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STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF WASTEWATER ONE DBA RIVERS EDGE UTILITY, INC FOR A NEW SCHEDULE OF RATES AND CHARGES FOR WATER SERVICE	**) CAUSE NO. 44876 U** **)** **) APPROVED:** AUG 0 9 2017

ORDER OF THE COMMISSION

Presiding Officers:
David E. Ziegner, Commissioner
David E. Veleta, Senior Administrative Law Judge

On November 7, 2016, Wastewater One d/b/a River's Edge Utility, Inc. ("Applicant") filed its application with the Indiana Utility Regulatory Commission ("Commission") for a small utility rate change (the "Application") pursuant to the provisions of Indiana Code § 8-1-2-61.5 and 170 IAC 14-1. On November 23, 2016, the Water and Wastewater Division of the Indiana Utility Regulatory Commission ("Commission") issued a Memorandum finding that the Application was complete.

A public field hearing was held on March 28, 2017, at 6:00 p.m. at Charlestown Senior High School, #1 Pirate Place, Charlestown, Indiana. On April 19, 2017, as required by 170 IAC 14-1-4(a), the Indiana Office of Utility Consumer Counselor ("OUCC") filed its report making certain recommendations (the "OUCC Report"). On May 9, 2017, Applicant filed its reply.

Based on applicable law and the evidence presented, the Commission finds as follows:

1. **Notice and Jurisdiction.** Notice of the public hearings conducted by the Commission in this Cause was given as required by law. Applicant is a "public utility" as that term is defined under Indiana Code § 8-1-2-1(a). Applicant is a for-profit corporation which owns and operates both water and wastewater utilities serving residential and campground customers within the River's Edge subdivision in Clark County, Indiana.

2. **Applicant's Characteristics.** Applicant is located several miles east of Charlestown, Indiana on the Ohio River. Applicant provides water service to 90 customers consisting of 71 non-metered and 19 metered water users. Additionally, Applicant has 69 flat rate and six metered wastewater customers.

3. **Test Period.** The test period selected for determining Applicant's revenues and expenses reasonably incurred in providing water utility service to its customers included the 12 months ending December 31, 2015. With adjustments for changes that are fixed, known, and measurable, the Commission finds that this test period is sufficiently representative of Applicant's normal operations to provide reliable data for ratemaking purposes.

4. **Relief Requested and Background.** Applicant requested a 68.7% across-the-board rate increase, which would increase annual water operating revenues by $19,046 for higher operating expenses related to Indiana Department of Environmental Management's ("IDEM") recent classification of its system from a transient non-community water system to a community public water system on February 10, 2014. This new classification requires Applicant to employ a certified operator on-site daily, daily test of its water for various parameters, and distribution of a customer confidence report and well head protection plan annually.

5. **OUCC Report.** The OUCC Report was prepared by Richard J. Corey, James T. Parks, and Edward R. Kaufman. In response to the Application, the OUCC recommended Applicant be allowed to increase its revenues by $16,923 or an increase of 55.09%. The specific issues raised by the OUCC Report are addressed below.

6. **Commission Discussion and Findings.**

A. **Revenue Adjustments.** Applicant proposed a customer growth normalization adjustment that would decrease pro forma present rate revenues by $2,940. This was calculated by multiplying an average residential bill of $10.57, derived from dividing metered revenues by both metered customers and unmetered customers times the decrease in the number of total bills. OUCC witness Mr. Corey disagreed with Applicant's calculation, and stated that the inclusion of seasonal, unmetered customers skews the calculation. The OUCC's calculation resulted in a decrease of one bill for the year, in comparison to Applicant's estimated decrease of 278 bills. Therefore, Mr. Corey proposed a $36 pro forma residential water normalization decrease, which based its calculation solely on metered revenues and metered customers. Applicant did not respond to this adjustment in its rebuttal testimony. We find that the OUCC's revenue adjustment is reasonable, supported by evidence of record, and should be approved.

B. **Expense Adjustments.** Applicant proposed pro forma expense adjustments related to insurance expense of $2,756 and rate case expense of $500, which the OUCC accepted. Mr. Corey recommended several pro forma expense adjustments including a reduction in contractual services of $1,479, purchased power expense reduction of $2, and an increase in the IURC Fee of $33 Applicant did not respond to these adjustments in its rebuttal testimony. We find that the OUCC's expense adjustments are reasonable, supported by evidence of record, and should be approved.

Also, Mr. Richard Corey recommended denial of Applicant's pro forma depreciation expense of $2,318 because Applicant did not provide sufficient documentation to support its water UPIS balance, upon which depreciation expense is calculated. Therefore, Mr. Corey proposed the removal of test year depreciation expense of $2,133 from Applicant's operating expense. Mr. Corey also testified Applicant has one set of books for both the water and sewer divisions, and should maintain a separate set of books for each.

On rebuttal, Applicant witness Mr. Tolliver stated that Applicant provided documentation of its capital investment in its depreciation schedules to the OUCC. Mr. Tolliver reiterated several capital items that Applicant has installed since 2010 including the replacement of three bladder tanks, two 52-gallon tanks, one 100-gallon tank with four 80-gallon bladder tanks, two well sampling systems, and a chlorine chemical feed system with new controls. Mr. Tolliver stated that the depreciation schedules and trial balance sheets it provided the OUCC list separate water and sewer assets.

On June 27, 2017, the OUCC filed with the Commission, Applicant's responses to OUCC Data Requests dated January 20, 2017 related to Applicant's Water Utility Plant in Service. This documentation included invoices of Applicant's capital additions. Based on the invoices provided by Applicant to support its water plant investment and the testimony of Mr. Parks who directly inspected Applicant's in service water additions, it appears that Applicant has invested in water assets since its acquisition in Cause No. 43115. Thus, we decline to remove test year depreciation expense as the OUCC proposes. However, going forward Applicant shall maintain separate asset and depreciation expense ledgers for its water and wastewater assets.

C. <u>Affiliated Contracts</u>. OUCC witness Mr. Corey stated that Applicant's management agreement with its affiliate company, Aqua Utility Services, LLC ("AUS"), titled "Agreement for Management, Administrative, Operations, and Maintenance Services" included a provision for a 15% markup on any expenses, and should be denied. He indicated that since it is an agreement between affiliated companies, any additional expenses from the parent company or affiliate should be passed through to Applicant at actual cost with no markup. Mr. Corey's adjustment to remove the 15% is $1,480. OUCC witness Mr. Corey indicated that Applicant shows a note payable to an associated company of $131,250 on its balance sheet. He indicated that no copy of the note, terms of repayment, interest rate or origination date were made available to the OUCC upon request. He further noted that the Commission did not approve this debt issuance.

On rebuttal, Mr. Tolliver stated the 15% markup should be included because this was part of an affiliated agreement submitted in Cause No. 43115, and was not objected to by the OUCC. In rebuttal, Mr. Tolliver indicated he provided the OUCC with a copy of a contract which demonstrated that there is an affiliated agreement in place between Applicant and AUS that allows the issuance of capital loans as needed.

The affiliate agreement currently on file with the Commission labeled "Agreement for Management, Administrative, Operations, and Maintenance Services WW1: Agreement 2010-3" dated April 1, 2010, differs from the affiliate agreement labeled "Agreement for Management, Administrative, Operations, and Maintenance Services WWI: Agreement 2016", dated April 1, 2016, submitted in this Cause.

While both agreements contain a 15% handling fee on actual costs for parts, materials, supplies, equipment, and/or other costs, the 2016 affiliate agreement also includes "expenses at a cost plus 15%" in addition to AUS' monthly standard management and administrative fee of $2,500. The 2016 affiliate agreement also charged customer billing and services at a cost of labor, materials, billing software, banking deposits, and other bookkeeping duties as required, at a cost plus 15%. Similarly, accounting and bookkeeping duties which may be subcontracted to firms, individuals or employees will be invoiced to Applicant at cost plus 15%. Finally, laboratory testing services performed by a third party state approved laboratory will be charged to Applicant at cost plus 15%.

Pursuant to Indiana Code § 8-1-2-49(2)(g), no management, construction, engineering, or similar contract, made after March 8, 1933, with any affiliated interest, as defined in Indiana Code § 8-1-2-49, shall be effective unless it shall first have been filed with the Commission. Because the 2016 affiliate agreement has not been submitted for review and approval by the Commission, it is invalid. Therefore, we are disallowing the new 15% premiums totaling $1,480 added to third-party contractors, customer billing and services, accounting and bookkeeping services, and third-party operational contractors.

Furthermore, Applicant has on file with the Commission an affiliate agreement with the Hughes Group, LLC labeled "Revolving Line of Credit Agreement WW1: Agreement 2010-1", dated March 25, 2010. This agreement enables the Hughes Group, LLC to provide a revolving, open-end line of credit to Applicant up to the principal amount of $300,000. The agreed interest rate is the prime rate as published in *The Wall Street Journal* plus two percent. Applicant agreed to pay monthly interest-only payments on the outstanding balance beginning on April 30, 2010, with a maturity date of March 31, 2011, unless extended by Hughes Group, LLC. Pursuant to Indiana Code § 8-1-2-78, Applicant must obtain approval from the Commission to issue "stock, certificates of stock, bonds, notes, or other evidence of indebtedness payable at periods of more than 12 months." Applicant shall comply with its duty to seek Commission approval prior to incurring future long-term debt.

D. <u>Federal and State Income Taxes, Property Taxes</u>. Applicant's rate application lists pro forma Federal and State Income Tax expense of negative $3,093 and $1,407, respectively. This is despite the fact that Applicant is not requesting any income on its rate base in this case.

OUCC witness Mr. Corey recommended denial of Applicant's pro forma Federal and State Income Tax expense stating that because Applicant is a division of Wastewater One, LLC, it is also a limited liability corporation. For state and federal income tax purposes, revenues and expenses of an LLC are not taxed at the corporate level, but are passed through to shareholders, and taxed on their individual income tax returns. Therefore, the OUCC has not made a pro forma adjustment for Federal and State Income Taxes.

On rebuttal, Mr. Tolliver stated that Applicant pays its annual real property and personal property taxes directly through the Clark County Treasurer's office twice a year as required by law. These property taxes are not being passed through to any member/shareholder's personal tax returns.

The Commission has provided income tax recovery to utilities organized as a limited liability corporation, if the shareholders provide information about their personal income tax rates. However, income taxes are not an issue in this case because the Applicant has elected to forgo a return on its investment. Without a return there is no net operating income for which to tax. We are denying Applicant's Federal Income Tax expense of $280.

E. **Approved Rates and Revenue Requirement.**

Rate Base	$111,041
Times: Cost of Capital	0%
Net Operating Income Required	$0
Less: Pro forma NOI at Present Rates	(18,704)
Increase in Net Operating Income Required	$18,704
Multiply by: Gross Revenue Conversion Factor	1.0154
Recommended Increase	$18,992
Recommended Percentage Increase	61.83%

Net Operating Income:

Operating Revenue:	
Metered Revenue	$ 12,503
Unmetered Revenue	35,295
Forfeited Discounts	1,914
Total Operating Revenue	49,712
Operation & Maintenance Expense	46,712
Depreciation Expense	2,318
Utility Receipts Tax	682
Net Operating Income	$ -

F. **Outdated Well Information.** OUCC witness Mr. Parks noted discrepancies between well specifications reported by Applicant in its 2015 Annual Report and the DNR Significant Water Withdrawal Facility Data. The OUCC recommended Applicant update its well information with DNR to reflect actual values for its wells.

Applicant's witness Mr. Tolliver responded that Applicant has made significant improvements to the wells and water system between 2010 and 2015. He acknowledged that the data reported in the 2015 Annual Report does not match the data contained in the DNR Significant Water Withdrawal Facility Data. He stated that Applicant does not provide annual updates to its Annual Reports to the Commission and DNR. He stated that Applicant will communicate corrections to those agencies in an effort to clarify these facts.

G. **Rate Design.** Applicant has approximately 19 metered year-round customers who are currently charged a water volumetric charge of $7.97 per 1,000 gallons, and no minimum bill. This equates to $39.85 per month, if a metered customer had an average usage of 5,000 gallons. Depending on the time of year, there are between 15 – 71 unmetered, seasonal customers, who use water hook-ups at mobile home and camp lots. These customers currently must pay a minimum of $239.10 per year for water, which is the fixed rate of $39.85 for water per month for at least 6 months. These customers are being charged as if they actually use 5,000 gallons per month.

OUCC witness Mr. Kaufman indicated that at the field hearing some unmetered, seasonal customers indicated they actually use less than 5,000 gallons per month, so they are paying more than metered customers for less water. Some unmetered customers requested Applicant to install meters on their lot, but were denied.

Mr. Kaufman indicated the appropriate rate design for Applicant is difficult to develop because the vast majority of Applicant's costs are fixed, while the majority of its customers are seasonal. He indicated that if Applicant had both a fixed charge and a volumetric charge, it would help mitigate disparities between the metered and unmetered customers. However, such a dramatic change is typically only considered when a utility prepares a cost of service study, which is likely cost prohibitive in Applicant's case.

Mr. Kaufman provided an example to partially resolve the rate design dilemma. He suggested Applicant could initiate a minimum charge equivalent to using 4,000 gallons for its metered customers, and reduce the minimum charge to its unmetered customers to the equivalent of using 4,500 gallons.

As to installing meters, Mr. Kaufman indicated that at approximately $1,000 each, this option is cost prohibitive.

On rebuttal, Mr. Tolliver acknowledged Mr. Kaufman's discussions on the flat rate versus metered rate customers, but stated Mr. Kaufman offered no real affordable solution in this Cause. Mr. Tolliver indicated that Applicant is open to discuss the possibility of implementing a minimum rate option to metered customers with permanent residences. Due to high costs, he was skeptical of installing meters for unmetered customers, estimating the cost of each meter at $1,750 each, plus the cost of installation and future meter reading costs.

Applicant has customer characteristics that make rate design complex, as the number of permanent residents is small relative to the total number of customers. But like all water utilities, it must be designed to meet peak demand, which is during the summer when most of the nonpermanent residents use water. Thus, Applicant shall meet with the OUCC, and Water/Wastewater Division staff to begin to discuss alternative rate designs.

H. Alternative Regulatory Program ("ARP"). If Applicant elects to participate in the Small Utility ARP in accordance with procedures approved in Cause No. 44203, the eligible operating expenses to which the Annual Cost Index will be applied are $46,712. Utility Receipts Tax of $682 is also an eligible expense to which the Annual Cost Index will be applied. All other components of Applicant's revenue requirement will remain unchanged.

I. Effect on rates. A residential customer using 5,000 gallons per month will experience an increase of $24.64 per month from $39.85 to $64.49.

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

1. Consistent with the findings above, Applicant is hereby authorized to increase its rates and charges by 61.83% across-the-board, to produce additional revenue of $18,992.

2. Prior to placing into effect the rates and charges approved herein, Applicant shall file with the Commission's Water/Wastewater Division a schedule of rates and charges in a manner consistent with this Order and the Commission's rules for filing such schedules. Once the Commission's Water/Wastewater Division approves the rate schedule, it shall cancel all prior rates and charges.

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

ATTERHOLT, FREEMAN, HUSTON, WEBER, AND ZIEGNER CONCUR:

APPROVED: AUG 09 2017

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

Mary M Becerra

Mary M. Becerra
Secretary to the Commission