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|  | | Public Meeting held October 25, 2018 | | |
| Commissioners Present: | |  | | |
| Gladys M. Brown, Chairman  Andrew G. Place, Vice Chairman  Norman J. Kennard  David W. Sweet  John F. Coleman, Jr. | | | | |
|  | | | | |
| Pennsylvania Public Utility Commission  v.  Sugarcreek Water Company | | | R-2018-3001506 | |

**ORDER**

**BY THE COMMISSION:**

On July 26, 2018, Sugarcreek Water Company (Sugarcreek), Utility Code 212920, filed Supplement No. 10 To Water - Pa. P.U.C. No. 3 to become effective November 15, 2018. The subject tariff would increase Rhodes Sewer’s total annual operating revenues for wastewater service by approximately $7,038, or 20.96%.

Analysis of the proposed tariff filing and supporting data indicates that the proposed changes in rates, rules, and regulations may be unlawful, unjust, unreasonable, and contrary to public interest. It also appears that consideration should be given to the reasonableness of Sugarcreek’s existing rates, rules, and regulations. At the same time, analysis of the tariff filing and supporting data indicates that a lesser increase in rates may be just and reasonable;[[1]](#footnote-1) **THEREFORE,**

**IT IS ORDERED:**

1. That if, on or before ten (10) days after the date of entry of this Order, Sugarcreek Water Company files a tariff or tariff supplement, effective upon five (5) days’ notice to the Commission, which cancels and supersedes Supplement No. 10 To Water - Pa. P.U.C. No. 3, and which contains proposed changes in rates calculated to produce additional annual revenues of approximately $3,245 incorporating the schedule of rates shown on Attachment A, attached hereto, the tariff or tariff supplement proposing the increase shall be permitted to become effective upon five (5) days’ notice.
2. That if Sugarcreek Water Company has not filed a tariff or tariff supplement cancelling and superseding Supplement No. 10 To Water - Pa. P.U.C. No. 3 as described in Ordering Paragraph 1 of this Order, on or before ten (10) days of the date of entry of this Order, or been granted additional time to do so by Order of the Commission, the following shall apply:
   1. That an investigation on Commission motion shall be instituted, without further Order of the Commission, to determine the lawfulness, justness, and reasonableness of the rates, rules, and regulations contained in Sugarcreek Water Company’s proposed Supplement No. 10 To Water - Pa. P.U.C. No. 3;
   2. That Supplement No. 10 To Water - Pa. P.U.C. No. 3 shall be, without further Order of the Commission, suspended until June 15, 2019, unless otherwise directed by Order of the Commission;
   3. That within ten days following the suspension of Supplement No. 10 To Water - Pa. P.U.C. No. 3, pursuant to 52 Pa. Code § 53.71, Sugarcreek Water Company shall file (or e-file) a tariff supplement, which shall bear no effective date, with the Commission and post the tariff supplement at the offices of Sugarcreek Water Company announcing that the aforementioned tariff is suspended until June 15, 2019. A sample copy of a suspension supplement is attached to this Order as Attachment B;
   4. That this investigation shall include consideration of the lawfulness, justness, and reasonableness of the existing rates, rules, and regulations of Sugarcreek Water Company; and
   5. That this case be assigned to the Office of Administrative Law Judge for Alternative Dispute Resolution, if possible, for the prompt scheduling of such hearings as may be necessary culminating in the issuance of a recommended decision.
3. That a copy of this Order shall be served upon Sugarcreek Water Company, the Bureau of Investigation and Enforcement, the Office of Consumer Advocate, the Office of Small Business Advocate, and any persons who have filed formal complaints against the Sugarcreek Water Company’s proposed tariff.
4. That this Order is without prejudice to any formal complaints timely filed against the Sugarcreek Water Company’s proposed rate increase.

**BY THE COMMISSION,**

Rosemary Chiavetta

Secretary

(SEAL)

ORDER ADOPTED: October 25, 2018

ORDER ENTERED: October 25, 2018

ATTACHMENT A

**Schedule of Rates**

Service Charge

5/8” meter, per month $16.51

3/4" meter, per month $16.51

1” meter, per month $41.24

2” meter, per month $131.95

Consumption Charge

Rate per 1,000 gallons $4.51

ATTACHMENT B

Sample Suspension Supplement

Supp. No. \_\_\_\_\_\_ to

\_\_\_\_\_\_\_ Pa. P.U.C. No. \_\_\_\_\_

(COMPANY NAME)

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

(TERRITORY SERVED BY COMPANY)

The application of rates proposed in Tariff \_\_\_\_\_\_\_\_\_\_ Pa. P.U.C. No. \_\_\_\_\_\_ filed to become effective \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, is hereby suspended until \_\_\_\_\_\_\_\_\_\_\_\_\_, at Docket No. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_. Presently effective rates contained in Tariff \_\_\_\_\_\_\_\_\_\_ Pa. P.U.C. No. \_\_\_\_\_\_ and supplements thereto, will continue in effect until otherwise amended. Issued in compliance with Title 66 Pa. C.S. § 1308.

ATTACHMENT C

**Adjustments and Reductions to Sugarcreek Water Company Claims**

1. Water Revenues - After applying Commission adjustments, the anticipated income available for return under proposed rates of $7,038 represents a 10.89% return on the original cost rate base of $76,481 which is excessive. If Sugarcreek accepts the Commission’s recommendation to increase revenues approximately $3,245 rather than Sugarcreek’s proposal of $7,038, the anticipated income available for return would be approximately $5,736 which would produce a return of 7.50% on the original cost rate base.
2. Operating Labor - The Commission adjusted Sugarcreek’s claim for operating labor by -$632.64. This includes two separate amounts:
   * Sugarcreek’s sister company, Venango Water Company, provided a response to TUS Data Request R-19 indicating Sugarcreek incorrectly allocated its share of distributed wages, joint expenses and insurance costs and provided a corrected allocation. This $298.86 adjustment is consistent with the corrected allocation provided by Venango; and
   * Sugarcreek’s response to TUS Data Request R-7 indicated a 2017 expense for plant lid painting of $1,035. The Commission has normalized this expense over 10 years, resulting in a -$931.50 adjustment.
3. Depreciation - The Commission adjusted Sugarcreek’s claim for depreciation by   
   -$50.60. The adjustment is due to the early retirement of water meters and the capitalization, and resulting depreciation, of a 2016 amount of $175 for meter installation that was improperly expensed.
4. Rate Base at Original Cost - The Commission adjusted Sugarcreek’s net plant in service by -$232. This adjustment is comprised of the following:
   * $110.23 to add the undepreciated value of meter installation, less the early retirement of water meters;
   * -$343.09 to adjust Sugarcreek’s cash working capital claim both to agree with other adjustments or reductions and to exclude tax and depreciation expenses from Sugarcreek’s calculation; and
   * $0.85 to adjust Sugarcreek’s material and supplies claim to agree with other adjustments.
5. Rate Case Expense - The Commission reduced Sugarcreek’s rate case expense by -$1,200 to reflect a 5-year normalization period as opposed to Sugarcreek’s proposed 2-year normalization period.
6. Non-Operating Income/Expense - The Commission adjusted Sugarcreek’s non-operating income/expense by $46.30 to exclude these revenues and expenses from rates.

**Rate Base**

|  |  |  |  |
| --- | --- | --- | --- |
| **Test Year Ended 2017** | Company ($) | Adjust ($) | Commission ($) |
| Total Depr. Plant in Service | 124,939 | (3,954) | 120,985 |
| Less: Accrued Depr. | 55,964 | (4,065) | 51,899 |
| Net Depreciable Plant | 68,975 | 110 | 69,085 |
| Add: Non-Depr. Plant | 3,211 | - | 3,211 |
| Net Plant in Service | 72,186 | 110 | 72,296 |
| Add: |  |  |  |
| Cash Working Capital | 3,838 | (343) | 3,495 |
| Materials and Supplies | 690 | 1 | 691 |
| Rate Base | 76,714 | (232) | 76,482 |

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| ATTACHMENT D  **RATE OF RETURN ANALYSIS SHEET** | | | | | | | | | | | |
|  | |  | |  | |  | | | |  | | | | |
|  | |  |  | | **Capital Structure Employed** | | | **Interest Expense Used for Tax Calculation** | | | | | |
| Docket Number: | | R-2018-3001506 |  | |  | | |  | | | | |
| Date: | |  |  | | ( ) | | Company | | (X) | | Actual | |
| Name: | Sugarcreek Water Company | |  | | ( ) | | Cons. System | | ( ) | | Hypothetical | |
| Affiliation: | |  |  | | (X) | | Hypothetical | | ( ) | | Normalized | |
| Test Year End: | | December 31, 2017 |  | | ( ) | | Other | | ( ) | | Other | |

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| **Capital Structure and Cost Rates** | | | | | | | | | | | | | | |
| **Per Commission** | | | | | | | | **Company Claimed** | | | | | | |
|  | | | | | | |  | | | | | | | |
| Debt | 50 | x | 5.00 | = | 2.50 |  | Debt | | n/a | x | n/a | = | | n/a | |
| P/S | 0 | x | 0 | = | 0 |  | P/S | | n/a | x | n/a | = | |  | |
| C/E | 50 | x | 10.00 | = | 5.00 |  | C/E | | n/a | x | n/a | = | | n/a | |
| Total | 100 |  |  |  | 7.50 |  | Total | | n/a |  | | | n/a | | | |

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Sugarcreek Water Company (Sugarcreek or the Company) is financed at test year end with $6,075 long-term debt and $81,633 equity. This capitalization is considered atypical for the water utility industry. The Commission has previously utilized hypothetical capital structures when a utility’s capitalization is atypical relative to the barometer group used to determine the return on equity. The Commission has based its return recommendation on a market-based water utility barometer group because the water utility industry offers the most suitable surrogate for determining a rate of return. The hypothetical capital structure (50% debt and 50% equity capital) is a market determined capitalization profile reflecting the risks associated with the industry. The market DCF equity cost rate relates to this structure.

The Commission recommends a 5.00% cost rate to be applied to the debt capital portion of the Sugarcreek’s capitalization. This rate is based on an estimated debt cost of Baa corporate bonds. The pre-adjusted cost of equity is based on a Discounted Cash Flow analysis of a barometer group of water utilities with actively traded common stock. The barometer group-related range of appropriate, market-derived returns is currently 6.41 to 12.93% with a mean of 9.67%. The Commission recommends a return to the Company’s equity of 10.00% based upon adjusting their return to reflect size, current market conditions and the scope of operations differentials vis-à-vis the barometer group. The resulting return on the Company’s rate base is 7.50%.

\_ Andrew Herster\_

Andrew Herster

**Rate of Return-Company Claimed and Per Commission**

**Sugarcreek Water Company**

**Commission Rate of Return:**

Capital Capital Cost Weighted

Components Ratios Rates Cost

% % %

Total Debt 50 5.00 2.50

Preferred Stock

Common Equity 50 10.00 5.00

Total Return 100.0 7.50

**Company Claimed Rate of Return:**

Capital Capital Cost Weighted

Components Ratios Rates Cost

% % %

Total Debt n/a n/a n/a

Preferred Stock

Common Equity n/a n/a n/a

Total Return n/a n/a

1. See Attachments A, C and D of this Order for the adjusted rate schedule and summary of the Commission analysis and adjustments. [↑](#footnote-ref-1)