

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION



PETITION OF INDIANA-AMERICAN WATER)
 COMPANY, INC. FOR APPROVAL OF (A) A)
 NEW DISTRIBUTION SYSTEM)
 IMPROVEMENT CHARGE ("DSIC")) CAUSE NO. 42351 DSIC 7
 PURSUANT TO IND. CODE CHAP. 8-1-31; (B))
 A NEW RATE SCHEDULE REFLECTING) APPROVED:
 THE DSIC; AND (C) INCLUSION OF THE) DEC 27 2012
 COST OF ELIGIBLE DISTRIBUTION)
 SYSTEM IMPROVEMENTS IN ITS DSIC)

ORDER OF THE COMMISSION

Presiding Officers:
Carolene Mays, Commissioner
Aaron A. Schmoll, Senior Administrative Law Judge

On October 1, 2012, Indiana-American Water Company, Inc. ("Indiana-American" or "Petitioner") filed with the Commission its Petition and Submission of Case-in-Chief for approval of a new distribution system improvement charge ("DSIC") pursuant to Indiana Code ch. 8-1-31 and 170 I.A.C. 6-1.1. On October 16, 2012, Petitioner filed an updated version of Petitioner's Exhibits GPR-3 and SSH-1 to correct for an error in the classification of a project booked to the wrong account. The update did not affect Petitioner's requested DSIC percentage rate. On October 19, 2012, the City of Crown Point, Indiana ("Crown Point") filed its Petition to Intervene in this Cause, which was granted by the Commission's Docket Entry dated November 5, 2012. The Indiana Office of Utility Consumer Counselor ("OUCC") and Crown Point filed their respective cases-in-chief on October 31, 2012. Petitioner filed its rebuttal testimony and exhibits on November 7, 2012.

Pursuant to notice given as provided by law, proof of which was incorporated into the record by reference and placed in the official files of the Commission, a public evidentiary hearing was convened in this Cause on November 15, 2012 at 1:30 p.m. in Room 222 of the PNC Center, Indianapolis, Indiana. The hearing was continued to and concluded on November 20, 2012. At the evidentiary hearings, the prefiled evidence of Petitioner, Crown Point and the OUCC was offered and admitted into the record of the proceedings of this Cause. No members of the general public appeared or participated at the evidentiary hearing.

Having considered the evidence and being duly advised, the Commission now finds:

1. Notice and Jurisdiction. Due, legal and timely notice of the public hearing in this Cause was given and published as required by law. Petitioner is a "public utility" within the meaning of that term in Indiana Code § 8-1-2-1 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. The Commission has jurisdiction over Petitioner and the subject matter of this proceeding.

2. **Petitioner's Characteristics.** Petitioner is an Indiana corporation engaged in the business of rendering water utility service to customers in numerous municipalities and counties throughout the State of Indiana for residential, commercial, industrial, public authority, sale for resale and public and private fire protection purposes. Petitioner also provides sewer utility service in Wabash and Delaware Counties.

3. **Relief Requested.** Petitioner seeks approval of a DSIC pursuant to Indiana Code ch. 8-1-31, a new rate schedule reflecting the DSIC, and approval of the costs of the eligible Distribution System Improvements ("Improvements") in Petitioner's DSIC. Petitioner's most recent rate order was approved in Cause No. 44022 on June 6, 2012 (the "2012 Rate Order"). Petitioner's most recent DSIC was approved in Cause No. 42351 DSIC 6 on October 20, 2010 (the "DSIC-6 Order"), but the DSIC was reset to zero as a result of the 2012 Rate Order. In accordance with the Commission's rules, Petitioner submitted a Reconciliation Report on November 21, 2011, which included the twelve month reconciliation of DSIC-6 (October 20, 2010 through October 19, 2011). Petitioner's Case-in-Chief included an updated Reconciliation Report which includes the reconciliation for the period of October 20, 2011 through June 14, 2012, which was the final DSIC billing period before the DSIC surcharge was re-set to zero due to the implementation of new rates pursuant to the 2012 Rate Order. This final reconciliation showed an over-recovery, which Petitioner showed as an offset to its proposed DSIC revenues.

The rate base cutoff in Cause No. 44022 consisted of property in service as of June 30, 2011. Therefore, Petitioner proposes to implement a DSIC to include non-revenue producing projects placed in service between July 1, 2011 and August 31, 2012 that were not included in Petitioner's rate base in the 2012 Rate Order. Petitioner's proposed DSIC would produce total annual DSIC revenues of \$6,194,699, which would equate to an increase of approximately 3.19% above the base revenue level approved in Petitioner's 2012 Rate Order.

4. **Petitioner's Direct Evidence.** Petitioner presented the direct evidence of Gregory P. Roach, Manager of Rates for Indiana American, and Stacy S. Hoffman, Director of Engineering for Indiana American.

A. **Calculation of DSIC 7.** Mr. Roach testified regarding the filing requirements and methodology for calculating the DSIC. Mr. Roach provided evidence concerning the calculation of the proposed DSIC and sponsored Petitioner's proposed rate schedules reflecting the DSIC in the same format as the existing tariff on file with the Commission. He explained that Petitioner is proposing to treat the DSIC as per the Commission's April 2, 2008 Order in Cause No. 42351 DSIC 4, in that the rate would be a percentage that would be applied to both the consumer's volumetric and metered service charge revenues. He further explained that, as per the Commission's April 30, 2010 Order in Cause No. 43680, Petitioner calculated the DSIC as a single percentage of bills that will be the same for all rate groups.

Mr. Roach testified that Petitioner proposes to include only non-revenue producing projects placed in service between July 1, 2011 and August 31, 2012 that were not included in rate base in the 2012 Rate Order. He added that all DSIC projects included in Petitioner's request are new used and useful water utility plant projects that: (1) do not increase revenues by connecting the distribution system to new customers; (2) are in service; and (3) were not

included in Petitioner's rate base in the 2012 Rate Order.

Mr. Roach testified that Petitioner's proposed DSIC would apply to public and private fire protection in a manner consistent with Petitioner's tariff that is presently on file with the Commission. Petitioner's tariff as filed in Cause No. 44022 makes the DSIC applicable to public and private fire protection. Mr. Roach explained that Petitioner made this modification to its tariff in Cause No. 44022. He testified that the change eliminates the temporary subsidy of public and private fire service customers by non-fire service customers that occurs when the Commission approves a DSIC for Petitioner that was applied to all charges except those on public and private fire service. Mr. Roach stated with public and private fire service tariff charges available for inclusion in the DSIC, the result is lower increase in rates for all customers than what would occur if public and private fire service tariff charges were excluded from the DSIC. He testified that the Commission Staff has indicated they were uncertain the Commission had meant to approve this modification to Petitioner's tariff and that Petitioner had agreed with Staff to raise the question for the Commission in this DSIC proceeding. He testified if the Commission finds the DSIC should not apply to public and private fire protection, the resulting DSIC would increase to 3.58%.

Mr. Roach then discussed how Petitioner calculated the Net Investor Supplied DSIC Additions. He stated that Petitioner reduced the DSIC Improvements of \$51,119,265 by the amount of the related plant retirements associated with the DSIC Improvements, consistent with the DSIC-6 Order. Mr. Roach stated that the amount of retirements made from July 2011 through August 2012 was \$4,014,075. Mr. Roach explained that he further adjusted the retirement amount for the actual amount of the cost of removal, net of salvage in the amount of \$4,442,365. Mr. Roach stated that there were total reimbursements from the Indiana Department of Transportation ("INDOT") and others, in the amount of \$95,277. These reimbursements were removed from the DSIC Improvements, resulting in Net Investor Supplied DSIC Additions of \$51,452,278, as shown on Line 5 of Petitioner's Exhibit GPR-3-U.

Mr. Roach also sponsored Petitioner's Exhibit GPR-4, Petitioner's rate of return summary. Mr. Roach explained that the rate of return used in this proceeding is Petitioner's weighted average cost of capital computed from Petitioner's capital structure as approved by the Commission in the 2012 Rate Order. He testified that Petitioner used the embedded debt cost rate as of June 2011 to determine the long-term debt cost rate. The common equity cost rate of 9.70% was determined in the 2012 Rate Order, and the weighted cost of capital is 6.95% and a pre-tax rate of return of 9.79%. Mr. Roach stated the pre-tax rate of return was calculated using a gross revenue conversion factor of 1.6934, calculated using Utilities Receipts Tax of 1.4%, State Corporate Adjusted Gross Income Tax of 7.75% and Federal Income Tax of 35%. He explained that the State Income Tax was calculated using an average of the effective tax rate for the period July 1, 2012 to June 30, 2013 by averaging the rates of 8% (2012) with the rate of 7.5% (2013). Mr. Roach stated that the resulting pre-tax return is \$5,037,176 when the pre-tax overall rate of return is multiplied by the net investor-supplied original cost of the Improvements.

Mr. Roach stated that Petitioner determined its depreciation expense of \$1,536,531 by using the annual depreciation rates by primary plant account previously approved by the Commission, multiplied by the Improvements, net of related retirements.

Mr. Roach testified and provided exhibits showing that the proposed DSIC Revenues are within the 5% range of Petitioner's base revenues as approved by the Commission in the 2012 Rate Order.

Petitioner's witness Stacy S. Hoffman sponsored Petitioner's Exhibit SSH-1 (as updated, Petitioner's Exhibit SSH-1-U), which provides a brief description of each Improvement project, the costs of each project, the date each project was placed in service, the account number assigned to each project based on accounting standards found in the National Association of Regulatory Utility Commissioners ("NARUC") Uniform System of Accounts for Class A Water Utilities ("USoA") and Petitioner's Operation area where each project exists.

Mr. Hoffman provided greater detail regarding the individual Improvements exceeding \$100,000 in total costs. For each of these Improvements, he explained why the improvement was needed, the resulting benefits to Petitioner and its customers and whether the plant had been retired. This is consistent with Petitioner's presentation in its past DSIC cases. Mr. Hoffman stated that Petitioner has invoices and other cost support for all projects listed in Petitioner's Exhibit SSH-1.

Mr. Hoffman generally described the Improvements as either replacement or reinforcement infrastructure. He explained that replacement infrastructure includes mains, tanks, tank coating systems, valves, hydrants, service lines and meters, while reinforcement infrastructure consists of mains, valves and hydrants with the purpose of improving pressure and flow of the existing distribution system. Mr. Hoffman testified about the inclusion of tank-related projects in Petitioner's proposed DSIC, referring to the Commission's February 27, 2003 Order in Cause No. 42351 DSIC-1 in which the Commission stated it would consider future requests to include "Distribution Reservoir" (i.e., water storage tank) projects for DSIC recovery on a case by case basis. He stated the tank-related projects included in this proceeding consist of certain foundation rehabilitations, a paint rehabilitation, a tank roof replacement and some distribution pump work to enable Indiana American to take the tanks offline. He said the projects are recorded in Uniform System of Accounts distribution Accounts, do not increase water storage capacity, and otherwise meet the statutory criteria to qualify as eligible distribution system improvements.

Mr. Hoffman testified that all of the retirements associated with the new infrastructure have been completed, but some cost of removals were estimated because, although the work was complete, the cost of removals were not yet paid. The estimates for these removals were included in Mr. Hoffman's work papers submitted in support of Petitioner's case in chief. Mr. Hoffman proposes to reconcile any variance between the estimated and actual removal costs in Petitioner's reconciliation report.

Mr. Hoffman testified that all Improvements listed in Petitioner's Exhibit SSH-1 meet the DSIC statutory requirements. He testified the following about the projects included for recovery in this Cause: none of the projects increase revenues by connecting the distribution system to new customers, all of the projects are in service, none of the projects were included in rate base in the last general rate proceeding, all necessary local, state and federal permits, approvals and authorizations have been obtained, and there was no affiliate involvement in any of the transactions. Mr. Hoffman explained that as Director of Engineering he has familiarity with

these projects through regular communication with Indiana-American Engineering staff during the planning, design and construction phases of these projects. Indiana-American project managers also confirm projects are in service through a physical inspection and then enter in-service dates for completed projects in the Indiana-American accounting software system.

Mr. Hoffman testified regarding the funding of the Improvements. He stated that projects included in this DSIC 7 were funded by Petitioner or were reimbursed by INDOT or others, as noted by Mr. Roach.

Mr. Hoffman stated Petitioner has a five-year Strategic Capital Expenditure Plan that provides for budgeted amounts of approximately \$171,500,000 for replacement mains, reinforcement mains, DSIC tank related work, hydrants, services and meters for the period 2013-2017. He testified that included in this amount is approximately \$32,000,000 budgeted over the same period for water main replacements required by state and local governments as a result of road improvements and other projects.

5. OUCG's Case-in-Chief. The OUCG presented testimony of Harold H. Riceman, Edward R. Kaufman and Margaret A. Stull. Mr. Riceman described his review of Petitioner's application for DSIC and concluded that, based on Mr. Kaufman's testimony, the OUCG proposes excluding the entire meter category of expenditures totaling \$18,005,555 and that Petitioner's proposal to apply the DSIC to public and private fire protection revenues be rejected. Mr. Riceman stated the OUCG recommends a DSIC of 2.12%. He also recommended in future DSIC filings Petitioner provide Petitioner's Exhibit SSH-1 sorted by account number and then by district.

Mr. Kaufman testified in support of the OUCG's proposal to exclude meter expenditures from the DSIC. Mr. Kaufman clarified that to the extent Petitioner has replaced meters at the end of their life of service, the OUCG does not object to including those meters in a DSIC, but that the OUCG objected to recovery of the cost of meter registers or any automated meter reading ("AMR") equipment through a DSIC. He also advocated for exclusion of the cost to replace any meters that were less than ten (10) years old. Mr. Kaufman contended that including these expenditures in the DSIC calculation stretches the definition of distribution system beyond that contemplated in the Commission's rules. He argued replacing properly functioning meters with AMR meters to implement a change in Petitioner's operations is not necessary to transport treated water. He further argued that replacing meter registers does not aid in the transportation of water. Mr. Kaufman noted that the meter replacement program was not discussed in Petitioner's direct testimony in this Cause, although "Accelerated AMR" appears numerous times in Petitioner's Exhibit SSH-1. He relied on a capital improvement plan submitted in Petitioner's last rate case (Cause No. 44022) as forecasting approximately \$7,549,723 in meter replacement expenditures for the period covered by this DSIC (July 2011 through August 2012) in contrast to the \$18,005,555 proposed to be included in this case. He asserted that such a large scale meter replacement program is inconsistent with the purpose of a DSIC because it is not equivalent to replacing aged infrastructure. He suggested that the funds Petitioner spent to install registers and replace meters less than ten (10) years old might have been better devoted to the replacement of aged pipe infrastructure. Mr. Kaufman concluded that the OUCG does not object to including the costs to replace meters older than ten (10) years in this DSIC, but that Petitioner has not provided sufficient evidence to determine such costs and therefore the OUCG's proposed

DSIC calculation excludes the entire meter category.

Ms. Stull testified in support of the OUCC's recommendation to deny Petitioner's request to modify the DSIC calculation to include fire protection revenues. She concluded the modification to the DSIC calculation to include fire protection revenues should be addressed in a proceeding other than an expedited DSIC proceeding where the OUCC and other parties can fully review, understand and consider the effects of the proposed change.

Eliminating all meter expenditures and related depreciation expense and excluding any public or private fire protection revenues, Ms. Stull calculated the OUCC's recommended DSIC percentage to be 2.12%.

6. Crown Point's Case-in-Chief. Gregory T. Guerrettaz, President of Financial Solutions Group, Inc., offered testimony on behalf of Crown Point. Mr. Guerrettaz recommended Petitioner provide additional information in future DSIC filings that would increase transparency, simplify review, and facilitate the expedited DSIC process schedule. He pointed out that while the OUCC has only 30 days to file its report and the Commission has only 60 days to issue its order, Petitioner has on average filed its DSIC's about every 18 months. This gives Petitioner much more time to reasonably prepare the DSIC than other DSIC stakeholders have to investigate its content and respond. He asserted Petitioner has the opportunity to prepare testimony and exhibits in a manner that provides transparency, reasonable explanations of important matters, and minimizes the need for costly, time-consuming discovery, in all facilitating the expedited DSIC review and order process. He explained that without this reasonable level of upfront disclosure, the other DSIC stakeholders and the Commission are left to pursue explanations and details that should reasonably be part of Petitioner's case-in-chief presentation.

Mr. Guerrettaz first pointed out that Petitioner's Exhibit SSH-1 is formatted across the 8 ½ inch axis of the page rather than formatted in landscape along the 11 inch axis. He pointed out that the Commission's GAO 2005-4 set forth the required DSIC forms with the SSH-1 form printed in landscape while all other forms are printed across the 8 ½ inch axis. He testified that, as printed from the Commission's website, by not using the landscape format, Petitioner's SSH-1 has very fine print and is difficult to read and use.

Second, he suggested that the brief two or three sentence description of all projects exceeding \$100,000 in cost presented in Exhibit SSH should provide more information. This additional information would facilitate a more user friendly and efficient, timely review in the expedited DSIC procedural schedule and also would result in a more transparent, complete Petitioner's case-in-chief presentation. For example, rather than requiring DSIC stakeholders to dig through the fine print of SSH-1, Petitioner should simply state the cost of each project in its brief, written description. Similarly, when Petitioner describes main replacements or installation of a second main, Petitioner should state the size of the original main and the size of the replacement or supplemental main. He suggested one additional line per project description would accomplish this, e.g.: "Total cost of \$360,000, main sizes, original two inch, replacement ten inch." He explained that under the accelerated DSIC schedule, participants are pressed for time and want to quickly and efficiently focus on the largest projects. Stating a total cost for each project in the short Exhibit SSH project description would facilitate that effort and would

relieve the reviewer of the time consuming burden of having to dig around in SSH-1 for each summarized project's total cost and then correlate that cost to each written project description. He also explained that stating the size of the original main and the replacement main would allow the reviewer to focus during the first read through of Petitioner's Exhibit SSH testimony on those instances where the main size has substantially increased, thereby eliminating the need to hunt and peck through SSH-1 for core pieces of information on projects that otherwise the reviewer just finished reading about in Petitioner's Exhibit SSH. He testified in the current two or three sentence SSH description format of main replacement projects, a small main which is replaced or supplemented by a much larger main to accommodate service to new area or a current area of expected customer growth, can in essence be hidden and treated like any DSIC recovery of cost for deteriorated main replacement.

Third, Mr. Guerrettaz recommended when Petitioner proposes to include in DSIC recovery a new cost description not previously included in prior DSIC Exhibits SSH-1, or proposes to include electronic technology or computer related costs, it should say so in its testimony. He pointed out that Petitioner includes substantial "AMR" and accelerated AMR Program costs in Exhibit SSH-1 but never listed any "AMR" or accelerated AMR Program costs in any prior DSIC Exhibits SSH-1. This lack of information creates an invitation for problems, delay, and inefficiency.

Fourth, Mr. Guerrettaz pointed out that 25 of the 43 listed main replacements in SSH are described as the original main being "undersized", but nowhere in Petitioner's testimony did it define what undersized means. He referred to the Response to Crown Point's Data Request 1-5 where Petitioner stated, "When Mr. Hoffman was referring to mains being undersized, he was referring to being undersized for purposes of fire protection. As a result, none of the replacement mains which are replacing mains that were "undersized" will increase revenues by allowing the connection of new customers that could not previously be connected." Thus, Mr. Guerrettaz recommended that if it is Petitioner's position that undersized mains are only "undersized" for purposes of fire protection and were not replaced or augmented by a second main to facilitate new connections or new sales revenue, it should state the main was only undersized for fire protection in the short Exhibit SSH project descriptions. Mr. Guerrettaz testified it is axiomatic that larger size mains have the ability to move more water and thereby the potential to serve additional customers. Yet, he pointed out that the \$1.3 million installation in Noblesville of 16 inch and 12-inch water mains and an \$844,000 Northwest reinforcement project to "improve marginal system pressures" only received a one sentence description in Petitioner's Exhibit SSH. Mr. Guerrettaz stated that "it seems reasonable that for the installation of large, new costly mains, if Petitioner wants DSIC expedited recovery, it would offer more than just a one sentence description regarding the nature of the project and would briefly explain why such large, new mains will not support connection of new customers. To offer only a one sentence explanation is to invite time consuming and costly discovery. The approach of providing bare bones and having the other DSIC participants divide the details is not conducive to an expedited schedule." It is also a disservice to the transparency of public rate increase documents, and is not conducive to an expedited schedule.

Mr. Guerrettaz also testified regarding water tank related projects included in this DSIC. He pointed out that in DSIC 1, the Commission rejected inclusion of the Hobart Water tank and

explained the rationale therefore. He testified the Commission was on the right path in DSIC 1 when it rejected water tank DSIC recovery. He testified that water tanks are very different from distribution system mains and should properly be excluded from DSIC recovery. He explained unlike hundreds or thousands of miles of aging, deteriorated, below ground distribution mains, above ground water tanks are easily susceptible to periodic inspection at distinct locations. He testified water towers may be water utility plant but they are not “distribution system.” He recommended Petitioner’s request for DSIC inclusion of water tower costs be denied.

Mr. Guerrettaz also addressed AMR. He testified that while Exhibit SSH-1 lists many millions of dollars of “accelerated AMR program,” nowhere in its testimony or in its Petition, does Petitioner describe what those costs are, or justify their inclusion in this DSIC 7. He pointed out that none of the previous DSIC-1 through 6 Exhibits SSH-1 listed costs as “AMR” or “accelerated AMR program.” Mr. Guerrettaz recommended rejection of the accelerated AMR program costs in this DSIC-7 pointing out that Petitioner did not present a single sentence in its testimony to even acknowledge their existence, no less justify AMR inclusion within the limits of DSIC recovery. In his view, automated meter reading equipment is distinguishable from the need to replace aged or deteriorating distribution mains in aged appurtenances so as to not be considered recoverable in the DSIC. Electronic meter reading equipment and related items should not be considered part of the “distribution system” for DSIC inclusion. He testified to the extent Petitioner is replacing existing functional meters with new, electronic data sending meters, that is not improving the mains and piping through which water flows and should not be DSIC recoverable. Finally, to the extent that meter reading expense and related operating expenses are reduced by AMR, a proper match of that new technology’s cost with the intended technology savings should be considered in the context of a base rate case where the offsetting savings may be included, rather than within the confines of the expedited DSIC process.

7. Petitioner’s Rebuttal.

A. AMR. Alan J. DeBoy, President of Indiana American, offered testimony to respond to Mr. Kaufman’s and Mr. Guerrettaz’s suggestion that Petitioner’s AMR program be excluded from DSIC recovery. Mr. DeBoy first apologized that the AMR program acceleration had not been raised in Petitioner’s case-in-chief testimony. He stated Petitioner simply had not anticipated that the AMR program acceleration would raise any concerns. Mr. DeBoy explained the AMR program represents a significant investment by Petitioner. He testified the program fits plainly within what the Commission has indicated in prior DSIC cases and in the Commission’s rules is eligible for recovery in a DSIC. He stated AMR meters have been included in past DSIC and general rate cases without question. He explained the OUCC’s and Crown Point’s proposal to change to a more restrictive interpretation of eligible distribution system improvements would have a significant impact on Indiana American and its earnings and would expedite the filing of Indiana American’s next general rate case. He calculated the OUCC’s and Crown Point’s interpretation would deprive Indiana American of approximately \$1.5 Million in annual net income and would produce a reduction in return on equity of almost 50 basis points. In contrast, Mr. DeBoy testified the difference in interpretations between the OUCC’s and Petitioner’s position produces about a 1% difference in overall rates or approximately 50¢ per month for the average residential customer. Mr. DeBoy explained that the differences between the parties on the inclusion of AMR relate to whether Indiana American’s speed of implementation is appropriate or whether the implementation should be spread over a couple of years more. He

cited to the Commission's Order in Indiana American's first DSIC proceeding in which the Commission found the only limitation on DSIC eligibility once an improvement is found to be distribution system is whether it results in connection of the distribution system to new customers. He testified the OUCC's and Crown Point's interpretation and proposed exclusion of AMR would be a dramatic shift away from the Commission's prior DSIC Orders.

Mr. Hoffman also testified in support of Petitioner's inclusion of AMR in this DSIC. He too opined that Mr. Kaufman's opposition to including AMR appears based on the timing of implementation of the program. He testified that extending the time to convert to AMR technology would delay realization of the benefits of the technology and, in the interim, create systems with multiple generations of equipment, resulting in inefficiencies of operating and maintaining the equipment. In contrast, Mr. Hoffman testified, a shorter technology conversion time reduces conversion costs. He presented evidence that Indiana American had realized a savings of greater than 25% in material costs based on the quantities and conversion time for Petitioner's AMR conversion. He referred to other water utilities who have converted to AMR technology over relatively short periods. He explained that expanding the conversion time for AMR conversion would be contrary to recognized best practices and that prudent conversion time to AMR technology must include replacement of meters and meter registers less than ten (10) years old with AMR technology. Mr. Hoffman testified that AMR costs have been included in Indiana American's DSIC filings since 2007. In addition, he stated Indiana American had met with representatives of the OUCC and the Commission in July 2010 to discuss the benefits of AMR technology. Mr. Hoffman testified he does not believe the timing of implementation came up during that or any other meeting.

Mr. Hoffman responded to Mr. Kaufman's suggestion that Indiana American's meter replacement program takes funds away from replacing aged infrastructure, explaining that not only is AMR technology very important but appropriate types of distribution system investments vary over time. Mr. Hoffman presented evidence that showed Petitioner has increased investments in main replacements to a yearly average of \$18.7 Million per year over the last five years.

Mr. Hoffman then offered detailed testimony on the benefits of AMR technology, including benefits to meter reading, employee safety, enhanced customer services, billing benefits, distribution system water quality and backflow detection benefits and related potential for capital expenditures deferrals, in addition to cost savings benefits. According to Mr. Hoffman, all of these benefits cannot be fully realized until conversion to AMR technology is complete. He also explained that Mr. Kaufman's suggestion that replacing registers on meters does not aid in the transportation of water does not take into consideration that meter registers are integral components of the entire meter assembly.

Finally, Mr. Hoffman testified that AMR technology is critical to Indiana American's performance of its capacity factor study as ordered by the Commission in Cause No. 44022. He explained that AMR technology installed on a sufficient number of meters across all customer classes is required to conduct the new capacity factor study because it provides a record of dynamic water use profiles of actual customers in all customer classes through time. He stated this requirement and desire to complete the modern capacity factor study meant more AMR conversions were necessary even sooner than Indiana American had previously planned. In

addressing Mr. Kaufman's reliance on the capital plan submitted in Cause No. 44022, Mr. Hoffman noted that the capital plan submitted in that Cause was developed over 2 ½ years ago and has undergone re-evaluations and updates since that time. As a result, he stated that the capital plan has little relevance regarding the AMR technology conversion issue in this case.

B. Tank-Related Projects. In rebuttal, Mr. Hoffman addressed Mr. Guerrettaz's testimony that tank-related projects should not be included in this DSIC. Mr. Hoffman distinguished the tank-related projects included in this DSIC filing and the Hobart water tank disallowed in the first DSIC case. He stated all of the work on the tank-related projects is capital rehabilitation work on existing tanks and not construction of new tanks. He explained the projects do not increase storage capacity and none of the work was for the purpose of adding new customers.

C. Fire Protection. Mr. DeBoy testified that the lack of testimony in Petitioner's last rate case concerning the change to the tariff to include fire protection revenues in the DSIC was pure oversight. He testified that Petitioner did not realize the oversight until the issue was raised after the current tariff had already been approved by the Commission. He explained that Petitioner was uncertain how the tariff could be changed back to the prior methodology without an Order from the Commission to do so in a docketed proceeding and that is why it was proposed in this DSIC proceeding. Mr. DeBoy conceded that the Commission may prefer to delay a decision on this issue until the next general rate case.

D. Filing Requirements. Mr. Roach responded to Mr. Guerrettaz's recommendations. He disagreed with Mr. Guerrettaz's contention that the proper orientation of Petitioner's Exhibit SSH-1 has been ordered by the Commission and pointed out that, upon request, Petitioner had provided Crown Point with an electronic copy of the exhibit so that Mr. Guerrettaz could print the exhibit in whatever size and format he desired. He further testified that the additional information recommended by Mr. Guerrettaz to be included in Petitioner's exhibits is not required by the Commission's rules and is unnecessary. Mr. Roach testified that Mr. Guerrettaz's recommendation regarding additional information to be included regarding undersized mains is likewise not required by the Commission's rules and would impose a test for DSIC eligibility not heretofore espoused by the Commission.

Mr. Hoffman also responded to Mr. Guerrettaz's suggestion that Indiana American did not provide sufficient evidence to support the main replacement projects included in Petitioner's case-in-chief. Mr. Hoffman noted that in the Commission's Order in Indiana American's first DSIC proceeding, the Commission recognized that mains may be replaced with mains of a larger size and remain eligible for DSIC recovery. In response to Mr. Guerrettaz's concern over the "Reinforcement Projects" described in Petitioner's case-in-chief, Mr. Hoffman explained that providing reliable service was the sole purpose of the construction of the reinforcement projects.

Mr. Hoffman responded to Mr. Riceman's suggestion of sorting the data in Petitioner's Exhibit SSH-1 by account number first and then by district, stating that would be acceptable to Indiana American.

8. Commission Discussion and Findings.

A. DSIC Requirements. Indiana Code ch. 8-1-31-1 requires the Commission to approve a DSIC in order to allow a water utility to adjust its basic rates and charges to recover a pre-tax return and depreciation expense on eligible distribution system improvements. Indiana Code § 8-1-31-5 defines eligible distribution system improvements as new, used and useful water utility plant projects that:

- (a) do not increase revenues by connecting the distribution system to new customers;
- (b) are in service; and
- (c) were not included in the public utility's rate base in its most recent general rate case.

Under Indiana Code § 8-1-31-6, the rate of return allowed on eligible distribution system improvements is equal to the public utility's weighted cost of capital. Unless the Commission finds that such determination is no longer representative of current conditions, Indiana Code § 8-1-31-12 provides that the cost of common equity to be used in determining the weighted cost of capital shall be the most recent determination by the Commission in a general rate proceeding of the public utility.

Indiana Code ch. 8-1-31 establishes the process for the Commission to follow and authorized the Commission to adopt rules to establish procedures not inconsistent with Chapter 8-1-31 or 170 IAC 6-1.1.

B. Discussion of Proposed DSIC. In our first DSIC order in Cause No. 42351 DSIC-1, issued on February 23, 2003, we addressed the fact that the statutory definition of "eligible distribution system improvements" does not explicitly include any requirement that the new, used and useful plant projects be improvements to the utility's *distribution system*.¹ We addressed that omission in our order in DSIC 1, recognizing the importance of interpreting the law with respect to DSIC's in Indiana by looking at the legislation as a whole. We noted that in *Brown v. Grzeskowiak*, 230 Ind. 110, 101 N.E. 2d 639 (1951), "The intention of the legislature, as ascertained from a consideration of the act as a whole, will prevail over the literal meaning of any of the terms used therein." We also relied on the holding in *City of Indianapolis v. Evans*, 216 Ind. 555, 24 N.E. 2d 776 (1940), noting the court said "The legislative intent, however, is to be ascertained by an examination of the whole, as well as the separate parts of the act, and when so ascertained, the intention will control the strict letter of the statute or the literal import of particular terms or phrases, where to adhere to the strict letter or literal meaning would lead to injustice, absurdity, or contradict the evident intention of the legislature."

¹ Both Indiana Code § 8-1-31-5 and 170 IAC 6-1.1-1(g) define "eligible distribution system improvements" as new, used and useful water utility plant projects that:

- (a) do not increase revenues by connecting the distribution system to new customers;
- (b) are in service; and
- (c) were not included in the public utility's rate base in its most recent general rate case.

In DSIC 1, Indiana-American had included in its DSIC application improvements to source of supply, water treatment plant, general plant and security, which the OUCC said should not be included in a DSIC despite the lack of specific exclusion in the definition of “eligible distribution system improvements.” Determining the intent of the legislature and looking at the act as a whole, including the title to establish the purpose and scope of the act, we agreed with the OUCC that a DSIC should only include distribution system improvements.

Just as it did in DSIC 1, Petitioner again relies on an overly inclusive interpretation of “eligible distribution system improvements” that does not recognize the Commission’s understanding, as set forth in DSIC 1, of DSICs in Indiana. In that order, we specifically referenced the statements of Indiana American’s former Vice-President, who spoke in favor of the passage of DSIC legislation in order to “allow for the replacement of aged infrastructure.” DSIC 1 Order at 16. In fact, the Commission specifically stated that “We agree with the Public’s testimony that the purpose of a DSIC proceeding is to encourage, through an expedited and automatic rate increase, *repair or replacement of a distribution system’s aging and failing infrastructure.*” *Id.* at 21 (emphasis added).

In its application in this case, Petitioner seeks recovery of more than \$18 million for numerous meter related projects later identified as an “accelerated AMR program.” Indiana-American included in its DSIC the cost of approximately 90,000 meters to put into place AMR technology by replacing meters without regard to their condition. Petitioner replaced meters with no less than five to ten years of expected remaining useful life. Petitioner replaced meter registers on meters placed in service less than five years ago. In addition to new AMR meters and meter registers, the proposed \$18 million DSIC costs include AMR meter reading equipment and meters not yet placed in service. (Response to OUCC DR 3-1, attached to SSH-R1, and OUCC CX-5). The OUCC questioned whether a project that involved replacing plant that did not otherwise need to be replaced merely to institute automatic meter reading qualified as “eligible distribution system improvements.” The OUCC asserted that the definition of “distribution system” in our rule, which we must consider to be within the definition of “eligible distribution system improvements,” indicates that to be included in a DSIC, a project must be necessary for the transportation of water. The OUCC based its position in part on the fact that the definition of “distribution system” includes the provision that the addition must be “necessary to transport treated water . . . to the customer.” The OUCC maintained that institution of an AMR program, while it could be prudent and includable in rate base, does not qualify for special ratemaking treatment through a DSIC since retiring equipment early to improve billing and other operational functions does not promote the transportation of water. Ultimately, the OUCC considers such projects not to be within the evident intent of DSICs in Indiana. We agree.

In its proposed order, Petitioner asserted there are three basic problems with excluding AMR meters from the DSIC. First, the AMR meters are booked within Account Number 334 of the NARUC Uniform System of Accounts. Second, Petitioner had disclosed in Cause No. 44022 that it was planning to spend approximately \$7,549,723 on meters and meter replacements over the period covered by this DSIC and neither the OUCC nor Crown Point raised any objection at that time. Third, Petitioner disclosed in that Cause that it needed to expedite its meter replacement program to comply with our requirement to conduct a new and more detailed

capacity factor study before Petitioner's next rate case.

Petitioner asserted that since NARUC System of Accounts indicates meters do not need to be installed before they are so booked, that meters not yet in use should be included as a cost in a DSIC. Although uninstalled meters may be considered "in service" for accounting purposes, we do not find such meters to be "in service" for ratemaking purposes, and specifically, for inclusion in a DSIC. As Petitioner notes in its Reply Brief, any DSIC-eligible plant must be used and useful, i.e., actually devoted to providing utility service and reasonably necessary for the provision of that service. Meters on shelves do not provide utility service, even if they are "in service" for accounting purposes. Accordingly, uninstalled meters may not be included in a DSIC.

Further, recovery of the replacement cost of newer traditional meters with AMR meters does not fit within the context of the DSIC, in that the Commission stated in DSIC 1 that the purpose of DSIC recovery is to replace aged infrastructure. We agree with Mr. Kaufman's assessment that the replacement of meters older than 10 years could be recoverable in a DSIC. However, despite having the opportunity to respond to Mr. Kaufman, Petitioner did not include in the record the necessary information for the Commission to determine what the DSIC factor would be if only 10 year and older meters were considered. While Petitioner's Exhibit SSH-R1 indicates the number of meters replaced older than 10 years, it is unclear whether that discovery response is solely for the DSIC 7 period. Further, we do not have the retirement costs of the 10 year and older meters that were replaced, nor do we have the cost of meters and associated installation costs related to the AMR meters used to replace 10-year or older meters.

We next address Petitioner's argument that it had disclosed in the last rate case that it was planning to spend approximately \$7,549,723 on meters and meter replacements over the period covered by this DSIC, and neither the OUCC nor Crown Point raised any objection at that time. We note that while Petitioner provided its plan in Cause No. 44022, it made no mention of any intention to include accelerated AMR replacements in a DSIC. Contrary to Mr. DeBoy's statement of what he interpreted as frustration by the Commission over the frequency of rate cases, the Commission seeks to address issues in each given proceeding fairly and completely. While we do not find that Petitioner's accelerated AMR meter replacement, as proposed, should be approved under a DSIC proceeding, the Commission has addressed plant replacement programs in the confines of a rate case. Here, we simply do not find that the expedited DSIC process is an appropriate avenue for cost recovery.

Finally, Petitioner's represented need to replace functional non-AMR meters with AMR meters to perform its capacity factor study does not make plant that would otherwise not qualify for recovery in a DSIC, as defined by the Commission's rules, eligible for inclusion in a DSIC.

Based on the foregoing, we deny Petitioner's request to include \$18 million of costs associated with its accelerated AMR meter replacement program in this DSIC.

i. Tank Rehabilitation Projects. Crown Point's witness Guerrettaz recommended we disallow recovery for Petitioner's investments in tank rehabilitation projects based on our decision to disallow the Hobart Water tank in DSIC 1. The evidence demonstrates that there are meaningful distinctions between the tank rehabilitation projects Petitioner seeks to

include in this DSIC and the Hobart water tank project from DSIC 1. Most notably, the tank projects in this proceeding were necessary rehabilitations of existing distribution infrastructure and were not construction of new tanks. Petitioner's evidence shows the projects did not increase storage capacity and none of the work was for the purpose of adding new customers. Accordingly, we decline to exclude the tank rehabilitation projects from DSIC recovery.

ii. Fire Protection. A question has arisen in this proceeding whether changes made to Petitioner's tariff in its last rate case to include in DSIC public and private fire protection revenues should be applicable in this DSIC. The evidence in this case shows that this change went largely overlooked in Cause No. 44022. Petitioner's evidence in Cause No. 44022 did not discuss the change and no party to that proceeding addressed it. Nevertheless, the tariff filed by Petitioner and approved by the Commission contained the change. As such, we agree with Petitioner's witness DeBoy that the tariff could not be further revised outside of a docketed proceeding.

However, we do not agree that this modification to the DSIC calculation is appropriately considered within the expedited timeframe of a DSIC proceeding. We are not convinced that the change to Petitioner's tariff to include public and private fire protection revenues in the DSIC calculation has been presented to date in a manner that will allow all interested parties to fully review this proposed change or to state their position with respect to the change. Accordingly, we defer consideration of the proposed modification to Petitioner's next general rate case.

iii. Filing Requirements. Mr. Guerrettaz has made a number of suggested additional requirements for the evidence to be filed in support of DSIC requests. We have noted above the applicable statute and rules governing DSIC filings. Mr. Guerrettaz's suggestions go beyond what is required by statute and under our rules. We decline to adopt his suggested changes. In addition, we note that we have previously acknowledged that, with respect to main replacements, a utility may replace mains "with larger diameter mains in response to or anticipation of new customers, yet still be DSIC eligible." DSIC 1 Order at 20.

We accept the OUCC's proposed change to the organization of Petitioner's Exhibit SSH-1 and direct Petitioner, in future DSIC filings, to sort the exhibit first by account number and then by district.

iv. Projects and Amounts to be Included as Distribution System Improvement Charges. The OUCC's direct evidence provides a detailed explanation of the methodology used to calculate the proposed DSIC revenue requirements of \$3,666,274. The total cost for the net investor supplied DSIC Additions is \$34,629,904, and the evidence shows the pre-tax return associated with those additions, as calculated in accordance with Indiana Code ch. 8-1-31 is \$3,390,268. The revenue requirement for depreciation on the Improvements is \$648,100. Finally, total DSIC revenues of \$4,038,368 are reduced by \$372,094 to reflect the reconciliation (over-recovery) of revenues under DSIC-6. We find that Petitioner is therefore authorized to collect from its water customers a DSIC of 2.12% calculated on a percentage of bill basis.

C. Reconciliation of Petitioner's DSIC. Petitioner should be prepared to reconcile the DSIC approved by this Order in the manner prescribed by Indiana Code § 8-1-31-14 and 170 I.A.C. 6-1.1-8. Under Indiana Code § 8-1-31-14, at the end of each 12-month period

a DSIC is in effect the difference between the revenues produced by the DSIC and the expenses and the pre-tax reflected in it should be reconciled and the difference refunded or recovered as the case may be through adjustment of the DSIC.

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

1. A Distribution System Improvement Charge calculated on a percentage of bill basis and designed to generate \$3,666,274 in additional annual revenues shall be and hereby is approved for Petitioner Indiana-American Water Company, Inc.

2. Prior to placing into effect the above-authorized DSIC, Petitioner shall file with the Water/Sewer Division of the Commission an appendix to its schedule of rates and charges for water service.

3. The above-authorized DSIC shall be subject to reconciliation as described in Finding No. 8(C) above.

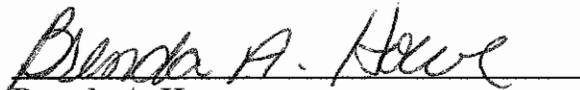
4. This Order shall be effective on and after the date of its approval.

ATTERHOLT, BENNETT, LANDIS, MAYS AND ZIEGNER CONCUR:

APPROVED:

DEC 27 2012

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



Brenda A. Howe

Secretary to the Commission