

**IN THE SUPREME COURT OF APPEALS
OF WEST VIRGINIA
CHARLESTON**

JEFFERSON UTILITIES, INC.,

Petitioner,

v.

No. 11-0505

**PUBLIC SERVICE COMMISSION OF WEST VIRGINIA;
HOMEOWNERS ASSOCIATIONS OF BRECKENRIDGE,
DEERFIELD, GAP VIEW, MEADOWBROOK, SHERIDAN ESTATES,
AND BRIAR RUN; CITIZENS FOR FAIR WATER, INC.; AND
KAY MOORE, SCOTT TATINA AND REGINA FITE, INDIVIDUALS,**

Respondents.

**STATEMENT OF THE RESPONDENT PUBLIC
SERVICE COMMISSION OF WEST VIRGINIA
OF ITS REASONS FOR THE ENTRY OF ITS ORDER
OF FEBRUARY 18, 2011, IN CASE NOS.
10-00974-W-PC AND 10-1329-W-42T**

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April 25, 2011

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AND CASE NO. 10-1329-W-42T**

**TO THE HONORABLE JUSTICES OF THE SUPREME COURT
OF APPEALS OF WEST VIRGINIA:**

The Respondent, Public Service Commission of West Virginia (hereinafter "Commission"), hereby tenders for filing with this Honorable Court this statement of its reasons for the entry of its Order of February 18, 2011, in Case No. 10-0974-W-PC and Case No. 10-1329-W-42T.

STATEMENT OF THE CASE

Jefferson Utilities, Inc. ("JUI" or "Utility") petitioned for appeal of the Commission Order entered on February 18, 2011, in Case Nos. 10-0974-W-PC and 10-1329-W-42T ("2010 Rate

Order”). This petition for appeal challenges the 4.4 percent increase granted to JUI and the Commission’s refusal to approve, *at this time*, certain affiliate agreements between JUI and Snyder Environmental Services (“SES”).

By its holdings, the Commission rejected JUI’s extraordinary and excessive request for a 72 percent rate increase. The Commission set rates for JUI customers based upon demonstrated costs and a fair return, in accordance with West Virginia Code §§ 24-1-1(a)(4), 24-2-3 and 24-2-4a. After the Commission approved JUI’s 4.4 percent increase in these cases, JUI ranks the 17th highest out of 397 water utilities in the State based on 4,000 gallons of usage and the 19th highest for 4,500 gallons of usage for monthly water bills. See, West Virginia Public Service Commission “Water Utility Cost Ranking” (April 15, 2011).¹

The Commission’s refusal in this rate case to approve the affiliate agreements between JUI and SES, and the large rate impacts associated with those agreements, was proper because JUI failed to meet its burden under W.Va. Code § 24-2-12(f) to demonstrate that: (i) the agreements are reasonable, (ii) the affiliates had not exercised an undue advantage over JUI, and (iii) the customers of JUI were not adversely affected.

JUI is a privately held water public utility authorized to provide service to several areas of Jefferson County. On June 30, 2010, in Case No. 10-0974-W-PC-42T, JUI filed revised tariffs reflecting requested increased rates and charges of approximately \$998,657, for furnishing water service to approximately 2,196 customers in Jefferson County, to become effective August 1, 2010. The requested revenue represented an increase of approximately 72.2 percent in rates before

¹This information is available on the internet at the Public Service Commission of West Virginia Website: www.psc.state.wv.us Reports and Publications, Water Utility Rankings in WV.

application of a previously approved \$12 per month surcharge per customer. 2010 Rate Order p. 1. For an average residential JUI customer using 4,500 gallons per month, the water bill would have increased from \$56.34 to \$88.34, including the \$12 surcharge.

JUI also petitioned for approval of an operation and maintenance agreement and certain real property leases with affiliates. JUI and SES are both owned by, operated by, and affiliates of Lee Snyder. SES is a construction utility and environmental management company headquartered in Kearneysville, West Virginia. The maintenance agreement is between JUI and SES, and the lease agreements are between Lee and Cynthia Snyder, JUI, Snyder, LLC (Lee Snyder is the only member) and SES. 2010 Rate Order p.3. JUI has only one employee, Lee Snyder, (the owner of SES), and receives all of its operation and maintenance services from SES.

The Commission held the initial rate filing of JUI to be deficient because it did not provide accurate notice (Tariff Form No. 8), detailing the effect of the requested rate change on various classes of customers, as required by the Commission's Rules for the Construction and Filing of Tariffs, 150 C.S.R. 2 (2002) ("Tariff Rules"). The rate filing was dismissed, but Case No. 10-0974-W-PC-42T was re-designated as a petition for consent and approval to consider the affiliated operation and maintenance agreement and the affiliated lease agreements (Case No. 10-0974-W-PC).

JUI subsequently made a new rate filing for an increase in rates and charges that was designated as Case No. 10-1329-W-42T. 2010 Rate Order p. 2. In that filing, JUI requested increases based on average water usage by customer class as follows:

Before \$12 per Month Surcharge:

Class	Monthly Increase	Percentage Increase
Residential	\$28.95	72.2%
Commercial	\$63.67	72.2%
Governmental	\$422.61	72.1 %
Bulk	\$306.69	72.2%

In addition to these increases in volumetric rates, each customer would be required to pay a \$12.00 monthly surcharge.

By Order issued October 6, 2010, the Commission consolidated Case Nos. 10-0974-W-PC and 10-1329-W-42T; suspended the JUI tariff until February 19, 2011; established a filing date for the Staff audit report and recommendations in Case No. 10-1329-W-42T and its report and recommendations regarding the affiliate agreements in Case No. 10-0974-W-PC; and referred the consolidated cases to the Division of Administrative Law Judges (ALJ Division) for decision no later than January 7, 2011.

In Case No. 10-0974-W-PC, JUI requested Commission approval of a Revised Operation and Maintenance Agreement (Revised O&M Agreement), pursuant to which JUI's affiliate, SES, would continue to provide operation and maintenance services for JUI's utility systems. JUI operates eight water utility systems in Jefferson County: Walnut Grove, Meadowbrook, Shenandoah Junction, Burr/Bardane, Deerfield, Keyes Ferry Acres, Westridge Hills, and Harpers Ferry Campsites. The first five water systems are sometimes referred to collectively as the Valley Systems; while the last three water systems are sometimes referred to collectively as Mountain Systems. SES provides construction, utility and environmental management services to JUI's utility systems pursuant to eight separate operation and maintenance agreements. Although these eight agreements had been used in prior rate proceedings, JUI argued that these eight agreements are now inadequate and should

be replaced by the Revised O&M Agreement because the eight agreements do not accurately reflect the costs of goods and services provided to those systems by SES.

JUI also sought Commission approval of four lease agreements (Leases) relating to an office building at 270 Industrial Boulevard, Kearneysville, West Virginia, and two lots on which the building (“Snyder Building”) is located (lots 16 and 17). Under the first lease, Lee and Cynthia Snyder, affiliates of JUI, would lease Lot 16 to JUI. 2010 Rate Order p.3. Under the second lease, Snyder LLC, an affiliate of JUI, would lease Lot 17 to Lee and Cynthia Snyder, also affiliates of JUI. Under the third lease, Lee and Cynthia Snyder, affiliates of JUI, would sublease Lot 17 to JUI. Under the fourth lease, JUI and SES (affiliates) would share and allocate the costs of certain office space and expenses related to the leased property. Id.

Because of large prior rate increases² and lingering issues with quality of service³, the ratepayers of the JUI systems have been active in recent JUI filings in the last several years. (I Tr. p. 246).⁴ A large number of protests have been submitted and numerous interventions have been granted by the Commission in JUI formal proceedings.

In JUI’s last rate case, the Commission authorized a total revenue increase of \$503,684. That revenue increase, including the impact of the surcharge (\$12.00 per customer per month times 2100

²In JUI’s most recent rate case *preceding* these filings, Jefferson Utilities, Inc., Case No. 08-0544-W-42A (Commission Order, December 21, 2009) (“JUI 2008 Rate Order”), a tremendous number of protests were received. Numerous homeowners’ groups and the Jefferson County Commission participated as intervenors in that rate proceeding.

³For example, in Case No. 03-2019-W-PC-T, Jefferson Utilities, Inc. (Commission Order September 30, 2007), JUI was unsuccessful in developing a plan to lift a moratorium on new customer connections in the Westridge Hills and Keys Ferry Acres water systems.

⁴The transcript of the first day of hearing will be referred to as “I Tr.,” and the transcript of the second day of hearing will be referred to as “II Tr.”

customers), resulted in the following percentage increases for ratepayers across the eight water systems:

<u>JUI System</u>	<u>Number of customers</u>	<u>Percentage Rate Change Effective Dec. 21, 2009</u>
Walnut Grove	1,146	108.5%
Meadowbrook	352	7.2%
Shenandoah Junction	262	63.3%
Burr/Bardane	71	101.9%
Deerfield	34	(6.8%)
Harpers Ferry Campsites	152	40.9%
Keys Ferry Acres	131	14.3%
Westridge Hills	80	40.9%

That Final Order was entered on December 21, 2009, and just eight months later JUI filed a second rate case (the case on petition for appeal) seeking an additional rate increase of 72 percent. Given those two events the Commission, understandably, received a large number of protests in the two cases that are the subject of the current petition for appeal. The Commission received petitions to intervene in this rate case from the County Commission of Jefferson County (“Jefferson Commission”); the Homeowners Associations of Breckenridge, Deerfield, Gap View, Meadowbrook, Sheridan Estates, and Briar Run; and Citizens For Fair Water, Inc. (collectively, the “Citizens”). 2010 Rate Order p. 5.

The ALJ convened the hearing on December 1, 2010, in Ranson, West Virginia, as scheduled and heard statements from fifteen JUI customers and the testimony of nine witnesses. The ALJ considered briefs filed by JUI, Citizens and Staff, and reply briefs filed by JUI and Citizens.

On January 7, 2011, the ALJ issued a recommended decision addressing the various issues in contention and recommended a revenue increase to JUI of \$310,946, or an additional increase in rates of approximately 22.4 percent and a continuation of the previously approved \$12 per month

surcharge. The ALJ recommended that the Revised O&M Agreement be approved for a three-year term and recommended that the Commission not approve the Leases.

In advance of exceptions being filed by any party, on January 12, 2011, the Commission on its own motion, entered an Order stating it would review the recommended decision. More specifically, the Commission observed that the recommended decision failed to include a schedule reflecting the derivation of the revenue requirement, or a reconciliation of the dollar difference, between the recommendations filed by Commission Staff and the recommended decision. The Order required Staff to file a post-hearing exhibit setting forth a revenue requirement schedule consistent with the recommended decision and reconciling the dollar difference, on an issue-by-issue basis, between the Staff recommendations and the recommended decision.

Even though it received a 22.4 percent rate increase under the recommended decision, JUI filed exceptions asserting that the ALJ erred by: denying its request for approval of affiliate Leases; sunsetting the Revised O&M Agreement in three years (nothing in the Revised O&M Agreement provides for a three-year sunset); denying inclusion of Mr. Snyder's requested salary in cost of service; denying JUI's share of actual building expenses in cost of service; adopting a tariff rule with a typographical error; and miscalculating the rate of unmetered customers.

Staff also filed exceptions asserting that the ALJ erred in the decisions on rent allocation; approval of the O&M Agreement; approval of \$86,926 in rate case expense; and adoption of JUI's position on accumulated depreciation.

The Citizens filed exceptions asserting that the ALJ erred in the decision allowing any rent allocation to JUI; approving the O&M Agreement; allowing tank painting expense; and approving \$86,926 in rate case expense.

On February 18, 2011, the Commission after a review of the record and all exceptions, entered its final order: 1) disapproving the Revised O&M Agreement between SES and JUI; 2) disapproving the four Lease agreements filed by JUI; 3) initiating a General Investigation, Case No. 11-0235-W-GI, of JUI's utility operations, including the Revised O&M Agreement and the proposed four Leases for JUI; 4) approving an annual salary expense of \$40,000 for Mr. Snyder in the total revenue requirement; 5) denying JUI's request for tank painting as unsupported based on historical data; 6) finding JUI's request for Commission fees to be in error; 7) adopting the Staff recommendation for rate case expense; 8) adopting an amount agreed to by JUI for depreciation; 9) denying JUI's request to modify accumulated depreciation that JUI had previously used for ratemaking purposes; 10) modifying language relating to JUI Supplemental Tariff Rules; and 11) as requested by JUI, correcting a tariff rate for Non-Metered Customers.

On March 21, 2011, the Petitioner filed its Petition for Appeal of the Commission's February 18, 2011 Order with this Court essentially asserting the Commission should have upheld the exact same recommended decision on which it had earlier filed exceptions with the Commission.

SUMMARY OF ARGUMENT

The Commission fulfilled its statutory mandates consistent with W.Va. Code §§ 24-1-1(a)(4), 24-2-3 and 24-2-4a, and properly exercised its ratemaking authority by establishing rates for JUI based upon the demonstrated costs, including a fair rate of return, for providing water service to the 2,196 customers of the eight JUI water systems. The Commission reviewed the evidence presented and determined that an annual increase to JUI of \$66,324 (equating to a 4.4 percent increase over current rates) would adequately compensate JUI. The Commission also continued the \$12.00 surcharge for all customers approved in the JUI 2008 Rate Order.

The Commission gave reasoned consideration to the evidence presented by both JUI and the Staff on particular rate issues including, insurance premiums, rent, rate case expense, depreciation and officer salary. The Commission entered appropriate findings of fact and conclusions of law based upon the record.

Under its statutory authority, the Commission may grant its prior consent and approval for a utility to enter into agreements with an affiliates “upon proper showing by the utility that the terms and conditions thereof are reasonable and that neither party thereto is given an undue advantage over the other, and do not adversely affect the public in this state.” W. Va. Code §24-2-12. After consideration of the evidence and the arguments of the various parties in this proceeding, the Commission Order properly held that JUI has failed to make the “proper showing” that the Revised O&M Agreement and the four Leases with JUI’s affiliates met the statutory test and denied its consent and approval to enter into these five agreements.

The Commission initiated a General Investigation in Case No. 11-0235-W-GI of JUI’s utility operations to further evaluate the Revised O&M Agreement and the proposed four Leases. As a result of the Commission’s expressed concern for the magnitude of the current rates and the level of rate increase requested by JUI, the Commission will also consider in the general investigation whether JUI customers should continue to be served by the SES or whether JUI should employ its own utility personnel. The Commission will also evaluate JUI’s long-term plans to operate and rehabilitate its utility facilities. The Commission will examine JUI’s stated possibilities regarding private-public agreements. 2010 Rate Order p. 7. Further inquiry in these areas is clearly supported by the interests of JUI current and future ratepayers.

STATEMENT REGARDING ORAL ARGUMENT AND DECISION

Oral argument is necessary pursuant to R. App. P. 14(k): “The date for oral argument under Rule 19 or Rule 20 will be set forth in the scheduling order. Unless otherwise provided by order, the petitioner, the Commission and any respondent who filed a brief shall be entitled to present argument.”

STANDARD OF REVIEW

The authority for review of a Final Order of the Public Service Commission by the Supreme Court of Appeals of West Virginia is set forth in W. Va. Code §24-5-1, which provides in part:

Any party feeling aggrieved by the entry of a final order by the commission, affecting him or it, may present a petition in writing to the supreme court of appeals, or to a judge thereof in vacation, within thirty days after the entry of such order, praying for the suspension of such final order.

In the process of reviewing a Commission Order, this Court is guided by the well established holdings set forth in Sexton v. Public Service Commission, 188 W. Va. 305, 423 S.E.2d 914 (1992) and Monongahela Power Company v. Public Service Commission, 166 W. Va. 423, 276 S.E.2d 179 (1981). In Syllabus Point 1 of Sexton this Court reiterated previous holdings: “[A]n order of the public service commission based upon its findings of facts will not be disturbed unless such finding is contrary to the evidence, or is without evidence to support it, or is arbitrary, or results from a misapplication of legal principles.” (citations and quotation marks omitted). In Monongahela Power Company, this Court adopted the comprehensive standard of review applied by many states and set forth in Permian Basin Area Rate Cases, 390 U.S. 747 (1968):

In reviewing a Public Service Commission order, we will first determine whether the Commission’s order, viewed in light of the relevant facts and of the Commission’s broad regulatory duties, abused or exceeded its authority. We will examine the manner in which the Commission has employed the methods of regulation

which it has itself selected, and must decide whether each of the order's essential elements is supported by substantial evidence. . . The Court's responsibility is not to supplant the Commission's balance of these interests with one more nearly to its liking, but instead to assure itself that the Commission has given reasoned consideration to each of the pertinent factors.

Monongahela Power Company, Syllabus Point 2 (in relevant part).

This Court summarized its three-pronged analysis in Monongahela Power Company in Syllabus Point 1 of Central West Virginia Refuse, Inc. v. Public Service Commission, 190 W.Va. 416, 438 S.E.2d 596 (1993) as follows:

The detailed standard for our review of an order of the Public Service Commission contained in Syllabus Point 2 of Monongahela Power Co. v. Public Service Commission, 166 W.Va. 423, 276 S.E.2d 179 (1981) may be summarized as follows: (1) whether the Commission exceeded its statutory jurisdiction and powers; (2) whether there is adequate evidence to support the Commission's findings; and (3) whether the substantive result of the Commission's order is proper.

Similarly, in Chesapeake and Potomac Telephone Company v. Public Service Commission, 171 W.Va. 494, 300 S.E.2d 607 (1982), this Court began by repeating the three-pronged standard of review established in the Monongahela Power Company case, *supra*, and went on to hold that "[t]his Court will not substitute our judgment for that of the Public Service Commission on controverted evidence". Chesapeake, Syllabus Point 2. This Court further held that "[f]indings of fact made by the Public Service Commission will be overturned as clearly wrong when there is no substantial evidence to support them." Chesapeake, Syllabus Point 3.

STATEMENT OF REASONS AND NOTE OF ARGUMENT

I. THE COMMISSION HAS FULFILLED ITS STATUTORY MANDATES IN ESTABLISHING JUST AND REASONABLE RATES FOR JUI CUSTOMERS BASED ON THE COST OF PROVIDING WATER SERVICE

In its Petition, JUI claims the Commission improperly rejected findings of fact and conclusions of law in the recommended decision and failed to make its own independent findings and conclusions. Interestingly, JUI is so zealous in its support of the ALJ's recommendations it appears to abandon its own original proposed rate request, seeking almost \$1 million dollars (equivalent to an approximate 72 percent increase to average customers), in favor of the ALJ recommendations for an annual revenue increase of \$310,946 or a 22.4 percent increase for average customers.

While the Commission may refer matters to an ALJ, the Commission is not required to accept, in whole or in part, the ALJ's rulings. The ALJ's order is a recommended decision. By W.Va. Code §24-1-1(a), the Legislature conferred upon the Commission "[t]he authority and duty to enforce and regulate the practices, services and rates of public utilities" In order to fulfill its regulatory function, the Commission is empowered with the authority to designate other employees to conduct hearings and render recommended decisions; however, the ultimate authority to render decisions remains with the Commission. In accordance with W.Va. Code § 24-1-9(d) after the filing of a recommended decision, "[t]he commission, after review, upon the whole record, or as supplemented by a further hearing, shall decide the matter in controversy and make appropriate order thereon." Further, subsection (e) provides that even when no exceptions are taken to a recommended decision the Commission on its "own motion" may review any such matter and take action thereon as if exceptions thereto had been filed. In Harrison Rural Electrification Association, Inc., v. Public

Service Commission, 190 W.Va. 439, 438 S.E.2d 782 (1993), the Court reviewed a final order of the Commission, in which exceptions had been filed and the Commission made findings of fact and conclusions of law different from those recommended by the ALJ. The Court held that it would not substitute its judgment for that of the Commission on controverted evidence and that findings of fact by the Commission will only be overturned as clearly wrong when there is no substantial evidence to support them.

On the rate issues presented to the Court and in establishing the proper overall revenue requirement for JUI, the Commission entered proper findings of fact and conclusions of law. In these proceedings, it is the recommended decision (which JUI touts as “well reasoned”) that is not based upon ratemaking principles. For example, at page 30 of the recommended decision, in discussing rent the ALJ states she has a “suspicion” the reasonable amount of rent is somewhere between the Staff and JUI recommendations and states that while it might not be accurate she is “splitting the difference.” In contrast, as will be explained in more detail below, the Commission relied upon the record credible evidence and followed the statutory mandates provided in W.Va. Code §24-1-1(a)(4) requiring rates to be just and reasonable and importantly based primarily on the costs of providing those services.

W.Va. Code §24-2-3 directs that the Commission must investigate and review transactions between utilities and affiliates when determining just and reasonable rates. The Commission is charged with evaluating and limiting the total return of the utility to a level which, when considered with the level of profit or return the affiliate earns on transactions with the utility, is also just and reasonable.

Moreover, W.Va. Code §24-2-4a unequivocally provides that in a rate proceeding before the

Commission, “[t]he burden of proof to show the justness and reasonableness of the increased rate or proposed increased rate . . . *shall* be upon the public utility making application for such change.” In this rate proceeding, JUI was required to demonstrate its costs of rendering service. JUI appears to recognize the dramatic shortfalls of its own request by its eagerness to rely on the non-ratemaking principle offered by the ALJ of “splitting the difference.” The Court must reject this unsound reasoning. A close scrutiny of the Commission’s Order reveals that the Commission relied upon credible evidence to support its conclusions.

The Commission is familiar with JUI’s financial condition. It recently authorized a sizeable rate increase for JUI that went into effect less than eight months before this rate proceeding was filed with the Commission. In the JUI 2008 Rate Order, the Commission authorized a total revenue increase of \$503,684, which consisted of \$302,400 annually to be collected as a \$12.00 monthly surcharge to all ratepayers and additional rate schedule increases totaling \$201,284 of revenue. This earlier rate increase was more than a 100 percent rate increase for a majority of the JUI customers and makes the second requested 72 percent additional increase filed immediately thereafter all the more staggering.

The credible evidence supports a \$66,324 annual revenue increase, equivalent to a 4.4 percent increase over current rates and charges, for the 2,196 customers of the eight JUI water systems in addition to a continuation of the \$12.00 surcharge authorized in the last rate proceeding for JUI.

II. THE COMMISSION GAVE REASONED CONSIDERATION TO THE EVIDENCE PRESENTED BY JUI AND THE STAFF ON EACH RATE ISSUE

The Commission did not adopt all of JUI’s requested adjustments, the Staff’s recommended adjustments or the ALJ’s recommendations; rather, the Commission established just and reasonable

rates for the ratepayers of JUI based upon the evidence presented and proper ratemaking principles. The Commission entered findings of fact and conclusions of law based on the record.

A. INSURANCE PREMIUM WAS DOUBLE BOOKED BY JUI

JUI is mistaken when it argues that the Commission “[d]enied JUI any insurance expense.” Petition p. 21-22. In JUI’s initial filing, JUI included an insurance premium expense amount of \$18,853 as an indirect cost from SES. JUI also included \$18,853 a second time in its Rule 42 Exhibit, JUI Ex. 2 at Adjustment No. 32 on page 103. This expense was booked twice by JUI for the purposes of calculating rates.

In its audit report, Staff included the \$18,853 insurance premium in its recommended O&M expenses. Inclusion of the insurance premium is reflected in Staff’s allocation of indirect costs from SES on Staff’s Ex. 3, Exhibit DLP-2 (See Line 17-Second General Insurance line). The \$18,853 amount is included in the \$58,768 amount as shown on that Staff exhibit. However, Staff disallowed JUI’s Adjustment No. 32, which is where JUI included the insurance expense of \$18,853 a second time.

At the hearing, JUI submitted JUI Ex. 15, which was a second revision of the indirect cost allocation from SES. Testifying in support of JUI Ex. 15, JUI witness Womack admitted that it was appropriate to remove \$18,853 from the Second General Insurance entry on line 17 in order not to duplicate the insurance expense. (II Tr. 67).

The Commission’s total O&M expense calculation for JUI of \$959,161 properly includes the insurance expense adjustment requested by JUI of \$18,853.

B. THE COMMISSION APPROVED A REASONABLE AMOUNT FOR JUI'S RATE CASE EXPENSE

JUI originally requested in its Rule 42 filing a rate case expense of \$120,000 normalized by four years resulting in an expense adjustment of \$30,000. (JUI Ex. 2, Rule 42). Extraordinarily at the hearing, JUI revised its requested rate case expense upward to \$409,431 and proposed a five-year amortization of \$81,886. (I Tr. 79-81 and JUI Ex. 10). In its hearing exhibit, JUI estimated expenses for the current rate case at \$168,899, and added that to the actual expenses for the 2008 rate case of \$240,532, for a total of \$409,431, which JUI then amortized over a five year period deriving an expense adjustment of \$81,886. JUI's witness Griffith went on to sponsor an even higher adjustment request of \$86,926. Witness Griffith stated that since the current 2010 rate case expenses are not complete, his calculation of \$86,926, which provides for additional estimated expenses in the current rate case, should be included for JUI. Id.

Staff recommended a rate case expense allowance of \$30,000 per year. (Staff Ex. 2: II Tr. 137). This is exactly the expense allowance that JUI had sought in its original filing. (JUI Ex. 2, Rule 42).

The ALJ recommended a rate case expense in excess of the amount JUI originally requested and also over the amount calculated in JUI's Ex. 10, accepting JUI witness's speculated amount of \$86,962 for rate case expense.

In its 2010 Rate Order the Commission discussed its treatment of the recovery of rate case expenses in recent major rate cases:

Although the parties, and even the Commission, often refer to a rate case allowance as being an 'amortization' of rate case expense over some period of time, the Commission has historically allowed an increment for rate case expenses not subject to deferral or amortization. The term amortization has become a common usage for

an averaging of rate case expense over some period of time. The CAD'S proposal, which includes an argument that 'unamortized' amounts from this case can be recovered in a future rate case, is inconsistent with the Commission's past practices. Although deferral and amortization have been used for some significant non-recurring items, we have not historically considered rate case expense as falling into this category.⁵ (FNote 2 supplied below).

2010 Rate Case Order at pp. 10-12, citing West Virginia-American, Case No. 08-0900-W-42T, Commission Order March 25, 2009 at p. 54.

The Commission concluded the recommendation for rate case expense did not follow Commission policy and rejected it. The Commission does not authorize companies to defer rate case expenses and amortize these expenses. The Commission attempts to calculate what the rate case expense will be. JUI Ex. No. 10 shows JUI wishes to continue to recover \$5,040 more than its calculations on this expense not \$5,040 less, as the ALJ erroneously concluded. Even more disconcerting is the fact that the recommended decision seems to be based on the assumption that JUI should be recovering prospectively the costs that it incurred in a past case. This is not the

⁵ FNote 2 See e.g., The Potomac Edison Company, Case No. 79-230-E-42T, Order dated June 30, 1980. (Discussing Rate Case Expenses) - This Commission must make rates to be followed in the future, not the past. While we occasionally allow past unrecovered expenses to be included in a Company's cost of service . . . such treatment has been limited to instances in which the expense is clearly extraordinary in nature. Armstrong Telephone Company, Case No. 92-0884-T-42T, Order dated May 28, 1993 - As to the first issue, prior rate case expense, the allowance over time, and not an intention to defer and amortize costs that are properly expensed in the years incurred. . . costs associated with the Company's prior rate case should not be included in its test year calculations. (See, The Potomac Edison Company, Case No. 8280, 64 ARPSCWV 352 (1977); and Columbia Gas of West Virginia, Inc., Case No. 9147, 66 ARPSCWV 488, (1978)).

Commission policy with regard to rate case expenses.

The Commission policy is to allow for an increment for future rate case expense. In making that assessment the Commission can review rate case expense from past years, however the Commission is setting rates for JUI on a going-forward basis. The proper ratemaking treatment is to allow a reasonable amount for expenses in rates on a going-forward basis and is not intended to attempt to allow utilities to recover prior rate case expense. Id.

It was not clear whether JUI was asking for amortization of prior rate case expenses, or leaving expenses from prior cases, which are booked in the test year, in its prospective cost of service. The Commission held that either approach is inconsistent with the Commission treatment of rate case expenses. 2010 Rate Order p. 12.

The Commission determined that it was unreasonable to assume that JUI would incur \$86,962 per year in future rate case expenses, on average. Contrary to the ALJ's misunderstanding of the evidence, the Commission pointed out that the \$86,962 was more than even the Company witness had calculated. The Commission, based on its expertise and on the record presented, determined that an ongoing expense of over \$81,000 per year was unreasonable. The Commission evaluated the evidence and determined that JUI's updated requested rate case expense was excessive, and the ALJ's recommendation for rate case expense unreasonable. The Commission properly held that the Staff Rule 42, Adjustment 11, supports the appropriate rate case expense adjustment.

**C. THE COMMISSION AUTHORIZED A FAIR RENT
FOR JUI TO PAY BASED ON ITS USE OF THE
SNYDER BUILDING FACILITIES**

JUI included building rent of \$6,602 per month in its revenue requirement. JUI calculated rent based on its affiliate Owners' claimed investment amount of \$3.1 million. (JUI Ex.4). Staff

recommended that JUI pay building rent of \$2,252 per month. (Staff Ex.3 DLP-4). In testimony, the Staff disagreed with the calculations for the rent expense to JUI, arguing that the amount of rent should be based on investment in the land and building, a return on that investment, and a reasonable allocation of the space needed in the building for JUI to operate. 2010 Rate Order p. 8.

W.Va. Code §24-2-3 provides: “The Commission shall limit the total return of the utility to a level which, when considered with the level of profit or return the affiliate earns on transactions with the utility, is just and reasonable.” Accordingly, Staff calculated that the utility should only pay a return on investment to the owner equal to the allowed rate of return for JUI which is “just and reasonable.” (II Tr. 147). The Commission disallowed the attempt by JUI at the hearing to increase the claimed value of the investment by the owner for the building.

The Commission determined the JUI proposed rent calculation allocated too much square footage to JUI. The Snyder Building has 27,489 square feet. Staff allocated 2,828 square feet to JUI compared to JUI’s proposed allocation of 6,295 square feet. Also, Staff added depreciation expense as an owner cost and adjusted the other expenses to reasonable levels for a utility of approximately 2,196 customers. Staff calculated a reasonable rent expense for JUI utility operations to be \$2,252 monthly, or \$27,024 annually. (Staff Ex. 3, DLP-4).

The Commission denied the excessive requests of JUI. The Commission found the Staff calculations to be credible. In the Commission’s opinion allowing costs to ratepayers in excess of the Staff calculation of a net annual occupancy cost of \$27,000 would result in financial harm to the ratepayers of JUI.

D. THE COMMISSION PROPERLY HELD THAT JUI SHOULD NOT BE PERMITTED TO RETROACTIVELY ADJUST ITS ACCUMULATED DEPRECIATION

In this rate case, JUI sought to adjust its accumulated depreciation balance, which is currently based on the accelerated tax depreciation rates used by JUI in its tax filings, rather than the straight-line depreciation rates required by the Uniform System of Accounts for regulated water utilities. See, Rules for the Government of Water Utilities 150 C.S.R. § 7-2.5. (2003).

On Page 37 of its December 17, 2010, Initial Brief, JUI admitted: “Whether by oversight, mistake or simple ineptitude, the utility continued to record its accumulated depreciation on its regulatory books and records using the accelerated tax depreciation rates it uses for its tax filings.” JUI has not used straight-line depreciation rates to compute the accumulated depreciation balance on its regulatory books and records. JUI, as a utility, has the duty to maintain accurate books and records and to report historical numbers, such as accumulated depreciation balances on those books and records and in its Annual Reports filed with the Commission. The result of JUI’s failure to record accumulated depreciation on its books and records using straight-line depreciation is that a larger amount of accumulated depreciation and a smaller rate base are recorded in its books. Because of these results, the Commission denied JUI’s request to recalculate its accumulated depreciation for the years past and establish a current accumulated depreciation balance based on the straight-line depreciation method that it should have been using all along in its Commission rate cases. As the Commission explains on Pages 13 and 14 of the 2010 Rate Order:

It was not the Commission that calculated the depreciation reserve that is reflected on JUI’s books. JUI was not forced to book depreciation expenses that it now claims were excessive, giving rise to an overstated reserve for depreciation. It did so on its own, and in doing so JUI presented financial results to the Commission which

formed the basis for any review that the Commission may have been called upon to make regarding the financial condition of JUI.

JUI fails to discuss that its rate base and accumulated depreciation reserve that it proposed for modification have been the basis for past Commission ratemaking decisions.

In this case, the ALJ recommended JUI be allowed to adjust its accumulated depreciation balance based upon a November 30, 2010, Recommended Decision issued in Megan Oil and Gas Co., Case No. 10-0757-G-D (“Megan”). The Staff filed exceptions to the Megan decision. By Commission Order entered January 25, 2011, the Commission refused to adopt the Recommended Decision in Megan and instead determined the Staff recommendation was reasonable for ratemaking treatment of accumulated depreciation. The Staff also filed exceptions in the current JUI cases regarding the accumulated depreciation issue and recommended that JUI begin accounting for appropriate straight-line depreciation expense and accumulated depreciation prospectively in the same manner as the Commission decision in Megan. After careful consideration of this issue by the Commission in Megan and its similarities to this case, the Commission adopted the same decision.

This Court previously found that an adjustment that looks backward and reduces a utility rate base that had been previously reviewed and approved by the Commission is improper and cannot be sustained. See, The Chesapeake and Potomac Telephone Company of West Virginia v. Public Service Commission of West Virginia, 171 W. Va. 494, 300 S.E. 2d 607, 619 (1982). By not allowing JUI to make a retroactive adjustment to the detriment of JUI ratepayers, the Commission applied the same logic in the current rate case as this Court used in Chesapeake. Customers are entitled to the same certainty of prior approved rate base. The Commission’s 2010 Rate Order approved similar treatment for JUI’s annual depreciation expense adjustment using the straight-line method application to the rate base prospectively is consistent with this Court’s decision in

Chesapeake.

E. THE COMMISSION AUTHORIZED A FAIR OFFICER'S SALARY BASED UPON THE WORK PERFORMED

JUI requested a salary of \$55,000 from JUI for Mr. Snyder is a \$15,000 increase over the authorized salary in the 2008 Rate Case. JUI presented the testimony of Mr. Snyder describing his work effort. (Tr. 234;252-54; 278-79 and JUI Ex. 12). JUI also presented three witnesses to support Mr. Snyder's work effort and time. (I Tr. 68; 126 witness Griffith; I Tr. 144-46; 167-68; 197 witness Womack; and I Tr. 230 witness McFarland).

Staff recommended a salary of only \$15,000 for Mr. Snyder, claiming Mr. Snyder had not provided adequate documentation of his work time.

The ALJ recommended no salary be authorized for Mr. Snyder. The ALJ reasoned that as the owner of JUI, Mr. Snyder will collect profits.

After a review of the evidence, the Commission determined that the ALJ recommendation of no salary for Mr. Snyder was unreasonable. Likewise, the Commission concluded that there was insufficient support for the Staff recommendation, which amounted to a reduction in salary to Mr. Snyder of \$25,000. The Commission also determined the record was insufficient to support an increase of salary to Mr. Snyder; however, the Commission determined that the \$40,000 for the officer salary established eight months ago in the JUI 2008 Rate Order continued to be reasonable.

III. THE COMMISSION PROPERLY WITHHELD AND DEFERRED ITS CONSENT AND APPROVAL FOR JUI TO ENTER INTO THE PROPOSED AFFILIATE TRANSACTIONS

SES has in place eight affiliated contracts with JUI, whereby SES provides all of the employees, equipment, and services necessary to operate the utility. JUI's sole employee is the

President, owner, and principal of affiliate companies, Lee Snyder. JUI and SES present a unique situation where an affiliated, non-regulated construction company performs all, or practically all, operation, maintenance, billing, collecting and construction services necessary to operate the water systems of a regulated utility company. JUI, SES, Lee Snyder and Cynthia Snyder are affiliates of one another.

The complex, interrelated and layered affiliate relationships between JUI, SES, and Lee and Cynthia Snyder seem to be controlled by President, Lee Snyder. (I Tr. 233-4, 270; and II Tr. 31 and 41). It is President Snyder that has developed the affiliate Revised O&M Agreement. (I Tr. 270). It is President Snyder that has designed and implemented the complex leasing arrangements between his affiliates. (II Tr. 41).

After reviewing the evidence, the Commission determined that JUI had not met its statutory burden under W.Va. Code §24-2-12. Thus, the Commission denied its consent and approval to any of the transactions but directed a further investigation and review into the affiliate transactions.

Affiliated agreements are inherently suspect. The Commission has an initial and ongoing duty to ensure the reasonableness of affiliate transactions in order to protect the interests of ratepayers. This is especially true when affiliate terms and conditions affect costs to ratepayers. Under W.Va.Code §24-2-12, the Commission may grant its consent and approval of affiliate agreements only “upon proper showing that the terms and conditions thereof are reasonable and that neither party thereto is given an undue advantage over the other, and do not adversely affect the public in this state.” JUI failed to meet its burden. The Commission expressed its grave concern that the Revised O&M Agreement and the Leases, if approved as filed, would result in great financial harm to the ratepayers of JUI.

A. THE REVISED AFFILIATED OPERATION AND MAINTENANCE AGREEMENT, IF APPROVED, WOULD PLACE EXCESSIVE COSTS AND FEES ON THE CUSTOMERS OF JUI

JUI's glowing references to the recommended decision as an endorsement of the Revised O&M Agreement are misplaced. For example, the ALJ concluded at page 31 of the Recommended Decision that she agreed with Staff that the transactions between JUI and SES should be based on costs and that the format of the agreement presented for approval did not provide the necessary transparency. The ALJ did not find the operating agreement to be reasonable. In fact, she adjusted the costs flowing from those agreements downward. Her findings were based on a determination that JUI had not met its burden to show that the resulting costs were reasonable.

The Commission noted problems with the Revised O&M Agreement between JUI and SES. Most significantly, the Revised O&M Agreement contains a flat fee per month provision for billing, collecting, meter reading, and treatment station monitoring plus a provision that any maintenance or repair work is billed separately on a time and materials basis. The actual services and costs to JUI under the flat fee are not functionally measured by SES, and the actual costs cannot be controlled or negotiated by JUI.

The Revised O&M Agreement also contains a per customer escalator clause where, for each new customer added to the system, the flat fee will be increased \$19.54 per customer per month. This, however, was changed by JUI at the hearing to \$14.83 per new customer. Regardless of the reduced cost suggested by JUI, neither the ALJ nor the Commission found that JUI had met its burden to demonstrate that the charges to add a new customer were reasonable.

The affiliated charges between JUI and SES are the most important issue in these cases and by and large form the basis for the large requested rate increase. The Revised O&M Agreement, if

approved, would increase these affiliated charges even more. For example the proposed Revised O&M Agreement increases flat fee charges from SES to \$514,844 annually, an increase by \$196,668, from the current amount of \$318,176. The Agreement also provides time and material charges to JUI for everything not covered by the flat fee based on the rates SES charges to “third parties.”

In its testimony, Staff advocated eliminating several expenses included by SES that are inappropriate for setting rates. In addition, Staff argued that a few allocation factors should be corrected. These Staff adjustments, which the Commission found credible, resulted in a finding that the amount SES invoices to JUI should be decreased by \$111,137 for the test year. (Staff Exhibit No. 2, Adjustments 15 and 16 on Page 48). Staff witness Pauley’s Exhibit DLP-1 in Staff Exhibit No. 3 shows the calculations supporting the Staff Adjustments 15 and 16. Staff’s calculation shows that for the test year, the total amount of cost that SES should have charged JUI was \$513,365.

As Staff witness Pauley points out, the charges from SES to JUI should be billed only at cost plus the return on investment that JUI is authorized to earn. SES must specifically allocate costs that are absolutely essential to operate the utility. Transparency must be the goal, so that JUI can record expenses to the proper accounts and provide a proper audit trail that is not shielded by confidentiality agreements.

JUI at page 11 of its Petition, quotes the ALJ, stating that “[c]learly the eight old agreements (Exhibit C-1) are outdated, if for no other reason than that they require JUI and SES to treat the various JUI systems as separate entities.” This is untrue. The Commission issue is not with the blending of the eight contracts into one contract, but rather is the increase in costs to be charged to JUI. In fact, more than half of the almost \$1 million dollar increase sought by JUI was for increased

costs provided in the Revised O&M Agreement.

The Commission determined that JUI had not shown that the charges resulting from the agreement were reasonable or that those costs reflected the costs of SES plus a reasonable profit on the equipment and facilities dedicated to or used from time to time for the benefit of JUI. The Commission gave reasoned consideration to the evidence of JUI and Staff and determined that the Staff numbers were more credible.

The Commission withheld its approval of the Revised O&M Agreement between JUI and SES because JUI had failed to meet its statutory burden. The Agreement is not reasonable and JUI failed to demonstrate that the structure and terms fairly allocate costs to JUI and the utility ratepayers.

**B. THE AFFILIATED LEASE AGREEMENTS
UNREASONABLY PLACE JUI, A SMALL UTILITY,
IN THE POSITION OF LANDLORD**

JUI requested approval of four lease agreements (JUI Exhibit No. 1, Attachment 11): 1) Lease #1 is between Lee and Cynthia Snyder-Landlord and JUI-Tenant for Lot 16 (the Building lot) with JUI paying rent, repairs, taxes, insurance, and ground maintenance; 2) Lease #2 is between Snyder, LLC-Landlord and Lee and Cynthia Snyder-Tenant for Lot 17 (the Storage lot) with Lee and Cynthia Snyder paying rent, repairs, taxes, insurance, and ground maintenance; 3) Lease #3 is an assignment by Lee and Cynthia Snyder-Assignor (Tenant) to JUI (Assignee) for Lot 17 with JUI paying rent, repairs, taxes, insurance, and ground maintenance; and 4) Lease #4 is Sublease Agreement and Agreement to Share Space and Expenses where JUI Sublessor and SES-Subleasee for Lots 16 and 17 with SES paying its share to the total rent to JUI.

The Snyder Building as constructed contains 27,489 square footage of office space. (JUI Ex.

No. 3). It was planned to house SES operations, JUI utility operations and provide for additional rental space. SES is licensed and operates in the four-state area of West Virginia, Virginia, Pennsylvania and Maryland. JUI 2008 Rate Order p.2.

At the hearing, President Snyder testified that the complexity of the arrangement of these four lease agreements is most beneficial for tax purposes for the owners, Lee and Cynthia Snyder, and not for the ratepayer for utility rate-making purposes. (II Tr. 41). JUI is a utility and should focus on providing quality service at reasonable rates. The arrangement of these leases instead, uses JUI as a conduit to receive some Rent Revenue from SES and pay a higher amount in Rent Expense. These four lease agreements put JUI in the office rental business, an activity unrelated to its regulated water utility. According to Mr. Snyder's testimony, there is still vacant office space in the Building. (II Tr. 42). The Commission expressed concern with these lease agreements and especially expressed concern with JUI being in the rental business.

The record further reflects that prior to the summer of 2009 the operations of both SES (which provides service to 39 other utility systems in addition to the JUI utility affiliate (I Tr. 270)) and JUI were conducted out of "two trailers and a shop/warehouse." (I Tr. 260). JUI has argued vigorously that the operations of JUI for a mere 2,196 customers cannot support the hiring of utility employees or conduct stand alone operations. It is, however, President Snyder's position that it is proper for JUI, (with himself as the sole employee) to be the landlord for an office space that JUI alleged at hearing had a market value for owner's investment of \$3,118,524. (JUI Ex.4). This facility has over 27,000 square feet and multiple business tenants. Staff calculated the appropriate annual rental for JUI at \$27,024 based on an audited construction cost of \$2,352,704 for owner's investment. (Staff Ex.3 DLP-4).

The Commission faced the question of whether the lease agreements presented for Commission approval were reasonable and in the public interest. The Commission determined that JUI had failed to meet its burden to show that the Leases were reasonable and in the public interest.

The Commission explained:

Considering both the cost numbers that JUI proposes for Snyder's investment in the facilities and its work space allocation of 22.9 percent, JUI would have the Commission determine that a facilities investment allocation of approximately \$710,000 is reasonable and necessary for JUI, resulting in a net annual occupancy cost (rental fee) of \$79,000. Considering the Staff cost numbers and work space allocation, a facilities investment allocation of approximately \$250,000 is reasonable and necessary for JUI, resulting in a net annual occupancy cost of \$27,000. Although the ALJ observed that a correct answer may be somewhere between the two numbers, we do not find that the record supports a finding that this issue should be decided on the basis of 'split the difference.' On balance, the Staff recommendation appears to be more reasonable, and we will adopt the Staff recommended occupancy cost.

2010 Rate Order p.8.

The sniff test supports the reasonableness of the Commission's decision. JUI calculated rental based on its claimed affiliated owners' investment of \$3.1 million; Staff calculated rental based on an audited construction cost owners' investment of \$2.4 million. The difference between JUI and Staff owner's investment is that JUI relied on a market cost and Staff based its calculation on audited construction costs. JUI then requested a work space allocation of almost 23 percent of the Snyder Building to the utility operation, while Staff recommended a space allocation of approximately 10 percent. JUI disputes Staff's allocation as being arbitrary. The record reveals that Staff based its allocation on "numbers and space requirements for employees involved directly, and nearly exclusively, on JUI-related activities and on observations of work areas and other areas within the shared space used by SES employees that provide services, but not exclusive services to JUI."

2010 Rate Order p. 8. The Commission was asked by JUI to approve the Utility leasing a \$3 million building. JUI needed less than one-fourth of the space ((closer to one-tenth) under the Staff analysis), but was expected to assume the risk of being able to sublease the 75 to 90 percent that it did not need to an affiliated company or other prospective tenants. All of this for businesses that up until 2009 had been operated out of “two trailers and a shop warehouse.”

JUI inaccurately claims: “Respectfully, because JUI’s evidence was not rebutted regarding the reasonableness of the Lease Agreements, this Court should approve those agreements and remand to the PSC with directions to include JUI’s expenses from those agreements in its rate calculations.” The Commission disagrees. A contract between a utility and its affiliate is not reasonable simply because the witness for the applicant says that it is. The Commission did review the evidence, all of the evidence, and found the Utility argument to be wrong and unsupported by the facts. The Commission correctly determined that the Petitioner had failed to prove that the leasing agreements were reasonable and were not adverse to the public.

C. THE COMMISSION’S GENERAL INVESTIGATION INTO THE AFFILIATED TRANSACTIONS IS IN THE PUBLIC INTEREST

The Commission’s Order withheld granting JUI consent and approval to enter into the Revised O&M Agreement and the four Lease Agreements after concluding that JUI failed to meet the statutory test to enter into these affiliate agreements. The Commission, however, has not shut the door on JUI concerning these five affiliated agreements. The Commission is giving JUI a second chance by initiating a General Investigation in Case No. 11-0235-W-GI in which JUI will be allowed to modify and resubmit the Revised O&M agreement and the four Lease agreements with its affiliates.

This general investigation will include the following issues and concerns of the Commission: 1) requiring JUI to show that JUI's customers are better off with an affiliate furnishing all required services as opposed to JUI employing its own utility personnel; 2) studying JUI's long-term plans to operate and rehabilitate its utility facilities; 3) receiving further details of JUI's current and future use of the \$12 surcharge; and 4) requesting information about future possibilities of private-public agreements. The general investigation is supported by W.Va. Code §24-2-3 which directs, in relevant part: "In determining just and reasonable rates the commission shall investigate and review transactions between utilities and affiliates." The Commission also has the general authority and obligation under W.Va. Code § §24-1-1 and 24-2-7 to assure reasonable utility services and practices at reasonable rates.

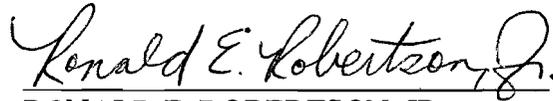
CONCLUSION

WHEREFORE, acting within the scope of its statutory authority, the Public Service Commission in its Order of February 18, 2011 has: properly exercised its ratemaking authority by establishing rates for JUI based upon the demonstrated costs of providing water service to JUI customers; correctly determined that an annual increase to JUI of \$66,324, equating to a 4.4 percent increase over current rates, is reasonable; properly denied its consent and approval for the Revised O&M Agreement between SES and JUI and the four Lease agreements filed by JUI; and finally properly and in the public interest of JUI customers initiated a General Investigation, Case No. 11-0235-W-GI, of JUI's utility operations, including the Revised O&M Agreement and the proposed four Leases as well as other issues. The evidence in this matter supports the Commission decision and the substantive result is proper. In the interest of the public, it is respectfully requested that this Court deny the petition for appeal filed by JUI.

Respectfully submitted this 25th day of April, 2011.

THE PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA

By Counsel,

A handwritten signature in cursive script that reads "Ronald E. Robertson, Jr." The signature is written in black ink and is positioned above a horizontal line.

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CERTIFICATE OF SERVICE

I, RONALD E. ROBERTSON, Counsel for the Public Service Commission of West Virginia, do hereby certify that a copy of the foregoing "Statement of the Respondent, Public Service Commission, of its Reasons for the Entry of its Order of February 18, 2011, in Case No. 10-0974-W-PC and Case No.10-1329-W-42T" has been served upon the following parties of record by First Class United States Mail, postage prepaid this 25th day of April, 2011.

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