

**STATE OF NORTH CAROLINA  
UTILITIES COMMISSION  
RALEIGH**

DOCKET NO. W-100, SUB 54

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Petition for Rulemaking to Implement	) ORDER ADOPTING RULES TO
G.S. 62-133.12, North Carolina Session	) IMPLEMENT G.S. 62-133.12
Law 2013-106 (House Bill 710)	)

BY THE COMMISSION: On August 21, 2013, the Public Staff filed a Petition for Order Establishing Rulemaking Proceeding in this docket. In the Petition, the Public Staff requested that the Commission establish a rulemaking to implement G.S. 62-133.12, enacted by North Carolina Session Law 2013-106 (House Bill 710), and adopt the proposed rules that the Public Staff attached to the Petition with such modifications as may be appropriate in light of any comments that might be presented during the rulemaking proceeding. The draft rules established procedures for determining and implementing the rate adjustment mechanisms contemplated in the provisions in G.S. 62-133.12, i.e., a Water System Improvement Charge (WSIC) and a Sewer System Improvement Charge (SSIC).

On August 22, 2013, and August 23, 2013, respectively, Aqua North Carolina, Inc. (Aqua), and Utilities, Inc. (UI), the parent company of Carolina Water Service, Inc. of North Carolina (CWS) and five other regulated water and/or wastewater utilities in North Carolina, filed petitions to intervene in this docket. In support of its Petition, Aqua stated that it had filed a general rate case in Docket No. W-218, Sub 363 on August 2, 2013, and that, pursuant to the authority granted in the newly enacted G.S. 62-133.12, Aqua had requested that the Commission approve a rate adjustment mechanism in that rate proceeding to allow Aqua to recover reasonable and prudent investments in eligible water and sewer system improvements. UI stated that its subsidiary CWS had filed a general rate case in Docket No. W-354, Sub 336 on June 28, 2013, with a similar request.

On August 28, 2013, the Commission issued an Order Establishing Rulemaking and Granting Petitions of Aqua and Utilities, Inc., to Intervene. This order established dates for the parties to file comments and reply comments on the proposed rules.

On October 7, 2013, Aqua and UI filed joint Initial Comments and stated that Aqua and UI planned to negotiate with the Public Staff on the proposed rules.

On November 8, 2013, the Public Staff, Aqua, and UI (Joint Movants) filed a Joint Motion Requesting Approval of Rules. In support of the Joint Motion, the Joint Movants stated that they had reached agreement on the recommended WSIC Rule R7-39 and SSIC Rule R10-26, which were attached thereto as Exhibit A and B, respectively. The

Joint Movants also stated that they believed the recommended rules would ensure that the objectives of G.S. 62-133.12 are maintained and provide for effective implementation, continued stringent regulatory review and oversight, and appropriate consumer protections. Further, Joint Movants noted that the semi-annual adjustments proposed in the rules would reasonably reduce regulatory lag and provide for efficient administration of these rate adjustments, but not result in an excessive frequency of rate adjustments. Joint Movants also observed that the recommended WSIC Rule R7-39 and SSIC Rule R10-26 were identical with the exceptions of the interchangeable words WSIC and SSIC, water and sewer, and water quality and effluent. Lastly, the Joint Movants noted that Aqua and UI are provided different “WSIC Periods” and “SSIC Periods” in subparagraphs (b)(7) in order to expedite the Public Staff review and Commission approvals of the semi-annual adjustments described in paragraph (i).

The Commission takes judicial notice that, as stated in the petitions to intervene, Aqua and CWS filed general rate cases shortly after the General Assembly adopted G.S. 62-133.12 requesting that the Commission approve WSIC and SSIC rate adjustment mechanisms in each case. Numerous hearings were held across the State to allow the public to comment on the rate increase and WSIC/SSIC rate adjustment requests. In each docket, various customers testified in opposition to Commission approval of a WSIC/SSIC rate adjustment mechanism. Much of the customer opposition stemmed from the belief that the mechanism would be devoid of stringent regulatory oversight and would allow the company to implement and collect the adjustment without customer input or knowledge.

The Commission noted in the Aqua and CWS rate cases that the General Assembly recognized a need in North Carolina and adopted the rate adjustment mechanisms in G.S. 62-133.12 to incentivize water and sewer utilities to invest in needed water and sewer infrastructure improvements. In its order in the Aqua rate case, for example, the Commission stated as follows:

The Commission believes that the primary purpose of G.S. 62-133.12 was to encourage and accelerate investment in needed water and sewer infrastructure by means of a mechanism which will alleviate the effects of regulatory lag by allowing for earlier recovery of some portion, not to exceed 5% of approved service revenues, of the incremental depreciation and capital costs associated with eligible investments made between general rate case proceedings. In accordance with G.S. 62-133.12, eligible water system and sewer system improvements would be installed, for example, to comply with primary drinking water standards, to implement solutions to wastewater problems, and to comply with State and federal law and regulations. Further, G.S. 62-133.12 allows, upon the Commission’s specific direction, for the utility to implement solutions to comply with otherwise non-mandatory secondary water quality standards.

...

The Commission believes that Aqua will be incentivized and encouraged to accelerate its investment in water and sewer infrastructure improvements to comply with applicable water quality and effluent standards, including secondary water quality standards, if authorized to utilize a WSIC/SSIC mechanism to alleviate the effects of regulatory lag. ... Providing an incentive to Aqua to undertake more extensive improvements to address secondary water quality issues in those individual subdivision service areas which have, for example, iron and manganese concentration levels that exceed federal and state standards which have not been sufficiently remedied on a sustained basis by past treatment methods, benefits the Company's customers. Moreover, the recovery mechanism is of further benefit to customers because it will be available to fund projects to address problematic systemic secondary water quality issues should the Commission direct the Company to undertake them in individual subdivision service areas, even though such projects may not be specifically required by federal and/or state standards and might not be high priority to the Company absent the direction of the Commission. The Commission determines that some secondary water quality improvement projects generally may have been given lower priority in the past by water utilities because limited available capital budget funds are spent first on primary water quality improvements. The availability of the WSIC recovery mechanism should, to customer benefit, provide the Company with increased incentive and wherewithal to address secondary water quality issues on a sustained basis and sooner than it would otherwise be able.

...

With respect to the timing of cost recovery of infrastructure improvements, the Commission believes that, to the extent that necessary investments would result in rate increases at some point in time irrespective of the mechanism, customers will benefit from the rate-smoothing effects of more gradual increases made possible by recovery through a WSIC/SSIC surcharge. Furthermore, if the ability to increase rates to recover certain costs between general rate cases actually results in fewer or less frequent rate cases as claimed by the Company, ratepayers would benefit from lower rates because the Company's recoverable expenses would be reduced by the elimination of the substantial costs associated with the preparation and litigation of a general rate case.

The Commission has carefully reviewed and considered the proposed rules, the arguments for and against the rate adjustment mechanisms, the input received from customers during the Aqua and CWS public hearings, the joint recommendations of the parties to this proceeding, and the record proper. Based upon this review, the Commission concludes that the recommended rules would, for the most part, ensure that the objectives of G.S. 62-133.12 are maintained and provide for effective implementation. The Commission is not convinced, however, that the rules as proposed

in this proceeding would adequately address the concerns raised by consumers during the public hearings in the Aqua and CWS rate cases. In the Commission's opinion, the proposed rules could be strengthened to address those concerns: (1) by requiring the utility to provide advanced notice of the potential dollar impact that the proposed adjustment might have on the average customer's monthly utility bill if the requested rate adjustment mechanism and rate increase are granted in the rate proceeding; (2) by requiring the utility to notify the Commission 60 days in advance of the effective date of any WSIC/SSIC rate adjustment; (3) by requiring the Public Staff to provide 15 days' notice to the Commission before a WSIC/SSIC adjustment is submitted to the Commission for consideration at a regularly scheduled staff conference; and (4) by informing parties interested in receiving notice of these filings that they may subscribe to the Commission's electronic notification system.

While approving WSIC and SSIC rate adjustment mechanisms for the utilities in the Aqua and CWS rate cases, the Commission modified the utilities' proposals in order to address concerns raised by customers at the public hearings and other parties. The rules adopted herein for all regulated water and sewer companies retain the procedural safeguards and requirements imposed in those cases. As further stated in the Aqua rate case order, for example,

the rate adjustments related to the WSIC/SSIC mechanism are not automatic. Prior to the initiation of each surcharge, the Company must obtain approval from the Commission. Aqua may file a request with the Commission for authority to impose the WSIC and/or SSIC mechanism to be effective no less than 60 days after filing the request. Prior to the requested effective date of the mechanism, the Public Staff will present the Company's request for Commission consideration at a regularly scheduled staff conference. Based upon its detailed review and investigation, the Public Staff will recommend that the Commission issue an order approving, modifying and approving, or rejecting the proposed WSIC/SSIC.

Moreover, any request for cost recovery through the mechanisms will be thoroughly reviewed. As the Commission stated in the Aqua rate case order,

The eligible system improvements must be completed and placed in service prior to the Company requesting approval; as a result, actual cost data and other pertinent information will be available for review and analysis. The Public Staff will review and scrutinize such information to determine whether the specific system improvements to be included in the requested surcharge are eligible for recovery through the WSIC/SSIC mechanism, pursuant to G.S. 62-133.12, before customers are actually charged under the mechanism. ... Consequently, the Commission determines that the Public Staff, in its role as the consumer advocate, will carefully review and scrutinize each project proposed for recovery through the WSIC/SSIC mechanism for eligibility and reasonableness before providing its recommendation to the Commission.

Further, the requirement in the alternative procedures for Aqua to provide an ongoing three-year plan which includes a description of all proposed eligible system improvements, including an estimate of the cost of the improvements and dates when the improvements will be placed into service will allow the Public Staff to review such filings and have discussions with Aqua concerning such proposed improvements prior to the Company expending the funds and requesting ratepayer recovery through the WSIC/SSIC mechanism. The Public Staff's scrutiny and review of the ongoing three-year plan between general rate case filings and its routine discussions with Aqua concerning the same, would provide the Public Staff with detailed information concerning eligible system improvement projects for which Aqua may eventually seek WSIC or SSIC recovery and should also keep the Public Staff more informed regarding matters concerning the quality of service provided by Aqua to its customers.

...

The Commission determines that the procedures provided in Appendices C and D should provide ample regulatory oversight of the WSIC/SSIC mechanism for the protection of the customers. All infrastructure improvements will be reviewed by the Public Staff and the Commission to determine whether they are eligible for cost recovery through the WSIC/SSIC mechanism and will be reviewed again for prudence and reasonableness in the Company's next general rate case proceeding.

Furthermore, any rate adjustments authorized under the WSIC and SSIC mechanisms outside of a general rate case will be allowed to become effective, but not unconditionally approved. In other words, the adjustments will be provisional, will not be deemed prima facie just and reasonable, and, thus, may be rescinded retroactively in the utility's subsequent general rate case, at which time the adjustment may be further examined for a determination of its justness and reasonableness. As the Commission noted in the Aqua rate case order:

The Commission finds that while an approved mechanism will allow cost recovery resulting in limited or capped rate increases between general rate cases, Aqua is not unconditionally guaranteed recovery of such costs. WSIC/SSIC surcharges are subject to Commission review and scrutiny for reasonableness and prudence in general rate case proceedings as has been the case for investments and expenses prior to the enactment of G.S. 62-133.12. Consequently, the Commission continues to have authority in a general rate case proceeding to disallow costs related to investments in water and sewer improvements recovered under the WSIC/SSIC mechanism that were subsequently determined to be unreasonable or imprudent. The Commission is unpersuaded that the WSIC/SSIC mechanism will discourage Aqua from investing in projects that are efficient and economical but not eligible for the favorable accelerated recovery, as

asserted by the Attorney General, because the Company's investment decisions remain subject to the reasonable and prudent standard set forth in G.S. 62-133 and such investments will be scrutinized by the Public Staff and the Commission in a general rate case proceeding. Any costs deemed to be unreasonable or imprudent upon review by the Public Staff and the Commission will be disallowed.

As Public Staff witness Fernald testified in the Aqua rate case,

due to the detailed examination which would occur with respect to the specific plant additions reviewed between rate case proceedings in regard to the WSIC/SSIC mechanism, those same plant additions would likely not require as much review in a general rate case proceeding, but would nonetheless be subject to further review. Consequently, the Commission determines that the Public Staff, in its role as the consumer advocate, will carefully review and scrutinize each project proposed for recovery through the WSIC/SSIC mechanism for eligibility and reasonableness before providing its recommendation to the Commission.

In response to the concerns raised in the Aqua and CWS rate cases about the utility's ability to impose new charges without any notice to customers or public hearings, the WSIC and SSIC rate adjustment mechanisms adopted in the Aqua and CWS rate cases and the rules adopted herein provide that any utility customer will have the opportunity to participate if they so choose in proceedings when rate adjustments are proposed to be made. Again, as noted in the Aqua rate case order, the WSIC and SSIC rate adjustment mechanisms adopted therein

require that Aqua file a request with the Commission for authority to impose the WSIC/SSIC mechanism once the eligible system improvements are in service. The effective date of the WSIC/SSIC would be no less than 60 days after filing the request. Such request must also be provided to the Public Staff. Other parties interested in receiving notice of Aqua's request to impose the WSIC/SSIC mechanism may subscribe to the Commission's electronic notification system, for Docket No. W-218, Sub 363A, through the Commission's website at [www.ncuc.net](http://www.ncuc.net).

As previously discussed, prior to the requested effective date of the mechanism, the Public Staff will present the Company's request for Commission consideration at a regularly scheduled staff conference and recommend that the Commission issue an order approving, modifying and approving, or rejecting the proposed WSIC/SSIC. Witness Roberts testified that customers may contact Aqua at any time to discuss the inclusion or exclusion of a specific project included on Aqua's three-year plan and that the Company is willing to meet with customers regarding any water quality concerns and associated remedies. Customers also may contact the Public Staff or file a formal complaint with the Commission regarding matters

concerning their regulated utility service. All infrastructure improvements recovered through the WSIC/SSIC mechanism will be reviewed again by the Public Staff and the Commission for prudence and reasonableness in the Company's next general rate case proceeding. Customers may also express any concerns regarding the WSIC/SSIC mechanism to the Commission at that time. The Commission is of the opinion and therefore, so finds and concludes, that the foregoing procedure will provide adequate notice to interested parties and provide various opportunities for input by interested parties with respect to the proposed imposition of the WSIC/SSIC mechanism by Aqua between general rate case proceedings.

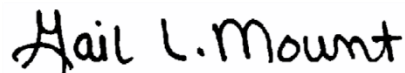
In summary, the Commission concludes that paragraph (d) in the proposed WSIC and SSIC rules shall be amended: (1) to reflect the potential dollar impact that the proposed adjustment might have on the average customer's monthly utility bill if the requested rate adjustment mechanism and rate increase are granted in the rate proceeding; and (2) to adopt a notice to that effect. Further, the Commission amends paragraph (f) in the WSIC and SSIC rules to reflect that: (1) the utility shall request approval of the proposed WSIC/SSIC adjustment at least 60 days in advance of the effective date of the rate change; (2) the Public Staff shall notify the Commission 15 days in advance before a WSIC/SSIC adjustment is submitted to the Commission for consideration at a regularly scheduled staff conference; and (3) parties interested in receiving notice of these filings may subscribe to the Commission's electronic notification system.

IT IS, THEREFORE, ORDERED that Rules R7-39 and R10-26, as set forth in Appendices A and B attached hereto, are hereby adopted effective as of the date of this Order.

ISSUED BY ORDER OF THE COMMISSION.

This the 6<sup>th</sup> day of June, 2014.

NORTH CAROLINA UTILITIES COMMISSION

A handwritten signature in black ink that reads "Gail L. Mount". The signature is written in a cursive, flowing style.

Gail L. Mount, Chief Clerk

**R7-39 WATER SYSTEM IMPROVEMENT CHARGE MECHANISM**

(a) Scope of Rule. – This rule provides the procedure for the approval and administration of a rate adjustment mechanism pursuant to G.S. 62-133.12 to allow a utility to recover the incremental depreciation expense and capital costs related to the utility's reasonable and prudently incurred investment in eligible water system improvements.

(b) Definitions. – As used in this rule:

(1) "Capital costs" means the pretax return on costs permitted to be capitalized pursuant to the National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts, net of accumulated depreciation and accumulated deferred income taxes, using the current federal and state income tax rates and the utility's capital structure, cost of long-term debt, and return on equity approved in the utility's most recent general rate case.

(2) "Depreciation expense" means the annual depreciation accrual rates employed in the utility's most recent general rate case for the plant accounts in which the cost of each eligible water system improvement is recorded applied to the cost of eligible water system improvements.

(3) "Eligible water system improvements" means the improvements set forth in G.S. 62-133.12(c) and shall include only those improvements found necessary by the Commission to provide safe, reliable, and efficient service in accordance with applicable water quality standards.

(4) "Incremental depreciation expense and capital costs" means depreciation expense and capital costs that have been incurred since the utility's most recent rate case and have not been included in the utility's cost of service for ratemaking purposes.

(5) "Water System Improvement Charge or WSIC" means an adjustment to customer bills that allows a utility to recover the WSIC Revenue Requirement.

(6) "WSIC Revenue Requirement" means the annual revenue required to allow a utility to recover the annual incremental depreciation expense and capital costs of eligible water system improvements.

(7) "WSIC Period" means the 12-month period ended December 31 for Aqua North Carolina, Inc. and the 12-month period ended March 31 for Utilities, Inc., and its North Carolina affiliates. The WSIC Period for other water utilities shall be a 12-month period established by the Commission in conjunction with the approval of a WSIC mechanism for that utility.



(8) “WSIC mechanism” means a rate adjustment mechanism approved by the Commission in a general rate case pursuant to G.S. 62-133.12.

(c) Request for Water System Improvement Charge Mechanism. – A utility seeking approval of a WSIC mechanism shall include in its application for a general rate increase under G.S. 62-133 and Commission Rule R1-17 the following:

(1) A three-year plan that includes the following:

a. A detailed description of all proposed eligible water system improvements expected to be completed in the initial WSIC Period and an estimate of the cost of the improvements and dates when the improvements will be placed into service; and

b. A brief description of the proposed eligible water system improvements, estimated costs, and completion dates for improvements that the utility plans to complete during the two years following the initial WSIC Period.

(2) The proposed effective dates of the WSIC and semiannual adjustments to the charge.

(3) Testimony, affidavits, exhibits, or other evidence demonstrating that a WSIC is in the public interest and will enable the utility to provide safe, reliable, and efficient service in accordance with applicable water quality standards.

(4) Any other information required by the Commission.

(d) Customer Notice. – The notice to customers of the utility’s general rate increase application shall include the proposed WSIC mechanism and the estimated impact of the charges under the mechanism on the utility’s monthly service rates. The Notice shall include the following statement:

### **Water System Improvement Charge Mechanism**

Pursuant to G.S. 62-133.12 and Commission Rule R7-39, the Company is requesting that the Commission approve a Water System Improvement Charge Mechanism. This mechanism will allow the Company to recover the annual incremental depreciation expense and capital costs of eligible water system improvements completed and placed in service between rate cases. In support of this request, the Company has filed a three-year plan with its application which list various projects which may be eligible for recovery pursuant to this mechanism, the cost and/or estimated costs of those projects, and the estimated completion date of those projects. By law, the cumulative maximum charges between rate cases that the Company can recover through the use of this mechanism cannot

exceed five percent of the total service revenues that the Commission will approve in this rate case. Customers may subscribe to the Commission's electronic notification system through the Commission's website at [www.ncuc.net](http://www.ncuc.net) to receive notification of any Company requests to utilize the Water System Improvement Charge Mechanism, if approved.

In this Application, the Company has requested that the Commission allow it to recover total service revenues of \$\_\_\_\_\_. Five percent of these revenues is \$\_\_\_\_\_. If the Commission permits the Company to recover the revenue requirements requested in the Application, the Company projects that the average monthly water bill for a typical residential customer (based upon monthly water usage of x,xxx gallons) would be \$\_\_\_\_\_. Based upon these figures, the Company estimates that the maximum that the average residential customer's monthly water bill could be increased by this adjustment mechanism between rate cases is \$\_\_\_\_\_.

The Commission may eliminate or modify any rate adjustment mechanism approved in this case upon a finding that it is no longer in the public interest.

(e) General Rate Case Review. – Following notice and hearing, the Commission shall approve a WSIC mechanism only upon a finding that it is in the public interest.

(f) Initiation of Charge. – Once a WSIC mechanism is approved and eligible water system improvements are in service, the utility may file a request with the Commission for authority to impose the water system improvement charge pursuant to the mechanism, to be effective no less than 60 days after filing the request. The Company shall also provide a copy of the request to the Public Staff.<sup>1</sup> Prior to the effective date, the Public Staff shall schedule the request for Commission consideration at the regularly scheduled staff conference and recommend that the Commission issue an order approving, modifying and approving, or rejecting the proposed water system improvement charge. The Public Staff shall formally notify the Commission at least 15 days in advance of the date that the request shall be scheduled for Commission consideration at the regularly scheduled staff conference.

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<sup>1</sup> Parties interested in receiving notice of these filings may subscribe to the Commission's electronic notification system through the Commission's website at [www.ncuc.net](http://www.ncuc.net).

(g) Computation of the WSIC Revenue Requirement. – The WSIC Revenue Requirement shall be computed for each WSIC Period as follows:

Eligible water system improvements	\$X,XXX,XXX
Less: Accumulated depreciation	X,XXX,XXX
Less: Accumulated deferred income taxes	<u>X,XXX,XXX</u>
Net plant investment	\$X,XXX,XXX
Pre-tax rate of return	<u>X.XX%</u>
Capital costs	\$X,XXX,XXX
Plus: Depreciation expense	<u>XXX,XXX</u>
Subtotal, excluding regulatory fee	\$X,XXX,XXX
Regulatory fee gross-up factor	<u>XXXX</u>
Total	<u><u>\$X,XXX,XXX</u></u>

(h) Computation of Water System Improvement Charge. –

(1) The WSIC shall be expressed as a percentage carried to two decimal places and shall be applied to the total utility bill of each customer under the utility's applicable service rates and charges.

(2) The WSIC shall be computed by dividing the annual WSIC Revenue Requirement by the projected revenues of the utility during the 12-month period following implementation of the charge.

(i) Semiannual Adjustments. – A utility may file a request for a WSIC adjustment no more frequently than semiannually.

(1) The request shall include the computation and supporting data for the adjustment.

(2) Cumulative WSIC Revenue Requirements may not exceed five percent of the total annual service revenues approved in the utility's last general rate proceeding.

(3) The procedural requirements set forth in subsection (f) of this Rule shall apply to requests for semiannual adjustments.

(j) Experience Modification Factor. – The WSIC shall be modified through the use of an experience modification factor (EMF) that reflects the difference between the WSIC Revenue Requirement and the revenues that were actually realized under the WSIC during the WSIC Period. The EMF shall remain in effect for a 12-month period. Pursuant to G.S. 62-130(e), any overcollection of reasonable and prudently incurred costs of the utility for eligible water system improvements to be refunded to a utility's customers through operation of the EMF shall include an amount of interest at such rate as the Commission determines to be just and reasonable, not to exceed the maximum statutory rate.

(k) Water System Improvement Charge Reset. – The WSIC shall be reset at zero as of the effective date of new base rates established in the utility's general rate case. Thereafter, only the incremental depreciation expense and capital costs of new eligible water system improvements that have not previously been reflected in the utility's rates shall be recoverable through the WSIC.

(l) Audit and Reconciliation. – The WSIC shall be subject to the following:

(1) Within 60 days following the end of each WSIC Period, each utility shall file a report, in a format prescribed by the Commission, reconciling its actual eligible water system improvement costs, actual WSIC revenues, and EMF computation.

(2) The Public Staff shall audit the utility's actual eligible water system improvement costs, actual WSIC revenues, and EMF computation, and shall file a report on its audit no later than four months after the end of the WSIC Period of the utility.

(m) Ongoing Three-Year Plan. – Within 60 days following the end of each WSIC Period, the utility shall file an updated three-year plan containing the information prescribed in Section (c)(1) of this Rule and any other information required by the Commission.

(n) Quarterly Filings with the Commission. – Within 45 days after the end of each calendar quarter, the utility shall file the following reports:

(1) A quarterly earnings report consisting of the following:

a. A balance sheet and income statement for the calendar quarter and calendar year to date for the utility;

b. A statement of the per books net operating income for the calendar quarter and calendar year to date for each rate division of the utility based on North Carolina ratemaking;

c. A statement of rate base at the end of the calendar quarter for each rate division of the utility based on North Carolina ratemaking; and

d. The number of customers and gallons sold for each month of the calendar quarter for each rate division by rate type (meter size, flat rate, etc.).

(2) A quarterly report of WSIC collections from customers consisting of amounts collected for the quarter by rate division and rate type.

(3) A construction status report which includes by rate division the following information for each eligible water system improvement project:

- a. The costs incurred during the quarter;
- b. The cumulative amount incurred;
- c. The estimated total cost for each project;
- d. The estimated completion date; and
- e. The actual completion date.

(o) Elimination or Modification of WSIC Mechanism. – After notice to the utility and opportunity to be heard, the Commission may eliminate or modify any previously authorized WSIC mechanism upon a finding that it is not in the public interest.

(p) Burden of Proof. – The burden of proof as to whether a WSIC mechanism is in the public interest, the correctness and reasonableness of any WSIC, and whether the investment in the water system improvements was reasonable and prudently incurred shall be on the utility.

**R10-26 SEWER SYSTEM IMPROVEMENT CHARGE MECHANISM**

(a) Scope of Rule. – This rule provides the procedure for the approval and administration of a rate adjustment mechanism pursuant to G.S. 62-133.12 to allow a utility to recover the incremental depreciation expense and capital costs related to the utility's reasonable and prudently incurred investment in eligible sewer system improvements.

(b) Definitions. – As used in this rule:

(1) "Capital costs" means the pretax return on costs permitted to be capitalized pursuant to the National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts, net of accumulated depreciation and accumulated deferred income taxes, using the current federal and state income tax rates and the utility's capital structure, cost of long-term debt, and return on equity approved in the utility's most recent general rate case.

(2) "Depreciation expense" means the annual depreciation accrual rates employed in the utility's most recent general rate case for the plant accounts in which the cost of each eligible sewer system improvement is recorded applied to the cost of eligible sewer system improvements.

(3) "Eligible sewer system improvements" means the improvements set forth in G.S. 62-133.12(d) and shall include only those improvements found necessary by the Commission to provide safe, reliable, and efficient service in accordance with applicable effluent standards.

(4) "Incremental depreciation expense and capital costs" means depreciation expense and capital costs that have been incurred since the utility's most recent rate case and have not been included in the utility's cost of service for ratemaking purposes.

(5) "Sewer System Improvement Charge or SSIC" means an adjustment to customer bills that allows a utility to recover the SSIC Revenue Requirement.

(6) "SSIC Revenue Requirement" means the annual revenue required to allow a utility to recover the annual incremental depreciation expense and capital costs of eligible sewer system improvements.

(7) "SSIC Period" means the 12-month period ended December 31 for Aqua North Carolina, Inc. and the 12-month period ended March 31 for Utilities, Inc., and its North Carolina affiliates. The SSIC Period for other sewer utilities shall be a 12-month period established by the Commission in conjunction with the approval of a SSIC mechanism for that utility.

(8) “SSIC mechanism” means a rate adjustment mechanism approved by the Commission in a general rate case pursuant to G.S. 62-133.12.

(c) Request for Sewer System Improvement Charge Mechanism. – A utility seeking approval of a SSIC mechanism shall include in its application for a general rate increase under G.S. 62-133 and Commission Rule R1-17 the following:

(1) A three-year plan that includes the following:

a. A detailed description of all proposed eligible sewer system improvements expected to be completed in the initial SSIC Period and an estimate of the cost of the improvements and dates when the improvements will be placed into service; and

b. A brief description of the proposed eligible sewer system improvements, estimated costs, and completion dates for improvements that the utility plans to complete during the two years following the initial SSIC Period.

(2) The proposed effective dates of the SSIC and semiannual adjustments to the charge.

(3) Testimony, affidavits, exhibits, or other evidence demonstrating that a SSIC is in the public interest and will enable the utility to provide safe, reliable, and efficient service in accordance with applicable effluent standards.

(4) Any other information required by the Commission.

(d) Customer Notice. – The notice to customers of the utility’s general rate increase application shall include the proposed SSIC mechanism and the estimated impact of charges under the mechanism on the utility’s monthly service rates. The Notice shall include the following statement:

### **Sewer System Improvement Charge Mechanism**

Pursuant to G.S. 62-133.12 and Commission Rule R10-26, the Company is requesting that the Commission approve a Sewer System Improvement Charge Mechanism. This mechanism will allow the Company to recover the annual incremental depreciation expense and capital costs of eligible sewer system improvements completed and placed in service between rate cases. In support of this request, the Company has filed a three-year plan with its Application which list various projects which may be eligible for recovery pursuant to this mechanism, the cost and/or estimated costs of those projects, and the estimated completion date of those projects. By law, the cumulative maximum charges between rate cases that the Company can recover through the use of this mechanism cannot

exceed five percent of the total service revenues that the Commission will approve in this rate case. Customers may subscribe to the Commission's electronic notification system through the Commission's website at [www.ncuc.net](http://www.ncuc.net) to receive notification of any Company requests to utilize the Sewer System Improvement Charge Mechanism, if approved.

In this Application, the Company has requested that the Commission allow it to recover total service revenues of \$\_\_\_\_\_. Five percent of these revenues is \$\_\_\_\_\_. If the Commission permits the Company to recover the revenue requirements requested in the Application, the Company projects that the average monthly sewer bill for a typical residential customer (based upon monthly water usage of x,xxx gallons) would be \$\_\_\_\_\_. Based upon these figures, the Company estimates that the maximum that the average residential customer's monthly sewer bill could be increased by this adjustment mechanism between rate cases is \$\_\_\_\_\_.

The Commission may eliminate or modify any rate adjustment mechanism approved in this case upon a finding that it is no longer in the public interest.

(e) General Rate Case Review. – Following notice and hearing, the Commission shall approve a SSIC mechanism only upon a finding that it is in the public interest.

(f) Initiation of Charge. – Once a SSIC mechanism is approved and eligible sewer system improvements are in service, the utility may file a request with the Commission for authority to impose the sewer system improvement charge pursuant to the mechanism, to be effective no less than 60 days after filing the request. The Company shall also provide a copy of the request to the Public Staff.<sup>1</sup> Prior to the effective date, the Public Staff shall schedule the request for Commission consideration at the regularly scheduled staff conference and recommend that the Commission issue an order approving, modifying and approving, or rejecting the proposed sewer system improvement charge. The Public Staff shall formally notify the Commission at least 15 days in advance of the date that the request shall be scheduled for Commission consideration at the regularly scheduled staff conference.

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<sup>1</sup> Parties interested in receiving notice of these filings may subscribe to the Commission's electronic notification system through the Commission's website at [www.ncuc.net](http://www.ncuc.net).



(g) Computation of the SSIC Revenue Requirement. – The SSIC Revenue Requirement shall be computed for each SSIC Period as follows:

Eligible sewer system improvements	\$X,XXX,XXX
Less: Accumulated depreciation	X,XXX,XXX
Less: Accumulated deferred income taxes	<u>X,XXX,XXX</u>
Net plant investment	\$X,XXX,XXX
Pre-tax rate of return	<u>X.XX%</u>
Capital costs	\$X,XXX,XXX
Plus: Depreciation expense	<u>XXX,XXX</u>
Subtotal, excluding regulatory fee	\$X,XXX,XXX
Regulatory fee gross-up factor	<u>XXXX</u>
Total	<u><u>\$X,XXX,XXX</u></u>

(h) Computation of Sewer System Improvement Charge. –

(1) The SSIC shall be expressed as a percentage carried to two decimal places and shall be applied to the total utility bill of each customer under the utility's applicable service rates and charges.

(2) The SSIC shall be computed by dividing the annual SSIC Revenue Requirement by the projected revenues of the utility during the 12-month period following implementation of the charge.

(i) Semiannual Adjustments. – A utility may file a request for a SSIC adjustment no more frequently than semiannually.

(1) The request shall include the computation and supporting data for the adjustment.

(2) Cumulative SSIC Revenue Requirements may not exceed five percent of the total annual service revenues approved in the utility's last general rate proceeding.

(3) The procedural requirements set forth in subsection (f) of this Rule shall apply to requests for semiannual adjustments.

(j) Experience Modification Factor. – The SSIC shall be modified through the use of an experience modification factor (EMF) that reflects the difference between the SSIC Revenue Requirement and the revenues that were actually realized under the SSIC during the SSIC Period. The EMF shall remain in effect for a 12-month period. Pursuant to G.S. 62-130(e), any overcollection of reasonable and prudently incurred costs of the utility for eligible sewer system improvements to be refunded to a utility's customers through operation of the EMF shall include an amount of interest at such rate as the Commission determines to be just and reasonable, not to exceed the maximum statutory rate.

(k) Sewer System Improvement Charge Reset. – The SSIC shall be reset at zero as of the effective date of new base rates established in the utility's general rate case. Thereafter, only the incremental depreciation expense and capital costs of new eligible sewer system improvements that have not previously been reflected in the utility's rates shall be recoverable through the SSIC.

(l) Audit and Reconciliation. – The SSIC shall be subject to the following:

(1) Within 60 days following the end of each SSIC Period, each utility shall file a report, in a format prescribed by the Commission, reconciling its actual eligible sewer system improvement costs, actual SSIC revenues, and EMF computation.

(2) The Public Staff shall audit the utility's actual eligible sewer system improvement costs, actual SSIC revenues, and EMF computation, and shall file a report on its audit no later than four months after the end of the SSIC Period of the utility.

(m) Ongoing Three-Year Plan.–Within 60 days following the end of each SSIC Period, the utility shall file an updated three-year plan containing the information prescribed in Section (c)(1) of this Rule and any other information required by the Commission.

(n) Quarterly Filings with the Commission. – Within 45 days after the end of each calendar quarter, the utility shall file the following reports:

(1) A quarterly earnings report consisting of the following:

a. A balance sheet and income statement for the calendar quarter and calendar year to date for the utility;

b. A statement of the per books net operating income for the calendar quarter and calendar year to date for each rate division of the utility based on North Carolina ratemaking;

c. A statement of rate base at the end of the calendar quarter for each rate division of the utility based on North Carolina ratemaking; and

d. The number of customers and gallons sold for each month of the calendar quarter for each rate division by rate type (meter size, flat rate, etc.).

(2) A quarterly report of SSIC collections from customers consisting of amounts collected for the quarter by rate division and rate type.

(3) A construction status report which includes by rate division the following information for each eligible system improvement project:

- a. The costs incurred during the quarter;
- b. The cumulative amount incurred;
- c. The estimated total cost of each project;
- d. The estimated completion date; and
- e. The actual completion date.

(o) Elimination or Modification of SSIC Mechanism. – After notice to the utility and opportunity to be heard, the Commission may eliminate or modify any previously authorized SSIC mechanism upon a finding that it is not in the public interest.

(p) Burden of Proof. – The burden of proof as to whether a SSIC mechanism is in the public interest, the correctness and reasonableness of any SSIC, and whether the investment in the sewer system improvements was reasonable and prudently incurred shall be on the utility.