

**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.

(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	X.XX%
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>\$X,XXX,XXX</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.

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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).

(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.

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