of service study. While he generally agreed with the Company's use of the base-extra capacity water cost of service methodology, he recommended adjustments to the maximum hour extra capacity factors developed by Indiana American for the Industrial and Sales for Resale customer class. He also recommended modifications to the Company's assignment of mains costs to the transmission and distribution functions. Mr. Mierzwa presented a revised class cost of service study for water which reflects his recommended adjustments and modifications. Pub. Ex. 8 at 3. Mr. Mierzwa testified the extra capacity factors proposed by the Company for the Industrial and Sales for Resale 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. *Id.* at 13. He stated it is

unclear why the Company 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. *Id.* Mr. Mierzwa recommended application of the AWWA M1 Manual estimated hourly ratios to the maximum day capacity factor developed by the Company for the Industrial and Sales for Resale customers. This would increase the maximum hour capacity factor for the Industrial class from the 1.20 shown on schedule CBR-4, p. 9 to 1.60 and would result in a Sales for Resale maximum hour capacity factor of 2.32. *Id*. at 13-14.

Mr. Mierzwa testified it is unreasonable to assign mains costs to the transmission and distribution functions based on mileage as the Company has done because it fails to recognize that the costs of purchasing and installing mains generally increase as the diameter of the main increases. He recommended that mains be assigned to the transmission and distribution functions based on the weighted installed costs of those mains. *Id.* at 14.

iii. <u>Industrial Group</u>. Ms. York expressed various concerns regarding the Company's COSS model, which she said call into question the validity of the results. IG Ex. 2 at 3. She identified certain adjustments to the Company's proposed COSS in an attempt to improve the accuracy of the Company's measurement of each class's cost of service. However, Ms. York stated 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. She recommend changes to INAWC's proposed class allocation of the spread of the revenue requirement awarded in this case based on my findings related to the Company's COSS. According to Ms. York, because the COSS model presented by the Company cannot be adequately validated, she recommended the use of an across-the-board rate increase. IG Ex. 2 at 3. Ms. York contended that the Company's "new, pared down" COSS model is "unreliable, inaccurate and should not be relied on to guide revenue apportionment in this case." *Id.* at 3. Ms. York referenced criticisms American Water affiliates have faced with respect to similar COSS models in Illinois and Missouri. *Id.* at 12-13. She criticized the Company's failure to accurately functionalize transmission and distribution costs. *Id.* at 14-15. She testified there is no evidence to support the Company'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. *Id.* at 17. 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. *Id.* at 18.

Ms. York also took issue with the manner in which certain costs were allocated to customer classes within Mr. Rea's COSS. In particular, she disagreed with the Company'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 contends, Factor 1 does not accurately allocate purchased power costs to the customer classes that drive the electric demands for pumping, which in turn causes the Company to incur the purchased power costs. *Id.* at 19. She stated Factor 2 is a more appropriate allocator than Factor 1 because it reflects both average flow and Maximum-Day demand requirements. *Id.*

Ms. York objected to the distribution multiplier for the Industrial Class of 0.50, contending 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 very small fraction of the total length of distribution mains on the system. *Id.* at 22. She presented a "corrected" distribution multiplier to reflect the actual portion of Industrial class usage that is served by distribution mains based on evidence provided by INAWC, which she characterized as a reasonable proxy under the circumstances. *Id.* at 24.

Ms. York disagreed with the Company's approach of not allocating any Source of Supply or Water Treatment costs to Private Fire or Public Fire classes. She recommended that a portion of Source of Supply and Water Treatment costs be allocated to the Public Fire and Private Fire classes, consistent with the methodology used in the prior rate case. 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. *Id.* at 26. 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. *Id.*

iv. Wholesale Customers. Mr. Callocchia recommended rejection of INAWC's COSS based on what he characterized as 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. WC Ex. 1 at 3. Mr. Callocchia stated the two-step COSS approach used by INAWC was significantly different from the single-step COSS approach used in its previous rate case and produces "radically different results with no justification or explanation from the Company as to why." *Id.* He referenced challenges to the two-step COSS approach in cases brought by INAWC affiliates Illinois American Water and Missouri American Water. *Id.* at 10. 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. *Id.* at 13.

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. *Id.* at 3. He contended that it costs INAWC significantly less to serve SFR customers because INAWC's 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. *Id.* at 4. He raised issues related to the manner in which the Company distinguished between transmission and distribution costs in the COSS. He sated 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 the Company'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 the Company's investment in the system's Transmission and Distribution facilities. *Id.* at 14.

Mr. Callocchia objected to recovery of costs related to COVID-19, 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. *Id.* at 15. He stated COVID-19 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 the Company 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 the Company'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 the Company related to credit card fees. *Id.*

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 the Company did not properly recognize distribution-level water losses in the Company's system when developing Class Allocation Factor 1. *Id.* at 16-17. He disagreed with the Company treating metered data from different service levels the same in the allocation of costs. *Id.* at 17. Mr. Callocchia stated that the majority of water loss occurs within the Company's distribution system, because almost 74% of all water mains within the INAWC system are categorized as distribution and given the vast size of the distribution system and the number of valves and connections within this system, the changes of line breaks, water leaks and unauthorized usage are much more substantial at this service level. *Id.* at 18. 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. *Id.* 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 Class Allocation Factor 1. *Id.* at 19-20. He then calculated average day demand factors that he said would result in a properly calculated Class Allocation Factor 1. *Id.* at 20.

v. <u>Crown Point</u>. Crown Point witness 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 SFR Wholesale Group's cost of service expert, 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 COSS proposed in this Cause be disallowed and accordingly any increase approved be applied across the board.

vi. Whiteland. Whiteland witness Young testified that the Company 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 the Company's point of delivery of its wholesale water to the SFR customers. Whiteland Ex. 1 at Q&A 9. She also states that the Company does not account for SFR customers having their own low-income customers and that Whiteland's customers, including low-income customers, will have to subsidize Indiana American's low-income customers but will not receive any benefits under the Company's Low-Income proposal. *Id.* at Q&A 11.

vii. INAWC Rebuttal. INAWC witness Chuck Rea responded to the OUCC and intervenor positions on his cost of service study. He testified that his cost of service analysis, even as modified for changes upon which the Company 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. Pet. Ex. 18 at 32. 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, the Company 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. *Id*. at 32. He stated that in Cause No. 44450 (also a settled case), the cost of service study demonstrated that Industrial and SFR customers should have received a rate increase of more than twice the system average to achieve cost of service. In Cause No. 44022, Industrial customers would have needed an increase of almost twice the system average and SFR would have needed an increase of more than twice the system average. The case before that was Cause No. 43680, where again Industrial and SFR customers were being subsidized. That cost of service study at that time called for an increase for Industrial below 150% of system average but for SFR again in excess of 200% of system average. *Id.* at 32-33. Mr. Rea testified that there have been five different cost of service studies 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. *Id.* at 33. Mr. Rea opined that the complaints they raise about changes in the modeling approach used and other particular issues without providing their own cost of service study seem to me to be aimed at arriving at an across-the-board increase and continuation of the subsidy. *Id.*

With respect to the two-step COSS model Mr. Rea employed, he explained that the two-step 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. *Id.* at 34. Mr. Rea testified he has used this two-step approach successfully for Iowa-American Water Company, West Virginia-American Water Company, and New Jersey-American Water Company, and the form of the cost of service model was not challenged in those jurisdictions and was accepted by stakeholders in those jurisdictions, including intervenors for industrial and sales for resale customers. *Id*. Attachment CBR-4R to Mr. Rea's rebuttal testimony provides 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 the Company has proposed in this case. 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. *Id.* at 36. 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. *Id.*

Mr. Rea testified that the Company'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. *Id*. at 37. Mr. Rea presented the volumetric rates for each major customer class coming from the Company'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, which directly reflects the unique circumstances that SFR customers face. *Id*. at 37-38.

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. Pet. Ex. 18 at 41.

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. *Id*. at 45.

Mr. Rea accepted OUCC witness Mierzwa's approach with respect to hourly capacity factors for Industrial and SFR classes. *Id*. at 47.

Mr. Rea testified that Ms. York has not provided any evidence to suggest that cost per kilowatt-hour ("kWh") that the Company 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 the Company uses electricity, then there is no reason to allocate costs disproportionately to certain customer classes. Mr. Rea testified that given that 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. *Id.* at 49.

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. *Id*. at 50.

Mr. Rea agreed with Ms. York that an allocation of Source of Supply and Water Treatment costs to Private Fire 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. Pet. Ex. 18 at 51.

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.

viii. <u>OUCC's Cross Answering Testimony</u>. OUCC Witness, Mr. Mierzwa responded to the testimony of the Intervenors' cost of service witnesses. Mr. Mierzwa testified that despite Ms. York's assertions, she was still able to determine how the classification of costs were functionalized, classified, and allocated based on Petitioner's COSS. Therefore, contrary to her claims, Petitioner's COSS *does* show what portion of Source of Supply investment was classified to the base, maximum day, and maximum-hour categories. Mr. Mierzwa acknowledged Petitioner's COSS model does not provide the basis for understanding how it used system design and usage but explained that a COSS is not designed to provide that information but rather show how costs are functionalized, classified, and allocated. *Id*. at 4-5.

Mr. Mierzwa noted that Ms. York proposed to assign main costs to the transmission and distribution functions based on calendar year 2022 main lengths reducing the percentage of mains assigned to the transmission function from 28% to 17% and increasing the percentage of mains assigned to the distribution function from 72% to 83%. This decreased the main costs allocated to the industrial class. Mr. Mierzwa criticized Ms. York's recommendation because she continued to assign main costs based on the *length* of transmission and not on *actual costs*. *Id*. at 8-9.

Mr. Mierzwa explained that purchased power expenses were allocated based on Factor 1 in Petitioner's COSS, adding that Factor 1 allocates purchased power costs between customer classes based on each class's annual consumption. Mr. Mierzwa noted that Ms. York proposed that Petitioner allocate these costs based on Factor 2, decreasing the indicated cost of service for the Industrial class by approximately $170,000. *Id.* at 11. Mr. Mierzwa criticized Ms. York's proposal because as Mr. Rea explained, on days with maximum rates of flow, purchased power expenses increase, as does the amount of water consumed. Factor 1 results in customers paying for this expense in proportion to their consumption and thus is an appropriate methodology.

Mr. Mierzwa described the distribution multiplier used by Petitioner as an adjustment to water sales for Industrial and sale-for-resale ("SFR") customers such that only the distribution-level sales in each class are allocated distribution-related costs. Petitioner does this to recognize that some large customers take service directly from the transmission mains. Mr. Mierzwa noted that Ms. York suggested that significantly less than half of Industrial usage is served by distribution mains as suggested by the .5 distribution multiplier Petitioner identified and recommended that multiplier be 0.098. Mr. Mierzwa pointed out Ms. York's analysis did not consider that a portion of residential, commercial, and public authority customers are also

directly served by transmission mains. Mr. Mierzwa noted that the revised multiplier should be .32. *Id.* at 12.

Mr. Mierzwa agreed with Ms. York's position that Petitioner should have allocated Source of Supply and Water Treatment costs to the private and public fire classes. *Id*. at 12-13. Mr. Mierzwa noted that Ms. York presented her own COSS that reflected her proposed revisions. In her COSS, Ms. York recommended an across-the-board revenue increase for all customer classes.

Mr. Mierzwa noted that Ms. York recommended that the $1.63 million wastewater subsidy be reduced by the greater of 25%, or the approved reduction to Petitioner's proposed wastewater revenue requirement plus an additional $100,000. *Id.* at 13-14. Mr. Mierzwa retorted that if a class of water customers pay rates that are less than the indicated COSS, that class is also shifting costs to other customers which is contrary to cost-causation principles. Mr. Mierzwa further argued that it is not likely to materially impact rates and therefore his recommendation remains reasonable and should be adopted rather than Ms. York's. *Id*. at 14.

Mr. Mierzwa testified that he agreed with Ms. York's recommendation that Petitioner begin moving toward class-specific rates in this Cause by establishing a separate rate schedule for the industrial customers. *Id*. at 15.

Mr. Mierzwa noted Ms. York recommended that the DSIC and SEI revenue requirement should continue to be recovered through a fixed monthly charge based on meter size after the costs have been allocated under the COSS to the customer classes responsible for the costs. Mr. Mierzwa disagreed because it would eventually result in the recovery of all fixed costs through fixed monthly customer charges and only the recovery of variable costs through usage charges. *Id*. at 16. Mr. Mierzwa explained that straight fixed variable ("SFV") is not in the best interests of Petitioner's customers as recommended by Ms. York. Mr. Mierzwa elaborated that it would significantly reduce incentive of customers to conserve water, result in increased usage, and is inconsistent with cost-causation. *Id.* at 16.

Mr. Mierzwa explained Mr. Callocchia recommended that an alternative approach to cost allocation should be considered wherein any approved increase would be assigned across-the-board and the Commission reject Petitioner's COSS. *Id*. at 19-20. Mr. Mierzwa stated that Mr. Callocchia is concerned that Petitioner's deviation from the single step approach is resulting in drastically different outcomes with no explanation or justification. *Id*. at 18. Mr. Mierzwa also testified that Mr. Callocchia's excess/subsidy comparison is invalid. Reiterating his response to Ms. York's arguments on allocation of transmission and distribution mains costs., Mr. Mierzwa recommended the Commission reject Mr. Callocchia's recommendation that Petitioner's COSS be rejected. Mr. Mierzwa noted Petitioner's COSS in this Cause as compared to Cause No. 45142 is not producing a drastically different result which merits rejection of Petitioner's COSS.

Mr. Mierzwa testified that he agreed with Mr. Callocchia's recommendation to change allocation Factor 1 to recognize distribution-level water losses which was presented in Table 4 of Mr. Callocchia's direct testimony. *Id*. at 22. But he disagreed with both Mr. Callocchia and Mr. Guerrettaz in their recommendation that DSIC and SEI costs continue to be collected 100%

through fixed meter charges after they are rolled into rate base for the same criticisms to Ms. York's recommendation for DSIC recovery. *Id.* at 23.

Mr. Mierzwa testified that he modified the COSS presented in his direct testimony to adopt 4 positions that the Intervenor's recommended. Mr. Mierzwa modified his COSS to (1) reflect an allocation of Source of Supply and Water Treatment costs to Public and Private Firm service; (2) include base usage volumes for the Public and Private Fire classes; (3) reflect a distribution multiplier for the Residential, Commercial, and Public Authority classes, and updated the distribution multiplier for the Industrial class; and (4) adjust allocation Factor 1 to account for distribution loss. Mr. Mierzwa presented a comparison of his modified COSS with Petitioner's COSS and a summary of Step 3 revenues using the modified COSS. *Id.* at 24.

OUCC witness Margaret Stull responded to the intervenors' proposal that the return on and of plant associated with Petitioner's DSIC and SEI capital trackers should continue to be recovered through a fixed charge rather than volumetric. Ms. Stull explained that costs recovered through a DSIC consist of a pre-tax return on eligible infrastructure additions, depreciation expense, and property tax expense. At its inception, the DSIC charge was recovered through a volumetric charge based on a customer's consumption; however, Ms. Stull further explained that since 2017 the DSIC tracker has been calculated as a fixed monthly charge based on the customer's meter per IC 8-1-31-8(a). Pub. Ex. 13 at 3. Ms. Stull explained that once a DSIC is established that charge does not continue until all costs are recovered. IC 8-1-31-15 establishes that the DSIC is reset to zero once a utility receives an order from the Commission establishing its rates.

Ms. Stull then addressed the background concerning a system enhancement improvement charge ("SEI"). Ms. Stull explained that the Indiana General Assembly ("IGA") created the SEI in 2020 through the enactment of Ind. Code 8-1-31-7. Furthermore, Ms. Stull explained that Ind. Code 8-1-31.7.-2 establishes that eligible additions include any new utility plant or equipment that do not increase revenues by connecting to new customers, are used and useful, and were not included in the utility's rate base in its most recent rate case. IC 8-1-31.7-7 states two types of improvements are eligible for SEI treatment. *Id*. at 4. Ms. Stull testified that under IC 8-1.31.7, the SEI tracker charge is calculated as a fixed monthly charge based on the size of the customer's meter. Ms. Stull further explained that an SEI is reset to zero after a Commission order authorizing a general increase in rates has been issued.

Ms. Stull described the intervenors proposals that the return on and of plant associated with Petitioner's DSIC and SEI capital trackers should continue to be recovered through a fixed charge rather than volumetric. *Id.* at 5. Ms. Stull testified that she does not agree with the arguments of the Intervenors. Ms. Stull stated Mr. Guerrettaz's interpretation of the DSIC and SEI statutes is misguided. She further explained that his position is based on a faulty premise that the IGA used the statutes to dictate rate design in base rate cases. Ms. Stull stated the statutes are stand-alone statutes and nothing in the statutes pretend to dictate how rates should be designed. Moreover, Ms. Stull explained that the IGA did not remove the Commission's discretion to reject rate designs that have a disparate effect on certain customers or its ability to consider reasonable allocation of costs. *Id.* at 7. Conclusively, Ms. Stull argued that the Commission's powers to set cost-based rates in base rate cases remains unfettered by the DSIC and SEI statutes.

Ms. Stull testified that the capital improvements recovered through existing DSIC and SEI trackers are not included in Petitioner's rate base. Instead, Petitioner has proposed to include the cost of the eligible capital improvements in rate base in this case and, once it is approved by the Commission, the costs will be included in Petitioner's rate base resulting in the DSIC and SEI being reset to 0. Furthermore, Ms. Stull stated that the revenue requirement in a capital tracker filling is not allocated to customer classes. Ms. Stull explained that it is neither reasonable nor necessary to continue to include capital tracker charges in the fixed monthly charge to address any perceived rate class inequities. Instead, that is the purpose of the cost-of-service study in a base rate case. *Id.* at 8.

Ms. Stull noted the Commission did not address Petitioner's proposal regarding the recovery of capital tracker revenue requirement through a fixed charge in Cause No. 45142. Ms. Stull then addressed the reasonableness to continue to include capital tracker charges in the fixed charge for residential and other small water consumers, to which she deferred to the testimony of OUCC witness Jerome D. Mierzwa. *Id.* at 9.

Finally, Ms. Stull addressed Mr. Callocchia's assertion that Petitioner's proposed $20 fixed charge is based on including 50% of the current capital tracker plant as part of the fixed charge. Ms. Stull addressed that this position does not add up, stating the current cost of water is greater than the difference between $15.26 and $20.00. *Id.* at 9. Moreover, Ms. Stull stated that the OUCC's lack of opposition to the proposed $20.00 is not because it thinks it is appropriate to include 50% of DSIC plant costs into the fixed charge. Ms. Stull ultimately recommended that the Commission deny the recommendations of the Industrial Group, Wholesale Customers, and the City of Crown Point that the DSIC and SEI trackers should continue to be collected through a fixed charge once those costs are moved into base rates. *Id.* at 9.

ix. <u>Discussion and Findings</u>. As is not infrequent in general rate cases involving multiple intervenors consisting of different customer types, there is much disagreement among the parties regarding the assumptions made in Petitioner's cost of service study. We will proceed to address those disagreements, but it is important to put those disagreements in the context of this case. Petitioner has not designed its rates based upon its cost of service study. Instead, the underlying reason for the dispute over the cost of service study is that Mr. Rea's analysis shows that the industrial and SFR customers are being heavily subsidized by residential customers. Because of that subsidy, Mr. Rea has proposed the increases for these two classes be held at 150% of the overall system average. In contrast, the witnesses for the Industrial and SFR customers ask for Mr. Rea's study to be ignored and that rates be increased in across-the-board fashion. 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. Notably, none of the intervenors representing Industrial or SFR customers presented their own cost of service study.

The subsidy identified by Mr. Rea is not new. We find compelling Mr. Rea's summary on rebuttal of the results of the cost of service studies presented in the Company'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. This does not strike us as coincidental. Instead, it reveals that these three cost of service study professionals have identified a long-standing and growing subsidy in the Company's rate structure, and none

of the Industrial or SFR intervenors have presented their own study proving otherwise. This is relevant background information as we address the request of the Industrial and SFR customers that we disregard Mr. Rea's study in favor of an across-the-board increase. With that background, we now proceed to address their objections.

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 myriad ways suggested by the OUCC and 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. SFR intervenors have suggested that it is cheaper to serve their class than any other customer class and the cost of service analysis indeed bears that out.

Transmission and Distribution Costs. In the cost of service analysis in this case, the total net plant split for mains between the Transmission and Distribution function is 25.8% for Transmission and 74.2% for Distribution. In the current 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 would be logical based on the nature of investment made since the last case which has been reflected in the DSIC mechanism. As a result, a bigger share of total mains investments is allocated to residential and commercial customers and away from industrial and SFR customers. *See* Pet. Ex. 18 at 38.

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. *Id.* at 45.

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 the Company for these classes.

Purchased Power Costs. While we agree the Company 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 the Company incurs is significantly higher during periods of high demand than during periods of low demand. Accordingly, 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. Pet. Ex. 18 at 51.

Low Income and COVID Costs. INAWC's rebuttal cost of service analysis removes allocation of these expenses to the SFR class.

In sum, we find that Mr. Rea's cost of service study, as modified on rebuttal, is appropriate and useful for purposes of reviewing the Company's proposed rate increase allocation.

B. Rate Design.

i. INAWC Case-in-Chief. Mr. Rea also sponsored the Company's proposed rate design. Mr. Rea 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. Pet. Ex. 5 at 18-19. He explained that while cost causation is the foundation of the Company's rate design, the other principles are layered on top of cost causation to result in a rate design that is fair to all customer groups and is just and reasonable. *Id.* at 20. Mr. Rea explained that the Company's current rate design for general service and sales for resale 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. *Id.* Monthly meter charges are differentiated between general service and sales for resale. Meter charges are not differentiated between Area 1 and Area 2. *Id.* at 20-21. Mr. Rea explained that Distribution System Improvement Charges ("DSIC") and Service Enhancement Improvement ("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. *Id.* at 21. Volumetric rates for sales for resale are separate from general service rates and are also on a declining block rate structure. Volumetric rates for sales for resale are not differentiated between Area 1 and Area 2. *Id.* 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. *Id.* Additional tariffs are in place to provide service to two newly acquired service territories; River's Edge and Lowell. *Id.*

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, the Company is proposing to consolidate volumetric rates for Area 1 and Area 2 customers. *Id*. at 21. 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 in the Company's proposed rate) at no additional charge beyond the monthly meter service charge. *Id.* at 21-22. Mr. Rea testified that the Company is proposing an allowance-based rate to enhance affordability of Basic Water Service, especially for the Company'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. Changes to pricing structures that automatically

reach all customers with no need to apply or enroll or track customer data are consistent with rate designs that adhere to the rate design principle of simplicity and feasibility. *Id.* at 22-23. He stated an allowance-based rate design reduces 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). *Id.* at 23. He presented data from the National U.S. Census Bureau on the average size of household by household 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. *Id.* at 24.

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. *Id.* at 25. This comparison showed that the vast majority of the Company's customer base that may have issues of affordability of service would do better under the allowance-based rate than under the Company's standard rate design. *Id.* at 25-26. 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. *Id.* at 29. 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. *Id.* at 30. Mr. Rea stated that if a) 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, b) higher income customers are more likely to have significant higher cost seasonal water use than lower income customers, and c) a single volumetric rate applies to all service for all customers, both Basic Water Service and seasonal service as is the case in the Company's service territory, the result is that lower income customers are actually subsidizing higher income customers under the Company's current rate design. *Id.* He testified the biggest impact of the allowance-based rate will be seen by lower use residential customers regardless of their household income. *Id.* at 31. 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 the Company's proposed rates. *Id.* at 32.

Mr. Rea further testified that the Company proposes to consolidate Area 1 and Area 2 rates and to increase the base rate monthly meter charge. He then described the treatment of recently acquired systems within the Company's proposed rate design. *Id.* at 33.

Mr. Rea testified that the Company used the following general guidelines in allocating the proposed Step 3 revenue increase to customer classes as follows: (1) Increases to industrial and sales for resale 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 sale for resale customers and as noted previously, Mr. Rea noted that cost of service continues to indicate significant increases for industrial and resale 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. *Id.* at 34.

Mr. Rea also presented the Company'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 is proposing to move 35% of the proposed wastewater revenue requirement (Step 3) to water service customers to be collected through water service rates. *Id.* at 36. 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. *Id.* 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. The Company'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. *Id.* He noted the impacts on water service customers of this proposal is minimal, representing approximately $0.07 per hundred gallons for the Company's residential water service customers or a bill impact of approximately $0.27 per month for a residential customer with average usage. *Id.* at 37. Without this proposal, however, the average wastewater service bill would be approximately $150 per month.

ii. **OUCC**. 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 the Company for the Industrial and Sales for Resale classes. Pub. Ex. 8 at 3-4. For Steps 2 and 3, Mr. Mierzwa recommended Sales for Resale rates should be proportionately increased to provide for an increase which 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. *Id.* at 4. He also recommended that any reduction to the Company's requested wastewater revenue requirement first be applied to reducing the wastewater revenue requirement to be recovered from water service customers. *Id.* at 4.

Mr. Mierzwa testified that at the conclusion of Step 3, under the Company'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 Sales for Resale classes will be contributing revenues less than the indicated cost of service. Pub. Ex. 8 at 22-23. He recommended reducing these differences to the extent possible while maintaining gradualism. *Id.* at 23.

Mr. Mierzwa noted that while Petitioner has proposed increases of approximately 2.0 times the system average increase at Step 1 for the under-earning Industrial and Sales for Resale classes, the Public Authority class is also under-earning. He recommended a separate schedule of volumetric charges be established for the Public Authority class that would result in a Step 1 increase comparable to the 2.0 times system average increases proposed for the Industrial and Sales for Resale classes. He then 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. *Id.* at 23. For Steps 2 and 3, Mr. Mierzwa recommended the Sales for Resale rates be proportionately increased to provide for an increase which is 2.0 times the system

average increase. *Id.* For the Industrial and Public Authority classes, he recommended that the volumetric rates for rate blocks 3 and 4 be proportionately 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 Sales for Resale, Industrial, and Public Authority customer class should be utilized to reduce the rate block 2 volumetric rate. *Id.* at 24.

iii. Industrial Group. Ms. York proposed that the subsidy proposed by Petitioner to be paid by water customers for the cost of providing wastewater service be reduced by the greater of either 25% of the Company's proposed subsidy of $1.6 million, or by the amount of reduction in wastewater revenue requirement Mr. Gorman recommends, plus $100,000. IG Ex. 1 at 4. Under this proposal, wastewater rates would be set equal to those proposed by the Company, with any reduction to the wastewater utility's revenue requirement being reflected as a reduction in the amount of wastewater revenue requirement the Company has proposed to collect from water customers. *Id.*

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 sale-for-resale 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 the Company begin this process by implementing an Industrial rate schedule at the conclusion of this case. *Id.* at 3 and 33. She contended that a separate Industrial rate would allow the Company to more accurately allocate costs within the class to reflect the distinction in infrastructure used to provide service. She stated it would also allow the Company to recover costs from Industrial customers in a manner consistent with cost of service principles, without materially impacting other rate classes. *Id.* at 33. She designed an industrial rate for illustrative purposes. *Id.* at 35; Attachment JAY-3.

Ms. York also recommended that the revenue requirements that are being rolled to base rates associated with the Distribution System Improvement Charge ("DSIC") and the Service Enhancement Improvement ("SEI") charge continue to be recovered from customers on a per meter basis. *Id.* at 3 and 37.

iv. 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 plan language of IC 8-1-31-8, the Company's previous testimony, and cost causation principles. Wholesale Customers Ex. 1 at 3-4. He stated the Company 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 the Company collect DSIC and SEI revenue requirements related to the currently effective charges 100% via meter charges. *Id.* at 23.

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 the Company to wheel water through the Company's system. *Id.* at 24-25.

v. Crown Point. 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." Crown Point Ex. 1 at 7 and 10. He advocated for a transportation rate as an alternative for Crown Point to obtain Lake Michigan water. *Id.* at 7.

vi. **CAC**. 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. CAC Ex. 1 at 29-30. 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. *Id.* at 30. 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. *Id*.

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. *Id.* at 32.

vii. **INAWC Rebuttal**. Mr. Rea responded to the OUCC and intervenor challenges to Petitioner's rate design proposals. He opposed CAC witness Inskeep'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. Pet. Ex. 18 at 6. In addition, Mr. Rea testified that approximately 10% of the water that the Company 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. *Id.* 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. *Id.*

Mr. Rea testified that the proposed $20.00 meter charge is supported by the Company'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. The Company's proposed $20.00 charge is just under that calculated value. Pet. Ex. 18 at 59.

With respect to DSIC and SEI related costs, Mr. Rea responded on rebuttal that he proposed the 50-50 split as a compromise on the allocation of DSIC and SEI charges in anticipation that parties would have the same dispute among them as in the last rate case. He explained that DSIC and SEI related investments are not accounted for separately in the

Company'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 cost of service study. *Id.* at 43.

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 has been suggested by Ms. York or implied in part by Mr. Mierzwa. *Id.* at 60. 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 of the impacts to customers are well understood. *Id.* 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. *Id.* at 61. He stated there will always be winners and losers in the process of changing rate design and these impacts need to be well understood. *Id.*

Mr. Rea opposed the recommendation of the Wholesale Customers 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. *Id.* at 62. 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 which would need to be calculated so as to avoid harming the non-transportation customers. Mr. Rea stated that if the transportation customers desired the Company to serve as a back-up source of supply, then an appropriate back-up rate would need to be calculated. *Id*. at 62-63.

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. *Id.* at 65-66. 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. *Id*. at 69-70. He testified that Ms. York's proposal was unacceptable because it would in many cases result in higher wastewater bills than those proposed by the Company and would run counter to the Company's goal of keeping the average residential wastewater bill below $100 per month. *Id.*

viii. <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.[44] We further find that Petitioner's proposals achieve a rate design that is fair to all customer groups and is just and reasonable. As noted in our discussion of "Affordability" we find Petitioner's proposed allowance-based rate to be an innovative manner 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 Mr. Rea'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. The Company proposed in its case and chief that these classes receive an allocation of 150% of the overall system average. The OUCC proposed that the SFR and Industrial classes receive an increase supported by cost of service capped at 200% or 2.0 times the overall system average. The Industrial and SFR customers proposed an across-the-board increase disregarding the cost of service findings in Petitioner's study. Based on our prior findings regarding cost of service and the subsidies currently enjoyed by Industrial and SFR customers, we reject their proposal. The Company proposed we reject the OUCC's proposal to cap the increase at 2.0 of system average, stating the OUCC had cited no prior decisions approving an increase for a class so high in relation to the overall system average.

We reject the supposition that the OUCC must rely on prior orders to support an allocation that is closer to cost of service than any proposed by the Company or the SFR and Industrial class parties to this proceeding. Indeed, the burden must be on the parties deviating from cost of service to justify such a departure. Mr. Mierzwa testified that, while there is no hard and fast rule as to applying the principle of gradualism, typically, an increase of 1.5 to 2.0 times the system average increase would be consistent with the concept of gradualism. Pub. Ex. 8 at 18. We consider the OUCC's proposal to be a more moderate departure from cost of service and consequently more reasonable under the facts of this case. Mr. Rea testified in his rebuttal case that such a move would be too drastic in the name of cost of service. Mr. Mierzwa summarized the increases Indiana American proposed in Table 3 of his primary testimony. Pub. Ex. 8 at 18. His Table 3 indicates IA gives Industrials and the SFR customer classes 200% of system average increases in year 1 (i.e., Step 1) and 5.7% of system average in Steps 2 and 7.5% of system average in Step 3. The OUCC's proposal would have the SFR and Industrial Classes an increase of 11% of system average in Step 2 and 15% in Step 3. We do not find the OUCC's recommendation to be unreasonable for classes that are allocated less than their cost of service, particularly since the Residential class will be receiving higher than system average increases. The Company proposed we find that an 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 and of gradualism." We disagree. Petitioner's DSIC and SEI revenues are recovered through a fixed per meter charge between rate cases, which results in a subsidization of the SFR and Industrial classes between rate cases. This subsidization is not corrected by a subsequent rate

[44] NTD: In the event that the Commission authorizes an increase in water rates that is less than the requested increase, the Company proposes to reduce water service volumetric rates on a pro rata basis until the difference between the authorized increase and the requested increase is met (OUCC DR 03-001). *See* Pub. Ex. 8 at 21.

order to the extent that rate order does not implement full cost of service. Exceptions to cost of service principles that may be established by the DSIC or SEI, only apply to implementation of those trackers, which are reset to zero with the implementation of new base rates.

The Commission's powers to set cost-based rates in base rate cases remains unfettered by the DSIC and SEI statutes. Such subsidization should be extinguished by intervening rate orders. An allocation to the SFR and Industrial classes at 150% of the overall system average does not *strike an appropriate balance between gradualism and moving these classes closer to cost of service.* Rather, it is too slanted toward gradualism because it exacerbates subsidization by the residential class. Further, for Steps 2 and 3, the Company proposes the under-earning Industrial, Public Authority, and Sales for Resale customer classes be assigned slightly lower increases than the over-earning Residential and Commercial customer classes. We agree with the OUCC that this is unreasonable. We find an allocation for the SFR and Industrial classes at 200% of the overall system average does strike an appropriate balance between gradualism and moving these classes closer to cost of service. *Wastewater Reallocation*. 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. Accordingly, we find that a reallocation should be approved. The only dispute centers on how the reallocation changes based upon any changes to the Company'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 the Company 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.

Meter Charge/Allowance Rate. No party opposed the Company'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 only other issue on the meter charge is the proposal by the Industrial Group and SFR customers that costs previously being recovered through the DSIC and SEI continue to be recovered through a fixed charge. We reject the suggestion by these customers that the General Assembly intended these costs to be recovered through a fixed charge in perpetuity. The legislation is clear that the DSIC and SEI charges are to be a fixed charge by meter size but that these charges are reset in the context of a general rate case. We find that Mr. Rea's proposal to recover half of the costs through fixed charges and half the costs through volumetric charges strikes an appropriate balance in the context of this case.

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 this Commission has approved a transportation rate for a water utility. More tellingly, they did not testify that such a rate would be in the public interest or that it would not harm other customer classes. This is not like the natural gas industry, where a federal policy exists to unbundle the sales of natural gas. This is water, and there can be a multitude of reasons 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. There was insufficient evidence accompanying the proposal as to its potential impacts on non-transportation customers. Accordingly, we reject it.

C. Universal Affordability Tariff.

i. INAWC Case-in-Chief. 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 FPL. The tariff offers discounts on both the basic 5/8" meter charge and the volumetric charges for water service. Pet. Ex. 5 at 38. INAWC witness Rea explained that the driving principle behind the Company'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. *Id.* at 39. 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, regardless of the level of rates approved in this proceeding. Mr. Rea stated the Company's proposed tariff along with the tariffs and process proposed for general water service in this proceeding will provide every Indiana American water service customer access to pricing tools that are designed to help ensure that the cost of Basic Water Service will be no more than 2% of their annual household income. *Id.* The Company's proposed tiered discounts are designed to provide customers at each interval of FPL the opportunity to have Basic Water Service bills in the 1% to 2% range of household income. *Id.* at 41.

ii. OUCC. Mr. Bell testified that the proposed Universal Affordability Tariff is not in the public interest and should be rejected. He asserted it does not protect the affordability of utility services for present and future generation of Indiana citizens as required by Ind. Code § 8-1-2-0.5. Mr. Bell explained that neither Indiana American nor American Water Works Company, Inc. proposes to contribute any funds to providing bill discounts through the proposed "Universal Affordability Tariff." Rather, the bill discounts are to be funded solely and involuntarily by captive ratepayers who will not have the option to opt-in or opt-out of funding the discounts.[45] Finally, 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

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[45] Mr. Bell noted Indiana American's response to OUCC DR 22-021(a) which stated that the "proposed water affordability discount provided to low-income customers is being subsidized primarily by residential customers because it is residential customers who are primarily the beneficiaries of the subsidies provided by low-income customers."

of bill discounts to qualifying low-income customers in the Terre Haute, Muncie and Northwest/Gary districts.[46]

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 also pointed out that 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 what Petitioner proposes to recover in this case. Mr. Bell explained 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, while I.C. § 8-1-2-46(c) allows utilities to establish programs to charge customers lower rates or provide discounts based on something other than usage characteristics of a kind of customer, that does not mean that any program a utility proposes is in the public interest or should be approved. He added 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 company contribution whatsoever. Mr. Bell noted that nothing in I.C. § 8-1-2-46(c) 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. ("American Water"), 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 noted Mr. Rea proposed a 10% level of customer participation in the bill discounts to determine the amount of funds to include in rates to recover from customers. Mr. Bell pointed out that this proposed 10% 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. considered Mr. Rea's prospective level of assistance to customers to be unsupported by Mr. Rea's testimony. Mr. Bell pointed out that in Cause No. 45142, Mr. Rea testified that one of the reasons Indiana American was proposing its LIPP was to "gauge interest in the program among low-income customers to see if rollout of the program on a statewide basis is useful."

Mr. Bell explained that in the Settlement Agreement in Cause No. 45142, Indiana American agreed to add the Gary/NW district to the LIPP and contribute up to $150,000 per year

[46] Mr. Bell explained that in the Settlement Agreement in Cause No. 45142, Indiana American agreed to add the Gary/NW district to the LIPP and contribute up to $150,000 per year to fund the LIPP. Customers were to contribute up to $150,000 (recorded as a deferred asset) to fund the program, for a combined total of up to $300,000 of assistance per year - up to $1.2 million over the past four years (2019-2022). He explained that Indiana American has administered only $90,885 out of $1.2 million of available assistance to qualifying low-income customers. 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 testified that Company estimates that there are approximately 28,000 water service customers in the Gary, Muncie, and Terre Haute service territories that would qualify for these benefits based on their household income.

to fund the LIPP. Customers were to contribute up to $150,000 (recorded as a deferred asset) to fund the program, for a combined total of up to $300,000 of assistance per year - up to $1.2 million over the past four years (2019-2022). He explained that Indiana American has administered only $90,885 out of $1.2 million of available assistance to qualifying low-income customers. 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 were embedded in the proposed rate design.

iii. **CAC**. 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. CAC Ex. 1 at 23 and 26-27.

iv. **INAWC Rebuttal**. Mr. Rea testified on rebuttal that more households and families in Indiana will have access to affordable water and wastewater service with the Company's proposed universal affordability tariff than without it. Pet. Ex. 18 at 23. In his opinion this meets the definition of protecting the affordability of utility service for present and future generations of Indiana citizens. *Id.* 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). *Id.* at 24. Given that, Mr. Rea opined it does not make sense to ask Company shareholders to forego recovery of its cost of providing service in order to fund discounts for lower income customers and leave higher income customers still being subsidized. *Id.* Mr. Rea explained that the LIPP and Universal Affordability tariff are designed differently, and the LIPP launched just prior to the COVID-19 emergency. Therefore, the challenges of the LIPP should not be used to deny the Universal Affordability Tariff proposed here. *Id.* at 24-25.

Mr. Rea disagreed with CAC witness Inskeep's recommendation to expand eligibility for the Universal Affordability Tariff. While Mr. Rea recognized that many Indiana families live every day under financial hardships and every penny counts, he stated there does need to be balance between reducing bills in order to make them more affordable and the costs of the discounts that must be borne by others. *Id.* at 25.

v. **Discussion and Findings**. I.C. § 8-1-2-46(c) provides the Commission may approve requests by utilities to establish programs to charge customers lower rates or provide discounts based on something other than usage characteristics of a kind of customer. And while it provides that a lower rate or discount for certain customers is not considered discriminatory, it does not state that the utility may impose the cost of such a program on the customers of the utility. However, as Mr. Bell pointed out Indiana American proposes that the bill discounts under its proposed "Universal Affordability Tariff" are to be funded solely and involuntarily by captive ratepayers who will not have the option to opt-in or opt-out of funding the program. Indiana American proposes no contribution or participation from Indiana American or its parent company. In prior years, the Commission has approved two settlements of rates

cases that included low-income programs that were funded in part by non-voluntary contributions from other ratepayers. However, those programs differed from the program Indiana American now proposes in three important ways. First, they were pilot programs authorized pursuant to settlement agreements. Second, those two programs involved finite and established levels of ratepayer participation. Finally, both utilities proposing those programs committed to afford funds for the program.

In CWA Authority, Inc., Cause No. 45151, we approved a program that was funded via a $0.45 monthly charge per customer and a $200,000 annual utility contribution. The second involved this utility. In Indiana-American Water Company, Inc., Cause No. 45142, we approved a three-year pilot low-income program that was funded through both customer rates and matched contributions from the utility. In both Cause Nos. 45151 and 45142, the low-income programs were part of a case settlement.

In CUII, Cause No. 45651 we denied a water and wastewater utility's request for approval of a CUII proposed a customer assistance program not unlike the program Indiana American has proposed in this case. Like Indiana American, CUII proposed to have its ratepayers fund 100% of its low-income program without any utility contribution. Where in that cause the OUCC pointed out the lack of company participation in the expense, the utility responded that any imposition of a requirement for the utility or its shareholders to subsidize the rates of its customers would be confiscatory; arguing that the utility is entitled to its authorized return. We found that it would not be confiscatory for CUII or its shareholders to voluntarily fund a portion of Petitioner's low-income program. And we agreed that it would not be confiscatory for CUII's customers to voluntarily subsidize other customers through a round-up or opt-in program. As in that case, Indiana American chose to design a program that has its non-qualifying residential ratepayers fund 100% of its low-income program without any utility contribution. As we noted in the CUII case where we denied approval of its program, Indiana American's proposal would unreasonably shift the longstanding responsibility of the utility for providing just and reasonable rates to all customers onto its non-qualifying residential ratepayers.

Mr. Bell explained 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. While procuring such benefits for its shareholders will be free to Indiana American or its parent, its customers will pay a cost. 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).

Also, 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 what Petitioner proposes to recover in this case. Thus, unlike the customer assistance programs we approved through settlements, the price tag for its customers in the future is unknown. Such recovery presents two inequities. Customers will be subsidizing other customers' usage, and further such usage will be from the past causing an intergenerational inequity of undetermined amount.

Finally, this request for approval of customer assistance program is unique because it is the only request under IC 8-1-2-46 that is from a utility that had been approved another program as a pilot. We cannot ignore the fact that under its LIPP program, which we approved in our final order in Cause No. 45142 (June 26, 2019), Indiana American proved itself inept at providing financial assistance to low-income customers. Where Indiana American had indicated a 10% level of customer participation in the bill discounts participation was one half of one percent (.5%). Mr. Rea's explanation that it is because the LIPP was launched just prior to the COVID-19 emergency is not convincing. There is no evidence customer need for assistance was interrupted by COVID-19. If anything, the COVID-19 would have increased the need for assistance. As to the explanation that the LIPP and the Universal Affordability Tarriff are structure differently, we see no difference that makes one more viable than the other. But Indiana American's lack of success in its pilot program makes us reluctant to embed the cost of the program in rates.

As Mr. Bell noted in the Settlement Agreement in Cause No. 45142, Indiana American agreed it would contribute up to $150,000 per year to fund the LIPP. Customers were to contribute up to $150,000 (recorded as a deferred asset) to fund the program, for a combined total of up to $300,000 of assistance per year - up to $1.2 million over the past four years (2019-2022). But Indiana American has administered only $90,885 out of $1.2 million of available assistance to qualifying low-income customers. 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. And where in the Settlement Agreement Indiana American agreed to add the Gary/NW district to the pilot program, participants in Gary/NW were 1 customer in 2020, 1 customer in 2021, and no customers in 2022. Pub. Ex. 1, p. 25.

After considering the evidence of record, and for the foregoing reasons, we find that Indiana American's proposed low-income program is not in the public interest and is therefore denied.

D. Montgomery County Surcharge.

i. INAWC Case-in-Chief. Petitioner proposed a new surcharge that would apply to the Company's operations in Montgomery County based upon an ordinance adopted by the Montgomery County Board of Commissioners establishing an "Infrastructure Zone" and requesting the Company extend water mains pursuant to I.C. § 8-1-2-42.6. Pet. Ex. 2 at 44, Attachment GDS-3.

Mr. Shimansky described the Company's investment in Montgomery County. Phase 1 consisted of installation of a water main to extend service east towards I-74. Pet. Ex. 2 at 45. Phase 2 consisted of installation of a main, a booster station, and a water tower. *Id*. 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. *Id*. 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. Pet. Ex. 2 at 45.

Mr. Shimansky further testified that $2,777,506 is included in the Rate Base actuals through September 2022 for this project. *Id*. He explained that these costs are to be recovered through a surcharge on Montgomery County customers in the Company's Crawfordsville District only. *Id*. He testified there are 6,339 customers, not counting private fire protection meters, and, in order for these customers to reimburse the Company for these costs in compliance with the ordinance, the Company will charge $3.54 per meter per month on their regular water bill. *Id*. Mr. Shimansky testified this number has been reduced for revenues received from a large customer in the area. *Id*. at 45-46. Mr. Shimansky sponsored two attachments in connection with the Montgomery County surcharge - Attachment GDS-3 is a copy of the Montgomery County Ordinance and Attachment GDS-4 is a workpaper calculating the per-meter monthly charge. *Id*. at 46.

Mr. Shimansky testified that the extension satisfies subsection (c) of Section 46.2. *Id*. He testified, however, that if the request under subsections (d) and (e) were denied, without the surcharge, Indiana American would recover the Company's costs of its portion of the investment from all customers across the State. *Id*.

ii. <u>OUCC.</u> Ms. Stull opposed Indiana American's proposed Montgomery County surcharge because: (1) the Company did not request approval of the project before completing it; (2) application of the surcharge throughout Montgomery County is contrary to the Company's agreement with the County and the County Redevelopment Commission; and (3) the OUCC has questions about the overall calculation of the surcharge. Pub. Ex. 3 at 48-53. Ms. Stull proposed that the Company include "the costs [of the project] in its rate base and recover[] these costs through its cost-of-service allocation to the appropriate customer classes." *Id*. at 52.

iii. <u>INAWC Rebuttal.</u> On rebuttal, Mr. Shimansky responded to Ms. Stull's criticisms of the Montgomery County surcharge. Pet. Ex. 15 at 17-20. Mr. Shimansky explained that Ms. Stull did not oppose the project underlying the proposed surcharge; instead, she only opposes the surcharge and proposes that the Company include the costs of the project in rate base and recover those costs through its cost-of-service allocation to the appropriate customer classes. *Id*. at 18. In response to Ms. Stull's contention that the request for approval of the project should have been made prior to installation in order for 42.6 to apply, Mr. Shimansky testified that the statute only requires approval of the project and there is no objection to the underlying project. *Id*. at 18. Mr. Shimansky testified the question is one of rate design, which he believes the Commission can approve with or without a statute specifically directing it. *Id*. Mr. Shimansky further testified that the Montgomery County Board of Commissioners specifically requested a main extension to support an economic development project for Montgomery County, and they did so with full understanding that it would result in a surcharge imposed on the constituents who are customers of Indiana American. *Id*. Mr. Shimansky did not understand why the OUCC opposes the surcharge and instead requests that the costs of the underlying project be rolled into the calculation of the rates of all customers. *Id*.

In response to Ms. Stull's contention that the imposition of the surcharge is contrary to the agreement between the Company 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

and this ordinance was included as Attachment GDS-3 to his direct testimony. *Id*. at 19. Mr. Shimansky testified that the ordinance very 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." Mr. Shimansky testified that therefore between signing the agreement and adopting the ordinance, the County concluded it would be better for the surcharge to apply throughout Montgomery County. Pet. Ex. 15 at 19.

Mr. Shimansky also responded to the four concerns Ms. Stull raised regarding how the surcharge was calculated, and addressed her concerns in his rebuttal testimony, arguing that the surcharge was correctly calculated. *Id*. at 19-20. Mr. Shimansky testified the Company is accepting the OUCC's position that the Company'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 Attachment GDS-3R. *Id*. Mr. Shimansky ultimately recommended that the Montgomery County Surcharge be approved as revised in Attachment GDS-3R (removing the property taxes). *Id*. at 20.

iv. <u>Discussion and Findings.</u> Montgomery County requested Indiana American extend water service to an area that had been designated as an infrastructure development zone ("IDZ"), pursuant to I.C. § 6-1.1-12.5-4, which in turn implicates I.C. § 8-1-2-46.2(d). Indiana American cites I.C. § 8-1-2-46.2 to support its request for a surcharge payable by its customers in the Town of Waveland and the City of Crawfordsville ("Montgomery County Surcharge"). The specific statutory sections discussing the implementation of a surcharge are I.C. § 8-1-2-46.2(d) and (e):

> (d) Subsection (e) applies if:
> (1) a county executive, a municipal legislative body, or, in Marion County, the county fiscal body, establishes an infrastructure development zone under IC 6-1.1-12.5-4; and
> (2) the county executive, municipal legislative body, or county fiscal body requests a public utility to extend water or wastewater utility service to the geographic territory established as the infrastructure development zone.
>
> (e) A water or wastewater utility that receives a request described in subsection (d)(2) may file a petition with the commission seeking approval of the requested extension of service. If the commission approves the petition, in future general rate cases, the commission shall approve rate schedules that include a surcharge payable only by customers located in the geographic area within the jurisdiction of the governmental entity described in subsection (d), or, if requested by the governmental entity, only within the geographic area established as an infrastructure development zone. The surcharge shall recover depreciation expense, weighted cost of capital, and federal and state income tax applicable to the extension of water or wastewater utility service.

Montgomery County requested that Indiana American extend water service, and the County created a specific IDZ under I.C. § 8-1-2-46.2(d). The County both passed an ordinance and entered into an agreement with Indiana American memorializing the extension of service. *See* Pub. Ex. 3, Att. MAS-11. Thus, the requirements of I.C. § 8-1-2-46.2(d) were met. As described in the agreement, Phase I of the proposed project included "the extension of water

distribution facilities from INAW's Crawfordsville facilities east along State Road 32 to Nucor Road." *Id*., p. 3. Phase II of the project included "the extension of water distribution facilities from the intersection of State Road 32 and Nucor Road south along Nucor Road to County Road 100 South." *Id*. As shown in Indiana American's evidence, Phases I and II of the Project were not in either the Town of Waveland or the City of Crawfordsville. Pub. Ex. 3, Att. MAS-12.

Triggering the conditions of I.C. § 8-1-2-46.2(e) required Indiana American to seek approval from the Commission; assuming that approval was granted, the Commission in a *future rate case* would be obligated to impose a surcharge on *either* customers within the jurisdiction of the governmental entity (Montgomery County) *or,* if requested by the governmental entity, upon customers in the established IDZ.

Mr. Shimansky stated that the County passed an ordinance after it signed the agreement with Indiana American, and therefore between signing the agreement and adopting the ordinance, the County concluded it would be better for the surcharge to apply throughout Montgomery County. Pet. Ex. 15 at 19. We note two things about this statement. First, it is unsupported by any documentary evidence that Montgomery County chose the course of action asserted by Mr. Shimansky. The agreement between Montgomery County and Indiana American states that its terms may only be changed by written agreement of the parties, and there is no evidence of such a modified agreement. Second, the language of the agreement binds the parties to its terms, and those terms mandate payment of the surcharge by customers within the IDZ. Although the agreement was amended (as shown in MAS-11), the amendments did not change who was responsible for paying the surcharge. In the agreement, Indiana American committed to:

> recover the cost of design, construction, easement acquisition and other expenses over a period of 20 years by way of a *surcharge to users in the Service Territory* after approval of such surcharge by the [Commission. The [County Redevelopment Commission] may, but is not obligated to, contribute its funds to INAW in order to offset the costs of construction in order to lower the amount of the Surcharge to ratepayers. For purposes of this agreement, *the term "service territory" means the approved infrastructure development zone*[.]

Pub. Ex. 3, Att. MAS-11, p. 4 (emphasis added).

Reviewing the language of I.C. § 8-1-2-46.2(e), we note that the statute imposes a temporal element; it states that if the Commission approves a petition by a utility for an extension, "in *future* general rate cases, the commission shall approve rate schedules that include a surcharge[.]" IAWC argues that it did not need to seek approval for the extension and that the OUCC does not contest the prudence of the project. The question is not one of prudence; the question is how Indiana American will recover the remaining costs of the extension. As Indiana American did not have Commission approval for the extension at the time it brought this rate case, its use of I.C. § 8-1-2-46.2(d) for approval of the surcharge is misplaced. The statute sets a clear condition precedent for the approval of a surcharge: *if* a utility gets approval, *then* the Commission shall approve a surcharge. On this basis alone, we could reject Indiana American's request for the Montgomery County surcharge.

Even had Indiana American received prior Commission approval for its extension, any applicable surcharge would be payable by Indiana American customers in the IDZ. The reason for this is the statutory language that the surcharge would be "payable only by customers located in the geographic area within the jurisdiction of the governmental entity described in subsection (d), *or, if requested by the governmental entity, only within the geographic area established as an infrastructure development zone.*" Emphasis added. The agreement between Indiana American and Montgomery County clearly states that the surcharge is payable by users in the Service Territory, defined as the approved IDZ. As shown in Indiana American's evidence, the IDZ does not cover Waveland or Crawfordsville. Through its agreement with Indiana American, Montgomery County evidenced its intent that the surcharge be payable by customers within the IDZ. We view this as the governmental entity "requesting" that the surcharge be paid by users in the IDZ, as contemplated by I.C. § 8-1-2-46.2(e). We therefore reject Indiana American's argument to the contrary.

While I.C. § 8-1-2-46.2 creates a means to cost recovery for extensions of service, we find that Indiana American did not comply with the requisite statutory terms. While some measures were followed (Montgomery County passed an ordinance, established an IDZ, and reached an agreement with IAWC), the provision that a utility seek Commission approval prior to the granting of a surcharge was not. The statute clearly states that "[i]f the commission approves the petition, in future general rate cases, the commission shall approve rate schedules that include a surcharge[.]" The language is clear that the approval must occur first, not at the same time as the surcharge being sought.

As a consequence, the default result is that the requested $2.7 million for the extension should be included in IAWC's rates. This is consistent with Indiana American's alternate position presented by Mr. Shimansky, in such case that this Commission refuses to approve Indiana American's requested surcharge. Shimansky Rebuttal at 46. As is the case with all physical plant, it will be recovered through base rates payable by all of IAWC's customers. We therefore deny Indiana American's request for a surcharge payable by its customers in Waveland and Crawfordsville.

15. <u>URT Repeal</u>.

A. <u>INAWC Case-in-Chief</u>. INAWC witness Shimansky explained the URT over-collection. He described the repeal of the URT through House Enrolled Act ("HEA") 1002 effective May 1, 2022 and the Company's 30-Day filing to remove the URT from its revenue requirement effective July 1, 2022. Pet. Ex. 2 at 46. 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. *Id.* 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 $1,356,008.24 that needs to be returned to customers. *Id.* 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. *Id.* at 47, Attachment GDS-5 and GDS-6.

B. <u>OUCC</u>. 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 the Company should pay customers for the use of the over-collected funds at the Company's weighted average cost of capital. Ms. Sullivan noted that there was no reason for the Company to wait to refund the overcollection. Pub. Ex. 2 at 18-19. She contended that the Company's proposed revenue adjustment would only incorporate URT collected through September 30, 2022 despite URT being included in rates through November 23, 2022. The OUCC contends that customers should receive a direct refund in the amount of $1,356,008 plus carrying costs, to allow customers to know an overcharge has been corrected. *Id*.

C. <u>Industrial Group</u>. Mr. Gorman expressed concern that under INAWC's proposal, the Company will not have fully refunded customers until June 2024, roughly two years after it should have ceased collecting the URT from customers. IG Ex. 1 at 16. Mr. Gorman testified that throughout that period of time the Company has had access to, and been able to use, those funds for its benefit. He opined that customers should be compensated for the use of these customer funds by the Company. 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. *Id.* 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 *Northern Indiana Public Service Co. v. Citizens Action Coalition of Indiana, Inc*., 548 N.E.2d 153 (Ind. 1989), that ratepayers were entitled to simple interest at the statutory rate of 8% in the context of a utility refund. IG Ex. 1 at 17. 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 in order to properly compensate customers for the Company's ability to utilize the over-collection of the URT. *Id.* at 18. He proposed to include a carrying charge on the customer held funds from the time the excess tax was collected from customers until the customer refunds are completed in June 2024. He calculated this would increase the URT refund amount by approximately $184,000. *Id*., Attachment MPG-3.

D. <u>CAC</u>. Mr. Inskeep testified the Company had failed to follow directives and suggests INAWC 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 the Company not following the state law. CAC Ex. 1 at 33-34.

E. <u>INAWC Rebuttal</u>. INAWC witness Shimansky opposed the OUCC and intervenors' proposal to include carrying costs on a simple over-collecting, stating this is inconsistent with the other regulatory accounts included in the case, including the recovery of deferred COVID-19 costs, Comprehensive Planning Studies and Universal Affordability tariff costs. Pet. Ex. 15 at 44-45. 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. *Id.* at 45.

Moreover, Mr. Shimansky testified that Mr. Gorman's calculation of the additional refund amount to account for interest was incorrect. Mr. Gorman's proposed adjustment assumes that 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. *Id.* Mr. Shimansky further stated that if carrying charges were to be applied, they should be no higher than the weighted average cost of capital that the Commission finds in the Order this case, because there was no wrongdoing on the part of the Company. *Id.*

In response to Ms. Sullivan's testimony on the URT over-collection, 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 the Company 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. *Id.* at 46.

With respect to Ms. Sullivan's other recommendations, Mr. Shimansky opined that a separate line item on the bill would only create confusion as the URT is no longer in rates. He stated that calling out a particular line item on a bill for such a brief period of time will add unnecessary complexity to the bill. *Id.* at 46.

As for Mr. Inskeep's contention that the Company somehow acted improperly and as a result obtained ill-gotten revenues, Mr. Shimansky testified that is completely false and does not support Mr. Inskeep's recommendation that the Company be penalized through the ROE as a result. Pet. Ex. 15 at 47. Mr. Shimansky relayed how the Company followed the statute and IURC procedure. The OUCC objection to that 30-Day letter filing and the conclusion reached at the IURC made no mention of the Company doing anything incorrectly, illegal, or in lack of compliance. *Id.* He stated it is clear from the copies of the Company's URT repeal submissions (included in Pet. Ex. 15, Attachment GDS-7R) that the Company did nothing incorrectly and followed the established regulatory process. Mr. Shimansky urged that Mr. Inskeep's proposal to punish the Company should be denied. Pet. Ex. 15 at 47.

F. <u>Discussion and Findings</u>. Indiana American timely filed its tariff to remove URT, however, its filing was objectionable and resulted in the overcollection. See Cause No. 45734 S1. As between ratepayers and INAWC, INAWC was at fault for this overcollection and retention. Furthermore, INAWC did not take alternative action to return the funds to ratepayers, and instead, included the refund of overcollection in this rate case, which will have the effect of unjustly enriching INAWC for its continued retention of the overcollection. Applying carrying costs is not a punitive measure, but instead is a fair and reasonable measure to place ratepayers in the position as they would have been had the overcollection not been caused and had not occurred. We find the OUCC's recommendation is warranted.

16. **Non-Recurring Charges**.

A. **INAWC Case-in-Chief**. Mr. Shimansky presented the proposed Tariffs as Attachments GDS-1 and GDS-2 to Petitioner's Ex. 2. This included redlines of proposed changes to the Tariffs. As shown on GDS-1, p. 30 and GDS-2 p. 12, Indiana American did not propose any changes to its non-recurring fees, including its reconnection charge, insufficient funds charge, and after hours service charge. Pet. Ex. 2, Attachment GDS-1, at 30 and GDS-2 at 12. Mr. Rea explained how revenue projections for these fees were developed. Pet. Ex. 5 at 76. 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 twelve months ended September 2022 base year projected to forecast test year revenue amounts. *Id*.

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). Public's Ex. 2 at 27. She opined that Petitioner's non-recurring charges are out-of-date. *Id.* She said that the costs of these services have certainly increased over the past 10 to 13 years. Ms. Sullivan 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. Ms. Sullivan opined that waiting until the next general rate case, or just prior to the next general rate case, prevents over collection. *Id*.

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 the Company's stated goals underlying its Utility Affordability Tariff. CAC Ex. 1 at 45-47.

D. **INAWC Rebuttal**. In response to Mr. Inskeep, Mr. Shimansky explained he did not agree that all late fees, reconnection fees, after-hour charges, and insufficient fund charges should be eliminated. Pet. Ex. 15 at 62. He said these charges have been approved by the IURC as part of the Company's tariff and there was no forecast created in this case to change those fees. *Id.* He said the miscellaneous revenues created by those fees as they currently exist 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 the Company is not opposed to a filing to update these rates prior to the next rate case should the IURC feel that is necessary. He concluded that said, these fees and charges recover costs incurred by the Company, so outright elimination of the fees would not be appropriate. *Id*. Mr. Shimanski made no response to the testimony of Ms. Sullivan.

E. **Discussion and Findings**. As evidenced by the Company's case-in-chief filing and explained by Indiana American witness Shimansky, the Company 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. CAC seeks

to eliminate the charges. OUCC recommends the charges be updated to better reflect actual costs, and that Petitioner do so in its next rate case, or in a 30-day filing just prior to its next rate case.

The Commission is not persuaded to do as the CAC recommends and eliminate these fees. While the Commission has suspended the collection of these fees in extenuating circumstances, providing these services comes at a cost to the Company and as such, should be reflected in rates. Further, without a study, which no party put forth, there is a lack of evidence to show if costs to providing these services have increased or decreased and what the effect on the Company'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 amongst all customers. Pet. Ex 15 at 62. The Commission, in this instance, declines to make a change that affects costs allocation without further information. However, based on Mr. Shimansky's rebuttal, it appears the Company is not opposed to the OUCC's recommendation to update these fees prior to or in its next rate case. Pet. Ex. 15 at 62. Given the Company's willingness, the Commission finds that the Company shall evaluate whether the costs of these services have changed and, as appropriate, adjust the non-recurring fees in its next rate case or in a 30-day filing just prior to its next rate case.

17. Tariff Matters.

A. INAWC Case-in-Chief. As discussed above, Mr. Shimansky presented the proposed Tariffs as Attachments GDS-1 and GDS-2 to Pet. Ex. 2, inclusive of redlined changes.

B. OUCC. Ms. Sullivan testified Petitioner's current tariff is difficult to understand. She also said moving Area 2 and Area 3 ratepayers 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. She said customers should be able to quickly discern how Indiana American has calculated their bills. Pub. Ex. 2 at 28.

C. CAC. Mr. Inskeep asks the Commission to direct Indiana American to publish its entire tariffs, rules, and regulations on the Company's website in an accessible manner. CAC Ex. 1 at 6-7. 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 general public and all of Indiana American's ratepayers, including individuals with disabilities, should be able to access all of the Company's tariffs. *Id.* at 36.

D. INAWC Rebuttal. Mr. Shimansky testified that the Company appreciates the feedback on its tariffs and has since ensured that the tariffs and rules on the Company's website are fully searchable. Pet. Ex. 15 at 65. Mr. Shimansky explained that the Company hopes this helps provide customers easier access to its tariffs. *Id.*

E. Discussion and Findings. The OUCC and CAC pointed out issues with INAWC's tariffs, tariff language, and accessibility concerns as to INAWC's tariffs. INAWC shall continue to review and maintain its tariffs in a manner that is accessible, and provides clear, understandable, and unambiguous tariff language and tariff format and structure, which

empowers ratepayers to more easily understand their bills and their rights and obligations under the respective tariffs. The Commission further finds that INAWC shall evaluate the readability, understandability, and accessibility of its Tariffs, and, as appropriate, seek to revise its tariffs to be more clear, understandable, and unambiguous through appropriate filings, including, but not limited to, and not later than, in its next rate case. And the Commission also encourages Indiana American to continue to be responsive to customer and stakeholder feedback about improving the presentation of and ability to understand the Company's tariff.

18. Customer Service.

A. Lowell Service Area. OUCC Witness Seals highlighted and discussed certain of the customer comments received by the OUCC in this Cause, with emphasis on comments received regarding the Lowell operation, which Indiana American acquired in 2021. Pub. Ex. 10 at 10-12. Mr. Seals discovered, based upon records of the Indiana Department of Environmental Management, that for the first six months of 2023, the Lowell operation experienced 28 boil advisories, with twelve of these caused by main breaks. Mr. Seals compared this level of boil advisories to Indiana American's larger Wabash operation, which experienced three boil advisories during the same period. Based on the situation in the Lowell system, Mr. Seals recommended that the Commission order Indiana American 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 responded to the concerns raised by Mr. Seals. She 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 did not agree with Mr. Seals' recommendation, stating "Indiana-American 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 Indiana American's Lowell system. As it appears from Ms. Britto's rebuttal testimony that Indiana American 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/NW 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, basement flooding from lines being cut, and the closure of Indiana American's in-person payment center, which has been a hardship. Petitioner declined to address these customer complaints in its Rebuttal filing. Petitioner's response to these customer complaints only came through cross examination and the Presiding Officers asking INAWC witness Britto about locations where customers can make in-person payments or ask questions in the Gary area. Hr. 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). Hr. 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 pm and others closing at 4:30 pm. *Id*. The evidence does not indicate whether customers are charged by these check cashing businesses to make their payments. We find it is important for customers to have access

to locations where they can make payments without additional charge. We approved almost thirty 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 (IURC 2/2/1994) at 19-21. However, consolidation should not result in the loss of important customers services including access to the company within the communities served. Petitioner is hereby ordered to evaluate the costs of providing local customer service activities within Gary and other locations.

In its proposed order (p. 123), Petitioner proposed we find "To the extent Petitioner intends to study the cost impacts of providing local customer service activities (including receipt of payments) in Gary based upon the evidence presented in this Cause, the costs of such study shall be deferred for recovery in Petitioner's next general rate case." Thus, Petitioner requires a promise of deferred recovery, without a real commitment to engage in the analysis. We reject that finding as the costs of such an evaluation should be considered to fall within the scope of its management's responsibilities and hence is a normal operating expense already included in Petitioner's revenue requirement.

19. <u>Non-Revenue Water</u>.

A. <u>INAWC Case-in-Chief</u>. Ms. Britto testified regarding the steps the Company is taking to improve water and wastewater efficiency. Pet. Ex. 4 at 17. She explained that improving water and wastewater efficiency means using improved practices and technologies to deliver water and wastewater service more efficiently. *Id*. She testified that the Company'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. *Id*. From an operations perspective, Ms. Britto explained that improving water and wastewater efficiency requires achieving a cost-effective mix of prudent investments and improved operations and maintenance management capabilities targeting safety, customer satisfaction, sustainability, and system efficiency. *Id*.

Ms. Britto discussed the efforts the Company has taken to improve water and wastewater efficiency, including, among others, the use of technology, deploying advanced metering infrastructure ("AMI") technology, and the use of enhanced leak detection efforts. *Id*. at 17-22. Ms. Britto further testified the Company is planning to expand its efforts in improving apparent losses through large meter testing and profiling, conducting fire service audits, and improving the Company's billing process. *Id*. at 22.

B. <u>OUCC</u>. Mr. Seals discusses 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 further explains that four districts experienced greater than 30% non-revenue water during the five-year period, causing the Indiana Department of Environmental Management 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 recommends increased emphasis and resources utilized on addressing non-revenue water, especially on leak detection and on fire service audits, but also consideration of district metering. Mr. Seals also expresses concern that Indiana American may not be concerned about non-

revenue water as long as it remains below 25% based upon the response received to a data request (38-008).

Regarding private fire services, Mr. Seals first explains that private fire services are connections to the water distribution system that enable customers to install fire protection systems such as overhead sprinklers or private fire hydrants within their internal property. He then explains that only 36% of Indiana American's private fire services are metered, making this problematic for non-revenue water. Unmetered water may pass through this 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 then describes how this potential source of non-revenue water can be mitigated by metering all private fire service lines and conducting regular audits of these lines by the utility. Consequently, Mr. Seals recommends 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. INAWC Rebuttal. On rebuttal, Ms. Britto testified that the Company is continuously analyzing and evaluating the amount of NRW in its system to determine what cost effective steps can be taken to reduce the amount even further. *Id*. at 15. With respect to Mr. Seals' recommendation that Indiana American: (1) increase the emphasis and resources utilized on addressing NRW, especially on leak detection and on fire service audits given the increase in NRW; (2) investigate other means of measuring and reducing NRW, such as establishing district-metered areas, especially as the Company 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 NRW. *Id*. at 16-17. Ms. Britto testified that in addition to these steps and those identified in her direct testimony, the Company 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. *Id*. at 17. Ms. Britto testified these steps will allow Indiana American to more accurately capture the flows for these services. *Id*. Ms. Britto further testified, however, that these activities all have costs associated with them, and the Company cannot do all of these things without the increased dollars/headcount to do so. *Id*.

With respect to Mr. Seals' recommendations regarding private fire services, Ms. Britto testified that what Mr. Seals recommends will be an expensive investment. *Id*. at 18. She testified that for many customers this cost could run as much as $200,000, since the customer frequently owns the vault. *Id*. She further testified there would also be significant impact in larger meters being added to these vaults. *Id*. Mr. Britto testified that the Company would be unwilling to commence this program absent assurance that the costs could be included in rate base. *Id*. She further testified that should the Commission order Indiana American to make these investments, the Company would commence doing so and would include the costs in future Distribution System Improvement Charge ("DSIC") cases.

D. Discussion and Findings. The record shows that Indiana American has taken numerous significant steps to address NRW in its system. Pet. Ex. 4 at 17-23; Pet. Ex. 17 at 15. The record further shows that the OUCC witness Seals agrees with the steps Indiana American has taken to reduce NRW and acknowledges that these steps are effective first steps toward reducing non-revenue water. Pub. Ex. 10 at 4. Mr. Seals also recommends that Indiana

American place an increased emphasis and dedicate more resources to addressing non-revenue water, including additional leak detection activities, metering of all private fire services, increased fire service audits, explore district-metering in problematic areas, and acting upon recommendation from water audits. Pub. Ex. 10 at 4, 6, 8.

Ms. Britto testified that Indiana American is already engaging in each of the activities the OUCC recommended in an effort to help reduce NRW. Pet. Ex. 17 at 17. However, the OUCC presented evidence that Indiana American's total Company NRW increased slightly over the five-year period from 2018-2022, from 18.5% in 2018 to 21.2% in 2022. Pub. Ex. 10 at 3. Additionally, four districts experienced greater than 30% non-revenue water during the five-year period, causing the Indiana Department of Environmental Management to identify a significant deficiency for these districts. Pub. Ex. 10 at 5.

We agree that Indiana American is taking adequate first steps to manage water loss and address NRW within its system. Ms. Britto testified regarding all of the steps the Company is taking to reduce NRW and testified Indiana American is continuously analyzing and evaluating the amount of NRW in its system to determine what cost effective steps can be taken to reduce the amount even further. Pet. Ex. 17 at 15. However, we also agree that Indiana American can take additional steps to address NRW, as described by Mr. Seals.

While Indiana American is addressing NRW within its systems, we find Indiana American should take additional steps as referenced by Mr. Seals to address NRW, such as increased fire service audits and exploring district-metering in problematic areas within its system. With regard to metering of private fire services, Indiana American shall audit its private fire services customers every five years and report to the Commission the results on an annual basis. This report should include the number of private fire services audits performed, the number of private fire services using water, the amount of water being used, and the estimated cost (both Indiana American's and the customer's) of installing a meter to record flows on the private fire service lines.

20. <u>Regulatory Accounting Treatment</u>.

A. <u>INAWC Case-in-Chief</u>. INAWC witness Shimansky described three proposals for regulatory accounting treatment, whereby recovery of deferred costs would be determined in INAWC's next general rate case. Pet. Ex. 24. 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 the Company in Cause No. 43680 which was denied. He described how, had that balancing account been approved, Pension and OPEB costs that had gone down in the subsequent years would have been returned to customers. Pet. Ex. 2 at 26-28.

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. *Id.* 30-31.

As explained elsewhere in this Order, the Company is proposing a Universal Affordability Tariff that will provide discounts to participating and qualified customers. INAWC has proposed an assumption that 10% will participate, and it has 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. *Id.* at 32-33.

B. <u>OUCC</u>. OUCC Witness Margaret Stull responded to Indiana American proposed regulatory accounting deferral treatment for production costs and costs related to its proposed affordability tariff. She explained that Indiana American proposed that the annual level of expense for each of these costs established in this rate case be compared to the actual expenses incurred with any difference between the two deferred to a regulatory asset or liability with any recovery determined in the next general rate case. Pub. Ex. 3 at 22-23. Ms. Stull addressed Indiana American proposal for regulatory treatment with respect to production costs, which included chemical costs, (2) purchased water, (3) fuel and power, and (4) waste disposal. She explained that the OUCC opposed the proposal because it would remove any incentive for Petitioner to efficiently manage and operate its utility operations and otherwise negates basic regulatory principles. Ms. Stull explained that when a utility's rates are set by the IURC, a utility is given the opportunity to earn its authorized return, which is not a guarantee it will earn its authorized return. Ms. Stull explained 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 -- eliminating waste and finding more efficient ways of producing and delivering water to customers. She added that through good management, a utility may retain more of its earnings, but through poor management or failure to operate efficiently, a utility may earn less that its authorized net income. But, she added, 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 for regulated monopolies. Pub. Ex. 3 at 23.

Ms. Stull noted that Indiana American intends to track any and all differences between actual and projected production costs included in its revenue requirement. In OUCC Data Request No. 9-20 (OUCC Attachment MAS-3), the OUCC asked whether all variances in production costs would be tracked and whether Petitioner intended to differentiate between production cost increases due to increased demand because of customer growth or customer consumption versus increases in price. Petitioner responded that it did not and stated that the proposed regulatory treatment of production costs would be "all-inclusive since there are varying drivers that must be taken into consideration." Ms. Stull indicated the plan is problematic as Indiana American is not limiting its proposal to only increases or decreases in production cost pricing, but also increases due to variances in customer consumption. 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 including for example (1) higher than projected customer growth and (2) higher than projected customer consumption, which can be caused by such things as a drought. She explained both these factors would create increased production costs that would be recovered through increased operating revenues. Pub. Ex. 3 at 25. Ms. Stull testified this approach would allow it 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 already has the option of submitting a purchased water tracker under the Commission's 30-day administrative filing process (170 IAC 1-6) to recover the increase in its purchased water expense. She stated that in that regard there is no need to provide another mechanism for Indiana American to recover these cost increases.

Ms. Stull also addressed Indiana American's proposed affordability tariff. She explained that Indiana American proposes to track the difference between actual and projected discounts claimed under its requested affordability tariff. INAWC assumes 10% of eligible customers will participate in its proposed universal affordability tariff in this proceeding. She noted Indiana American has projected approximately $1.3 million (Step Two) and $1.4 19 million (Step Three) affordability tariff discounts in this Cause. If more or fewer customers participate in Petitioner's proposed affordability tariff, INAWC proposes to include the difference between actual and projected discounts in a deferred asset or liability account and recover these costs in its next general rate order. Pub. Ex. 3 at 25. Ms. Stull noted the OUCC did not accept Petitioner's proposal and recommended the proposal be disallowed for the reasons explained in the testimony of witness Scott Bell. Therefore, no deferred accounting treatment would be warranted on that basis.

C. Industrial Group. Industrial Group Witness Gorman rejected INAWC's proposal to defer in regulatory assets without carrying costs, the difference between the costs included in rates and the actual costs for the following items: (1) pension and OPEB expenses; (2) production expenses; and (3) universal affordability expenses.testified that the three deferral mechanisms proposed by INAWC place too much cost risk on customers and do not include significant protections for customers from paying rates that are no more than a just and reasonable level. He testified that the Company had 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. IG Exhibit No. 1 at 12-13.

D. INAWC Rebuttal. Mr. Shimansky responded to Ms. Stull and Mr. Gorman. He testified that these accounts are not being proposed to provide a rate of return but to protect both customers and the Company 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 the Company to do all it can do to manage costs. Pet. Ex. 15 at 30-31.

E. Discussion and Findings. In 2010, this Commission rejected a proposal put forth by the Petitioner to create a "Pension and OPEB Balancing Account" which would have allowed Indiana-American 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 (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 properly and effectively

manage its business. 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, and the expenses related to the implementation of its Universal Affordability rate. The Company now requests authority to create four separate regulatory accounts for these expenses, which will all 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. Pet. Ex. 2 at 24 ln. 9-19.[47]

The Company requests this extraordinary relief because, in the case of pension, OPEB and production costs, it claims the relief will protect itself, and customers, from volatility in those expenses. Pet. Ex. 2 at 25 ln. 16-18 and at 31 ln. 16-19. In the case of the Universal Affordability rate, the Company asks for the treatment because it simply does not know the level of participation to expect in the proposed program and, accordingly, does not know the costs it will incur. Pet. Ex. 2 at 34 ln. 12-21. Indiana-American further argues that this treatment will "ensure both the Company and its customers only experience the actual . . . expenses incurred by the Company" in these four categories. Pet. Ex. 2 at 24 ln. 17-19.

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 revisit our prior decision.

What Petitioner requests is to be shielded from volatility inherent to the operation of a utility. It offered the same justification in Cause No. 43680 where we found that "Petitioner's proposal attempts to mitigate" the instability caused by annual fluctuations in a single category of expense. Essentially, Indiana-American wants to disassociate the recovery of a set of expenses from any outside variables which might impact recovery of the expense through rates set in this case. But such risks are known and understood parts of 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.

Rather, this Commission has previously stated that when considering requests for approval of deferred accounting treatment:

[47] We note that Petitioner indicated in testimony that, if approved, future treatment of any regulatory balance would be addressed in a future rate case. Pet. Ex. 3 at 24 ln. 6-8. In its Proposed Order, however, it asks that we establish an amortization rate in this proceeding. Pet. Proposed Order at 127. ("In ensuing rate cases, the amount reflected in said regulatory assets/liabilities shall be amortized for ratemaking purposes over the anticipated life of the rates.") Even if we were to grant the relief requested, it would be inappropriate for us to judge today whether just and reasonable rates can be set in a future case based on an unknown amortization period and unknown regulatory balance. We decline IAWC's invitation to establish future rates today.

. . . it is necessary to consider the balance struck between the utility and its ratepayers by approving such a request. For example, the gravity of the financial event involved and its impact upon the utility is appropriate to consider, as well as the impact such accounting and/or ratemaking treatment will have upon the utility's ratepayers. Further, it is necessary for the utility requesting such extraordinary treatment to be able to demonstrate with convincing evidence that the financial event is in fact occurring, and that such financial impact is fixed, known and measurable. If all of these elements are established, a utility **might** receive approval for such an extraordinary request.

Indiana Michigan Power Co., Cause No. 40980 (IURC Nov. 12, 1998) (emphasis added).

Nothing in the record provides any indication that the "gravity of the financial event" associated with changes in the investment market or market for goods and services are so grave as to endanger Indiana-American's ability to operate. In fact, recently, faced with the unprecedented effects of the worldwide COVID-19 pandemic, this Commission specifically rejected requests by the State's public utilities (including Indiana-American) to implement deferred accounting treatment associated with increases in O&M and pension expense. *See COVID Dockets*, Consolidated Cause Nos. 45377/45380 (IURC June 29, 2020). We did so principally on the grounds that there was insufficient "evidence demonstrating that these expenses have created or will create any substantial financial burden on the utility or that the expenses are in any way so significant as to warrant extraordinary relief." *Id*. We further noted that "[w]ithout knowing the extent of the financial impact, it is difficult to balance the interests of the utility and its customers." *Id*.[48]

We face the same situation here. Petitioner offers speculation about the potential impact of market fluctuations and price volatility, but that is the limit of the evidence before us. The only example Petitioner provides is a historical "look back" on how a balancing account might have played out for OPEB and pension expense. Pet. Ex. 3 at 28. This, however, is no substitute for evidence that the variability in costs will expose the utility to the risk of meeting its service obligations. Nor is it evidence that the requested relief will fundamentally benefit ratepayers. In short, the Company offers no concrete evidence that rates set using at 2025 test year will prove inadequate to support is operations and that interests of ratepayers will be served by approval of its requested balancing accounts.

Indeed, with respect to the alleged benefit to ratepayers, it is difficult to find any under these circumstances. The Company claims that ratepayers will pay no more and no less than the actual cost associated with the four expenses it seeks to embed in rates, but that is not quite accurate. Today's ratepayers will pay rates which reflect the amount of expenses we have found to be reasonable and necessary. Tomorrow's ratepayers are a different story. As we have previously noted, approval of deferred accounting treatment carries "with it a general presumption that such costs, if determined to be reasonable and necessary are entitled to future

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[48] Importantly, we gave all utilities the opportunity to present evidence of those impacts in a separate phase of Consolidated Cause Nos. 45377/45380, but no utility did so, and Indiana-American specifically "noted it had not identified a need" to take advantage of that opportunity. *See COVID Dockets*, Consolidated Cause Nos 45377/45380 (IURC Aug. 25, 2021). It is hard to conclude that Indiana-American would disclaim the need for special regulatory accounting in the midst of the COVID-19 pandemic, but need it now.

recovery in rates." *COVID Dockets*, Consolidated Cause Nos. 45377/45380 (IURC June 29, 2020).[49] Accordingly, at some point tomorrow's customers will be exposed to the risk of paying not just those rates meant to recover the then present reasonable and necessary costs of operating the utility, but also the amortization of costs incurred by the utility today. In the absence of any indication of what the impact on future customers of the proposed arrangement might be, we cannot adequately balance the interest of the utility and 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, Indiana-American (or any 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 by implementing proposals such as balancing accounts. *See, e.g.*, *Indiana-American Water Co., Cause No*. 43680 (IURC April 30, 2010); *In re Investigation into Rate Design Alternatives*, Cause No. 43180 (IURC Oct. 21, 2009). We have also previously stated that if a utility seeks to shift its risks to ratepayers, "that reduction in risk should be considered in determining an appropriate return on equity." *SIGECO*, Cause No. 43427 (IURC Dec. 16, 2009). Here, however, Petitioner made no adjustment to its requested authorized return to reflect the shift in risk to ratepayers on account of its proposed balancing account.

We are also troubled by the fact that the balancing account mechanism is unnecessary. A utility always has the right to petition for rate relief in the event of an emergency, and Indiana-American has access to several tracking mechanisms to recover costs associated with a range of investments. Indeed, there is also a well-used rule and practice in place of allowing utilities to quickly amend their rates to cover increases in purchased water costs – one of the costs IAWC seeks to include in the balancing account. The existence of this mechanism makes the need to defer purchased water costs not only not extraordinary in nature, but entirely unnecessary.

To the extent that Petitioner tries to justify creation of the balancing account on the grounds that "a purchased water tracker would not address increases the Company may experience in its production costs, which is a much larger portion of Petitioner's deferral request than just the purchased water expense," Pet. Proposed Order at 127, we are not persuaded. Again, granting authority to defer such costs exposes future ratepayers to the risk of bearing the burden of those costs and introduces issues with intergenerational inequity. The Company's approach with respect to increasing purchased water costs illustrates its focus on shifting risk and costs from itself to its customers. The Company should not be encouraged to abdicate its

[49] Petitioner suggests further limiting later recovery, at least with respect to the pension and OPEB balancing accounts, to whether imprudence can be found. *See* Pet. Ex. 3 at 26 ln. 18-21 ("If imprudence is found, those balances would be subject to Commission scrutiny as to whether or how much would be recovered.").

responsibility of running its utility in a manner that protects "the affordability of utility services for present and future generations of Indiana citizens." I.C. §8-1-2-0.5 (emphasis added).[50]

In conclusion, 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. It has not shown that the cost risks from which it seeks to isolate itself are of an extraordinary nature or of such a magnitude as to endanger its ability to operate. Nor has it shown that there are substantial benefits to ratepayers associated with authorizing the proposal. We deny the Indiana-American's request to implement the balancing accounts.

21. Confidentiality. 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 shall be and hereby 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 $304,047,437, which are calculated to provide the opportunity to earn net operating income of $107,976760. 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 Findings Section 12, which schedules shall be effective upon submission on an interim subject to refund basis subject to the compliance filing process described in that same finding paragraph.

3. The OUCC's proposed depreciation accrual rates shall be and hereby are approved upon the submission of Step 1 rates.

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[50] We also note that Petitioner's proposal puts at risk conservation efforts. By deferring costs, Petitioner is introducing the potential for significant delays in communicating price signals to those customers who may respond by moderating their consumption. Doing so further exposes customers to otherwise avoidable plant additions and expansions unnecessary to the benefit of all ratepayers.

4. Petitioner's requests for deferred accounting authority described in Findings Section 20 is hereby denied.

5. Petitioner's proposed Montgomery County surcharge is denied.

6. Petitioner's proposed Universal Affordability tariff is denied.

7. Petitioner's plans to develop future water sources of supply pursuant to Ind. Code § 8-1-2-23.5 is denied.

8. Petitioner shall issue a direct refund of its URT overcollection in the amount of $1,356,008 plus carrying costs consistent with our findings under Section 15.

9. Petitioner shall evaluate its non-recurring charges, such as its returned check charges, reconnect fees, and after-hours charges to determine whether the related costs have changed and, as appropriate, adjust the non-recurring fees in its next rate case or in a 30-day filing just prior to its next rate case.

10. Petitioner shall evaluate the readability, understandability, and accessibility of its Tariffs, and, as appropriate, seek to revise its tariffs to be more clear, understandable, and unambiguous through appropriate filings, including, but not limited to, and not later than, in its next rate case.

11. Petitioner shall conduct the study as set forth in Section 18.

12. 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, is exempt from public access and disclosure by Indiana law, and it shall be held confidential and protected from public access and disclosure by the Commission.

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

HUSTON, BENNETT, FREEMAN, VELETA, AND ZIEGNER CONCUR

APPROVED:

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

____
Dana Kosco
Secretary to the Commission

DMS 27430397.8