***OCC EXHIBIT NO.\_\_\_\_\_\_\_\_\_\_***

**BEFORE**

**THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of Aqua )

Ohio, Inc. to Increase Its Rates for Water ) Case No. 13-2124-WW-AIR

Service. )

**TESTIMONY IN OPPOSITION TO THE STIPULATION AND RECOMMENDATION**

**OF**

**STEVEN B. HINES**

**On Behalf of**

**The Office of the Ohio Consumers' Counsel**

*10 West Broad Street, Suite 1800*

*Columbus, Ohio 43215-3485*

**August 4, 2014**

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# I. INTRODUCTION

Q1. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND POSITION.

***A1.*** My name is Steven B. Hines. My business address is 10 West Broad Street, Suite 1800, Columbus, Ohio 43215-3485. I am employed by the Office of the Ohio Consumers’ Counsel (“OCC” or “Consumers’ Counsel”) as a Principal Regulatory Analyst.

***Q2. ARE YOU THE SAME STEVEN HINES WHO PREVIOUSLY FILED DIRECT TESTIMONY IN THIS PROCEEDING?***

***A2.*** Yes.

Q3. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

***A3.*** My testimony, in addition to other OCC witness testimony, explains the reasons why the Public Utilities Commission of Ohio (“PUCO”) should reject the Stipulation and Recommendation (“Stipulation” or “Settlement”) filed in this proceeding on July 21, 2014. The proposed Settlement will result in unjust and unreasonable charges collected from the residential customers of Aqua Ohio, Inc. (“Aqua Ohio” or “the Utility”). As a result, the proposed Stipulation does not represent a fair and reasonable compromise, does not benefit the customers, is not in the public interest, and violates important regulatory principles and practices. Therefore, the proposed Stipulation should not be approved.

# II. EVALUATION OF THE STIPULATION WITH RESPECT TO THE THREE-PRONG TEST USED BY THE PUCO.

***Q4. WHAT CRITERIA DOES THE PUCO USUALLY RELY UPON FOR CONSIDERING WHETHER TO ADOPT A STIPULATION?***

***A4.*** It is my understanding that the PUCO will adopt a Stipulation only if it meets all three of the criteria below. The PUCO must analyze the Stipulation and decide the following:

1. Is the settlement a product of serious bargaining among capable, knowledgeable parties representing diverse interests?
2. Does the settlement, as a package, benefit customers and the public interest?
3. Does the settlement package violate any important regulatory principle or practice?

***Q5. DOES THE STIPULATION FILED IN THIS PROCEEDING MEET THOSE CRITERIA?***

***A5.*** No.The Stipulation fails to meet any of the three criteria considered by the PUCO when evaluating a stipulation, and should therefore be rejected. I address each of the three criteria individually.

***Q6. REGARDING THE FIRST CRITERION, IN YOUR OPINION WAS THE STIPULATION A PRODUCT OF SERIOUS NEGOTIATION AMONG ALL PARTIES REPRESENTING DIVERSE INTERESTS?***

***A6.*** No. The Stipulation was signed by Aqua, the PUCO Staff and the cities of Marion and Tiffin (collectively referred to as “Signatory Parties”). Although Marion and Tiffin were representing approximately 16,000 and 7,000 residential customers respectively, a large portion of Aqua’s residential customers are not represented by the Signatory Parties to the Stipulation. Specifically, there are approximately 28,500 residential customers in the Lake Division, 1,400 residential customers in the Masury Division, and 24,600 residential customers in the former Ohio American Water Division that are not represented by any of the Signatory Parties (See Attachment SBH-A). Thus, about 70% of Aqua’s residential customers’ interests are not represented by the Signatory Parties.[[1]](#footnote-1)

***Q7.*** ***REGARDING THE SECOND STIPULATION CRITERION, DOES THE SETTLEMENT, AS A PACKAGE, BENEFIT CUSTOMERS AND THE PUBLIC INTEREST?***

***A7.*** No, the Stipulation violates the second criteria in several respects. Below, I will individually set forth each specific reason supporting this answer.

***Q8. WHAT IS THE FIRST ISSUE YOU ADDRESS WITH REGARD TO THE SECOND CRITERIA?***

***A8.*** The first issue I address is the plant allocation factor used to assign Service Center Plant costs to the Aqua Divisions in Ohio.

***Q9.*** ***WHAT SERVICE CENTER PLANT ALLOCATOR IS USED IN THE STIPULATION?***

***A9.*** The Stipulation is using a plant allocator of 63.00% to allocate Service Center Plant costs at issue in this case among the Aqua Divisions in Ohio.[[2]](#footnote-2)

***Q10. HOW WAS THIS ALLOCATION FACTOR DETERMINED?***

***A10.*** According to Application Workpaper WPB-7.1, the amount of Utility Plant in Service, Depreciation Reserve, Construction Work In Progress, Customers’ Advances for Construction, Related Facilities, Contributions in Aid of Construction, and Deferred Accounts for the Total Company and the Rate Area are summed individually and then divided by each other to arrive at the Service Center Plant Allocation Factor.[[3]](#footnote-3)

***Q11. SHOULD THE 63% ALLOCATION FACTOR BE USED TO ALLOCATE SERVICE CENTER RATE BASE TO THE AQUA DIVISIONS AT ISSUE IN THIS CASE?***

***A11.*** No. In the calculation of the 63.00% plant allocation factor set forth in Application Workpaper WPB-7.1, the entire amount for the Deferred Accounts in is not included. According to Application Schedule B-6, the total of Deferred Accounts carried forward to Application Schedule B-1 is $(10,009,497.00) and not $(7,821,296.42). Recalculating Application Workpaper WPB-7.1 would yield a plant allocation factor 62.04%.[[4]](#footnote-4)

***Q12.*** ***WHAT IS THE EFFECT OF THIS CHANGE IN ALLOCATION FACTOR ON THE PLANT, DEPRECIATION RESERVE, OTHER RATE BASE ITEMS AND DEPRECIATION EXPENSE PROPOSED IN THE STIPULATION?***

***A12.*** Using a plant allocation factor of 62.04% would result in the following adjustments: the stipulated Gross Plant would decrease from $10,766,843 to $10,587,448; the stipulated Depreciation Reserve would decrease from $3,871,212 to $3,799,332; the stipulated Other Rate Base Items would decrease from $480,184 to $472,867 (See Schedule SBH-2); and the stipulated Depreciation Expense would decrease from $969,184 to $952,555.[[5]](#footnote-5) I have also made an adjustment to reduce Property Tax Expense by $6,512.[[6]](#footnote-6)

***Q13.*** ***WHY DOES THE PLANT ALLOCATION FACTOR PROPOSED IN THE STIPULATION NOT BENEFIT CUSTOMERS AND IS NOT IN THE PUBLIC INTEREST?***

***A13.*** In calculating the plant allocation factor, the Stipulation neglects to include the amounts in all of the Deferred Accounts. Hence, the 63.00% plant allocation factor used in the Stipulation fails to reduce rate base by an additional $100,198[[7]](#footnote-7) and fails to reduce expenses by an additional $23,141.[[8]](#footnote-8) This error results in higher rates; therefore, it does not benefit customers and is not in the public interest.

***Q14.*** ***WHAT IS THE SECOND ISSUE YOU ADDRESS WITH REGARD TO THE SECOND CRITERIA?***

***A14.*** The second issue I address is the amount of rate case expense included in Stipulation Joint Exhibit 2.0.

***Q15.*** ***DOES THE STIPULATION INCLUDE RATE CASE EXPENSE?***

***A15.*** Yes. On Stipulation Schedule C-3.6 there is an estimated current rate case expense of $350,000. When that amount is amortized over a period of three years, it results in an estimated annual rate case expense of $116,667.

***Q16.*** ***DO YOU AGREE WITH THIS ADJUSTMENT?***

***A16.*** No. Although I agree with the amortization of the rate case expense over three years, I do not agree with the level of rate case expense that should be amortized. Only half of the rate case expense estimate of $350,000 should be included because customers should not have to pay for the entire cost of a rate case that disproportionately benefits the Utility and its shareholders over customers billed the increased charges.

***Q17.*** ***WHAT ADJUSTMENT TO RATE CASE EXPENSE ARE YOU PROPOSING?***

***A17.*** I propose that $175,000 be excluded from the rate case expense of $350,000 as it was currently estimated at the time the Stipulation was filed at the PUCO. This would result in an incremental adjustment of $(58,333) from Stipulation Schedule C-3.6. My adjustment is shown on Schedule SBH-5. If Aqua submits a final rate case expense amount to the PUCO for inclusion in the Revenue Requirement, it too should be accorded the same treatment that I am proposing.

***Q18.*** ***WHY DOES THE AMOUNT OF RATE CASE EXPENSE PROPOSED IN THE STIPULATION NOT BENEFIT CUSTOMERS AND IS NOT IN THE PUBLIC INTEREST?***

***A18.*** The amount of rate case expense included in the Stipulation does not recognize the fact that the Utility and its shareholders also benefit from this expenditure. It would not benefit customers to pay more than their fair portion of rate case expense. As a reasonable compromise, customers should only pay for half of rate case expense, which would be $175,000 or $58,333 amortized over three years.

***Q19. WHAT IS THE THIRD ISSUE YOU ADDRESS WITH REGARD TO THE SECOND CRITERIA?***

***A19.*** The third issue I address concerns the signing bonuses that are included in Stipulation Joint Exhibit 2.0.

***Q20. DID THE UTILITY INCLUDE SIGNING BONUSES IN ITS CALCULATION OF WAGE ANNUALIZATION ON SCHEDULE C-3.4 OF THE APPLICATION?***

***A20.*** Yes. On Application Schedule WPC-3.4b, Aqua included signing bonuses totaling $10,500 in the calculation of its Wage Annualization.

***Q21. DID THE PUCO STAFF INCLUDE THESE SIGNING BONUSES IN ITS CALCULATION OF WAGES ANNUALIZED ON SCHEDULE C-3.4 OF THE STAFF REPORT?***

***A21.*** In my review of the PUCO Staff Workpapers, the PUCO Staff did include $10,500 of signing bonuses related to Union Employees.[[9]](#footnote-9)

***Q22. WAS THERE AN ADJUSTMENT TO REMOVE SIGNING BONUSES FROM THE SCHEDULES FOUND IN STIPULATION JOINT EXHIBIT 2.0?***

***A22.*** No. There was no such adjustment to remove signing bonuses from the calculation of Wages Annualized.

***Q23.*** ***DO YOU AGREE WITH THE INCLUSION OF THESE SIGNING BONUSES IN THE CALCULATION OF WAGES?***

***A23.*** No. The signing bonus was offered by Aqua in the context of labor negotiations to provide an incentive for acceptance of a negotiated union contract.[[10]](#footnote-10) This bonus has nothing to do with the improvement of customer service or the percentage of the wage increase agreed to in the contract.[[11]](#footnote-11) In addition, even if an employee were to do no work during the year, then he/she would still receive the $500 signing bonus. Hence, these bonuses, which were used as an enticement for employees to agree to a labor contract package, has resulted in no quantifiable increase in labor productivity to the benefit of consumers.

***Q24. DID YOU MAKE AN ADJUSTMENT TO EXCLUDE THE SIGNING BONUSES FROM STIPULATION JOINT EXHIBIT 2.0?***

***A24.*** Yes. My adjustment to exclude the signing bonuses of $10,500 from the calculation of wages is shown on Schedule SBH-6. After the O&M Allocation Percentage of 88.60% is applied, the adjustment would be $(9,303). I have also prepared an adjustment of $(712) on Schedule SBH-7 that reflects the reduction in FICA Taxes associated with my elimination of the $9,303 in Signing Bonuses.

***Q25. WHY DO THE SIGNING BONUSES INCLUDED IN THE STIPULATION NOT BENEFIT CUSTOMERS AND IS NOT IN THE PUBLIC INTEREST?***

***A25.*** The signing bonuses are not a part of the hourly labor rate in the labor contract and were simply an incentive for the union to agree to sign the contract. Even if there was no work performed during the year, each employee in the union would still get a bonus of $500. It does not benefit customers to pay for $10,500 in signing bonuses that could be used toward reducing their rates for water service.

***Q26. WHAT IS THE FOURTH ISSUE YOU ADDRESS WITH REGARD TO THE SECOND CRITERIA?***

***A26.*** The fourth issue I address is the inclusion in Stipulation Joint Exhibit 2.0 of certain sundry costs that were incurred by the Corporate Office (or “Service Center”).

***Q27. DID AQUA INCLUDE IN ITS APPLICATION ANY SUNDRY COSTS IN ACCOUNT 923-2, MANAGEMENT SUPERVISION FEES AND EXPENSES?***

***A27.*** Yes. As set forth on Workpaper WPC-2.1b, Aqua included these types of costs in the total test year amount of $4,114,247 in its Application for Corporate Office (or “Service Center”) Account No. 923-2, Management Supervision Fees and Expenses.[[12]](#footnote-12)

***Q28.*** ***DID THE PUCO STAFF EXCLUDE ANY SUNDRY COSTS IN ACCOUNT 923-2, MANAGEMENT SUPERVISION FEES AND EXPENSES AT THE SERVICE CENTER LEVEL?***

***A28.*** No. It does not appear that the PUCO Staff made any adjustments to Service Center Account No. 923-2 in the Staff Report.

***Q29. WAS THERE AN ADJUSTMENT TO REMOVE SUNDRY COSTS INCURRED AT THE SERVICE CENTER FROM THE SCHEDULES FOUND IN STIPULATION JOINT EXHIBIT 2.0?***

***A29.*** Yes, in part. On Schedule C-3.20 of the Stipulation, the parties excluded $1,394 worth of sundry costs addressed in my Direct Testimony filed on June 24, 2014.[[13]](#footnote-13) These sundry costs related to expensive meals, catering, country clubs, casinos, bar associations, and alumni affairs that were incurred at the Service Center.

***Q30. SHOULD AN ADDITIONAL ADJUSTMENT BE MADE TO EXCLUDE CERTAIN EXPENSES WITHIN SERVICE CENTER ACCOUNT NO. 923-2?***

***A30.*** Yes. After reviewing the actual sundry costs incurred during April – June 2013 of the test year, I also determined that an adjustment should be made to exclude costs related to Board of Directors (“BOD”) Restricted Stock.[[14]](#footnote-14)

***Q31. WHY DO YOU RECOMMEND THAT BOARD OF DIRECTORS RESTRICTED STOCK SHOULD BE EXCLUDED FROM THE CALCULATION OF THE RATES THAT AQUA CHARGES ITS CUSTOMERS FOR WATER SERVICE?***

***A31.*** This is an expense being allocated from the Service Center that does not provide a direct and primary benefit to customers of the Utility.

***Q32. WHAT DO YOU RECOMMEND WITH REGARD TO THE AMOUNT OF THE EXCLUSION FOR THESE COSTS THAT YOU HAVE IDENTIFIED?***

***A32.*** After allocation to the Divisions at issue in this case,[[15]](#footnote-15) I recommend that $39,455 be excluded from consideration in this case. My adjustment is set forth on Schedule SBH-8.

***Q33. WHAT IS THE FIFTH ISSUE YOU ADDRESS WITH REGARD TO THE SECOND CRITERIA?***

***A33.*** The fifth issue I address is the application of the rates to be determined in this on a bills-rendered basis instead of a service-rendered basis.

***Q34. WHAT METHOD OF BILLING RATES DOES THE UTILITY CURRENTLY USE?***

***A34.*** Aqua currently applies its rates on a service-rendered basis, which means that all water delivered to the customer on and after the effective date of the rate change is billed at the new rate. In other words, under a service-rendered billing method, the water rates in effect at the time of service are the rates that are applied to customers’ bills.

***Q35. WHAT METHOD OF BILLING RATES DOES THE STIPULATION PROPOSE?***

***A35.*** The Stipulation proposes that the tariffed rates will go into effect on a bills-rendered basis immediately after the PUCO approves the Stipulation.[[16]](#footnote-16) In other words, under bills-rendered billing, the water rates in effect at the time the bill is rendered are applied to its customers’ bills.

***Q36. WHY DOES THE SWITCH FROM SERVICE-RENDERED BILLING TO BILLS-RENDERED BILLING NOT BENEFIT CUSTOMERS IN THIS CASE?***

***A36.*** If there is a switch to bills-rendered billing, Aqua will be able to apply retroactively the new rates to customer water usage that occurred at least 15 days before the PUCO approves the Stipulation. This would allow Aqua to collect approximately $159,000 of the rate increase from customers prematurely.[[17]](#footnote-17)

***Q37.*** ***HOW DOES THE STIPULATION ADDRESS THE UTILITY’S FEDERAL INCOME TAX EXPENSE?***

***A37.*** As described in the Testimony of Michael J. Majoros, the Stipulation includes $4,202,711 of federal income taxes included in the rates that Aqua would be permitted to annually charge customers during the time period that the rates from this case are in effect.[[18]](#footnote-18)

***Q38.*** ***DO YOU HAVE A RECOMMENDATION WITH RESPECT TO HOW THE FEDERAL INCOME TAX EXPENSE WAS CALCULATED IN THE STIPULATION?***

***A38.*** Yes. I have incorporated into my testimony a schedule containing a Federal Income Tax expense adjustment that is based upon the recommendations made in the testimony of OCC witness Michael J. Majoros. This adjustment is shown on Schedule SBH-10 with Schedule SBH-11 being the supporting schedule.

***Q39. DID YOU PREPARE A SCHEDULE THAT SUMMARIZES THE ADJUSTMENTS YOU HAVE MADE TO RATE BASE AND OPERATING INCOME?***

***A39.*** Yes. Schedule SBH- 12 summarizes both my recommended adjustments and the proposed adjustments advocated by OCC witness Michael Majoros to rate base and operating income.

***Q40. DID YOU PREPARE A SCHEDULE THAT SHOWS YOUR RECOMMENDED REVENUE REQUIREMENTS WHEN YOUR ADJUSTMENTS ARE CONSIDERED?***

***A40.*** Yes. Taking into consideration the additional adjustments to rate base and operating income over and above what is set forth in the Stipulation (see Exhibit SBH-12), and using the rate of return of 7.20% recommended by OCC witness Daniel Duann and the Federal Income Tax adjustment advocated by OCC witness Michael Majoros, I have developed a revenue requirement of approximately $58,813,286. The calculation of this revenue requirement is shown on Schedule SBH-13. Based on this analysis I recommend a revenue increase of $2,163,585 or 3.82%. The Stipulation, however, recommends a revenue increase of $3,820,000 or 6.74%. Thus, given the greater amount of the rate increase identified in the Stipulation, it does not benefit customers and is not in the public interest.

***Q41. REGARDING THE THIRD STIPULATION CRITERION, DOES THE SETTLEMENT, AS A PACKAGE, VIOLATE ANY IMPORTANT REGULATORY PRINCIPLE OR PRACTICE?***

***A41.*** Yes, the Stipulation violates the third criteria in several respects. I will elaborate further below.

***Q42. CONCERNING YOUR FIRST, SECOND AND THIRD ISSUES SET FORTH ABOVE, HOW DOES THE STIPULATION VIOLATE IMPORTANT REGULATORY PRINCIPLES OR PRACTICES?***

***A42.*** These costs, that are included in the tariffed rates proposed in Stipulation Joint Exhibit 3.0, are not just and reasonable as required by the Ohio Revised Code.[[19]](#footnote-19)

***Q43. CONCERNING YOUR FOURTH ISSUE SET FORTH ABOVE, HOW DOES THE STIPULATION VIOLATE IMPORTANT REGULATORY PRINCIPLES OR PRACTICES?***

***A43.*** The Corporate Office expense for the Board of Directors restricted stock does not provide a direct and primary benefit to customers.[[20]](#footnote-20)

***Q44.*** ***CONCERNING YOUR FIFTH ISSUE SET FORTH ABOVE, HOW DOES THE STIPULATION VIOLATE IMPORTANT REGULATORY PRINCIPLES OR PRACTICES?***

***A44.*** The shift from service-rendered billing to bills-rendered billing results in the retroactive billing of rates in this case, which violates the principles set forth in *Lucas County Commissioners v. PUCO*.[[21]](#footnote-21)

# III. CONCLUSION

***Q45. DOES THIS CONCLUDE YOUR TESTIMONY AT THIS TIME?***

***A45.*** Yes.

**CERTIFICATE OF SERVICE**

I hereby certify that a copy of *Testimony in Opposition to the Stipulation of Steven B. Hines on Behalf of the Office of the Ohio Consumers’ Counsel* was provided to the persons listed below via electronic transmission this 4th day of August, 2014.

*/s/ Melissa R. Yost*\_\_\_\_\_\_\_\_\_\_\_

Melissa R. Yost

Deputy Consumers’ Counsel

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1. (54,500 + 23,000)/54,500 = 70.32%. [↑](#footnote-ref-1)
2. Stipulation and Recommendation, Joint Exhibit 2.0, Schedule B-2.1, pages 13-15 (July 21, 2014). [↑](#footnote-ref-2)
3. Application, at Workpaper WPB-7.1; See also, Attachment SBH-B. [↑](#footnote-ref-3)
4. See, Schedule SBH-1. [↑](#footnote-ref-4)
5. See, Schedule SBH-3. [↑](#footnote-ref-5)
6. See, Schedule SBH-4. [↑](#footnote-ref-6)
7. Schedule SBH-2, $179,395 - $71,880 - $7,317. [↑](#footnote-ref-7)
8. Schedule SBH-3, Depreciation Expense of $(16,629); Schedule SBH-4, Property Tax of $(6,512). [↑](#footnote-ref-8)
9. Staff Report, Staff Workpapers for Staff Schedule C-3.4, Wages Annualized (See Attachment SBH-C). [↑](#footnote-ref-9)
10. Aqua response to OCC Interrogatory No. 8 (See Attachment SBH-D). [↑](#footnote-ref-10)
11. Aqua response to OCC Request to Produce No. 18 (See Attachment SBH-E). [↑](#footnote-ref-11)
12. See Attachment SBH-F. [↑](#footnote-ref-12)
13. Direct Testimony of Steven B. Hines, pages 14-15 and Schedule SBH-12 (June 24, 2014). [↑](#footnote-ref-13)
14. Aqua response to OCC Request to Produce No. 31 (See Attachment SBH-G). [↑](#footnote-ref-14)
15. Aqua response to Staff Data Request No. 8 (See Attachment SBH-H). [↑](#footnote-ref-15)
16. Stipulation and Recommendation, Case No. 13-2124-WW-AIR at 3 (July 21, 2014). [↑](#footnote-ref-16)
17. See Schedule SBH-9. [↑](#footnote-ref-17)
18. See, Stipulation and Recommendation, Schedule C4, page 2of 2, line 22, Column (F); see also, Testimony of Michael J. Majoros in Opposition to the Stipulation and Recommendation, at p. 3 (August 4, 2014). [↑](#footnote-ref-18)
19. R.C. 4905.22. [↑](#footnote-ref-19)
20. *Cleveland v. Pub. Utilities Comm.*, 63 Ohio St. 2d 62, 406 N.E.2d 1370 (1980); *see also Office of Consumers' Counsel v. Pub. Utilities Comm.*, 67 Ohio St. 2d 153, 423 N.E.2d 820 (1981) (Justice Brown dissenting). [↑](#footnote-ref-20)
21. *Lucas County Comm'rs v. PUC*, 80 Ohio St. 3d 344, 348, 686 N.E.2d 501, (1997); see also, *Keco Industries, Inc. v. Cincinnati & Suburban Bell Tel. Co.*, 166 Ohio St. 254, 141 N.E.2d 465 (1957). [↑](#footnote-ref-21)