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September 11, 2009

Sara Kyle, Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

Via E-mail and Hand Delivery

filed electronically in docket office on 09/11/09

Attention: Sharla Dillon

Re: Petition of Lynwood Utility Corporation to Change and Increase Rates and
Charges
Docket No. 09-00034


Dear Chairman Kyle:

I have enclosed for filing an original and five copies of Lynwood Utility Corporation's
Post Hearing Brief in this docket.

This Post Hearing Brief and this cover letter are being filed electronically by electronic
mail this same date. A copy has been served on the Ryan McGehee and T. Jay Warner, Counsel
for the Consumer Advocate. Please return the additional copy of the Post Hearing Brief stamped
filed to me.

Thank you for your assistance.

Sincerely yours,



DONALD L. SCHOLES

c: Ryan McGehee
Tyler Ring
Jim Ford

BEFORE THE TENNESSEE REGULATORY AUTHORITY

Nashville, Tennessee

IN RE:

PETITION OF LYNWOOD UTILITY)	
CORPORATION TO CHANGE AND)	DOCKET NO. 09-00034
INCREASE RATES AND CHARGES)	

POST HEARING BRIEF OF LYNWOOD UTILITY CORPORATION

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BEFORE THE TENNESSEE REGULATORY AUTHORITY

Nashville, Tennessee

IN RE:

PETITION OF LYNWOOD UTILITY)	
CORPORATION TO CHANGE AND)	DOCKET NO. 09-00034
INCREASE RATES AND CHARGES)	

POST HEARING BRIEF OF LYNWOOD UTILITY CORPORATION

Lynwood Utility Corporation (Lynwood or Company) submits this post-hearing brief in support of its Petition to increase its rates and charges as requested in the Petition. Lynwood asserts that the Petition, the staff requests and responses, the discovery requests and responses and the testimony at the hearing justify the approval of new rates and charges to produce additional annual revenues of \$185,440. This post-hearing brief will primarily address the issues in this docket which were contested at the hearing by the Consumer Advocate and Protection Division (the Consumer Advocate).

I. Introduction

Lynwood Utility Corporation provides sewer service to approximately 830 customers within its service area in Williamson County just north of the City of Franklin. Lynwood was granted its original certificate of public convenience and necessity by the Tennessee Public Service Commission on June 14, 1976. Lynwood provides sewer service to residential customers located in the Cottonwood Subdivision, Legends Ridge Subdivision, River Landings

Subdivision and a few residences near these subdivisions and to two non-residential customers, a church and a school.

In establishing just and reasonable rates for Lynwood, the Authority must take into account the actual costs of Lynwood to operate its sewer treatment plant and collection system and must provide it a fair rate of return on its investment in its sewer system. As a sewer utility the operation of Lynwood's sewer system is strictly regulated by the Tennessee Department of Environment and Conservation (TDEC). Lynwood must operate, maintain and replace its sewer infrastructure to meet the rules and regulations of TDEC governing sewer systems and must comply with the terms and parameters of its NPDES permit issued by TDEC to discharge its effluent into the Harpeth River. If Lynwood fails to comply with TDEC regulations or with the terms and parameters of its NPDES permit, Lynwood and its owners are subject to civil penalties issued by TDEC, and the owners of Lynwood could be criminally prosecuted for such noncompliance. T.C.A. § 69-3-115. Unless the Authority approves rates to provide Lynwood with sufficient revenue to operate, maintain and replace its sewer infrastructure, Lynwood cannot meet its service obligations or and cannot meet its environmental obligations to its customers and the citizens of Tennessee who use and enjoy the Harpeth River.

Lynwood asserts that in developing its revenue requirements, the Authority should recognize that Lynwood is a small sewer utility. As a small utility Lynwood has fewer customers than most municipal sewer systems which are able to spread its cost of providing sewer service over a larger customer base. Lynwood is not like Tennessee-American Water Company which has shareholders which can finance expenses the Authority may deem inappropriate for ratemaking purposes and which is capable of going to the capital markets to

obtain funding for capital improvements. Lynwood is owned by Southern Utility Corporation. Tyler Ring and John Ring are the sole shareholders of Southern Utility Corporation. Tyler Ring and John Ring have taken their obligations to operate the Lynwood sewer system seriously. They have personally secured and guaranteed the \$1,450,000 outstanding debt of Lynwood. The Authority must approve a fair rate of return on Lynwood's investment to permit it to continue meeting its public utility obligations.

II. Criteria for Establishing Just and Reasonable Rates

The Authority is vested with the power to establish utility rates that are "just and reasonable." This duty requires the Authority to examine not only what is just and reasonable for the customer, but also what is a just and reasonable rate of return for the utility.¹ "When these rates are fixed so low that the utility cannot get a fair return, this amounts to the taking of property for public use without just compensation and is confiscatory."² The Authority "is obligated to balance the interests of the utilities subject to its jurisdiction with the interests of Tennessee consumers, *i.e.*, it is obligated to fix just and reasonable rates."³

The Authority has traditionally considered four criteria when determining the appropriate rate for a utility:

- 1) The investment or rate base upon which the utility should be permitted to earn a fair rate of return;
- 2) The proper level of revenues for the utility;
- 3) The proper level of expenses for the utility; and

¹ *Southern Bell Tel. & Telegraph Co. v. Tenn. Public Serv. Comm'n*, 304 S.W.2d 640, 642-43 (Tenn. 1957).

² *Id.* at 643.

³ *Tennessee Cable Television Ass'n v. Tennessee Public Service Comm'n*, 844 S.W.2d 151, 159 (Tenn. Ct. App. 1992).

- 4) The rate of return the utility should earn on its rate base.⁴

The United States Supreme Court has provided the following guidance on establishing a fair rate of return:⁵

- 1) The rate of return should maintain the financial integrity of the utility;
- 2) The rate of return should allow the company to attract capital for investment and operations; and
- 3) The rate of return on equity should be commensurate with returns investors could achieve by investing in other enterprises of corresponding risk.

III. Test Period and Attrition Period

In this case Lynwood selected a historical test period of the twelve months ending December 31, 2008. Lynwood made adjustments for known and measurable changes to develop a forecast for the attrition year, the twelve months ending December 31, 2009. No dispute exists between Lynwood and the Consumer Advocate on the test period and attrition year used by Lynwood.

IV. Contested Issues

Lynwood and the Consumer Advocate do not agree on the revenues and expenses for the attrition year as a result of a dispute on six issues. Lynwood and the Consumer Advocate do not agree on the Lynwood's rate base for the attrition year as a result of a dispute on three rate base related issues. The position of Lynwood is summarized in Exhibit 1 which is attached to this post-hearing brief.

⁴ See e.g., *In re: Petition of Tennessee-American Water Company to Change and Increase Certain Rates and Charges so as to Permit it to Earn a Fair Rate of Return on Its Property Used and Useful in Furnishing Water Service to its Customers*, Docket No. 06-00290; *In re: Petition of Aqua Utilities Company for Approval of Adjustment of its Rates and Charges and Revised Tariff*, Docket No. 06-00187, 2007 Tenn. PUC LEXIS 405, at 9.

⁵ See *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Bluefield Water Works & Improvement Co. v. P.S.C.*, 262

- (1) Tap fees should continue to be treated as contributions in aid of construction for the attrition year and should not be considered revenue to Lynwood.

Lynwood has historically treated the payment of tap fees as contributions in aid of construction. The Authority has not considered tap fees paid by Lynwood customers as revenue for ratemaking purposes.⁶ In setting Lynwood's rates in its last two rate cases, Docket No. 99-00507 and Docket No. 07-00007, the revenues used in setting and approving rates for Lynwood did not include tap fees as revenue. The Consumer Advocate intervened and participated as a party in both of these rate case dockets and did not take the position that Lynwood's tap fees should be considered revenues in either case.

In the present case the Consumer Advocate has asserted that tap fees should be considered revenue for the test period and the attrition year.⁷ In the 2008 test period, Lynwood received five tap fees in the amount of \$17,500.⁸ The Consumer Advocate asserts that the Authority should set rates for the attrition year based upon the receipt of 18 tap fees in the 2009 attrition year.⁹ Therefore, the Consumer Advocate asserts that \$63,000 in tap fee revenue should be included as operating revenue for ratemaking purposes for the attrition year.¹⁰ The Consumer Advocate's position is unrealistic, inappropriate and contrary to accepted ratemaking principles for a utility such as Lynwood.

U.S. 679 (1923).

⁶ James B. Ford, Rebuttal Testimony at 5.

⁷ Dave Peters, Direct Testimony at 6; Hearing Transcript at 205-06 (hereinafter cited as Tr. ____.)

⁸ Dave Peters, Supplemental Direct Testimony, Exhibit 2.

⁹ Dave Peters, Supplemental Direct Testimony, Exhibit 2.

¹⁰ James B. Ford, Rebuttal Testimony at 4.

Setting rates by assuming the receipt of \$63,000 in annual tap fees as operating revenue is unrealistic. Mr. Peters' projected increase of tap fees of \$45,500 for the attrition year over the tap fees actually received in the test period is based upon a fictitious number and is unsupported by the record in this case. In the test period Lynwood received five tap fees in the amount of \$17,500. Mr. Ford testified that through June 30, 2009, Lynwood had received only one tap fee in 2009.¹¹ Mr. Peters provided no facts to the Authority upon which the Authority can rely in setting the attrition year revenue based upon the payment of 18 tap fees to Lynwood. Mr. Peters mistakenly assumed Lynwood received a tap fee for each new customer gained by Lynwood in 2008. Mr. Peters' assumption was not correct. Mr. Ford explained that a time lag exists between the time a tap fee is paid by a homebuilder for a lot and a new customer is added to Lynwood's system upon the completion of a home on the lot; therefore, there is no direct correlation between changes in Lynwood's customer count each year and the tap fees received in a year.¹²

Certainly, Mr. Peters' increase in tap fees is not an appropriate "known and measureable change" in tap fees for the attrition year. To the contrary, the potential number of building lots the Company's service area supports a finding that Lynwood's level of tap fees paid in 2008 test period will likely continue. In its Response to the Staff's Clarifying Question No. 6 filed on July 22, 2009, Lynwood outlined the number of lots in the subdivisions it is serving which are still vacant.¹³ Out of the 865 lots in these existing subdivisions, only 47 potential buildable lots remain.¹⁴ Of these 47 potential buildable lots, only 33 may potentially become customers of Lynwood since the City of Franklin may very well service the 14 lots in the Farmington

¹¹ James B. Ford, Rebuttal Testimony at 4.

¹² *Id.*

¹³ Response to Staff's Clarifying Questions, No. 6. (July 22, 2009)

¹⁴ *Id.*

Subdivision under any agreement with Williamson County.¹⁵ Therefore, Mr. Peters' assumption that Lynwood will receive 18 taps per year in the future is unrealistic.

Mr. Peters cites the Authority's decision in *In Re: Petition of Aqua Utilities Company for Approval of Adjustment of its Rates and Charges and Revised Tariff*, Docket No. 06-00187, 2007 Tenn, PUC Lexis 405 (November 27, 2007) (hereafter cited as *Aqua Utilities*) as support for the Authority to consider Lynwood's tap fees as revenue in this case.¹⁶ The specific facts in *Aqua Utilities* which led the Authority to treat taps fees as revenues are substantially different from the facts in the present case. In *Aqua Utilities* the utility forecasted customer growth at the rate of 27 customers per year for a two year period based upon historical growth.¹⁷ The Authority approved customer growth of 27 water/sewer customers and an additional 12 water only customers for the attrition year.¹⁸ *Aqua Utilities* had projected a revenue deficiency of \$559,109 for its attrition year and had a customer base of 294 customers.¹⁹ The huge revenue deficiency of Aqua Utilities and its small customer base coupled with the projected increase in customers led the Authority to include its tap fees as revenue.

Neither circumstance exists in the present case. Lynwood projected no specific customer growth in this case. Lynwood only had five tap fees paid in the 2008 test period, and only had one tap fee paid through June 30, 2009.²⁰ The revenue deficiency projected by Lynwood of \$185,440 with a customer base of 832 customers is not comparable to Aqua Utilities. Therefore,

¹⁵ Tr. 108.

¹⁶ Tr. 213-14.

¹⁷ *Aqua Utilities* at 12-13.

¹⁸ *Id.*

¹⁹ *Id.* at 43 and at 20 n.18.

²⁰ James B. Ford, Rebuttal Testimony at 10.

the Authority should not use *Aqua Utilities* as a precedent to treat Lynwood's tap fees as revenue.

The treatment of tap fees as revenue is inappropriate for setting rates for Lynwood. If the Authority sets rates for Lynwood assuming \$63,000 of tap fees as revenue, Lynwood will be filing another rate case in 2010 based upon the actual tap fees it has received in 2008 and in 2009. Setting rates using a fictitious number of tap fees to be received as operating revenue will not provide sufficient revenue for Lynwood to meet its operating expenses and provide it a reasonable return on its investment. Moreover, tap fees received by Lynwood may vary significantly from year to year depending on the economy, the number of buildable lots within subdivisions within Lynwood's service area and the level of development activity in Lynwood's service area.²¹ To set rates based upon a revenue source which may vary significantly from year to year will cause Lynwood to have revenues in excess of or less than the amount of revenue used to set rates in this case. Using tap fees as revenues to set Lynwood's rates in this case will set it up to either over earn or under earn its projected earnings for the attrition year and is simply not appropriate for Lynwood or its customers.

Lynwood asserts that the Authority should continue to treat its tap fees as contributions in aid of construction. Mr. Ford testified that under the NARUC system of accounting, tap fees are to be charged to Account 271 – Contributions in Aid of Construction.²² The NARUC accounting instructions for Account 271 – Contributions in Aid of Construction provides that this account shall include “[a]ny amount or item of money, services or property received by a utility, from any person or governmental agency, any portion of which is provided at no cost to the utility,

²¹ James B. Ford, Rebuttal Testimony at 5.

which represents an addition or transfer to the capital of the utility, and which is utilized to offset the acquisition, improvement or construction costs of the utility's property."²³ Tap fees paid by Lynwood customers fall within this definition. While the Authority may have the discretion to deviate from this NARUC accounting instruction for a compelling reason for a particular utility, the Authority should have a compelling reason for doing so. No such compelling reason exists in the present case. The Authority should continue to treat Lynwood's tap fees as contributions in aid of construction as it has historically done so in past rate cases.

- (2) Purchased power expense for the attrition year should be based upon the actual electric bills paid by Lynwood during 2009.

Lynwood projected purchased power expense for the attrition year at \$62,794.²⁴ The Consumer Advocate projected purchased power expense for the attrition year at \$52,328 which was Lynwood's actual electric power expense for the 2008 test period.²⁵ The Consumer Advocate assumes no increase in Lynwood's power expenses for the attrition year. For the first six months of 2009, Lynwood paid its electric provider, Middle Tennessee Electric Membership Corporation, \$36,830 for electricity which represents a 14.7% increase over the first six months of 2008.²⁶ If Lynwood pays the same amount for electricity for the last six months of the 2009 attrition year as it paid for the first six months, Lynwood's purchased power expense for 2009 will be \$73,660. If the 14.7% increase experienced for the first six months of 2009 is applied to the 2008 test period expense of \$52,328, Lynwood's purchased power expense will be \$60,020

²² *Id.* at 4-5.

²³ James B. Ford, Rebuttal Testimony, Exhibit JBF-2

²⁴ James B. Ford, Direct Testimony at 4.

²⁵ Dave Peters, Direct Testimony at 4 and Schedule 2.

for the attrition year. The most accurate estimate of Lynwood's purchased power expense for the 2009 attrition year should be based upon its actual experience in 2009 to date rather than assuming no increase as asserted by the Consumer Advocate. Therefore, Lynwood's projected purchased power expense of \$62,794 is fair and reasonable and should be used for setting rates in this case.

- (3) Compensation to Tyler Ring in the amount of \$32,000 for work performed in connection with the management and operation of Lynwood should be included in this rate case.

Lynwood included \$32,000 of the compensation for Tyler Ring in this rate case which was his compensation from Lynwood for the 2008 test period.²⁷ Mr. Ford testified that \$16,000 of his compensation was charged to Account 734.2 – Management Fee and \$16,000 of his compensation was charged to Account 105 – Construction Work in Progress.²⁸ Mr. Ford testified that Mr. Ring's compensation was based upon his working 15 hours a week for Lynwood for a total of 780 hours a year.²⁹ Mr. Ford testified that in 2008 Mr. Ring actually worked 1,146 hours for Lynwood based upon time sheets completed by Mr. Ring for 2008.³⁰ The allocation of Mr. Ring's compensation between Account 734.2 – Management Fee and Account 105 – Construction Work in Progress was based upon a study of his actual time spent on management of operations and maintenance and administration of construction oversight for

²⁶ James B. Ford, Rebuttal Testimony at 1 and Exhibit JBF-1.

²⁷ Second Supplemental Response to Second Discovery Request of the Consumer Advocate and Protection Division, Request No. 4, (July 31, 2009).

²⁸ Tr. 149.

²⁹ Tr. 148-49.

³⁰ *Id.*

the months of October through December of 2007.³¹ Mr. Ford testified that using an allocation of Mr. Ring's compensation based upon a study was an appropriate way to allocate his compensation for the test period.³²

Mr. Ring testified that he is involved in all aspects of the management, daily operation and plant additions of Lynwood.³³ Mr. Ring has a degree in civil engineering and 15 years experience in utility construction.³⁴ Mr. Ring has daily meetings with the sewer treatment plant operator and maintenance personnel for the plant and collection system.³⁵ Mr. Ring has daily discussions with a person who works as a part time secretary for Lynwood on customer related issues.³⁶ He personally responds to all emergencies at the Lynwood system.³⁷ He meets with individuals and the development community regarding capacity and connections to the Lynwood system.³⁸ He researches all expenditures of Lynwood and discusses expenditures and regulatory financial issues with Mr. Ford.³⁹ He meets with all government agencies which regulate or deal with Lynwood including the Authority, TDEC, Williamson County, City of Franklin and H. B. & T. S Utility District.⁴⁰ Mr. Ring testified that the Lynwood sewer treatment plant discharges into the Harpeth River which is a 303(d) stream which has discharge requirements which require

³¹ *Id.* at 165-66.

³² *Id.* at 167.

³³ Tyler Ring, Direct Testimony at 2.

³⁴ James B. Ford, Direct Testimony at 148.

³⁵ Tyler Ring, Direct Testimony at 2; Tr. 51.

³⁶ *Id.*

³⁷ *Id.*

³⁸ *Id.*

³⁹ Tr. 52.

⁴⁰ Tyler Ring, Direct Testimony at 2; Tr. 51.

extreme environmental protection of the river.⁴¹ As such, Lynwood's NPDES permit has very tight parameters for water discharged into the river which Mr. Ring anticipates will continue to get tighter which will increase Lynwood's costs of treating its sewer for discharge in the future.⁴²

Mr. Peters testified that in his opinion Mr. Ring's compensation for ratemaking purposes should be limited to \$15,000 for the attrition year.⁴³ Mr. Peters appears to base his opinion on the fact that Mr. Ring is involved in several other companies;⁴⁴ however, Mr. Peters does not provide any evidence to indicate that Mr. Ring does not work the 780 hours for Lynwood which Mr. Ford included in Lynwood's case. Therefore, the time spent by Mr. Ring in working for Lynwood is undisputed. Mr. Peters attempts to support his opinion based upon the 2008 Salary and Benefit Survey performed by the Tennessee Association of Utility Districts.⁴⁵ Mr. Peters testified that this Survey shows that the average salary for a general manager of a wastewater utility in Middle Tennessee to be \$19.52 per hour.⁴⁶ A review of the Survey shows that the average salary for a general manager in the Survey makes no distinction among water, wastewater and natural gas utilities.⁴⁷ The Survey does not distinguish general manager positions for wastewater systems which are collection only systems and wastewater systems which operate treatment plants.⁴⁸ The Survey does not distinguish general manager positions for sewer treatment systems which operate treatment plants with different levels of discharge

⁴¹ Tr. 118.

⁴² Tr. 118.

⁴³ Dave Peters, Supplemental Direct Testimony at 1.

⁴⁴ *Id.*

⁴⁵ Tr. 214.

⁴⁶ *Id.*

⁴⁷ See First Supplemental Response to First Discovery Request of the Consumer Advocate and Protection Division, No. 6 (June 2, 2009).

⁴⁸ *Id.*

quality.⁴⁹ The Survey does not indicate the educational level or experience of the general managers who responded to the Survey.⁵⁰ Moreover, the general manager's salary does not include the value of fringe benefits a general manager receives as an employee.⁵¹ Therefore, this Survey provides little reliable comparison information on the compensation of Mr. Ring for his work for Lynwood. Aside from this Survey Mr. Peters laid no foundation for his opinion on the value of Mr. Ring's services to Lynwood. He testified that he did not know what work and processes were involved in the operation of Lynwood's sewer collection and treatment system.⁵² He testified that he had no idea how the operation of the Lynwood system would compare to other sewer companies which operated sewer treatment systems different from and with less stringent TDEC parameters than Lynwood.⁵³ Mr. Peters made no independent evaluation or comparison of Mr. Ring's compensation other than the Survey provided to him.

Mr. Peters testified that none of Mr. Ring's compensation should be capitalized and become a part of utility plant because "utility plant is something you should be able to touch, look at."⁵⁴ Mr. Peters' testimony is contrary to the uniform system of accounts which provides for certain intangibles to be capitalized in recording utility plant in service.⁵⁵ Paragraphs 14 and 15 of the Accounting Instructions for the Uniform System of Accounting for Utility Plant in Service provide that construction costs to be included in utility plant in service include intangibles such as "engineering, supervision, general office salaries and expenses, construction

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² Tr. 225.

⁵³ Tr. 221, 227.

⁵⁴ Tr. 216.

⁵⁵ Letter to Sara Kyle, Chairman dated July 31, 2009 in response to Staff Request.

engineering and supervision by other than the accounting utility, legal expenses, insurance, injuries and damages, relief and pensions, taxes and allowance for funds used during construction.”⁵⁶

Mr. Ring’s compensation of \$32,000 included for the attrition year is reasonable based upon the testimony of Mr. Ring, and Mr. Ford’s accounting for his compensation for ratemaking purposes is appropriate.

4. Lynwood’s regulatory expense for the attrition year includes an appropriate amount for rate case expenses.

Mr. Ford included \$33,524 for regulatory expenses for the attrition year.⁵⁷ In regulatory expenses he included \$15,000 related to Lynwood’s 2007 rate case, \$12,000 related to this rate case, \$4,153 for utility inspection and assessment fees and \$2,371 for expenses connected to Authority filings and issues not related to its rate cases.⁵⁸ On behalf of the Consumer Advocate, Mr. Peters adjusted Lynwood’s regulatory expense by \$8,371.⁵⁹ He made his adjustment by reducing the annual rate case expense related to this rate case by \$6,000 and excluding the \$2,371 in other Authority related expenses.⁶⁰ Mr. Peters did not object to the \$4,153 for utility inspection and assessment fees. Mr. Peters gave no testimony in support of his exclusion of the \$2,371 in other Authority related expenses; therefore, this amount should be included in regulatory expenses for the attrition year since Mr. Ford’s testimony on including this amount is uncontradicted in the record.

⁵⁶ *Id.*

⁵⁷ James B. Ford, Rebuttal Testimony at 3.

⁵⁸ *Id.*

⁵⁹ Dave Peters, Direct Testimony, Schedule E-5

Mr. Peters testified that Lynwood's rate case expense in this case should be \$18,000 rather than \$36,000.⁶¹ Mr. Peters' justification for this reduction was his opinion that \$18,000 was "a more realistic cost based upon the amount of Regulatory Expenses in relation to total expense increases approved" and because of "rate case frequency."⁶² Lynwood questions the validity of Mr. Peters' opinion on an appropriate amount of rate case expense since he has only filed testimony in one utility rate case in his career before this case.⁶³

The Authority should not reduce Lynwood's projected rate case expense in this case from \$36,000 to \$18,000. In *Aqua Utilities* the Authority recognized "the Company's right to due process and the retention of outside consultants and attorneys" in preparing for a rate case.⁶⁴ In that case the Authority approved a rate case expense of \$46,250 for a utility with 294 customers resulting in a rate case expense per customer of \$157.31.⁶⁵ The Authority approved this rate case expense although it recognized the expense was high.⁶⁶ In comparison, the rate case expense included by Lynwood of \$36,000 in the present case results in a rate case expense of approximately \$43.00 per customer (assuming a Lynwood customer count of 832 customers). Moreover, the rate case expense included by Lynwood for the present case is less than its actual rate case expense for its 2007 rate case of \$45,000.⁶⁷ When the Authority seeks to reduce a

⁶⁰ Dave Peters, Direct Testimony at 4.

⁶¹ *Id.*

⁶² *Id.*; Tr. 209.

⁶³ Tr. 219.

⁶⁴ *Aqua Utilities* at 21.

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ Tr. 151. – Mr. Ford testified he did not believe that the amount included in Lynwood's 2007 rate case for rate case expense was an agreed upon amount between Lynwood and the Consumer Advocate because the settlement agreement in the rate case provided that the rate case determined no issue other than the agreed amount of revenue deficiency and provided that the settlement agreement have no precedent effect in any future proceeding or be

utility's rate case expense, such a reduction places a small utility such as Lynwood in a dilemma. The utility has the burden of proving its need for rate relief and is strongly encouraged to maintain its books and records in the manner required by the uniform system of accounting in doing so. A small utility must hire outside consultants to meet its burden. The reduction in rate case expense sends an opposite signal to the utility that it should keep its rate case expenses down to reduce the costs to its customers. Lynwood believes that its rate case expense for the present case strikes an appropriate balance between these two competing interests. Therefore, Lynwood's regulatory expenses for the present case are reasonable and appropriate.

5. No adjustment to Lynwood's sludge removal expense of \$34,617 for the attrition is warranted.

Mr. Peters adjusted Lynwood's sludge removal expense by \$3,147 because Lynwood was allegedly recovering this amount of sludge removal expense in its sewer surcharge.⁶⁸ Mr. Ford explained that the sludge removal expense included with the sewer surcharge was charged to Account 186.7 and was removed from the test period.⁶⁹ Because Mr. Peters had no grounds for making his adjustment to Lynwood's sludge removal expense, this adjustment should not be accepted.

6. Lynwood's working capital amount of \$52,579 is reasonable based upon its actual operations and Authority precedent on this issue.

Mr. Ford testified that the working capital amount included in the rate base of \$52,579 was based upon a lead/lag time study between when cash is expended and cash is received for

binding on the parties. Tr. 153.

⁶⁸ Dave Peters, Direct Testimony at 5.

⁶⁹ James B. Ford, Rebuttal Testimony at 3.

funding Lynwood's operations.⁷⁰ Mr. Peters claims that the working capital requirement should be 1/12 of total operating expenses less depreciation which amount is \$39,845, but he states no reason for using this standard.⁷¹ In contrast, in *Aqua Utilities* the Authority stated that working capital to be included in the rate base for the utility in that case should be 1/8 of the attrition year operating expenses less depreciation.⁷² If the Authority used this standard in the present case, the working capital amount for Lynwood would be \$64,430. Lynwood's working capital amount of \$52,579 is fully supported based upon its lead/lag time study and prior Authority precedent on this issue.

7. Mr. Peters' adjustment of \$301,578 to Lynwood's contribution in aid of construction should be rejected.

Since the 2007 rate case Mr. Ford testified that he completed a detailed property study related to Lynwood's plant records, depreciation calculations and contributions in aid of construction to arrive at an accurate utility plant in service amount for Lynwood.⁷³ Mr. Ford testified that this property study was begun as a part of the 2007 rate case to arrive at a proper amount of utility plant in service upon which to base rates and that he worked with the Consumer Advocate to accomplish this goal.⁷⁴ The portions of the property study related to contributions in aid of construction and the collection system were completed after the 2007 rate case settlement.⁷⁵ In this study a detail accounting was made of all tap fees received by Lynwood by

⁷⁰ James B. Ford, Rebuttal Testimony at 7, Exhibit JBF-8.

⁷¹ Dave Peters, Direct Testimony at 7-8.

⁷² *Aqua Utilities* at 32.

⁷³ James B. Ford Rebuttal Testimony at 6, Exhibit JBF-4; Tr. 188.

⁷⁴ James B. Ford, Rebuttal Testimony at 6; Tr. 155, 188.

⁷⁵ James B. Ford, Rebuttal Testimony at 6.

the year in which they were received and recorded as contributions in aid of construction.⁷⁶

Then, the correct amortization expense for these tap fees was calculated by year to arrive at an accurate amount for contributions in aid of construction to be used for Lynwood's utility plant in service account.⁷⁷ The result of this detailed accounting was to bring utility plant in service to the proper amount for the test period.

Mr. Peters objects to Mr. Ford's adjustment to correct utility plant in service to take into account the correct amount of contributions in aid of construction to bring the rate base back to the proper level upon which Lynwood's rate of return should be based.⁷⁸ Mr. Peters suggests that Mr. Ford's correction by crediting retained earnings required Authority approval.⁷⁹ On cross-examination Mr. Ford explained that because Lynwood has no retained earnings, the adjustment to retained earnings has no effect on Lynwood's rates.⁸⁰ Moreover, Mr. Ford testified that the corrected utility plant in service amount was included in Lynwood's 2007 Annual Report.⁸¹

Lynwood asserts that proper ratemaking mandates that its utility plant in service account be accurate. Mr. Ford has reviewed Lynwood's property records and properly amortized tap fees recorded as contributions in aid of construction. The Consumer Advocate's position that the proper amortization of Lynwood's contributions in aid of construction in determining Lynwood utility plant in service should not be permitted in this case is inappropriate and unsupported in the record.

⁷⁶ *Id.*

⁷⁷ James B. Ford, Rebuttal Testimony, Exhibit JBF-5

⁷⁸ Tr. 211.

⁷⁹ Tr. 211.

⁸⁰ Tr. 188.

8. Lynwood's rate base should include \$191,089 for its collection system.

Mr. Ford testified that the detailed property study in 2007 determined that no cost had been captured for Lynwood's internal costs of adding a tap to its collection system.⁸² Mr. Ford recommended that for connections prior to January 1, 2007, Lynwood capitalize \$500 per tap based on the time incurred by Company personnel to bring a tap for service on line in the collection system, and Lynwood outlined the work required for new connections to its collection system.⁸³ These collection system amounts were determined by year and the proper amounts of depreciation were calculated for each year.⁸⁴ The amounts related to the study were recorded in Lynwood's books through December 31, 2006 of \$151,750 and accumulated depreciation of \$22,252.⁸⁵ Mr. Ford stated that from January 1, 2007 to December 31, 2008, Lynwood instituted and has followed construction order procedures to capture Lynwood's direct costs and internal costs incurred for additions to the collection system.⁸⁶ Since January 1, 2007, collection system additions based upon these construction order procedures have been \$39,339.⁸⁷ Mr. Ford stated that Lynwood's direct and internal costs incurred in the addition of taps to its collection system are properly charged as component costs to Lynwood's utility plant in service and is consistent with the uniform system of accounting instructions for utility plant in service.⁸⁸

⁸¹ Tr. 187.

⁸² James B. Ford, Rebuttal Testimony at 6.

⁸³ James B. Ford, Rebuttal Testimony at 6-7, Exhibit JBF-6.

⁸⁴ *Id.*

⁸⁵ James B. Ford, Rebuttal Testimony at 7.

⁸⁶ James B. Ford, Rebuttal Testimony at 7; Tr. 182-83

⁸⁷ James B. Ford, Rebuttal Testimony at 7.

⁸⁸ Tr. 182-83. Letter to Sara Kyle, Chairman dated July 31, 2009 in Response to Staff Request.

As previously stated, Mr. Peters took the position that only a tangible asset which can be touched or looked at should be included as utility plant in service.⁸⁹ Therefore, he concludes the internal costs of Lynwood incurred in adding new connections to its collection system should not be included in utility plant in service.⁹⁰ Mr. Peters' position is not consistent with the accounting instructions of the uniform system of accounting for utility plant in service. Under paragraph 15 of these accounting instructions, utility plant in service is to include as construction costs "[a]ll overhead costs such as engineering, supervision, general office salaries and expenses, construction, engineering and supervision by others than the accounting utility, legal expenses, insurance, injuries and damages, relief and pensions, taxes and allowance for funds used during construction."⁹¹ Therefore, Mr. Peters' recommendation that no collection system additions should be added to Lynwood's utility plant in service should be rejected.

Again, Mr. Ford has established the appropriate amount for utility plant in service to bring it up to the proper level for ratemaking purposes by including the direct and internal construction costs related to the collection system. For the calendars years 2007 and 2008, the collection system additions are based upon the construction work order system set up by Lynwood to capture direct and internal costs related to new connections to the collection system. The amount for the 2008 test period was \$22,839.⁹² If this amount is not included as utility plant in service related to the collection system for 2008, then this amount needs to be included in operating expenses for the attrition year. Mr. Peters agreed.⁹³

⁸⁹ Tr. 211.

⁹⁰ Tr. 211.

⁹¹ Letter to Sara Kyle, Chairman dated July 31, 2009 in Response to Staff Request.

⁹² *Id.*

⁹³ Tr. 230-31.

Lynwood's utility plant in service account must be accurate for rates to be set properly. Lynwood's utility plant in service account should include its direct and internal (overhead) costs incurred for new connections to its collection system in accordance with the uniform system of accounting. Therefore, Lynwood utility plant in service should include the \$191,089 amount related to its collection system. Because the collection system amount of \$191,089 should be included in utility plant in service, the adjustment made by Mr. Peters of \$8,413 to the depreciation expense for the attrition year related to the collection system should also be rejected.

9. Lynwood is entitled to earn a return of 8% on its rate base.

Mr. Ford testified that Lynwood should earn a return of 8% on its rate base.⁹⁴ Mr. Peters asserts that Lynwood should only earn a return of 7.5%, its interest cost on its outstanding debt.⁹⁵ Mr. Ford stated that Lynwood's cost of capital is comprised its of interest cost on debt plus the cost to place the debt which includes legal, accounting, appraisals, title searches, insurance and bank fees etc.⁹⁶ Since 2000, the Authority has set Lynwood's cost of capital at 8%.⁹⁷ In the past the two rate cases, the Consumer Advocate has agreed with the wisdom of the Authority in setting an 8% return on rate base. The rate of return should remain at 8%.

V. Conclusion

Lynwood has carried its burden of demonstrating that it needs additional annual revenue of \$185,440. The Consumer Advocate's recommended adjustments are based primarily upon

⁹⁴ James B. Ford, Rebuttal Testimony at 9.

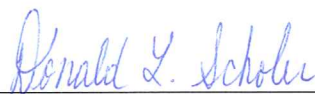
⁹⁵ Dave Peters, Direct Testimony, Schedule 7.

⁹⁶ James B. Ford, Rebuttal Testimony at 9.

⁹⁷ *Id.*

conjecture and the unsubstantiated opinion of its witness, Mr. Peters. Lynwood must have the additional revenue it seeks to operate its sewer treatment plant and collection system in compliance with TDEC regulations and the terms and conditions of its NPDES permit and to provide adequate customer service.

Respectfully submitted,



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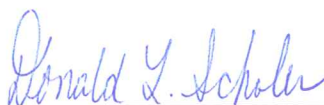
Dated: September 11, 2009.

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of this Post Hearing Brief of Lynwood Utility Corporation was served via U.S. Mail and electronic mail upon:

Ryan L. McGehee
T. Jay Warner
Associate Attorney General
Office of the Attorney General
Consumer Advocate and Protection Division
P.O. Box 20207
Nashville, Tennessee 37202-0207

This the 11th day of September, 2009.



DONALD L. SCHOLES

Lynwood Utilities Corporation
Operating Income and Rate Base
For Attrition Year Ending December 31, 2009

Line #

1	Sewer Revenue - Usage Based	\$539,105
3	Penalty Fees	\$8,163
4	Inspection Fees	\$1,000
5	Total Revenues	<u>\$548,268</u>
6	Purchased Wastewater	\$2,551
7	Sludge Removal	\$34,617
8	Purchased Power	\$62,794
9	Chemicals	\$42,450
10	Materials & Supplies	\$20,502
11	Engineering Inspections	\$2,701
12	Testing	\$31,488
13	Repairs & Maintenance	\$89,030
14	Operations Management	\$28,800
15	Billing and Collection Fees	\$44,966
16	Bad Debt Expenses	\$10,334
17	Accounting and Bookkeeping	\$16,635
18	Tax Accounting	\$2,850
19	Accounting - Other	\$13,049
20	Legal	\$8,899
21	Management	\$16,000
22	Rent	\$10,344
23	Insurance	\$18,699
24	Other Misc. Expenses	\$1,629
25	Taxes Other Than Income Taxes	\$20,716
26	Regulatory Expenses	\$33,524
27	Depreciation & Amortization, Net	\$121,569
28	Total Operating Expense	<u>\$ 634,147</u>
29	Net Operating Income ("NOI")	<u>\$ (85,879)</u>
	Rate Base	
30	Plant in Service	\$ 3,122,341
31	Deferred Debits and Deposits	143,618
32	Cash Working Capital	<u>52,574</u>
33	Total	\$ 3,318,533
	Less Deductions:	
34	Accumulated Depreciation	1,602,052
35	Contributions In Aid of Construction	687,524
36	Total Deductions	<u>2,289,576</u>
37	Rate Base (line 38- Line 44)	<u><u>1,028,957</u></u>