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STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

IN THE MATTER OF THE)
PETITION OF PLEASANTVIEW) CAUSE NO. 44351 U
UTILITIES, INC. FOR A NEW)
SCHEDULE OF RATES AND) APPROVED: MAR 26 2014
CHARGES.)

ORDER OF THE COMMISSION

Presiding Officers:
David E. Ziegner, Commissioner
Marya E. Jones, Administrative Law Judge

On June 13, 2013, Pleasantview Utilities, Inc., (“Pleasantview” or “Petitioner”) filed its Small Utility Rate Application for a change in rates and charges (“Application”) with the Indiana Utility Regulatory Commission (“Commission”) pursuant to the provisions of Ind. Code § 8-1-2-61.5 and 170 IAC 14-1. Petitioner is seeking an across-the-board two-phase revenue increase totaling 107.73%, consisting of a Phase I rate increase of 74.13% and Phase II rate increase of 19.29%. On July 3, 2013, the Commission’s Water and Sewer Division issued a Memorandum stating that Petitioner’s Application was incomplete. On July 8, 2013, Petitioner filed additional information in support of the Application, including proofs of the notice it had published describing the filing of its Application as required by 170 IAC 14-1-2(b). On July 10, 2013, the Commission determined that the Application was complete.

Pursuant to Ind. Code § 8-1-2-61.5, a formal public hearing is not required in rate cases involving small utilities with fewer than 5,000 customers, unless a hearing is requested by at least ten customers, a public or municipal corporation, or by the Indiana Office of Utility Consumer Counselor (“OUCC”). On August 29, 2013, the OUCC filed a request for a public field hearing in response to a communication it received from 23 customers of Petitioner. The Commission granted the request on September 11, 2013. Pursuant to notice duly published as required by law, proof of which was incorporated into the record by reference and placed in the official files of the Commission, a public field hearing was held in this Cause on September 25, 2013 at 6:00 P.M., in the Connersville City Hall Council Chambers, 500 N. Central Avenue, Connersville, Indiana. Approximately 14 people out of a customer base of 194 connections attended the field hearing. The Commission held a public field hearing in lieu of an evidentiary hearing pursuant to Ind. Code § 8-1-2-61.5(b).

On October 7, 2013, the OUCC filed its report (“Report”) with the Commission as required by 170 IAC 14-1-4(a). The Report detailed its review of the Application and made several recommendations to the Commission concerning the relief requested by Petitioner. On November 29, 2013, Petitioner filed a notice of its intent to respond to the OUCC’s Report pursuant to 170 IAC 14-1-4(b). Petitioner failed to make any further filings thereafter. On February 6, 2014, a Docket Entry was issued and Petitioner responded on February 20, 2014.

Based upon the applicable law and the evidence presented herein, the Commission now finds as follows:

1. **Commission Jurisdiction and Notice.** Petitioner is a public utility as defined in Ind. Code § 8-1-2-1(a). The evidence presented by Petitioner in this Cause establishes that legal notice of the filing of the Application was published in accordance with applicable law and that Petitioner gave proper notice of the nature and extent of the relief it is seeking to its customers. The Commission thus finds that due, legal, and timely notice of this matter was given and published as required by law. Further, the Commission finds Petitioner is an Indiana public utility, provides water service to fewer than 5,000 retail customers and does not extensively serve another utility. The Application satisfies all of the requirements of Ind. Code § 8-1-2-6I.5 and 170 IAC 14-1 for treatment as a small utility. Therefore, the Commission has jurisdiction over the Petitioner and subject matter of this case.

2. **Petitioner's Characteristics.** Petitioner is an investor-owned public utility that provides water and sewer utility service to approximately 194 customers in the Pleasantview subdivision, located west of the City of Connersville, in Fayette County, Indiana. Petitioner is an S corporation whose common stock is solely owned by Mr. Matthew Sherck who also serves as President of the utility. Petitioner's collection system consists of clay tiles from homes that connect through 66 manholes to clay tile mains that deliver the raw sewage on a gravity basis to the wastewater treatment plant in the development. The wastewater treatment plant was constructed in 1974 and is a packaged plant rated to treat 60,000 gallons per day. The existing facilities include an abandoned equalization tank, two polishing ponds, and chlorination in advance of the ponds. The original surge tank and digester have been converted to perform aeration. Two blowers and a flow meter are in service. A new blower and flow meter were installed in 2012. Despite recent improvements, the condition of the wastewater plant has been allowed to deteriorate for several years. Due to repeated violations of its National Pollutant Elimination System ("NPDES") permit, Petitioner has been subject to an Agreed Order with the Indiana Department of Environmental Management ("IDEM") since 2005. Administrative Cause No. 2005-14957-W ("Agreed Order"). On September 4, 2013, IDEM approved a construction permit for capital improvements at Petitioner's wastewater treatment plant.

3. **Existing Rates and Relief Requested.** Petitioner's rates and charges were originally established in the Commission's September 25, 2002 Order in Cause No. 42202 U. At that time the Commission approved a \$21.61/month Phase I flat sewer rate, granted financing authority to borrow funds totaling \$305,000 at a maximum interest rate of 8% to build an interconnection with Connersville, and authorized a \$40.75/month Phase II rate that would be effective after the Connersville interconnection was built and in service. Phase II rates were never implemented because Petitioner has not made the approved borrowing or built the interconnection. Subsequently, in an Order dated April 23, 2008 in Cause No. 43313 U, the Commission approved a 12.82% increase, authorizing a \$24.38 monthly sewer service charge. The Commission denied Petitioner's request to recover debt service on plant that had yet to be built. Currently, Petitioner requests an across-the-board two-phase revenue increase totaling 107.73%, consisting of a Phase I rate increase of 74.13% and Phase II rate increase of 19.29%. The rate increase applies to wastewater usage and monthly service charges.

4. **Test Period.** The test period selected for determining Petitioner’s revenues and expenses reasonably incurred in providing water utility service to its customers includes the twelve (12) months ending December 31, 2012. With adjustments for changes that are fixed, known and measurable, the Commission finds that this test period is sufficiently representative of Petitioner’s normal operations to provide reliable data for ratemaking purposes.

5. **Application.** In its Application, Petitioner represented that the rate increase is necessary to implement capital improvements to its Wastewater Treatment Plant to comply with IDEM’s Agreed Order, and to cover increased operating costs. Phase II rates will not go into effect until the Wastewater Treatment Plant project is in service.

A. **Phase I Adjustments.**

I. **Revenue Adjustments.** Petitioner has no proposed revenue adjustments in the Application.

II. **Expense Adjustments.** Petitioner proposed the following *pro forma* adjustments to test year expenses:

i. **Salaries and Wage Expense:** An increase of \$13,375, which includes a proposed annual salary of \$12,000 for the President and allowance of \$1,950 for billing services.

ii. **Maintenance Expense:** An increase of \$13,355 to reflect the utility’s average annual cost of system maintenance, including pond maintenance, smoke testing, and the cost to televise and clean 10% of utility’s system.

iii. **Insurance Expense:** An increase in insurance premiums of \$202.

iv. **Rate Case Expense:** An increase of \$500 per year, which reflects a total rate case expense of \$2,500 over five years.

v. **Certified Operator Expense:** An increase of \$15,975 for Certified Operator services.

vi. **Laboratory Expense:** An increase of \$8,400 for accredited laboratory services.

vii. **Depreciation Expense:** An increase of \$2,881, based on utility plant in service of \$157,275 and a 2.5% composite depreciation rate.

viii. **Payroll Taxes:** An increase of \$1,067 to reflect increases in Salaries and Wage expense.

ix. **Property Taxes**: An increase of \$14.

x. **IURC Fee**: A decrease of \$1 and an increase of \$45 to reflect *pro forma* present and proposed adjustments, respectively.

xi. **Utility Receipts Tax**: A decrease of \$92 and an increase of \$527 to reflect *pro forma* present and proposed adjustments, respectively.

B. Phase II Adjustments.

I. Capital Improvements. To address IDEM's concerns set forth in the Agreed Order, Petitioner hired Hometown Engineering to assess the needs and estimate the cost of improvements to its wastewater treatment plant. Hometown Engineering determined that Petitioner's existing packaged plant is adequate to treat the average daily flows to the wastewater treatment plant, but plant improvements totaling \$127,500 are necessary to comply with IDEM's Agreed Order. This consists of \$107,500 in construction costs and \$20,000 for engineering costs. Therefore, for Phase II, Petitioner requests approval to incur \$127,500 in debt over a five-year period at an interest rate of 8% for wastewater treatment plant improvements.

II. Expense Adjustments.

i. **Operation and Maintenance Expense**: An increase of \$1,000, due to increased purchased power and chemical expense.

ii. **Depreciation Expense**: An increase of \$3,188, due to additional utility plant in service.

iii. **Property Taxes**: An increase of \$2,746, due to additional utility plant in service.

C. Rate Base. Petitioner's Application shows that in Phase I, Petitioner calculated a rate base of \$17,534, based on utility plant in service of \$157,275 as of December 31, 2012. For Phase II, Petitioner calculated a rate base of \$145,114, based on utility plant in service of \$284,775, which includes the proposed Wastewater Treatment Plant capital improvements. Petitioner calculated working capital of \$8,976 and \$9,056, for Phase I and Phase II, respectively. For Phase I, Petitioner proposed a 100% common equity capital structure, with a cost of equity rate of 12%. For Phase II, Petitioner proposed a capital structure consisting of 2.3% common equity and 97.7% long term debt, resulting in a weighted cost of capital of 8.09%.

6. OUCC Report. The OUCC filed its Report, which was prepared by Richard Corey, Harold Rees and Edward Kaufman. The Report recommended several adjustments to Petitioner's revenue and expense calculations. The OUCC Report recommended an across-the-board two-phase revenue increase totaling 42.20%, consisting of a Phase I rate increase of 11.96% and Phase II rate increase of 27.01%.

A. Phase I Adjustments.

I. **Revenue Adjustments.** The OUCC proposed the following adjustments to *pro forma* test year revenues:

i. **Accrued Water Revenue:** An increase of \$1,863 to reflect billed but uncollected wastewater revenue.

ii. **Accrued Penalty Revenue:** During the test year Petitioner billed \$3,112 in penalties for both water and wastewater services. The OUCC's calculations added 47% of the \$3,112 total penalty revenues, or \$1,471 to *pro forma* present wastewater revenues.

iii. **Revenue Normalization:** The OUCC's normalization method results in a *pro forma* present rate increase of \$1,815 for wastewater revenues.

II. **Expense Adjustments.** The Report indicated that Petitioner proposed several operation and maintenance expense adjustments yielding Phase I *pro forma* present rate operating and maintenance expense of \$79,100. The OUCC accepted Petitioner's proposed adjustments to insurance expense, rate case expense, and depreciation expense. However, the OUCC disagreed with Petitioner's remaining proposed adjustments, including:

i. **Salary and Wage Expense:** An increase of \$1,950 for billing services of 130 hours per year at \$15 an hour. The Report also stated a proposed \$12,000 annual salary for Petitioner's President has not been justified and the OUCC recommended disallowing the \$12,000 salary.

ii. **Maintenance Expense:** The OUCC agreed with the Petitioner's proposed maintenance expense. However, the OUCC determined that Petitioner's actual test year cost for maintenance expense was \$1,172 rather than \$345. Therefore, OUCC supports \$13,700 for annual maintenance which includes \$8,000 for pond maintenance, \$4,500 for beginning to clean and televise the collection system, and \$1,200 for some smoke testing.

iii. **IURC Fee Expense:** An increase of \$12 to reflect the IURC fee rate of .001329888% for fiscal year 2013-2014.

iv. **Certified Operator and Laboratory Expense:** Petitioner incurred \$5,625 of test year expense associated with retaining a Certified Operator. Petitioner adjusted its costs to reflect an increased cost of the Certified Operator. Subsequent to the end of the test year, Petitioner began using a Certified Operator and proposed to include in its revenue requirement for this new operator \$21,600 per year (\$1,800 per month). Petitioner incurred \$7,800 of test year laboratory testing expense and indicated that its testing expense has increased since it now uses an accredited laboratory. As such, Petitioner has requested \$16,200 per year for laboratory testing. Since Petitioner provided a single invoice from the new Certified Operator for \$1,500 for testing, the OUCC looked to a similarly situated utility, Prairie Utilities, and its contract with Astbury Water Technology to determine an appropriate expense for Petitioner. The OUCC determined the monthly fee of \$2,185 charged to Prairie is more representative of an

appropriate cost for a wastewater operator and laboratory testing, and therefore, adjusted Petitioner's proposed expenses to \$26,220.

v. **Bad Debt Expense**: An increase of \$838 reflects an estimated bad debt of 1.5%.

vi. **Payroll Taxes**: An increase of \$149 based on the OUCC's proposed salary and wage expense of \$1,950.

vii. **Property Tax**: Petitioner failed to include the local option income tax property tax replacement credit of \$406 on its additional utility plant in its Phase II *pro forma* property tax calculation.

viii. **Utility Receipts Tax**: *Pro forma* utility receipts tax incorporates all revenue adjustments discussed above.

B. Phase II Adjustments. The OUCC agreed with Petitioner on *pro forma* post-Phase II Operations and Maintenance expenses of \$1,000 and depreciation expense of \$3,188. The OUCC proposed the following Phase II adjustment:

I. Property Tax: The OUCC made a small correction to the Petitioner's *pro forma* Property tax adjustment to account for a credit that Petitioner overlooked. The OUCC has a *pro forma* Phase II property tax expense of \$2,340 rather than Petitioner's stated expense of \$2,746.

C. Rate Base. The OUCC accepts Petitioner's proposed utility plant in service of \$157,275 for Phase I and \$284,775 in Phase II. However, the OUCC's accumulated depreciation amounts include the *pro forma* adjustments to depreciation made in Phases I and II. The OUCC, therefore, recommended accumulated depreciation for Phase I in the amount of \$151,598 and \$154,786 for Phase II. This results in net utility plant in service of \$5,667 for Phase I and \$129,989 for Phase II. The OUCC also proposed working capital of \$6,030 for Phase I and \$6,169 for Phase II based on the changes to operating expenses discussed above.

The OUCC Report indicated Petitioner proposed a cost of equity and weighted cost of capital of 12.00%. The OUCC noted that Petitioner did not provide a study to support its proposed cost of equity, but agreed with Petitioner's decision not to incur the expense necessary to perform such a study. The OUCC does not oppose Petitioner's proposed cost of equity of 12.00%.

The Report noted Petitioner uses a capital structure that is 100% common equity. Taking into account Petitioner's customer deposits, the OUCC proposed a capital structure of 56.70% equity and 43.30% customer deposits in Phase I and 2.24% equity, 1.71% customer deposits and 96.04% debt in Phase II. Using cost of equity of 12.00%, cost of debt of 8.00%, customer deposits of 6%, and the capital structure, the OUCC proposed a cost of capital of 9.40% in Phase I and 8.05% in Phase II.

D. Accounting Practices. The OUCC indicated several concerns with Petitioner's accounting practices.

I. Billings and Accounts Receivable. The OUCC Report stated that Petitioner's billing system consists of a Microsoft Excel spreadsheet with more than 200 tabs, with the first tab providing a summary of all accounting information contained in the remaining tabs. The Report indicated that each customer has an individual tab containing a variety of information including water and wastewater sales, arrearages, date and amount paid, sales tax and penalties charges. The Report noted that once each individual tab is updated, the billing information is then transferred by hand to a postcard and sent to the customer. The OUCC noted that Petitioner's accounting system was not only cumbersome, but also prone to error. The Report indicated that Petitioner recorded cash receipts of wastewater revenue during the test year of \$50,729 and sold \$55,513 in wastewater services during the test year so that Petitioner billed \$4,784 more than it collected in cash for wastewater. The OUCC opined that Petitioner's accounting system creates an unacceptable risk for error since the OUCC cannot determine the reason for the discrepancy based on the utility's records. The OUCC recommended that Petitioner set up its accounts receivable system on its Quickbooks system with a sub account for each customer to allow Petitioner to track its receivables, revenues and number of customers on a real time basis.

II. Cash Management and Chart of Accounts. In reviewing Petitioner's financial records, the OUCC noted that Petitioner does not balance its checkbook on a regular basis and cannot, therefore, maintain proper control of expenditures and manage liquidity. The OUCC recommended that Petitioner balance its checkbook on a monthly basis.

The OUCC also noted that Petitioner has comingled its water utility and wastewater utility's accounts so that it is very difficult to separate the individual account information for the water utility and the wastewater utility. The OUCC recommended that Petitioner revise its chart of Accounts so that each utility's transactions are maintained in separate accounts.

E. IDEM Non-Compliance. The OUCC Report noted that Petitioner has had a history of non-compliance with state and federal environmental laws since 2003. Petitioner has been subject to an Agreed Order with IDEM since April 13, 2007, primarily due to repeated violations of its NPDES permit, pursuant to Administrative Cause No. 2005-14957-W.

The Report gave context to this issue and its relevance in this matter by noting that an IDEM representative conducted an inspection on Aug. 17, 2005, and noted the following:

1. The Operator's certification had expired on June 30, 2005.
2. A bypass line allowed excess secondary effluent to flow directly to the receiving stream.
3. Grease and sewage debris were found below the Sanitary Sewer Overflow outfall.
4. The packaged plant was off-line.
5. No means available for the wasting of sludge (both ponds were full of sludge).
6. The flow meter was in need of calibration and the V-notch weir was partially submerged causing inaccurate measurements.

7. No functional chlorine contact tank existed.

The Report further stated that subsequently on April 20, 2012, IDEM filed a Verified Petition for Civil Enforcement seeking enforcement of the Agreed Order, and on May 22, 2012, the Fayette Circuit Court entered a Judgment against Petitioner ordering the Utility to comply with the Agreed Order in all respects. The Report stated that on Aug. 21, 2013, IDEM and the Indiana Office of the Attorney General petitioned the Fayette Circuit Court to issue an order to Petitioner requiring the Utility to show cause as to why it should not be held in contempt of court for failing to comply with the Court's May 22, 2012 order. The Court set the matter for hearing on Sept. 9, 2013, but later continued the hearing at the request of IDEM and the Attorney General's Office after IDEM's approval of a construction permit for Petitioner's Wastewater Treatment Plant on Sept. 4, 2013.

The Report stated that Petitioner retained Hometown Engineering, specifically Ethel L. Morgan, PE, in 2012 to assess its wastewater treatment plant and to provide recommendations to bring the plant into compliance. Hometown Engineering determined that the existing packaged plant is adequate to treat the average daily flows to the wastewater treatment plant, and based on the results of flow monitoring, Hometown Engineering recommended the following improvements to the plant:

1. A new flow control and splitter box and an influent bar screen to divert flows to the new equalization basin (Est. cost = \$6,000).
2. A new flow 30,000 gallon capacity equalization basin with dimensions of 12 ft. x 36ft. x 11ft. – excavation cost at \$6/CY, concrete cost at \$600/CY – wall thickness at 14 inches and the floor at 18 inches). (Est. cost = \$50,000).
3. The transfer pumps for the basin (\$4,000) and aeration piping/diffusers (\$8,000).
4. A new blower (Est. = \$2,500, based on the cost of the existing blower)
5. The flow meter will be located to a new manhole with a flume – materials and labor cost of \$6,000.
6. New pellet feed systems (chlorination and de-chlorination) and a new 12 inch manhole (Est. cost = \$12,000).
7. Telemetry and SCADA work for high flow protection (Est. cost = \$4,000)
8. Conversion of the existing surge tank (aeration) requiring piping revisions (Est. cost = \$5,000).
9. Required piping and appurtenances (Est. cost = \$10,000) includes 175 ft of 8-in. piping with rearrangements totaling about \$5,200 and \$4,800 for a new headwall structure.

The OUCC reported that Hometown's total estimate for improvements to Petitioner's wastewater treatment plant is \$107,500 for construction costs and \$20,000 for engineering costs. Hometown's estimate also included a number of additional long-term construction engineering recommendations, including a proposed \$300,000 improvement to Petitioner's wastewater treatment plant. In spite of the foregoing, the OUCC recommends that Petitioner conduct a cost-benefit analysis of connecting to the City of Connersville, to ensure that funding these improvements is the most prudent course of action. The OUCC noted that 10 years ago Petitioner

obtained a cost estimate of connecting to Connersville's wastewater system which totaled \$500,000 and discussions with Connersville Utilities regarding fees to treat the water made the project infeasible because Connersville's fee would be by the gallon so that the cost to treat wastewater and inflow & infiltration was higher than Petitioner could recoup. The OUCC recommended that this estimate be updated.

F. OUCC Recommendations. The OUCC recommends that the Commission's Order incorporate three recommendations as follows: 1) Reflect the adjustments and the rates indicated in the OUCC's Sch. 1 – 9, resulting in a net revenue increase of \$6,684 or 11.96% increase in Phase I, and a net revenue increase of \$16,898 or 27.01% increase in Phase II; 2) Require Petitioner to conduct a cost-benefit analysis to determine the viability of connecting to the City of Connersville wastewater system; and 3) Require Petitioner to improve its bookkeeping and accounting systems to comply with generally accepted accounting principles.

7. Commission Discussion and Findings.

A. Revenues. Petitioner submitted its filing on a cash basis and recorded test year utility wastewater revenue of \$50,729. Petitioner accepted the OUCC's three *pro forma* present wastewater revenue adjustments for unrecognized revenue of \$1,863, accrued penalty revenue of \$1,471, and residential customer growth revenue of \$1,815. This results in Petitioner's *pro forma* present rate revenue of \$55,878. The Commission finds this *pro forma* present rate revenue to be reasonable, and is hereby approved.

B. Operations & Maintenance. Petitioner and the OUCC agreed on all *pro forma* Operations & Maintenance expenses except for the following:

I. Salaries and Wages. Petitioner requested an increase of \$13,950 in its Application, which includes an annual salary for the President of \$12,000 and a \$1,950 allowance for billing services. The OUCC agreed with the \$1,950 allowance for billing services, but recommended no salary for Petitioner's President citing the fact that he has not provided any detailed documentation of the duties he provides, and because the utility has a history of non-compliance with state and federal environmental regulations since 1997. The OUCC further noted Petitioner's President has not corrected the utility's wastewater treatment problems nor remedied its discharge permit violations. The Commission finds the utility's President performs all daily operations, billing, accounting, and maintenance services for the utility and should be compensated for these services. Petitioner's proposed Salaries & Wages expense adjustment of \$13,950 is reasonable and is hereby approved. Petitioner's Payroll Tax Expense shall reflect a *pro forma* increase of \$1,067 as a result of the Salaries & Wages expense adjustment.

II. Certified Operator and Laboratory Expense. Petitioner incurred \$5,625 of test year expense associated with retaining a Certified Operator. Petitioner adjusted its costs to reflect an increased cost of the Certified Operator when, subsequent to the end of the test year, Petitioner began using a Certified Operator and proposed to include in its revenue requirement \$21,600 per year (\$1,800 per month) for this new operator. Petitioner incurred \$7,800 of test year laboratory testing expense and indicated that its testing expense has increased

since it now uses an accredited laboratory. Petitioner has, therefore, requested \$16,200 per year for laboratory testing. Since Petitioner initially provided a single invoice from the new Certified Operator for \$1,500 for testing, the OUCC looked to a similarly situated utility, Prairie Utilities, and its contract with Astbury Water Technology to determine an appropriate expense for Petitioner. The OUCC determined the monthly fee of \$2,185 charged to Prairie is more representative of an appropriate cost for a wastewater operator and laboratory testing, and therefore, adjusted Petitioner's proposed expenses to \$26,220. In response to a Docket Entry dated February 6, 2014, Petitioner submitted invoices covering June 2013-November 2013, yet also stated no formal contract with the Certified Operator or laboratory has been executed. These invoices, while not detailed, support Petitioner's proposed *pro forma* Certified Operator expense of \$21,600 and laboratory testing expenses of \$16,200. Therefore, the Commission finds that Petitioner's *pro forma* adjustment for Certified Operator and laboratory expenses is approved. Further, we find that working with a contract in place is preferred and a better means by which to accurately determine the work to be completed and subsequent expense. We encourage Petitioner to enter into a formal contract with both the Certified Operator and the laboratory.

III. Bad Debt. Petitioner did not propose a bad debt *pro forma* adjustment. The OUCC proposed Petitioner recover bad debt expense of 1.5%, which when applied to *pro forma* revenues of \$55,878, results in an \$838 *pro forma* bad debt adjustment. The Commission finds that the OUCC's proposed bad debt adjustment is reasonable, and is therefore approved.

IV. Property Taxes. Petitioner proposed a *pro forma* property tax expense of \$14 in Phase I, and \$2,746 in Phase II. The OUCC accepted Petitioner's Phase I *pro forma* property tax adjustment, but proposed a \$2,340 Phase II *pro forma* property tax expense, based on a correction of Petitioner's omission of a \$406 local option income tax property tax replacement credit on its additional utility plant in Phase II. The credit is calculated by multiplying the gross tax by the applicable credit ($\$2,746 \times 14.799\% = \406). The Commission finds the OUCC's Phase II property tax correction to be accurate. Therefore, the Commission finds the Phase I and Phase II *pro forma* property tax adjustments of \$14 and \$2,340, respectively, to be reasonable, and therefore are approved.

After incorporation of the aforementioned adjustments, Petitioner's total *pro forma* present rate operations & maintenance expense is \$79,124 in Phase I, and \$79,647 after applying the gross revenue conversion factor.

In Phase II, Petitioner proposed and the OUCC agreed with two of the three adjustments related to increased costs due to the proposed wastewater treatment plant. These *pro forma* adjustments are post-Phase II Operations & Maintenance expenses (purchased power and chemicals) of \$1,000, depreciation expense of \$3,188, and property tax expense of \$2,340. The Commission finds that the Phase II operations & maintenance expense adjustments reasonable, and are therefore approved. Thus, Petitioner's Phase II total *pro forma* present rate operations & maintenance expense is \$80,647, and \$80,924 after applying the gross revenue conversion factor.

C. Rate Base. Petitioner proposed utility plant in service of \$157,275 in Phase I, \$284,775 in Phase II, and accumulated depreciation of \$148,717 in both Phase I and

Phase II. This resulted in a net utility plant in service of \$8,558 in Phase I and \$136,058 in Phase II. The OUCC accepted Petitioner's proposed utility plant in service for both Phases I and Phase II. However, the OUCC's accumulated depreciation amounts include the *pro forma* adjustments to depreciation made in both Phase I and II. Accordingly, accumulated depreciation for Phase I is \$151,598 and \$154,786 in Phase II, which results in net utility plant in service of \$5,677 and \$129,989 in Phases I and II, respectively. The Commission agrees with the OUCC's accumulated depreciation adjustments. Using the approved *pro forma* operations and maintenance expense of \$79,124 in Phase I and \$80,647 in Phase II, yields working capital of \$8,978 in Phase I and \$9,168 in Phase II. This results in an original cost rate base of \$14,655 and \$139,157 for Phase I and Phase II, respectively.

Rate Base

Phase I

Utility Plant in Service at 12/31/12	\$ 157,275
Less: Accumulated Depreciation	151,598
Net Utility Plant in Service	<u>5,677</u>
Add: Working Capital (see below)	8,978
Total Original Cost Rate Base	<u><u>\$ 14,655</u></u>

Phase I Working Capital Calculation

Operations & Maintenance Expense	79,124
Less: Purchase Power	<u>7,304</u>
Adjusted Operations & Maintenance Expense	71,820
Times: 45 Day Factor	<u>0.125</u>
Working Capital Requirement	<u><u>\$ 8,978</u></u>

Phase II

Utility Plant in Service at 12/31/12	\$ 157,275
Add: Plant Work	<u>127,500</u>
Gross Utility Plant in Service	284,775
Less: Accumulated Depreciation	<u>154,786</u>
Net Utility Plant in Service	129,989
Add: Working Capital (see below)	<u>9,168</u>
Total Original Cost Rate Base	<u><u>\$ 139,157</u></u>

Phase II Working Capital Calculation

Operations & Maintenance Expense	\$ 80,647
Less: Purchased Power	<u>7,304</u>
Adjusted Operations & Maintenance Expense	73,343
Times: 45 Day Factor	<u>0.125</u>
Working Capital Requirement	<u><u>\$ 9,168</u></u>

D. Cost of Capital. We note that Petitioner's cost of capital is made up of the weighted cost of debt, customer deposits, and the weighted cost of equity. While the OUCC accepted Petitioner's cost of equity of 12.00% because the costs to challenge Petitioner's proposed cost of equity would typically exceed any benefit, the Commission finds 12.00% to be inappropriate and instead finds the cost of equity should be 9.90%. To determine 9.90%, we looked first to the recommended cost of equity in recent similarly situated small investor owned utility cases. We also considered past cases where service quality was an issue and the Commission reduced the cost of equity to reflect that poor service quality.¹ Accordingly, as in recent similar small utility cases, we started with a cost of equity of 10.50% for Petitioner. We find that reducing the cost of equity by 0.60% for repeated IDEM violations is also appropriate in this Cause. This equation yields a cost of equity for Petitioner of 9.90%. The Commission accepts Petitioner's 8% cost of debt for Phase II.

Petitioner proposed a capital structure that is 100% common equity in Phase I and a capital structure of 97.7% debt and 2.3% common equity in Phase II. The OUCC proposed a capital structure of 56.7% equity and 43.3% debt in Phase I and 2.24% equity and 97.75% debt in Phase II, which takes into account Applicant's customer deposits. The amount of customer deposits allocated to wastewater is calculated by taking the combined total of customer deposits shown on Petitioner's balance sheet at the end of the test year (\$4,840) and multiplying it by the percentage of wastewater revenues to the total of both water and wastewater revenues in the test year (47%). This results in an overall weighted cost of capital of 8.21% in Phase I, and 8.01% in Phase II. The Commission finds this weighted cost of capital to be reasonable, and is therefore approved.

¹The Commission has reduced cost of equity for investor owned utilities in the past. See *Twin Lakes*, Cause No. 43957, 2012 Ind. PUC LEXIS 70 (IURC February 22, 2012). The Commission reduced the cost of equity by .60% where it found service quality to be an issue. See *Utility Center, Inc. D/B/A Aqua Indiana, Inc.*, Cause No. 43874, 2011 Ind. PUC LEXIS 94 (IURC April 13, 2011). The Commission recently found that a cost of equity of 10.50% was reasonable for a similarly sized small investor owned utility. See *Pioneer Water, LLC*, Cause No. 44309 U, 2014 Ind. PUC LEXIS 1 (IURC January 14, 2014).

**Pro Forma Capital Structure
As of Dec. 31, 2012**

Phase I	Percent of		Weighted	
	Amount	Total	Cost	Cost
Common Equity	\$ 2,979	56.70%	9.90%	5.61%
Customer Deposits	2,275	43.30%	6.00%	2.60%
Total	<u>\$ 5,254</u>	<u>100%</u>		<u>8.21%</u>

Phase II	Percent of		Weighted	
	Amount	Total	Cost	Cost
Common Equity	\$ 2,979	2.24%	9.90%	0.22%
Customer Deposits	2,275	1.71%	6.00%	0.10%
Long Term Debt	127,500	96.04%	8.00%	7.68%
Total	<u>\$ 132,754</u>	<u>100%</u>		<u>8.01%</u>

E. **Operations.** Petitioner has been subject to an Agreed Order with IDEM since 2005 primarily due to repeated violations of its NPDES permit. On August 17, 2005, an IDEM representative conducted an inspection and noted several infractions set out more fully herein. For those items that relate directly to its wastewater treatment plant, Petitioner hired Hometown Engineering to assess the needs and estimate the cost of plant improvements. Hometown Engineering determined that Petitioner's existing packaged plant is adequate to treat the average daily flows to Petitioner's wastewater treatment plant, but would need the plant improvements totaling \$127,500 to comply with IDEM's Agreed Order. This consists of \$107,500 in construction costs and \$20,000 for engineering costs. In Phase II, Petitioner requests approval to incur \$127,500 in debt over a five-year period at an interest rate of 8% for its wastewater treatment plant improvements.

The OUCC does not dispute the need for or the estimated costs of Petitioner's proposed wastewater treatment plant improvements. However, before Petitioner proceeds with its wastewater treatment plant improvements, the OUCC recommends that Petitioner conduct a cost-benefit analysis of connecting to the City of Connersville's wastewater treatment facilities. In a response to an OUCC Data Request, Petitioner stated that 10 years ago it obtained a cost estimate of connecting to Connersville Utilities' wastewater system, which totaled \$500,000. Petitioner stated that its discussions with Connersville Utilities regarding fees to treat the water made the project infeasible since the fee would be by the gallon and the cost to treat wastewater and inflow & infiltration was higher than Petitioner could recoup.

We find that Petitioner's proposed wastewater treatment plant improvements are prudent, cost effective, and necessary to comply with IDEM's Agreed Order. Noting both the lapse of time since Petitioner's last discussion with Connersville Utilities regarding a possible wastewater connection to Connersville Utilities and the magnitude of capital expenditures for such a small customer base when considering the prior quote from Connersville Utilities, we find that

Petitioner need not conduct a cost-benefit analysis of connecting to the City of Connersville's wastewater treatment facilities prior to implementation of its wastewater treatment system improvements. We find that it is unlikely that the current cost of interconnection will be more cost effective than either Petitioner's proposed improvements of \$127,500 or the \$500,000 quote previously obtained.

F. Financial Record Keeping. Petitioner uses the cash basis method of accounting which is appropriate for a Class C utility under the NARUC System of Accounts. Petitioner uses Excel spreadsheets and QuickBooks accounting software to process its monthly billing. The OUCC noted discrepancies between what Petitioner recorded as cash receipts in the test year vs. what was billed in the test year. The OUCC recommends Petitioner set up its Accounts Receivable in QuickBooks, reconcile its checkbook to its bank statement monthly, use separate water and wastewater accounts to track transactions, and consider obtaining the services of a billing company to provide billing services. We find merit in the OUCCs recommendations; therefore, we find that that Petitioner shall set up its Accounts Receivable in QuickBooks, reconcile its checkbook to its bank statement monthly, use separate water and wastewater accounts to track transactions, and consider obtaining the services of a billing company to provide billing services. We also find that Petitioner shall conform to the NARUC Uniform System of Accounts for Class C Wastewater utilities and generally accepted accounting principles.

G. Authorized Rate Increase. Petitioner originally proposed an across-the-board two-phase revenue increase totaling 107.73%, consisting of a Phase I rate increase of 74.13% and Phase II rate increase of 19.29%. The rate increase applies to wastewater usage and monthly service charges. The OUCC Report recommended an across-the-board two-phase revenue increase totaling 42.21%, consisting of a Phase I rate increase of 11.96% and Phase II rate increase of 27.01%. Based upon the evidence presented and the discussion above, the Commission finds that a two-phase revenue increase totaling 87.74%, consisting of a Phase I rate increase of 57.35% and Phase II rate increase of 19.31% are approved for Petitioner. Phase I rates shall become effective on the approval of Petitioner's tariff to be filed in accordance with this Order and the Phase II rate adjustment shall become effective upon completion of the wastewater plant improvements and notification to the Commission that the improvements are in service and filing of updated tariffs. The Petitioner's revenue increase and revenue requirements approved by the Commission are shown below:

	IURC Phase I	IURC Phase II
Revenue Increase		
Rate Base	\$ 14,655	\$ 139,157
Times: Cost of Capital	<u>8.21%</u>	<u>8.01%</u>
Net Operating Income Required	1,203	11,144
Less: Pro-forma NOI at Present Rates	<u>(29,880)</u>	<u>(5,323)</u>
Increase in NOI Required	31,083	16,467
Times: Gross Revenue Conv. Factor	<u>103.11%</u>	<u>103.11%</u>
Recommended Increase	<u>\$ 32,048</u>	<u>\$ 16,979</u>
Recommended Percentage Increase	<u>57.35%</u>	<u>19.31%</u>
Revenue Requirements		
Operations and Maintenance Expenses	\$ 79,647	\$ 80,924
Depreciation Expense	3,932	7,119
Taxes Other Than Income	3,143	5,717
Income Taxes	-	-
Return on Rate Base	<u>1,204</u>	<u>11,145</u>
Total Revenue Requirements	<u>\$ 87,926</u>	<u>\$ 104,905</u>

H. Effect on Rates. The results for a residential customer will be an increase of \$13.98 per month from \$24.38 to \$38.36 for Phase I, and an increase of \$7.41 per month from \$38.36 to \$45.77 for Phase II based on the approved rate adjustments.

I. Alternative Regulatory Program (“ARP”). If Pleasantview Utilities elects to participate in the Small Utility ARP Program in accordance with procedures approved in Cause No. 44203, the eligible operating expenses and Taxes Other Than Income to which the Annual Cost Index will be applied for Phase I are \$79,647 and \$3,143, respectively. Similarly, the eligible operating expenses and Taxes Other Than Income to which the Annual Cost Index will be applied for Phase II are \$80,924 and \$5,717. All other components of the revenue requirement will remain unchanged.

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

1. Consistent with the above findings, Pleasantview is authorized to increase its monthly recurring rates and charges by 57.35% so as to produce revenue of \$32,048 for Phase I, and to make an adjustment in Phase II resulting in an increase of 19.31% producing revenues of \$16,979.

2. Prior to placing into effect the rates and charges approved herein, Petitioner shall file with the Water/Sewer Division of the Commission a schedule of rates and charges in a manner consistent with this Order and the Commission’s rules for filing such schedules. When approved by the Commission’s Water/Sewer Division, such schedule shall cancel all prior rates

and charges.

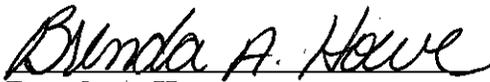
3. Petitioner shall obtain financing and implement the plant improvements as discussed above in Finding Paragraph 7.E. Petitioner shall notify the Water/Sewer Division of the Commission and OUCC upon completion of the plant improvements and shall also file a revised schedule of rates and charges with the Water/Sewer Division of the Commission reflecting the Phase II rates. When approved by the Commission's Water/Sewer Division, such schedule shall cancel all prior rates and charges.

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

ATTERHOLT, MAYS, STEPHAN, WEBER, AND ZIEGNER CONCUR:

APPROVED: MAR 26 2014

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



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