BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 94-304-W - ORDER NO. 94-1279

DECEMBER 21, 1994

IN RE: Application of Upstate Heater Utilities, Inc. for Approval of an Increase in its Water Rates and Charges.	) ORDER DENYING) INCREASE) IN RATES) AND CHARGES

I.

INTRODUCTION

This matter comes before the Public Service Commission of South Carolina (the Commission) on the July 11, 1994 Application of Upstate Heater Utilities, Inc. (the Company or Upstate) for approval of a new schedule of rates and charges for water service provided to its customers in its service area in South Carolina. This Application was filed pursuant to S.C. Code Ann. §58-5-240 (1976, as amended) and 26 S.C. Regs 103-821 (1976).

By letter, the Commission's Executive Director instructed the Company to cause to be published a prepared Notice of Filing, one time, in a newspaper of general circulation in the area affected by the Company's Application. The Notice of Filing indicated the nature of the Company's Application and advised all interested parties desiring participation in the scheduled proceeding of the manner and time in which to file the appropriate proceedings. The Company was likewise required to directly notify all customers affected by the proposed rates and charges. The Company furnished affidavits demonstrating that the Notice had been duly published

in accordance with the instructions of the Executive Director and certified that a copy of the Notice had been mailed to each customer affected by the rates and charges proposed in the Company's Application. Petitions to Intervene were filed on behalf of the Consumer Advocate for the State of South Carolina (Consumer Advocate), Thomas J. Studebaker, Daryl E. Lewis, and Chester G. Kapp.

The Company's presently authorized rates and charges were approved by Order No. 92-350, dated May 13, 1992, in Docket No. 91-095-W. According to Upstate's Application, the proposed rates and charges would increase water revenue by approximately $71,309.

The Commission Staff (the Staff) made on-site investigations of the Company's facilities, audited the Company's books and records, and gathered other detailed information concerning the operations. The Consumer Advocate likewise conducted discovery in the rate filing of Upstate as did the Intervenor Chester G. Kapp.

A public hearing relative to the matters asserted in the Company's Application was commenced on December 7, 1994 in the Commission's Hearing Room. A public night hearing was held on the evening of November 28, 1994. Pursuant to S.C. Code Ann. §58-3-95 (Supp. 1993), a panel of three Commission members composed of Chairman Mitchell, presiding, and Vice-Chairman Butler and Commissioner Bradley, was designated to hear and rule on this matter. Darra W. Cothran, Esquire, represented the Company; Elliott F. Elam, Jr., Esquire, represented the Consumer Advocate; Thomas J. Studebaker and Chester G. Kapp appeared pro se; and F. David Butler, General Counsel, represented the Commission Staff.

The Intervenor Daryl E. Lewis did not appear.

The Company presented the testimony of William E. Grantmyre, President of the Company, Jerry H. Tweed, Director of Environmental and Regulatory Affairs, and Freda Hilburn, Director of Rates. The Consumer Advocate presented the testimony of Philip E. Miller, Accountant. Chester G. Kapp presented testimony. The Commission Staff presented the testimony of Bruce Hulion, Public Utilities Accountant, and Charles A. Creech, Chief of the Commission's Water and Wastewater Department, to report Staff's findings and recommendations. Nineteen witnesses and three public officials appeared to testify at the night hearing.

II.

FINDINGS OF FACT

Based upon the Application, the testimony and exhibits received into evidence at the hearing, and the entire record of these proceedings, the Commission now makes the following findings of fact:

1. Upstate Heater Utilities, Inc. is a water utility providing water service in its service areas within South Carolina, and its operations in South Carolina are subject to the jurisdiction of the Commission, pursuant to S.C. Code Ann.§58-5-10, et seq. (1976, as amended).

2. The appropriate test period for the purposes of this proceeding is the twelve-month period ending March 31, 1994.

3. By its Application, the Company is seeking an increase in its rates and charges for water service of $71,309 which Staff has calculated to be $71,836.

4. The appropriate per book operating revenues for the Company for the test year under present rates are $364,341.

5. The appropriate operating expenses for the Company's South Carolina operations for the test year per book under its present rates is $308,087.

6. The Company's appropriate level of net operating income for return per books is $56,864.

7. A year end, original cost rate base per books of $792,313 should be adopted.

8. The Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates and the fixing of just and reasonable rates.

9. A fair operating margin that the Company should have the opportunity to earn is 1.19% which is produced by the appropriate level of revenues and expenses found reasonable and approved herein.

10. The rate designs and rate schedules approved by the Commission as described herein are appropriate and should be adopted.

11. The rates and charges depicted in Appendix A, attached herein, and incorporated by reference, are approved and effective for service rendered on and after the date of this Order.

III.

EVIDENCE AND CONCLUSIONS

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1.

The evidence supporting this finding concerning the Company's business and legal status is contained in the Company's Application

and in prior Commission Orders in the docket files of which the Commission takes notice. This finding of fact is essentially informational, procedural, and jurisdictional in nature, and the matters which it involves are essentially uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 2 AND 3.

The evidence for these findings concerning the test period and the amount of the revenue increase requested by the Company is contained in the Application of the Company and the testimony and exhibits of the Company's witnesses.

The Company's filing was based on a test period consisting of the twelve months ending March 31, 1994. The Commission Staff and the parties of record herein likewise offered their evidence generally within the context of that same test period.

A fundamental principle of the ratemaking process is the establishment of a test year period. The Commission finds the twelve months ending March 31, 1994, to be the reasonable period for which to make its ratemaking determinations herein.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4.

The evidence for the findings concerning the level of operating revenues is found in the testimony and exhibits of Company witness Hilburn and Commission Staff witness Hulion. For purposes of this proceeding, the appropriate operating revenues for the Company for the test year under the present rates per book is $364,341. Using the Commission's Finding of Fact No. 9 and the Evidence and Conclusions, infra., approving a 1.19% operating margin, the Company's per book operating revenues shall remain at $364,341.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 5, 6, AND 7.

Operating expenses per book for the test year were $308,087 as reflected in the testimony of Company witness Hilburn and Staff witness Hulion. The Commission, at this time, approves no adjustments, since it hereby holds that the per book figures correctly reflect operating revenues and operating expenses. Therefore, the total operating expenses for the test year per book of $308,087 are hereby approved in this proceeding. The Company's appropriate level of net operating income for return per books is $56,864.

The Company's rate base is determined by the Commission to be appropriate for the purposes of this proceeding is set forth as follows:

TABLE B

ORIGINAL COST RATE BASE

March 31, 1994

Gross Plant in Service	$ 1,200,336
Accumulated Depreciation	(195,642)
Net Plant in Service	1,004,694
Meters & Supplies	9,811
Cash Working Capital	31,028
Contributions in Aid of Construction	(224,214)
Accumulated Deferred Income Taxes	(29,006)
TOTAL RATE BASE	$ 792,313

Again, the Commission adopts the per book numbers since we believe these correctly reflect the Company's rate base in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 8, 9, 10, AND 11.

Under the guidelines established in the decisions of Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679 (1923), and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944), this Commission does not ensure through regulation that a utility will produce net revenues. As the United States Supreme Court noted in the Hope Natural Gas decision, supra, the utility "has no constitutional rights to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." However, employing fair and enlightened judgment and giving consideration to all relevant facts, the Commission should establish rates which will produce revenues "sufficient to assure confidence in the financial soundness of the utility and...that are adequate under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, supra, at 692-693.

Neither S.C. Code Ann. §58-5-290 (1976) nor any other statute prescribes a particular method to be utilized by the Commission to determine the lawfulness of the rates of a public utility. For ratemaking purposes, this Commission examines the relationships between expenses, revenues, and investment in an historic test period because such examination provides a constant and reliable factor upon which calculation can be made to formulate the basis for determining just and reasonable rates. This method was recognized and approved by the South Carolina Supreme Court for

ratemaking purposes involving utilities in Southern Bell Telephone and Telegraph Co. v. The Public Service Commission of S.C., 270 S.C. 590, 244 S.E.2d 278 (1978).

For water utilities, where the utility's rate base has been substantially reduced by customer donations, tap fees, contributions in aid of construction, and book value in excess of investment, the Commission may decide to use the "operating ratio" and/or "operating margin" as guides in determining just and reasonable rates, instead of examining the utility's return on its rate base. The operating ratio is the percentage obtained by dividing total operating expenses by operating revenues. The obverse side of this calculation, the operating margin, is determined by dividing net operating income for return by the total operating revenues of the utility.

The Commission finds that its use of the operating margin has resulted in fair rates to both the utility and ratepayer. In this proceeding, the Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates and the fixing of just and reasonable rates. This method was recognized as an acceptable guide for ratemaking purposes in Patton v. South Carolina Public Service Commission, 280 S.C. 288, 312 S.E.2d 257 (1984).

The following Table indicates the Company's gross revenues for the test year under the presently approved schedules; the Company's operating expenses for the test year; and the operating margin under the presently approved schedules for the test year.

TABLE B

Operating Revenues	$ 364,341
Operating Expenses	308,087
Net Operating Income (Loss)	56,254
Add: Customer Growth	610
Total Income for Return (Loss)	56,864
Operating Margin (After Interest)	1.19%

The Commission is mindful of those standards delineated in the Bluefield decision, supra, and of the balance between the respective interests of the Company and of the consumer. The Commission has considered the spectrum of relevant factors in this proceeding: the revenue requirements for the Company, the proposed price for which the Company's service is rendered, the quality of that service, and the effect of the proposal upon the consumer, among others.

The three fundamental criteria of a sound rate structure have been characterized as follows:

> ...(a) the revenue-requirement or financial-need objective, which takes the form of a fair-return standard with respect to private utility companies; (b) the fair-cost apportionment objective which invokes the principle that the burden of meeting total revenue requirements must be distributed fairly among the beneficiaries of the service; and (c) the optimum-use or consumer rationing under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is economically justified in view of the relationships between costs incurred and benefits received.
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> Bonbright, Principles of Public Utility Rates (1961), p. 292.

The Commission has considered the proposed increase presented by the Company in light of the various standards to be observed and the interests represented before the Commission. The Commission has also considered the impact of the proposed increase on the

ratepayers of the Company.

The Commission must balance the interests of the Company -- the opportunity to make a profit or earn a return on its investment, while providing adequate water service -- with the competing interests of the ratepayers -- to receive adequate service at a fair and reasonable rate. In balancing these competing interests, the Commission has determined that the proposed schedule of rates and charges is unjust and unreasonable and inappropriate for both the Company and its ratepayers.

We think that the case of Seabrook Island Property Owners Association v. South Carolina Public Service Commission, et. al., ___ S.C. ___, 401 S.E.2d 672 (1991) must be strongly considered in the case at bar. That case indicates that during the process of approving rates which are just and reasonable, the Commission must consider the price at which the Company's services are rendered and the quality of that service. Pursuant especially to the night hearing held in Anderson, South Carolina, on November 28, 1994, we conclude that the quality of service of Upstate Heater Utilities, Inc. is deficient. Numerous witnesses appeared before the Commission complaining about poor quality water. The difficulties with the water were many: large quantities of iron, calcium and other chemical deposits present in the water, a mud color which cannot be cleaned out of sinks and other water receptacles, peculiar smell, staining of clothes, and bad taste. During the hearing, Jerry H. Tweed, Director of Environmental and Regulatory Affairs for the Company, attempted to answer the concerns of the customers who testified at the night hearing. However, Tweed

admitted in his testimony that Upstate is going to study the conversion of three systems presently supplied by wells to all purchased water, due to customer testimony received at the hearing. The Company has, therefore, admitted that the quality of the water in a number of its systems is poor. Under these conditions, the Commission does not find that any increase is appropriate for this Company. In light of those factors as previously discussed, and based upon the record in the instant proceeding, the Commission concludes that a fair operating margin that the Company should have an opportunity to earn is 1.19% which requires annual operating revenues of $364,341. The Following table reflects an operating margin of 1.19%:

TABLE C

Operating Revenues	$ 364,341
Operating Expenses	308,087
Net Operating Income	56,254
Add: Customer Growth	610
Total Income for Return	58,864
Operating Margin (After Interest)	1.19%

The Commission finds that the present rate structure is appropriate based on the findings already discussed herein. This rate structure appears in Appendix A attached hereto. The Commission finds that the rates and charges approved herein achieve a balance between the interests of the Company and those of its customers. These rates and charges result in a reasonable attainment of the Commission's ratemaking objectives in light of applicable statutory safeguards.

IT IS THEREFORE ORDERED THAT:

1. The proposed schedule of rates and charges by the Company

is found to be unreasonable and is hereby denied.

2. The schedule of rates and charges attached hereto as Appendix A is hereby approved for service rendered on or after the date of this Order. The schedule is deemed to be filed with the Commission pursuant to S.C. Code Ann.§58-5-240 (1976), as amended.

3. The Company shall maintain its books and records for water operations in accordance with the NARUC Uniform System of Accounts for Class B Water Utilities, as adopted by this Commission.

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

BY ORDER OF THE COMMISSION:

Rudolph Mitchell
Chairman

ATTEST:

Gary E. Walsh
Deputy Executive Director

(SEAL)

APPENDIX A

UPSTATE HEATER UTILITIES INC.
P.O. Drawer 4889
Cary, N.C. 27519
(919) 467-7812

FILED PURSUANT TO DOCKET NO. 94-304-W - ORDER NO. 94-1279
EFFECTIVE DATE: DECEMBER 21, 1994

THE SCHEDULE OF WATER RATES AND CHARGES ARE AS FOLLOWS:

METERED RATES (PER SINGLE FAMILY EQUIVALENT):

Basic Facility Charge (monthly)	-	$ 8.75
Commodity Charge (per 1,000 gal.)	-	$ 2.60
Water Reconnection Charge	-	$ 30.00
New Customer Account Charge	-	$ 22.00

One time fee charged to each account to defray cost of initiating service.

* Tap fee	-	$500.00

* The full gross up will be added to the tap fee.