223 Va. 100

SUPREME COURT OF VIRGINIA

Lake of the Woods Utility Company,

Appellant,

v.

Record No. 810785

Lake of the Woods Association, Incorporated, et al.,

Appellees.

CLERK
SUPREME COURT OF VIRGINIA
RECEIVED
SEP 29 1981
RICHMOND, VIRGINIA

Lake of the Woods Association, Incorporated,

Appellant,

v.

Record No. 811206

Lake of the Woods Utility Company, et al.,

Appellees.

CLERK
SUPREME COURT OF VIRGINIA
RECEIVED
SEP 29 1981
RICHMOND, VIRGINIA

76

JOINT APPENDIX

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TABLE OF CONTENTS

	Page
Application	1
Order Revising Interim Order - August 4, 1980	8
Protest of Lake of the Woods Association - October 20, 1980	14
Report of Hearing Examiner	19
Exceptions of Lake of the Woods Association to Report of Hearing Examiner - March 3, 1981	49
Exceptions of Lake of the Woods Utility Company to Report of Hearing Examiner - March 5, 1981	61
Final Order - April 1, 1981	68
Suspension of Final Order - May 12, 1981	73
Opinion - July 28, 1981	75
Assignments of Error	116
Assignment of Cross-Error	119
Transcript of Testimony:	
James Hinkle	121
Thomas L. Thorpe	125
Robert L. Frasher	212
S. Frank Leis	247
E. Jackson Tice	292
Alan Potter	303
Warren J. Lodge	321
William W. Carpenter	344
Harold J. Wade	357
Brenda McCall	361
Albin L. Lindall	364
George P. Beard	370
Exhibits:	
TLT-1	376
RLF-2	379
SFL-3	387
ALP-4	395
WWC-5	396
Letter (with five exhibits) dated January 9, 1981 from Mr. Riely to Mr. Farrar - January 13, 1981	401

VIRGINIA

BEFORE THE STATE CORPORATION COMMISSION

APPLICATION
OF
LAKE OF THE WOODS UTILITY COMPANY
For an Increase in Rates for
Sewer Service on an Emergency Basis.

Lake of the Woods Utility Company (the Company) respectfully shows:

1. It is a Virginia public service company providing water and sewer service in the Lake of the Woods development in Orange County, Virginia.

2. Its investment in plant applicable to sewer service, plus working capital and materials and supplies, at December 31, 1979, was $1,865,733. Its net operating income from such service during the twelve months then ended was a loss of $205,698. Additional revenues are, accordingly, urgently needed to prevent wasting of the assets of the Company and to permit it to continue to render service.

3. An increase in the monthly charge to residential customers from $8 to $24 will increase gross revenues (on the basis of 1979 results of operations) by $147,648. Reduction in net operating loss, however, will be reduced only to $99,044 due to a projected increase in operating expenses. This increase will not result in a rate of return on rate base for sewer operations, nor will interest of allocated debt be covered.

4. An increase in the sewer connection fee and the sewer installation fee from $785 to $1,050 and $285 to $400 respectively, will allow the Company to barely cover its actual cost for installation (on the basis of 1979 results). This increase will not result in a rate of return to the Company.

5. An increase in the turn-on charge from $1.50 to $5.00 will allow the Company to cover the cost incurred for such services.

6. A revision of Rule No. 11 (H) in the Rates, Rules and Regulations to allow the Company to bill service customers bi-monthly in arrears as an alternative to the presently allowed monthly, quarterly, and semi-annual billing periods.

7. An emergency exists. Such proposed rates will provide revenues not in excess of the actual costs incurred by the Company in serving its customers and will not produce a positive return on its rate base. Such proposed rates contain reasonable classification of customers.

8. A proposed tariff is filed herewith as Exhibit A.

The Company, therefore, requests that this matter be set down for prompt public hearing and that a temporary increase in rates in the amount requested be authorized under §56-245 of the Code of Virginia, the Company being prepared to file the required bond.

Dated: June 12, 1980

Respectfully submitted,

LAKE OF THE WOODS UTILITY COMPANY

BY _____

President

SCHEDULE NO. 1

METER RATES

Applicable in all territory served by the Company.

AVAILABILITY OF SERVICE:

Available to all metered customers other than customers purchasing water for resale.

WATER RATE:

	Gallons Per		Rate Per
	Month	Quarter	1,000 Gallons
For the first	12,000	36,000	.50
For all over	12,000	36,000	.45

SEWERAGE RATE:

The monthly sewerage service charge shall be 90% of the charge for water for commercial customers and $24.00 per month for residential customers.

MINIMUM CHARGES:

No bill will be rendered for less than the minimum charge of $4.00 per month for water and $24.00 per month for sewerage for each separate living unit on the premises served.

RULE NO. 3 - SERVICE CONNECTIONS:

(a) Before a water service connection is provided, the owner of the premises to be supplied, or his duly authorized representative, shall make application for water service upon form prescribed by the company. Upon approval of the application, the Company will install the service connection form the main in the street to the meter box, and will charge for the installation a connection fee of $385. The availability fee will terminate as of the end of the month in which the connection is made.

(b) Before a sewerage service connection is provided, the owner of the premises to be supplied, or his duly authorized representative, shall make application for sewerage service upon forms prescribed by the Company. No application for sewerage service shall be approved for a premises for which an application for water service has not first been approved. Upon approval of the application, the Company will install the service connection, including converting equipment, from the sewage collection main to the foundation of the customer's house or, if converting equipment is available to the premises, from the converting equipment to the foundation of the customer's house, and will charge a connection fee of $1,050 and a line installation fee of $400. The availability fee will terminate as of the end of the month in which the connection is made. Every customer upon those premises converting equipment is located shall permit other connections to such equipment without compensation.

(c) The Company will not be obligated to provide a water or sewerage service connection, however, until the owner of the premises to be supplied has paid the availability fees which would have been payable by such owner under Rule No. 2 had he been obligated by contract or deed restriction to pay such fees, whether or not he was so obligated.

(d) The Company will maintain and replace when necessary all water service connections from the main in the street to the meter and all sewerage service connections from the main in the street to the converting equipment.

(e) The Company will make all connections to its mains and will specify the size, kind and quality of all materials entering into the service connection.

(f) The corporation cock, meter cock, meter box and service pipe from the water main to the meter box laid at right angles to the main and the service pipe (including converting equipment) from the sewerage main to the customer's house will be furnished and installed by and shall remain the property of the Company and under its sole control and jurisdiction.

EXHIBIT A-2

RULE NO. 3 - SERVICE CONNECTIONS: - Continued

(g) These rules and regulations shall not apply to service of a temporary nature. Such services of a temporary nature shall be installed, maintained, replace, and removed at the expense of the owner, but such installations shall be subject to approval by the Company.

RULE NO. 10 - TURN-ON CHARGE:

(a) When it has been necessary to discontinue water or sewerage service to any premises because of a violation of these Rules and Regulations, or because of non-payment of any bill, a charge of Five Dollars ($5.00) may be made for turning on the water or providing sewerage service. This charge, together with any arrears that may be due the Company for charges against the customer, must be paid before the water or sewerage service will be resumed.

(b) If at the time of such discontinuance of service for non-payment of bill, the customer does not have a deposit with the Company, the Company may require a deposit as a guarantee of the payment of future bills, as set forth in Rule No. 8, before service will be resumed.

EXHIBIT A-4

RULE NO. 11 - BILLS FOR WATER AND SEWERAGE SERVICE:

(a) Customers are responsible for furnishing the Company with their correct address. Failure to receive bills will not be considered an excuse for non-payment nor permit an extension of the date when the account will be considered delinquent.

(b) If bills are to be sent to an address other than the premises served, the Company should be notified in writing by the customer of any change of address.

(c) If requested in writing by the customer, the Company will send bills to and will receive payments from agents or tenants. However, this accommodation will in no way relieve the customer of the liability for all charges, and the Company shall not be obligated to notify the customer of the non-payment of bills by such agents or tenants.

(d) Payments shall be made at the office of the Company or at such other places conveniently located as may be designated by the Company.

(e) The Company reserves the right to correct any bills rendered in error as to the service supplied.

(f) Each "Premises" as described in Rule No. 1 shall be billed separately for service.

(g) If the meter should fail to register for any reason, or if the meter reader should be unable to gain admittance to the premises at the time the meter is due to be read, an estimated bill will be submitted. Such bill shall be based on an average of the consumption shown by three (3) previous consecutive billing periods, or, in the case of a new customer, where previous consumption cannot be so used for computing average consumption, reasonably estimated consumption shall be utilized.

(h) Bills for availability fees or service shall be rendered monthly, bi-monthly, quarterly or semi-annually in arrears.

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COMMONWEALTH OF VIRGINIA

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STATE CORPORATION COMMISSION

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AT RICHMOND, AUGUST 4,1980

APPLICATION OF

LAKE OF THE WOODS UTILITY COMPANY CASE NO. PUE800081

To revise its tariffs

ORDER REVISING INTERIM ORDER

By an interim order dated July 17, 1980, the Commission approved interim rates and established intermediate dates for the filing of testimony, mailing of notice, etc. prior to the public hearing previously set by order dated July 1, 1980. On July 29, 1980, Company filed a proposed revised schedule with the Commission to increase the sewerage rate beyond that approved in the July 17, 1980, interim order. This revised schedule is designed to increase Company's gross annual revenues by $147,648 above that to be received through the interim rates.

IT NOW APPEARING to the Commission that the notice contained in paragraph (10) of the July 17 interim order should be changed,

IT IS ORDERED that the notice in paragraph (10) of the July 17, 1980, order be amended to read as follows:

NOTICE TO THE PUBLIC OF AN INTERIM RATE INCREASE BY LAKE OF THE WOODS UTILITY COMPANY FOR PROVIDING SEWERAGE SERVICE IN LAKE OF THE WOODS DEVELOPMENT, ORANGE COUNTY, VIRGINIA, AND A PUBLIC HEARING FOR CONSIDERATION OF A PERMANENT INCREASE

TAKE NOTICE that on June 17, 1980, Lake of the Woods Utility Company (hereinafter "Company") filed an application with the Commission for an increase in rates for sewerage service. It is stated that the tariff revisions are designed to increase Company's gross annual revenues by $147,648.

By order dated July 17, 1980, the Commission found that Company has demonstrated a reasonable probability that an increase in rates in the amount of $147,648 will be justified after a full investigation and hearing. The Commission order permits Company to implement the proposed rates for service rendered on and after August 1, 1980. The revenues shall be collected on an interim basis, subject to refund, and shall be separately accounted for on Company's books and records. The Commission will order that any portion of such increased revenues not justified by the Company be refunded to customers. The interim rate for sewerage service shall be $24 per month for residential customers.

On July 29, 1980, Company filed a revised schedule with the Commission proposing to increase the sewerage rate beyond that approved in the July 17, 1980, interim order to $40 per month for residential customers. The Company states that this proposed tariff revision is designed to increase Company's gross annual revenues by $147,648 above that received through the interim rates.

The revised proposed rates are as follows:

SEWERAGE RATE:

The monthly sewerage service charge shall be 90% of the charge for water for commercial customers and $40.00 per month for residential customers.

MINIMUM CHARGE:

No bill will be rendered for less than the minimum charge of $4.00 per month for water and $40.00 per month for sewerage for each separate living unit on the premises served.

RULE NO. 3 - SERVICE CONNECTIONS:

(b) Before a sewerage service connection is provided, the owner of the premises to be supplied, or his duly authorized representative, shall make application for sewerage service upon forms prescribed by the Company. No application for sewerage service shall be approved for a premises for which an application for water service has not first been approved. Upon approval of the application, the Company will install the service connection, including converting equipment, from the sewage collection main to the foundation of the customer's house or, if converting equipment is available to the premises, from the converting equipment to the foundation of the customer's house, and will charge a connection fee of $1,050 and a line installation fee of $400. The availability fee will terminate as of the end of the month in which the connection is made. Every customer upon those premises converting equipment is located shall permit other connections to such equipment without compensation.

(c) The Company will not be obligated to provide a water or sewerage service connection, however, until the owner of the premises to be supplied has paid the availability fees which would have been payable by such owner under Rule No. 2 had he been obligated by contract or deed restriction to pay such fees, whether or not he was so obligated.

(d) The Company will maintain and replace when necessary all water service connections from the main in the street to the meter and all sewerage service connections from the main in the street to the converting equipment.

(e) The Company will make all connections to its mains and will specify the size, kind and quality of all materials entering into the service connection.

(f) The corporation cock, meter cock, meter box and service pipe from the water main to the meter box laid at right angles to the main and the service pipe (including converting equipment) from the sewerage main to the customer's house will be furnished and installed by and shall remain the property of the Company and under its sole control and jurisdiction.

(g) These rules and regulations shall not apply to service of a temporary nature. Such services of a temporary nature shall be installed, maintained, replaced, and removed at the expense of the owner, but such installations shall be subject to approval by the Company.

RULE NO. 10 - TURN-ON CHARGE:

(a) When it has been necessary to discontinue water or sewerage service to any premises because of a violation of these Rules and Regulations, or because of non-payment of any bill, a charge of Five Dollars ($5.00) may be made for turning on the water or providing sewerage service. This charge, together with any arrears that may be due the Company for charges against the customer, must be paid before the water or sewerage service will be resumed.

(b) If at the time of such discontinuance of service for non-payment of bill, the customer does not have a deposit with the Company, the Company may require a deposit as a guarantee of the payment of future bills, as set forth in Rule No. 8, before service will be resumed.

The Commission has scheduled a hearing to begin at 10:00 a.m., November 5, 1980, in the Commission's Courtroom, 13th Floor, Blanton Building, Bank and Governor Streets, Richmond, Virginia, to receive evidence relevant to establishing reasonable and just rates.

Copies of Company's proposed tariffs and accompanying materials are available for public inspection during regular business hours at the Commission Document Control Center, Floor B1, Blanton Building, Bank and Governor Streets, Richmond, Virginia, and at the Lake of the Woods Office, Route 3, Locust Grove, Virginia. On and after September 24, 1980, a copy of Company's prefiled testimony and exhibits will be available for public inspection at the same locations.

Any person desiring to comment in writing on the application may do so by directing such comment to the Clerk of the Commission as provided below.

Any person (public witness) desiring to make a statement at the November 5 public hearing, either for or against the application, need only appear in the Commission's Courtroom at 9:45 a.m. on the day of the hearing and identify himself or herself as a public witness.

On or before September 17, 1980, persons desiring to participate as protestants, as defined in Rule 4:6 of the Commission's Rules of Practice and Procedure ("SCC Rules"), to present evidence and cross-examine witnesses, shall file an original and five (5) copies of a Notice of Protest, as described in SCC Rule 5:16(a) with the Clerk of the Commission and serve a copy upon Company. Service upon Company shall be directed to John W. Riely, Esquire, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212.

On or before October 22, 1980, each protestant shall file an original and five copies of a Protest (SCC Rule 5:16(b)) and an original and ten copies of the prepared testimony and exhibits protestant intends to present at the November 5 hearing, and serve a copy upon Company.

All written communications to the Commission regarding this case should be directed to William C. Young, Clerk, SCC Document Control Center, P.O. Box 2118, Richmond, Virginia 23216.

LAKE OF THE WOODS UTILITY COMPANY

ATTESTED COPIES hereof shall be sent to John W. Riely, Esquire, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212; Office of the Attorney General, Division of Consumer Counsel, 11 South 12th Street, Richmond, Virginia 23219; and to the Commission's Divisions of Energy Regulation and Accounting and Finance.

A True Copy
Teste: William C. Young
Clerk of State Corporation Commission

VIRGINIA

BEFORE THE STATE CORPORATION COMMISSION

APPLICATION OF	)	
LAKE OF THE WOODS UTILITY COMPANY	)	CASE NO. PUE800081
To revise its tariffs	)	

PROTEST

OF

LAKE OF THE WOODS ASSOCIATION, INC.

Somerville, Moore & Joyner, Ltd.
Post Office Box 629
Orange, Virginia 22960,
Counsel for Protestant,
Lake of the Woods Association, Inc.

PROTEST

OF

LAKE OF THE WOODS ASSOCIATION, INC.

Lake of the Woods Association, Inc. comes now and for its Protest to the Application of Lake of the Woods Utility Company says:

1. The Protestant, Lake of the Woods Association, Inc., has an interest in this proceeding in that it is a customer of Lake of the Woods Utility Company and an increase in rates will adversely affect the operations of Lake of the Woods Association, Inc. In addition, it says that its members are customers of Lake of the Woods Utility Company and the increase in rates will adversely affect each of its members.

2. The Protestant has this day filed its testimony and exhibits setting forth its position in this matter. Reference thereto is made for a detailed statement of the facts which the Protestant is prepared to prove. By way of summary the Protestant submits that:

(a) A careful analysis of the financial condition of Lake of the Woods Utility Company will reveal that it is not sustaining the losses alleged by the company;

(b) Some of the fees and charges reported as expenses of Lake of the Woods Utility Company are exorbitant and unreasonable;

(c) Management of Lake of the Woods Utility Company is not efficient and results in unnecessary expenses;

(d) Expenses are not properly allocated between maintenance and capital improvements;

(e) The increase in utility rates is exorbitant and will work an undue hardship on the Protestant and all members of Lake of the Woods Association, Inc.; and

(f) The increase in utility rates at Lake of the Woods will adversely affect the further development of the community and will deter the building of additional homes at Lake of the Woods.

3. Lake of the Woods Association, Inc. requests that:

(a) Appropriate steps be taken by Lake of the Woods Utility Company to provide competent management and to eliminate the waste and inefficiency in the operation of the utility system at Lake of the Woods;

(b) An audit of the books of Lake of the Woods Utility Company be made by the State Corporation Commission of Virginia for the purpose of determining how expenses are allocated and whether or not the expenses reported are reasonable and proper;

(c) Unreasonable, inappropriate and unnecessary expenses be deleted from the financial statement of Lake of the Woods Utility Company;

(d) The impact of a rate increase upon property owners and future development at Lake of the Woods be

carefully considered in determining whether there should be a rate increase; and

(e) No rate increase be approved until such time as Lake of the Woods Utility Company clearly establishes that its losses are real and its operations are being conducted efficiently.

Lake of the Woods Association, Inc. recognizes that Lake of the Woods must have an adequate utility system in order to survive. It insists that Lake of the Woods Utility Company operate efficiently and economically. The Association and its members should not be required to pay for inefficiency and expensive operations. The future of the Association, its members and Lake of the Woods Utility Company is dependent upon the maintenance of a reasonable utility rate. The exorbitant utility rates proposed by Lake of the Woods Utility Company will seriously affect the economic life of all concerned.

LAKE OF THE WOODS ASSOCIATION, INC.

By _____
Of Counsel

Somerville, Moore & Joyner, Ltd.
P. O. Box 629
Orange, Virginia 22960,
Counsel for the Protestant,
Lake of the Woods Association, Inc.

CERTIFICATE

This is to certify that a copy of the foregoing Protest was mailed, postage prepaid, to John W. Riely, Esquire, Hunton & Williams, Post Office Box 1535, Richmond, Virginia 23212, counsel for the Applicant, this the 17th day of October, 1980.

Atwell W. Somerville
Of Counsel for Lake of
the Woods Association, Inc.

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COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION
RICHMOND

Case No. PUE800081 - Application of Lake of the Woods Utility Company to revise its tariffs

REPORT OF STEWART E. FARRAR, HEARING EXAMINER

February 18, 1981

HISTORY OF THE CASE

Pursuant to order of the Commission entered July 1, 1980, this matter came on for hearing before the undersigned Hearing Examiner on November 5, 1980. A transcript of the hearing is filed with this report.

Counsel appearing were John W. Riely, Esquire, for the applicant, Atwell W. Somerville, Esquire, for the protestant, Lake of the Woods Association, Inc., Eric M. Page, Esquire, for the Division of Consumer Counsel, Office of the Attorney General, Kenworth E. Lion, Jr., Esquire, for the Commission. Only one intervener actually testified at the hearing. However, the hearing, which was held in Senate Room B of the General Assembly Building, was attended by approximately 150 persons.

Proof of the requisite notice was received at the hearing as Exhibit A.

On June 17, 1980, the Company had originally filed an application for an emergency increase in sewerage rates under Virginia Code §56-245 designed to increase gross annual revenues by $147,648. By order of July 1, 1980, the Commission denied such application, directed the Staff to consider the appropriateness of interim relief under Virginia Code §56-240, and scheduled the present hearing. By order of July 17, 1980, the Commission found, after consideration of the Staff report, that the Company had demonstrated a reasonable probability that such an increase would be justified after a full investigation and hearing. It therefore permitted the Company to institute the above rates. The rates were ordered collected under bond and subject to refund pending completion of the case, and public notice of the scheduled hearing was directed.

On July 29, 1980, Company filed a revised application designed to increase its annual revenues by $147,648 above

the identical amount to be received through the interim rates. By order of August 4, 1980, the Commission accepted said revised application and directed the necessary revisions to the previously ordered public notice of the hearing.

Lake of the Woods Utility Company's last sewerage rate increase was granted by this Commission by order of August 5, 1977, Case No. 19867. In that case the Company was allowed to put into effect rates designed to produce approximately $112,000 in gross additional revenues based on operations for the test year ended May 31, 1977. No rate base or rate of return was determined by the Commission, as it found such increase would still leave the Company with a net operating loss of approximately $142,000, based on test period operations.

On November 24, 1980, the Examiner requested additional data from the Company concerning its employee expenses, expenses of consultants and affiliated interests, and long-term indebtedness. Company's response to this request was received on January 13, 1981. Additional correspondence from the parties concerning this new data was received through January 28, 1981.

SUMMARY OF THE HEARING RECORD

The evidence establishes that Lake of the Woods is a residential subdivision in Orange County, Virginia consisting of approximately 4,200 lots, all of which have been sold, and of which about 800 have been improved with dwellings. The lots cover approximately 2,600 acres and are clustered around a 500 acre man-made lake. About 75 percent of the homes are now occupied full time. In the recent past new homes have been added to the subdivision at the rate of about 70 per year. Commercial development is quite limited. The community is improved by hard surfaced roads, and has numerous public use facilities such as swimming pools, community building, golf course, parks, playgrounds and picnic areas. An association of property owners known as the Lake of the Woods Association, Inc. operates and maintains the common use facilities.

Lake of the Woods Utility Company ("the Company") is a wholly-owned subsidiary of AtPac Land Company of Santa Barbara, California, which purchased the Company as one of a number of acquisitions from Boise Cascade Home and Land Corporation in December of 1978. The Company provides water and sewerage services to the community. Of the

approximately 800 connected customers, all but three use both water and sewer services. Three homes have their own septic fields and purchase only water service.

The water service to the community is supplied by a conventional system of eight wells, storage tanks and mains. The Company is not requesting an increase in its metered water rates in this proceeding. Those customers who own lots but do not yet take water service are charged an availability charge of $4.00 per month. Water rates have not been increased since the commencement of service in 1967.

Sewerage service is provided by a very unusual system. It was determined early in the life of the development that the soil would not "perc" for the most part, making use of septic systems impossible. The hilly terrain in the area also prevented the use of conventional gravity flow sewer systems. Since the sewage cannot move by gravity to the central treatment facilities, it must be forced there against the pull of gravity during much of the trip. The system employed here maintains a vacuum on the sewer lines to move the sewage through the lines. Sewage discharged from a home flows by gravity to a nearby storage tank which is shared normally by one other home. From the storage tank it is pulled by vacuum pressure to one of 13 pumping stations in the subdivision; from there it is pumped into a sewage force main and then to a larger gravity flow main connected to the sewage treatment plant.

Valves on each individual storage tank are designed to open at appropriate times to allow the force of the vacuum on the line outside the tank to empty the tank. Earlier versions of these valves were electrically operated, necessitating an electric meter at each such storage tank. There are presently 260 valves of this type in the system. New valves now being installed are operated pneumatically without the necessity of electric power. Malfunctions at such storage tanks seem somewhat common, sometimes resulting in overflowing tanks which have to be pumped out by a crew with a tank truck.

The entire system is labor and energy intensive. According to Company witnesses, only about six sewer systems in the country, including Maryland Marine Utilities of Berlin, Maryland, a sister company also owned by AtPac, use similar technology.

Sewer rates in effect before the August 1, 1980, interim increase were a flat usage rate of $8.00 per month for residential customers, a $3.75 per month availability charge for lots not connected to the system, and sewer connection and installation fees totaling $1,070.

Under the interim rates, the $8.00 per month fee was raised to $24.00 per month, and would be raised to $40.00 per month under the amended application. The $3.75 per month availability charge would not be changed, but the amended application would increase the sewer connection and installation fees to a total of $1,450. As Staff accountant Leis noted in his report, the change in basic rates would be a 400 percent increase in rates and should cause a 116 percent increase in gross annual revenue for the Company.

Mr. Leis' prefiled testimony indicated that the Company suffered an adjusted net operating loss of $170,667 in its sewerage operations for the test year ended December 31, 1979 with a sewerage rate base of $1,979,507. Granting the Company's application in full would produce additional revenue of $295,296, and would give the Company net operating income of $115,258 on a rate base of $1,979,835, for a return of 5.82 percent, based on test year operations. (A correction he made during his oral testimony to the allowance for gross receipts tax expenses would add about $1,500 to the Company's additional expenses caused by the rate increase.)

Mr. Thomas L. Thorpe, General Manager of the Company from Berlin, Maryland, was the Company's first witness. He said that although the financial condition of the Company's water operations was generally satisfactory, an analysis of the sewerage operations showed a net operating loss of $205,698 during the calendar year 1979. He attributed the loss to increases in the basic costs of maintaining and operating the sewerage system, especially the cost of electric power and payroll, which are the two largest categories of operating expenses for the Company.

Thorpe said that payroll expenses were about $134,000 during the test period and were projected to be $145,000 for 1980. He said the time of 16.1 personnel is charged to the Company, the fraction being due to the fact that the time of four people in Berlin, Maryland, including himself, is allocated in various proportions between this Company and Maryland Marine Utilities. Fifteen people

actually work on site at Lake of the Woods. These include a field superintendent, maintenance foreman, construction foreman, two office workers, and various construction and maintenance personnel.

Although Staff engineer Jack Tice said he felt the number of employees was excessively high, constituting one person per 50 customers, Mr. Thorpe said he did not feel that a reduction in personnel could be achieved without affecting service, claiming that the maintenance and construction problems associated with this system require a larger labor force than does the traditional sewer system. Thorpe noted that the Company has had as many as 21 employees, in 1978.

Thorpe explained that the salaries of the personnel are allocated between water and sewer operations based on a work order system. He agreed that such an allocation of the time of administrative personnel was something of an educated guess, but said that the time of labor and construction people could be accurately apportioned according to the work orders produced.

Thorpe said that a field superintendent lives at the subdivision, was actively involved in the construction of the system, and in Thorpe's opinion is fully capable of handling the day-to-day operations of the Company.

The construction work necessary at the Company involves such things as adding new storage tanks as needed, replacing old tanks and valves, and upgrading vacuum lines to larger sizes.

The protestant's views on the size of the work force and its effectiveness were quite different from that of the Company's.

Mr. Alan Potter, President of Lake of the Woods Association, claimed that there is no effective supervision on site at the community, and that this defect encouraged considerable "feather-bedding".

Mr. Warren Lodge, General Manager of the Association, echoed Potter's sentiments. He said that the Company's witnesses had indicated before this Commission in 1975 that there would be a full-time manager on site and that a total of eight people should be able to maintain and operate the system. He claimed the field superintendent was not capable of doing an adequate job and that the size

of the staff was grossly inflated due to lack of management supervision and technical ability. He said often no satisfactory answer is found to serious service problems until calls are made to the personnel in Maryland. He cited instances of employees engaged in horseplay and driving aimlessly around the subdivision as examples of conditions caused by lack of effective supervision on the site.

According to Lodge, there have been hundreds of service difficulties in his nine months with the Association. He listed various problems such as overflowing sewage holding tanks, broken sewer lines, sewage running into the lake, excessive odor from pumping stations, and lack of adequate water pressure. He said that in some cases, overflowing tanks are simply pumped out repeatedly and no attempt is made to solve the underlying technical problem.

Considerable criticism was also leveled against the extensive use of outside consultants and services from affiliated interests in the conduct of operations.

For example, the Company's accounting data was presented by Robert L. Frasher of Brockmeier Consulting Engineers, Inc. of Santa Monica, California. This firm is not an affiliate of the Company, but does charge it a retainer of $1,250 per month, and according to Frasher, provides management consulting on rates and utility matters, design services, master planning, and capital budgeting. Mr. Thorpe said the Company also provides help on problems that arise with regard to the specialized technology of the vacuum sewer system. Major design projects are not covered by the retainer, and are billed separately. Brockmeier also is on retainer with the sister company, Maryland Marine Utilities. Thorpe said that Mr. Brockmeier had been to Lake of the Woods four times in 1980 in trips of up to one week's duration. Data received from the Company after the hearing reveals that the Brockmeier firm was paid $16,510.95 during the test year.

Thorpe defended the use of that firm since not many engineering concerns understand vacuum sewer technology, and Brockmeier is very familiar with this type of system. Mr. Thorpe denied that the work done by Brockmeier was duplicative of services performed by other employees or affiliates of the Company.

William W. Carpenter, the protestant's accounting witness, eliminated the $15,000 annual Brockmeier retainer

from the Company's operating expenses, as he said personnel of the firm are rarely at Lake of the Woods and he had seen no proof of consulting services actually being performed.

The Company also uses various services provided by affiliated companies. To repeat, during December of 1978, all of the stock of the Company was sold to AtPac Land Company. This sale was approved by the Commission in April, 1979. Transcontinental Development Company (TDC), described as a partner of AtPac by Mr. Thorpe, has an agreement with the Company to provide a number of administrative services, principally with regard to insurance, employee benefit programs, budget review and preparation, accounting reviews, and financial data.

Frasher said TDC is paid a fee equal to 5 percent of Lake of the Woods Utility Company's operating expenses for its services.

Mention has already been made of the fact that certain personnel of Maryland Marine Utilities, another affiliate, provide day-to-day administration, accounting, and billing services for the Company.

No actual contracts between the Company and its affiliates were introduced into evidence at the hearing. It was clear at that time, however, that such arrangements have not yet been approved under the Affiliates Act. Previous affiliate agreements had been approved between Lake of the Woods Utility Company and its former parent, Boise Cascade, but Staff accountant Leis pointed out that new agreements between the present parties are now necessary. Leis said he had not seen an application for such new agreements, nor had the Company provided the Staff with adequate documentation to verify the actual costs to the affiliated companies of providing services to the Company. Leis had included $26,060 of expenses in his financial statements, based on fee percentages in the old agreements, for informational purposes only, but said that the inclusion of such figures should not be construed to imply Staff acceptance of them. The affiliate expenses had not been justified, in his opinion, to the degree which the Staff would require in order to approve their reasonableness.

Mr. Lion contended in his closing statement that even though AtPac purchased the stock of the utility in April 1979, no affiliate agreement was supplied to the Commission until October 29, 1980. He said that adequate information

to support these expenses had not been presented as required by statute, and that they should be disallowed.

As part of the data he furnished on January 13, Mr. Riely submitted a copy of an application for approval of certain affiliates agreements which he stated was being filed contemporaneously with the Commission.

This application recites basically that AtPac has agreed to make loans to the Company when required; that the Company receives management assistance from Maryland Marine Utilities in Berlin, Maryland; and that it receives additional management services from TDC in Santa Barbara, California. According to the agreements supplied, Maryland Marine Utilities is paid for its services on a time-expended basis plus out-of-pocket expenses, and TDC is paid a monthly fee of $1,500 plus expenses.

Problems with affiliates arose once again when discussing the major portion of the Company's indebtedness. According to the testimony received at the hearing, in 1975, Boise Cascade had purchased Lake of the Woods Service Company and had transferred the assets to the Boise subsidiary, Lake of the Woods Utility Company. In return Boise received an 8 percent note and stock from the utility company. This note payable is still shown on the balance sheet in the amount of $2,402,702. Questions developed as to the disposition of this note upon the sale of the Company from Boise to AtPac Land Company in 1978. Information on this subject at the hearing was sketchy and conflicting.

Mr. Thorpe stated that the utility company was simply one part of a package acquisition by AtPac Land Company from Boise. However, he said he did not know the actual details of the transaction. He did say he believed the above note was now payable to an affiliate of AtPac, name unknown.

Mr. Frasher testified that the note is not held by an affiliate, to his knowledge, but is held by Perry R. Bass, Inc., and he believed this assignment may have been made at about the time of the sale of the Company to AtPac.

Mr. Leis testified that he presumed that the interest on the note was payable to the new parent company, AtPac, but had not seen any documentation to that affect.

On January 13, 1981, Company submitted further information about this note. That information indicates that a demand

note was given by the Company to Boise Cascade on December 1, 1978, in the above amount, bearing 8 percent interest. When AtPac purchased the Company's stock, the note was sold by Boise to Perry R. Bass, Inc., which purchased various debts from different entities at that time for a discount, amount unstated. According to the application, the Bass corporation later transferred interests in these debts to Perry R. Bass, a shareholder, and another corporation owned by Perry R. Bass. The application states that Perry R. Bass is the father of sons, who, in general terms, have various business interests which can be traced eventually to Lake of the Woods Utility Company. The application contends, however, that neither Perry R. Bass, Inc. nor any co-owners of the note have holdings in any company with direct ties to the utility.

It does seem clear from all the evidence that interest is not being paid on this note, and that no one is making efforts to force such payments.

AtPac Land Company paid $900,000 for 100 percent of the Company's stock in December 1978. This having been established, and the status of the above note being doubtful, Mr. Lion argued at the close of the hearing that under the Commission's policy of allowing only a return on actual investment in the utility plant, an acquisition adjustment should be made to the Company's rate base to reflect a value of only $900,000 on a total Company basis, or approximately 3/4 of that amount on a sewerage operations basis. (The adjusted sewerage operations rate base was listed at approximately $1.9 million on the Staff accounting statements.)

Mr. Riely objected to such a proposal, arguing that the rate base is composed of the plant and equipment which is designed to be used for public service, not the purchase price of the stock of the Company. He also argued that no allowance should be made in fixing rates simply because the Company was in serious financial condition when AtPac purchased it, or for the fact that it presently has only about 800 out of a potential 4,200 customers. In his opinion the entire rate base of the Company is used and useful and merits an adequate return.

As mentioned earlier, a major item of the Company's expense is its electric power cost. Mr. Thorpe said that the system demands over 200 kilowatts of electricity per hour, which in 1979 cost about $108,000. He projected that for the 12 months ended December 31, 1980, the cost

would be $141,420, a 31 percent increase over the test year. He explained that in arriving at this estimate he had applied the rates of Rappahannock Electric Cooperative in effect at the end of 1979 and a three month's average of the fuel adjustment cost for the months of January through March, 1980, to the Company's kwh usage during 1979. (Mr. Leis had increased electric power costs on his statements by $27,929, based on the Company's projection.)

Several other miscellaneous points were raised by the parties concerning the Company's operating results for the test year.

First, the protestant and the Attorney General contended that the Commission should examine the Company's financial condition on a total company basis rather than looking only at the sewerage operations, as the Company proposed. The Staff accountant's statements were prepared on a sewer operations basis. Mr. Riely stressed that the Company has historically been regulated on the basis of separate services, and he argued that this is in accord with the Commission's traditional approach. The opposing parties replied that except in three cases, all customers of the utility take both water and sewer service. Mr. Lodge said that the soil percolation problems would make it mandatory that future homes take sewer service, and lot owners would not be permitted to drill individual wells on the lot. All new customers are therefore likely to need both types of services. The protestant also emphasized the inherent difficulties in making allocations of various expenses between two different departments, and said that the many judgmental decisions necessary in this process made such separations inherently suspect. Protestant's accounting witness had performed his analysis on a total company basis, and he said that he felt that was a much more simple and logical method.

On another issue, the Company figures reflected about a 60 percent uncollectible rate on total billings for the test year, a major portion of which consisted of availability fees. Mr. Thorpe said that the Company made the "usual" efforts to collect these bills, such as letters to delinquent customers, but claimed that the Company had little success since customers being charged only an availability fee had no service which could be terminated for nonpayment. He said the utility had never used formal legal action in an attempt to collect these amounts.

Mr. Leis had allowed only a 1 percent bad debt expense, which decreased expenses for the test year by over $21,000. He admitted this was to an extent an arbitrary allowance, but he said that it was in line with current Staff policy and with the uncollectible experience of other regulated utilities. Mr. Riely argued, however, in effect, that most utilities are not in a position of attempting to collect bills from customers to which they render no service and that this unique situation merited a larger bad debt allowance.

The last significant expense item needing some comment here was that involving the cost of conducting this rate case. Mr. Frasher, of Brockmeier Consulting Engineers, said that the projected cost of the rate case was $28,000, to be amortized over four years. He said this figure was an estimate based on the time of his firm, legal expenses, and similar costs. He estimated the cost of his firm's participation alone would amount to about $25,000. Mr. Leis had made a similar adjustment to his figures, and noted that $28,000 was "purely an estimate." (Tr. p. 205). He said however that as of August 31, 1980, $19,640 had been booked for rate case expenses, and he assumed that before the case was over the total expenses would equal the figure requested.

Transcending all arguments about individual expense items and accounting treatments was the Protestant's central theme that a rate increase of the magnitude proposed would be devastating to the community of Lake of the Woods. Alan Potter, President of the Association, contended that Lake of the Woods is important to Orange County. It is the third largest population center in the County and contributes 15 percent of its total real estate taxes. He said the proposed rates would place the development at a tremendous disadvantage compared to other parts of the general Northern Virginia area in its ability to attract new residents. He presented an exhibit which showed sewer rates in the general area to range from about $73 a year in Alexandria to $188 a year in Fairfax City, as compared to a proposed $480 a year in Lake of the Woods. Upon objection by Mr. Riely, he denied that he was presenting these figures to try to have rates fixed on a comparative basis, but merely to show that a person planning to build a new home in the area will be disinclined to locate in Lake of the Woods. Potter concluded that even the interim rate increase "will kill the future development and growth of this community" (Tr. p. 230).

Several witnesses said the impact of the rate increase on present residents with fixed incomes would be very severe. If they found they could not pay the increased rates, they would be forced to offer their property for sale, but yet might not be able to find a buyer at a reasonable price for the very reason which would compel them to sell. Warren Lodge claimed that "both Lake of the Woods and Lake of the Woods Utility Company rely upon steady growth to survive. The large sewerage rate increase will cause us both to shrivel up and die." (Tr. p. 247).

Albin L. Lindall, a resident of Lake of the Woods and a licensed real estate broker, testified that he has been active in the real estate field in the Lake of the Woods area for the past five years. In the past, about 70 new homes have been built in the development each year, and the market for existing homes has been a good one until recently. However, he said that when the proposed increase was announced, the effect on salability of property was immediate and adverse. Several prospective lot purchasers have broken off negotiations, and the sale of existing homes has been hampered. He said that to the best of his knowledge, the sewer charge proposed would exceed the taxes on every piece of property within Lake of the Woods, and in some instances would more than triple them. He said that even the interim increase level would cause the growth rate of the community to decline, and the larger rate increase would have an even more damaging effect.

Mr. George P. Beard, Jr., Chairman of the Board of the Second National Bank of Culpeper, said that this situation makes his bank much more cautious in making mortgage money available in the development, and also causes it concern with the security of existing mortgages, which amount to approximately $1 million at present.

In the same vein, Mr. Leis remarked, "This Company isn't going to do anything until they get a greater density on that sewer system, with greater customer load." (Tr. pp. 195, 196)

Mr. Thorpe said that although the Company had considered the impact of this increase on the present customers and the prospects for future development in the area, he really did not have any opinion as to whether the increase would slow new construction there. He went on to say that a different concern for him is that the parent company cannot continue to fund an operation which cannot even meet expenses

and which does not have the ability to borrow money from outside sources.

DISCUSSION OF THE ISSUES

As is obvious by now, this case did not lack for numerous and complex issues. An attempt will be made here to discuss the subjects in ascending order of difficulty.

First, I am of the opinion that the revenue requirements of this Company should be determined on a total company basis in the future. This does not mean that I favor a single uniform rate for combined water and sewer services. Different rates for different services are recognized as appropriate for all utility companies. It does mean that the Commission should determine total company revenue requirements, and should not attempt to treat this Company as two different entities for ratemaking purposes. The much more logical method is to focus on the total company, and there is no reason not to follow this approach in this case. Out of approximately 800 connected customers, only three do not take both water and sewer service. The evidence is that all future connections will probably require both types of service. The same personnel serve both systems.

It is true that in this Company's last rate case, Case No. 19867, Final Order entered August 5, 1977, an allocation between the two operations was made. I am unable, however, to read anything in that order which indicates that this was a contested issue in the case or that the Commission specifically approved of this procedure. Virtually the only mention of the subject came when the Commission noted: "In this proceeding, Lake of the Woods is requesting an increase in its rates for sewer service; it is not proposing any change in its rates for water service." Application of Lake of the Woods Utility Company, 1977 SCC 299, 300. The topic was never mentioned further, and the Commission merely proceeded to examine the Company's sewer operations, presumably because that was the format in which the evidence was presented. I do not see in this order a mandate to treat this Company on a separated basis.

Inasmuch as the Staff analyzed only the sewerage operations for purposes of this case, in my opinion there is insufficient evidence in the record to determine revenue requirements on a total company basis in this proceeding. I respectfully recommend, however, that the Commission order that this Company be treated as a single entity in all future cases.

I agree with Mr. Leis that the bad debt allowance should be limited to one percent of revenues. It is appropriate to make some allowance for bad debts with any company, as uncollectibles are a fact of business life. In making rates for the future, however, we are not bound to recognize the actual bad debt expense of the Company, but only a reasonable amount. It is the responsibility of the Company to undertake collection efforts to bring its experience in line with that of other regulated utilities. This Company has not done that. It has written letters to its delinquent customers, but it has never undertaken any legal action against them. The Company sought to imply during the hearing that the costs of such action would outweigh the benefits. Apparently it has never investigated the possibility of contingent fee arrangements on collection matters.

The collection of bad debts directly affects the profitability of the Company. If management chooses to forgo the effort to collect these revenues it may do so; however, I do not believe it should ask the ratepayers to make up for this relinquished opportunity.

The bad debt allowance is not designed solely to reflect actual experience, but should also recognize the fact that it would be unjust to charge paying customers an unreasonable rate which burdens them with the sins of their delinquent neighbors. Those customers who do not pay have little concern about the rate which is set, but it is the others whom we must protect in this proceeding.

Next to be discussed are the Company's arrangements with affiliated interests. The figures in Mr. Leis' statements for these items of expense are derived from the Company's previous agreements with its former parent company, Boise Cascade, and have no relationship to the Company's future expense levels. They should, therefore, be removed from the Company's allowed operating expenses.

Should, however, a different figure be substituted to take account of the Company's relationship with its new affiliates, TDC, Maryland Marine Utilities, and AtPac? Virginia Code §56-77 provides that:

> No contract or arrangement providing for the furnishing of management, supervisory, construction, engineering, accounting, legal, financial, or similar

> services, . . . made or entered into between a public service company and any affiliated interest shall be valid or effective unless and until it shall have been filed with and approved by the Commission. It shall be the duty of every public service company to file with the Commission a verified copy of any such contract or arrangement, regardless of the amount involved, ...

AtPac purchased the utility company in December, 1978. The date(s) upon which the Company originally made arrangements for these affiliated services are not in the record. Mr. Lion did represent in his closing statement, and was not contradicted, that the Company had not filed any affiliated agreements with the Commission until October 29, 1980, seven days before the hearing. The formal application for approval of these agreements was not filed until January 13, 1981. That is a very long time after the purchase of the Company by the parent, and the evidence from the Company's own witnesses implies that such service agreements have actually been in effect for some time. Under Code §56-77, supra, these agreements are not valid or effective because they have not been approved by the Commission.

Code §56-78 states the Commission may, in any rate proceeding, disallow payments to affiliates, "unless satisfactory proof is submitted to the Commission of the cost to the affiliated interest rendering the service . . .." Code §56-79 provides that:

> No proof shall be satisfactory, within the meaning of the foregoing sections, unless it includes the original (or verified copies) of the relevant cost records and other relevant accounts of the affiliated interest, or such abstract thereof or summary taken therefrom, as the Commission may deem adequate, properly identified and duly authenticated; provided, however, that the Commission may, where reasonable, approve or disapprove such contracts or arrangements without the submission of such cost records or accounts.

The record in this case was not only deficient, it was completely devoid of any such cost data, at least until January 13 of this year. Even the data filed on that date cannot be said to provide much in the way of actual cost figures, as opposed to estimates of the value of affiliated services. I do not believe it is reasonable in this case to excuse the failure to submit full cost records and accounts.

Thus, there is ample statutory basis for refusing to make allowance for any affiliated expenses.

Based on what we do know about the services furnished by TDC, I also have considerable doubt as to the reasonableness of such expenses even had they been furnished by nonaffiliated parties, however. That company was said by Mr. Thorpe to provide services related to insurance, employee benefit programs, budget review, accounting and financial data. For this it is paid, according to Mr. Frasher, 5 percent of Lake of the Woods operating expenses for the year, which during the year 1979 would have resulted in a fee of over $24,000 based on his figures for the total company's adjusted operating expenses. According to the application received recently, the amount of the fee is now $1,500 per month, $18,000 annually. Whichever figure is correct, from reading the above list of services, one would think that such assistance was being rendered to a large corporation with hundreds of employees and complicated budgetary and financial problems. This Company, it bears repeating, has 15 on-site employees and about 800 active customers. Why such a small company needs to pay an outside consultant to handle its insurance and employee benefit programs, for example, was never explained. There are certain basic functions which a small company's internal management should be expected to be competent to perform itself, with reasonable amounts of outside assistance on a periodic basis. I saw nothing in the evidence to lead me to conclude that this Company's employee, financial, or accounting situations are so complex as to require such expensive extra services.

Company's adjustment to increase electric power expenses about 31 percent over test year levels based on its estimates for 1980 contains all the elements of a projected test year concept. The Company took its energy usage for the test year and multiplied it by rates in effect at the end of the year plus an average fuel cost based on fuel rates for the first three months of 1980. In this calculation we thus have three items of conjecture: (1) That the Company's power usage will remain the same in the future as in the

test year; (2) That the electric utility's base rates will remain fixed throughout the period; and (3) That fuel cost levels will remain fixed at the rates established in the first quarter of the year. This Commission traditionally does not allow adjustments for future expenses to be incurred within one year after the test year unless they are known and definite. See Virginia Code §56-235.2. A contractual wage increase is a good example of such an allowed adjustment. I believe that failure to allow more conjectural adjustments arises not because of a belief that expenses will remain fixed, but from a policy decision that permitting such expenses to be projected involves too much speculation and opportunity for exaggeration when compared to the historic test year approach, as modified by the "known and definite" standard.

Going beyond these general legal considerations, the Company's manner of calculating the adjustment also appears to be rather arbitrary. The Company's power usage for 1979 has not been shown to be a representative level over time, for example. Also, the use of the first quarter 1980 fuel factors may well be unrepresentative of future trends, inasmuch as fuel costs for electric utilities have tended to fluctuate significantly in the recent past. Third, the reason for using base rates from one period and fuel costs from another period was not explained. In short, I do not believe the Company has shown that its estimate is a more reasonable figure for ratemaking purposes than that shown on its books for the test period.

For these reasons, I do not believe the proposed upward adjustment in power expenses should be allowed.

The proposed allowance for the cost of this rate case ($28,000 amortized over four years) is excessive in my opinion. That figure exceeds 11 percent of the sewer operation's adjusted test year revenues, as determined by Mr. Leis. I have said before, and will repeat, that I do not believe this Commission is required to impose upon the ratepayers whatever a company might choose to spend for legal and accounting assistance in connection with a rate case.

Mr. Frasher said that $25,000 of the above amount was destined to go to his firm, Brockmeier Consulting Engineers. This presumably leaves $3,000 for legal counsel, and I find that figure is reasonable. It is generally in line with other rate case allowances made by this Commission for small utility companies.

In addition, based on the evidence which was presented, I fail to see why it was necessary for the Brockmeier firm to participate in this case at all. To begin with, Mr. Thorpe, from Maryland Marine Utilities, did quite a good job of describing the technology of the sewer system, its problems, and other details of the Company's operations. The Brockmeier witness added virtually nothing to this aspect of the case, although that firm is supposedly expert in such engineering matters. In fact, that witness' testimony was nothing more or less than that which could have been given by any competent accountant familiar with the Company's operations and with utility accounting. In addition, the witness lacked specific knowledge of many facets of the Company's operations. For example, he did not know the details of the purchase of the Company by AtPac Land Company, (Tr. p. 133); knew little about the various accounts payable to associated companies, (Tr. pp. 137, 138); did not know how much was paid to those furnishing bookkeeping and data processing services to the Company, (Tr. p. 140); and was uncertain as to the relationship, if any, of AtPac and TDC to the holder of the Company's major long-term indebtedness, (Tr. pp. 147, 148). In short, so far as appears in the record, Brockmeier Consulting Engineers merely prepared very generalized accounting testimony, for which it expects to be paid $25,000 (over and above the $15,000 annual retainer already charged by the firm). Quite a bit of this amount was undoubtedley consumed by coast-to-coast travel and telephone expenses. I do not believe this is a reasonable proposal, and I find that it should be disallowed for ratemaking purposes. Rate case expenses of $3,000 are approved for amortization over four years.

On a related issue, I am not persuaded, however, that it would be advisable to disallow the $16,510.95, consisting of retainers and additional compensation, paid to Brockmeier for services during the test year. I have already alluded to the technological problems with which this system seems to be plagued, and, at least based on this record, it appears prudent to allow the Company to retain engineering expertise to deal with these matters.

The last specific expense item to be discussed is that dealing with payroll. Company General Manager Thorpe said the payroll in 1979 was $134,000, not including taxes, overhead and benefits. (Tr. p. 38). This figure constitutes almost 30 percent of the total Company's per books operation and maintenance expenses for the test year. Staff engineer

Tice notes that the 16.1 employees are about one for every 50 customers, compared to a gravity flow system of Lake of the Woods size within Mr. Tice's knowledge which has a ratio of one employee to 240 customers. Mr. Tice considers the number of employees at Lake of the Woods to be excessive. (Tr. p. 215). There is evidence of poor service, about which more will be said later, and evidence of wasting of time by employees. (Tr. pp. 254-256). The Company has five people classified as full-time construction workers - an equipment operator, two laborers, a construction foreman, and a construction lead man (Tr. pp. 49, 95), even though engineer Tice said that the construction work in the development does not appear to be a daily operation. (Tr. p. 215).

In my opinion, there is therefore considerable evidence that this company is probably overstaffed. It is not possible from this record to quantify with any degree of certainty the amount to which labor expenses should be reduced, if any, because of this situation, however. Engineer Tice said he felt the Company should provide a detailed accounting of its work force (Tr. p. 216), and I agree that this area merits further study. Information received from the Company on January 13, 1981 on this topic was of limited additional assistance, since it simply listed the names of all people employed by the Company during the test year, the amounts paid to each, and a note as to whether each was still employed at the end of the year. Rather than suggest a specific reduction in labor expenses at this time, I therefore recommend that the Commission direct the Staff to undertake a separate, detailed examination of the entire employment situation at Lake of the Woods to include a determination of how many and what types of employees are reasonably necessary to operate and maintain the system, both on and off-site, reasonable pay levels for such personnel, and the effectiveness of on-site management in directing and supervising the work force.

That completes my discussion of several important individual issues in this case. However, there is a much more pervasive problem with this application which encompasses all the above matters and much more besides. To deal exclusively with individual items such as those above, in this case, is to concentrate on the trees and miss the forest. The following discussion therefore concerns an alternative, and equally important, ground for my decision in this case.

This Company's application is founded on the premise that a regulated utility is always entitled to rates which will permit it to cover its operating expenses and earn a reasonable return on its investment. I agree that this is probably one of the most widely quoted and accepted general principles of ratemaking, and I also agree that one could easily become convinced that there are no exceptions to such a rule.

I believe there are exceptions, however, and that they are constitutionally recognized, although perhaps not often applied. Failure to apply them widely, however, is probably because the factual situation in an individual case rarely calls for it. I hope to demonstrate that there is no constitutional requirement that this principle be followed in every case, and especially not in this one.

Indications that such a rule is not absolute are found early in the history of regulation in this country.

In Smyth v. Ames, 169 U.S. 466, 547, 42 L.Ed. 819, 849 (1898) the Court said:

> What the company is entitled to ask is a fair return upon the value of that which it employs for the public convenience. On the other hand, what the public is entitled to demand is that no more be exacted from it . . . than the services . . . are reasonably worth.

Surely it would be naive to suggest that the Court thought those two principles need never come into conflict. Rather I believe it must have recognized that neither right was absolute if it impinged unreasonably on the other, and that if rates which would give a utility a fair return would nevertheless exceed the value of the service to the consumer, an accomodation might be necessary.

To the same effect, in Denver Union Stockyard Company v. U.S., 304 U.S. 470, 475, 82 L.Ed. 1469, 1475 (1938) the Court said of the regulated company there:

> . . . appellant is entitled to rates, not per se excessive and extortionate, sufficient to yield a reasonable rate of return upon the value of property used, at the time it is being used, to render the services. (Emphasis supplied)

In Simpson v. Shepard, "The Minnesota Rate Cases", 230 U.S. 352, 433-434, 57 L.Ed. 1511, 1555 (1913), the Court made a similar observation:

> The property of the railroad corporation has been devoted to a public use. There is always the obligation springing from the nature of the business in which it is engaged - which private exigency may not be permitted to ignore - that there shall not be an exorbitant charge for the service rendered.

Priest has also pointed to the conflict between the value of the service to the ratepayer as opposed to the utility's desire for a full recovery under traditional accounting standards:

> Ours is a profit and loss economy and regulation cannot alter that fact. It is axiomatic that a utility rate cannot exceed the value of the service rendered. When the rate charged exceeds the economic worth of the service it renders, that utility is on its way to bankruptcy. 2 A.J.G. Priest, Principles of Public Utility Regulation 499 (1969).

These authorities point to the inescapable conclusion, I believe, that a utility's right to full rate relief based on general accounting principles may be tempered by a consideration of the impact of the proposed rates on the consumer. The Commission itself recognized this principle even in this Company's last rate case:

> If total revenue were the only consideration in this case the Commission should approve the proposed increase in rates. However, before deciding upon the reasonableness of the proposed rates it is necessary to consider their affect upon individual customers. Application of Lake of the Woods Utility Company, 1977 S.C.C. 299, 301.

Of course, in the case of FPC v. Hope Natural Gas Company, 320 U.S. 591, 88 L.Ed. 333 (1944), this famous statement regarding the investors' prerogative is found:

> . . . the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the finanical integrity of the enterprise, so as to maintain its credit and to attract capital. Hope, at 603, 88 L.Ed. at 345.

Even in that case, however, there is an inference in the very next sentence of the Opinion that that principle is not absolute in all circumstances. "The conditions under which more or less might be allowed are not important here." Hope, supra. Though furnishing no explicit guidance, this sentence certainly is at least an indication that the "universal rule" might be modified when appropriate.

Reinforcing this conclusion is language found in the more recent "Permian Basin Area Rate Cases" 390 U.S. 747, 20 L.Ed. 2d 312 (1968). The Court, there dealing with a federal statute, quoted the usual criteria from the Hope case, but then said:

> These criteria, . . . remain pertinent, but they scarcely exhaust the relevant considerations.
>
> The Commission cannot confine its inquiries either to the computation

> of costs of service or to conjectures about the prospective responses of the capital market; it is instead obliged at each step of its regulatory process to assess the requirements of the broad public interests entrusted to its protection by Congress. Accordingly, the "end result" of the Commission's orders must be measured as much by the success with which they protect those interests as by the effectiveness with which they "maintain credit . . . and . . . attract capital." Permian Basin, at 791, 20 L.Ed. 2d at 350.

Later in the Opinion this proposition is repeated:

> The Commisson's responsibilities necessarily oblige it to give continuing attention to values that may be reflected only imperfectly by producers' costs; a regulatory method that excluded as immaterial all but current or projected costs could not properly serve the consumer interests placed under the Commission's protection. Permian Basin, at 815, 20 L.Ed. 2d at 363.

Under what circumstances, then, is it appropriate to disregard traditional adjusted-income-statement, rate-of-return accounting techniques when making rates? We have already seen that occasions on which the impact on the consumer would be excessive is one such circumstance, but there are others as well.

In San Diego Land and Town Company v. Jasper, 189 U.S. 439, 47 L.Ed. 892 (1903) the Court was faced with a situation in which a County Board of Supervisors had based the rates of a water and irrigation company on the assumption that the amount of water available for irrigation was enough for about 6,000 acres. They then fixed the rates as if the company supplied this acreage, although it actually supplied much less. Naturally, the actual receipts were below the receipts thus assumed by the Board in fixing rates, and the company complained that it was

being denied an adequate return under the California statute, which mandated that the return on rate base be set at between 6 and 18 percent. The Court, noting that it was first necessary to distinguish between the Constitution and the state statute said:

> If a plant is built, as probably this was, for a larger area than it finds itself able to supply, or, apart from that, if it does not, as yet, have the customers contemplated, neither justice nor the Constitution requires that, say, two-thirds of the contemplated number should pay a full return. . . . If the original company embarked upon a great speculation which has not turned out as expected, more modest valuations are a result to which it must make up its mind. San Diego Land and Town Company, at 446-447, 47 L.Ed. 896.

A Virginia case has treated the same area. In Petersburg Gas Company v. Peterburg, 132 Va. 82 (1922), the Court, citing with approval San Diego Land and Town Company, supra, said that:

> a rate may be reasonable, although it fails to produce an adequate return . . . owing to the fact that the business has not developed sufficiently to be remunerative, or to the fact that the plant is on a larger scale than is justified by the present demand. Petersburg Gas Company, at 102.

Those cases concerned developing companies, but the U. S. Supreme Court has made similar comments with regard to failing companies as well. See Market Street Railway v. R.R. Comm. of Calif., 324 U.S. 548, 566, 89 L.Ed. 1171, 1184 (1945).

Finally, as this Commission has long recognized, the adequacy of service furnished by the utility is also a factor to be considered when fixing its return. App. of Continental Tele. Co. of Va., Case No. PUC800019 (Dec. 19,

1980), App. of C&P Tele. Co. of Va., 1977 S.C.C. 139 at 152. See Virginia Code §56-234 and 1 A.J.G. Priest, Principles of Public Utility Regulation 207-208, 279 (1969).

Applying these principles to the case at hand, it is obvious first of all that the amount of the requested rate increase is exorbitant from the standpoint of the consumer. The evidence establishes that such an increase would be devastating to this community. We have the testimony of an experienced real estate agent and banker that even the interim rates and the pendency of this case have had a depressing effect on the real estate market and the availability of mortgage money. Rates so significantly higher than those available in adjacent areas will make Lake of the Woods unattractive to prospective home purchasers, and will discourage those who now own vacant lots from building. As many residents pointed out, the viability of the Company is tied to the viability of the community. Rates which will strangle growth, or cause an out-migration, can hardly benefit this Company. The evidence is that the proposed rates would have this effect.

It is particularly necessary to be mindful of the impact of drastic rate increases on consumers of residential utility services. When, in the words of Priest, the rate charged exceeds the economic worth of the service, purchasers of some regulated services can make this quickly apparent. Transportation customers, for example, can simply cease using the service, as they did in Market Street Railway, supra, and substitute other methods of travel. See also Re D.C. Transit System, Inc., 85 PUR3rd 1 (1970). Except in rare situations, such as switching from electric to gas heat for example, the matter is not so easy for customers who purchase residential services. Short of selling their home, they have little means of substitution for the service offered. Regulatory agencies should therefore be especially watchful to avoid trapping such consumers in intolerable situations from which they have no realistic escape.

Secondly, despite considerable evidence of excessive numbers of personnel, there is also much evidence of poor service. Inadequate service is unacceptable by any utility and at any price, but poor service in the sewerage area can be very disagreeable and disruptive to customers' lives indeed.

Third, this case falls squarely in line with San Diego Land and Town Company and Petersburg Gas Company, supra, in respect to the extent of development which has occurred

so far in the area. Approximately 4,200 lots are available and in fact have been sold, but only about 800 have been built upon. The Company therefore now serves barely 1/5th of its potential. Despite the number of years the Company may have been in existence, it is still in a real sense in its developmental stage. The utility was built originally to serve the entire subdivision. Lines, pumping stations, and treatment facilities are in place. Apparently only additional individual storage tanks, lot connections, and some upgrading of facilities would be necessary to serve all 4,200 lots. It could therefore scarcely be reasonable to force a fraction of the potential customers to pay for a system designed to serve many more.

The circumstances under which AtPac Land Company purchased this utility also should not be forgotten. As Mr. Riely agreed, the Company was a losing proposition at that time. The Company's own exhibits state that the total company suffered adjusted net operating losses of over $163,000 during 1979 on a total company adjusted rate base of about $2.4 million. Apparently, a similar environment had existed for some time. In the last rate case, Case No. 19867, concluded by order of August 5, 1977, the Commission approved rates which were designed merely to reduce the operating loss for the test year ended May 31, 1977 from about $222,000 to $142,000. Even the Company's proposed rates in that case would have still resulted in a test year net operating loss of over $86,000.

AtPac must therefore be charged with the knowledge of Lake of the Woods' serious financial condition when it purchased it as part of a package transaction from Boise Cascade. It must also be charged with knowledge of the unique, costly, and troublesome sewer system employed at the development. As we have seen, the system is labor and energy intensive; it is prone to frequent malfunctions; it apparently requires constant tinkering to keep it working. The fact that there are only six others like it in the country does not speak well for its acceptance by the industry.

AtPac also knew of other conditions mentioned earlier - that only 1/5th of the lots are occupied at the present, and that a massive rate increase would be necessary to bring this Company into the black. Indeed, it appears that a reasonably prudent investor would have considered all these matters when negotiating the purchase price.

Nevertheless, having faced these unpleasant facts and future prospects at the time it bought the Company, it now seeks to have this Commission erase all these woes with one stroke of the pen, to increase revenues by 116 percent, to raise rates by 400 percent, to allow the Company to cover all its operating expenses, to include in its operating expenses quite a bit of unsubstantiated payments to affiliates, and not only that, but to give it a return on its investment; all within the space of two years after it made this distinctly risky investment. If the Constitution requires us to accede to these demands, purchases of ailing utility companies will become some of the most desirable investment opportunities in years.

In the Bluefield case, it was said:

> A public utility is entitled to such rates as will permit it to earn a return . . . equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties . . .. Bluefield W. W. and Imp. Co. v. Pub. Ser. Comm. of W. Va., 262 U.S. 679, 692, 67 L.Ed. 1176, 1182-1183 (1923).

I believe the new owner of an unregulated company plagued by as many problems as Lake of the Woods had at the time of its purchase would not reasonably expect to make any return on its investment at this time. In fact, it would consider itself fortunate, extremely fortunate, if it could merely "turn around" that Company in two years to the point where it was able to cover its reasonable operating expenses. Actually, I entertain considerable fears that permitting a "break-even" result in this case may be too generous, and I am not convinced that even that is constitutionally required under these circumstances, after considering the authorities cited above. However, I am willing to recommend that this Company be allowed an increase in net revenues which will enable it to exactly cover its reasonable test year operating expenses, as calculated pursuant to the analysis in the first section of this discussion, with no return allowed on rate base. The impact on consumers of rates designed to produce this effect will still be burdensome, an increase from $8.00 per month to $20.43 per month. Nevertheless, I believe such a finding will strike a reasonable balance between the interests of the consumers and the Company.

Having recommended no return on rate base, I likewise express no opinion as to the proper amount of that rate base.

Based on the above analysis, and accepting the Staff's figures except as indicated earlier, the following is a summary of my findings of the Company's revenue requirement.

Lake of the Woods Utility Company
Test Period Ending 12/31/79

Adjusted Operating Revenues (Leis, Statement 1, Column 5)		$253,636
Operating Revenue Deductions, per Staff (Leis, Statement 1, Column 5)		$424,303
Net Operating Loss, per Staff (Leis, Statement 1, Column 5)		($170,667)
Add back disallowed expenses:		
Affiliate Expenses	$26,060	
Rate Case Expenses	$ 6,250	
Projected Electric Power Expenses	$27,929	
		$ 60,239
Adjusted Net Operating Loss		($110,428)
Gross Additional Revenue Requirement to Produce $110,428 of Additional Net Revenue (Conversion Factor is .963, after permitting 1 percent bad debt allowance and 2.7 percent gross receipts tax allowance):		$114,671
Monthly Sewer Usage Rate to Produce $114,671 Gross Additional Revenue (calculated per Leis, Statement 2):	$20.43/month	

CONCLUSION

In summary, based on the evidence, and for the reasons explained above, I find that:

(1) In all future proceedings, Lake of the Woods Utility Company should be treated as a single entity for the purposes of determining overall rate of return and revenue requirements.

(2) A reasonable bad debt allowance for this Company is 1 percent of revenues, as recommended by Staff Accountant Leis.

(3) No allowance should be made in the Company's operating expenses for any payment to its affiliated interests, AtPac Land Company, Maryland Marine Utilities, or TransContinental Development Corporation.

(4) Company's proposed adjustment to project electric power expenses above test year levels is not reasonable, and should be denied.

(5) Company's proposed allowance for expenses of this rate case is excessive, and should be denied. Rate case expenses in the amount of $3,000, amortized over 4 years, are reasonable and should be approved.

(6) With the exception of the matters described in findings (3) through (5) above, the Staff figures for the Company's test year operating results are accepted. The Company's adjusted net operating loss for the test year ending December 31, 1979 was therefore $110,428.

(7) The impact of the proposed sewerage service rate increase on the Company's customers and on the residential development itself would be extremely detrimental. There is substantial evidence of inadequate service to customers in this record. This Company presently serves only a fraction of the customers which the system was designed to serve. The sewerage system in use at Lake of the Woods is technologically unconventional and problem prone. Lake of the Woods Utility Company has been in serious financial condition for some years prior to the current rate case. The Company's new owner, AtPac Land Company, must be charged with knowledge of all these facts at the time it purchased the Company in December, 1978. No investor in AtPac's position would therefore reasonably expect to have such Company return a profit within two years after this transfer of ownership. Full recovery of reasonable operating expenses at this point in the Company's history would in fact be an unusual and significant accomplishment.

For all the above reasons, no return on rate base is appropriate for this Company. Allowing the Company to earn additional revenue sufficient to cover its test year net operating loss of $110,428 will constitute fully adequate, just and reasonable rate relief in this case.

(8) Company's gross additional revenue requirement based on test year operations is $114,671. Company should be permitted to put rates into effect which are designed to produce this amount of additional revenue. Company's redesigned tariffs may also include the previously proposed charges for sewer connections and installations, which appear reasonable.

(9) Interim rates of $24 per month having been in effect since August 1, 1980, customers are now due a refund based on the difference between that rate and the rates approved above for all collections made during the interim period. The Commission should direct such refunds to be made within a reasonable time as a part of its order in this case.

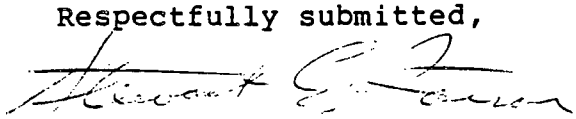
(10) Staff should undertake, in a separate proceeding, a detailed examination of the Company's personnel situation as described in this report.

It is therefore respectfully recommended that the Commission enter an order in accordance with the above findings.

The parties are advised that any exceptions to this report must be filed with the Clerk of the Commission in writing, in an original and four copies, within 15 days of the date hereof. The mailing address to which any such filing must be sent is Document Control Center, P.O. Box 2118, Richmond, Virginia 23216. Any party filing such exceptions shall attach a certificate to the foot of such document that copies have been mailed or delivered to all other counsel of record and to any party not represented by counsel.

I certify that copies of this report were mailed or delivered on February 18, 1981 to John W. Riely, Esquire, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212; Eric M. Page, Esquire, Assistant Attorney General, 11 South 12th Street, Richmond, Virginia 23219; and Atwell W. Somerville, Esquire, P.O. Box 629, Orange, Virginia 22960.

Respectfully submitted,



Stewart E. Farrar
Hearing Examiner

BEFORE THE STATE CORPORATION COMMISSION
OF VIRGINIA

CASE NUMBER PUE800081-Application of Lake of the Woods Utility Company to revise its tariffs

Exceptions of Lake of the Woods Association to the report of Stewart E. Farrar

INTRODUCTION

Comes now Protestant, Lake of the Woods Association, Inc., by its attorney, and respectfully submits these exceptions to the report of Stewart E. Farrar, Hearing Examiner in this proceeding.

PREFATORY STATEMENT

As the Hearing Examiner himself recognized, the recommended monthly charge for sewerage service of $20.43 will have an almost catastrophic effect upon the customers of the sewerage services of the applicant utility company. It will be extremely burdensome not only to those customers as such, but will also have a suppressing effect upon the marketability of their existing properties and upon the potential of the Lake of the Woods community for growth and, thus, for enlargement of the patronage of the services of the applicant utility. The recommended rate is more than two and one-half times the rate charged prior to the inception of these proceedings and is substantially higher than existing rates for similar services in communities in the general area surrounding the Lake of the Woods.

This Protestant is in hearty agreement with all of the factual findings of the Hearing Examiner, and with most of the

conclusions he drew therefrom. It is particularly anxious that the Commission accept and act upon his recommendation that the Commission's staff investigate the efficiency of the operation and the need for and qualification of the on-site personnel presently engaged in that operation.

The law is well settled that a utility must be efficiently and economically operated as a condition to the exercise of its right to impose rates that will yield an adequate rate of return. See Public Utility Commission v. Bangor Gas Company (Maine, 1948) 74 PUR(NS) 23, Ex Parte Breaux Bridge Telephone Co. (Louisiana, 1961) 41 PUR 3d 260, and Island Lake Water Company v. Illinois Commerce Commission (Illinois, 1978) 382 NE 2d 835. The customers of the applicant utility have never been blessed with anything approaching efficient and economical operations of their sewerage service. It is their position that until the applicant utility achieves that minimum standard it is entitled to recover no more than its out-of-pocket costs of operation, if that.

The law is also well settled that a utility is never guaranteed any return, but is entitled only to rates which will give it an opportunity to earn a fair return. See Re North Carolina Telephone, Co. (North Carolina, 1960) 35 PUR 3d 88 and Re General Telephone Co. of Florida (Florida, 1962) 44 PUR 3d 247. Until the applicant utility can demonstrate that its operating expenses have been prudently expended to produce an economical and efficient operation, it has no right to claim any revenue in excess of its operating expenses.

The report of the Hearing Examiner is in essential agreement with the foregoing fundamental principles of regulatory law and recommends that the increased sewerage rate sought by the applicant utility be limited to one which will enable it to break exactly even, after exclusion from its profit and loss statement of all of those expenditures which were not supported by evidence in this case, and which, on their face, are improper. The primary error in the report lies in the fact that the break-even point of the operation was calculated for the sewerage service only, ignoring the fact that the applicant utility has been making a handsome profit on the water service which it supplies.

EXCEPTIONS

Exception No. 1: The report errs in failing to find that the break-even point in the operation of the applicant utility should be determined from its total operation, consisting of both water and sewerage services.

Exception No. 2: The report errs in failing to find that a monthly charge of $9.48 will provide sufficient additional revenue for the utility to enable it to recover its total justifiable operating expenses on the basis of the test-year data.

Exception No. 3: The report errs in failing to find that $12.00 per month is the maximum reasonable charge which can be made for sewerage service by the applicant utility, all circumstances considered.

ARGUMENT IN SUPPORT OF EXCEPTIONS

This Case Should Be Decided Upon The Basis Of Total Operations

At the very inception of its discussion of the issues the report of the Hearing Examiner reads as follows at page 13:

> "First, I am of the opinion that the revenue requirements of this Company should be determined on a total company basis in the future. This does not mean that I favor a single uniform rate for combined water and sewer services. Different rates for different services are recognized as appropriate for all utility companies. It does mean that the Commission should determine total company revenue requirements, and should not attempt to treat this Company as two different entities for ratemaking purposes. The much more logical method is to focus on the total company, and there is no reason not to follow this approach in this case. Out of approximately 800 connected customers, only three do not take both water and sewer service. The evidence is that all future connections will probably require both types of service. The same personnel serve both systems." [Emphasis supplied.]

Yet in the paragraph commencing at the bottom of page 13 of the report the following is found:

> "Inasmuch as the Staff analyzed only the sewerage operations for purposes of this case, in my opinion there is insufficient evidence in the record to determine revenue requirements on a total company basis in this proceeding."

The report overlooks the fact that there is in this proceeding staff data respecting the revenues and expenses of the water phase of the applicant utility's operation. Statement No. 1 of Witness Leis shows those data for the water department in Column 2 thereof. Even if no adjustment were made therein the report errs in ignoring the fact that those operations produced a net operating income of $74,437 for the test year and a rate of return of

13.72%. As the report itself recognizes, there is only one group of employees of the applicant utility at Lake of the Woods and they work interchangeably in both the sewerage and water services. As stated by Mr. Leis at page 8 of his testimony, the Commission's staff accepted the utility's allocation of expense between the two separate services, the staff allocating only certain administrative and general expenses on a 50/50 basis. That fact alone is enough to justify indeed to require that this case be decided upon the basis of the financial results of total operations of the applicant utility.

The recommendation of the Hearing Examiner's report that the revenue needs of the applicant utility shall be decided in all future cases upon the basis of total operations is certainly beyond cavil. It is equally certain that adequate evidence exists in the record of this case to permit a similar determination on that basis in this proceeding. The report errs in failing to do so.

A Sewerage Rate of $9.48 Per Month
Will Permit Break-even Operations

Attached hereto as Appendix A is a restatement of the financial results of operation of the applicant utility, covering both water and sewerage services. All of the data in that Appendix have been taken from the evidence of record and the Appendix itself shows the source of each item. Using the utility's own

figure of 769 customers as of the end of the test year, the Appendix shows that a sewerage rate of $9.48 per month will permit the utility, on a total-operation basis, to recover its justifiable expenses.

It should here be emphasized that Appendix A makes no adjustment in the expenses of the sewerage service of the applicant utility other than those made by the report of the Hearing Examiner. Moreover, the expenses of the water service are exactly those shown in Column 2 of Statement I of Witness Leis with but one single adjustment. That adjustment consists of the application of the limitation of the bad-debt allowance to 1% of revenue. It is discussed at the top of page 14 of the report of the Hearing Examiner and was recommended by Mr. Leis of the Commission's staff.

It is the position of this Protestant that every adjustment in operating expense recommended by the Commission's staff and made by the Hearing Examiner in his report is fully justified. Certainly the members of this Association, who are the only customers of the applicant utility, ought not to be burdened with the necessity of reimbursing that utility for its improvidently incurred expenses, expenses which could be avoided by good business practices. On that basis, therefore, this Protestant prays that the Commission find that a monthly charge of $9.48 for sewerage service is adequate to permit the applicant utility to break even on its total operation and that a break-even operation is all that the utility is entitled to at the present time.

A Maximum Reasonable Rate For Sewerage Service
Cannot Exceed $12.00 Per Month

There are in this case certain considerations which are not fully reflected by the financial results of the utility's operation during the test year. One such consideration is, of course, the impact of inflation upon the utility's operation. Another and related consideration is the utility's claim that it will incur added expense for electric power. As to the former, it is to be hoped that operating efficiencies under the guidance of the Commission's staff after investigation of the need for the total number of on-site personnel at Lake of the Woods will offset in large measure the effects of inflation. As to the latter consideration, namely an increase in charges for electric power, this Protestant calls attention to the fact that the Virginia Electric Power Company, from which the Rappahannock Electric Co-operative gets the power it sells to the applicant utility, is entering upon a phase in which a major portion of its total generating capacity will be from nuclear reactors. VEPCO has already announced that when those nuclear powered generators all come on line there will be a reduction in the cost of its electric power. It is by no means certain that the applicant utility will incur the added costs of electricity which it projects.

Even if this Protestant is wrong in its belief that the applicant utility will be able to avoid the preponderant portion of its anticipated increased expenses, there is another consideration which will certainly go far to offset whatever added expenses the utility may incur. The revenue level at which the financial

results for the test year were calculated reflect the use factor of 769 customers. That was the number stated by the company itself to comprise its list of customers as of December 31, 1979. As the report of the Hearing Examiner states, the rate of building growth at Lake of the Woods has approximated 70 homes per year over the past few years. As of this date, there are approximately 850 homes now utilizing the sewerage service of the company. Inasmuch as each new home pays the cost of the installation of the necessary equipment for connection to the sewerage system, the addition of those homes has not occasioned any added expense for the applicant utility. And, of course, the revenues of the utility have been increased by the added number of homes. That added revenue should more than offset whatever added expense the utility may incur by reason of inflation or increased costs of electric power. In any event, the allowance of a monthly rate of $12 for sewerage service will generously accommodate any revenue need of the applicant utility to achieve a break-even operation. As the Hearing Examiner has pointed out in his report, that is the most that the utility could expect in the second year of its ownership of the facilities.

CONCLUSION

For all of the above reasons, Protestant Lake of the Woods Association, Inc. respectfully prays that the Commission find that a monthly sewerage charge of $9.48 is adequate to permit the Lake of the Woods Utility Company to recover its justifiable operating expenses. In the alternative, and should the Commission feel that some additional revenue should be permitted,

Protestant Lake of the Woods Association, Inc. respectfully prays that the monthly sewerage rate be set at a maximum of $12.00.

Respectfully submitted,

Lake of the Woods Association, Inc.

BY _____
ATWELL W. SOMERVILLE

C E R T I F I C A T E

I hereby certify that I have on this 30th day of March, 1981 mailed copies of the foregoing exception to the following: Eric M. Page, Esquire, for the Division of Consumer Counsel, Office of the Attorney General; Kenworth E. Lion, Jr., Esquire, for the Commission, John W. Riely, Esquire, for the applicant utility.

_____
ATWELL W. SOMERVILLE

LAKE OF THE WOODS UTILITY COMPANY
TEST PERIOD ENDING 12/31/79
TOTAL COMPANY OPERATIONS

Adjusted Operating Revenues (Attached Statement I, Column 6)		$ 485,758
Operating Revenue Deductions (Attached Statement I, Column 6)		559,141
Net Total Company Operating Loss: (Attached Statement I, Column 6)		$ (73,383)
Add back disallowed expenses:		
Affiliate Expenses	$ 26,060	
Rate Case Expenses	6,250	
Projected Electric Power Expenses	27,929	
		60,239
Adjusted Net Total Company Operating Loss:		$ (13,144)

- Gross Additional Revenue Requirement to Produce $13,144 of Additional Net Revenue (conversion factor is .963 after permitting 1 percent bad debt allowance and 2.7 percent gross receipts tax allowance): $13,649.

- Monthly Sewerage Usage Rate to produce $13,649 Gross Additional Revenue (calculated per Leis' Statement 2): $9.48.

- Assuming an increase of monthly sewerage rate of $4.00 (to a total of $12.00) would generate additional annual revenue of $36,912. Adding this to the adjusted net total company operating loss of $13,144 would produce net operating income of $23,768. This would represent a 0.94% rate of return on the adjusted rate base of $2,522,004.

LAKE OF THE WOODS UTILITY COMPANY
RATE OF RETURN STATEMENT
FOR 12 MONTHS ENDED DECEMBER 31, 1979

	Total Co. Oper. per Books Col. (1)	Water Department Col. (2)	Adj. to Water Department Col. (3)	After Adj. to Water Dept. Col. (4)	Sewer Dept. After SCC Adj. Col. (5)	Total Adj. Co. Operations Col. (6)
OPERATING REVENUES:	$ 484,207	$232,122		$232,122	$ 253,636	$ 485,758
OPERATING REVENUE DEDUCTIONS:						
Operation & Maint. Expense	449,274	117,398	$(22,847)	94,551	330,076	424,627
Deprec. & Amortization	128,872	31,053		31,053	65,719	96,772
Taxes other than Federal Income	37,323	9,234		9,234	28,508	37,742
Federal Income Tax	---	---		---	---	---
TOTAL OPERATING DEDUCTIONS:	$ 615,469	$157,685	$(22,847)	$134,838	$ 424,303	$ 559,141
NET OPERATION INCOME (LOSS):	$ (131,262)	$ 74,437	$ 22,847	$ 97,284	$ (170,667)	$ (73,383)
UTILITY PLANT:						
Utility Plant in Service	$4,026,768	$996,286		$996,286	$3,036,576	$4,032,862
Construction Work in Progress	767	---		---	767	767
Less: Accumulated Deprec.	684,394	193,536		193,536	388,876	582,412
Acquisition Adjustment	90,579	---		---	90,579	90,579
Contributions in Aid of Construction	1,084,248	281,904		281,904	799,111	1,081,015
NET UTILITY PLANT:	$2,168,314	$520,846		$520,846	$1,758,777	$2,279,623
Plus: Allowance for Working Capital	49,919	13,044		13,044	36,675	49,719
Materials & Supplies	192,662	8,607		8,607	184,055	192,662
NET UTILITY PLANT & ALLOWANCES:	$2,410,895	$542,497		$542,497	$1,979,507	$2,522,004
RATE OF RETURN:	-0-	13.72%		17.93%	-0-	-0-

SOURCES: - SEE FOLLOWING PAGE

SOURCES:

Column 1 - Statement I of Witness Leis.

Column 2 - Statement I of Witness Leis.

Column 3 - Adjustment is to decrease uncollectible water accounts expense to 1% rate of gross annual revenue in accordance with Commission policy shown in SCC staff testimony, item 10 schedule A to Statement I.

Column 4 - Combined Column 2 and Column 3.

Column 5 - Shows the sewer operations after SCC staff adjustments shown in Column (4) Statement I of Witness Leis.

Column 6 - Shows total company operations after adjustment in Column (3) and SCC staff adjustments reflected in Column (5).

VIRGINIA

BEFORE THE STATE CORPORATION COMMISSION

APPLICATION OF LAKE OF THE WOODS UTILITY COMPANY TO REVISE ITS TARIFFS FOR SEWERAGE SERVICE	))))	CASE NO. PUE800081

EXCEPTIONS TO REPORT OF HEARING EXAMINER

Lake of the Woods Utility Company (the Company), believing that it is clear that the report of the hearing examiner, if adopted by the Commission, will result only in the bankruptcy of the Company and the cessation of all service -- water and sewerage -- files exceptions to that report as follows:

1. The examiner reports that the Commission should deny the Company any return on rate base.

No similar suggestion has ever been made to this Commission as to any Virginia utility. Despite the erudite quotation of precedents, none of the authorities quoted is a case where such a result was reached. The suggestion would be, if adopted, a shocking deprivation of property without due process of law. The State may condemn the properties of a utility as a matter of constitutional law; it may not consciously deny any return at all -- even on an opportunity cost of capital basis.

The bases for this determination are, perhaps, two. The first is certain asserted deficiencies in service. But for the last year or two, the Commission's files are substantially

void of service complaints. The service complaints arose only when a proposal for a rate increase was filed. Mr. Tice, the Commission's engineer, makes no comment as to service deficiencies (Tr. 208-221). Denial on the basis of asserted service deficiencies has no substantial support in the evidence.

The second reason advanced by the examiner is that the present owner of the stock of the Company knew that the Company was losing money when it was purchased; for this reason, the purchaser should be allowed no return. That is a very unusual argument. The owner that sold had a right to the opportunity to earn a fair return on its investment; the fact of sale does not result in denial of that right to the vendee. What is said here is that dollars actually invested in a utility can earn no return; the utility should not be permitted the opportunity to earn because it has a history of failing to earn.

Only the cases cited by the examiner need be cited to show the illegality of such a conclusion. Even such a basic case as Bluefield requires that rates for a utility "permit it to earn a return"; the examiner denies this basic premise. The conclusion that

> "...no return on rate base is appropriate for this Company" (Report, p. 30)

is error and, we believe, would be reversible error if adopted by the Commission.

Finally, this is not a case where there is no rate base. The examiner does not suggest, and could not suggest on

the basis of the record, that the dollars of rate base proposed by the Accounting Staff were not dollars invested in fact in the Company's plant. They were so invested and he recognizes that fact. He says simply that this investment of good dollars should result in no return at all.

This conclusion is unprecedented and unconstitutional. It should not be upheld by the Commission.

2. After such an appalling determination, the other issues seem insignificant. But they are not. They may, however, be briefly summarized.

(a) The examiner would limit rate case expense to $3,000. From a personal point of view, counsel can only express a measure of affront at this evaluation of his services. The examiner eliminates any payment to Brockmeier Consulting Engineers, Inc. Mr. Frasher, who presented the accounting testimony for the Company, is employed by Brockmeier; presumably, the examiner would consider that Mr. Frasher is not entitled to compensation. There was no testimony in the record that rate case expenses were unreasonable; there is only the examiner's conclusion that counsel and the expert witnesses should do all that was required -- including the preparation of this document -- for $3,000. In fact, expenses incurred will be much greater than $3,000 as bills rendered to the Company already substantiate.

There is no support in the evidence for this conclusion and it should be overturned.

(b) The examiner would eliminate all affiliate expenses. In fact, payments to affiliates help rather than hurt the customers of the Company. At Lake of the Woods and on the Company's payroll are a service foreman and laborers. Without payments to affiliates, the Company would have no General Manager, it would have no one to keep the books, it would have no one to do any planning or any engineering or to provide for the construction of additional facilities. There would be no one to keep employment records or to pay employees. The Company could not compile tax returns or prepare the many reports required by the Commission and other agencies of the Commonwealth. All of these activities are required if service is to be continued by the Company; they cannot be rendered unless those who render them are paid. The examiner suggests their discontinuance and, as a result, the immediate discontinuance of service.

When the Company was owned by a previous owner, payments to affiliates were approved by the Commission for these purposes. They are necessary for the Company to stay in operation. There is no justification for denying them at this late date.

(c) The examiner reports that the Company should not be permitted to adjust charges for electric service to the level of charges actually experienced at the end of the test year but must be limited to charges in fact booked during the

test year. This is obviously unfair and can only create delusions.

Because many of the tanks require electric motors for pumps, the cost of electricity is a major operating expense of the Company. Let us see what the Commission's Col. Leis says on this subject:

> "Staff adjustment number (4) annualizes a power increase by the Rappahannock Electric Cooperative (formerly Virginia Electric Cooperative) effective October 1, 1979. The possibility of future rate reductions was explored with the Cooperative. The Cooperative's Management Engineering Planning staff indicated that future rate revisions were in planning, and that those rate schedules under which the utility operates would probably show future increases of 1 to 1.3 percent under the "B-1" Schedule, and 4 to 5 percent for the "LS" and "A-1" Schedules." (Prepared Testimony, p. 11).

Col. Leis increased the actual power expense by $27,929. Yet the examiner approves no adjustment at all.[1/]

Rates are set for the future and not for the past. This adjustment is entirely proper and should have been allowed.

(d) The examiner says that a reserve for bad debts equal to 1% of revenues is adequate. Col. Leis testified that the use of 1% for uncollectibles is "current Staff policy" (Tr. 180). About 60% of the Company's revenues come from availability charges -- $3.75 per month -- assessed against lot

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[1/] The intervener suggests that electric rates will decline in the future (Exceptions, p. 7). There is no basis whatsoever for anticipating this result; the contrary is to be expected. But the adjustment was based on the current experienced level of rates.

owners who do not have improvements to their lots and who may live miles from Lake of the Woods (Tr. 185). Col. Leis talks about requiring the use of this 1% limitation arbitrarily whether it accords with experience or not (Tr. 189). The examiner accepts this judgment because the Company has not sued to collect these charges -- the management has chosen "to forgo the effort to collect these revenues" (Report, p. 14).

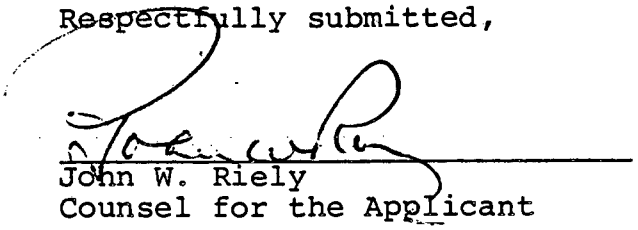
This conclusion is obviously unrealistic. One does not sue in a foreign locality to collect $11.25. The expense would be prohibitive. The Company can dun; there is no practicable way to collect. There is no justification for this adjustment and the Commission should not accept it.

There are a number of other conclusions in the examiner's report that are arbitrary, unreasonable and without support in the evidence. He has simply sought ways to reduce the Company's request. His conclusion is not justifiable.

The Commission should reject the report of the examiner. It should examine the record and decide the case fairly on the contents of the record.

Dated March 5, 1981.

Respectfully submitted,



John W. Riely
Counsel for the Applicant

HUNTON & WILLIAMS
P. O. Box 1535
Richmond, Virginia 23212
Of Counsel

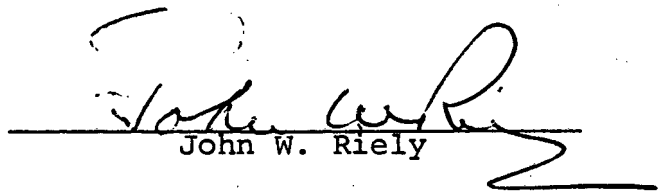
CERTIFICATE OF SERVICE

I, John W. Riely, a member of the Virginia State Bar, hereby certify that on March 5, 1981, I caused a copy of the above document to be mailed by first class mail, postage prepaid, to each of the following:

Lewis S. Minter, Esquire
General Counsel
State Corporation Commission
P. O. Box 1197
Richmond, Virginia 23209

Eric M. Page, Esquire
Assistant Attorney General
11 South Twelfth Street
Richmond, Virginia 23219

Atwell W. Somerville, Esquire
P. O. Box 629
Orange, Virginia 22960



John W. Riely

3-C-62—7-9-58—15M

COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

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AT RICHMOND, APRIL 1, 1981

APPLICATION OF

LAKE OF THE WOODS UTILITY COMPANY CASE NO. PUE800081

To revise its tariffs

FINAL ORDER

On June 17, 1980, Lake of the Woods Utility Company (hereinafter "Company") filed an application with the Commission for a temporary emergency increase in rates for sewerage service pursuant to Code §56-245. In the application, it is stated that the tariff revisions are designed to increase Company's gross annual revenues by $147,648. By letter filed June 24, 1980, Company submitted financial statements detailing Company's operations for the calendar year 1979. In this letter Company requested that the Commission consider the application as one under §56-240 if the Commission found §56-245 to be inapplicable.

By order dated July 1, 1980, the Commission (1) denied emergency rate relief under §56-245, (2) set a public hearing before a Hearing Examiner for November 5, 1980, for the purpose of receiving evidence relevant to Company's proposed tariff revision, and (3) directed the Commission's Staff to investigate and report on the appropriateness of interim relief under §56-240.

The Commission's Staff concluded its investigation and filed its report on July 15, 1980. By order dated

July 17, 1980, the Commission found that Company had demonstrated a reasonable probability that an increase in gross annual revenues in the amount of $147,648 would be justified after a full investigation and hearing. The Commission order permitted Company to collect these revenues on an interim basis, subject to refund, for service rendered on and after August 1, 1980.

On July 29, 1980, Company filed a proposed revised schedule with the Commission to increase the sewerage rate beyond that approved on an interim basis in the July 17, 1980, order. This revised schedule was designed to increase Company's gross annual revenues by $147,648 above that to be received through the interim rates.

Stewart E. Farrar, Hearing Examiner, presided over the November 5, 1980, hearing. Appearances were entered as follows: John W. Riely, Esquire, counsel for Company; Atwell W. Somerville, Esquire, counsel for the Protestant, Lake of the Woods Association, Inc.; Eric M. Page, Esquire, Division of Consumer Counsel, Office of the Attorney General; and Kenworth E. Lion, Jr., Esquire, counsel for the Commission. One intervenor testified at the hearing.

The Hearing Examiner filed a report on February 18, 1981, sending copies to Messrs. Riely, Somerville and Page. The Hearing Examiner made the following findings:

(1) In all future proceedings, Lake of the Woods Utility Company should be treated as a single entity for the purposes of determining overall rate of return and and revenue requirements.

(2) A reasonable bad debt allowance for this Company is 1 percent of revenues, as recommended by Staff Accountant Leis.

(3) No allowance should be made in the Company's operating expenses for any payment to its affiliated interests, AtPac Land Company, Maryland Marine Utilities, or TransContinental Development Corporation.

(4) Company's proposed adjustment to project electric power expenses above test year levels is not reasonable, and should be denied.

(5) Company's proposed allowance for expenses of this rate case is excessive, and should be denied. Rate case expenses in the amount of $3,000, amortized over 4 years, are reasonable and should be approved.

(6) With the exception of the matters described in findings (3) through (5) above, the Staff figures for the Company's test year operating results are accepted. The Company's adjusted net operating loss for the test year ending December 31, 1979 was therefore $110,428.

(7) The impact of the proposed sewerage service rate increase on the Company's customers and on the residential development itself would be extremely detrimental. There is substantial evidence of inadequate service to customers in this record. This Company presently serves only a fraction of the customers which the system was designed to serve. The sewerage system in use at Lake of the Woods is technologically unconventional and problem prone. Lake of the Woods Utility Company has been in serious financial condition for some years prior to the current rate case. The Company's new owner, AtPac Land Company, must be charged with knowledge of all these facts at the time it purchased the Company in December, 1978. No investor in AtPac's position would therefore reasonably expect to have such Company return a profit within two years after this transfer of ownership. Full recovery of reasonable operating expenses at this point in the Company's history would in fact be an unusual and significant accomplishment.

For all the above reasons, no return on rate base is appropriate for this Company. Allowing the Company to earn additional revenue sufficient to cover its test year net operating loss of $110,428 will constitute fully adequate, just and reasonable rate relief in this case.

(8) Company's gross additional revenue requirement based on test year operations is $114,671. Company should be permitted to put rates into effect which are designed to produce this amount of additional revenue. Company's

redesigned tariffs may also include the previously proposed charges for sewer connections and installations, which appear reasonable.

(9) Interim rates of $24 per month having been in effect since August 1, 1980, customers are now due a refund based on the difference between that rate and the rates approved above for all collections made during the interim period. The Commission should direct such refunds to be made within a reasonable time as a part of its order in this case.

(10) Staff should undertake, in a separate proceeding, a detailed examination of the Company's personnel situation as described in this report.

Exceptions to certain findings and recommendations contained in the Hearing Examiner's report were filed by the Protestant on March 3, 1981, and by Company on March 5, 1981.

NOW, THE COMMISSION, having considered Company's application, the testimony and exhibits introduced at the public hearing, the Hearing Examiner's report, the exceptions to the Hearing Examiner's report, and the applicable law, is of the opinion that the Hearing Examiner's findings should be adopted. Accordingly,

IT IS ORDERED:

(1) That the Hearing Examiner's findings are hereby adopted by the Commission;

(2) That, on or before April 15, 1981, Company file with the Commission revised tariffs designed to produce $114,671 gross additional revenue based on test year operations, said revised tariffs to become effective for service rendered on and after April 16, 1981;

(3) That on or before April 15, 1981, Company file

a proposed plan to refund all revenue collected from the application of the interim rates which the Commission permitted to become effective for sewerage service rendered on and after August 1, 1980, to the extent that it exceeds the revenue which would have been collected by application, in lieu thereof, of the permanent rates to be filed in compliance with this order;

(4) That upon the approval of Company's refund plan, as proposed or as modified by the Commission, Company is to implement same forthwith; and

(5) That there being nothing further to come before the Commission, the case be removed from the docket and the papers placed in the file for ended causes.

ATTESTED COPIES hereof shall be sent to John W. Riely, Esquire, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212; Atwell W. Somerville, Esquire, P.O. Box 629, Orange, Virginia 22960; Office of the Attorney General, Division of Consumer Counsel, 11 South 12th Street, Richmond, Virginia 23219; and to the Commission's Divisions of Energy Regulation and Accounting and Finance.

A True Copy

Teste: William C. Young

Clerk of State Corporation Commission

-7-9-58—15M

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AT RICHMOND, MAY 12, 1981

APPLICATION OF

LAKE OF THE WOODS UTILITY COMPANY CASE NO. PUE800081

To revise its tariffs

SUSPENSION OF FINAL ORDER

On April 14, 1981, as permitted by §8.01-676F of the Code of Virginia, Lake of the Woods Utility Company (hereinafter "Company") filed an application with the Clerk of the Commission for suspension of the Final Order entered in this case on April 1, 1981, pending decision of the Supreme Court of Virginia of the appeal of said Final Order. Company heretofore timely filed a Notice of Appeal on April 23, 1981.

NOW, THEREFORE, in the exercise of the discretionary authority granted by Code §8.01-676F, the Commission is of the opinion and hereby concludes that operation of its order of April 1, 1981, heretofore entered in this proceeding, will be suspended pending decision of the appeal by the Supreme Court of Virginia, thus leaving in effect the interim rates permitted by Commission order dated July 17, 1980.

PROVIDED, HOWEVER, prior to the entering of a suspending order as above contemplated, Company, or someone in its behalf, shall first execute and file with the Clerk of the Commission a suspending bond, with corporate surety, in the amount of $60,000, payable to the Commonwealth, conditioned upon payment, or credit to customers of Company

as the Commission may direct, of all amounts or sums of money which Company shall collect or receive pursuant to the interim rates authorized by prior order herein and effective August 1, 1980, in excess of those rates and charges fixed, or authorized by the final decision on appeal.

ATTESTED COPIES hereof shall be sent to John W. Riely, Esquire, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212; Atwell W. Somerville, Esquire, P.O. Box 629, Orange, Virginia 22960; Office of the Attorney General, Division of Consumer Counsel, 11 South 12th Street, Richmond, Virginia 23219; and to the Commission's Divisions of Energy Regulation and Accounting and Finance.

A True Copy

Teste: William C. Young

Clerk of State Corporation Commission

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COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION
RICHMOND

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AT RICHMOND, JULY 28, 1981

APPLICATION OF

LAKE OF THE WOODS UTILITY COMPANY CASE NO. PUE800081

To revise its tariffs

OPINION

On June 17, 1980, Lake of the Woods Utility Company (hereinafter "Company") filed an application with the Commission pursuant to Code §56-245 for a temporary emergency increase in rates for sewerage service. In the application Company stated that the tariff revisions were designed to increase Company's gross annual revenues by $147,648. By letter filed June 24, 1980, Company submitted financial statements detailing its operations for the calendar year 1979. Company also requested that the Commission consider the application under §56-240 if the Commission found §56-245 to be inapplicable.

By order dated July 1, 1980, the Commission (1) denied emergency rate relief under §56-245, (2) set a public hearing before a Hearing Examiner for November 5, 1980, for the purpose of receiving evidence of Company's proposed tariff revision, and (3) directed the Commission's Staff to investigate and report on the appropriateness of interim relief under §56-240.

The Commission's Staff concl ded its investigation and filed its report on July 15, 1980. By order dated July 17, 1980, the Commission found that Company had demonstrated a reasonable probability that an increase in gross annual revenues in the amount of $147,648 would be justified after a full investigation and hearing. The Commission order permitted Company to collect these revenues on an interim basis, subject to refund, for service rendered on and after August 1, 1980.

On July 29, 1980, Company filed a proposed revised schedule with the Commission to increase the sewerage rate beyond that approved on an interim basis in the July 17, 1980, order. This revised schedule was designed to increase Company's gross annual revenues by $147,648 above the amount authorized under the interim rates.

Stewart E. Farrar, Hearing Examiner, presided over the November 5, 1980, hearing. Appearances were entered by: John W. Riely, Esquire, counsel for Company; Atwell W. Somerville, Esquire, counsel for the protestant, Lake of the Woods Association, Inc.; Eric M. Page, Esquire, Division of Consumer Counsel, Office of the Attorney General; and Kenworth E. Lion, Jr., Esquire, counsel for the Commission; Mr. James Hinkle appeared as an intervener and read a petition signed by eighty-eight (88) property owners in opposition to Company's proposed rate increase. Testimony was received

from two Company witnesses: Thomas L. Thorne, General Manager of Lake of the Woods Utility Company and Robert L. Frasher, Project Accountant with Brockmeier Consulting Engineers, Inc. The Commission's Staff presented two witnesses: S. Frank Leis, Deputy Director of the Division of Accounting and Finance and E. Jackson Tice, Engineer in the Division of Energy Regulation. Lake of the Woods Association, Inc., presented seven witnesses: Alan L. Potter, President of Lake of the Woods Association Inc.; Warren J. Lodge, General Manager of Lake of the Woods Association Inc.; William W. Carpenter, property owner and retired controller of the American Psychological Association in Washington, D. C.; Harold J. Wade, property owner and retiree; Brenda McCall, property owner and retiree; Albin L. Lindall, property owner and real estate broker; and George P. Beard, Jr., Chairman of the Board of the Second National Bank of Culpeper.

By letter dated November 24, 1980, the Hearing Examiner requested Company to provide additional evidence on several issues. Company filed the additional information on January 13, 1981. No objection having been made by the Staff or other parties, this material became part of the record. In his report filed February 18, 1981, the Hearing Examiner made the following findings:

(1) In all future proceedings, Lake of the Woods Utility Company should be treated as a single entity for the purposes of determining overall rate of return and revenue requirements.

(2) A reasonable bad debt allowance for this Company is 1 percent of revenues, as recommended by Staff Accountant Leis.

(3) No allowance should be made in the Company's operating expenses for any payment to its affiliated interests, AtPac Land Company, Maryland Marine Utilities, or TransContinental Development Corporation.

(4) Company's proposed adjustment to project electric power expenses above test year levels is not reasonable, and should be denied.

(5) Company's proposed allowance for expenses of this rate case is excessive, and should be denied. Rate case expenses in the amount of $3,000, amortized over 4 years, are reasonable and should be approved.

(6) With the exception of the matters described in findings (3) through (5) above, the Staff figures for the Company's test year operating results are accepted. The Company's adjusted net operating loss for the test year ending December 31, 1979 was therefore $110,428.

(7) The impact of the proposed sewerage service rate increase on the Company's customers and on the residential development itself would be extremely detrimental. There is substantial evidence of inadequate service to customers in this record. This Company presently serves only a fraction of the customers which the system was designed to serve. The sewerage system in use at Lake of the Woods is technologically unconventional and problem prone. Lake of the Woods Utility Company has been in serious financial condition for some years prior to the current rate case. The Company's new owner, AtPac Land Company, must be charged with knowledge of all these facts at the time it purchased the Company in December, 1978. No investor in AtPac's position would therefore reasonably expect to have such Company return a profit within two years after this transfer of ownership. Full recovery of reasonable operating expenses at this point in the Company's history would in fact be an unusual and a significant accomplishment.

For all the above reasons, no return on rate base is appropriate for this Company. Allowing the Company to earn additional revenue sufficient to cover its test year net operating loss of $110,428 will constitute fully adequate, just and reasonable rate relief in this case.

(8) Company's gross additional revenue requirement based on test year operations is $114,671. Company should be permitted to put rates into effect which are designed to produce this amount of additional revenue. Company's redesigned tariffs may also include the previously proposed charges for sewer connections and installations, which appear reasonable.

(9) Interim rates of $24 per month having been in effect since August 1, 1980, customers are now due a refund based on the difference between that rate and the rates approved above for all collections made during the interim period. The Commission should direct such refunds to be made within a reasonable time as a part of its order in this case.

(10) Staff should undertake, in a separate proceeding, a detailed examination of the Company's personnel situation as described in this report.

Exceptions to certain findings and recommendations contained in the Hearing Examiner's report were filed by Protestant, Lake of the Woods Association, Inc., on March 3, 1981, and by Company on March 5, 1981.

By Final Order filed April 1, 1981, the Commission adopted the Hearing Examiner's findings and required Company to file revised tariffs and a proposed refund plan.

BACKGROUND

Lake of the Woods is a residential-community in Orange County, Virginia, consisting of approximately 4,200 lots,

all of which have been sold, and of which about 800 have been improved with dwellings. The lots cover approximately 2,600 acres and are situated around a 500 acre man-made lake. About 75 percent of the homes are occupied full time. Commercial development is quite limited. The community is improved by hard-surfaced roads and has numerous public use facilities such as swimming pools, community building, golf course, parks, playgrounds, and picnic areas. An association of property owners known as the Lake of the Woods Association, Inc. operates and maintains the common use facilities.

Lake of the Woods Utility Company is a wholly-owned subsidiary of AtPac Land Company of Santa Barbara, California, which purchased the stock of Company as one of a number of acquisitions from Boise Cascade Home and Land Corporation in December, 1978. Company provides water and sewerage services to the community. Of the 769 customers receiving service at the end of the test year, December 31, 1979, all but three use both water and sewer services. These three homes have their own septic tank-drainfield systems and purchase only water service.

The water service to the community is supplied by a conventional system of eight wells, storage tanks and mains. The Company did not request an increase in its

metered water rates in this proceeding. Those customers who own lots but do not yet take water service are charged an availability charge of $4.00 per month. Water rates have not been increased since the commencement of service in 1967.

Sewerage service is provided by a somewhat unusual vacuum system. The vacuum system was installed because the soil in the area is unsuitable for individual septic tank - drainfield systems and the hilly terrain prevented the use of a conventional gravity flow sewer system. The system employed here maintains a vacuum on the sewer lines to transport the sewage. Sewage discharged from a home flows by gravity to a nearby holding tank which is shared normally by one other home. From the holding tank it is pulled by vacuum pressure to one of 13 pumping stations in the subdivision; from there it is pumped through a sewage force main into a larger gravity flow main connected to the sewage treatment plant.

Valves on each individual holding tank are designed to open at appropriate times to allow the force of the vacuum on the discharge line to empty the tank. Earlier versions of these valves were electrically operated, necessitating an electric meter at each such holding tank. There are

presently about 300 valves of this type in the system. New valves now being installed are operated pneumatically without the necessity of electric power.

Prior to this proceeding, residential users of the sewerage system were paying a flat rate of $8.00 per month. By order herein dated July 17, 1980, the Commission approved, on an interim basis subject to refund, an increase in gross annual revenues which resulted in increasing the flat rate paid by residential users to $24.00 per month. However, if the interim increase is made permanent, together with the increase reflected by the revised schedule filed herein on July 29, 1980, the residential user rate will increase to $40.00 per month. Company has proposed no change to the $3.75 per month availability fee charged to those customers who own lots but do not yet take the sewerage service.

TOTAL COMPANY OPERATIONS - Future Proceedings

Both Protestant and the Attorney General contend that the Commission should examine Company's financial condition on a total company basis, rather than to look only at the sewerage operations as proposed in Company's application. Witnesses for Protestant indicate that, with only three

exceptions, all customers of the utility take both water and sewer service. These three customers have their own septic tank - drainfield systems for sewage disposal. Protestant witness Lodge stated that other lot owners cannot obtain septic tank construction permits because percolation tests indicate that the soil is unsuitable for septic tank - drainfield systems. He further stated that wells are not allowed on individual lots. All new customers are therefore likely to require both water and sewer service.

Protestant witness Carpenter testified as to the difficulties encountered in allocating revenues, expenses, and capital expenditures to the water and sewer systems. He contends that the revenues from the $7.75 per month availability charge ($4.00 per month for water and $3.75 per month for sewer) are improperly allocated since Company's investment in the sewer system is larger than its investment in the water system. He also pointed out that since Company allocates the costs of operations and maintenance and capital construction by use of a work-order system, a complete audit of all work-orders in conjunction with the payroll and material records would be required to ascertain if all costs are properly allocated. He concluded that the true position of any company from an accounting or financial standpoint should

be determined by the total company operations as opposed to individual operations within the company.

We believe that the position of Protestant and the Attorney General on the foregoing matter is well taken. Since the same personnel serve both systems, it is necessary to allocate expenses. The many, inevitable judgmental decisions involved in this allocation process make such separations inherently suspect. Since both the water and sewer systems serve essentially the same customers and the systems are maintained by the same personnel, it appears to be logical and eminently more fair to both Company and its customers, to determine Company's revenue requirements on a total Company basis. Inasmuch as the water operations and the allocation of availability charges received little or no analysis by either the Staff or the parties, there is insufficient evidence in the record to determine revenue requirements on a total company basis in this proceeding. We find, however, that the revenue requirements of Company should be determined on a total company basis in all future rate proceedings.[1]

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[1] This should not be interpreted to mean that we are requiring a single rate for combined water and sewer services. We recognize different rates for different services as being appropriate for all utilities.

UNCOLLECTABLE ACCOUNTS EXPENSE

Company's books reflect an uncollectable accounts expense for the sewer operations of $23,924 for the test year. Company's Mr. Thorpe stated that Company has made the "usual" efforts to collect delinquent accounts, such as letters to the non-paying customers, but claimed that Company has had little success since most of the delinquent customers are being charged only an availability fee and have no service which can be terminated for nonpayment. He said the utility has never used formal legal action in an attempt to collect these amounts.

Staff witness Leis allowed an uncollectable sewer accounts expense of only one percent of gross annual sewer revenues by decreasing this expense by $21,403. He testified that this is current Staff policy and is in keeping with experience with other utilities.

Since bad debts are a fact of business life, the Commission recognizes that it is appropriate to make some allowance for uncollectable accounts with any company. In making rates for the future, however, we are not bound to recognize Company's actual bad debt experience, but only a sum which we find reasonable. Experience with other utilities has resulted in a Staff policy fixing one percent of gross annual revenues as a reasonable uncollectable account expense.

Company bears the burden of proving that it is entitled to a level of bad debt expenses greater than that experienced by most utilities. By making only a minimal attempt to collect delinquent accounts, Company has not met that burden to our satisfaction. Company may forego the effort to collect these revenues if it so chooses, but we will not ask the ratepayer to make up for this relinquished opportunity. Consequently, we find that one percent of gross annual sewer revenues is a reasonable uncollectable account expense.

ELECTRICITY EXPENSE ADJUSTMENT

Company has proposed an adjustment to increase Company's test year electricity expense of $108,351 by $26,583 in order to "annualize" a Rappahannock Electric Cooperative rate increase which became effective October 1, 1979. The Staff made an electricity expense adjustment of $27,929 which it labeled as a "Company projection." The record does not indicate the reason for the discrepancy between these numbers. Staff witness Leis stated that Company operates under the Cooperative's Rate Schedules "B-1", "A-1", and "LS".

Company witness Frasher testified that he calculated this adjustment by applying (1) the increase on base rates effective October 1, 1979, and (2) the average of the fuel adjustment clause factors for the first three months of 1980,

to the number of kilowatt hours consumed by Company during the 1979 test year.

This method of calculation is not, as Company and the Commission Staff indicated, merely an annualization of the Cooperative's known rate increase, because it contains all the elements of a projected test year concept. Company's calculation is based upon two assumptions: (1) that Company's power usage will remain the same in the future as in the test year, and (2) that the electric rates utilized by Company in making its calculation are representative of the future. These assumptions are arbitrary and without justification. Company appears not to have done trend analyses (1) to show that its power usage for 1979 is representative over time, and (2) to show that first quarter 1980 fuel factors are representative of the future. As the Commission well knows, and even Mr. Frasher admits, the fuel factor for electric cooperatives changes monthly.[2] Knowing this, Mr. Frasher apparently had no basis for going outside of the test year and using the average fuel factor

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[2] Additionally, these fuel factors may decrease just as readily as they increase and they may even become negative, which would, in effect, cause a reduction in the cooperative's rates. [Each of the Cooperative's rate schedules under which Company receives service contains the following provision: "The amount of charges calculated at the above rate is subject to increase or decrease under provisions of the Cooperative's wholesale power cost adjustment clause, Schedule "WPCA"."]

for first quarter, 1980. In fact, no basis for either of Company's assumptions appears in the record.

This Commission ordinarily does not allow adjustments for future expenses to be incurred within one year after the test year unless they are known and definite. We, therefore, find that Company's electricity adjustment as calculated is speculative and should be disallowed.

AFFILIATE EXPENSES

During the hearing Company witnesses testified that Transcontinental Development Company (TDC), an affiliate of Company, provides the following services to the utility: administration of Company employee benefit plans, administration of Company insurance plans, budget review and assistance in preparation of the budget, accounting reviews, financial data, workmen's compensation, and tax considerations. Company witness Frasher stated that for its services TDC is paid a fee equal to five percent of the operating expenses of the utility.

Maryland Marine Utilities, another affiliate, provides day-to-day administrative, accounting, and billing services to Company. Company witness Thorpe is the general manager of both Company and Maryland Marine Utilities. Mr. Thorpe's office is located in Maryland. The Company Controller, the Operations Manager, and the Data Controller are also

located in Maryland and their salaries are llocated between Company and Maryland Marine.

Staff accountant Leis included $26,060 of Company's booked affiliate expenses in the Staff accounting exhibit based upon the old affiliate agreement between Company and its former parent, Boise Cascade. He stated that these expenses were factored into the Staff calculations for informational purposes only and that the inclusion of such figures should not be construed to imply Staff acceptance of them.

Protestant witness Carpenter recommended the elimination of the management fee because his investigation disclosed no instance of any management service being performed for Company by its parent. He stated that the relationship between the two companies appeared to be the normal one where the parent company receives the profits or stands the losses of its subsidiary.

Although AtPac purchased the stock of the utility in December, 1978, no affiliate agreements were filed with the Commission until October 29, 1980, only seven days before the public hearing. These agreements were filed with the Clerk of the Commission by Company counsel, presumably for approval since the cover letter indicated that the "requisite formal application" was being prepared. Company's post-hearing filing on January 13, 1981, included a copy of an application for approval of affiliate transactions which was formally filed along with new affiliate agreements,

the same day with the Clerk of the Commission for review by the Commission.[3] The agreement between TDC and Company which was filed on October 29, 1980, is essentially identical to the agreement between these parties which was filed on January 13, 1981, except that the monthly charge for management services was to be $3,000 rather than the $1,500 charge listed in the later submittal. A memorandum to the Commission purports to explain what management services are supplied by TDC in return for the $1,500 per month payments from Company.

There are numerous benefits available to the parties of affiliated relationships. Parent companies may be able to share the expense of sophisticated equipment and personnel with subsidiaries and receive tax advantages not otherwise available to them. Parent and subsidiaries often are able to take advantage of economies of scale.

Subsidiaries often benefit as a result of their attracting and retaining management which could not be attracted or retained if operating alone. Further, utility-owned subsidiaries are often able to obtain equipment and materials at lower costs through their parent or sister subsidiaries. A subsidiary may benefit from having access to financial resources which

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[3] The affiliate agreements filed on January 13, 1981, are dated November 17, 1980, twelve days after the hearing.

would not otherwise be available because of size or location, or other reasons. Ratepayers may benefit by lower costs and better service because of affiliate arrangements.

However, affiliate transactions do not take place at arms length. For that reason, the Virginia legislature enacted Chapter 4 of Title 56 of the Code of Virginia ("Regulation of Relations with Affiliated Interests"). This chapter requires the Commission to scrutinize affiliate transactions on two levels. The first level pertains to contracts and/or arrangements between the affiliates. Contracts and/or arrangements are not valid, or effective, until they are filed with, and approved by, the Commission.

At the second level of scrutiny, Chapter 4 requires the Commission to focus on specific transactions, payments or compensations made by a utility to an affiliated interest. Such individual transactions generally should be reviewed during the course of a rate proceeding. Virginia Code §56-79 sets out the nature of the proof necessary to permit the Commission to determine the reasonableness of specific transactions, together with the arrangements or contracts under which they were made. Virginia Code §56-80 provides that the Commission may disallow affiliate payments, even those made under contracts previously approved.

Based upon the facts in the record, we have considerable doubt that the expenses booked for services furnished by TDC

would be reasonable even if their services had been provided by nonaffiliated firms. By examining the list of services contained in Company's January 13, 1981, submittal and the discussion of these services by the Company witnesses, one would think that such assistance was being rendered to a large corporation with hundreds of employees and complicated budgetary and financial problems. This company, however, has only 15 on-site employees and about 800 active customers. Why such a small company needs to pay an outside consultant to handle its insurance and employee benefit programs, for example, was never explained.

There are certain basic functions which a small company's internal management should be expected to be competent to perform itself, with reasonable amounts of outside assistance on a periodic basis. There is no evidence in the record to lead us to conclude that this Company's employee, financial, or accounting situations are so complex as to require the expensive extra services retained by Company.

Virginia Code §56-78 provides that any payment or compensation to an affiliate may be disallowed by the Commission unless satisfactory proof is submitted of the cost to the affiliated interest rendering the service. The record in this case was not only delinquent, it was completely devoid of any such cost data, at least until January 13, 1981. Even the limited amount of data filed on that date

was superficial and, by Company's own admission, an estimate. Considering the fact that at least a portion of the affiliate expenditures do not appear to have been reasonable even if paid to non-affiliated companies, it would be totally irresponsible of us to excuse Company's failure to submit full cost records and accounts in this case. Thus, we find that it would be improper to make an allowance for affiliated expenses incurred during the test year.

RATE CASE EXPENSE

Company has proposed an allowance for rate case expenses totaling $28,000, to be amortized over four years at $7,000 per year. Company witness Frasher testified that this is an estimate based on the time devoted to the case by his firm, Brockmeier Consulting Engineers, Inc., the cost of Company's legal counsel, and any costs incurred by others. He further stated that approximately $25,000 of the estimated $28,000 cost of the rate case was to pay for the participation of his firm. Staff witness Leis said that as of August 31, 1980, $19,640 had been booked for rate case expense and that he assumed that before the case was over, the total expense would equal the figure requested.

We believe that the proposed allowance for the cost of this rate case is excessive. It exceeds 11 percent of the

sewer operation's adjusted test year revenues as determined by Staff witness Leis. The Commission is not required to impose upon the ratepayers whatever a company might choose to spend for legal and accounting assistance in connection with a rate case.

Mr. Frasher's testimony was of limited value, and based on the evidence presented, we fail to see why it was necessary for his firm to participate in this case. Mr. Frasher's presentation at the hearing was not the knowledgeable and informed testimony that we would expect to receive from a competent utility accountant familiar with a utility's operations. In fact, the witness lacked knowledge of many facets of Company's operations. He did not know the details of the purchase of Company by AtPac Land Company. His knowledge of Company's $2.4 million dollar promissory note, the apparent current holder of the note, the relationship of the apparent current holder of the note to Company and its affiliates, and the transaction whereby the apparent holder of the note acquired the note, was very imprecise, at best. Several of his responses to cross-examination questions on these matters included the phrase "I believe." In response to another question, he replied "that is my understanding, yes." To yet another question he responded "not to my knowledge." Finally, under continued cross-examination, Mr. Frasher admitted

that he didn't know if there was an affiliate relationship between the apparent holder of the note and Company. Put in their best light, these responses show that Mr. Frasher did not have a clear knowledge, if any whatsoever, of the facts involved in Company's liability on a $2.4 million note of indebtedness.

In response to a question regarding a $123,323 entry identified as "Payables to Associated Companies" on Company's balance sheet, Mr. Frasher indicated that he could not identify the "associated companies" or the services provided by these "associated companies." Mr. Frasher also could not quantify the cost of bookkeeping and data processing services provided to Company by other firms.

In short, so far as appears in the record, Brockmeier Consulting Engineers merely prepared some very generalized accounting testimony,[4] for which it expects to be paid $25,000 over and above the $15,000 annual retainer already charged by the firm. Quite a bit of this firm's rate case charges were undoubtedly consumed by coast-to-coast travel and telephone expenses. We believe that the $25,000 charged by Brockmeier Consulting Engineers for their participation in this proceeding is unreasonable. Since there is no evidence

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[4] Company's financial statements were prepared by an affiliated company, Maryland Marine.

in the record to allow a determination of a reasonable fee for the services rendered, we find that $25,000 should be disallowed for ratemaking purposes. The remaining $3,000 of rate case expenses are approved for amortization over four years.

PAYROLL EXPENSE

Company witness Thorpe testified that payroll expenses were about $134,000 during the test period. He said the work time of 16.1 personnel is charged to the Company, the fraction being due to the fact that the time of four people in Berlin, Maryland, including himself, is allocated in various proportions between Company and Maryland Marine Utilities. Fifteen people actually work on site at Lake of the Woods. These include a field superintendent, maintenance foreman, construction foreman, two office workers, and various construction and maintenance personnel.

Although Staff engineer Tice said he felt the number of employees was excessively high, constituting one person per 50 customers, Mr. Thorpe said he did not feel that a reduction in personnel could be achieved without affecting service, claiming that the maintenance and construction problems associated with this system require a larger labor force than does the traditional sewer system. Mr. Thorpe noted that the Company had as many as 21 employees in 1978.

Mr. Thorpe stated that the field superintendent lives at the subdivision, was actively involved in the construction of the system, and, in Thorpe's opinion, is fully capable of handling the day-to-day operations of Company.

The construction work necessary at Company involves such things as adding new sewage holding tanks as needed, replacing old tanks and valves, and upgrading vacuum lines to larger sizes.

The protestant's views on the size of the work force and its effectiveness were quite different from that of Company. Protestant witness Potter, President of Lake of the Woods Association, claimed that there is no effective supervision on site at the community and that this defect encouraged considerable "feather-bedding". Protestant witness Lodge, General Manager of the Asociation, echoed Potter's sentiments. He said that Mr. Brockmeier, then of Company's former parent, Boise Cascade, and now retained as a consultant to Company, testified before this Commission in 1975 that there would be a full-time manager on site, and that a total of eight people should be able to maintain and operate the system. He claimed that the field superintendent was not capable of doing an adequate job and that the size of the staff was grossly inflated due to lack of management supervision and technical ability. He said that often no satisfactory answer is found

to serious service problems until calls are made to the personnel in Mar land. He cited instances of employees engaged in horseplay and driving aimlessly around the subdivison as examples of conditions caused by lack of effective supervision on the site.

According to Mr. Lodge, there have been hundreds of service difficulties in his nine months with the Association. He listed various problems such as overflowing sewage holding tanks, broken sewer lines, sewage running into the lake, excessive odors from pumping stations, and lack of adequate water pressure. He said that in some cases, overflowing tanks are repeatedly pumped out with no attempt being made to solve the underlying technical problem.

In observing that Company's 16.1 employees are about one employee for every 50 customers, Staff witness Tice compared this to a gravity flow system of Lake of the Woods' size within Mr. Tice's knowledge which has a ratio of one employee to 250 customers. Company has five persons classified as full-time construction workers: an equipment operator, two laborers, a construction foreman, and a construction lead man. Even though Company employs 5 full-time workers, Mr. Tice said that the construction work in the development does not appear to be a daily operation. Mr. Tice felt that Company should give a detailed accounting of its work force.

After some very pointed cross-examination, Mr. Thorpe admitted that one man classified as a sewage treatment plant operator was actually a seventh maintenance man who is also a part time treatment plant operator. Generally, his duties around the plant consist only of collecting water samples in a jar twice a day and doing the "housekeeping and grounds maintenance" at the plant.

Information received from Company on January 13, 1981, listed twenty-seven on-site employees for the test year. Ten of these employees are listed in terminated status on the last day of the test year. The $10,842 salary of one employee, R. Trenary, who apparently was terminated after the end of the test year, was adjusted out of the test year payroll expense by the Commission staff. Reducing the number of listed on-site employees (27) by the number terminated during the test year (10) and the number known to have been terminated after the test year (1), we are left with 16 employees, one more than the 15 on-site employees for which Mr. Thorpe listed classified positions. There appears to be at least one extra employee's salary included in the Staff's adjusted test year payroll expense. Company also appears to have a turnover ratio of at least 67 percent among on-site employee positions, assuming that two positions which existed during the test year have been eliminated.

We find in the record conside able evidence that Company is overstaffed. However, it is not possible from the record of this case to quantify with any degree of certainty the amount by which labor expenses should be reduced. Therefore, we find that the Staff should undertake a separate, detailed examination of the entire employment situation at Lake of the Woods. The examination shall include a determination of how many and what types of employees are reasonably necessary to operate and maintain the system both on and off-site, reasonable pay levels for such personnel, and the effectiveness of on-site management in directing and supervising the work force.

CONSULTING ENGINEER EXPENSE

According to Company witness Frasher, his firm, Brockmeier Consulting Engineers, Inc., of Santa Monica, California, is paid a retainer of $1,250 per month for providing management consulting on rates and utility matters, design services, master planning, and capital budgeting. Company witness Thorpe indicated that this firm is very knowledgeable regarding vacuum sewer systems. Pipeline design projects are not covered by the retainer and are billed separately. Brockmeier is also on retainer with Maryland Marine Utilities. Mr. Thorpe stated that he has no knowledge of any ownership connection between

Brockmeier and Company's parent, AtPac. Mr. Frasher stated that Brockmeier is a separate, independent corporation, having AtPac, Company, and Maryland Marine among its clients.

Protestant witness Carpenter would eliminate the $15,000 annual Brockmeier retainer from Company's operating expenses because personnel of the firm are rarely at Lake of the Woods and he had seen no evidence of consulting services having been performed.

Based upon the technological problems inherent in operating the vacuum sewer system, it would appear prudent to allow Company to retain engineering expertise to deal with design matters. However, since Mr. Thorpe stated that the Brockmeier firm does not become involved in maintenance problems, and since most of the problems mentioned during the hearing involved maintenance and managerial problems, there appears to have been very little, if any, design work on the vacuum system done during the test year. There was testimony that the consultant redesigned a force main to replace an existing force main (apparently outside of the test year). Mr. Lodge pointed out that force mains are a part of traditional sewerage systems and are not peculiar to vacuum systems alone. It does not appear to be reasonable to retain a consulting engineer located 3,000

miles away to handle conventional sewerage system problems which any consulting sanitary engineering firm would be competent to do. Although we question the wisdom of retaining a consultant located in California to handle the design problems of both the conventional and the vacuum portions of the sewerage system, there is no evidence in the record itemizing or otherwise identifying the elements (i.e., vacuum sewer work, force main work, travel expense and telephone expense) of work or services rendered in justification of the $16,510.95 actually paid to Brockmeier during the test year. However, despite our obvious reservations regarding the propriety of the payments, because of the nature of the system and its attendant problems, we will accept - for this proceeding - the aforesaid consulting engineering expense.

EFFECT ON THE CONSUMERS

Transcending all arguments about individual expense items and accounting treatments was the Protestant's central theme that a rate increase of the magnitude proposed would be devastating to the community of Lake of the Woods. Alan Potter, President of the Association, contended that Lake of the Woods is important to Orange County. It is the third largest population center in the County and contributes

15 percent of the County's total real estate taxes. He said the proposed rates would place the development at a tremendous disadvantage compared with other parts of the general Northern Virginia area in its ability to attract new residents. He presented an exhibit which showed sewer rates in the general area to range from about $73 a year in Alexandria to $188 a year in Fairfax City, as compared with the proposed $480 a year in Lake of the Woods. Upon objection by Company counsel, he denied that he was presenting these figures for the purpose of fixing the subject rates on a comparative basis, but merely to show that a person planning to build a new home in the area would likely be disinclined to locate in Lake of the Woods. Potter concluded that even the interim rate increase "will kill the future development and growth of this community".

Several witnesses said the impact of the rate increase on present residents with fixed incomes would be very severe. If they found they could not pay the increased rates, they would be forced to offer their property for sale, and yet might be unable to find a buyer at a reasonable price for the very reason compelling the offer to sell. Mr. Lodge claimed that "both Lake of the Woods and Lake of the Woods Utility Company rely upon steady growth to survive. The large sewerage rate increase will cause us both to shrivel up and die."

Albin L. Lindall, a resident of Lake of the Woods and a licensed real estate broker, testified that he has been active in the real estate field in the Lake of the Woods area for the past twelve years. In the past, about 70 new homes have been built in the development each year, and the market for existing homes has been good until recently. However, he said that when the proposed increase was announced, the effect on saleability of property was immediate and adverse. Several prospective lot purchasers have broken off negotiations and the sale of existing homes has been hampered. He stated that the interim rate level would cause the growth rate of the community to decline, and the larger proposed rates would have a "very much greater" adverse effect.

George P. Beard, Jr., Chairman of the Board of the Second National Bank of Culpeper, testified that this situation makes his bank much more cautious in making mortgage money available in the development and also causes it concern with the security of existing mortgages, which amount to approximately $1 million at present.

Company witness Thorpe said that although Company had considered the impact of this increase on the present customers and the prospects for future development in the area, he really did not have any opinion whether the increase

would slow new construction. He went on to say that his concern was whether the parent company can continue to fund an operation which cannot meet expenses and which does not have the ability to borrow money from outside sources.

It is obvious that the amount of the requested rate increase is exorbitant from the standpoint of the consumer. The evidence establishes that such an increase would be devastating to this community. The testimony of an experienced real estate broker and a banker demonstrates that even the interim rates and the pendency of this case have had a depressing effect on the continuing development of the subject properties and the availability of mortgage money. Rates so significantly higher than those available in adjacent areas will make Lake of the Wood unattractive to prospective home purchasers and will discourage those who now own vacant lots from building. As many residents pointed out, the viability of Company is tied to the viability of the community. Rates which will strangle growth, or cause an out-migration, can hardly benefit Company. The evidence is that the proposed rates would have this effect.

It is particularly important that one be mindful of the impact of drastic rate increases on consumers of residential

utility services. When the rate charged exceeds the economic worth of the service, purchasers of some regulated sevices can make this quickly apparent. Transportation customers, for example, can simply cease using the service and substitute other methods of travel. Except in rare situations, such as switching from electric to gas heat for example, the matter is not so easy for customers who purchase residential services. Short of selling their home, they have no alternative to the service offered. Regulatory agencies must be especially watchful to avoid trapping such consumers in intolerable situations from which they have no realistic escape.

SYSTEM UTILIZATION

As we mentioned previously, although only about 800 lots have been improved with dwellings, the development consists of approximately 4,200 lots. Company therefore serves less than 20 percent of its potential. Despite the number of years Company has operated, in a real sense, it remains in its developmental stage.

Company witness Thorpe testified that the utility was built originally to serve the entire development. Apparently, only additional individual holding tanks, lot connections, and some upgrading of facilities would be

necessary to serve all 4,200 lots. The conclusion is inescapable that this system is presently overbuilt. Even though sewage may be flowing through every pipe and pumping station in the system, those pipes and pumping stations are sized to carry a much greater volume of sewage than they are now carrying.[5] Obviously, the entire investment in utility plant is not used and useful. It is unreasonable to force a fraction of the potential customers to pay for a system designed to serve many more. Unfortunately, however, the evidence in the record is insufficiently detailed to allow us to determine the dollar value of that portion of the utility plant that is used and useful, or the dollar value of the expenses incurred by Company's necessary maintenance of that portion of the utility plant which is not used and useful.

$2.4 MILLION PROMISSORY NOTE

Problems with affiliates arose once again when discussing the major portion of Company's indebtedness. Staff witness Leis testified that, in 1975, Boise Cascade Home and Land

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[5] For example, the gravity sewer pipe leading to the sewage treatment plant is designed and built to carry approximately 5.25 times more sewage than it is currently carrying (4,200 total lots divided by 800 lots with dwellings equals 5.25).

Corporation purchased Lake of the Woods Service Company and transferred the assets to the Boise subsidiary, Lake of the Woods Utility Company. In return, Boise received a promissory note which accrued interest at 8 percent per year and stock from the utility company. This note payable is shown on Company's balance sheet in the amount of $2,402,702.[6] Questions developed in the hearing as to the disposition of this note upon the sale of the utility stock from Boise to AtPac Land Company in 1978. Information on this subject at the hearing was sketchy and conflicting.

Mr. Thorpe stated that the utility company was simply one part of a package acquisition by AtPac Land Company from Boise. However, he said that he did not know the actual details of the transaction. He did say he believed the above note was now payable to an affiliate of AtPac, name unknown. Mr. Frasher testified that the note is not held by an affiliate, to his knowledge, but is held by Perry R. Bass, Inc., and he believed this assignment may have been made at about the time of the sale of the Company stock to AtPac.

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[6] By order dated September 29, 1977, in Case No. A-592, the Commission authorized open account indebtedness owed to Boise Cascade in the amount of $2,347,280 with interest chargeable at the rate of 8 percent per year. The order further provided that no payment of such interest shall in fact be made without the further order of this Commission.

Mr. Leis testified that he presumed that the interest on the note was payable to the new parent company, AtPac, but he had not seen any documentation to that affect.

On January 13, 1981, Company submitted further information about this note. That information indicates that a demand note was given by Company to Boise Cascade on December 1, 1978, in the amount of $2,402,702, bearing 8 percent interest.[7] When AtPac purchased Company's stock, the note was sold in a "related but separate transaction" by Boise to Perry R. Bass, Inc., which purchased receivables of "various entities" at that time for cash at a discount, amount unstated. According to the affiliate application included with the January 13, 1981, submittal, the Bass corporation later transferred interests in these debts to Perry R. Bass, a shareholder, and another corporation owned by Perry R. Bass. The application states that Perry R. Bass is the father of sons, who, in general terms, have various business interests which can be traced eventually to Lake of the Woods Utility Company. Another stockholder of the Bass corporation consists of trusts for the children of the Bass brothers. Trusts for the children of "one or more" of the Bass brothers are also stockholders in an admitted affiliate of AtPac and Company.

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[7] Approval for the issuance of this note was never obtained from the Commission as required by Chapter 3 of Title 56 of the Code of Virginia.

The application contends, however, that neither Perry R. Bass, Inc. nor any co-owners of the note have holdings in any company with direct ties to the utility.

Although the status of the $2.4 million note for rate-making purposes has great significance in the determination of the size of Company's rate base and its capital structure, the record is inadequate to permit a definitive determination of the affiliate relationship, if any, of the holders of the note to Company. Company's witnesses were unable to provide the evidence necessary to resolve this matter and Company's January 13 submittal raised as many questions as it answered. Consequently, this matter will be addressed in a separate proceeding.[8]

CIRCUMSTANCES UNDER WHICH ATPAC PURCHASED UTILITY STOCK

As Company counsel agreed, Company was a losing proposition at the time AtPac acquired it. Company's own exhibits state that the total company suffered adjusted net operating losses

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[8] It is anticipated that the relationship between the note holder and Company will be investigated in conjunction with Company's application for approval of affiliate agreements filed on January 13, 1981 (Case #PUA810003). If the Commission finds that the holder of the $2.4 million note is an affiliated interest of Company within the meaning of §56-76 of the Code, the value of the note, for ratemaking purposes, will become equal to the discount price paid for the note. The rate base or investment of Company would thus be reduced.

of over $163,000 during 1979 on a total company adjusted rate base of about $2.4 million. Apparently, a similar environment had existed for some time. In the last rate case, Case No. 19867, concluded by order of August 5, 1977, the Commission approved rates which were designed merely to reduce the operating loss for the test year ended May 31, 1977 from about $222,000 to $142,000. The Company's proposed rates in that case still would have resulted in a test year net operating loss of over $86,000.

AtPac must therefore be charged with the knowledge of Company's serious financial condition when it purchased company as part of a package transaction from Boise Cascade. It must also be charged with knowledge of the unique, costly, and troublesome sewer system employed at the development.

AtPac also knew of the other conditions mentioned earlier - that less than 20 percent of the lots are occupied and that a massive rate increase would be necessary to bring this Company into the black. Indeed, it appears that a purchaser such as AtPac would have considered all these matters when negotiating the purchase price. Additionally, in the application for approval of affiliate relationships and contracts which was part of the January 13, 1981, submittal, AtPac admitted that acquisition of the $2.4 million note by the Bass Corporation was a consideration in its decision to purchase the stock of the utility.

NET OPERATING LOSS

Disallowing (1) the proposed electricity expense adjustment, (2) Company's identified affiliate expenses, and (3) $25,000 of Company's rate case expenses, limiting Company's bad debt allowance to one percent of gross annual sewer revenues, and accepting Staff's accounting and pro forma adjustments otherwise not in issue in this proceeding, we find the level of Company's earnings for its sewer operations under existing permanent rates to be as follows for the 1979 test year:

Adjusted Operating Revenues	$253,636
Adjusted Operating Revenue Deductions	$364,064
Adjusted Net Operating Loss	$110,428

NO RETURN ON RATE BASE

Utility companies are natural monopolies, requiring vigorous regulation for the protection of the public. Waste and extravagance is eliminated from free markets by management competence and competition. The same standards of efficient and economical management must be applied by regulators to the monopolies they regulate.

As regulators we must base our decisions on informed and impartial judgment. Our decisions must not, however,

be rendered in a vacuum by blindly plugging numbers into a formula designed to produce rates which will permit the utility to cover its operating expenses and earn a return on its investment. The cost of waste, inefficiency, and poor business decisions must be borne by the utility, its managers and stockholders.

The foregoing discussion may be reduced to the following points, among others:

(1) The sewer system is overbuilt in relation to present customers' needs. Consequently, Company is still, in a real sense, in its developmental stage.

(2) There is considerable evidence that Company is overstaffed and inefficient.

(3) There is also evidence of poor service.

(4) Company appears to make excessive and questionable use of the services of affiliates and a California consulting firm.

(5) It appears that the lack of on-site management personnel contributes to and exacerbates Company's other problems.

(6) Company's lack of a meaningful collection program for delinquent accounts contributes to its financial woes.

(7) Company's requested rate increase is exorbitant from the standpoint of the consumer and such an increase would be devastating to the Lake of the Woods community.

(8) Although the status of the $2.4 million promissory note issued by Company has great significance in the determination of the size of Company's rate base, its depreciation expense, and its capital structure, the present record is inadequate to permit a determination of the affiliate relationship to Company, if any, of the holders of the note and the propriety of including the note in Company's capital structure.

(9) At the time of the purchase of Company's stock, AtPac must be charged with the knowledge (a) of Company's serious financial condition, (b) of the relatively unique, costly, and troublesome sewer system employed at the development, and (c) that the sewer system is overbuilt.

In consideration of the above, we conclude that Company should be authorized to revise its tariffs to produce additional net revenues of $114,671.[9] This will allow Company to "break-even" based on the adjusted test year results but will not provide for a return on the questionable amount of Company's investment. Actually we entertain considerable fears that permitting a "break-even" result in this case may be somewhat generous. The impact on consumers of rates designed to produce this effect will still be burdensome, an increase from $8.00

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[9] Calculated by grossing up the $110,428 adjusted net operating loss for the test year to provide for a one percent bad debt allowance and additional gross receipts tax payments.

per month to $20.43 per month. Nevertheless, based on the evidence in this record, we believe that such a finding strikes a reasonable balance between the interests of the consumer and Company.

AN ATTESTED COPY hereof shall be sent to John W. Riely, Esquire, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212; Eric M. Page, Esquire, Assistant Attorney General, 11 South 12th Street, Richmond, Virginia 23219; Atwell W. Somerville, Esquire, P.O. Box 629, Orange, Virginia 22960; and to the Commission's Divisions of Energy Regulation, Accounting and Finance and Economic Research and Development.

A True Copy

Teste: William C. Young

Clerk of State Corporation Commission.

SUPREME COURT OF VIRGINIA

LAKE OF THE WOODS UTILITY
COMPANY,

Appellant,

v. Record No. 810785

LAKE OF THE WOODS ASSOCIATION,
INCORPORATED and STATE CORPORATION
COMMISSION OF VIRGINIA,

Appellees.

ASSIGNMENTS OF ERROR

Lake of the Woods Utility Company, Appellant herein, assigns error as follows to the order appealed from:

1. The determination by the Commission that Appellant is entitled to no return whatsoever on its investment in facilities devoted to the public service is erroneous and unsupported by the evidence of record and deprives Appellant of its property without due process of law.

2. The determination by the Commission to limit permitted rate case expense to $3,000 is erroneous and unsupported by the evidence of record, and deprives Appellant of its property without due process of law.

3. The refusal of the Commission to allow Appellant to include in its operating expenses the cost of necessary administrative, accounting and other services provided to Appel-

lant by its affiliates and for which Appellant had no facilities is erroneous and unsupported by the evidence of record and deprives Appellant of its property without due process of law.

4. The refusal of the Commission to permit Appellant to include in its operating expenses the increased amount that Appellant will have to pay for electricity to operate its pumps and other facilities is erroneous and unsupported by the evidence of record and deprives Appellant of its property without due process of law.

5. The arbitrary decision of the Commission that Appellant's reserve for bad debts should be limited to 1% of revenues is erroenous, unsupported by the evidence of record and deprives Appellant of its property without due process of law.

6. The rates authorized by the Commission are unreasonably and unjustly low and will not permit the Appellant adequate funds to pay for its costs of operation, and the determination by the Commission is therefor unlawful.

Dated August 21, 1981

LAKE OF THE WOODS UTILITY COMPANY

By _____
John W. Riely
Its Counsel

John W. Riely
C. Page O'Neill
HUNTON & WILLIAMS
P. O. Box 1535
Richmond, Virginia 23212
Of Counsel

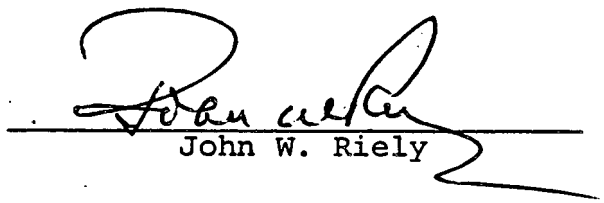
CERTIFICATE OF SERVICE

I, John W. Riely, a member of the Virginia State Bar, hereby certify that a copy of the foregoing Assignments of Error was mailed by first class mail, postage prepaid, on August 21, 1981, to each counsel of record for Appellees as follows:

Lewis S. Minter, Esquire
General Counsel
State Corporation Commission
P. O. Box 1197
Richmond, Virginia 23209

Eric M. Page, Esquire
Assistant Attorney General
11 South 12th Street
Richmond, Virginia 23219

Atwell W. Somerville, Esquire
Somerville, Moore & Joyner, Ltd.
P. O. Box 629
Orange, Virginia 22960



John W. Riely

SUPREME COURT OF VIRGINIA

LAKE OF THE WOODS UTILITY
COMPANY,

Appellant,

v. Record No. 810785

LAKE OF THE WOODS ASSOCIATION,
INCORPORATED and STATE CORPORATION
COMMISSION OF VIRGINIA,

Appellees.

ASSIGNMENT OF CROSS-ERROR BY LAKE
OF THE WOODS ASSOCIATION, INCORPORATED, APPELLEE

Lake of the Woods Association, Incorporated, an Appellee herein, assigns cross-error as follows to the order appealed from:

1. The Commission erred in not finding that the revenue requirement of Lake of the Woods Utility Company should be determined on a total combined basis (sewerage and water) in this proceeding and in not determining the combined revenue requirement at this time.

Dated August 25, 1981

LAKE OF THE WOODS ASSOCIATION, INCORPORATED

By _____
Atwell W. Somerville
Its Counsel

Atwell W. Somerville
SOMERVILLE, MOORE & JOYNER, LTD.
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Of Counsel

CERTIFICATE OF SERVICE

I, Atwell W. Somerville, a member of the Virginia State Bar, hereby certify that a copy of the foregoing Assignment of Cross-Error by Lake of the Woods Association, Incorporated, Appellee, was mailed by first class mail, postage prepaid, on August 25, 1981, to each counsel of record as follows:

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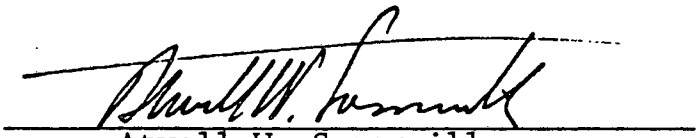

Atwell W. Somerville

Testimony of James Hinkle

16 A My name is James Hinkle. I'm a
17 resident of Lake of the Woods, Box 525, LOW, Locust
18 Grove, Virginia 22508.
19 I would like to preface my remarks
20 by saying that this statement that I'm about to
21 give you is signed by eighty-eight people. I believe
22 there are approximately a hundred or more who were
23 on the bus attending. It's a possibility that people
24 did not have the opportunity to sign this, so there
25

could be more than the eighty-eight signatures that you have received here.

The State Corporation Commission, Richmond, Virginia. Honorable Chairman: We, the undersigned, who are all in attendance here today, are property owners at Lake of the Woods located in Orange County, Commonwealth of Virginia.

We have appeared before you to plead that you deny the rate increases that have been requested by the Lake of the Woods Utility Company. The interim increase which was approved July 17th, 1980, without our knowledge or the privileges of being heard, and the additional proposed increase that has been requested, create a severe financial burden on many of the undersigned who are living on fixed retirement incomes. In some cases, individuals at seventy years of age have found it necessary to return to the job market to supplement their income in order to meet the increased cost of living.

Such exorbitant increases will effect not only the elderly but also our younger residents who are attempting to cope with the costs

of raising a family. Further, it is our belief that the growth of our community is being placed in grave jeopardy by these increases, due to the indisputable fact that housing costs will be much less expensive in nearby developments and townships.

Members of this private community, in addition to paying County and State taxes, share the cost of maintaining our facilities by an annual assessment, plus user fees for the recreational amenities. The survival of our community is dependent upon the future growth to bear the burden of these charges.

The amount of the rate increases and the excessive hook-up charges, could not only curtail such growth, but could easily result in a need to sell and relocate the situation. The probability of a glut on the market condition prevailing can easily be visualized. Several hundred very modest houses have been built at the Lake of the Woods for the purpose of week-end use. And in some cases are used only sixty days a year.

These proposed increases in, every case, place the utility costs of maintaining a secondary home in excess of the cost of maintaining a primary home. Buyers with the inclination or ability to pay these excessive charges may not be easy to find.

As the megalopolis growth advances in our direction, other business firms are becoming established nearby. Certainly the return on the investment made by these firms will be negligible until the growth potential is more fully realized.

Surely it cannot be unreasonable to expect the utility company, the Applicant, to exercise restraint and caution in their demands when such demands can destroy not only a community but their own future as well.

We sincerely trust that this Honorable body will view our plea for relief from the proposed increase favorably.

THOMAS L. THORPE, a witness called by and on behalf of the Applicant, Lake of the Woods Utility Company, having first been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. RIELY:

Q State your name and residence.

A My name is Thomas L. Thorpe. My business address is Post Office Box 384, Berlin, Maryland 21811.

Q What is your occupation?

A I am the General Manager of the Lake of the Woods Utility Company. I am also General Manager of Maryland Marine Utilities of Berlin.

A In support of its application for a rate increase in this case, the utility company will offer testimony that will demonstrate the underlying need for such increase, and its reasonableness in the light of increased costs of operation. For the benefit of those who are not familiar with the Company and the utility systems that it operates at Lake of the Woods, we will give a brief resume of Company services, a quick history of those services at the Lake, and an explanation of the somewhat unusual design of the sewerage system.

We will then review the projected financial effect of the proposed rate change and conclude with a presentation of the reasons why the proposed rate is just, reasonable and required.

Q Please describe the Company's service areas.

A Lake of the Woods Utility Company provides water and sewerage service to a community called Lake of the Woods, which is located off of Virginia State Route 3, approximately sixteen miles west of Fredericksburg. Lake of the Woods is

a recreation-oriented development consisting of approximately forty-two hundred single family residential lots on approximately twenty-six hundred acres. Its name derives from the five hundred acre man-made lake around which the wooded lots were subdivided.

Community recreational amenities include facilities for boating, fishing, swimming, golf and tennis. Of the forty-two hundred lots, approximately eight hundred have been improved with homes. These include a mixture of vacation homes and permanent residences in a ratio of about three to one.

There is a very limited amount of commercially developed or zoned property within the community.

Q Please describe the facilities owned by the Company.

A The utility provides service to the community through operation of its central water supply and distribution system and its sewage collection and treatment system. Water is supplied from eight producing wells, ranging in

depth from two hundred to four hundred fifty feet, with a combined pumping capacity of approximately four hundred and thirty gallons per minute. That equates out to about six hundred and twenty thousand gallons per day. Primary storage is in an above-ground steel tank-type reservoir with a three hundred thousand gallon capacity.

Distribution is accomplished through a system of water mains of various sizes of approximately two hundred thousand feet in length.

The sewerage system consists of a three hundred twenty-five thousand plus or minus foot of vacuum-type collection system supported by thirteen vacuum pump stations and a quarter of a million gallon per day treatment plant employing secondary treatment technology and surface discharge of treated effluent.

Due to the technology employed, both the collection system and the treatment system are very energy-intensive, demanding over two hundred kilowatts of electricty per hour. In 1979, the cost of this power amounted to approximately one hundred thousand dollars.

As I just stated, the sewerage system at Lake of the Woods employs a vacuum sewer techonology rather than the more common gravity flow technology. This vacuum --

Q Mr. Thorpe, excuse me for interrupting, but people in the back of the room apparently can't hear. If you could, pull that microphone up towards you a little bit; it would be better.

Q Now, would you please continue?

A Is that better? Very good. As I've just stated, the sewerage system at the Lake of the Woods employs a vacuum sewer technology, rather than your more common gravity flow technology. This vacuum technology has a direct, and largely uncontrollable, effect on the costs of operating and maintaining the system. Hence, a brief explanation I feel of the vacuum system is germane to this rate case.

The basic technology of vacuum sewage collection and transport was developed in 1950 and has, since that time, been utilized throughout the world in a variety of applications, including large public housing developments, primary residential

subdivisions, recreational and vacation housing developments, this type.

The primary difference between the vacuum transport sewer and the conventional sewer is implied by its name. Sewage discharged from an individual home flows by gravity to a nearby storage tank. From the storage tank, it is transported by vacuum, or differential pressure, to one of the thirteen vacuum pump stations. From the pump station, the sewage is next pumped, or pneumatically ejected, into a sewage force main which transports it to the larger gravity main flowing into the sewage treatment plant.

In more technical terms, the vacuum system employs a differential air pressure to force the sewage from point to point. A vacuum is created in the sewer main by an electric vacuum pump at the receiving point; then, sewage introduced into the main by a special vacuum valve at the sending point is forced through the main in a plug. That plug, by the relatively higher pressure air outside emitted from the main -- and that is by the special vacuum valve -- to enter the main

behind the sewage plug. As the plug moves through the main, friction forces the plug to elongate and eventually to lose contact with the pipe walls which breaks the vacuum.

To restore that vacuum and the differential pressure necessary for continued transport, the liquid plug is reformed through the use of deflections or U-shaped traps in the vacuum main. When the trap fills, differential pressure is restored and the sewage plug continues toward the vacuum station.

Two costly aspects of the vacuum system are particularly relevant here. First is the need for relatively large quantities of increasingly expensive electric power to run the vacuum pumps. Electric power rates are increasing very substantially, and as this Commission is very much aware are beyond the control of this Company.

The second costly aspect of the vacuum system is its requirement for relatively large amounts of labor to operate and maintain the vacuum pumping equipment, the vacuum valves and the main.

Unfortunately, the vacuum system is simultaneously power and labor-intensive. And, as we are all aware, those two resources both carry hefty price tags.

Before leaving the subject of engineering aspects of the Lake of the Woods sewerage system, brief mention should be made of the sewage treatment. The utility treatment plant is located on the northern side of Route 3, opposite the community itself. Due to Department of Health -- that's the NPDES, or National Pollutant Discharge Elimination System -- requirements and the amount of space available, the treatment plant employs extended aeration and chemical treatment to produce safe sewage effluent.

This secondary type treatment is essential but is also relatively more costly than ordinary or primary treatment.

Q You just mentioned the labor-intensity of the vacuum system. Please explain the effect of that on your operation and maintenance expenses.

A The water and sewerage systems are maintained, operated and administered by a crew of

approximately sixteen men and women with a combined payroll of approximately a hundred and thirty-four thousand dollars in 1979 and a projected full year of 1980 figure of one hundred forty-five thousand. Now, these payroll figures do not include taxes, overhead or benefits.

Payroll and electric power costs are the two most important categories of operating expense for the Company.

Q How many customers does the Company have?

A Employing the resources described, the utility provides service to approximately eight hundred connected water and sewer customers; however, we stand ready to serve the additional potential customers represented by the thirty-four hundred odd unimproved lots in the community.

Q What is the structure of the Company's rates?

A The Company's rate structure is set forth in detail in its filed tariffs and rules. The basic structure is as follows: The water charges on a gallons-used basis for connected

customers and a flat rate basis for availability customers. Sewer charges are a flat rate for residential customers and ninety percent of the water bill for the commercial customers, both subject to the same minimum monthly service charge.

The Company's rules also provide for customer connection fees for both water and sewer service. These connection charges are intended to approximate the average actual cost of connection. This portion of the rate structure has been in effect since the inception of service in 1967.

During the intervening fourteen years, the water rates have never been increased and the sewerage rates have been increased only once, in 1977.

Q Please outline briefly the history of these utility operations.

A Water and sewerage services were a prerequisite to the development of Lake of the Woods, and were designed and constructed from 1967 through 1969 as the community itself was developed.

Lake of the Woods Water Company

was formed in 1967 by the Virginia Wildlife Clubs, Incorporated, the original developer of Lake of the Woods. In that same year, the water company was acquired by Boise Cascade Home and Land Corporation when Boise acquired the stock of U. S. Land Corporation, the parent of the Virginia Wildlife Clubs.

In 1968, the name of the water company was changed to Lake of the Woods Service Company and shortly thereafter, in January 1969, it received a certificate of public convenience and necessity for a sewerage certificate to supplement its certificate for order for water service. And in July, and in my testimony there is an error; it says July 1979, and that should be July 1969, the Service Company was sold to Utilities, Inc., which is a large utilities holding company which maintained the ownership until 1975.

During that period, litigation ensued between the Utilities, Inc. and Boise concerning certain terms of their agreement for the purchase and sale of the Service Company. In June

of 1975, in settlement of this litigation, Boise reacquired the assets of the Service Company and transferred them to the newly-created, wholly-owned subsidiary, which is now Lake of the Woods Utility Company.

Because Boise paid less than the depreciated cost of the utility plant then in service, the new utility company recorded on its books in 1975 an acquisition adjustment of some six hundred and thirty-nine thousand dollars to reflect the difference between depreciated cost and the price actually paid. The adjustment has since been amortized and, by month-end September 1980 will be completely eliminated.

In April of 1979, the utility's stock was sold by Boise to AtPac Land Company which is the present owner of the utility.

Q Mr. Thorpe, what plans does the Company have to construct additional facilities in the community?

A Well, there are certain requirements of our NPDES permit that would require certain improvements in the treatment plant. In addition,

there are always capital improvements needed in the water distribution system such as pumps and motors, these types of replacements.

In the sewer system there is a constant requirement to increase the size of certain vacuum pipelines, together with replacement of pumps and equipment. Unfortunately, as Mr. Frasher's exhibit will show, the revenue produced by the Company hardly allows major construction projects at all and, indeed, jeopardizes even the smallest project.

Our future construction program inevitably will be tied directly to the Company's ability to fund that construction and we will not be able to justify large expenditures when our financial posture is as precarious as it is today.

Q Mr. Thorpe, have you read Mr. Tice's testimony presented to the Commission?

A Yes, I have.

Q Mr. Tice comments that the number of employees per customer seems extraordinarily high for this Company.

Would you like to comment on that?

A Mr. Tice's testimony refers to eighteen employees. Actually there are sixteen point one employees, including management.

Q Has that number increased or decreased over the last few years?

A In 1978, actually we had twenty-one employees. And we are now at sixteen point one.

I might qualify the sixteen point one. It's not part of a body laying out there; it is a time sharing thing.

Q Mr. Tice seems to think this is an awful lot of employees, considering the numbers served.

Would you like to comment on that?

A Actually, if you compare it to a conventional system in which is not really possible here in this system, because it's apples and oranges, obviously it is a great percentage -- or, actually there is more employees per customer served than the average that you would expect to see in the normal area around; however, again, this system is unique.

Q If you eliminated some of these positions, would the character of the service rendered

suffer, in your opinion?

A It would have to. Yes, sir.

Q Now, Mr. Tice also commented on your connections. Have you determined the basis for those fees?

A Yes, we have. I think Mr. Frasher's exhibit would justify that. Actually, what the connection fees are to do is we have -- to recapture the costs of our actual installation, and that includes the connection to the vacuum main through to the house.

Q And what was that flat cost incurred by, you say, during 1979?

A It averages fourteen hundred and fifty-seven dollars.

Q And what is the connection fee that your propose here?

A Fourteen hundred and fifty.

Q And that's based on actual 1979 experience?

A That is correct.

CROSS EXAMINATION

BY MR. LION:

Q Mr. Thorpe, I believe you testified that AtPac Land Company purchased the stock of Lake of the Woods Utility Company in April of '79; is that correct?

A Yes.

Q What were the terms whereby AtPac acquired the stock?

A To the best of my knowledge, I can answer that, Mr. Lion. It was involved in a kind of a package, if you will, acquisition. The utility company was not the only thing that was acquired at that time by AtPac. It was involved in a number of other things that AtPac did acquire from Boise. The utility just came along with it.

Q So, would you say that AtPac really did not desire to acquire the utility except that it could not acquire these other properties without the utility?

A I really don't know that that would be a true statement on my part.

Q So you have no knowledge as to the actual terms of the purchase which was consummated between AtPac and Boise Cascade?

A No, I do not.

Q As far as you know, the only thing paid by AtPac for the stock was nine hundred thousand dollars, is that --

A Again, I'm not familiar with the terms of the acquisition. The stock, yes, I am. There is a note, and that's about all I can identify for you, sir.

Q All right. The note. I believe that note is for approximately two point four million dollars; is that correct?

A That's correct.

Q And this note is payable to Boise Cascade?

A No, it is not.

Q Who is it payable to?

A To an affiliate of AtPac.

Q The note, two point four million dollar note, is payable to an affiliate of AtPac?

A At this point in time. I may stand

corrected. At the time of the acquisition it may well have been to Boise. Yes, sir.

Q What affiliate of AtPac presently holds this note?

A I have no idea.

Q Would you know, is this affiliate of AtPac, still carrying this note upon his books and expect the notes to be repaid?

A I would assume so.

Q Was the transfer, do you know, of this note part of the agreement between AtPac and Boise Cascade at the time the utility stock was purchased?

A No. I don't, to my personal knowledge, don't -- I was not with the Company at the time this acquisition was made and, therefore, I'm a little hazy on the terms and conditions.

Q Okay. To be clear, then, you say you have no knowledge of when this took place or whether or not it was part of the package; is that correct?

A That is correct.

Q You mentioned this morning significant labor expenses associated with maintaining the sewerage system. Would you please explain and outline the construction and maintenance organization of the utility?

A Certainly. At the present time we have what we define as maintenance people, and they are specifically that, concerned with the operation and maintenance of the system itself.

The construction entity, as it is known, presently consists of three men which is an equipment operator and two laborers. Their particular assignments are the manufacture and fabrication of the holding tanks and the installation of those together with the laying of the necessary pipelines for the vacuum and also the gravity portions of those connections.

We have two female staff employees at the office.

Q That's all right. For now I'm just interested in the labor and maintenance.

You say it's for the construction and there are three men and -- there is an equipment

operator and two laborers?

A That's correct.

Q Are they full time?

A Yes. They are full time employees. They are paid by the hour and if they get rained off the job or something like that, no, their pay stops.

Q All right. But are these three men occupied year-round with putting in these tanks and constructing these tanks?

A That is not all they do. No. There is building modifications, pipeline replacement work that we do in-house as opposed to outside contracting. We have to be careful about the size of those particular jobs.

Three people are not really that many when you expect to do a whole lot.

Q Is all this outside work for the sewerage portion of the utility company?

A No. They are sometimes involved in the water side, if it's necessary.

Q Is a record kept of their hours spent in the water --

A They very definitely are. The system we use is what they call a standard work order system, and there is a work order for everything that is done within the utility. And the hours actually charged against that particular work order or that assignment is accountable. Yes. Yes.

Q How many individuals are in the maintenance portion?

A There are six.

Q Do all six of these handle the sewerage maintenance or is it sewerage and water combined?

A There is one of them that is assigned as a water, and that is not a full time operation as far as he is concerned, but he does check the wells, reads the meters and makes sure that the equipment is operating. The balance of them are full time.

Q And what do these individuals do. What does their job actually consist of?

A Actually maintaining the operation of a vacuum station, the vacuum stations, together

with the individual tanks, if you will. And may I just explain it briefly. Not just the tank but there is an air control valve and in the Lake of the Woods, particularly right now, we have a combination of some electrically controlled valves and some that are pneumatically controlled, and it's a different type of a valve; it's a kind of a modernized version of the old system as it was.

These are the highest maintenance problems that we do have within the system. And that would entail most of it by the maintenance people.

Q Do these -- are these new valves, these air vac valves, do they tend to be more maintenance free or are they possibly a greater headache than the valves you are replacing?

A No. Actually they are much less. It is much less maintenance involved in them. They are much more reliable; they offer a greater opportunity to evacuate the holding tank than the small electrical valves that were previously used.

One of the big things in using these valves, and they are a little more expensive

than the original installation; however, in the original valves, the electrical ones, we call Grenell (phonetic) right at this time, requires a separate electric service for each one of those; and there is some two hundred and sixty of those in the system right now. And so obviously we have two hundred and sixty individual power bills that represent the necessary equipment out there to operate these electrically controlled valves.

The new valve that we are using is a pneumatically actuated valve and totally independent of any electrical need, which we feel is going to ultimately be a far better system, more effective system, and a more accurate one.

Q From what you have indicated, the water and sewer operations are fairly closely related, in that you have employees doing work in both areas?

A Oh, yes.

Q You mentioned that in the construction end of it, and I assume in the maintenance end of it, that the allocation as to what the expenses are, sewer expenses or water

expenses, the expenses -- that is done in accordance with the work order for that job; is that correct?

A That is correct.

Q How is this allocation made in regards to the administrative type personnel?

A It's kind of on a proportionate basis, and it's not a guess necessarily but it's an allocated percentage of actual time for the administration.

Q So actual time is not kept? This is just an educated --

A Yeah, that's correct.

Q -- guess?

A For the administration people only.

Q And when you say administration people only, you are referring only to office personnel, or are you possibly also referring to your --

A I'm including myself in that.

Q How about the managerial, your operations, foreman and so on who actually oversee

construction?

A No. They are subject to the work order system. That is not included in administration.

Q You are familiar, I assume, with the Company's availability charges?

A Yes, I am.

Q All right. I believe the breakdown is three seventy-five for the sewerage operations, allocated to sewer; and, four dollars allocated to water?

A That is correct.

Q All right. I understand that this breakdown was accomplished I believe in 1977 with the last rate case? And the Commission approved this breakdown at that time; is that correct?

A That is correct.

Q Looking at the rate base of the water utility as opposed to the sewer utility operations, wouldn't this breakdown appear to be somewhat inequitable?

I guess what I'm getting at, your utility plant for sewer is valued in the

neighborhood of maybe two million dollars, whereas the rate base for the water plant is more on the order of five hundred thousand. Also, your expenses for the sewer appear to be much, much higher than the expenses for -- encountered with the water operation.

A That is true. Yes.

Q Therefore, wouldn't it appear that possibly a different allocation of availability fees between water and sewer would be appropriate?

A It probably -- it wouldn't --

HEARING EXAMINER: I apologize for the sound problems. I really don't know what is causing the problems. But, can those of you in the back hear when the microphone is being used? Can you hear the attorney and the witness and everyone else?

SPECTATOR: Ask him to talk into the mike.

HEARING EXAMINER: The witness or the attorney?

SPECTATOR: Both.

HEARING EXAMINER: Let's try once again using the microphone, and speak a little closer to them. Perhaps we won't be plagued with this problem.

Go ahead, Mr. Lion.

BY MR. LION: (Continuing)

Q Mr. Thorpe, before we were interrupted by the sound system, I believe you indicated that you agreed that possibly a reallocation of the availability charges between sewer and water would be appropriate; is that correct?

A That is -- am I being heard now? (Spectators indicating they cannot hear the witness)

Is that the business end of this now? The allocation of the differences between the availability charge certainly imposes no real concern. Really, the way we arrived at that it wasn't us. The present rate or the availability charge, the allocation was given by the Commission in the 1977 hearing when they raised at that time the sewer availability charge, it was two dollars.

The Company had asked for an increase to five dollars of the availability charge then. The Commission set that rate at four, or at three seventy-five. I'm sorry. Three seventy-five for sewer and allowed the water to remain where it was.

I understand what you are saying but we have no real quarrel with that.

Q In view of the operating relationship between the water and the sewer operations and the fact that many of the same personnel provide services for labor for both the sewer and the water operations, wouldn't it seem reasonable that the entire company operations should be considered in setting a rate of return for the Company?

A No. I think we -- I have done that; and, I think in Mr. Frasher's exhibits will show a combined operation as well as an individual operation. So that the investment can be made individually or combined either way.

Q I would like to go back for just a moment to your number of employees. You mentioned six maintenance men and three construction. That

totals nine. Where are your other personnel?

A We have two -- as I started to say, our office, one field superintendent and the balance is in the general administration. Myself, as a part of that; the Controller, the Data Controller, and that's where we get into those percentage of man years. There are actually four percentage factored, percentage wise including myself.

Q How many customers does the utility presently serve?

A As of right now, probably just a little in excess of eight hundred, and that's a guess on my part since I have not checked. Last week we are about eight hundred and four.

Q And how many lots are in the development?

A Approximately forty-two hundred.

Q Does the Company already have installed the main vacuum lines and pump stations in place which are necessary to serve all forty-two hundred lots?

A That is correct. It does. This is one of the problems that comes from your

high cost of operation. We are maintaining actually and operating an entire system and, albeit, it may not seem practical, but that is the way it is. And that extends to both the water and the sewer.

Q All right. So the utility started out constructing a plant which is adequate to serve the entire development, realizing that it would take a while for it to, of course, get up to the fully utilized level; is that correct?

A That is correct.

Q Has the Company considered the impact of the proposed rate increase from eight dollars to forty dollars per month on its present customers or on the future development of the Lake of the Woods community?

A Obviously they have.

Q And isn't it likely that this forty dollars per month sewerage rate would slow down the rate at which new homes are being constructed?

A That would be a guess on my part. Really, I don't know. I just have no feel for what

impact it may have. I -- one of the things that I have to look at is that the parent company of Lake of the Woods Utility Company cannot continue to pump the cash or capital into an operation that can't even break even. I can't go out and borrow money for the utility. And the parent obviously is not going to be too excited about putting dollars into something that they can see no breakeven on it.

Q On Page 10 in your prefiled testimony you refer to improvements in the sewerage treatment plant required by the NPDES permit?

A Yes.

Q Exactly what are you referring to here?

A There are two immediate considerations that must be, and that is the sludge handling program together with the sludge drying beds. And that's kind of a companion part of it. And those are the closest things to improvements right now that we must consider.

Q What is presently being done with the sludge?

A It is presently being semi-dewatered and vacuum pumped out to a farm west of Lake of the Woods somewhere.

Q And your new -- your proposed procedure in handling this is just to install drying beds; is that correct?

A That is correct.

Q And exactly what are these drying beds?

A These actually take the effluent from the sewerage treatment plant and dehydrate it or dry it, if you will, and allow the material to percolate back into the soil. The solids then would be hauled off as a solid not as a liquid.

Q Rather than the effluent, you mean the sludge?

A That is correct.

Q So these drying beds consist of really, say, four walls with --

A Oh, yeah.

Q -- a bed of sand which the liquid can then drain through leaving the solids on top; is that correct?

A That's right. They are very shallow ponds.

Q So we are not talking about anything very complex or expensive?

A No. The construction of the drying beds would not be that complex nor expensive. The equipment to move the material within the plant to the drying beds may well be.

Q Well, would not the only equipment necessary be a pump to pump the sludge?

A Yes, that's correct. But what the size of the pump has to be and the configuration necessary with the future expansion of the plant, due to the widening of Route 3, presents a problem.

Q Would you -- has the Company developed a record of what the actual cost would be of installing these drying beds?

A We are in the process of doing that now. Yes.

Q How soon do you anticipate that this construction will begin?

A Oh, it will not be this year. Probably next. It would be after the first of 1981.

Q Would you anticipate the entire construction project would cost less than twenty thousand dollars?

A No, I would not. It would be more than that.

Q Less than fifty thousand dollars?

A I really would be guessing to try to give you an idea on that, Mr. Lion.

Q Again, we are only talking about four walls with a sand bed through which the liquid can percolate through?

A Yeah, as far as the drying beds are concerned. Yes. But the other related equipment --

Q And, then, a pump to take it from the sludge holding tank to the drying bed?

A That's correct.

Q So we are talking about a pump, some sand, cinder block, some gravel underlying the sand, and some pipe to get the sludge from the treatment plant to the drying bed?

A That's correct.

Q And this would be pumped more than

fifty feet, one hundred feet?

A No. It could well be that we would have to raise the elevation due to the configuration of the plant itself and the utilization of the space that we have in there. Where the drying beds were proposed originally would be in the future under Route 3. So we are in the process of re-designing the configuration of the ultimate treatment plant. And this may well be that we have to pump, flow the sludge uphill and regrade and acquire property. There you get into an expensive phase of it.

Q Your treatment plant sets above ground level?

A That's correct. Partly.

Q And at least on one or more sides the ground is lower than the treatment plant?

A On one side. Yes.

Q Could not the drying beds be placed on that side?

A We are looking at that now, and I don't want to say no, that they can't. There are some real problems because on the density of that

material that is just at the lower end of the plant is very wet, it's almost a swamp, if you will.

Q Does the Company retain any consultants on a retainer basis?

A We pay a retainer, yes, to one of the consultants.

Q What consulting firm is that?

A Brockmeier Engineers.

Q What is the amount of the retainer?

A In the case of Lake of the Woods is twelve hundred and fifty dollars a month, but there is an exchange for services that is included. That isn't just an out and out retainer per se. Actually there is work performed within the amount of that retainer.

Q What is the relationship of Brockmeier to Lake of the Woods and AtPac?

A As a consultant.

Q It is an independent firm?

A That is true.

Q There is no connection as far as ownership goes of the consulting firm and AtPac?

A No. None to my knowledge.

Q Is the same consulting firm retained for Maryland Marine Utilities of which you are also the General Manager?

A Yes, it is.

Q Is it the same contract, the same retainer basis?

A It's on the same retainer basis, yes. The same terms of the contract but it's two contracts, one for Maryland Marine --

Q Exactly what services does Brockmeier provide in return for this twelve hundred and fifty dollars per month?

A One of them -- well, the most important ones would be engineering review of capital improvements, budget, recreation and review.

Some of the day-to-day operational problems that arise would require a little technology as far as specialized field, the vacuum system. Brockmeier consultants are very knowledgeable in the vacuum sewerage systems.

Q Since the system was installed to

serve all forty-two hundred plus lots it would appear that there is really very few capital projects to do --

A That's not exactly true. Actually the system that was installed and the system we have today doesn't really resemble one another. In concept, yes. But remember, if you will, think back when the system was installed it was a test system. Actually it was on an experimental basis for a number of years with the State Health Department.

The configurations in a number of cases, particularly one of the valve, the size of the pipelines, the sizing and the vacuum stations alone, a number of these have had to be changed to actually meet the needs or the demands. What was projected and what was guessed, if you will, in the original design has changed considerably since the technology, and the state of the art of vacuum sewer systems today has actually increased our chances of making a suitable system out of this.

Q Has any consideration been given to making this contract whereby you pay the consultant

for work done on a job-to-job basis rather than on a retainer basis?

A We do that when we are involved in specific things. Yes. We identify those.

However, the retainer covers more of the non-described specific capital jobs, those that we can identify as a project, yes. Certainly the contract doesn't interfer with that and does set out separately by a purchase order.

Q Mr. Thorpe, the Company books reflect quite a significant uncollectible sewer accounts expense for the test year.

What efforts has the Company made to collect these delinquent accounts?

A Probably I can use the phrase "usual". Letters to the delinquent accounts, primarily most of these are non-resident. They are absentee owners, people that bought the lots for speculation.

Really there is no legal recourse that we have. We can't terminate service; we can't shut them off, since they really don't have any service at this point in time. Really, the opportunity --

the only really bona fide opportunity that we have of collecting those -- and we do -- is when a lot sells or somebody decides to build a home on it. And, then, those delinquent accounts are brought up to date.

Q Have you ever taken these delinquent individuals to court and obtained a lein against the property?

A No. We have considered it but really it's a management decision on my part, and I can see turning it over to a collection agency and perhaps settling for half or something of that nature.

But taking them to court, I'm afraid the utility would be in a lot worse condition financially to try and settle those individual accounts by legal action; it would cost us more than what we've got on the books right now.

CROSS EXAMINATION

BY MR. PAGE:

Q Mr. Thorpe, let's just go through some of the numbers. The Company requested and the Commission did approve an increase in rates for the Company from eight dollars a month to twenty-four dollars a month in July; isn't that true?

A That is true.

Q And, also the Company in July requested that a permanent rate be allowed which is an increase to forty dollars a month; isn't that true?

A That's true.

Q And one of the reasons you cite in your testimony for this further request was what you called the 1980 inflationary pressures; is that true?

A (Witness nodded in the affirmative)

Q Yes?

A Yes.

Q What was the annual Consumer Price Index increase during the last month, do you know?

A No, I don't.

Q Would you say it's around twelve, twelve point seven?

A Twelve or thirteen, something in that area.

Q Was the increase anywhere near the sixty-seven percent increase from the July approved rates that you are asking the Commission to approve here?

A I would have to defer that to our accountant.

Q You don't know?

A No.

Q How many sewer companies in the country utilize the vacuum sewer technology, do you know?

A Probably about half a dozen.

Q And what percentage would that be? Very small?

A Oh, yes. It's a minute amount. Normally the gravity system is the most conventional way.

Q And Maryland Marine Utilities also

uses the technology?

A Yes, they do.

Q Two of about six in the country, right?

A That's correct.

Q Are there any customers who take sewerage service without water service?

A Yes.

Q How many of those do?

A I think we have three within the development.

Q Three out of?

A Eight hundred.

Q Do you know what the average water consumption for residential customers is?

A In terms of dollars, gallons or what?

Q Anything. Dollars, gallons.

A I would have to guess at that, and I would rather not do it. We can get you that very quickly, though.

Q Is it anywhere near forty dollars a month, do you know?

A For water?

Q For water.

A No. No. I would think not.

Q It would be about half maybe?

A Yeah, I would think maybe. And again we can develop those numbers for you, if I may.

Q Just a rough -- I'm sure the Protestants may have --

A Sure. We will be glad to do that for you.

Q Have you discussed -- you discussed your capital improvement program with Mr. Lion recently, and do you know what the Company is projecting it will spend in 1981 on capital improvements for the sewerage system only?

Do you have a projection?

A Yes. It would be probably in the neighborhood of two hundred thousand dollars projected right now.

Q And that includes the sludge drying program that you discussed with Mr. Lion?

A Yes.

Q And that's assuming that you get all the rate relief that you are asking for here?

A That is one big assumption, yes.

Q How about 1982? Would you be able to tell us what that projection is?

A We have generally projected out -- and I think just as a rule of thumb to go by, you would be looking at somewhere between one hundred and fifty to two hundred thousand dollars a year for the next five years.

Q How much did you spend in 1980? Do you know?

A I could -- I would have to refer back to --

Q Is it more or less than two hundred thousand dollars?

A Probably be less.

Q And in 1981 and so on, most of the capital improvements would be to increase the size of certain vacuum pipelines?

A That is one of the elements, yes.

MR. PAGE: Thank you. I have no further questions.

HEARING EXAMINER: Mr. Somerville.

Why don't you use the microphone if you can, Mr. Somerville?

MR. SOMERVILLE: Thank you.

CROSS EXAMINATION

BY MR. SOMERVILLE:

Q Mr. Thorpe, let me pick up on that, on the vacuum lines. Are you actually increasing the size or laying parallel lines?

A That would depend on the location and the particular job definition in general. Right now we are increasing the lines, the size of the lines.

Q Increasing the size?

A Yes.

Q The diameter?

A Yes, that's correct, increasing the diameter of the line to -- what we are doing is primarily most of the vacuum system originally was just four inch and in some cases, due to the build-out of certain areas, we find that the four inch is not adequate any longer.

Now in some certain cases you may find that they parallel and four would suffice; however, the six would -- does so much better.

Q All right, sir. Let me leave that and go back to your prepared testimony. I'm looking at Page 4, top of the page, where you made this statement: "These include a mixture of vacation homes and permanent residences in a ratio of about three to one".

Now, that would indicate that the vacation homes there are three times as many as the permanent residences. Isn't the reverse of that true?

A That may well be. And that was more or less a judgment call on my part about the three to one ratio. Nothing finite about it.

Q So you just don't know?

A (Witness nodded in the affirmative)

Q Let me go back to your operational center at Lake of the Woods.

It's my opinion that your operational center includes the water operations as well as the sewerage at the same place?

A That's correct.

Q And you have some of the same people working on both?

A Oh, yes.

Q And the female staff of two people handle both?

A Uh-huh.

Q Now, who runs that operation of Lake of the Woods?

A The direct supervision for the field personnel is the Field Superintendent obviously.

Q Who is that?

A That's Mr. Donald Harris.

Q He resides there?

A Yes, he does.

Q And he is on duty every day?

A Every day.

Q What is his educational and work background?

A Professionally he has no formal education beyond high school. As far as administration. Construction wise and in technology he does have. Donald was -- or, Mr. Harris was very instrumental in the -- actually he was one of the supervisors that built the original system there.

Q So he fully understands the system and is knowledgeable?

A He most certainly does.

Q And he is competent to handle the day-to-day problems of development?

A He does.

Q There has been no difficulty as far as you know insofar as his handling of the day-to-day problems?

A No. In fact, he has demonstrated to me since my tenure here that he is very capable of doing just that.

Q Now, he makes the decisions, day-to-day decisions, as to what work is to be performed?

A Yes, he does. He lays out the work schedules.

Q Who makes the determination as to whether it's a capital improvement or a maintenance operation?

A That's pretty much made or determined by the description of the job and it's made by the Controller. Actually the distribution of dollars is made at that time.

Q In other words, that's based on work orders that are prepared and submitted to the Controller?

A That's correct.

Q Do you supervise that?

A Not on a day-to-day basis, no. I do review the work orders from time to time, particularly those that are in question or that I would like to review for a special reason.

Q Who prepares the work orders?

A Usually they are prepared in some cases by the individuals themselves. In other words, the workers, the minor ones, complaints of that type; where it entails constructions, materials and/or labor, usually the foreman and/or the superintendent.

Q Do the laborers do that?

A No.

Q So the foreman or superintendent would prepare the work order?

A That's right. He initials every one of them.

Q What standing rules and instructions do you have for preparing the work orders to

distinguish between what is capital improvements and maintenance?

A At that point we don't. In other words, that characteristics occurs not at the time the work order is prepared but by the definition and description for that work order, what it's for. Then, the Controller makes that division.

Q So if the work order is not properly prepared, the Controller would have difficulty in making a distinction?

A He may have, yes. And it would require him to come back and question it.

Q But you -- what you have, through the years, is a system that was built that you have been continuing to make capital improvements to?

A I'm sorry.

Q You have been making capital improvements each year?

A Oh, yes.

Q So that's an ongoing --

A That is an ongoing program.

Q You speak of the high cost of electricity. From whom do you purchase your electricity?

A Rappahannock Cooperative.

Q And does Rappahannock in turn purhcase from VEPCO?

A I believe they do.

Q And does your power come from North Anna?

A I don't think so. I'm really not sure of where the actual --

MR. RIELY: If he knows the answer to that question, Mr. Somerville, he is a very fine engineer.

WITNESS THORPE: I really don't know where the power source is.

BY MR. SOMERVILLE: (Continuing)

Q What is your latest information about anticipated costs of electricity?

A The best guess that we can get is an increase. We had projected a thirty percent increase over 1979 through 1980 and into '81. Actually, actual numbers of 1980 shows where our projection was way low. We did not project

sufficient dollars to cover our purchased power. This comes from the Coop itself and their rate.

Q You have no further information on 1981?

A No. That's really where we came from, the rates were provided us and their best guess is their projection. And we just took that and interpreted it into our dollars.

Q Getting back to this matter of your maintenance and construction people, as I heard your testimony it would appear to me that the actual construction that is going on there is not as complicated?

A In some degree it is complicated. But, no, as far as pipeline workers, something like that, it's really not.

It doesn't take a highly trained person.

Q And would this be true of the maintenance also?

A No. It would not be. Maintenance does require a different degree of ability and skill.

Q But your Field Superintendent has that ability?

A Yes, he does.

Q Now, what does the Brockmeier Consulting firm do in terms of maintenance?

A In terms of maintenance, probably very little. As far as day-to-day maintenance. And I'm not quite sure I follow where you are going.

Q I would agree with you that would seem to me to be correct.

A Yes. No. No. Maintenance is something that we would not expect to get Mr. Brockmeier's outfit involved in.

Q You are using his services in the construction?

A That's correct. In design work or redesign work, yes.

Q Within the year 1980 can you tell me how much time Mr. Brockmeier spent with Lake of the Woods?

A Let's see, three -- this would make his fourth trip this year.

Q How long would he be there on each trip?

A Oh, he spent the better part of a week on one occasion. It varies. Sometimes two to three days, whatever the real need is.

Q And he confers with you regarding capital improvements and changes that need to be made, et cetera?

A Yes, he does.

Q Now, getting back to your earlier testimony, did I understand you correctly to say that in addition to the retainer that Mr. Brockmeier is paid for additional specific services?

A Yes, if it's required. Yes.

Q What type of specific services?

A Pipeline design is one of the quickest I can think of. We just recently finished the design and are out to bid on a forced main project for the Lake.

Q So, design is not covered by the retainer?

A No, that is not. To a degree it

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3 is, but in other words the retainer doesn't
4 really allow for too much of that type of dollars.

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REDIRECT EXAMINATION

BY MR. RIELY:

Q Mr. Thorpe, you've referred to the two young ladies that work at the office; they work on both water and sewerage matters, do they not?

A Yes, they do.

Q And how are the costs of their services allocated between the two?

A I would have to ask my Controller.

Q Would Mr. Frasher know the answer to that question?

A Mr. Frasher would know the answer by the time he comes up, yeah.

Q Now, you mentioned that the entire system was constructed initially. When the lots in the Lake of the Woods sold, were lots sold throughout the area or were they -- was there sort of a march from one end to the other?

A Really, I'm not sure just how it was as far as the original selling of the lots. I think probably any time someone found a lot they

wanted to buy they would be able to buy it regardless of what area it was in.

Q Did that make it necessary to build the whole system at one time?

A Yes, that together with the fact that the development company used the idea of making sure there was a water and sewerage system available to all the lots. And, therefore, they had to develop the entire system at that time.

RECROSS EXAMINATION

BY MR. LION:

Q Mr. Thorpe, I'm quite confused as to the relationship between your Company Controller and the Brockmeier Consulting firm.

They appear to be doing the same job.

A No. No. They would not be.

Q Isn't the -- you said that Brockmeier did engineering review, capital projects review?

A Yes.

Q Isn't this work that is normally done by the Company Controller?

A No. The Company Controller actually does -- that is his title, but he is responsible for the financial structure and the records keeping, keeping the Company out of jail, if you will, and making sure that the income taxes are paid.

Actually, his is an accounting function more than an engineering. He doesn't get

involved in that at all.

Q How about the capital projects review?

A Yes, as far as dollars are concerned. But that's the only involvement the Controller has in that function.

His main emphasis is in accounting and money management.

Q Is your Controller full time?

A Yes, he is.

HEARING EXAMINER; Is he located at Lake of the Woods?

WITNESS THORPE; No, he is located at the office in Berlin. His time is allocated at the Lake and he can spend, and does upon requirement, whatever time is necessary or his presence is necessary here, why, yes, he is here.

I say here. At the Lake.

BY MR. LION: (Continuing)

Q Is all of his time, then, utilized between the Maryland Utility and the Virginia Utility?

A Yes.

Q Does he have any other ties or any other companies --

A No.

Q -- that his time is allocated to?

A No, he does not.

Q Has any consideration been given to retaining the services of a local consultant; the D. C. area, of course, is pretty large and there are many nationally recognized consulting firms which have offices in the Reston/Washington, D. C. area --

A Uh-huh.

Q Has any consideration been given to retaining a local firm on a job-by-job basis due to the proximity, the ease with which they could come down to the utility plant to look it over and converse with utility officials and so on?

A Yes. Actually there has, and we find it quite often advantageous, particularly in

the attorneys' requirements, legal requirements, not so much in the engineering, because there are not too many engineers that really understand the vacuum concept. And that may sound unreal.

The Brockmeier consultant actually was instrumental in the -- or, they have been kind of -- this is a baby of theirs which was taken over by the original designer and installer and they have lived with this system for many years and are one of the most familiar in the country and probably one of the best-first consultants on vacuum technology.

And that's one of the reasons that we choose to stay with that firm.

RECROSS EXAMINATION

BY MR. SOMERVILLE:

Q Mr. Thorpe, I'm still a bit confused about your personnel. Could you very briefly run through this with me?

You told me you had six maintenance people at the Lake?

A Yes, sir.

Q And three construction people?

A That's correct.

Q Two girls in the office?

A Uh-huh.

Q That is eleven. And you gave us I think a sixteen point one figure.

Give me the other five point one, would you?

A I sure will. In fact, I think I have -- if I may refer to my notes -- do you just want me to run them down in a list very quickly?

The General Manager, he is equal to half. In other words, that's point five 0.

Q You mean you are there half the time?

A That's right.

My Operations Manager is point two five, or a quarter of his time. The Controller is point two five. And the Data Controller is point one 0.

Now those are generally associated with the office site. Management, that is equivalent to one point one 0 man-years.

All right. Field Superintendent. That's one. Maintenance Foreman, an Account Clerk.

Q What was that?

A An Account Clerk.

Q Is that one of your ladies?

A Uh-huh.

Q All right.

A And the secretary. A maintenance lead man. A construction equipment operator. Construction lead man. A treatment plant operator. A maintenance man One. Three maintenance men Three. Two laborers and one construction foreman. That should total your fifteen, and adding your one point

one 0 for G&A gives you sixteen point one.

Q Treatment plant operator, is that full time?

A Yes, it is.

Q That is all he does?

A Yes. Well, that's not exactly correct either. That's his prime thing. He may well get involved in maybe a problem at a vacuum station or something like that that is associated with the sewer, but he is actually full time sewer.

MR. SOMERVILLE: Thank you. I have no further questions.

HEARING EXAMINER: Mr. Page, do you have any recross?

MR. PAGE: I have no questions.

REDIRECT EXAMINATION

BY MR. RIELY:

Q The Controller was full time. You mean, he is full time for both Maryland and Virginia?

A That's correct.

10 HEARING EXAMINER: Mr. Thorpe, I
11 have a few questions which were suggested
12 by your testimony this morning. You said,
13 I believe, that of the forty-two hundred
14 lots in the development, all of them have
15 been supplied with all equipment necessary
16 to provide sewer and water service, is that
17 right?
18 WITNESS THORPE: That is correct.
19 HEARING EXAMINER: So in the event
20 a home is built on a vacant lot, the only
21 thing that needs to be done is to hook up
22 the home connections to the system.
23 WITNESS THORPE: That is correct.
24 HEARING EXAMINER: And disregarding
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the approximately eight hundred customers which you have which have active service with the Company, as I understand the prefiled material, the other people are charged these availability fees.

WITNESS THORPE: That is right.

HEARING EXAMINER: Everyone who owns a lot is charged an availability fee.

WITNESS THORPE: That is correct.

HEARING EXAMINER: And you said that part of your delinquency problem was in collecting these fees from absentee owners and so forth, and you mentioned that about the only time you are able to collect is when the lot is sold or built upon, is that right?

WITNESS THORPE: That is right.

HEARING EXAMINER: If you don't have a judgment lien, how do you go about collecting it at that time?

WITNESS THORPE: At that time we do have, in the sales contract, that all

indebtedness against that particular lot must be cleared before a building permit is issued.

HEARING EXAMINER: All right. And you have described Mr. Harris' work with the Company. How long has he been in the position of field superintendent?

WITNESS THORPE: He was promoted to actually Field Superintendent -- the definition of that -- about a year-and-a-half ago; prior to that time he had held the same responsibility under a different definition or title, if you will.

HEARING EXAMINER : And you said that three customers take sewer service without water service?

WITNESS THORPE: Yes. Actually, they were old, existing homes, and they do have their own sewer or septic system.

HEARING EXAMINER: Well, that is what I was wondering about. Don't you mean they take water service without sewer?

WITNESS THORPE: They take water without sewer service.

HEARING EXAMINER: All right. I understood you to testify to the contrary earlier.

WITNESS THORPE: I am sorry. That is correct.

HEARING EXAMINER: So three customers take the water service but do not take the sewer.

WITNESS THORPE: Without sewer.

HEARING EXAMINER: But the rest of the customers take both services.

WITNESS THORPE: Yes.

HEARING EXAMINER: I see you mention in one of the accounts, of a Mr. Rick Trenery.

WITNESS THORPE: Rick Trenery.

HEARING EXAMINER: Who is that, please?

WITNESS THORPE: He was a former employee at Lake of the Woods, had a combined job. Probably best defined as an administrative assistant. Kind of a semi-management

type responsibility.

HEARING EXAMINER: He is no longer with the Company?

WITNESS THORPE: No, he is no longer there.

HEARING EXAMINER: There is also mention of a F. L. Atkins. Who is that?

WITNESS THORPE: F. L. Atkins was a management consultant employed by the parent company at the acquisition time, who managed actually Lake of the Woods and also Maryland Marine as an interim type thing. That was on a contractual arrangement.

HEARING EXAMINER: At about the time of the acquisition by At Pac?

WITNESS THORPE: That is correct.

HEARING EXAMINER: Does Maryland -- is Maryland Marine a subsidiary of At Pac also?

WITNESS THORPE: Yes, it is.

HEARING EXAMINER: And how about the firm known as Trans-Continental Development?

WITNESS THORPE: Trans-Continental Development Company is a partner to At Pac.

HEARING EXAMINER: Does the Company have an agreement with Trans-Continental Development Company for certain services?

WITNESS THORPE: Yes, we do. I think you will find that that is one of the agreements that is on file, and has not yet been approved.

HEARING EXAMINER: As I understand your description of the system, there is a storage tank initially which is shared by what, two or three homes?

WITNESS THORPE: Most generally two.

HEARING EXAMINER: Two homes?

WITNESS THORPE: Yes. In some cases it could be one. I think we have one case where there are three.

HEARING EXAMINER: And some of these systems use the electrical valve and some use the air vac system?

WITNESS THORPE: That is correct.

HEARING EXAMINER: Can you tell me a breakdown of the percentage of how many use each system?

WITNESS THORPE: I think we have probably, as I referred to, about two hundred and sixty power services, which would indicate in the terms of about three hundred likely are the electrically controlled valves. Everything that has been installed in the last two to two and a half years has been the air vac. So we are less than half of the old system -- maybe a sixty/forty split is about an equitable way to assign it.

HEARING EXAMINER: Passing that point in the system, do the laterals in the home connect to a main in the street much as an ordinary sewer system?

WITNESS THORPE: No. The laterals from the home connect to the holding tank. The holding tank then connects to the main.

HEARING EXAMINER: All right. And

those mains are in or along side the street normally?

WITNESS THORPE: Yes. Normally they are. There could be in easements to the rear of the property, or wherever.

HEARING EXAMINER: What sort of services does Trans-Continental Development Company provide?

WITNESS THORPE: They provide basically a number of administrative services. I think probably the most definitive would be the insurance policy benefits for employees. Budget review and assistance in preparation. Accounting reviews, financial data.

HEARING EXAMINER: You don't mean that they are the insurer, do you?

WITNESS THORPE: No, no. They administer the insurance.

HEARING EXAMINER: I see in other testimony would indicate, which I expect would be filed today, a description of

a sediment lease between Boise Cascade and Utilities, Inc.; are you familiar with that transaction, generally? The details of it?

WITNESS THORPE: No, I am not familiar with the finite details of it.

HEARING EXAMINER : Would Mr. Frasher be?

WITNESS THORPE: He would be able to speak to that.

HEARING EXAMINER: Any further questions of this witness, Mr. Riely?

BY MR. LION (Continuing)

Q If we can talk once again about this sewerage treatment plant operator. Is not the sewerage treatment plant automated -- the activated sludge unit?

A Yes, it is.

Q This is for the most part fully automated, is this not correct?

A No, at one time probably. The original conceptual design of it is pretty much

automated, but it does requir an operator to do what we do now other than just primary treatment.

Q All right. This activated sludge unit, the sewerage floats into the system through a commenator, which chews up the solids in the activated sludge unit, which is aerated, is that correct?

A That is correct.

Q These aerators are either on full time or on timer, so that there needs to be no adjustment made, is that correct?

A Normally, they are on timer, but they are pretty much full time.

Q So they run continuously.

A That is correct.

Q From there, the sewerage affluent flows to a sediment tank, clears out the sludge, and flows to a holding tank, is that correct?

A We are well versed on it, yes.

Q So the only time the operator really needs to do anything is when something is not operating properly, is that not correct?

A That, together with gathering samples.

The daily samples for testing.

Q Gather samples for testing. How long does that take?

A Possibly two hours a day. The morning and the afternoon.

Q Two hours to gather the samples? What does that gathering of the samples encompass?

A It encompasses, actually, preparing the samples for lab examination, and the two hours, he spends some time in the morning and again in the afternoon doing just that.

Q So he goes to the plant in the morning. He grabs a sample in a jar, and the sample is transported to an outside lab for analysis.

A Actually it is for analysis, that is correct.

Q So actually he does not do any real testing. He just grabs the water sample himself.

A He prepares the sample for transport, that is all. No, he does not do any lab actually analysis on site.

Q By preparing the sample for transport, what do you mean other than putting a cap on the bottle?

A Collecting them in the sample bottles and capping them.

Q All right. So he goes down and collects these samples twice a day for transport to the lab. The system -- the aerators are automatic, everything is automatic within the system, so -- how could this be a full time job?

A Actually, as I explained to you, he doesn't really spend eight hours at the plant. He is associated or affiliated with work in the vacuum stations, together with what he does at the plant. He also does the housekeeping and grounds maintenance at the plant, too. You can't just flip a switch and turn around and walk away and leave it, you know.

Q So he is a maintenance man.

A That is correct; he is a maintenance man and operator combined.

Q So instead of six maintenance men, you actually have seven, one of which is a part time operator.

A Well, that is true. You are right.

MR. LION: Thank you, Mr. Thorpe.

REDIRECT EXAMINATION

BY MR. RIELY:

Q Mr. Thorpe, you stated that the system was entirely built, and as I understand it, what has to be done when a new customer comes on the line --

A When a new customer applies for a connection, actually the vacuum main is tapped but a vacuum line to a storage tank or a holding tank, those are the large concrete tanks, that is then set and connected to the vacuum line. Then, there is a vacuum valve that is set in the line from the vacuum tank, or the holding tank, to the vacuum line. That is the air vac valve and/or the electronically controlled valve as in some cases they have in the older system.

There is a lateral line then connected from the tank to the house.

Q But it's not just simply running the service line from the house to the tank?

A Oh, no.

Q And that's what your studies show

costs fourteen hundred and fifty-seven dollars on the average in 1979?

A That's correct.

MR. RIELY: Fine. I have no further questions.

MR. LION: That brings up one more question.

HEARING EXAMINER: All right, Mr. Lion.

RECROSS EXAMINATION

BY MR. LION:

Q So this additional work is at least in theory fully covered by the connection fee which the lot owner pays to the utility?

A In theory, yes, sir.

Q And this amount is capitalized as part of the utility plant?

A That is correct.

Q And what the individual pays is logged as a contribution in aid of construction?

A That's right.

Q So they totally offset each other; is that correct?

A Hopefully they do. But they haven't. That is the intent.

MR. RIELY: It will offset each other if this increase is granted.

WITNESS THORPE: That is correct.

MR. RIELY: They do not at the present.

I have nothing else to say.

HEARING EXAMINER: Any other questions?

(No response)

Mr. Thorpe, let me make sure I understand this now. Assuming a vacant lot in the development, as I understand your testimony earlier you said that the storage tank and the air vac system and possibly the electronic system, whichever happens to be in place, is already there; is that right?

WITNESS THORPE: No, not in all cases. When a new connection comes on, it usually requires a tank. In some cases it may be the second connection to that tank and there would be an existing tank.

HEARING EXAMINER: That would be the case where there was a home next door?

WITNESS THORPE: That's correct, yes.

HEARING EXAMINER: But a vacant lot that is isolated from occupied lots would not have all this equipment in place?

WITNESS THORPE: No, it would not. It would require the tank, valve connection.

HEARING EXAMINER: I did have one other question. You said that probably there were about half a dozen of these systems in the United States in use.

WITNESS THORPE: Yes.

HEARING EXAMINER: You estimate --

WITNESS THORPE: Let me just qualify that a bit. There are vacuum systems other than the half a dozen I had reference to; actually there are about half a dozen systems like the one we are talking about. And this is the environed technology. There are some air vac systems, and one of them is under construction right now, and that's

a total air vac system utilizing the air vac valves that we presently utilize now, being built over at Kent Island.

HEARING EXAMINER: Was the reason for choosing this system here the hilly terrain and the difficulties with the gravity feed system?

WITNESS THORPE: I'm sure that was the idea of going to vacuum technology.

HEARING EXAMINER: Would there have been other options available if this particular system had not been chosen for a terrain of this nature?

WITNESS THORPE: The only other option would have been the conventional gravity system with the forced pumps, and I think a study had been done on the system to compare that capability or possibility and I think the number of seventy-six actual pumping stations would be required to convert that system to a gravity feed system as opposed to the thirteen vacuum stations we now use.

So really the vacuum system does make sense for this particular application.

HEARING EXAMINER: What would you say is the average sized lot in this development?

WITNESS THORPE: Probably the average size would be eighty feet by one hundred twenty, I guess. And that is purely a guess on my part.

HEARING EXAMINER: Any other questions? (No response)

Thank you, sir. You may stand down.

ROBERT L. FRASHER, a witness called by and on behalf of the Applicant, having first been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. RIELY:

Q Mr. Frasher, would you please state your name, business occupation and business address?

A I am Robert L. Frasher, Project Accountant with Brockmeier Consulting Engineers, Incorporated, in Santa Monica, California.

Q Mr. Frasher --

A If you will bear with me, I have a cold.

Q Please discuss your capacity in this proceeding.

A Our firm has been engaged by the Utility to assist in engineering and rate structure matters on a continuous basis. My testimony will present the Utility's accounting exhibits which are true to the best of my knowledge and belief.

10 Q Have you prepared a rate of return
11 statement for Lake of the Woods Utility Company?
12 A Yes. I have prepared a rate of
13 return statement for total company operations for
14 the calendar year 1979 that is Statement 1 of my
15 exhibit.
16 Additional statements present the
17 sewer operations by themselves in Statement 2, and
18 water operations, Statement 3, for the same period.
19 Q Please explain Statement 1.
20 A Statement 1 is the rate of return
21 statement for total Company operations for the year
22 ended December 31, 1979. It shows, in the first
23 column, that per books the Company had a net operating
24 income loss of one hundred thirty one thousand two
25 hundred sixty-one dollars during 1979. The second

column shows certain annualized adjustments, to which I will refer later, which increases the 1979 net operating loss to one hundred sixty-three thousand four hundred seventy dollars as shown in the third column.

In the fourth column, it will be seen that if the interim rate of twenty-four dollars per month were used to compute sewerage charges during the test period, revenues would be increased by one hundred forty-seven thousand six hundred and forty-eight dollars and expenses by eleven thousand six hundred and fourteen dollars, resulting in an increase in net operating income of one hundred and thirty-six thousand thirty-four dollars. With the twenty-four dollar a month interim rate, the Company would still suffer a net operating loss of twenty-seven thousand four hundred and thirty-six dollars, as shown in the fifth column.

The next to the last line in the fifth column shows the total Company rate base of two million four hundred nine thousand four hundred forty-five dollars and the last line shows that the twenty-four dollars per month rate yields a negative

return on rate base.

The sixth and seventh columns show that the effect of the proposed forty dollar per month rate for sewerage. The sixth column shows that this rate will result in a revenue increase of two hundred ninety-five thousand two hundred and ninety-six dollars. Operating revenue deductions will increase to sixteen thousand two twenty-eight, resulting in a net increase in operating income of two hundred seventy-nine thousand sixty-eight dollars. This would result in net operating income for the test year of one hundred fifteen thousand five hundred ninety-eight dollars which yields a nominal return on rate base of approximately four point eight percent.

Q Now, turning to Statement 1 for a minute, Mr. Frasher, the six hundred -- the two hundred ninety-five thousand two hundred ninety-six dollars operating revenues additional shown in Column 6 is the difference between the eight dollar rate and the forty dollar rate?

A That's correct.

Q To get the total of seven hundred

and eighty-one thousand dollars from three sixty-six shown in Column 7, you add together Column 3 plus Column 6 to get Column 7; isn't that correct?

A That's correct.

Q You don't add Column 5 plus Column 6?

A No. I hope to get a little more than seven eighty-one.

Q I just simply wanted to explain that.

All right, sir. Will you please discuss Statement 2?

A Statement 2 shows the Company's sewer operations and these figures were included in Statement 1 to determine the total Company rate of return.

The actual 1979 net operating loss incurred on sewer service, per the Utility's books, was two hundred five thousand six hundred ninety-eight dollars as shown in Column 1. Even with the interim rate of twenty-four dollars per month, the loss would be over ninety-nine thousand dollars.

At the forty dollar per month rate proposed in this proceeding, there would be a net

operating income of forty-three thousand nine hundred and ninety dollars, as shown in Column 7. This income, if actually achieved, would yield a slightly positive rate of return of about two point three six percent on the Utility's one point eight million dollar sewer plant rate base.

Q Please explain Statement 3.

A Statement 3 is similar to Statement 2, and it shows the Company's water operations which have been included in Statement 1 and is presented in exactly the same format as Statements 1 and 2.

The Company believes that present rates are sufficient to provide reasonable compensation for water services rendered and thus no increase in water rates has been proposed.

Q Now, discuss Statement 4.

A Statement 4 explains the Company's adjustments that appear in Columns 2, 4 and 6 on the rate of return Statements 1, 2 and 3. These adjustments are broken down between sewer operations and water operations.

Q Please take a moment and discuss the adjustments to the sewer operations.

A The first adjustment, totaling one thousand seven hundred and eighty-five dollars, in effect brings revenues for the test year up to the level that they would have been if the number of connected customers at the end of the year had been served throughout the year of 1979. Although we recognize that this is not an adjustment this Commission requires, we believe it is informative to the Commission at this time.

The next adjustments to sewer operations and maintenance expenses total twenty-nine thousand and sixty-two dollars. The increase in payroll cost is to annualize a general increase that was effective April 1st of '79.

The second operations and maintenance adjustment annualizes the corresponding increase in payroll related taxes, group insurance and other benefits effective in the test year. The last operations and maintenance adjustment is to annualize the effect of the general increase in Virginia Electric Cooperative's electric power rates that took effect on October 1, 1979, and also to utilize a more

current wholesale power adjustment charged by the Coop.

The more accurate reflection of purchased power cost which this adjustment presents is very important as power expenses represents about one-third of total sewer operations and maintenance expenses.

The adjustment in depreciation expense was made to show the level of annual depreciation expense based on year-end '79 plant balances. The last adjustment to expenses reflects the additional gross receipt taxes due on the revenue increase shown in the first adjustment. All of the foregoing adjustments are before any adjustments were made to reflect the increased sewer rates.

The next group of adjustments are those that would arise from the rate increase proposed in this case. The statement explains the adjustments related to the proposed increase of forty dollars per month in sewer rates.

The final section of Statement 4 shows similar Company adjustments made to water operations for the test year.

Q Please discuss your fifth Statement.

A Statement 5 is the Company's balance sheet as of December 31, 1979, consolidating both water and sewer operations.

Q Now, please discuss Statement 6.

A Statement 6 presents net utility plant and allowances both for the total company and as divided between its water and sewer operations.

The figures are taken from the balance sheet of December 31, 1979. The statement shows the derivation of the rate bases used in Statements 1, 2 and 3.

Q How are the Company's financial operations proceeding in 1980?

A The Company's financial position is continually reviewed, and operating statements for the eight months ended August 31, 1980, reconfirm the continuing trend of losses displayed in the 1979 test year. The results serve to reemphasize the need for the proposed sewer rate increase.

Q Do you have a statement that compares 1979's financial results with those projected for 1980?

A Yes. Statement No. 7 is a comparative operating statement that reflects in the first column actual results for the eight months ended August 31, 1980. The Statement further shows a projection of the full year's results based on two different levels of rates.

First, for revenue purposes we assumed that the twenty-four dollars per month interim sewer rate was in effect throughout 1980

and further used the August level of customers connected, which is eight hundred, for the entire year. For expenses, we used actual expenses through August and projected the remainder of the year to continue at the same level.

This calculation is shown in Column 2 of my Statement 7 and as you see would result in a net operating loss of thirty-two thousand, seven hundred and ninety-nine dollars for 1980. The third column was computed in the same manner as Column 2, except that revenues were projected using the proposed forty dollars per month sewer rate. Under that assumption, the Company would see net operating income of about one hundred and sixteen thousand dollars. The final column shows the actual results for 1979.

As can be seen from Statement 7, even with the help of the twenty-four dollar per month sewer rate and an increased number of connected customers, the Company could expect major losses in 1980. This is due largely, and most noticeably, to

the significant 1980 increases in the payroll costs and electric power.

These costs are expected to exceed the 1979 levels by approximately thirteen percent for labor and thirty percent for power. Although this comparision is somewhat simplified, it nonetheless demonstrates that the twenty-four dollar per month sewer rate is inadequate to offset the Company's operating losses. Even the proposed forty dollar rate, applied in the same way as the interim rate, would only allow minimum operating income -- and I have a correction in the prepared testimony -- the figure should read eighty-nine thousand, seven hundred and seventy-three dollars.

Q Now, is Statement 7 sewer and water combined, or sewer only?

A I believe this is sewer and water combined.

12 CROSS EXAMINATION

13 BY MR. LION

14 Q Turn the switch in front of you.

15 Mr. Frasher, you are employed by whom?

16 A Brockmeier Consulting Engineers.

17 Q Do you know -- have any information

18 regarding the terms whereby At Pac Land Company

19 purchased the stock of Lake of the Woods Utility

20 Company?

21 A Not in detail. Just that they did

22 purchase the stock.

23 Q Do you have any knowledge as to how

24 an affiliate of At Pac acquired the note which had

25

been previously held by Boise Cascade?

A To my knowledge, the note is not held by an affiliate.

Q Who is it held by?

A I believe it is Perry R. Bass, Incorporated.

Q Mr. Thorpe, I believe, testified that it was held by an affiliate. You say it is held by Perry R. Bass, who is not an affiliate.

A That is my understanding, yes.

Q Do you know for a fact that it is held by Perry Bass? You said you believe.

A I have seen a copy of the note. The note is actually payable to Boise Cascade. I believe on the note was assigned to pay Perry R. Bass, Inc.

Q Do you know what was paid for this note?

A No, I do not.

Q Was this done at the same time as the other transactions by which the stock of Lake of the Woods Utility Company was purchased by At Pac?

A I don't know it for a fact. I believe it was at or about that same period, but I don't know

that for a fact.

Q Is there any relationship at all between Perry Company and At Pac?

A Not to my knowledge.

Q But could there be? The relationship that you are not aware of?

A Speculation, possibly.

Q What is the relationship between Brockmeier Consulting Engineers and At Pac Land Company, and Lake of the Woods, and Maryland Marine Utilities?

A Brockmeier Consulting Engineers has as clients At Pac and Lake of the Woods Utility Company. Brockmeier Consulting Engineers is an individual corporation with many clients.

HEARING EXAMINER: Do your clients include Maryland Marine also?

WITNESS FRASHER: Yes, it does.

BY MR. LION (Continuing)

Q Mr. Thorpe has indicated that your firm is on retainer to Lake of the Woods Utility

Company. What is that retainer fee, please.

A The retainer fee is twelve hundred and fifty dollars a month.

Q And what services does your company provide for the utility company?

A Our company provides management consulting in the rates and the utility matters, design services, master planning. We work very closely with the utility on their capital budgeting and planning what the cost of certain facilities will be, when they will be required, and that is essentially the types of services.

Q I assume you are aware that expenses were booked as being owed to At Pac for management fees. How does that relate to what you do?

A That has no relationship.

Q It sounds as if your consultant firm, and consulting in these management areas, is actually doing the managing for the work which At Pac is claiming it does as part of these management fees.

A I don't believe that we are duplicating the work that they are doing. To my knowledge they

are administering employee benefit programs and things of this nature. Insurance plans as well as they obviously are also involved in the budgeting process. But I would think that would be from the standpoint of how it would be financed, whereas our input is essentially in determining what the cost would be, and perhaps determine when those facilities would be required.

Q Your Exhibit RLF-2, Statement 5, is the Company balance sheet for 1979. Would you turn to that, please? What is the liability which you have listed as Payables to Associated Companies, one hundred twenty-three thousand, three hundred and twenty-three dollars.

A I don't have the details exactly of what that includes. It may include some of the management fee that was accrued.

Q You know that they are associated companies.

A Yes.

Q Could you identify what companies?

A No, I can't. That information could be obtained from the Company's books.

Q All right, sir. You don't know at the present time what companies are involved, or what services were provided for this?

A No, I do not.

Q Who does the bookkeeping for Lake of the Woods?

A Mr. Ed Leach is the Controller for Lake of the Woods Utility Company. And he is the essential one that keeps the books.

Q And, as I understand it, he is shared with an affiliate, Maryland Marine Utilities, and his expense is allocated; is that correct?

A That is correct.

Q Who does the billing and payroll for Lake of the Woods?

A That is all done through Mr. Leach's office.

Q Could you tell me, then, what services are provided by Data Services, Inc.?

A I believe they are the computer service that actually prints the bills and provides the billing registers that are used in the office for collections and so forth.

Q So, this firm is employed by Mr. Leach?

A I would assume he was the one that oversees their activities.

Q Who prepares the financial statements for Lake of the Woods Utility Company?

A Mr. Leach.

Q Your firm does not prepare these?

A No.

Q Could you quantify the expense incurred by Lake of the Woods for Mr. Leach's services during --

A Well, I believe the allocation that is being made is twenty-five percent of his time is the allocation to Lake of the Woods.

Q Could you break that down to dollars?

A We can. I don't have that number at my fingertips.

Q And could you quantify the billing and payroll expenses or the -- which are done by Data Services, Inc.?

A Again, we can provide that; I don't have that specific number.

MR. LION: Thank you, Mr. Frasher. I have no other questions.

HEARING EXAMINER: Mr. Page?

MR. PAGE: Thank you.

CROSS EXAMINATION

BY MR. PAGE:

Q Mr. Frasher, let me back up on a couple of questions that Mr. Lion asked you concerning the two point four million dollar note.

Do you remember Mr. Thorpe's testimony to say that this note was payable to an affiliate of AtPac?

A I recall his making the statement.

Q Okay. You are saying now that the note is not payable to an affiliate of AtPac?

A That -- to my knowledge, it is not payable to an affiliate.

Q Okay. Who are we to believe? You or Mr. Thorpe?

A I don't know.

HEARING EXAMINER: One witness can't really characterize another's testimony. I think the conflict would be on the record for consideration.

MR. PAGE: Okay.

BY MR. PAGE: (Continuing)

Q And the note, you say, is held by Perry or --

A I believe it's a Perry R. Bass, Inc.

Q And you don't know of any relationship that any of the principals in that company have with AtPac?

A No, I don't.

Q Okay. Let's talk about this rate case expense. Do you have that itemized anywhere in your testimony?

A I believe it is shown that the estimated cost of the rate case would be twenty-eight thousand dollars.

Q Okay. And how are you accounting for this? Are you amortizing it?

A Amortizing on a four year period at seven thousand dollars per year.

Q How about the -- do you have that broken down at all anywhere, like what the twenty-eight thousand dollars would consist of?

A No, I don't have the breakdown. This was an estimate based on the time of our firm, the attorney's cost and any cost that would be

incurred by any of the other parties.

Q How about your time in this case?

A Our time, we believe, will approximate twenty-five thousand dollars.

Q How about attorney's fees?

A Right. I don't know.

Q So, twenty-five thousand dollars of the twenty-eight thousand dollar rate case expense is your organizational fees?

A Yes.

MR. RIELY: In case you are interested, I think that doesn't leave anough for me.

MR. PAGE: That's for you and the Company to work out, Mr. Riely.

MR. RIELY: I think the estimate is probably low.

BY MR. PAGE: (Continuing)

Q On Page 6 of your testimony, you discuss the sewer operations for the eight months of 1980. That reconfirms the continued trend of

losses. How about the water operations? How are they doing? How would you characterize that?

A I would say the trend on water would be as 1979 indicated, that water is doing -- still in a positive return.

Q Okay. And, let's look at Statement 7. Mr. Somerville discussed with Mr. Thorpe the power expenses. I see here you say that for the twelve months ended December 31, 1979 the Company spent one hundred eight thousand three hundred fifty-one dollars on power expenses and, then, the projected twelve months ended December 31, 1980 will be a hundred forty-one thousand four hundred twenty dollars?

A That's correct.

Q And that's about a thirty, thirty-one percent increase?

A Yes.

Q So you are saying that your Company has projected that power costs will increase by thirty-one percent?

A What I did was take the actual twelve months power bills for 1979 and repriced those same bills with the rates that were in effect from

the power company as of the end of 1979.

And I also took basically a three month average of the fuel cost adjustment charge based on January, February and March of 1980, and I took an average of what those three months for the fuel cost adjustment and the repricing of 1979 power is one hundred thirty-nine thousand seven hundred and eighty-eight dollars, which compares basically with the experience that is occurring right now.

Q And you based the fuel adjustment on the January, February, March 1980 figures?

A That's correct.

Q I understand that the Company buys power from Rappahannock Electric Cooperative?

A Yes. It was previously called Virginia Electric Coop. It has changed names.

Q And they in turn purchase their power from Virginia Electric and Power Company?

A I guess they do.

Q And you don't know what has been happening to the fuel costs of Virginia Electric and Power Company since March 1980, do you?

A No, I do not.

CROSS EXAMINATION

BY MR. SOMERVILLE:

Q Mr. Frasher, we were talking about Bass and AtPac. Are you familiar with Trans Continental Development?

A Yes.

Q What does that concern -- what is the relationship, if any, between that concern and AtPac?

A I'm not sure. Honestly.

Q Do you know that Bass is a partner in Trans Continental?

A I believe there is a Bass that is a partner in --

Q So, really, we've got Bass and Trans Continental and AtPac, and isn't it a fact that there is a relationship between these parties?

A I don't know.

Q You just don't know?

Of course, all this has to get back with the matter of the note and who holds it and what the relationship is there.

But you really just don't know?

A I don't.

Q Now, as I have listened to the testimony, what I hear is this: Lake of the Woods Utility Company requires the accounting management and engineering services of your concern and AtPac.

A We don't provide -- I'm speaking of Brockmeier now, what you would say accounting services in terms of keeping your books. It is more in an advisory or in matters concerning rates, or regulations. But we do not do the actual accounting for them.

Q Are you, then, saying that on an ongoing basis, on a day-to-day operation you really don't provide any services of that type?

A Of that type, no.

Q So you provide specialized accounting services?

A That's correct.

Q But you do provide those services and engineering services to the Company, and you say also that AtPac provides certain management services?

A That's correct. Well, yeah, I believe it's AtPac.

Q Now, let me direct your attention to the employee benefit program. Do you know whether or not there is one in effect?

A Yes, there is. I don't know the exact details of what it is. I mean, as far as what the actual benefit --

Q But you are prepared to say there is one in effect at this time?

A To my knowledge, yes.

MR. SOMERVILLE: I have no further questions.

HEARING EXAMINER: Redirect?

MR. RIELY: I have no redirect. That's our case, if Your Honor --

MR. LION: Could I, Mr. Farrar, ask a couple more questions?

HEARING EXAMINER: Well, let me ask a few questions of Mr. Frasher at this point, and let's see what else we need to inquire into.

HEARING EXAMINER: Mr. Thorpe said in his testimony that the Company had presented financial statements through you, on both a total company basis and the water and sewer separating basis. And I gather from what he said that perhaps he did not have strong objections as to which way it was considered, because he said the information was there to consider either way. What is your feeling about the desirability or appropriateness of separating the sewer operations -- isolating them and looking at them separately in this proceeding?

MR. RIELY: Mr. Examiner, please, I think that is a question of law, and not of fact. I think I ought to state the position of the Company on that.

HEARING EXAMINER: Very well.

MR.RIELY: This company has historically been regulated on the basis of separate services, and I believe that has been the position of the Commission in my experience

since my experience started to run, which is a few years back.

On the other hand, as far as this Company is concerned, to consider it on a combined basis doesn't really make much difference, but you always have to take into account the fact that although there are now only three customers, there may be in the future other customers who take one service and not the other, and I believe that it has been the practice of the Commission to cost separate services separately.

MR. LION: For the record, I might add it is my understanding in the future all new customers of this utility will take both water and sewer services.

MR. RIELY: You say that now, but that may not happen. There is no requirement that they will do it.

HEARING EXAMINER: Well, we will entertain closing arguments.

MR. RIELY: That is the sum total of

my argument.

HEARING EXAMINER: Do you know what fees are paid to Trans-Continental Development Company or At Pac for their services, such as administering the employee benefit program?

WITNESS FRASHER: I believe it was based upon five percent of their operating expenses. I believe that was the basic formula.

HEARING EXAMINER: Five percent of whose operating expenses?

WITNESS FRASHER: The utility Company's.

HEARING EXAMINER: As I understand it, there are three firms at least that provide consulting services on a more or less continuing basis, and that is your firm, and Trans-Continental, and/or At Pac, and Maryland Marine. Is that right?

WITNESS FRASHER: Yes.

HEARING EXAMINER: I hate to ask you to go through all that again, but I wonder

if you could just briefly distinguish each of those services , and in addition to that, explain what services are provided in addition by the people who are on site at Lake of the Woods.

WITNESS FRASHER: Well, I believe in the case of Maryland Marine that essentially the day-to-day work as far as the direct overview of administration, accounting, billing, and collection efforts are provided by that one staff, with the two girls in the local Lake of the Woods office, being kind of local, on-site, and handling the calls that come in for service or things of this nature. But the basic administration is handled through the Maryland Marine.

The services of Brockmeier Consulting Engineers is primarily in the areas of the engineering, of the more technical considerations, with also some work being done in the area of rates and regulations. But it

is primarily a planning a costing facilities and basically on the technical engineering side.

To my knowledge, the services that are being provided through At Pac or TDC is in the realm of financing directly, in determining the financial requirements of the utility, as to where that money is going to come from, administration of their employee benefit plans, administration of their insurance, which I believe is both the employer insurance as well as property insurance. Workmen's Compensation, tax considerations, payroll tax.

HEARING EXAMINER: All right. In regard to this note, I gather from your testimony, and the material filed by the staff accountants, that interest has not been paid on this note for some time, is that right?

WITNESS FRASHER: That is correct.

HEARING EXAMINER: Are you aware of

any collection efforts underway by the note holder, whoever that might be, to force payment of this interest?

WITNESS FRASHER: No, I am not.

HEARING EXAMINER: All right. Any further questions of this witness?

MR. LION: You indicated that your electricity estimate is based on January 1980 electric costs, is that right?

WITNESS FRASHER: Well, just the fuel adjustment portion. The basic rates, as far as service charges and charges per kilowatt hour, not counting the fuel adjustment, which is basically a separate charge, which has a tendency to change every month, the base rates I believe were October '79 was the last general rate increased that Rappahannock itself had. So those were the base rates that were used to reprice all of the actual power used in 1979.

The fuel adjustment, I used an average of the first three months of 1980.

MR. LION: Once you have this fuel adjustment charge, how is it applied to the Company's electricity usage in order to come out with a dollar charge?

WITNESS FRASHER: It is applied as a rate per -- I don't recall whether it is for a single kilowatt or for a hundred kilowatt hours. But it is based on the kilowatt hour usage.

MR. LION: Did you then determine how many kilowatt hours of power was consumed by the utility in 1979, and then apply these known changes in the rates and the fuel adjustment to the number of kilowatt hours consumed in '79?

WITNESS FRASHER: That is exactly the way I did it.

11 S. FRANK LEIS,

12 a witness introduced on behalf of the Commonwealth,

13 being first duly sworn, testified as follows:

14

15 DIRECT EXAMINATION

16 BY MR. LION

17 Q Will you state your name and position

18 you hold with the State Corporation Commission?

19 A My name is S. Frank Leis. I am the

20 Deputy Director of the Division of Accounting and

21 Finance for the Commission.

22

5 Q Did you prefile twelve pages of
6 testimony, with four statements, and one appendix
7 attached?
8 A That is correct.
9 Q Do you have any additions or corrections
10 to that testimony?
11 A I would like to make one correction.
12 On page 13 of my prefiled testimony, in the third
13 paragraph, I say the Company is now operating under
14 an interim rate increase of twenty-four dollars. I
15 would like to scratch out the word 'increase.' That
16 is an interim rate of twenty-four dollars per month
17 for residential and commercial, and then add the
word, 'sewerage' before 'usage'. Sewer usage.

Analysis of my Statement I shows the Company's proposed rates would produce a net operating income of a hundred and fifteen thousand, two hundred and fifty-eight dollars, and generate a five point eight-two percent rate of return on the Staff's adjusted rate base for sewer.

However, it should be emphasized that this amount of net operating income will be insufficient to cover the sewer department's share which is seventy-five percent of the Company's interest cost in the amount of one hundred forty-eight thousand nine hundred sixty-four dollars a year. In addition, when the sewer department's net operating income is related to total Company, as shown by Column 1 of my Statement 1, total Company operations will still show a loss approximating sixteen thousand no hundred and four dollars for the test year, with total Company interest charges amounting to one hundred ninety-eight thousand eight ten.

Now, although the Company has booked its interest charges each year, they have not paid them, and at the present time the books show five hundred eighty-three thousand four hundred seventy-seven dollars of accrued interest payable.

It would appear from the foregoing analysis that while the sewer department's financial position threatens the viability of the Company as a whole, the increase request, on the other hand, impacts on the rate payer in an equally detrimental manner. Consequently, it would seem that some middle ground would be appropriate at this time.

The Company is now operating under an interim rate increase of twenty-four dollars per month for residential and commercial usage. These rates granted under bond and subject to refund produce one hundred forty-seven thousand six hundred and forty-eight dollars of additional gross annual revenue, resulting in a net operating loss of twenty-six thousand nine hundred and sixty-seven dollars.

The only source of internally generated cash flow, in this instance, would come from the depreciation expense in the amount of sixty-five thousand seven hundred and nineteen dollars.

This concludes my summary.

Q Mr. Leis, in I believe it was 1976, Boise Cascade reacquired the Lake of the Woods Utility Company from Utilities, Inc.; is that correct, sir?

A That's correct.

Q At that time, an acquisition adjustment was placed on the books in the amount of, I believe, six hundred and thirty-nine thousand dollars; is that correct?

A Six hundred and thirty-nine thousand

three hundred and eighty-one.

Q Since that time, has this acquisition adjustment been placed, once again, into the Company's rate base?

A That's correct.

Q Has the Commission Staff changed its policy regarding acquisition adjustment since that time?

A Yes, we have. At the time this acquisition adjustment was made we allowed the Company to amortize the adjustment over a five year period and booked the credit to income below the line. And this was done in an effort to compensate the utility for the losses that they incurred during the transition at that time.

Since that time, however, in the last three rate cases, our policy has changed to amortization of the acquisition adjustment instead of some figure, such as we did in this case, of five years to over the remaining life of the property. It gives you a longer period of amortization and the booking being to credit income rather than below the line to extraordinary income to operating income.

Q And what is the purpose of this change?

A This change --

Q Or, is this change -- is the purpose of this change in procedure by which the Commission Staff handles acquisition adjustments? Is it done in order to -- in order that the owners of the utility will only gain a return -- earn a return on the actual investment?

A Well, that's correct. That's point one. But, also under the Uniform System of Accounts it specifies that we do it this way. We had deviated from that the last time because of some external considerations I mentioned that we figured were, at that time, in the interest of the consumer, the ratepayer.

But if were to do it accurately, as the Uniform System prescribed, the way I've outlined we've done in the last three rate cases, or more than three really -- last several rate cases -- is the way to do it.

Q Could you give me the numbers which would result when this acquisition adjustment is handled in a manner consistent with current

Commission policy?

A Well, you are asking for a tall order there. If we were to do that -- I had to go back -- I had one of my accountants go back and make changes and, of course, it just changes numbers all over my rate of return statement. That's almost impossible to understand.

So you have to -- anything that I give you right now would be subject to check by the Company and subject to our own review afterwards. But, so that you might get a feel for what this would do, if you look at my Statement 1, what we did here, we went all the way back to 1975 and just took everything off the books that we had and estimated that the useful life of the plant would be twenty-seven years, and this would mean an acquisition adjustment amortizing that out over the twenty-seven years of remaining life, would be twenty-three thousand six hundred and eighty-one dollars.

And what this would do to the last column would be to, instead of the Company showing a hundred and fifteen thousand two hundred and fifty-eight dollars net income there, since the

credit were to be amortized above the line, it would increase that to one hundred and thirty eight eight seven. Recognizing, of course, that there is no cash flow with these dollars that go up there.

The rate base -- the last number on the line would instead of being one million nine seven nine eight three five would be one million -- would be one million five four eight four eighty-eight.

Wait a second. No. Erase that number. It would be one million seven twenty-six five seven zero. And, of course, this would give you a rate of return of seven point five eight percent.

Q Regarding the Company's affiliate expenses, has the Company submitted an application for approval of affiliate expenses?

A Under the new arrangement, I have not seen it.

Q Has the Company provided the Commission Staff with adequate documentation with which the Staff could verify the actual costs to the affiliated companies that are providing these services to Lake of the Woods Utility?

A No. I would say no. We, in our

audit, took the Company's -- what the Company had booked for these services. We didn't have anything to, you know, really verify exactly in detail what they were doing.

Q So, your testimony today reflects only the expenses which the Utility Company booked?

A That's right.

Q As being owed to the affiliated companies?

A That's right. And, of course, they booked these expenses based on the affiliates agreement that was in effect between Utilities, Inc. and Boise Cascade.

Q And this affiliate agreement is, of course, void at this time?

A I would say so.

Q And there is no approved affiliate agreement?

A No.

Q Between the current parent and affiliates, Lake of the Woods?

A That's true. But we had nothing to go on, so we assumed this would give us a benchmark to depart from.

Q In your prefiled testimony, you indicated that these figures had been factored into the Staff's calculations for informational purposes and this is not to be construed to infer Staff's acceptance nor does Staff express any opinion as to the reasonableness of these amounts; is that still a true statement?

A That's true. Of course, we can't accept them and we can't express an opinion until such time as the Commission rules on it.

However, in order to have something in there we used the older figures, percentages, that were in the previous agreement.

Q And do you agree that the Company has presented no evidence in this hearing which would lead you to change your testimony?

A Well, that's correct. I wouldn't say that they haven't presented any evidence, but I would not change my testimony until such time as there is a ruling by the Commission on what these affiliate factors will be.

Q These affiliate expenses, then, have not been justified to the degree which would be required by the Commission's Staff in order to

approve them as being reasonable; is that correct, Mr. Leis?

A That's correct.

MR. LION: I move that Mr. Leis' statement be identified as exhibits and his prefiled testimony be read in the record as if presented at this hearing.

HEARING EXAMINER: Any objection? (No response)

Mr. Leis' testimony, therefore, will be copied into the record as if given orally. His exhibits will be admitted as a package as Exhibit SFL-3.

NOTE: At this point, the prefiled direct testimony of S. Frank Leis is copied into the record.

PREPARED TESTIMONY
OF
S. FRANK LEIS

LAKE OF THE WOODS UTILITY COMPANY
CASE NO. PUE800081

November 5, 1980

Q. Will you state your name and position you hold with the State Corporation Commission?

A. My name is S. Frank Leis. I am the Deputy Director of Accounting and Finance Division for the Commission.

Q. Would you briefly describe your professional experience and background?

A. A brief resume of my professional qualifications and background is contained in Appendix I to my testimony.

Q. Has the Accounting Division Staff made an examination of the books and records of Lake of the Woods Utility Company?

A. Yes, three Staff accountants spent approximately one week at the Company's office located in Locust Grove, Virginia. An additional period of time was then required to review the working papers and prepare Staff exhibits.

During the course of the audit several exhibits have been prepared. These will provide accounting information showing the net utility plant investment (Rate Base) after

Staff adjustments of $1,979,507, a net operating loss, after adjustments, for the test period of $170,667, and other supporting statements and schedules. In this audit I have made adjustments to the book figures for the purpose of developing as fairly and accurately as possible proforma earnings, expenses, and investment applicable to the Company's sewer operations and the amount of additional revenue the Company will derive from the latest proposed rates based on our examination.

This briefly summarizes my exhibits and testimony which I submit at this time.

(COUNSEL FILES REPORT)

BACKGROUND

During 1967 Lake of the Woods Water Company was issued a Certificate of Convenience and Necessity to construct and operate a water system at the Lake of the Woods development. This development, consisting of 4,200 lots, surrounds a recreational lake and includes a clubhouse, golf course, swimming pool and other recreational facilities. At that time, the Company was owned by the Virginia Wildlife Clubs, Inc. (a U. S. Land subsidiary). Thereafter, Boise Cascade Recreational Communities, Inc. (a Boise Cascade Home & Land Corporation subsidiary) purchased all of the outstanding stock of U. S. Land, thereby acquiring Virginia Wildlife Clubs Inc., and Lake of the Woods Water Company.

In 1968 Lake of the Woods Water Company changed its name to Lake of the Woods Service Company. Later, during 1969 the Company was granted a Certificate of Convenience and Necessity to construct and operate a sewer system.

Following its entry into sewer service, all of the Company's outstanding stock and notes were purchased in 1969 by Utilities, Inc. from the Virginia Wildlife Clubs, Inc. During the interim between 1969 and 1975 Utilities Inc., a Chicago based corporation, operated the Lake of the Woods Service Company providing water and sewer service to the expanding Lake of the Woods development. While water service was satsifactory during this period, the Company did experience considerable difficulty with the maintenance of its sewer system. The sewer collection system, in use by the Company, was an experimental vacuum type system wherein considerable operational difficulties were experienced. However, there was no difficulty in the operation of the treatment facilities used in the complete sewer service system.

The operational difficulties encountered by Utilities Inc. with the vacuum operated sewage collection system subsequently developed into legal action by Utilities Inc. against Boise Cascade. The ensuing out of court action resulted in the purchase, in 1975, of Lake of the Woods Service Company by Boise Cascade and subsequent transfer of these utility facilities to Boise's wholly owned subsidiary, Lake of the Woods Utility Company. Also on

September 15, 1975 Lake of the Woods Utility Company was issued a Certificate of Convenience and Necessity to operate the utility company at the Lake of the Woods development.

Boise Cascade Home & Land Corporation costs as partial consideration in its settlement with Utilities Inc. amounted to payment of $925,000. In addition, as a part of this settlement Boise:

(1) Forfeited the right to receive payments from Utilities Inc., based on future connections to the Lake of the Woods sewage system;

(2) Assumed a contingent liability for claims filed (up to a certain amount) against Utilities Inc.;

(3) Assumed legal, accounting, and expert witness fees in connection with the transfer: and

(4) Assumed costs to be incurred necessary to remedy the defects attributable to deferred maintenance of the sewer system.

Boise Cascade Home & Land Corporation subsequently transferred the assets of Lake of the Woods Service Company to its subsidiary Lake of the Woods Utility Company. In return for these assets, the parent (Boise) received from its subsidiary 8% interest on its long-term debt plus all the issued shares of stock of the utility company. These items were the subject of an affiliates transaction subsequently approved (Case No. A-592 9/29/77) by the State Corporation Commission and interest on debt while not paid was booked by the Company.

During April of 1979 all of Lake of the Woods Utility Company stock was sold by Boise Cascade Home and Land Corporation to AtPac Land Company, the Utility's present owner, for $900,000. In addition, there is an affiliates agreement being prepared by the Company to cover such matters as salaries and wages for employees and management fees for services rendered by AtPac Land Company and/or its subsidiaries.

HISTORY OF THE CASE

In the Company's last rate proceeding (Case No. 19867) the Commission authorized an increase in rates designed to produce approximately $111,963 of additional gross annual revenue. These new rates became effective on or after September 1, 1977.

On June 17, 1980 the Company filed an application with the Commission for a temporary emergency increase of $16.00 in rates, from $8.00 to $24.00 per month, for sewerage service to residential and commercial customers. This proposed rate was designed to increase the Utility's gross annual revenue by $147,648.

On July 17, 1980 the Commission granted the Company's request for the $16.00 interim increase in monthly rates to be effective for sewerage service rendered on or after August 1, 1980. The revenues are to be collected by the Company on an interim basis, accounted for separately on the Company's books, and are subject to refund until the Commis-

sion's decision is rendered following a full investigation and a public hearing set for November 5, 1980.

SCOPE OF REVIEW

In its application the Company filed rates and charges sufficient to produce $295,296 of additional gross annual revenue based on increasing its sewer rates only. The Company is not filing for a change in their water rates or the water and sewer service availability fee. The rates that will be in effect if the increase is granted are as follows:

Water Rate:

	Gallons Per Month	Gallons Per Quarter	Rate Per 1,000 Gallons
For the first	12,000	36,000	$.50
For all over	12,000	36,000	$.45

Sewerage Rates:

The monthly sewerage service charge shall be 90% of the charge for water for commercial customers and $40.00 per month for residential customers.

Minimum Charges:

No bill will be rendered for less than the minimum charge of $4.00 per month for water and $40.00 per month for sewerage for each separate living unit on the premises served.

Availability:

	Per Month
Water Service Availability Fee	$4.00
Sewer Service Availability Fee	$3.75

Revenue projections from the foregoing charges were computed using a customer base of 4,292 customers for the test period. Of this amount 769 customers are on line and using the service. The remaining 3,523 are availability customers only.

In light of these new rates, a Commission Staff audit was conducted to review Company projections and in so doing it was necessary to:

(1) Review the Company's operations for the 12 month test period (January 1, 1979 through December 31, 1979);

(2) Prepare the Company's Rate of Return for the test period and determine if the rate is adequate to service capital.

The scope of the audit included an review of revenues, expenses, net income, number of customers, a detailed analysis of specific expense accounts and utility plant in service. As a result of this review, several exhibits have been prepared and are assembled in report form as follows:

Statement I. Rate of Return Statement based on operating results for the twelve (12) month test period ended December 31, 1979 and Net Utility Plant at December 31, 1979.

Schedule A to Statement I. Explanation of adjustments appearing in Column (4) of Statement I.

Schedule B to Statement I. Explanation of adjustments appearing in Column (6) of Statement I.

Statement II. Revenue projections based on proposed rates for Sewer Department.

Statement III. Income Statement-per books for the twelve (12) months ended December 31, 1979.

Statement IV. Balance Sheet-per book at December 31, 1979.

STAFF EXHIBIT

STATEMENT I

This is a Rate of Return Statement based on the operating results for the test period ended December 31, 1979. It measures the Company's sewer department performance against a "year end" rate base. The first column reflects the Company's per-books figures on a total company basis. It shows operating revenues of $484,207: Operation and Maintenance Expenses, Depreciation and Taxes of $615,469. Deducting this total from total operating revenues leaves a balance, shown here as a net loss of $131,262. This when related to the rate base of $2,410,895 does not generate a positive rate of return.

Columns (2) and (3) show the operating results of the water and sewer departments of the Company individually, with only the water department showing an operating profit of $74,437 and a 13.72% rate of return. Operating results by department are shown per books, hence the allocation of expenses, in most cases, was not necessary. The Company books plant, revenues, and most expenses by department. For those administrative and general expenses not booked by department the Staff made an allocation on a 50/50 basis.

Column (4) shows the effect of those Staff adjustments made to revenues, expenses, depreciation, taxes, and rate base in order to restate book costs to amounts applicable to the test period. The sum total of these adjustments is a decrease in the net operating loss of the sewer department for the test year and a slight increase to the rate base. The net effect of these adjustments, as shown by Column (5), amounts to a net operating loss of $170,667. All of these adjustments are explained in detail by Schedule A to Statement I.

Column (6) is a summary of the effect that the Company's rates would have on revenues after Staff accounting adjustments. These adjustments are discussed in detail by Schedule B to Statement I.

Column (7) shows the results after the inclusion of these adjustments which generates a net operating income of $115,258 and a 5.82% rate of return on rate base.

THE RATE BASE

The Rate Base is composed of the Company's plant and facilities used and useful in the rendition of its utility service to the public. The principal elements which must by considered in computing the rate base are: Gross Plant, Depreciation Reserve and Allowances for Working Capital. The original cost method of valuation of property was used as it most fairly states the actual investment made by the investor in the Company's plant and the value which rate-

payers, present and future, will be required to return in the form of depreciation expense.

ADJUSTMENTS

A total of twenty (20) adjustments were made to revenues, expenses and rate base. One (1) adjustment was made to operating revenues which had the effect of increasing book revenue. Fifteen (15) adjustments were made to operating expenses, depreciation and taxes which had the net effect of decreasing these expenses and reducing net loss; while four (4) adjustments were made to rate base. These adjustments are explained in detail by Schedule A to Statement I. However, some of the more significant operating expense adjustments thereto need additional amplification.

The Company has booked certain salaries & wages, associated benefits, management fees and adjustments thereto, based on a previous letter of understanding between itself and the former parent (Boise Cascade) which was approved by the State Corporation Commission, Case No. A-592 September 29, 1977.

At the present time this agreement is no longer valid. A new agreement must be negotiated between the Company and its new parent, AtPac Land Co. This agreement must in turn be approved by the State Corporation Commission under Chapter four of Title 56 of the Virginia Code. These

expenses in the aggregate after proforma staff adjustments for the Company's sewer operations are as follows:

1.	Management Fees	$10,762
2.	Salaries, Wages & Benefits	15,298
		$26,060

Although the foregoing expenses have been factored into the Staff calculations, for informational purposes, this should not be construed to infer Staff acceptance, nor does the Staff express any opinion as to the reasonableness of these amounts at this time. Accordingly, the Company must bear the burden of proving the reasonableness of these affiliate expenses.

Staff adjustment number (4) annualizes a power increase by the Rappahannock Electric Cooperative (formerly Virginia Electric Cooperative) effective October 1, 1979. The possibility of future rate reductions was explored with the Cooperative. The Cooperative's Management Engineering Planning staff indicated that future rate revisions were in planning, and that those rate schedules under which the utility operates would probably show future increases of 1 to 1.3 percent under the "B-1" Schedule, and 4 to 5 percent for the "LS" and "A-1" Schedules.

Staff adjustments No. 13 and 18 remove depreciation taken by the Company on contributed property, and calculate the expense at a 3% composite rate. The net effect of these adjustments reduces depreciation expense by $32,100 for the test year, and increases utility plant by $101,982.

Adjustment No. 10 calculates uncollectible accounts expense at 1% of gross annual revenue. The 1% limitation is current Staff policy, and is in keeping with experience with other utilities. The net effect of this adjustment reduces this expense by $21,403.

SUMMARY AND CONCLUSION

Lake of the Woods Utility Company is requesting approval of their proposed rates and charges for sewer service only. These rates, if approved, will approximate a 400% increase in the residential and commercial usage rate and produce an overall gross annual revenue increase of 116% or $295,296.

The Company contends that approval of the proposed rates is necessary in order to reverse the trend in operating losses and "maintain its financial viability and its ability to serve." However, one of the major considerations in determining the rate of return to be achieved by the proposed rates, concerns those charges to operation and maintenance expense subject to approval under the Public Utilities Securities and Affiliates Act.

Analysis of Statement I shows the Company's proposed rates would produce a net operating income of $115,258, and generate a 5.82% rate of return on the Staff's adjusted rate base. However, it should be emphasized that this amount of net operating income will be insufficient to cover the sewer department's share (75%) of the Company's interest

cost in the amount of $148,964. In addition, when the sewer department's net operating income is related to the total company, as shown by Column (1) of Statement I, Total Company operations will still show a loss approximating $16,004 for the test year, with total company interest charges amounting to $198,810. Although, the Company has booked its interest charges each year, they have not paid them, and at the present time, the books show $583,477 of accrued interest payable.

It would appear from the foregoing analysis, that while the sewer department's financial position threatens the viability of the Company as a whole, the increase requested, on the other hand, impacts on the rate payer in an equally detrimental manner. Consequently, it would seem that some middle ground would be appropriate at this time.

The Company is now operating under an interim rate increase of $24.00 per month for residential and commercial usage. These rates granted under bond and subject to refund, produce $147,648 of additional gross annual revenue, resulting in a net operating loss of $26,967. The only source of internally generated cash flow, in this instance, would come from the Depreciation Expense in the amount of $65,719.

Q. Does this conclude your testimony?

A. Yes, it does.

NOTE: Thus concludes the prefiled direct testimony of S. Frank Leis.

* * * * * * * * * *

CROSS EXAMINATION

BY MR. RIELY:

Q Colonel, I'm confused. When Boise reacquired this corporation, the stock and assets of this corporation, this acquisition adjustment was established; isn't that right?

A That's correct.

Q And you had a rate case here in 1977?

A Yes, that's correct.

Q And at that time the Commission accepted the amortization on the five year period?

A That's correct.

Q And the whole acquisition adjustment was completely amortized as of December of this year; isn't that correct?

A That's correct.

Q So, if you go back and do what you suggest, we would have to amortize it twice; isn't that right?

A You would go back and -- all I did was go back as if it had never been done, as if that had not been --

Q But it has been done and amortized?

A That's true. And I don't fault you on that; that's a fact; that's a legal matter, and it's completely out of my hands.

Q But if we start on the twenty-seventh year we would be amortizing it twice, wouldn't we?

A No. If you were to do what I just did, you would go back and correct your books and start out with zero and start out all over again and, then, you would be amortizing only once.

But you would be amortizing it on twenty-seven years instead of five.

Q But what the Company has done up until today is what the Commission had previously approved; isn't that correct?

A You are absolutely right.

Q Thank you, sir.

This Company gets revenues in two sources, two ways, does it not? It gets a charge for services rendered and a charge for availability; isn't that correct?

A That's correct.

Q Approximately how much of its revenues are derived from availability charges?

Do you know?

A Well, if you go over to Statement 2, we have a statement there that shows what comes from availability charges. For example, you can see by using availability, three thousand five hundred and twenty-three, three dollars and seventy-five a month, it's forty-five dollars a year, that comes out for that number of customers to a hundred fifty-eight thousand five thirty-five.

Q So, roughly sixty percent of its revenues under the old rates was for availability charges?

A Right.

Q And those are charged to customers who are not there physically; isn't that correct?

A That's correct.

Q And would you think, as a practical businessman, as well as an accountant, that it's harder to collect money from people who are not there than from people who are there?

A I would say so.

Q And, then, I get confused by the

top of Page 12 of your testimony which you say Adjustment Number 10 calculates uncollectible accounts, expenses, at one percent of gross annual revenues.

The one percent is current Staff policy and is in keeping with experience with other utilities.

What other utilities? What other utilities such as this one that have availability charges?

A What adjustment number is that?

Q Adjustment Number 10. But I'm looking at your language at the top of Page 12.

A All right. We looked at Virginia American Water Company.

Q Does that have an availability charge?

A It doesn't have an availability charge, but it has uncollectible accounts expense.

Q Yes. But maybe you and I misunderstand each other. I'm talking about a company that tries to collect a lot of money from people it doesn't give service to.

Have you got any examples of those?

A I've got an example of one of the last rate cases we did that I would have availability charge and we did the same thing. This particular individual wanted forty percent in the way of bad debts; we knocked them down to one percent.

The fact of what you are asking me, without -- if I did any checking, a bad debt is a bad debt; it's an uncollectible account. Granted, it's hard. But I don't know what -- and I think this was brought out -- has your Company done in order to try to collect these bad debts beyond just notifying them. But you asked me about checking in the case of Virginia American Water Company.

Q Is that really relevant to the circumstances here?

A Well, you asked me and I would like to give you the figures anyhow.

The figure is three-tenths of a percent in the Alexandria District; a half or six-tenths of a percent on Prince William; point three on Hopewell. If you go to big utilities, of course, it's another decimal point lower than that. There just isn't anything --

Q But, does Virginia American Water

Company try to collect any money from any customer to whom it doesn't render any service?

A No, it does not.

Q When you say that this one percent limitation is in keeping with experience with other utilities, are you talking about other utilities that have availability charges, or other utilities who only have charges to render service?

A I am talking about both. Those utilities that have your problem have experienced -- as experience shows -- have a -- have higher bad debts, but we have limited them to one percent.

Q You do that arbitrarily?

A Yes, we do it arbitrarily.

Q Without any reflection whatsoever as to actual experience.

A Without any whatsoever.

Q Would you recommend that the Company sue a customer for an account that was thirty dollars?

A I think what we have to do is keep an open mind on the subject, and let the Commission decide after we have heard the evidence. After we have heard my presentation and your arguments, what might be a fair percentage.

Q Is that an answer to my question?

I asked whether you would recommend to a utility that it sue a customer for a thirty dollar bill?

A No, I wouldn't sue them for thirty dollars, but over a period of years, if that individual stays delinquent, which I am sure he probably has, I am sure some of your delinquent accounts have been up there since time began, since you opened up. It gets into hundreds of dollars, and I think maybe you should take some action, sue them or whatever.

Q Now, would you turn to Schedule B to your Statement I? To your Adjustment 3. Is it not true that your adjustment for gross receipt taxes should be increased because of the fact that the first step rate has already been applied to other revenues, and that the two point six percent should be applied to the entire increase?

A Yes, you are absolutely correct. We took the increase of two hundred and ninety-five thousand dollars, two hundred ninety-six, and we took the first hundred thousand of that and applied the lower rate of one point one two five percent, and that was incorrect, because that had already been

1 done on the revenues you have on the books. Had
2 that adjustment been made correctly, we would have
3 increased that expense, that gross receipt expense,
4 from six thousand, four hundred and eighteen dollars
5 to seven thousand, eight hundred and ninety-two
6 dollars. It would be an increase of one thousand,
7 four hundred and seventy-five dollars.
8 MR. RIELY: Thank you, Colonel. I
9 have no further questions.
10

13 CROSS EXAMINATION

14 BY MR. SOMERVILLE

15 Q Mr. Leis, going back to your testimony

16 on page 3, where you make refererence to interest

17 on the books of five hundred and eighty-three, four

18 seventy-seven.

19 A Page 3 of my prefiled.

20 Q Page 13, page 13.

21

22

23

24

25

A All right.

Q First paragraph, you make reference to accrued interest payable.

A That's correct.

Q Did your examination reveal to whom that was payable?

A Well, originally the payable was -- when started, was payable to Boise Cascade and, then, when the new company bought it they bought the stock and, of course, they assumed the liabilities that have been accruing all this time. And I would presume now that the new owner, or rather the new parent, would be the beneficiary of that, that debt.

Q But you are not certain of who the holder might be?

A Well, I haven't seen a document that says.

Q And it was nothing in your examination?

A These things have just been accrued on the books. It was an open account advances originally.

Q Let me ask you to look at your Schedule A to Statement 1 at the bottom of the page,

and I'm coming back to your decrease for uncollectible sewer accounts of twenty-one four 0 three.

In your examination and analysis, you are dealing just with the sewer side, are you not?

A Just the sewer side.

Q And if you followed through on this, it would be a comparable decrease on the water side?

A Had we done total Company there would have been a comparable --

Q You don't have that figure for the water?

A (Witness nodded in the negative)

Q Now, let me ask you to look with me at your Statement 1, your rate of return statement, and as I understand it, Column 1 is the total Company, Column 2 is water, and Column 3 is the sewer. And Column 4 would be Staff adjustments with reference to sewer?

A To sewer only, that's correct.

Q And, the next column is sewer only?

A Sewer only.

Q All the way through?

A All the way through.

Q The only column relating to water would be the first column and the second column?

A That's correct.

Q However, is it not correct that in Column 4 on depreciation, that your deduction of thirty-two thousand one hundred is a depreciation with regard to water and sewer?

A No. That is just for sewer.

Q How much --

A Had --

Q How much water?

A Had we done this on a total Company basis, it would have been a reduction in the depreciation and amortization of the water department. I don't know what the figure would be because I did not do it.

Q So, you are saying that that is just sewer and it does not --

A That is correct.

Q If you added the water in, it would be a further reduction?

A Yes.

Q It would increase -- which would increase the profit on the water side?

A That's correct.

Q Now, also down below the line under utility plant with your accumulated provision for depreciation, you have in Column 4, one 0 one nine eight two, and again that's just sewer?

A Just sewer.

Q And we would have the same principle with regard to the water?

A It has a tendency to increase the rate base.

Q Now, in your analysis and examination of the Company, were you able to look behind the Company's figures with regards to allocations of expenses to capital and maintenance?

A Yes. We made an adjustment for that. We examined all the work orders during the test period of two hundred dollars or more, and we went through them and picked out those items which we figured probably should have been capitalized, capital items, and they consisted mainly of these barrel assemblies and deducted those out.

Q So you did analyze the work orders?

A Yes, we did.

MR. SOMERVILLE: I have no further questions.

HEARING EXAMINER: Any redirect?

MR. LION: No, sir.

HEARING EXAMINER: Mr. Leis, let me ask you a couple of questions.

SPECTATOR: Louder, please.

HEARING EXAMINER: All right.

Just one minor item in your expenses. I see you had placed in Adjustment Number 13, Statement 1, increase in depreciation expense to a uniform composite rate on end-of-year plant balances.

I'm aware of the fact that the Commission in a recent decision, which I'm sure you are familiar with, a decision in the case of VEPCO, that was the last FOR, financial operating review case, denied a similar adjustment for increase in depreciation expense to end-of-year plant.

Do you see some reason for treating

this adjustment differently in this case?

WITNESS LEIS: In this particular case, we did not increase; we decreased the depreciation expense. The purpose of this adjustment was not to make a depreciation expense adjustment in the same sense that you are talking about where you take the year-end balance and they have X number of dollars booked, because it's on an average base throughout the year and we take the year-end balance and we up it and we increase it. That's what was disapproved in this particular case you are talking about.

In this case here, what we did, was non, or contributed property, and based our depreciation on contributed property. That was the philosophy and rationale behind this adjustment which is, you might say, diametrically opposed philosophically to the one you mentioned.

HEARING EXAMINER: So the adjustment here was designed to allow depreciation?

WITNESS LEIS: On non-contributed property because the Company had taken depreciation on contributed property. And that was to get that out.

HEARING EXAMINER: All right. I guess my question, then, is what level of plant balances was used for non-contributed property?

WITNESS LEIS: We used the year-end balance.

HEARING EXAMINER: Do you disagree that that was the type of adjustment that was disallowed in the VEPCO case, or is there some difference?

WITNESS LEIS: Well, I guess there is two parts. Number one, we took out the contributed property but we left in the contributed property and that part that covers rather the non-contributed property is in there and the depreciation is calculated on the year-end balance.

So, I guess you might say half of that -- part of the adjustment could be in error, or could be contrary to the

decision of VEPCO FOR. However, another way to look at it, too, Mr. Farrar, is that this is a rate case and that was a financial operating review case. We are not as liberal, of course, in our financial operating review as we would be in this rate case.

We are moving the test year forward just a little bit and allowing some degree, additional degree, to the pro forma estimate. And I would think that that is appropriate in a rate case.

HEARING EXAMINER: All right. Your Adjustment Number 5, you have amortized the Company's rate case expense. Was that based on figures supplied by the Company?

WITNESS LEIS: That was based on the Company's estimate of twenty-eight thousand dollars. I might add that's purely an estimate, but as of 8/31/80 they had booked nineteen thousand six hundred forty dollars for rate case expense. I would assume that

before this case is concluded that the expense will -- the remainder, it will equal twenty-eight thousand dollars.

HEARING EXAMINER: Mr. Leis, in your Report you say that the Company has quite a bit of accrued interest payable. This is on page 13.

WITNESS LEIS: That is correct.

HEARING EXAMINER: Are you aware of any efforts by anyone to collect this interest, or to force payment of it?

WITNESS LEIS : No.

HEARING EXAMINER: But you are not sure who the present holder of the note is?

WITNESS LEIS: Well, it would be the parent of Lake of the Woods.

HEARING EXAMINER: So to the best of your information, At Pac is the holder of the note?

WITNESS LEIS: Yes. At Pac would be the one they would have to pay it to.

Testimony of E. Jackson Tice

11 DIRECT EXAMINATION

12 BY MR. LION

13 Q Please state your name and position

14 with the Commission?

15 A I am E. Jackson Tice. I am an

16 engineer in the Division of Energy Regulation.

17 Q Have you recently visited the

18 Company?

19 A I visited the Company on October 9,

20 1980.

21 Q Did you prefile four pages of

22 testimony?

23 A I did.

24

25

Q Do you have any additions or corrections to that testimony?

A I have corrections to make, which I was discussing the number of employees employed by the Company. Mr. Thorpe shows sixteen point one, and I was handed a sheet of paper at the office showing nineteen point six employees, with the notiation that I had made that two employees were the same people, so I subtracted that and came up with eighteen point six. And I have now been informed today that this paper that he showed me was a projection of what they wanted in the budget, and they never did get it, so I guess we will have to ride with the sixteen point one as the number of total employees of the Company.

And where I indicated that this Company has one employee for every forty-two customers, based on this it would be one employee to every fifty customers.

That would be the only corrections that I would want to make.

Q So, in fact, you do not have available, prior to today, actual breakdown of the Company

employees, is that correct?

A That is right.

Q Would you please summarize your testimony?.

A Although this case is only involving the rate increase for the sewer company, we are concerned with the physical part of the whole company, and I did make a comment that the Company has eight wells with the three hundred thousand gallon storage tank. They have already drilled two wells, which they haven't put into service, and they have plans to add another three hundred thousand gallons storage capacity tank, which I should think would handle the water needs well into the future, when these are put on line.

We have already heard that the sewer system is very unique, very few in the United States. This vacuum-type system probably is very complicated, but probably the best system for this type of terrain. It is very highly energy concious, and it has a great number of demand for maintenance personnel.

I made a comparison along with two companies, and I would have to admit these companies are gravity flow-type of companies, and one with about nine thousand customers had a one point one employee for every four hundred customers, and another one about the size of Lake of the Woods, seven hundred customers, at a ratio of one to two hundred and forty customers; I believe, two hundred and fifty customers.

I would like to comment on two items which weren't discussed by the Company in March, but I have no objection to it. The sewer connection fee which is proposed to be increased from seven hundred and eighty-five dollars to a thousand fifty, and the sewer installation fee from two eighty-five to four hundred. This is a total of proposed rate of fourteen hundred and fifty dollars. I have said that I really don't see any need for the two different fees being in the tariff, but be that as it may, each of these figures are applied at the same time when the connection is made. So

1 essentially I would consider fourteen hundred and
2 fifty dollars connection charge.
3 I pointed out that this Commission
4 -- this connection charge is a little different from
5 the standard company. It has a sewer line running
6 down the street, and about all the sewer company
7 does is run a lateral line from the main in the
8 street to the property line of the property owner.
9 In this case, the lines run from
10 the vacuum line to the holding tank; from the
11 holding tank to the foundation of the house, and
12 at least seven hundred and forty dollars is required
13 just for the discharge mechanism that they have to
14 install either separately or in conjunction with
15 other people.
16 This concludes my testimony.
17 MR. LION: I move that Mr. Tice's
18 prefiled testimony be read into the record
19 as if presented at this hearing.
20 HEARING EXAMINER: That will be
21 done.
22 (Prefiled testimony follows)
23
24
25

TESTIMONY OF
E. JACKSON TICE
LAKE OF THE WOODS UTILITY COMPANY
CASE NO. PUE 800081

Q. Please state your name and position with the Commission.

A. I am E. Jackson Tice and I am an engineer in the Division of Energy Regulation.

Q. Have you recently visited this utility?

A. Yes. I visited the utility on October 9, 1980.

Q. Please give your report.

A. In this case the company is requesting a substantial increase in rates for sewerage service and intends to retain the present rates for water service. Although the water system is not directly involved in this case, I would like to comment on a couple of water related items. Since water was made available some 58 wells have been drilled. Most of these were abandoned due to low yields. The company is now using eight wells. They have two additional wells already drilled which they intend to place in service which have a yield of 186 GPM. They also intend to add another 300,000 gallon steel storage tank. With these two additions, the water system should be able to take care of the area's needs well into the future.

The sewer system is now and has been in the past a complicated and an expensive operation. The vacuum type system is one of the few being used in the United States. At the time it was installed it was believed to be better suited for the undulating terrain found at Lake of the Woods. Experience has probably proved it effective in principle but one requiring daily maintenance and high electrical usage. Also since prior experience was limited with this type of system this company and the prior operators have made numerous

changes to improve the operation.

The major problem with the system has not been in the vacuum lines or pumps but in the 750 gallon storage tanks and their companion discharge mechanisms which are shared by several customers.

A number of changes have been made in the containers for the discharge mechanisms as well as with the mechanism itself. These changes have been expensive.

Within the past year the company has been installing at the storage tanks more durable containers and Air Vac pneumatic discharge mechanisms. Whenever an old tank and its electricially operated discharge mechanism is replaced by the Air Vac the electric service is discontinued to that unit. The container and the preumatic discharge unit cost about $700. Since there are 300 to 400 old units in place the conversions will take place as funds are available.

The elimination of the need for electric power at these discharge units will effect some savings in power cost but since these are not as energy-intensive as the vacuum pumps only the minimum charge for service will be eliminated. However, this is a step in the right direction to reduce the power cost. This should considerably reduce the more than 80 individual services and bills the company receives from the electric company at the present time.

The system has 13 vacuum pump stations and these are not only power intensive but require at least twice a day maintenance by the labor force. It has been found necessary to increase the size of certain vacuum lines. Two lines have been replaced using a sawtooth method which assists in re-creating

the vacuum along the lines. As funds become available other stations will have their pipelines replaced with larger lines laid in the sawtooth method.

Mr. Thorp reports that there is a labor force of approximately 16 men and women, however, according to information furnished me at the office of the company, the total present payroll is 18.60 people or as they refer to it as "Work Years". Administration which includes 40% of the time of a General Manager, Operations Manager, Controller, Data Controller, full time Accounting Clerk and Secretary accounts for 3.60 "Work Years". The Water operation is charged for 1.50 "Work Years" and the sewer operation for 13.50 "Work Years". The sewer operations includes a break down of approximately 6 people listed under the heading "Construction". They are involved in manufacturing the concrete storage tanks and the installation of these and the discharge tanks. The remainder are listed as "Maintenance" personnel including the operations of the Waste Water Treatment Plant.

The personnel of the utility breaks down to a ratio of approximately one employee for every 42 customers. Although I am aware that this sewer opeation is quite different there does appear to be an excessive number of employees. A sewer company under our jurisdiction has a ratio of approximately 1 to 400 and a smaller company with about the same number of customers as Lake of the Woods has a 1 to 250 employee-customer ratio.

The 13.50 "Work Years" charged to the maintenance of the sewer system is the questionable area of the labor expenses. This includes approximately 6 people listed under "construction". From what I observed the construction of concrete storage tanks is not a daily operation and there does not appear to be that many new tanks being placed in the ground to require so many employees.

I feel the company should provide a detailed accounting of the work force at this hearing.

CROSS EXAMINATION

BY MR. SOMERVILLE

Q Mr. Tice, have you or the members of your staff recently made an inspection of the operation at Lake of the Woods?

A I saw the sewerage treatment plant. I saw the water system, especially the pumping system, and the storage tank. I visited at least four of the discharge mechanisms at the house. I saw the place and how they constructed the storage tanks, and I was given an explanation of the new air vac discharge mechanism, which is to replace the electric mechanism that they have been using in the past. That was the extent of my visit. Plus a lengthy interview regarding personnel, which part of it was not right.

Q Did you have an opportunity to observe the construction force and the construction operation and the maintenance force and their work to determine what type of work was being done, and how efficient the operation was?

A No, sir. I would have to admit that other than one person -- the field superintendent

1 and Mr. Thorpe, and the gentleman from Maryland --
2 were the only personnel that I observed.
3 MR. SOMERVILLE: Thank you very much,
4 Your Honor.
5 HEARING EXAMINER: Any redirect?
6 (NOTE: No response)
7
8 HEARING EXAMINER: Mr. Tice, did
9 your investigation of the system lead you
10 to believe that it is generally adequate
11 for the maximum number of homes that can
12 be built in that area, or is there going
13 to be some further work needed as more
14 homes are to be built?
15 WITNESS TICE: Well, just on the
16 water system, what I just mentioned, would
17 have to be installed and put into service
18 before that would be adequate for the total
19 number of homes, and I would assume that
20 the sewerage treatment plant would have
21 to be expanded at some future date, but
22 I don't think it is immediate.
23
24 HEARING EXAMINER: Thank you, sir.

Testimony of Alan L. Potter

DIRECT EXAMINATION

14 BY MR. SOMERVILLE

15 Q Please state your name, age, and
16 residence.

17 A I am Alan Potter, I am fifty years
18 old, and I am a resident of Lake of the Woods.

19 Q What is your connection with Lake
20 of the Woods Association, Inc?

21 A I am the President of Lake of the
22 Woods Association.

23 Q Would you state briefly your education
24
25

and occupational background?

A Yes. I have a Bachelors Degree in Chemistry, and a Doctor's Degree from George Washington University Law School. I have been in the law practice and in business all of my career.

Q Mr. Potter, your testimony is filed with the Commission. On pages 1 through 8, with a chart on page 9, let me ask you to summarize your testimony and highlight any specific points that you think should be made to Mr. Farrar.

A All right, sir. First of all, I would like to clarify a couple of points which have been made here previously today. Mr. Thorpe referred to our ratio of homes in the community as being three vacation homes, with one permanent residence. That is absolutely the opposite. About seventy-five percent of the homes are occupied full time, and about one quarter of them are in fact just weekend, summer time residences.

The other point that was made was we are a recreational retirement community. The community actually started as a recreational resort community. We have attracted a pretty high proportion of retired people. But we are growing very rapidly. We are attracting a very large number of young families into the community. At this point, we send over two hundred children into the Orange County school system. Then, we have about -- we have a lot of young families.

I would like to emphasize my testimony also that the growth rate of our community has been excellent from its inception through today, about thirteen years. We've averaged about seventy new homes per year and we continue that rate right through 1979, despite the tight mortgage money rate and is continuing into 1980. And I bring this up simply to point out that the Utility Company is looking at a future expansion of users to its system. It is not facing a stagnant situation but is facing a rapidly growing situation with more and more customers coming on line each year.

I would also like to emphasize that while I am the elected representative of all of the consumers of the Utility Company, I stand in

a somewhat unusual positi n. I'm here today to oppose this rate increase, but the last time the Utility Company came here, the Association appeared before the State Corporation Commission to support the Utility Company in its rate increase. I don't think you have many consumer groups who come in to support the Uility Company; it's rather rare.

We did it because we think we are economic realists and we thought that increase that they asked for in 1977 was justified. We saw the need then for their increased fees. We don't see the need now. We feel that they have totally failed to support their case, first of all on the figures which they have presented, which have gone into the record here. We have heard testimony that there is some overlapping and unsupported charges and fees of very highly questionable values to us.

We don't know what these people are supposed to do for this; we don't know what these fees are charged for.

There are other questions in their figures. A witness will follow me who is an accountant, who will raise questions about their accounting practices and other figures which they

have presented to this Commission.

In addition to that, we have high questions about the efficiency of their operation. The testimony today has been to the fact that they have one field superintendent on site at Lake of the Woods. The next closest supervisor is over a hundred and fifty miles away, I believe it is about three and a half hours by car, and generally when he has a problem he only knows it because we call him up and tell him he has a problem. We have no effective supervision on site.

And the feather bedding that goes in within that community and this Utility Company is unbelievable because there is no supervision of any work there. So we do not support the fee increase based on that.

But I have another much deeper concern also, and that is the impact this increase will have on our community. We think that this increase would be totally unmitigated and a disaster for Lake of the Woods, for a growing and thriving community. We are, as every community is, in competition to attract people to live in our community. And so far we are very successful at it. Certainly, people look at the cost of moving into our community

as opposed to other communities. The chart that I attached to my testimony, I would like to refer to that right now. If you would look at it, Mr. Farrar, it shows an article that was taken from The Washington Post published September 28th of this year. It shows --

MR. RIELY: Mr. Examiner, I object to the introduction of this chart and the testimony about it for the same reasons that I have previously given about comparable rates.

WITNESS POTTER: The only comment, if I may comment, on that, sir --

HEARING EXAMINER: What was the basis of the objection?

MR. RIELY: It's nothing but a statement of attempting to compare rates; and, as the Supreme Court of Virginia has said, as you recognize, it's not proper in a rate case of this character.

WITNESS POTTER: I believe, sir, the case you refer to --

HEARING EXAMINER: All right. Mr. Potter, I think what Mr. Riely said is basically true. I'm going to permit it to be placed in the record, but --

MR. RIELY: I simply wanted to note my objection.

HEARING EXAMINER: Yes, sir. Go ahead.

WITNESS POTTER: I will note in this statement, sir, that I'm not presenting these figures with the idea that I'm trying to show what is reasonable but fair, which was the case he is referring to.

What I'm showing here is that someone getting ready to move into the Lake of the Woods certainly reads The Washington Post; he doesn't read the Virginia Supreme Court Reports. And he is going to see in the Metropolitan Washington area that water and sewer costs him a hundred and ninety-six dollars; and if this rate increase goes through, he will see at Lake of the Woods it is

1 going to cost him five hundred and
2 twenty-eight dollars. Now he knows
3 that. He is not blind. He can see
4 what his costs are. He can see this.
5 Even the interim increase, which has
6 already been granted, is three hundred
7 and thirty-six dollars per year and
8 that's seventy-one percent higher than
9 the average of the Metropolitan Washington
10 area costs.
11 To him, that's just one of the
12 costs he has to look at in moving into
13 Lake of the Woods. He has another cost;
14 we charge him two hundred and forty-eight
15 dollars Lake of the Woods' assessments.
16 What does he get? He gets fifty-four
17 miles of hard surfaced roads that are
18 maintained by us at our total expense.
19 He gets a full time police force with a
20 twenty-four hour guard at the gate. He
21 gets two lakes, one of them with fifteen
22 miles of shore line. He gets four tennis
23 courts. He gets two swimming pools. He
24 gets stables, a marina, a golf course and
25

a pro shop, a club house and the administrative and management staff to run all of this at a figure less than half of what the Utility Company is asking him for water and sewer.

Now, that's what he is going to look at coming into our community. And I don't think he is going to come. It will be a total, total disaster for him.

I think that this rate increase, if it goes through, even the interim increase, is going to kill Lake of the Woods. It will kill the future development and growth of this community. It will kill the Utility Company because they will not have another expanding base of customers, and it's going to be very detrimental to Orange County because today we supply fifteen percent of the real estate tax revenues to Orange County.

That's my testimony, sir.

HEARING EXAMINER: All right.

MR. SOMERVILLE: I submit Mr. Potter for cross-examination.

HEARING EXAMINER: All right. Mr. Somerville, do you wish to admit his prefiled testimony into the record?

MR. SOMERVILLE: Yes, I do. I ask that the prefiled testimony be admitted into the record as his testimony.

HEARING EXAMINER: All right. That testimony will be copied into the record as if given orally in this proceeding.

NOTE: At this point, the prefiled direct testimony of Alan L. Potter is copied into the record.

LAKE OF THE WOODS ASSOCIATION, INC.

Testimony

of

Alan L. Potter

I am Alan L. Potter, and I reside at 110 Castle Hill Court, Lake of the Woods. My mailing address is: Box 913, Lake of the Woods, Locust Grove, Virginia 22508.

I am President of Lake of the Woods Association, Inc. I am also a practicing attorney with offices on the commercial property of the Lake of the Woods development on Virginia State Route Number 3.

The Lake of the Woods Association, Inc. occupies a unique position in both fact and law. The Lake of the Woods development was conceived initially as a private residential and recreational community. Covenants running with the land were attached to each lot in the development and are of record in the Clerk's Office of the Circuit Court of Orange County, Virginia. By those Restrictive Covenants the administration of the affairs of the Lake of the Woods community was vested in the Lake of the Woods Association, Inc. and every purchaser of a lot was required to become a member of that Association. The Association was organized as a Virginia non-stock corporation and functions as such today. All of its officers and directors, including me, serve without pay and are assisted in their duties by a large number of committees of the residents of the community. The Association hires a General Manager whose duties are to oversee and supervise the performance of a substantial staff of maintenance

and operating personnel. The Lake of the Woods community has 54 miles of hard surface roads which are maintained at the sole expense of the Association. It has its own police force, a controlled access gate, and virtually no crime. There are two lakes, one of which has over fifteen miles of shoreline, an eighteen-hole golf course, four tennis courts, two swimming pools, stables, a marina, and a clubhouse which, within the past year, was destroyed by fire. At the present time there are 825 homes within Lake of the Woods which reflects a fairly steady growth rate of slightly over 70 homes per year. It is important to note, moreover, that that growth rate continued through the mortgage money crunch of 1979 and 1980.

The Lake of the Woods community is only thirteen years old. Although it was envisioned by its developer as a residential and recreational community of primarily vacation homes, it has developed quite differently from its original concept. Today it is primarily a residential community, encompassing a full spectrum of residents. We have young families who send over 200 children to county schools, we have many families of retired persons, and we still have quite a number of weekend residents. Lake of the Woods is now the third largest population center in Orange County and sends over 200 children to the county schools. We have become a factor in the economic, social, and political life of Orange County and currently contribute 15% of the total real estate taxes of the county.

The developers of the Lake of the Woods community were

obviously motivated by the potential for profit from the sale of the individual residential lots into which the development was divided. In order to make those lots attractive to prospective purchasers at the asking prices, the developers created the lakes and the other recreational amenities at Lake of the Woods. In addition, and as was clearly necessary, the developers constructed a water and sewerage system to serve the builders of homes upon the lots which they purchased. After the sale by the developers of virtually all of the residential lots in 1970, the developers became amenable to the sale to the Association of all of the non-residential property within the community, including all of the recreational amenities, with the sole exception of the water and sewerage system. The Lake of the Woods Association, Inc. negotiated the transaction with the developer and acquired all the described property with the exception of the water and sewerage system. The current owners of the Lake of the Woods Utility Company purchased the capital stock of that company from the developer, and, presumably, did so after an economic analysis which indicated a profit could be made from the operation. Prior to the new owners purchasing the water and sewerage facilities, the former owners applied for a rate increase in May, 1977. Prior to doing so, however, they advised Lake of the Woods Association, Inc. of this and the Association supported the major portion of the request in the hearing before the State Corporation Commission -- certainly an unusual posture for a group of consumers. That history makes it extremely hard to

understand why the present utility company has pursued the course which it has followed in this instance.

Without any discussion with any of the Association officers at Lake of the Woods and, indeed, without any notice to its Lake of the Woods customers, the Lake of the Woods Utility Company successfully sought from the State Corporation Commission an order permitting it to make an interim increase in its sewerage rates which amounts to 200% of the then-current charge. As a lawyer I find it awfully hard to understand how that could have happened. I have particularly noted that the initial application filed with the Commission by the Lake of the Woods Utility Company on June 17, 1980, sought a temporary emergency increase in rates pursuant to Section 56-245 of the Virginia Code of 1950. I have also noted that on June 24, 1980, counsel for the utility sent a letter to the State Corporation Commission advising that the general counsel of the Commission had raised a question as to whether the application could properly be granted under Section 56-245. The letter went on to state that if the Commission should be of the view that that section of the Virginia Code is inapplicable, the company requested that the application be considered as one under Section 56-240 or any other section of Title 56 of the Code that may be used to give the company prompt and effective relief.

By order dated July 1, 1980, the Commission denied the emergency rate relief requested by the utility under Section 56-245 and set the proposal for public hearing before a Hearing Examiner for November 5, 1980. In addition, the Commission

directed the Commission's staff to investigate and report on the appropriateness of interim relief under Section 56-240. The important point here is that Section 56-237.1 of the Virginia Code provides for notification to the customers of the utility of its intent to seek a rate change. No such notification was ever given. In spite of that fact, by order dated July 17, 1980, the Commission entered its interim order which confirmed the assignment of the matter for hearing on November 5, 1980, but also found that the company had demonstrated a reasonable probability that an increase in rates in the amount sought would be justified after a full investigation and hearing. Reference to the report of the Commission's staff, however, discloses that no "full audit investigation" of the company had yet been made. That fact, plus the fact that no opportunity was given to the customers of the utility to submit any evidence in opposition to the interim increase, raises in my mind a serious question as to the propriety of the interim order itself.

As though the foregoing were not bad enough, on July 28, 1980, and again without any notice to its customers, the utility sought a further increase in the same amount as the one which had been approved on an interim basis. The net result is that the company is now proposing to quintuple the former charge for sewerage services. To exacerbate the matter even further, the data submitted by the Commission's staff to justify its recommendation that an interim increase be allowed, were restricted to an operating statement purporting to relate to the sewerage operations only. That obviously necessitated some sort of

division between the water and sewerage operations of the utility and that separation is, almost by definition, suspect.

Laying to one side for the moment the entire question of the propriety of the interim increase which has been allowed, it is beyond cavil that any utility asking for such a drastic increase as one which would quintuple its current charges should be able to demonstrate not only a compelling need for the additional funds, but a carefully drawn analysis of the impact which the increase would have on the future of both the company and the community it serves. I have reviewed the evidence support by Lake of the Woods Utility Company in this case and I can find neither in its testimony.

As Mr. William W. Carpenter, a resident of the Lake of the Woods who has spent his entire career in accounting, will testify, the financial data filed by Lake of the Woods Utility Company in support of its request come from its unaudited books. Those figures reflect in the expense column a management fee which purportedly goes to the California owners of the utility. The data also reflect a charge for supervisory personnel although there is no "on-site" manager of the operations at Lake of the Woods. Mr. Carpenter's testimony will also point to other substantial items of expense which can hardly be justified as appropriate and proper under the circumstances.

The manager of Lake of the Woods, Mr. Warren Lodge, will also testify as to the effect of the absence of "on-site" supervision of the utility operations upon the economy and efficiency of those operations themselves.

Looking at the matter from a different standpoint, I call attention to the fact that the utility is asking the Commission to approve a charge for sewerage service which is at least twice as much as the average charge paid by the homeowners at Lake of the Woods in real estate taxes to the State of Virginia. It is also about twice as much as those homeowners pay for the maintenance and operation of the entire community of Lake of the Woods. I do not believe that our community could even survive, let alone grow, in the face of such an outrageous cost increase. I know of people who must leave our community if the increase is approved. I have had telephone calls from people who are delaying purchases of homes in our community pending the outcome of this hearing. For the information of the Commission, I am attaching hereto a chart which shows the comparative cost for sewerage services in communities near us and in the "high cost" Northern Virginia area. A community, just like a business, can price itself out of the market. And if we do that, we will stagnate or die and Lake of the Woods Utility Company will stagnate or die right along with us.

Lake of the Woods Utility Company can do a great deal to solve its own financial problem if it is willing to do so. We know more about its business than it does because the closest thing it has to a full-time manager is 150 miles from us. We have to telephone him to tell him what his problems are and ask him to come down and solve them.

Let Lake of the Woods Utility Company put a competent

manager on the site to stop the waste and inefficiency. Let Lake of the Woods Utility Company have an independent audit of its books. Let Lake of the Woods Utility Company allocate the expense of its executives based upon actual time spent at or concerning Lake of the Woods. And let the parent of Lake of the Woods Utility Company stop taking out so-called "consultant" and "management" fees for which we at Lake of the Woods receive nothing. Then and only then should Lake of the Woods Utility Company be considered for a rate increase.

NOTE: Thus concludes the prefiled direct testimony of Alan L. Potter.

* * * * * * * * * * *

WARREN J. LODGE, a witness called by and on behalf of the Protestants, having first been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. SOMERVILLE:

Q Please state your name, age and residence.

A I am Warren J. Lodge, aged fifty-three. I reside at Lake of the Woods, Locust Grove, Virginia.

Q What is your position with Lake of the Woods Association, Inc.?

A I am the General Manger of the Lake of the Woods Association, Incorporated.

Q Would you state your educational and occupational background?

A I have a Bachelors degree in Business from the University of Omaha. I have a Masters in Business from George Washington University.

My background basically has been military. I spent thirty-four years and nine months in the military in ever-increasing positions

of responsibility in managing communities.

Q Mr. Lodge, you have given testimony which has been prefiled with the Commission, and I'm sure that you are familiar with the testimony, since it is yours.

Do you have any additions or changes to make in that testimony?

A I do not.

Q Would you simply highlight the main points of your testimony at this time?

A I will. Lake of the Woods Utility Company operates a water and sewerage system at the Lake of the Woods which I believe is adequate to meet the present and future needs of the community; however, because of the lack of qualified and capable management personnel and technical personnel, operations and maintenance costs are inordinantly high. With the Manager and Operations Officer located three and a half hours away by automobile, virtually no supervision on the site. We observe on a daily basis the total inefficiency of the operation.

It appears no employee stationed at Lake of the Woods understands the basic fundamental of management which requires organization and assignment

of work, monitoring of progress and a final checking to assure satisfaction, and completion of each job.

I have received virtually hundreds of complaints about water and sewerage service in the nine months I have served as General Manager at Lake of the Woods. These are brought to me after unsatisfactory resolutions with on-site personnel.

Some of these problems I am able to resolve with the on-site field superintendent. But many I must take to the parent office in Berlin, Maryland by long distance telephone, either to the General Manager or to the Operations Manager there in an attempt to resolve the problems. Simply again because the problems cannot be resolved by the people on the ground at Lake of the Woods.

Some of those problems remain uncorrected today. Those complaints range from overflowing water and sewer tanks, some of which run into our Lake, broken sewer lines, excessive odors from pumping stations, and low or no water pressure available on site. Examples of the ineffiency of operation -- and certainly not isolated examples -- include allowing the water holding tank to run dry over the Labor Day weekend and several other weekends

during this Summer which created an intolerable living conditions and a real fire hazard to Lake of the Woods.

The Utility Company has yet to answer my written complaints on this matter.

Having the Utility Company personnel respond to emergency calls, simply walk around the sewer holding tank and driving off without solving the problem. Attempts to solve overflowing tank problems by dispatching of pump trunk day after day to remove the wastes rather than solving the problem which caused the overflow. Maintenance personnel wasting time at bull sessions or out in the maintenance yard or in using Utility Company vehicles to travel to the local 7-Eleven Store in mass during lunch periods. Maintenance personnel driving around the Lake property in an aimless fashion, obviously killing time.

Each incident of this type reflects lack of supervision by management and runs up operation and maintenance costs which are ultimately passed onto Lake of the Woods residents.

The consultant, who is paid fifteen thousand dollars a year, indicated in 1975 that

a full time manager should be on the ground. To date, we do not have one.

He indicated before this Commission in 1975 that a total of eight people should be able to maintain and operate the system. And that construction work should be done on contract outside the organization. As we found to date, the Company has sixteen people on the ground which leads to the conclusion that the size of the staff is grossly inflated because of lack of management supervision and technical ability.

The consultant, to the best of my knowledge, has been at the Lake of the Woods once in the nine months that I've been General Manager. That hardly justifies a salary of fifteen thousand dollars a year. Again, paid by Lake of the Woods home owners through the Utility Company and now asked to bear the burden of a four hundred percent sewerage rate increase.

Lake of the Woods Association is serviced in seventeen common areas by the LOW Utility Company. Six of these locations, such as rest rooms and parks are open only five months a year. A cost of forty dollars per month per location,

or four hundred and eighty dollars per year for a hundred and fifty days of operation is certainly exorbitant.

Our steady growth of seventy-one new homes per year will stagnate under a forty dollar a month sewerage charge. People are now reluctant to build until the issue is resolved and others on fixed incomes will have to move out of the development because of costs. Both LOW and LOW Utility Company rely upon steady growth to survive. The large sewerage rate increase will cause us both to shrivel up and die.

On-the-site general management and technical expertise will go far toward improving the efficiency of operations and greatly reduce operations and maintenance costs of the LOW Utility Company, possibly to the point that no increased rate is required to insure solvency. Only when the management of the Company produces the efficiency required, will the Company have an opportunity to earn a fair rate of return on their investment. That step logically precedes any increase in sewerage rates.

1 That is the summary of my testimony.

2 HEARING EXAMINER: All right.

3 Any questions of this witness?

4 MR.RIELY: No questions.

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CROSS EXAMINATION

BY MR. LION

Q Mr. Lodge, could you please provide the Commission's staff with specific dates and instances to which you have alluded today as problems with maintenance, or overflows, or whatever, so that the Commission Staff ---- and also supply the same list to the Company so that the Commission staff can follow up on this outside this hearing procedure today.

A Yes. I can go back and reconstruct such a chart. I will say on that point I was in error when I tried to become general manager of Lake of the Woods. When people brought this type of problem to me with the threat that if it were not solved they would take it to the State Corporation Commission, I urged them not to do so, but to let me try to solve the problem for them. That obviously was a mistake, and will not happen in the future.

You will get the copies in the future, but I will go back and try to reconstruct as best

I can the list of complaints that I have, and provide it to you.

MR. LION: All right, sir. I appreciate that.

HEARING EXAMINER: Mr. Page?

MR. PAGE : I have no questions.

MR. SOMERVILLE: Mr. Farrar, I move that the prefiled testimony of Mr. Lodge be read into the record as evidence.

HEARING EXAMINER: That will be done.

(Prefiled testimony follows)

LAKE OF THE WOODS ASSOCIATION, INC.

Testimony

of

Warren J. Lodge

I am Warren J. Lodge, General Manager of Lake of the Woods Association, Inc. I have served in this capacity for nine months. My background is that of a combat arms officer in the U. S. Army where I served as a manager of people and resources for 34 years and 9 months. My last seven years in the military were served as Post Commander of major installations in both the United States and overseas. In this capacity I served, in effect, as City Manager for communities ranging in size from three thousand to twenty thousand people, with responsibility for housing, maintenance, and utilities for the entire installation and its geographic area.

As General Manager of Lake of the Woods Association, Inc., I am the senior member of the paid staff and am ultimately responsible for every aspect of operation of Lake of the Woods. As a result, when our property owners require assistance with outside agencies, they turn to me. One of the very first categories of concern which demanded my attention was the water and sewer facilities. Those services are, of course, fundamental in any community where the population is other than purely rural and where septic fields are the exception and not the rule. The Lake of the Woods community, as Mr. Thorpe has testified, consists of a development of 4,200 (the number is actually 4,258)

individual lots which are designed to accommodate separate, single-family residences. Lake of the Woods is, however, not only a recreational, but also a residential community. At present there are 799 single-family residences already built and the rate of building is continuing at about 71 homes per year. With the exception of only three houses, built long ago, each of the homes now in existence and those which will be constructed in the future are dependent upon the Lake of the Woods Utility Company for both water and sewer services. The three exceptions which I have mentioned each has its own septic field, but is dependent for its water supply on the Lake of the Woods Utility Company. All of the 796 other homes are dependent upon the Lake of the Woods Utility Company for both sewerage and water. In addition, there are 42 homes presently under construction and each will use both the water and sewer services of the Lake of the Woods Utility Company.

In addition to the 838 homes mentioned above, there are certain facilities and installations of the Lake of the Woods community which are dependent upon Lake of the Woods Utility Company for both water and sewerage services. There are seventeen such community-owned installations. These consist of the clubhouse (now being rebuilt after a destructive fire last spring), two swimming pools, the golf pro shop, a community building, comfort stations at parks, playgrounds, and picnic areas, the teen center, the administrative building, the security gate, and other facilities of the community.

The obvious importance of the water and sewerage services readily explains why I found those services to be a matter of primary importance and one which demanded and got early attention from me. My earliest investigation convinced me of two things. First, I became convinced that the system used for supplying those two services was a good one. The water supply, which includes a series of fire hydrants, depends on eight drilled wells which produce water of such purity that it needs no treatment prior to distribution for all purposes, including drinking. As Mr. Thorpe has explained, a satisfactory pressure is maintained by elevating the water from the wells to a tank from which it is drawn as needed. The entire water supply system is relatively inexpensive from both the production and distribution standpoints. So long as an appropriate level is maintained in the tank, the pressure throughout the community is adequate and, as I have said, the quality is excellent. Even so, during the past Labor Day weekend, there was a failure of the operating personnel and the level of the water in the tank fell to a dangerously low point with resulting loss of pressure. Had there been a serious fire in the area, the possible damage to the community would have been inestimable. At that particular time there had been an extended drought and the undeveloped wooded lots were practically tinder.

The failure of the Lake of the Woods Utility Company personnel to maintain adequate water pressure during the Labor Day weekend was due, I am convinced, to a lack of adequate on-site

supervision and not to any inherent flaw in the water-supply system. It was just another manifestation of inefficient operation which afflicts both the water and the sewerage services at Lake of the Woods.

The system used by the Lake of the Woods Utility Company to provide sewerage service is much more sophisticated than the water system. Mr. Thorpe has explained it in some detail and I will not try to embellish what he has said. I do want to add that from my own observation and study, I am convinced that it is a good system and one that will work well and effectively if given proper supervision, maintenance and monitoring. It is, therefore, regretable that the Lake of the Woods Utility Company has not seen fit to provide competent and knowledgeable supervisory personnel on the site of the operations. As Mr. Thorpe himself has stated, he is based at Ocean Pines, Maryland, a residential and recreational community near Berlin, Maryland. That is three-and-one-half hours from Lake of the Woods by automobile and automobile is the fastest and most direct means of travel between the two points.

On a daily basis I receive complaints from our property owners and requests for assistance to resolve problems with the Lake of the Woods Utility Company. These requests, in every case, are of the last resort type; that is, after attempting to solve the problem with the Lake of the Woods Utility Company, the property owners contact me to attempt to solve the problems. Problems range from overflowing sewer holding tanks to broken sewer lines, sewerage running into the lake, excessive odor from

pumping stations, and low or no water pressure. These complaints have run into the hundreds in my nine months on the job. I am able to resolve some problems through the local Field Superintendent; many require calls to the Lake of the Woods Utility Company General Manager or Operations Officer at Ocean Pines. Most problems are ultimately resolved; some remain and have never been resolved.

My analysis of the overall problem is that because there is no General Manager or technically qualified Operations Officer on the ground at Lake of the Woods, operations and maintenance costs far exceed the costs they should be. Reports which reach me, and my personal observations are as follows:

a. Lake of the Woods Utility Company maintenance personnel receive calls for service and in most cases do respond. Response sometimes results in personnel arriving, walking around a holding tank, getting into a truck and driving off. Other reports reveal that at times the maintenance man does not even get out of his truck, but sits for several minutes and then drives off.

b. In cases of overflowing or full tanks, the solution has sometimes been to send a pump truck, empty the tank, and drive off, followed by repeat calls and repeat truck pumping on subsequent days with no effort or no ability to solve the technical problem involved.

c. Reports that the maintenance personnel of Lake of the Woods Utility Company spend fifteen minutes to an hour at a time standing around the maintenance yard involved in talk and

horseplay instead of working to maintain the system.

d. Reports that maintenance personnel drive aimlessly around Lake of the Woods seemingly going no place in particular except to put mileage on vehicles. I, personally, observed on one day an employee in a pickup truck visit three of our beach areas, sit there in the truck, then move on to another beach area.

e. Reports that as many as three Lake of the Woods Utility Company pickup trucks, carrying five men, were at the local 7-11 store about two miles from their maintenance yard. I observed this. Although at the noon hour and possibly authorized off-duty time, the fact that three trucks made the trip certainly runs up fuel and maintenance costs on Lake of the Woods Utility Company vehicles.

Each of the type incidents reported increases greatly the operation and maintenance costs of the Lake of the Woods Utility Company, which are eventually borne by our property owners. These incidents occur specifically because there is no on-the-ground General Manager or Operations Officer for the Lake of the Woods Utility Company who should organize and assign work, monitor progress, and check on final satisfactory completion of each job. On-the-ground management would go far to reduce operations and maintenance costs and could reduce or eliminate a requirement for a rate increase of the magnitude requested.

It is interesting to note that in testimony before the State Corporation Commission on August 26, 1975, Case No. 19564, Mr. Brockmeir, then of Boise Cascade Co. and who is now, as we understand, retained as a consultant to Lake of the Woods

Utility Company at a cost of $1,250 per month, stated in direct testimony that he "very definitely" anticipated a full-time manager on the site at Lake of the Woods. He further stated that there were three candidates for the job, each of whom had adequate experience in managing a sewerage and water company and each of whom had "a specific ability in the vacuum sewerage system". As of this date, no full-time, on-site manager has been kept. Mr. Brockmeir also testified that a proper technical staff would be employed and trained to insure a reliable system. As of this date no proper technical staff has been employed or trained. The result as I have stated is an almost total lack of general management and technically qualified personnel which leads to greatly increased operation and maintenance costs to the Lake of the Woods Utility Company and, ultimately, to the property owners.

Mr. Thorpe, in his testimony, indicated the second costly aspect of the vacuum system is its requirement for relatively large amounts of labor to operate and maintain the vacuum pumping equipment, vacuum valves, and vacuum mains. He stated, "Unfortunately, the vacuum system is simultaneously power and labor-intensive, and as we are all aware, those two resources both carry hefty price tags". It is relevant to note that the developer and installer of the system maintained that only one part-time operator would be required to maintain the system since it was so fully automatic and automated. Many of our property owners purchased at Lake of the Woods with this fact in mind. In his testimony in 1975, Mr. Brockmeir indicated

staffing of the Lake of the Woods Utility Company would consist of one manager who would be an engineer-operator and licensed water and sewerage operator, one bookkeeper-secretary, three electronic technicians, two installers of equipment and three pump truck operators who would eventually be reduced to one. Additional construction personnel were to be provided by an outside contractor. Thus, there was to be a total requirement of eight employees. Today there is a staff of sixteen employees. The only conclusion I can draw is that the size of the staff is greatly inflated because of lack of management supervision and technical ability.

Mr. Thorpe, in his testimony, stated that in the sewer system there is the constant requirement to increase the size of certain vacuum lines, which results in requirements for capital expenditures. While I am not privy to all aspects of the daily operation of the Lake of the Woods Utility Company, I am made aware of happenings on the property. I am not aware, during my nine months as General Manager, when or where vacuum lines were replaced because an increased size was required. Many repairs are accomplished on existing broken lines, but I am aware of no upgrading of sizes. In his testimony of 1975, Mr. Brockmeir, presently consultant to Lake of the Woods Utility Company, stated it was more economically prudent to modify the system or divide an area by laying parallel lines "because they might be able to save a lot of maintenance costs, a lot more

maintenance personnel, because it does take less maintenance personnel to operate system that has higher vacuum. If you have a heavier load, most likely you will have a lower vacuum available in the mains, which may take more manual attention."

Incidentally, in my nine months as General Manager, I have seen the consultant once, and that was when he visited my office in reference to replacement of a force main system in Section 5, a function of traditional sewerage systems and not one peculiar to vacuum systems alone. That project which was promised the residents of Section 5 several months ago to preclude force main breaks and sewage running into the lake, has still not been started. One visit by a consultant in nine months, if I am correct, hardly justifies a salary of $1,250.00 per month which is ultimately paid by the property owners of Lake of the Woods.

With respect to the proposed increase in sewerage rates, the increased costs to Lake of the Woods Association, Inc. to operate administrative and maintenance facilities and our amenities will be $3,264 per year at $24 per month and $6,578 at $40 per month. These increased costs are charged directly to our property owners through increased assessments. These are the same people who will be directly affected by the large proposed increases on their residential sewerage. Of the seventeen Association hookups, six operate only May 1 to October 1, or five months a year, and then are closed for the remaining seven months of the year with no water or sewerage usage. At a rate of $24 per month for sewerage, because of minimum charge

billing, we would pay $288 per year for 150 days of operation for each of the six facilities. At $40 per month we would pay $480 per year for 150 days usage for each of these facilities. The total cost for these six part-year operations of park comfort stations and the marina would be $2,880 per year to have them operational for five months at $40 per month. It certainly seems exorbitant. Many of our property owners who visit Lake of the Woods only occasionally on weekends, holidays, and the like, will find themselves in an equivalent situation. It is essential that if higher rates are authorized by the State Corporation Commission as a result of this hearing, some rate be developed which would take into account only partial annual operation of a facility or residence.

In recent years Lake of the Woods has experienced a steady and healthy growth rate of an average of 71 new homes per year. We believe that rate will continue and, in fact, may accelerate. During the recent housing slump across the United States our growth rate continued at its previous rate. However, tripling or quintupling the present sewer rate may well lead to total stagnation of our growth. I have received a number of comments from residents on fixed incomes which indicate they simply cannot absorb a rate increase of the magnitude requested and will be forced to sell their homes and move. Selling their homes may prove impossible if they find themselves in a situation where sewerage rates are twice what their real estate taxes are and that would be the case at a $40 per month rate. Several others

who have unimproved lots have indicated to me that they would have to wait for final decision in the sewerage rate increase case before deciding whether to build on their lots. The very thing the Lake of the Woods Utility Company needs to insure profitability in the future, development of many of the 3,400 undeveloped lots, may well shrivel and die because of the huge proposed sewerage rate increase. Lake of the Woods Association, Inc. also needs a growing population if it is to remain healthy and to be able to operate its recreational amenities with a break-even financial result. This large proposed increase threatens the very existence of Lake of the Woods as a financially viable residential community

(End of prefiled testimony)

HEARING EXAMINER: Let me see if I have any questions. Just a moment. You mention the fact that three homes, I believe, which I gather have their own septic system?

WITNESS LODGE: That is correct, sir.

HEARING EXAMINER: Do you happen to know whether the covenants in the subdivision would allow other lot owners to either dig a well for water, or to install a septic system?

WITNESS LODGE: They cannot install a septic system. The reason we have a sewer system today instead of everybody being on a septic tank, the development was planned to be a septic tank system, everybody having their own septic tank. The initial test -- the perk test -- the ground would not perk properly. They could not get the permits. Therefore, that is why the sewer system was brought

1 into play. But they would not be
2 authorized to dig wells in the individual
3 lots.
4 HEARING EXAMINER: All right.
5 You say in your testimony that there
6 is no on-sight supervisor, and you feel
7 that is part of the problem.
8 WITNESS LODGE: I think that is
9 the total problem. I think that is the
10 total problem with the inefficiency of the
11 system, and the total problem as far as
12 operation and maintenance costs are
13 concerned. I heard the previous testimony
14 here today about the field superintendent,
15 both to his technical knowledge and his
16 general management capabilities.
17 I disagree totally with those
18 statements. The problems that I end up
19 taking to either the General Manager
20 or the Operations Officer at Maryland
21 Marine Utilities at Berlin is because they
22 cannot be solved on the ground. And those
23
24
25

problems range about fifty/fifty -- about fifty percent are technical problems, and he cannot solve, and we end up with Mr. Tom Forilla, the operations officer coming down from Berlin and solving them, or their general management problems, for which he is not able to organize his work or get the work done, and end up either calling Mr. Thorpe, the General Manager, or Mr. Forilla, and then in all honesty and fairness, once I have done that, most of the problems get solved, but it is not because of anybody on the ground at Lake of the Woods.

HEARING EXAMINER: All right, thank you, sir. You may stand down.

5 William W. Carpenter,

6 a witness introduced on behalf of the Protestants,

7 being first duly sworn, testified as follows:

8

9 DIRECT EXAMINATION

10 BY MR. SOMERVILLE

11 Q Please state your name and address.

12 A My name is William Carpenter. Lake

13 of the Woods, Virginia. I am sixty-one years old.

14 My address is P. O. Box 430,Locust Grove, Virginia.

15 Q Are you employed by Lake of the

16 Woods Association, Inc?

17 A No, I am not.

18 Q Now, you have done some work in

19 preparation for this case. Have you been compen-

20 sated, or will you be compensated for this?

21 A No, I will not.

22 Q Please give us your educational and

23 occupational background.

24

25

A hold a masters degree in Commercial Science from Benjamin Franklin University in Washington. I began my accounting career in 1941 with Stone and Webster Engineers. I spent seventeen years sith them at various locations in the country. For the past seventeen years I have been manager and controller of the American Psychological Association in Washington, D. C.

Q Mr. Carpenter, I believe that your prefiled testimony begins on page 21, and runs through your statement -- the last of which would be on page 31. Do you have any additions or changes which you would like to make at this time?

A I have one comment to make on an item that Mr. Leis submitted in his testimony. And that is on the uncollectible accounts expense. And we will come to that later.

Q All right. Would you proceed to highlight your evidence, and point out the things that you feel are most important at this time.

A Well, I reviewed the testimony and exhibits of Mr. Frasher which he submitted in these proceedings, and as an accountant I found four

areas that I thought should be adjusted. But first I think I should point out that as an accountant I think the operation of the Company should be considered as a whole, as opposed to its various components.

There are many reasons for that, most which have already been stated, but from an accounting standpoint the only way you can get a true picture of any Company is by viewing the operation as a total if you are considering profit and loss, gain, or whatever. So I wouldn't dwell on that too much, but I do think from an accounting standpoint the only equitable way is to view it as one operation.

The four areas that I find that I would question as to the reasonableness of the expenses that are being charged -- and I prepared two exhibits -- one I restated 1979 position as of December 31, '79, and I restated the pro forma statement for 1980, but similar adjustments. These adjustments fall in four areas; the first one is in the provision for uncollectible accounts. In reviewing the year-end balance sheet for 1979, I

noted that the reserve for uncollectible accounts has already passed six percent of the total accounts receivable, which is rather unheard of in the accounting field. So on that basis I just eliminated the expense of forty-nine thousand, ninety-one dollars for that item, because they had exceeded any reasonable amount of reserve for that particular item.

Now, after I did that, I noted the testimony of Mr. Leis, the Staff Accountant, and I know that they apparently have a policy to limit that expense to one percent of the gross revenues, and he did make an adjustment for the sewer operation of twenty-one thousand, four hundred and three. So I then created a statement, going back to the 1975 point of origin, to determine what the adjustment should be for the water operation in '79, and it amounts to twenty-two thousand, eight hundred and forty-seven, which would be an additional adjustment that should be made in that area.

And I might add --

Q Is this attached to your statement?

A Yes, it is.

Q That is Statement 3, Carpenter?

A That is Statement 3, Carpenter.

I might add, as a result of preparing that statement, that was the only way I could arrive at the current figure was to start at the beginning.

I note that the total excess deduction, that is the excess over the one percent that would be allowable for that period, amounts to two hundred and twenty-nine thousand, seven hundred and ninety-four dollars, if we are only speaking of 1979.

So that is not totally pertinent.

I agree with Mr. Leis' deduction on the depreciation, which I made a similar deduction or adjustment on the depreciation factor, slightly over thirty-two thousand dollars for depreciation that had been taken on the contribution to construction which didn't cost them anything, although they do have it in their capital, but it has to be backed out in the rate base. So, obviously, depreciation would come out, too.

And there were two other small areas -- not too small. One was a management fee that is

1 being charged by the parent company.

2 Normally, a parent company gathers

3 in the profits or sustains losses of any subsidiary

4 company, and I saw no evidence of any services being

5 rendered, so I just, as an accountant, thought that

6 was unjustified, so I eliminated that particular

7 item.

8 And I did the same thing with the

9 engineering consultants fee of fifteen thousand

10 dollars, because in my review of all the records

11 that I could get my hands on, I could see no evidence

12 of any services being rendered by the consulting

13 organization in Santa Monica on an organization in

14 Lake of the Woods, Virginia.

15 And that, really, are the four basic

16 areas that I found that I thought should be

17 adjusted to state the Company's true position.

18

LAKE OF THE WOODS ASSOCIATION, INC.

Testimony

of

William W. Carpenter

I am an accountant and hold a Masters Degree in Commercial Science from the Benjamin Franklin University in Washington, D. C. My early experience in the field of accounting commenced in 1941 when I was employed by the Stone and Webster Engineering Corporation as a field accountant. I spent 17 years with that firm in various locations, including Cleveland, Ohio; Philadelphia, Pennsylvania; Washington, D. C.; Alexandria, Virginia; and Dickerson, Maryland. For the past seventeen years, I have been a manager and the controller of the American Psychological Association in Washington, D. C. I am now retired and reside in Lake of the Woods. My mailing address is Post Office Box 430, Locust Grove, Virginia 22508.

I have reviewed the testimony and exhibits of Mr. Frasher in these proceedings and have prepared a restatement of the exhibits to reflect changes therein which I believe should be made. Attached hereto are my Statements #1 and #2. Each has appendant to it an explanation of the adjustments I have made and the effect thereof on the pro forma financial results of operations of the Lake of the Woods Utility Company. As will be seen from those two statements, each is based on the total operations of the Lake of the Woods Utility Company. I believe it is preferable to treat those operations as a whole rather than breaking down the revenue and expense accounts between sewerage and water. There

are several reasons for so doing.

In the first place, there are only three existing residences at the Lake of the Woods which do not use both services. One of them is on the north side of Route #3 and has its own septic field. The other two are homes which were built some years ago and also have their own septic fields. Every other customer of the Lake of the Woods Utility Company utilizes both the sewerage and the water services. All homes which are to be built in the future will use both services. It follows, therefore, that from the standpoint of the homeowner, the two services are interdependent and ought to be viewed as just one.

The second important reason for treating the accounts of the Lake of the Woods Utility Company on a combined basis, that is, both water and sewerage, is the difficulty encountered in separating the operations into individual component parts. For example, Mr. Frasher's exhibits allocate 48% of the total 1979 revenues of the company to the water service and 52% of those revenues to the sewerage service. My search of the records made available to me by the Lake of the Woods Utility Company leads me to believe that this is primarily the result of the company treating the availability charge of $7.75 per month as being $4.00 per month for the availability of water and $3.75 per month for the availability of sewerage. I do not view that as a fair separation of the availability charge. The rationale of an availability charge is to compensate the company immediately for having made the initial investment in the utility plant. The investment made by the Lake of the Woods Utility Company in the sewerage system is obviously far larger than its investment in the water system and, therefore, a much larger allocation of the

availability charge should be made to sewerage. It is better, however, to avoid the problem in its entirety by treating th total operation as a unit.

Looking at the problem from the standpoint of operating expenses, the separation of accounts becomes extremely difficult. The maintenance crew at Lake of the Woods works interchangeably on both water and sewerage services. From my observation at the office of the company at Lake of the Woods, the costs of the operation and maintenance and capital construction are allocated by the company by the use of a work-order system. To ascertain if all costs are properly allocated would require a complete audit of all work-orders in conjunction with the payroll and material records. This would also include an inventory of all new additions to the utility plant to determine if the costs are reasonable. It is my understanding that the Lake of the Woods Utility Company has never had an audit by an outside independent accounting firm.

In the final analysis, the true position of any company from an accounting or financial standpoint should be determined by the total company operations as opposed to individual operations within the company. There are many ways to allocate costs to individual operations within a company, each of which is no better than the method and accuracy of the particular system used. On the other hand, the results of the entire company operations give an accurate picture of the company.

As Mr. Potter, the President of the Lake of the Woods Association, Inc., has explained, the administration of the

affairs of the Lake of the Woods community is performed by the residents themselves on a volunteer and unpaid basis. Because of my background in accounting, I was asked to review the financial and accounting data of the Lake of the Woods Utility Company to determine the justification, if any, for the proposed increases in sewerage charges. I called upon the company to provide me with the data which had been submitted to the State Corporation Commission in support of the proposal and I also asked the company to provide me with copies of its annual reports to the Commission for the past five years. I reviewed all of that material and used it as the basis for restating the exhibits which were submitted to Mr. Frasher. In so doing, I restricted myself to identifiable expense items which, in my judgment, should not be charged as operating expenses and used as a basis for a proposed rate increase. I might add that there are other elements of expense which are highly questionable, but I have made no adjustment for these in my exhibits. For example, the labor charges in the general and administrative area include a substantial amount for supervisory personnel located in Berlin, Maryland. These personnel spend a minimum amount of time at the Lake of the Woods. No adjustment has been made in those charges as they cannot be identified clearly. However, consideration should be given to the exclusion of a portion of those costs in proportion to the time spent at the two locations.

Another example is the assumption by Mr. Frasher that the 30% increase in the cost of power during 1980 will be continued

for the remainder of the year and into the future. It is well known that the Rappahannock Electric Co-operative, which supplies power to the Lake of the Woods Utility Company, purchases its electricity from the Virginia Electric and Power Company. Vepco has recently become a large producer of electric power from nuclear reactors. An article in the Wall Street Journal of September 16, 1980, quoted the company as stating that when the North Anna Number 2 nuclear plant is operating fully, expected before year end, the net offset will be a reduction in Vepco rates of 7.2% in 1980.

My statement #1 attached hereto shows the results of the company's operations for the calendar year 1979 as restated with the adjustments I believe should be made. Those adjustments would reduce the 1979 loss from $131,261 to $12,136. The schedule explaining the adjustment and which was attached to Statement #1 shows that those adjustments cover four items. The first would eliminate the expense item for the provision for uncollectable accounts. The company evidently has no program for collecting outstanding customer accounts. The provision for uncollectable accounts has increased over the years with an expense taken each year. As of December 31, 1978, this account amounted to 60% of the total customer accounts receivable. Good management and a serious program to collect outstanding receivables should limit the provision for uncollectable accounts to no more than 20 or 25 per cent of total receivables. It is an unfair burden to have the property

owners at Lake of the Woods charged for Lake of the Woods Utility Company's lack of effort in this area.

The second adjustment I have made is to eliminate the management fee charged by the parent company located in Santa Barbara, California.

My investigation has disclosed no instance of any management service being performed by the California company for the Lake of the Woods Utility Company. Rather, the relationship between the two companies appears to be the normal one where the parent company receives the profits or stands the losses of its subsidiary.

The third adjustment I have made is to eliminate the engineering consulting fee being paid to a firm located in Santa Monica, California. The personnel of that firm are rarely at the Lake of the Woods. I am told that the frequency of a representative visiting the project is about once a year and I have found no evidence of consulting services actually being rendered.

The fourth adjustment I have made eliminates the depreciation taken on contributions to construction. That portion of the utility plant that is paid for by the connection charges received from the property owners was obviously billed at no cost to the Lake of the Woods Utility Company. Therefore, the company is not entitled to take depreciation on it and, in addition, such contributions to construction should be excluded from the rate base.

My Statement #2 appendant hereto restates the financial results of operations as projected by Mr. Frasher for the year 1980. As will be observed, my restatement utilizes the rate of

$8.00 per month for sewer and $4.00 per month for water. It also makes adjustments in the same four areas of expense as were adjusted on Statement #1 and, in addition, would eliminate the $4,800 in gross receipts tax that would have been incurred on the proposed increase to a $24.00 per month charge for sewerage. As will be seen from my Statement #2, the projected loss of the Lake of the Woods Utility Company would be $81,213. It may well be argued that that loss could be wholely eliminated if proper supervision of the operations at Lake of the Woods were provided. As an accountant, however, I have no means of identifying the reduction of expense which would flow from such an eventuality.

(End of prefiled testimony)

HAROLD J. WADE, a witness called by and on behalf of the Protestants, having first been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. SOMERVILLE:

Q Please state your name, age and residence.

A I am Harold J. Wade, and I live at Lake of the Woods, 434 Eastover Parkway. My mailing address is Box 555, LOW, Locust Grove, Virginia.

Q And what is your age?

A I'm sixty-seven years old.

Q You are retired, I believe?

A Yes.

Q All right. Would you please proceed to read your statement?

A Yes. Lake of the Woods is a combination residential and recreational community. Some of the landowners there have built homes which they use primarily on weekends. Others have built homes in which they reside on a full time basis.

Some of the full time residents are still employed and commute between Lake of the Woods and their places of employment in the general area. Others are retired persons, as I am. I feel sure that some of the retired residents of Lake of the Woods enjoy substantial incomes. On the other hand, there are many of us who live on fixed incomes of limited size.

I personally find my own retirement income barely adequate to meet my expenses.

My working years were spent in the employment of the Western Electric Company from which I retired in 1975, at which time I took up residence at Lake of the Woods. My pension has no built-in adjustment for inflation and, as a consequence, I am forced to limit carefully the money that my wife and I spend.

My home is mortgaged and the monthly payments made thereon, together with the rising cost of living, have put a real strain upon my budget. I frankly doubt that I can continue living at Lake of the Woods if I am forced to pay forty dollars a month for sewerage charges. Even the twenty-four dollars a month sewerage charges,

which have been approved on an interim basis, will be a burdensome payment for me to make.

Property values at Lake of the Woods have not increased as much as they have in urban centers during the past several years. I cannot help but believe that if the sewerage charge at Lake of the Woods is permitted to remain at twenty-four dollars per month, let alone rise to forty dollars per month, property values will fall. If that happens, I will be doubly injured.

Not only will my ability to continue living at Lake of the Woods be threatened, but also my ability to sell my present home without suffering a real financial sacrifice will be impaired.

I realize that no privately financed corporation such as Lake of the Woods Utility Company can be expected to provide a public service at a loss. On the other hand, I believe that it is incumbent upon any such company to conduct its operations in the most efficient and economical manner possible.

If the LOW Utility Company has been doing that and still suffers an operating loss, then I suppose an increase in its charges is inevitable.

If it has not been conducting its operations efficiently and economically, I believe it should be required to do so before making any increase in its charges to its customers.

BRENDA McCALL, a witness called by and on behalf of the Protestants, having first been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. SOMERVILLE:

Q Please state your name and residence.

A My name is Brenda McCall. I live at 600 Monticello Circle, Lake of the Woods.

Q I believe you are over eighteen?

A Oh, yes.

Q Would you proceed to read your statement?

A Yes, sir. It is my understanding that there are a number of people like myself, living at Lake of the Woods who live on a fixed income, an income which is not large. Like myself, they built or bought in Lake of the Woods in order to be able to live within that income in a reasonable and dignified manner.

If the increase in the sewer rates proposed by the Lake of the Woods Utility Company is

allo ed to go through, people like myself will not be able to continue to live there.

I don't know if my arithmetic is correct, but it seems to me that it is approximately a four hundred percent increase. It also seems incredible that anyone could believe that such a huge increase could be justified in the light of the present rate of inflation which I think is around thirteen percent.

I could not afford to pay it, and I wonder whether, under such an extremity, I would even be able to sell my house should that action be necessary. Who would want to buy where such exorbitant costs exist?

The prospect is very frightening. Unable to live in Lake of the Woods and yet unable to sell and get out, too. The alternative would be the loss of everything.

To people like myself, therefore, granting such a huge increase in the cost of sewer maintenance would be a disaster.

I am a retiree; I built my house in order to have a decent, reasonable-costing, secure place to live when I retired. Presently I

get by without much left over, but without having to go into debt and without having to ask help from anyone. That would not be the case if this huge increase is allowed.

Please consider carefully the effect of such action on people like me, myself.

ALBIN L. LINDALL, a witness called by and on behalf of the Protestants, having first been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. SOMERVILLE:

Q Please state your name and residence.

A I am Albin L. Lindall, age fifty-eight, Birchside Circle, Lake of the Woods.

Q Mr. Lindall, I believe you have been living at Lake of the Woods since the beginning, haven't you?

A Yes, sir. I am a charter member.

Q All right, sir. What is your educational and occupational background?

A I am a war graduate of the Virginia Military Institute and obtained a B.A. degree from George Washington University. And I presently am in the real estate business.

Q You stated you are in the real estate business. Can you tell us exactly what your business is?

A Yes. I have a broker's license in real estate from the State of Virginia. I've held that the last five years. I had a real estate salesman's license before that, yes, for ten years.

I belong to the Piedmont Board of Realtors, which includes the Orange County and Lake of the Woods. I belong to the Virginia Association of Realtors and the National Association of Realtors.

Q How long have you been active in the real estate field in the Lake of the Woods area?

A I've been active in Lake of the Woods since 1968. I didn't actually open up my office until 1975.

Q So you have observed the growth and development of the community?

A Yes, sir, I have.

Q Based on your experience and your situation, are you in a position to offer some opinion as to what the increase might do to any further development?

A Yes, sir. I feel like I am.

My principal concern with the proposal of the Lake of the Woods Utility Company to increase drastically the sewer charges is -- the effect it will have on the growth of the Lake of the Woods community, and upon the value of the real estate there.

As other witnesses have testified, only about one-fifth of the residential lots in the community have buildings upon them. There is, therefore, plenty of room for growth. About seventy new homes have been built each year. The market for existing homes have been quite active. There are a good many retired persons in the Lake of the Woods, and as to be expected, physical incapacitations and mortalities have made necessary the sale of a good many of existing homes.

A ready market for such homes is essential to the willingness of retired and aging people to continue living on property which they own. Up until now, that market has been a good one and my office has participated in the selling and buying of a large number of such homes, as well as

large number of undeveloped lands in the community.

When the Lake of the Woods Utility Company announced the proposed increases in the charges for sewerage service, there was an immediate effect upon the saleability of property at Lake of the Woods. We felt, in our office, compelled to advise prospective purchasers of that announcement and we did so.

Several prospective purchasers of lots upon which they intended to build declined to go forward with their negotiations and there has certainly been a very dampening effect upon the sale of homes. That is by no means surprising when consideration is given to the fact that most propsective purchasers of real estate look at the cost of ownership, including taxes and public utility services. The sewerage charges proposed would, I believe, exceed the cost of taxes on every bit of property within the Lake of the Woods community and in some instances would be more than double the -- I heard today that there are some that have tripled.

If the interim increase in the sewerage charges, which amounts to an increase of two hundred percent, is not rolled back, I believe there will be a decline in the rate of growth of the Lake of the Woods community.

I also think that the interim increase will have a depressing effect upon the saleability of the existing homes. If the proposed four hundred percent increase in the sewerage charge is permitted to become effective, the suppression of construction and sales will be very much greater.

That is all I have to say.

MR. RIELY: No questions.

HEARING EXAMINER: So you mention the point about taxes, and the fact that your rates may exceed the taxes, or will according to your calculations. The development is located in Orange County?

WITNESS LINDALL: Yes, sir, it is.

HEARING EXAMINER: Do they assess property at a hundred percent of fair market value?

WITNESS LINDALL: Yes, sir; they do.

HEARING EXAMINER: And they tax at that rate also?

WITNESS LINDALL: Yes, sir. The average tax would probably be in the vicinity of -- this is a guess -- two hundred to three hundred dollars a year.

GEORGE P. BEARD, JR.,

a witness introduced on behalf of the Protestants, being first duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. SOMERVILLE

Q Please state Your name, age, and residence.

A George P. Beard, Jr., 59, Culpeper, Virginia.

Q I believe you are connected with the Second National Bank of Culpeper.

A That is correct.

Q What is your position with that bank.

A I am Chairman of the Board.

Q How long have you been with the Bank?

A Since 1941; thirty-nine years.

Q And I believe you were formally President of the Bank?

A Former President, yes, sir. Bookkeeper, teller, most anything they had there.

Q Has your bank been involved in financing of homes at Lake of the Woods?

A Yes, sir, Mr. Somerville. As I remember, in 1967, I believe it was, when the Boise Cascade people started this project, we were approached about financing some lots in the area. This, of course, is in our adjoining county. We are reluctant to go over the county line, but apparently they approached all the banks in the area, knowing -- being a native of the area, born and raised in Culpeper, and as flat as it was, I questioned the perkilation of this land. So low and behold, the Orange County Review came out with a headline saying that the land at the Lake of the Woods would not perk. So instead of not touching this one with a ten foot pole, we decided to go to a twenty foot pole, and we didn't have to finance any lots whatsoever to Lake of the Woods at the time.

When we found out several years

later that the utility company was coming in, we became a little more interested. Then we were reluctant, because we found out even though you had no building there, you had to pay a monthly sewer fee for unimproved land. So we waited until the '70s and got into it a little bit better and in 1975 we went into it at great length.

We had financed several homes at Lake of the Woods. We based our loans on the income of the people. The assessment at Lake of the Woods is lower than it is in Culpeper, and the real estate taxes, and it sounded like a pretty good deal.

In the late 1975, we certainly had a surge of Culpeper people wanting to move to Lake of the Woods, to start buying their retirement home at an early age, because they could pay for it while they were employed. Now we are concerned because this rate increase, what it is going to do to the present mortgages we have at Lake of

the Woods if foreclosure is to be made. Who is going to buy the houses with this thing starring them in the face?

We are not more relucant to finance houses at Lake of the Woods because of this increase. We check more carefully the income of the buyer. We find out whether or not their retirement income is sufficient to make the purchase, and now when people come to approach us about buying a home in Lake of the Woods, we take a little more pains on the income aspect of it. We have a bank officer who lives there, and we just gave him a wage increase because of the cost of gasoline, but I don't think we are going to give him a wage increase because of the sewer fee.

He is a good man and respect him, but we are concerned about what is going to happen what is already down there in the way of mortgages and what we are going to do for the future.

It is a good community. We are proud of the fact we are in there now. We just recently, financed two construction loans down at Lake of the Woods for a builder down there, but we wouldn't do that

until he showed us he had a permanent take-out, and the people buying the houses had sufficient income to not only pay to build the house, but to pay for increased sewer tap if it comes up.

And I believe I left a letter with you based on our concern.

Q Mr. Beard, prior to the interim rate change, the monthly sewer rate was eight dollars?

A Eight dollars.

Q The interim rate went to twenty-four?

A That is right. That is when we began to take a little closer look. We even recommended some of our widows to go to Lake of the Woods, because their real estate taxes were lower than ours.

Q I have heard your testimony. Did your testimony refer to the twenty-four dollar rate? Or to the forty dollar rate?

A To both. When it went to twenty-four, we began to call in our officers and make a better study of what we were doing, and then when it recently went to about forty, then the officers are on us for good until this thing is over with.

CROSS EXAMINATION

BY MR. RIELY

Q How many mortgages do you have at Lake of the Woods?

A Mr. Riely, nice to see you again.

Q How are you, George?

A I think, Mr. Riely, we have pretty close to a million dollars worth of mortgages.

Appendix A

EXHIBIT TLT-1

THOMAS L. THORPE

Address: 3611 Ocean Pines
Berlin, Maryland 21811

Telephone No. 301/641-3131

PROFESSIONAL EXPERIENCE

May 1979 - Present	Vice President/General Manager, Maryland Marine Utilities, Inc., Vice President/General Manager, Lake of the Woods Utility Company. Responsible for: Maintenance and operation of water and vacuum sewer systems within the individual projects of Ocean Pines and Lake of the Woods with an anticipated total population of 10,000 and 7,000, respectively, including budget preparation, engineering reviews, collection procedure and customer policy.
September 1977 - April 1979	Director of Public Services Department, City of Beverly Hills, California. Department of 150 employees, operating budget of $9 million, capital improvement budget of $14 million. Responsible for: Maintenance of city streets, storm drains, sewers, street trees; provision of water and rubbish collection; municipal building, vehicle, and equipment maintenance; municipal engineering.
January 1974 - September 1977	Water Operations Manager, City of Beverly Hills, California. Municipally-owned Water Department with annual revenue budget of $3.5 million. Responsible for: Design system improvements and pipeline replacements of water system serving 10,800 customers. Administer contracts and establish water rates. Manage operation of two water treatment plants with combined total of 12 mgd.
November 1973 - January 1974	Administrative Assistant with Beverly Hills Water Department. Responsible for: Direct customer service section of municipal water operations including meter reading, billing and collections.

September 1969 - November 1973	Assistant Field Superintendent with Beverly Hills Water Department.
March 1968 - September 1969	Managed own business (C.S.T. Enterprise, an oil and water well service company).
June 1963 - March 1968	Division Manager for Orange County Division, Southern California Water Company serving 6 Orange County cities and unincorporated county areas, 31,000 customers. Responsible for: Operation of three commercial offices employing eight cashier clerks and 31 field employees. Preparation of division budgets, accounting and office procedures within the division, operation reports necessary to file rate adjustment requests to Public Utilities Commission.
January 1954 - June 1963	Operations Superintendent, Southern California Water Company. Responsible for: Maintenance and operation of total system employing 44 persons, including four separate commercial offices serving approximately 27,000 customers.
September 1951 - January 1954	Assistant Superintendent, Southern California Water Company, serving 27,000 customers. Responsible for: Supervision of 31 employees; in charge of pipeline crews as well as system operation.
August 1947 - September 1951	District Foreman, Southern California Water Company, for Gardena, serving 11,000 customers. Responsible for: Supervision of 16 employees to operate and maintain water supply system including pumping, purification and water treatment plants.
October 1946 - August 1947	Serviceman, Southern California Water Company, Los Angeles.

POLITICAL EXPERIENCE

1957 - 1961	City Councilman, City of Lawndale, California. Part-time position, served on City Engineering and Planning Committee.
1962 - 1963	Mayor, City of Lawndale, California. Part-time position. Major projects: Obtaining County money for widening two major arteriials; construction of two city-owned parks and recreational facilities.

EDUCATION

1964	Completed two-year course in Business Administration and Management at Orange State College (formerly Fullerton College).
1969	UCLA Extension Course - Management by Objectives
1971	UCLA Extension Course - Communication in Management
1971	State Department of Public Health - Public Health Aspects of Domestic Water Supplies (two courses)

MILITARY SERVICE

1940 - 1946	Enlisted in the U. S. Coast Guard - received an Honorable Discharge as Chief Machinist Mate.

PROFESSIONAL ORGANIZATIONS	American Public Works Association American Water Works Association Southern California Utilities Association

379

EXHIBIT RLF-2

Exhibit RLF

Statement 1

LAKE OF THE WOODS UTILITY COMPANY

Total Company Operations

Rate of Return Statement
December 31, 1979

	Per Books	Company Adjustments	After Company Adjustments	Effect Of Company Proposed Interim Rates	After Effect Of Company Proposed Interim Rates	Effect Of Company Proposed $40 Rates	After Effect Of Company Proposed $40 Rates
	1	2	3	4	5	6	7
Operating Revenues	$ 484,208	$ 1,862	$ 486,070	$ 147,648	$ 633,718	$ 295,296	$ 781,366
Operating Revenue Deductions							
Operation and Maintenance	449,274	31,786	481,060	7,000	488,060	7,000	488,060
Depreciation	125,184	2,227	127,411	-	127,411	-	127,411
Amortization Expense	3,688	-	3,688	-	3,688	-	3,688
Taxes, Other Than Income	37,323	58	37,381	4,614	41,995	9,228	46,609
Income Taxes	-	-	-	-	-	-	-
Total	$ 615,469	$ 34,071	$ 649,540	$ 11,614	$ 661,154	$ 16,228	$ 665,768
Net Operating Income (Loss)	$(131,261)	$(32,209)	$(163,470)	$ 136,034	$(27,436)	$ 279,068	$ 115,598
Net Utility Plant and Allowances	$ 2,409,445	$ ---	$ 2,409,445	$ ---	$ 2,409,445	$ ---	$ 2,409,445
Rate of Return	---%		---%		---%		4.8%

Exhibit RLF-

Statement 2

LAKE OF THE WOODS UTILITY COMPANY

Sewer Operations

Rate of Return Statement
December 31, 1979

	Per Books	Company Adjustments	After Company Adjustments	Effect Of Company Proposed Interim Rates	After Effect Of Company Proposed Interim Rates	Effect Of Company Proposed $40 Rates	After Effect Of Company Proposed $40 Rates
	1	2	3	4	5	6	7
Operating Revenues	$ 252,086	$ 1,785	$ 253,871	$ 147,648	$ 401,519	$ 295,296	$ 549,167
Operating Revenue Deductions							
Operation and Maintenance	331,876	29,062	360,938	7,000	367,938	7,000	367,938
Depreciation	95,975	2,047	98,022	-	98,022	-	98,022
Amortization Expense	1,844	-	1,844	-	1,844	-	1,844
Taxes, Other Than Income	28,089	56	28,145	4,614	32,759	9,228	37,373
Income Taxes	-	-	-	-	-	-	-
TOTAL	$ 457,784	$ 31,165	$ 488,949	$ 11,614	$ 500,563	$ 16,228	$ 505,177
Net Operating Income (Loss)	$(205,698)	$(29,380)	$(235,078)	$ 136,034	$(99,044)	$ 279,068	$ 43,990
Net Utility Plant and Allowances	$ 1,865,733	$ ---	$ 1,865,733	$ ---	$ 1,865,733	$ ---	$ 1,865,733
Rate of Return	---%		---%		---%		2.36%

Exhibit RLF -

Statement 3

LAKE OF THE WOODS UTILITY COMPANY

Water Operations

Rate of Return Statement
December 31, 1979

	Per Books	Company Adjustments	After Company Adjustments	Effect Of Company Proposed Interim Rates	After Effect Of Company Proposed Interim Rates	Effect Of Company Proposed $40 Rates	After Effect Of Company Proposed $40 Rates
	1	2	3	4	5	6	7
Operating Revenues	$ 232,122	$ 77	$ 232,199	$ -	$ 232,199	$ -	$ 232,199
Operating Revenue Deductions							
Operation and Maintenance	117,398	2,724	120,122	-	120,122	-	120,122
Depreciation	29,209	180	29,389	-	29,389	-	29,389
Amortization Expense	1,844	-	1,844	-	1,844	-	1,844
Taxes, Other Than Income	9,234	2	9,236	-	9,236	-	9,236
Income Taxes	-	-	-	-	-	-	-
TOTAL	$ 157,685	$ 2,906	$ 160,591	$ -	$ 160,591	$ -	$ 160,591
Net Operating Income (Loss)	$ 74,437	$(2,829)	$ 71,608	$ -	$ 71,608	$ -	$ 71,608
Net Utility Plant and Allowances	$ 543,712	$ ---	$ 543,712	$ ---	$ 543,712	$ ---	$ 543,712
Rate of Return	13.69%		13.17%		13.17%		13.17%

LAKE OF THE WOODS UTILITY COMPANY

Schedule Of Company Adjustments
December 31, 1979

Sewer Operations	
Revenues:	
Revenues resulting from use of 12-31-79 customers for full year revenue calculations	$ 1,785
Total Adjustment	$ 1,785
Operation and Maintenance:	
Annualization of payroll cost increase which was effective 4-1-79	$ 2,032
Increase in employee payroll taxes, and insurance due to annualization of payroll cost	$ 447
Annualization of additional power costs due to Virginia Electric Co-op rate increase on October 1, 1979	$ 26,583
Total Adjustment	$29,062
Depreciation Expnese:	
Increase due to recalculating depreciation expense on plant balances at 12-31-79	$ 2,047
Total Adjustment	$ 2,047
Taxes Other Than Income:	
Increase in gross receipts tax due to adjusted revenues	$ 56
Total Adjustment	$ 56
Effect Of Company Proposed Rates	
Revenues:	
Sewer revenue increase due to applying company proposed rates to 12-31-79 customers	$ 295,296
Operation and Maintenance:	
Increase in expenses to cover the costs of this filing amortized over 4 (four) years	$ 7,000
Taxes, Other Than Income:	
Increase in gross receipts tax due to proposed revenue increase	$ 9,228
Water Operations	
Revenues:	
Revenues resulting from using 12-31-79 customers for full year revenue calculations	$ 77
Total Adjustment	$ 77

LAKE OF THE WOODS UTILITY COMPANY

Schedule Of Company Adjustments
December 31, 1979

Water Operations (con't.)

Operation and Maintenance:	
Annualization of payroll cost increase which was effective 4-1-79	$ 432
Increase in employee payroll taxes, insurance and pensions due to annualization of payroll increase	95
Annualization of additional power costs due to Virginia Electric Co-Op rate increase on October 1, 1979	$ 2,197
Total Adjustment	$ 2,724
Depreciation Expense:	
Increase due to recalculating depreciation expense on plant balances at 12-31-79	$ 180
Total Adjustment	$ 180
Taxes, Other Than Income:	
Increase in gross receipts tax due to adjusted revenue	$ 2
Total Adjustment	$ 2

Exhibit RLF -

Statement 5

LAKE OF THE WOODS UTILITY COMPANY

Balance Sheet
12-31-79

ASSETS AND OTHER DEBITS	
Utility Plant in Service	$ 4,026,768
Construction in Progress	767
Less:	
Utility Plant Acquisition Adjustment	90,579
Accumulated Depreciation	684,394
	$ 774,973
Net Utility Plant	$ 3,252,562
Current and Accrued Assets	
Cash and Working Funds	$ 13,596
Customer Accounts Receivable, Net of $247,310 Allowance for Uncollectables	140,941
Other Accounts Receivable	509
Materials and Supplies Inventory	192,662
Prepayments	325
	$ 348,033
Deferred Debits	
Other Deferred Debits - Rate Case	$ 1,981
Total Assets and Other Debits	$ 3,602,576

LIABILITIES AND OTHER CREDITS	
Stockholders Equity	
Common Stock	$ 10,000
Retained Earnings - Deficit	(623,915)
	$(613,915)
Current and Accrued Liabilities	
Notes Payable	$ 2,402,702
Payables to Associated Companies	123,323
Accounts Payable - Trade	251
Taxes Accrued	1,867
Interest Accrued	583,477
Other Current and Accrued Liabilities	20,623
	$ 3,132,243
Contributions in Aid of Construction	$ 1,084,248
Total Liabilities and Other Credits	$ 3,602,576

385

Exhibit RLF-

Statement 6

LAKE OF THE WOODS UTILITY COMPANY

Net Utility Plant and Allowances
December 31, 1979

	Sewer	Water	Total
Utility Plant in Service	$ 3,030,482	$ 996,286	$ 4,026,768
Less: Accumulated Depreciation	490,858	193,536	684,394
Contributions in Aid	802,344	281,904	1,084,248
Unamortized Acquisition Adjustment	90,579	-	90,579
Net Utility Plant	$ 1,646,701	$ 520,846	$ 2,167,547
Plus: Material and Supplies Inventory	182,662	10,000	192,662
Working Capital (40 days oper. exp.)	36,370	12,866	49,236
Net Utility Plant and Allowances	$ 1,865,733	$ 543,712	$ 2,409,445

Statement 7
(Revised)

LAKE OF THE WOODS UTILITY COMPANY

COMPARATIVE FINANCIAL RESULTS

	8 Months Ended 8/31/80 (Actual)	12 Months Ending 12/31/80 (Projected $24 per month sewer)*	12 Months Ending 12/31/80 (Projected $40 per month sewer)**	12 Months Ended 12/31/79 (Actual)
Operating Revenues:	$ 345,762	$ 652,872	$ 806,472	$ 484,207
Operative Revenue Deductions:				
Operation and Maintenance				
Labor	65,346	98,019	98,019	86,948
Power	94,280	141,420	141,420	108,351
Other O & M	102,354	153,532	153,532	124,429
Total	$ 261,980	$ 392,971	$ 392,971	$ 319,728
Administrative and General	98,681	148,023	148,023	138,812
Depreciation, taxes and other expenses	110,736	170,905	175,705	156,928
Net Operating Income (loss)	$(125,635)	$(59,027)	$ 89,773	$(131,261)

* Revenues are annualized using $24/month sewer rate.

** Revenues are annualized using $40/month sewer rate.

Exhibit No. SFL-3
Witness: Leis
Schedule A to
Statement I
Page 1 of 3

LAKE OF THE WOODS UTILITY COMPANY

Explanation of Adjustments Appearing in Column (4) of Statement I

Adjustment Number	Explanation	Amount
	Operating Revenues	
1	To annualize revenues based on number of customers at December 31, 1979. (See Statement II)	$ 1,551
	Operating Revenue Deductions Operations and Maintenance	
2	To annualize an 8% salaries and wages increase effective April 1, 1979 net of Rick Trenary's applicable salary	$ 1,831
3	To increase employee pensions and payroll taxes associated with pay raises effective April 1, 1979.	403
4	To annualize a power increase by Virginia Electric CO-OP on October 1, 1979. (Company projection)	27,929
5	To amortize $\frac{1}{4}$ of Company's rate case expense. Rate Case Expense: $\frac{\$28,000}{4 \text{ yrs}}$ = $7,000-$2,971 (expensed)	4,029
6	To adjust management fee per affiliate agreement.	(492)
7	To decrease outside services for amounts paid to F. L. Atkins - consultant, considered non-recurring for ratemaking purposes.	(5,942)
8	To decrease injuries and damages to a three year average using 1977 thru 1979.	(436)
9	To amortize outside services (legal fees) over a three year period due to litigation between Company and customer (Gay) resulting in a $1,000 damage claim to the customer.	(1,641)
10	To decrease uncollectible sewer accounts to a nominal 1% rate of gross annual revenue.	(21,403)

Exhibit No. SFL-3
Witness: Leis
Schedule A to
Statement I
Page 2 of 3

LAKE OF THE WOODS UTILITY COMPANY

Explanation of Adjustments Appearing in Column (4) of Statement I

Adjustment Number	Explanation	Amount
	Operating Revenue Deductions Operations and Maintenance (Cont'd)	
11	To increase uncollectible sewer accounts to nominal 1% rate on the above revenue adjustment (Adjustment No. 1).	$ 16
12	To decrease maintenance expenses for amounts determined by the staff to be capital items.	(6,094)
		$ (1,800)
	Depreciation	
13	To adjust depreciation expense to a 3% composite rate on the 12/31/79 balances of non-contributed property.	$(32,100)
	Taxes Other Than Federal Income Taxes	
14	To adjust for gross receipts taxes applicable to revenue adjustment no. 1 ($1,551 x 1.225%)	$ 19
15	To increase gross receipts taxes due to a decrease booked during the test period, but applicable to a prior period.	666
	Adjustments to 1978 (January 1979 $ 529.14; April 1979 751.76) = $1,280.90; Sewer Percentage x 52% = $ 666	
16	To decrease real estate taxes for an amount that was erroneously booked twice during the test period.	(266)
		$ 419
	Utility Plant Utility Plant in Service	
17	To increase utility plant for amounts expensed during the test period that should have been capitalized.	$ 6,094

Exhibit No. SFL-3
Witness: Leis
Schedule A to
Statement I
Page 3 of 3

LAKE OF THE WOODS UTILITY COMPANY

Explanation of Adjustments Appearing in Column (4) of Statement I

Adjustment Number	Explanation	Amount
	Accumulated Depreciation	
18	To adjust accumulated depreciation to a 3% composite rate on non-contributed property.	$(101,982)
	Contributions in Aid of Construction	
19	To decrease contributions per books, based on the amount that was included in case no. 19867 and the additions thru December 31, 1979.	$ (3,233)
	Allowances for Working Capital	
20	To decrease allowances pertaining to the total O & M expense adjustment.	$ (200)

( ) Denotes Negative Amount

Exhibit No. SFL-3
Witness: Leis
Schedule B to
Statement I

LAKE OF THE WOODS UTILITY COMPANY

Explanation of Adjustments Appearing in Column (6) of Statement I

Adjustment Number	Explanation	Amount
	Operating Revenues	
1	To reflect the estimated increase in annual revenues from the company's proposed rates.	$295,296
	Operating Revenue Deductions	
	Operation and Maintenance	
2	To increase uncollectible accounts - sewer for a nominal 1% rate on the above revenue adjustment.	$ 2,953
	Taxes Other Than Federal Income Taxes	
3	To adjust for gross receipts taxes applicable to adjustment No. 1 less No. 2.	$ 6,418

adjustment No. 1		$295,296
less: adjustment No. 2		2,953
		$292,343
special tax		x .1%
		$ 292
gross receipts	$100,000	
first $100,000	x 1.125%	1,125
1980 rate on balance	$192,343 x 2.6%	5,001
		$ 6,418

	Allowances for Working Capital	
4	To increase allowances for working capital by the amount pertaining to adjustment No. 2.	
	40/360 days X $2,953	$ 328

Exhibit No. SFL-3
Witness: Leis
Statement I

LAKE OF THE WOODS UTILITY COMPANY

Rate of Return Statement
For 12 Months Ended December 31, 1979

	Total Company Per Books Col. (1)	Water Department Col. (2)	Sewer Department Col. (3)	SCC Staff Adjustments Col. (4)	After SCC Staff Adjustments Col. (5)	Effect of Company's Proposed Rates Col. (6)	After Effect of Company's Proposed Rates Col. (7)
Operating Revenues	$ 484,207	$232,122	$ 252,085	$ 1,551	$ 253,636	$295,296	$ 548,932
Operating Revenue Deductions							
Operation and Maintenance Expenses	$ 449,274	$117,398	$ 331,876	$ (1,800)	$ 330,076	$ 2,953	$ 333,029
Depreciation and Amortization	128,872	31,053	97,819	(32,100)	65,719		65,719
Taxes Other Than Federal Income Taxes	37,323	9,234	28,089	419	28,508	6,418	34,926
Federal Income Taxes	-	-	-		-		-
Total Operating Revenue Deductions	$ 615,469	$157,685	$ 457,784	$ (33,481)	$ 424,303	$ 9,371	$ 433,674
Net Operating Income (Loss)	$ (131,262)	$ 74,437	$ (205.699)	$ 35,032	$ (170,667)	$285,925	$ 115,258
Utility Plant							
Utility Plant in Service	$4,026,768	$996,286	$3,030,482	$ 6,094	$3,036,576		$3,036,576
Construction Work in Progress	767	-	767		767		767
Less: Accumulated Provision for Dep.	684,394	193,536	490,858	(101,982)	388,876		388,876
Acquisition Adjustment	90,579	-	90,579		90,579		90,579
Contributions in Aid of Const.	1,084,248	281,904	802,344	(3,233)	799,111		799,111
Net Utility Plant	$2,168,314	$520,846	$1,647,468	$ 111,309	$1,758,777		$1,758,777
Plus: Allowances for Working Capital (Approx. 40 days of O&M Expenses)	$ 49,919	$ 13,044	$ 36,875	$ (200)	$ 36,675	$ 328	$ 37,003
Materials and Supplies	192,662	8,607	184,055		184,055		184,055
Net Utility Plant and Allowances	$2,410,895	$542,497	$1,868,398	$ 111,109	$1,979,507	$ 328	$1,979,835
Rate of Return	-0-	13.72%	-0-		-0-		5.82%

( ) Denotes Negative Amount

Exhibit No. SFL-3
Witness: Leis
Statement II

LAKE OF THE WOODS UTILITY COMPANY

Sewer Department
Schedule of Proposed Increase in Annual Revenues

	Number of Customers at 12-31-79	Present Annual Rates	Present Annual Revenues	Proposed Annual Rates	Proposed Annual Revenues	Increase In Annual Revenues
Usage						
Residential	745	$96.00	$ 71,520	$480.00	$357,600	$286,080
Commercial	24	96.00	2,304	480.00	11,520	9,216
Availability	3,523	45.00	158,535	45.00	158,535	-0-
Penalties						
Usage			523		523	-0-
Availability			20,754		20,754	-0-
Total	4,292		$253,636		$548,932	$295,296

Exhibit No. SFL-3
Witness: Leis
Statement III

LAKE OF THE WOODS UTILITY COMPANY

Income Statement - Per Books
For the Year Ended December 31, 1979

Operating Revenues		$ 484,207
Operating Revenue Deductions		
Operation and Maintenance Expenses	$449,274	
Depreciation and Amortization Expenses	128,872	
Taxes Other than Income Taxes	37,323	
Total Operating Revenue Deductions		615,469
Net Operating Income (Loss)		$(131,262)
Other Income Deductions		
Interest on Long-Term Debt	$192,216	
Interest on Debt to Associated Companies	6,402	
Other Interest Expenses	192	
Total Other Deductions		198,810
Extraordinary Income		127,876
Net Income (Loss)		$(202,196)

( ) Denotes Negative Amount

Exhibit No. SFL-3
Witness: Leis
Statement IV

LAKE OF THE WOODS UTILITY COMPANY

Balance Sheet - Per Books
At December 31, 1979

ASSETS AND OTHER DEBITS

Utility Plant		
Utility Plant in Service	$4,026,768	
Construction Work In Progress	767	
Less: Accumulated Depreciation	684,394	
Less: Acquisition Adjustment	90,579	
Net Utility Plant		$3,252,562
Current and Accrued Assets		
Cash	$ 13,596	
Accounts Receivable - Customer (Net)	140,941	
Accounts Receivable - Other	509	
Materials and Supplies	192,662	
Prepayments	325	
Total Current and Accrued Assets		348,033
Deferred Debits		
Other Deferred Debits - Rate Case		1,981
TOTAL ASSETS AND OTHER DEBITS		$3,602,576

LIABILITIES AND OTHER CREDITS

Equity Capital		
Common Stock	$ 10,000	
Retained Earnings (deficit)	(623,915)	
Total Equity Capital		$ (613,915)
Current and Accrued Liabilities		
Notes Payable (8.0% Payable to BCHL)	$2,402,702	
Accounts Payable - Trade	251	
Payables to Associated Companies	123,323	
Accrued Taxes	1,867	
Accrued Interest	583,477	
Other Current and Accrued Liabilities	20,623	
Total Current and Accrued Liabilities		3,132,243
Contributions in Aid of Construction		1,084,248
TOTAL LIABILITIES AND OTHER CREDITS		$3,602,576

( ) Denotes Negative Amount

Chart
Alan L. Potter

EXHIBIT ALP-4

CHART

FROM WASHINGTON POST

September 28, 1980

COST/YEAR

COST OF WATER AND SEWER SERVICES

	Water	Sewer	Total
Rockville, Maryland	$68.80	$ 97.60	$166.40
Bowie, Maryland	$96.00	$120.00	$216.00
Arlington, Virginia	$67.20	$101.60	$168.80
Alexandria, Virginia	$99.36	$ 73.20	$172.56
Fairfax County, Virginia	$69.00	$112.80	$181.80
Falls Church, Virginia	$78.80	$120.00	$198.80
Fairfax City, Virginia	$78.67	$188.80	$267.47

Above figures are cost for the normal family of four using 80,000 gallons of water a year. Local taxes and service charges are included.

EXHIBIT WWC-5

STATEMENT #1
WILLIAM W. CARPENTER

LAKE OF THE WOODS UTILITY COMPANY
TOTAL COMPANY OPERATIONS
TWELVE MONTHS ENDED DECEMBER 31, 1979

	Per Company Books	Less Adjustments	After Effect of Adjustments
Operating Revenues	484,208		484,208
Operating Revenues Deductions:			
Operations & Maintenance	449,274	86,598	362,676
Depreciation	125,184	32,527	92,657
Amortization Expenses	3,688		3,688
Taxes, Other than Income	37,323		37,323
Income Taxes	--		
Total Deductions	615,469	119,125	496,344
Net Operating Income (Loss)	(131,261)	119,125	(12,136)

STATEMENT #1
WILLIAM W. CARPENTER

LAKE OF THE WOODS ASSOCIATION, INC.

Schedule of Adjustments to
Lake of the Woods Utility Company Statement
For Twelve Months Ended December 31, 1979

OPERATIONS AND MAINTENANCE		$86,598
1. Provision for Uncollectable Accounts This item eliminated as the Reserve for Uncollectable Accounts as of December 31, 1978 amounted to 60% of total Customer Accounts Receivable. Good accounting practice should limit the Reserve for Uncollectable Receivables to no more than 25%.	$49,091	
2. Management Fee This item eliminated as the management fee is being charged by the parent company located in Santa Barbara, California. The personnel from the parent company are rarely seen at Lake of the Woods and there is no evidence of any management services being rendered but is the normal relationship of a parent company with a subsidiary	$22,507	
3. Engineering Consulting Fee This item eliminated as the consulting firm receiving the fee is located in Santa Monica, California. The personnel from the consulting firm are seldom seen at Lake of the Woods with little evidence of consulting services being rendered.	$15,000	
DEPRECIATION		$32,527
Depreciation was taken on the total cost of the utility plant whereas no depreciation should have been taken on contributions to construction of $1,084,248 as of December 31, 1979.		

STATEMENT #2
WILLIAM W. CARPENTER

LAKE OF THE WOODS UTILITY COMPANY
PROJECTED FINANCIAL RESULTS FOR
TWELVE MONTHS ENDING DECEMBER 31, 1980

	Projected at Current Rates per Company	Less Adjustments	After Effect of Adjustments
Operating Revenues	499,700		499,700
Operating Revenue Deductions:			
Labor	98,019		98,019
Power	141,420		141,420
Other Operations and Maintenance	153,532	49,091	104,441
Total	392,971	49,091	343,880
General and Administrative	148,023	42,175	105,848
Depreciation, Taxes and Other Expenses	170,905	39,720	131,185
Total Deductions	711,899	130,986	580,913
Net Operating Income (Loss)	(212,199)	130,986	(81,213)

STATEMENT #2
WILLIAM W. CARPENTER

LAKE OF THE WOODS ASSOCIATION, INC.

Schedule of Adjustments to Lake of the Woods
Utility Company Statement of Projected Financial
Results for Twelve Months Ending December 31, 1980

The Operating Revenues have been restated to show total revenue on the basis of the present $8.00 per month rate for sewer rather than $24.00 per month proposed. This is done to reflect better the effect of the adjustments recommended by Lake of the Woods Association, Inc. on the total company operations.

Provision for Uncollectable Accounts The 1979 figure is used as the amount the company would use for 1980 is not known.		$49,091
General and Administration:		$42,175
Management Fee The 1980 Management Fee is projected from the actual total through July 31, 1980	$27,175	
Engineering Consulting Fee	$15,000	
Depreciation and Taxes:		$39,720
Depreciation The depreciation on contributions to construction is calculated at 3% annually on the connection fees amounting to $1,164,000 charged for the 800 homes the company used in its calculations	$34,920	
Taxes, Other than Income This represents the gross receipts tax included by the company in its calculation of the increase in revenue from the proposed $24.00 per month for sewer based on 800 customers used by the company.	$ 4,800	

Lake of the Woods Utility Company
Schedule of Gross Revenue and Uncollectible Accounts Expense
for the years 1975 - 1979

	1975	1976	1977	1978	1979
Gross Revenues					
Water	NA	$ 214,364	$ 218,420	$ 221,706	$ 232,122
Sewer	NA	119,954	159,896	241,573	252,086
Total	$ 91,479(1)	$ 334,318	$ 378,316	$ 463,279	$ 484,208
Uncollectible Accounts Expense					
Water	NA	$ 36,967	$ 35,743	$ 34,915	$ 25,168
Sewer	NA	18,617	23,095	33,024	23,924
Total	$ 15,857(1)	$ 55,584	$ 58,838	$ 67,939	$ 49,092
Balance of Reserve for Uncollectible Accounts	$ 15,857	$ 71,441	$ 130,279	$ 198,218	$ 247,310
1% of Gross Revenues					
Water	$ NA	$ 2,144	$ 2,184	$ 2,217	$ 2,321
Sewer	NA	1,199	1,599	2,416	2,521
Total	$ 915	$ 3,343	$ 3,783	$ 4,633	$ 4,842
Excess Expense Taken					
Water	NA	$ 34,823	$ 33,559	$ 32,698	$ 22,847
Sewer	NA	17,418	21,496	30,608	21,403
Total	$ 14,942	$ 52,241	$ 55,055	$ 63,306	$ 44,250

(1) The utility company's report to the State Corporation Commission for 1975 shows one total for gross revenues for combined water and sewer operations.

In accordance with the State Corporation Commission's policy of permitting up to 1% of annual gross revenues as an expense for uncollectible accounts the above schedule was prepared to show the amounts expensed by the Lake of the Woods Utility Company in excess of this policy for the years 1975-1979. The cumulative total of excess expense for this period amounts to $229,794.

HUNTON & WILLIAMS
707 EAST MAIN STREET P.O. BOX 1535
RICHMOND, VIRGINIA 23212
TELEPHONE 804-788-8200

WACHOVIA BANK BUILDING
P.O. BOX 109
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FIRST VIRGINIA BANK TOWER
101 ST. PAUL'S BOULEVARD
NORFOLK, VIRGINIA 23510
804-625-5501

1919 PENNSYLVANIA AVENUE, N.W.
P.O. BOX 19230
WASHINGTON, D.C. 20036
202-223-8650

FILE NO.

DIRECT DIAL NO. 804 788- 8313

January 9, 1981

Case No. PUE800081 - Lake of the Woods Utility Company

Dear Mr. Farrar:

I apologize for the delay in replying to your letter of November 24, 1980, concerning the case referred to above. The fact is that much correspondence and conversation with people spread from Maryland to California have delayed the collection of the required information. I hope that we are now in a position to supply what you need.

Exhibit 1 enclosed herewith is the entire payroll of the Company for 1979. The total varies slightly from aggregate salaries because the total is stated on an accrual basis while the aggregate is on a cash basis. The total is broken down between amounts charged to expense and capitalized with overhead and benefits (consisting of insurance and taxes) added. There is no pension plan.

Exhibit 2 shows payroll charges of Maryland Maine Utilities, Inc., allocated to Lake of the Woods.

Exhibit 3 shows 1979 payments to C. R. Brockmeier Consultant Engineers.

During the test year, a management fee of $22,507 and interest of $198,618 were accrued but nothing was paid on these amounts.

There is also enclosed a copy of an application being filed by the Company today under the Utility Securities Act and the Utility Affiliaties Act. I believe that this will supply the information requested in the antepenultimate paragraph of your letter.

HUNTON & WILLIAMS

Please let me know if you need further information that the Company can supply.

Yours very truly,

John W. Riely

11/662

Enclosures

Stewart E. Farrar, Esquire
State Corporation Commission
Box 1197
Richmond, Virginia 23209

cc: Kenworth E. Lion, Esquire
Office of the General Counsel
State Corporation Commission
Box 1197
Richmond, Virginia 23209

Eric M. Page, Esquire
Assistant Attorney General
11 South 12th Street
Richmond, Virginia 23219

Atwell W. Somerville, Esquire
Somerville, Moore & Joyner, Ltd.
PO Box 629
Orange, Virginia 22960

bcc: Mr. Lawrence F. Dunn, Jr.
Director of Administration
Transcontinental Development Co.
PO Box 458
Santa Barbara, CA 93102

Mr. Thomas L. Thorpe
Maryland Marine Utilities, Inc.
Route 4, Box 384
Berlin, Maryland 21811

EXHIBIT "1"

LAKE OF THE WOODS UTILITY CO.

Employee Roster

Test Year 1979

Employee	Gross	Work Comp Status at 12/31/79
V. Burgess	$ 3,920.00	E
S. Coleman	7,318.99	E
J. Dyson	9,831.08	E
J. Gibson	3,162.50	E
O. Hansell	4,927.78	E
D. Harris	13,084.00	E
C. Johnson	214.40	E
O. Lee	285.58	E
N. Lewis, Jr.	6,859.97	E
D. Merryman	5,326.63	E
K. Nixon	8,876.97	E
R. Pittman, Jr.	5,487.63	E
J. Steen	294.80	E
W. Stoddard	13,104.34	Term.
L. Thompson	7,006.13	E
M. Toth	5,219.45	E
I. Young	11,245.79	E
R. Trenary	10,842.00	E
S. Boley	4,787.74	Term.
M. Crawford	156.50	Term.
D. Hansen	2,613.80	Term.
G. Nowakoski	5,572.78	Term.
D. Thompson	192.00	Term.
J. White	3,482.30	Term.
J. Williams	21.00	Term.
D. Woolfrey	96.00	Term.
W. Kenny	288.00	Term.

		Overhead 22.47%
Total Payroll	$134,218.16	
Charged to Capital	26,726.68	$ 6,166.85
Charged to Expenses	109,563.50	24,459.29
Total Chgs. Gen. Led.	136,290.18	30,626.14
Maryland Marine Utilities, Inc.		(2,982.30)
Charged to Capital		6,166.85
Work Comp Ins.		1,540.00
Employee Benefits (926)		16,636.73
Company Portion - F.I.C.A.		8,564.52
Virginia - U.C.C.		700.34
Federal - U.C.C.		-0-

PAYROLL CHARGES

From Maryland Marine Utilities, Inc. to Lake of the Woods Utility Co.
Test Year 1979

E. Leech	$ 4,441.75
D. Sigrist	423.48
R. Huntington	738.38
T. Thorpe	7,400.00
Miscellaneous	7.58
Total Payroll	13,011.19
Overhead	2,982.30
Total Payroll and Overhead	$15,993.49

EXHIBIT "3"

PAYMENTS

From Lake of the Woods Utility Co.

To C. R. Brockmeier Consultant Engineers

Test Year 1979

January	$ -0-
February	-0-
March	-0-
April	-0-
May - for Jan., Feb., Mar., Apr.	5,442.89
June	2,879.46
July	3,121.20
August	-0-
September	1,250.00
October	67.40 1,250.00
November	1,250.00
December	1,250.00
Total:	$16,510.95

DOCUMENT CONTROL CENTER

810110293

JAN 13 8 59 AM '81

VIRGINIA

BEFORE THE STATE CORPORATION COMMISSION

APPLICATION OF LAKE OF THE WOODS UTILITY COMPANY, MARYLAND MARINE UTILITIES, INC., TRANSCONTINENTAL DEVELOPMENT CO., and ATPAC LAND CO.	)))))	CASE NO. _____

LAKE OF THE WOODS UTILITY COMPANY (the Company) respectfully shows:

1. The Company is a Virginia public service company providing water and sewer service in the Lake of the Woods Development of Orange County, Virginia. All of its outstanding shares of capital stock are owned by AtPac Land Co. (AtPac), a partnership. AtPac also owns all of the outstanding shares of capital stock of Maryland Marine Utilities, Inc. (MMU), that provides similar services to a development in Maryland.

2. AtPac acquired the stock of the Company from Boise Cascade Home & Land Corporation (Boise) on December 20, 1978. This acquisition was subsequently approved by the Commission in April, 1979. AtPac paid Boise $900,000 in cash for the stock of the Company. The financial position of the Company is such that (a) its revenues do not provide it with an adequate cash flow to enable it to continue in operation and (b) it has no external

source of funds except AtPac. It has, accordingly, asked AtPac to advance it additional funds in order for it to continue its operations. AtPac has agreed to do so, so long as it wishes to do so, if the Company will accrue interest on such advances at the rate of 10% per annum from the date of the advance. This understanding is recorded in a letter agreement appended hereto as Exhibit 1.

3. The Company and Maryland Marine Utilities, Inc. (MMU) are under common management, having the same general manager, controller and other officers. These officers are located at the headquarters of MMU in Berlin, Maryland. The Berlin office provides management, accounting, payroll and data processing services to the Company. The Company proposes to pay for such services on the basis of allocable time actually devoted to the business of the Company plus out-of-pocket expenses. No expenses other than salaries, wages and payroll taxes and benefits will be allocated. These services are to be rendered pursuant to a letter agreement appended hereto as Exhibit 2.

4. The Company requires additional management services and proposes to contract for these services with Transcontinental Development Co. (TDC). The nature of these services is set forth in the letter agreement appended hereto as Exhibit 3 and in the memorandum appended as Exhibit 4. The Company proposes to pay TDC $1,500.00 per month for such services which is less than the cost of rendering the services. TDC is a partnership whose two

partners are Transcontinental Corporation (TC) and Motyko, Inc. (Motyko). The sole shareholder of TC is Ronald F. Boeddeker who is also a general partner of AtPac. The sole stockholder of Motyko is a corporation named Bass Brothers Enterprises, Inc. (BBE) whose stockholders are Sid R. Bass (Sid), Robert M. Bass (Robert), Lee M. Bass (Lee), Edward P. Bass (Edward), and certain trusts established for the children of one or more of them. Sid, Robert, and Lee are also the partners of SRL Enterprises, a partnership which is, in turn, the second partner of AtPac. TDC may, therefore, be held to be an affiliate of the Company.

5. Prior to the acquisition of the stock of the Company from Boise by AtPac, the Company was indebted on open account to Boise in the amount of $2,402,702. This open account indebtedness, at least to the amount of $2,347,280, was authorized by the Commission in Case No. A-592. On December 1, 1978, the Company issued its demand note to Boise in the principal amount of $2,402,702 with interest at the rate of 8% per annum. No approval was obtained from the Commission for the issuance of this note. A copy of the note is appended hereto as Exhibit 5. At the time of the sale of the stock of the Company by Boise to AtPac, the note and the indebtedness represented thereby was sold by Boise, in a related but separate transaction, to Perry R. Bass, Inc. At that time, Perry R. Bass, Inc. (PRB) purchased notes and open accounts (Receivables) of various entities, including the note or open account of the Company. The

Receivables were purchased for cash at a discount from the full face value of the Receivables. There was no allocation of the cash purchase price among the Receivables purchased. PRB subsequently transferred certain undivided interests in the Receivables to Perry R. Bass (Perry), an individual, and to Sid Richardson Carbon and Gasoline Co., a corporation of which Perry is sole stockholder. The stockholders of PRB are Perry (who is the father of Sid, Robert, Lee, and Edward); Dora Neely, an individual; and four trusts established for the benefit of the children of Sid, Robert, Lee, and Edward (Trusts). Although Sid and Robert are co-trustees of these Trusts, neither they nor Lee nor Edward have any beneficial interest in Trusts. Likewise, none of them has any interest in PRB or the Receivables. Conversely, neither PRB nor any other owner of an interest in the Receivables has any interest in AtPac, SRL Enterprises, TDC, Motyko, or BBE. The Company now proposes to issue to Perry R. Bass, Inc., a note identical in words and figures to Exhibit 5 except that it will be payable to Perry R. Bass, Inc., and will omit the endorsement.

The Company therefore requests that the Commission approve the agreements filed herewith as Exhibits 1, 2 and 3 and authorize the issuance of the note referred to in paragraph 5.

Dated November 17, 1980

LAKE OF THE WOODS UTILITY COMPANY

By _____
Vice President

MARYLAND MARINE UTILITIES, INC.

By _____
President

TRANSCONTINENTAL DEVELOPMENT CO.
By Transcontinental Corporation
A general partner

By _____
President

ATPAC LAND CO.

By _____
A general partner

STATE OF Maryland

COUNTY OF Wicomico

I, Susan A. Lankford, a Notary Public in and for the State and County aforesaid, hereby certify that this day appeared before me Thomas L. Thorpe who, being by me duly sworn, made oath and said that he is a Vice President of LAKE OF THE WOODS UTILITY COMPANY and that the facts stated in the above Application are true to the best of his knowledge and belief.

Given under my hand and notarial seal this day of December, 1980. My Commission expires: July 1, 1982

Susan A. Lankford
Notary Public

SUSAN A. LANKFORD NOTARY PUBLIC WICOMICO CO., MARYLAND

STATE OF CALIFORNIA)
)
COUNTY OF SANTA BARBARA)

I, LAURENCE F. DUNN JR., a Notary Public in and for the State and County aforesaid, hereby certify that this day appeared before me RONALD F. BOEDDEKER who, being by me duly sworn, made oath and said that he is a President of MARYLAND MARINE UTILITIES, INC. and that the facts stated in the above Application are true to the best of his knowledge and belief.

Given under my hand and notarial seal this 10th day of December, 1980. My Commission expires: July 5, 1983

OFFICIAL SEAL
Laurence F. Dunn Jr.
NOTARY PUBLIC-CALIFORNIA
PRINCIPAL OFFICE IN
SANTA BARBARA COUNTY
My Commission Expires July 5, 1983

Laurence F. Dunn Jr.
Notary Public

STATE OF CALIFORNIA)
)
COUNTY OF SANTA BARBARA)

I, LAURENCE F. DUNN, JR., a Notary Public in and for the State and County aforesaid, hereby certify that this day appeared before me RONALD F. BOEDDEKER who, being by me duly sworn, made oath and said that he is a President of TRANSCONTINENTAL CORPORATION which is a general partner of TRANSCONTINENTAL DEVELOPMENT CO., a partnership, and that the facts stated in the above Application are true to the best of his knowledge and belief.

Given under my hand and notarial seal this 10th day of December, 1980. My Commission expires: July 5, 1983

OFFICIAL SEAL
Laurence F. Dunn Jr.
NOTARY PUBLIC-CALIFORNIA
PRINCIPAL OFFICE IN
SANTA BARBARA COUNTY
My Commission Expires July 5, 1983

Laurence F. Dunn L.
Notary Public

STATE OF CALIFORNIA)
)
COUNTY OF SANTA BARBARA)

I, LAURENCE F. DUNN, JR., a Notary Public in and for the State and County aforesaid, hereby certify that this day appeared before me RONALD F. BOEDDEKER who, being by me duly sworn, made oath and said that he is a general partner of ATPAC LAND CO., a partnership, and that the facts stated in the above Application are true to the best of his knowledge and belief.

Given under my hand and notarial seal this 10th day of December, 1980. My Commission expires: July 5, 1983

OFFICIAL SEAL
Laurence F. Dunn Jr.
NOTARY PUBLIC-CALIFORNIA
PRINCIPAL OFFICE IN
SANTA BARBARA COUNTY
My Commission Expires July 5, 1983

Laurence F. Dunn L.
Notary Public

"EXHIBIT 1"

Lake Of The Woods Utility Co.

P.O. Box 349
Locust Grove Va. 22508
703-972-2133

413

17 November 1980

Maryland Marine Utilities, Inc.
Route 4, Box 378
Berlin, MD 21811

Gentlemen:

AGREEMENT FOR MANAGEMENT & ADMINISTRATIVE SERVICES.

This letter, when executed and returned by you, will serve as our agreement concerning management and administrative services to be provided by Maryland Marine Utilities, Inc. ("MMU") to this Company.

MMU hereby agrees to provide, on a part-time, as-required basis, general and operational management and administrative services including certain bookkeeping, payroll, and data processing services to Lake of the Woods Utility Company ("LOWU").

LOWU, in consideration of the foregoing, agrees to compensate MMU for such services by paying MMU an amount equal to the percentage of salaries, wages and related payroll taxes and benefits of MMU employees equivalent to the percentage of their compensable time actually devoted to the business of LOWU. In addition to such amounts, LOWU will reimburse MMU for the out-of-pocket expenses of MMU employees while they are engaged in the business of LOWU and for the cost of any materials, supplies, services, or other items paid for by MMU on behalf of LOWU.

This agreement may be terminated by either party on ninety (90) days written notice to the other.

Very truly yours,

LAKE OF THE WOODS UTILITY COMPANY

By _____
Its Vice President

ACCEPTED & AGREED:

MARYLAND MARINE UTILITIES, INC.

By _____
Pres.

"EXHIBIT 2"

ATPAC LAND CO.

414

17 November 1980

Lake Of The Woods Utility Co.
P. O. Box 349
Locust Grove, VA 22508

Gentlemen:

AGREEMENT CONCERNING ADVANCES OF FUNDS

This letter will reconfirm and record our understanding with respect to advances of funds from AtPac Land Co. ("ATPAC") to Lake Of The Woods Utility Co. ("LOWU"). Please execute and return one copy for our files.

ATPAC is the sole stockholder of LOWU, having acquired all the common stock of LOWU pursuant to a purchase agreement dated December 20, 1978, which was approved by the Virginia State Corporation Commission in April, 1979.

It is understood that ATPAC, in its sole discretion and without any obligation to do so, may from time to time advance funds to LOWU on open account in an aggregate amount not in excess of that approved by the Virginia State Corporation Commission. It is further understood that such advances are temporary loans; not permanent investments.

It is agreed that to the extent that such advances have been, or are in the future, made by ATPAC to LOWU, these advances shall bear interest at the rate of 10% per annum on the total amount of such open account advances, computed from date of advance, until such advances are repaid.

Very truly yours,

ATPAC LAND CO.

By _____
Its General Partner

ACCEPTED & AGREED:

LAKE OF THE WOODS UTILITY COMPANY

By _____
Its Vice President

MAILING ADDRESS: P. O. BOX 458, SANTA BARBARA, CALIFORNIA 93102
420 EAST CARRILLO STREET, SANTA BARBARA, CALIFORNIA • TELEPHONE (805) 963-6851
LOS ANGELES • HONOLULU

TRANSCONTINENTAL DEVELOPMENT CO.

17 November 1980

Lake Of The Woods Utility Co.
P. O. Box 349
Locust Grove, VA 22508

Gentlemen:

AGREEMENT FOR MANAGEMENT & ADMINISTRATIVE SERVICES

This letter, when executed and returned by you, will constitute an agreement for management and administrative services to be provided by Transcontinental Development Co. ("TDC") to Lake of the Woods Utility Company ("LOWU").

LOWU is a public service company engaged in the provision of water and sewerage services to the community of Lake of the Woods in Orange County, Virginia. It desires to retain outside management, advisory, and administrative services from TDC to supplement those provided by its own employees and others. TDC has experience in providing such services and desires to provide same to LOWU according to the terms outlined below.

Services To Be Provided. TDC shall provide management, advisory, and administrative services including but not limited to the following: planning and management control; budgeting and financial analysis; advice and assistance in the preparation of reports and other filings with government entities; retention, direction, and coordination of outside professionals and consultants for legal, auditing, engineering, rate making, and other matters; administration of employee benefit programs and casualty and liability insurance programs; other similar services as LOWU may, from time to time, request.

It is understood that the scope of services to be provided by TDC does not include day-to-day operational management, supervision of utility operations, or customer relations.

Fees, Costs, And Expenses. LOWU shall pay to TDC, as reimbursement for the cost of its services, a fixed monthly fee of $1,500.00 which shall cover all regular services rendered by TDC within the scope and intent of this agreement. (Additional or extraordinary services provided by TDC at the specific request of LOWU shall be at additional cost, the amount of which shall be agreed to by LOWU and TDC apart from this agreement.)

...1

MAILING ADDRESS: P. O. BOX 458, SANTA BARBARA, CALIFORNIA 93102
420 EAST CARRILLO STREET, SANTA BARBARA, CALIFORNIA • TELEPHONE (805) 963-6851

Lake Of The Woods Utility Co.
Page 2
17 NOV 1980

In addition to the aforementioned fixed fee, LOWU shall reimburse to TDC, upon receipt of proper request and accounting,

(a) actual or properly allocated direct costs of materials, supplies, services of outside consultants, insurance premiums, etc. incurred by TDC at the request of LOWU pursuant to this agreement, and

(b) reasonable out-of-pocket expenses of employees of TDC or its partners while such employees are away from their principal office and engaged in the business of LOWU pursuant to this agreement;

provided, however, that TDC shall not be entitled to any profit or overhead on such reimbursable costs and expenses.

Miscellaneous. This agreement is not intended to, nor shall it, create any right or interest in any person, firm, corporation, or other entity not a party hereto. This agreement may be terminated by either party by ninety (90) days written notice to the other. This agreement may not be assigned by either party without the prior written consent of the other.

Very truly yours,

TRANSCONTINENTAL DEVELOPMENT CO.
By TRANSCONTINENTAL CORPORATION,
Its Managing General Partner,

By _____
Its President

ACCEPTED & AGREED:

LAKE OF THE WOODS UTILITY COMPANY

By _____
Its Vice President

ok/(45)

TRANSCONTINENTAL DEVELOPMENT CO.

M E M O R A N D U M

18 November 1980

TO: THE VIRGINIA STATE CORPORATION COMMISSION

FROM: TRANSCONTINENTAL DEVELOPMENT CO.

SUBJECT: LAKE OF THE WOODS UTILITY COMPANY ("LOWU")
AGREEMENT FOR MANAGEMENT AND ADMINISTRATIVE SERVICES

REFERENCE: Letter agreement dated 17 November 1980, subject as above, between LOWU and Transcontinental Development Co. ("TDC").

Gentlemen, concerning the management agreement noted above, we represent (1) that the services to be provided to LOWU under that agreement consist of those listed in the agreement and hereinbelow; (2) that to the best of our knowledge and belief, these services supplement, but do not duplicate, similar services provided to LOWU by others; and (3) that the fees charged for these services do not result in a profit thereon to TDC. Services provided are described below.

1. Senior executive management, including strategic planning, budgeting, control, and review of operations. TDC provides the "top management" for the Utility. On a month-to-month basis, this involves several hours of senior executive time for general direction and review of operations which are directly supervised by the Utility's general manager and his staff. Specific on-going activities include review of financial performance and status; consultation and communications with, and direction of, outside consultants retained by or on behalf of the Utility; communications with, and direction of, the Utility general manager.

   On an annual basis, approximately 40 hours of senior management time are devoted to long-range and annual planning for the Utility including development and review of both operating and capital budgets.

2. Accounting and financial services provided by TDC to LOWU are of three main types: Banking and cash management; tax accounting and audit coordination; financial analysis. Of these, banking and cash management -- including account reconciliation and oversight of cash transfers -- requires approximately four hours per month on an ongoing basis. Tax accounting, planning, and reporting and coordination of audits are annual activities that require approximately two to four man-days. Financial analysis of capital investment alternatives is done as required. In addition to the foregoing activities, TDC also provides direction of, and assistance in, accounting for rate making purposes.

3. Administrative services provided by TDC under this agreement include but are not limited to the following: (1) general property and liability insurance administration including annual review and renewal of policies for casualty, general and auto liability, and workers compensation

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420 EAST CARRILLO STREET, SANTA BARBARA, CALIFORNIA • TELEPHONE (805) 963-6851

coverage; (2) employee group insurance administration and claims processing; (3) personnel recordkeeping and reporting; (4) coordination and follow-up with outside consultants (e.g. engineers, attorneys) engaged by or for the Utility.

4. On-site review of operations and inspection of facilities. TDC executives and professionals visit the Utility several times each year spending in aggregate, about three to five man-days at Lake of the Woods to consult face-to-face with local management and to observe, firsthand, the operation of the utility's business and development of its systems and facilities.

We wish to note, particularly, that TDC does not provide day-to-day operational management of LOWU nor does it become involved in supervision of labor, customer relations, payroll accounting, local billing and bookkeeping, data processing, or similar "first line" management activities (except as noted above). Most of these services, we understand, are provided by the Utility's own staff and/or the staff of Maryland Marine Utilities, Inc., an affiliate.

To recapitulate, services provided by TDC are summarized in the following table which also shows approximate costs of the services provided.

TYPE OF SERVICE PROVIDED	APPROXIMATE COST OF SERVICE HOURS/MO*	x RATE	= TOTAL
1. Senior executive management	4	$100	$ 400
2. Accounting & Financial services	8	50	400
" " "	8	20	160
3. Administrative services	4	50	200
" "	8	20	160
4. On-site review/inspector	1	100	100
" " "	2	50	100
	35		$1520
*includes annual services times ÷ 12		SAY	$1500

TDC does not presently account precisely for the hours which it devotes to the provision of services to LOWU. We believe that the foregoing represents with reasonable accuracy the approximate staff hours provided to LOWU and request that the Commission accept this estimate in lieu of detailed time records which are not available.

If additional information is desired, please contact the undersigned.

TRANSCONTINENTAL DEVELOPMENT CO.
By Transcontinental Corporation
Its Managing General Partner

Laurence F. Dunn Jr.

by Laurence F. Dunn Jr.
Director of Administration

cc T.L. Thorpe/LOWU R.F. Boeddeker/TDC J.W. Riely, Esq./Hunton & Williams

PROMISSORY NOTE

"EXHIBIT 5"

$2,402,702

December, 1, 1978
San Francisco, California

A. FOR VALUE RECEIVED, the undersigned, Lake of the Woods Utility Company, promises to pay to the order of BOISE CASCADE HOME & LAND CORPORATION, a Delaware corporation ("Payee"), on demand, the principal sum of Two Million Four Hundred and Two Thousand Seven Hundred and Two Dollars ($2,402,702) with interest on the unpaid balance of said amount outstanding, payable quarterly, at the rate of eight percent (8%) per annum.

B. Principal and interest shall be payable in lawful money of the United States at P. O. Box 50, Boise, Idaho 83728, or such other place as the holder of this Note may, from time to time, designate to the undersigned in writing.

C. This Note may be prepaid in whole or in part at any time or times without penalty.

D. No course of dealing between the undersigned and the holder of this Note and no delay on the part of the holder of this Note in exercising any rights under this Note shall operate as a waiver of the rights of the holder of this Note. No covenant or provision of this Note nor any default or event of default in connection therewith may be waived otherwise than by a written instrument signed by the parties so waiving such covenant or other provision or default or event of default; provided, however, that no such waiver shall extend to or

impair any obligation not expressly waived or impair any right consequent thereon. Any waiver may be given subject to satisfaction of conditions stated therein.

E. All covenants and agreements herein shall be deemed material, and shall bind each of the undersigned's successors and assigns, whether so expressed or not, and all such covenants and agreements shall inure to the benefit of the Payee and its nominees, successors and assigns, whether so expressed or not. This Note and all rights of BOISE CASCADE HOME & LAND CORPORATION (and any and all successor holders of this Note) hereunder shall be freely assignable without notice.

F. No extension of time for the payment of this Note made by agreement with any person now or hereafter liable for the payment of this Note shall operate to release, discharge, modify, change or affect the original liability under this Note, either in whole or in part, of the undersigned. Notwithstanding any provision herein, the total liability for payments in the nature of interest shall not exceed the limits imposed by the applicable usury laws.

G. As to this Note, the undersigned and any endorsers severally waive presentment, protest and demand, notice of protest, demand and dishonor and nonpayment of this Note.

H. If the holder of this Note refers it to an attorney for collection or seeks legal advice for default under this Note or any instrument securing this Note, or if an action is instituted on this Note, or if any other judicial or non-judicial action is instituted by the holder hereof or by any person, and an attorney is employed by the holder hereof to appear in any such action or proceeding or to reclaim,

sequester, protect, preserve or enforce the holder's interest in any security for this Note, including but not limited to proceedings to foreclose the loan evidenced hereby, proceedings under the Federal Bankruptcy Act, or in eminent domain, or under the Probate Code, or in connection with any state or with any state or federal tax lien, or for the appointment of a receiver, the undersigned and every endorser and guarantor hereof, and every person who assumes the obligations evidenced by this Note, jointly and severally promise to pay reasonable attorneys' fees for services performed by the holder's attorneys and all costs and expenses incurred incident to such employment.

I. The undersigned waives all rights of setoff and counterclaim with respect to this Note.

LAKE OF THE WOODS UTILITY COMPANY

By _____
Its _____

Without recourse for value received the undersigned hereby assigns all of its right, title and interest in and to this note to Perry R. Bass Inc.

BOISE CASCADE HOME AND LAND CORPORATION

_____
L. O. Legg
Senior Vice President