

**PUBLIC SERVICE COMMISSION  
OF WEST VIRGINIA  
CHARLESTON**

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA in the City of Charleston on the 28<sup>th</sup> day of September, 2007.

CASE NO. 07-0448-W-42T-CN

VALLEY WATER AND SEWER SERVICES, INC.

In the matter of increased rates and charges for water service and application for a certificate of convenience and necessity to replace the water tank serving the Deerwood Subdivision in Berkeley County, West Virginia

**COMMISSION ORDER**

By this order, the Public Service Commission (Commission) grants Commission Staff's (Staff) exceptions in part and denies the exceptions in part. Further, the Commission denies Valley Water and Sewer Services, Inc.'s (Utility) exceptions.

**BACKGROUND**

On August 16, 2007, a Recommended Decision was entered in this matter. The Recommended Decision granted the Utility's application for a certificate of convenience and necessity with certain conditions and ordered that certain rates be approved for use by the Utility for all service rendered on and after September 30, 2007.<sup>1</sup>

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<sup>1</sup>See the Recommended Decision for a complete discussion of the procedural background in this case.

Staff filed exceptions to the Recommended Decision on August 31, 2007. Staff took exception with Conclusions of Law numbered 3, 5, and 6.

The Utility filed a response to Staff's exceptions on September 10, 2007, arguing that Conclusions of Law numbered 3, 5, and 6 were correct. In its response, the Utility requested that the Commission alter the Administrative Law Judge's (ALJ) decision to disallow \$40,389 in legal and accounting expenses incurred in Case No. 06-0508-S-C and the present case. The Utility requested that these expenses be amortized over a period of three years at \$13,463 per year.

## DISCUSSION

### Conclusion of Law 3 – Financing the Tank

Staff takes exception with Conclusion of Law 3 which states:

3. Given all the circumstances, it is not reasonable for the Commission to attempt to force the stockholder of the Utility to make a major infusion of equity capital in the Utility. The Commission should approve financing the tank and should permit recovery of the cost of financing from the ratepayers.

If the customers were responsible for 100% of the debt service on the tank, Staff argued, the Utility would have a capital structure of 91% debt and 9% equity. Staff argued that this was not a reasonable capital structure that would lead to a healthy utility, but rather would impair the Utility's ability to attract capital in the long run. At the hearing in this matter, Staff recommended that customers fund 50% of the cost of the tank and the Utility's owners fund 50% of the cost of the tank by way of an increase in the equity of the Utility.

After construction, the tank would become a part of the rate base under ordinary ratemaking principles. Staff argued that, if the customers pay the entire cost of the tank, the Utility's stockholder would unreasonably benefit because he would be earning a return on investment without contributing any capital to the investment project. Staff also argued that the Utility's stockholder would benefit from a sale of the company after construction of the tank.

Staff further argued that rate shock was an issue in this case with the rates approved, post project, being some of the highest in the state.

Staff requested that the Commission decline to adopt Conclusion of Law 3 and, instead, conclude that the ratepayers and Utility owner should each pay 50% of the cost of the tank, providing for a capital structure of 47.7% debt and 52.3% equity.

The Utility noted in response to Staff's arguments that it had never made a profit, and in fact, the Utility has not paid other entities, owned by the Utility's stockholder, for work performed for the Utility. The Utility's cash flow must be considered when determining appropriate financing for the tank. Furthermore, the Utility argued that for purposes of any possible sale of the Utility, the value of the Utility would likely reflect the net book value of the assets which would include zero for a tank entirely encumbered by debt. The Utility argued that any earnings on the tank would be principal and interest that would flow directly to the bank.

Having considered both parties' arguments, the Commission believes that it should deny Staff's exception concerning Conclusion of Law 3. The Commission does not find fault with the ALJ's decision regarding the "infusion of capital" issue in this particular case. Among other things, there is no dispute among the parties that the water tank must be built. Given that the tank must be built, it must have a realistic funding source. Having said this, the Commission would not agree with any future inference or argument drawn from the Recommended Decision that argues the Commission does not have a legitimate role in reviewing and ensuring that investor-owned utilities have appropriate debt-equity structures. Obviously, the Commission has exercised, and will continue to exercise, such a role.

Conclusions of Law 5 and 6 – Surcharge to Repay Debt Owed to SES

Staff takes exception with Conclusions of Law 5 and 6 in the Recommended Decision which state:

5. It is not reasonable to simply ignore the debt owed by the Utility to SES. The debt was incurred for legitimate purposes under a contract with an affiliate. It would be unfair to expect SES to simply donate its services to the Utility. The ratepayers benefitted from the services which underlie the debt and it is reasonable for them to pay for such services.

6. A surcharge should be added to the tariff, which spreads the debt owed to SES for O&M services over a period of twenty-five years. The utility should be required to make quarterly reports to the Commission regarding the status of the debt and should be required to seek immediate removal of the surcharge upon the repayment of the debt.

Staff argued that recovery of the monies owed to SES for operations and maintenance occurring prior to the historical test year would be retroactive ratemaking. Staff's Exceptions at 11.

In the rate case, the Utility was seeking to put \$79,230 of debt owed to SES, and incurred prior to the test year, into rate base. The Recommended Decision did not include the debt in rate base; however, the ALJ did allow the Utility to recover the monies owed for the debt by allowing a surcharge in the Utility's tariff. The tariff would be applied to rates for a 25-year period.

The Utility argued that it should be allowed to earn a return on the investor supplied capital. Further, the Utility argued that the Commission should acknowledge that the many small, private utilities in West Virginia have large capital and operating expenses and too few customers over which to spread the costs, thereby requiring high rates. Finally, the Utility cautioned that if the Commission did not allow it, and utilities like it, to recover these costs, service would deteriorate, and there would be no incentive for potential owners to acquire the utility. The Utility requested that the Commission affirm conclusions of law 5 and 6 and, additionally, allow the utility to add 5% of the unpaid balance at the end of each year to the debt to help pay for the time-cost of money.

The Commission understands that the Utility should be able to recover its costs; however, basic ratemaking principles must be followed by any utility operating in this State. Nothing has prevented the Utility from seeking recovery of this item in more timely and earlier rate proceedings. Rule 42 of the Commission's *Rules for the Construction and Filing of Tariffs (Tariff Rules)* requires a utility filing for a rate increase to provide financial information regarding the historical test year, the most recent 12 month period ending on a calendar quarter. The Commission typically limits information regarding a utility's financial condition to the historical test year and does not allow adjustments outside of the test year. The Commission finds no reason to deviate from that course in the present case. The Commission will decline to adopt conclusions of law 5 and 6 in the Recommended Decision and not allow a surcharge for the recovery of debt incurred prior to the test year.

#### Utility's Accounting and Legal Expenses

In its response to Staff's exceptions, the Utility requested that the Commission allow it to recover accounting and legal expenses totaling \$40,389. These expenses were incurred by the Utility in Case No. 06-0508-S-C and the present case. The Utility requested that the rates be amortized over a period of three years at \$13,463 per year. The ALJ adopted Staff's rate case expense position which allowed \$10,000 to be amortized over 5 years or \$2,000 per year. The Commission finds no reason presented in the Recommended Decision or in the Utility's response to Staff's exceptions to change or alter the ALJ's recommendation on this issue.

#### Petition for General Investigation

Notwithstanding the fact that the Commission has reduced the rates in this Order to be implemented by the Utility, the Commission is seriously concerned about the level of the rates and the continued viability of the Utility. Staff should file a petition with the Commission requesting a general investigation of this Utility. Staff may include in its petition the issues Staff deems appropriate; however, at a minimum, the petition should include a request to investigate the long-term viability of the Utility, its relationship to Snyder Environmental Services, Inc. (SES), the opportunities and alternatives for the transfer of ownership, and whether receivership is appropriate.

Furthermore, the Utility shall file quarterly status reports, beginning on October 15, 2007, regarding the status of the possible sale of the Utility to another utility in the area.

### FINDINGS OF FACT

1. A Recommended Decision was filed in this case on August 16, 2007.
2. Staff filed an exception to conclusion of law 3 of the Recommended Decision and requested that the Commission require ratepayers and the Utility to each pay 50% of the cost of the tank.
3. Staff also filed an exception to conclusions of law 5 and 6 of the Recommended Decision and requested that the Commission disallow recovery by the Utility for operating and maintenance debt incurred by the Utility outside of the historical test year.
4. The Utility filed a response to Staff's exceptions in support of conclusions of law 3, 5 and 6.
5. The Utility filed an exception to the ALJ's treatment of rate case expenses and requested that the Commission not adopt the Recommended Decision on this issue, but allow \$40,389 in expenses incurred in the present case and Case No. 06-0508-W-C to be amortized over a period of three years at \$13,463 per year.

### CONCLUSIONS OF LAW

1. It is reasonable to adopt conclusion of law 3 of the Recommended Decision.
2. It is reasonable to decline to adopt conclusions of law 5 and 6 of the Recommended Decision. The debt sought to be recovered by the surcharge was debt incurred outside of the historical test year and, therefore, should not be included in determining rates and charges in the present case.
3. It is reasonable to deny the Utility's exception concerning recovery of attorney and accounting expenses because the Utility provided no compelling argument to overturn the Recommended Decision on this issue.
4. It is reasonable to require Staff to file a petition with the Commission requesting a general investigation of this Utility. Staff may include in its petition the issues Staff deems appropriate; however, at a minimum, the petition should include a request to investigate the long-

term viability of the Utility, its relationship to Snyder Environmental Services, Inc. (SES), the opportunities and alternatives for the transfer of ownership, and whether receivership is appropriate.

**ORDER**

IT IS THEREFORE ORDERED that the Recommended Decision is hereby adopted by the Commission except that conclusions of law 5 and 6 shall be stricken therefrom and Appendix A and Appendix B attached to the Recommended Decision shall be replaced with Appendix A and Appendix B attached hereto.

IT IS FURTHER ORDERED that, consistent with the above ordering paragraph, Staff's exception to conclusion of law 3 is hereby denied.

IT IS FURTHER ORDERED that, consistent with the first ordering paragraph, Staff's exception to conclusions of law 5 and 6 is hereby granted.

IT IS FURTHER ORDERED that, consistent with the first ordering paragraph, the Utility's exception regarding the treatment of accounting and attorney expenses is hereby denied.

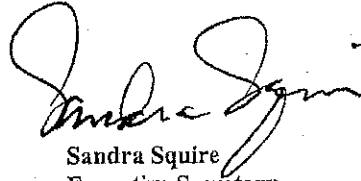
IT IS FURTHER ORDERED that Staff shall file a petition with the Commission requesting a general investigation into the viability of the Utility. The petition shall be consistent with the directive given to Staff in the Discussion and Conclusion of Law sections of this Order.

IT IS FURTHER ORDERED that the Utility shall file quarterly status reports in this case, beginning on October 15, 2007, regarding the status of the possible sale of the Utility to another utility in the area.

IT IS FURTHER ORDERED that, upon entry hereof, this proceeding shall be removed from the Commission's docket of active cases.

IT IS FURTHER ORDERED that the Commission's Executive Secretary serve a copy of this Order upon all parties of record by United States First Class Mail and upon Commission Staff by hand delivery.

A True Copy, Teste:



Sandra Squire  
Executive Secretary

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