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STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF SWITZERLAND COUNTY )  
NATURAL GAS COMPANY, INC. FOR ) CAUSE NO. 45117  
AUTHORITY TO CHANGE ITS RATES, )  
CHARGES, TARIFFS, RULES, AND ) APPROVED: APR 17 2019  
REGULATIONS )

ORDER OF THE COMMISSION

**Presiding Officers:**  
**Stefanie N. Krevda, Commissioner**  
**Carol Sparks Drake, Senior Administrative Law Judge**

On June 26, 2018, Switzerland County Natural Gas Company, Inc. (“Switzco” or “Petitioner”) filed a Petition with the Indiana Utility Regulatory Commission (“Commission” or “IURC”) seeking authority to change its existing rates, charges, tariffs, rules, and regulations. That same day, Switzco prefiled the testimony and exhibits of the following witnesses:

- Bonnie J. Mann, Certified Public Accountant and Principal with LWG CPAs and Advisors (“LWG”);
- Earl L. Ridlen, III, Certified Public Accountant, Financial Advisor, and Managing Partner of LWG; and
- Kerry A. Heid, Licensed Professional Engineer and Utility Rate Consultant.

On July 9, 2018, the Indiana Office of Utility Consumer Counselor (“OUCC”) filed a motion asserting that Switzco failed to provide the Commission and the OUCC with notice 30 days before initiating this base rate case as required by General Administrative Order (“GAO”) 2013-5. In its motion, the OUCC asked that Switzco not be allowed to proceed with this rate case or that 30 days be added to the procedural schedule to enable the OUCC and the Commission to examine the issues. In responding to the OUCC’s motion, Switzco averred that Petitioner initially provided the OUCC with notice on July 19, 2017, of Switzco’s intent to file a base rate case and thereafter periodically referenced the case in discussions with the OUCC. Petitioner also expressed its willingness to meet with the OUCC to discuss a procedural schedule. Ultimately, on August 2, 2018, Petitioner and the OUCC (collectively the “Parties”) filed a Stipulation and Agreement (“Stipulation”) wherein they proposed a procedural schedule, and the OUCC withdrew its motion. Consistent with the Parties’ Stipulation, a Docket Entry was issued on August 3, 2018, establishing the procedural schedule for this Cause. On September 24, 2018, Petitioner filed a copy of the notice Switzco provided to its customers as ordered by the Docket Entry of August 3, 2018.

On November 2, 2018, the OUCC prefiled its case-in-chief, including the testimony and exhibits of the following OUCC employees in its Natural Gas Division:

- Isabelle L. Gordon, Utility Analyst;
- Amy E. Larsen, Utility Analyst II;
- Edward T. Rutter, Chief Technical Advisor;
- Leon A. Golden, Utility Analyst II;
- Bradley E. Lorton, Utility Analyst;
- Jennifer L. Reed, Utility Analyst; and
- Brien R. Krieger, Utility Analyst.

On November 30, 2018, Switzco prefiled its rebuttal evidence. This included rebuttal testimony and exhibits by Ms. Mann, Mr. Ridlen, and Mr. Heid.

A Docket Entry was issued on December 12, 2018, requesting Petitioner to provide certain additional or clarifying information. Petitioner filed responses to this Docket Entry on December 18, 2018.

The Commission conducted a public evidentiary hearing in this Cause on December 21, 2018, at 9:30 a.m. in Hearing Room 222 of the PNC Center, 101 West Washington Street, Indianapolis, Indiana. Proofs of publication of the notice of the evidentiary hearing were incorporated into the record and placed in the official files of the Commission. Petitioner and the OUCC appeared by counsel and participated.

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

1. **Notice and Jurisdiction.** Due, legal, and timely notice of the public evidentiary hearing in this Cause was given and published as required by law. Petitioner is a public utility as defined in Ind. Code § 8-1-2-1. Petitioner seeks authority to change its existing rates, charges, tariffs, rules, and regulations under Ind. Code §§ 8-1-2-1, -6, -42.7, and -61. The Commission, therefore, has jurisdiction over Switzco and the subject matter of this Cause. Pursuant to the Stipulation, this proceeding is deemed to have been initiated on July 27, 2018, for purposes of the 300 day procedural schedule in Ind. Code § 8-1-2-42.7.

2. **Petitioner's Characteristics.** Switzco is a small public utility, organized as a corporation under the laws of the State of Indiana. Its office is located in Vevay, Indiana. Petitioner is owned by the Kiwanis Club of Vevay, the Town of Vevay, and the Vevay/Switzerland County Foundation. Switzco provides natural gas service to approximately 680 customers in rural and municipal areas in Switzerland and Jefferson Counties, Indiana, under various prior Commission Orders.

3. **Existing Rates, Test Year, and Relief Requested.** Petitioner's current base rates were established by the Commission's Order in Cause No. 44293 approved on May 15, 2013. Under the settlement agreement in Cause No. 44293, the rates approved were reduced in September 2017. Based on the Petition initiating this Cause and the Parties' Stipulation, the test year for this proceeding is September 30, 2017, as adjusted for changes that are fixed, known, and measurable and occurring within 12 months following the end of the test year. Petitioner's cut-off date for determining the used and useful status of its utility plant in service and the value of its rate base is also September 30, 2017. Based on Petitioner's case-in-chief, Switzco seeks to increase its rates by

7.71% inclusive of the cost of gas, which represents additional operating revenue of \$83,699 over pro forma rate revenue as of the test year, exclusive of the cost of gas.

4. **Switzco's Case-in-Chief.**

A. **Bonnie J. Mann.** Petitioner's witness Bonnie J. Mann described her work as a Certified Public Accountant specializing in public utility matters. Ms. Mann testified that she began discussions with Petitioner's Board of Directors in February 2017 about the possibility of Petitioner filing a rate case because Switzco was not achieving its authorized earnings. She explained that LWG's subsequent work included advising Petitioner's management upon the impact the Tax Cuts and Jobs Act of 2017 ("TCJA") will have on Switzco's rates, adjustments that should be made in a rate case, and the appropriate level of revenue required to recover Petitioner's cost of service. Ms. Mann testified upon the adjustments to Petitioner's September 30, 2017, test year records, the results of these adjustments, and Switzco's rate base as of September 30, 2017. She explained that Switzco's largest customer, Belterra Casino ("Belterra"), paid for a line extension ("Belterra main"), the cost of which was excluded from rate base in this Cause consistent with its treatment in Switzco's previous rate cases. Ms. Mann testified that Switzco should be authorized to increase its operating revenue by \$83,699, representing an overall increase of 7.71% over pro forma rate revenue as of September 30, 2017, as set forth in Exhibit BJM-1, Exhibit C.

B. **Earl L. Ridlen, III.** Mr. Ridlen described his work as a financial advisor analyzing current market conditions, unique factors associated with particular utilities, and appropriate rates of return. He explained that the analysis he performed for Switzco included reviewing prior Commission Orders, the reported earnings of other utilities, and various ratios, including price to book, price to earnings, and price to sales for Vectren, NIPSCO, and the natural gas utility industry. He testified that his conclusion on a rate of return for Switzco is based upon this analysis, but he also considered the risks associated with this particular utility. He identified these risks as including that Petitioner's stock is not listed; its service area is not diversified, and it faces regulatory risks. Mr. Ridlen stated the overall economy of the United States, and specifically, the State of Indiana, has improved since Petitioner's last rate case, Cause No. 43897 U, in which a return on equity was established at 9.90%. Based on his analysis, Mr. Ridlen recommended 10.25% as the appropriate return on equity now for Switzco. Mr. Ridlen testified that because Petitioner was required to reduce its rates to eliminate the cost of its last rate case from base rates and was unable to adjust its base rates for the increase in its federal income tax rate, Switzco no longer has the opportunity to earn a reasonable return.

C. **Kerry A. Heid.** Mr. Heid stated the purpose of his testimony is to present evidence on Petitioner's cost of service, Petitioner's subsidy reduction and revenue distribution among its rate schedules, and the rate design and levels of rates and charges applicable to each rate schedule. Mr. Heid testified that he has 40 years of experience working on utility rates, including analyzing and presenting cost of service studies to the Commission. He stated he had previously performed work for Switzco in Cause No. 44293. Mr. Heid testified that the purpose of a cost of service study is to allocate the pro forma revenue requirement to the utility's rate classes based on the investment the utility has made in plant and the operating costs associated with its customer classes.

Mr. Heid began his review of Petitioner's proposed allocation by noting Switzco has three customer classes: Rate 1R, Rate1G, and Rate 2. Rate 1R is a class designed to serve residential

customers. Rate 1G is designed to serve nonresidential customers, and Rate 2 is designed to serve large commercial and industrial customers whose annual volumes are greater than 10,000 therms. As of the test year, Mr. Heid testified that Rate 1R served 564 customers. Rate 1G served 130 customers, and Rate 2 served 13 customers. Based on his cost of service study, the monthly customer charge for Rate 1R should increase from \$10.86 to \$13.00. He testified that with this increase, Petitioner will still only collect 32% of the allocated fixed costs related to this customer class. For Rate 1G, Mr. Heid proposed a \$13.00 per month customer charge, noting the current charge for Rate 1G is the same as Rate 1R. For Rate 2, Mr. Heid proposed an increase in the monthly customer charge from \$90.52 to \$100 per meter. Mr. Heid testified that all volumetric rate changes are reflected in his Exhibit KAH-8. He also testified that he did not include a revised tariff in his exhibits because of the uncertainty of the impact on rates attributable to the TCJA and the Commission's pending tax proceedings. In Mr. Heid's opinion, the better approach in this Cause is to file Switzco's final tariff after the Order in this proceeding is approved.

**5. OUCC Case-In-Chief.**

**A. Isabelle L. Gordon.** In her testimony, Ms. Gordon discussed the OUCC's proposed adjustments to Switzco's revenue requirements, including operating revenues and expenses, rate base, and capital structure. Ms. Gordon recommended Petitioner's pro forma revenue requirement increase be reduced to \$18,306, yielding an increase of 3.33% in Petitioner's gross margin.

Ms. Gordon stated she made corrections to Petitioner's revenue requirement schedules included in Ms. Mann's Exhibit BJM-1. She included deferred tax in the calculation of synchronized interest. Ms. Gordon also included Petitioner's Belterra note payable for the Belterra main in her calculation of synchronized interest and the capital structure.

Ms. Gordon testified that Petitioner calculated new National Oceanic and Atmospheric Administration ("NOAA") averages for the Normal Temperature Adjustment ("NTA") by weather normalizing test year Heating Degree Days using both the 1971-2000 NOAA averages and the 1981-2010 NOAA averages. She stated Petitioner used the variance between the two normalizations to find the necessary adjustment for the test year. Ms. Gordon agreed with Petitioner's methodology, but she found errors in its calculation. Her corrections result in a decrease to sales revenue of \$1,527.

Ms. Gordon disagreed with several components of Switzco's natural gas purchased adjustment calculation. She testified that she updated Petitioner's unaccounted for gas ("UFG") calculation using the UFG approved in Petitioner's GCAs 88, 92, 95, 97, and 99, whereas Petitioner's calculation relied on GCAs 68, 88, 92, 95, and 97. Ms. Gordon disagreed with Petitioner's estimated \$3.89 per Dth cost of purchased gas, noting that Petitioner's supplemental workpaper calculated the cost of purchased gas as \$3.8295 per Dth. She testified the difference between her estimated cost and Petitioner's estimated cost is due to the Utility Receipts Tax ("URT"). Ms. Gordon stated the Indiana URT is inappropriately included in the calculation of estimated cost of purchased gas for purposes of calculating Petitioner's cost of UFG.

Ms. Gordon agreed with Petitioner's amortization period of five years for rate case expense based on the average Ms. Mann calculated, as shown in Ms. Mann's testimony on page 5, lines 16-17. After accounting for Mr. Rutter's proposed adjustment to rate case expense and the rate case

expense embedded in Petitioner's test year, Ms. Gordon testified her adjustment for rate case expense is an increase of \$1,844.

Ms. Gordon testified that Petitioner's IURC fee adjustment did not remove bad debts from applicable revenue at present rates. She stated Petitioner did not use the current IURC rate, which became effective July 1, 2018. Ms. Gordon stated her adjustment to the new NOAA averages for the NTA and to the natural gas purchased adjustment impacted her IURC fee adjustment.

Ms. Gordon also addressed Petitioner's lack of a miscellaneous expense adjustment. She testified that Petitioner included within the test year several expenses that should not be recovered in rates. These included expenses for advertising, donations, and gifts. Ms. Gordon testified that Switzco provided no evidence that the advertising expense met the exception recognized in 170 IAC 1-3-3. Ms. Gordon also testified that Petitioner included outside service expense related to the current proceeding. She stated rate case expenses should be deferred and included in rate case expense rather than in general outside service expense.

Ms. Gordon agreed with Petitioner's methodology used in calculating URT and state and federal income taxes. She testified her changes to these calculations are a result of changes to pro forma revenue and expenses.

Ms. Gordon changed Petitioner's capital structure, suggesting the capital structure should be the capital structure as of September 30, 2017, not December 31, 2017, as Petitioner used in its case-in-chief. She testified the purpose of the capital structure is to fund rate base; therefore, the appropriate date of the capital structure is the date of Petitioner's rate base cut-off. She stated that using a capital structure as of December 31, 2017, as Petitioner proposed does not reflect the connection between Petitioner's capital structure and rate base. Ms. Gordon also addressed long-term debt that Petitioner did not include in its capital structure. She testified Switzco did not include the Belterra note payable in its proposed capital structure, and as a result, the value of Petitioner's rate base was greater than the amount of capital used to fund that rate base. Ms. Gordon testified that excluding the Belterra note payable provides an incomplete picture of the funding available to Switzco and is inappropriate considering the immense value to Petitioner from the Belterra note that carries no interest. She also made an adjustment to long-term debt to include a service truck note in the amount of \$25,000 in Petitioner's capital structure. She stated this loan was included in the trial balance as of December 31, 2017, but not in the trial balance as of September 30, 2017, though the date of the note was September 22, 2017.

Ms. Gordon also testified concerning Petitioner's customer deposit policy. She stated Switzco requires \$100 deposits from its customers and that in responding to OUCC Data Request ("DR") 6.2, Petitioner provided no indication that Switzco allows customers to prove their creditworthiness or make installment payments as required by 170 IAC 5-1-15. Ms. Gordon recommended the Commission conduct a review to ensure Petitioner is evaluating customer creditworthiness and communicating pertinent information to its customers, with the requested information provided to the Commission within 45 days of the Order in this Cause.

**B. Amy E. Larsen.** OUCC witness Larsen testified concerning Petitioner's operating expense adjustments. Specifically, she offered adjustments to Petitioner's test year related to payroll expense, retirement contribution expense, health insurance expense, payroll taxes, and property taxes.

With respect to payroll, Ms. Larsen acknowledged Switzco proposed an increase to its payroll following the test year cut-off and an additional increase to payroll as a result of action by Switzco's Board of Directors on October 2, 2018. She disagreed with Petitioner's payroll expense adjustments. First, Ms. Larsen disagreed with Petitioner applying a 3% increase to test year wages. She testified Petitioner should apply the actual percentage increase Switzco's Board of Directors approved on May 22, 2017; therefore, she reduced Petitioner's normalized test year wages because the Board approved a 2% increase at that time. Ms. Larsen also disagreed with Petitioner including bonuses in its payroll adjustment. She testified bonuses are not necessary to the provision of utility service. In addition, Ms. Larsen disagreed with allowing the additional salary expense the Board of Directors approved at its October 2, 2018, meeting to be included in Petitioner's payroll adjustment. Ms. Larsen testified the October 2, 2018, action by the Board increasing salaries happened more than 12 months after the end of the test year and should not be included in the payroll adjustment. She recommended removing the bonuses and adjusting for a 2% increase, with a final adjustment of \$2,184.

Ms. Larsen also disagreed with Switzco's adjustment to retirement contribution expense due to her disagreement with Petitioner's payroll expense increase because payroll expense flows through to retirement contribution expense. While she did not disagree with including Petitioner's contribution to retirement expense in the revenue requirement, her pro forma payroll revenue requirement was lower than Petitioner's because she reduced Petitioner's pro forma payroll revenue requirement. She recommended a \$218 adjustment to retirement contribution expenses.

Ms. Larsen disagreed with Petitioner's adjustment for health insurance expense. She testified that Petitioner's adjustment includes a \$300 reimbursement for each employee per month for health insurance and \$184 per employee per month for AFLAC services. Ms. Larsen took issue with this amount after reviewing the general ledger and determining Switzco actually pays \$300 per month to two employees and \$262.50 per month to the third employee; therefore, she reduced the health insurance contribution, opining that Petitioner's health insurance adjustment should be based on what Petitioner actually reimburses. Ms. Larsen recommended an adjustment of \$712 to the health insurance contribution expense.

Ms. Larsen also disagreed with Petitioner's adjustment for payroll taxes due to her disagreement with Petitioner's payroll expense adjustment because payroll expense flows through to payroll taxes. Ms. Larsen recommended payroll tax expense be adjusted by \$167.

Finally, Ms. Larsen disagreed with Switzco's adjustment to property taxes. Specifically, she disagreed with Petitioner's amount for 2016 property taxes paid during 2017. She testified Petitioner did not include all the property tax invoices that were paid in 2017 for 2016 and recorded an incorrect amount for one invoice that was originally included. Ms. Larsen recommended an adjustment of \$321 to Petitioner's property tax expense.

C. **Edward T. Rutter.** Mr. Rutter testified that as a small utility, Switzco has the ability and the right to file an application under 170 IAC 14-1 *et seq.* for a rate change ("Small U" filing). He testified that 170 IAC 14-1-1(h) defines a small utility as follows:

‘Small utility’ means any public or municipally owned utility subject to the jurisdiction of the commission that:

- (1) serves less than five thousand (5,000) customers as of the date any application for rate change is filed;
- (2) primarily provides retail service to customers; and
- (3) does not serve extensively another utility.

Mr. Rutter testified the Commission’s brochure on Small U filings for rate changes recognizes this procedure is designed for small utilities that “need to increase rates but don’t have the staff or the money needed to finance a full-blown rate case.” Public’s Ex. 3 at p. 2. Mr. Rutter stated this brochure further explains:

The small utility rate application was established to provide small utilities with an opportunity to increase rates and charges through a less costly regulatory procedure. Under the small utility rate application procedure, a utility completes standard forms that can be obtained through the Commission. These forms can be filed with the Commission without the need for an attorney or accountant.<sup>1</sup>

Public’s Ex. 3 at p. 2. Mr. Rutter opined that Switzco meets the requirements for a Small U filing, is able to use the Commission’s Small U rate change application, and could have submitted a Small U filing to change its rates. He testified that doing so would effectuate the Commission’s purpose for the Small U filing process by allowing Switzco to change its rates without incurring all the expense associated with filing a rate case.

Mr. Rutter testified upon the unreasonableness of Petitioner’s request to recover \$230,500 in this Cause from ratepayers for rate case expenses. He stated Petitioner is requesting an annual amortization increase attributable to these expenses of \$35,944. Given Switzco’s relatively small customer base, Mr. Rutter testified this amount of rate case expense will result in each customer paying \$89.24 per year or \$7.44 per month for five years attributable to rate case expense. This level of rate case expense represents 59% of Petitioner’s original requested increase; consequently, more than half of Petitioner’s proposed revenue increase is attributable to its rate case expense which Mr. Rutter opined could have been minimized if Switzco had pursued rate relief as a Small U filing.

Mr. Rutter testified that in response to an OUCC DR, Petitioner provided invoiced rate case expense through August 31, 2018, of \$72,418. He estimated an additional 65% or \$47,072 for rate case expense through the end of this proceeding, for a total recommended rate case expense of \$120,000. Mr. Rutter testified the estimated rate case expense of \$120,000 should cover Petitioner’s remaining rate case expense, including preparation and filing of any rebuttal testimony, witness preparation for the evidentiary hearing, attendance and testifying at the evidentiary hearing, and preparation of a proposed order. Mr. Rutter recommended the Commission reduce the amount to be included in rates by 50% to \$60,000, thereby resulting in rate case expense being shared equally between Switzco’s ratepayers and shareholders. He stated the reduction is based on his recommendation that when a small utility, as defined in 170 IAC 14-1-1(h), chooses to not seek rate

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<sup>1</sup> IURC Small Utility Filing Brochure, [https://www.in.gov/iurc/files/Small\\_UTILITY\\_Filing\\_Brochure\(1\).pdf](https://www.in.gov/iurc/files/Small_UTILITY_Filing_Brochure(1).pdf), accessed 9/25/2018 (Public’s Ex. 3, Attachment ETR-1, pp. 1-4).

relief using a Small U filing, it should only collect 50% of the incurred or reasonably estimated rate case expense from its ratepayers.

Mr. Rutter also recommended that if new rates have not gone into effect in five years after the final Order is approved in this Cause, Petitioner be ordered to submit a revised tariff showing a reduction in its rates to eliminate this amortization.

**D. Leon A. Golden.** Mr. Golden offered testimony on Petitioner's rate base, providing his analysis of Petitioner's proposed rate base calculations and its adjustments to depreciation expense. Mr. Golden testified that Switzco had not proposed changes in its depreciation rates from those the Commission previously accepted. He testified that he was able to tie Switzco's test year depreciation expense found in its schedules with its income statement and recommended a smaller decrease in Petitioner's depreciation expense due to a truck loan Ms. Gordon identified that was not recorded on Petitioner's financial statements. Mr. Golden's final adjustment to depreciation expense is a decrease of \$518.

With regard to Petitioner's rate base calculation, Mr. Golden testified that he confirmed Petitioner's financial statements tied with its proposed total utility plant in service. He did not agree with the amount Switzco proposed for total utility plant in service due to the removal of the Belterra main. He referenced Ms. Gordon's testimony indicating the Belterra note payable which was not included in Petitioner's proposed capital structure. Mr. Golden stated the absence of the Belterra note payable from capital structure resulted in a rate base greater than the capital used to fund the rate base; therefore, he added the Belterra main back into rate base. In addition, Mr. Golden added the truck to Petitioner's rate base that was associated with the loan Ms. Gordon described. He also proposed a different amount for accumulated depreciation based on removal of accumulated depreciation for the Belterra main. Mr. Golden agreed with Switzco's methodology of calculating working capital but proposed an adjustment to working capital based on the adjustments made to operation and maintenance ("O&M") expense by OUCC witnesses Gordon, Larsen, and Rutter. Mr. Golden testified that Petitioner does not keep an inventory of materials and supplies and did not include an adjustment for materials and supplies. He agreed with this approach. Taking into account the foregoing adjustments, Mr. Golden calculated a total original cost rate base of \$1,805,494.

**E. Bradley E. Lorton.** Mr. Lorton testified regarding the cost of common equity capital, also referred to as the authorized return on equity ("ROE"). Mr. Lorton stated that based on the results of the Discounted Cash Flow ("DCF") method and Capital Asset Pricing Model ("CAPM"), a cost of equity of 9.1% is reasonable and an appropriate ROE for Petitioner. He testified that neither his DCF nor CAPM analysis yielded a return near Switzco's current 9.9% ROE nor Petitioner's proposed 10.25% cost of equity. He testified Petitioner's proposed 10.25% cost of equity is too high. He presented data from S&P Global Market Intelligence showing a decline in the average authorized ROE since 1990 for natural gas companies in the United States. Mr. Lorton testified the average ROE for natural gas utilities in 2017 was 9.72%, and the quarterly averages were below 10% in all but two quarters since the first quarter of 2014.

Mr. Lorton testified a 9.1% ROE is reasonable for Switzco. His DCF result was 9.1%, while his CAPM result was 7.36%. Because Petitioner's stock is not listed, Mr. Lorton established a proxy group for these analyses using the following entities: Atmos Energy Corporation; Chesapeake Utilities; New Jersey Resource Corporation; South Jersey Industries; Southwest Gas Corporation; Spire, Incorporated; and UGI Corporation. He used Duff & Phelps normalized risk free rate of 3.5%

in his CAPM calculations as it remained higher than current long-term bond yields. Mr. Lorton stated the sum of the Duff & Phelps normalized risk free rate and normalized risk premium produced a market rate of return of 8.5%. He also used a growth rate considerably higher than Value Line's forecasts in his DCF analysis. With these factors, he stated current trends do not justify a higher ROE. Mr. Lorton opined that macroeconomic considerations such as long-term interest rates and inflation also do not support an increased ROE. Mr. Lorton cited the testimony of OUCC witness Reed as elaborating on macroeconomic trends. He also cited the *Duke University CFO Magazine Business Outlook Survey* result of S&P 500 stocks over the next ten years yielding only a 6.34% average return.

Mr. Lorton compared Switzco's proposed ROE to those authorized for other natural gas utilities in 2017 as published by the Regulatory Research Associates in *Regulatory Focus* in January 2018. He testified the authorized ROE for 18 of the 24 utilities listed was below 10%, and 14 had an authorized ROE between 8.7% and 9.6%.

Mr. Lorton described the "Constant Growth" DCF model used in his analysis. He stated the underlying principle of the DCF model is that the price of a firm's stock reflects the expected cash flows (i.e. dividends) associated with that stock, discounted at a rate equal to the cost of equity. Mr. Lorton stated the DCF model, when combined with reasonable judgment, provides a realistic and reliable method of estimating a utility's cost of equity. He testified that most of the controversy associated with DCF calculations focuses on the growth rate, but a reasonable growth rate estimate can be developed by evaluating variables such as dividends, earnings, and book value per share. Mr. Lorton stated the forward dividend yield calculation adjusted current dividend yield to reflect likely dividend growth in the subsequent year. This was accomplished by increasing the current dividend yield for one-half of a year's growth in dividends. This is known as the "half-year method."

Mr. Lorton stated he used the half-year method in his DCF analysis to convert current dividend yields to forward dividend yields, and this method has been recognized by the Commission as valid and reasonable. His calculation yielded a 2.6% forward dividend yield for the Gas Utility Proxy Group which, based on Mr. Lorton's comparison, equaled the average of the Value Line dividend yields for the same group. Mr. Lorton testified 6.5% is a reasonable growth rate for the Gas Utility Proxy Group. This growth rate resulted from analyzing both historical and projected earnings per share ("EPS"), dividends per share ("DPS"), and book value per share ("BPS") growth rates for the proxy group, along with long-term economic growth historical data from the St. Louis Federal Reserve Bank. Mr. Lorton stated that 6.5% is above the average economic growth rate since 1980.

Mr. Lorton calculated a 7.36% CAPM cost of equity. He did not include an additional risk premium for small stocks in his calculation because Switzco is a regulated utility. He stated the applicability of a small stock adjustment to regulated public utilities is questionable and opined that regulation reduces the financial risks Petitioner faces. In support of his position, Mr. Lorton cited the *Utility Stock and the Size Effect: An Empirical Analysis* as well as *Do Smaller Companies Warrant a Higher Discount Rate for Risk?: The "Size Effect" Debate*, and he quoted two Commission Orders, including the Order in Cause No. 43680 dated April 30, 2010, in which the Commission, according to Mr. Lorton, rejected a proposed premium adjustment based on size. Mr. Lorton testified the Commission rejected that petitioner's equity size premium adjustment because it could not be directly applied to regulated water utilities that do not experience the same risks as

other small companies. Mr. Lorton stated the same principle could be applied to regulated natural gas companies.

**F. Jennifer L. Reed.** Ms. Reed testified on macroeconomic factors, including interest rates, economic growth, and inflation. She reviewed the macroeconomic factors and trends that influence ROE. Her testimony upon macroeconomic trends supported OUCC witness Lorton's recommendation of 9.1% as a reasonable ROE for Switzco as compared to Mr. Ridlen's recommended 10.25%.

Ms. Reed reviewed three macroeconomic variables influencing the cost of equity capital. First, she examined interest rates. She testified that interest rates on 5-year, 10-year, 20-year, and 30-year Treasury bonds remain low by historical standards, and recent increases have been modest. According to Ms. Reed, U.S. Treasury Bonds have commonly been used to establish the risk-free rate of return in the CAPM and other risk premium analyses. She stated that changes in the bond yields and interest rates affect investor expectations. Ms. Reed testified that lower yields have occurred for the past two decades, and at the end of September 2018, long-term bond yields remained comparatively low.

Second, Ms. Reed examined economic growth trends. She stated the Congressional Budget Office forecasts real Gross Domestic Product growth over the next ten years to range from 3.3% in 2018, declining to 2.4% in 2019, 1.8% in 2020, 1.5% for 2021-2022, and 1.7% for 2023-2028. Ms. Reed opined that these projections do not point to a period of high inflation and large interest rate increases. Her analysis of recent data indicates the U.S. economy is in a mature recovery. She stated that for calendar year 2017, the economy experienced a real annual growth rate of 2.6% (U.S. Department of Commerce, Bureau of Economic Analysis).

Third, Ms. Reed testified the economy remains in a relatively low inflation period, with the Federal Reserve still aiming to increase overall inflation to a sustainable 2% level. Ms. Reed acknowledged the Federal Reserve has increased the federal funds borrowing rate seven times in the last two years, but in her opinion, this trend does not translate to increased bond yields. Ms. Reed stated the overall Consumer Price Index has remained at 2.1% for the past two years, and the Federal Reserve Bank of Philadelphia is projecting core inflation at 2.3% in 2018 and 2.4% in 2019. Ms. Reed testified that her research and analysis show inflation remains low by historical standards, and low inflation rates support lower interest rates and lower cost of financing for capital investment, including utility plant investments.

Ms. Reed acknowledged that real economic growth has occurred since Petitioner's last base rate case when a return on equity for Switzco was set at 9.9%, but she does not believe this economic growth translates into a higher return on equity. She stated Switzco's proposed 10.25% ROE far exceeds market expectations. Ultimately, Ms. Reed concluded that Mr. Lorton's recommended 9.1% ROE is reasonable given current economic conditions.

**G. Brien R. Krieger.** Mr. Krieger testified regarding Petitioner's cost of service study ("COSS"), proposed rate design, and monthly customer charge. Mr. Krieger did not object to Switzco's COSS, but he disagreed with one of the proposed customer charges in Switzco's proposed rate design. Specifically, he recommended the residential rate monthly customer charge be set at \$12.00 instead of \$13.00 as Petitioner proposed.

Mr. Krieger testified Petitioner's most recent COSS prior to this proceeding was performed in Cause No. 42844 (IURC Order August 31, 2005). He stated the COSS in Cause No. 42844 focused on reducing subsidies between the two rate classes at that time. Subsidies were reduced 50% with approximately \$11,000 in subsidy paid by Rate 2 – Large C&I to Rate 1 – General Service which was predominantly residential customers. Subsequently, in Cause No. 43897 U (IURC Order January 5, 2011), Mr. Krieger testified the rate increase was applied across the board without a COSS. In Cause No. 44293 (IURC Order May 15, 2013), he stated no COSS was performed, and the parties reached a settlement that resulted in Rate 1 – General Service being responsible for 58% of the authorized increase. Mr. Krieger testified that Rate 1 – General Service was split into two rates, Rate IR-Residential and Rate 1G-General Service, with both having the same customer charge and volumetric charge.

Mr. Krieger pointed out the COSS similarities between Cause No. 42844 and this Cause. He testified the allocation percentages, or assigned rate class responsibility, for FERC 376 – Distribution Mains are almost identical for the COSS in this Cause and the COSS performed in 2005. Both Causes divide FERC Account 376 – Distribution Mains, with approximately 85% allocated to peak demand and 15% allocated on rate class number of customers. Mr. Krieger stated that allocating 85% of distribution mains with peak demand is a strong weighting towards heat-sensitive loads and represents the vast majority of Petitioner's customers – residential and the hotel/casino. Residential and General Service customer counts are approximately equal in Cause No. 42844 (98.6%) and in this proceeding (97.8%). Also, in this Cause, peak demands are almost equal for Rate 1 (49.8%) and Rate 2 (50.2%). Mr. Krieger stated Rate 2 is only 2% of the customer count and is 67% of the total annual volume throughput, with Belterra being more than half of Rate 2's annual throughput. He agreed with Switzco's COSS allocation method for distribution mains. Mr. Krieger also did not contest Petitioner's allocation of Services, Meters, General Plant/Intangibles, and O&M because it assigns a reasonable share to the responsible rate classes and is similar to the methods and percentages in Cause No. 42844.

Mr. Krieger testified Petitioner is proposing a total margin increase of 15.46% (Petitioner's Exhibit KAH-5) with a 22.04% rate increase for Rate 1R/1G and an 8.60% rate increase for Rate 2. He testified that Mr. Heid did not change the subsidy dollar magnitude in Switzco's existing rates, but the percent subsidy of each rate (paid or received) was reduced because all margin costs have increased. Mr. Krieger recommended the Commission accept Petitioner's COSS as a basis for determining class revenue requirements.

Mr. Krieger disagreed with Petitioner's proposed residential monthly customer charge increase from \$10.86 to \$13.00. He testified a \$12.00 per month customer charge for Rate 1R customers is more appropriate. Mr. Krieger stated that his analysis showed the proposed residential monthly charge of \$13.00 is greater than three similar Indiana natural gas utilities. He also testified there are three large Indiana natural gas utilities (Citizens Gas, Vectren North, and Vectren South) that have residential customer charges of \$12.00 per month or less. In addition, Mr. Krieger testified that Switzco's requested 19.7% increase to its residential class and small general service monthly customer charge is substantially greater than the OUCC's recommended overall rate increase of approximately 3.33%. Mr. Krieger stated Switzco did not provide revised tariff sheets in its case-in-chief and recommended the OUCC have an opportunity to review Petitioner's revised tariffs before Switzco's new rates are implemented.

**6. Switzco's Rebuttal.**

**A. Bonnie J. Mann.** In her rebuttal testimony, Ms. Mann addressed the testimony and exhibits of OUCC witnesses Gordon, Larsen, Golden, and Rutter. Turning to OUCC witness Gordon, Ms. Mann noted the OUCC made two adjustments related to the estimated cost of natural gas for purposes of the revenue requirement. With respect to the cost of unaccounted for gas, Ms. Mann stated the OUCC used more recent data. Since new information became available, and Petitioner's rates are to be in place for a long period of time, Ms. Mann agreed with using this newer information and accepted the OUCC's adjustment. However, with respect to the second OUCC adjustment related to the estimated cost of gas, Ms. Mann testified the actual cost of gas as reflected on NYMEX Futures has increased above the price Petitioner estimated and used in its direct case. She testified that since this element of the revenue requirement is based on an estimate of costs, the OUCC should have recognized the new NYMEX information and, at a minimum, not reduced Switzco's estimated cost of gas.

Ms. Mann next reviewed the OUCC's adjustment described as "miscellaneous expenses." Initially, Ms. Mann addressed the OUCC's adjustment reducing outside services within the test year that the OUCC believed were related to rate case preparation in this Cause. Ms. Mann stated Switzco incurred the expenses at issue when reducing its tariff in 2017; therefore, these expenses should not be eliminated. Ms. Mann also testified the OUCC reduced miscellaneous expenses by \$269 based on mischaracterizing advertising expenses. She testified the disputed expenses were for advertisements in a local newspaper advising customers they should "call before you dig," and were, therefore, safety-related. She opposed this OUCC adjustment.

Ms. Mann also addressed OUCC witness Gordon's change to the date of the capital structure Petitioner used in its case-in-chief. Switzco proposed December 31, 2017. The OUCC proposed September 30, 2017, indicating there is no precedent supporting Petitioner's proposed use of a different date than the test year date. In her rebuttal, Ms. Mann disagreed, testifying that a different date was used for the capital structure in filings before the Commission in Cause Nos. 44768 and 44062. She noted both of those cases were litigated. Ms. Mann testified that Petitioner used December 31, 2017, in this Cause to accommodate the OUCC's recent positions in tax investigation proceedings. She stated that deferred taxes are part of the capital structure, and if Petitioner had used the capital structure as of September 30, 2017, Switzco would have been using deferred taxes in an amount and at a tax rate that will not exist going forward. As such, she stated Switzco believes the appropriate date for the capital structure is December 31, 2017, in keeping with changes in the federal income tax rate.

Ms. Mann next addressed OUCC witness Gordon's adjustment to add elements to the capital structure. She testified that Ms. Gordon believes new debt existed for the purchase of a truck that should be reflected in the capital structure. Ms. Mann testified, however, that the truck debt was already included in Petitioner's capital structure as originally filed. She clarified that when this debt was issued in September 2017, it was included in a general ledger account that included other debt. Between September and December, Switzco moved the truck debt into a new account to make the loan easier to track. As a result, Ms. Mann stated the debt balance included in the capital structure did not omit the new truck related debt.

Ms. Mann testified that the final capital structure adjustment Ms. Gordon presented relates to the note with Belterra. Ms. Gordon proposed the Belterra note be included in the capital structure.

Ms. Mann testified that historically the value of the plant built with that note was removed from Petitioner's rate base. Petitioner's capital structure currently does not include the Belterra note or the related Belterra main. Ms. Mann testified the OUCC's position in this Cause is problematic because it reverses a capital structure and rate base arrangement that Switzco and the OUCC initially agreed upon more than ten years ago that has been used in all of Petitioner's base rate proceedings since 2005. The treatment of the Belterra note and the underlying utility plant in service was part of a settlement agreement that Petitioner, the OUCC, and Belterra reached and the Commission accepted in 2005 in Cause No. 42844. Ms. Mann testified Petitioner filed its next base rate case in 2010 (Cause No. 43897 U, IURC Order January 5, 2011) in which a settlement was again reached excluding the Belterra note and the underlying utility plant. She testified Switzco filed its next base rate case in 2012 which was also settled with no changes to either capital structure or rate base. After multiple settled cases in which neither the capital structure nor rate base was changed, Ms. Mann testified Petitioner rejects the adjustments Ms. Gordon is proposing in its capital structure and rate base. The Commission's 2005 Order in Cause No. 42844 put in place the capital structure methodology Petitioner is still using, and Ms. Mann stated Petitioner is unsure why the OUCC is now changing its long-standing position.

Ms. Mann also disagreed with OUCC witness Larsen's reduced payroll. She rejected Ms. Larsen's payroll reduction for bonuses. She also rejected Ms. Larsen's reduction in salary and related expense increases that Ms. Larsen based on Board approval occurring during a meeting on October 2, 2018, two days after the end of Petitioner's test year cut-off. With respect to the portions of the payroll described as bonuses, Ms. Mann testified that for this small utility to keep good employees and provide quality utility service, Switzco provides various benefits, one of which is a bonus at Christmas for its three full-time employees. She stated the OUCC's adjustment would eliminate an important employee benefit because Petitioner characterized this as a bonus. Ms. Mann stated the cost of losing employees is high in time and dollars, and it is in the best interest of Petitioner and its customers to retain current employees. She stated Petitioner believes this compensation is a payroll expense, though characterized as a bonus, and should be kept in Petitioner's payroll calculation. Petitioner's employees expect these payments, and in essence, these payments are part of their overall benefits. Importantly, like other employee benefits Petitioner offers, eliminating this benefit could create significant problems for Petitioner in retaining its employees, as evidenced by the employee resignation that led to the Board of Directors holding an emergency meeting on October 2, 2018, and increasing employees' pay. Ms. Mann testified the loss of one employee left Switzco without field coverage if the remaining field employee was sick, on vacation, or multiple service calls occurred. This led the Board to learn it will cost \$8,000 per week to replace that employee through a contractor. Ms. Mann testified the total salary increases in pay and the flow through effect to the benefits require an additional \$25,000 annually in payroll and additional payroll tax and retirement contributions. In contrast, Ms. Mann stated the net operating income the OUCC recommends is \$47,484, which means that to provide the additional payroll expense needed to maintain its employees will require Petitioner to absorb 62% of its earnings to cover this additional operating expense. In Ms. Mann's opinion, this is not a sustainable position for Petitioner going forward; therefore, Ms. Mann testified it is much more efficient and less expensive to recognize the Board's emergency approval of a pay increase is a unique situation. She recommended the OUCC's payroll adjustment be rejected and that dollars be provided in Switzco's revenue requirement to cover benefits and increased payroll.

Ms. Mann also addressed Ms. Larsen's suggestion that health insurance be adjusted downward because one employee's health insurance contribution was \$262.50 per year, not \$300.

Ms. Mann testified that as of January 1, 2018, the particular employee Ms. Larsen referenced was actually receiving \$300 due to increased health insurance costs. As such, Ms. Mann rejected the OUCC's proposed downward adjustment.

Ms. Mann stated that because of Petitioner's disagreement with the OUCC's payroll adjustments, Petitioner also disagrees with the OUCC's adjustment to payroll tax which is a flow through based upon the amount of payroll included in the revenue requirement.

Ms. Mann also addressed the adjustments OUCC witness Golden proposed to utility plant. Specifically, Mr. Golden proposed to add a truck to Petitioner's rate base. Ms. Mann testified the truck Mr. Golden added was already included in utility plant and rate base. A second proposed OUCC adjustment was to remove certain negative amounts related to the utility plant associated with the Belterra note. Ms. Mann stated this adjustment to rate base changes the methodology Petitioner used—and the Commission approved—to establish rate base in Cause Nos. 42844, 43897 U, and 44293. She was critical of Mr. Golden changing this methodology without explaining the rationale for this change, and she testified this should be rejected.

Ms. Mann addressed OUCC witness Rutter's testimony which focused on Petitioner's rate case expense and encouraged use of a Small U filing. She stated that Mr. Rutter calculated rate case expense based on a multiplier but did not explain how he knows his suggested 65% multiplier is adequate. With respect to rate case expense, Ms. Mann stated that in recently filed settlement testimony in Cause No. 45116 the petitioner in that Cause and the OUCC agreed to rate case expense of \$137,500. She testified that in a fully litigated small gas utility rate case for Midwest Natural Gas, Cause No. 44880 litigated in 2017, the Commission found \$260,000 in rate case expense to be reasonable and stated Petitioner's requested rate case expense of \$230,000 is less; therefore, Ms. Mann testified the OUCC's rate case expense adjustment should be rejected. We note that in responding to the Docket Entry of December 12, 2018, and follow up questions during the hearing, Switzco's estimated rate case expense was reduced to \$171,426 based on estimates Ms. Mann compiled in response to the Docket Entry.

Ms. Mann also addressed Mr. Rutter's testimony suggesting Switzco should have used the Small U filing process and, thereby, incurred less rate case expense. She stated this proceeding required a COSS to be filed and ultimately required Petitioner to address testimony from seven OUCC witnesses whose testimony included an adjustment to Petitioner's capital structure and a separate adjustment to Petitioner's rate base that diverged from Switzco's last three base rate cases. She further stated the OUCC's downward adjustments to Petitioner's payroll evidenced a refusal to acknowledge that Switzco's Board of Directors needed to boost Petitioner's payroll to retain its employees. The OUCC rejected this payroll adjustment because the Board's action fell two days outside the 365 day window for changes to the test year. Ms. Mann testified the OUCC did not work with this small gas utility to determine the best possible outcome, instead rejecting the payroll increase needed to retain its employees. Ms. Mann also stated that Petitioner, whose owners are not-for-profit entities,<sup>2</sup> is currently authorized a return on equity of 9.9%, but Switzco faces an adjustment from the OUCC that will drive its return down to 9.1%. Ms. Mann stated Petitioner is

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<sup>2</sup> Ms. Mann identified Petitioner's shareholders/owners as the Town of Vevay, the Vevay/Switzerland County Foundation, and the Kiwanis Club of Vevay. She testified these are not deep pocket shareholders that are able to cover losses created by Petitioner's inability to recover its reasonable costs to operate.

not opposed to prospectively using a Small U filing, but nothing in the way the OUCC handled this rate case indicates that filing will be less expensive.

Ms. Mann concluded her rebuttal testimony by sharing revised revenue requirements identified as Exhibit BJM-1R. She identified the OUCC adjustments Petitioner agrees with, stating Petitioner accepts the OUCC's adjustments related to the adjustment of revenue for changes in the NOAA weather normals, a decrease in the estimated rate of unaccounted for gas, an update to the IURC rate used and the use of bad debts as an offset of revenue in that calculation, miscellaneous expenses for charitable contributions, \$115 in advertising expenses, and property tax expense. Ms. Mann testified Petitioner also agrees with the OUCC's methodology for calculating URT taxes, payroll taxes, state income taxes, federal income taxes, and the working capital portion of rate base. Ms. Mann testified that Petitioner rejects the OUCC's adjustments related to payroll, pension, health insurance, rate case expense, the estimated price of natural gas, miscellaneous expenses related to compliance filings, advertising expenses for safety advertisements in print media, depreciation, the calculation of utility plant in rate base, the date of the capital structure, return on common equity, and the value of debt in the capital structure. Based on the updated schedules Petitioner provided in response to the Docket Entry issued on December 12, 2018, Petitioner now proposes an increase in its rates of 7.22%, which will provide Petitioner increased revenue of \$78,532 and the opportunity to earn a net operating income of \$67,315.

**B. Earl L. Ridlen, III.** In his rebuttal testimony, Mr. Ridlen addressed the OUCC witnesses' recommendations on ROE, use of a Small U filing, and Petitioner's capital structure and rate base. He testified Switzco is currently authorized a 9.9% return on equity, and he believes 10.25% is a reasonable return. Petitioner's current revenue requirement, which includes a 9.9% return, was established in a Small U filing, Cause No. 43897 U. According to Mr. Ridlen, while Petitioner was obtaining a 9.9% return on equity, other small gas utilities were obtaining a 10.1% return on equity. Mr. Ridlen opined that if the OUCC wants small utilities like Petitioner to use the Small U filing, the OUCC should recommend a ROE that is comparable to what other small gas utilities are authorized. Mr. Ridlen stated that Community Natural Gas Company, Inc. (Cause No. 44768), and Midwest Natural Gas Corporation (Cause No. 44880), in fully litigated proceedings, were authorized a return on equity in 2017 of 10% and 10.1%, respectively, which is higher than the OUCC is proposing in this proceeding. He testified Community Natural Gas Company, Inc. and Midwest Natural Gas Corporation were proceedings this Commission decided, not Commissions in other jurisdictions. Further, both cases were decided before Petitioner filed this base rate case. In Mr. Ridlen's opinion, it is inappropriate for the OUCC to propose a ROE that is significantly lower than what similar small gas utilities were authorized. Mr. Ridlen stated the economy has improved significantly since Petitioner's current ROE was established.

Mr. Ridlen identified risks associated with Petitioner that have increased since the Commission last considered a ROE for Switzco. He testified these risks include regulatory risks, the risks associated with serving one very large customer, Petitioner's stock not being listed and being divided among non-profit organizations, and Petitioner's size. With respect to regulatory risks, Mr. Ridlen testified the OUCC is not recognizing the difficulty Petitioner faces because of the TCJA, which raised Switzco's federal income tax rate and the Commission's decision relative to the Petitioner in Cause No. 45032.

Mr. Ridlen also addressed why a Small U filing would not have worked in lieu of this proceeding. He testified the OUCC inappropriately recommended a reduced ROE from what is

currently authorized, a change to Petitioner's capital structure methodology from what is being used, a change in the rate base methodology currently being used, and failed to recognize the limited staff Petitioner employs and the associated unique issues this creates. Mr. Ridlen testified that Petitioner needs the assistance of accountants, engineers, and attorneys to seek and obtain the necessary increase in its revenue regardless of the type of filing made. He stated the Commission's brochure on Small U filings suggests a Small U filing may be a way to obtain increased revenue but does not mandate this alternative being used.

Mr. Ridlen disagreed with OUCC witnesses Gordon and Golden's proposed change in the methodology used for calculating Petitioner's capital structure and its rate base. He stated the methodology Switzco currently uses has been in place more than ten years. Mr. Ridlen testified the methodology on capital structure and the corresponding rate base was agreed upon by Petitioner, the OUCC, and Belterra, who was an intervenor in the proceeding where this methodology was established. Mr. Ridlen testified the basis for this methodology is, essentially, to provide Petitioner with a reasonable method of calculating its rate base and capital structure. In response to questions at the hearing, Mr. Ridlen testified the OUCC's proposed changes to Petitioner's capital structure and rate base will not provide Switzco with the ability to repay the Belterra note as the Commission previously approved.

**C. Kerry A. Heid.** In his rebuttal testimony, Mr. Heid testified the OUCC accepted the COSS he prepared for Petitioner. He stated the OUCC also agreed to all monthly customer charge proposals for all rates except Rate 1R, which provides service to residential customers. Petitioner proposed Rate 1R be increased to \$13 per customer per month. The OUCC proposed Rate 1R be increased but only to \$12 per month. Mr. Heid stated the OUCC offered no cost support for this proposal. In accepting Petitioner's COSS, according to Mr. Heid, the fixed cost associated with Rate 1R is \$41 per month; therefore, Petitioner's proposed customer charge will only recover 32% of the fixed cost allocated to Rate 1R. Mr. Heid testified the trend in monthly customer charges for gas utilities is actually higher than the \$13 per month Switzco proposes for residential customers under Rate 1R, and the OUCC in numerous cases has supported a higher monthly customer charge for residential customers than what Petitioner is proposing.

Mr. Heid also addressed Mr. Rutter's testimony that a small utility choosing not to use the Small U filing process, that thereafter incurs significant rate case expense, should not be allowed to recover more than 50% of those costs from ratepayers. Mr. Heid stated this is not the first time the OUCC has suggested sharing these expenses. He testified the OUCC first suggested the 50/50 rate case expense sharing in *Kokomo Gas and Fuel Company* (Cause No. 38096) in which the Commission approved an Order on July 29, 1987, and again most recently in *Community Natural Gas Company*, Cause No. 44768 (IURC March 22, 2017). Mr. Heid testified the Commission rejected the OUCC's proposed sharing of rate case expenses and in doing so found this sharing would unfairly disadvantage small utilities that do not have the resources in-house to handle a rate case. Mr. Heid stated that in the prior cases, the Commission found there was no supportive evidence explaining why the proposed split of 50/50 was appropriate. He testified the OUCC has proposed a similar 50/50 sharing in this Cause, and this should be rejected. In addressing the OUCC's suggestion that such a sharing will encourage Petitioner to use a Small U filing, Mr. Heid testified there is nothing that mandates the use of a Small U filing versus a traditional rate case proceeding. Even with a Small U filing, the OUCC's brochure on such a filing indicates the process will not change the standard of review or the utility's burden of proof. In this proceeding, Mr. Heid testified Petitioner faces what he characterized as a number of complex issues raised by seven

OUCC witnesses. Mr. Heid opined that if Petitioner had initiated this matter as a Small U filing, because of all these issues, it is likely the OUCC would have requested a public hearing, and Petitioner would have been required to fully litigate this proceeding.

7. **Commission Discussion and Findings.** Based on the evidence presented, Switzco and the OUCC, while disagreeing upon significant issues, have also resolved many of the issues raised by accepting the other party's position or adjustment. We begin our findings by addressing those issues and then address the outstanding disputed issues.

A. **Agreed Adjustments.** Having reviewed the evidence, the OUCC did not take issue with the following accounting adjustments as originally included in Petitioner's Exhibit No. 1, Exhibit BJM-1:

- GCA revenue
- Revenue relating to a tariff rate decrease
- Other operating revenues
- Property insurance expense
- Bad debt expense
- Tariff change expense
- Outside services.

In rebuttal, Switzco agreed in Petitioner's Exhibit No. 7 with the OUCC's calculation of the following adjustments:

- NOAA average for NTA revenue
- Property tax expense.

Switzco and the OUCC also agreed upon the methodology to be used to calculate the URT, state and federal income taxes, and the proposed rate increase adjustments. We find the evidence presented and discussed above under Sections 4, 5, and 6 supports the above adjustments to Petitioner's test year operating revenues and expenses as agreed.

B. **Small U Filing.** In reviewing Petitioner's rate case expense, we begin with the premise underlying the OUCC's related recommendations — that Switzco should have filed this base rate case using the Small U filing alternative available under 170 IAC 14-1 *et seq.* Having not done so, OUCC witness Rutter recommends only 50% of Switzco's reasonable rate case expense be collected through rates because Petitioner chose to not pursue rate relief as a Small U filing. While Switzco characterizes the OUCC's recommendation as a penalty, the OUCC's position seems instead focused on limiting the impact upon Petitioner's ratepayers from Switzco's original request for \$230,000 in rate case expense (plus \$500 for mailing notices to its customers).

Petitioner is a small utility, having only approximately 700 customers. Based on Mr. Rutter's calculations, if the Commission approves the rate case expense Switzco originally requested, each of Petitioner's customers will pay \$89.24 per year related to rate case expense. The magnitude of this amount for Switzco's ratepayers is troublesome, particularly since Petitioner seems to be an optimal candidate for the Small U filing process yet chose a different path. While we acknowledge Petitioner's position that a fully litigated proceeding was necessitated because of the number and

type of issues the OUCC raised, it is not apparent to us that the issues in this Cause merited the controversy they yielded in this litigated proceeding. We encourage Switzco (and other small utilities) to consider the Small U process in the future. As our brochure explains:

The small utility rate application was established to provide small utilities with an opportunity to increase rates and charges through a less costly regulatory procedure. Under the small utility rate application procedure, a utility completes standard forms that can be obtained through the Commission. These forms can be filed with the Commission without the need for an attorney or accountant.<sup>3</sup>

Because of Petitioner's limited staff, Switzco may need the help of an accountant or other professional(s) for the Small U process, but the Commission's technical staff—and the OUCC's—have the expertise to assist Petitioner with navigating a Small U filing. Further, the rules governing the Small U process are designed to foster collaboration by relaxing ex parte standards. Potentially, only if an impasse is reached, will extensive professional services be needed. Although the Commission will not require Switzco to use this process, it is important Switzco and its Board of Directors understand that the Small U process, unlike this proceeding, enables our staff and the OUCC to work directly with small utilities. This process is designed specifically to help small utilities avoid costly regulatory proceedings. The Small U process encourages, we believe, more amicable dialogue and information exchange than seems to have occurred in this Cause.

Importantly, when Switzco filed this rate case, 59% of the revenue increase Switzco originally requested was attributable to its projected rate case expense totaling \$230,500. Some of this expense was for the COSS the Commission ordered in Cause No. 44293, but based on Petitioner's Exhibit 7, those services were the least costly of the professionals Switzco contracted in this case, ultimately equating to approximately \$33,113. While we decline to order Switzco to prospectively use the Small U process, when the bulk of a utility's requested rate relief, i.e. more than 50%, is needed to cover the expenses to be incurred for the case, the prudence of spending this level of dollars should be carefully evaluated by the utility and the professionals working with that utility. It is unclear to the Commission whether Switzco's Board of Directors understood that for every dollar of increase Petitioner originally requested in this Cause, 59% was earmarked for rate case expense, and only 41% was requested to meet Switzco's increased operational needs. As a small utility with only around 700 customers from whom to recover the amount spent upon this rate case, the Commission is concerned about each customer's amount of this total, to be billed on a monthly basis in addition to the amount that customer otherwise pays for Switzco's services. While we believe Mr. Rutter's rate case expense per customer is inflated because it is grossed-up for taxes, the Commission's calculations produced an annual impact of approximately \$65 per customer. Switzco has the responsibility to efficiently manage and control its costs, and we strongly encourage investigating and taking advantage of the Commission's Small U procedure for Petitioner's next rate case.

C. **Rate Case Expense.** We recognize rate case expense is a cost of doing business, but these expenditures must be prudent and reasonable given the complexity of the issues presented. Petitioner asserts it could not have used the Small U process because “[i]t is not designed

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<sup>3</sup> IURC Small Utility Filing Brochure, [https://www.in.gov/iurc/files/Small\\_UTILITY\\_Filing\\_Brochure\(1\).pdf](https://www.in.gov/iurc/files/Small_UTILITY_Filing_Brochure(1).pdf) (Attachment ETR-1 at pp. 1-4).

for rate cases where controversial issues are raised.” Petitioner’s Proposed Order at p. 12. We are, however, dubious that the issues in this Cause required the controversy they yielded. A small utility’s rate filing may not be the most appropriate matter in which to parse issues out to seven OUCC witnesses. In this proceeding, doing so seemed to exacerbate the number of issues. By the same token, the quantity of accounting errors in Petitioner’s case-in-chief and rebuttal created confusion that would otherwise not have become issues. Parties may certainly disagree, but we encourage handling small utility rate cases with greater communication and collegiality, mindful of the relatively small number of ratepayers who bear the impact of doing otherwise.

The OUCC proposes that Petitioner’s recoverable rate case expense be reduced and recommended rate case expense be shared equally between ratepayers and Petitioner. Setting aside that Petitioner’s owners are three not-for-profit entities, this approach was previously sought by the OUCC in *Kokomo Gas & Fuel Co.*, Cause No. 39086 (IURC July 29, 1987). In *Kokomo Gas*, the Commission rejected this sharing for numerous reasons, noting as we have above, that rate case expense is a cost of doing business for a regulated utility. More recently, in *Community Natural Gas Co., Inc.*, Cause No. 44768 (IURC March 22, 2017) (“44768 Order”), the OUCC again pursued this treatment of rate case expenses, contending rate case expense should be equally shared between ratepayers and shareholders because both parties benefit from the cost increase proposed. In *Community Natural Gas*, the Commission again rejected the OUCC’s proposal. We noted that splitting these costs in this manner unfairly disadvantages small utilities that do not have in-house staff to handle their rate cases. 44768 Order at p. 22. Our position has not changed. Switzco is owned by three not-for-profit entities. Switzco has only three full-time employees, two of whom typically serve in the field. Given the evidence, we reject the premise that Petitioner’s rate case expenses should be shared 50/50 as the OUCC proposes. The recovered expenses must, however, be reasonable.

In this proceeding, Petitioner originally requested \$230,000 in rate case expense. Switzco’s witness Mann claimed this amount was comparable to that approved for other small gas utilities. Specifically, she testified on rebuttal that in *Midwest Natural Gas Corporation*, Cause No 44880 (IURC August 16, 2017) (“44880 Order”) recovery of \$260,000 of rate case expense was approved, and in the settled base rate case for *South Eastern Indiana Natural Gas Company, Inc.*, Cause No. 45027 (IURC October 3, 2018) (“45027 Order”) \$230,000 was approved. Petitioner’s Exhibit No. 5 at p. 10. Importantly, Midwest Natural Gas and South Eastern Indiana Natural Gas both have more than 700 customers. South Eastern Indiana Natural Gas has over twice as many customers as Switzco, 45027 Order at p. 3, and Midwest Natural Gas has approximately 113,895 customers, 44880 Order at p. 2, which equates to almost 20 times the number of customers Switzco has from whom to recover rate case expenses. We find that what is a reasonable level of rate case expense is not a one-size-fits-all measure, i.e., simply because \$230,000 was approved in one case does not make that amount reasonable in another. Based on the record, particularly Mr. Rutter’s testimony, we would be challenged to find the level of rate case expense Petitioner originally proposed is reasonable, given its disproportionate percentage of Switzco’s rate increase request and the issues in this Cause. We find that spending 59% of every dollar requested upon rate case expenses was not shown to be prudent. Fortunately, this request was revised to \$171,426 when Switzco responded to Docket Entry questions on December 18, 2018, Petitioner’s Ex. 7,<sup>4</sup> based on amounts billed through

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<sup>4</sup> Petitioner’s witness Mann provided a revised set of revenue requirement schedules in responding to the Docket Entry that showed a total rate case expense of \$101,000. Petitioner’s Ex. 7, Schedule C-1 at p. 3. We believe this figure is inaccurate. When questioned at the hearing, Ms. Mann testified neither the \$101,000 nor the \$171,426 was the rate case

November 2018 and estimates of the rate case expenses remaining. Though less, this remains a significant amount relative to Petitioner's customer base.

We have previously reviewed the issue of rate case expense that was disproportionately large compared to a utility's customer base. In *Water Service Company of Indiana*, Cause No. 44104, 2013 WL 1345652 (IURC March 27, 2013) ("44104 Order"), the OUCC raised concerns because that petitioner's proposed rate case expense was high given the utility's small size. We held:

[T]he level of rate case expense proposed by the Petitioner is neither prudent nor reasonable for the complexity of the issues presented in this Cause or for a utility with such a small customer base. ... Not all expenditures are prudent and recoverable from ratepayers just because a utility claims to have incurred them. The utility has a responsibility to efficiently manage and control its costs.

44104 Order at p. 25. In another proceeding, the OUCC was critical of the utility's requested rate case expense in part because it was 72% of the annual increase in revenue. *Riverside Water Co.*, Cause No. 42122, 2003 WL 21041242 (IURC February 19, 2003) at p. 7. We face a similar dilemma in this case.

Although Petitioner ballparked an updated expense estimate in responding to the Docket Entry, the support provided was a statement that Barnes & Thornburg, London Witte Group, and Mr. Heid are estimated to each be charging a certain amount. The absence of detailed billing information and the errors in Switzco's accounting exhibits make it challenging to determine the prudence of what Petitioner is ultimately being charged and seeks to recover.<sup>5</sup> Because Switzco demonstrated it has, however, through November 30, 2018, been billed \$107,894 and allocated the remaining estimated \$63,532 based on updated information Ms. Mann gathered from legal counsel and the consultants, we decline the OUCC's recommendation to cap these fees at \$120,000 given the more definitive information Ms. Mann provided. We, therefore, find it acceptable for Petitioner's revenue requirement to include rate case expense of \$171,426, plus an additional \$500 incurred to mail notice to customers, for a total of \$171,926. We do so cautioning Switzco that the absence of more detailed billing information in the future could place a similar request at risk. We also, again, encourage Switzco to consider a Small U filing for future rate relief to alleviate the financial impact of rate case expense on its small customer base.

Petitioner and the OUCC agree that the rate case expense the Commission approves should be amortized over five years. Given the historical frequency of Petitioner's rate filings, we find this amortization is reasonable. The Commission, however, also finds the rate case expense to be amortized, as discussed above, represents significant dollars for Petitioner's ratepayers; consequently, at the conclusion of the five-year amortization period, this amount should be removed from Switzco's rates as the OUCC requests. Accordingly, if by April 17, 2024, new base rates are

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expense being requested, but Petitioner's proposed order uses \$171,426 consistent with Petitioner's Docket Entry responses.

<sup>5</sup> As an example of the errors throughout this proceeding, we note that the schedules Petitioner filed on December 18, 2018, in response to the Docket Entry questions showed a rate case expense for Switzco of \$101,000, which contradicts the detail Petitioner provided in that same filing for rate case expenses billed through November 2018. If the Commission accepted the amount shown in these schedules as accurate, Switzco could be harmed financially.

not in effect as a result of a base rate proceeding filed subsequent to this Order, Switzco shall make a compliance filing at least 30 days prior to said date to remove from rates the amount associated with recovery of the rate case expense approved in this Order.

We remind all parties that very small utilities like Switzco have relatively few customers to bear rate case expense and encourage considering strategies that enable the regulatory process to be navigated in a manner that promotes the utility's health while minimizing the impact on ratepayers. We also encourage collaboration and engagement with the OUCC and the Commission aside from during pending proceedings with the objective of furthering mutual understanding of a small utility's unique issues and challenges.

**D. Cost of Natural Gas.** Petitioner and the OUCC ultimately agreed on the cost of natural gas as it relates to the calculation of unaccounted for gas. Based on their agreement, we find the appropriate percentage of unaccounted for gas to be included in the calculation of the cost of natural gas is 1.58%. The Parties, however, disagree on the appropriate estimate for the cost of natural gas going forward. Petitioner estimated a natural gas cost based on NYMEX futures as of the time this case was initiated. The OUCC proposed to adjust that estimated cost downward due to Petitioner including URT on the estimated cost of gas. OUCC witness Gordon testified, "Indiana URT is collected by utilities on behalf of the consumer; it is not an expense Petitioner would pay on UAFG because no consumer received those Dths." Public's Ex. 1 at p. 8, lines 17-19. On rebuttal, Ms. Mann disagreed with the OUCC's cost estimate on the basis that it does not recognize that NYMEX costs reflect that the cost of gas is actually increasing. Petitioner's workpapers show a weighted average cost of gas of \$3.8295<sup>6</sup> before management and transportation fees.

Public's Ex. CX-1, introduced by the OUCC during cross-examination, shows the cost of gas for April 2019 through November 2019 and during the period of March 2020 through December 2024 is lower than Petitioner's weighted average cost of gas of \$3.8295. Other than Ms. Mann's statement that natural gas prices are going to be higher, Petitioner provided no evidence supporting her statement. Given the evidence, we agree with Ms. Gordon that URT should not be included on the estimated cost of gas since it is not an expense Switzco will incur because no consumer will receive those dekatherms. We also find that Public's Ex. CX-1 demonstrates the cost of gas has actually decreased since Petitioner filed its case-in-chief; therefore, we find the OUCC's estimate for the cost of gas is reasonable, and for purposes of the revenue requirement, the OUCC's estimated cost of natural gas will be used.

**E. Payroll.** The Parties disagreed on the adjustment for payroll to Petitioner's test year. Petitioner initially proposed an adjustment that the OUCC reduced based, in part, on decisions by Switzco's Board of Directors reflected in its May 2017 Minutes, as described in the testimony of OUCC witness Larsen. Ms. Larsen also made an adjustment to decrease payroll for bonuses paid to employees during the year. Notably, Petitioner's Board changed the payroll again at an emergency meeting held on October 2, 2018, to counter the impact of an employee's resignation. On rebuttal, Petitioner demonstrated it will cost \$8,000 per week to hire a contractor to perform the duties of the employee who quit, but for the Board's emergency approval of raises two days outside of the test year adjustment cut-off. Petitioner's rebuttal testimony reflects payroll over the test year should be increased by \$25,000, and this increase should flow through to retirement contribution

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<sup>6</sup> Petitioner's Accounting Workpaper filed on June 27, 2018 – Cost of Gas Summary.

and payroll tax. Petitioner also provided, through its response to the Docket Entry, a payroll analysis showing the annualized payroll that will actually occur as of October 2018.

We first turn our attention to the OUCC's removal of bonuses from payroll. The OUCC provided Switzco's response to an OUCC DR indicating that for calendar year 2017, \$500 plus taxes were paid to Petitioner's full-time employees, and \$250 plus taxes paid for part-time employees. Public's Ex. 2, AEL-1 at p. 3. Although the OUCC asked Petitioner to describe how each of these amounts was derived, it is unclear any metrics must be met other than being a full or part-time employee. In her rebuttal testimony, Ms. Mann stated Petitioner's employees expect these amounts each year. While this alone does not merit the inclusion of these amounts in Petitioner's payroll, we find that under the circumstances presented, the dollars characterized as "bonus" are for Petitioner's employees more akin to being part of what they understand as their overall compensation as opposed to being amounts paid to them above reasonable compensation for their services. We also recognize that Switzco demonstrated a critical need to employ and retain three competent employees to serve its customers, the costs associated with hiring and training new employees or contractors to fulfill these responsibilities, and the reasonableness of the dollars at issue. We are persuaded these amounts are part of overall compensation.

We next examine the payroll increase of \$25,000 that Switzco's Board of Directors approved on October 2, 2018. Ms. Mann testified on rebuttal that the Board's action provided raises sufficient to bring back the employee who resigned and to retain Petitioner's other employees. If the employee did not return, Petitioner projected a cost of \$8,000 per week for a contractor to perform the duties of the employee who quit, at least until a new employee could be secured. Although the Board's approval came two days outside the test year cut-off, the emergency that necessitated this meeting arose during that timeframe and was going to prospectively impact Petitioner's payroll or outside services expenses. In recognition of this timing, we find it preferable to use our discretion and permit limited flexibility from the test year cutoff, given the circumstances, by approving an expense increase that Petitioner demonstrated was required to rehire or retain its employees. Also, given the limited resources of this small utility and our concern about rate case expense, we find it is more prudent to establish Switzco's rates based on Petitioner's fixed, known, and measurable expenses, even if that expense became known just past the cutoff date. We, therefore, find Petitioner's revenue requirement should be increased to provide actual pro forma salaries and wages of \$191,916. This requires an adjustment to the test year of \$27,461.

**F. Retirement Contribution.** The Parties are in agreement upon the methodology to calculate and the inclusion of retirement contributions in Petitioner's revenue requirement. The only issue separating the Parties is the mathematical result that flows from the payroll from which each starts. Based on our findings above on payroll, we find Petitioner's retirement contribution over and above test year should be increased by \$2,746.

**G. Health Insurance.** Petitioner proposed to increase health insurance to recognize the additional costs associated with Petitioner's contribution to the health insurance of its employees. The OUCC reduced the adjustment based upon its belief that Petitioner did not contribute the same amount for health insurance for all its employees. Petitioner's rebuttal evidence demonstrated all employees' contributions are now the same. Based on Petitioner's rebuttal schedules, we find this requires an increase over and above test year expense of \$1,162 and that Petitioner's adjustment is reasonable.

**H. Payroll Tax.** The Parties agreed as to the methodology associated with payroll tax. Given our findings above about payroll, we agree the methodology used by Petitioner and the OUCC should be used in calculating Petitioner's adjustment to test year and find this calculation results in an increase of \$2,101.

**I. IURC Fee.** In calculating the IURC fee rate to be applied to the adjustment, Ms. Gordon stated Petitioner should have removed bad debts from applicable revenues at present rates and used the most recent IURC fee in its calculations. In rebuttal, Petitioner agreed with the OUCC's revenue changes but did not make changes to its IURC fee in its rebuttal schedules. A review of the Commission's form used to calculate the IURC fee shows that bad debt expense should be deducted when performing this calculation. We find the most recently approved IURC fee should be used to calculate the amount to be collected in this Cause; therefore, we accept the OUCC's calculation of the IURC fee, resulting in an adjustment to the test year expenses of \$10.

**J. Miscellaneous Expenses.** The OUCC proposed an adjustment characterized as miscellaneous expenses. In responding to the OUCC's adjustment, Petitioner rejected two categories included within miscellaneous expense as being inappropriate adjustments. The first relates to the OUCC adjustment for outside services. The OUCC believed these dollars were attributable to services performed as part of this rate case, but on rebuttal, Ms. Mann testified the outside services were costs Petitioner incurred to adjust its tariff in accordance with the settlement in Petitioner's last base rate case as opposed to costs incurred for the current proceeding. Public's Ex. 5 at pp. 2-3, lines 21-5. This tariff change was filed on August 29, 2017, as a compliance filing; therefore, we reject this portion of the OUCC's miscellaneous expense adjustment.

The second adjustment the OUCC proposed to miscellaneous expenses is for advertising in the amount of \$269. Petitioner demonstrated this expense was incurred to remind its customers they should "call before you dig" and provided three sample advertisements. The "call before you dig" effort is an important part of pipeline safety; consequently, we find the OUCC's elimination of these expenses is inappropriate. 170 IAC 1-3-3 recognizes the propriety of costs associated with advertising that produces a material benefit for ratepayers such as the safety advertising at issue. We find the appropriate adjustment to Petitioner's test year miscellaneous expenses is a reduction of \$4,802 as reflected in Petitioner's schedules attached to its Docket Entry responses.

**K. Depreciation.** The Parties are in agreement as to the method of calculating depreciation and the percentages to be used relative to total utility plant, transportation equipment, and other depreciable assets. Because we rejected the OUCC's rate base adjustment, we find the depreciation expense adjustment shown on Petitioner's Docket Entry responses is appropriate and will be used in the revenue requirement for Petitioner.

**L. Taxes Other Than Income Taxes.** Consistent with our findings above, we find it is appropriate to increase Petitioner's revenue requirement to recognize the increased payroll Petitioner's Board approved to retain its employees. There are, however, other taxes which the Parties also discussed. With respect to property taxes, Petitioner has agreed with the OUCC's property tax adjustment, and finding it appropriate, that property tax expense adjustment will be included in Petitioner's revenue requirement. With respect to the URT, the Parties are in agreement as to how URT should be calculated, and we will include such methodology as reflected on Petitioner's schedules filed in response to the Docket Entry.

**M. Income Tax.** The Parties are in agreement about the methodology of calculating both state and federal income tax. Petitioner and the OUCC used the same income tax rates. These are the new rates applicable for both federal and state income tax. Based on the evidence, we find the Parties' proposed income tax rates appropriate and will include these tax rates in calculating Petitioner's revenue requirement based on the adjustments detailed above.

**N. Capital Structure.** Switzco and the OUCC disagreed upon matters related to Petitioner's capital structure. Petitioner proposed using a capital structure as of December 31, 2017, which differs from the test year period. Switzco contends that by moving the entire capital structure up to December 31, 2017, it is matching the forward looking operating adjustments for the new income tax rate created by the TCJA to the results of booking those differences into deferred taxes. The OUCC disagreed with this approach, asserting the purpose of the capital structure is to fund rate base, so the dates should align and both be September 30, 2017. Under Cause No. 45032, the Commission ordered all regulated utility companies to begin implementing the federal income tax changes. Such changes will impact a regulated utility's capital structure; therefore, we find Petitioner's justification for using December 31, 2017, is reasonable. The Commission has previously approved a capital structure date that differs from the test year cutoff date,<sup>7</sup> and we find Petitioner has demonstrated the appropriateness of doing so in this proceeding.

Switzco also objects to the OUCC's adjustment of Petitioner's capital structure as originally filed by adding debt related to a service truck and the Belterra note. In her rebuttal testimony, Ms. Mann states the truck debt OUCC witness Gordon identified was issued in September 2017 and not a new debt account in the general ledger in December 2017. Public's Ex. 5 at p. 4. Ms. Mann testified Petitioner moved the debt out of the general ledger account after the debt was issued in September 2017 to make both loans easier to track because the general ledger account included other debt; therefore, the OUCC is, effectively, double counting the debt associated with the truck purchase because the truck is already in the capital structure. We find Petitioner has demonstrated this debt is already included in the capital structure.

With respect to the Belterra note, the evidence shows the Belterra note has been excluded from Petitioner's capital structure since 2005 when doing so was approved in our Order in Cause No. 42844 on August 31, 2005 ("42844 Order"). Although a settlement was approved in the 42844 Order, Switzco's accounting witness on direct and in settlement testimony testified that since the Belterra line extension was customer provided capital, it was inappropriate to include this amount in rate base, and the associated note was excluded from the capital structure. The Parties held to this treatment of the Belterra main and promissory note in two subsequent cases, Cause No. 43897 U and Cause No. 44293. Now, more than 13 years after our 42844 Order, the OUCC seeks alternative treatment. We find the Belterra main has been properly excluded from rate base and the capital structure because Switzco should not earn a return on an investment its customer, Belterra, funded in full. We approved that capital structure in Cause No. 42844, and we find the OUCC has provided no compelling evidence to deviate from the consistency principle of accounting and change today the longstanding ratemaking treatment for the main and note. In so finding, we are also mindful of the impact the OUCC's about-face would have on Switzco. Petitioner has consistently under-earned its authorized net operating income based on the earnings test submitted in its GCA proceedings. If the Commission accepted the OUCC's proposal and included 58% of its capital structure at 0% cost

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<sup>7</sup> See IURC Cause No. 44768 in which the rate base was September 30, 2016, and the capital structure was September 30, 2015 and Cause No. 44062 in which the rate base was June 30, 2011, and the capital structure was March 31, 2011.

(since the note has no interest), we find it would have an unreasonable, adverse impact on Petitioner's rate of return. We are also mindful that the OUCC recommends Petitioner be encouraged to use the Small U procedure. Changes to the capital structure from what was previously justified, approved, and in effect since 2005 do not encourage this alternative. The Commission finds it is not appropriate to change Petitioner's capital structure in this Cause by adding the debt related to the service truck or the Belterra note.<sup>8</sup>

**O. Rate Base.** The OUCC's adjustment to Petitioner's rate base is based on the OUCC's adjustment to Petitioner's capital structure. As discussed above, we reject the OUCC's adjustment to the capital structure and, therefore, also reject the OUCC's adjustment to Petitioner's rate base. We note that Petitioner and the OUCC have both proposed including working capital on the basis of pro forma O&M expenses. We agree that Petitioner's rate base should include working capital and agree with the Parties' methodology in calculating working capital. Working capital is, consequently, included in our rate base finding below. Based on our findings above, including the level of rate case expense to be included in Switzco's revenue requirement, we find Petitioner's fair value rate base is calculated as follows:

Utility Plant in Service as of 9-30-17	\$3,394,460
Less Belterra Main	(\$1,700,592)
Less Accumulated Depreciation	(\$1,659,298)
Accumulated Depreciation – Belterra Main	\$ 822,659
Net Utility Plant in Service	\$ 857,229
Working Capital	\$ 51,757
Total Original Cost Rate Base	\$ 908,986

**P. Cost of Capital/Fair Rate of Return.** The issue between the Parties on the cost of capital is the fair and reasonable return on equity capital to be used in the capital structure and the resulting weighted cost of capital to be used as the fair return on Petitioner's rate base. The Parties seem to agree that the equity return must: (1) be sufficient to attract capital on reasonable terms; (2) allow Petitioner to maintain its financial integrity; and (3) be commensurate with available investments with corresponding risks. Petitioner requests a return on equity of 10.25% and a weighted cost/fair rate of return of 7.42%. The OUCC recommends a return on equity of 9.1% and a weighted cost of capital/fair rate of return of 2.63%. As we consider the evidence, we are cognizant of the wide range of results the Parties' respective analyses and proposals present.

While Mr. Ridlen recommends Switzco's cost of equity be increased to at least 10.25%, he did not perform a DCF analysis or a CAPM analysis for Petitioner. Instead, he stated a return of 10.25% is justified because Switzco's stock is not publicly listed, its service area is not diversified, and it faces regulatory risk that Mr. Ridlen asserts is demonstrated by the Commission's denial of Petitioner's Phase I tariff in Cause No. 45032. Mr. Ridlen also contends Petitioner's cost of equity should be increased from the 9.90% approved in Cause No. 43879 U because interest rates have risen significantly since that rate case; the trend is for continued increases, and the risks associated with Switzco have increased.

<sup>8</sup> We note that as Switzco makes each monthly payment on the Belterra note, Petitioner arguably gains equity in the main, but neither of the Parties proposed to incrementally phase the main into Switzco's ratemaking schedules.

The OUCC, on the other hand, recommends a cost of equity of 9.10% based on its CAPM and DCF models producing results ranging from 7.36% to 9.10%. After reviewing the Parties' evidence, the Commission finds the appropriate cost of equity should fall in the range of costs of equity the Parties provided. The OUCC's recommendation is too low for a utility like Switzco that has demonstrated through its GCA proceedings that it is not earning its authorized net operating income. The Commission finds, given the totality of the evidence provided and weighing the current economic trends and relatively low risk of a regulated gas utility, that a return on equity of 9.90% remains appropriate for Switzco. This is within the range of reasonableness, is comparable to the returns authorized for similarly situated utilities, and allows Petitioner the opportunity to adequately compensate investors, attract capital, maintain its credit rating, and operate a financially sound utility. The inclusion of a 9.90% cost of equity in the capital structure produces a rate of return of 7.19%.

**Q. Pro Forma Revenue Requirement.** Having considered the evidence and based upon our findings above, we find Petitioner's current rates and charges are insufficient to allow Switzco appropriate funds for the safe and reliable operation of the utility and to earn a reasonable return on its investment in utility rate base; consequently, we find Petitioner's pro forma revenue requirement is as illustrated by the following table:

Net Original Cost Rate Base	\$908,986
Fair Rate of Return	7.19%
Authorized Net Operating Income	\$ 65,356
Pro Forma Net Operating Income	\$ (3,494)
Increase in Net Operating Income	\$ 68,850
Required Revenue Increase with Gross Up	\$ 94,619
Percentage Increase Required	17.19% <sup>9</sup>

**R. Cost of Service.** Petitioner's witness Heid sponsored a cost of service study. OUCC witness Krieger acknowledged this cost of service study is acceptable. Mr. Krieger agreed the monthly customer charge should be increased for all classes, but he suggested a lower increase for Rate 1R. We have reviewed the evidence and recognize that under the accepted COSS, the monthly customer charge for Rate 1R will only collect 32% of the actual fixed costs attributable to this rate class. On rebuttal, Mr. Heid stated a reasonable rate design would provide for Switzco to structure its rates to recover a greater portion of its costs through the monthly customer charge. We concur and, therefore, approve Petitioner's proposed cost of service allocations, including increasing its Rate 1R customer charge to \$13 per month.

**S. Customer Deposits.** While the Parties did not dispute the amount of customer deposits included within the capital structure, Ms. Gordon raised concerns with Petitioner's customer deposit policy. She testified that Petitioner requires a \$100 deposit from each

<sup>9</sup> For purposes of calculating the percentage increase of 17.19%, the cost of gas was excluded. In contrast, Petitioner included the cost of gas when making this calculation, so Switzco's requested revenue increase of 7.22% is a percentage of a higher number, thereby appearing to create a lower revenue increase percentage. Petitioner also incorrectly included \$101,000 for rate case expense in Ms. Mann's schedules, whereas consistent with our findings above, the amount of rate case expense is \$171,926. When gas costs are excluded and rate case expense of \$171,926 is included, the revenue increase Petitioner seeks exceeds the pro forma revenue requirement approved.

new customer and does not appear to account for the customer creditworthiness criteria that 170 IAC 5-1-15(b) requires when providing new customers service. Ms. Gordon stated it also does not appear that Switzco allows its customers to make installment payments in compliance with 170 IAC 5-1-15(c)(2)(A). She recommended the Commission require Petitioner to evaluate individual customer's creditworthiness and to provide customers with information regarding deposit installment plans when service is initiated and the deposit is required. She also recommended the Commission conduct its own review to ensure Petitioner is evaluating customer creditworthiness and communicating pertinent information to its customers.

Petitioner provided no rebuttal testimony on these matters and no evidence that it offers installment payments as required for customer deposits over \$70. Compliance with the Commission's rules regarding customer deposits is important; consequently, we find that Switzco shall, within six months of the date this Order is approved, comply with 170 IAC 5-1-15(b) and (c)(2)(A) by evaluating the creditworthiness of those from whom a deposit is being held and return any deposit before the conclusion of said six month period to Petitioner's customers who are creditworthy. In addition, for deposits over \$70, Switzco shall assure installment payments and related information are provided to customers prospectively in compliance with 170 IAC 5-1-15(c)(2)(A). Petitioner shall also make a compliance filing with the Commission revising its customer deposit requirements in compliance with 170 IAC 5-1-15(b) and 170 IAC 5-1-15(c)(2)(A) within 60 days of the date of this Order and provide a copy of the information Petitioner will be sharing with new customers about deposits and deposit installments.

**T. Tariffs.** Petitioner did not provide revised tariffs when filing its case-in-chief ostensibly due to uncertainty upon the impact of the TCJA on its rates. The OUCC requested the opportunity to review Switzco's revised tariffs prior to Commission approval, and Mr. Krieger recommended Petitioner be required to file redlined and clean versions to facilitate this review. Ind. Code § 8-1-2-42.7(b)(9) requires "proposed rate design and pro forma tariff sheets" to be submitted as part of Petitioner's case-in-chief. Accordingly, we find the OUCC's requests reasonable and that Petitioner will be ordered to file redlined and clean versions of its tariff sheets, as requested, and the OUCC will be afforded ten business days after this filing to review these and file any objections to the updated versions under this Cause.

**U. Other Matters.** We recognized above that at the outset of this proceeding, the OUCC filed a motion requesting that rate relief be denied because Petitioner had not filed written notice with the Commission of this base rate case at least 30 days prior to filing this Cause consistent with GAO 2013-5. With the OUCC's motion later withdrawn, we decline to address the propriety of the relief the OUCC originally requested; however, we encourage compliance with GAO 2013-5.

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

1. Petitioner is authorized to increase its rates and charges in accordance with our findings above in order to produce additional revenue exclusive of the cost of gas of \$94,619 beyond that provided by its current rates and charges. This requires an increase in Petitioner's rates of 17.19%

2. Prior to implementing the rates, Petitioner shall file a redlined and clean tariff and applicable rate schedules under this Cause for approval by the Commission's Energy Division. Petitioner shall also serve the OUCC with a copy of said relined and clean tariff and applicable rate schedules, and the OUCC shall file any objection thereto in this Cause within ten business days of said filing. Such rates shall be effective on or after the Order date, subject to the OUCC's potential objection(s) and to Energy Division review and agreement with the amounts reflected.

3. If by April 17, 2024, new base rates are not in effect as a result of a base rate proceeding filed subsequent to this Order, Switzco shall make a compliance filing at least 30 days prior to said date to remove from rates the amount associated with recovery of the rate case expense approved in this Order.

4. Within six months of the date of this Order, Switzco shall comply with 170 IAC 5-1-15(b) and (c)(2)(A) by evaluating the creditworthiness of its customers from whom a deposit is being held and return any deposit before the conclusion of said six month period to Petitioner's customers who are creditworthy. In addition, for deposits over \$70, Switzco shall assure installment payments and related information are provided to customers prospectively in compliance with 170 IAC 5-1-15(c)(2)(A), shall also make a compliance filing with the Commission revising its customer deposit requirements in compliance with 170 IAC 5-1-15(b) and 170 IAC 5-1-15(c)(2)(A) within 60 days of the date of this Order, and shall provide the Commission at that time with a copy of the information Petitioner will be sharing with new customers about deposits and deposit installments.

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

**HUSTON, FREEMAN, KREVDA, OBER, AND ZIEGNER CONCUR:**

**APPROVED:** APR 17 2019

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

*Virginia Bucay acting for Mary Becerra*  
**Mary M. Becerra**  
**Secretary of the Commission**