

**BEFORE THE TENNESSEE REGULATORY AUTHORITY**

**NASHVILLE, TENNESSEE**

**November 12, 2015**

**IN RE:**

**JOINT PETITION OF AQUA UTILITIES  
COMPANY AND TRA STAFF (AS A PARTY)  
TO INCREASE RATES AND CHARGES**

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**DOCKET NO.  
15-00044**

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**FINAL ORDER APPROVING *JOINT PETITION***

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This matter came before Chairman Herbert H. Hilliard, Director Kenneth C. Hill and Director James M. Allison of the Tennessee Regulatory Authority (the “Authority” or “TRA”), the voting panel assigned to this docket, at a regularly scheduled Authority Conference held on June 29, 2015, for consideration of the *Joint Petition* filed on April 9, 2015, by Aqua Utilities Company (“Aqua” or “Company”) and Authority Party Staff (“Party Staff”).<sup>1</sup>

Upon consideration of the entire record, including all exhibits and the testimony of the witnesses, the panel unanimously concluded that the Company had a Revenue Deficiency of \$72,416 which should be recovered through increases to the base and volumetric rates for residential and commercial customers and an increase in tap fees for new customers.

**BACKGROUND AND TRAVEL OF THE CASE**

Aqua is a public utility as defined by Tenn. Code Ann. § 65-5-103 and provides water and wastewater service to approximately 371 residential water customers and 301 residential wastewater customers located in Aqua’s service territory in Hardin County, Tennessee.<sup>2</sup> The

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<sup>1</sup> Party Staff in this matter consists of Joe Shirley and David Foster, employees of the Authority; *Memorandum*, (April 7, 2015).

<sup>2</sup> *Joint Petition*, p. 1 (April 9, 2015).

Company purchases water from the City of Savannah which Aqua delivers to customers.<sup>3</sup> Aqua has no employees and relies upon contractual services to perform and maintain utility operations.<sup>4</sup> Aqua's service area is predominately a lake resort community bordering the Tennessee River near Pickwick Landing State Park and serves residential customers only.<sup>5</sup> Aqua's last rate case before the Authority was Docket No. 06-00187.<sup>6</sup>

On April 9, 2015, Aqua and Party Staff filed a *Joint Petition* requesting approval of a rate increase. According to the *Joint Petition*, the Company is projected to experience a net operating loss of \$57,597 for the Twelve Month Attrition Period Ending May 31, 2016.<sup>7</sup> Utilizing a proposed Operating Margin Method, as opposed to the Rate Base Method, the Company projects a revenue deficiency of \$72,416 during the attrition period absent any rate relief.<sup>8</sup>

At a regularly scheduled Authority Conference held on April 20, 2015, the panel voted unanimously to convene a contested case proceeding and appoint the Authority's General Counsel or her designee to act as Hearing Officer to prepare this matter for hearing, including establishing a procedural schedule, entering a protective order, and ruling on intervention requests and discovery issues.<sup>9</sup> On May 5, 2015, the Consumer Advocate and Protection Division of the Office of the Attorney General ("Consumer Advocate") filed correspondence with the Authority indicating it had reviewed the filings in the docket, including the proposed rates and supporting documentation, and had determined it would not intervene.<sup>10</sup> The Consumer Advocate stated it has determined that the rates and charges proposed by Aqua and

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<sup>3</sup> James E. Clausel, Pre-filed Direct Testimony, p. 1 (April 10, 2015).

<sup>4</sup> *Id.* at 3.

<sup>5</sup> Joe Shirley, Pre-filed Direct Testimony, p. 3 (April 10, 2015).

<sup>6</sup> *In re: Petition of Aqua Utilities Company for Approval of Adjustment of Its Rates and Charges and Revised Tariff*, Docket No. 06-00187, *Final Order Approving Rates and Rate Design* (November 27, 2007).

<sup>7</sup> *Id.* at 2.

<sup>8</sup> *Id.* at 12.

<sup>9</sup> *Order Convening a Contested Case and Appointing a Hearing Officer* (May 5, 2015).

<sup>10</sup> *Letter of the Consumer Advocate to Chairman Hilliard* (May 5, 2015).

the TRA Party Staff are fair and reasonable.<sup>11</sup>

This matter was noticed for hearing by the Authority and placed on the agenda for the May 11, 2015, Authority Conference.<sup>12</sup> On May 8, 2015, a letter of opposition to the proposed rates was filed by the President of the Points of Pickwick Owners Association (“Pickwick Association”), an association of home and lot owners served by Aqua. In addition to opposing the *Joint Petition*, the Pickwick Association requested “adequate time” to engage legal representation for the purposes of intervening in the docket.<sup>13</sup>

At the Authority Conference held May 11, 2015, the panel, on its own motion, voted to hold the hearing in abeyance until the next Authority Conference on June 29, 2015, and allow the Pickwick Association until June 1, 2015, to file for intervention in the docket.<sup>14</sup> Thereafter, neither the Pickwick Association nor any other party sought intervention in the docket. A Hearing on this matter was scheduled for June 29, 2015, as noticed by the Authority on June 19, 2015.

### **JOINT PETITION**

Prior to the filing of the *Joint Petition*, Party Staff inspected the Company’s books and records at the Company’s office in Savannah, Tennessee, solicited information from Aqua’s ownership and toured the utility plant and service area.<sup>15</sup> Based on the information obtained from inspecting Aqua’s books and records, Party Staff performed a cost of service study. The Party Staff created a test year and an attrition year, utilizing the Twelve Months Ended December 31, 2014, as the test period and the Twelve Months Ended May 31, 2016, as the

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<sup>11</sup> *Id.*

<sup>12</sup> *Notice of Hearing* (April 20, 2015).

<sup>13</sup> *Letter of Opposition from Points of Pickwick Homeowners Association to Proposed Rates Increase*, p. 2 (May 8, 2015).

<sup>14</sup> Transcript of Authority Conference, pp. 4-9 (May 11, 2015).

<sup>15</sup> Joe Shirley, Pre-filed Direct Testimony, p. 5 (April 10, 2015); Transcript of Authority Conference, p. 32 (June 29, 2015).

attrition period.<sup>16</sup> The Party Staff used historical data, including expense invoices, and made adjustments to reflect a “normal” year of operations, a review requiring the removal of non-recurring expenses and items which are disallowed for ratemaking purposes.<sup>17</sup> Based on this analysis, the Party Staff built the attrition year with adjustments for known and measureable changes.<sup>18</sup> The Party Staff projected operating revenues of \$174,103 and operating expenses of \$231,700 at the end of the attrition period, resulting in a net operating loss of \$57,597.<sup>19</sup>

As part of the calculations of the fair profit component of revenue requirement, the Party Staff recommended using the Operating Margin Method.<sup>20</sup> In the Company’s previous rate case in Docket No. 06-00187, the revenue requirement used to set rates used the Rate Base Method to calculate a fair return on investment.<sup>21</sup> In this docket, Party Staff proposed an operating margin of 6.5%, a proposal Aqua agreed with.<sup>22</sup> Party Staff testified that generally, the Operating Margin Method is used to build reserves for smaller utilities that have little customer growth and insignificant rate base.<sup>23</sup>

Aqua invested in a significant expansion of its water and wastewater system in anticipation of new customer growth which has not been realized.<sup>24</sup> Party Staff concluded that the Company’s new construction in combination with little customer growth has resulted in under-utilized plant.<sup>25</sup> Party Staff testified that the amount of utility plant on a per customer basis has more than doubled since the Company’s last rate case.<sup>26</sup> According to the Party Staff,

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<sup>16</sup> *Id.* at 4.

<sup>17</sup> *Id.* at 4-5.

<sup>18</sup> *Id.*

<sup>19</sup> *Id.* TRA Staff Exhibit Schedule 3.

<sup>20</sup> *Id.* at 2-4.

<sup>21</sup> *In re: Petition of Aqua Utilities Company for Approval of Adjustment of Its Rates and Charges and Revised Tariff*, Docket No. 06-00187, *Final Order Approving Rates and Rate Design*, p. 19 (November 27, 2007).

<sup>22</sup> Joe Shirley, Pre-filed Direct Testimony, p. 4 (April 10, 2015).

<sup>23</sup> *Id.* at 3.

<sup>24</sup> *Id.*

<sup>25</sup> *Id.*

<sup>26</sup> *Id.*

Aqua's current customers should not be required to pay higher costs associated with under-utilized plant through the Rate Base Method.<sup>27</sup>

Utilizing an Operating Margin of 6.5%, Party Staff calculated a "fair profit" component requirement is \$15,060.<sup>28</sup> This amount, taken together with a projected net operating loss of \$57,597 and a revenue conversion factor of 0.996683 that recognizes the impact of forfeited discounts and taxes on new revenues results in a revenue deficiency of \$72,416.<sup>29</sup>

Mr. Shirley testified that in comparison to the revenue deficiency of \$72,416 calculated using the Operating Ratio Method, the revenue deficiency calculation under the Rate Base Method is \$199,791.<sup>30</sup> Mr. Shirley concluded that the effect of shifting to rates established using the Operating Margin Method, as opposed to the Rate Base Method, has the effect of significantly reducing the projected revenue deficiency which must be recovered through rates.<sup>31</sup> Mr. Shirley noted that the Authority has previously approved settlement agreements in rate cases for small utilities that included the provision of operating margins of 6.5%.<sup>32</sup> Party Staff stated that Aqua could return to using the traditional Rate Base Method of setting rates if the Company experiences enough customer growth in the future to warrant it.<sup>33</sup>

The Party Staff proposed the following rate design, which increases both the fixed and volumetric charges for water and wastewater customers intended to recover the revenue deficiency: 1) For water service, increase the minimum monthly charge for the first 1,000 gallons from \$12.00 to \$19.65; increase the volumetric charge for monthly water use in excess of 1,000 gallons from \$2.89 per 1,000 gallons applied pro-rata to \$3.05 per 1,000 gallons applied

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<sup>27</sup> *Id.*

<sup>28</sup> *Id.* at 12

<sup>29</sup> *Id.*; TRA Staff Exhibit Schedules 1, 5.

<sup>30</sup> *Id.* TRA Staff Exhibit Schedules 1-1a.

<sup>31</sup> *Id.* at 14.

<sup>32</sup> *Id.* at 4; *See In re: Petition of Tennessee Wastewater Systems, Inc. for Approval to Amend Its Rates and Charges*, Docket No. 08-00202, *Order Approving Settlement Agreement*, p. 4, 6 (July 8, 2009); *In re: Petition of Cartwright Creek, LLC to Change and Increase Rates and Charges*, Docket No. 09-00056, *Order Approving Settlement Agreement*, p. 3 (March 2, 2010).

<sup>33</sup> *Id.* at 4.

pro-rata; increase the reconnect charge due to seasonal disconnects from \$60.00 to \$120.00; and increase the new water service connection charge (tap fee) from \$1,000.00 to \$1,425.00; and

2) For wastewater service, increase the minimum monthly charge for the first 1,000 gallons from \$12.00 to \$19.65; increase the volumetric charge for monthly wastewater use in excess of 1,000 gallons from \$2.89 per 1,000 gallons applied pro-rata to \$3.05 per 1,000 gallons applied pro-rata; increase the reconnect charge due to seasonal disconnects from \$60.00 to \$120.00; and increase the new wastewater service connection charge (tap fee) from \$1,000.00 to \$1,425.00.<sup>34</sup>

According to Mr. Shirley, if the proposed rates and charges proposed by the Party Staff are approved, it would result in an increase of the average monthly residential water bill from \$18.85 to \$26.88, which constitutes a 42.6% increase over the eight-year period since Aqua's last rate adjustment; and the average monthly residential wastewater bill is projected to increase from \$17.11 to \$25.04, which constitutes a 46.3% increase over the eight-year period since Aqua's last rate adjustment.<sup>35</sup>

The Party Staff testified that rates paid by Aqua customers will still be lower than those paid by neighboring residential customers in Hardin County who are served by the City of Savannah.<sup>36</sup> While recognizing the proposed rates are a material increase, the Party Staff testified such increases are justified by the reasonable and necessary costs the Company is experiencing in order to provide utility service.<sup>37</sup>

### **THE HEARING**

A Hearing on this matter was held on June 29, 2015, as noticed by the Authority on June 19, 2015. Participating in the Hearing were the following parties:

Aqua Utilities Company – Charles B. Welch Jr., Esq., Farris Bobango PLC, 618 Church Street, Suite 300, Nashville, TN 37219.

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<sup>34</sup> *Id.* at 13-14; Party Staff Exhibit, Schedule 7.

<sup>35</sup> *Id.* at 14.

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*; Transcript of Authority Conference, p. 38 (June 29, 2015).

TRA Party Staff – David Foster and Joe Shirley, Tennessee Regulatory Authority, 502 Deaderick Street, Fourth Floor, Nashville TN 37243.

At the Hearing, the panel heard testimony from Company witness James E. Clausel and Party Staff witness Joe Shirley in support of the *Joint Petition*. In addition, members of the public were given the opportunity to present comments to the panel. The Consumer Advocate made public comments and stated it had no opposition to the *Joint Petition*.<sup>38</sup> No one else submitted or offered public comments at the Hearing on June 29, 2015. No opposition to the *Joint Petition* was presented.

### **CRITERIA FOR JUST AND REASONABLE RATES**

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.<sup>39</sup> The Authority must also approve rates that provide regulated utilities the opportunity to earn a just and reasonable return on their investments.<sup>40</sup> The Authority considers petitions for a rate increase, filed pursuant to Tenn. Code Ann. § 65-5-203, in light of the following criteria:

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
4. The rate of return the utility should earn.

Applying these criteria, and upon consideration of the entire record, including all exhibits and the testimony of the witnesses, the panel made the following findings and conclusions.

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<sup>38</sup> Transcript of Authority Conference, pp. 27-28 (June 29, 2015).

<sup>39</sup> Tenn. Code Ann. § 65-5-201 (2015).

<sup>40</sup> See *Bluefield Water Works and Improvement Company v. Public Service Commission of the State of West Virginia*, 262 U.S. 679, 43 S.Ct. 675 (1923).

## **FINDINGS AND CONCLUSIONS**

After the Hearing on June 29, 2015, the panel considered the *Joint Petition*. The panel found that the rates and charges proposed in the *Joint Petition* filed by Aqua and the Party Staff were just and reasonable and in the public interest.

In summary, the provisions of the proposed rate increase include:

1. A historic Test Period of the twelve-months ended December 31, 2014;
2. A forward looking Attrition Period of the twelve-months ended May 31, 2016;
3. An Operating Margin Ratio of 6.5%;
4. Total Attrition Period Operating Revenues of \$174,103;
5. Total Attrition Period Operating Expenses of \$231,700;
6. Fair Operating Margin of \$15,060;
7. Gross Revenue Conversion Factor of 0.996683; and
8. A Revenue Deficiency of \$72,416.<sup>41</sup>

Based on the uncontested evidence in the docket, the panel voted unanimously to approve the *Joint Petition* as filed. The panel found that the proposed rates were within the “zone of reasonableness” that takes into consideration both the interests of the consumer and the utility,<sup>42</sup> and further promote the public interest by balancing the interests of the utility consumers and the provider. The panel further voted unanimously to approve the tariff filed with the *Joint Petition* with an effective date of June 29, 2015, to implement the proposed rates to generate the revenues required to cover the Revenue Deficiency.

### **IT IS THEREFORE ORDERED THAT:**

1. The *Joint Petition* is approved as filed.
2. The tariff filed with the *Joint Petition* is approved with an effective date of June 29, 2015.

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<sup>41</sup> *Id.*; TRA Staff Exhibit Schedules 1, 3-5.

<sup>42</sup> See *Tennessee Cable Television Ass’n v. Public Serv. Comm’n*, 844 S.W. 2d 151, 159 (Tenn. Ct. App. 1992).



3. Any party aggrieved by the Authority's decision in this matter may file a Petition for Reconsideration with the Authority within fifteen days from the date of this Order.

4. Any party aggrieved by the Authority's decision in this matter has the right to judicial review by filing a Petition for Review in the Tennessee Court of Appeals, Middle Section, within sixty days from the date of this Order.

**Chairman Herbert H. Hilliard and Director Kenneth C. Hill concur. Director James M. Allison concurred with the motion.**

**ATTEST:**



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**Earl R. Taylor, Executive Director**