

FILE

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

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In the Matter of the Application of :
Water and Sewer LLC for an Increase :
in its Rates and Charges for Sewage :
Disposal Service. :

Case No. 11-4509-ST-APR

WATER AND SEWER LLC
OBJECTIONS TO STAFF REPORT OF INVESTIGATION
AND
SUMMARY OF MAJOR ISSUES

Water and Sewer ("W&S"), pursuant to Section 4909.19, Revised Code, and Rule 4901-1-28, Ohio Administrative Code ("OAC"), hereby submits the following objections to the Staff Report of Investigation ("Staff Report") filed in this docket on February 22, 2012.

(REVENUE REQUIREMENTS)

1. W&S objects to the Staff's recommended revenue requirement range set forth in Schedule A-1 of the Staff Report. As more fully described in the objections that follow, the recommended revenue requirement range is understated because Staff has failed to recognize certain allowable expenses. Thus, Staff's recommended revenue requirement range would result in a rate that is insufficient to compensate W&S for the cost of the sewer service it renders its customers and provide it with a fair and reasonable return on the value of its property used in providing such service.

(RATE BASE)

2. W&S objects to the Staff's recommended allowance for working capital set forth in Schedule B-5 in the Staff Report to the extent that the O&M expense component of the cash working capital fails to recognize certain expenses that were improperly disallowed by Staff.

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(OPERATING INCOME)

3. W&S objects to Staff's determination of adjusted test-year O&M expense set forth in Schedule C-2 of the Staff Report based on the Staff's failure to include the previously authorized annual recovery associated with certain expense amortizations approved by the Commission in Case Nos. 03-318-WS-AIR and 08-227-WS-AIR that have not yet been completed. These amortizations include the following:

(a) The ten-year amortization of \$7,122 in sludge removal expense related to the clean up required due to the poor maintenance practices of the sewer plant's prior owner, which was initially approved by the Commission in Case No. 03-318-WS-AIR,¹ and reaffirmed by the Commission in Case No. 08-277-WS-AIR,² resulting in an authorized annual recovery of \$712;

(b) The ten-year amortization of the \$3,700 cost of the sludge management plan mandated by the Ohio EPA, which was initially approved by the Commission in Case No. 03-318-WS-AIR,³ and reaffirmed by the Commission in Case No. 08-277-WS-AIR,⁴ resulting an authorized annual recovery of \$370;

(c) The ten-year amortization of the \$25,000 expense associated with emergency septage hauling during certain months of 2007 approved by the Commission in Case No. 08-277-WS-AIR,⁵ resulting in an authorized annual recovery of \$2,500; and

¹ See Case No. 03-318-WS-AIR, Opinion and Order dated October 6, 2004, at 15.

² See Case No. 08-227-WS-AIR, Paragraph 2.g of Joint Stipulation and Recommendation dated April 29, 2009 adopted by Opinion and Order dated May 27, 2009, at 15.

³ See Case No. 03-318-WS-AIR, Opinion and Order dated October 6, 2004, at 14.

⁴ See Case No. 08-227-WS-AIR, Paragraph 2.g of Joint Stipulation and Recommendation dated April 29, 2009 adopted by Opinion and Order dated May 27, 2009, at 15.

⁵ See Case No. 08-227-WS-AIR, Paragraph 2.c of Joint Stipulation and Recommendation dated April 29, 2009 adopted by Opinion and Order dated May 27, 2009, at 15 (providing that the actual cost associated with emergency septage hauling of \$51,905 should be capped at \$25,000 for ratemaking purposes and amortized over ten years); see also Case No. 08-227-WS-AIR, Direct Testimony of Staff Witness Ed Richardson, April 29, 2009 Hearing Transcript, at 9.

(d) The four-year amortization of the \$14,920 road repair expense approved by the Commission in Case No. 08-277-WS-AIR,⁶ resulting in an authorized annual recovery of \$3,730.

The Staff's determination of allowable adjusted test-year O&M expense is understated by the sum of these previously authorized annual recovery amounts, or \$7,312. Although the five-year amortization of the allowance for rate case expense approved by the Commission in Case No. 08-227-WS-AIR is also incomplete, W&S recognizes that the Commission's long-standing policy has been to exclude unrecovered rate case expense resulting from an amortization in the prior case in determining the allowable expenses in the applicant utility's next rate case. Thus, despite the fact that it has not yet been made whole for the costs incurred in connection with the preparation and prosecution of its application in Case No. 08-227-WS-AIR, W&S has no objection to the Staff's failure to include an allowance for this unrecovered cost. However, in all other instances where the Commission has approved a multi-year amortization of a specific test-year expense due to its extraordinary nature, but cost recovery has not been completed at the time of the applicant utility's next rate case, the Commission has routinely approved the continuation of the amortization in its order in the succeeding case, as evidenced its order in Case No. 08-227-WS-AIR approving the continuation of the amortizations authorized in Case No. 03-318-WS-AIR.

4. W&S objects to the Staff's adjustment to test-year insurance expense set forth in Schedule C-3.7 of the Staff Report. As described at page 6 of the Staff Report, the Staff's

⁶ See Case No. 08-227-WS-AIR, Paragraph 2.e of Joint Stipulation and Recommendation dated April 29, 2009 adopted by Opinion and Order dated May 27, 2009, at 15 (providing that that the road repair expense component of the Staff proposed allowance general plant maintenance expense shown in Schedule C.3.11 of the Staff Report in that case should be increased by \$4,836 and that the resulting total road repair expense should be subject to a four-year amortization). See also Staff Stipulation Workpapers, Schedule C-3.11.

(\$15,988) adjustment to insurance expense has two separate components: (a) adjustments to annualize insurance expense based on the level of the insurance premiums applicable at the end of the test year, and (b) an allocation of one-half of the test-year pollution, umbrella, and property insurance expense to “non-regulated business operations.” W&S agrees that the annualization adjustments are appropriate and have been correctly calculated, but objects to the exclusion of one-half of the resulting adjusted insurance expense, which, as shown in the underlying Staff workpaper, Schedule WPC-3.7, reduced the allowance for insurance expense by \$9,178.

Although the narrative at page 6 of the Staff Report does not identify the “non-regulated business operations” to which Staff has allocated one-half of the insurance expense, Staff Schedule WPC-3.7 indicates that the expense was divided between W&S and Richfield Furnace Run Associates (“RFRA”). Although W&S and RFRA have the same member-owners, RFRA is a totally separate legal entity from W&S, has no ownership interest in W&S or in any of W&S’s property or business, and maintains its own insurance coverage on its own property and business. The insurance premiums in question were paid solely and directly by W&S and were for coverage that relates solely to W&S’s sewer plant and sewer business. Accordingly, Staff’s allocation of one-half of W&S’s insurance expense to RFRA is unreasonable and improper.

Although the rationale is not stated in the Staff Report, it may be that Staff allocated one half of the insurance expense to RFRA based on the fact that RFRA is also identified as a named insured on the policies. If so, Staff has incorrectly interpreted the significance of RFRA being included as named insured. The utility facilities were acquired from the previous owner as a part of a larger transaction that also included the purchase of some 125 acres of real property adjacent to the utility service area. RFRA orchestrated the purchase, but, at closing, W&S, an LLC

created to operate the utility facilities as a public utility, took title to the utility facilities, RFRA took title to the real property, and the total purchase price was allocated between the two companies. In view of the manner in which the interests were transferred, the management of W&S and RFRA foresaw the possibility that RFRA could also be named as a defendant in an action for damages in connection with the sewer operations, whether brought against the previous owner of the sewer facilities, against W&S as the successor to the previous owner, or against W&S in its own right. Thus, RFRA was identified as a named insured on the W&S policies to provide RFRA with protection in the event any of these scenarios occurred. However, the important point for the purpose at hand is that identifying RFRA as an additional insured on the W&S policies had no effect on the cost of the premiums; *i.e.*, W&S would have incurred precisely the same expense for pollution, umbrella, and property insurance had RFRA not been named as an additional insured. Thus, Staff erred in failing to include the entire amount of the annualized insurance premiums paid by W&S as an allowable expense.

5. W&S recognizes that the recommended allowance for rate case expense set forth in the Staff Report must necessarily be based on an estimate, and, thus, does not object to the Staff's proposed \$15,000 allowance as a placeholder for this item. Further, because the level of actual expense W&S will ultimately incur in connection with this proceeding is a function of whether the case is actually litigated, which, of course, cannot be known at this time, W&S endorses the Staff recommendation that the Commission review the late-filed rate case expense exhibit W&S will submit after the conclusion of the hearing in this matter before making a final determination of the appropriate allowance for rate case expense.⁷ However, in supporting this Staff recommendation, W&S wishes to make it clear that it is not agreeing to the Commission's

⁷ See Staff Report, 6.

usual practice of using the initial rate case expense estimate as an upper bound of the rate case expense allowance and adjusting the initial estimate only when the late-filed exhibit indicates that the actual costs will be less than the estimate. Although this approach may arguably be appropriate where the original estimate is prepared by the applicant utility, because this is an abbreviated application, the \$15,000 estimate in the Staff Report represents the Staff's estimate, not that of W&S. Under these circumstances, the updated estimate in the late-filed exhibit should control without regard to whether it is above or below the initial Staff estimate. W&S does not object to the Staff's proposal that the allowance for rate case expense be amortized over five years.

(RATES AND TARIFFS)

6. Although W&S did not propose any changes to its tariff as a part of its application in this case other than the substitution of the rates proposed in the application for the current rates,⁸ Staff has recommended revisions to several current tariff provisions, some of which relate to rule changes adopted by the Commission after the application was filed,⁹ and the remainder of which are basically housekeeping-type changes.¹⁰ Staff recommends that these changes be incorporated in the compliance tariff filing following the Commission's order in this case. Although the non-rate provisions of its Commission-approved tariff were not placed in issue by the application, W&S has no objection to the tariff changes proposed by Staff.

With respect to the change to its current bill format required by the OAC rule amendments adopted by the Commission in its November 29, 2011 finding and order in Case

⁸ See Application, Exhibit 1.

⁹ See *In the Matter of the Amendment of Certain Rules of the Ohio Administrative Code to Implement Section 4911.021, Revised Code*, Case No. 11-4910-AU-ORD (Finding and Order dated November 29, 2011) (amending, *inter alia*, Rules 4901:1-15-16 and 4901:1-1-15-23(A)(13), OAC, which govern the content of the references to contact information for the Office of the Ohio Consumers' Counsel in the notification of customer rights and bill messages, respectively).

¹⁰ See Staff Report, 9-11.

No. 11-4910-AU-ORD, W&S notes that, by its March 16, 2012 motion for waiver in the rulemaking proceeding, W&S has specifically requested that the changes to the bill format set forth in Appendix C of its tariff be considered in the context of this proceeding. However, W&S suggests that the interests of efficiency would be best served if W&S provides draft language for the bill message and the other provisions in question to Staff in advance of the hearing of this matter so that any issues can be resolved by the Commission before W&S files its compliance tariffs in response to the Commission's order. W&S supports the Staff recommendation that the bi-monthly customer and the flat bi-monthly rate be consolidated into a single bi-monthly flat charge,¹¹ and will modify the current rate format accordingly as a part of the draft provisions provided to the Staff.

7. Although W&S appreciates Staff's recognition of the problem created by W&S's inability to disconnect its customers residing in multi-unit condominiums for nonpayment and understands that the two potential remedies suggested in the Staff Report are merely intended to promote discussion of this issue,¹² W&S questions the efficacy of these remedies. While W&S agrees that making the condominium association the customer could address the problem, W&S must point out that the Commission has no jurisdiction over the arrangements between a condominium association and its members and no authority to require a condominium association to become the customer. Further, W&S does not understand how Staff's suggestion that a rate option that that would include a "no usage" component would create an incentive for customers than cannot be disconnected to pay their bills in a timely manner. Thus, W&S requests that Staff clarify this recommendation in its testimony in the case and reserves the right to object to this proposal pending clarification by the Staff.

¹¹ See Staff Report, 15.

¹² See Staff Report, 11-12, 15.

8. W&S objects to the Staff's failure to recommend that the rate increase authorized herein be implemented on a bills-rendered basis. Although recognizing that the Staff Report is silent on this subject, and, thus, does not signal Staff's position on this issue, W&S wishes to emphasize that, with bi-monthly billing, if the rate increase is implemented on a service-rendered basis, collection of the new rate could be delayed for as long four months from the date of the Commission's order. Such a result would clearly be unreasonable, particularly in light of the substantial operating losses W&S has sustained under its current rates. Moreover, with a flat rate, the usual argument for implementing a rate increase on a service-rendered basis – that customers should have an opportunity to adjust their usage in response to the higher rate – does not apply.

SUMMARY OF MAJOR ISSUES

Pursuant to the attorney examiner's entry of February 24, 2012, W&S identifies the following as major issues in this case:

1. The appropriate allowance for insurance expense;
2. The appropriate annual allowance to reflect amortizations approved by the Commission in Case Nos. 03-318-WS-AIR and 08-227-WS-AIR; and
3. The appropriate effective date of the rate increase authorized in this proceeding.

Respectfully submitted,



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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing has been served upon the following parties by first class mail, postage prepaid, this 23rd day of March 2012.


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