

DIRECT TESTIMONY

of

**Dianna Hathorn
Accountant**

**Accounting Department
Financial Analysis Division
Illinois Commerce Commission**

**Apple Canyon Utility Company; Cedar Bluff Utilities, Inc.; Charmar Water
Company; Cherry Hill Water Company; Northern Hills Water and Sewer
Company**

**Citation for Failure to Comply with Commission Order
and with Commission rules**

Docket No. 06-0360

October 24, 2006

**OFFICIAL FILE
ILLINOIS COMMERCE COMMISSION**

06-0360

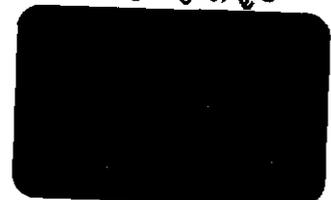


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1 Witness Identification

2 Q. Please state your name and business address.

3 A. My name is Dianna Hathhorn. My business address is 527 East Capitol
4 Avenue, Springfield, Illinois 62701.

5 Q. By whom are you employed and in what capacity?

6 A. I am an Accountant in the Accounting Department of the Financial
7 Analysis Division of the Illinois Commerce Commission ("Commission").

8 Q. What is the function of the Accounting Department of the Illinois
9 Commerce Commission?

10 A. The Accounting Department's function is to monitor the financial condition
11 of public utilities as part of the Commission's responsibilities under Article
12 IV of the Illinois Public Utilities Act ("Act") and to provide accounting
13 expertise on matters before the Commission.

14 Q. Please describe your background and professional affiliation.

15 A. I am a licensed Certified Public Accountant. I earned a B.S. in Accounting
16 from Illinois State University in 1993. Prior to joining the Commission Staff
17 ("Staff") in 1998, I worked as an internal auditor for another Illinois state
18 agency for approximately 3.5 years. I also have 1.5 years experience in
19 public accounting for a national firm.

20

21 Q. Have you previously testified before this Commission?

22 A. Yes, I have.

23 Purpose of Testimony

24 Q. What is the purpose of your testimony in this proceeding?

25 A. The purpose of my testimony is to address five Utilities Inc. subsidiaries
26 non-compliance with the Commission's rules and Order in Docket Nos.
27 03-0398/ 03-0399/ 03-0400/ 03-0401/ 03-0402 Consolidated ("the Rate
28 Cases"). The five subsidiaries at issue are Apple Canyon Utility Company,
29 Cedar Bluff Utilities, Inc., Charmar Water Company, Cherry Hill Water
30 Company, and Northern Hills Water and Sewer Company ("the
31 Companies"). The Companies are wholly-owned subsidiaries of Utilities,
32 Inc. ("UI").

33

34 Background

35 Q. Please provide background from the Rate Cases to the instant
36 proceeding.

37 A. On April 7, 2004, the Commission entered an order in the Rate Cases
38 approving a general increase in water and/or sewer rates. The Commission
39 set forth several conditions for its approval, including that:

40 Cedar Bluff Utilities, Inc., Apple Canyon Utility Company,
41 Charmar Water Company, Cherry Hill Water Company, and
42 Northern Hills Water and Sewer Company shall establish
43 and maintain continuing property records ["CPRs"] in

44 compliance with the Commission's rules, and must file a
45 report with the Manager of the Commission's Accounting
46 Department as to the successful implementation of the
47 property record program within 12 months after the final
48 order in this proceeding. (Order, Docket Nos. 03-0398/03-
49 0399/ 03-0400/03-0401/03-0402 (Consol.), p. 26)
50

51 Q. When was the deadline for this Commission condition?

52 A. The deadline for filing the report with the Manager of the Commission's
53 Accounting Department was April 7, 2005.

54

55 Q. When did the Companies provide this report?

56 A. It was filed on the Commission's e-docket system July 13, 2006, over one
57 year after the deadline.

58

59 Q. What is the status of the Companies' CPRs?

60 A. The report indicates the Companies CPRs are updated for the years 2004,
61 2005, and 2006 to date. The Companies confirmed in Staff data request
62 response DLH-2.01 that its continuing property records database has not yet
63 been updated for years prior to 2004.

64

65 Discussion of the Commission's Rules

66 Q. What are CPRs and which Commission rules apply to them?

67 A. Continuing property records show a history of individual assets. According to
68 the Uniform System of Accounts for Water Utilities (83 Ill. Adm. Code 605

69 "USOA"), continuing property records are a system of preserving original cost
70 of plant in a manner so that it is possible to identify, locate, obtain cost and
71 age of all used and useful property. The proof of the value of utility assets
72 should be readily available on the books of the regulated utility. This
73 information is required for the determination whether an investment is prudent
74 and thus should be capitalized and to the quantification of the capitalization.

75 Instruction 28 C of the USOA states as follows:

76 C. Each utility shall maintain records in which, for each plant
77 account, the amounts of the annual additions and retirements are
78 classified so as to show the number and the cost of the various
79 retirement units or other appropriate record units included therein
80

81 Q. Do any other Commission rules address CPRs?

82 A. Yes. Absent continuing property records, the Companies are not in
83 compliance with "The Preservation of Records for Water Utilities". (83 Ill.
84 Adm. Code 615) Part 615 requires:

85
86 (22) (a) Ledgers of utility plant accounts, including land and other
87 ledgers, showing the cost of utility plant by prime accounts. –
88 Period to be retained: Permanently.

89
90 (b) Continuing plant inventory records, showing description,
91 location, quantity, cost, etc. of physical units (or items) of utility
92 plant owned. – Period to be retained: Until record is superseded
93 or 6 years after plant is retired, provided mortality data are
94 retained as provided in Item 31.

95
96 (83 Ill. Adm. Code 615, Appendix A)

97

98 Effect of Lack of CPRs and Available Remedies

99 Q. What was the effect of the Companies lack of CPRs in the Rate Cases?

100 A. During the Rate Cases, the failure to maintain continuing property records in
101 compliance with Parts 605 and 615 resulted in the Companies being unable
102 to locate invoices to support its rate base additions, and therefore the
103 Commission adopted several Staff adjustments to disallow the Companies'
104 unsupported rate base. The continued failure to establish and maintain CPRs
105 will result in the same problem being repeated in the next rate case filed by
106 the Companies. As discussed above, the Companies have made progress
107 with their CPRs but the CPRs are not yet complete. Therefore, I recommend
108 that the Commission find in this docket that the procedure used in the past
109 Rate Cases to disallow rate base additions which had no CPR support be
110 followed in future rate cases.

111

112 Q. Does the Commission have the authority to impose penalties upon the
113 Companies?

114 A. Yes. Section 5-202 of the Act provides for the imposition of civil penalties for
115 a public utility's failure to obey, observe, or comply with any Commission
116 order, decision, rule, regulation, direction or requirement. In the case of
117 continuing violations, each day's continuance is a separate and distinct
118 offense. For small public utilities such as the Companies (see Section 4-

119 502(b) of the Act), the penalty range is from not less than \$500 to no more
120 than \$2,000 for each and every offense. A continuing violation constitutes a
121 separate offense for each day that the violation continues with a limit of
122 \$35,000 for the civil penalty imposed on small public utilities. (Section 5-202)

123

124 Q. What are the standards to be used by the Commission in determining the
125 amount of a penalty?

126 A. Section 4-203(a) states that in determining the amount of the penalty, the
127 Commission shall consider (1) the appropriateness of the penalty to the size
128 of the business of the public utility, (2) the gravity of the violation, (3) other
129 mitigating or aggravating factors as the Commission may find to exist, and (4)
130 the good faith of the public utility in attempting to achieve compliance after
131 notification of a violation.

132

133 Q. Please describe the size of the business of the Companies?

134 A. According to page 2 of the Rate Cases order, "The Companies are wholly-
135 owned subsidiaries of UI, and together, these five companies provide
136 water and/or sewer service to approximately 1,500 customers in various
137 Illinois counties. UI owns and operates approximately 81 water and/or
138 wastewater systems in 17 different states."

139

140 Q. Please describe the gravity of the violation?

141 A. Failure to maintain continuing property records in compliance with Parts 605
142 and 615 results in the Companies being unable to support the increase to
143 plant for plant additions since the last rate case. If the Companies continue to
144 maintain the CPRs on a prospective basis, the Companies will have support
145 for all plant additions since 2004.

146

147 Q. Are there any aggravating factors the Commission should consider?

148 A. Yes. Utilities Inc. has more water and sewer utilities in Illinois than the five
149 companies cited in this proceeding. Thus, the parent company, Utilities Inc.
150 is not a small utility as defined by the Public Utilities Act. It has twenty-
151 four subsidiaries, with 17,400 customers in the state. Utilities Inc. should
152 be aware of the requirements of the Illinois Public Utilities Act in regard to
153 CPRs as all of its subsidiaries are required to keep them. By this order the
154 Commission needs to send a message to Utilities Inc that plant additions
155 since the previous rate cases that are not supported by a CPR system will not
156 be allowed in rate base in future rate cases of the remaining companies.

157

158 Q. Describe the good faith of the public utility in attempting to achieve
159 compliance after notification of the violation.

160 A. The order in the rate proceeding of Docket Nos. 03-0398/03-0399/03-
161 0400//03-0401/03-0402 (Consol.) that ordered the Companies to establish
162 and maintain a CPR system in compliance with the Commission's rules was
163 not the first time that the Commission has told Utilities Inc to maintain a CPR

164 system. The Commission's Order in *Apple Canyon Utility Co.*, Docket 94–
165 0157, (March 22, 1995, 1995 Ill. PUC Lexis 203) required the Companies
166 to maintain Continuing Property Records using the "Will County
167 Continuing Property Records" as a model. This is discussed at length in
168 the Rate Cases order as well. (Order, Docket Nos. 03-0398/03-0399/ 03-
169 0400/03-0401/03-0402 (Consol.), at pages 20-21)

170 In addition, the Companies do not appear to have been diligent in
171 complying with the consolidated rate order entered April 7, 2004. This
172 order required the Companies to file a report as to the successful
173 implementation of a CPR program with the Manager of the Commission's
174 Accounting Department within 12 months after the final order was entered.
175 Thus, the Companies should have implemented a CPR program and
176 reported that to the Commission's Manager of Accounting by April 7,
177 2005. However, Utilities Inc. did not meet that deadline and filed motions
178 for extension of time to comply with the Commission order on May 26,
179 2005, July 15, 2005, August 31, 2005, and December 30, 2005. The
180 fourth Motion requested an extension of time for compliance to March 31,
181 2006. On January 3, 2006, the Administrative Law Judge issued a notice
182 that it appeared that the Companies were in violation of Finding 14 of the
183 Final Order entered on April 7, 2004 and ordered the Companies to show
184 cause why they should not be held in contempt for violating the final order.

185

186 Recommendation

187 Q. What is Staff's recommendation?

188 A. I recommend that the Commission impose a civil penalty on each of the
189 Companies of \$1,000, for a total of \$5,000. I further recommend that the
190 Commission order put Utilities Inc. on notice that all of its companies must
191 comply with the Commission's rules regarding the maintenance of CPRs or
192 be subject to disallowances of plant additions to rate base in future rate
193 cases.

194

195 Q. How does your recommendation comply with the standards of Section 4-
196 203(a) discussed above?

197 A. The penalty I recommend is minimal but appropriate for the size of the
198 Companies. The Commission recently imposed a \$1,000 fine on another
199 small utility in its order in Docket No. 05-0452, Galena Territory Utilities, Inc.,
200 page 11, Finding (7), entered August 30, 2006.

201

202 The Companies appear to have been less than diligent in getting into
203 compliance with the Commission order and the penalty sends a message to
204 Utilities Inc. that the Commission is serious in monitoring the utilities for
205 compliance with Commission orders, administrative rules, and statutes.

206

207 Q. Does this conclude your prepared direct testimony?

208 A. Yes, it does.