

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 2014-346-WS - ORDER NO. 2018-68
JANUARY 31, 2018

IN RE: Application of Daufuskie Island Utility)
 Company, Inc. for Approval of an Increase)
 for Water and Sewer Rates, Terms and)
 Conditions)

ORDER ON REHEARING

TABLE OF CONTENTS

<u>I.</u>	<u>INTRODUCTION</u>	2
<u>II.</u>	<u>REVIEW OF THE EVIDENCE AND EVIDENTIARY CONCLUSIONS</u>	11
	<u>Standards and Required Findings</u>	11
	<u>Test Year</u>	12
	<u>Rate of Return on Rate Base</u>	14
	<u>Capital Structure and Cost of Debt</u>	15
	<u>Cost of Equity/Return on Equity</u>	17
	<u>Rate Base</u>	20
	<u>Property Taxes</u>	28
	<u>Management Fees</u>	30
	<u>Rate Case Expenses</u>	36
	<u>Bad Debt Expense</u>	39
	<u>Deferral of \$155,328 for Future Rate Recognition</u>	41
	<u>Performance Bond</u>	42
	<u>Other Adjustments</u>	42
	<u>Income Taxes</u>	42
	<u>Refunds</u>	44
<u>III.</u>	<u>FINDINGS OF FACT</u>	44
<u>IV.</u>	<u>CONCLUSIONS OF LAW</u>	46
<u>V.</u>	<u>ORDER</u>	47
<u>VI.</u>	<u>COMMISSIONER BOCKMAN, CONCURRING</u>	50
<u>VII.</u>	<u>COMMISSIONERS FLEMING AND ELAM, DISSENTING</u>	51

I. INTRODUCTION

This rehearing is before the Public Service Commission of South Carolina (“Commission”) upon a remittitur from the South Carolina Supreme Court (“Supreme Court”).

Originally, the matter came before the Commission on the Application (“Application”) of Daufuskie Island Utility Company, Inc. (“DIUC” or “the Company”) filed on June 9, 2015, seeking approval of a new schedule of rates and charges for water and sewer service that DIUC provides to its customers within its authorized service area in South Carolina. The Application was filed pursuant to S.C. Code Ann. Section 58-5-240 and 10 S.C. Code Ann. Regs. 103-712.4.A and 103.512.4.A.

In the Application, DIUC requested to increase revenues for combined operations by \$1,182,301, consisting of a water revenue increase of \$590,454 and a sewer revenue increase of \$591,847. The proposed revenue increase utilized a return on equity (“ROE”) of 10.5% based on the rate of return on rate base methodology and a 2014 historical test year. Tariff changes to bring the rates between the Haig Point and Melrose communities to uniformity were also requested.

Prior to the filing of the Application in this Docket, DIUC’s last rate case before this Commission was in Docket No. 2011-229-WS. In that case, Commission Order No. 2012-515 approved a Settlement Agreement entered into by the Haig Point Club and Community Association, Inc. (“HPCCA”); Melrose Property Owner’s Association, Inc. (“MPOA”); Bloody Point Property Owner’s Association (“BPPOA”) (collectively the “POAs”); and DIUC that was not objected to by the South Carolina Office of Regulatory

Staff (“ORS”); whereby DIUC received a revenue increase of \$291,485 based on a \$5,000,000 rate base; an operating margin of 16.64%; and an ROE of 8.81%. DIUC also agreed not to seek another rate adjustment prior to July 1, 2014.

DIUC’s South Carolina operations are classified by the National Association of Regulatory Utility Commissioners (“NARUC”) as a Class B water and wastewater utility according to water and sewer revenues reported on its Application for the test year ending December 31, 2014. The Commission-approved service area for DIUC is on Daufuskie Island located in Beaufort County, South Carolina.

The Commission’s Clerk’s Office instructed DIUC to publish a prepared Notice of Filing, one time, in newspapers of general circulation in the area affected by DIUC’s Application. The Notice of Filing described the nature of the Application and advised all interested persons desiring to participate in the scheduled proceedings of the manner and time in which to file appropriate pleadings for inclusion in the proceedings as a party of record. The Commission also instructed DIUC to notify each affected customer by mailing or, where the customer had previously agreed to electronic notice, by e-mailing each customer a copy of the Notice of Filing. DIUC filed Affidavits of Publication and Mailing demonstrating that the Notice of Filing had been duly published and provided to all customers.

Petitions to Intervene were filed on behalf of the POAs on July 23, 2015, and Beach Field Properties, LLC (“Beach Field”) on July 27, 2015. Beach Field did not participate in the Company’s appeal of the original Commission decisions in this matter, nor in this Rehearing.

Subsequent to their intervention, the POAs requested the Commission schedule a public night hearing at a convenient time and location for customers of DIUC to present their comments regarding the service and rates of DIUC. In response, the Commission held a public night hearing pursuant to Order No. 2015-586. Under that Order, a public hearing was set and noticed by the Commission, and the Company provided an affidavit certifying that it had provided notice of the date, time, and location of the local public hearing via publication in *The Beaufort Gazette* and *The Island Packet*. On September 15, 2015, the Commission held a night hearing beginning at 6:00 pm at the Haig Point Club Clubhouse, 130 Clubhouse Lane, Daufuskie Island, South Carolina.¹

On October 28, 2015, the Commission, with Chairman Nikiya "Nikki" Hall presiding, heard the matter of DIUC's Application beginning at 10:30 am at the Commission Hearing Room located at 101 Executive Center Drive in Columbia, South Carolina.

DIUC was represented by G. Trenholm Walker, Esquire, and Thomas P. Gressette, Jr., Esquire. The POAs were represented by John J. Pringle, Jr., Esquire, John F. Beach, Esquire, and Lyndey Ritz Zwing, Esquire. Beach Field was represented by M. John Bowen, Jr., Esquire, and Margaret M. Fox, Esquire. ORS was represented by Shannon Bowyer Hudson, Esquire, and Andrew M. Bateman, Esquire.

At the October 28, 2015 hearing, a Settlement Agreement between the POAs and ORS was entered into the record after an objection to it by DIUC was overruled. DIUC,

¹ Hearing Exhibit 1 consists of the night hearing sign-in sheets and Hearing Exhibit 2 consists of comments filed by public witness Andy Mason.

the POAs and ORS presented testimony and exhibits after one public witness, Mr. Reid Delaney,² testified. Mr. Delaney testified that he owns property on which assets are located and utilized by DIUC for its regulated water and sewer business.

DIUC presented the testimony of: John F. Guastella³ (direct and rebuttal testimony), President of Guastella Associates, LLC (“GA”), a utility management, valuation and rate consulting firm headquartered in Boston, Massachusetts; Gary C. White (direct), Vice President and Director of Accounting at GA; Eric Johanson (direct), DIUC Chief Operator; and the Honorable Maria Walls⁴ (rebuttal), Beaufort County Treasurer. Mr. Guastella and Mr. White testified as a panel about the management and finances of DIUC. Mr. Johanson’s testimony addressed the operations of DIUC. Mr. Johanson was excused from the hearing without appearing before the Commission after his testimony was accepted into the record without objection from the other parties. Ms. Walls provided testimony on property taxes.

The POAs presented two panels of witnesses. The first panel consisted of Paul Vogel⁵ (direct), Haig Point Club and Community Association resident; Doug Egly⁶ (direct), Chief Operating Officer of the Haig Point Association; and Tony Simonelli (direct), real estate broker on Daufuskie Island. The second panel consisted of Lynn M.

² Hearing Exhibit 4 is a survey provided by Mr. Delaney.

³ Hearing Exhibit 7 consists of Guastella Direct Exhibits A and B. Hearing Exhibit 8 consists of Guastella Rebuttal Exhibits 1 through 5. Hearing Exhibit 9 is the GA Management Agreement. Hearing Exhibit 10 consists of the ORS and POAs responses to DIUC’s discovery requests.

⁴ Hearing Exhibit 5 consists of Walls Rebuttal Exhibit A.

⁵ Hearing Exhibit 11 is Vogel Exhibit 1.

⁶ Hearing Exhibit 12 is Egly Exhibit 1.

Lanier⁷ (direct) and Charles Loy⁸ (direct and surrebuttal), Principals of GDS Associates, Inc., a utility consulting and engineering firm with its principal offices in Marietta, Georgia; and Harry Jue⁹ (direct), water and sewer consultant with Hussey Gay Bell Engineering. POA witnesses Vogel, Egly, and Simonelli presented testimony illustrating the points of view of their respective organizations, and each providing various facts and opinions opposing DIUC's request. POA witness Loy provided testimony regarding accounting and rate base issues. POA witness Lanier provided testimony on the overall Application and incorporated Mr. Loy's recommended adjustments. Beach Field did not pre-file or present testimony or cross examine any witness at the Commission hearing.

ORS presented the testimony of Douglas H. Carlisle¹⁰ (direct), ORS Economist; Ivana C. Gearheart¹¹ (direct), ORS Audit Manager; and Willie J. Morgan¹² (direct and surrebuttal), ORS Deputy Director for the Water and Wastewater Department. Dr. Carlisle's testimony included an analysis and recommendation for an ROE. Ms. Gearheart's direct testimony described ORS's examinations of the Application and DIUC's books and records, as well as the subsequent accounting and pro forma adjustments recommended by ORS. Mr. Morgan's direct testimony focused on DIUC's compliance with Commission rules and regulations, ORS's business audit of DIUC's water and wastewater systems, test-year and proposed revenue, and performance bond requirements.

⁷ Hearing Exhibit 14 consists of Lanier Exhibits 1 through 5. Exhibit 3 was revised at the hearing.

⁸ Hearing Exhibit 15 is Loy Surrebuttal Exhibit 1. Hearing Exhibit 16 is Loy Direct Appendix A.

⁹ Hearing Exhibit 13 is Jue Exhibit 1.

¹⁰ Hearing Exhibit 17 is Carlisle Direct Exhibits 1 through 10.

¹¹ Hearing Exhibit 18 is Gearheart Direct Exhibits 1 through 8.

¹² Hearing Exhibit 19 is Morgan Direct Exhibits 1 through 8. Hearing Exhibit 20 is Morgan Surrebuttal Exhibits 1 and 2.

On December 8, 2015, this Commission issued Order No. 2015-846 approving the Settlement between the POAs and ORS and accepting the adjustments to rates laid out therein.

On December 21, 2015, counsel for DIUC filed a Petition for Reconsideration and/or Rehearing with the Commission. According to the Petition for Reconsideration and/or Rehearing, if DIUC were forced to implement the rates as established by the Settlement Agreement, it would default on its loan obligations and its ability to provide service would be threatened.

On January 20, 2016, DIUC filed a Petition for Bond Approval in which it notified the Commission that, pursuant to S.C. Code Ann. § 58-5-240, DIUC intended to put its originally requested rates into effect under bond during the pendency of its appeals.¹³

On February 25, 2016, the Commission issued Order No. 2016-50 denying DIUC's Petition for Reconsideration and/or Rehearing. In that Order, the Commission stated that the evidence presented by ORS in the original hearing was competent and credible. Additionally, the only adjustment put forth to the Commission as part of the Settlement Agreement that was not an ORS adjustment was DIUC's original bad debt adjustment, for which DIUC provided support in its Application.

On March 1, 2016, the Commission approved the proposed surety and bond in the amount of \$787,867, effective July 1, 2016, for a period of one year.¹⁴

¹³ While the Commission Order denying DIUC's Petition for Reconsideration and/or Rehearing was not issued until February 25, 2016, the Commission issued a Directive denying DIUC's Petition for Reconsideration and/or Rehearing on January 13, 2016.

¹⁴ Due to the length of the Appellate and remand process, a Joint Request was filed on June 15, 2017, by DIUC and the POAs that sought to extend DIUC's surety bond by an additional six months. This Commission issued an Order on June 30, 2017, approving the joint request.

On March 22, 2016, DIUC filed a Notice of Appeal with the Supreme Court in which DIUC appealed the decision and order of the Commission that approved the Settlement Agreement between the ORS and POAs.

On December 14, 2016, the Supreme Court held oral arguments between the Appellant, DIUC, and the Respondents, ORS and the POAs. On July 26, 2017, the Supreme Court issued its Order, reversing the Commission's Order and remanding the matter back to the Commission for a *de novo* hearing. In its opinion, the Supreme Court held that the Commission erred in approving and adopting the Settlement Agreement, and that DIUC is entitled to a new hearing in which the parties may present additional evidence. In addition, the Supreme Court gave guidance to the Commission on three matters: inclusion of the Elevated Tank Site in rate base, property tax expense, and bad debt expense.¹⁵

On August 11, 2017, the Supreme Court issued a remittitur, thereby remitting the matter back to the Commission.

On August 24, 2017, DIUC filed a Motion for Costs with the Supreme Court in which it sought attorney's fees and costs against Respondents in the amount of \$60,382.37.¹⁶

¹⁵ Despite the fact that this case was remanded to the Commission for a *de novo* hearing, the parties that participated in the rehearing primarily confined their testimony to previously unresolved issues and issues brought about by newly introduced evidence. Therefore, much of this Order's discussion on issues not litigated at the rehearing remains unchanged from the previous Commission Order.

¹⁶ Of the \$60,382.37, \$53,726 is attributable to bond premiums for bonds obtained pursuant to S.C. Code Ann. § 58-5-240(D), while the remaining, \$6,656.37 is attributable to Court fees, copy fees, and capped attorney's fees.

On November 15, 2017, the Supreme Court issued an Order on DIUC's Motion for Costs granting DIUC the amount of \$6,656.37 to be recovered against ORS, Haig Point Club and Community Association, Inc., Bloody Point Property Owner's Association, and Beach Field Properties, LLC. These costs were directed by the Supreme Court to be added to the remittitur. The Supreme Court's Order denied the \$56,726 amount for bond premiums that DIUC sought. On December 29, 2017, the Supreme Court issued its Amended Order on DIUC's Motion for Costs. The only difference in the Amended Order is that it removed Beach Field Properties, LLC as a party responsible for costs and added Melrose Property Owner's Association, Inc. as a party responsible for costs. The Amended Order was issued pursuant to a consent motion filed by the parties with the Supreme Court.

On December 6 and 7, 2017, the Commission, with Chairman Swain E. Whitfield presiding, heard the rehearing on the matter of DIUC's Application beginning at 10:30 am at the Commission Hearing Room located at 101 Executive Center Drive in Columbia, South Carolina.

At the rehearing, DIUC was represented by G. Trenholm Walker, Esquire, and Thomas P. Gressette, Jr., Esquire. The POAs were represented by John J. Pringle, Jr., Esquire, and John F. Beach, Esquire. Again, Beach Field did not participate in the rehearing. ORS was represented by Jeffrey M. Nelson, Esquire, and Andrew M. Bateman, Esquire.

At the rehearing, DIUC presented the testimony of: John F. Guastella¹⁷ (rehearing direct and rehearing rebuttal testimony) and Gary C. White¹⁸ (rehearing direct and rehearing rebuttal). Mr. Guastella and Mr. White testified as a panel about the management and finances of DIUC.

The POAs also presented its two witnesses as a panel. The panel consisted of Lynn M. Lanier¹⁹ (rehearing direct and rehearing surrebuttal) and Charles Loy²⁰ (rehearing direct and rehearing surrebuttal), Principals of GDS Associates, Inc., a utility consulting and engineering firm with its principal offices in Marietta, Georgia. POA witness Loy provided testimony regarding accounting and rate base issues. POA witness Lanier provided testimony on the overall Application and incorporated Mr. Loy's recommended adjustments.²¹

ORS presented the testimony of Douglas H. Carlisle (rehearing direct), ORS Economist; Daniel F. Sullivan²² (rehearing direct and rehearing surrebuttal), ORS Deputy Director of Auditing; and Dawn M. Hipp²³ (rehearing direct and rehearing surrebuttal), ORS Director for the Utility Rates and Services Department. Dr. Carlisle's testimony adopted and reaffirmed the positions taken in his direct testimony and exhibits, which were filed on October 2, 2015, and his oral testimony given to the Commission on October 28,

¹⁷ Rehearing Exhibit 1 consists of Guastella Direct and Rebuttal Exhibits.

¹⁸ Rehearing Exhibit 3 consists of White Direct and Rebuttal Exhibits.

¹⁹ Rehearing Exhibit 6 consists of Lanier Exhibits 1 through 7 corresponding to his rehearing direct testimony. Rehearing exhibit 7 consists of Lanier Exhibits Exhibit LML-8, corresponding to his rehearing surrebuttal testimony.

²⁰ Rehearing Exhibit 5 is Loy rehearing direct Exhibits 1 through 6.

²¹ At the hearing, the Commission overruled a DIUC objection to the introduction of the POAs witnesses' testimonies and exhibits.

²² Rehearing Exhibit 8 is Sullivan rehearing Direct Exhibits 1 through 9.

²³ Rehearing Exhibit 9 is Hipp rehearing Direct Exhibits 1 through 5. Rehearing Exhibit 10 is Hipp Surrebuttal Exhibit 1.

2015. Mr. Sullivan's rehearing direct testimony adopted the previously filed testimony of ORS witness Ivana C. Gearheart.

Additionally, Mr. Sullivan's testimony described ORS's examinations of the rehearing testimony and exhibits filed by DIUC in conjunction with the guidance provided by the Supreme Court in its Opinion No. 27729 and any accounting and pro forma adjustments recommended by ORS resulting therefrom.

Ms. Hipp's rehearing direct testimony adopted the direct testimony and exhibits of ORS witness Willie J. Morgan, and re-affirmed the positions taken by ORS witness Morgan during the hearing, with the exception of any changes made to comply with the guidance given by the Supreme Court. Additionally, Ms. Hipp presented ORS's findings and recommendations related to ORS's review of the rehearing testimony and exhibits filed by John Guastella and Gary White on behalf of DIUC and applicable discovery related to DIUC's rate case invoices, management fees, and requested deferral of \$155,328. Ms. Hipp's rehearing surrebuttal testimony responded to DIUC witness John Guastella's rebuttal testimony. Specifically, Ms. Hipp addressed ORS's recommendation to remove certain rate case expenses, a 5 year amortization period for recovery of rate case expenses, ORS's analysis of management fees, and DIUC's assertions regarding Guastella and Associates.

II. REVIEW OF THE EVIDENCE AND EVIDENTIARY CONCLUSIONS

Standards and Required Findings

DIUC's Application was filed pursuant to S.C. Code Ann. Sections 58-5-210 and 58-5-240 and 10 S.C. Code Ann. Regs. 103-712.4.A and 103.512.4.A. In considering the

Application originally and on rehearing, the Commission must ascertain and fix just and reasonable rates, standards, classifications, regulations, practices, and measurements of service to be furnished. Thus, the Commission must give due consideration to the Company's total revenue requirements and review the operating revenues and operating expenses of DIUC to establish adequate and reasonable levels of revenues and expenses. The Commission will consider a fair rate of return for DIUC based on the record and any increase must be just and reasonable and free of undue discrimination. DIUC has also asked this Commission to establish revenues based on an authorized ROE which is established to allow DIUC the opportunity to earn a fair return.

After discussion of the positions of the parties, the Commission reaches the legal and factual conclusions below based on its review of the facts and evidence of record.

The evidence supporting the Company's business and legal status is contained in the Application filed by DIUC, testimony, and in prior Commission orders in the docket files of the Commission, of which the Commission takes judicial notice. This finding of fact is informational, procedural, and jurisdictional in nature, and the matters which it involves are not contested by any party.

Test Year²⁴

With respect to the test year, DIUC utilized a historic test year – the twelve months ending December 31, 2014, with adjustments for 2015 expectations. ORS used the 2014 historical test year for two reasons: 1) because it was chosen by DIUC and 2) the underlying

²⁴At the rehearing, the Test Year was not actively litigated. As a result, the evidence relied upon in this section was primarily obtained during the October 28, 2015, hearing.

transactions in the 2014 books could be tested to ensure that the transactions were adequately supported, had a stated business purpose, were allowable for ratemaking purposes, and were properly recorded. Consistent with past practice and in accordance with generally accepted regulatory principles and prior Commission orders, ORS adjusted, as necessary, the revenues, expenditures, and capital investments to normalize the Company's operating experience and rate base. The POAs also utilized a 2014 historic test year with adjustments.

A fundamental principle of the ratemaking process is the establishment of a historical test year as the basis for calculating a utility's operating margin or, in this case, a return on rate base, and, consequently, the validity of the utility's requested rate increase. In order to determine what a utility's expense and revenues are for purposes of determining the reasonableness of a rate, one must select a 'test year' for the measurement of the expenses and revenues. *Heater of Seabrook v. Public Service Commission of South Carolina*, 324 S.C. 56, 478 S.E.2d 826, 828 n.1 (1996). While the Commission considers a utility's proposed rate increase based upon occurrences within the test year, the Commission will also consider adjustments for any known and measurable out-of-test year changes in expenses, revenues, and investments, and will also consider adjustments for any unusual situations which occurred in the test year. Where an unusual situation exists which shows that the test year figures are atypical, the Commission should adjust the test year data. *See Southern Bell v. The Public Service Commission*, 270 S.C. 590, 244 S.E. 2d 278 (1978); *see also, Parker V. South Carolina Public Service Commission*, 280 S.C. 310, 313 S.E.2d 290 (1984), *citing City of Pittsburgh v. Pennsylvania Public Utility Commission*,

187 P.A. Super. 341, 144 A.2d 648 (1958). Based on the information available to the Commission and that all parties agreed to a 2014 test year, the Commission is of the opinion, and therefore concludes, that the test year ending December 31, 2014, is appropriate for the purposes of this rate request.

Rate of Return on Rate Base²⁵

DIUC requested that its rates be determined in accordance with the rate of return on rate base methodology. The determination of rate of return on rate base requires three components: 1) capital structure; 2) cost of debt; and 3) cost of equity (or return on equity). However, by statutory requirement, the Commission must also specify an allowable operating margin in all water and wastewater orders. Although the Commission must specify an operating margin in its order, this does not mean that the operating margin methodology must be used in determining a fair rate of return. *Heater of Seabrook* at p. 64 and 830. Operating margin “is less appropriate for utilities that have large rate bases and need to earn a rate of return sufficient to obtain the necessary equity and debt capital that a larger utility needs for sound operation.” *Id.* No party actively contested the use of the rate of return on rate base methodology and given DIUC’s large rate base, the Commission finds the rate of return on rate base methodology appropriate in this case.

²⁵At the rehearing, the Rate of Return on Rate Base was not actively litigated. As a result, the evidence relied upon in this section was primarily obtained during the October 28, 2015, hearing.

Capital Structure and Cost of Debt²⁶

With respect to the capital structure, DIUC recommended a pro forma capital structure of 41.2% debt and 58.8% equity. During the October 28, 2015, hearing ORS witness Dr. Carlisle testified there are two concerns with the method DIUC used to calculate its capital structure: 1) DIUC included pro forma long-term debt in its long-term debt calculation; and 2) DIUC proposed an inflated equity amount. (October 28, 2015, Hearing Tr. p. 472, ll. 17-20). Dr. Carlisle noted that both result in an increase in the ROE. (Id.) The pro forma debt is based on the cost of debt DIUC expects, and as Dr. Carlisle noted, the outcome of DIUC's negotiations with banks or lenders is unknown at this time; therefore, DIUC's pro forma debt should not be included. (October 28, 2015, Hearing Tr. p. 473). The POAs also agreed that debt should not include future amounts. (October 28, 2015, Hearing Tr. p. 436, ll. 8-14). Dr. Carlisle further testified that DIUC's capital structure is weighted more heavily with equity, which is more expensive than debt. (Id.) In contrast to a projected or pro forma capital structure, ORS recommended a hypothetical capital structure of 46% long-term debt and 54% equity calculated by averaging the known capital structure used by water companies in the United States with publicly traded stock. (Id.) The POAs produced an adjusted capital structure of 57.55% debt and 42.45% equity (Hearing Exhibit 14, Amended Lanier Exhibit 3), based on a downward adjusted rate base, which is discussed later in this Order.

²⁶At the rehearing, the Capital Structure and Cost of Debt was not actively litigated. As a result, the evidence relied upon in this section was primarily obtained during the October 28, 2015, hearing.

As to the specific cost of debt rate, during the original hearing DIUC recommended 6.20%. The POAs testified that 6.20% is relatively high in the current interest rate environment, but is probably a reasonable rate given DIUC's precarious financial state. To calculate the 6.20% debt rate, DIUC included anticipated legal and GA fees in the financing fees. In support of the debt amount, Mr. Guastella testified that the debt he used is based on his knowledge of prior financing costs applied to the costs expected to be incurred for future refinancing. As a percentage of the total debt, the anticipated fees are 13.56% per ORS's calculations. ORS did not incorporate the additional fees into the debt rate because the fees are a large percentage of the total debt and did not originate from a lending institution. ORS recommended that the actual debt rate being paid by DIUC to the current lending institution, 5.29%, be used.

At the rehearing, Dr. Carlisle reaffirmed his previously recommended capital structure of 46% long-term debt and 54% equity. (Rehearing Tr. p. 433, ll. 1-2).

Upon consideration of evidence, the Commission adopts the capital structure, 46% long-term debt and 54% equity, and debt rate, 5.29%, recommended by ORS since they are based on known data instead of expected events. The Commission declines to use the POAs capital structure because it is based on a downward adjusted rate base (discussed in the Rate Base section below) that this Commission declines to use.

Cost of Equity/Return on Equity²⁷

At the October 28, 2015 hearing, DIUC witness Guastella testified that the requested 10.5% ROE is based on his experience and judgment. The POAs witness Lanier testified, “This is the same rate the Company requested in its 2012 rate case²⁸, which was a specified rate, rather than a rate developed through justification of the ROE required to meet its needs for profit margin and to attract the needed debt capital.” (October 28, 2015, Hearing Tr. p. 437, ll. 1-4). In contrast to DIUC, ORS’s Dr. Carlisle recommended an ROE of 9.31% based on a range of 8.91% to 9.71% using results from the Discounted Cash Flow model (“DCF”), Capital Asset Pricing Method (“CAP-M”) and the Comparable Earnings Model (“CEM”). (October 28, 2015, Hearing Tr. pp. 471 and 474). Dr. Carlisle testified the DCF and CAP-M are known and generally accepted methods for determining a recommended ROE. (Id.) The POAs testified that the DCF is the prevailing method used for determining appropriate ROEs. The POAs also testified that while the DCF and CAP-M are recognized as methods for calculating ROEs, the DCF and CAP-M provide challenges since there are not many publicly traded companies similar to DIUC. For his analyses, Dr. Carlisle examined data on companies with publicly traded stock of which more data is available, because DIUC requested rates based on rate of return. (October 28, 2015, Hearing Tr. p. 475). Companies with publicly traded stock yield more data than what is available for privately held companies. (Id.) Specifically, Dr. Carlisle testified that he used publicly traded companies classified as “water utilities” by Value Line or *Yahoo!*

²⁷At the rehearing, the Cost of Equity/Return on Equity was not actively litigated. As a result, the evidence relied upon in this section was primarily obtained during the October 28, 2015, hearing.

²⁸The merits hearing for DIUC’s last rate case in Docket No. 2011-229-WS was held in 2012.

Finance for his DCF and CAP-M since they are in the same line of business as DIUC and share similar risks. (Id.) For his CEM analysis, Dr. Carlisle used companies with comparable betas to those of the companies used in his DCF and CAP-M group. (Id.)

DIUC did not provide analyses similar to those used by Dr. Carlisle; however, Schedule A-3 of DIUC's Application shows the following references to ROE:

Connecticut DPUC Formula:

Average Large Company	9.69%
Small Company Adder	0.50%
Performance Adder	<u>0.50%</u>
	<u>10.69%</u>

Florida PSC Leverage Graph Formula:

$5.6\% + (2.279 / \text{Equity Ratio})$	= ROE
Range	100% = 7.88%
	40% = 11.30%
Equity Ratio	58.8% = <u>9.47%</u>

There is no discussion of these components in Schedule A-3 or testimony, with the exception of Mr. Guastella's rebuttal testimony containing the following single sentence, "Under the Connecticut Public Utilities Regulatory Authority formula for return on equity for small companies, the rate of return on equity for DIUC is 10.69%." ORS provided no testimony on either the Connecticut or Florida ROE formulas. The POAs could find no other reference to the Connecticut formula and challenged DIUC's portrayal of the Florida formula. Witness Lanier for the POAs testified, "[S]imply including a formula on a schedule and a calculated number is not sufficient rationale to support a ROE, particularly of 10.5%, when the company is requesting a revenue increase of over 100% in order to achieve such return." (October 28, 2015, Hearing Tr. p. 439, ll. 7-9). The POAs did not perform a DCF, CAP-M, or CEM analysis for determining a ROE and acknowledged Dr.

Carlisle as a source to support an appropriate ROE. In consideration of a lower rate base and based on various examples of DIUC's "irresponsibility in its operations since the rate increase authorized in 2012 and in the use of debt funds, in view of the critical need for cash," the POAs recommended an ROE in the range of 8.5% to 9.0% in pre-filed direct testimony. (October 28, 2015, Hearing Tr. p. 441, ll. 2-3).

In summary, at the October 28, 2015, hearing, DIUC requested an ROE of 10.5%; ORS recommended an ROE of 9.31% based on a range of 8.91% to 9.71%; and the POAs recommended an ROE in the range of 8.5% to 9.0%.

At the rehearing, Dr. Carlisle reaffirmed his previously recommended ROE of 9.31%. (Rehearing Tr. p. 430, l. 5).

Upon consideration of the various witnesses, the Commission adopts a rate of return on equity of 9.31% set forth in evidence as produced by ORS. ORS used the well-known and commonly-accepted DCF method, CAP-M, and CEM for developing a rate of return on equity of 9.31%, based on a range of 8.91% to 9.71%. Those methods, as applied by ORS, are grounded in sound analysis. While the POAs relied upon the testimony of Dr. Carlisle they recommended a ROE range falling below the low end of Dr. Carlisle's range. This Commission declines the range proposed by the POAs. The Commission finds DIUC's ROE recommendation lacking in support and analysis.

The fair rate of return on common equity which Daufuskie should be allowed the reasonable opportunity to earn is 9.31%, which is the rate of return adopted by the Commission for this proceeding. The capital structure and cost of capital which the

Commission has approved herein produce an overall rate of return of 7.46% for Daufuskie's water and wastewater operations as depicted in the following table:

Table A

<u>Component of Capital Structure</u>	<u>Ratio</u>	<u>Embedded</u>	<u>Overall</u>
		<u>Cost/Rate</u>	<u>Cost/Rate</u>
Long Term Debt	46%	5.29%	2.43%
Common Equity	<u>54%</u>	<u>9.31%</u>	<u>5.03%</u>
	<u>100%</u>		<u>7.46%</u>

Rate Base

At the October 28, 2015, hearing, the rate base proposed by DIUC for combined operations was \$7,085,475.²⁹ In support of its rate base, DIUC included several plant assets, particularly a 125,000 gallon elevated water storage tank, well and facilities (the "facilities") which are located on real property not owned by DIUC. Specifically, the facilities are located on real property (the "Site") that, as described below, was sold at a delinquent tax sale. DIUC does not dispute that it is not the owner of the Site. However, DIUC offered testimony and evidence that it owns these facilities, namely that 1) the tax sale did not include the storage tank, well and facilities, only the Site; 2) DIUC pays property taxes to Beaufort County for the facilities; 3) DIUC has the right to operate those facilities on any parcel of land in the Haig Point development; and 4) these facilities are

²⁹ See Application Schedule A-4; however the December 31, 2014 rate base total from Application Schedules W-B and S-B totals \$6,914,024.

“used and useful” in providing water service. (October 28, 2015, Hearing Tr. p. 195 and pp. 82-83). DIUC offered the testimony of the Beaufort County Treasurer who stated the Company is paying a utility tax on water system infrastructure. (October 28, 2015, Hearing Tr. p. 83).

At the October 28, 2015, hearing, both ORS and the POAs excluded the facilities from rate base. ORS testified that DIUC did not provide enough information for ORS to determine whether or not DIUC is the owner of those facilities. (October 28, 2015, Hearing Tr. p. 502 and p. 517).

In its Opinion No. 27729, the Supreme Court stated that on remand, when the Commission recalculates DIUC’s rate base, it should take into account DIUC’s ownership of the water tank, well, pipes, and other utility equipment located on the property sold at a tax sale in October 2010 to Mamdouh Sabry Abdelrahman (“Elevated Tank Site”).

In accordance with the guidance handed down by the Supreme Court, at the rehearing ORS added the water tank, pipes, and other utility equipment located on the Elevated Tank Site into DIUC’s rate base.

At the October 28, 2015, hearing, with respect to the overall rate base, the POAs recommended that DIUC’s as proposed rate base of \$7,085,475 be reduced by \$3,745,530 as a result of 1) increased accumulated depreciation, 2) contributions in aid of construction (“CIAC”) and 3) CIAC amortization. (October 28, 2015, Hearing Tr. p. 371). Witness Loy for the POAs testified that Generally Accepted Accounting Principles (“GAAP”) and appropriate regulatory accounting required that accumulated depreciation be calculated on a straight-line basis from the “in service” date through the end of the test year. (Id.) In

addition, Mr. Loy testified that an adjustment increasing accumulated depreciation “reflects the proper age and condition of the utility property.” (Id.) At the October 28, 2015 hearing, the POAs witness Mr. Jue echoed Mr. Loy’s conclusion, opining that the DIUC system “would be expected to reflect accumulated depreciation of approximately 30%.” (October 28, 2015, Hearing Tr. p. 362).

Mr. Loy also testified that certain DIUC plant purchased from Haig Point Utility Company (“HPUC”) should be classified as CIAC rather than invested plant. According to Mr. Loy, International Paper (the original owner of HPUC) and later Haig Point, Inc. (“HPI”) treated the utility plant in HPUC as inventory, expensed those costs, and donated those assets to HPUC. (October 28, 2015, Hearing Tr. p. 380). As support for this conclusion, Mr. Loy testified that HPUC Water Annual Reports for the years 2000-2003 showed no plant balances at all. (October 28, 2015, Hearing Tr. p. 381). According to the witness, the failure to classify plant as CIAC requires adjustments to both net plant and CIAC amortization. Mr. Loy also testified that the appropriate characterization of DIUC plant as CIAC would greatly reduce the DIUC property tax burden, both for back taxes (a reduction of \$402,108 for tax years 2011-2013) and in the test year (a reduction of \$115,995 for tax year 2014). (October 28, 2015, Hearing Tr. p. 396).

In sum, at the October 28, 2015, hearing, the POAs recommended adjustments, largely to net utility plant, accumulated depreciation, contributions in aid of construction, and accumulated amortization to CIAC that would reduce the rate base for combined operations to \$3,276,311.

At the rehearing, Witness Loy testified that DIUC's proposed rate base is overstated due to an erroneous \$4.6 million accounting adjustment. (Rehearing Tr. p. 308, ll. 11-13). He further testified that a large portion of DIUC's utility plant was donated, and thus DIUC had no original cost to pay for that plant; therefore, it was improper for DIUC to claim the cost of the utility plant to its balance sheet as paid in capital. (Rehearing Tr. p. 309, ll. 19-22, p. 310, ll. 1-2).

Additionally, Witness Loy testified that DIUC significantly overstated net plant by under recording accumulated depreciation. (Rehearing Tr. p. 308, ll. 17-18). According to witness Loy, the net plant values of DIUC are artificially high because plant representing excess capacity has not been depreciated according to NARUC guidelines, which require straight-line depreciation over the useful life of the plant in service. (Rehearing Tr. p. 308, ll. 17-20).

With respect to the overall rate base, the POAs recommended as part of their evidence in the rehearing that DIUC's rate base as proposed be reduced to \$2,304,944. This reduction resulted from a combination of 1) classifying donated plant as contributions in aid of construction ("CIAC") and 2) applying straight line depreciation to the Company's plant investment, thereby increasing accumulated depreciation and reducing net plant. See LML-R3, Schedule C-2, Rehearing Exhibit 6. (In addition, the POAs also pointed out that simply applying straight-line depreciation to the Company's plant causes an increase in accumulated depreciation and a corresponding decrease in net plant. This adjustment alone, according to the POAs, reduces combined rate base to \$4,613,231. See Exhibit LML-R8, Schedule C-2, Rehearing Exhibit 7.)

DIUC witness Guastella testified at the rehearing that the Company's accounting methodology has been relied upon by DIUC and other parties in the past, and that, in previous rate cases, the balance sheets have been determined to accurately reflect the books and records. (Rehearing Tr. pp. 102-103). According to witness Gaustella, there is no violation of the NARUC Chart of Accounts concerning how the utility reflected the actual cost of the utility and actual financial structuring of the utility, based on what typically happens with newly formed, developer-related utilities. (Rehearing Tr. p. 49). Guastella explains that in establishing a developer owned utility all of the construction costs and utility assets that had to be paid for by the developer are turned over to the utility in the form of an equity investment in the utility. (Rehearing Tr. p. 50). Guastella further explains that when an equity investment is made in a utility, it is not made in the form of a donation. (Rehearing Tr. p 51). Witness Guastella's arguments are supported by the NARUC Chart of Accounts, Accounting Instruction 18, which states that all amounts included in the accounts for utility plant acquired as an operating unit or system, shall be stated at the cost incurred by the person who first devoted the property to utility service.

The record in this case shows that International Paper (IP) was the developer of a residential golf community named Haig Point at Daufuskie Island, S.C. and that the net book value of their investment in the Haig Point development of \$13 million at June 30, 1997, was considered permanently impaired and written down to zero in its 1999 SEC Form 10-K. (Rehearing Tr. pp. 315-316.) According to witness Loy's testimony, at the time of IP's 1999 Securities Exchange Commission (SEC) filing, IP still owned Haig Point, Inc., whose assets continued to include the stock and plant of Haig Point Utility Company

(now renamed DIUC) (Rehearing Tr. p. 315.). The record shows that IP formed Haig Point Utility Company (now DIUC), and was therefore the first entity to devote its investment in utility plant and equipment to public service. It is irrelevant that IP wrote off its investment for SEC reporting purposes because the amounts in the books and records of the utility for ratemaking purposes may be different than the amounts reported to other agencies such as the SEC. The ORS has determined the correct amount of contributions in aid of construction for this case.

Witness White testified concerning utilization factors and provided an explanation of the utilization factor analysis. According to witness White, the utilization percentage is based on the number of active connections as a percentage of all potential connections for the system and has the effect of decreasing the depreciation rate and depreciation expense charged to the current customer. Therefore, current customers are only paying their fair share of depreciation expense. (Rehearing Tr. p. 120.) According to White, it is not a used and useful study that would determine the utilization of plant facilities. Those numbers do not indicate how much of the system is used and useful. (Rehearing Tr. p. 121). On cross examination, witness White explained that utilization factors are merely the percentage of customers currently connected to the system, versus the number of customers that could be connected to the system. (Rehearing Tr. p. 221.) Witness White further explained that availability fees are charged to customers to cover their cost of having facilities available. (Id.) Such fees are included as revenue in this case.

In contrast to the position taken by the POAs³⁰, ORS carried forward the amount of rate base from the last rate case in Docket No. 2011-229-WS, \$4,615,755, and made adjustments through December 31, 2014³¹. (October 28, 2015, Hearing Tr. p. 524). Using DIUC's utilization factor method with ORS's adjustments, and taking into account the Supreme Court guidance, ORS recommended that \$1,134,068 be deducted from the Company's December 31, 2014 Application rate base. (Rehearing Tr. p. 445-446, ORS Audit Exhibit DFS-1, Rehearing Exhibit 8). Of the amount deducted, \$699,361 is gross plant in service representing non-allowable plant, adjustments from the previous case not carried forward by DIUC in this Application, and asset retirements. (Id.) ORS Audit Exhibit DFS-5 (Rehearing Exhibit 8) shows the specific items composing the \$699,361. (Rehearing Tr. p. 453, ORS Audit Exhibit DFS-5, Rehearing Exhibit 8). ORS adjustments also deducted \$180,067 from rate base for accumulated depreciation and deducted \$254,853 from rate base for Construction Work in Progress ("CWIP"). (Rehearing Tr. p. 445-446, ORS Audit Exhibit DFS-1, Rehearing Exhibit 8). Accumulated amortization of CIAC added \$213 to the rate base to arrive at a total net rate base deduction of \$1,134,068. (Id.) When \$87,676 in working capital was added to rate base, the total net rate base reduction became \$1,046,392. (Id.) After deducting the rate base adjustment from the Application Schedules W-B and S-B December 31, 2014, per books rate base of \$6,914,024, ORS's recommended rate base for combined operations was \$5,867,632. (Id.)

³⁰ At the rehearing, ORS testified that while it found the POA methodology to be reasonable, it chose to follow the same carryforward method it utilized at the October 28, 2015 hearing, and in past rate cases.

³¹ For the carryforward amount, ORS used the rate base it calculated in the prior rate case instead of using the settlement agreement rate base in Docket No. 2011-229-WS.

In summary, on rehearing, DIUC's recommended adjusted rate base was \$7,085,475, the POAs' was \$2,304,944, and ORS's was \$5,867,632.

The POAs' arguments have some merit. However, considering the discussion above, the Commission declines to adopt a different rate base than the one carried forward from the last rate case by ORS, with some adjustments. The determination of rate base for this case is largely driven by the Applicant's need for an expedited evaluation of its case on remand, and the fact is that the burden was on intervenors to present a defensible alternative rate base proposal. While we do not believe that burden was met in this case, we do not preclude parties from proposing a different rate base in future rate proceedings, which they would be free to do in any event. This Commission may not rely solely on past practice in making its findings. See Porter v. S.C.P.S.C. and BellSouth Telecommunications, Inc., 333 S.C. 12, 507 S.E. 2d 328 (1998).

After reviewing the evidence presented by DIUC, ORS, and the POAs, the Commission accepts the rate base determination methodology and adjustments proposed by ORS. The ORS methodology accounts for the guidance given by the Supreme Court and is logical in its steps, and sets forth sound methods for determining a proper rate base on which a return may be granted.

The Commission hereby adopts the following as the Company's rate base for purposes of this proceeding:

Table B

Approved Rate Base

	<u>\$</u>
Gross Plant in Service	7,265,018
Less: Accumulated Depreciation	<u>(970,091)</u>
Net Plant in Service	6,294,927
Construction Work in Progress	0
Cash Working Capital	171,348
Contributions in Aid of Construction	<u>(590,813)</u>
Total Rate Base	<u>5,875,462</u>

Property Taxes

Since the last DIUC rate case in 2011, all parties agree that DIUC has property tax issues. DIUC did not pay 2009 and 2010 property taxes when due. As discussed above, DIUC's property was subject to a delinquent tax sale as a result. DIUC testified that Beaufort County mailed the tax bills to the wrong address. In addition, the Company's 2012, 2013, and 2014 Beaufort County property taxes were significantly higher than what they had been in years prior. At issue among the parties is how much property taxes should be paid by the ratepayers.

After learning about the delinquent taxes, DIUC and the Beaufort County Treasurer entered into a settlement agreement that was entered into evidence. The settlement agreement allowed DIUC to pay Beaufort County monthly payments of \$5,487.95 to cover property taxes totaling \$526,843.39 for 2012, 2013, 2014, and 2015. The Beaufort County Treasurer testified that the monthly payment was derived by amortizing the \$526,843.39 over eight years. Originally the amount was \$651,267.27, but the settlement agreement was amended to the reduced amount of \$526,843.39 after the SC Department of Revenue (“DOR”) submitted lower asset values to Beaufort County.

With respect to its property tax request in this case, DIUC requested additional annual property tax expense of \$65,856 for the 2012, 2013, 2014 and 2015 taxes and \$188,092 for the annual amount of taxes going forward. DIUC’s property tax expense request totaled \$258,158 (\$4,210 per books plus \$65,856 plus \$188,092).

At the October 28, 2015, hearing, the POAs recommended that DIUC’s tax expense be based on the POAs’ downward-adjusted rate base. ORS testified that DIUC’s current books reflected approximately \$4,000 annually for property taxes and, with the ORS adjustments, DIUC would have \$171,492 annually to pay property taxes. Specifically, ORS recommended that DIUC receive \$30,612 annually for the 2012 and 2013 taxes totaling \$244,899 amortized over 8 years and \$140,880 for the 2014 or test year taxes. ORS based its 2012 and 2013 adjustment amount and amortization period on DIUC’s settlement with Beaufort County. The 2014 adjustment was based on the actual tax bills/assessment. ORS witness Gearheart testified that ORS allowed amounts for the 2012 and 2013 taxes, because DIUC did not have an opportunity to request a rate increase to pay

the taxes after agreeing to a moratorium through July 1, 2014, in the settlement in Docket No. 2011-229-WS. ORS declined to allow property taxes for 2015 since ORS utilizes a historical test year.

In its Opinion No. 27729, the Supreme Court stated that an annual bill of \$65,856 is a substantial expense for which the Commission should have adjusted the test year data.

As a result of the guidance given by the Supreme Court, ORS computed an adjustment to amortization expense for property taxes of \$526,848 amortized over eight (8) years for an annual amortization of property taxes of \$65,856. (Rehearing Tr. p. 450, ll. 15-19). DIUC did not disagree with this approach taken by ORS and the resulting adjustment recommended by ORS. (Rehearing Tr. p. 450, ll. 18-19).

Additionally, based on guidance from the Supreme Court, ORS computed an adjustment to property taxes to reflect calendar year 2015 level. (Rehearing Tr. p. 451, ll. 1-5). Calendar year 2015 property taxes amounted to \$192,302 less the per book amount of \$4,210, for an adjustment to \$188,092. (Id.) DIUC agrees with this adjustment in its rehearing testimony and exhibits. (Rehearing Tr. p. 451, ll. 4-5).

Based on the evidence in the record and the guidance given by the Supreme Court, the Commission adopts the property tax amounts as computed by ORS as they are based on known and measurable amounts and incorporate the guidance given by the Supreme Court.

Management Fees

In its Application, DIUC requested \$171,365 for outside management services. As previously stated herein, DIUC has a contract with Guastella Associates LLC (“GA”) for

management services which was entered into evidence. *See* October 28, 2015, Hearing Tr. Hearing Exhibit 9. GA provides management, valuation, and rate consulting services to water and wastewater utilities around the country, and has been the contract manager of DIUC (and its predecessors) since July 9, 2008. The most recent management agreement dated June 18, 2015, states, and DIUC witness Guastella confirmed in testimony, that DIUC pays GA a management fee of \$13,596.85 per month with an annual 3.5% increase. (Id.)

The \$171,365 for management fees included in the Application reflect charges under the agreement between GA and DIUC and its owners. That agreement spells out GA's responsibilities and duties, and has provisions for fees and charges, including day-to-day management, finance, capital, and incentive fees. *See Id.*

In accordance with the management agreement, GA's scope of services include:

1. Supervise the day to day operation and maintenance of the Company's system, including supervision of operating employees, vendors and contractors.
2. Maintain books and records, including accounting, financial and operation records, in accordance with the uniform system of accounts prescribed by the PSC and required by the DHEC.
3. Perform all billing, accounting and collecting (other than commencing litigation), including the preparation of customer account records and billing analyses as necessary for rate filing requirements.
4. Prepare financial and operating reports to regulatory agencies, including annual reports to the PSC and monthly operating reports to DHEC. Prepare annual budgets and financial reports to stockholders, as well as periodic (quarterly) financial and operating reports.
5. Provide information and assistance to outside tax accountants, consultants, engineers and attorneys as required in the normal course of business.
6. Obtain short and long term financing, as available and necessary, for operations and capital improvements and prepare the necessary

documentation for lenders.

7. Employ and supervise all employees, vendors, contractors and outside professionals as appropriate to operate, maintain and expand the Company's system, to direct and supervise all plant expansion, capital improvements and replacements, and to carry out all other services required of GA under this Agreement.
8. Implement existing contracts with developers and customers, and negotiate and implement new contracts and applications for service.
9. Revise and maintain general tariff provisions as to rates and terms of service, in compliance with changes approved by the PSC.
10. Be responsible for and carry out all other business incidental to the ordinary course of business management and operation of the Company.

See Id.

ORS proposed to reduce the management fee to \$132,211, a level that it asserts the Commission previously approved.³² At the original hearing, ORS witness Gearheart asserted that the management services provided by GA did not increase from 2011. She testified, "During the review, ORS did not find that the management services provided by Guastella and Associates ("GA") increased and did not find the requested increase justifiable." *See* October 28, 2015, Hearing Tr. p. 493. This assertion does not consider that the specific term of the management agreement requires an annual increase of 3.5% per year and does not take into account any amount for inflation. *See Id.* at page 5 ("The Management Fee shall increase annually beginning on January 1 of each year this Agreement is in effect by ... 3.5%.").

Neither ORS nor Intervenors presented any performance analysis or any review of the events and issues faced by DIUC since it was acquired from Haig Point, Inc. in 2008.

³² The Commission did approve a settlement in DIUC's 2011 rate case, but the settlement does not make any reference to the management fee.

The Company, on the other hand, provided the Commission with a comprehensive Report on Capital Improvements that includes information regarding the various problems faced by the Company and how those problems were addressed by GA pursuant to its management agreement. *See Id.* In the original hearing, neither ORS nor Intervenor performed any analysis to evaluate whether the GA's management fees are competitive or whether DIUC could have obtained management with the same level of expertise as provided by GA at a lower cost. On the other hand, the record provides the following, *inter alia*, as obtained from Mr. Guastella's testimony and exhibits from October 28, 2015, regarding the work of GA for DIUC:

- The hiring of GA was required in the settlement with an intervenor for the purchase of the stock of HPUC from Haig Point, Inc. to assure that DIUC would have competent management. *See* Hearing Transcript at 213.
- GA directed the transition for the HPUC acquisition as well as the merger of MUC, improving records, billing and operations. *See* Hearing Transcript, Hearing Exhibit 7.
- GA managed the operations despite an immediate 25% annual shortfall of revenues because of MUC's failure to pay its share of the jointly owned wastewater treatment plant. *See* Hearing Transcript, Hearing Exhibit 7.
- GA directed the operation of MUC, when its owners abandoned the utility operations and filed for bankruptcy in order protect the MUC's customers from interruption of water and sewer service, without compensation and despite DIUC's cash shortage. *See* Hearing Transcript at 214.
- GA undertook an extensive effort over about a three year period trying to obtain financing, including about 15 months after the 2012 rate increase. *See* Hearing Transcript at 220.
- GA worked with the president of DIUC to use his contracting firm to make temporary repairs to the failed wastewater lagoon liner, when

there were insufficient funds to pay for the improvements. *See* Hearing Transcript, Hearing Exhibit 7.

- GA saved DIUC and its customers over \$350,000 in property taxes and another \$100,000 in present value savings related to the 8 year payment agreement. *See* Hearing Transcript at 213 and Hearing Exhibit 7.

In the original proceeding, the POAs opposed the requested management fees; however, they have not proposed a specific dollar adjustment for management fees. Mr. Lanier did state that he “would support any reductions in expenses proposed by the ORS staff,” however, this statement was made without providing any rationale, standard, or benchmark for any such reduction. *See* October 28, 2015 Hearing Tr. p. 435.

ORS witness Hipp raised the issue of checks and balances in the GA management agreement. In her rehearing testimony, Ms. Hipp states: “In addition, it is ORS's position that the management agreement lacks sufficient checks and balances to protect DIUC, its parent company and its ratepayers from decisions made by its vendor, GA.” (Rehearing Tr. pp. 477-478.) Ms. Hipp then goes on to cite the tax sale of the Elevated Tank Site, which DIUC continues to assert did not occur due to any fault of the utility or its management. This “checks and balances” argument is not persuasive. The ultimate check is the utility’s right to terminate the Management Agreement for cause if GA has failed to perform and to cure any deficiency in performance.

Ms. Hipp also presented Rehearing Exhibit DMH-5, which she asserted “indicates the dollar amount of management fees requested by DIUC are in excess of what other similarly situated investor-owned water and wastewater utilities pay for similar services.” (Rehearing Tr. p.478.) However, if this Commission is to make a comparison between utilities for the basis of a ratemaking decision, the party proposing the comparison must

provide enough facts for this Commission to prepare an order that is “sufficiently detailed to enable the reviewing court to determine whether the findings are supported by the evidence and whether the law has been properly applied to those findings.” *Heater of Seabrook, Inc. v. Pub. Serv. Commn. of S.C.*, 503 S.E.2d 739, 742 (S.C. 1998) citing *Able Communications, Inc. v. South Carolina PSC*, 290 S.C. 409, 411, 351 S.E.2d 151, 152 (1986).

ORS made no attempt to analyze the management services that GA has provided versus those provided by the management of Harbor Island Utility (“HIU”) or Kiawah Island Utility (“KIU”). Further, ORS did not show that DIUC is substantially similar to HIU and KIU, nor that the services provided under their management agreements are substantially similar to those of GA, nor that the challenges and conditions of the three utilities are substantially similar. Mr. Guastella’s rehearing rebuttal testimony regarding the differences between DIUC and HIU and KIU is persuasive. First, Mr. Guastella notes that HIU and KIU are not comparable to DIUC “just because they both provide water and wastewater service and are regulated by this Commission.” (Rehearing Tr. p. 16.) He then goes on to provide the following analysis:

- HIU only has about one-tenth of the cost of DIUC’s utility assets, it has no wells, no water treatment plant, and it is accessible by roadway-bridge.
- KIU has no source wells, no treatment plant, and only one wastewater plant, compared to DIUC’s operation of 7 wells outfitted with water treatment and pumping as well as ongoing operation by DIUC of two wastewater treatment plants.
- KIU has about ten times more customers than DIUC over which to spread costs.

- KIU's management fees are not limited to the \$365,095 shown in Rehearing Exhibit DMH-5. That \$365,095 amount is the amount affiliated corporations allocate to KIU, but day-to-day management of KIU is also provided by its direct, full-time employees. Those employee costs are not included in the amount Ms. Hipp is attempting to compare.

(Rehearing Tr. pp. 97-98.

Mr. Guastella's testimony and exhibits as to GA's qualifications and performance in managing DIUC are persuasive. We also acknowledge the unique location of this utility and the impact that has upon the costs of doing business, as explained by Mr. Guastella in his original testimony and during the rehearing.

The Commission finds the requested amount of \$171,365 to be reasonable and justified.

Rate Case Expenses³³

At the rehearing, DIUC requested \$794,210 for current and unamortized rate case expenses to be recovered over 3 years. (Rehearing Tr. p. 473, ll. 15-17). ORS proposed that rate case expenses total \$272,382 and be amortized over five years. (Rehearing Tr. p. 474, ll. 18-22, p. 476, ll. 21-22, p. 477, ll. 1-2). The \$272,382 consists of capped current rate case expenses in the amount of \$75,000 for GA's preparation of the Application³⁴, developing rate models, calculating test year data, filing other rate case documents and legal expenses. (Rehearing Tr. p. 450, ll. 8-14). ORS recommended \$75,000 as a

³³ Rate Case expenses were not specifically mentioned in South Carolina Supreme Court Opinion No. 27729; however, in keeping with the Court's Opinion, DIUC introduced new evidence that altered its original Rate Case expense request. As a result, this issue was litigated at the rehearing.

³⁴ The \$75,000 is a figure that was used in the previous hearing and was arrived at during settlement negotiations between the ORS and POAs.

reasonable amount for rate case expenses in the last rate case. Additionally, \$22,500 of the \$272,382 is unamortized rate case expenses from the previous rate case. The remaining amount is accounted for by legal services. (Id.)

At the rehearing ORS testified regarding a number of adjustments to rate case expenses that were not contested by DIUC. (Rehearing Tr. p. 86, ll. 4-7). The one rate case expense adjustment DIUC did contest at the hearing was ORS's adjustment of \$542,978, which corresponded to GA invoices. (Rehearing Tr. p. 476, l. 11). According to ORS witness Hipp, GA invoices contained mathematical errors, lacked sufficient detail, and/or did not appear to be paid. (Rehearing Tr. p. 476, ll. 11-18). ORS witness Hipp testified that, when reviewing invoices, ORS checks for mathematical accuracy, whether the invoice is for a valid business purpose, whether the expense was incurred during the period under review, whether the invoice was properly recorded on the books and records of the Company, and whether the invoice was paid. (Id.) ORS testified that generally the GA invoices failed this criteria, and also offered specific examples. (Rehearing Tr. p. 476, ll. 11-18, ORS DMH Surrebuttal Exhibit 1, Rehearing Exhibit 10). During her testimony ORS witness Hipp specifically cited a number of examples of invoices that were insufficient for reasons varying from lack of detailed description of work performed to mathematical errors. (ORS DMH Surrebuttal Exhibit 1, Rehearing Exhibit 10). Additionally, ORS witness Hipp attached an exhibit detailing the problems with each invoice for which ORS recommended an adjustment. (Id.) Furthermore, ORS witness Hipp testified that, on August 24, 2015, ORS discussed certain GA invoice deficiencies at an exit conference held with the Company. (Rehearing Tr. p. 486, l. 22, p. 487, ll. 1-3).

Finally, ORS witness Hipp testified that it is not the role of ORS to properly support the rate case of a company seeking a rate increase, and it was DIUC that failed to provide additional support for the work performed by GA. (Rehearing Tr. p. 487, ll. 4-9).

DIUC's witness Guastella testified that DIUC is seeking \$794,201.17, plus the \$60,781.56 incurred for the bonds and associated letter of credit, for rate case expenses. (Rehearing Tr. p. 76, ll. 8-12). According to DIUC witness Guastella, no regulatory agency has ever raised any questions about the amount of detail in GA's invoices. (Rehearing Tr. p. 87, ll. 16-17). Additionally, he testified that, without any notice, ORS suddenly declared GA's invoicing insufficient. (Rehearing Tr. p. 88, ll. 9-10). DIUC witness Guastella also testified that delayed payments which create accounts payable does not mean that costs incurred are not allowable for rate setting purposes. (Rehearing Tr. p. 89, ll. 19-21).

At the rehearing DIUC requested a 3 year amortization period for rate case expenses. (Rehearing Tr. p. 92, ll. 7-23). ORS affirmed its position that a 5 year amortization period is a reasonable balance between the shareholders and ratepayers for this proceeding. (Rehearing Tr. p. 476, ll. 21-22, p. 477, ll. 1-2). DIUC witness Guastella testified at the rehearing that a 5 year amortization period would mean that actual rate case expenses would not be fully recovered until January 2023. (Rehearing Tr. p. 92, ll. 20-21). ORS witness Hipp testified that the rate case amortization period should begin on July 1, 2016, which is the same date that DIUC chose to implement higher rates under bond. (Rehearing Tr. p. 490, ll. 13-18).

The Commission agrees with ORS that a rate case expense total of \$272,382 is a reasonable amount for this rate case. The evidence shows that a large sum of what DIUC

seeks was based on invoices that could not be verified. It is the responsibility of the regulated utility – not the Commission, ORS, or any other party – to support the operating expenses that contribute to the utility's revenue requirements. We cannot presume that the expenses a utility proposes to recover in its rates and charges are legitimate if they cannot be subjected to the scrutiny of an audit or examination. Porter v. SCPSC, 333 S.C. 12, 507 S.E. 2d 328 (1998). Moreover, the fact that no other regulatory agency has questioned the level of detail in GA's invoices cannot serve to cure the deficiencies that the evidence here reveals.

However, we will allow the Company to request approval of these expenses in its next rate case, if it can provide supporting information for its invoices that satisfy the criteria listed by ORS witness Hipp presented at the rehearing.

We disagree with the ORS proposal for a five (5) year amortization period of rate case expenses, since full recovery of rate case expenses would not occur until January 2023 under this schedule. We agree with the Company that a three (3) year amortization period provides a more reasonable recovery period. DIUC has been filing Applications for rate relief at approximately three-year intervals. (Rehearing Tr. p. 92, ll. 7-12) We do agree with ORS that the inclusion of unamortized rate case expenses from the last case is reasonable. See Porter v. S.C.P.S.C and Carolina Water Service, 328 S.C. 222, 493 S.E. 2d 92 (1997).

Bad Debt Expense

In its Application, DIUC proposed bad debt expense associated with its proposed increase in revenues to equal \$30,852. Initially, ORS provided testimony proposing to

adjust the bad debt expense upward to \$213,732. (October 28, 2015, Hearing Tr. p. 498). In the Settlement Agreement between the ORS and the POAs, and consistent with DIUC's request in its Application, ORS revised its adjustment to bad debt expense to utilize the methodology proposed by DIUC in its Application. (October 28, 2015, Hearing Tr. pp. 502-503). When discussing the bad debt expense, the Supreme Court stated that the evidence in the record establishes DIUC's bad debt expense to exceed \$100,000. In compliance with the Supreme Court's guidance, ORS applied its calculated bad debt percentage of 9.82% to DIUC's rehearing proposed increase to calculate an adjustment to bad debt expense of \$116,056, for a total bad debt expense of \$221,439. (Rehearing Tr. p. 453, ll. 16-20). Without expounding any further on the topic, DIUC witness Guastella stated that he disagreed with ORS adjustment to the bad debt expense. (Rehearing Tr. p. 84, l. 8).

The POAs' witness Lanier testified that ORS's evaluation of bad debts at the rehearing failed to fully analyze the Company's actual test year bad debt expense and failed to consider the prudence of the amount of \$105,667. (Rehearing Tr. p. 370, ll. 16-19). Therefore, witness Lanier proposes exactly what the Company included in its Application, 0.5% on water and sewer rate revenues and 2.5% on water and sewer availability revenues. (Rehearing Tr. p. 371, ll. 4-8).

We conclude the bad debt expense methodology performed by ORS, and the resultant bad debt percentage of approximately 9.82% by which to adjust the bad debt expense, is just and reasonable, reflects the actual bad debt expense incurred by DIUC, and complies with guidance handed down by the Supreme Court. This Commission hereby

adopts the ORS as adjusted bad debts amount of \$105,384. Applying the 9.82% bad debts percentage to the approved revenue increase of \$950,166 results in total bad debts expense of \$198,690.

Deferral of \$155,328 for Future Rate Recognition

DIUC seeks to have a deferral of \$155,328 for future rate recognition. (Rehearing Tr. p. 80, ll. 8-12). ORS testified that it believes that, to the extent DIUC has incurred recoverable rate case expenses, those expenses should be recovered in the case presently before the Commission. (Hipp Rehearing Revised p. 9, ll. 1-10). DIUC testified that the \$155,328 is the amount in excess of the 108.9% increase DIUC originally requested in its Application, and its recovery is necessary to make DIUC whole and delay a portion of the rate increase to the customers. (Rehearing Tr. p. 101, ll. 13-15).

The Commission concludes that the expenses properly incurred should be recoverable in the present case, to the extent allowable. Therefore, the Commission does not believe that \$155,328 should be deferred to a future rate case.

Customer Growth

The ORS proposed to adjust for customer growth after the proposed increase. The Commission agrees with the ORS that the effects of customer growth should be recognized. The effect on the operating results approved herein is \$1,529 using a composite growth rate of 0.35% applied to positive net operating income. The composite growth rate was determined by dividing the ORS recommended combined customer growth after the proposed increase of \$2,137 by the combined net operating income of \$614,109 contained on Revised Rehearing Audit Exhibit DFS-1

Performance Bond

DIUC is currently providing the maximum amount required for its performance bond in the amount of \$350,000 for water and \$350,000 for sewer operations. Using the criteria set forth in 10 S.C. Code Ann. Regs. 103-512.3.1 and 103-712.3.1, ORS recommended that DIUC be required to continue the current performance bond amounts. DIUC and the POAs did not challenge the performance bond amounts. Accordingly and pursuant to S.C. Code Ann. § 58-5-720 and 10 S.C. Code Ann. Regs. 103-512.3 and 103-712.3, the Commission requires that DIUC maintain its performance bond in the amount of \$350,000 for water and \$350,000 for sewer operations.

Other Adjustments

Although adjustments must be made to a number of items, as fallout adjustments under this Order, including cash working capital, the remaining ORS adjustments are accepted by this Commission without discussion. They either were not disputed by the parties or were caused by carrying out the effects of the adjustments adopted above.

Income Taxes

We take judicial notice of the fact that a 34% Federal Tax rate was applicable at the time of the rehearing in this matter. However, we would refer the Company to our requirements established under Docket No. 2017-381-A to determine a possible revision in the rate on a going forward basis.

The following table reflects Daufuskie's revenue and expenses after accounting and pro forma adjustments under presently approved rates for the test year:

Table C

Total Operating Revenue	\$1,073,577
Total Operating Expenses	<u>1,310,664</u>
Total Operating Income (loss)	(237,087)
Customer Growth	<u>0</u>
Net Income (loss)	<u>\$(237,087)</u>

Note: Interest Expense for Operating Margin purposes is \$142,973.

The following table illustrates the effect after accounting and pro forma adjustments and rates approved in this Order:

Table D

Total Operating Revenue	\$2,023,743
Total Operating Expenses	<u>1,586,921</u>
Total Operating Income (loss)	436,822
Customer Growth	<u>1,529</u>
Net Income (loss)	<u>\$438,351</u>

Note: Interest Expense for Operating Margin purposes is \$142,973.

Refunds

DIUC placed its originally requested rates into effect under bond while its rate case was on appeal, as allowed under S.C. Code Ann. Section 58-5-240 (2015). Since this Order results in less additional revenue than would have resulted under approval of the originally requested rates in this case, refunds to the DIUC's customers are in order, pursuant to the terms of the same statute. The Company must refund to its customers the difference between the amount of additional revenue allowed by this Order, and the full amount of additional revenue originally requested by the Company, along with 12% interest. These amounts must be calculated from the date that the Company placed its originally requested rates into effect under bond.

III. FINDINGS OF FACT

1. DIUC is a water and sewer utility providing water and sewer service in its assigned service area on Daufuskie Island, Beaufort County, South Carolina. The Commission is vested with authority to regulate rates of every public utility in this state and to ascertain and fix just and reasonable rates for service. S.C. Ann. § 58-5-210, *et. seq.* DIUC's operations in South Carolina are subject to the jurisdiction of the Commission.

2. DIUC requested in its Application to increase revenues for combined operations by \$1,182,301, consisting of a water revenue increase of \$590,454, and a sewer revenue increase of \$591,847, based on the rate of return on rate base methodology utilizing an ROE of 10.5% and a 2014 historical test year. At the rehearing, DIUC re-affirmed that it sought the Application's originally proposed revenue requirement of \$2,267,721.

3. The appropriate test year period for this proceeding, selected by the Company, is January 1, 2014, through December 31, 2014.

4. The Commission will use the return on rate base methodology in determining and fixing just and reasonable rates.

5. The return on rate base methodology requires three components: capital structure, cost of debt, and cost of equity (or return on equity).

6. The Commission adopts the capital structure of 46% long-term debt and 54% equity; a cost of debt rate of 5.29%; and ROE of 9.31%. The approved return on rate base is 7.46%.

7. The Commission sets DIUC's rate base at \$5,875,462

8. The Commission-approved revenues and expenses establish a fair and reasonable operating margin of 14.60%. S.C. Code Ann. § 58-5-240(H).

9. For certain rate case expenses, DIUC failed to provide invoices that could be verified; as a result, DIUC is ineligible for cost recovery of those expenses at this time. However, the Company may reapply for recognition of these expenses in its next rate case, if its invoices meet the criteria established by ORS.

10. A three (3) year amortization period for rate case expenses is a reasonable balance between DIUC's shareholders and the ratepayers. Additionally, the amortization period began running on the date which DIUC first implemented its higher rates.

11. A bad debt percentage of 9.82% applied to the revenue requirements approved herein is a reasonable and appropriate manner of calculating DIUC's bad debts.

12. The deferral of \$155,328 is not appropriate where it could reasonably be recovered in a future rate case.

13. Refunds must be made to DIUC's customers, consisting of the difference between the amount of additional revenue allowed by this Order and the full amount originally requested by the Company, together with 12% interest. These amounts must be calculated from the date the Company placed its originally requested rates into effect under bond.

IV. CONCLUSIONS OF LAW

Based upon the Discussion, Findings of Fact as set forth herein, and the record of the instant proceeding, the Commission makes the following Conclusions of Law:

1. DIUC is a public utility as defined in S.C. Code Ann. § 58-5-10(3) and as such is subject to the jurisdiction of this Commission.

2. The appropriate test year on which to set rates for DIUC is the twelve month period ending December 31, 2014.

3. Based on the information provided by the parties, the Commission concludes the appropriate rate setting methodology to use as a guide in determining the lawfulness of DIUC's proposed rates and for the fixing of just and reasonable rates is return on rate base.

4. In order for DIUC to have the opportunity to earn the 9.31% ROE, which is found fair and reasonable herein, DIUC must be allowed additional revenues of \$950,166.

5. The Commission sets the amount to be recovered for management fees at \$171,365.

6. The Commission concludes that the appropriate amount to be recovered for rate case expenses is \$272,382.

7. The Commission concludes that the appropriate amortization period to recover rate case expenses is 3 years.

8. The Commission concludes that the appropriate bad debt expense adjustment is 9.82% of the revenue requirement.

9. The Commission concludes that DIUC cannot defer the \$155,328 requested for future rate recognition.

10. Pursuant to S.C. Code Ann. § 58-5-720 and 10 S.C. Code Ann. Regs. 103-512.3 and 103-712.3, DIUC shall post a performance bond of \$350,000 for water and \$350,000 for sewer operations.

11. Pursuant to S.C. Code Ann. § 58-5-240(D), “[a]ll increases in rates put into effect under the provisions of this section which are not approved and for which a refund is required shall bear interest at a rate of twelve percent per annum. The interest shall commence on the date the disallowed increase is paid and continue until the date the refund is made. In all cases in which a refund is due, the Commission shall order a total refund of the difference between the amount collected under bond and the amount finally approved.”

V. ORDER

IT IS THEREFORE ORDERED THAT:

1. The Company shall design and file rates that produce the revenue increase granted in this Order. The Company shall also file a schedule with the Commission demonstrating that the rate design produces the revenue granted in this Order. The

Company shall serve these documents on the other parties to this case, who shall verify with this Commission that said rates are consistent with the provisions of this Order.

2. Appeal costs in the amount of \$6,656.37 will be shared equally between ORS, Haig Point Club and Community Association, Inc., Melrose Property Owner's Association, Inc. and Bloody Point Property Owner's Association, and paid to DIUC.

3. The Company is to provide thirty (30) days' advance notice of the increase to customers of its water and wastewater services prior to the rates and schedules being put into effect for service rendered. The schedules shall be deemed to be filed with the Commission pursuant to S.C. Code Ann. § 58-5-240.

4. A return on equity of 9.31% and operating margin of 14.60%, based on the new rates, fees, and charges, is approved for DIUC.

5. The Company shall continue to maintain current performance bonds in the amounts of \$350,000 for water operations and \$350,000 for wastewater operations pursuant to S.C. Code Ann. § 58-5-720.

6. The Company shall implement all Commission-approved adjustments on its books and records.

7. The Company's books and records shall be maintained according to the NARUC Uniform System of Accounts. The Company is directed to make any necessary adjustments to its accounting system, including the use of straight line depreciation without utilization factors, to conform to the NARUC Uniform System of Accounts.

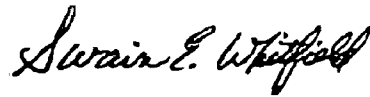
8. The Company shall refund the difference between the amount it collected under bond and the amount this Commission approves herein to the customers that paid

the excessive rates at an interest rate of twelve percent per annum. The interest commenced on the date the disallowed increase was paid and continues until the date the refund is made.

9. The Company shall comply with any order of the Commission in Docket No. 2017-381-A, and conform its taxes going forward to the appropriate Federal Tax rate.

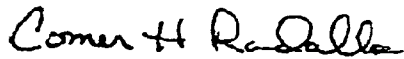
10. This Order shall remain in full force and effect until further order of the Commission.

BY ORDER OF THE COMMISSION:



Swain E. Whitfield, Chairman

ATTEST:

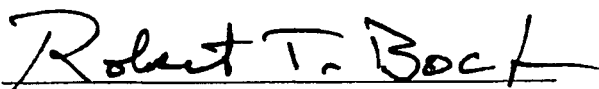


Comer H. Randall, Vice Chairman

VI. Commissioner Bockman, concurring:

I concur in the findings of fact and conclusions of law which the Commission has reached, which I agree produce rates and charges for DIUC which are just and reasonable. I write separately only to comment with respect to the Commission's discussion and decision of one matter relating to the determination of DIUC's rate base.

The Commission's discussion of the parties' evidence and arguments concerning issues relating to rate base is clear and comprehensive. In my view, the adoption of \$5,867,632 for DIUC's rate base is consistent with the evidence in this rehearing on remand and in the original hearing in 2015 and with the guidance in the Supreme Court's opinion. In Order No. 2015-846, the Commission adopted ORS's methodology for the calculation of DIUC's rate base to be appropriate for rate-making purposes and in the public interest. In addressing the issue of rate base, the Supreme Court directed the Commission on remand to recalculate DIUC's rate base, taking into account certain facilities, which the Commission has done here. I see no compelling reason to do anything other than that. The Commission's extensive discussion of the POAs' approach to calculating rate base and its recognition that the POAs' arguments "have some merit" neither constitute error in the Commission decision to adopt ORS's proposed rate base nor undermine the reasoning for that decision. Moreover, as the Commission here pointedly recognizes, nothing in this Order would preclude any of the parties from advancing different positions in future proceedings in which sufficient probative evidence and application of relevant principles of law might lead to some other result.


Robert T. Bockman

VII. Commissioners FLEMING and ELAM, dissenting:

We respectfully dissent and would adopt the rate base proposed by the POAs in this rehearing.

Prior settlement agreements and Commission orders in DIUC's past rate and stock transfer proceedings have stated that there was no binding conclusion reached on the appropriate rate base. Therefore, the instant case represents the Commission's first opportunity to establish the Company's rate base in a fully contested case.

The majority opinion fully discusses the evidence of record in this case concerning the appropriate rate base to be used in setting DIUC's rates in this case. It further agrees with the assessment of the ORS, in its testimony and in its proposed Order, that the recommendation of the POAs to exclude all donated property from rate base has merit. At the rehearing, ORS testified that while it found the POAs methodology to be reasonable, it chose to follow the same carryforward method it utilized at the October 28, 2015 hearing, and in past cases.

The POAs have presented compelling evidence as to the appropriate value of the rate base in this proceeding. Indeed, DIUC witness Guastella admitted in the Rehearing (Rehearing Tr. p. 50-51) that Haig Point (the predecessor company to DIUC) did not pay anything in exchange for the plant assets in question. Therefore, we believe the Commission should accept the adjustments to rate base as proposed by the POAs, or at a minimum, their proposal regarding depreciation expense.

South Carolina Code Regulations, Reg. 103-517 for sewer and Reg. 103-719 for water, require utilities to keep all books and records in accordance with the NARUC

Uniform System of Accounts (USoA). Contrary to USoA Accounting Instruction 18, “*Utility Plant – To Be Recorded at Cost*” Part D, DIUC erroneously booked the donated “Property Plant and Equipment” by crediting “Paid-in Capital” (Note 8 of Loy Exhibit CEL-R2, Rehearing Exhibit 5) instead of Contributions in Aid of Construction (CIAC). The NARUC USoA requires that entries to utility plant accounts for plant donated to the utility must be offset by credits to CIAC. NARUC defines CIAC as “[a]ny amount or item of money, services or property received by a utility, from any person or governmental agency, any portion of which is provided at no cost to the utility, which represents an addition or transfer to the capital of the utility, and which is utilized to offset the acquisition improvement or construction costs of the utility’s property, facilities, or equipment used to provide utility services to the public.” (Emphasis added). Section 271(A). (Rehearing Tr. p. 312, ll. 18-26). Whether the investment is called an equity investment or paid-in-capital, as opposed to a CIAC does not change the fact that the utility was provided the plant at no cost, and should therefore be treated as CIAC for ratemaking purposes.

While the majority opinion does not explicitly make such a finding, it appears the Commission is effectively waiving its regulations to reach its result. While the Commission has the authority to waive these regulations pursuant to Reg. 103-501(3) and 103-701(3), we do not believe it is appropriate in this case. With regard for sewer utilities, Reg. 103-501(3) states that:

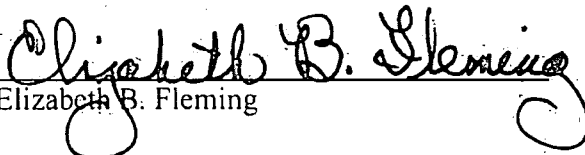
In any case where compliance with any of these rules and regulations introduces unusual difficulty or where circumstances indicate that a waiver of one or more rules or regulations is otherwise appropriate, such rules or regulations may be waived by the

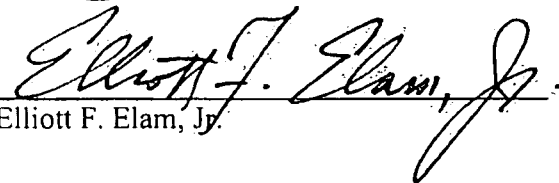
commission upon a finding by the commission that such waiver is not contrary to the public interest.

The same provisions are contained in Reg. 103-701 (3) for water. Accurately establishing the value of a utility's rate base is one of the most basic items the Commission must consider in setting just and reasonable rates. A utility with the ratemaking experience of DIUC should have no difficulty in complying with this requirement.

The majority's acceptance of the ORS rate base results in an excessive increase in customers' rates, which is clearly not in the public interest. Therefore, we believe any waiver is not appropriate in this case.

We respectfully dissent.


Elizabeth B. Fleming


Elliott F. Elam, Jr.