

ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF SOUTH EASTERN)
INDIANA NATURAL GAS COMPANY,) CAUSE NO. 45027
INC. FOR AUTHORITY TO CHANGE)
ITS RATES, CHARGES, TARIFFS,) APPROVED: OCT 03 2018
RULES, AND REGULATIONS)

ORDER OF THE COMMISSION

Presiding Officers:

David E. Ziegner, Commissioner

Brad J. Pope, Administrative Law Judge

On December 20, 2017, South Eastern Indiana Natural Gas Company, Inc. ("South Eastern"), filed its Verified Petition with the Indiana Utility Regulatory Commission ("Commission") seeking authority to change its existing rates, charges, tariffs, rules, and regulations. The Commission held a Prehearing Conference on January 31, 2018, at 10:30 a.m. in Room 224 of the PNC Center, 101 W. Washington Street, Indianapolis, Indiana. At the Prehearing Conference, South Eastern and the Office of Utility Consumer Counselor ("OUCC") (collectively, the "Parties") were present and participated. On February 7, 2018, the Commission issued its Prehearing Conference Order, which established the test year, rate base cutoff, and the procedural schedule to be used in this Cause.

An Evidentiary Hearing was held in this Cause on June 27, 2018, at 9:30 a.m. in Room 224 of the PNC Center, 101 West Washington Street, Indianapolis, Indiana. South Eastern and the OUCC were present and participated, and they offered into evidence their respective prefiled testimony and exhibits. The Parties waived cross-examination of all witnesses, and the prefiled evidence and exhibits were admitted into the record without objection. Additionally, South Eastern and the OUCC formally advised the Commission that they had reached a settlement in principle on all issues. Based on the Parties' request for additional time to reduce the settlement to writing and file the settlement and supporting settlement testimony with the Commission, this matter was continued to August 21, 2018. On July 25, 2018, the Parties prefiled the Stipulation and Settlement Agreement ("Settlement") and the settlement testimony of Bonnie J. Mann, Kerry A. Heid, and Heather R. Poole in support of the Settlement. On August 21, 2018, South Eastern filed its response to the Commission's docket entry of August 17, 2018.

On August 21, 2018, at 1:30 p.m., the Commission reconvened the Evidentiary Hearing in this Cause. South Eastern and the OUCC appeared and offered into evidence the Settlement and the settlement testimony. The Parties waived cross-examination of all settlement witnesses, and the prefiled settlement evidence and exhibits were admitted into the record.

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

1. Notice and Jurisdiction. Notice of these proceedings was given and published as required by law. South Eastern is a public utility as defined in Ind. Code § 8-1-2-1. South Eastern seeks authority to change its existing rates, charges, tariffs, rules, and regulations. The Commission

has authority to approve rates and charges for utility service under Ind. Code § 8-1-2-42. Therefore, the Commission has jurisdiction over South Eastern and the subject matter of this Cause.

2. South Eastern's Characteristics. South Eastern is a public utility organized and existing under the laws of the State of Indiana. South Eastern's principal office is located at 106 East Main Street, Morristown, Indiana. South Eastern provides natural gas utility service to its customers in Dearborn and Ripley Counties in Indiana and owns, operates, manages, and controls plant and equipment for the distribution and furnishing of such service.

3. Existing Rates, Test Year, and Relief Requested. South Eastern's current base rates are those established by this Commission on November 7, 2012, in Cause No. 44128. Based on the Verified Petition initiating this Cause and the Prehearing Conference Order, the test year for this proceeding is the 12 months ended March 31, 2017, as adjusted for fixed, known, and measurable changes occurring within 12 months following the end of the test year. South Eastern's cutoff date for determining the used and useful status of its utility plant in service and the value of its rate base is March 31, 2017. Based on the Verified Petition and South Eastern's case-in-chief, South Eastern sought to increase its rates by 20% inclusive of the cost of gas, or additional annual revenue in the amount of \$329,542 over pro forma present rate revenue.

4. Evidence of the Parties.

A. South Eastern's Case-in-Chief. South Eastern's case-in-chief was filed on December 20, 2017, and consisted of the Direct Testimony of Jason L. Wortman, South Eastern's Vice President; the Direct Testimony and Exhibits of Bonnie J. Mann, Certified Public Accountant ("CPA") with LWG CPAs and Advisors; the Direct Testimony of Earl L. Ridlen III, CPA with LWG CPAs & Advisors; and the Direct Testimony and Exhibits of Kerry A. Heid, an independent utility rate consultant.

In his testimony, Mr. Wortman described his role as South Eastern's Vice President. He explained that he regularly shared the work of managing South Eastern with the assistance of its President. He described South Eastern's existing rates, which were established in November 2012. He indicated that the costs of operating the utility have increased since the test year of 2011, which was used in South Eastern's last base rate case. He stated that South Eastern is not earning its previously authorized return on its investment, noting that South Eastern has negative earnings for the current test year. He explained that South Eastern's investment in its utility plant has increased since South Eastern's rates were last established. He testified that the utility plant is used and useful. Finally, Mr. Wortman stated what South Eastern was seeking by this base rate case in the form of new revenue and changes in its current tariff.

In her testimony, Ms. Mann described her work as a CPA specializing in public utility matters. She explained that she was retained to review South Eastern's financial records for purposes of forming an opinion on the appropriate level of revenue required to recover South Eastern's cost of service, to advise South Eastern's management on various adjustments that should be made in the rate case, and to prepare testimony and exhibits supporting South Eastern's request to increase its rates and charges. Ms. Mann explained each adjustment to South Eastern's March 31, 2017 test year records, the results of such adjustments, and the rate base as of March 31, 2017. She also stated that South Eastern's rates and charges should be increased by 20% over pro forma rate revenue including the cost of gas, or an additional \$329,542 as set forth in Exhibit C of her Direct Testimony.

Mr. Ridlen described his work as a financial advisor in which he analyzes market conditions, considers unique factors associated with each utility with which he is working, and has previously provided his opinion to other small gas utilities on an appropriate rate of return. Mr. Ridlen explained the analysis he performed for South Eastern, which included review of prior Commission Orders, review of the reported earnings of other utilities, and review of various ratios, including price to book, price to earnings, and price to sales for Vectren, NIPSCO, and the natural gas utility industry. He explained that his conclusion on a rate of return for South Eastern was based upon such analysis but also considered the risks associated with this particular utility. Finally, he pointed out that the overall economy of the United States, and specifically the State of Indiana, had improved since South Eastern's last rate case where a return on equity of 10.1% was set. Based on such analysis, Mr. Ridlen concluded that a return of 10.25% was the appropriate return on equity for South Eastern, which would recognize the improvement in the economy since South Eastern's last base rate case.

Mr. Heid explained the purpose of the cost of service study ("COSS") was to allocate the pro forma revenue requirement to the rate classes of a utilities' customers based on the investment the utility had made in the plant and operating costs associated with these customer classes. He began his review of South Eastern's proposed allocation by noting that South Eastern has three customer classes. He stated that Rate RS is a class designed to serve residential customers, Rate GS is a class designed to serve non-residential customers, but the class has customers with different-sized meters, and Rate STS is a class designed to serve school transportation customers. Mr. Heid stated that South Eastern has approximately 1,655 customers under Rate RS for the test year. Under Rate GS, he stated that South Eastern has approximately 284 customers, of which approximately 158 use a meter of 250 cubic feet per hour ("CFH") or less. He added that approximately 99 of the GS customers have meters that fall between 250 CFH and 800 CFH, and approximately 27 customers served in this class use meters with rated capacities greater than 800 CFH. Mr. Heid explained that such different meter sizes should be recognized in the monthly customer charges being proposed by South Eastern. With respect to Rate STS, Mr. Heid explained that South Eastern had no customers during the test year taking service through this rate.

Turning to the proposed rates and charges, Mr. Heid explained that based on his COSS, he believed that the monthly customer charge for Rate RS should be increased from \$11.00 to \$13.00. He stated that with the increase, South Eastern will still only collect 28% of the allocated fixed costs related to this customer class. For Rate GS, Mr. Heid proposed that those customers using a meter size of 250 CFH or lower be charged a monthly customer charge of \$13.00 based on the same proposed increase to Rate RS. For those customers using meters that fall between 250 CFH and 800 CFH, Mr. Heid proposed a monthly customer charge of \$24.00. For those customers that use a meter greater than 800 CFH, Mr. Heid proposed a monthly customer charge of \$80.00. He explained that with these increases, GS customers will be paying approximately 19% of the allocated fixed costs through the monthly customer charge. For Rate STS, even though South Eastern has no current customers, Mr. Heid proposed that the monthly customer charge and a separate monitoring charge be increased in order to make them revenue neutral for Rate STS customers based on the charges to Rate GS. He noted that the proposed revisions to the Rate STS rates and charges are intended to correspond to the Rate GS customer charges and distribution rates, such that existing Rate GS customers migrating to Rate STS will be margin neutral for these rate components.

B. OUC's Case-in-Chief. On March 28, 2018, the OUC offered the testimony and exhibits of Heather R. Poole, Isabelle L. Gordon, Amy E. Larsen, Mark P. Dermody, Bradley E.

Lorton, Brien R. Krieger, Leja D. Courter, and the email comments from two consumers. While the OUCC accepted a number of South Eastern's proposals, the OUCC through its witnesses offered various additional adjustments and recommendations.

Ms. Poole summarized all of the OUCC's pro forma adjustments and offered the accounting schedules from the OUCC as her Attachment HRP-1. In addition to summarizing all of the OUCC's adjustments, Ms. Poole addressed specific adjustments related to an Internal Revenue Service ("IRS") penalty, utility receipts taxes, state income taxes, and federal income taxes. She noted that all issues related to taxes, other than a proposed property tax adjustment offered by Ms. Larsen, utilized the same methodology as proposed by South Eastern.

Ms. Gordon raised issues related to the calculation of the impact of the new National Oceanic and Atmospheric Administration ("NOAA") averages used by South Eastern to calculate its Normal Temperature Adjustment ("NTA") revenue. She also proposed an adjustment to eliminate unaccounted for gas revenue. Finally, she proposed adjustments related to charitable contributions, bad debt averages, and various miscellaneous expenses.

Ms. Larsen proposed adjustments related to payroll, pension expense, and rate case expense. With respect to payroll expense, Ms. Larsen questioned the calculation of capitalized payroll and the pay for one salaried employee who was also affiliated with Fountaintown Gas Company, and she proposed an adjustment of one additional salaried employee based on the testimony of Mr. Courter. She noted that in addition to these adjustments, there are other adjustments to payroll tax and pension expense. With respect to rate case expense, Ms. Larsen testified South Eastern may over-collect its proposed rate case expense from its prior base rate case. Ms. Larsen proposed an adjustment to property insurance expense indicating certain pro forma amounts had been accounted for twice. With respect to certain legal fees associated with future gas cost adjustment ("GCA") filings, she eliminated South Eastern's adjustment, stating insufficient support for the adjustment had been provided. Finally, Ms. Larsen proposed certain flow-through adjustments as related to the IURC fee and payroll taxes.

Mr. Dermody raised questions about the existence of long-term debt in South Eastern's capital structure, the calculation of deferred taxes within the capital structure, and the amount of customer deposits held by South Eastern.

Mr. Lorton testified regarding South Eastern's proposed cost of equity and an appropriate return on South Eastern's equity investment. He indicated he had prepared a discounted cash flow ("DCF") analysis and a capital asset pricing model ("CAPM") analysis. Based on such analysis, he concluded South Eastern's cost of equity capital should be established at 9.1% in South Eastern's capital structure used to create a weighted cost of capital for South Eastern.

Mr. Kreiger agreed with South Eastern's COSS and rate design. However, he recommended that South Eastern should use actual costs and quantities of meters and services by rate class in its next COSS. He also recommended South Eastern's next COSS should include a minimum size or zero-intercept distribution pipe study because it will provide better understanding and allocation to all customers for allocating a portion of the distribution mains.

Mr. Courter raised issues with respect to South Eastern's payroll for its President, the lack of corporate bylaws, the lack of Board of Directors' meeting minutes, the elimination of Board of Directors' fees, and the elimination of a \$3,500 expense within the revenue requirement for a

valuation report prepared by LWG for the Hanover Group IV, LLC, the entity that owns all of South Eastern's stock. With respect to corporate bylaws and Board of Directors' meeting minutes, Mr. Courter indicated maintenance of such items would assist the Commission and the OUCC in reviewing the decisions made by South Eastern's management. However, he acknowledged neither corporate bylaws nor Board of Directors' meeting minutes are required for investor-owned utilities such as South Eastern under Indiana law. He proposed to eliminate Board of Directors' fees since Board of Directors' minutes were not maintained. With respect to officer salaries, he noted South Eastern's number of customers is small relative to other gas utilities. Mr. Courter prepared a chart reflecting the salaries of the highest paid officer of various small gas utilities and also listed the number of customers served. Mr. Courter proposed South Eastern's salary for its President be reduced. With respect to the valuation report, Mr. Courter noted that it was done as a shareholder benefit for Hanover Group IV, LLC as the sole South Eastern stockholder and should not be recovered as an operating expense of the utility.

C. South Eastern's Rebuttal. On April 25, 2018, South Eastern filed the Rebuttal Testimony and Exhibits of Bonnie J. Mann, the Rebuttal Testimony of Earl L. Ridlen III, and the Rebuttal Testimony of Kerry A. Heid.

Ms. Mann explained that her rebuttal of proposed OUCC adjustments was arranged in three categories. Category 1 included those adjustments proposed by South Eastern with which the OUCC agreed and adjustments where the difference between South Eastern and the OUCC's adjustments are so small as to have no material effect on South Eastern's revenue requirement. Thus, South Eastern offered that Category 1 adjustments resulted in agreed adjustments, even if the reason for the adjustment differed. Ms. Mann stated that these adjustments included the following: elimination of GCA revenue, adjustment to revenue for the change to newer NOAA data for NTA calculations, adjustment to natural gas purchased, adjustment to health insurance expense, adjustment to remove energy efficiency rebate contributions, adjustment to postage expense, adjustment of charitable contributions, adjustment for bad debt, adjustment to legal fees, adjustment for the amortization of energy efficiency-related regulatory costs, adjustment for depreciation, adjustment for property taxes, and adjustments to reflect net utility plant in service and materials and supplies in the rate base. Ms. Mann also explained that Category 1 includes adjustments for which South Eastern and the OUCC agreed on the methodology, but the exact amount will change based on other changes to the revenue requirement including: IURC fee, pension costs, 401(k) costs, payroll taxes, utility receipts taxes, state and federal income taxes within the operating expenses, and working capital within rate base.

Ms. Mann stated that Category 2 included adjustments proposed by the OUCC to which South Eastern would not object even though South Eastern did not accept the basis for some of these adjustments. Specifically, Category 2 adjustments included removal of unaccounted for gas, removal of non-recurring IRS penalty, removal of certain miscellaneous expenses, and removal of a certain accounting fee.

Ms. Mann stated that Category 3 included those remaining adjustments where South Eastern and the OUCC continued to disagree. She testified that these included adjustments to payroll, payroll expense, property insurance, rate case expense, Board of Directors' fees, the cost of equity to be used, long-term debt, customer deposits, and deferred taxes.

With respect the Category 3 adjustments, Ms. Mann explained that South Eastern disagreed with the rate case expense adjustment proposed by the OUCC. She stated that in South Eastern's last

base rate case, South Eastern agreed that it would remove recovery of rate case expense if it had not filed a new rate case within five years. However, Ms. Mann explained that South Eastern's last base rates were implemented in December 2012 and this case was filed in December 2017, five years later. Ms. Mann stated that South Eastern has not been earning its authorized return, and as such, it could not have over collected on the revenue requirements that made up that authorized return.

Ms. Mann next explained her concern with the OUCC's adjustment related to payroll. She noted that South Eastern was not opposing all of the OUCC's payroll adjustments, only the adjustment of South Eastern's President's salary. She stated that the OUCC proposed to set this salary at \$100,000 per year. She stated that Ms. Larsen's argument was centered on a schedule that OUCC witness Courter had prepared comparing the size of South Eastern's President's salary to the number of customers served by the utility. Ms. Mann reproduced that same schedule but explained that there was no correlation between the annual salary among these small gas utility Presidents and the number of customers their respective utilities served. She then re-sorted the OUCC's schedule and presented it arranged by the largest number of customers served to the smallest number of customers served. She noted that the highest paid President actually served in the middle of this list based on number of customers served. In her new arrangement, South Eastern's President was the lowest annual salary. Ms. Mann concluded that there was no correlation between the salary of the President and the number of customers served. Ms. Mann also stated that some of the work of a utility including meter reading, billing, and collections can be scaled or correlated to the number of customers. However, other work doesn't scale, including searching for affordable health insurance, hiring employees, supervising day-to-day work of the operations, purchasing gas at the lowest reasonable price, maintaining or extending utility plant, dealing with interstate pipelines, responding to regulatory issues, and various other activities of the management of any small utility. Based on this, Ms. Mann opined that often the total staffing for small utilities is such that each member of the management team must take on more responsibilities than the responsibilities taken on by the management of larger utilities to ensure appropriate customer service.

Ms. Mann next addressed the issue of insurance costs. She agreed with the OUCC that South Eastern had originally double counted an invoice. However, she disagreed with the resulting calculations of Ms. Larsen on insurance costs, noting that the OUCC had miscalculated the adjustment. In support of her rebuttal, Ms. Mann attached copies of the invoices for insurance costs in the 12 months following the test year.

Next, Ms. Mann discussed the OUCC's elimination of Directors' fees due to the lack of Board of Directors' meeting minutes. She referenced Mr. Courter's testimony that there are no legal requirements to have written minutes of the Board of Directors' meetings, and she discussed the various times the Board of Directors actually met.

Ms. Mann responded to the OUCC's comments regarding South Eastern's long-term debt. With respect to long-term debt, she acknowledged that South Eastern's Case-in-Chief erroneously included \$250,000 in long-term debt, which in fact had been paid off. She stated that the testimony of the OUCC about the possibility of \$500,000 of debt is incorrect; rather, South Eastern originally borrowed money from a family trust and thereafter decided to replace that money with a loan from a commercial banking establishment. She stated that the bank loan has already been paid off.

Next, Ms. Mann offered rebuttal of the OUCC's recommendation regarding customer deposits. Ms. Mann explained that OUCC witness Dermody assumed that South Eastern was not

returning customer deposits appropriately. She pointed out that the OUCC found customer deposits that were made more than 15 months prior to the test year. Ms. Mann reasoned that since they had not been returned, the OUCC concluded that these deposits were being kept inappropriately. In rebutting this assumption, Ms. Mann highlighted the Commission's specific rules regarding creditworthiness. Such rules require the customer to make 12 consecutive payments on time with no more than two late payments within any 15-month period. She noted that those customers whose deposits have been kept by the utility for more than 15 months have not met this creditworthiness test but are still receiving natural gas service.

Finally, Ms. Mann addressed the OUCC's recommendation that South Eastern update its deferred taxes from December 31, 2016, to March 31, 2017. She noted this change in deferred tax would be insignificant. She stated that South Eastern would prefer to update its deferred tax amount as part of the IURC tax investigation in Cause No. 45032.

Mr. Ridlen addressed the OUCC's proposed return on equity by concluding that Mr. Lorton did not take into consideration the Commission's most recent decisions related to small gas utilities where the rate of return was fully litigated. He stated that Community Natural Gas Co., Inc., Cause No. 44768, was decided in 2017 based upon a test year of September 2015, and that the Commission's decision found a return on equity for Community Natural Gas Co., Inc. of 10.00% was reasonable. He stated that thereafter, the Commission in Midwest Natural Gas Corporation, Cause No. 44880, issued an Order in 2017, based on a test year of March 2016, in which the Commission found a return on equity of 10.10% was reasonable. Mr. Ridlen also noted that OUCC witness Lorton failed to provide for or recognize South Eastern's small size and lack of stock listing. He observed that in prior small gas utility rate cases, the Commission has previously found that an adjustment needs to be made for size. Mr. Ridlen concluded his rebuttal by describing various economic measures that reflect that the economy of the country and Indiana have improved since South Eastern's last base rate case.

Mr. Heid offered rebuttal testimony to the OUCC's positions regarding South Eastern's COSS, rate design, and suggestions. With respect to the COSS, he began by noting that the OUCC agreed with South Eastern's proposed rate design. He recognized that the OUCC requests that South Eastern begin keeping data going forward in order to have its own data available for future special studies. Mr. Heid noted that the lack of utility-specific data does not cause a COSS result to be suspect. He indicated that he has on many occasions used data from other similar situated utilities to assist him in his analysis of the appropriate allocation of the revenue requirement to the customer classes. He continued that if South Eastern would follow the OUCC's recommendation, then South Eastern's payroll would be required to increase. He also addressed the various responsibilities that the management of natural gas utilities hold, noting that larger utilities typically have more managers to fulfill those responsibilities beyond the President and Vice President, as occurs with South Eastern.

D. Settlement and Settlement Testimony. At the June 27, 2018 Evidentiary Hearing, the Parties formally advised the Commission that they had reached a settlement in principle. The Parties reduced their Settlement to writing and filed it with the Commission on July 25, 2018. The Parties indicated in the Settlement that all contested issues in the proceeding have been resolved. The Settlement specifically includes the descriptions of resolutions to a number of the issues for which the Parties had originally presented significant disagreements. The Parties also request in the Settlement that the Commission accept and approve the Settlement and base the Final Order in this Cause on the terms of the Settlement.

In support of the Settlement, South Eastern offered the testimony of its witnesses Ms. Mann and Mr. Heid. Ms. Mann explained that South Eastern and the OUCC reached agreement regarding all issues raised in this Cause. Ms. Mann also sponsored the accounting results of the Settlement through Exhibit BJM-1S attached to South Eastern's Exhibit 10. Ms. Mann stated that it was clear following the filing of the testimony in this Cause that there were few issues that actually separated the positions of South Eastern from those of the OUCC. Therefore, the Settlement in her opinion is a reasonable compromise to those remaining positions, and she recommended that the Commission approve the Settlement in this Cause.

Mr. Heid offered testimony in support of the Settlement and sponsored Exhibit KAH-1S, attached to South Eastern's Exhibit 11, which reflected the allocation of the compromised revenue requirement to the rates and charges of South Eastern's customer classes. Mr. Heid also opined that the Settlement was a reasonable compromise between positions of the Parties in this Cause.

Ms. Poole offered Settlement testimony on behalf of the OUCC in which she described the contested issues that remained between South Eastern and the OUCC through the filing of testimony and described the resulting compromise that was reached on those issues. Ms. Poole concluded each of the Parties had made material concessions by entering into the Settlement, but she opined the Settlement is in the public interest and should be approved by the Commission in this proceeding.

5. Discussions and Findings. Settlements presented to the Commission are not ordinary contracts between private parties. *United States Gypsum, Inc. v. Indiana Gas Co.*, 735 N.E.2d 790, 803 (Ind. 2000). When the Commission approves a settlement, that Settlement "loses its status as a strictly private contract and takes on a public interest gloss." *Id.* (quoting *Citizens Action Coalition v. PSI Energy*, 664 N.E.2d 401, 406 (Ind. Ct. App. 1996)). Thus, the Commission "may not accept a settlement merely because the private parties are satisfied; rather [the Commission] must consider whether the public interest will be served by accepting the settlement." *Citizens Action Coalition*, 664 N.E.2d at 406. Furthermore, any Commission decision, ruling, or order, including the approval of a settlement, must be supported by specific findings of fact and sufficient evidence. *United States Gypsum, Inc.*, 735 N.E.2d at 795. The Commission's own procedural rules require that settlements be supported by probative evidence. Therefore, before the Commission can approve the Settlement, we must determine whether the evidence in this Cause sufficiently supports the conclusions and that the Settlement is reasonable, just, and consistent with the purpose of Ind. Code ch. 8-1-2. We must also consider whether the Settlement serves the public interest.

The Parties, through their respective prefiled testimony and exhibits, have provided this Commission with substantial evidence supporting their original positions, their rebuttal positions, and the compromise outlined in the Settlement. The evidence recognizes the appropriateness of adjusting South Eastern's operating revenue and expenses for purposes of: eliminating revenues recovered through the GCA, adjusting natural gas purchased in base rates using the most recent NOAA data, reducing South Eastern's gas cost for unaccounted for gas, adjusting South Eastern's payroll net of any payroll capitalized, adjusting South Eastern's pensions, providing for an adjustment to South Eastern's 401(k), recovery of South Eastern's rate case expense, an increase in South Eastern's recurring accounting expenses, an increase in South Eastern's recurring legal expenses, a reduction of expense associated with the NTA, the recovery of ongoing regulatory expenses associated with the energy efficiency program, an increase in postage, various increases in insurance costs, the elimination of charitable contributions and other miscellaneous expenses, an increase in depreciation

due to the increase in utility plant in service, an adjustment for property taxes, an adjustment for the IURC fee, and an adjustment for various taxes that flow from South Eastern's increased revenue.

The evidence also reveals that the Parties are in agreement on South Eastern's capital structure and requests that we use such capital structure as included in South Eastern's Exhibit BJM-1S attached to South Eastern's Exhibit 10 as the capital structure in this proceeding. Further, the Parties agree that for purposes of Settlement, a return on equity of 10.10% is appropriate as detailed in the capital structure below.

**Capital Structure
As of March 31, 2017**

Description	Amount	Percent of Total	Cost	Weighted Cost
Common Equity	\$ 1,309,253	59.50%	10.10%	6.01%
Long-term Debt	\$ 250,000	11.36%	6.50%	0.74%
Customer Deposits	\$ 129,725	5.90%	6.00%	0.35%
Deferred Tax	\$ 511,359	23.24%	0.00%	0.00%
Total	\$ 2,200,337	100.00%		7.10%

The Parties also agreed to various non-accounting schedule matters. South Eastern agreed that going forward, its Board of Directors will maintain minutes of their meetings and that the Board of Directors will establish corporate bylaws. The Commission finds that South Eastern should establish corporate bylaws and by calendar year end 2018, file with the Commission that they have met the requirement of this Order.

The Parties also agreed on the treatment of rate case expense. Specifically, the Parties agree that following five full years of recovery of the agreed-upon rate case expense here, if South Eastern has not filed for a new base rate case it will file a change to its tariff to remove the element associated with rate case expense recovery in its revenue requirement. On or before October 3, 2023, South Eastern shall file a Petition for a new base rate case or to change its tariff to remove the amount associated with recovery of rate case expense from this proceeding.

Based on the evidence of record, including South Eastern's direct and rebuttal cases, the OUCC's direct case, and South Eastern and OUCC's Settlement testimony and schedules, along with the Parties' Settlement, we find South Eastern's current rates and charges are insufficient and should be increased. We further find that South Eastern should be authorized to increase its rates and charges in order to produce additional annual operating revenue exclusive of the cost of gas in an amount of \$250,651. This additional revenue will provide South Eastern with the opportunity to earn a net operating income of \$149,868, which reflects the opportunity to earn approximately 7.10% on South Eastern's original cost rate base of \$2,110,816 as of the test year, as shown in the tables below:

Original Cost Rate Base	
Utility Plant in Service as of March 31, 2017	\$ 4,278,553
Less: Accumulated Depreciation	\$ (2,296,008)
Net Utility Plant in Service	\$ 1,982,545
Plus: Working Capital	\$ 109,919
Materials & Supplies	\$ 18,352
Total Original Cost Rate Base	\$ 2,110,816
Revenue Requirement	
Rate Base	\$ 2,110,816
Times: Rate of Return	7.10%
Net Operating Income Authorized	\$ 149,868
Less: Adjusted Net Operating Income	\$ (32,531)
Increase in Net Operating Income	\$ 182,399
Times: Revenue Conversion Factor	1.3742
Revenue Increase	\$ 250,651
Overall Percentage Increase	24.30%

This represents an increase of approximately 15.45% in South Eastern's total revenues inclusive of gas costs and represents an approximate 24.30% increase in the non-gas portion of South Eastern's operating revenues. In its August 21, 2018 response to the Commission's August 17, 2018 Docket Entry, South Eastern stated that the residential bill impact calculation that would result with the approval and implementation of the Settlement would be an overall average increase to residential customers of 18.2% including gas costs.

We have also considered that the Parties proposed allocation of this increased revenue requirement to the increased monthly customer charges and the allocation of the remaining increased revenue requirement to the volumetric rates of South Eastern's customer classes. We agree with the Parties that South Eastern's proposed allocation is reasonable as reflected in Mr. Heid's Exhibit KAH-1S attached to South Eastern's Exhibit 11. South Eastern shall file with the Commission under this Cause a revised tariff that reflects the Settlement and this Order.

Finally, we note that the Parties are in agreement that the Settlement should not be used as precedent in any other proceeding or for any other purpose except to the extent necessary to implement or enforce the terms of the Settlement. Consequently, with regard to future citation of the Settlement, we find that our approval in this Cause should be construed in a manner consistent with our findings in *Richmond Power & Light*, Cause No. 40434 (IURC March 19, 1997).

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

1. The attached Stipulation and Settlement Agreement is approved and incorporated into this Order.
2. South Eastern is authorized to increase its rates and charges in accordance with our findings above to produce additional revenue, exclusive of the cost of gas, of \$250,651 beyond that provided by its current rates and charges.
3. South Eastern shall file a new tariff under this Cause prior to placing into effect the rates, charges, rules, and regulations approved by this Order and shall become effective upon approval by the Commission's Energy Division.
4. On or before October 3, 2023, South Eastern shall file a Petition for a new base rate case or a compliance filing under this Cause to remove the amount associated with recovery of rate case expense from this proceeding.
5. The Commission finds that South Eastern shall establish corporate bylaws and file under this Cause by December 31, 2018, that they have met the requirement of this Order.
6. This Order shall be effective on and after the date of its approval.

HUSTON, FREEMAN, OBER, AND ZIEGNER CONCUR; KREVDA ABSENT:

APPROVED: OCT 03 2018

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



Mary M. Becerra
Secretary of the Commission

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF SOUTH EASTERN INDIANA)
NATURAL GAS COMPANY, INC. FOR)
AUTHORITY TO CHANGE ITS RATES,) CAUSE NO.: 45027
CHARGES, TARIFFS, RULES, AND)
REGULATIONS)

STIPULATION AND SETTLEMENT AGREEMENT

South Eastern Indiana Natural Gas Company, Inc., (hereafter "Petitioner") and the Indiana Office of Utility Consumer Counselor (hereinafter "OUCC") have, through their respective representatives, discussed the evidence of record and the potential for compromise of all issues in this cause. The result of such discussions between the Petitioner and the OUCC (hereinafter collectively the "Parties") is a settlement on all issues raised in this Cause.

The Parties believe that the evidence of record supports the terms of this Stipulation and Settlement Agreement (hereinafter the "Settlement"). The Parties acknowledge that the terms and conditions of this Settlement are a result of negotiation and compromise between the Parties relative to the position each has taken or would take in further proceedings in this Cause. The Parties further recognize that their respective testimony resolved numerous adjustments and recommendations prior to the further negotiations that have now resulted in this Settlement. In the interest of efficiency, saving the limited resources of the regulatory bodies involved, and recognizing the reasonableness of the results produced by this Settlement, the Parties herein stipulate and agree as follows:

1. **Rate Increase.** Based on the test year ending March 31, 2017, as adjusted for matters that are fixed, known, and measurable, and occurring within 12 months of the test year, Petitioner proposed in its direct case filed December 20, 2017, that its operating revenue should

be increased, exclusive of the cost of gas, by \$329,542. The OUCC proposed in its direct case filed March 28, 2018, that operating revenue be increased by \$166,169, exclusive of the cost of gas. The Parties now agree that Petitioner should be authorized to increase its base rates and charges for purposes of natural gas service to its various customers to produce additional annual operating revenue, exclusive of the cost of gas, by \$250,651. This represents an increase of approximately 15.45% over adjusted test year operating revenue.

2. **Proforma Adjustments.** Petitioner proposed in its direct case various adjustments to its test year results as set forth numerically in Petitioner's Exhibit BJM-1, Exhibit C, and accompanying schedules. The pro forma adjustments were further described by Petitioner's witnesses Mann and Ridlen. The proposed pro forma adjustments related to operating revenue and operating expense, included: adjustments to eliminate revenues recovering gas commodity costs and the cost of natural gas purchased from base rates based on the most recent NOAA data; adjustment to reduce gas costs for unaccounted for gas; an adjustment in payroll, net of amount capitalized; adjustment for pensions; adjustment for 401 (k); recovery of rate case expense; increase in recurring accounting expenses; increase in recurring legal expenses; reduction of expense for rebates associated with NTA; recovery of ongoing regulatory expenses of the energy efficiency program; changes in the IURC fee; increase in postage; increases in various insurance costs; removal of charitable contributions; increase in depreciation relative to increased utility plant in service; adjustment for bad debt expense; adjustment for FICA taxes; adjustment for property taxes; and recovery of various other taxes that are associated with and flow from Petitioner's proposed increased revenue, including utility receipts tax, state income tax, and federal income tax. Petitioner also sought to establish the value of its rate base; and the costs associated with its capital structure.

With the filing of the OUCC's case-in-chief on March 28, 2018; the OUCC accepted some of Petitioner's adjustments, but also suggested different adjustments including various OUCC proposals. The OUCC's adjustments related to synchronized interest; original cost rate base, proforma gas sales revenue; unaccounted for gas; charitable contributions; bad debt expense; payroll; pension expense; 401k contributions; rate case expense amortization period; property insurance; recurring legal fees; recurring accounting expenses; various miscellaneous adjustments; the IURC fee; non-recurring IRS penalties; cost of capital; directors fees related to the maintenance of board of director minutes; and establishment of corporate bylaws. The OUCC also agreed with the methodology used to calculate various flow through taxes, such as payroll tax, utility receipts tax, state income tax and federal income tax, but calculated differing amounts from Petitioner due to the OUCC's other accounting adjustments made.

Through rebuttal testimony, Petitioner divided the various adjustments offered by the Petitioner and the OUCC to test year operating results into 3 categories. Category 1 included adjustments that the Petitioner had proposed and the OUCC had accepted and adjustments the OUCC had proposed to which the Petitioner would accept because of the limited impact on the revenue requested. Category 2 adjustments were additional OUCC adjustments, which the Petitioner was willing to accept, though it did not necessarily agree with the basis for such adjustment. Category 3 adjustments were those OUCC adjustments on which there was complete disagreement by Petitioner and to which its rebuttal testimony was focused. Thus the Parties recognized that as of the Petitioner's rebuttal testimony, the Parties were in agreement on a number of adjustments to test year, described as both Category 1 or Category 2 adjustments, which included adjustments to: GCA revenue; revenue changed by NOAA data; natural gas purchased; health insurance; energy efficiency rebates; postage costs; charitable contributions; bad debt

expense; recurring legal fees; depreciation; property taxes; amortization of energy efficiency regulatory costs; net utility plant in service; materials and supplies in the rate base; unaccounted for gas; non-recurring IRS penalties; a certain accounting fee; and various miscellaneous expenses.

Based on the recognition of the numerous adjustments on which the Parties had already essentially reached agreement, the Parties continued to negotiate their remaining disagreements. Now based on further compromise, the Parties have agreed as follows:

1. **Payroll Expense.** The difference in total payroll costs before capitalization between the Parties through the Petitioner's rebuttal was \$57,500. The Parties have agreed that removing \$25,000 from the total proforma payroll cost is a reasonable compromise to their respective positions. Thus the adjustment for total proforma payroll is an increase of \$22,533 to test year payroll expense for a total proforma payroll expense of \$534,178. As a result of the increase in payroll expense, pension contributions were increased by \$2,253, 401(k) contributions were increased by \$1,407 and payroll tax expense was increased by \$1,724.

2. **Directors Fees.** The difference in operating expenses for the Board of Director fees between the Petitioner and the OUCC was \$24,000. The Parties have now agreed that Petitioner's operating expenses should include the test year expense of \$24,000 for Directors Fees. The Parties disagreement over directors' fees also included disagreement over the maintenance of minutes of Board of Directors meetings, and the establishment of bylaws for the Corporation. The Petitioner has agreed going forward to maintain minutes of the Board of Director meetings and to establish corporate bylaws.

3. **Property Insurance.** The difference between the Parties relative to property, workers compensation, casualty, and general liability insurance through the Petitioner's rebuttal filing was the difference between the OUCC's adjustment of (\$12,869) and the Petitioner's

adjustment of (\$7,620) both related to property insurance. The Parties have now agreed that the adjustment of (\$7,620) should be used for purposes of the proforma expense for property, workers compensation, casualty, and general liability insurance. The total proforma insurance expense will be \$19,244.

4. **Rate Case Expense.** The Parties agreed on the amount of rate case expense but disagreed on the timing of a future reduction of the recovery of rate case expense. The Parties have now agreed that following five full years of recovery of rate case expense, Petitioner will change its tariff to remove the element included in its revenue requirement for rate case expense recovery, unless it has filed a new base rate case prior to the expiration of the five-year amortization period.

5. **Flow-Through Adjustments.** The Parties each offered flow-through adjustments for the IURC fee, utility receipts tax, state income tax and federal income tax based on their own respective case-in-chief positions. All flow-through adjustments included in the revenue requirement schedules attached to this Settlement are the result of the settlement adjustments made.

6. **Return on Equity.** The Parties disagreement on the return on equity in the capital structure through Petitioner's rebuttal testimony is based on Petitioner's direct testimony proposing a return on equity of 10.25% and the OUCC's testimony proposing a return on equity of 9.10%. The Parties have agreed that a reasonable return on equity for Petitioner's capital structure for the establishment of Petitioner's revenue requirement in this proceeding is 10.10%.

7. **Long-Term Debt.** In its case-in-chief testimony, the OUCC questioned whether Petitioner had any long-term debt, even though it had long-term debt on the balance sheet. In rebuttal, Petitioner indicated the check to pay off the loan was mistakenly recorded as dividends instead of loan payments. Petitioner also stated the removal of the debt would result in an increase

in retained earnings and elimination of debt from the synchronized interest calculation. This would result in a higher overall weighted average cost of equity and a higher income tax expense in the revenue requirement. For purposes of settlement, the Parties agree to leave the long-term debt in the capital structure, which results in a lower overall weighted average cost of equity and a lower income tax expense in the revenue requirement. The OUCC also raised issue with Petitioner's calculation of synchronization of interest in the capital structure, which Petitioner corrected in rebuttal testimony.

8. **Rates and Charges.** The Parties agreed to Petitioner's proposed rates and charges, subject to the reduced revenue requirement established by this Settlement. Petitioner's Witness Heid will prepare a new Exhibit representing the resulting rates and charges.

9. **Request for Prompt Approval by the Commission.** The Parties acknowledge that a significant motivation for the Petitioner to enter into this Settlement is the expectation that a final order will be issued promptly by the Commission authorizing increases in its rates and charges as reflected by this Settlement and the accepted positions of the Parties as reflected by the evidence in this Cause. The Parties have spent significant time and effort to resolve the issues raised in this case. However, the Parties also recognize the insufficiency of Petitioner's current rates. Under these circumstances, the Petitioner requests prompt approval of this Settlement by way of a final order of the Commission.

10. **Sufficiency of the Evidence.** The Parties believe that the Petitioner's direct testimony and exhibits, the OUCC's direct testimony and exhibits, the Petitioner's rebuttal testimony and exhibits, the Parties' settlement testimony and exhibits, along with this Settlement, constitute substantial evidence sufficient to support this Settlement and provide an adequate

evidentiary basis upon which the Commission may make findings of fact and conclusions of law necessary to issue a final order adopting and approving this Settlement.

11. **Settlement Effect, Scope, and Approval.** The Parties acknowledge and agree as follows:

- (a) The Settlement is conditioned upon and subject to its acceptance and approval by the Commission in its entirety without change or condition that is unacceptable to either the Petitioner or the OUCC. Each term of the Settlement is in consideration and support of each and every other term.
- (b) The Settlement is the result of compromise by the Parties within the settlement process. Neither the making of this Settlement nor any of the individual provisions or stipulations herein shall constitute an admission or waiver by any Party in any other proceeding; nor shall they constitute an admission or waiver in this proceeding if the Settlement is not accepted by the Commission. The Parties hereto shall not use this Stipulation or the Order provided by this Stipulation as precedent or offer the same as an admission in any other proceeding or for any other purpose except to the extent necessary to implement or enforce its terms. In the event this Stipulation or resulting Order is offered for any purpose prohibited by this Agreement, the Parties agree that objections by the non-offering party are proper.
- (c) The communications and discussions among the Parties, along with the materials produced and exchanged during the negotiation of this Settlement, relate to offers of settlement and compromise, and as such, all are privileged and confidential. Such material cannot be used in this or any other proceeding without the agreement of the Parties herein.

(d) The undersigned represent and agree that they are fully authorized to execute this Settlement on behalf of their designated clients who will thereafter be bound by this Settlement.

(f) The Parties hereto will either support; or not oppose on rehearing, reconsideration, and/or appeal; an IURC order accepting and approving this Settlement in accordance with its terms.

Accepted and agreed this 18th day of July, 2018.

SOUTHEASTERN INDIANA
NATURAL GAS COMPANY, INC.

By: _____
Its Counsel of Record

INDIANA OFFICE OF UTILITY
CONSUMER COUNSELOR

By: _____
Its Counsel of Record