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**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of)
Ohio American Water Company) Case No. 07-1112-WS-AIR
To Increase Its Rates in Its Entire Service)
Area for Water and Sewer Service.)

**OBJECTIONS TO THE PUCO STAFF'S REPORT
OF INVESTIGATION
AND SUMMARY OF MAJOR ISSUES
BY
THE OFFICE OF THE OHIO CONSUMERS' COUNSEL**

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The Office of the Ohio Consumers' Counsel ("OCC"), an intervenor in this case, hereby submits to the Public Utilities Commission of Ohio ("Commission" or "PUCO") these objections¹ to the PUCO Staff's Report of Investigation ("Staff Report") that the Staff filed on May 28, 2008 concerning the Application of Ohio American Water Company ("OAW" or "Company") to increase its rates for water and sewer service. OCC is the state representative of approximately 51,600 residential customers of OAW.

OCC submits that these objections meet the specificity requirement of Ohio Adm. Code 4901-1-28. Additionally, OCC's objections are supplemented and/or supported with the testimony of Steven B. Hines, Rusty P. Russell, and Scott J. Rubin filed on June 27, 2008. OCC's objections identify matters in the Staff Report where PUCO Staff fails to recommend against or actively supports rates or service terms that contravene what is reasonable and lawful for OAW's residential consumers.

¹ The objections are filed pursuant to R.C. 4909.19 and Ohio Adm. Code 4901-1-28(B).

OCC reserves the right to amend and/or supplement its objections in the event that the PUCO Staff changes, modifies, or withdraws its position, at any time prior to the closing of the record, on any issue contained in the Staff Report. Additionally, where PUCO Staff has indicated that its position on a particular issue is not known at the date of the Staff Report, OCC reserves the right to later supplement its objections once PUCO Staff's position is made known. OCC also reserves the right to file additional expert testimony, produce fact witnesses and introduce additional evidence. Moreover, the OCC reserves its rights, through the amended and/or supplemented testimony of Steven B. Hines, Rusty P. Russell, and Scott J. Rubin, in the event that the PUCO Staff changes, modifies, or withdraws its position on any issue contained in the Staff Report. OCC also submits that the lack of an objection in this pleading to any aspect of the Staff Report does not preclude OCC from cross-examination or introduction of evidence or argument in regard to issues on which the PUCO Staff changes, modifies, or withdraws its position on any issue contained in the Staff Report.

Pursuant to R.C. 4903.083, OCC submits a "Summary of Major Issues" that outlines the major issues to be determined in this proceeding. OCC respectfully requests that these issues be included in the notices of the local public hearings in accordance with R.C. 4903.083.

OBJECTIONS TO THE STAFF REPORT

I. RATE BASE AND OPERATING INCOME

A. Rate Base

1. OCC objects to Staff Report's determination of rate base to the extent that other OCC objections may have an effect upon the rate base the various components of rate base as set forth in Schedules B-1 through B-6 of the Staff Report.

B. Operating Income

Operating Revenues:

2. OCC objects to the Staff Report's failure to recommend adjustments to Other Miscellaneous Adjustments shown on Schedule C-3.2, Other Operating Revenue Adjustment. Staff failed to annualize the revenue related to Activation Fees, Reconnection Charges and Non-Sufficient Funds Fees ("NSF Fees") but only recognized eleven months of actual revenue from each of these sources. OCC witness Hines' testimony addresses this objection.
3. OCC objects to the Staff Report's failure to recommend adjustments to Other Operating Revenue on Schedule C-3.2, Other Operating Revenue Adjustment. Staff failed to adjust Usage Data Reading revenues to reflect annualized amounts of \$20,999 for Water A, \$3,271 for Water C and \$2,841 for Wastewater. OCC witness Hines' testimony addresses this objection.

4. OCC objects to the Staff Report's failure to recommend adjustments to Other Operating Revenue on Schedule C-3.2, Other Operating Revenue Adjustment. Staff failed to adjust Frozen Meter revenues to reflect an annualized amount of \$10,825 for Water A. OCC witness Hines' testimony addresses this objection.
5. OCC objects to the Staff Report's failure to recommend adjustments to Other Operating Revenue on Schedule C-3.2, Other Operating Revenue Adjustment. Staff failed to include in its adjustment \$11,956 in revenues for Wastewater related to a land lease contract OAW currently has with SprintCom Inc. OCC witness Hines' testimony addresses this objection.

C. Operating Expenses

Management Fees Expense:

6. OCC objects to the Staff Report's failure to recommend adjustments to Management Fees Expense on Schedule C-3.18, Management Fees Expense Adjustment. Staff failed to exclude a total of \$72,800 out of approximately \$182,000 related to Incentive Plan Expenses. This exclusion is in proportion to the adjustment Staff made to OAW incentive compensation expenses on its Schedule C-3.3, Labor and Labor Related Expense Adjustment. Such incentive expenses should be excluded because they stem from goals that focus on shareholder gain. OCC witness Russell's testimony addresses this objection.

7. OCC objects to the Staff Report's failure to recommend adjustments to Management Fees Expense on Schedule C-3.18, Management Fees Expense Adjustment. Staff failed to exclude a total of \$3,970 for Trade Shows because these expenses are related to Demonstration and Selling Expenses and are, thus, promotional in nature. OCC also objects to the Staff Report's failure to recommend other adjustments to Management Fees Expense. Staff failed to exclude a total of \$3,470 for Charitable Contributions since these expenses are related to goodwill and are not necessary for the provision of utility service and do not provide a direct and primary benefit to customers. OCC witness Russell's testimony addresses this objection.
8. OCC objects to the Staff Report's failure to recommend adjustments to Management Fees Expense on Schedule C-3.18, Management Fees Expense Adjustment. Staff failed to exclude a total of \$17,108 in Community Relations Expense since these expenses are related to public relations and goodwill and do not provide a direct and primary benefit to Ohio customers. OCC witness Hines' testimony addresses this objection.
9. OCC objects to Staff Report's failure to recommend adjustments to Management Fees Expense on Schedule C-3.18, Management Fees Expense Adjustment. Staff failed to exclude a total of \$43,808 in Business Development expenses. These kinds of expenses are

institutional activities designed to promote goodwill and a favorable company image and do not provide a direct and primary benefit to Ohio customers. OCC witness Hines' testimony addresses this objection.

10. OCC objects to the Staff Report's failure to recommend adjustments to Management Fees Expense on Schedule C-3.18, Management Fees Expense Adjustment. Staff failed to exclude a total of \$39,483 in External Affairs expenses. These kinds of expenses are institutional activities designed to promote goodwill and a favorable company image and do not provide a direct and primary benefit to Ohio customers. OCC witness Hines' testimony addresses this objection.
11. OCC objects to the Staff Report's failure to recommend adjustments to Management Fees Expense on Schedule C-3.18, Management Fees Expense Adjustment. Staff failed to exclude a total of \$5,806 in Investor Relations expenses. These kinds of expenses are related to services provided only to shareholders and, as such, do not provide a direct and primary benefit to Ohio customers. OCC witness Hines' testimony addresses this objection.

D. Revenue Requirements

12. OCC objects to the Staff Report's recommended revenue requirement and resulting revenue increase on Schedule A-1 as it is excessive due to the use of inappropriate and incorrect rate base, operating income, and rate of return, as detailed below in the OCC's objections to Staff's determination of incorrect rate base, operating income, and rate of return.
13. OCC objects to the Staff Report's calculations that do not agree with the flow-through consequences of OCC's other objections regarding revenue requirements:
 - a) OCC objects to the Staff Report's calculation of rate base on Schedule B-1, to the extent that other objections have an impact on this calculation.
 - b) OCC objects to the Staff Report's calculation of working capital allowance on Schedule B-5, to the extent that other objections have an impact on this calculation.
 - c) OCC objects to the Staff Report's calculation of operating revenues and operating expenses on Schedule C-2, to the extent that other objections have an impact on this calculation.

- d) OCC objects to the Staff Report's calculation of taxes other than income on Schedule C-3.20, to the extent that other objections have an impact on this calculation.
- e) OCC objects to the Staff Report's calculation of federal income taxes on Schedule C-4, to the extent that other objections have an impact on this calculation.

II. RATE OF RETURN

- 14.** OCC objects to the Staff's Report's calculated common equity cost and rate of return on the following bases:

- a) The Staff, in its DCF analysis, incorporated a growth rate based on the average annual change in GNP for the years 1929 to 2005, which neither reflects investors' most recent or current dividend and earnings growth, nor investors' expectations of the long term dividend growth in the future, thereby artificially increasing the common equity cost.

The Staff provided no theoretical or empirical support to justify using the projected GNP growth rate as the expected long-term DCF growth rate.
- b) The Staff, in its Capital Asset Pricing Model, utilized an inappropriate equity risk premium, thereby artificially increasing the common equity cost. The equity risk

premium in the Staff Report is based on historic stock and bond returns and on the arithmetic mean of annual returns. Thus, Staff's Capital Asset Pricing Model utilized an equity risk premium that is upwardly biased, excessive and does not reflect current market fundamentals.

Staff's approach is subject to a myriad of empirical errors which make these historical returns poor measures of expected returns.

- c) The Staff used the arithmetic mean of annual returns rather than the geometric mean of annual returns in deriving its equity risk premium, thus inflating the estimated cost of equity because arithmetic means unrealistically assumes that the relevant investment time horizon is only one year even though investors are expected to hold their stocks for longer time horizons.
- d) OCC objects to the Staff's use of results obtained from historical data for the growth rate of the GNP over the period 1929-2005 and the Ibbotson historical data from 1926 to 2006. Staff weighed all years equally, thus ignoring periods that include wars like the World War II, the Great Depression, shifts in financial markets, significant changes in tax laws, etc., that have changed investors' expectations.

- e) The Staff inappropriately increased the cost of equity by allowing an adjustment for flotation or equity issuance costs even though there is no reason to believe that the Company incurred any flotation costs (and, of course, no support for the magnitude of flotation costs provided for by the Staff). The Company has not requested a flotation cost adjustment. Therefore, the Staff is recommending that the Company receives annual revenues in the form of a higher return on equity for flotation costs that have not been identified by either the Staff or the Company.
- f) The OCC objects to the Staff Report's failure to make an adjustment to reduce the recommended rate for common equity in recognition of the Company's continued poor quality of service noted by the Staff in the Service Monitoring and Enforcement section of the Staff's Report. The Staff Report acknowledges that service quality issues remain in the Company's territory, but Staff failed to make any corresponding reductions to the rate of return to reflect the poor service quality.

III. RATES AND TARIFFS

A. Dishonored Payment Charge-Miscellaneous Charges

15. OCC objects to the Staff Report's failure to recommend adjustment to the dishonored payment charge of \$20.75. The Staff based its calculation of the cost of dishonored payments from the original OAW response to Staff DR 27. The Staff failed to revise its calculation based upon more recent information provided through an updated response to DR 27.

B. Cost of Service Study

16. OCC objects to the Staff Report's reliance on the amount of revenues a class contributes to overall revenues (i.e. "Factor 19") in allocating miscellaneous revenues to the customer classes. Instead the miscellaneous revenues should be allocated to classes based upon how the miscellaneous charge is applied to customers and the degree to which the class contributes to the specific miscellaneous charge.
17. OCC objects to the Staff Report's reliance on Factor 19 in allocating the dishonored payment charge revenues to classes. More of the dishonored payment revenues should be allocated to the residential class because it should be allocated based upon the number of customers in each class.
18. OCC objects to the Staff Report's reliance on Factor 19 in allocating the activation charge revenues to classes. Instead the

activation charge revenues should be allocated to classes based upon the numbers of customers in each class because the activation charge is applied against each customer equally and is not applied to customers based upon the amount of revenues for which they are billed.

19. OCC objects to the Staff Report's reliance on Factor 19 in allocating the reconnection charge revenues to classes. Instead the reconnection charge revenues should be allocated to customer classes based upon the number of customers. The reconnection charge is not applied differently to customers based upon the amount of revenues they are billed, rather the revenues received through the charge are based upon the number of customers who are reconnected.
20. OCC objects to the Staff Report's reliance on Factor 19 in allocating the data reading to classes. Revenues contributed to third party wastewater service providers are based upon the number of meters read by OAW for the third party. Therefore, the appropriate method of allocating data reading revenues to classes is by the number of meters in the class.
21. OCC objects to the Staff Report's reliance on Factor 19 in allocating the frozen meter charge revenues. Revenues contributed through the frozen meter charge are applied to customers based upon the cost of freeing up the meter not on the revenues the

customer is billed. Therefore, the revenues from the frozen meter charge should be allocated to customer classes based upon the number of meters in the class.

22. OCC objects to the Staff Report's failure to recognize in its Staff Report that there are over 1,000 unmetered residential customers in the OAW service territory. These customers should be subtracted from the total number of customers when allocating meter reading costs among the customer classes. The fixed rates applied to these customers should be credited in the cost of meter reading services and applied to the customers with meters.
23. OCC objects to the Staff Report's failure to allocate more meter reading costs to customers whose meters OAW reads more frequently than to customers OAW reads less frequently. Most of the meters of OAW Water A residential and commercial customers are read bimonthly, while the Water A industrial and public authority customers have monthly reads. The meters for all Water C customers are read monthly. Accordingly, meter reading costs should be allocated based on the actual number of annual meter reads in each customer class.
24. OCC objects to the Staff Report's failure to allocate meter reading costs based upon the differences in the cost of reading different classes of meters. Reading industrial meters is more time-consuming and requires more travel to read the meters.

Accordingly, Staff should have re-allocated the costs of meter reading to reflect different meter reading costs for different classes.

C. Third Consumption Block

25. OCC objects to the Staff Report's failure to recommend adjustments to OAW's proposals regarding a third consumption block that is not justified by the cost of service study. The rate of the third consumption block is lower than the unit base cost, which is contrary to sound rate design.

D. Rates for Unmetered Customers

26. OCC objects to the Staff Report's design of rates for unmetered customers. Unmetered rates should be based on the residential customer charge and average level of residential consumption, with an appropriate credit for metering costs.

IV. SERVICE MONITORING AND ENFORCEMENT

27. OCC objects to the Staff Report's failure to recommend procedures to correct OAW's non-compliance with the requirements of Ohio Adm. Code 4901:1-15-28(I) that prohibits OAW from discontinuing service when discontinuing service may be especially dangerous to health as certified by a licensed physician or local board of health physician.
28. OCC objects to the Staff Report's failure to recommend that the Company provide notice to all customers that budget billing is

available, rather than just providing it to customers upon customers' request. In addition, the Staff Report should have recommended that the Company make budget billing available to customers who are on monthly billing and not just to customers who are on bi-monthly billing.

29. OCC objects to the Staff Report's failure to recommend that the Company identify a specific date by which the Company will have all residential customers metered or in the alternative failed to recommend that the Company should accept metering information available through sewage meters owned by a different entity.
30. OCC objects to the Staff Report's failure to recommend that the Company comply with Ohio Adm. Code 4901:1-15(C)(2) by providing notice to customers of one specific date of an upcoming flushing rather than two possible alternative dates.

V. WATER QUALITY

31. OCC objects to the Staff Report's failure to recommend that the Company conduct a cost-benefit analysis on whether alternatives to the current method of water softening at Lake Darby would be more beneficial for Lake Darby customers. The Company should provide Lake Darby customers the results of the cost-benefit analysis and allow Lake Darby customers to make a choice about the method of water softening OAW employs to soften the water.

32. OCC objects to the Staff Report's failure to recommend that the Company send its water samples from the Lake Darby system to a certified lab for analysis for a six-month period from the date of the Opinion and Order given the history of water hardness in the Lake Darby area.
33. OCC objects to the Staff Report's failure to recommend that the Company continue to pre-treat groundwater supply with sodium permanganate for removal of the manganese to a level less than the SMCL of .05 mg/l. The Company should monitor the manganese concentrations of the groundwater supply and the sand filters' effluent stream on a daily basis for a six-month period to optimize the sodium permanganate treatment and the manganese removal.
34. OCC objects to the Staff Report's failure to recommend continued treatment and evaluation of the Huber Ridge Plant's finished water supply with poly/orthophosphate blend to guard against future discoloration issues and to minimize corrosion within the distribution system. If the poly/orthophosphate blend does not continue to prevent discoloration and corrosion, other chemical treatment options should be considered.
35. OCC objects to the Staff Report's failure to recommend that the Company continue to *unidirectionally* flush, not just flush, the Huber Ridge system to prevent additional accumulated sediment in its distribution piping.

36. OCC objects to the Staff Report's failure to recommend daily, instead of weekly, sampling of tap water at the Huber Ridge Plant for iron and manganese for a one year period from the date of the Opinion and Order in this case, given the history of water discoloration in this system.
37. OCC objects to the Staff Report's failure to recommend consequences to deal with the Company's non-compliance with prior stipulation commitments that required OAW to refrain from applying for an increase in rates for customers in Water C until OAW could demonstrate that the Company had resolved the discolored water service quality issue *for twelve consecutive months* in the Huber Ridge area of Water C.

VI. CONSERVATION

38. OCC objects to the Staff Report's failure to recommend the effective treatment of customer water conservation in the following respects:
- a) The Staff Report failed to recommend that OAW should evaluate the effectiveness of its current customer water conservation efforts and provide a timely report on such an evaluation in the public dockets administered by the Commission.
 - b) The Staff Report failed to recommend that OAW analyze the technical and economic potential for customer water

conservation in their system and provide a timely report on such an analysis in the public dockets administered by the Commission.

- c) The Staff Report failed to recommend that OAW design and implement additional innovative energy efficiency programs for all customer classes found to be cost effective based upon the results of a timely report on the Company's analysis of the technical and economic potential for customer water conservation that should be timely submitted in the public dockets administered by the Commission.

39. OCC objects to the Staff Report's failure to recommend effective treatment of utility energy conservation in the following respects:

- a) The Staff Report failed to recommend that the Company focus on energy savings, efficiency and economics of their own pumps and pumping systems and provide a timely report on such an OAW evaluation in the public dockets administered by the Commission. The Company's pumping systems account for a significant amount of energy use, and attractive paybacks are available to companies that seek efficiency improvements within motor-driven systems.
- b) The Staff Report failed to recommend that the Company be ordered to conduct a broad-based energy management and

performance optimization audit within the next year and
report its findings and recommendations in the public
dockets administered by the Commission.

- 40.** OCC objects to the Staff Report's failure to recommend
consequences to deal with the Company's non-compliance with
prior stipulation commitments that required OAW to propose
conservation programs.

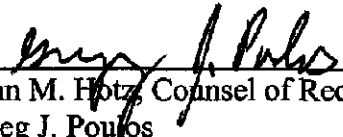
SUMMARY OF MAJOR ISSUES

Pursuant to Ohio R.C. 4903.083, the Commission should include the following as major issues in this proceeding:

1. Is the quality of service provided by Ohio American Water ("OAW") to customers adequate under the Ohio Revised Code?
2. What actions should the Commission order the Company to take to ensure that the quality of service improves for OAW customers?
3. How much of an increase will OAW's customers have to pay for water and/or sewer services?
4. What is the amount of profit that OAW will have an opportunity to earn for providing water and sewer services to residents in Ohio as the result of this proceeding?
5. Which expenses that OAW incurred during the test year will be recoverable from OAW's customers?
6. Are differences in the rates customers pay based on differences in the cost of providing service to customers?

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the Office of the Ohio Consumers' Counsel's
Objections to the PUCO Staff's Report of Investigation and Summary of Major Issues
was served upon the persons listed below via first class U.S. Mail, postage prepaid, this
27th day of June, 2008.



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