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S.C. Supreme Court

THE STATE OF SOUTH CAROLINA

In the Supreme Court

APPEAL FROM THE SOUTH CAROLINA PUBLIC SERVICE COMMISSION

PSC Docket No. 2013-42-S

Sensor Enterprises, Inc. and J-Ray, Inc.....Appellants

v.

Palmetto Utilities, Incorporated and
South Carolina Office of Regulatory Staff..... Respondents

INITIAL BRIEF OF APPELLANTS

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**ATTORNEYS FOR APPELLANTS SENSOR
ENTERPRISES, INC. AND J-RAY, INC.**

March 21, 2014

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ISSUES ON APPEAL

1. **The Public Service Commission's ("PSC") rejection of the Appellants' alternate rate design based upon metered water usage was not based upon substantial evidence and was arbitrary and capricious.**
2. **The PSC's approval of the Respondents' proposed equivalency rate of 10 gallons per drive through vehicle was not based upon substantial evidence and was arbitrary and capricious.**
3. **To the extent the PSC based any part of its decision upon the assumed strength of the Appellants' wastewater discharge, such decision was not based upon substantial evidence and was arbitrary and capricious.**
4. **The PSC erred in holding that the Appellants were required to propose a particular rate and to demonstrate the effect of their alternatives on the overall rate design in order to demonstrate that the rate design proposed by PUI is unjust and unreasonable.**
5. **The PSC erred in accepting PUI's estimated monthly car counts for J-Ray, Inc. despite the fact that J-Ray, Inc. presented testimony regarding the actual number of cars visiting the drive through window of its restaurant each month.**

STATEMENT OF THE CASE

On March 13, 2013, Palmetto Utilities, Inc. ("PUI") filed an Application for adjustment of rate and charges for and modification to certain terms and conditions related to the provision of sewer service. (Application, dated March 13, 2013.) On April 23, 2013, Appellants Sensor and J-Ray intervened in the rate case. (Petitions to Intervene of Sensor and J-Ray.) The matter was heard by the PSC on August 13, 2013. (Order, dated September 17, 2013.) Subsequently, the PSC issued its Order Granting Adjustment to Rates and Charges, Commission Order No. 2013-669, ("Order") on September 17, 2013. (*Id.*) The Appellants filed a Petition for Rehearing and/or Reconsideration on October 7, 2013. (Petition for Rehearing and/or Reconsideration of Sensor Enterprises, Inc. and J-Ray, Inc., filed October 7, 2013.) The PSC denied this Petition by Commission Directive, Order No. 2013-771, dated October 23, 2013. (Commission Directive,

dated October 23, 2013.) Sensor and J-Ray timely filed a Notice of Appeal with the Supreme Court of South Carolina.

STATEMENT OF THE FACTS

As part of its Application, PUI proposed to charge commercial customers a rate of \$39.00 per Single Family Equivalent (“SFE”). (Application, Ex. A § 1.) PUI proposed to utilize the South Carolina Department of Health and Environmental Control’s Guidelines for Unit Contributory Loading for Domestic Wastewater Treatment Facilities, 25 S.C. Code Ann. Regs. 61-67 Appendix A (Supp. 2010) (“DHEC Unit Contributory Loading Guidelines”), as the basis for calculating the number of single family equivalents attributable to each commercial customer. (Application, Ex. A § 12.)

Both Appellants own McDonald’s restaurants within PUI’s service area. Mike Pippin, Director of Operations for Sensor, testified at the hearing on behalf of Sensor. (Tr. of Hrg. pp. 163-181.) Chris Valdes, Supervisor for J-Ray, testified on behalf of J-Ray. (*Id.* pp. 181-193.) Mr. Pippin and Mr. Valdes testified that prior to the filing of this most recent Application by PUI, Sensor and J-Ray consistently received sewer charges from PUI of approximately \$400 per month and \$800 per month, respectively. (*Id.* p. 165 lines 4-6; p. 183 lines 20-22.) Under the rate plan originally proposed by PUI, Sensor and J-Ray faced sewer charges of \$5,266.80 per month and \$5,065 per month, respectively, which equated to increases of 1,311% and 627%. (*Id.* p. 173 line 19 – p. 174 line 1; p. 187 line 19 – p. 188 line 1.) By contrast, residential customers faced only an 18% increase in rates. (Application, Ex. A § 1.) Under the rates in PUI’s Application, Sensor and J-Ray would have paid an increased amount of more than \$50,000.00 per year for sewer service.

On July 1, 2013, prior to the hearing before the PSC, PUI and ORS entered into a Settlement Agreement. (Settlement Agreement.) Sensor and J-Ray were not parties to the Settlement Agreement. (*Id.*) Pursuant to the terms of the Settlement Agreement, PUI agreed to reduce the number of SFEs attributable to each car at a drive-thru restaurant from 40 gallons per car to 10 gallons per car. (*Id.* p. 2 ¶ 3.)

Because the manner in which PUI proposed to charge Sensor and J-Ray is based in part on the number of drive-thru cars per day, Mr. Pippin and Mr. Valdes also provided testimony regarding the number of cars that utilize the drive-thru at each of their stores. Mr. Pippin testified that the actual number of cars served per day at Sensor store is 1,035. (Tr. of Hrg. p. 166 line 23-24.) PUI originally estimated the number of cars at Sensor store at 1,400 per day. Rick Melcher of PUI testified that PUI subsequently reduced its estimate of the number of cars for Sensor store to 1,225 but that this number included a multiplier of 120%. (*Id.* p. 299 lines 8-22.) Mr. Valdes testified that the actual number of cars served per day at the J-Ray store is 1,141. (*Id.* p. 187 lines 16-17.) Rick Melcher testified that PUI used estimated the number of cars at the J-Ray store to 1,635, which included a multiplier of 120%. (*Id.* p. 299 lines 26-29.)

Sensor and J-Ray retained David Russell as an expert witness to testify regarding the reasonableness of the rates proposed by PUI and to propose alternate methods of assessing sewer rates for Sensor and J-Ray. Mr. Russell testified that even under the Settlement Agreement, the increase in rates propose to be charged to the Appellants were unjust and unreasonable. (*Id.* p. 210 line 14 – p. 211 line 14.) Mr. Russell further testified that the PSC should approve one of two alternate methods:

1. For PUI to assess sewer rates based upon the water usage or
2. For PUI to decrease number of SFEs attributable to each car to 2.

(*Id.* p. 202 line 8 – p. 203 line 9.) Mr. Russell expressed concern about the use of the DHEC Unit Contributory Loading Guidelines for the following reasons:

1. The Guidelines were developed to be used for the design of wastewater system facilities and not to estimate average flow from customers; the two purposes are completely different.
2. The Guideline's unit contributory loading factors are estimates of peak or maximum daily contributions per unit measure and do not represent average or typical use.
3. The Guidelines are outdated having been originally issued over 40 years ago.

(*Id.* p. 211 line 16 – p. 212 line 13.)

Following the hearing, the PSC issued its Order rejecting the Appellants' alternate proposals for rate design. (Order, dated September 17, 2103.) Sensor and J-Ray filed a Petition for Rehearing, which was also denied by Commission Directive, Order No. 2013-771, dated October 23, 2013. (Commission Directive, dated October 23, 2013.) It is from these two Orders that the Appellants now appeal.

STANDARD OF REVIEW

The general standard for judicial review of administrative decisions is set forth in the Administrative Procedures Act as follows:

The court may not substitute its judgment for the judgment of the agency as to the weight of the evidence on questions of fact. The court may affirm the decision of the agency or remand the case for further proceedings. The court may reverse or modify the decision if substantial rights of the appellant have been prejudiced because the administrative findings, inferences, conclusions, or decisions are:

- (a) in violation of constitutional or statutory provisions;
- (b) in excess of the statutory authority of the agency;
- (c) made upon unlawful procedure;
- (d) affected by other error of law;
- (e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole

- (f) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.

S.C. Code Ann. § 1-23-380(5). Regarding review of decisions of the PSC in particular, this Court has held:

The PSC's ratemaking decisions are entitled to deference, and will be affirmed if supported by substantial evidence. *S.C. Energy Users Comm. v. S.C. Public Service Comm'n*, 388 S.C. 486, 490, 697 S.E.2d 587, 589 (2010). “Substantial evidence is relevant evidence that, considering the record as a whole, a reasonable mind would accept to support an administrative agency's action.” *Porter v. S.C. Public Service Comm'n*, 333 S.C. 12, 20, 507 S.E.2d 328, 332 (1998). “We will not substitute our judgment for that of the PSC where there is room for a difference of intelligent opinion.” *Kiawah Property Owners Group v. Public Service Comm'n of S.C.*, 357 S.C. 232, 237, 593 S.E.2d 148, 151 (2004). However, we “may reverse or modify the decision if substantial rights of the appellant have been prejudiced because the [PSC's] findings, inferences, conclusions, or decisions are: ... (b) in excess of the statutory authority of the agency; (c) made upon unlawful procedure; [or] (d) affected by other error of law.” S.C. Code Ann. § 1-23-380(5) (2005 & Supp.2010).

Utilities Servs. of S.C., Inc. v. S.C. Office of Regulatory Staff, 392 S.C. 96, 103-04, 708 S.E.2d 755, 759 (2011).

Thus, this Court may reverse a decision of the PSC if the Court determines that the decision is not supported by substantial evidence or if the decision is arbitrary and capricious.

ARGUMENT

The overarching policy question underlying this appeal is whether it was appropriate for the PSC to approve PUI's Application where it premised commercial wastewater rates upon the DHEC Unit Contributory Loading Guidelines. PUI's witness, Marion Sadler, testified that these guidelines were developed in the 1970's for the sole purpose of providing guidance in the design of wastewater systems so as to ensure adequate capacity for those systems. (Tr. of Hrg. p. 111 line 2-8.) The Appellants' expert witness, David Russell, testified that the design of a wastewater treatment system and estimating flow from particular customers are completely different purposes. (*Id.* p. 212 lines 3-4.) Accordingly, the Appellants assert that the use of the

DHEC Unit Contributory Loading Guidelines in rate-making results in unjust and unreasonable rates being charged to commercial customers with drive-thru restaurants.

1. The PSC's rejection of the Appellants' alternate rate design based upon metered water usage was not based upon substantial evidence and was arbitrary and capricious.

Sensor and J-Ray contend that the fairest sewer rate would be based upon metered water usage. At the assumed and excessive rate of 10 gallons per car the amount of wastewater that Sensor and J-Ray would be billed for far exceeds any amount of historical use. For Sensor, the PSC accepted PUI's estimate of 1,225 cars per day. Based upon the assumed rate of 10 gallons per car, that would equate to a billed-for 10,225 gallons of waste water per day or 306,750 gallons of waste water per month. Mr. Pippin testified that Sensor's water bills show that Sensor uses an average of 86,000 gallons per month. Thus, Sensor would be charged for approximately 350% more wastewater than it could possibly produce.

As for J-Ray, the PSC accepted PUI's estimate of 1,635 cars per day. Again, using the assumed and excessive per car rate of 10 gallons per car, this equates to 16,350 gallons per day or 490,500 gallons of water per month. Mr. Valdes testified that J-Ray's average monthly water usage is in fact only 107,063 gallons per month. Thus, under the plan approved by the PSC, J-Ray will be charged for more than 400% more wastewater than it could possibly produce.

In response to these significant increases, Sensor and J-Ray produced an alternative rate design that would fairly account for the actual amount of wastewater discharged to the PUI system. Sensor and J-Ray proposed that billing be based upon metered water usage rather than upon a monthly flat rate per SFE.

In rejecting this proposal, the PSC held that "Sensor and J-Ray's alternative rate design proposal is not feasible" because "PUI does not have access to water billing records or the right

to meter flow from City of Columbia water line or Town of Winnsboro water line.” (Order, p. 27.) This statement is not supported by the evidence presented at the hearing. First, Edward Wallace of PUI testified that a sister company to PUI, Palmetto Richland County, does in fact utilize “volume billing” and bases waste water billing upon metered water usage. (Tr. of Hrg, p. 100 lines 3-17.) Furthermore, both Sensor and J-Ray testified that they would be willing to compile their water bills and provide them on a regular basis directly to PUI. (Tr. of Hrg, p. 167 lines 15-21; p. 185 lines 7-17.) Thus, water volume information is obtainable. Contrary to the PSC’s determination, volume billing is feasible because it is being gathered in other states and in South Carolina in other systems within the PUI’s family of utility companies. (Tr. of Hrg, p. 100 lines 1-9.) And, the Appellants offered and are willing to provide the information directly to PUI. (Tr. of Hrg, p. 167 lines 15- 21; p. 185 lines 13-17.) The only evidence that volume billing might be difficult was Mr. Edward’s speculative and unsupported testimony that water utilities might be resistant to turning over their billing information. (Tr. of Hrg, p. 100 lines 9-17.)

In further contradiction of PUI’s contention that water usage information is unobtainable, PUI’s rate design specifically provides that it can base a customer’s billing upon the volume of water used if it appears that the actual volume exceeds the number of SFEs estimated pursuant to the Unit Contributory Loading guidelines. This section provides in pertinent part:

Where the Utility has reason to suspect that a person or entity is exceeding design loadings established by the Guidelines for Unit Contributory Loadings for Domestic Wastewater Treatment Facilities, the Utility shall have the right to request and receive water usage records from the provider of water to such person or entity. Also, the Utility shall have the right to conduct an “on premises” inspection of the customer’s premises. If it is determined that the actual flows or loadings are greater than the design flows or loadings, then the Utility shall recalculate the customer’s equivalency rating based on actual flows or loadings and thereafter bill for its services in accordance with such recalculated loadings.

(Application, Ex. A § 12.) The Appellants' expert witness, David Russell, testified that permitting PUI to increase billing based upon actual usage but not to require the utility to base billing upon actual usage is unreasonable and unfair to the customer. In particular, Mr. Russell testified as follows:

This section as currently written is unfair and biased in favor of PUI. It would be appropriate and reasonable to allow adjustment in both directions. PUI should be allowed to adjust its billing for customer that uses significantly more than what is estimated by the SFE methodology. Conversely to be equitable, a customer who uses significantly less than what is estimated by the SFE methodology, should (if verified) have their bills adjusted downward to closely match their actual usage (metered water consumption). What is fair and reasonable for PUI should also be fair and reasonable for the customer. It is simply unreasonable and inequitable to charge a customer for much more than they contribute to the system and for much more than it actually costs to serve that customer when it can be easily demonstrated that their actual usage is much less.

(Tr. of Hrg, p. 13 lines 7-19.)

As the above demonstrates, the current rate of billing places an unfair burden on drive-thru restaurants to subsidize other rates. The only reliable evidence indicates that volume billing is feasible. Thus, there is no substantial evidence to support the PSC's determination that volume billing is not feasible.

In addition, if it is fair and reasonable to permit PUI to increase its billing based upon metered water usage, the converse, i.e. to permit a customer to decrease its billing based upon metered water use, must also be fair reasonable. In both instances the critical consideration is volume of wastewater contributed to the system. To find that the volume of wastewater contributed to the system is important in one instance and not in the other is arbitrary and capricious.

2. The PSC's approval of the Respondents' proposed equivalency rate of 10 gallons per drive through vehicle was not based upon substantial evidence and was arbitrary and capricious.

As calculated in the previous section, Sensor will be charged for at least 350% more water than it actually uses, and J-Ray will be charged for at least 400% more water than it actually uses. In arriving at its estimate of 10 gallons per car, PUI utilized a formula based upon compiled estimates. (Tr. of Hrg, p. 80 line 1 – p. 82 line 12.) In contrast, the Appellants' expert witness reached an estimate of gallons per car based upon the actual number of cars and water consumption for Sensor and J-Ray. (Tr. of Hrg, p. 218 line 20 – p. 219 line 17.) In the face of calculations tied to hard numbers and not merely estimates, the PSC should have granted PUI's calculation little credibility, leaving the PSC's decision without substantial evidence. To ignore the overwhelming weight of evidence as to the actual documented usage of water per car was arbitrary and capricious.

3. To the extent the PSC based any part of its decision upon the assumed strength of the Appellants' wastewater discharge, such decision was not based upon substantial evidence and was arbitrary and capricious.

One of the arguments that PUI's rebuttal testimony addressed was that Sensor and J-Ray should be required to pay higher wastewater rates because it is presumed that the "strength" of their wastewater stream is greater than that of the average residential household. (Tr. of Hrg, p./ 301 line 27 – p. 302 line 15.) There is no credible evidence in the record to support this position and was error for the PSC to premise its decision in any part on the presumed greater strength of the wastewater flows from the Appellants. (Order, p. 29.)

PUI asserts that one of the main contributors to the strength of wastewater is grease. (Tr. of Hrg, p. 132 line 16 – p. 133 line 3; p. 302 lines 7-9.) Rick Melcher testified on behalf of PUI that grease from commercial customers is much more highly regulated than grease from

residential customers. (Tr. of Hrg, p. 133 lines 9-17.) For example, PUI requires food service establishments to install, inspect, maintain, and regularly pump out grease traps. *Id.* In fact, PUI requires one of its employees to be on site to observe when a grease trap is pumped out. *Id.* PUI further requires grease disposal companies to provide proof of proper disposal of all grease collected. *Id.* By contrast, PUI has no ability to regulate grease coming from residential customers and can only provide them education in the hopes that they will not introduce grease into the system. (*Id.* p. 133 lines 4-8.)

Mr. Pippin testified that his restaurant has grease traps and that those traps are installed, maintained, and pumped out in accordance with all of PUI's requirements. (*Id.* p. 167 line 22 – p. 168 line 10.) Because grease is so highly regulated for food service establishments, it is more reasonable to expect that their waste water flow strength is not significantly greater than that of residential customers in terms of the presence of grease. Mr. Melcher also speculated that the Appellants use commercial cleansers that would increase the strength of the Appellants' waste water stream. (*Id.* p. 302 lines 6-7.) However, mere speculation is not probative, *McDowell v. Stille Plywood Co.*, 210 S.C. 173, 41 S.E.2d 872, 875 (1947), and cannot form the basis of substantial evidence.

Accordingly, PUI presented no evidence that the Appellants or any other commercial customer's wastewater discharge is of any different strength from that of a residential customer. Therefore, there was no substantial evidence in the record upon which the PSC could have based a finding on this point, and to have based a finding upon mere speculation while rejecting testimony based upon the personal knowledge of the Appellants was arbitrary and capricious.

4. **The PSC erred in holding that the Appellants were required to propose a particular rate and to demonstrate the effect of their alternatives on the overall rate design in order to demonstrate that the rate design proposed by PUI is unjust and unreasonable.**

Throughout its Order the PSC states that it rejects the Appellants' position because the Appellants failed to propose an alternate rate design. However, the PSC fails to provide any authority for this foundation of its decision.

In fact, the Appellants did propose two alternate rate designs. The Appellants did not propose a specific rate to be charged nor did the Appellants evaluate the effect that the change in the rate billed to them would have on the overall revenue stream of PUI. To require this type of information from any and all customers who are aggrieved by a rate increase would essentially preclude the majority of customers from ever intervening or filing complaints in rate cases. The cost of preparing such a response would be prohibitive for almost any party other than the utility. For example, in this rate case alone, PUI incurred almost \$180,000 in rate case expenses. (Tr. of Hrg, p. 241 lines 10 – 24.)

On the other hand, PUI knew prior to this hearing that the Appellants would argue for these two alternate rate plan proposals. PUI presented no information at the hearing of this matter regarding how a decrease in proposed revenue from customers in Appellants category would affect its overall revenue recovery. Thus, it is arbitrary and capricious for the PSC to find that the Appellants solely shouldered this burden and to reject their claims for this reason.

5. **The PSC erred in accepting PUI's estimated monthly car counts for J-Ray, Inc. despite the fact that J-Ray, Inc. presented testimony regarding the actual number of cars visiting the drive through window of its restaurant each month.**

Because PUI's rate plan bases its billing in great part upon the number of cars per day per restaurant, it is important to ascertain an accurate count of those vehicles. Despite evidence to the contrary presented by J-Ray, the PSC appears to have accepted PUI's car counts. Rick Melcher

testified that PUI estimated the number of cars for the J-Ray restaurant to be 1,635 per day. Chris Valdes testified that his personal knowledge of the average number of cars per day at the J-Ray store is 1,141. This is a difference of 494 cars per day, or a 43% difference. Under the 10 gallon per car per day formula, this translates to J-Ray being charged for an excess of 4,940 gallons of waste water per day and 148,200 gallons of waste water per month. This mean J-Ray would be required to pay for an excess of 12.35 SFEs per month, which at the rate of \$36 per SFE equates to an overcharge of \$444.60 per month.

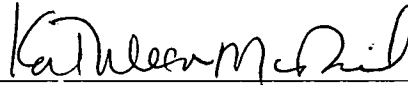
As for Sensor, Rick Melcher testified that PUI estimated Sensor's car count to be 1,225, but Mr. Pippin testified that the car count should actually be 1,035. This is a difference of 190 cars per day, or a 15% difference. Under the 10 gallon per car per day formula, this translates to Sensor being charged for an excess of 1,900 gallons of waste water per day and 57,000 gallons of waste water per month. This means Sensor would be required to pay for an excess of 4.75 SFEs per month, which at the rate of \$36 per SFE equates to an overcharge of \$171 per month.

PUI's estimates of cars at J-Ray's store cannot be a credible count in light of J-Ray's testimony concerning the actual counts based upon Mr. Valdes's personal knowledge. Accordingly, the only evidence upon which to base a decision is that provided by Mr. Valdes. To find contrary to Mr. Valdes's estimate would not be supported by substantial evidence and would be arbitrary and capricious.

CONCLUSION

Based upon the foregoing, Sensor and J-Ray respectfully request that this Court reverse the PSC and determine that the rates imposed by the PSC upon Sensor and J-Ray are unjust and unreasonable and remand to the PSC for further determination of the appropriate rate to be charged to commercial customers in the same category as Appellants.

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THE STATE OF SOUTH CAROLINA

In the Supreme Court

APPEAL FROM THE SOUTH CAROLINA PUBLIC SERVICE COMMISSION

PSC Docket No. 2013-42-S

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v.

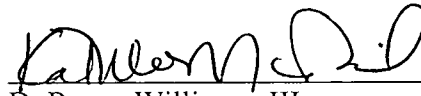
Palmetto Utilities, Incorporated and
South Carolina Office of Regulatory Staff..... Respondents

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I certify that I have served the Initial Brief of Appellants on the following parties by causing a copy to placed in the United States Mail, first-class postage affixed, addressed as follows, on March 21, 2014:

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