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December 16, 2013

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, Filing Room, 2 North
Harrisburg, PA 17120

RE: Columbia Water Company; Docket No. R-2013-2360798;
REPLY EXCEPTIONS OF THE COLUMBIA WATER COMPANY

Attached are Columbia Water Company's Reply Exceptions in response to the Exceptions filed by the Office of Consumer Advocate and Bureau of Investigation and Enforcement in the above-referenced matter. Copies have been served in accordance with the attached Certificate of Service, as well as upon Administrative Law Judge Dennis J. Buckley.

If you have any questions regarding this filing, please do not hesitate to contact the undersigned.

Very truly yours,

Thomas J. Sniscak
William E. Lehman

Counsel to the Columbia Water Company

WEL/bcs
Enclosure
cc: Per Certificate of Service
Honorable Dennis J. Buckley, Administrative Law Judge
Office of Special Assistants (via hand delivery with enclosed CD)

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BEFORE THE
PENNSYLVANIA PUBLIC UTILTY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket No. R-2013-2360798
	:	
The Columbia Water Company	:	

REPLIES OF COLUMBIA WATER COMPANY TO THE EXCEPTIONS OF THE OFFICE OF CONSUMER ADVOCATE AND THE BUREAU OF INVESTIGATION AND ENFORCEMENT

The Columbia Water Company ("Columbia" or the "Company") hereby submits the following replies to the exceptions of the Pennsylvania Office of Consumer Advocate ("OCA") and the Bureau of Investigation and Enforcement ("I&E") to the Recommended Decision ("RD") of the Honorable Dennis J. Buckley ("ALJ") issued on November 21, 2013. For the reasons stated herein, the OCA and I&E's exceptions should be denied, and the ALJ's decision on those issues should be adopted without modification.

INTRODUCTION AND SUMMARY OF REPLY EXCEPTIONS

Columbia's corporate objective is, as it has been since the Company's inception in 1823, to provide safe and reliable water service to its customers in Lancaster and York Counties. As any other undertaking, however, the Company requires reasonable funds to achieve this objective. Despite this goal, however, the OCA, in particular, and I&E have engaged in an all-out litigation war in this rate case, attacking and fully litigating almost every aspect of the Company's filing. OCA and I&E continue that attack by the filing of these Exceptions challenging the ALJ's well-reasoned and record supported RD on those issues. As recognized by the ALJ, at page 17 of the RD, Columbia is a small, "local" water company, not, say, a major provider of intrastate electric service. As a small company it does not have the luxury of a large staff overseeing internal operations to achieve the costly recommendations of the public advocates. *Id.*

Both the OCA and the I&E have set forth a revisionist argument calculated to deny Columbia necessary cash flow to support $4.9 million in plant in service which both of these parties admitted is used and useful in providing service. Their argument is based on challenging the PennVest rate base/rate

of return and depreciation based volumetric rate which the Commission set in a 1993 Order to which OCA, via one of its counsel in the instant case, agreed to rate base/rate of return treatment. Notably, ***both I&E's and OCA's witnesses who proposed revising history to treat the rate and plant at issue other than rate base/rate of return, admitted they were unaware of the Commission's 1993 rate base/rate of return Order when they did their prefiled testimony and adjustment.*** (Tr. at 179-180; 187) OCA and I&E should have dropped their adjustments at that point but stubbornly now contend it is a debt-service only surcharge some 20 years later, and seek to remove $4.9 million in rate base that no one disputes is in service and has to be supported. By mounting this collateral attack on that Order, however, both I&E and OCA are challenging a Commission-made rate, and as such, they bear the burden to show that the rate was a debt-service only surcharge. Contrary to their positions, 66 Pa.C.S. §316 mandates that the 1993 final order is conclusive on all parties affected thereby.

The ALJ correctly saw through this collateral attack on the 1993 Order and rejected the public advocates' position, stating "once the plant treatment was approved by final Order in 1993 as a rate base/rate of return volumetric rate, it became '*prima facia* evidence of the facts found and remains conclusive on all parties affected thereby.' ... The Commission's Opinion and Order in *Pa. PUC v. Columbia Water* Company, Docket No. R-00932594 (1993) ***cannot be ignored.***" (RD at 21-22; emphasis added). Besides Section 316 and the 1993 Order, there are numerous other reasons why OCA and I&E's PennVest rate base adjustment should be rejected.

This rate was never a debt-service only rate, as a comparison of the characteristics of Columbia's rate base/rate of return rate versus a Commission debt-service rate shows. Specifically, in *Pa PUC v. Pennsylvania-American Water Company*, the Commission described a debt-service surcharge as not rate base/rate of return in that it "is a dollar-for dollar form of recovery... [that] will *not* provide return on or of PAWC's investment and/or will not produce a profit to PAWC," but rather only principal and interest. (1998 WL 456747; emphasis in original). Moreover, Commission debt service surcharges typically are kept in a separate account for repayment so that monies collected from ratepayers are available and used to pay the loan, and often are customer based charges as opposed to volumetric.

There was no separate account requirement and in any event rates were not the sole source of monies for Columbia's repayment of the loan. Moreover, as discussed below, and contrary to I&E's claim the record shows that Columbia did not collect revenues sufficient to cover the entire loan's debt service on a dollar-for-dollar basis, and in fact was at least approximately $200,000 short. Clearly this was not a Commission-style debt service only surcharge.

The few reconciliations of the rate at the request of the Commission did not and could not change the nature of the charge. The reconciliations did not recapture past underages that the plant produced under rate/base rate of return and depreciation relative to debt service; rather they adjusted the rate up or down prospectively to try to meet the rate base/rate of return and depreciation money stream target of the 1993 Order and are consonant with the Commission's obligation under the PennVest Act itself to provide sufficient rates (note the Act does not mandate any particular ratemaking method) to repay the loan.

Similarly, I&E and OCA's argument that the Company did not include the plant in rate base in subsequent rate cases should be rejected because the 1993 rate was an essentially unbundled rate base/rate of return rate with depreciation which was periodically reviewed by the Commission and treated separately. Claiming that plant again as part of a separate rate case, as Columbia's rate expert testified, would have resulted in double claiming or counting that plant.

Finally, both OCA and I&E have also failed to meet their burden of proof with respect to the PennVest adjustment in numerous other important respects including, conflicting with the United States Tax Code, retroactive acceleration of depreciation contrary to the 1993 Order, rendering depreciation lives meaningless, transforming company-financed debt or loans used to construct plant into retroactive CIACs simply because the debt or loan was paid off using rate revenues as a source of monies[1] – all in violation of the fundamental Constitutional provisions against confiscation of property and the right to earn a return on and of plant investment, GAAP principles and well-established ratemaking principles.

[1] The I&E and OCA use the tautology that if a utility uses revenues from rates to pay off a loan that such debt and plant in service financed by such debt/loan should be removed because ratepayers funded the plant. That has never been the law in the United States or in PA, and the fallacy and inappropriateness of this argument is addressed herein.

The Company must be allowed its legal right to recover a fair rate of return on the undepreciated amount of the investment at issue, which is $4.9 million, and annual depreciation expense (i.e., return on and return of) under standard ratemaking principles and the United States Constitution as required by the *Hope* and *Bluefield* decisions.

The OCA and I&E also make numerous negative adjustments to the Company's expense claims based on speculative allocations to the Marietta Division over and above what the Company had already allocated and not included in its filing. The Company's allocations are based on the general manager's first-hand knowledge of the Company's operations and reflect the actual times spent on Marietta Division tasks unlike the speculative assumptions that OCA, in particular, and I&E in regard to Officer's compensation, make from afar. These adjustments were correctly denied by the ALJ stating, "the Commission is not a super board of directors, nor should it act as such, and I am concerned that a number of the proposed adjustments would have that effect if accepted." RD at 17.

The OCA also attacks the reasonableness of the Company's Officers' and Directors' compensation, which same or higher compensation was approved as being reasonable in the Company's 2008 rate case, by taking the novel approach of converting the salaries and fees to hourly rates and imputing their subjective values or worth of each to the Company. OCA's relatively new witness admitted under cross that this approach has never been accepted by the Commission and does not capture the responsibility, liability or legal risks associated with these positions and should be rejected. The ALJ correctly denied this adjustment noting, "OCA's argument is based on hours and dollar amounts that are entirely hypothetical and which take no recognition of any unique qualities of individual officers or of the challenges they face." RD at 37 The Exceptions of OCA and I&E should be denied.

I. COLUMBIA'S REPLY TO:

OCA EXCEPTION NO. 1 – CWC should not be permitted to collect PennVest-funded plant twice from ratepayers.

I&E EXCEPTION NO. 1 - The ALJ erred by not recommending that the Commission exclude the fully financed PennVest plant from the Company's measure of value [rate base] claim.

I&E EXCEPTION NO. 2 - **The ALJ erred by not recommending a reduction to the Company's depreciation expense claim by $115,913 to reflect the I&E-recommended removal of the PennVest plant from rate base.**

Both the OCA and the I&E except to the ALJ's rejection of their challenge to the Company's inclusion of undepreciated PennVest plant in rate base and the associated accrued and annual depreciation. RD at 20-22, 39-40. OCA's Exception No. 1 and both I&E's Exception No. 1 and No. 2 address this issue and, therefore, for ease of reply and review, Columbia will respond to these exceptions in one reply.

a. Introduction

The ALJ rejected the OCA's and I&E's revisionist[2] argument which is calculated to deny the Company necessary cash flow to support $4.9 million of plant in service that both of those parties admitted upon cross was used and useful in providing service. (Tr. at 177, 187) I&E and OCA would also ask the Commission to ignore the 1993 Order discussed below and 66 Pa.C.S. § 316 which mandates such Order "shall be prima facia evidence of the facts found and shall remain conclusive upon all parties affected thereby, unless set aside, annulled or modified on judicial review." The ALJ understood that the 1993 Order set the PennVest volumetric rate using rate base/rate of return methodology, was never appealed, and thus became conclusive upon all parties. RD at 21-22. ***Both I&E's and OCA's witnesses admitted on cross that they were unaware of the 1993 Order*** when they did their prefiled testimony and adjustment. (Tr. at 179; 187) As discussed in greater detail below, I&E and OCA's revisionism should be rejected.

b. I&E and OCA failed to carry their burden for their PennVest plant adjustments.

In Ordering Paragraph No. 4 of its Final Order entered June 1, 1993 at Docket No. R-00932594 the Commission approved a Joint Stipulation of Settlement, dated April 30, 1993 between the Company

[2] In these Exceptions, both the OCA and I&E have challenged the Company's inclusion of undepreciated PennVest plant in rate base and the associated accrued and annual depreciation. This challenge is based primarily on OCA and I&E's bald allegation that although the PennVest volumetric rate was set in 1993 by the Company (and OCA) based on rate base/rate of return principles, this rate was somehow converted, ***without Commission order***, into a debt-service only surcharge which permitted the Company to only recover the principal and interest on the PennVest loan. As set forth in the Company's main brief at 9-16 and reply brief at 7-27, and described below, the PennVest volumetric charge was set using rate base/rate of return methodology in 1993 and was requested and fully supported by OCA. The rate was never transformed into a debt-service only surcharge designed to only recover the principal and interest on the loan.

and OCA that established a return-on and a recovery-of (annual depreciation expense) the investment in the PennVest plant and facilities. The Joint Stipulation set forth the ratemaking treatment as follows:

> 7. Regarding the ratemaking treatment of Plant in Service, the Company agrees to Rate Base treatment for plant additions of $4,547,617, constituting amount attributable to PennVest funding, rather than apply a surcharge equal to the debt service on the PennVest loan. The following items are also reflected in the total revenue of increase proposed in this Stipulation: (a) the inclusion of these plant additions in the rate base, along with the return on the increase plant at an overall rate of return of 7.27%; (b) depreciation expense computed at the Company's current composite depreciation rate; (c) reflection of increased deferred income taxes.[3]

Therefore, the PennVest "surcharge" as OCA and I&E, as revisionists, refer to it, was actually a volumetric rate base/rate of return and depreciation based charge applicable to all customer classes. (CWC St. No. 2R at 2:14-16)[4]

The ALJ correctly realized that once rate base/rate of return and depreciation treatment for the plant at issue was approved by final order in 1993 via a rate base/rate of return volumetric rate, it became "prima facia evidence of the facts found and remains conclusive upon all parties affected thereby, unless set aside, annulled or modified on judicial review." 66 Pa.C.S. § 316. The volumetric rate base/rate of return rate for this plant was never appealed and thus became ***final and conclusive.***

Further yet, the OCA has admitted this conclusive effect on page 12 of their main brief and page 5 of their Exceptions:

> The determination of rate base/rate of return treatment versus principal and interest surcharge is made during the case in which the plant first becomes used and useful. ... ***once that determination is made by the Commission, there is no opportunity to change the methodology***. (emphasis added)

The OCA and I&E's revisionist arguments, and OCA's contradictory argument should, as did the ALJ, be rejected.

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[3] CWC St. No. 2R at 13:1-15; GDS Rebuttal Exhibit No. 1.

[4] In OCA's own statement in support of the 1993 Joint Stipulation, counsel for OCA stated the following:

> The Proposed Settlement provides for an overall base rate increase of $342,508 on an ongoing basis. This lesser amount is the result of permitting the Company to recover the costs of its PennVest-financed plant additions through rate base (including the provision of a reasonable rate of return and an allowance for depreciation expense), rather than through the imposition of a debt-service based surcharge. The OCA submits that, given the size (nearly 6,000 customers) and financial condition of the Company, the Company should not be permitted to impose a debt-service based surcharge. (Tr. 140-141; GDS Rebuttal Exhibit No. 1)

In addition, our Supreme Court has held that it was "proper for the PUC, in making its financial and economic determinations, ***to disregard proposed incomplete adjustments ... if the advocates fail to qualify their adjustments properly.***"[5] As stated in full in the Company's reply brief at 14-20, OCA and I&E have failed to qualify their PennVest exclusion because it also violates the IRS code, the US Constitution, GAAP and generally accepted ratemaking principles.

First, in reliance upon the Commission's 1993 Order approving the rate base/rate of return and depreciation treatment that OCA wanted in the stipulation, the Company, since that time, has kept its books and tax accounts in reliance upon that treatment. Now, some 20 years later, the I&E and OCA want to retroactively unwind that by essentially removing that plant – which they admit is used and useful – from the Company's rate base and therefore books. (Tr. at 177, 187) To remove this plant from the rate base and the Company's books (i.e. reflect a zero value), there are only two accounting methods to attempt to accomplish that, and neither of them appear lawful or generally accepted. Both have adverse legal consequences that I&E and OCA blithely fail to consider and address, and as they have the burden on their adjustment, it must fail in addition to the other reasons raised by Columbia. As stated in Columbia's reply brief at 15, to adopt the PennVest adjustment proposed by the OCA and I&E, the Company would be forced to take one of the following two accounting actions:

> First, the Company would need to reflect the PennVest adjustments proposed by OCA and I&E as a Contribution in Aid of Construction ("CIAC")[6] but the repayment of a loan with proceeds from rates does not meet that test under any accounting or Uniform System of Accounts since a CIAC must be given up front by a customer or developer for a utility to fund and install facilities.
>
> Moreover, in generally accepted ratemaking in Pennsylvania the use of monies from rates to repay a loan has <u>never</u> been deemed to be a retroactive CIAC; rather it is debt financing by the Company that is built into the total cost of service. If I&E and OCA's unorthodox theory were correct, then when ***any utility paid off a loan using monies from rates then that plant's useful and depreciable life would be irrelevant and the plant would come out of rate base as a retroactive CIAC.*** That has never been the case and would create financial chaos to utilities. I&E and OCA completely overrule the US

[5] *Popowsky v. Pa. P.U.C.*, 706 A.2d 1197, 1201 (Pa. 1997); *Pa. P.U.C. v Breezewood*, 74 Pa. P.U.C. 431,437 (1991); *Pa. P.U.C. v. PECO*, Docket No. R-891364 (Final Order Entered May 16, 1990).

[6] If a retroactive CIAC were directed, as I&E and OCA invite, then the Company would have been taxed improperly since 1993, and neither I&E nor OCA offer any solution as to how or if that can be done under the Tax Code. This again typifies the significant problems created by said parties' attempts to rewrite 20 years of financial history by this retroactive adjustment.

> Supreme Court's *Hope* and *Bluefield* decisions which Pennsylvania and this Commission follow, which provide that a utility is entitled by law to return on (i.e. profit) and return of (i.e. depreciation over depreciable lives) assets it invests in whether by debt or equity. Taken to its end, this same argument could be made or applied to equity funded investment by a utility; for example, if a utility used retained earnings (monies whose source was rates from ratepayers) to build a plant.
>
> Second, and illustrative of the unreasonableness of I&E and OCA's retroactive and untimely adjustment to revise the 1993 Order providing rate base/rate of return and depreciation treatment, the only other way to adopt the PennVest adjustment proposed by OCA and I&E to zero out (remove) the PennVest plant from rate base and the Company's books is to somehow show that it had been depreciated over 20 years or the life of the loan. That, however, results in two illegalities that I&E and OCA ignore. First, under IRS and the Tax Code the facilities involved cannot be depreciated – even if accelerated – for less than 25 years, because the "applicable recovery period" is 25 years.[7] Second, the 1993 Order by the Commission directed ordinary rate base/rate of return and depreciation treatment which obviously does not provide for accelerated depreciation. This illustrates how I&E and OCA overlooked or ignored legal problems with their adjustment and as such failed to carry their burden. (Columbia RB at 15-16)

Finally on this point, this retroactive adjustment by I&E and OCA should be rejected, akin to the doctrine of laches or estoppel. Specifically, the Company was directed by the 1993 Order, in which OCA was the primary driver, to treat the facilities as rate base/rate of return with depreciation, and now, some 20 years later, after the company in reliance upon that Order and OCA's preference, is now facing an *untimely and retroactive adjustment that attempts to unwind the Company's reliance and compliance with* that Order, clearly creating harm including removing $4.9 million in used and useful rate base (as I&E and OCA admit), and prospectively requiring the Company to support that plant without any revenue stream mandated by *Hope* and *Bluefield*.

Second, there are more deficiencies to I&E and OCA's wrong and retroactive adjustment to the PennVest total utility plant in service of $4,902,136 and the corresponding accumulated depreciation reserve of $1,853,844,[8] resulting in a reduction to the Company's utility plant measures of value of $3,048,292. Both adjustments ignore the effect on the Company's accumulated deferred income taxes for rate making purposes, and as such their adjustments are insufficiently developed and lack ratemaking symmetry, and even if they were correct (which they are not for the reasons stated in Columbia's Main

[7] 26 U.S.C. § 168(c); IRS Pub. 946 (2-15-13).

[8] I&E appears not to have made this correction in its revision to its revenue requirement calculation offered into evidence at the conclusion of the hearing, and appears to have made this correction instead in its brief. Its adjustment could be disregarded on this basis alone.

and Reply Briefs), they should be rejected on that basis alone. *Popowsky, UGI, Breezewood.* As set forth in the Company's reply brief at 17-18:

> Specifically, I&E and OCA's witnesses admitted on cross as to the used and usefulness of the remaining undepreciated utility plant assets of $3,048,292 well beyond the 20 year term of the PennVest loan. (Tr. at 177, 187) However, in making their adjustments, they ignored the offsetting increase to the Company's rate base created by the reduction to the Company's accumulated deferred tax balance as of December 31, 2013 if the assets, as OCA and I&E propose, are stated at a zero (0) dollar value for ratemaking purposes. The Commission's 1993 Order established the annual depreciation expense and overall return appropriate for the assets funded by the PennVest loan. Now both I&E and the OCA are challenging that order and ***changing*** the basis of the Company's cost recovery mechanism as stated in that order from a rate base/rate of return basis to a concocted "principal and interest basis."
>
> The Company, for the reasons stated in its Main and Reply Brief, submits that there is no basis for I&E and OCA's removal of PennVest plant from rate base. However, *arguendo*, since the life expectancies of the assets are far greater than those lives used for deferred tax purposes, I&E and OCA should have made a significant downward and offsetting adjustment to the Company's claimed accumulated deferred income taxes as of December 31, 2013. At the very minimum, the Company's effective combined state and federal tax rate of approximately 42% applied to the $3,048,292 results in a reduction of $1,280,283 to the Company's accumulated deferred tax balance as of December 31, 2013. This would have increased the Company's measures of value at December 31, 2013 by at least $1.3 million.

Finally, this PennVest plant adjustment is not ground in ratemaking or accounting principles. Neither I&E nor OCA have set forth the accounting and/or rate making adjustment for the taking of the Company's assets. There are no accounting rules contained in the NARUC Uniform System of Accounts or GAAP that allow for the instant removal of PennVest funded plant, or in fact any assets upon the retirement of the associated debt, thereby stranding the undepreciated assets.[9]

The only accounting treatments contained in the NARUC Uniform System of Accounts that even remotely address the parties' position in this proceeding would be the booking of the total $4,902,136 as a Contribution In Aid of Construction (CIAC).[10]

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[9] To the Company's knowledge, this Commission has never considered or ordered the confiscation of utility assets nor have they accelerated the annual depreciation expense for utility assets to equal the term of the funding for those assets. In fact, accepting the OCA and I&E adjustments, in light of the fact that the depreciation was not accelerated, leaves undepreciated assets floating in limbo. No law or rate making procedure establishes, or even contemplates, the removal of assets from rate base upon the retirement of debt.

[10] However, a CIAC requires an upfront payment of cash from either a customer or a developer. An upfront cash payment was not received from the customers and, thus, this approach must be eliminated. The only other method for removing (establishing zero value for) the assets in this proceeding as proposed by OCA and I&E would have been to

...continued on next page

For these reasons alone, the PennVest adjustment recommended by OCA and I&E can and should be denied. However, as stated below, there are numerous other reasons to deny the OCA and I&E's surcharge conversion arguments.

c. Periodic monitoring or review of the rate by the Commission did not change the 1993 Order or how the rate was developed.

First, under the Commission's general powers under Chapter 13 of the Public Utility Code, 66 Pa.C.S. § 1301 *et. seq.*, any rate can be examined to see that it is meeting the revenue and return objective, and if necessary, adjusted. This does not magically turn a rate base/rate of return volumetric rate into a debt-only PennVest surcharge.[11] OCA and I&E provide no cite to any case or indicate anywhere where the Commission converted this PennVest rate from a rate base/rate of return volumetric rate into a debt-service only surcharge. As Mr. Shambaugh testified:

> Such PennVest volume rate was an unbundled rate base/rate of return rate which eventually became reconcilable. The 1997 Commission Order allowed Columbia Water to reconcile their rate, but the rate remained one developed based on rate base/rate of return. The reconciliation was to refine the rate to ensure it hit its rate base/rate of return income target. (Tr. at 139)

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accelerate the annual depreciation expense to 20 years (which the Company has not been doing) to match the PennVest loan period. The parties have directly or indirectly testified, and incorrectly, that a full cost recovery of the loan was accomplished through customer rates indicating that accelerated depreciation is the likely basis for their position in this case. There are several serious problems with this approach. The Commission would have had to approve the reduction in useful lives of the plant to 20 years (accelerated depreciation) at the time the assets were placed on the books, which is less time than the parties have previously testified as being used and useful lives. Even if accelerated depreciation is appropriate, and it rarely is adopted for ratemaking purposes, the life expectancies of the assets and annual depreciation rates would have had to have been determined during the 1993 case, not retroactively during a rate case proceeding in 2013, and even then the acceleration would have been in conflict with the tax code. The PennVest assets have been and continue to be depreciated to date for ratemaking purposes utilizing the 4% Compound Interest Method. (CWC St. No. 2R at 20:16-17)

[11] This rate was a volumetric rate based on usage which is different from a typical PennVest debt-service only surcharge which is a separate line item surcharge divided equally and applied evenly to every customer. *Pa. P.U.C. v. Olwen Heights Water Service Co.*, Docket No. R-00040011 (2005 WL 1060740) (Order entered April 7, 2005) (PUC authorized PennVest Surcharge of $21.02 per customer per quarter); *Pa. P.U.C. v. Wilbar Realty Co. Inc.*, 88 Pa. PUC 1, 1998 (Order entered June 16, 1998) (PUC authorized PennVest Surcharge of $28.80 per customer); and *Pa. P.U.C. v. Mountain Spring Water, Inc.*, Docket No. R-00984346 (1998 WL 8422814) (Order entered July 24, 1998) (PUC authorized PennVest Surcharge of $39 per customer, per quarter for 5/8 inch meters, and $254 per customer, per quarter for 2 inch meters). Therefore, return on Columbia's volumetric rate would fluctuate much more than a separate line item surcharge.

The few reconciliations of the rate at the request of the Commission[12] did not and could not change the nature of the charge. The Commission's request for information regarding the rate base/rate of return based rate for the plant and for reconciliations is neither surprising nor unusual. After all, the Commission has an affirmative obligation under The PennVest Act, 35 P.S. § 751.1 *et seq.* to make sure the ratemaking process enables the utility an opportunity to repay the loan.

Unlike a debt service only surcharge with annual or numerous reconciliations, the few reconciliations of Columbia's volumetric rate did not recapture past underages that the plant produced under rate base rate of return and depreciation relative to debt service; rather they adjusted the rate up or down prospectively to try to meet the rate base/rate of return and depreciation money stream goal of the 1993 Order and is consonant with the Commission's obligation under the PennVest Act itself to provide sufficient rates (note the Act does not mandate any particular ratemaking method) to repay the loan.

Furthermore, I&E and OCA's reading of the Policy Statement itself is wrong as it does not mandate a debt service surcharge as the only PennVest driven rate that may be reconciled. Specifically, 52 Pa. Code Section 69.363(c) states that "Amounts collected under the Section 1307(a) PENNVEST automatic adjustment by means of a sliding scale of rates ***or other method*** are subject to reconciliation and refund." (emphasis added). The 1993 unbundled rate base/rate of return rate clearly under the policy statement itself is an "***other method***."

Finally, to suggest that the rate was "transformed" in 1997, just a few short years after it was set by a Commission Order and even fewer years after the 1994 Commission policy was established, without any mention of the "transformation" by the Commission or any of the parties in the 1997 Settlement Order is absurd. It was not mentioned in the 1997 Settlement because the 1993 rate case was still fresh in everyone's mind and it was clear that no transformation was occurring.[13]

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[12] Columbia simply followed the Commission's orders with regard to reconciliations and providing information to the Commission. (Tr. at 145)

[13] In the 1993 case, the OCA was vehemently against the idea of a debt-service only surcharge and, indeed, brokered the settlement in which the PennVest debt was set using rate base/rate of return methodology. OCA would have never let the Company switch this rate to a debt-service only rate in 1997 as OCA and I&E suggest. The Company's actions subsequent to the 1993 Order ***did not*** magically transform the rate base/rate of return set volumetric rate into a debt-service only surcharge.

d. OCA and I&E's claim that the PennVest plant was not claimed in subsequent rate cases does not support its position; as that would have resulted in double counting such PennVest plant in rates.

I&E and OCA's argument that the Company did not include the plant in rate base in subsequent rate cases should be rejected because the 1993 volumetric rate was an essentially unbundled rate base/rate of return rate with depreciation, which was periodically reviewed by the Commission and treated separately. Claiming that plant again as part of a separate rate case, as Columbia's rate expert testified, would have resulted in double claiming or counting that plant during the time the PennVest plant rate base/rate of return rate was in effect (it is presently not in rates which is why the undepreciated rate base/return value has been sought and bundled back into rate base in this case). Specifically, with respect to the Company excluding the PennVest plant and depreciation from subsequent rate cases, Mr. Shambaugh explained, regarding those past rate case rate base claims, why the PennVest plant was not included in those cases:

> The PennVest plant was excluded for this particular calculation, because as I testified in my rejoinder testimony, there are two components to the base volume rate. This filing that I'm looking at in Supporting Schedule No. 6 is relative only to the one portion of volume rate that this filing considered. The PennVest rate was a separate rate that had already been determined, and those two rates then were combined in the Company's subsequent tariff to equal one base rate volume rate. If I would have included the PennVest in here, it would have, as I testified in my rejoinder testimony, resulted in a double recovery of that investment. (Tr. at 163-164)

Despite I&E and OCA's continued assertion that the PennVest rate was not a rate base/rate of return rate, the facts and law (the 1993 Order and 66 Pa.C.S. § 316) say otherwise. The PennVest volumetric rate was set in 1993 as a rate base/rate of return rate including rate base and depreciation treatment.[14] Thus, as Mr. Shambaugh testified, rate base inclusion and associated ratemaking treatment was and remains appropriate. Consequently, the undepreciated remaining used and useful PennVest plant is properly includable in rate base/rate of return including associated annual depreciation expense.[15]

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[14] Simply because that rate is no longer in Columbia's tariff does not mean the remaining undepreciated plant and facilities do not remain used and useful in providing service to the Company's customers. They are, and the fact that the Company did not have a general rate case since 2008 or 2011 until now is of no consequence regarding whether such rate base exists, is used and useful, and subject to further rate recognition relative to its useful and depreciable life.

[15] CWC St. No. 2R at 2:21-24.

c. The Policy Statement does not support I&E's and OCA's adjustment.

OCA and I&E also argue that the Commission's 1994 policy statement at 52 Pa. Code § 69.361 allows only one method of PennVest loan recovery, either by rate base inclusion or by a PennVest surcharge, (I&E Exceptions at 12-13; I&E MB at 23) and that the policy statement allows only recovery of principal and interest on the PennVest loans (OCA Exceptions at 3-5; OCA MB at 11). These arguments should be rejected for several reasons.

First, upon cross, I&E witness Cline conceded that the 1994 policy statement was intended to apply to companies ***who had not yet elected*** rate base or surcharge treatment, and ***Columbia's election in 1993 precedes the 1994 policy statement.*** (Tr. at 179) As stated above, Columbia elected ***in 1993 (before the policy statement cited by the I&E witness)*** through a settlement driven by the OCA, to recover the rates through a rate base/rate of return volumetric charge instead of a debt-service surcharge.

In addition, the policy statement by its own terms does not forbid the continuance of capital recovery and return on investment for the remaining useful and depreciable life of the assets.[16] As Columbia witness Shambaugh explained, under ratemaking fundamentals and longstanding Commission positions, the term of a loan does not establish the basis for the service lives of the assets or the future life expectancies. (Tr. at 141) Rather, Mr. Shambaugh explained, useful service lives are the basis for depreciable and service lives for ratemaking purposes. *Id.* The Commission should decline OCA and I&E's invitation to replace sound engineering service life judgment with loan terms written by bankers or lenders. Now that the PennVest debt service has been retired, the Company simply wants ***to continue*** to claim the undepreciated amount of the PennVest plant in service. That is the case with any loan used by utilities to fund plant - particularly plant with a long term life that exceeds loan terms. Indeed, OCA itself explained that a PennVest loan is no different than any other loan:

> PENNVEST acts very much like a commercial lender on these projects. It frequently requires personal guarantees of stock pledges from the stockholders. It also takes a secured interest in the utility's plant. The documentation and guarantees required by PENNVEST are very similar to those which a commercial lender would require. Thus, the risk to the stockholders is the same as it would be with any other debt financing.

[16] I&E's witness essentially amends the policy statement to add a prohibition. This prohibition desired by I&E's witness would infringe on a utilities constitutional right to a return on and return of used or useful assets.

> Specifically, PENNVEST has first call on the assets of the company. Further, in many instances the stockholders have personal liability to PENNVEST in the event that the utility is unable to meet its obligations. Thus, in a strict financial sense, the stockholders of the utility are bearing risk equivalent to that which they would bear with any debt financing. (Tr. at 144-145; CWC Rejoinder Exhibit No. 5)

f. The *National Utilities* case cited by OCA in support of the adjustment is distinguishable on the facts and the law and thus inopposite.

The OCA relies on the case of *Pa. P.U.C. v. National Util. Inc.*, 1994 WL 711488 (Pa. P.U.C. 1994) for the argument that post surcharge inclusion of PennVest plant in rate base is not allowed. (OCA Exceptions at 12-17; OCA MB at 17-20) Reliance on this case, however, is inappropriate because the facts and situation surrounding the PennVest plant in that case are completely different from this case. In *NUI*, the utility was trying to eliminate its initially established PennVest surcharge rate and ***convert*** the surcharge rate into a rate base/rate of return rate. *Id.* at *6. That is the complete opposite of what we have here, which is a volumetric rate that is a rate base/rate of return rate, which included the plant in rate base, rate of return, depreciation expense, and income taxes. (CWC St. No. 2R at 13:1-15; GDS Rebuttal Exhibit No. 1) The Company simply wants to ***continue*** including the plant in rate base in order to realize a return on its original cost minus depreciation investment, as is its right.

g. Using revenues from rates to pay a loan does not transform a loan into a retroactive contribution in aid of construction.

Both OCA and I&E make a tautological argument that because a utility loan is paid off with revenues from rates (although for most utilities rates are the only form of revenue and thus all debt is retired using rate generated revenue), and then somehow the ratepayers, not the utility, provided the plant. This assertion is incorrect as rate expert Gary Shambaugh explained:

> This view by I&E, to which OCA proposes the same adjustment, does not comport with basic Pennsylvania ratemaking. Indeed, for any utility that uses debt as a financing vehicle for its plant investment, which is common, the fact that a utility may use revenues from ratepayers to pay off a loan does not transform that into some type of retroactive contribution in aid of construction. A flaw in their thinking is the reality that a term of a loan does not equal useful or depreciable lives.
>
> That has never been the rule in Pennsylvania ratemaking, and virtually every utility in Pennsylvania has used debt to finance plant and the fact they pay that loan in whole or in part with revenues from rates does not transform that plant into customer-provided plant. The basic source of monies for utilities are rates, so it is improper to conclude that repayment of loans with monies from rates equals a customer purchasing rate base. Thus,

rates relative to plant must be viewed on a macro basis and not just on a micro basis fixated on debt service as I&E and OCA have. (CWC St. 2R at 4:3-17)

Moreover, the record clearly shows rates from ratepayers was not the sole source used to repay the loan; rather, there were multiple sources. Thus, I&E witness Cline's supposition fails entirely. Specifically, Company witness Lewis testified the Company used: "[s]everal sources including draws on a line of credit/loan, monies from sales of metering information, a dividend received annually from Workers Compensation insurance, and of course, monies we receive from all our rates under our tariff." (CWC St. No. 1R at 23:13-15) There was no earmarking or separate account required as for a surcharge under Section 69.363(c) – again another fact distinguishing this rate base rate of return and depreciation based rate from a debt service only surcharge.

h. Comparison of characteristics of Columbia's rate base/rate of return and depreciation rate versus surcharge debt service only rate.

The rate here has the characteristics of a rate base and rate of return rate as opposed to a debt service only surcharge that guarantees 100% collection of the loan, as a comparison of the characteristics of Columbia's rate base/rate of return rate versus a Commission debt-service shows. Specifically, in *Pa PUC v. Pennsylvania-American Water Company*, the Commission described a debt-service surcharge as not rate base/rate of return in that it "is a dollar-for dollar form of recovery... [that] will *not* provide return on or of PAWC's investment and/or will not produce a profit to PAWC," but rather only principal and interest. (1998 WL 456747; emphasis in original). Moreover, Commission debt service surcharges typically are kept in a separate account for repayment so that monies collected from ratepayers are available and used to pay the loan, and often are customer based charges as opposed to volumetric.

Here, in contrast, Columbia's volumetric rate for the PennVest plant in the 1993 Order provided for rate base/return and depreciation. (1993 Order *infra.*). The record shows the Company, in compliance and reliance on the 1993 Order depreciated the plant using normal Commission permitted depreciation principles and lives. (CWC St. No. 2R at 20:12-21) Moreover, as discussed below, the record shows that Columbia did not collect revenues sufficient to cover the entire loan's debt service on a dollar-for-dollar basis, and in fact was at least $200,000 short. Further, there was no separate account requirement for

revenues collected from the charge and in any event ***revenues from the rate were not the sole source of monies for Columbia's repayment of the loan***. (Section g, *supra*.) Clearly this was not a Commission-style debt service only surcharge.

Revenues produced for rates such as the volumetric rate base/rate of return rate set by the Commission in 1993 have many variables, such as changes in use habits by customers caused by factors like the economy or water use habits. Clearly the Commission was attempting through monitoring and if necessary a few adjustments to the rate, to fulfill its obligation to provide for the chance of repayment. Moreover, the Company never fully recovered the total amount of the PennVest loan. As Mr. Shambaugh testified on cross-examination regarding a company discovery request regarding monies collected versus loan payments due and paid:

> I would like to point out that those same documents reflect the fact that the company never recovered their full principal and interest. On the final total column, payments are $7,465,166; total revenues received, 7,276,630. So there are fluctuations and variations throughout the course of a company's life and their revenue requirements, and that's just a function of sales, earnings and so forth.
>
> So to look at one specific year and a debt repayment schedule, you could do this with any debt that's out there. They could maybe earn 10 percent this year instead of 9 percent and have excess revenues, and you could apply that then to their outstanding debt and say there is an over-recovery. You have to look at the debt in its totality, and here we're seeing an under-recovery. (Tr. at 159-160)

Notably, ***Mr. Shambaugh explained that such over or under recovery is not unusual under a rate base/rate of return methodology***. (Tr. at 159) Accordingly, this important factual distinction distinguishes the rate at issue from a debt service only surcharge that is 100% reconciled.

In sum on this point, these Commission-requested reconciliations of a rate base/rate of return volumetric rate did not transform the rate into a debt-service only surcharge, and neither I&E nor OCA have carried their burden on this point. Moreover, the Commission cannot deny a utility return on plant it assumed the obligation to fund during the useful life of that plant.[17]

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[17] *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Bluefield Waterworks Improvement Co. v. Public Service Commission*, 262 U.S. 679 (1923).

i. I&E's concern of a precedential effect.

On pages 10-12 of its Exceptions, I&E raises a concern that, despite the ALJ's assertion that this particular issue involves a "unique regulatory history of this PennVest plant" (which the OCA insisted on in 1993), this may embolden other utilities to attempt to claim rate base treatment of their undepreciated PennVest plant after their debt service surcharge terminates. This argument should be rejected because, as fully explained above, the Company's PennVest volumetric rate at issue was never a debt-service only surcharge, so there is no precedential effect for debt service surcharges. Any claims by any company relative to that are for another day under another set of facts.

For the reasons stated above, these Exceptions should be denied.

II. COLUMBIA'S REPLY TO:

OCA EXCEPTION NO. 2 - CWC's materials and supplies claim is inconsistent with prior Commission cases and should be denied.

Columbia's full position on this issue is set forth in its main brief at 7-9 and reply brief at 5-6. The OCA excepts to the ALJ's rejection of its $4,592 negative adjustment to the Company's material and supplies rate base claim of $62,314 (RD at 22) on the basis that its 13-month averaging better recognizes the volatile nature of the balance of this account. The ALJ correctly rejected this claim by reasoning that a 3-year average works best for the Company by stating "this is an instance where 'what works best and what is reasonable,' for this utility specifically should not be disturbed by what another party thinks is optimal and requests based on general policy." RD at 22. The ALJ accepted Company witness Shambaugh's testimony on this matter that if a test year element is volatile, then a larger sample of operating results would be warranted, such as the 3-year average[18] he recommends. RD at 22 (CWC St. No. 2 at 15:5-7)

Mr. Shambaugh further explained that:

> [t]o accurately reflect a 13-month average of materials and supplies, the Company would *have to close its books on a monthly basis, which it does not.* (CWC St. No. 2R at 14:18-20) Mr. Shambaugh also noted that to use a 13-month average would require the Company to count each month and to price the inventory for each item that is in inventory, as that is the only way to get an accurate accounting of the inventory for that month. He

[18] The Company in its 2008 rate case claimed the same treatment for that portion of M&S that were balance sheet/rate base items (2008 filing, Dkt. No. R-2008-2045157 page 1-20 and Columbia St. No. 4 at 13:10-16) and that treatment and claim were not challenged by the parties, and thus were included into the rates approved in the 2008 case.

> explained that the company closes its books annually, which is more economical for smaller companies, and that these annually audited numbers ***(as opposed to the monthly estimates OCA relies on from a discovery response)***, based on actual inventory, better represents M&S than Ms. Everette's use of monthly estimates. (Tr. at 135-136) Furthermore, it is not economical for small companies like Columbia to have such a sophisticated accounting system that dovetails with both materials and supplies that would allow the Company to produce accurate numbers on a monthly basis. (Tr. at 165)

In the alternative, Mr. Shambaugh testified that if the OCA's 13-month position is accepted, the most recent 13-months, as provided in CWC Rejoinder Exhibit No. 3 (updating the response to discovery request OCA-I-7) should be used as opposed to the stale and outdated 13 months Ms. Everette used, which understates M&S. Mr. Shambaugh identified that if the most recent 13 months are used, it results in an M&S inventory claim of $64,888, which is $2,574 above the Company's 3-year average, and is also above Ms. Everette's stale 13-month period. (Tr. at 136)

For the reasons stated above, the OCA's Exception No. 2 should be denied.

III. COLUMBIA'S REPLY TO:

OCA EXCEPTION NO. 3 - CWC's revenues for merchandising sales and jobbing work should be reflected for ratemaking purposes.

Columbia's full position on this issue is set forth in its main brief at 16-17 and reply brief at 27-28. The OCA excepts to the ALJ's rejection of its negative adjustment of $5,838 of the revenue that the Company included in the Merchandizing Sales and Jobbing account as non-operating income. This includes revenue for bulk water sales and customer disconnect revenue. (Tr. at 133-134) The ALJ correctly accepted Company witness Shambaugh's position on this matter.[19] Mr. Shambaugh testified:

> [r]elative to the other items for bulk water sales and customer disconnect revenue, an average basis calculation will not reflect the lack of stability in those items. Those items are not under the direct control of the Company.' (Tr. at 133-134) Mr. Shambaugh testified that those revenues should be booked to the depreciation reserve for the respective plant items under the Uniform System of Accounts. (CWC St. No. 2R at 17:13-17; GDS Rebuttal Exhibit No. 2)

This position was corroborated by I&E witness Wilson who agreed. (I&E St. No. 2-SR at 3:4-19)

For the reasons stated above, the OCA's Exception No. 3 should be denied.

[19] The OCA argues that similar expenses to these were accepted by the Company as operating revenue in the Company's 2008 rate case. However, Mr. Shambaugh testified that he was not the rate expert in that case and he disagrees that it should have been accepted by the Company. (Tr. at 134) Furthermore, the Commission encourages settlements and just because the Company accepted in a previous rate case settlement similar items is not preclusive on the Company in a subsequent case.

IV. COLUMBIA'S REPLY TO:

OCA EXCEPTION NO. 4 - *Columbia's bad debt expense claim should reflect a four-year average to account for year to year variations.*

Columbia's full position on this issue is set forth in its main brief at 20-22 and reply brief at 31-32. The OCA excepts to the ALJ's rejection of its negative adjustment of the Company's bad debt expense from $11,000 to $9,192. RD at 27-28. The OCA argues that a four-year average should be used instead of the Company's pro forma claim.[20]

The ALJ reached the proper conclusion, as he described it, "based on the utility's understanding of its business and customer base." RD at 28. For example, Company witness Shambaugh[21] explained:

> [t]he Company's filing has a known and measurable level of bad debt expense. (Tr. at 134) He went on to explain that when figuring bad debt expense, it is his position that the Company should use audited numbers and not estimates derived from an averaging basis as suggested by the OCA. (Tr. at 134) ... [w]hen you are dealing with rental apartments and things like that you have a higher level of bad debt expense going forward. (Tr. at 134)

Mr. Shambaugh's observations and testimony were, in essence, corroborated by the public input testimony offered by the Manager of the Borough of Columbia, who testified that, "[t]he borough is an economically challenged community with a disproportionately high percentage of low-income households, senior citizens and rental housing." (Tr. at 35)

The ALJ determined that the Company's position of using audited, known and measurable current numbers, instead of OCA's 4-year guesstimate is a more accurate way of predicting bad debt expense and is reasonable. RD at 28.

For the reasons stated above, the OCA's Exception No. 4 should be denied.

V. COLUMBIA'S REPLY TO:

OCA EXCEPTION NO. 5 - Columbia's allocations to the Marietta Division must be adjusted to reflect actual experience.

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[20] The ALJ did not improperly shift the burden as the OCA alleges. He simply stated that the OCA did not present a convincing argument why their method is better than the one proposed by the Company. RD at 28.

[21] Mr. Shambaugh has over 40 years' experience in preparing various financial studies, including rate studies for electric, gas, water, wastewater, steam heat, chilled water and telephone companies as compared to OCA's inexperienced witness who proposed the 4-year average.

Columbia's full position on this issue is set forth in its main brief at pp. 22-32 and reply brief at 32-44. The OCA is unhappy that the ALJ rejected its inexperienced witness's general allocation factor of 15% for certain Company expenses to the Marietta Division in favor of the Company's "real world" allocations that were made by its general manager, Dave Lewis.[22] Mr. Lewis works on a day-to-day basis managing the Company; Ms. Everette does not. It is simply impossible for someone who has no experience working with the water company – and who has never even been there – to make remote suppositions on the amount of time a Columbia employee spends or should spend working on Marietta Division tasks.

a. Employee salaries and wages and payroll taxes.

The ALJ rejects the OCA's speculative allocations of Columbia's employees' time to the Marietta Division as "what adjustment its witness wants," and instead correctly accepted Columbia's allocations based on its general manager's "real world" allocations and the fact that "Columbia employees must still do Columbia Division work." RD at 29 (CWC St. No. 1R at 2:4-5)

With regard to OCA's corresponding adjustment to the Company's payroll tax claim, Mr. Lewis testified that this allocation is based on OCA's flawed and speculative allocations of the Company's employee salaries and wages to the Marietta Division. As Mr. Lewis explained, the Company had already allocated an average of 8% of its employees' time to the Marietta Division; however, the specific percentage varies by employee and the specific amount of time devoted to Marietta Division tasks.[23]

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[22] The Company's general manager, Dave Lewis, testified that the Company had already allocated an average of 8% of its employees' time to the Marietta Division; however, the specific percentage varies by employee. *Columbia's allocations to the Marietta Division are based on Mr. Lewis' first-hand knowledge of Columbia's* operations. Mr. Lewis testified that he is Vice President and General Manager of Columbia, he has been employed by Columbia for eight years, and before that worked for ARRO Consulting, Inc., providing engineering services to Columbia for approximately 15 years. (CWC St. No. 1 at 1:7-17) He further testified that he is responsible for the day-to-day management of the Company and his responsibilities include oversight and management of the business office (3 employees), the distribution department (9 employees), the water production department (5 employees), and several part-time/seasonal employees. (CWC St. No. 1 at 1:20-23) On the other hand, OCA witness Everette's adjustments are not fact-based and are speculative at best. She conceded on cross that she has never spent any time observing what amount of time the Columbia employees spend working on the Marietta Division tasks. (Tr. at 205) She admitted she is not an expert on private utility water system operations, design or utility financing. *She did not even attend the tour of the Company's* operations and facilities requested by OCA and I&E and held on July 24, 2013. (Tr. at 190)

[23] CWC St. 1R at 2:14-3:8.

b. Pension and benefits.

The OCA excepts to the ALJ's rejection of its negative adjustment to total pension expense from $59,682 to $57,944 or $1,738. The OCA's adjustment is based solely on its allegation that Columbia did not support the full amount of its claim because although it claimed $59,682, the check it provided in support was only for $57,944. The ALJ correctly rejected this petty argument because if there is actually a $1,738 shortfall in its pension expense payment to its provider, then Columbia would be required to make that payment good to the provider. Therefore, Columbia's total claim should stand. RD at 31.

c. Disability and Life Insurance

The OCA excepts to the ALJ's rejection of its negative adjustment of $1,029 because it believes the ALJ relied on an unsupported statement that the insurance premium would increase. RD at 31. The ALJ, however, made it very clear that the testimony of Mr. Lewis that the insurance premium would increase was both honest and accurate. RD at 31. This cost is known and measurable, and the Company doubts the OCA would ask the Commission to ignore the notice if it was a decrease in insurance rates.[24]

The ALJ also correctly rejected the OCA's speculative allocation to the Marietta Division. RD at 32. The ALJ correctly accepted Mr. Lewis's testimony that "the Company's allocations of disability and life insurance benefits were based upon the percentage of the person's time allocated to the Marietta Division and the actual costs of the person's benefits." (CWC St. 1R at 11:9-13)

d. Vehicle Insurance

The OCA excepts to the ALJ's rejection of its negative adjustment of $586, which is based on OCA's speculative and hypothetical allocation of its vehicle insurance premium to the Marietta Division. RD at 33. Once again, the ALJ based his decision on the credible testimony of the Company's general manager, Dave Lewis, instead of the speculative allocation of OCA's inexperienced witness, who has no first-hand knowledge of Columbia's operations. RD at 33. Mr. Lewis testified:

> [t]he Marietta Division has its own vehicle, and, thus, most of the vehicle costs are associated with that vehicle. (Tr. at 114) He explained that many of the employees that do Marietta Division work do not use vehicles; for example, customer service personnel, the

[24] OCA's position to ignore the increase, if accepted, will guarantee a lack of expense coverage at the approximate time the rates will become effective. That should not be the goal of ratemaking

> office manager, and the production superintendent. Even meter readers mainly walk and only use the vehicle to get to the service area. (Tr. at 114) He further explained that the vehicle use associated with the Marietta Division is minimal even when you include the hours of those employees that do Marietta Division tasks and use vehicles and, if anything, it is less than 4 percent, which is the amount of time the Company allocated for the foreman and the meter readers and other employees who do Marietta tasks. (Tr. at 114-115)

The OCA also excepts to the ALJ's acceptance of the Company's increase in premiums because the OCA alleges that it falls outside the test year. This negative adjustment should also be rejected because, like the increase in the disability and life insurance premium above, the cost is known and measurable and the rate will be in effect at the time the insurance increase becomes effective.

e. Worker's Compensation.

The OCA excepts to the ALJ's rejection of its negative adjustment of $2,927 for allocation of Workers' Compensation expenses to the Marietta Division using the same faulty, speculative allocation logic it used for Pensions and Benefits. RD at 33-34. The OCA alleges that the ALJ relied on a conclusory statement by Mr. Lewis that 3.8% had already been allocated to the Marietta Division. As Mr. Lewis testified:

> [w]orkers compensation insurance premiums are based upon wages and the classification of the employee, and it is unreasonable to use a blanket amount to allocate and should be based on the actual amount of time allocated to the Marietta Division. He also explained that the 3.8% allocation in the original filing is based upon the actual hours worked on Marietta Division tasks. (CWC St. 1R at 13:14-19)

This statement is not conclusory as the OCA suggests, rather it is the credible testimony of the general manager in charge of the everyday operations of the Company.

Once again, the OCA requests rejection of the Company's increase to its premium for worker's compensation insurance. As above, this increase is known and measurable and will be in effect when these rates go into effect and the ALJ correctly included it in the Company's expense.

For the foregoing reasons, the OCA's Exception No. 5 should be rejected.

VI. COLUMBIA'S REPLIES TO:

OCA EXCEPTION NO. 6 - Columbia's claims for Officers' salaries and Directors' fees *should be reduced to reflect a reasonable level of costs.*

I&E EXCEPTION NO. 3 - **The ALJ erred by not recommending that the Commission adopt the I&E recommended reduction of $5,512 to the Company's updated expense claim of $66,144 for Officers, Directors and majority stockholders salaries.**

OCA's Exception No. 6 deals with both the reasonableness of the Company's Officers' and Directors' compensation and the allocation of that compensation to the Marietta Division. I&E solely challenges the allocation to the Marietta Division. Because these issues have been dealt with together throughout this proceeding, the Company will respond to both Exceptions together.

a. Officers' and Directors' compensation.

The OCA excepts to the ALJ's rejection of its subjective (never previously proposed to or accepted by the Commission) proposal by its first-time full rate case witness of attempting to micromanage the Company's officers' and directors' compensation. The ALJ's findings that "OCA's argument is based on hours and dollar amounts that are ***entirely hypothetical***, and which take no recognition of any unique qualities of individual officers or of the challenges they face or the services they render to a company with its own unique business environment," (emphasis added) and "the OCA, if not engaged in micromanaging and invading the Company's managerial discretion, is coming very close to it," are right on point and are in line with the evidence provided in this matter.

As set forth in the Company's main brief at 33-45 and reply brief at 44-51, the OCA's evaluation of the reasonableness of the Officers' and Directors' compensation centers solely around the subjective managerial-like substitute view that the value or worth to the Company of an Officer or Director can be measured by the amount of recorded time spent on Company business and then conveniently converted to an hourly rate. While this method might be convenient and easy for OCA's witness to calculate, it has nothing to do with the real business world and particularly the water business that OCA's witness admitted in which she had no direct experience. It is also not based on any Commission precedent and does not capture the responsibility, liability, or legal risks associated with these positions.

The Company's claim for Officer and Director salaries is substantially less than the $80,800 that was approved for Officers and $68,000 that was approved for Directors by the Commission in

Columbia's last rate case in 2008.[25] The OCA has provided no evidence since that Order that the performance of the Company's Officers or Directors has lessened in any way. In fact, as Mr. Lewis testified, and is set forth in detail in the performance factor section of the Company's main brief at 52-57 and reply brief at 56-60, the Company has provided exemplary performance over the past several years,[26] including significant management, analysis, and decision making regarding the acquisition of a neighboring challenged water company the Commission found to be in the public interest. (CWC St. No. 1 at 5:8-8:17; Tr. at 120-121) This did not happen by accident, but instead is the direct result of the thorough and effective oversight and guidance provided by the Officers and Directors.

Moreover, Mr. Lewis testified that neither the Company's Officers nor Directors have had any raise in salaries or fees since 2009. (CWC St. No. 1 at 17:17-18) The Company is not requesting a raise in salaries or fees in this filing. Certainly, the salaries that were accepted as being reasonable in 2009 (and are less in 2013) are reasonable today, particularly given the continued outstanding performance of the Company.

Furthermore, OCA's hourly computation is a bad fit from the start for a non-hourly job, and it is rife with OCA witness Ms. Everette's subjective judgment. She conceded she has never been an officer or director of a single company, has never been on a Board of Directors and has never met with Columbia Directors or visited Columbia Water. (Tr. at 190) She fails to comprehend the true responsibilities, liabilities, or legal obligations of the Company's Officers and Directors. She also fails to recognize or identify any portion of their salary that is associated with the responsibilities, liabilities, personal exposure and legal obligations that they assume, but instead tries to tie all of the compensation to the time spent within the walls of the Company's office.

Finally, specific to the Directors' fees, Mr. Lewis pointed out in his testimony, the per-meeting cost of the Directors' fees in this filing is $570. (CWC St. No. 1R at 19:7-8) This is far below the $1,560 average per-meeting cost that the OCA advocated for recently as being reasonable compensation for the

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[25] *Pa. Pub. Util. Commn. v. Columbia Water Co.*, Docket No. R-2008-2045157 (Final Order Entered June 10, 2009).
[26] A review of the Company's management audits at D-2011-2218445 and D-08MEI002 reveals that the Commission found no problems with the compensation of the Officers or Directors.

directors of Newtown Artesian Water Company. (CWC St. No. 1R at 19:15-23; DTL Rebuttal Exhibit No. 3)

b. Allocation of the Officers' and Directors' compensation to the Marietta Division.

The OCA and I&E both except to the ALJ's rejection of their speculative and hypothetical allocations of a portion of Columbia's Officers' and Directors' compensation to the Marietta Division. Once again, the ALJ is right on point with his reasons for rejecting these allocations:

> I am, however, unwilling to impose adjustments based on hypothetical calculations. ... As with OCA's proposed adjustment, I find I&E's proposed adjustment to be a hypothetical construct which takes no recognition of any unique qualities of individual officers or of the challenges they face or the services they render to a company with its own unique business environment.

RD at 41-42. These findings are fully supported by the evidence provided by the Company's general manager, Dave Lewis, who had already allocated 4.3% of the Officers' and Directors' compensation to the Marietta Division as reasonable based on his experience with the Company:

> [e]quating Officer and Directors' time spent on Marietta Division business with the amount of time that Company field supervisors spend on Marietta Division tasks is simplistic and simply wrong. (CWC St. No. 1R at 20:10-12) ... the supervisors for Columbia are overseeing personnel, interacting with regulatory agencies, establishing schedules and work tasks, inspecting work products, evaluating equipment performance and reviewing water quality goals and results. (Columbia St. No. 1R at 20:5-10) ... equating the time spent by Officers and Directors to that of the supervisors is not reasonable on this basis alone and incorrectly compares full time supervisors to part-time Officers and Directors. (Columbia St. No. 1R at 20:5-10) ... OCA fails to recognize that the Company's Directors and Officers still will have to provide the same level of effort and work – and potentially more if the need arises – for the Columbia Division. (Columbia St. No. 1R at 20:21-24) The Company believes that the 4.3% that it agreed to allocate is a more realistic allocation of the Officers' salaries and Directors' fees to the Marietta Division. (CWC St. No. 1R at 21:1-5) ... The Marietta Division work is additional work and in no way becomes shared work with the Columbia Division. The Company's 4.3% allocation represents a representative allocation for the Marietta Division's portion of the work done by the officers and directors. (Tr. at 117-118)

For the foregoing reasons the OCA's Exception No. 6 and I&E's Exception No. 3 should be denied.

CONCLUSION

For the foregoing reasons, the Exceptions filed by the OCA and I&E should be denied in their entirety and the Commission should adopt the ALJ's recommendations with respect to the RD's finding on the matters discussed herein.

Respectfully submitted,

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Counsel for the Columbia Water Company

DATED: December 16, 2013

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the foregoing document upon the parties, listed below, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a party).

VIA FIRST CLASS U.S. MAIL

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Dated this 16th day of December 2013.

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