

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Aqua )  
Ohio, Inc. for Authority to Assess a ) Case No. 11-5849-WW-SIC  
System Improvement Charge in the Lake )  
Erie Division. )

FINDING AND ORDER

The Commission finds:

- (1) On September 17, 2003, the Ohio General Assembly enacted Section 4909.172, Revised Code, authorizing waterworks and sewage disposal companies to file an application with the Commission for approval to collect a system infrastructure improvement surcharge (SIC). The surcharge mechanism is designed to recover, and provide a return on, specified costs associated with certain plant investments.
- (2) Guidelines to be followed by companies filing SIC applications are appended to Rule 4901:1-15-35, Ohio Administrative Code (O.A.C.), and became effective on August 22, 2008.
- (3) On December 1, 2011, Aqua Ohio, Inc. (Aqua, applicant) filed an application (Application) for authority to collect a proposed SIC in its Lake Erie Division.
- (4) By attorney examiner entry, a schedule was established, requiring that any interested party wishing to comment on the Application must file those comments with the Commission by no later than February 10, 2012.
- (5) On February 10, 2012, staff of the Commission (staff) submitted comments (Comments) describing the process followed by staff in investigating the substance of the Application, and the results of that investigation. The review of the Application included interviews of applicant's key management personnel; review of internal and published financial reports; testing of the original cost of property for reasonableness through examination of continuing property records; verification of the existence and the used and useful nature of assets through physical inspections; and performance of any other independent analysis considered necessary by staff under the circumstances. Staff examined 28

specific projects, representing approximately 66 percent of the total dollar value of the additions covered by the Application. The applicant's distribution system infrastructure improvements reviewed by staff amount to \$1,627,703 out of the total proposed by the applicant for recovery of \$2,448,746. (Comments at 3.)

- (6) Section 4909.172, Revised Code, includes several requirements that must be met before the Commission may approve a proposed SIC:
  - (a) The costs of infrastructure plant upon which a proposed SIC may be based may only include the costs of certain capital improvements. For a waterworks company like the applicant, those allowable capital improvements are:
    - (i) service lines for, and hydrants, mains, and valves installed as a part of, a replacement project for an existing facility; main extensions that eliminate dead ends to resolve documented water supply problems presenting significant health or safety issues to then existing customers, and main cleaning or relining;
    - (ii) unreimbursed capital expenditures for waterworks facility relocation required by a governmental entity due to a street or highway project; and
    - (iii) minimum land or land rights acquired by the company as necessary for any service line, equipment, or facility previously described.
  - (b) The Commission must determine that the covered capital improvements are used and useful in rendering public utility service.
  - (c) The cost of those capital improvements may include depreciation expenses.

- (d) The cost of those capital improvements may not include the cost of any improvement which provides any more than minimal additional revenue associated with elimination of a dead end.
  - (e) The proposed SIC must be just and reasonable, and must be sufficient to meet, but not to exceed, the revenue requirement necessary to both:
    - (i) cover such infrastructure plant costs as are described in the statute, incurred after March 1, 2003, and before the date of filing, and not already reflected in schedules filed under Section 4905.31, Revised Code; and
    - (ii) provide a fair and reasonable rate of return on the valuation (as of the date of filing of the application) of that infrastructure plant.
  - (f) The SIC may not exceed three percent of the rates and charges applicable to any affected customer class and, as to the allowed percentage increase, must be uniform for each such class.
  - (g) No more than three SICs under this section may be in effect at any given time.
  - (h) The Commission is prohibited from authorizing a SIC under this section if it would cause the applicant to earn an excessive rate of return on its rate base.
- (7) As a result of its investigation, staff reached the following conclusions:
- (a) All projects requested in the Application consisted of mains and valves, service lines, and hydrants installed as part of replacement projects for existing facilities or to address documented service quality issues, in accordance with Section 4909.172(C)(1), Revised Code. (Comments at 3.)

- (b) All projects included in the filing have been completed and are rendering public utility service to the applicant's customers. (Comments at 3.)
- (c) The depreciation accrual rates used by applicant were previously found by the Commission to be proper and adequate. (Comments at 4.)
- (d) The proposed surcharge will recover only those costs specifically related to the applicant's infrastructure improvements. (Comments at 4.)
- (e) The proposed surcharge will provide a fair and reasonable rate of return on the applicant's valuation of the relevant infrastructure plant for the period November 10, 2010, to October 31, 2011. (Comments at 5.)
- (f) The proposed surcharge does not exceed three percent and is distributed uniformly to all classes. (Comments at 5.)
- (g) The applicant has one existing SIC surcharge in effect in the Lake Erie Division, which became effective on all bills issued after February 10, 2011, in Case No. 10-2771-WW-SIC. The existing SIC will continue in effect with the new proposed SIC being a second, additional surcharge of three per cent. (Comments at 5-6.)
- (h) The applicant's pre-tax rate of return is correct and consistent with the guidelines. (Comments at 5.)
- (i) The proposed SIC of three percent would be charged in addition to the charges provided for in the applicant's tariff for all metered and private fire service in the Aqua Lake Erie Division and, for customers in the Norlick Place and Lake Seneca Subdivisions, the surcharge will be in addition to all flat-rate unmetered charges. The surcharges would apply to all bills issued after approval of the new tariff. (Comments at 5.)

- (j) The Commission should approve the Application.  
(Comments at 7.)
- (8) Based on the applicant's books of record and staff's identification of those accounts, the Commission finds that the improvements upon which the proposed SIC is based are replacements of service lines, hydrants, and mains. (Application at schedule 2 of exhibit C; Comments at 3.) These improvements are ones upon which a SIC may be based.
- (9) Based on staff's findings, the Commission determines that the infrastructure improvements upon which the proposed SIC is based are used and useful in rendering public utility service to the customers of the applicant. (Comments at 2.)
- (10) As allowed by the authorizing statute, the costs of the capital improvements underlying the proposed SIC do include depreciation expenses. The Commission finds that those depreciation expenses were based on rates approved in the applicant's last rate case and are, therefore, proper and adequate. *In the Matter of the Application of Aqua Ohio, Inc. for Authority to Increase its Rates in the Lake Erie Division*, Case No. 09-1044-WW-AIR, Opinion and Order (September 1, 2010). (Comments at 4-5.) The annualized depreciation expense on the underlying capital improvements is \$41,958. (Application at schedule 5.) The depreciation expense on the items being replaced is \$4,306. (Application at schedule 6.)
- (11) All of the underlying infrastructure improvement costs were incurred by the applicant after March 1, 2003, and before the date of filing of the Application. (Application at schedule 2.) The following summarizes the costs of the infrastructure improvements underlying the proposed SIC, and the fair and reasonable return on the valuation of that infrastructure (Application at schedule 1):

<b>RETURN ON ADDITION TO RATE BASE</b>			
<b>Change to plant-in-service</b>			
Cost of improvements	\$2,448,746		
Less: Cost of retired items	<u>266,035</u>		
Net addition to plant-in-service		\$2,182,711	
<b>Less: Accumulation provision for depreciation</b>			
Depreciation on improvements	\$ 7,563		
Less: Original cost retired	<u>266,035</u>		
Net provision for depreciation		<u>(258,472)</u>	
<b>Change to return on rate base</b>			
Net addition to rate base		\$2,441,183	
Pre-tax rate of return on rate base		10.84%	
<b>Annual rate of return on new rate base</b>			\$264,624
<b>OPERATING EXPENSES</b>			
Annualized depreciation on improvements	41,958		
Less: Annualized depreciation on retired items	4,306		
Annualized property taxes on improvements	210,561		
Less: Annualized reduction for property taxes	<u>6,552</u>		
<b>Net annual depreciation change</b>			<u>241,661</u>
<b>ANNUALIZED REVENUE REQUIREMENT FOR IMPROVEMENTS</b>			\$506,285

Thus, the Commission finds that the annual revenue requirement associated with the underlying infrastructure improvements is \$506,285.

The Application also sets forth the anticipated annual revenues resulting from the proposed SIC. (Application at schedule 10.) The Commission finds that the proposed SIC of three percent, applied to annual revenues of \$15,839,083 will yield additional revenues of approximately \$475,171. Although this annual revenue yield is less than the annualized revenue requirement, the amount of the SIC is limited by Section 4909.172(B)(2), Revised Code, to three percent. In addition, the proposed SIC will apply uniformly to all classes with the appropriate exclusion of Auburn Lakes. (Comments at 5.)

Staff reports that utilization of the pretax rate of return contained in the applicant's last rate case is consistent with the guidelines, as the date certain in this proceeding is not later than three years from the date when the applicant's existing rates and tariffs went into effect.

According to staff's investigation, the applicant's calculation of the pretax rate of return is correct. (Comments at 5.) The Commission agrees.

Finally, the Commission is required by Section 4909.172, Revised Code, to ensure that any authorized SIC will not cause a company to earn an excessive rate of return on its rate base. As calculated by both staff and the applicant, the proposed SIC will result in the applicant earning a return of 5.74 percent on its rate base as of October 31, 2011, which rate base includes the infrastructure improvements upon which the SIC is based. (Application at schedule 8.) The Commission finds that this return is not excessive.

The guidelines state that "[i]f a surcharge is granted by the Commission, the company's actual and pro forma profitability will be reviewed on an annual basis to determine whether a reduction or elimination of such surcharge or subsequent surcharges is required by this restriction." (Guidelines at 3.) In order to make the required annual review, the applicant will be ordered to file its SIC schedule 8 on an annual basis concurrent with the applicant's filing of its annual report to the Commission, using the most recent calendar year.

- (12) The Commission, therefore, finds that the proposed SIC is just and reasonable, and is sufficient to meet (subject to the statutory maximum SIC percentage), but not to exceed, the statutorily mandated revenue requirement associated with the cost of, and the fair and reasonable return on, the underlying infrastructure improvements.
- (13) The applicant proposed a form of the customer notices. (Schedule 11 of exhibit C to the Application.) The Commission has reviewed the form of customer notices and finds that the notices docketed on December 1, 2011, are adequate. The customer notices should be forwarded to all customers affected by the SIC surcharge approved in this proceeding, on or with the first bill that contains the surcharge.
- (14) The Commission has reviewed the proposed revised tariff pages that were filed as a part of the Application. (Schedule 9 of exhibit C of the Application.) The Commission finds that the proposed revised tariff pages are approved, conditioned upon the addition of the date on which the revised tariff pages are filed in final form.

It is, therefore,

ORDERED, That the system infrastructure improvement charge proposed by the applicant in this proceeding be approved. It is, further,

ORDERED, That Aqua be authorized to file, in final form, four complete, printed copies of tariffs consistent with this finding and order. Aqua shall file one copy in its TRF Docket No. 89-7028-WW-TRF (or may make such filing electronically as directed in Case No. 06-900-AU-WVR) and one copy in this case docket. The remaining two copies shall be designated for distribution to the Rates and Tariffs, Energy and Water Division of the Commission's Utilities Department. It is, further,

ORDERED, That the proposed tariff sheets be effective upon filing in final form, on a services rendered basis. It is, further,

ORDERED, That nothing in this finding and order shall be binding upon this Commission in any future proceeding or investigation involving the justness or reasonableness of any rate, charge, rule, or regulation. It is, further,

ORDERED, That the applicant shall file, on an annual basis until such time as the surcharge is eliminated, an updated schedule 8, as attached as part of exhibit C of the Application. The schedule 8 shall be filed under this docket, concurrently with the applicant's filing of its annual report to the Commission, using information for the most recent calendar year. It is, further,

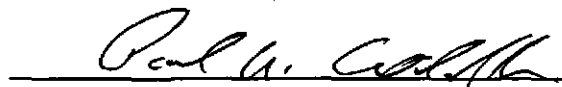
ORDERED, That the customer notices filed with the Commission on December 1, 2011, be delivered to each customer affected by the surcharge approved in this finding and order, with or on each customer's first bill containing the surcharge. It is, further,



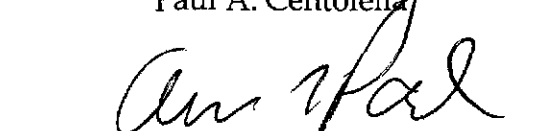
ORDERED, That a copy of this finding and order be served upon all parties of record.


THE PUBLIC UTILITIES COMMISSION OF OHIO

  
Todd A. Snitchler, Chairman

  
Paul A. Centolella

  
Steven D. Lesser

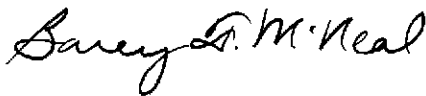
  
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Barcy F. McNeal  
Secretary