

ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

JOINT PETITION OF INDIANA-AMERICAN )  
WATER COMPANY INC. ("INDIANA- )  
AMERICAN") AND MARION HEIGHTS )  
CONSERVANCY DISTRICT ("MARION )  
HEIGHTS") FOR APPROVAL AND )  
AUTHORIZATION OF: (A) THE )  
ACQUISITION BY INDIANA-AMERICAN OF )  
MARION HEIGHTS CONSERVANCY )  
DISTRICT ("MARION HEIGHTS") UTILITY )  
PROPERTIES ("MARION HEIGHTS )  
SYSTEM") IN VIGO COUNTY, INDIANA )  
("THE MARION HEIGHTS AREA"); (B) )  
APPROVAL OF ACCOUNTING AND RATE )  
BASE TREATMENT; (C) APPLICATION OF )  
INDIANA-AMERICAN'S RATES AND )  
CHARGES FOR PETITIONER'S WABASH )  
VALLEY OPERATION TO WATER SERVICE )  
RENDERED BY INDIANA-AMERICAN IN )  
THE AREA SERVED BY THE MARION )  
HEIGHTS OPERATION; (D) ALL )  
NECESSARY LICENSES, PERMITS, AND )  
FRANCHISES FOR INDIANA-AMERICAN TO )  
PROVIDE WATER SERVICE IN THE )  
MARION HEIGHTS AREA; (E) )  
APPLICATION OF INDIANA-AMERICAN'S )  
DEPRECIATION ACCURAL RATES TO )  
SUCH ACQUIRED PROPERTIES; AND (F) )  
THE SUBJECTION OF THE ACQUIRED )  
PROPERTIES TO THE LIEN OF INDIANA- )  
AMERICAN'S MORTGAGE INDENTURE. )

CAUSE NO. 43817

APPROVED: MAR 10 2010

**BY THE COMMISSION:**

**James D. Atterholt, Commissioner**  
**David E. Veleta, Administrative Law Judge**

On October 15, 2009, Joint Petitioners, Indiana-American Water Company, Inc. ("Indiana-American") and Marion Heights Conservancy District ("Marion Heights") filed their joint petition with the Indiana Utility Regulatory Commission ("Commission") in this matter. On October 16, 2009, Joint Petitioners filed their prepared testimony and exhibits constituting their case-in-chief. On January 15, 2010, the Indiana Office of Utility Consumer Counselor ("OUCC") filed the testimony of Harold H. Riceman, utility analyst.

Pursuant to notice of hearing duly given and published as required by law, proof of which was incorporated into the record by reference and placed in the official files of the Commission, an evidentiary hearing in this Cause was held at 9:30 a.m. on February 10, 2010 in Room 224, National City Center, 101 W. Washington Street, Indianapolis, Indiana. Joint Petitioners and the OUCC appeared and participated in the evidentiary hearing. No members of the general public appeared.

Based upon the applicable law and evidence, the Commission now finds:

1. **Notice and Jurisdiction.** Due, legal and timely notice of the public hearing conducted herein was given by the Commission as required by law. Indiana-American is a “public utility” within the meaning of that term in Ind. Code §8-1-2-1 and is subject to the jurisdiction of the Commission in the manner and to the extent provided by law. Marion Heights is a conservancy district formed pursuant to Ind. Code § 14-33 *et seq.* and is subject to regulation by the Commission as a public utility.<sup>1</sup> The Commission has jurisdiction over Joint Petitioners and the subject matter of this proceeding.

2. **Joint Petitioners’ Characteristics.** Indiana-American 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. Indiana-American also provides sewer utility service in Wabash and Delaware Counties.

Marion Heights owns and operates water utility property which is used and useful for the provision of water utility service to customers located in rural areas of northwest Vigo County.

3. **Relief Requested.** Joint Petitioners request that the Commission (1) grant such approvals as may be necessary to consummate the acquisition of the Marion Heights System (as defined in the Joint Petition) by Indiana-American and permit the operation thereof by Indiana-American on the terms described in the Asset Purchase Agreement, including all necessary licenses, permits and franchises to provide utility service through the Marion Heights System following closing; (2) find that public convenience and necessity require water service by Indiana-American in the areas now served by the Marion Heights System; (3) authorize Indiana-American to charge customers currently served by the Marion Heights System the current rates and charges and apply the same rules and regulations for water service and private and public fire service applicable in Indiana-American’s Wabash Valley Operations on file with and approved by the Commission, as the same may be changed from time to time; (4) approve the accounting entries as described in the direct testimony of Michael J. Hoffman to reflect the acquisition of the Marion Heights System; (5) authorize Indiana-American to apply its existing depreciation accrual rates to the Marion Heights System; and (6) approve the encumbering of the properties comprising the Marion Heights System with the lien of Indiana-American’s Mortgage Indenture.

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<sup>1</sup> Contemporaneously with Joint Petitioners’ filing of its case-in-chief in this proceeding, Marion Heights filed a petition with the Vigo County Circuit Court pursuant to Ind. Code § 14-33-15-1 *et seq.* for authorization to dissolve the conservancy district and wind up its affairs.

**4. Evidence Presented.**

(a) Joint Petitioners' Evidence. The complete terms and conditions of the purchase and sale of the Marion Heights System are set forth in the Asset Purchase Agreement, filed as Petitioners' Exhibit JCH-3. Mr. Henson testified that Indiana-American proposes to acquire all the wells, water plants, water storage tanks, water mains, service lines, meters, hydrants, equipment, real estate, easements and permits and all other assets located within the Marion Heights System which are part of the production, treatment, transmission and distribution system utilized to provide water service to customers, excluding (a) liabilities, contingent or otherwise, (b) customer service connections which are and shall remain the property of the customer, (c) furniture, (d) transportation equipment, (e) tools, shop and garage equipment, (f) the meeting facilities utilized by Marion Heights located on Highway 150 but owned by the Sisters of Providence, (g) communication equipment, (h) miscellaneous equipment, (i) cash and accounts receivable, and (j) customer deposits.

As described in Mr. Henson's direct testimony, the Asset Purchase Agreement between Indiana-American and Marion Heights provides for the acquisition by Indiana-American of the utility assets of Marion Heights for a purchase price of \$900,000. The purchase price was determined through arms-length negotiations with the Marion Heights Board along with consideration of an independent valuation of the Marion Heights System. The Asset Purchase Agreement further provides that any proceeds, after Marion Heights' expenses and liabilities have been completely satisfied, resulting from the sale of the Marion Heights System will be distributed to Marion Heights System customers that meet certain eligibility criteria. In particular: (A) the account in the name of customer of record must be active on the Closing Date; (B) the account must have no outstanding balance; and (C) in the event any customer shall be deceased as of the Closing Date, no allocation will be made to that account. Petitioners' Exhibit JCH-3, Schedule 2.5.

Ms. Helen A. Ruhl, Chairperson of the Marion Heights Board, testified that Marion Heights decided to sell the water utility due to the Board's lack of time, technical expertise and resources to manage a water utility in the current environment of increasing drinking water regulation. Ms. Ruhl also indicated that there are a number of short- and long-term improvements that would be necessary if Marion Heights were to continue to own and operate the system. These improvements would result in a significant and immediate rate increase even though Marion Heights rates are already significantly higher than Indiana-American's rates in the area. Ms. Ruhl explained that although Indiana-American will need to recover the costs of the needed repairs and corrections to operational deficiencies, Indiana-American's rates should be lower than the rate Marion Heights is projecting were it to retain ownership.

Michael J. Hoffman, Finance Manager for American Water Works Service Company, a sister company to Indiana-American, provided testimony in support of the valuation study of the Marion Heights System presented as Petitioners' Exhibit MJH-4. Mr. Hoffman explained that Indiana-American hired Robert E. Curry & Associates, Inc. to conduct a valuation study of the Marion Heights System, which included providing quantities and vintages of assets by type and an estimate of the costs to install those assets. Mr. Hoffman noted that the net original cost of \$1,044,714.73 shown on page 43 of Petitioners' Exhibit MJH-4 does not include the original cost of the land and land rights acquired by the Marion Heights System.

Mr. Hoffman also provided testimony on the accounting and ratemaking treatment proposed by Indiana-American in connection with its acquisition of the Marion Heights System. Petitioners' Exhibit MJH-7 sets forth the proposed journal entry, which shows a recorded net original cost of the Marion Heights System assets as the purchase price plus transaction costs. Mr. Hoffman explained that this accounting treatment is appropriate where (1) the price resulted from an arm's length negotiation between the buyer and seller, and (2) the system being acquired is small or troubled. Mr. Hoffman stated that although the Marion Heights System is not troubled, it is certainly small, with approximately 410 customers.

The accounting entries proposed by Indiana-American, consistent with Commission policy, would be to record the original cost of the Marion Heights System as a debit to Account 101 - Utility Plant in Service and to record all associated accumulated depreciation as a credit to Account 108 - Accumulated Depreciation. Mr. Hoffman stated that the new steel water treatment package plant would be recorded in Account 151 - Materials and Supplies. Mr. Hoffman further stated that the net original cost of the Marion Heights System would be the gross cost of the facilities, including adjustments for closing and transaction costs (i.e., the \$900,000 purchase price plus an estimated \$25,000 in transaction costs, to be adjusted for actual costs). Mr. Hoffman further testified that the depreciation accrual rates to be applied to the Marion Heights System assets would be the rates approved by the Commission in Cause No. 43081 on November 21, 2006, as included in the calculation of rates with the approval of Indiana-American's rate case in Cause No. 43187.

Mr. Henson and Deron E. Allen, Indiana-American's Director of Operations in charge of the Western Indiana Districts, testified that the customers of the Marion Heights System and Indiana-American's existing customers will benefit from the acquisition. Marion Heights customers will have consistent access to highly trained and experienced operational resources and will not have to be concerned with their water supply meeting water treatment regulations. In addition, being part of the American Water system also provides an advantage in economies of scale that will directly benefit these customers as environmental, water quality, and operational issues become the responsibility of Indiana-American. Mr. Henson explained that Marion Heights System customers will gain full time management of their water system including, but not limited to, a full time operations staff, 24/7 customer service and emergency response, along with full time functional specialists such as engineering and water quality. Mr. Henson further explained that Marion Heights System customers will benefit from many programs that Indiana-American uses to ensure customer satisfaction, such as routine valve operating programs, hydrant flushing and inspection, meter replacement, and plant security. Finally, Mr. Henson stated that most Marion Heights System customers will experience a decrease in their monthly water bill as a result of the acquisition. Based on Indiana-American's rates as of the filing of its testimony in this Cause, Mr. Hoffman estimated the average residential customer's monthly bill would decrease from \$51.88 to \$30.49,<sup>2</sup> based on usage of 6,000 gallons.

According to Mr. Henson's testimony, Indiana-American's existing customers will benefit from expanded economies of scale and an extended service area that could result in additional future growth. He explained that the added customers and potential to serve a larger

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<sup>2</sup> Joint Petitioner's calculation does not include the Distribution System Improvement Charge or the Public Fire Protection Surcharge.

service area in the Terre Haute area will provide a larger base over which Indiana-American can spread fixed cost and increase efficiencies.

Mr. Hoffman's testimony described Indiana-American's intention to apply the tariff rates, rules and regulations on file from time to time and applicable to Indiana-American's Wabash Valley Operation to the customers of the Marion Heights System. Support offered by Mr. Hoffman for application of the Wabash Valley Operation rates includes the proximity of the Wabash Valley Operation's service area to the Marion Heights System's current service area and the fact that, upon consummation of the transaction, the Marion Heights System will be managed by personnel from the Wabash Valley Operation. Mr. Hoffman stated that utilizing Indiana-American's existing Wabash Valley rates is also consistent with the approach taken in past Commission orders to simplify Indiana-American's overall rate structure with a goal of having single tariff pricing for the entire state of Indiana.

Mr. Hoffman's direct testimony also described the encumbrance that would be placed on the Marion Heights System assets as a result of the acquisition under Indiana-American's General Mortgage, which secures most of Indiana-American's utility property for the benefit of Indiana-American's bond holders. Mr. Hoffman testified that Indiana-American has access to all of the necessary funds to support the acquisition. Initially, Mr. Hoffman explained, those funds will come from internally generated funds and/or short-term debt, but when appropriate, the short-term debt will be funded with permanent common equity and long-term debt financing, upon approval from the Commission. The short-term debt for the initial financing would be funded through Indiana-American's cash management arrangement with American Water Capital Corporation, an affiliate of Indiana-American. Mr. Hoffman testified that Indiana-American does not believe the acquisition would impair its ability to raise necessary capital on reasonable terms while maintaining a reasonable capital structure. According to his testimony, the projected investment to acquire the Marion Heights System is equal to less than 0.2% of Indiana-American's total capital structure.

(b) OUCC's Evidence. The OUCC's witness Harold H. Riceman, a utility analyst in the OUCC's Water/Wastewater Division, testified in support of the proposed acquisition. Mr. Riceman stated that the OUCC agrees that the proposed acquisition is in the interest of the rate payers and should be approved.

Mr. Riceman stated that the OUCC agrees that public convenience and necessity require water service by Indiana-American in the areas now served by Marion Heights. Mr. Riceman recommended that Indiana-American's Wabash Valley District's rules, regulations, rates and charges be applicable to the existing Marion Heights customers once the purchase is consummated.

Mr. Riceman agreed with Indiana-American's determination to include the full purchase price of \$900,000 in net original cost rate base for both accounting and rate base purposes. He noted that the price for the Marion Heights System was established through negotiations between two unrelated parties and reflects a value for the assets that is not greater than the net book value. Mr. Riceman stated that he had no objection to Indiana-American's proposed accounting entries as shown on Petitioners' Exhibit MJH-7 and agreed with Indiana-American's proposal that the Marion Heights System assets be subject to Indiana-American's depreciation accrual rates approved by the Commission in Cause No. 43081 on November 21, 2006, and as included in the calculation of rates with the approval of Indiana-American's rate case in Cause No. 43187 on

October 10, 2007. Finally, Mr. Riceman expressed no objection to the Marion Heights System assets becoming subject to Indiana-American's Indenture of Mortgage upon their acquisition by Indiana-American.

However, Mr. Riceman indicated that the OUCC disagreed with one aspect of how Marion Heights planned to distribute proceeds of the purchase to its customers. This concern related to the eligibility requirements for customers to receive a share of these proceeds. He explained that Criterion B states that the account must have no outstanding balances in order to receive a share of the proceeds. Thus, a customer of ten years could, at the time of the closing date, have an outstanding balance because that customer for some reason forgot to pay the bill on time that month and arguably be cut-off from all shares of the proceeds. Mr. Riceman stated that a better approach would be for Marion Heights to simply apply the customer's portion of the proceeds to any outstanding balance, and recommended conditioning the transfer on Marion Heights employing that practice.

(c) Joint Petitioners' Rebuttal Evidence. In rebuttal, Ms. Ruhl responded to the OUCC's testimony regarding the distribution of the proceeds from the sale of the Marion Heights System. Ms. Ruhl testified that Marion Heights is agreeable to modifying its proposed method of distributing proceeds as requested by Mr. Riceman. She stated that Criterion B regarding no outstanding balances shall be eliminated and Marion Heights will apply the proceeds first to any outstanding balance and then distribute the net amount to the customer.

## **5. Commission Discussion and Findings.**

(a) Public Convenience and Necessity. The evidence demonstrates that the Marion Heights System can be easily integrated into Indiana-American's existing system. The public now served by the Marion Heights System will benefit from Indiana-American's financing capability, management and technical expertise. As a result of this acquisition, certain necessary capital improvements will be made and at less cost to customers of the Marion Heights System than if the system were to remain under Marion Heights' ownership. Marion Heights System customers and Indiana-American customers will benefit from the increased number of customers over which fixed costs will be spread. Finally, Marion Heights System customers will gain access to many programs that Indiana-American uses to ensure customer satisfaction. Based on the evidence of record, the Commission finds that the acquisition and operation of the Marion Heights System by Indiana-American on the terms described in the Asset Purchase Agreement is supported by public convenience and necessity and is in the public interest. Furthermore, following the closing, Indiana-American shall be authorized to serve in the areas currently served by the Marion Heights System.

(b) Rates and Rules. Indiana-American currently has on file with the Commission a schedule of rates and charges and rules and regulations applicable to water utility service provided by Indiana-American in the Wabash Valley Operation. Consistent with the Asset Purchase Agreement, we find that, on and after the closing, Indiana-American's generally applicable rates and charges and rules and regulations for water service and private and public fire service applicable in Indiana-American's Wabash Valley Operation on file with and approved by the Commission should apply to services provided by Indiana-American through the Marion Heights System, as the same are in effect from time to time.

(c) Accounting Treatment. Indiana Code §§ 8-1-2-12 and -14 give the Commission authority over the accounting procedures utilized by public utilities in Indiana. In this Cause, it

is appropriate to allow Indiana-American to book as net original cost the purchase price plus reasonable transaction costs. We note that the purchase price was reached through arm's length negotiations and was confirmed by the appraisers. Such accounting treatment is also consistent with prior Commission orders involving Indiana-American.

We find that Indiana-American's proposed accounting and journal entries as described by Mr. Hoffman in his direct testimony and Petitioners' Exhibit MJH-7 and set forth in Finding No. 5 above, should be approved and that the costs so reflected on the books and records of Indiana-American be used as the original cost of such properties for accounting, depreciation, and rate base valuation purposes. We find that Indiana-American's existing depreciation accrual rates approved by the Commission in Cause No. 43081 on November 21, 2006 and as included in the calculation of rates with the approval of Indiana-American's rate case in Cause No. 43187 on October 10, 2007 should be applied on and after the closing date of the acquisition to depreciable property purchased from Marion Heights pursuant to the Asset Purchase Agreement.

(d) Encumbrance. The properties owned by Indiana-American are subject to the lien of Indiana-American's Indenture of Mortgage. Upon consummation of the acquisition, the properties comprising the Marion Heights System will also become subject to the lien of Indiana-American's Indenture of Mortgage.

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

1. Subject to the modification to the distribution of the proceeds as described by Ms. Ruhl on rebuttal, public convenience and necessity require the acquisition and operation of the Marion Heights System by Indiana-American on the terms and conditions described in the Asset Purchase Agreement, and Indiana-American shall be and hereby is granted an indeterminate permit to provide water service in the area currently served by the Marion Heights System effective upon consummation of the acquisition by Indiana-American of the Marion Heights System.

2. Joint Petitioners are hereby authorized to consummate the acquisition of the Marion Heights System by Indiana-American and permit the operation thereof by Indiana-American on the terms described in the Asset Purchase Agreement, including all necessary licenses, permits and franchises to provide utility service through the Marion Heights System following closing.

3. Indiana-American is hereby authorized to charge customers currently served by the Marion Heights System the current rates and charges and apply the same rules and regulations for water service and private and public fire service applicable in Indiana-American's Wabash Valley Operation on file with and approved by the Commission, as the same are in effect from time to time.

4. Indiana-American is hereby authorized to reflect the acquisition of the Marion Heights System on its books and records as of the closing by making the accounting and journal entries described in Finding No. 5(c) above.

5. The original cost of the acquired property, as described in Finding No. 5(c) above, shall be used for accounting, depreciation and rate base valuation purposes after closing.

6. Indiana-American shall be and hereby is authorized to apply its depreciation accrual rates on and after the closing date of the acquisition to depreciable property purchased from Marion Heights pursuant to the Asset Purchase Agreement.

7. Indiana-American is hereby authorized to encumber the properties comprising the Marion Heights System with the lien of Indiana-American's mortgage indenture.

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

**HARDY, ATTERHOLT, LANDIS, MAYS, AND ZIEGNER CONCUR:**

**APPROVED: MAR 10 2010**

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

  
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**Brenda A. Howe**  
**Secretary to the Commission**