

**BEFORE THE TENNESSEE PUBLIC UTILITY COMMISSION
NASHVILLE, TENNESSEE**

**PETITION OF LIMESTONE WATER
UTILITY OPERATING COMPANY, LLC TO
INCREASE CHARGES, FEES AND RATES
AND FOR APPROVAL OF A GENERAL
RATE INCREASE AND CONSOLIDATED
RATES**

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DOCKET NO. 24-00044

CONSUMER ADVOCATE DIVISION'S POST-HEARING BRIEF

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I. STATEMENT OF THE CASE

Limestone Water Utility Operating Company, LLC (“Limestone” or “Company”), a Tennessee limited liability company, is authorized to provide water and wastewater service to customers in Tennessee. Limestone serves approximately 573 water connections in two water systems and approximately 1,914 wastewater/sewer connections in eight wastewater systems.¹ Currently, Limestone serves customers in Hardin, Williamson, Marshall, Hardeman, and Campbell counties in Tennessee.²

Limestone’s principal place of business is located at 1630 Des Peres Road, Suite 140, St. Louis, Missouri.³ Limestone Water is an indirect wholly owned subsidiary of CSWR, LLC, which provides managerial and operational services to the Company.⁴ As of the date of its filed testimony, Limestone stated it has invested more than \$9.5 million in Tennessee to acquire, upgrade, and improve the water and wastewater systems it currently operates in Tennessee.⁵

This rate case Docket is the subject of ten (10) water and wastewater systems owned by Limestone in Tennessee.⁶ Limestone is seeking to increase rates and consolidate those rates across all of those water and wastewater systems. The ten (10) water and wastewater systems are geographically dispersed from West Tennessee to East Tennessee. Since the filing of the Petition, the Commission approved another acquisition by Limestone which includes one wastewater system in Decatur County. Currently, Limestone has one (1) pending system acquisition docket with TPUC.

¹ *Petition of Limestone Water Utility Operating Company, LLC to Increase Charges, Fees and Rates and For Approval of a General Rate Increase and Consolidated Rates*, TPUC Docket No. 24-00044, at 1, July 16, 2024.

² *Id.* at 1.

³ *Id.* at 2.

⁴ *Id.*

⁵ *Direct Testimony of Mike Duncan* at 4.

⁶ *Petition* at 2.

According to Limestone, many of the systems' former owners/operators did not timely seek appropriate and reasonable rate relief or did not seek sufficient, reasonable and appropriate rates to maintain regulatory compliance, failed to invest in system infrastructure, and did not allow for the provision of safe and reliable water and wastewater service and therefore, an increase in rates and consolidation of rates is necessary.⁷

In its Petition, Limestone claimed the systems that it acquired were poorly managed and most of the prior owners of those systems did not have the technical, managerial, and financial ability to make the necessary capital investments to ensure regulatory compliance and provide safe, efficient, and reliable service to customers.⁸ Also, Limestone stated that since previous owners of the systems it acquired failed to timely seek rate increases necessary to enable them to properly operate and maintain the systems, the rates that were in effect and the rates adopted by Limestone were insufficient to cover the operating costs for operations. Limestone further alleged the systems were woefully unprofessional and inadequate and did not provide Limestone with the opportunity for a fair rate of return.⁹ As an example, Limestone used Aqua Utilities system and stated this system has not had a rate increase in 18 years. Similarly, the Shiloh Falls system had not had a rate increase since 2007 and the DSH – Lakeside Estates system had not had a rate increase since 2011.¹⁰

The Company stated this rate filing is designed to achieve two (2) primary objectives.¹¹ First, Limestone needs to increase rates to a level to allow it to provide services that properly serve and protect the public interest and also to permit the Company to recover reasonable operating costs, as well as an opportunity for a fair return on the investments it makes to serve customers. Limestone

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Id.

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Direct Testimony of Mike Duncan at 9.

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Id.

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Id.

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Petition at 3.

also stated it was necessary to unify the terms of service and consolidate rates statewide in a manner that streamlines and simplifies the Company's tariff and supports the economies of scale and related benefits offered by Limestone.¹² Additionally, according to Limestone, there have been increased costs for professionally operating the systems that it had acquired and the systems must comply with applicable laws and regulations.¹³ Limestone stated that several of the systems it had acquired had significant long-term compliance and operational issues, and this rate request reflects the increased capital and operating costs required to address those deficiencies.¹⁴ Limestone had adopted the current rates in effect upon the respective acquisitions of the systems and most did not provide adequate recovery of operating costs, capital investments, or an opportunity to earn a fair return on that investment.¹⁵ Limestone concedes the rates proposed in this case represent a measurable increase over current rates, however, Limestone claims this is the result of previous owners not exercising regulatory diligence in terms of making critical repairs, capital investment, and having professional operations necessary for safe and reliable service to customers.¹⁶

As to Limestone's rate consolidation request, Limestone wants to maximize the benefits from owning several systems to mitigate the rate increase in this case by consolidating rates across the two water systems and eight wastewater systems. This would result in Limestone's customers being charged the same statewide rate for water or wastewater service.¹⁷ Limestone's claim is that consolidating rates allows them to spread costs to a larger customer base and thereby mitigates the rate impacts to small systems whose current capital investment requirements exceed statewide averages.¹⁸ Limestone claims consolidated rates and tariffs also makes rates more affordable for

¹² *Id.*

¹³ *Id.*

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ *Petition at 3.*

¹⁷ *Id.* at 3-4.

¹⁸ *Id.* at 4.

all Limestone's customers and allows the Company to operate the geographically dispersed systems under a single set of uniform standards that promotes and enhances regulatory and administrative efficiency.¹⁹ Limestone stated CSWR, LLC, and its affiliates have significant experience implementing and observing first-hand the benefits of consolidated rates because they have done so in other jurisdictions.²⁰

As to capital improvements for Limestone's systems, Limestone stated there are three (3) large capital projects currently planned: Grassland Wastewater System upgrade, Shiloh Falls spray field expansion, and the Candlewood Lakes redundant well drilling.²¹

This is Limestone's first rate case to set base rates filed in Tennessee. Limestone requests approval for a total annual revenue requirement for the water operations of \$649,455²² and total annual revenue of \$2,410,952 for its sewer operations based on the 12-month test period ending April 30, 2024.²³ Limestone is not seeking an attrition period and instead has used a test period ending April 30, 2024.²⁴

Limestone claimed it has incurred operational losses on its water and sewer operations. The total retained net operating loss as of the end of the test year is \$2,630,461.²⁵ Limestone claimed that the accumulated loss is reflective of many factors including the cost associated with proper and professional operations of the Company's systems and because several of the acquired systems had not had rate increases in many years. The Company's Return on Equity ("ROE") for water operations, based upon current rates, is (35.6)%. Similarly, the Company's ROE for sewer

¹⁹ *Id.*

²⁰ *Id.*

²¹ *Direct Testimony of Jacob Freeman at 3-4.*

²² *Petition at 4.*

²³ *Id.*

²⁴ *MFG Question 021, Responsible Witness: Mike Duncan.*

²⁵ *Petition at 5.*

operations, based upon current rates, is (35.5)%.²⁶

As part of the revenue requirement, Limestone is requesting that it be permitted to earn a 11.90% ROE, which includes an upward adjustment of 1.50% for extraordinary Company specific risks.²⁷ Although Limestone is wholly financed with equity capital, the revenue requirement proposed in this case is based on a hypothetical capital structure consisting of 43.00% long-term debt, at an assumed embedded cost rate of 6.64%, and 57.00% common equity.²⁸ The requested ROE produces a weighted average cost of capital (“WACC”), or overall rate of return, of 9.64% on a total rate base of \$3,272,329.²⁹

The Company submitted pre-filed direct testimony for the following witnesses: Dylan D’Ascendis, Clare Donovan, Mike Duncan, Jacob Freeman, Aaron Silas, Brent Thies, and Todd Thomas.³⁰ The Consumer Advocate presented the pre-filed testimony of William H. Novak, Clark Kaml, Alex Bradley, David N. Dittmore, and Aaron Rothchild. Following the filing of direct testimony by the Consumer Advocate, Limestone submitted pre-filed rebuttal testimony of Dylan W. D’Ascendis, Clare Donovan, Mike Duncan, Aaron Silas, Brent Thies, and Todd Thomas.

A hearing on the merits began on February 18, 2025, and concluded on February 20, 2025. The *Order Establishing Post-Hearing Procedural Schedule* outlined deadlines for the filing of post-hearing briefs and set forth a request by Commission Staff for the filing of additional information from Limestone related to the acquisition premium and rate design.

II. CRITERIA FOR ESTABLISHING JUST AND REASONABLE RATES

The Tennessee Public Utilities Commission (“TPUC” or the “Commission”) has the power

²⁶ *Id.*

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Petition* at 5-6.

to fix just and reasonable rates, which requires the Commission to balance the interests of utilities with the interests of Tennessee consumers.³¹ When any public utility seeks to increase an existing rate the utility has the burden of proof to show such an increase is just and reasonable.³²

Just and reasonable rates should provide a utility with the opportunity to earn a rate of return on used and useful property commensurate with the returns on alternative investments with similar risks.³³ As a general rule, public utility commissions such as the Commission examine investments by a utility to determine whether such investments were “prudent.”³⁴

In prior cases, the TPUC has stated that it considers petitions for a rate increase, filed pursuant to Tenn. Code Ann. § 65-5-203 (now § 65-5-103(a)), 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.³⁵

The Commission has further stated that it “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.”³⁶

In determining rates, the Commission should also ensure that expenses and costs charged to consumers are not so high as to constitute, in effect, capital contributions to the utility:

But if the amounts charged to operating expenses and credited to the

³¹ Tenn. Code Ann. § 65-5-101.

³² Tenn. Code Ann. § 65-5-103(a).

³³ *Bluefield Water Works & Improvement Co. v. West Virginia Public Service Commission*, 262 U.S. 679, 692-3 (1923); *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591 (1944).

³⁴ *Missouri ex rel. Southwestern Bell Telephone Co. v. Public Serv. Comm’n of Mo.*, 262 U.S. 276, 291 (1923); *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 309 (1989).

³⁵ *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 And Adequate Rate Of Return On Its Property Used And Useful In Furnishing Water Service To Its Customers*, TPUC Order, Docket 06-00290, at 20 (June 10, 2008).

³⁶ *Id.*; see also *Tennessee Cable Television Ass’n v. Tennessee Public Service Comm’n*, 844 S.W.2d 151, 159 (Tenn. Ct. App. 1992) (rates should take into consideration the interests of both the consumer and the utility).

account for depreciation reserve are excessive, to that extent subscribers for the telephone service are required to provide, in effect, capital contributions, not to make good losses incurred by the utility in the service rendered and thus to keep its investment unimpaired, but to secure additional plant and equipment upon which the utility expects a return.³⁷

Tennessee law prohibits any utility from making unjust discriminatory charges or unreasonable preferences in its charges.³⁸ In fixing such rates, the Tennessee law provides that the Commission shall take into account the safety, adequacy and efficiency or lack thereof of the service or services furnished by the public utility.³⁹

As an initial matter, however, the Commission must first set the test period and attrition period.⁴⁰

III. TEST PERIOD AND ATTRITION PERIOD

The first step in a rate case is to set and determine the appropriate test period and attrition period. The test period takes into consideration the estimated impact of calculations related to investments, revenues, and expenses; it also helps indicate the rate of return that will be produced. Neither the Commission nor the intervening parties are confined by law or regulatory practice to accepting the test year proposed by the regulated utility seeking a rate increase. Tennessee courts have never required the Commission to use a specific test period methodology for setting rates; and the courts have stated repeatedly that the Commission has the discretion to choose its own test period.⁴¹

³⁷ *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 607 n. 10 (1944).

³⁸ Tenn. Code Ann. § 65-4-122.

³⁹ *Id.*

⁴⁰ As this is a general rate case, consistent with Tenn. Code Ann. §§ 65-5-103(d)(6), *et. seq.*, Limestone respectfully requests that the Commission adopt in this case the methodologies required to allow for the consideration of an annual review of its rates, in the event the Company later determines, at some point in the future within the time frame established by statute, to pursue such an annual review petition before the Commission.

⁴¹ *CF Industries v. T.P.S.C.* 599 S.W. 2d 536, 542 (Tenn. 1980); *Powell Telephone v. T.P.S.C.*, 660 S.W.2d 44, 46 (Tenn. 1983); *Tennessee Cable Tel. v. T.P.S.C.* 844 S.W. 2d 151, 159 (Tenn. Ct. App. 1992) (cert. denied);

The only limit placed on a ratemaking body is the statutory requirement that rates be just and reasonable. Rates need not be determined using definite rules or precise formulas.⁴² Thus, the TPUC is not bound by any specific means by which rates are set so long as the end result produces just and reasonable rates.

In setting rates, the TPUC has unfettered discretion to select the test year period.⁴³ A “test year” is a measure of a utility’s financial operations and investment over a specific twelve month period. It is the “raw material” for developing an attrition year measure of the utility’s financial operations and investment (Rate Base, Operations and Maintenance Expense, Depreciation Expense, and Taxes).

Thus, it is essential that a test year contain and/or be updated with the most accurate and current information available. Normally, a test year is used to calculate and forecast the attrition year. In this case, the Company used a historic test year, and did not use a projected test year. As such, the attrition year and historic test year are the same. The test year is the “finished product” and is the chief determinant in whether a revenue deficiency or surplus exists such that rates must be adjusted.

The use of an up-to-date test year is essential to test the veracity of the company’s proposed rate increase. The methodology of applying a more recent test year has the advantage of providing more accurate and current information for the forecast of the attrition year.

In this rate case, Limestone selected a historical test period of the twelve months ending April 30, 2024 (“Test Period”).⁴⁴

AARP v. T.P.S.C., 896 S.W. 2d 127, 133 (Tenn. Ct. App. 1994) (cert. denied); and *TAWC v. TPUC*, No. M2009-00553-COA-R12-Filed, at 20, January 28, 2001.

⁴² *Tennessee Cable Tel. v. T.P.S.C.* 844 S.W. 2d 151, 159 (Tenn. Ct. App. 1992) (cert. denied).

⁴³ *See Order*, Docket 06-000187 (November 27, 2008), pp. 5-6 for a clear example of the Commission’s conclusions as to its discretion in selecting a test year period. See also *Powell Telephone v. T.P.S.C.*, 660 S.W.2d 44, 46 (Tenn. 1983) (citing *CF Industries v. T.P.S.C.*, 599 S.W. 2d 536, 542 (Tenn. 1980)).

⁴⁴ *Petition* at 4.

Limestone started with an analysis of Test Period revenues, expenses, and rate base. Limestone used a 12-month average for rate base and capitalization for the Test Period ending April 30, 2024. Limestone adjusted the test year for various normalizations and annualizations to attempt to make the historic test year representative of ongoing operations.⁴⁵

IV. LACK OF HISTORICAL BILLING DETERMINANTS AND INSUFFICIENT DATA

“One of the most important and gravest responsibilities that this Commission has is setting rates.”⁴⁶ To set rates, the Commission needs full and complete information from the Petitioner. Limestone has the burden of proof to show that its proposed increase and changes in its tariff are just and reasonable.⁴⁷ Therefore, the utility must supply the necessary rate schedules with supporting exhibits, documentation and explanations to justify any increase. According to Limestone, the acquisition adjustment and the extraordinary proposed rate increase are due, in part, to the troubled nature of all the systems requiring multiple improvements in the condition and compliance status of the ten systems; these improvements would allegedly result in improvements in the quality of service. However, Limestone has failed to meet its burden of proof due to missing, inaccurate, and inconsistent documentation in support of the condition of the systems, environmental compliance, and improvements to customer service. Additionally, Limestone failed to support its extraordinary proposed rate increase due to deficiencies in its books and records regarding its expenses and revenues, rate base, and failure to provide complete and detailed information in a timely manner. Although the Commission has great latitude in the methodology it employs to set rates, its analysis must start with confidence in the data and information supplied

⁴⁵ *Id.*

⁴⁶ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, at 395:7-9 (Cross Examination of William H. Novak).

⁴⁷ Tenn. Code Ann. § 65-5-103(a).

to it by the utility. Unfortunately, the Commission cannot have such confidence in this rate case.

A. Missing or Limited Revenue Data: No “Shortcut” To A Revenue Requirement

“Historical billing data is critical to the rate setting process and setting appropriate billing rates in the future.”⁴⁸ However, Limestone is asking the Commission to take a “short cut”⁴⁹ and to set rates without multiple years of billing data, including one system that has only two months of historical data.⁵⁰ In a rate case, historical billing records are examined over a four-year period to ensure that there are no anomalies in the data. For example, in a situation where the billing was somehow delayed for a particular month and then doubled-up in the following month. Also, there can be significant end-of-year adjustments to historical billing data that need to be considered when setting future rates. Examining this historical billing data over a four-year period allows the Consumer Advocate to become comfortable with recommending what is expected to occur during the test year. However, the historical billing data has not been preserved and is not available for the Consumer Advocate’s review and analysis or for the Commission’s review and consideration.⁵¹

Limestone failed to retain a copy of the historical billing determinants for multiple years for any of its acquisitions. The retention of such accounting records from buyer to seller are so important that the Parties specifically addressed this issue in their settlement agreements for the acquisitions by Limestone. For example, in Paragraph 15 of the Stipulation & Settlement Agreement approved by the Commission in TPUC Docket No. 21-00053 regarding Limestone’s acquisition of Cartwright Creek, LLC reads as follows:

⁴⁸ *Direct Testimony of William H. Novak* at 10:16-17.

⁴⁹ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, at 395:14-15 (Cross Examination of William H. Novak).

⁵⁰ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, at 394:5-7 (Cross Examination of William H. Novak). For some of the most recent acquisitions, only two months of historical data is available during the test period. See WHN Revenue Workpaper R-7-1.07 regarding billing data for DSH & Associates.

⁵¹ For some of the most recent acquisitions, only two months of historical data is available during the test period. See WHN Revenue Workpaper R-7-1.07 regarding billing data for DSH & Associates.

*The Parties agree that, at closing, Cartwright Creek shall transfer to Limestone complete copies of Cartwright Creek's accounting records for the two calendar years immediately preceding the date of acquisition as well as the complete year-to-date accounting records for the calendar year in which closing occurs. Limestone shall maintain these records intact at least through completion of its first rate proceeding before the Commission.*⁵²

This Stipulation & Settlement Agreement is then referenced by the Commission in the Order for that docket. Limestone was required to obtain complete copies of Cartwright Creek's accounting records for a minimum of two calendar years immediately preceding the date of acquisition, as well as the complete year-to-date accounting records for the calendar year in which closing occurs. Further, Limestone was required to maintain these records intact at least through completion of its first rate proceeding before the Commission. Limestone explained that it does request "all relevant accounting records and documentation from the seller to ensure a thorough understanding of the acquired entity's financial and operational position."⁵³ However, Limestone's position is that "detailed data reflecting specific customer usage metrics and calculations are generally not considered part of core accounting records, and, as such, were not specifically requested from sellers."⁵⁴ It is unfathomable that Limestone, which touts itself as a professional water and wastewater operator, would fail to appreciate the importance of historical billing data for determining rates in Tennessee. In fact, Mr. Novak stated "to my knowledge, the Commission has never adjusted rates with so little billing data to review."⁵⁵ Because of the incomplete billing data for multiple years at each of the ten systems at issue, the Commission should find that Limestone has not met its burden of proof to set rates with any degree of confidence.

⁵² This exact language requirement was also included in the Stipulation & Settlement Agreement for Limestone's acquisition of Aqua Utilities in TPUC Docket No. 19-00062, Shiloh Falls in TPUC Docket No. 21-00055, Chapel Woods in TPUC Docket No. 21-00060, Candlewood Lakes in TPUC Docket No. 21-00059, and DSH & Associates in TPUC Docket No. 23-00016.

⁵³ Company Response to Consumer Advocate DR No. 2-1.

⁵⁴ *Id.*

⁵⁵ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, at 388:9-12 (Summary of Testimony of William H. Novak).

B. Inaccurate, Inconsistent, or Missing Support for Acquisition Adjustment: All Systems Are Not “Troubled”

Josiah Cox, President⁵⁶ of CSWR, explained that he “created a business plan to acquire and recapitalize failing systems as investor-owned and regulated wastewater utility companies.”⁵⁷ According to CSWR’s website, it is “on a trajectory to take more domestic wastewater systems from noncompliance with environmental, health, and safety regulations to compliance than any other water utility in U.S. history.”⁵⁸ Although, Limestone stated that “the systems it acquired were all troubled systems,” this is not a correct characterization of the systems at issue.⁵⁹ The “troubled systems” at issue and the date of the Commission’s orders at located in Table 1 below:

Table 1: Dates of Commission Orders for Acquisition Dockets

Selling Utility	Systems Acquired ⁶⁰	TPUC Docket Number	Date Petition Filed	Date TPUC Ordered Issued ⁶¹	Letter to TDEC - Ownership Transfer
Aqua Utilities	1 water & 1 wastewater	19-00062	7/26/2019	12/7/2020	3/18/2021 ⁶²
Cartwright Creek (“CC”)	4 wastewater	21-00053	5/6/2021	1/24/2022	12/21/2021 ⁶³
Shiloh Falls	1 wastewater	21-00055	5/17/2021	12/2/2022	2/22/2023 ⁶⁴
Candlewood Lakes POA	1 water	21-00059	5/20/2021	1/5/2023	11/17/2022 ⁶⁵
Chapel Woods HOA	1 wastewater	21-00060	5/20/2021	12/2/2022	10/12/2022 ⁶⁶
DSH & Associates	1 wastewater	23-00016	3/1/2023	12/26/2023	1/23/2024 ⁶⁷

In reviewing this Docket’s filings, the term “troubled” is used frequently. However, the term is not

⁵⁶ Petition, MFG003, Organizational Chart.

⁵⁷ Amended Petition, Exhibit 9, Pre-Filed Rebuttal Testimony of Limestone Witness Josiah Cox at 3, TPUC Docket No. 19-00062 (December 13, 2019).

⁵⁸ CSWR, “Our Impact,” “2022 ESG Report,” (last visited March 5, 2025) <https://centralstateswaterresources.com/esg-report/>. CSWR quotes a report from Bluefield. *Id.*

⁵⁹ Rebuttal Testimony of Mike Duncan at 18:1-2.

⁶⁰ Direct Testimony of Mike Duncan at 4.

⁶¹ The Commission’s orders for these dockets can be accessed on TPUC’s Docket Page at <https://share.tn.gov/tra/indexes/TPUCActiveDocketIndex.htm>.

⁶² Acquisition Status Update, TPUC Docket No. 19-00062 (June 2, 2021).

⁶³ Acquisition Status Update, TPUC Docket No. 21-00053 (January 26, 2022).

⁶⁴ Acquisition Status Update, TPUC Docket No. 21-00055 (April 19, 2023). It should be noted that in its testimony, Limestone says it closed on Candlewood Lakes on May 11, 2023. Pre-Filed Direct Testimony of Limestone Witness Jacob Freeman at 6:3, Table.

⁶⁵ Acquisition Status Update, TPUC Docket No. 21-00059 (June 12, 2023).

⁶⁶ Acquisition Status Update, TPUC Docket No. 21-00060 (April 20, 2023).

⁶⁷ Acquisition Status Update, TPUC Docket No. 23-00016 (February 22, 2024).

defined. Mr. Duncan stated during his redirect at the hearing “all technical, managerial, and financial aspects have to be looked at when we’re looking at whether a system is in distress or troubled.”⁶⁸ Despite its failure to perform its full financial due diligence⁶⁹ and complete a deep review into the financial aspects of the acquired systems, Limestone seeks to characterize its small systems as financially troubled. For example, Mr. Thies stated that two utilities, DSH & Cartwright Creek, were “financially troubled” since the utilities “relied heavily on financial security escrow rather than investor supplied capital” like Limestone. Limestone fails to recognize that the Commission regularly requires escrow accounts for the small wastewater systems under its jurisdiction as a proactive approach in ensuring that small systems can address extraordinary expenses or necessary capital projects.⁷⁰ In fact, Cartwright Creek completed a significant project to address Infiltration and Inflow in a section the Grasslands system in 2020.⁷¹ The use of escrow accounts is so common that the Commission addresses them within its rules for wastewater systems by establishing the timing⁷² of a determination of need and the purpose⁷³ of an escrow account. Therefore, the mere existence of an escrow account for a selling utility is inaccurate and insufficient

⁶⁸ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL at 106:19-22 (Re-Direct Examination of Mike Duncan).

⁶⁹ *Id.* at 394:1-11; 394:22 – 395:6 (Cross Examination of Consumer Advocate Witness William H. Novak).

⁷⁰ The following utilities have such escrow accounts: Aqua Green (TPUC Docket No. 21-00128); Superior Wastewater (TPUC Docket No. 19-00018); Tennessee Wastewater Systems, Inc. (TPUC Docket No. 20-00009); and IRM Inc. (TRA Docket No. 15-00130).

⁷¹ *Engineering Report: Cartwright Creek, Sewer System Rehabilitation Effectiveness*, TPUC Docket No. 19-00049 (April 14, 2021).

⁷² Tenn. Comp. R. & Regs. Rule 1220-04-13-.07(6)(2018). The rule states:

Upon the filing of an initial CCN application, a determination shall be made regarding the establishment of a reserve/escrow account. The Commission may review the financial condition of any public wastewater utility at any time to determine whether a reserve/escrow account balance is adequate or an account should be established. The requirement for a public wastewater utility to maintain a reserve/escrow account shall be determined by the Commission on a case-by-case basis.

⁷³ Tenn. Comp. R. & Regs. Rule 1220-04-13-.07(7)(2018). The rules states:

Reserve/escrow accounts established by a public wastewater utility shall be limited to paying for or reimbursing the utility for extraordinary expenses of the utility or for necessary capital projects, unless otherwise permitted by the Commission. Extraordinary expenses are those resulting from events which are infrequent and unusual in nature, and unrelated to the utilities’ routine service or business activities.

to prove a utility is financially troubled.

As for the technical and managerial capabilities of the previous owners of the acquired systems, Mr. Duncan touted that Limestone “sought to modify current system assets to attain optimal performance rather than simply replacing all the systems.”⁷⁴ However, another explanation of why systems were not replaced is that the systems just did not need to be replaced. Mr. Duncan stated that at the date of his testimony, “Limestone had invested more than \$9.5 million in Tennessee to acquire,⁷⁵ and improve the water and wastewater systems it currently operates.”⁷⁶ Mr. Freeman highlighted the work performed by Limestone, but only three of the eight systems⁷⁷ are the subject of this rate case – Grasslands,⁷⁸ Candlewood Lakes,⁷⁹ and Shiloh Falls. If the point of Mr. Freeman’s testimony is to show the poor condition of the systems it has acquired, then Mr. Freeman should focus on the ten systems at issue. Of course, maybe the seven systems not addressed by Mr. Freeman were just not “troubled” enough to make his point. On the other hand, Mr. Todd Thomas provided descriptions of system improvements for each of the ten systems.⁸⁰ However, simply because work is performed on a system does not necessarily mean a system is troubled. If replacing pipes, replacing broken parts, and other maintenance activities indicate a “troubled system” then all water and wastewater systems would be considered troubled systems. For example, Tennessee-American Water spent \$36,689,431⁸¹ in capital expenditures for 2023; yet no one would say that Tennessee-American Water’s systems are troubled or failing.

⁷⁴ *Direct Testimony of Mike Duncan* at 10.

⁷⁵ In this Docket, Limestone is seeking approximately \$2.2 million in acquisition adjustments. *Direct Testimony of Brent Thies* at 13:13, Table.

⁷⁶ *Direct Testimony of Mike Duncan* at 4. There are approximately \$2.2 million in acquisition costs. *Direct Testimony of Brent Thies* at 3:17, Table of Acquisition adjustments.

⁷⁷ *Direct Testimony of Jacob Freeman*, Table of Contents at 3:16-19.

⁷⁸ It has been 3 years since taking ownership of the Grasslands system, and Limestone has yet to obtain approval from TDEC for engineering plans for the new system.

⁷⁹ It has been two years since taking ownership of the Candlewood Lakes system, and there is still no backup drinking water well. *Direct Testimony of Jacob Freeman* at 41:20-21.

⁸⁰ *Direct Testimony of Todd Thomas* at 17-133.

⁸¹ *Direct Testimony of TAWC Witness Grady Stout*, Attachment “2023 Actual v. Budget Capital Expenditures,” TPUC Docket No. 24-00011 (March 8, 2024).

Whether a system is troubled can be subjective so one should look to objective professional opinions of a system. For example, one expects that a technically and managerially troubled system would have the attention of the designated environmental regulator, the Tennessee Department of Environment and Conservation (“TDEC”). In a review of TDEC’s public dataviewers,⁸² only two of Limestone’s systems have previous and current formal enforcement orders: (1) the Grasslands Wastewater System,⁸³ and (2) the Candlewood Lakes Water System,⁸⁴ as shown in Table 2 below:

Table 2: Informal and Formal Enforcement by TDEC.

Limestone System	Type of System	TDEC Permit No. or Public Water System ID #	Formal Enforcement: Director or Commissioner’s Order
Aqua	Water	TN0000948	No ⁸⁵
Aqua	Wastewater	SOP-92082	No ⁸⁶
The Grasslands (CC)	Wastewater	NPDES TN0027278	Yes ⁸⁷
The Hideaway (CC)	Wastewater	SOP-07090	No
Arrington Retreat (CC)	Wastewater	SOP-04019	No
Hardeman Springs (CC)	Wastewater	SOP-17002	No
Shiloh Falls	Wastewater	SOP-94011	No ⁸⁸
Candlewood Lakes	Water	TN0000797	Yes ⁸⁹
Chapel Woods	Wastewater	NPDES TN0062073	No ⁹⁰
Lakeside Estates (DSH)	Wastewater	SOP-07073	No ⁹¹

⁸² The search of TDEC’s Enforcement Program Dataviewer for Limestone’s orders can be located at <https://dataviewers.tdec.tn.gov/dataviewers/f?p=9001:700;>

A search of TDEC’s Water Resources Dataviewer for Limestone’s wastewater systems can be accessed at <https://dataviewers.tdec.tn.gov/dataviewers/f?p=2005:34001:7306067262502:::RIR;> Drinking water systems are not issued a permit but rather are provided a Public Water System Identification Number. Documents related to Limestone’s water systems can be accessed using the name of the water system at <https://dataviewers.tdec.tn.gov/dataviewers/f?p=2005:34308:7306067262502.>

⁸³ *Hearing Transcript*, 2025-02-18 TPUC - 24-00044 - Volume I, at 96:1-14 and Hearing Exhibit 6 (Cross Examination of Mike Duncan). A search of TDEC’s Enforcement Program Dataviewer for the Grasslands System shows 3 enforcement actions, which can be accessed at <https://dataviewers.tdec.tn.gov/dataviewers/f?p=9001:700.>

⁸⁴ *Id.* at 94:1-4; 95:8; and Hearing Exhibit 5. In TDEC’s enforcement order, DWS24-0053, previous enforcement orders were also identified – DWS10-0013 and DWS17-0052. Hearing Exhibit 5, at 3. These enforcement orders can be accessed at <https://dataviewers.tdec.tn.gov/dataviewers/f?p=9001:700.>

⁸⁵ *Id.* at 98:21 – 99:2.

⁸⁶ *Id.*

⁸⁷ *Id.* at 96:1-14 and Hearing Exhibit 6.

⁸⁸ *Hearing Transcript*, 2025-02-18 TPUC - 24-00044 - Volume I, at 98:12-20.

⁸⁹ *Id.* at 94:1-4; 95:8; and Hearing Exhibit 5.

⁹⁰ *Id.* at 98:1-11.

⁹¹ *Id.* at 99:18-22.

Due to the discrepancies and inconsistencies described above, the statement that “the systems it acquired were all troubled systems,”⁹² whether financially, managerially, or technically, is inaccurate. As such, the Commission should find that Limestone has not met its burden of proof for either the recovery of acquisition adjustments and has not shown that its extraordinary proposed rate increase and changes in its tariff are just and reasonable.

C. Inaccurate or Inconsistent: Improved Compliance And Quality of Service, Was Not So Immediate

As previously explained above, Limestone’s business model is to acquire and recapitalize failing systems and bring such systems back into compliance. Mr. Duncan claimed that customers have received tangible benefits from these acquisitions by Limestone due to improved operations of the wastewater systems and improved levels of discharges into the environment.⁹³ Although Mr. Duncan touts improved financial and engineering expertise at systems that need to be replaced – Grasslands, Shiloh Falls, and Candlewood Lakes – it should be noted that Limestone has yet to begin construction for the proposed new or expanded systems.⁹⁴ Further, Mr. Duncan stated that due to Limestone’s high level of technical, financial, and managerial expertise, the systems are “operating at an optimal level.”⁹⁵ But, this is not the case.

For example, Mr. Duncan explained that the technical expertise includes Limestone’s Environmental, Health and Safety (“EHS”) Team which provides “immediate benefits” for the small systems it acquires by ensuring all samples are taken consistent with operating permits and state environmental regulations.⁹⁶ However, after six months of taking ownership of the Grasslands system,⁹⁷ TDEC issued a Notice of Violation (“NOV”) to Limestone for its failure to accurately

⁹² *Rebuttal Testimony of Mike Duncan* at 18:1-2.

⁹³ *Direct Testimony of Mike Duncan* at 6.

⁹⁴ *Direct Testimony of Todd Thomas* at 34:6-8; 40:9-11; and 41:20-25.

⁹⁵ *Direct Testimony of Mike Duncan* at 6.

⁹⁶ *Id.* at 20.

⁹⁷ Limestone took ownership of the Cartwright Creek systems, like Grasslands, on December 21, 2021. See Table 1 on p. 12 of this Post-Hearing Brief.

transfer information from laboratory benchsheets to Monthly Operation Reports (“MORs”) submitted to TDEC.⁹⁸ TDEC explained in its NOV that such inaccurate reporting is a violation of the permit.⁹⁹ During the hearing, Mr. Duncan explained that “when this was brought to our attention,” Limestone dismissed the certified operator and hired a new operator who was provided proper training.¹⁰⁰ Unfortunately, for the nearby customers of the Hideaway system, Limestone did not learn much from the problems identified at the Grasslands system. Because one year later, TDEC issued a NOV the Hideaway system for discrepancies and issues with the benchsheets which “lead [TDEC] to question of the veracity of the documentation.”¹⁰¹ The time period for the Hideaway NOV includes 12 additional months after the Grasslands NOV was issued. Therefore, for 18 months after taking ownership of the Hideaway system, Limestone was in non-compliance with its permit due to “inadequate sampling, failure to provide reports in a timely manner, lack of self-monitoring on Quarterly Operating Reports, unsupported data reported to [TDEC], and exceedances of permitted effluent limits.”¹⁰² The time period of violations for both the Grasslands and the Hideaway systems are set out in Figure 1 below.

Figure 1. Time period of Non-compliance.



Despite these problems, Mr. Duncan believes that “customers are receiving improved water

⁹⁸ *Hearing Transcript*, 2025-02-18 TPUC - 24-00044 - Volume I, at 90:24 – 91:19 and Exhibit 3 (Cross Examination of Mike Duncan). The time period covered by the NOV is January 2022 – April 2022. *Id.* at Exhibit 3, TDEC NOV-Grasslands at 2.

⁹⁹ *Id.* at Exhibit 3, TDEC NOV-Grasslands at 4.

¹⁰⁰ *Id.* at 91:7-12.

¹⁰¹ *Id.* at Exhibit 4, TDEC NOV-Hideaway at 2.

¹⁰² *Id.* at Exhibit 4, TDEC NOV-Hideaway at 6.

and wastewater services” due to the Limestone’s technical, managerial, and financial expertise.¹⁰³ In fact, Mr. Thomas boasted about the score of a recent Sanitary Survey¹⁰⁴ conducted by TDEC in which one of Limestones’ water systems received a score of 97%.¹⁰⁵ In a review of TDEC documentation for Limestone’s two water systems, Aqua and Candlewood Lakes, it is the Candlewood Lakes water system that recently received a score of 97% after an inspection by Nicholas Bolin.¹⁰⁶ However, Mr. Thomas does not mention that prior to Limestone’s ownership, TDEC issued a slightly higher score of 98% for the Candlewood Lakes Property Owners Association in 2019 and 2022.¹⁰⁷ It is a similar situation with the Aqua water system. By letter dated May 30, 2023, TDEC issued a Sanitary Survey rating of 100% to Limestone, which is excellent.¹⁰⁸ However, this recent score is only slightly higher than the previous two Sanitary Survey evaluations in 2019 and 2021¹⁰⁹ which resulted in a score of 99%.¹¹⁰

¹⁰³ Direct Testimony of Mike Duncan at 5.

¹⁰⁴ TDEC’s Sanitary Survey Manual explains:

A sanitary survey is an onsite evaluation and documentation of a water system’s capabilities, operations, sources, facilities, treatment process, equipment, distribution network, monitoring, reporting and data verification, pump facilities, controls and overall management needed to continually provide safe drinking water and any deficiencies that might impact the provision of safe drinking water.

Sanitary Survey Manual for Community and Non-Community Public Water Supplies (February 2021)(https://www.tn.gov/content/dam/tn/environment/water/drinking-water-unit/wr_wq_dw-sanitary-survey-manual-02-2019.pdf).

¹⁰⁵ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, at 295:10-13 (Summary of Direct Testimony of Todd Thomas).

¹⁰⁶ *TDEC Sanitary Survey Report Correspondence*, Candlewood Lakes, PWSID #TN0000797 (March 20, 2024). This correspondence can be accessed at https://dataviewers.tdec.tn.gov/dataviewers/f?p=2005:34031:7024995920883:::34031:P34031_SITE_ID:59315.

¹⁰⁷ *TDEC Sanitary Survey Report Correspondence*, Candlewood Lakes, PWSID #TN0000797 (March 8, 2022). *TDEC Sanitary Survey Report Correspondence*, Candlewood Lakes, PWSID #TN0000797 (March 8, 2022). Both documents may be accessed at https://dataviewers.tdec.tn.gov/dataviewers/f?p=2005:34031:7024995920883:::34031:P34031_SITE_ID:59315.

¹⁰⁸ *TDEC Sanitary Survey Report Correspondence*, Aqua, PWSID #TN0000948 (May 30, 2023). This correspondence can be accessed at https://dataviewers.tdec.tn.gov/dataviewers/f?p=2005:34031:16523295174211:::34031:P34031_SITE_ID:99687.

¹⁰⁹ It should be noted that the site visit by TDEC personnel happened on March 30, 2021, which is 12 days after Limestone took ownership of the Aqua water system.

¹¹⁰ *TDEC Sanitary Survey Report Correspondence*, Aqua, PWSID #TN0000948 (April 19, 2023). This correspondence can be accessed at https://dataviewers.tdec.tn.gov/dataviewers/f?p=2005:34031:16523295174211:::34031:P34031_SITE_ID:99687.

It appears the theme of Limestone's Petition is that customers of all the troubled systems acquired are almost immediately receiving improved water and wastewater services; however, Limestone's performance falls decidedly short of this promise. Beginning with the example of the continued non-compliance at two wastewater systems described above and the lack of significant improvement in the technical and managerial operations of two water systems from the previous owners, Limestone's actual performance conflicts with its statement of immediate and tangible benefits of improved operations. As such, the Commission should find that Limestone has not met its burden of proof for either the recovery of acquisition adjustments or the justification that its proposed increase and changes in its tariff are just and reasonable.

D. Inappropriate Expenses: Far Beyond Acquisition Transaction Costs

For the recovery of expenses, Limestone must provide supporting documentation of the proposed expenses and that the expenses be appropriate. However, once again, Limestone falls short of its statutory obligation. Within the proposed transaction costs, Limestone includes expenses that are inappropriate to recover from ratepayers. An example is the [REDACTED] [REDACTED]¹¹¹ in the amount of [REDACTED] [REDACTED]¹¹². Excerpts from [REDACTED] are provided below:

[Intentionally Blank, Excerpts on Following Page]

¹¹¹ Hearing Transcript, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, Exhibit 9 – [REDACTED] (Cross Examination of Limestone Witness Brent Thies).

¹¹² Id. at Exhibit 8 – [REDACTED]. In this spreadsheet, [REDACTED] See also Limestone's Response to Consumer Advocate DR No. 1-67(a), CONFIDENTIAL File <DR-67 – Transaction Costs>, Tab "67a – Detail."

[Confidential Images Removed]

It appears these costs are associated with [REDACTED]
[REDACTED]. During the cross-examination,
Mr. Thies admitted that [REDACTED].¹¹³ He argued that the
[REDACTED]
[REDACTED]
[REDACTED].¹¹⁴ However, after further questioning, Mr. Thies [REDACTED]
[REDACTED]
[REDACTED].¹¹⁵ On re-direct by Mr. Dollarhide, Mr. Thies
[REDACTED]

¹¹³ *Id.* at 174:9-8 (CONFIDENTIAL).

¹¹⁴ *Id.* at 175:2-9 (CONFIDENTIAL).

¹¹⁵ *Id.* at 175:10-15 (CONFIDENTIAL).

[REDACTED] 116
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

Another example of inappropriate transaction costs is [REDACTED]

[REDACTED] 117 [REDACTED]

[REDACTED].¹¹⁸ An excerpt from Confidential Hearing Exhibits 8 is provided below:

[Confidential Image Removed]

Regarding the first charge from [REDACTED]

[REDACTED] An excerpt from [REDACTED] showing this charge is provided below:

[Intentionally Blank, Excerpt on Following Page]

¹¹⁶ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, at 202:1-8 (Cross Examination of Limestone Witness Brent Thies).

¹¹⁷ *Id.* at Exhibit 11 – [REDACTED]

¹¹⁸ *Id.* at Exhibit 8 – [REDACTED]. In this spreadsheet, [REDACTED]. See also Limestone’s Response to Consumer Advocate DR No. 1-67(a), CONFIDENTIAL File <DR-67 – Transaction Costs>, Tab “67a – Detail.”

[Confidential Image Removed]

Part of the daily operations of a utility includes [REDACTED]

[REDACTED]

When asked at the hearing about this charge, Mr. Thies [REDACTED]

[REDACTED]

[REDACTED]

In addition, Limestone is attempting to recover costs associated with [REDACTED]

[REDACTED] An excerpt from Confidential Hearing Exhibits 12 showing these charges is provided below:

[Confidential Images Removed]

[REDACTED]

[REDACTED] It should also be noted that the Cartwright

Creek or CC systems were transferred to Limestone on December 21, 2021; [REDACTED]

[REDACTED] Mr. Thies confirmed that the charges involved [REDACTED]

[REDACTED]

[REDACTED] 119 [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Limestone is also seeking to recover charges [REDACTED]

[REDACTED]

Excerpts from the invoice regarding these charges are provided below:

[Confidential Image Removed]

The current Docket does not include [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] 120 [REDACTED]

[REDACTED]

¹¹⁹ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, at 182:11-18; 183:1-10 (Cross Examination of Limestone Witness Brent Thies).

¹²⁰ *Id.* at 183:17. (CONFIDENTIAL).

E. Missing And Delayed Support for Rate Base: Far Beyond Original Cost

Limestone is asking the Commission to approve the land and land rights of the acquired systems to be more than the original booked costs.¹²¹ The amount in question is significant [REDACTED].¹²² Limestone arrived at this amount by including costs such as “surveys, title costs, easements, and other land rights.”¹²³ These expenses do nothing to actually increase the value or usefulness of the land, and can be incurred repeatedly. If allowed to be included as part of land value, such costs simply inflate the rate base without adding any actual value to the plant and equipment. Furthermore, such costs occur, regardless of whether a transaction is consummated. In such a situation these expenses should not make it into rate base at all.

In support of its position, Limestone simply provided hard-coded values without supporting documentation.¹²⁴ The Consumer Advocate twice attempted to get the details and supporting documentation of the hard-coded numbers, but none were provided.¹²⁵ Fifty-four days after the Consumer Advocate filed its direct testimony and seven days before the hearing, Limestone provided details of its proposed land and land right values.¹²⁶ Since Limestone provided such details after the Consumer Advocate’s Direct Testimony, the Consumer Advocate was not afforded an opportunity to review, conduct discovery, and analyze the information prior to the scheduled hearing.

¹²¹ *Direct Testimony of Clark Kaml* at 12:1-3.

¹²² *Id.* at 13:7. (CONFIDENTIAL)

¹²³ *Rebuttal Testimony of Brent Thies*, at 2:18-20.

¹²⁴ *Hearing Transcript*, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, Exhibit 13-[REDACTED]; at 186:7-20 and Exhibit 14-[REDACTED]; 187:13-20. (Cross Examination of Limestone Witness Brent Thies)(CONFIDENTIAL).

¹²⁵ *Id.* at Exhibit 15-Response to CA Informal DR; Exhibit 16-[REDACTED]; Exhibit 17-[REDACTED]; Exhibit 18 - Response to CA DR No. 2-7; Exhibit 19 - Attachment to Response to CA DR No. 2-7. (CONFIDENTIAL)

¹²⁶ *Limestone’s Response to Commission Staff’s DR No. 2-5*, File<DR F- Land Detail – CONFIDENTIAL.xlsx>, Tab “STAFF DR 5 Land Rights Detail” (February 11, 2025).

Questions the Consumer Advocate could have asked, if afforded the opportunity, would include why expenses not associated with surveys, title costs, easements, and other land rights were included in the land rights detail provided by Limestone to Commission Staff. For example, Limestone included [REDACTED], which are shown below (CONFIDENTIAL):

[Confidential Image Removed]

Also, the Consumer Advocate would have requested explanations of similar type work being included in both transaction detail and land rights detail. For example, Limestone includes work associated with service maps on both the transactions costs detail and land rights detail, which are shown below:

[Confidential Images Removed]

Due to the untimely filing of its supporting documentation for Limestone's land rights detail which prevented the Consumer Advocate time to review, analyze, and issue discovery on prior to

its deadline for submitting direct testimony, the Commission should not approve Limestone's proposed inclusion in rate base of the increase land and land rights amounting [REDACTED].

V. REVENUE REQUIREMENT AND DEFICIENCY

A. The Consumer Advocate's Revenue Requirement And Deficiency Should Be Adopted by the Commission Because it Follows Methodologies Established by Prior Commission Order And Is Based on Reasonably Anticipated Adjustments

While the Consumer Advocate asserts that Limestone has provided insufficient data, unsupported data, and did not properly forecast revenues with verifiable data, the Consumer Advocate has made its revenue projections for Limestone to the best of its ability with the available data provided by Limestone. Nevertheless, the Consumer Advocate would urge the Commission to refrain from adopting a revenue forecast that is unsupported and unverifiable.

Limestone's revenue requirement is determined by applying the following generally recognized ratemaking formula: Revenue Requirement = (Rate Base x Rate of Return) + Operation and Maintenance Expense + Depreciation + Taxes. The revenue requirement is the sum of its O&M expenses, depreciation expense, income taxes and taxes other than income, and its authorized fair rate of return.

Limestone is seeking a total annual Revenue Requirement of \$3,060,407,¹²⁸ as reflected in the *Petition* and by Limestone's Witnesses Brent Thies in his *Direct Testimony*.¹²⁹ The Company calculated its water revenue deficiency to be \$450,561 and the sewer revenue deficiency of \$1,223,275¹³⁰ for a total revenue deficiency of \$1,673,836.

The Company later revised this number on February 25, 2025, at the direction of the Commission Staff, and provided updated revenue deficiency amounts for the systems to include the

¹²⁸ *Petition* at 2-4.

¹²⁹ *Direct Testimony of Brent Thies* at 8:20-21 – 9:2-4.

¹³⁰ *Petition* at 4.

acquisition adjustment Limestone is seeking to be authorized in this rate case. The revenue requirement increased by \$464,736.¹³¹ The revised revenue deficiency was changed for water (\$575,061) and (\$1,688,011) for wastewater.¹³² This resulted in a material change to the Company's total revenue deficiency request to \$2,263,072. This revised revenue deficiency amount includes the acquisition adjustment that was discussed in the testimony of several Limestone's witnesses but not included in the revenue deficiency request in the original Limestone *Petition*.

The Consumer Advocate's proposed current revenue forecast based on Limestone's original *Petition*, is \$1,742,924.¹³³ The Consumer Advocate proposes a 36.36% change in revenue to all customers based upon an across-the-board distribution of the attrition period margin under current rates.¹³⁴ This revenue increase allocation more equitably spreads the burden of any increase in rates and is preferable to the Company's consolidated rate results.¹³⁵

CA Total Revenue Forecast¹³⁶	
Revenue Type	Amount
Total Service Revenues	\$1,186,981
Other Revenues	\$555,943
Total Revenues	\$1,742,924

The Consumer Advocate's forecasted period service revenues by operating territory revenues are shown in the following table:¹³⁷

¹³¹ *Limestone Water Utility Operating Company, LLC's Replacement Attachment to Response No. 6 to Commission's January 31st, 2025 Data Request. The Attachment Was Originally Filed on February 25, 2025 as Confidential and Can be Replaced with This Attachment as Non-Confidential*, TPUC Docket No. 24-00044 (Feb. 27 2025).

¹³² *Pursuant to Commission Request at February 2025 Commission Hearing, Limestone Water Utility Operating Company LLC Updated Response to Commission January 31, 2025 Data Request No. 6 in Excel Format*, TPUC Docket No. 24-00044, (Feb. 25, 2025).

¹³³ *Direct Testimony of William H. Novak at 17; and Letter To Chairman David F. Jones Re Corrections To The Direct Testimony Of William H. Novak*, (Feb. 7, 2025). *Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections at 3:22-24, Schedule 2, File 1.1 and 1.2.*

¹³⁴ *Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections*, Schedule 10.

¹³⁵ *Direct Testimony of William H. Novak at 21:8-10.*

¹³⁶ *Id.*, WHN Revenue Workpaper R-1-1.00.

¹³⁷ *Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections*, Schedule 10.

CA Service Revenue Forecast	
Operating Territory	Amount
Cartwright Creek	\$672,400
Aqua Utilities	\$269,142
Candlewood Lakes	\$49,920
Chapel Woods	\$49,822
Lakeside Estates (DSH)	\$54,005
Shiloh Falls	\$91,692
Other Revenues	\$555,943
Total	\$1,742,924

The attrition period revenues were forecast by first applying a historic growth rate to the test period bills and water usage for those properties with anticipated growth. The Consumer Advocate then applied the current tariff charges to the attrition period billing determinants to get the attrition period service revenues.¹³⁸

The Consumer Advocate's attrition period forecast for Limestone's other revenues is \$555,943 as reflected in the following table:¹³⁹

Attrition Period Other Revenues¹⁴⁰	
Operating Territory	Amount
Forfeited Discounts	\$62,753
Non-Sufficient Fund Fees	65
Inspection Fees	11,550
Tap Fees	481,575
Total	\$555,943

The Consumer Advocate calculated Forfeited Discounts by taking the average rate used in the Company's most recent rate cases for Cartwright Creek and Aqua Utilities and then applied this average rate to the attrition period Service Revenues described above.¹⁴¹ To calculate Inspection Fees and Tap Fees, the Consumer Advocate anticipated customer growth for each service area to the current tariff rate for these charges as described earlier.¹⁴²

¹³⁸ Direct Testimony of William H. Novak at 18:3-4.

¹³⁹ Id. at 18:7-8.

¹⁴⁰ Id. at WHN Revenue Workpaper R-1-1.00.

¹⁴¹ Id. at 18:10-13.

¹⁴² Id. at 18:13-15.

The Consumer Advocate forecasted revenues for all customer classes by first obtaining the available test period billing determinants, then making adjustments for known and reasonably anticipated changes to bills and usage, and then pricing out this forecast at the Company's currently approved rates. The Consumer Advocate used a common-sense approach to forecast revenues for Limestone.

1. Forecasted Revenues

Limestone's total annual revenue requirement requested in Limestone's Petition was \$3,060,407.¹⁴³ The Company's filed water revenue requirement in this proceeding, equal to the cost of providing water service, is \$649,455 for the adjusted test year using the 12-months ending April 30, 2024.¹⁴⁴ Similarly, the sewer revenue requirement in this proceeding is \$2,410,952 for the adjusted test year using the 12-months ended April 30, 2024.¹⁴⁵

Limestone's water revenue deficiency is measured as the difference between the water revenue requirement of \$649,455 and Limestone's adjusted and annualized water revenues at present rates.¹⁴⁶ Thus, Limestone's water revenue deficiency in this proceeding is calculated to be \$450,561. Limestone's sewer revenue deficiency is calculated to be \$1,223,275.¹⁴⁷

During the rate case hearing, Commission Staff requested that Limestone submit corrected revenue deficiencies for water and wastewater since Limestone seeks to include the acquisition adjustments for five of the transactions that were not included in the rate base. Limestone was also asked to provide updated rate design calculations and exhibits in Excel format that include all proposed rates and charges needed to recover the updated revenue deficiency for water and sewer.¹⁴⁸

¹⁴³ Petition at 4.

¹⁴⁴ Direct Testimony of Brent Thies at 8:20-21 – 9:1-2; Exhibit BT-1.2.

¹⁴⁵ Id. at 9:2-5; Exhibit BT-1.1.

¹⁴⁶ Id. at 9:8-10; Exhibit BT-1.2

¹⁴⁷ Id. at 9:10-13; Exhibit BT-1.1.

¹⁴⁸ Order Establishing Post Hearing Procedural Schedule, TPUC Docket No. 24-00044, (Feb. 24, 2025).

The Commission requested the revised revenue deficiency requirements and rate design information be filed by Friday, February 28, 2025.¹⁴⁹ Limestone filed the revised revenue requirements in the Docket on February 25, 2025.¹⁵⁰

The Consumer Advocate relied on the original Petition to calculate the revenue total of \$1,186,981 based on adjustments for customer usage and customer growth.¹⁵¹ The revenues were forecast by first applying a historic growth rate to the test period bills and water usage for those properties with anticipated growth. Next, the Consumer Advocate applied the current tariff charges to the attrition period billing determinants to get the forecast period service revenues.¹⁵² The Consumer Advocate's total forecast for Limestone's other revenues is \$555,943 as shown below on the following Table:¹⁵³

Table 4 – Attrition Period Other Revenues¹⁵⁴	
Operating Territory	Amount
Forfeited Discounts	\$62,753
Non-Sufficient Fund Fees	65
Inspection Fees	11,550
Tap Fees	481,575
Total	\$555,943

To calculate Forfeited Discounts, the Consumer Advocate calculated the average rate used in the Company's most recent rate cases for Cartwright Creek and Aqua Utilities and then applied this average rate to the attrition period Service Revenues described above. To calculate Inspection Fees and Tap Fees, the Consumer Advocate applied the anticipated customer growth for each service area to the current tariff rate for these charges as described earlier.

¹⁴⁹ *Id.*

¹⁵⁰ Pursuant to the Commission Request at the February 2025 Commission Hearing, Limestone Water Utility Operating Company LLC Updated Response to Commission January 31, 2025 Data Request No. 6 In Excel Format, TPUC Docket No. 24-00044, (Feb. 25, 2025).

¹⁵¹ *Direct Testimony of William H. Novak at 17:11-15.*

¹⁵² *Id.* at 18:1-4.

¹⁵³ *Id.* at 18:7-8.

¹⁵⁴ *Id.* at 18:9.

The Consumer Advocate's total revenue forecast for the attrition period is \$1,742,924 composed of the Service Revenues and Other Revenue forecasts, as shown below on the following Table:

Consumer Advocate Total Revenue Forecast¹⁵⁵	
Revenue Type	Amount
Service Revenues	\$1,186,981
Other Revenues	555,943
Total Revenues	\$1,742,924

2. Limestone Had Errors in Recording Commercial Revenue

In TPUC Docket No. 21-00053, the Commission approved the Petition by Limestone to acquire the assets, property, and real estate of Cartwright Creek. Cartwright Creek's tariff provides for monthly commercial wastewater service at the rates shown below in the following Table:

Cartwright Creek Monthly Commercial Rate¹⁵⁶	
Charge Type	Rate
Rate per 1,000 Gallons per Month (Actual or Estimated Flow)	\$8.75
Minimum Monthly Charge	37.00

As shown in the above Table, the Cartwright Creek tariff provides for a charge based on the customer's monthly water usage. However, Limestone has not levied any usage charges to Cartwright Creek's commercial customers since its acquisition in January 2022. Instead, Limestone has only applied the monthly minimum bill to these commercial customers. As a result, the test period revenues are materially understated by these omitted charges.¹⁵⁷

Limestone did not apply the correct tariff rates to Cartwright Creek's commercial customers and stated that "it did not have any approved methodology for estimating flow for each commercial type. Rather than over-charge any particular customer due to a lack of relevant data, the Company

¹⁵⁵ WHN Revenue Workpaper R-1-1.00.

¹⁵⁶ Company Response to Consumer Advocate DR No. 1-1.

¹⁵⁷ *Direct Testimony of William H. Novak* at 5:14-15.

limited its billings to the base charge in the tariff.”¹⁵⁸

The monthly usage charges for Cartwright Creek’s commercial customers should have been included in this rate case. The previous owners of Cartwright Creek were able to obtain the usage of their commercial customers on a continuing basis and the failure of Limestone to capture and bill for commercial usage results in an over-stated revenue deficiency in this Docket.¹⁵⁹

Since Limestone has been unable to provide usage data for the commercial customers of Cartwright Creek, the true value of Commercial Revenues is unknown. As a result, the commercial customers are being clearly underbilled in this rate case. In Cartwright Creek’s last rate case in TPUC Docket No. 16-00127, the Commission Party Staff included commercial usage charges of \$91,230.¹⁶⁰ Therefore, the Consumer Advocate expects the test period commercial usage charges in the Cartwright Creek service area to be similar to this amount and has used this amount to project the commercial usage for Cartwright Creek.

Limestone’s omission of the commercial usage charges for the Cartwright Creek service area potentially has a material impact on the revenue deficiency in this Docket. This deficiency should be corrected before any change in rates is considered by the Commission.¹⁶¹

VI. TAP FEES & INSPECTION FEES

The Company classified receipts from tap fees and inspection fees from the charges to customers as Contributions in Aid of Construction (“CIAC”). The Company states that they record “the receipts from these charges as CIAC because these fees represent payments from customers to Limestone that help cover the cost of expanding infrastructure.”¹⁶²

¹⁵⁸ Company Response to Consumer Advocate DR No. 2-2(c).

¹⁵⁹ *Direct Testimony of William H. Novak* at 6:7-10.

¹⁶⁰ TRA Docket No. 16-00127, *Joint Petition of Cartwright Creek, LLC and TRA Staff (as a Party) to Increase Rates and Charges*, Pre-Filed Direct Testimony of Daniel Ray, TRA Party Staff Exhibits and Workpapers, TRA Staff Exhibit, Schedule 7, Nov. 10, 2016.

¹⁶¹ *Direct Testimony of William H. Novak* at 7:3-6.

¹⁶² Company Response to Consumer Advocate DR No. 1-19(b).

The Consumer Advocate maintains that Limestone has incorrectly recorded these receipts. The Commission has a long history of requiring utilities to record these types of receipts as revenues. For example, in the last rate case for Cartwright Creek, \$21,000 was included in Revenues for Tap Fees and Inspection Fees.¹⁶³ Likewise in the last rate case for Aqua Utilities, \$21,375 was included in Revenues for Tap Fees.¹⁶⁴ Finally, in the CCN Application for Shiloh Falls Utilities, \$25,500 was included in Revenues for Tap Fees.¹⁶⁵ The Commission has a clear history of the treatment for the classification of Tap Fees and Inspection Fees receipts as revenues.

Since Limestone was unable to provide any guidance for its anticipated level of activity,¹⁶⁶ the Consumer Advocate applied the ratio of Inspections and Re-Inspections from the last Cartwright Creek rate case in TRA Docket No. 16-00127 to the anticipated growth rate for properties with an Inspection Fee and priced these amounts out at the current tariff rate.¹⁶⁷

For Tap Fees, Limestone was also unable to provide any guidance for its anticipated level of activity,¹⁶⁸ therefore, the Consumer Advocate applied the anticipated customer growth for each service area to the current tariff rate for Tap Fees.¹⁶⁹

This process produced \$493,125 in total Inspection Fees and Tap Fees as shown below on the following Table:

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¹⁶³ TRA Docket No. 16-00127, *Joint Petition of Cartwright Creek, LLC and TRA Staff (as a Party) to Increase Rates and Charges*, Pre-Filed Direct Testimony of Daniel Ray, TRA Party Staff Exhibits and Workpapers, TRA Staff Exhibit, Schedule 3, Line Nos. 5 and 7, Nov. 10, 2016.

¹⁶⁴ TRA Docket No. 15-00044, *Joint Petition of Aqua Utilities and TRA Staff (as a Party) to Increase Rates and Charges*, Pre-Filed Direct Testimony of Joe Shirley, TRA Staff Exhibits and Workpapers, TRA Staff Exhibit, Schedule 7, Line No. 10, April 10, 2015.

¹⁶⁵ TPSC Docket 95-03948, *The Application of Shiloh Falls Utilities, Inc. for a Certificate of Convenience and Necessity*, Initial Order, Settlement Agreement, Schedule I, May 31, 1996.

¹⁶⁶ Company Response to Consumer Advocate DR No. 2-3.

¹⁶⁷ WHN Revenue Workpaper R-10-3.00. Note: Inspection Fees only apply to the Cartwright Creek property areas.

¹⁶⁸ Company Response to Consumer Advocate DR No. 2-5.

¹⁶⁹ WHN Revenue Workpaper R-10-4.00.

CA Attrition Period Inspection Fees and Tap Fees	
Charge Type	Amount
Inspection Fees	\$11,550
Tap Fees	481,575
Total	\$493,125

The Consumer Advocate recommends that the Commission should continue to treat Inspection Fees and Tap Fees as revenues. The Consumer Advocate further recommends that going forward such receipts should be recorded as revenue.

VII. RATE BASE

Rate base is the investment base to which a fair rate of return is applied to arrive at a net operating income requirement. Rate base is the measurement of the Company's net capital investment in the provision of water service, including the facilities for sourcing, treating, pumping, and distributing potable water for consumption, sanitation, and fire protection. It also encompasses the assets necessary to support customer accounting, customer service, and basic business operations.

The major components of rate base for this rate case are: Utility Plant In Service ("UPIS"), including the recovery of acquisition adjustments and pre-acquisition legal and engineering costs; cash working capital allowance; prepayments; accumulated depreciation; and CIAC.¹⁷⁰ The Company proposes a rate base of \$3,272,329. The components of rate base were generated from Petitioner's Exhibit BT 9.1 & 9.2.¹⁷¹

The Consumer Advocate reduced Limestone's rate base from \$3,272,329 to \$1,941,111, with two adjustments for Land and Land Rights of \$677,359 and the requirement that Financial Security Escrow Accounts be used for projects. This increases CIAC by \$653,857 and reduces rate base by this amount.¹⁷² The Consumer Advocate filed the Testimony of David N. Dittmore on these issues,

¹⁷⁰ Direct Testimony of Brent Thies at 10:6-12.

¹⁷¹ Id. Exhibits BT 9.1 & BT 9.2.

¹⁷² Direct Testimony of Clark Kaml at 28:15-20.

which adopted the testimony of Alex Bradley and made certain corrections. The Consumer Advocate revised the wastewater rate base to \$1,186,162 and the water rate base was revised to \$754,949 for a total revised rate base of \$1,941,111.¹⁷³

A. Utility Plant in Service (“UPIS”)

UPIS is the original cost of the acquired systems along with acquisition-related expenses and post-acquisition improvements necessary to provide safe and reliable service.¹⁷⁴ This is the largest component of rate base and is the average amount of utility assets for the test year on which the Company should be allowed the opportunity to earn a return. Limestone included asset values for all systems it acquired as of April 30, 2024 in the historic test period.¹⁷⁵ The UPIS includes the acquisition asset values, transaction costs, and construction costs associated with improvements completed through the end of the test year.¹⁷⁶ Limestone’s UPIS for sewer for the period ending April 30, 2024 was \$10,961,828 and UPIS for water was \$1,688,819.¹⁷⁷

The Consumer Advocate determined the Company’s plant addition forecast was both feasible and reasonable based on past activity.¹⁷⁸ The Consumer Advocate adopts the Company’s forecasted utility plant in service for the adjusted test period and agrees with the Company’s attrition period UPIS of \$10,961,828 for sewer and \$1,688,819 for water.¹⁷⁹

B. Acquisition Premium Recovery

An acquisition adjustment is an amount paid for the acquisition of an asset that exceeds the

¹⁷³ *Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections*, TPUC Docket No. 24-00044, (Feb. 6, 2025), p. 3:10-15 (hereinafter “*Dittmore Direct*”). Schedule 2, File 1.1 and 1.2.

¹⁷⁴ *Direct Testimony of Brent Thies* at 10:16-18.

¹⁷⁵ *Id.* at 10:18-19.

¹⁷⁶ *Id.* at 10:19-21.

¹⁷⁷ *Id.* Exhibits BT 10.1 & 10.2.

¹⁷⁸ *Direct Testimony of William H. Novak* at 8, <Consumer Advocate Exhibit>, Schedules 2 and 3.

¹⁷⁹ *Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections*, Schedule 2.

net book value of that asset.¹⁸⁰ Limestone should not be allowed to recover Acquisition Premiums for two fundamental reasons; first, because such premiums were not originally included in Limestone's Petition, and two, allowing such premiums is a deviation from the basic concept of original cost based rates. Allowing the premiums will result in unjust and unreasonable rates for customers and utility owners are not entitled to enrichment simply for selling or purchasing assets and becoming a new owner of a utility.

Tenn. Comp. R & Regs. 1220-04-12-.04 (Acquisition Adjustment) is the current Commission rule that allows the Commission to order an acquisition adjustment to be incorporated into the acquired rate base if the Commission determines such an adjustment is warranted under the circumstances and will not result in unjust or unreasonable rates and charges for the acquiring utility or for customers.¹⁸¹ Further, the Commission rule provides that the Commission may consider certain factors when determining whether any acquisition adjustment should be included in the rate base. These include: (a) cost savings or increases resulting from consolidation of the selling utility's system into the acquiring utility's operations; (b) improvements in public utility services from the acquisition; (c) remediation of public health, safety and welfare concerns of the selling utility's system resulting from the acquisition; (d) incentives for acquisition of financially or operationally troubled systems, which may be demonstrated by bankruptcy, receivership, financial distress, notice of violation, order of abatement, or inability to continue as a going concern of the selling utility; (e) amount of any assets contributed or donated to the selling utility included in the proposed acquisition transaction; and (f) any other measure benefits, costs or service changes affecting acquired and/or existing customers resulting from the acquisition.¹⁸² While Limestone has correctly noted that the Commission has

¹⁸⁰ *Direct Testimony of Todd Thomas* at 143.

¹⁸¹ TENN. COMP. R. & REGS. 1220-04-14-.04(1) (Nov. 2021 Revised).

¹⁸² TENN. COMP. R. & REGS. 1220-04-14-.04(2) (Nov. 2021 Revised).

promulgated a rule that may allow for the recovery of an Acquisition Premium, Limestone has not satisfied the list of factors for determining if such premiums should be included in rate base by the Commission.

Limestone hangs its hat on being a professional system operator and that somehow justifies the allowance of the acquisition premiums across a number of its acquired systems because it “costs more to professionally operate a system than it does to operate a failing, non-compliant system.”¹⁸³

Limestone states that there are cost savings resulting from consolidation of the selling utility’s system into the acquiring utility’s operations and improvements in public utilities services resulting from the acquisition.¹⁸⁴ According to Limestone, none of the systems acquired by Limestone would have been able to procure professional operations services at a similar cost to those attained by Limestone through its state-wide RFP process and as a result, there have been cost savings resulting from consolidation of each of these systems by Limestone.¹⁸⁵ Limestone discussed the DSH – Lakeside Estates system, which Limestone has owned for a short-period of time and made upgrades to the system that provide “improvements in public utilities services” for customers.¹⁸⁶ Limestone declares customers have not only seen “improvements in public utilities services,” but because Limestone has avoided long-term expensive repairs, customers have realized cost savings.¹⁸⁷ However, as shown at the hearing, the numerous live customer comments and hundreds of additional written comments filed in this Docket suggest that Limestone’s customers have neither seen nor felt the impacts of the improvements by Limestone since Limestone took over the systems from their original owners.¹⁸⁸ Also, Limestone has not provided any quantifiable evidence of cost savings in

¹⁸³ *Id.* at 144; *Direct Testimony of Mike Duncan* at 13.

¹⁸⁴ *Direct Testimony of Todd Thomas* at 144.

¹⁸⁵ *Id.* at 146.

¹⁸⁶ *Id.* at 152.

¹⁸⁷ *Id.* at 152-153.

¹⁸⁸ *Hearing Transcript*, 2025-02-18 TPUC - 24-00044 - Volume I, at 9-23; Public Comments to TPUC Docket No. 24-00044.

public utilities services for its systems.

Given the customer comments and TDEC feedback on improvements and remediation related concerns, it is safe to say that the only factor that supports Limestone's requested recovery of some of the Acquisition Premiums is the policy incentive of the Commission to allow larger companies to rescue failing systems.

Further, there has been minimal remediation of public health, safety and welfare concerns of the selling utility's system resulting from the acquisition. In fact, as evidenced from the public comments on February 11, 2025, February 13, 2025, and on the hearing date of February 18, 2025, there are still serious issues with several of Limestone's systems (Candlewood, Grasslands-Cartwright Creek and Shiloh Falls).

For example, the Acquisition Premium being sought for the Cartwright Creek system is \$198,892 as reflected in the table below.¹⁸⁹ It is ironic that Limestone is seeking recovery of an Acquisition Premium for a system that just had a major sewage leak in early 2025 and continues to have issues and remediate the problem.

Acquisition	Transaction Cost	
Aqua	\$	40,523
Cartwright Creek	\$	198,892
Chapel Woods	\$	40,516
DSH	\$	94,278
Shiloh Falls	\$	66,556
Candlewood Lakes	\$	103,690
Total	\$	544,454

There are still other Limestone systems that have public health and safety issues and have still not

¹⁸⁹

Direct Testimony of Clark Kaml at 20:10-12 citing Direct Testimony of Brent Thies at 21:1-6.

properly and completely been remediated – Candlewood Lakes and Shiloh Falls. These systems continue to impact the public health, safety, and welfare concerns following the acquisition by Limestone. Lastly, there are no measurable benefits, cost or service changes for existing customers following the acquisition by Limestone.

As a Cartwright Creek customer stated at hearing, “...I assume when they did their due diligence in acquiring Cartwright that they knew that these improvements needed to be made... If they didn’t have the funds to do it, maybe they shouldn’t have made the acquisition.”¹⁹⁰ This succinctly echoes the Consumer Advocate’s position that Limestone took a calculated risk when acquiring these systems and that there was the definite possibility that Limestone would not recover these premiums.¹⁹¹ Limestone did not receive pre-approval of cost recovery and is familiar with this Commission’s past decisions and the Consumer Advocate’s past positions on this issue. It is clear that incentivization to recover these costs through rates could have reasonably been one of the most important factors in determining the acquisition.¹⁹² Nevertheless, Limestone had the financial capabilities to take on these systems absent any assurance of Acquisition Premium recovery.

1. Acquisition Transaction Costs

Transaction costs are costs that are incurred as part of an acquisition proceeding. In general, these are expenses that would not have existed but for the acquisition and are separate from the purchase cost of the system. These might include costs that occur prior, during, or after an acquisition. In this rate case, Limestone has included transaction costs and of course, this impacts rates.¹⁹³ Acquisition adjustments impact the revenue requirement in two ways. Limestone requested to include the acquisition premiums in rate base. This is reflected in the revenue

¹⁹⁰ *Hearing Transcript*, 2025-02-18 TPUC - 24-00044 - Volume I, at 13:5-10.

¹⁹¹ *Direct Testimony of Clark Kaml* at 20:10-12.

¹⁹² *Id.* at 20:21-21:2.

¹⁹³ *Id.* at 15:18.

requirement calculation through the financing required for the investment, thus increasing the overall revenue requirement.¹⁹⁴ They would also be amortized; and result in an amortization expense added to the cost of service.¹⁹⁵ While transaction costs are normal in an acquisition, some of these costs are pre-transaction.¹⁹⁶ These costs provide a benefit to the acquiring company, allowing it to estimate the amount of capital that will be required to operate and maintain the system, discover legal defects to the title, and understand the operational issues specific to the target system.¹⁹⁷ The acquiring company gains valuable information regarding whether it would be beneficial for the Company to proceed with the transaction.¹⁹⁸

There are unique acquisition costs for regulated utilities. For a rate regulated utility, cost recovery is not within the control of the utility or the market. The final decision of cost recovery, including if and how the costs will be recovered, is made by a regulatory body. These regulators generally rely on original-cost ratemaking and are tasked with ensuring that rates are just and reasonable.¹⁹⁹ Thus, a rate-regulated utility will often assess the likelihood that a recovery will be necessary and authorized.²⁰⁰ In this rate case, Limestone has included a total of \$544,454 in transaction costs, with \$425,354 for wastewater and \$118,100 for water.²⁰¹ These transaction costs are for the acquisitions of Aqua in the amount of \$40,523, Cartwright Creek for \$198,892, Chapel Woods for \$40,516, DSH for \$94,278, Shiloh Falls for \$66,556 and Candlewood Lakes for \$103,690.²⁰²

Limestone did not explain the origins of these costs and merely provided a general

¹⁹⁴ *Direct Testimony of Clark Kaml* at 15:18-16:1.

¹⁹⁵ *Id.* at 16:1-2.

¹⁹⁶ *Id.* at 16:1-2.

¹⁹⁷ *Id.* at 16:5-6.

¹⁹⁸ *Id.* at 16:6-9.

¹⁹⁹ *Direct Testimony of Clark Kaml* at 16:9-10.

²⁰⁰ *Id.* at 16:17-19.

²⁰¹ *Id.* at 17:2-3 citing *Direct Testimony of Brent Thies* at 21:1-6.

²⁰² *Id.* at 17:1-4.

description and explained that transaction costs include real estate related legal costs, regulatory legal costs, system mapping, and engineering analysis.²⁰³ Limestone also included legal costs for each acquisition in response to a discovery request from the Consumer Advocate²⁰⁴ which was confidential; however, the actual amount that Limestone is seeking to recover is unclear. The legal costs are bundled into four types of expenses represented as transaction costs.²⁰⁵

In North Carolina, the Public Utility Commission denied other transactional costs in excess of \$300,00 and only allowed recovery of \$10,000 in the acquisition docket for Limestone's affiliate in North Carolina and stated that the costs were a benefit to the Company and were only a benefit to the ratepayers to the extent that they were reasonably and prudently incurred.²⁰⁶

As stated above and emphasized again, this Commission never gave any assurance to Limestone that these types of costs would be recoverable through rates. In fact, the Commission has deferred this issue. In TPUC Docket No. 21-00055 (Shiloh Falls), this Commission stated that these regulatory and transaction costs would be addressed in Limestone's initial rate case. TPUC further stated that Limestone was restricted from requesting recovery of legal expenses in excess of 50% of the amount paid to local legal counsel.²⁰⁷

Historically, Limestone was aware of the TPUC's position on whether ratepayers should be shouldering the burden of due diligence costs. TPUC has stated that due diligence costs are not

²⁰³ *Direct Testimony of Clark Kaml* at 17:6-11 citing *Direct Testimony of Brent Thies* at 21:13 – 22:21.

²⁰⁴ *Id.* at 17:6-11 citing Limestone's Response to Consumer Advocate DR No. 1-26.

²⁰⁵ *Id.* at 17:6-11 citing Limestone's Response to Consumer Advocate DR No. 1-26.

²⁰⁶ *Id.* at 18 citing Notice to Parties of Recommended Order, p. 27-28, NCUC Docket Nos. W-933, Sub 12 & W-1328, Sub 0 (Feb. 7, 2024). A copy of this Recommended Order is attached as Exhibit CDK-4. The Commission did allow for the Limestone affiliate the opportunity to provide detailed evidence supporting its request for \$300,000 in the Company's next rate case, but Staff would audit such a request. The Limestone affiliate subsequently withdrew its application. Notice of Dismissal and Withdrawal of Application, NCUC Docket Nos. W-933, Sub 12 & W-1328, Sub 0 (March 1, 2024). This NCUC docket can be accessed at <https://starw1.ncuc.gov/NCUC/page/docketdocs/PSC/DocketDetails.aspx?DocketId=2257a2df-9424-4397-8c98-2db4c3571cf8>.

²⁰⁷ *Direct Testimony of Clark Kaml* at 19:7-10 citing Order Approving Settlement Agreement and Transfer of Systems and Granting Certificate of Convenience and Necessity, p. 5, TPUC Docket No. 21-00055 (Dec. 2, 2022).

costs associated with the delivery of water services and such costs benefit shareholders and it is unacceptable for such costs to be funded solely by ratepayers.²⁰⁸

The Consumer Advocate is not convinced that there are direct benefits to consumers²⁰⁹ of these costs that would justify allowing those expenses into rates. Ratepayers should not have to shoulder this additional burden given the current economic conditions. Additionally, Limestone should have the burden to demonstrate that customers will benefit directly from them and that there will ultimately be cost savings.

Furthermore, although Limestone is requesting recovery of these transaction costs, the Company has not included these costs in the original revenue requirement calculation. Thus, the original filing understated the actual amount of the rate increase request, and more importantly the potential impacts of the Company's proposal have been understated in communication to its ratepayers. If Limestone was requesting recovery of these expenses, they should have been included in the original revenue requirement request. Since they were not included in the original Petition, they should not be considered and should be denied by the Commission. Including them at this juncture would seem to suggest that the rate case period should be reset since this would be a material change to the Petition originally filed by Limestone.

C. Cash Working Capital

Cash working capital is a component of rate base. It represents the amount of funds needed to finance the day-to-day operations of the utility and bridges the gap between the time when funds are required to provide service to customers, and the time revenues are received from customers as reimbursement for these services. The Cash Working Capital component of Rate Base

²⁰⁸ *Id.* at p. 19:11-18 citing *Order Approving Purchase Agreement, Franchise Water Agreement and Certificate of Public Convenience and Necessity*, p. 21, TRA Docket No. 12-00157 (Oct. 15, 2013).

²⁰⁹ *Direct Testimony of Clark Kaml* at 21:5-11.

may be positive or negative. A negative requirement will result when the lead in operating expense payments exceed the revenue lag associated with revenue collections. The Cash Working Capital calculation is not a measure of regulatory lag, but instead a measure of how much cash the utility must keep on hand to pay operating costs. Cash Working Capital is included in rate base and Limestone is permitted to earn a return on these amounts.

Limestone opted to use the 45-day convention, also known as the 1/8 convention.²¹⁰ This convention multiplies the operating expenses (excluding depreciation, overhead allocation and taxes) by 45/365 to produce a working capital amount to be included in rate base. The Company has used the 45-day convention to calculate the \$39,210 cash working capital amount for water and \$129,461 for sewer.²¹¹ These amounts are included in the rate base calculation.²¹² The Consumer Advocate believes that the 45-day approach does not accurately measure the true cash needs of the utility. A more accurate measure of Cash Working Capital is to perform a lead-lag study. However, such studies are quite time consuming (costly) to complete and are not cost justified for a smaller utility like Limestone. For the purposes of this rate case, the Consumer Advocate accepts Limestone's calculations for Cash Working Capital.²¹³

D. Land Price and Land Rights Values

In a utility rate case, "land price and land rights" refer to the cost of acquiring land and the associated property rights needed by a utility company to construct and operate its infrastructure, which is factored into the overall cost which is used to determine the rates charged to customers. As explained previously, the amount in question is significant [REDACTED].²¹⁴ However, these are

²¹⁰ Direct Testimony of Brent Thies at 23:13-14.

²¹¹ Id. at 23:20-22; Petitioner's Exhibit BT-13.1 and BT-13.2.

²¹² Pre-Filed Direct Testimony of Limestone Witness Brent Thies at 23:22.

²¹³ Consumer Advocate Wastewater Exhibit, Schedule 3.

²¹⁴ Direct Testimony of Clark Kaml, at 13:7. (CONFIDENTIAL)

not the original booked costs for the land and land rights.²¹⁵ The values proposed by Limestone are higher than those reported in other sources, which was confirmed in Limestone's response to discovery.²¹⁶ Limestone increased the land and land rights from the selling companies' books.²¹⁷

A fundamental premise of rate base rate of return regulation is the use of original (historical) cost.²¹⁸ This limits rate base to the cost of acquiring assets, less depreciation, rather than current market value or replacement cost.²¹⁹ This straightforward and transparent approach ensures that customers pay for costs incurred by a service provider only once, and that the cost paid is the actual cost incurred.

The Consumer Advocate has determined that the payment related to the acquisition of land and land rights is excessive. The Company has not provided any information to suggest that there are alternative uses for the land other than the operation of the utility. Since there is no alternative use for the property other than the provision of utility service, there is no basis to acquire the property for an amount in excess of its book value. The proposal to write-up the value of the land is essentially an Acquisition Premium, and a Gain on the Sale for the selling utilities. If allowed, it will result in increased rates simply due to the transfer of ownership.²²⁰

While Limestone claims this is not an Acquisition Premium, it is similar to an Acquisition Premium. An Acquisition Premium is defined as the amount of purchase price over the net book value. The land was on the books, at cost, and there is no indication that there was an inherent

²¹⁵ *Id.* at 13:1-3.

²¹⁶ *Id.* at 13:3-4 citing Limestone's Response to the Consumer Advocate DR No. 2-7 <DR 2-7 Land – Confidential.xlsx>.

²¹⁷ *Id.*

²¹⁸ "Tennessee is an 'original cost' jurisdiction. Under our system of regulation, utility plant is 'worth' only its present net book value (original cost less accumulated depreciation). The comparison between net book value and the cost of building new plant has no significance for rate-making purposes because it ignores the ratepayers' contribution to the existing plant." Order Upon Reconsideration, TPSC Docket No. U-84-7333 (Aug. 11, 1985). A copy of this order is attached as Exhibit CDK-2.

²¹⁹ *Direct Testimony of Clark Kaml* at 13:10-11.

²²⁰ *Id.* at 14:8-9.

accounting error from previous owners. Here, Limestone made a write-up without any actual capital investment, in which case there should not be an increase in value.²²¹ Also, Limestone has not provided any appraisals for the values in the rate base and in its responses to discovery the Company stated that they did not use appraisals for value included in rate base.²²² Limestone has not provided any support for its decision to increase the land values.²²³ The exclusion of the write-up in land values will decrease the rate base by the amount of the write-up. The revenue requirement will be reduced by the cost of capital multiplied by the write-up amount.²²⁴ The portion of land value and land rights exceeding the booked cost at the time of the purchase is excessive and should not be allowed and be removed from rate base.

One of the fundamental premises of calculating rate base is that assets are booked at original (historical) cost, meaning that rate base is limited to the original cost of the asset, less depreciation, rather than the current market value of the asset. Otherwise, rate base would not represent the actual costs incurred by the service provider at the time they were incurred. Limestone's proposed land prices related to the systems that it has acquired in Tennessee do not adhere to this essential tenet of calculating rate base. Instead, these marked-up values represent an Acquisition Premium or alternatively an arbitrary write-up of the land without actual, additional capital investment.

Limestone has provided no evidence to suggest that the land in connection with the systems it acquired in Tennessee serves any additional purpose beyond what that land was originally acquired for: operating the water and wastewater systems. The values should remain at original cost in rate base. If these values are not the original cost, it would result in an excess of book value of the asset

²²¹ *Id.* at 14:10-15.

²²² *Id.* at 14:19-20 - 15:1-2 citing Limestone's Response to the Consumer Advocate DR No. 2-7, File <DR 2-7 Land-Confidential.xlsx>

²²³ *Id.* at 14:16-18.

²²⁴ *Direct Testimony of Clark Kaml* at 15:7-9.

and the land prices would be an Acquisition Premium. For reasons similar to those addressed above, the Acquisition Premiums associated with these systems do not satisfy the Commission's criteria for awarding recovery. The Consumer Advocate recommends that this be disallowed from the calculation and recovery of rate base in this rate case.

E. Contributions in Aid of Construction ("CIAC")

CIAC is third-party, non-investor supplied capital in the form of non-refundable money or physical property. CIAC is a deduction from rate base because it represents that portion of rate base financed by customers or by other investors. Limestone's proposed CIAC is \$5,124,592 for sewer and \$166,937 for water totaling \$5,292,529.²²⁵ Limestone included Tap Fees that a customer pays to connect to the system in CIAC.²²⁶

The Consumer Advocate [REDACTED]

[REDACTED] The Consumer Advocate disputes the inclusion of Tap Fees and Inspection Fees receipts as Contributions in Aid of Construction. The Commission has a long history of requiring utilities to record these types of receipts as revenues. For example, in the last rate case for Cartwright Creek, \$21,000 was included in Revenues for Tap Fees and Inspection Fees. Likewise in the last rate case for Aqua Utilities, \$21,375 was included in Revenues for Tap Fees. Finally, in the CCN Application for Shiloh Falls Utilities, \$25,500 was included in Revenues for Tap Fees. There is a clear history of the Commission's treatment for the classification of Tap Fee and Inspection Fee receipts as revenues.²²⁸

The Consumer Advocate recommends that the Commission treat Inspection Fees and Tap Fees as Revenues and that going forward such receipts be recorded as revenue.

²²⁵ Direct Testimony of Brent Thies at 26:9-11; Petitioner's Exhibit BT-12.1 & B.T. 12.2.

²²⁶ Id. at 26:6-11.

²²⁷ [REDACTED]

²²⁸ Direct Testimony of William H. Novak at 12:17-18:1-4.

Additionally, Limestone has stated that Cartwright Creek CIAC balances were not amortized.²²⁹ The CIAC balance on the Cartwright Creek books is at the original level and creates a mismatch between the value of assets supported by the CIAC and the CIAC balances.²³⁰ Limestone stated that Cartwright Creek stopped recording any amortization or depreciation expense on its books, which has created difficulty in determining the proper balance of CIAC and accumulated depreciation associated with the Cartwright Creek assets.²³¹ Limestone proposes to utilize an average amortization rate of 5 percent based on the utility plant assets on the books of Cartwright Creek on the day of the acquisition by Limestone so that the CIAC balances match the Cartwright Creek assets.²³² This is reasonable from the perspective of an average life basis.²³³

Based on the CIAC balances and amortization rate of 5%, the Consumer Advocate recommends a Pro Forma CIAC amortization, credit expense, of \$14,896 for water and \$293,174 for wastewater.²³⁴

VIII. EXPENSES

A. Operating And Maintenance Expenses

Limestone's operating expenses included in cost of service are categorized into three main groups.²³⁵ First, costs that are directly incurred by Limestone, include contract operations, fuel and power, chemicals, maintenance, bad debt, depreciation and amortization, property taxes and administrative expenses.²³⁶ Second, there are costs incurred by Limestone which are part of contracts or invoices where services to all CSWR subsidiaries are combined for administrative and

²²⁹ *Direct Testimony of Clark Kaml* at 23 citing *Direct Testimony of Brent Thies* at 29:5-6.

²³⁰ *Id.* at 23 citing *Direct Testimony of Brent Thies* at 29:6-9.

²³¹ *Direct Testimony of Clark Kaml*, at 23:6-8, citing *Direct Testimony Of Brent Thies* at 29:14-17.

²³² *Id.* at 23:11-13, citing *Direct Testimony Of Brent Thies* at 29:18-22.

²³³ *Id.* at 23:14-15.

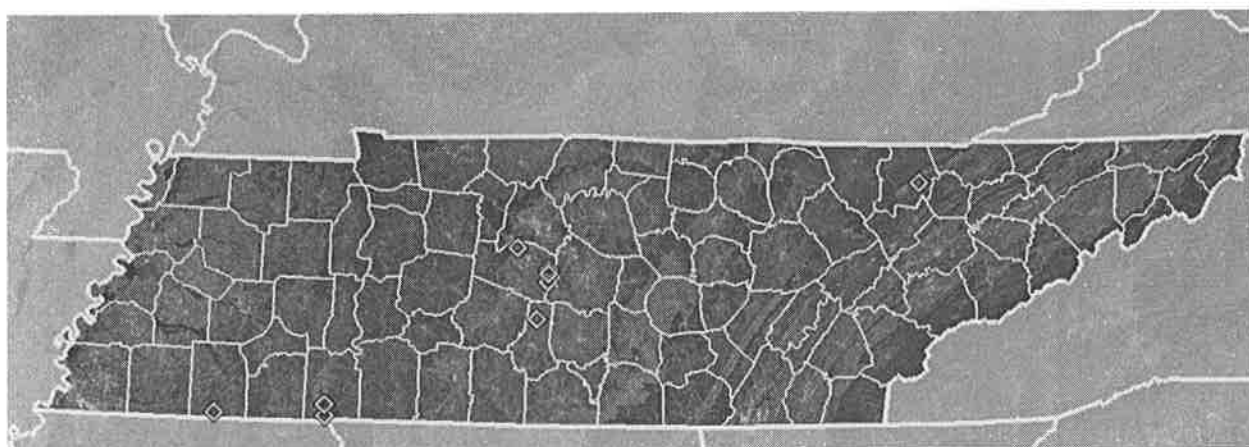
²³⁴ *Id.* at 24:1-3. These adjustments are set out in Confidential Workpaper CDK-11.

²³⁵ *Direct Testimony of Clare Donovan* at 7:4-5.

²³⁶ *Id.* at 7:5-8.

cost efficiency and directly charged to the operating utility subsidiaries.²³⁷ These jointly billed costs include property and liability insurance, certain software and management consulting services and billing system costs.²³⁸ Third, there are indirect charges in the form of overhead charges allocated to Limestone by its parent, CSWR.²³⁹ The methodologies used to assign direct charges, jointly billed charges and indirect charges to Limestone are the same as those used to assign charges to all other CSWR affiliates and are part of CSWR's written accounting policy as outlined in the Company's Cost Allocation Manual ("CAM").²⁴⁰

Limestone has two (2) water and eight (8) wastewater systems in Tennessee that are geographically dispersed across the state.²⁴¹



Limestone Exhibit TT-1

Limestone claims that since its systems are geographically dispersed it is not cost-effective for Limestone to internalize field operations for its service areas like Tennessee-American Water Company, whose systems are located within 30 miles of each other in southeast Tennessee and has a treatment plant in Chattanooga to serve its large service area.²⁴² According to Limestone, this

²³⁷ *Id.* at 7:8-11.

²³⁸ *Id.* at 7:11-13.

²³⁹ *Id.* at 7:13-14.

²⁴⁰ *Direct Testimony of Clare Donovan* at 7:14-18.

²⁴¹ *Direct Testimony of Todd Thomas* at 6.

²⁴² *Id.* at 5-6.

geographical dispersion and the limited number of connections served in Tennessee make it impossible for Limestone to cost-effectively employ an in-house workforce of sufficient size to perform all required O&M functions necessary to fulfill the objective of providing customers safe, reliable, and timely utility service at reasonable rates.²⁴³ As a result, Limestone uses an operations model based around contract operations.²⁴⁴

Limestone states that it is more economical to retain third-party contractors who already have experienced operators and the required state licenses.²⁴⁵ Limestone's current contractor in Tennessee is Clearwater Solutions, LLC ("Clearwater"). Clearwater operates and maintains the Company's water and wastewater systems and according to Limestone, provides a highly experienced, dedicated, professional team of onsite and bench strength resources for expert, compliant operations of water/wastewater systems.²⁴⁶

Limestone's professional third-party water and sewer operations and maintenance company²⁴⁷ is managed by an employee of CSWR, a Regional Manager for the system operations of Limestone.²⁴⁸ The contract operations costs are incurred exclusively for Limestone and are billed directly to Limestone.²⁴⁹ The Consumer Advocate is not aware of any other water or wastewater utility that relies solely on such a high level of contract services and suggests a more balanced approach by Limestone.²⁵⁰

The Consumer Advocate does not believe that the use of third-party contractors is the most efficient use of company resources.²⁵¹ First, Limestone has not provided any type of quantitative

²⁴³ *Id.* at 7.

²⁴⁴ *Id.* at 7.

²⁴⁵ *Id.* at 7.

²⁴⁶ *Direct Testimony of Todd Thomas* at 11.

²⁴⁷ *Direct Testimony of Clare Donovan* at 8:1-3.

²⁴⁸ *Id.* at 8:3-4.

²⁴⁹ *Id.* at 8: 6-8.

²⁵⁰ *Direct Testimony of William H. Novak* at 6:3-14.

²⁵¹ *Id.* at 15:1-4.

analysis verifying that its use of third-party contractors economically outweighs that of direct employees.²⁵² There is insufficient evidence to show it is more economical to use third-party contractors. Without a cost analysis, it is impossible to fully determine the cost/benefits of third-party contractors vs. direct employees.²⁵³

Next, Limestone's contrast of its operations to Tennessee-American Water Company is not really an apples-to-apples comparison. A better example would be to compare the operations of Limestone to Tennessee Wastewater Systems, Inc. ("TWSI"). TWSI provides wastewater services to approximately 2,760 residential customers and 804 commercial customers throughout Tennessee.²⁵⁴ In TWSI's last rate case, \$623,560 was included for wages while only \$386,670 was included for Outside Contractors.²⁵⁵ This distribution shows a balance between the use of outside contractors and direct employees rather than relying exclusively on one over the other.²⁵⁶

B. Other Expenses

1. Non-Revenue Water

Limestone stated it was currently experiencing a water loss percentage of 18.45%.²⁵⁷ This water loss amount of 18.45% is greater than the baseline amount used by the Commission in prior decisions. Further, the Company has not provided any support for their 18.45% Non-Revenue Water ("NRW") proposal.²⁵⁸

²⁵² *Id.* at 15: 4-6.

²⁵³ *Id.* at 15: 6-7.

²⁵⁴ *Id.* at 15: 9-14 citing Docket No. 20-00009, *Joint Petition of Tennessee Wastewater Systems, Inc and TPUC Staff (as a Party) to Increase Rates and Charges*, Joint Petition, p. 1, January 31, 2020.

²⁵⁵ *Direct Testimony of William H. Novak* at 15: 14-15 citing Docket No. 20-00009, *Joint Petition of Tennessee Wastewater Systems, Inc and TPUC Staff (as a Party) to Increase Rates and Charges*, Pre-Filed Direct Testimony of Kevin McClenathan, Commission Staff Exhibit, Schedules 4 and 5, January 31, 2020.

²⁵⁶ *Id.* at 15: 15-17.

²⁵⁷ *Direct Testimony of Aaron Silas* at 23:11.

²⁵⁸ *Direct Testimony of Alex Bradley* at 13:8-10, TPUC Docket No. 24-00044 (Dec. 19, 2024) (hereinafter "Bradley"). Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

Limestone is proposing to treat all known leaks as “accounted for” which resulted in the 18.45% water loss.²⁵⁹ Limestone appears to be following the same formula set forth in Tennessee-American Water’s last rate case which is the difference of the total water produced or purchased minus what is accounted for.²⁶⁰

The Consumer Advocate recently addressed the issue of a NRW limiter and its calculation in the Tennessee-American Water rate case.²⁶¹ The Commission has not yet issued its written decision. The Consumer Advocate requests that the Commission apply the same NRW limitation and calculation to Limestone as it will for Tennessee-American Water. With this in mind, the Consumer Advocate reduced water production costs to account for the Commission’s prior water loss policies. The Consumer Advocate reduced the water production costs to 96.55% to account for this and this results in a reduction in Water Expense O&M of \$6,004.²⁶²

2. State And Federal Income Tax Expense

Limestone is organized as a limited liability company and has elected treatment as a C-Corporation for federal and state tax purposes.²⁶³ The income tax rates used by Limestone are 21% for federal income and 6.5% for Tennessee state corporate income. The income tax was calculated by first using the estimated equity return on rate base included in the revenue requirement and multiplying that return by an Income Conversation Factor of 1.35%.²⁶⁴

²⁵⁹ *Direct Testimony of Aaron Silas* at 23:6-8; 182:25-183:1

²⁶⁰ *Direct Testimony of Alex Bradley* at 13:14-18. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025). *Direct Testimony of Alex Bradley* at 5:2-3. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

²⁶¹ *Consumer Advocate Division’s Post-Hearing Brief* at 52-54, TPUC Docket No. 24-00032 (December 10, 2024).

²⁶² *Direct Testimony of Alex Bradley* at 8:14-18. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

²⁶³ *Direct Testimony of Brent Thies* at 30:4-5.

²⁶⁴ *Id.* at 30:9-12.

The Gross Income Conversion Factor reflects that each dollar of equity granted to Limestone has a tax responsibility for both federal and state income tax.²⁶⁵ The Gross Income Conversion Factor incorporates the federal and state tax rates, along with an allowance for bad debt of 1%, into an income multiplier.²⁶⁶ Limestone used a Gross Income Conversion Factor of 1.35%.²⁶⁷

The revenue conversion factor is used to adjust a utility's projected revenue requirement to account for factors like income taxes and uncollectible accounts, essentially translating the "net" revenue needed into the "gross" revenue that must be collected from customers to cover all anticipated costs and generate the desired profit margin. In his testimony, Consumer Advocate witness Mr. Dittemore proposed modification to the Gross Revenue Conversion Factor of Limestone from 1.3867496 to 1.298829, a difference of -0.068667.²⁶⁸

On February 20, 2025, the Consumer Advocate filed supplemental testimony and workpapers of Mr. Dittemore in this Docket, including a correction to a formula error in the original schedules submitted on December 19, 2024. The Consumer Advocate included \$6,369 in General Taxes within the Company's Water Company Income Statement as reflected in Schedule 5 (water). In addition to Schedule 5, this change impacts information contained in: Water Schedules 1, 1.2, and 7; and Wastewater Schedules 1 and 10, which incorporates the rate increases for both water and wastewater services.²⁶⁹

Limestone's taxable income was \$204,974 for sewer and \$-315,274 for water. The Consumer Advocate made an adjustment to the state and federal income tax expense in the amount of \$-68,622 for water expense and \$-43,856 for wastewater expense. These amounts were modified

²⁶⁵ *Id.* at 30:14-15.

²⁶⁶ *Id.* at 30:14-17.

²⁶⁷ *Id.* at 30:17-18.

²⁶⁸ *Direct Testimony of David N. Dittemore Adopting the Direct Testimony of Alex Bradley with Corrections*, Schedule 1.

²⁶⁹ *Id.* at 5: 4-9; Schedule 5.

to \$-82,070 (water) and \$-53,570 (wastewater) in the Consumer Advocate's February 20, 2025, filing.

The Consumer Advocate's adjustments to the Company's pro-forma income statements are necessary to align Income Tax Expense with the Company's results of Operations. The Company did not calculate Income Tax Expense in its pro-forma operating results. Specifically, the Company inserted a value of zero for Income Tax Expense in its water and wastewater expenses as shown in its wastewater and water operating results, in Schedules BT-2.1 and BT-2.2, respectively.

The Company's failure to provide an Income Tax expense calculation distorts its test period operating results. Furthermore, the insertion of zero tax expense does not comply with Generally Accepted Accounting Principles "(GAAP)", whereby Income Tax Expense is required to be computed on actual operating results. The fact that a negative income tax expense exists is not justification for inserting an artificial zero expense within the Company's pro-forma operating results.

The Consumer Advocate's tax calculation is consistent with GAAP and with the Commissions' historic method for computing Income Tax Expense in the pro-forma test period. Accordingly, the Commission should adopt the Consumer Advocate's tax calculation recommendation and the revenue conversion factor proposed by the Consumer Advocate.

3. Rate Case Expense

The Company's rate case expense is the costs incurred by Limestone to prepare its rate case filing and comply with the regulatory process required by the Commission to adjust rates. These costs include legal fees, consultant fees, travel expenses, and other expenses. Limestone estimates its rate case expense will be [REDACTED] The Company proposes amortizing its forecasted total

rate case expense over a two-year period and recovering it through base rates.²⁷¹ The Consumer Advocate states that these legal costs for a case this size are excessive and actual legal costs should be substantially less than this forecast.²⁷²

The Company is requesting to collect [REDACTED] for these costs over a two-year period. This period is unusually short and results in an excessive cost recovery by the Company.²⁷³ Most utilities in Tennessee, before the ARM legislation was in place, did not file rate cases every two years. For any period in which rates are in effect beyond the two-year period the Company would receive revenue for an expense that terminates at the end of the two-year period, resulting in increased net income for Limestone. Since there is a 240-day review period associated with rate case filings, Limestone is essentially assuming it will file a new rate increase request within sixteen months of when new rates from this proceeding are established. This is an unreasonably short period and places ratepayers at risk for excessive costs.²⁷⁴

While the Consumer Advocate does not dispute that Limestone is entitled to recover its actual and reasonable rate case costs, the Consumer Advocate requests that the Commission remove the Company's rate case expense from base rates and establish a separate surcharge to recover these costs.²⁷⁵ The rationale behind both these recommendations is that they will allow actual costs to be

²⁷¹ Limestone Revenue Requirement, Tabs 3.1 and Tabs 3.2.

²⁷² *Direct Testimony of Alex Bradley* at 15:17-18. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025). *Direct Testimony of Alex Bradley*, at 5:2-3. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

²⁷³ *Id.* at 16:2-4. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

²⁷⁴ *Id.* at 16:8-15. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

²⁷⁵ *Id.* at 16:2-4. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

recovered instead of estimates.²⁷⁶ One advantage of a separate surcharge is that it would consider known costs at the conclusion of this rate case instead of estimates. In addition, a separate surcharge would restrict the Company to just the recovery of known rate case costs and would then terminate as opposed to being a continuing base rate adjustment. As a result of these advantages, the Consumer Advocate recommends the omission of the Company's estimated rate case costs and the related amortization from base rates and instead set a separate surcharge to recover these costs.²⁷⁷

The Consumer Advocate maintains that total expenses must meet an overall test of reasonableness in light of prevailing business plans, economic conditions, and, in comparison, to other utilities in Tennessee. In other words, not only does the methodology used to forecast each expense have to be reasonable, but these methodologies, when considered together, must also result in reasonable total expenses consistent with the current business and economic environment. The Consumer Advocate has determined Limestone's forecast of certain expenses fails to meet this overall test of reasonableness.

IX. CONDITION OF WATER AND WASTEWATER SYSTEMS AND SERVICE QUALITY ISSUES

According to Limestone, several of the systems acquired by the Company suffered from operational shortcomings and deficiencies. In many cases, these deficiencies resulted in a failure to meet environmental permit limits. For example, modifications were made by the Company to the Aqua Utilities wastewater system to return proper functioning to the aeration and spray field and to restore capacity at 41 lift stations.²⁷⁸

²⁷⁶ *Id.* at 16:8-15. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

²⁷⁷ *Direct Testimony of Alex Bradley* at 16:2-4. Letter to Chairman David F. Jones from Karen H. Stachowski Consumer Advocate Re Supplement Testimony and Workpapers Filed with the Direct Testimony of David N. Dittmore Adopting the Direct Testimony of Alex Bradley with Corrections (February 20, 2025).

²⁷⁸ *Direct Testimony of Mike Duncan* at 5.

Limestone indicated that the problems and challenges were much more extensive at the Grassland facility because it was a 50-year-old system that was allowed to deteriorate to the point that the system needs to be completely replaced.²⁷⁹ There is rusting and deterioration of the tanks and aeration facilities have reduced treatment efficacy.²⁸⁰ As a result, the plant has struggled to meet permitted limits for biochemical oxygen demand, ammonia, total nitrogen, dissolved oxygen, suspended solids, total residual chlorine, and E. coli.²⁸¹ Limestone stated that a new treatment facility is being designed and permitted, and has taken several steps to mitigate problems and achieve the highest level of performance from that system in the interim.²⁸² Limestone instituted a short-term solution by repairing the aeration equipment, including the replacement of rusted steel air headers, drop pipes and diffusers, to ensure the addition of oxygen to the aeration tank.²⁸³ Additionally, the system was plagued by impacted solids in the clarifier, chlorine contact chamber, filtration system tanks, lift stations, and the sludge return line. In such cases, impacted solids were pumped from these various system components, and service was restored.²⁸⁴ Limestone stated the system must be replaced to meet total loading limits for the increased flow that the plant is receiving, and Limestone has made short-term upgrades to allow the system to operate at its peak efficiency within the requirements for effluent concentration limits.²⁸⁵

However, it appears the system is not working at peak efficiency and there are several serious problems at the Grassland system. According to consumer comments at the public hearing and the public comments filed in this Docket, in or around January 2025, there was a sewage leak from two manholes at the Grassland facility due to a system failure. Customers have stated there

²⁷⁹ *Id.* at 5.

²⁸⁰ *Id.*

²⁸¹ *Id.*

²⁸² *Id.*

²⁸³ *Id.*

²⁸⁴ *Direct Testimony of Mike Duncan* at 5.

²⁸⁵ *Id.*

was a sewage backup, leak and other problems in the subdivision related to the treatment plant.²⁸⁶ Further, there is mud, and trucks are entering the community areas where there is sewage and it smells.²⁸⁷ As recently as January 2025, there was raw sewage, wastewater, and damage to the River Rest community facilities.²⁸⁸

According to Limestone, Hideaway Hills included a recent developer-constructed expansion, much of which was overly sophisticated, oversized relative to the flow generated, poorly configured, and lacked automation that was included in original design plans. As a result, Limestone had to make significant revisions to make that developer-constructed expansion operate properly.²⁸⁹

Limestone has a compliance function through CSWR and stated there was a CSWR compliance team.²⁹⁰ Limestone stated the Environmental, Health and Safety (“EHS”) team works with the state manager, O&M contractor and CSWR engineers to maintain compliance with the Clean Water Act, Safe Drinking Water Act, and Occupational Safety and Health Administration regulatory requirements. Limestone stated the EHS focuses primarily on four important functions:²⁹¹

- (1) Monitoring and completion of system compliance tasks for each system operated by Limestone Water including but not limited to issuing Consumer Confidence Reports (“CCRs”) for water systems, backflow device program management, and lead service line inventories;
- (2) Responding to Environmental Agency correspondence that arise from agency inspection, complaints to agencies, and violation of numeric standards. In this role, the EHS team ensures that corrective actions are completed and accurately reported to the relevant agency;

²⁸⁶ *Transcript Of Public Comments, Nashville, Tennessee*, at 10-11, TPUC Docket No. 24-00044 (Feb. 13, 2025).

²⁸⁷ *Transcript Of Public Comments, Nashville, Tennessee*, at 11, TPUC Docket No. 24-00044 (Feb. 13, 2025).

²⁸⁸ *Id.* at 43.

²⁸⁹ *Direct Testimony of Mike Duncan* at 6.

²⁹⁰ *Id.* at 19.

²⁹¹ *Id.*

- (3) Effectuation of state and local operating permit transfers and renewals; and
- (4) Facility inspections of any system acquisitions prior to closing and at least once a year thereafter to ensure compliance with regulations governing facility operations and maintenance.²⁹²

Limestone claimed the EHS team provides immediate benefits to the customers of the small systems acquired by the Company. As such, by applying the talents of such a team to the systems that are acquired, Limestone is capable of providing immediate benefits to customers.²⁹³

While Limestone claimed customers have received tangible benefits from the acquisition of the systems it acquired, the reality is that customers have not received tangible benefits.²⁹⁴ In fact, in the Candlewood system there are serious water quality issues that persist and have not been remediated by Limestone. Several customers have filed comments in this Docket with photographs showing brown colored water coming from their taps. Most of these customers have had to use bottled water on a continuous and ongoing basis for drinking, cooking and/or bathing.²⁹⁵ It does not appear the EHS team that is working with the state manager, O&M contractor and CSWR engineers is maintaining compliance at this Limestone system.

Based on the 283 customer complaints filed as of the hearing date, it does not appear the systems are operating at an optimal level, and customers are not receiving improved water and wastewater services.

Limestone also stated that as a result of the improved operation of wastewater treatment facilities, the discharge into the Tennessee environment has improved immensely.²⁹⁶ However, there continues to be issues concerning Limestone's wastewater treatment facilities. Limestone still has not undertaken the major capital projects urgently needed, such as the replacement at Grassland

²⁹² *Direct Testimony of Mike Duncan at 20.*

²⁹³ *Id.* at 20-21.

²⁹⁴ *Id.* at 21.

²⁹⁵ *Transcript Of Public Comments Counce, Tennessee January 30, 2025*, and Public Comments filed in TPUC Docket No. 24-00044.

²⁹⁶ *Direct Testimony of Mike Duncan at 7.*

or expansion at Shiloh Falls and Candlewood Lakes. Limestone has failed to provide evidence or proof of any tangible benefits to customers to date. There is no verifiable evidence that there has been improvements to the operation of wastewater treatment facilities, and that the alleged improvements are reducing the discharge into the Tennessee environment.

Limestone also argues it has brought professional services to its customers and has done so by leveraging the economies of scale inherent from Limestone's existence as part of a larger 11-state CSWR entity. Limestone highlighted the economies of scale benefit, particularly with the customer service function, claiming it allows them to leverage services because it is one of 11 CSWR-affiliated utility companies but there is no quantifiable evidence in this rate case to show any economies of scale benefits.

Limestone also claims that there are similar economies of scale in professional services including finance, accounting, billing, human resources, engineering, IT, regulatory, corporate communications, legal, and overall managerial support. According to Limestone, it stated that given the small size of the individual systems acquired by Limestone, and the associated small number of customers served by each system, it would have been virtually impossible for the previous owners to provide a similar level of utility services and investments as those currently being provided and made by the Company.²⁹⁷ During cross-exam Limestone Witness Thomas testified concerning vegetation management costs, and those costs did not support the economies of scale argument that was advanced by Limestone.²⁹⁸ Also, Limestone stated in response to the Consumer Advocate's first discovery requests that it was not possible for Limestone to identify specific metrics to identify cost drivers in economies of scale or other efficiencies.²⁹⁹ Limestone

²⁹⁷ *Direct Testimony of Mike Duncan* at 8.

²⁹⁸ *Hearing Transcript*, Vol. II, 2025-02-19 Docket 24-00044 Hearing Day 2 CONFIDENTIAL, at 301-313:11 (Cross Examination of Todd Thomas).

²⁹⁹ Company Response to Consumer Advocate DR No. 1-55.

merely stated that the economies of scale results from CSWR's ability to provide goods and services at a lower unit cost than smaller entities could obtain those services on its own.³⁰⁰ However, Limestone did not provide any tangible evidence of the economies of scale. Rather, Limestone merely made a blanket statement that services are provided at scale at CSWR and then allocated to its affiliates, such as Limestone, and are at a fraction of what it would cost each affiliate to provide or procure such services on its own.³⁰¹ The Consumer Advocate disputes Limestone's contention that CSWR provides services at a lower cost than each affiliate would be available to provide or procure on its own.

X. TERMINATION OF FINANCIAL SECURITY ESCROWS

Limestone seeks to terminate the financial security escrows. Financial security escrows are created to ensure that there is sufficient capital available to meet capital improvement requirements.³⁰² The Commission has promulgated a rule on escrow accounts, which states in part:³⁰³

Reserve/escrow accounts established by a public wastewater utility shall be limited to paying for or reimbursing the utility for extraordinary expenses of the utility or for necessary capital projects, unless otherwise permitted by the Commission. Extraordinary expenses are those resulting from events which are infrequent and unusual in nature, and unrelated to the utilities' routine service or business activities.

Limestone has financial security escrow accounts from the acquisition of the Cartwright Creek systems. Limestone assumed the obligation to maintain the financial security escrow account.³⁰⁴ Also, in its acquisition of the DSH system, Limestone agreed to maintain a similar, and separate,

³⁰⁰ *Id.*

³⁰¹ *Id.*

³⁰² *Direct Testimony of Clark Kaml* at 24:5-7.

³⁰³ *Id.* at 24:5-7 citing TENN. COMP. R. & REGS. 1220-04-13-.07(7) (Dec. 2018 Revised).

³⁰⁴ *Id.* at 24:5-7 citing Order Approving Settlement Agreement and Transfer of Systems and Granting Certificate of Convenience and Necessity, Exhibit 1, Part II. Settlement Terms, ¶ 4.i-ii, TPUC Docket No. 21-00053 (Jan. 24, 2022).

escrow account specific to DSH operations.³⁰⁵ Limestone noted that it also has open acquisition requests in which Limestone will have escrow accounts. These include IRM and the Cumberland Basin Wastewater Systems.³⁰⁶

In this rate case, Limestone is proposing to terminate or waive escrow account payments from customers for Cartwright Creek and DSH, and to close the existing escrow accounts.³⁰⁷ Limestone claims to be well-capitalized and that CSWR has invested close to \$11,000,000 in Limestone's Tennessee operations.³⁰⁸ Further, Limestone stated the improvements at Cartwright Creek and DSH were funded by investor contributions, without accessing escrow accounts.³⁰⁹

Limestone claims Commission Rule 1220-04-13.07 addresses financial security of public wastewater utilities holding or seeking a CCN. Specifically, "the Commission may review the financial condition of any public wastewater utility at any time to determine whether a reserve/escrow account balance is adequate, or an account should be established." According to Limestone, the escrow is designed to ensure that capital is available to reimburse "the utility for extraordinary expenses of the utility or for necessary capital projects." Prior to reimbursement, however, the "utility must first receive authorization from the Commission."

When Limestone acquired Cartwright Creek systems, Limestone also assumed obligation to maintain a financial security escrow account for the system. The approved settlement in TPUC Docket No. 21-00053 provided for the following conditions:

- i. At closing, Cartwright Creek will transfer to Limestone all fees held in escrow for Commission-authorized tap fees and the Capital Improvement Surcharge ("CIS").
- ii. At closing, Limestone will assume Cartwright Creek's obligation to collect tap fees and the CIS, deposit those funds in Commission

³⁰⁵ *Id.* at 24:17-19 citing Order Approving Settlement Agreement and Transfer of Systems and Granting Certificate of Convenience and Necessity, p. 7, #12, TPUC Docket No. 23-00016 (Dec. 26, 2023).

³⁰⁶ *Direct Testimony of Clark Kaml* at 24:1-3 citing *Direct Testimony of Brent Thies* at 32:4-24.

³⁰⁷ *Id.* at 24:1-3 citing *Direct Testimony of Brent Thies* at 32:22-33:2.

³⁰⁸ *Id.* at 24:1-3 citing *Direct Testimony of Brent Thies* at 37:16-19.

³⁰⁹ *Id.* at 24:1-3 citing *Direct Testimony of Brent Thies* at 37:20 – 38:2.

- approved escrow accounts, and obtain Commission pre-approval for disbursements from those accounts.
- iii. Limestone will report quarterly, in the manner prescribed in the Commission's 08/25/20 Order in Docket No. 19-00097, regarding quarter-end balances in each escrow account and any disbursements made during the reporting quarter.³¹⁰

Additionally, Limestone is aware that they filed an application to acquire the assets of IRM Utility, Inc. and the current IRM tariff provides for a monthly residential charge of \$10.13 to be placed in the Company's escrow account. Similarly, Limestone has filed an application to acquire the wastewater assets of Cumberland Basin Wastewater Systems. The current Cumberland Basin tariff for the Bluffs at Cumberland Cove provides for a monthly residential charge of \$7.03 to be placed into an escrow account and a monthly residential charge for Genesis Village Estates of \$14.94 to be placed into an escrow account.³¹¹

The current balance for the financial security escrow accounts maintained by Limestone as of May 31, 2024, for Cartwright Creek is \$603,003. The balance in the DSH escrow as of May 31, 2024, is \$50,853 for a combined total amount of \$653,857 being held in escrow accounts.

The Consumer Advocate has determined the impact of terminating these monthly escrow charges would result in a reduction of DSH monthly bills by \$10.24 and Cartwright Creek would see a reduction in the amounts on customer bills equal to the Tap Fees and the Capital Improvement Surcharge.³¹²

Limestone has posited that the most expedient and reasonable solution would be to close the escrow account with the funds retained by Limestone.³¹³ Limestone would treat the funds as CIAC and use it to offset rate base.

³¹⁰ *Direct Testimony of Brent Thies* at 30:20-24-31:1-27.

³¹¹ *Id.* at 32:1-23-33 1-2.

³¹² *Direct Testimony of Clark Kaml* at 26:21-23.

³¹³ *Id.* at 27:3-5 citing *Direct Testimony of Brent Thies* at 39:7-11.

The Consumer Advocate does not believe this is an appropriate solution. The escrow funds should be used for projects in the service areas where the funds were collected. This proposal is based on fundamental fairness, using the funds to provide improvements for the customers from whom they were collected and used in the area from which they were obtained.³¹⁴ Since Limestone does not plan to return the funds to all the customers who made the contributions, at the very least, the funds should be returned to the service areas and purposes for which it was collected and be used for capital projects, with the funds appropriately reflected as CIAC in the appropriate service area.³¹⁵

In the event the Commission allows Limestone to retain the funds, rate base should be reduced by the amounts in the escrow, totaling \$653,857. The Revenue Requirement should be decreased to reflect the reduction in the cost of capital and decreased by an additional \$32,692 in depreciation credit of the CIAC.³¹⁶

Additionally, if the Commission allows for the termination of escrow payments, the termination of escrow payments should not apply to new acquisitions. The individual acquisitions should be reviewed independently since each system is different. Just as rates, rate base, and other characteristics of a system are unique, the purpose for which, and method by which, an escrow is collected may vary.³¹⁷

XI. COST OF CAPITAL AND RATE OF RETURN

A. Recommendation for Cost Of Capital And Rate Of Return

The next general area of contention is Limestone's cost of capital and the overall Rate of Return ("ROR") that the Company should be allowed to earn. Included within this section is a

³¹⁴ *Direct Testimony of Clark Kaml at 27:8-14.*

³¹⁵ *Id.*

³¹⁶ *Id.*

³¹⁷ *Id. at 28:8-13.*

discussion of the appropriate capital structure for Limestone, Cost of Equity (“COE”), and the Company’s allowable Return on Equity (“ROE”).

As a regulated monopoly, Limestone’s authorized ROE should be consistent with the legal standards set by the United States Supreme Court for a fair rate of return in that (1) “...the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks”³¹⁸ and (2) “sufficient to . . . support its credit and . . . raise the money necessary for the proper discharge of its public duties.”³¹⁹ Limestone’s expert witness on cost of capital issues, Dylan D’Ascendis, calls for the Company to be allowed an ROE of 11.90%, including a 1.50% upward adjustment to reflect the Company’s business risk.³²⁰ Mr. D’Ascendis’ proposed capital structure is 57% common equity and 43% debt.³²¹

On the other hand, Aaron Rothschild, the expert witness testifying on behalf of the Consumer Advocate recommends Limestone should receive an authorized ROE of 8.28% and this rate should be applied to a capital structure of 51.82% common equity, 48.18% debt.³²²

1. The Commission Should Reject Limestone’s Requested Capital Structure Because its Common Equity Ratio Is Significantly Higher Than Both the Common Equity Ratio Used by Other Utility Companies in the Country And the Capital Structure in Mr. D’Ascendis’ Proxy Group

Limestone has requested a capital structure of 57% common equity, and 43% debt. Mr. D’Ascendis bases these figures on his creation of two proxy groups which he has named as follows: (1) the Utility Proxy Group (consisting of five companies); and (2) the U.S. Water Universe (consisting of nine companies).³²³ The U.S. Water Universe has an equity percentage range from

³¹⁸ *Fed. Power Comm’n v. Hope Nat. Gas Co.*, 320 U.S. 59, at 603 (1944).

³¹⁹ *Bluefield Water Works & Improvement Co. v. Pub. Serv. Comm’n of the State of W. Va.*, 262 U.S. 679, at 692-693 (1923).

³²⁰ *Direct Testimony of Dylan D’Ascendis* at 5 (Table 2).

³²¹ *Id.* at 19:7-8.

³²² *Direct Testimony of Aaron Rothschild* at 10:9-17.

³²³ *Direct Testimony of Dylan D’Ascendis* at 16:3-5 and 17:11-12.

31.67% to 57.59% in 2023.³²⁴ Thus, Mr. D'Ascendis' equity figure is at the high end of his range. Furthermore, it is a figure he chose with little explanation other than that Limestone is a "risky" company:

I chose the higher-than average hypothetical capital structure for Limestone Water due to its extraordinary operating risks as detailed by Company Witness Michael Duncan.³²⁵

The Consumer Advocate, on the other hand, proposes using a capital structure consisting of 51.82% equity and 48.18% debt, based on the average common equity ratios of the companies in Rothschild's proxy group which consists of other water utilities in the country.³²⁶ Using the average capital structure of the proxy group is consistent with the Commission's duty to set reasonable rates because otherwise using a common equity ratio higher than other companies creates unreasonably higher rates.

Mr. Rothschild's recommendations, including his capital structure recommendation, result in an overall rate of return of 7.36% as shown in Table 3 on page 15 of his *Direct Testimony*. Mr. D'Ascendis' recommendations result in an overall rate of return of 9.64%.³²⁷ Capital structure has a major impact on revenue requirement. Therefore, if TPUC adopts an equity component of the capital structure ratio that is higher than Mr. Rothschild's recommendation, there should be a corresponding reduction to ROE.

If Mr. D'Ascendis' capital structure recommendations are adopted it is important to make an adjustment to the overall ROR to account for the financial risk difference between his capital structure recommendation and that of the companies in the RFC Water Proxy Group used by Mr. Rothschild which have a significantly lower average common equity ratio (51.8%) than the

³²⁴ *Rebuttal Testimony of Dylan D'Ascendis* at 19:17-19.

³²⁵ *Direct Testimony of Dylan D'Ascendis* at 20:2-4.

³²⁶ *Direct Testimony of Aaron Rothschild* at 73:7-11 (referencing Exhibit ALR-7, page 5).

³²⁷ *Direct Testimony of Dylan D'Ascendis* at 3:12 (Table 1).

common equity ratios recommended by Mr. D'Ascendis.³²⁸ A higher common equity ratio means less debt, a lower chance of financial stress (financial risk), and therefore a lower COE. On the other hand, a lower common equity ratio means more debt, a higher chance of financial stress (financial risk), and therefore a higher COE. Based on a regression analysis of dozens of utility companies, Mr. Rothschild found a 0.04% reduction in the cost of equity results for every 1% increase in the common equity ratio.³²⁹ Therefore, if the Commission authorizes a capital structure with a higher common equity ratio for a specific applicant, including Limestone, then the authorized ROE for that applicant should be reduced by 0.04% for every 1% its authorized common equity ratio exceeds that of the proxy group.³³⁰ In this case, the difference between Mr. D'Ascendis' capital structure recommendation (57%) and Mr. Rothschild's capital structure recommendation (51.82%) would lead to a 21 basis point reduction in the appropriate authorized ROE (from 8.04% to 7.83%).³³¹

With regard to the cost of debt, Mr. Rothschild recommends adopting Limestone's requested cost of long-term debt of 6.64% and cost of short-term debt of 0.00%.³³²

Finally, it should be noted that certain problems can arise when a utility raises debt from a holding company or a related entity. Thus, if a utility raises debt at the holding company level and then injects that capital as equity into the regulated subsidiary, the reported common equity ratio at the subsidiary level could be artificially inflated. This type of capital structure manipulation could mislead regulators into approving an unnecessarily high common equity ratio, which results in

³²⁸ *Direct Testimony of Aaron Rothschild* at 74:14-18.

³²⁹ *Id.* at 74:21-23.

³³⁰ *Id.* at 74:23 – 75:1-3.

³³¹ This calculation is made as follows: $0.04 \times (57\% - 51.82\%) = .04 \times 5.18\% = 0.21\%$ (i.e., 21 basis points).

³³² *Direct Testimony of Aaron Rothschild* at 75:5-6.

higher rates for customers. There is no evidence in the record that Mr. D'Ascendis investigated whether Limestone has engaged in this type of debt reallocation.

2. The Consumer Advocate's Recommendation on the Cost Of Equity More Closely Reflects its Actual Cost And Is More Reasonable in Balancing the Interests Between Consumers And the Company

Mr. Rothschild's approach for calculating a cost of equity differs fundamentally from that of Mr. D'Ascendis in several specific ways: (a) Reliance on Market Data; (b) Growth Rate Assumptions in DCF Analysis; (c) the Application of the Capital Asset Pricing Model ("CAPM"); (d) the Use of the Risk Premium Model ("RPM"); (e) Avoidance of Business Risk Adjustments; and (f) Non-Price Regulated Proxy Group COE Analysis.³³³

a. Reliance on Market Data: Mr. D'Ascendis Failed To Rely Sufficiently on Market-Based Data

Mr. Rothschild focuses on using market data (e.g., stock prices, bond yields, stock option prices) to measure investors' expectations as much as possible. Mr. D'Ascendis, however, relies extensively on biased analyst forecasts even when it is possible to measure investors' equity return expectations using market data (such as stock and option prices).³³⁴ Market data is more reliable than analyst forecasts.

i. Superiority Of Market-Based Data Over Analyst-Based Data

Market data aggregates the expectations of a diverse group of participants who utilize a range of quantitative models and economic indicators (including analysts' forecasts). This distributed intelligence is inherently more robust than an individual or small group of analysts, regardless of expertise. Because market data includes thousands of participants, it is better equipped

³³³ Direct Testimony of Aaron Rothschild at 76-79.

³³⁴ For example, the market risk premium of Mr. D'Ascendis' CAPM analysis includes a 14.86% total return on the S&P 500 based on analyst forecasts (Bloomberg, Value Line, and S&P Capital IQ) instead of investor expectations as revealed by capital market prices. Direct Testimony of Dylan D'Ascendis at Exhibit DWD-6, page 2.

to capture the complex market interactions and nonlinear dynamics. Mr. Rothschild's use of market data more accurately captures investor expectations in real-time, providing a market-based COE that reflects current capital conditions.

Mr. D'Ascendis, however, utilizes more analyst-driven data and interest rate forecasts, which can diverge from the immediate expectations investors demonstrate through market behavior.

ii. Problems with Relying on Other States' Authorized Rates Instead Of Market-Based Data

Mr. D'Ascendis relies on authorized cost of equity and authorized rates of return from other states in an attempt to justify his own calculations. Authorized rates from other states, however, are not market-based data and are not useful in calculating the cost of equity.

Past authorized ROEs are applied to rate base, which is nearly identical to book value. In other words, they are accounting returns. In this case, we are not trying to determine what investors expect the return on book value to be. Rather, we are trying to determine the return investors expect/require on the market price of stock.

As discussed in Appendix A to the *Direct Testimony of Aaron Rothschild*, when the market to book ratio of water utility company is significantly above one, as it is now,³³⁵ it indicates that their COE is lower than their authorized ROE.³³⁶

In his 1970 book *The Economics of Regulation: Principles and Institutions*, regulatory economist Alfred Kahn wrote on why the cost of equity is lower than authorized returns when market to book ratios are significantly above one, saying:

[T]he sharp appreciation in the prices of public utility stocks, to one and half and then two times their book value during this period, reflected ... a growing recognition that the companies in question were in fact being permitted to

³³⁵ *Direct Testimony of Aaron Rothschild*, Exhibit ALR-5, page 1. The market to book ratios of the companies in Rothschild's proxy group averaged 2.40 over the year ending November 30, 2024.

³³⁶ An authorized ROE is applied to rate base, which is nearly identical to the return on the book value of equity; therefore, authorized ROEs are nearly identical to return on book equity.

earn considerably more than their cost of capital. ... The source of the discrepancy between market and book value has been that commissions have been allowing r 's [returns on equity] in excess of k [market cost of equity]; if instead they had set r equal to k , or proceeded at some point to do so ... the discrepancy between market and book value ... would have disappeared, or would never have arisen.³³⁷

A utility company's COE should not be based on authorized ROEs, which are accounting returns. The COE is set based on what investors in the market expect for a given risk profile. In the case of a utility stock, an increasing market value results in a lower return on market for the same expected return on book, all else equal.

In the present case, Mr. D'Ascendis attempted to use authorized rates from other states to argue that Mr. Rothschild's 8.28% ROE is too low. In particular, Mr. D'Ascendis stated in his Rebuttal Testimony that "Mr. Rothschild's recommended ROE of 8.04%, if authorized by the Commission, would be the lowest non-punitive ROE set from 2010 to the present."³³⁸

However, Mr. D'Ascendis' attempt to rely on authorized returns from other states such as South Carolina backfired because the Supreme Court of South Carolina fully justified a lower ROE than what Mr. D'Ascendis thought reasonable. In a case involving a small water company, in which both Mr. Rothschild and Mr. D'Ascendis testified, the South Carolina Supreme Court said as follows in its decision in an appeal from a Public Service Commission order:

"As a result, because there is a basis on which a reasonable person could find a **7.46% ROE** appropriate, the PSC's decision is supported by substantial evidence in the record, and we therefore affirm."³³⁹

* * *

"We find there is substantial evidence in the record supporting the PSC's decision. Specifically, the PSC found Rothschild's testimony to be the most

³³⁷ Alfred Kahn, *The Economics of Regulation: Principles and Institutions*, Mass. Inst. Tech. at 48 (fn. 69), 50 (1970).

³³⁸ *Rebuttal Testimony of Dylan D'Ascendis* at 5:7-8.

³³⁹ *Id.* at Workpaper 01, page 10 of 21.

credible.”³⁴⁰

In its decision, the South Carolina Supreme Court also criticized Mr. D’Ascendis’ methodologies in determining his ROE:

There is ample basis supporting the rejection of D’Ascendis’s testimony. For example, after summarizing Parcell’s and Rothschild’s testimony in which they thoroughly discredited D’Ascendis, the PSC found D’Ascendis’s calculations lacked “analytical transparency” and “statistical coherence.” Having reviewed the record, the evidence firmly supports the PSC’s extensive criticism of D’Ascendis’s testimony, and we thus do not discuss the specifics of that testimony any further.³⁴¹

In the present case, Mr. D’Ascendis did not claim that he had discarded any of the methodologies the South Carolina Supreme Court had found so objectionable.

iii. Value Of Stock Options Data As A Market-Based Measure Of Market Volatility

Volatility, uncertainty, and risk are synonymous. Mr. Rothschild testified that there are two primary types of volatility: “realized volatility” and “implied volatility.”³⁴² The former is based on historical returns, which may or may not represent future volatility. Implied volatility, on the other hand, is calculated from options data, which indicates investors’ future expectations for volatility.³⁴³ Mr. Rothschild used stock option data to measure risk for Limestone. Mr. D’Ascendis, however, did not use stock option data even though he used sources that referred to stock options.³⁴⁴

iv. The Market-Based Reality Check on Investor Expectations

Neither Mr. Rothschild nor Mr. D’Ascendis based their ROE wholly on investor expectations. Mr. Rothschild, however, did use the investor expectations as measured by major

³⁴⁰ *Id.* at Workpaper 01, page 8 of 21.

³⁴¹ *Rebuttal Testimony of Dylan D’Ascendis* at Workpaper 01, page 7 of 21, footnote 5.

³⁴² *Direct Testimony of Aaron Rothschild* at 34:8-9.

³⁴³ *Id.* at 34:10-11.

³⁴⁴ *Hearing Transcript*, TPUC Docket No. 24-00044, Vol II, February 19, 2025 CONFIDENTIAL at 238:5-

financial institutions as a kind of reality check on how his proposed ROE of 8.28% compared. Mr. D'Ascendis, on the other hand, did not acknowledge the value of such a reality check.³⁴⁵

As shown in Table 4 on page 17 of Mr. Rothschild's *Direct Testimony* (reprinted below), major financial institutions are informing their clients to expect returns on the overall market (S&P 500) of 6.2% to 7.9%. Duff & Phelps/Kroll, determined that the cost of equity for the overall market is 8.5%.³⁴⁶ As stated above, Limestone's authorized ROE should be based on investors' expectations as indicated by capital market data, not the opinions of small groups of people including those of major financial institutions. However, Mr. Rothschild chose to include the equity return expectations of major financial institutions as a kind of reality check and to encourage the Commission to consider why Mr. D'Ascendis' 11.90% ROE is so significantly higher than financial mainstream.

TABLE 4: U.S. EQUITY RETURN EXPECTATIONS AMONG MAJOR FINANCIAL INSTITUTIONS	
Duff & Phelps / Kroll (June 2024) [1]	8.5%
Horizon Actuarial Services, LLC Survey - 20 Year Horizon (August 2024) [2]	
U.S. Equity - Large Cap (5.3-10.2%, 50% Percentile - 6.7%)	6.7%
U.S. Equity - Small / Mid Cap (5.1-10.9%, 50% Percentile - 7.3%)	7.3%
J.P. Morgan Asset Management - Equity Long-Term Returns (2025) [3]	6.7%
Charles Schwab - 10-year U.S. Large Cap Returns (January 2024) [4]	6.2%

Sources:

[1] Kroll Recommended U.S. ERP and Corresponding RFR to be Used in Computing Cost of Capital: January 2008 - Present,

<https://www.kroll.com/en/insights/publications/cost-of-capital/recommended-us-equity-risk-premium-and-corresponding-risk-free-rates>

Note: Duff & Phelps acquired Kroll in 2021 and rebranded itself as Kroll.

[2] Horizon Actuarial Services, LLC, Survey of Capital Market Assumptions Survey, August 2024, page 19.

Survey participants include: Bank of New York Mellon, BlackRock, Goldman Sachs Asset Management, J.P. Morgan Asset Management, Merrill, Morgan Stanley Wealth Management, Royal Bank of Canada, UBS.

[3] J.P. Morgan Asset Management - 2025 Long-Term Capital Market Assumptions, 2024, page 30.

[4] Schwab's 2024 Long-Term Capital Market Expectations, January 2, 2024.

<https://www.schwab.com/learn/story/schwabs-long-term-capital-market-expectations>

³⁴⁵ Hearing Transcript, TPUC Docket No. 24-00044, Vol II, February 19, 2025 CONFIDENTIAL at 224:7-19.

³⁴⁶ It should be noted that Mr. D'Ascendis uses data from Kroll as part of the market risk premium portion of his CAPM analysis; see e.g., D'Ascendis *Direct* at 49, footnote 44 and Exhibit DWD-5, page 6 of 9 which shows a "Kroll Equity Risk Premium"; and D'Ascendis *Rebuttal* at 13:4-5.

The equity return expectations, shown in Table 4 above, are for the overall stock market (e.g., US Large Cap, S&P 500³⁴⁷), which should be higher than the return expectations for utility stocks because regulated monopoly utilities are lower risk than most, if not all, unregulated companies in the S&P 500, like Tesla and Amazon. Therefore, Mr. D'Ascendis' 11.90% ROE recommendation is even more out of line with the financial mainstream than it appears from the numbers presented in this table.

Even Mr. Rothschild's cost of equity recommendation of 8.04% (6.65% to 8.04%) for Limestone is in the middle to upper part of the range of these expectations, a fact which should give the Commission more confidence that if they adopt his recommendation Limestone will be able to raise the capital it needs to provide safe and reliable service.

b. Growth Rate Assumptions in DCF Analysis: Mr. D'Ascendis' Assumptions Are Flawed

The growth rate component of Mr. D'Ascendis' DCF model is based on relatively short-term analyst growth rates without adjusting for sustainable, long-term growth.³⁴⁸ This can inflate COE estimates because short-term growth is not a reliable measure over the long-term, particularly in regulated utilities with modest growth expectations. Rothschild's DCF analysis counters this by using sustainable growth rates, aligning growth assumptions with longer-term investor expectations. This method avoids overreliance on optimistic analyst projections that may not reflect future, consistent cash flows. Using a sustainable growth approach in the DCF model ensures that growth rates are realistic and more in line with utility sector norms. This stabilizes COE estimates

³⁴⁷ The S&P 500 is a stock market index that includes 500 of the largest U.S. companies, including 11 sectors to show the health of the U.S. stock market and broader economy. The Dow Jones Industrial Average, 30 of the largest U.S. companies, is another commonly used measure of equity markets in general.

³⁴⁸ *Direct Testimony of Dylan D'Ascendis* at Exhibit DWD-4, pg. 1.

and reduces overstatement, providing a more accurate long-term indicator of Limestone's financial needs.

c. The Application Of the Capital Asset Pricing Model: Mr. D'Ascendis' Use Of CAPM Is inflated

Mr. D'Ascendis' CAPM incorporates an inflated market risk premium (7.17% - 10.55%).³⁴⁹ The risk premium he uses is higher than what equity investors currently expect to earn when investing in equities, leading to an overstated COE.³⁵⁰ The risk premium portion of Rothschild's CAPM analysis (3.34% to 3.96%)³⁵¹ is based on a direct measure of investors' return expectations based on stock option prices. Mr. Rothschild calculates risk premium components based on both spot and historical averages to provide a more stable COE that accounts for changing capital market conditions without being overly influenced by short-term capital market turmoil. Incorporating both short-term and long-term risk-free rates in the CAPM smooths out fluctuations from daily market shifts, creating a more comprehensive view of investor expectations. Mr. Rothschild's balanced market risk premium also reduces the influence of historical extremes, delivering a COE grounded in both recent and past market conditions. Mr. D'Ascendis' approach significantly relies on the personal opinions of equity analysts in both his CAPM and DCF analysis instead of the supply and demand of stocks and bonds as indicated by market data. Calculating the cost of equity should be an interpretive approach (*e.g.*, using market data to measure investors' expectations as Mr. D'Ascendis did in some parts of his testimony) rather than a speculative one (*e.g.*, using interest rate forecasts instead of investors' expectations as revealed in the market yield).

³⁴⁹ *Id.* at 42 (Table 9).

³⁵⁰ The equity risk premium is related to the overall market (*e.g.*, the companies in the S&P 500). In order to equate this to the cost of equity for a utility company, it is required to make additional calculations.

³⁵¹ *Direct Testimony of Aaron Rothschild*, Exhibit ALR-6, page 4 and Exhibit ALR-6, page 5.

d. The Use Of the Risk Premium Model: Mr. D'Ascendis' Model Improperly Relies on Historical Equity Returns

Mr. D'Ascendis' Risk Premium Model or RPM produces inflated results for a number of reasons. One reason for the inflated results is that the historical market risk premium portion of Mr. D'Ascendis' RPM is based on historical equity return measures (11.91%)³⁵² that are likely above investors' current expectations. Another reason for Mr. D'Ascendis' inflated RPM results is that the projected equity risk premium portion of his RPM is based on unrealistically high measures of equity return expectations (12.27%)³⁵³ because it is highly influenced by upwardly biased analyst projections.

His use of Kroll's historical equity risk premium data in his CAPM analysis is flawed because it fails to account for forward-looking investor expectations and relies on an arbitrary one-year timeframe. Kroll itself (a source cited by Mr. D'Ascendis)³⁵⁴ acknowledges that past equity returns may not be sustainable and calculates a supply-side equity risk premium to reflect the likelihood that future equity returns could be lower than historical averages. Mr. D'Ascendis, however, does not adjust for this forward-looking consideration, inflating his equity risk premium by assuming that past returns are indicative of future expectations.³⁵⁵

e. Avoidance Of Business Risk Adjustments: Mr. D'Ascendis' 1.5% Business Risk Adjustment Is Unsupported

Mr. D'Ascendis makes an upward adjustment of 150 basis points or 1.50% to his indicated range of ROEs due to, what he calls, the "extraordinary operating risks" because of its small size and acquisition of troubled water and wastewater systems.³⁵⁶ Mr. D'Ascendis' upward adjustment

³⁵² *Direct Testimony of Dylan D'Ascendis* at 33:9-11.

³⁵³ *Direct Testimony of Dylan D'Ascendis* at Exhibit DWD-5, page 6.

³⁵⁴ It should be noted that Mr. D'Ascendis uses data from Kroll as part of the market risk premium portion of his CAPM analysis; *see e.g.*, D'Ascendis *Direct* at 49, footnote 44 and Exhibit DWD-5, page 6 of 9 which shows a "Kroll Equity Risk Premium"; and D'Ascendis *Rebuttal* at 13:4-5.

³⁵⁵ *Direct Testimony of Aaron Rothschild* at 89:5-15.

³⁵⁶ *Direct Testimony of Dylan D'Ascendis* at 47:8-10.

of 1.50% is not justified because: (1) research shows that investors do not demand a return premium to invest in small companies; and (2) acquiring troubled water systems represents a significant growth opportunity for Limestone.

Regarding Mr. D'Ascendis' claim that a size premium justifies a 150 basis point (1.5%) increase in Limestone's authorized ROE, contemporary financial research, including studies from AQR Capital Management and Yale University, has cast doubt on the persistence of a size premium.³⁵⁷ These studies show that the effect largely disappeared after its discovery, and earlier research suffered from methodological flaws such as delisting bias, which artificially inflated small-cap returns.

Additionally, Professor Aswath Damodaran has demonstrated that the size effect is not independent of other factors, such as liquidity and risk exposure, and that controlling for these variables often eliminates the premium entirely.³⁵⁸ This aligns with the 2021 SBBI Yearbook, the same source Mr. D'Ascendis relies on for his market risk premium in the CAPM model, which explicitly acknowledges the long-standing controversy surrounding the size premium:

The size effect is not without controversy, nor is this controversy something new. Traditionally, small companies are believed to have greater required rates of return than large companies because smaller companies are inherently riskier. It is not clear, however, whether this is due to size itself, or to other factors closely related to or correlated with size.³⁵⁹

This statement from SBBI, a prominent source relied on by Mr. D'Ascendis, undermines his justification for a size premium by acknowledging that any observed small-cap premium may be driven by other risk factors, not size itself. Given these findings, Mr. D'Ascendis' 1.5% size

³⁵⁷ *Direct Testimony of Aaron Rothschild* at 93:9-19.

³⁵⁸ *Direct Testimony of Aaron Rothschild* at 93:11-19; and footnote 98 (Aswath Damodaran, New York University, Stern School of Business, *Equity Risk Premiums (ERP): Determinants, Estimation, and Implications – the 2022 Edition*, pp. 53-54 (Updated March 23, 2022) at <https://pages.stern.nyu.edu/~adamodar/pdfiles/papers/ERP2022Formatted.pdf>).

³⁵⁹ *Id.* at 92:15-22.

premium is highly questionable and likely inflates his cost of equity estimate beyond what is justified by current market conditions.

During cross-examination at the hearing, Mr. D'Ascendis acknowledged that Limestone Water voluntarily acquired the water systems in its portfolio and had every opportunity to conduct due diligence before purchasing them. When asked whether any regulatory agency, such as a Public Service Commission, had ordered Limestone to acquire these systems, Mr. D'Ascendis responded, "Not to my knowledge."³⁶⁰

If Limestone positions itself as an expert in rehabilitating troubled water systems, as it claims, then it should also possess the necessary expertise to thoroughly evaluate the condition of a system before acquisition and negotiate appropriate terms that reflect any risks. It is therefore problematic for Limestone to request a risk premium tied to challenges that stem from its own voluntary business decisions. By asking for a higher return due to risks it had the ability to assess and mitigate—through better due diligence, improved financial planning, or stronger negotiations—Limestone is effectively seeking compensation for risks within its own control.

This raises concerns of a moral hazard, where a utility knowingly takes on high-risk acquisitions under the expectation that regulators will later grant a financial cushion through an inflated return on equity. Granting such a premium would incentivize utilities to take on additional risk unnecessarily, knowing they can shift the financial burden onto ratepayers rather than being held accountable for their own investment decisions.

Mr. D'Ascendis' reliance on a size premium is contradicted by contemporary financial research. As Mr. Rothschild noted in his testimony, a 2018 study by scholars at AQR Capital

³⁶⁰ *Hearing Transcript*, TPUC Docket No. 24-00044, Vol II, February 19, 2025 CONFIDENTIAL at 247-249 ("Not to my knowledge" at 248:6).

Management and Yale University found that “the size effect diminished shortly after its discovery and publication,” and that earlier studies suffered from methodological flaws, including a “delisting bias” that made smaller stocks appear to have higher returns than they actually achieved.³⁶¹

f. Non-Price Regulated Proxy Group COE Analysis: Mr. D’Ascendis’ Non-Price Regulated Proxy Group Is Too Different From Limestone To Be Valid

The companies in Mr. D’Ascendis’ Non-Price Regulated Proxy Group are not comparable in risk to Limestone because of significant operational characteristics, ongoing legal exposure, radically different capital structure ratios, and differing regulatory or political risks. Consistent with the *Hope/Bluefield* standards and Commission precedent, the results of Limestone’s COE analysis based on non-regulated utilities should be disregarded because the results do not represent an accurate measure of Limestone’s COE.

Mr. D’Ascendis’ non-regulated proxy group includes such companies as Pfizer and UPS. Non-regulated companies have a different business model and are exposed to different risks. For example, Pfizer is a pharmaceutical company that, unlike Limestone, spends enormous sums on research and development, faces intense competition, and operates in markets without an exclusive territory. As Mr. Rothschild noted in his testimony, “Pharmaceutical companies typically have high research and development costs and face regulatory risks distinct from those encountered by utilities (e.g., FDA approval processes), and their earnings are also subject to market demand for specific drugs, rather than the stable demand typical for utilities.”³⁶² Furthermore, Pfizer is in competition with other drug companies, while Limestone operates in an exclusive territory.

Similarly, UPS, another company in Mr. D’Ascendis’ non-regulated proxy group, also lacks the exclusive territory that Limestone benefits from. UPS faces significant competitive pressures

³⁶¹ Direct Testimony of Aaron Rothschild at 93:9-19.

³⁶² Direct Testimony of Aaron Rothschild at 95:11-14.

from FedEx, Amazon, and other shipping providers. Unlike Limestone, which operates as a regulated monopoly with an exclusive service territory, these companies must constantly innovate and adjust pricing in a competitive environment.³⁶³ These fundamental differences in business model and risk profile render the non-price regulated proxy group unsuitable for determining Limestone's cost of equity. As a regulated water utility, Limestone can file for rate increases to recover costs, a protection that companies in competitive markets do not enjoy.

For the foregoing reasons, the Commission should reject Mr. D'Ascendis' proposed ROE of 11.90% as well as his capital structure of 57% equity and 43% debt.

The Commission should adopt Mr. Rothschild's ROE of 8.28% and his capital structure of 51.82% equity and 48.18% debt.

XII. RATE DESIGN

A. The Company's Consolidated Rate Design Proposal Is Unreasonable And Inappropriate

The Company proposes to simplify and consolidate its rates. There are several important principles that regulators and policymakers consider when developing appropriate rate designs for water service. Cost causation is an important foundation of rate design. There are other ratemaking principles, including simplicity, feasibility, and affordability.

As explained by Company Witnesses Mike Duncan and Aaron Silas, Limestone is proposing consolidated statewide rates across its entire Tennessee footprint.³⁶⁴ Limestone argues that it has recognized that single tariff pricing and the consolidation of rates encourages the consolidation of small water and wastewater systems into larger utilities.³⁶⁵

While Limestone claims that consolidated rates of those in the more efficient systems will

³⁶³ Hearing Transcript, TPUC Docket No. 24-00044, Vol II, February 19, 2025 CONFIDENTIAL at 255:12-21.

³⁶⁴ *Direct Testimony of Mike Duncan* at 15-18; and *Direct Testimony of Aaron Silas*.

³⁶⁵ *Direct Testimony of Mike Duncan* at 16.

support the cost of improvements to those least efficient in the short-term, in the long-term this principle is not true.³⁶⁶ Limestone states that eventually all of the distribution and treatment systems will require major repairs and replacements, while some of those systems currently require more urgent investments for upgrades and improvements.³⁶⁷ Essentially, there will be benefits to all systems over time because the systems will all need major repairs and replacements.

Limestone also claimed that the average cost pricing and state-wide rates are the rule rather than the exception in utility pricing.³⁶⁸ Limestone also believes consolidated rates reflect common benefits to all of its Tennessee customers that are being served by Limestone and the services that are provided are done more cost-effectively by consolidating systems to realize economies of scale.

Limestone stated that consolidated rates provide a more gradual rate increase as compared to the huge rate increases that some systems may see under system-specific rates. In contrast, however, according to Limestone, a rate increase is tempered if such costs are allowed to be spread across all of Limestone's connections and this suggests that consolidation of rates across the board would be best for customers.³⁶⁹

The Consumer Advocate disagrees with this analysis. First, average cost pricing and state-wide rates are not the rule, but rather the exception in utility pricing. While "average cost pricing" (setting prices based on the average cost of production) and "state-wide rates" (uniform pricing across a whole state) are sometimes used in utility pricing, they are not the most common approach, and most utility companies utilize more nuanced pricing strategies based on factors like location, usage, and time of day, resulting in varied rates across different regions within a state. Additionally, most state statutes, including Tennessee, provide that utility rates must be "just and reasonable" and

³⁶⁶ *Direct Testimony of Mike Duncan* at 17.

³⁶⁷ *Id.*

³⁶⁸ *Id.* at 18.

³⁶⁹ *Id.*

not unduly discriminatory. Most importantly, customer protection of utility rates against the exercise of utility monopoly power is a core principle of ratemaking.

Limestone has not provided any evidence that services provided are more cost-effective by consolidating systems and rates. It is not readily apparent that Limestone will realize any economies of scale for services provided by CSWR. First, economies of scale can be achieved regardless of the rate structure implemented by Limestone. Also, as to major repairs and improvements to the various Limestone systems, these are done using local third-party contractors in Tennessee and not CSWR contractors, and the issue of economies of scale for engineering or construction services is inapplicable. There is no evidence in this Docket to support Limestone's argument concerning the economies of scale argument. The main benefit of consolidated rates is that as Limestone continues to acquire additional systems, it could result in the overall operation efficiency of Limestone, but primarily it will simplify the ratemaking process and expedite the process of the acquisition for Limestone. Ultimately, from an administrative perspective, it will be easier for Limestone to manage its systems in Tennessee. There are no benefits to consolidating rates for Limestone customers.

Additionally, Limestone states that rates have already been consolidated within the Limestone system. Limestone references the Cartwright Creek system which consists of four wastewater systems, of which the rates for three of the systems (Arrington Retreat, Hideaway, and Hardeman Springs) were consolidated to a flat monthly rate of \$55.25.³⁷⁰ Limestone fails to mention that when these systems were acquired by Limestone the rates had already been consolidated and these systems are geographically contiguous to one another and not spread across different parts of Tennessee.

Limestone claimed that in other states where CSWR affiliates are operating, such as

³⁷⁰

Id.

Louisiana, Mississippi, Texas, Missouri and Kentucky, rates have been consolidated.³⁷¹ However, Limestone fails to mention that in Tennessee, if rates are consolidated, the monthly rate for customers would be astronomical. In some cases, the rate increase for some ratepayers would be upwards of a 400% increase.

According to Limestone, on the wastewater side, the revenue requirement would be collected through a single flat charge multiplied by the appropriate equivalent residential unit (“ERU”) multiplier. On the water side, Limestone is proposing to use a combination of a base rate and volumetric charge for usage to meet the revenue requirement for providing water service to customers. Limestone is proposing a pass-through charge for one service area (Aqua), which purchases wholesale water for distribution to individual connections.³⁷²

For water residential customers by rate zone, the proposed consolidated tariff will have the following average residential bill impact:

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³⁷¹

Id.

³⁷²

Direct Testimony of Aaron Silas at 18:6-8.

TABLE 6: Average Residential Bill Impact⁴⁷⁸

Water Systems Average Rate Increase			
System & Meter Size	Usage	Present Rate	Proposed Rate
Aqua Utilities 3/4" & 5/8"	Average Bill of 3,000 gallons usage	\$25.75	\$82.29
Aqua Utilities 1"	Average Bill of 3,750 gallons	\$28.04	\$102.86
Aqua Utilities 1.5"	Average Bill of 15,000 gallons	\$62.35	\$411.44
Aqua Utilities 2"	Average Bill of 24,000 gallons	\$89.80	\$647.75
Candlewood Lakes (unmetered)	n/a	\$40.00	\$67.50

Water Systems Average Rate Increase			
System & Customer Type	Usage	Present Rate	Proposed Rate
Aqua Utilities Residential	Average Bill of 3,000 gallons usage	\$25.75	\$86.64
Shiloh Falls Residential	Average Bill of 3,000 gallons	\$20.03	\$86.64
Grassland Residential	n/a	\$42.00	\$86.64
Arrington Retreat Residential	n/a	\$55.25	\$86.64
Hideaway Residential	n/a	\$55.25	\$86.64
Hardeman Residential	n/a	\$55.25	\$86.64
Chapel Woods Residential	n/a	\$29.00	\$86.64
Lakeside Estates Residential	n/a	\$43.37	\$86.64
Grassland Commercial	Base	\$37.00	\$86.64
	Average Bill of 3,000 gallons	\$63.25	\$86.64
Arrington Retreat Commercial	Base	\$37.00	\$86.64
	Average Bill of 3,000 gallons	\$63.25	\$86.64
Hideaway Commercial	Base	\$37.00	\$86.64
	Average Bill of 3,000 gallons	\$63.25	\$86.64
Hardeman Commercial	Base	\$37.00	\$86.64
	Average Bill of 3,000 gallons	\$63.25	\$86.64
Lakeside Estates Commercial	Base up to 300 gallons per day	\$68.37	\$86.64
	Average Bill of 450 gallons per day	\$98.37	\$86.64

However, if an acquisition adjustment is included, these amounts will be even higher for customers.³⁷³ The Consumer Advocate also argues that the Limestone's proposed consolidated tariff creates "winners and losers."³⁷⁴ Most significantly, rates will go up for some customers by much more than others in order to create this single consolidated billing rate for Limestone.³⁷⁵

Limestone has not provided any estimates of economies of scale that might result from

³⁷³ Pursuant to Commission Request at February 2025 Commission Hearing, Limestone Water Utility Operating Company LLC Updated Response to Commission January 31, 2025 Data Request No. 6 in Excel Format, TPUC Docket No. 24-00044, (Feb. 25, 2025).

³⁷⁴ Direct Testimony of William Novak at 20:13-15.

³⁷⁵ Id. at 20:13-16.

consolidating rates. Further, Limestone's proposal is inconsistent with any ratemaking practices including rate stability, rates based on cost causation, acceptability, and possibly fairness and views of undue discrimination. The proposed changes run into questions of public acceptability, and, absent a cost to serve analysis in each zone justifying the change, this may raise questions of fairness. A practice in ratemaking is to consider cost recovery from those that cause the cost to be incurred. For each rate class, Limestone has proposed to group all rate zones for a given rate class into one common classification, without demonstrating that the actual cost to serve each of the zones is similar to the cost of serving all other zones.³⁷⁶

The consolidated rates will impact customers because the proposed rates differ from existing rates for both meter size and volume of use. As a result, there is not a consistent impact across all customers and customer classes.³⁷⁷ Limestone indicates that water rates for average customers could increase between 68.7 percent to 621.32 percent.³⁷⁸ Wastewater customers could see rate changes anywhere from a reduction of 11.93 percent to an increase of 332.54 percent.³⁷⁹

While having tariffs for each service area that are similar can produce benefits in efficiencies and may reduce confusion, tariffs can still be similar without having the same rates. The Consumer Advocate supports the idea of using the same tariff format but not having the same rates.³⁸⁰ Limestone stated that it would be cost prohibitive to provide services to many small systems if rates are established on a system-by-system basis.

While there can be economies of scale in the provision of water service, the economies of scale could exist through the consolidation of companies, but not with consolidating rates.³⁸¹

³⁷⁶ *Direct Testimony of Clark Kaml* at 38:3-16.

³⁷⁷ *Id.* at 40:4-5.

³⁷⁸ Petitioner's Exhibit AJS-6 Rate Comparison

³⁷⁹ *Direct Testimony of Clark Kaml* at 41:1-2.

³⁸⁰ *Id.* at 42:1-3.

³⁸¹ *Id.* at 42:11-15.

Limestone's proposal is inconsistent with any ratemaking practices and principles including rate stability, rates based on cost causation, acceptability, and possibly fairness and views of undue discrimination. Limestone has not demonstrated that the cost to provide service in the various service areas are similar.³⁸² The rates should be reasonably stable and predictable. Limestone's proposal is not predictable or stable.

The proposed changes also cause questions of public acceptability, and, absent a cost to serve analysis in each zone justifying the change, this raises questions of fairness. A practice in rate making is to consider cost recovery from those that cause the cost to be incurred. For each rate class, Limestone has proposed to group all wastewater rate zones for a given rate class into one common classification, without demonstrating that the actual cost to serve each of the zones is similar to the cost of serving all other zones.³⁸³

B. Consolidated Rate Design Ignores Important Rate-Making Considerations

As proposed in its filing, Limestone's rate consolidation is an averaging of cost recovery and applying the same rates and rate structure for each customer class across multiple systems. Under that consolidation proposal, all Limestone customers would be charged the same statewide rate.³⁸⁴

Limestone incorrectly states that the primary benefit of consolidated rates is that costs are recovered over a larger customer base. This is not necessarily true.³⁸⁵ If the larger customer base is creating economies of scale that reduce the average cost to customers, it is a benefit. However, if the larger customer base is not producing any cost saving and simply averaging rates, there is no real economic benefit. A larger customer base, and recovery of capital expenses over that larger base, can exist without rate consolidation.³⁸⁶

³⁸² *Direct Testimony of Clark Kaml* at 42:16-21.

³⁸³ *Id.* at 43.

³⁸⁴ *Id.* at 33:1-4 citing *Direct Testimony of Mike Duncan* at 15.

³⁸⁵ *Id.* at 43:17-24.

³⁸⁶ *Id.*

There are several basic principles of rate design that are generally accepted in utility regulation. The principles are drawn from those outlined by James Bonbright in *Principles of Public Utility Rates*:³⁸⁷

- Practical attributes of simplicity, understandability, public acceptability, and feasibility of application;
- Freedom from controversies as to proper interpretation;
- Effectiveness of yielding total revenue requirements under the fair return standard;
- Revenue stability from year to year;
- Stability of rates themselves, minimal unexpected changes seriously adverse to existing customers;
- Fairness of the specific rates in the apportionment of total costs of service on different consumers;
- Avoidance of “undue discrimination” in rate relations; and
- Efficiency in discouraging wasteful use while promoting justified types and amounts of use:
 - In control of total amounts of service; and
 - In the control of relative uses of alternative types of service. While in some cases rate consolidation may be appropriate, in this rate case, consolidating rates is not the answer and does not have any practical benefits except to make it easier for Limestone to account for revenue for the systems.

Those listed by Bonbright are the most common. However, there are other principles that have been offered depending on policies and goals.³⁸⁸ Some examples are:

- Cost causation: the price of utility service should reflect the economic cost of providing service to the customers who cause the utility to incur the expense.
- Offer customers multiple rate options.
- Engage with stakeholders during the process.
- Design customer-centric rates.
- Provide value of service pricing.

Limestone admits that consolidated rates are better at providing cost support for

³⁸⁷ *Direct Testimony of Clark Kaml* at 28 citing BONBRIGHT, JAMES, *PRINCIPLES OF PUBLIC UTILITY RATES*, p. 291 (1961).

³⁸⁸ *Id.* at 34.

improvements being made in some of the worst systems,³⁸⁹ and this can cause concerns of fairness by customers, especially those that will see rate increases.

Also, the Consumer Advocate does not agree that the average cost pricing and statewide rates are the rule rather than the exception. Limestone argues that electric and gas utilities have uniform rates for all customers within rate classes for decades is not applicable when dealing with water and wastewater utilities. While there are similarities among the provision of water service, natural gas services, and electric service, there are also significant differences.³⁹⁰ These services are natural monopolies that can benefit from economies of scale and the provision of the service by one company rather than multiple companies that are competing with one another.³⁹¹ However, there is a fundamental difference.³⁹² Natural gas provision and electric service are, for the most part, a nationwide, integrated system.³⁹³ Natural gas can move from any source point anywhere in the country, regardless of ownership structure of the service provider (municipality, investor-owned company, or cooperative).³⁹⁴ Electricity from any source on the system can be delivered to any customer on the system anywhere in the United States. Due to this interconnection, there are many common costs that support the entire system and the provision of service to all customers regardless of the location of the customer, the location of the investment, or the structure of the service company. Also, another consideration is that there are alternatives to natural gas such as propane and electricity.³⁹⁵ Another difference is that for the most part, electricity needs to be consumed at the same time it is generated.³⁹⁶

³⁸⁹ *Direct Testimony of Clark Kaml* at 33:18-21 citing *Direct Testimony of Mike Duncan* at 17. Mr. Duncan reasons that eventually the better-situated systems will eventually require investments, so this imbalance will right itself over time.

³⁹⁰ *Id.* at 34:4-8.

³⁹¹ *Id.* at 34:8-10.

³⁹² *Id.* at 34:11.

³⁹³ *Id.* at 34:11-12.

³⁹⁴ *Direct Testimony of Clark Kaml* at 34:12-15.

³⁹⁵ *Id.* at 34:20.

³⁹⁶ *Id.* at 34:4-5.

Further, there are differences in the cost of providing natural gas and electric services in geographic areas or based on population densities such as urban vs. rural areas. The cost of providing natural gas or electricity to any area can vary based on several factors such as location, population density, and terrain.³⁹⁷

Also, for natural gas service there are costs to serve differences which are reflected in services or rates. In areas of low population densities, there is the lack of natural gas service and often in those areas, a utility is often designed with parameters identifying a maximum free footage allowance for mains and service lines. Additional fees or rates often apply to the specific customer or customers for extensions beyond the free footage allowance.

Limestone's argument that rate consolidation has occurred in some areas in other states does not justify that rate consolidation be adopted in this rate case in Tennessee. Further, in the case of the Cartwright Creek systems, the Company has not provided any analysis or information explaining why rates were consolidated. Limestone has not provided any analysis that demonstrates that the conditions in the Cartwright Creek systems are applicable to the entire state.³⁹⁸ The same applies to decisions in other states. Without an analysis of the specific conditions of the approvals and the actual decisions related to those cases, a comment of the applicability of those situations to those in Tennessee is only policy or outcome driven, rather than fact based.³⁹⁹

Limestone's proposed rate design is not directly based on a cost-of-service analysis establishing the difference in cost necessary to deliver water service to the current rate zones.⁴⁰⁰ Limestone did not structure the current rate zone structure on a cost-of-service analysis for water or wastewater services. Limestone does not currently maintain the capability of isolating discreet

³⁹⁷ *Direct Testimony of Clark Kaml* at 35:11-15.

³⁹⁸ *Id.* at 36:19-21.

³⁹⁹ *Id.* at 37:1-4.

⁴⁰⁰ *Id.* at 39:13-16.

costs of service by rate zone. Also, the rate zone is geographically divided, with many areas in different parts of Tennessee.

While it may be recommended for smaller water systems to have consolidated rates, in this case, it is not ideal or beneficial. Limestone suggests that over a long-term, the costs are likely to be similar, however, it fails to provide any substantive evidence or documentation.⁴⁰¹

The Consumer Advocate has determined that the Company's proposal is generally inconsistent with ratemaking practices.⁴⁰² Limestone's proposal is inconsistent with rate stability, rates based on cost causation, acceptability, and possibly fairness in view of undue discrimination.⁴⁰³

The Consumer Advocate does not believe that Limestone's rate consolidation plan is reasonable. The Company's rate consolidation is not justified from a cost perspective.⁴⁰⁴ Furthermore, Limestone has not provided any evidence to support the argument that the cost to serve the existing zones is the same or similar. Limestone has not identified any cost savings, and there is no evidence that it would result in just and reasonable rates for customers.⁴⁰⁵

The Company's arguments for consolidated rates are primarily based on policy and have not justified rate consolidation from a cost perspective. There has been no evidence supporting an argument that the cost to serve the existing zones is the same or similar and would result in just and reasonable rates for customers.

XIII. CONCLUSION

For the foregoing reasons, the Commission should find that Limestone's *Petition* to increase water and wastewater rates is without merit. In fact, Limestone's rate case lacks sufficient evidence

⁴⁰¹ *Id.* at 39:14-16.

⁴⁰² *Direct Testimony of Clark Kaml* at 38:6-8.

⁴⁰³ *Id.* at 38:8-10.

⁴⁰⁴ *Id.* at 44:3-4.

⁴⁰⁵ *Id.* at 44:7-8.

and failed to provide proper historical billing determinants in this case for the Commission to authorize a rate increase or consolidate rates. In light of the facts and evidence in this case, Limestone has failed to carry its burden of proving that a rate increase would be just and reasonable at this time. The Commission therefore should deny Limestone's proposed rate increase and rate consolidation request in its entirety.

RESPECTFULLY SUBMITTED,

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