

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

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PETITION OF TWIN LAKES)
UTILITIES, INC. FOR AUTHORITY TO)
INCREASE ITS WATER AND SEWER) CAUSE NO. 43957
RATES AND CHARGES AND FOR)
APPROVAL OF A NEW SCHEDULE OF) APPROVED:
RATES AND CHARGES APPLICABLE) FEB 22 2012
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ORDER OF THE COMMISSION

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

On September 30, 2010, Twin Lakes Utilities, Inc. ("Petitioner" or "Twin Lakes") filed its petition with the Indiana Utility Regulatory Commission ("Commission") for authority to increase water and sewer rates and charges, and for approval of a new schedule of rates and charges. Petitioner prefiled its testimony and exhibits constituting its case-in-chief on October 15, 2010. Pursuant to notice and as provided for in 170 IAC 1-1.1-15, a Prehearing Conference in this Cause was held on November 9, 2010 in Room 224 of the PNC Center, 101 W. Washington St., Indianapolis, Indiana. The Petitioner, the Office of the Utility Consumer Counselor ("Public" or "OUCC"), and Intervenor Lakes of the Four Seasons Property Owners' Association ("LOFS") appeared and participated at the Prehearing Conference. At the Prehearing Conference, the Presiding Officers granted LOFS' Petition to Intervene. No members of the general public appeared. The Commission issued its Prehearing Conference Order on January 5, 2011. Petitioner filed supplemental direct testimony on November 15, 2010, and March 8, 2011.

The OUCC and LOFS filed their responsive testimony and exhibits on March 9, 2011. LOFS filed supplemental testimony and exhibits on March 30, 2011. On April 13, 2011, Petitioner filed its rebuttal testimony and exhibits. Petitioner filed corrected and supplemental rebuttal testimony on June 7, 2011.

Pursuant to notice duly given and published, the presiding officers conducted a field hearing at the Jerry Ross Elementary School in Crown Point, Indiana, at 6:00 p.m. C.S.T., February 10, 2011, at which the parties and members of the public appeared. An evidentiary hearing was conducted in this Cause on June 30, 2011 in Room 222 of the PNC Center, 101 W. Washington St., Indianapolis, Indiana. At the hearing, the testimony and exhibits of the parties were admitted into the record and the respective witnesses were made available for cross-examination.

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

1. **Notice and Jurisdiction.** Notice of the filing of Twin Lakes' Petition as well as each of this Commission's hearings was given as required by law. Twin Lakes is a public utility as defined by Ind. Code § 8-1-2-1 and we have continuing jurisdiction over the rates Twin Lakes

may charge for its utility service. Accordingly, we have jurisdiction over both Twin Lakes and the subject matter of its Petition.

2. **Petitioner's Characteristics.** Petitioner owns, operates, manages and controls plant and equipment which are used and useful in the provision of water and sewer services in Lake and Porter Counties pursuant to Certificates of Territorial Authority issued by the Commission to Petitioner by the Commission's Orders in Cause Nos. 33766 and 35611 on February 18, 1975 and May 18, 1979, respectively. Petitioner is currently serving approximately 3,200 water and sewer customers within a rural area straddling the Lake and Porter County line. Most of Twin Lakes' customers are residential and located within the Lakes of the Four Seasons development. Petitioner is a wholly-owned subsidiary of Utilities, Inc., which owns corporations that own over 90 systems providing utility service to approximately 280,000 customers in 15 states.

3. **Existing Rates.** Petitioner's existing water and sewer rates and charges were approved in Cause No. 43128 on January 16, 2008. Petitioner was authorized to implement its approved sewer rates pursuant to the Commission's November 12, 2009 Order in Cause No. 43128 S1.

4. **Relief Requested.** In its Petition, Twin Lakes states that since its rates and charges were last established it has made substantial capital investments to its system and the fair value of its utility properties has materially increased. Twin Lakes further asserts that expenses and other costs have increased and, as a result, its existing rates and charges now, are, and will continue to be insufficient to provide revenues adequate to cover its necessary and reasonable operating expenses and provide the opportunity to earn the fair return to which Twin Lakes is lawfully entitled. In its case-in-chief, Petitioner requested authorization to increase its present water rates by 42% and its present sewer rates by 19%.

5. **Test Year and Rate Base Cut-off.** As provided in the Prehearing Conference Order, the test year to be used for determining Petitioner's actual and *pro forma* operating revenues, expenses and operating income under present and proposed rates is the twelve months ended June 30, 2010, adjusted for changes that are fixed, known and measurable for ratemaking purposes and that will occur within twelve months following the end of the test year. The financial data for this test year, when adjusted for changes as provided in the Prehearing Conference Order, is a proper basis for fixing new rates for Petitioner and testing the effects thereof. As further provided in the Prehearing Conference Order, the rate base cut-off should reflect used and useful property as of September 30, 2010.

6. **Evidence Presented.**

A. **Petitioner's Direct Evidence.** Dimitry Neyzelman, Regulatory Accountant for Utilities, Inc. and its subsidiaries, including Twin Lakes, testified regarding Petitioner's need for increased water and sewer rates and sponsored Petitioner's financial exhibits. Mr. Neyzelman explained that Petitioner's present rates are insufficient to cover Petitioner's operating costs and provide a reasonable rate of return on Petitioner's investment in the Twin Lakes system. He testified Petitioner is requesting rate relief so that it can continue to provide safe, reliable and efficient water and sewer utility services to its customers.

The water utility had test year operating revenues of \$892,406 and total operating expenses of \$830,964, after adjustments, for a pro forma operating income under present rates of

\$61,442 and a return on rate base of 1.90%. The sewer utility had test year operating revenues of \$1,588,618 and total operating expenses of \$1,263,967, after adjustments, for a pro forma operating income under present rates of \$324,652 and a return on rate base of 5.62%. Mr. Neyzelman stated that the proposed increase of 42% for water rates and 19% for wastewater rates should allow Twin Lakes to earn a rate of return on net original cost rate base of 8.51% for each utility.

Mr. Neyzelman testified all pro forma adjustments were made to the test year revenues and expenses based on known, fixed and measurable changes through June 30, 2011. He explained the allocation methodology used to allocate salary and wage costs from the service company to Twin Lakes and stated that an adjustment was made to salaries and wages to remove from operating expense the amount of labor that was capitalized during the test year. Mr. Neyzelman summarized the various adjustments made by Petitioner to test year operating expenses. With respect to depreciation expense, he indicated that Petitioner is proposing depreciation rates of 25% for utility vehicles and 12.5% for computer equipment and software systems to better reflect their typical useful lives.

Mr. Neyzelman explained the rate base for the water and sewer utilities reflect rate base as of June 30, 2010, with adjustments to update rate base through September 30, 2010, net of accumulated depreciation reserve, and to annualize the allocation of vehicles and computers at the end of the test year. He stated all of the utility's property included in rate base, including plant adjustments, is used and useful and is currently or will be in service no later than September 30, 2010.

Mr. Neyzelman testified that rather than incur the costs associated with retaining a return on equity ("ROE") expert, Petitioner proposed to use a cost of common equity of 10.57%. He provided a table of recent ROEs granted to eight of Twin Lakes' sister companies and indicated that the average ROE was 10.57%. Based on a capital structure consisting of 52.02% long-term debt and 47.98% common equity, Mr. Neyzelman calculated a rate of return of 8.51% based on Petitioner's recommended cost of equity of 10.57%.

Mr. Neyzelman also described proposed changes to Twin Lakes' water rate design, billing cycle, non-recurring charges and other tariff language. He said that the components of the water revenue requirement are allocated between fixed and variable charges. He explained Petitioner is proposing to use the customer's meter size to establish the base facilities charge, which will result in a simpler, more accurate and less controversial method for determining the base facilities charge for each customer. Mr. Neyzelman testified Petitioner is proposing a monthly billing cycle to improve customer service and allow for more prompt detection of system and billing problems. He stated Petitioner is proposing to change its non-sufficient funds charge and to include a new after hours call out charge. Finally, he explained that Petitioner is proposing various clarifying changes to its tariff language.

Bruce T. Haas, Regional Director of Operations for the Midwest Region of Utilities, Inc., testified regarding Petitioner's water and wastewater operations. Mr. Haas explained that Petitioner provides water and wastewater utility services in Lake and Porter Counties to approximately 3,200 customers. He indicated the Twin Lakes water distribution system contains approximately 174,240 linear feet of water mains. According to Mr. Haas, Petitioner does not provide fire protection, but has flushing hydrants located throughout the system for seasonal flushing purposes. He said the wastewater collection system is comprised of fourteen lift stations and includes over 174,000 linear feet of gravity and pressure sewer mains. The sanitary sewage

is treated at the 1.1 MGD Wastewater Treatment Plant, which is a Class III extended aeration wastewater facility.

Mr. Haas provided a summary of the capital improvements made by Petitioner since its last rate case, which include the following:

1. Replacement North Aeration Filter at Water Plant #1 at a cost of \$386,559.
2. Rehabilitation of Well #9 at a cost of \$107,735.
3. Engineering to replace outdated Master Control Center at Water Plant #1 at a cost of \$15,871.
4. Locate water source for Water Treatment Plant #3 at a cost of \$15,917.
5. Repairs to Well #4 at a cost of \$9,905.
6. Rehabilitation of Mixer/Aerator Unit used in the sludge storage tank at a cost of \$29,459.
7. Replacement of 270' of sewer main on East Lake Shore Drive at a cost of \$79,102.
8. Installation of quick lock connections at Lift Stations C and H at a cost of \$10,206.
9. Landscaping for sewer main project at a cost of \$45,233.
10. Engineering survey of Lift Stations B and D at a cost of \$17,760.
11. Replacement of three gate valves at the Wastewater Treatment Plant at a cost of \$9,876.
12. Conducted jetting and televising of approximately 36,000 linear feet of the sanitary sewer gravity mains and made repairs related to the findings at a cost of \$53,365.
13. Installation of sanitary sewer main tap at 3956 S. Lakeshore Drive at a cost of \$9,150.
14. Removal of debris and grit from two aeration basins at Wastewater Treatment Plant at a cost of \$22,092.
15. Replacement of electrical control panel and switch at Lift Station G at a cost of \$20,923.
16. Engineering and plant additions related to Manhole 307 at a cost of \$189,286.
17. Conducted master plan study for future capital upgrades of the water and wastewater systems at a cost of \$177,367.

Mr. Haas testified regarding Petitioner's water and service quality. He said Petitioner is in compliance with all applicable water quality regulations and standards and that most of the intermittent instances of discolored water during the past twelve months occurred after a flushing or main break situation. With respect to the sewer collection system, Mr. Haas explained that Petitioner continues to receive significant amounts of inflow and infiltration ("I&I") because the sewer system is mainly comprised of transite pipe that is prone to failure with age. Mr. Haas stated the majority of this excess water is believed to be the result of inflow vs. infiltration and a good portion of this is believed to be coming from improper sump pump and roof drain connections. He explained Petitioner is currently planning an investigation that will include smoke testing of the sewer mains and laterals along with personnel visits to individual premises where improper connections are believed to exist.

Mr. Haas stated that in the Commission's November 12, 2009 Order in Cause No. 43128 S1 ("Subdocket Order") the Commission directed Petitioner to undertake a number of actions to

address the I&I issues, including (a) development of a strategic process to handle ongoing problems and a planned maintenance program; (b) flow monitoring of Petitioner's entire system; (c) submission of a design summary for the replacement of Lift Station B with a submersible station; (d) filing of a ten year televised line inspection and capital improvement program; and (e) continued work on improving the frequency, clarity and transparency of Petitioner's communications with LOFS. He summarized the incremental maintenance costs associated with complying with the requirements of the Subdocket Order. Mr. Haas also testified that Petitioner has complied with the terms of the Settlement Agreement approved in Cause No. 43128, Petitioner's last rate case.

Finally, Mr. Haas testified briefly regarding the nature of the customer complaints received within the last twelve months. He stated the majority of the complaints within the past twelve months have been related to billing issues. He explained that Petitioner updated its billing system in the past two years and more recently discovered a number of accounts which had been underbilled due to broken or slow running meters or meters without outdoor reading devices. He said that these issues are being resolved on a case-by-case basis and that proper bills are being sent to customers.

B. OUCC's Evidence. Richard Corey, Utility Analyst for the OUCC, presented the OUCC's adjustments to Petitioner's test year expenses, the general revenue requirements and their adjustments to Petitioner's rate base. Mr. Corey recommended a 23.86% increase to Petitioner's water rates and a 5.4% increase to Petitioner's wastewater rates.

Mr. Corey recommended a rate base of \$3,118,578 for water and \$5,556,114 for the sewer utility. This included the additional amount of accumulated depreciation from June 30, 2010 through September 30, 2010. The difference also includes an update to the balance of customer deposits and the elimination of master plan costs that had been included in rate base by Petitioner. Finally, Mr. Corey calculated a different level of working capital.

The OUCC accepted Petitioner's adjustments to property tax and amortization of contributions-in-aid-of-construction ("CIAC"). However, the OUCC rejected or modified the remainder of Petitioner's expense adjustments. With respect to salary and wage expense, Mr. Corey made an adjustment to reflect the filling of a vacant position at a rate of compensation \$9,200 less than projected in Petitioner's *pro forma* wage adjustment, along with a corresponding adjustment to payroll taxes. He also made an adjustment to Petitioner's benefits expense to reflect updated information regarding the current cost of health insurance and pensions and other benefits. Mr. Corey explained that an adjustment to capitalized labor is necessary to reflect a 3% merit raise awarded to Petitioner's employees effective April 2011.

Mr. Corey recommended that Petitioner's rate case legal expense be lowered from Petitioner's estimate of \$85,000 to \$30,000, stating that to date Petitioner had incurred \$24,250 in legal costs related to the rate case. Mr. Corey further removed expenses associated with water service personnel's work on the rate case, which totaled \$62,851. He stated these individual's wage expense has already been allocated to Petitioner through its wage adjustment and thus this additional adjustment is necessary to prevent a double recovery of labor costs. Finally, Mr. Corey amortized rate case expense over a four year period rather than the three years proposed by Petitioner, noting that Petitioner's last three rate cases had test years ending June 30, 2006, December 31, 2002 and June 30, 1992.

Rather than include master plan costs in rate base, Mr. Corey recommended that such costs be amortized over a ten year period. This resulted in a reduction to rate base and an increase in operating expenses.

Mr. Corey stated that the OUCC accepted Petitioner's proposal to switch to a monthly billing cycle, but added that such a change should cause an increase in billing costs. He stated that if Petitioner requested such additional costs in its rebuttal it should be able to provide adequate support.

Mr. Corey did not accept Petitioner's proposed bad debt expense adjustment, opining that Petitioner's proposed uncollectible expense percentages of 1.79% and 1.76% for water and sewer respectively are significantly higher than historical bad debt expense experienced by Petitioner. He stated that there are two methods to account for bad debt, the direct write off method and the allowance method. He said the allowance method is considered to be within generally accepted accounting principles ("GAAP"), while the direct write off method is considered to be non-GAAP. Mr. Corey stated it appears in the present case that Petitioner is in the process of changing from a direct write off to an allowance method as it has recorded a reserve for uncollectible accounts for the first time in 2009. He stated that the utility may use either method to calculate its bad debt percentage, but not a combination of the two. He opined that the appropriate calculation of bad debt expense in this case should be based on the average historical bad debt rate experienced by Petitioner during the period 2003 through 2009 as reported by Petitioner in its annual reports filed with the Commission. Based on this information, Mr. Corey recommended a bad debt percentage of 0.973% and 0.538% for water and wastewater, respectively.

Mr. Corey also took exception to Petitioner's consumer price index ("CPI") expense adjustments. He stated that Petitioner increased all test year operating and maintenance ("O&M") expenses except labor and benefits by 6.66% based on increases in the CPI from July 2006 to July 2010. Mr. Corey opined that this adjustment represents the effect of inflation over a four year period, not just the twelve months subsequent to the end of the test year. He explained that a CPI-based adjustment is not reasonable because it is not a fixed, known and measurable adjustment. Mr. Corey stated that even if one were to use a CPI as a proxy for actual price changes, a utility should not project test year costs four years into the future as Petitioner has done in this case.

Mr. Corey disagreed with Petitioner's proposal to use a different depreciation rate for vehicles and computers. He testified that absent a depreciation study a utility should depreciate all property at the 2% composite rate for water property and 2.5% composite rate for wastewater property. He recommended that Petitioner use the composite rate for all depreciable assets until Petitioner obtains approval from the Commission to use anything other than a composite rate.

Mr. Corey made a number of adjustments to Petitioner's other operating expenses, including Utility Receipts Tax, IURC Fee, and State and Federal Income Tax. He also proposed a slightly lower gross revenue conversion factor as a result of these adjustments.

Margaret Stull, Utility Analyst for the OUCC, testified regarding additional adjustments to Petitioner's test year operating revenues and expenses. She also discussed rate design for both the water and sewer utilities and proposed rates representative of the OUCC's proposed revenue requirements. Finally, Ms. Stull testified regarding Petitioner's request to change certain non-recurring charges included on its tariff.

Ms. Stull accepted Petitioner's proposed billing determinant revenue adjustment and made two additional normalization adjustments to water and wastewater revenues. First, she normalized customer growth that occurred on Petitioner's system during the test year by annualizing the number of bills that would accrue if each customer (as of 6/30/10) had been a customer of Petitioner's system for the entire test year and multiplying the additional bills by the average bill to yield an increase in test year revenues. Ms. Stull's second adjustment was calculated in the same manner, but was based on the growth in customers between the end of the test year and December 31, 2010. Ms. Stull also made an additional revenue adjustment to reflect monthly rental revenues associated with a cell tower lease agreement with T-Mobile.

Ms. Stull also proposed several adjustments to Petitioner's operating expenses. With respect to test year water maintenance expense, Ms. Stull proposed to calculate certain periodic maintenance expenses over a five year period, rather than on an annual basis. With respect to wastewater maintenance expense, she accepted Petitioner's proposed recurring maintenance expense adjustment with some modifications to reflect updated actual costs to perform the various inspections and activities. She also proposed to eliminate \$2,500 in prior year costs related to a payment made by Petitioner to LOFS to restock the lake with fish per a prior Commission order.

Ms. Stull made two adjustments to Petitioner's test year legal fee expense. First, she removed \$20,447 of charges related to an Illinois environmental matter that Petitioner acknowledged was recorded to Petitioner's books and records in error. Second, she eliminated test year expenses of \$35,513 related to a lawsuit brought by a developer to recover a non-refundable deposit paid to Petitioner in a previous period. Ms. Stull stated that these are not normal, recurring legal fees that will be incurred in the future by Petitioner and that they relate to a transaction that occurred prior to the test year.

Ms. Stull accepted Petitioner's methodology to normalize test year transportation expense but did not accept Petitioner's use of a CPI-based adjustment to transportation expense. She also made an adjustment to office utilities expense to account for a prior period adjustment.

Ms. Stull testified regarding Petitioner's proposed water and wastewater rate design. She agreed with Petitioner's proposal to bill its customers on a monthly basis rather than its current bi-monthly practice. She also agreed with Petitioner's proposal to recover more of its water revenue requirements from its fixed monthly charge than it currently does under its present tariff. With respect to Petitioner's wastewater rate design, Ms. Stull noted that Petitioner did not propose to incorporate a volumetric rate structure for its sewer utility at this time. She prepared a volumetric rate design study for the sewer utility and discussed the impact to customers if a volumetric rate design were to be implemented. Ms. Stull did not propose that Petitioner adopt a volumetric rate design.

Ms. Stull accepted Petitioner's proposal to increase its NSF charge from \$10 to \$25, but did not accept the inclusion of an After Hours Call-Out Charge to Petitioner's tariff. She opined that given Petitioner's historical service quality issues, the ability of Petitioner to charge this fee "for any reason" makes the fee undesirable. She also recommended Petitioner review its current connection charge of \$716 to verify that it is still representative of its costs to provide this service to customers.

Roger Pettijohn, Senior Utility Analyst for the OUCC, testified regarding Petitioner's facilities, its capital and operational plans and its progress with regard to previous commitments

to system challenges identified in previous Commission cases. He also discussed customer comments and complaints received at the Commission's public field hearing on February 10, 2011.

Mr. Pettijohn noted that evidence received at the public field hearing indicates that water quality is an issue for Petitioner's customers. He discussed water quality with Petitioner's employees during his tour of Petitioner's facilities. He testified that based on his investigation he believed the finished water pumped from the treatment plants is clear as a result of filtration and has very low or trace iron concentration from iron removal treatment facilities. He explained that typically iron problems stem from iron coming out of solution or sloughing off mains. Mr. Pettijohn said Petitioner, like other water utilities, schedules main flushing twice a year to control and minimize encrustation build-up and thereby prevent sloughing, but despite these efforts, particulate can still appear at the customer's tap. He indicated that in Petitioner's case there should be no iron problem as the finished water is very low in iron and pipe encrustation is minimal. Consequently, he believed that costly quality control measures to remove iron and prevent encrustation would appear to be of little benefit. He instead recommended that Petitioner work with affected customers to resolve water quality issues.

Mr. Pettijohn stated that some complaints at the field hearing were related to hard water problems and the make-up of hard water. He explained that Indiana well water is naturally and consistently hard because it dissolves many different types of minerals as it percolates through the soil. He indicated that Petitioner's well water is typical of Indiana well water in general and not necessarily inferior to other sources of supply in the way of rivers or lakes. He recommended that customers desiring soft water install a water softener in their home.

Mr. Pettijohn testified that another issue raised at the field hearing was odors emanating from the Wastewater Treatment Plant. He stated that the situation resulted from sewage going septic before its arrival at the headworks of the treatment plant. According to Mr. Pettijohn, Petitioner has enclosed the headworks and employed an activated carbon air filtration system to eliminate the odor problem.

With respect to Petitioner's seventeen capital improvement projects, Mr. Pettijohn testified that none of them appeared to be excessive, out of the ordinary or other than reasonable maintenance and repair practice. He stated that Petitioner's progress toward mitigating I&I will be deliberate based upon the scope of a ten year timeframe and a collection system in generally poor condition. He said that Petitioner has committed to cleaning and televising 10% of its collection system pursuant to the Subdocket Order but only cleaned 16,714 feet in 2009 and 11,009 feet in 2010. He recommended that Petitioner televise and earmark those areas known to be of high priority, such as areas with overflowing manholes. He recommended that Petitioner submit detailed semi-annual progress reports to the Commission including an explanation and detail of I&I projects completed with costs.

Mr. Pettijohn stated that Petitioner has satisfactorily completed the flow monitoring requirements from the Subdocket Order, but did not timely submit its customer complaint incidences for 2008 and 2009. He testified that Petitioner has made significant investment in its system, with expenditures on plant of approximately \$3.2 million with regard to sewer force main and approximately \$2.6 million on gravity sewer work. He recommended the Commission find Petitioner's capital projects to be used and useful. He further recommended that the Commission require semi-annual reporting on I&I remediation and other capital projects, along with water quality reports with call-out work sheets. He suggested that Petitioner inform the

Commission as to its long-term plans for treating waste odors with copies to the other parties to this Cause.

Mr. Edward Kaufman, Senior Analyst, responded to Mr. Neyzelman's proposed cost of equity. He testified that his analysis supported a range of cost of equity of 9.40% to 10.37% for Petitioner at this time. However, he noted the parties reached an agreement that Petitioner should be authorized a cost of equity of 10.20%. Mr. Kaufman agreed with Petitioner's decision to avoid the cost of paying for a cost of equity witness, but opined that Petitioner's originally proposed cost of equity is somewhat high. He also raised concerns regarding the direct application of cost of equity determinations from other states without demonstrating that each utility is reasonably comparable to Petitioner.

Mr. Kaufman stated that he accepted Petitioner's proposal to avoid the expense of a full cost of equity analysis and did not complete one himself. He relied upon the analysis provided by Petitioner and recent OUCC cost of equity estimates provided to the Commission. He explained that the OUCC recommended a cost of equity of 9.2% and 9.25% in recent rate cases involving Utility Center, Inc. and Indiana American Water Company, respectively. He said that both utilities are larger than Petitioner, and all other factors being held constant would merit a somewhat higher cost of equity. He discussed the company specific risk adjustment estimated in the Utility Center case and in Petitioner's last rate case and determined that adding the difference between these two adjustments to the estimated cost of equity in the Utility Center case would result in an estimated cost of equity of 9.40%.

Based on his analysis, Mr. Kaufman believed a range of 9.40% to 10.37% is reasonable for Petitioner at this time. However, he recommended that the Commission accept the agreement between Petitioner and the OUCC to authorize a cost of equity of 10.20%.

C. LOFS' Evidence. Rick Cleveland, Community Manager of LOFS, testified regarding the community's perspective on Petitioner's requested rate relief. He testified that there are four major areas of concern: (1) sewer discharges onto LOFS property and into customers' homes; (2) the quality of water Petitioner provides to its customers; (3) inoperable and neglected fire hydrants; and (4) poor and often unresponsive customer service. He recommended that the Commission order Petitioner to meet certain service quality standards and implement remedies to the problems identified by LOFS as a condition of the rate relief sought by Petitioner.

Mr. Cleveland stated that the first area of concern is Petitioner's persistent sewer discharges into homes and onto LOFS property. He testified that sewer backups during rain events have been an issue since at least 1991. He described the history of prior rate cases involving Petitioner and the agreement by Petitioner to spend at least \$500,000 between 2003 and 2007 on a program designed to diagnose and remediate sewer discharges. He indicated that in Petitioner's most recent rate case, Cause No. 43128, the issue of sewer backups was again raised by Petitioner's customers. He stated that according to Petitioner's responses in discovery, there were twenty-seven reported incidents involving sewer backups into homes or outdoor overflows from 2008 to November 5, 2010. He opined that Petitioner is not properly maintaining its system and that any preventative maintenance or replacement it might be undertaking is inadequate.

Mr. Cleveland testified that LOFS residents have also experienced poor water quality from Petitioner. He stated that many customers testified at the field hearing regarding discolored

water. He also stated his concern that Petitioner is not properly maintaining and replacing its aging system, as evidenced by the five different water leaks and/or water main breaks experienced during 2010 alone.

Mr. Cleveland also expressed concern regarding the condition of Petitioner's hydrants. He presented an affidavit from Mr. Brad Zupan, a member of the LOFS Fire Department, regarding the inoperable or damaged condition of twenty-two hydrants in the community. He recommended that the Commission require Petitioner to implement measures to restore all the hydrants to proper working order, to ameliorate the discolored water experienced by customers and to make improvements to eliminate wear and tear on customers' appliances.

Mr. Cleveland testified regarding Petitioner's customer service quality. He stated that he has made a number of phone calls on behalf of residents over the past three years who cannot get a response or resolution to their service quality problem from Petitioner. He testified that residents have told him they have waited several days after an initial customer inquiry before a technician is sent out for an evaluation or repair. He also testified that customers have indicated that Petitioner's customer service number may go unanswered for up to thirty minutes at a time. He stated that Petitioner should be responsive to all customers' requests without his intervention on their behalf.

Mr. Cleveland stated that ultimately LOFS wants the sewer backups and overflows to stop, the hydrants to be in good working order and the water to be fit for ordinary household use and consumption. He recommended that, at a minimum, Petitioner be required as a condition of receiving any rate increase to address these issues. He further recommended that the Commission place upon Petitioner a set of requirements for responding to customer calls in a timely and productive manner. More specifically, he believed it is reasonable that all customer calls be answered by a person within two minutes. If a call is answered by a machine or integrated voice response system, the customer ought to receive a return call within two hours from a representative of Petitioner. He encouraged the Commission to impose a remedy that will produce a solution to the decades-old sewer discharge problems, rather than a remedy that requires more investment but fails to cure the problem.

Anthony Kenning, a professional engineer with DLZ Indiana, LLC, also testified on behalf of LOFS. He testified that in his opinion, Petitioner's system does not appear to be adequately maintained. He based this opinion on several factors, including (1) there are numerous discolored water complaints scattered throughout the system; (2) sewage overflows occur at manholes; (3) basement backups occur; and (4) hydrants were inoperable or could not be opened upon inspection by LOFS. Mr. Kenning opined that Petitioner does not have an adequate preventative maintenance regime in place to prevent additional service disruptions.

Mr. Kenning conceded that he did not perform an engineering analysis of Petitioner's wastewater collection system, but offered the following recommendations: (1) upgrade Lift Station B; (2) timely implementation of Petitioner's sump pump inspection program and timely disconnection of sump pumps found to be connected to the sanitary sewer; (3) increased frequency of video inspection of Petitioner's gravity sewers; (4) implementation of a root treatment removal program in areas known to experience root issues; and (5) continued flow monitoring to allow for continued isolation of I&I issues in the system.

With respect to the cause of discolored water complaints, Mr. Kenning stated that water discoloration may be attributed to one of several factors. However, he indicated it was unclear

that Petitioner has determined what the actual cause is. He suggested that Petitioner develop a more regimented water main flushing program and that Petitioner consider whether more frequent flushing is necessary. He also suggested that Petitioner consider performing a unidirectional flushing program. Mr. Kenning opined that public education and notification may also be required so that customers have a better understanding of what flushing may do, what flushing may cause in their water, why flushing is required, and when flushing is to occur. He also recommended a detailed review of the condition of the filter systems at the water treatment plant to further evaluate whether there is a problem that may not be identified during testing.

LOFS also filed supplemental testimony from Mr. Cleveland and Mr. Kenning along with testimony from Kevin Misch, owner of Kevin Misch Excavating, regarding the condition of Lift Station E. Mr. Misch testified that on March 21, 2011, he received a call from Petitioner requesting that he jet out a plugged sewer line at Lift Station E. He stated that while at the lift station he observed that the steel on the inside of the lift station appeared to be rotted away in several places. Mr. Misch passed the information on to Petitioner's personnel. Mr. Misch testified that he had provided a quote to Petitioner five years ago to remedy Lift Station E.

In his supplemental testimony, Mr. Cleveland further addressed the condition of Lift Station E. He expressed concern that the sides of the lift station have rotted away such that raw sewage can leach through the ground and potentially flow into the lakes. He was also concerned that the lift station could collapse or fail at any time, which could affect at least twenty-nine homes and have a catastrophic impact on the lakes and wildlife. He worried that if the lift station collapsed while a resident walked or drove by the area the resident could be seriously injured or killed. Mr. Cleveland testified that it appears Petitioner has known for at least five years that Lift Station E needed repairs but has consciously chosen to neglect its responsibility to maintain that part of its system.

Mr. Kenning's supplemental testimony commented further on the condition of Lift Station E. He stated that there are two possible dangers that could result from the lift station conditions described by Mr. Misch. First, he explained that when steel in the sides of a lift station rots to the point that one can observe dirt through the hole it is reasonable to assume that some of the sewage that flows into the lift station will escape through the holes and into the soil. Second, he said a collapse of a lift station can occur where there is deterioration at the base of the long narrow shaft that meets the larger, wider vault at the bottom. He said that based on the conditions of Lift Station E as described by Mr. Misch, a collapse of the lift station is possible. He added that when a lift station collapses, the pumps cease to operate properly, soil and sediment fill the upstream sewer lines and sewage backups will occur. He indicated the collapse would also create sinkholes and voids that may not be visible to people or pets and the risk of someone becoming injured increases. He recommended that the lift station be completely replaced.

D. Petitioner's Rebuttal Evidence. In rebuttal, Mr. Neyzelman responded to the issues raised by Mr. Corey and Ms. Stull. He testified that he agreed with Ms. Stull's customer growth adjustment methodology for purposes of this case, but proposed to adjust revenues based on Petitioner's customer count as of February 28, 2011. In addition, Mr. Neyzelman applied his adjustment to all meter sizes.

With respect to the OUCC's adjustments to outside legal fees, Mr. Neyzelman agreed that the legal expenses erroneously booked to Petitioner should be eliminated. He disagreed, however, with the removal of prudently incurred legal fees incurred during the test year that relate to the operation of the utility. He explained the nature of the test year legal expenses and

cited prior Commission orders finding that an ongoing level of legal expense is appropriate to include in operating expense.

Mr. Neyzelman disagreed with the OUCC's proposed adjustment to depreciate vehicles and computers over fifty years, using the composite rate. He stated it was unreasonable to believe that these assets can last fifty years. He explained that the OUCC's proposal does not match the assets' depreciation expense with their useful lives and thus violates the matching principle of depreciation accounting. Mr. Neyzelman cited other jurisdictions in which Petitioner's sister companies are required to use a much shorter useful life for computers.

He also disagreed with Mr. Corey's proposal to remove master plan costs from rate base and amortize the costs over ten years. Mr. Neyzelman stated that these costs are properly included in Petitioner's rate base as they relate to the planning of future capital projects by Petitioner and do not address maintenance and other remediation needs.

Mr. Neyzelman updated rate case expense to current costs incurred as of the filing of rebuttal, along with estimated rate case expense up to the evidentiary hearing. He stated that for the time through the end of March, the total amount billed is approximately \$35,000. He said that this does not include the completion of rebuttal testimony or preparation for and participation in the final evidentiary hearing. At the evidentiary hearing, he updated the rate case legal expense number through mid-June to \$58,516, which still did not include hearing preparation, hearing and post-hearing. He maintained that the original estimate of \$85,000 is reasonable and should be close to the actual rate case expense incurred by Petitioner.

Mr. Neyzelman disagreed with the OUCC's proposal to remove all capitalized time related to rate case expense. He explained that all salary and wage costs are allocated to Petitioner either through a direct allocation or the use of allocation factors. He said that none of the test year amounts for labor expense which was allocated to Petitioner include any internal labor for work on the rate case. He described in detail the method by which Petitioner maintains capitalized rate case time separate from general labor expense and stated that the OUCC's proposal would deny recovery of prudently incurred capitalized time spent preparing and supporting the rate case.

Mr. Neyzelman disagreed with the OUCC's use of a four year amortization period for rate case expense. He also proposed an adjustment to operating expense to reflect Petitioner's request to switch from a bi-monthly to a monthly billing cycle.

Mr. Neyzelman disagreed with Ms. Stull's recommendation to deny the After Hours Call-Out charge. He also explained that the other changes to the tariff language were designed to clarify the nature of these charges and the circumstances in which they would be applicable. He agreed with the OUCC's recommendation that Petitioner review its current connection and reconnection charges.

Mr. Haas responded to the testimony filed by the OUCC and LOFS. He testified that Petitioner is cleaning and televising ten percent of its sewer collection system each year for the next ten years, consistent with the Subdocket Order. He explained that Petitioner implemented, in the second quarter of 2011, a more aggressive hydrant inspection and unidirectional flushing program.

Mr. Haas testified that the efforts made by Petitioner in the past several years have resulted in improvements in water and wastewater service. He said that sanitary overflows have been reduced considerably, and all of the overflow instances during the test year were caused by blockages in the collection system, which were cleared at the time of the investigations. He emphasized that the quality of the water from the water treatment plant is of good quality and meets all drinking water standards.

Mr. Haas stated he believed Petitioner is properly maintaining its system. That being said, Mr. Haas indicated Petitioner continually reviews its maintenance procedures to ensure that it continues to improve system performance. He described Petitioner's plans regarding video inspection and flow monitoring. He agreed with Mr. Pettijohn that a proactive I&I program is necessary to minimize wastewater overflows and stated Petitioner is concentrating its televising activities in areas known to be high priority. He disagreed with Mr. Cleveland's proposal to condition rate relief on the achievement of some future unspecified service goal. He explained that such an approach would hamper Petitioner's efforts to invest in its system and improve the quality of service it provides.

Mr. Haas next testified regarding the issue of discolored water. He explained that the raw water from the ground wells contains high iron content which is effectively removed during the treatment process. He recognized that residuals of mineral/iron deposits may remain in sections of Petitioner's distribution system but anticipated that the new flushing program would resolve many if not all of these issues. Mr. Haas described the substantial efforts made by Petitioner to address individual customer complaints regarding water quality.

Mr. Haas agreed with Mr. Kenning that additional customer education and notification regarding water flushing would be beneficial. He discussed the additional steps taken by Petitioner to notify its customers regarding its recent flushing activities.

Mr. Haas also responded to Mr. Cleveland's testimony regarding the condition of Petitioner's hydrants. He clarified that these hydrants are "flushing" hydrants, not "fire" hydrants, and are not designed to guarantee fire protection. He explained Petitioner does not object to the LOFS Fire Department using these hydrants in an emergency but wanted to eliminate any misunderstanding by the fire department that these flushing hydrants will provide adequate fire protection service. He discussed Mr. Zupan's affidavit, and indicated that based upon Petitioner's review of the hydrants, Petitioner found that of the 22 flushing hydrants claimed to be inoperable or damaged, only three hydrants were actually inoperable. He said those hydrants were immediately repaired or replaced. He emphasized Petitioner's desire that the LOFS Fire Department and Petitioner's customers work more closely with Petitioner in the future regarding these issues.

Mr. Haas described all of the investments made by Petitioner over the course of the past several years to systematically improve water quality and reduce water quality complaints. He indicated that Petitioner has previously addressed water quality issues by starting with the water supply and treatment facilities. Having remedied any issues with those facilities, Petitioner had shifted its focus towards possible improvements to the distribution system, including the implementation of a new flushing routine and improved customer communication and education. This also included the numerous Voice Reach messages sent out to customers, as well as, articles which have appeared in the LOFS Newsletter. He reiterated Petitioner's commitment to work with affected customers to determine and resolve the cause of water quality issues.

Mr. Haas responded to Mr. Cleveland's testimony regarding the condition of Petitioner's wastewater system. He reported that Petitioner has made strides to improve I&I and is committed to taking a proactive approach moving forward. He stated that, with the exception of overflows caused by Hurricane Ike in 2008, Petitioner has had relatively few overflow incidents in the past several years. He indicated that almost all overflows that occur now are determined to be caused by root or grease blockages, and that Petitioner responds immediately in the limited situations where the blockage causes a backup.

With respect to the comments made regarding odors emanating from the wastewater treatment plant, Mr. Haas indicated that the steps taken by Petitioner have eliminated the odor problems and that no odor complaints have been received since Petitioner completed its additional modifications to the headworks. He provided copies of monitoring results demonstrating that hydrogen sulfide levels have been reported as "0" from the headworks.

Mr. Haas testified that Petitioner reports to the Commission with its televised line inspection information and its plan for the upcoming year. He stated that Petitioner does not object to the ongoing reporting requirements suggested by Mr. Pettijohn. He added that Petitioner would also include in this report its status of odor remediation and what steps it has taken to eliminate odors at the headworks of the wastewater treatment plant.

Mr. Haas also testified regarding the condition of Lift Station E. He generally agreed with Mr. Kenning that upgrades to Lift Station E would be appropriate. He testified that Petitioner is working with its engineer to develop plans for submittal to IDEM to abandon the dry-pit area of the lift station. With respect to the concerns raised by Mr. Cleveland's supplemental testimony, Mr. Haas noted that Petitioner is unaware of any instance of water leaching out of the holes in the ceiling of the lift station. While he agreed that there is a potential for concern in the immediate area around Lift Station E, Mr. Haas opined that if Lift Station E were to collapse, it would not cause a major sinkhole in the earth.

Mr. Haas concluded his rebuttal testimony by stating that Petitioner is a small utility that must balance its capital investments and maintenance expenditures with the resulting impact on customer rates. He noted that a majority of the system was placed in service in the mid 1960s and, like anything else, it has aged. He testified that Petitioner could replace many of its assets all at once, but this would result in rates that would be astronomical and unacceptable. He stated Petitioner has made improvements to the system but this will not be an overnight result and will necessarily take some time.

In his supplemental testimony, Mr. Haas stated that Petitioner has televised and cleaned nearly 25,000 feet of its sewer collection system from July 1, 2010 through June 30, 2011. He stated that Petitioner intends to continue past this amount so that Petitioner will televise ten percent of its system both on a calendar year and reporting year basis in the future.

Mr. Haas also provided an update regarding the unidirectional flushing program. He said that since the more aggressive flushing protocol, Petitioner has received minimal water quality complaints, which were quickly resolved. He stated Petitioner is very confident that this flushing program has left the water distribution system clean and free from sediment. He discussed the various communications made by Petitioner to its customers regarding the flushing process.

Mr. Haas also updated his rebuttal testimony regarding Lift Station E. He stated that Petitioner has inspected all of its remaining lift stations and will fill five other lift stations with

sand to eliminate any risk of collapse. With respect to Lift Station E, he said that Petitioner has submitted plans to IDEM for review and approval of modifications.

Ms. Karen Sasic, Director of Customer Care for Utilities, Inc. explained that Petitioner is committed to providing exceptional service to all customers. She explained that the Company has established Key Performance Indicators (“KPIs”) for Operations and Customer Service in order to objectively measure performance. Focus is put on all areas to meet or exceed target metrics such as call handling, field activity response times and compliance. Ms. Sasic expressed disappointment with respect to Mr. Cleveland’s assertion that Petitioner’s personnel have been unresponsive or condescending and encouraged any customer who feels their complaint has not been adequately addressed to escalate their concerns to Petitioner’s Area Manager, Mr. Charles Alexander, or Petitioner’s Regional Manager, Mr. Tom Tapella. Ms. Sasic explained how customer service personnel are trained to handle calls of a technical nature, which are referred to Operations personnel who are knowledgeable and experienced in field issues.

Ms. Sasic disagreed with Mr. Cleveland’s assertion that often several days pass between the time of a customer inquiry and a response from Petitioner and explained Utilities Inc.’s internal customer complaint procedure which outlines standard response times to emergency and non-emergency calls. Petitioner’s customer calls go to one of Utilities, Inc.’s three customer service centers where it is immediately answered by the Company’s Automated Call Distribution System (“ACD”) then routed based on the menu selection by the customer.

Ms. Sasic does not agree that the Commission should impose a set of requirements regarding Petitioner’s customer service. In 2010, Utilities, Inc. made changes to consolidate its customer service operations to align processes and established KPIs for customer service operations to measure performance and bring more accountability to the process.

7. Commission Discussion and Findings.

A. Petitioner’s Rate Base. In its case-in-chief, Petitioner proposed an original cost rate base of \$3,226,719 for its water service and \$5,781,125 for its wastewater service. In rebuttal, Petitioner proposed an original cost rate base for its water plant of \$3,184,145, and an original cost rate base for its wastewater plant of \$5,673,709. The primary difference between Petitioner’s proposed rate base and that calculated by the OUCC relates to the treatment of Petitioner’s master plan costs.

Since its last rate case, Petitioner developed a master plan for its water and sewer utilities at a total cost of \$177,367, which Petitioner included in its rate base. The master plan consists of an engineering study to identify necessary capital projects for Petitioner’s water and sewer utilities. OUCC witness Mr. Corey testified that the master plan should not be capitalized as it is not a “component of construction,” citing the Commission’s April 30, 2010 Order in Cause No. 43680 involving Indiana-American Water Company (“Indiana-American”). Mr. Corey proposed instead to amortize the costs associated with the master plan over a ten year period, resulting in a decrease in rate base of \$177,367 and an increase in operating expense of \$17,737. In rebuttal, Mr. Neyzelman reiterated the costs are properly included in Twin Lakes’ rate base as they relate to the planning of future capital projects by Twin Lakes.

In its Order in Cause No. 43680, the Commission found that Indiana-American’s comprehensive planning studies “contain maintenance functions to ensure reliable operations,” and as such, are not components of construction that can be capitalized. *Re Indiana-American* at

115. While Mr. Neyzelman testified the master plan does not address maintenance and other remediation needs, we focus on the language of NARUC’s Uniform System of Accounts, Instruction 19, which describes “Engineering Services” as:

Amounts paid to other companies, firms or individuals engaged by the utility to plan, design, prepare estimates, supervise, inspect, or give general advice and assistance in connection with construction work.

We do not believe that master planning studies, or facility plans in this instance unrelated to construction work qualify as a capital cost under Instruction 19. While these documents provide some basic engineering information such as component sizing and gross level cost estimates, the final information needed for construction is ultimately included in the final design plans and construction documents. Accordingly, those costs should not be included in rate base at this time.

Considering our specific findings regarding pro forma operating expenses discussed below, the proper working capital allowances for Petitioner’s water and sewage disposal utilities should be \$54,774 for Petitioner’s water utility and \$67,389 for its wastewater utility.

Based on the above discussion, Petitioner’s rate base is shown in the following table:

<u>Description</u>	<u>Water</u>	<u>Sewer</u>
Utility Plant in Service as of 6/30/10	\$ 7,054,689	\$ 13,654,441
UPIS items added 7/1/10 – 9/30/10	88,154	71,661
Less: Adjustment of vehicles allocated	115,475	114,212
Adjustment of computers allocated	14,746	14,585
Master Plan Costs	<u>60,305</u>	<u>117,062</u>
Total Utility Plant in Service	<u>6,952,317</u>	<u>13,480,243</u>
Accumulated Depreciation as of 6/30/10	1,379,788	3,833,455
Add: G/L Additions 7/1/10 – 9/30/10	23,808	82,040
Less: Adjustment of vehicles allocated	92,190	91,181
Adjustment of computers allocated	16,643	16,461
Remove Master Plan Costs	<u>2,638</u>	<u>5,121</u>
Accumulated Depreciation as of 9/30/10	<u>1,292,125</u>	<u>3,802,732</u>
Net Utility Plant in Service	<u>5,660,192</u>	<u>9,677,511</u>
Less: Contributions in Aid of Construction	2,073,891	3,743,899
Deferred Income Taxes	507,309	432,023
Customer Deposits	8,839	8,743
Add: Working Capital	<u>54,774</u>	<u>67,389</u>
Total Original Cost Rate Base	<u>\$ 3,124,927</u>	<u>\$ 5,560,235</u>

B. Capital Structure and Weighted Cost of Capital. There was no disagreement among the parties in their prefiled testimony that Petitioner’s cost of long-term debt is 6.60%, or that such debt comprised 50.11% of Petitioner’s capital structure. In its case-in-

chief, Petitioner proposed a cost of equity of 10.57% based on the average return on equity granted to its sister utilities in recent rate cases. OUCC witness Mr. Kaufman testified that his analysis supports a range of cost of equity of 9.40% to 10.37% for Petitioner, but that Petitioner and the OUCC agreed to use a cost of equity of 10.20% for purposes of this case.

Although the OUCC and the Petitioner agreed to a 10.20% cost of equity, upon reviewing the entire record that was presented in this case, we do not believe that 10.20% represents an appropriate cost of equity for this utility.

As we noted in our August 25, 2010 Order in Cause No. 43526, a utility's "operational and financial performance were appropriate considerations in determining a utility's cost of equity." *Northern Ind. Pub. Serv. Co.*, Cause No. 43526, at 32 (Aug. 25, 2010). In Cause No. 43526, we found that customer service and customer satisfaction were criteria that "warranted some consideration in our ultimate cost of equity determination." *Id.* Further, we stated that the "Commission has a unique role in regulating its jurisdictional utilities, which at times requires us to send a clear and direct message to utility management concerning the need for improvement in the provision of its utility service. Our determination of the authorized cost of common equity capital can be a very direct means to incent improved service." *Id.*

In this Cause, there was substantial evidence, as documented by the consumer comments made at the field hearing and LOFS witness testimony, that significant quality of service issues remain in the Twin Lakes service territory. Sewer overflows continue to occur during weather events, and customers have complained that drinking water was not used, or unusable, for drinking or bathing. Despite what customers have indicated were long-standing water issues, Twin Lakes has only recently implemented a flushing program to remove sediment from the water mains.

We have recognized a utility's obligation to provide adequate service in exchange for recovery of investments through rates. *See Twin Lakes Utilities, Inc.*, Cause No. 43128 S1, at 12 (Nov. 12, 2009) ("Commission would suggest that Petitioner reconsider its duty as a public utility to provide adequate service in exchange for receiving appropriate rate relief--Petitioner appears to be too focused on the second half of that equation.") If Twin Lakes cannot provide water and sewer service to its customers adequate for the purposes reasonably expected by its customers, it is this Commission's responsibility to speak directly to the utility's management, through our Orders, to send a message that service must improve. As we noted in Cause No. 43128, this message has been repeated for more than a decade, with limited improvements noted.

Having considered the evidence at issue, we find that Twin Lakes' cost of equity shall be 9.50%, which is in the range proposed by Mr. Kaufman. The Commission recognizes that a 9.50% return reflects a lower end of the appropriate range and that a higher return may be appropriate if Twin Lakes is able to demonstrate improved performance in its next rate case. We do note that management personnel have changed since we issued our Order in Cause No. 43128, and that Mr. Haas appeared to be sincere at the hearing in focusing on improving the service quality. However, it remains to be seen whether that focus will result in actual improvements for Petitioner's customers.

This results in the following weighted cost of capital to be used in this case for rate making purposes:

<u>Class of Capital</u>	<u>Percent of total</u>	<u>Cost</u>	<u>Weighted Cost</u>
Common Equity	49.89%	9.50%	4.740%
Long Term Debt	<u>50.11%</u>	6.60%	<u>3.307%</u>
Total	<u>100.00%</u>		<u>8.047%</u>

C. Revenue Adjustments Under Present Rates. The OUCC and Petitioner agreed to an adjustment to Petitioner’s operating revenue to reflect rental income associated with a cell tower leased by Petitioner to T-Mobile. Petitioner accepted the OUCC’s customer growth adjustments, although it used a more recent customer count and applied the adjustment to all meter sizes. We find that the adjustment to the more recent customer count and applying the methodology to all meter sizes is appropriate. Based upon these adjustments, we find Petitioner’s *pro forma* revenue under present rates totals \$926,786 and \$1,614,499 for its water and wastewater utilities, respectively.

D. Operating Expense Adjustments. Both the OUCC and Petitioner proposed a number of adjustments to Petitioner’s operating expenses. In rebuttal, Petitioner accepted many of these adjustments, including adjustments to salaries and wage expense, reduced capitalized labor, pension and other employee benefits, sewer and water maintenance, non-recurring maintenance, transportation expense, office utilities, payroll taxes and bad debt expense. Our resolution of the disputed adjustments is discussed below.

(i) Outside Legal Fees. OUCC witness Ms. Stull proposed to eliminate \$35,513 in test year legal expenses related to a lawsuit brought by a developer to recover a non-refundable deposit paid to Petitioner in a previous period. She argued that such fees are not normal, recurring legal fees that will be incurred in the future by Petitioner. She added that even if one considered these legal fees to be a normal, recurring operating expense, the fees should not be recovered through rates in this proceeding. She said that the fees relate to a transaction that occurred prior to the test year and that Petitioner did not fully explain the nature of the deposit, how it was recorded and how much the deposit was for.

In rebuttal, Mr. Neyzelman explained that there were actually two different lawsuits filed against Petitioner for which Petitioner incurred legal expenses during the test year. With respect to the lawsuit involving the non-refundable deposit, Mr. Neyzelman explained that the deposit, which totaled nearly \$250,000, was recorded to the Contributions in Aid of Construction accounts. He explained that the second lawsuit involved a construction company that had purchased a burned house and lot inside the LOFS subdivision and determined that it could not rebuild on the lot due to the location of Petitioner’s sewer main on the property.

Mr. Neyzelman stated that these expenses are typical of the type of legal expenses Petitioner anticipates it will incur in subsequent years. He noted that the average level of legal expenses incurred by Petitioner over the past three years is approximately \$55,000, which is greater than the adjusted test year amount. He said this further demonstrated the reasonableness of the test year level of legal expense.

We agree with Petitioner that its test year legal expenses are properly recoverable through rates. The lawsuits that occurred during the test year, while “non-recurring” in some sense, are representative of the types of claims, and types of expenses, which Petitioner may reasonably

expect to incur in the future. Accordingly, we find that the OUCC's adjustment to remove \$35,513 in test year legal expenses should be rejected.

(ii) Master Plan Costs. OUCC witness Mr. Corey proposed to remove Petitioner's master plan costs from Petitioner's rate base and amortize the costs over ten years. As discussed above, we agree the master plan costs should not be included in Petitioner's rate base.

In addition, we do not believe that Petitioner has adequately supported its master plan costs to allow them to be expensed. In response to the Commission's April 20, 2011 Docket Entry, Petitioner represented that its Water Supply Plan and Wastewater Treatment Plant Facilities Plan constituted its master plans. Having reviewed these plans, however, the Commission does not find that the planning included therein is typical of what the Commission would consider to be a comprehensive master plan. The two reports provided were short-term facility plans based on a 10-year planning horizon as opposed to the 10-30 year horizon expected within a comprehensive masterplan. They focused on specific equipment and upgrades to the water and wastewater treatment plants as opposed to the entire systems. Although they did provide some basic footprints, preliminary sizing and gross level cost estimates, we do not believe these plans to be evolved enough to be considered "Engineering Services" as discussed in section 7A. Therefore, we disallow the \$177,367 requested for master plan costs.

(iii) Rate Case Expense. In its case-in-chief, Petitioner proposed total rate case expense of \$152,130 including \$85,000 in legal fees. Mr. Corey recommended that a more reasonable estimate of legal fees would be \$30,000 based upon legal fees incurred as of the OUCC's testimony. Mr. Corey further recommended that expenses associated with water service personnel's work on the rate case, totaling \$62,851, be removed. He asserted that each of these individuals' wage expense has already been included and allocated to Petitioner in its wage adjustment, and therefore including their labor expense again in rate case expense would allow Petitioner to double recover these labor costs. Mr. Corey also recommended that Petitioner's rate case expense be amortized over four years, rather than three years as proposed by Petitioner.

In rebuttal, Mr. Neyzelman updated rate case expense to \$188,127 to reflect costs incurred to date along with his estimate of the remaining rate case expense. Mr. Neyzelman disagreed with Mr. Corey's elimination of the capitalized time related to rate case expense. He explained in detail the process by which labor is allocated to Petitioner and the method by which Petitioner separately tracks labor expense related to the rate case. He stated that when a service company employee books their time to a rate case, the amount is recorded in a separate account from the salary and wage account. He said that the capitalized time amounts which are booked are offset in the salaries and wages expense and are therefore not double counted in Petitioner's books. Mr. Neyzelman further stated that Petitioner plans on filing its next rate case within three years and thus a three year amortization period is appropriate for rate case expense. At the evidentiary hearing, Mr. Neyzelman testified regarding the latest update to rate case expense. On redirect examination, he testified that he performed an analysis based on a request from Ms. Stull and Mr. Corey to update the actual rate case expense incurred at the time he received the request. Based on that analysis, Mr. Neyzelman opined that Petitioner is anticipated to incur \$240,155 in total rate case expense.

Petitioner has incurred and seeks to collect from its ratepayers nearly \$90,000 more than the amount Petitioner claimed in its initial case. Petitioner's initial estimate was developed by Mr. Neyzelman, who explained during cross-examination that it was "what we normally estimate

for rate cases depending on who's working on them." (Hr. Tr. A-40, lines 17 - 20.) Mr. Neyzelman further explained that "it's not necessarily a guess. It's based on how much we normally spend on rate cases." (Hr. Tr. A-40, line 21 - A-41, line 2.) However, the Commission believes that due in large part to the operational issues identified in this case, this case was not a normal case, as suggested by Petitioner's updated rate case expense in the amount of \$240,155. If we compare Petitioner's initial estimate with Petitioner's updated estimate, we note that the latest estimates for legal and accounting personal are very close to Mr. Neyzelman's initial estimate, but operations personnel costs exceeded greatly Mr. Neyzelman's initial estimate. It is a reasonable inference that the reason Petitioner incurred more rate case expense than would normally be incurred is because of the need to respond to and explain Petitioner's significant operations issues. Moreover, we note that Petitioner's updated rate case expense would be one of the highest seen by this Commission from a utility that serves fewer than 5,000 customers.

In *South Haven Sewer Works, Inc.*, Cause No. 41903 (IURC, June 5, 2002), we declined to permit the utility to pass on legal expenses incurred in response to an investigation ordered by the Commission stating that "the ratepayers should not be penalized for the mistakes of the utility's management." The issues raised by LOFS did not revolve around Petitioner's proposed revenue requirements, but were issues about the operations of the utility including Petitioner's maintenance of the system in a safe manner. We have similar concerns. As explained further below, a review of Petitioner's past cases raises questions about the effectiveness of Petitioner's management and the efficiency of its operations. We consider the amount of rate case expense that has been expended over and above Petitioner's initial estimate to be more related to Petitioner's operational issues as raised by the LOFS. As such, we find that Petitioner should not be permitted to recover the additional rate case expense associated with the continued operational issues.

Accordingly, the Commission finds that Petitioner's rate case expense shall be \$152,130 as originally proposed in its case-in-chief. However, we disagree with Petitioner's use of a three year amortization period, as Mr. Corey demonstrated that Petitioner's historical practice has been to seek rate cases less frequently. Amortizing the approved amount of \$152,130 over a four year period results in a *pro forma* annual rate case expense of \$38,033, with \$19,119 allocated to the water utility, and \$18,914 to the wastewater utility.

(iv) Depreciation Expense. In its case-in-chief, Petitioner proposed to use the composite depreciation rates of 2% and 2.5% for all of its water and sewer plant, respectively, with the exception of computers and vehicles. Mr. Neyzelman proposed the use of a depreciation rate of 25% for vehicles and 12.5% for computers. He testified that these rates better reflect the actual useful lives for these particular assets. OUCC witness Mr. Corey recommended that the Commission apply the composite rate for all of Petitioner's depreciable assets until Petitioner obtains approval from the Commission to use anything other than a composite rate. He stated that this may be accomplished by Petitioner completing a depreciation study for all its Indiana utilities and submitting one request.

In rebuttal, Mr. Neyzelman continued to advocate for the use of a more accurate depreciation rate for vehicles and computers. He stated it was unrealistic to believe that vehicles or computers used by Petitioner can last fifty years. He explained the purpose behind depreciation, namely that it is designed to recover through revenues the costs invested in the physical plant that contributed to the production of those revenues, over a period of time that reflects the plant's useful life. He testified that the OUCC's recommendation does not match the

vehicles' and computers' depreciation expense with their useful lives and therefore does not properly match capital recovery needs with capital consumption. In support of his position, Mr. Neyzelman cited a number of treatises and the American Water Works Association's M1 Manual. Mr. Neyzelman stated that Petitioner's use of a four year useful life for vehicles and eight year useful life for computers is consistent with Petitioner's and its parent company's historical and working knowledge and is consistent with the depreciation rates used in other jurisdictions for Petitioner's sister utilities.

Our discussion of this issue begins with a brief discussion of the development of the composite water and sewer rates of 2.0% and 2.5%, respectively. These rates were developed based upon a generic study of the application of depreciation rates of all water utilities in Indiana performed by the Commission's Engineering Division. This study was completed and the suggested rates made available on January 1, 1988. *See In Re Brookville Municipal Water Utilities*, 1989 Ind. PUC LEXIS 260, Cause No. 38777-U (IURC 7/12/89). That study considered various components of utility plant, including vehicles, and determined a composite rate reflecting the useful lives of the individual categories of utility plant. *See In Re City of Evansville, Indiana*, Cause No. 42176 at 13 (IURC 2/18/04) (explaining that the composite rate applied a seven year service life for transportation equipment).

By definition, a composite depreciation rate is not the correct depreciation rate to use for individual items, but in consideration of the total plant, composite depreciation rates provide a realistic measure for that expense. The Commission's composite rates were based on all depreciable plant, including vehicles and computers. If Petitioner believes that a composite rate provides inaccurate information, it should have conducted and submitted for Commission approval its own depreciation study to more accurately reflect the expense.

Based on these findings, the Commission concludes that Petitioner's *pro forma* depreciation expense should total \$137,192 and \$333,267 for Petitioner's water and sewer utilities, respectively.

(v) Billing Costs. In its case-in-chief, the OUCC noted that Petitioner did not include an expense adjustment to reflect the increased costs associated with switching to a monthly billing cycle. In rebuttal, Mr. Neyzelman provided a calculation of the increased billing costs associated with monthly billing. We find that Mr. Neyzelman's adjustments of \$24,160 for the water utility and \$12,361 for the sewer utility to test year operating expenses is reasonable and should be approved.

(vi) Income Taxes. Petitioner agrees with the OUCC's methodology used to calculate state and federal income taxes. Based on the adjustments found above, Petitioner's total *pro forma* present rate state and federal income tax expenses for its water utility are \$333 and (\$3,150), respectively and for its wastewater system are \$30,372 and \$103,520, respectively.

E. Net operating income at present rates. Based upon the evidence and determinations made above, the Commission finds that Petitioner's *pro forma* revenue and expense amounts are shown as follows:

<u>OPERATING REVENUES</u>		
Customer Revenues	\$ 894,558	\$ 1,592,676
Forfeited Discounts	9,510	16,701
Miscellaneous Revenues	22,718	5,122
Total Operating Revenues	<u>926,786</u>	<u>1,614,499</u>
<u>OPERATING EXPENSES</u>		
Salaries and Wages	\$ 230,294	\$ 227,821
Capitalized Labor	(91,277)	(90,297)
Pension & Other Benefits	52,780	52,214
Purchased Power	132,978	90,109
Chemicals	21,962	22,113
Maintenance & Repair	38,945	148,507
Transportation	22,141	21,902
Outside Services – Other		
Legal Fees	21,292	21,071
Engineering Fees	565	7,359
Accounting Fees	2,610	2,581
Other Outside Services	7,820	7,734
Office Expenses	51,605	51,050
Billing Costs	24,160	12,361
Liability Insurance	24,446	24,178
Bad Debt Expense	8,795	8,654
Rate Case Expense	19,119	18,914
Miscellaneous	11,732	11,604
Depreciation	137,192	333,267
Payroll Taxes	19,083	18,877
Property Taxes	82,179	81,351
Utility Receipts Tax	12,845	22,475
IURC Fee	1,102	1,920
Amortization of Investment Tax	(941)	(930)
Federal Income Tax	(3,150)	103,520
State Income Tax	333	30,372
Total Operating Expenses	<u>\$828,609</u>	<u>\$1,228,727</u>
Net Operating Income	<u>\$98,176</u>	<u>\$385,772</u>

8. **Authorized Rate Increase.** Based upon the above findings, Petitioner’s revenue requirement is calculated as follows:

Revenue Requirement

	<u>Water</u>	<u>Sewer</u>
Original Cost Rate Base	\$ 3,124,927	\$ 5,560,235
Times: Weighted Cost of Capital	8.047%	8.047%
Net Operating Income Required	251,457	447,422
Less: Adjusted Net Operating Income	<u>98,176</u>	<u>385,772</u>
Additional NOI Required	153,281	61,649
Gross Revenue Conversion Factor	<u>1.700206</u>	<u>1.692769</u>
Recommended Revenue Increase	<u>\$ 260,609</u>	<u>\$ 104,357</u>
Percent Increase	<u>28.83%</u>	<u>6.48%</u>

9. **Rate Design.** Petitioner proposed two changes to its current rate design. First, it proposed to bill its customers on a monthly, rather than bi-monthly, basis. Second, Petitioner proposed a water rate design that will recover more of its revenue requirements from fixed monthly charges than it currently does under its present rate design. No party took exception to these proposed changes. Accordingly, the Commission finds that Petitioner’s proposed rate design is reasonable, appropriately allocates Petitioner’s revenue requirements between fixed and variable charges and should be approved.

10. **Non-Recurring Fees and Charges.** Petitioner proposed a number of changes to its water and wastewater tariffs. Petitioner proposed to adjust its existing Non-Sufficient Funds (“NSF”) charge and clarify its current meter reading fee. Petitioner also proposed to add language to its tariff regarding billing and payment options and Petitioner’s rules and regulations. No party took exception to these tariff changes and we find they should be approved.

Finally, Petitioner proposed to include a new After Hours Call Out charge to reflect the costs incurred by Petitioner to respond to a non-emergency after hours service call. Ms. Stull recommended that the Commission deny the inclusion of the after hours charge because of Petitioner’s historical water quality and customer service issues. She opined that this charge would unreasonably discourage customers from calling after hours when service issues arise. In rebuttal, Mr. Neyzelman clarified that the after hours charge would be assessed on a “case by case” basis in situations where a customer insists on having field personnel respond to an issue that can be handled during normal business hours.

In its proposed order, Petitioner appears to withdraw its request for an after hours charge, and the Commission finds that Petitioner’s proposed After Hours Call Out charge should be denied. In response to questions from the bench, Petitioner’s witnesses at the evidentiary hearing indicated that there were no written policies or guidelines which would be used to determine whether or not to impose the after hours charge. Petitioner’s witnesses were also unable to identify who specifically would make that determination and when the customer would be notified of the charge. Accordingly, we find that the inclusion of an after hours charge is not reasonable at this time.

11. **Operational Issues.** As was true in Petitioner’s rate cases dating back to the early 1990s, service quality issues remain a concern for LOFS. Testimony was provided both at the public field hearing and through prefiled testimony identifying instances of discolored water,

SSOs, backups into basements and a decrepit lift station. These cases viewed together permit us to make certain conclusions about the operations of this utility that should be corrected. These include an apparent lack of continuity among the individuals operating Twin Lakes, which we consider an obstacle to meaningful improvement. While Petitioner continues to ensure the Commission that it is aware of the systems issues and are working toward remediation, continued evidence of a lack of understanding of the system, its needs and maintenance exists. We believe the amount of employee turn-over may have exacerbated these issues. In this case alone, there was undisputed evidence of abandoned lift stations not properly closed, significant root intrusion, foul odors, inoperable hydrants, discolored water, SSOs and sewage backups into customers' basements. In one instance, Petitioner testified that a few hundred dollar investment in inflow dishes could have avoided one of the events that causes the customers to continue to have a lack of confidence in the operations of this utility – SSOs. Although we disagree with that specific conclusion, no investment was made to rehabilitate the known inflow sources.

The service quality issues that were raised in this case are: (1) SSOs; (2) water discoloration; (3) condition of hydrants; (4) Lift Station E; and (5) customer service. We will now address these specific issues.

A. SSOs and Ongoing Remedial Measures. In its Subdocket Order, the Commission ordered Petitioner to televise and clean a minimum of ten percent of its wastewater collection system each year. In his supplemental rebuttal testimony, Mr. Haas testified that Petitioner cleaned and televised nearly 25,000 feet during the twelve months ended July 1, 2011. While there appears to be some confusion on the part of Petitioner as to whether it must televise ten percent of its system during each calendar year, as opposed to each annual reporting period, we conclude that Petitioner has substantially complied with the requirements of the Subdocket Order. At the evidentiary hearing, there were some questions regarding when specific repairs identified during the televising process would be made. Accordingly, we direct Petitioner to include in its semi-annual report, discussed in greater detail below, both the results of Petitioner's televising activities, along with the plans and timetable for addressing any issues found. We understand that whole pipe rehabilitation is preferable to point repairs as it impacts life cycle costs and effective I/I abatement. While not every defect encountered warrants immediate repair, we expect to see some sort of phased rehabilitation plan that will prioritize rehabilitation/replacement of the system that will be implemented. We further direct Petitioner to televise and clean at least ten percent of its system on a calendar year basis. Data generated from those activities shall be incorporated into the utility's rehabilitation plan.

We note that LOFS has asked that we impose a remedy that will produce a solution to the SSO problems, rather than perform an exercise that requires more investment but takes no action to cure the problem. The Commission's intent is that the televising data used in conjunction with the flow monitoring data provides the basis for the utility to rehabilitate the collection system on a comprehensive basis by developing a recurring capital plan to address the I/I and hydraulic issues. Petitioner now has adequate data to develop and implement such a plan and is expected to do so.

Petitioner is also expected to properly maintain its systems and make prudent and reasonable infrastructure investments. We are troubled that although significant plant investments have been made, most of the same service issues still remain some twenty years later. Therefore, the Commission orders Petitioner to hire an unaffiliated third party to perform a

management audit to be completed and submitted to the Commission within six months from the date of this Order with a copy also being provided to the OUCC and LOFS as explained below.

B. Water Discoloration. Several customers testified at the field hearing regarding occurrences of discolored water. The evidence shows that although there are several potential causes for discolored water, Petitioner has made the necessary improvements to its water treatment plant to effectively reduce or eliminate the level of iron in the water leaving the plant. The evidence also shows that Petitioner has moved to an aggressive uni-directional flushing program to further eliminate the possibility of discolored water. From the evidence, it appears that this aggressive flushing may have addressed some water quality concerns. With that said, we question the operational decisions Petitioner made in allowing its filters to corrode to the point where large holes existed demonstrating a lack of diligence in assessing the asset's condition and planning for its ongoing maintenance/replacement.

We agree with Mr. Pettijohn that additional costly measures to remove iron from Petitioner's treated water would be unlikely to provide further benefits. Based on the evidence presented by Mr. Haas in his supplemental rebuttal testimony, it appears that Petitioner's use of a new flushing protocol has resulted in fewer occurrences of discolored water. We direct the Petitioner to continue to work on identifying the causes of discolored water in its system and to take appropriate steps to eliminate such causes. To the extent any of Petitioner's specific customers experience discolored water, we encourage Petitioner to work with those customers to isolate the particular causes of their discolored water.

C. Hydrants. In its prefiled testimony, LOFS presented evidence regarding the inoperable condition of twenty-two "fire" hydrants operated by Petitioner. In rebuttal, Mr. Haas clarified that Petitioner's hydrants are not designed to provide fire protection but are instead designed to allow Petitioner to flush its system. Mr. Haas testified that Petitioner inspected all of its hydrants following LOFS' testimony and found only three hydrants that were in need of repair or replacement. Further, these hydrants have been repaired or replaced, and at this time all hydrants are in proper functioning order. We note that without properly functioning hydrants, proper maintenance (flushing) cannot be conducted within the system. In order to properly maintain the system, the hydrants too need to be maintained. We direct Petitioner to inspect its hydrants on at least an annual basis and provide a written summary of the inspection results as part of its annual reporting requirements to the Commission.

D. Lift Station E. In its supplemental testimony, LOFS presented evidence regarding the deteriorated condition of Lift Station E. In his rebuttal and supplemental rebuttal testimony, Mr. Haas indicated that Petitioner has subsequently submitted plans to the Indiana Department of Environmental Management ("IDEM") for review and approval for modifications to Lift Station E, which would include turning the existing manhole into the new lift station wetwell, installing new submersible duplex pumps, and properly abandoning/closing the old "can-style" lift station. Mr. Haas testified the remaining lift stations have all been inspected and will fill five other structures no longer in use with sand and be welded shut. We direct Petitioner to properly and permanently close the five abandoned lift stations.

E. Customer Service. The evidence demonstrates there is need for improvement to Petitioner's customer service. The experience of Ms. Carol Karpen, who testified at the field hearing, is of particular concern to the Commission. Ms. Karpen testified that she had repeated water discoloration issues at her residence, and that Petitioner's employees

were unable to resolve the problem. She testified that she escalated her concerns up Petitioner's management chain, including via a letter to the President of Utilities, Inc. without avail.

During the evidentiary hearing, Petitioner's witnesses were questioned about Ms. Karpen's experience by the presiding officers. Specifically, Petitioner's witnesses were asked what procedures are in place or could be implemented to avoid "dropping the ball" with a customer like Ms. Karpen. Based on Petitioner's responses to those questions, the Commission is not satisfied that Petitioner has adequate processes in place. While we recognize that Ms. Karpen's experience may be an outlier, it is nonetheless incumbent upon Petitioner to take reasonable measures to avoid similar failures in its customer service processes.

In rebuttal testimony, Ms. Sasic believes that the Commission should not impose a set of requirements regarding Petitioner's customer service given in 2010, Utilities, Inc. made changes to consolidate its customer service operations to align processes and established KPIs for customer service operations to measure performance and bring more accountability to the process. Nonetheless, in its proposed order, Petitioner proposed a mechanism to address these deficiencies. More specifically, Petitioner proposed an additional step in its customer complaint procedure related to service. Specifically, if a customer calls about a service quality issue, currently that complaint is referred to the local Operator or Area Manager. Petitioner proposes that if a customer calls and is dissatisfied with the response, then the matter also be referred to the Director of Customer Care. Further, it appears that Petitioner needs to address internal communication issues by implementing a mechanism for the operational staff to clear a complaint and notify the customer service representative, who will then be in a position to follow up with the customer. In addition, we direct that Petitioner include in its report to this Commission a summary of any such customer complaints which are forwarded to the Director of Customer Care and their resolution. We find these measures to be a reasonable first step in addressing Petitioner's customer service issues. As discussed below, we will impose reporting requirements on Petitioner to ensure that these measures are having the desired results.

12. Reporting Requirements. Mr. Pettijohn recommended that Petitioner be required to provide certain information on a semi-annual basis. In rebuttal, Mr. Haas testified that Petitioner already submits annual reports to the Commission with its televised line inspection information and its plan for the upcoming year, which includes all improvements made in the previous twelve month period since the last report. He indicated that Petitioner does not object to submitting a semi-annual report to the Commission, OUCC and LOFS and extend the parameters of this report to include copies of monthly operating reports to depict water quality and a listing of call-out worksheets. Petitioner also proposed to include in this report its status of odor remediation and what steps it has taken to eliminate odors at the headworks of the wastewater treatment plant, as well as, the results of its televising, its timeframe for addressing issues and reasoning for concluding any issues were not cost effective to remedy and a report on complaints elevated to the Director of Customer Care. We find these proposals to be reasonable and appropriate. We further direct Petitioner to include a copy of its most recent hydrant inspection report, including information regarding what actions it has taken to remedy any issues found, as part of this semi-annual report. Accordingly, Petitioner is directed to file a semi-annual report in this docket, with the first report due July 31, 2012, for the preceding January through June period. Subsequent reports shall be filed under this Cause on January 31 and July 31 for the July to December and January through June periods, respectively. Petitioner shall also serve copies of the report on the OUCC and LOFS.

As noted above, Petitioner is also directed to perform a management audit and submit the report within six month of the date of this Order. The management audit shall be performed by an independent third party, the identity of which shall be submitted within 30 days of this Order for Commission approval. The scope of the audit shall provide a comprehensive review of Petitioner's management structure and identify appropriate management policies and procedures that need to be in place to assure proper, timely and reasonable management of the utilities' operations. In Cause No. 43645 involving the City of Indianapolis ("City"), CH2M HILL based the format and content of its management review of the City's Waterworks Department on the Indiana Department of Environmental Management, Office of Water Quality: *Information Handbook for Preparing a Water System Management Plan* (IDEM Handbook). The IDEM Handbook criteria includes the management, financial and technical capacity necessary to construct, maintain and operate water systems. These elements of capacity are applicable to Petitioner's water system. Similar elements of capacity should also be considered for Petitioner's wastewater system that assesses the effectiveness of management and the efficiency of Petitioner's operations.

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

1. Twin Lakes shall be allowed to increase its water rates by 28.83% and its sewer rates by 6.48% on an across-the-board basis. Such rates and charges shall be designed to produce total annual operating revenues of \$1,187,394 for the water utility and \$1,718,856 for the sewer utility, which are expected to produce annual net operating income of \$251,457 for water and \$447,422 for the sewer utility. Prior to placing these rates into effect, Petitioner shall file a revised tariff with the Commission's Water/Sewer Division. These rates are effective for applicable water and sewer service on and after Water/Sewer Division approval of the tariff.

2. Petitioner's proposed modifications to its tariff are approved, with the exception of the After-Hours Call Out Charge.

3. Petitioner's request to move to a monthly billing cycle is approved.

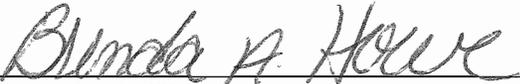
4. Petitioner is directed to file its first Semi-Annual Report in this docket and a copy of a complete management audit as set forth in Paragraph 12.

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

ATTERHOLT, BENNETT, LANDIS, MAYS AND ZIEGNER CONCUR:

APPROVED: FEB 22 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