

**BEFORE THE TENNESSEE PUBLIC UTILITY COMMISSION**

**NASHVILLE, TENNESSEE**

**February 21, 2018**

**IN RE:**

**PETITION OF TENNESSEE WATER SERVICE,  
INC. FOR APPROVAL OF AN INTERIM  
EMERGENCY WILDFIRE RESTORATION  
SURCHARGE, INTERIM EMERGENCY  
WATER SERVICE AVAILABILITY  
SURCHARGE, INTERIM EMERGENCY MAKE-  
WHOLE SURCHARGE, AND AN INTERIM  
EMERGENCY OPERATION COST PASS-  
THROUGH MECHANISM**

**DOCKET NO.  
17-00108**

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**FINAL ORDER**

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This matter came before Chairman David F. Jones, Vice Chairman Robin L. Morrison and Commissioner Keith Jordan of the Tennessee Public Utility Commission (the “Commission” or “TPUC”), the voting panel assigned to this docket, at a regularly scheduled Commission Conference held on January 16, 2018, for consideration of the *Petition for Emergency Interim Relief* (“*Petition*”) filed by Tennessee Water Service, Inc. (“TWS” or the “Company”) on September 25, 2017.

**BACKGROUND AND TRAVEL OF THE CASE**

TWS is a public utility subject to the Commission’s jurisdiction, providing water service to customers located in the Chalet Village Subdivision (“Chalet Village”) in Sevier County, Tennessee.<sup>1</sup> Chalet Village suffered extensive damage in the wildfires that swept through the Great Smoky Mountains in late November 2016 (“the Wildfire”). Prior to the Wildfire, TWS served about

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<sup>1</sup> *Petition for Emergency Interim Relief*, pp. 1-2 (September 25, 2017).

580 customers. After the Wildfire, approximately 90% of the customer base was lost with only 57 connections remaining active and the water system serving Chalet Village suffered damage.<sup>2</sup>

On September 25, 2017, TWS filed a *Petition* seeking emergency relief in the form of three monthly surcharges, an operational cost pass-through mechanism, and a deferral of costs and uncollectible revenues for potential future recovery. The *Petition* also proposed to file a petition for a general rate case no more than eighteen months after approval of the emergency relief requested by TPUC.<sup>3</sup> In support of its *Petition*, the Company filed the testimony of Richard Linneman,<sup>4</sup> Finance, Planning and Analysis Manager of TWS, and Bryce Mendenhall,<sup>5</sup> Vice President of Operations of TWS.

On September 28, 2017, the Consumer Protection and Advocate Division of the Office of the Tennessee Attorney General (“Consumer Advocate”) filed a *Petition to Intervene*.<sup>6</sup> The intervention of the Consumer Advocate was subsequently granted by the Hearing Officer.<sup>7</sup> Following the submission of discovery and pre-filed testimony pursuant to a procedural schedule, the parties prepared for a hearing. In addition, written comments were received from individual Chalet Village property owners as well as persons signing an online petition.

## **POSITION OF THE PARTIES**

### **POSITION OF TWS**

TWS presented two alternate requests for relief, styled “Option A” and “Option B,” each of which was an amended version of the relief requested in its *Petition*.<sup>8</sup> As presented, Option A consisted of the following components:

1. An Operation Cost Pass-Through mechanism allowing TWS to pass-

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<sup>2</sup> *Id.* at 2-3.

<sup>3</sup> *Id.* at 5-9.

<sup>4</sup> Richard Linneman, Pre-Filed Direct Testimony (September 25, 2017).

<sup>5</sup> Bryce Mendenhall, Pre-Filed Direct Testimony (September 25, 2017).

<sup>6</sup> *Petition to Intervene* (September 28, 2017).

<sup>7</sup> *Order Granting the Petition to Intervene Filed by the Consumer Advocate* (October 6, 2017).

<sup>8</sup> Transcript of the Hearing, pp. 52-57 (December 12, 2017).

through to customers nondiscretionary increases or decreases in costs incurred for purchases of treated water and/or purchased electricity;<sup>9</sup>

2. A Wildlife Restoration Surcharge of \$2.52 per month for eighteen months applicable to both active and inactive customers to provide a return on the capital needed to repair fire damage and restore the water system to operational capacity;<sup>10</sup>

3. A Water Service Availability Surcharge of \$4.51 per month for eighteen months applicable to both active and inactive customers to provide a return on capital assets that are already in place to serve customers;<sup>11</sup>

4. A Make-Whole Surcharge of \$11.09 per month for eighteen months applicable only to inactive customers to recover anticipated 2018 operational losses due to erosion of the customer base since the Wildfire;<sup>12</sup>

5. A Deferral of Prior Operating Losses for 2017 allowing TWS to accumulate and defer its operating losses incurred during 2017 into a regulator asset account for potential future recovery from customers over a proposed five-year amortization period; and,<sup>13</sup>

6. A Deferral of Case Expenses, deferring up to \$30,000 of case expenses amortized over a three-year period.<sup>14</sup>

TWS next presented Option B which consisted of the following components:

1. An Operation Cost Pass-Through mechanism allowing TWS to pass-through to customers nondiscretionary increases or decreases in costs incurred for

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<sup>9</sup> *Id.* at 55.

<sup>10</sup> *Id.* at 55-56.

<sup>11</sup> *Id.* at 56.

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

<sup>13</sup> *Id.* at 56-57.

<sup>14</sup> *Id.* at 57.

purchases of treated water and/or purchased electricity;<sup>15</sup>

2. A Deferral of Prior Operating Losses for 2017 allowing TWS to accumulate and defer its operating losses incurred during 2017 into a regulatory asset account for potential future recovery from customers over a proposed five-year amortization period;<sup>16</sup>

3. A Deferral of Prospective Operating Losses that authorizes TWS to accumulate and defer its operating losses incurred beginning January 1, 2018 for up to eighteen months into a regulatory asset account for potential future recovery from customers over a proposed five-year amortization period;<sup>17</sup>

4. A Deferral of Returns on Certain Capital Projects that authorizes TWS to calculate and accrue its currently-authorized rate of return on capital assets placed into service to repair and restore the water system from fire damage into a regulatory asset account for potential future recovery from customers over a proposed five-year amortization period; and,<sup>18</sup>

5. A Case Expenses Surcharge for recovery of case expenses of up to \$30,000 over a three year period through a surcharge of \$1.44 per month to both active and inactive customers with annual true-ups.<sup>19</sup>

TWS witness, Bryce Mendenhall, testified with regard to capital projects necessary to repair fire damage and restore the water system stating that TWS has already expended \$178,961 for Emergency System Activation, Gatlinburg Water Interconnect Repair, Meter Replacements, Valve Replacements, Service Line Replacements and Fire Hydrant Replacements.<sup>20</sup> Emergency System Activation and Gatlinburg Water Interconnect Repair projects have been completed, but repair and

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<sup>15</sup> *Id.*

<sup>16</sup> *Id.* at 56-58.

<sup>17</sup> *Id.* at 58.

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

<sup>19</sup> *Id.* at 58-59.

<sup>20</sup> *Id.* at 45-46 & Exh. 2.

replacement of meters, valves, service lines and hydrants are ongoing.<sup>21</sup> Mr. Mendenhall also provided testimony identifying proposed capital projects that have not been started, but will need to be completed in order to fully restore the water system: 1) Replacement of Well No. 1 Booster Station forecasted at \$125,000; 2) Replacement of Upper Booster Station forecasted at \$30,000; and, 3) Reconditioning of Upper Storage Reservoir forecasted at \$45,000.<sup>22</sup> These capital projects were facilitated by the fire according to Mr. Mendenhall.<sup>23</sup> TWS witness Richard Linneman testified that these capital projects are the projects for which TWS seeks deferral of returns under Option B as presented.<sup>24</sup>

### **POSITION OF THE CONSUMER ADVOCATE**

The Consumer Advocate presented testimony opposing the Wildfire Restoration, Service Availability and Make-Whole Surcharges requested under Option A, questioning whether the wildfire event represented a true financial emergency justifying the surcharges, raising concerns about the uncertainty of customer counts and forecasting techniques TWS used to compute surcharge amounts, and claiming that the proposed surcharges fail to share the risks between both investors and ratepayers.<sup>25</sup> However, Consumer Advocate witness David Dittmore agreed with TWS's proposed Operational Cost Pass-Through Mechanism, provided certain modifications were incorporated.<sup>26</sup> TWS agreed with the modifications proposed by the Consumer Advocate.<sup>27</sup>

In addition, the Consumer Advocate proposed that deferred accounting methods be used to authorize TWS to defer losses sustained from the Wildfire and recover deferred losses over a specified period of time.<sup>28</sup> The Consumer Advocate and TWS differ on the starting date for accrual

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<sup>21</sup> *Id.*

<sup>22</sup> *Id.*

<sup>23</sup> *Id.* at 49.

<sup>24</sup> *Id.* at 58.

<sup>25</sup> *Id.* at 96-103, 127-129.

<sup>26</sup> *Id.* at 97.

<sup>27</sup> Transcript of the Hearing, pp. 28, 55 (December 12, 2017).

<sup>28</sup> *Id.* at 96.

of accounting losses and the amortization period over which deferred losses should be recovered.<sup>29</sup> Finally, the Consumer Advocate requested that TWS be directed to: 1) conduct a business analysis of whether insurances should be obtained on a going forward basis to protect the Company and ratepayers in the event of such disaster in the future; 2) convert its books to the NARUC Uniform System of Accounting before its next rate case; 3) provide clear guidance to customers regarding their service options; and 4) to make monthly submittals of the Company's active customer accounts in this docket.<sup>30</sup>

### **THE HEARING**

A Hearing on this matter was held on December 12, 2017, as noticed by the Commission on December 1, 2017. Participating in the Hearing were the following parties:

Tennessee Water Service, Inc. – Joe Conner, Esq. and Ryan Freeman, Esq., Baker, Donelson, Bearman, Caldwell & Berkowitz, 1900 Republic Centre, 633 Chestnut Street, Chattanooga, TN 37450.

Consumer Protection and Advocate Division – Vance Broemel, Esq. and Karen Stachowski, Esq., Office of the Attorney General and Reporter, P.O. Box 20207, Nashville TN 37202-0207.

At the Hearing, the panel heard testimony from witnesses Bryce Mendenhall and Richard Linneman on behalf of the Company. Alex Bradley and David Dittmore testified before the panel on behalf of the Consumer Advocate.<sup>31</sup>

In addition, members of the public were given the opportunity to present comments to the panel. Mr. Jimmy Vance, a retired attorney and Chalet Village property owner who was accompanied by his former law partner, Nick Perenich, presented comments concerning the *Petition*. No other members of the public sought recognition to comment.<sup>32</sup>

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<sup>29</sup> *Id.* at 115-116, 121-123, 129.

<sup>30</sup> *Id.* at 129-130.

<sup>31</sup> Transcript of Hearing (December 12, 2017).

<sup>32</sup> *Id.* at 6-22.

## **FINDINGS AND CONCLUSIONS**

The Commission has jurisdiction to set the rates of public utilities operating in the State of Tennessee.<sup>33</sup> TWS is a public utility which was granted a Certificate of Public Convenience and Necessity (“CCN”) by the Commission in Docket No. U-83-7240.<sup>34</sup> TWS’s most recent rate case was completed in 2009.<sup>35</sup> It is appropriate, under ratemaking principles, to allow for recovery of non-recurring costs when a public utility incurred such costs as a result of extraordinary circumstances outside of the control of the public utility, such as a force majeure.

TWS has presented accounting and operational information and forecasts showing the Company has sustained and will continue to sustain material financial losses resulting from the Great Smoky Mountain wildfires that swept throughout its service territory in November 2016. Although the parties disagreed as to the starting point of the deferrals, both TWS and the Consumer Advocate stated that an accounting order authorizing deferred accounting treatment of reasonable costs and losses resulting from the wildfires would be appropriate in this case. Indeed, both TWS and the Consumer Advocate recognized the benefits of deferring accounting losses in this docket to future periods.<sup>36</sup> This accounting convention, which is described in Account 186 of the Uniform System of Accounts, permits the Company to create regulatory assets for accrual of reasonable accounting costs and losses sustained as a result of the wildfires and defer probable recovery of such costs and losses to future periods.

Specifically, the procedure for deferred accounting is recognized in Account 186.A(7) of the Uniform System of Accounts (“USOA”) adopted by the Commission:

Regulatory created assets, not included in other accounts, resulting from the ratemaking actions of regulatory agencies. (See Definition 27). The amounts

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<sup>33</sup> Tenn. Code Ann. §§ 65-4-101(6); 65-4-104; 65-5-101, *et seq.*

<sup>34</sup> *In Re: Petition of Tennessee Water Service, Inc. for a Certificate of Convenience and Necessity to Serve an Unincorporated Area of Sevier County Known as Chalet Village North and to Approve Tariffs as to Customer Rates, Rules and Regulations for Service*, Docket No. U-83-7240, *Order* (January 24, 1984).

<sup>35</sup> *In Re: Petition of Tennessee Water Service, Inc., to Change and Increase Certain Rates and Charges*, Docket No. 09-00017, *Order Approving Settlement Agreement* (September 15, 2009).

<sup>36</sup> Transcript of Hearing, pp. 57, 96 (December 12, 2017).

included in this account are to be established by those charges which would have been included in net income determination in the current period under the general requirements of the Uniform System of Accounts but for it being probable that such items will be included in a different period(s) for purposes of developing the rates that the utility is authorized to charge for its utility services. When specific identification of the particular source of a regulatory asset cannot be made, such as in plant phase-ins, Account 407.5 – Amortization of Regulatory Liabilities shall be credited. The amounts recorded in this account are generally to be charged, concurrently with the recording of the amount in rates, to the same account that would have been charged if included in income when incurred, except all regulatory assets established through the use of Account 407.5 shall be charged to Account 407.4 – Amortization of Regulatory Assets, concurrent with the recovery of the amounts in rates.

If rate recovery of all or part of an amount included in this account is disallowed, the disallowed amount shall be charged to Account 426 – Miscellaneous Nonutility Expenses, or Account 434 – Extraordinary Deductions, in the year of the disallowance.

Additionally, Definition 27 of the USOA provides:

“Regulatory Assets and Liabilities” are assets and liabilities that result from rate actions of regulatory agencies. Regulatory assets and liabilities arise from specific revenues, expenses, gains or losses that would have been included in determination of net income in one period under the general requirements of the Uniform System of Accounts but for it being probable that; 1) such items will be included in a different period(s) for purposes of developing the rates the utility is authorized to charge for its utility services; or 2) in the case of regulatory liabilities, that refunds to customers, not provided for in other accounts, will be required.

The Commission has used this procedure to defer costs related to extraordinary and unforeseen circumstances. For instance, in Docket No. 13-00121 the Commission authorized Kingsport Power Company d/b/a AEP Appalachian Power (“Kingsport Power Company”) to defer incremental storm damage costs as a regulatory asset, stating “[t]his method will allow the Company appropriate ratemaking treatment for extraordinary storm costs in a future rate proceeding.”<sup>37</sup>

The panel found that deferred accounting of TWS’s Wildfire losses, as outlined in Option B, is the best approach in this case because the losses are significant in relation to TWS’s eroded

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<sup>37</sup> *In re: Petition of Kingsport Power Company D/B/A AEP Appalachian Power for Approval of Deferred Accounting, Order Granting Deferred Accounting*, Docket No. 13-00121 (Nov. 13, 2013).



customer base and recovery from the Wildfire will be protracted for TWS and the customers. The deferred accounting approach will permit TWS to accumulate reasonable and necessary costs to repair and restore the water system and to track the amount of losses stemming from revenue shortfalls attributable to customer service interruptions. Giving TWS and customers additional time to recover and rebuild from the wildfires will provide a more complete picture of the financial impact of the Wildfire and will provide better financial and operational information on a going forward basis, which will be valuable in determining appropriate rates and recovery periods.

Based on the evidentiary record, the panel found that although the parties agree that deferred accounting should be used to account for the losses in this docket, they disagree about the starting point. The Consumer Advocate recommends that only prospective accounting losses beginning January 1, 2018 be allowed whereas TWS requests deferral of operating losses beginning January 1, 2017 and deferral of returns on capital assets placed in service to repair and restore the water system. Consumer Advocate witness David Dittmore testified that he did not take issue with any of the operational decisions subsequent to the Wildfire.<sup>38</sup> However, Mr. Dittmore proposed limiting the deferral of costs to the period beginning January 1, 2018 in order to share the losses between TWS and its customers.<sup>39</sup> The panel found that this Commission has addressed the issue of sharing losses resulting from storm damages previously. In dockets addressing deferral of storm damage costs, the Commission did not require shareholders of Kingsport Power Company to bear any of these costs.<sup>40</sup>

Additionally, the relief requested by TWS does not provide full recovery itself. The panel found that while Option B would provide for deferral of actual operating losses since January 1, 2017, as well as returns on capital investments required to restore the system, TWS is not seeking to

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<sup>38</sup> Transcript of Hearing, p. 121 (December 12, 2017).

<sup>39</sup> *Id.* at 115-117.

<sup>40</sup> *In re: Petition of Kingsport Power Company D/B/A AEP Appalachian Power for Approval of Deferred Accounting, Order Granting Deferred Accounting*, Docket No. 13-00121 (Nov. 13, 2013).

recover any operating losses for November and December 2016, nor is it seeking to earn a profit on its existing rate base investment.

Therefore, the panel voted unanimously that TWS should be authorized to create regulatory asset accounts to defer the following:

1. Actual operating losses resulting from reasonable and necessary operating expenses exceeding operating revenues, excluding any provision for return on rate base investment, incurred on operations beginning on January 1, 2017 and continuing until TWS's next rate case petition unless otherwise ordered by the Commission; and

2. Returns on capital projects necessary to repair fire damage and restore the water system to operational status, which were identified in Mr. Mendenhall's testimony, with such returns to be accrued on the actual amount of the capital assets placed into service at TWS' currently-authorized rate of return of 6.89%, and with such accruals beginning on the date the capital asset is placed into service and continuing until TWS's next rate case petition unless otherwise ordered by the Commission.

In addition, the panel voted unanimously to authorize TWS to accrue and defer up to \$30,000 of reasonable and necessary case expenses. The panel directed TWS to file quarterly reports detailing the accounting transactions and account balances for its deferred operating losses, returns on capital assets, and case expenses, with such reports being due at the same time the Company submits its routine quarterly surveillance reports to the Commission.

With regard to amortization of these regulatory assets, the panel found that due to current uncertainties surrounding rebuilding activities and future customer counts, a decision with respect to appropriate amortization periods should be postponed until the rate proceeding when recovery is considered. The panel cautioned TWS, consistent with prior Commission orders authorizing deferred accounting, that full recovery of deferred costs and losses is not guaranteed, and that TWS

should keep sufficient and appropriate financial records and documentation supporting the reasonableness and prudence of the costs and losses deferred pursuant to this docket.

Further, the panel found evidence showing that the deferred costs and losses in this docket are material, especially in relation to the Company's small customer base. Therefore, the panel voted unanimously to approve a \$7.00 per month increase to the minimum service charge for all current and future active customers effective immediately. The panel found that this rate increase will begin to address the Company's financial losses resulting from the Wildfire and will be used to offset the future amortization of the deferred regulatory assets authorized in this docket in an effort to minimize rate shock and shorten recovery periods. Accordingly, the panel voted unanimously that the Company shall report each quarter the amount of quarterly revenues and the amount of aggregate revenues collected from active customers as a result of this \$7.00 per month service rate increase. The quarterly reports shall be due at the same time the Company submits its routine quarterly surveillance reports to the Commission. For the sake of clarity, the Company shall not charge inactive customers or lot owners the minimum service charge.

TWS proposed an Operational Cost Pass-Through Mechanism to which the Consumer Advocate proposed modifications, but otherwise agreed. The voting panel found that the Operational Cost Pass-Through Mechanism, as modified by the Consumer Advocate in Mr. Dittmore's testimony at Exhibit DND-5, would adjust customer rates to reflect any increase or decrease in costs incurred for purchased water and power. Therefore, the panel voted unanimously to approve the mechanism as modified by the Consumer Advocate.

Finally, the panel voted unanimously to direct TWS to file a general rate case petition as soon as practicable in light of its recovery from the 2016 Wildfire, but in no event shall the Company file a rate case petition later than July 1, 2019, without first obtaining a Commission order extending this deadline for good cause.

The panel also voted unanimously to direct TWS to work with Commission staff to file a tariff consistent with this decision within thirty days and denied all other relief requested by the Company and the Consumer Advocate.

**IT IS THEREFORE ORDERED THAT:**

1. The *Petition for Emergency Interim Relief* filed on September 25, 2017 is granted as modified.
2. Tennessee Water Service, Inc. is authorized to create two regulatory asset accounts to defer: a) actual operating losses beginning January 1, 2017 until its next rate case or otherwise ordered; and, b) returns on identified capital projects necessary to repair fire damage and restore the water system to operational status, such returns to be accrued on the actual amount of the capital assets placed into service at Tennessee Water Service, Inc.'s currently-authorized rate of return of 6.89% and beginning on the date the capital asset is placed into service and continuing until its next rate case unless ordered otherwise.
3. Tennessee Water Service, Inc. is authorized to accrue and defer reasonable and necessary case expenses.
4. Tennessee Water Service, Inc. shall increase the minimum service charge for all current and future customers by \$7. Tennessee Water Service, Inc. is not authorized to charge inactive customers or lot owners the minimum service charge.
5. The Operational Cost Pass-Through Mechanism, as modified by the Consumer Protection and Advocate Division of the Office of the Tennessee Attorney General, is approved.
6. Tennessee Water Service, Inc. shall file quarterly reports detailing the accounting transactions and account balances for its deferred operating losses, returns on capital assets, rate case expenses, and the amount of quarterly revenues and the amount of aggregate revenues collected from active customers as a result of the minimum service charge increase.
7. Tennessee Water Service, Inc. shall file a rate case petition no later than July 1,

2019, unless an order from the Tennessee Public Utility Commission extending this deadline for good cause is obtained.

8. Tennessee Water Service, Inc. shall work with Tennessee Public Utility Commission staff to file a tariff consistent with this order within thirty days.

9. All other relief requested by Tennessee Water Service, Inc. and the Consumer Protection and Advocate Division of the Office of the Tennessee Attorney General is denied.

10. Any person who is aggrieved by the Tennessee Public Utility Commission's decision in this matter may file a Petition for Reconsideration with the Tennessee Public Utility Commission within fifteen days from the date of this Order.

11. Any person who is aggrieved by the Tennessee Public Utility Commission'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 David F. Jones, Vice Chairman Robin L. Morrison and Commissioner Keith Jordan concur.**

**ATTEST:**



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**Earl R. Taylor, Executive Director**