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June 14, 2022

Ms. A. Shonta Dunston
Chief Clerk
North Carolina Utilities Commission
430 N. Salisbury Street
Raleigh, NC 27603

Via Electronic Submittal

Re: In the Matter of
Application by Aqua North Carolina, Inc. for Approval of Annual
Adjustment to Conservation Pilot Program Revenue Reconciliation
Charge / Credit
Docket No. W-218, Sub 526A
Aqua's Proposed Order Approving Conservation Pilot Program Revenue
Reconciliation Surcredit and Requiring Customer Notice

Dear Ms. Dunston:

Under cover of this letter and at the request of Aqua North Carolina, Inc. (Aqua or Company), we herewith provide Aqua's Proposed Order Approving Conservation Pilot Program Revenue Reconciliation Surcredit and Requiring Customer Notice.

If you should have any questions concerning this filing, please let me know.

Thank you and your staff for your assistance.

Sincerely,
/s/ David T. Drooz
David T. Drooz
Attorney for
Aqua North Carolina, Inc.

Enclosures

cc: All parties of record

A Pennsylvania Limited Liability Partnership

California Colorado Delaware District of Columbia Florida Georgia Illinois Minnesota Nevada
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STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH

DOCKET NO. W-218, SUB 526A

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

| | | |
|-------------------------------------|---|-----------------------------|
| In the Matter of |) | AQUA NORTH CAROLINA, INC.'S |
| Application by Aqua North Carolina, |) | PROPOSED ORDER APPROVING |
| Inc., 202 Mackenan Court, Cary, |) | CONSERVATION PILOT |
| North Carolina 27511, for Approval |) | PROGRAM REVENUE |
| of Annual Adjustment to |) | RECONCILIATION SURCREDIT |
| Conservation Pilot Program |) | AND REQUIRING CUSTOMER |
| Revenue Reconciliation |) | NOTICE |
| Charge/Credit |) | |

HEARD: Monday, May 16, 2022, at 2:00 p.m., Commission Hearing Room
2115, Dobbs Building, 430 North Salisbury Street, Raleigh, North
Carolina

BEFORE: Commissioner ToNola D. Brown-Bland, Presiding; Chair Charlotte A.
Mitchell, and Commissioners Daniel G. Clodfelter, Kimberly W.
Duffley, Jeffrey A. Hughes, Floyd B. McKissick, Jr., and Karen
Kermerait

APPEARANCES:

For Aqua North Carolina, Inc.:

David T. Drooz, Fox Rothschild LLP, 434 Fayetteville Street, Suite
2800, Raleigh, North Carolina 27601

For the Using and Consuming Public:

Megan Jost, Staff Attorney, Public Staff – North Carolina Utilities
Commission, 4326 Mail Service Center, Raleigh, North Carolina
27699-4300

BY THE COMMISSION: On February 14, 2022, Aqua North Carolina, Inc.
(Aqua or Company), filed a Conservation Pilot Program annual reconciliation
request (Reconciliation Request) pursuant to the Commission's Order Approving
Partial Settlement Agreement and Stipulation, Deciding Contested Issues,

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JUN 14 2022

Granting Partial Rate Increase, and Requiring Customer Notice (Sub 526 Rate Case Order) issued on October 26, 2020, in Docket No. W-218, Sub 526 (Sub 526 rate case).

Adoption of a Conservation Pilot Program and the revenue reconciliation process was a contested issue in the Sub 526 rate case. The Sub 526 Rate Case Order addresses the issue in Findings of Fact 30 - 44, where the Conservation Pilot Program was approved for four of the five service areas proposed by Aqua. The Findings of Fact in the Sub 526 Rate Case Order include, in pertinent part:

33. For the pilot program, Aqua NC proposed four usage tiers with inclining block rates and separate irrigation rates to be charged to residential water customers in the Arbor Run, Merion, Pebble Bay, and Bayleaf Master System service areas (a portion of the Aqua NC Water Rate Division) and The Cape service area (Fairways Water Rate Division). The Company stated that its pilot program proposal is contingent upon Commission approval of its proposed revenue reconciliation process specific to the pilot areas. According to Aqua NC, the purpose of the proposed revenue reconciliation process is to assure that the Company will receive its full authorized revenue requirement, no more and no less.

43. It is reasonable and appropriate that a Conservation Pilot Program be designed to maintain revenue sufficiency and stability for Aqua NC. A revenue reconciliation mechanism is appropriate to support the Company's reasonable opportunity to recover its full Commission-approved revenue requirements despite implementation of a Conservation Pilot Program.

44. For purposes of implementing the Conservation Pilot Program in a portion of the Aqua NC Water Rate Division, a revenue reconciliation process applicable only to the pilot group is in the public interest. It is reasonable and appropriate that a revenue reconciliation process as set forth by the Company be integral to the pilot program; however, such revenue reconciliation process allowed in this docket for this specific purpose is not intended to establish the process by which any future revenue reconciliation for Aqua NC or other regulated utilities related to actual consumption variances from

Commission-approved levels in general rate case proceedings as allowed by N.C.G.S. § 62-133.12A will be calculated.

On April 1, 2022, the Public Staff filed its Notice of Public Staff's Plan to Present Comments and Recommendations at the Commission's April 18, 2022, Regular Staff Conference (Notice). The Public Staff recommends a different revenue reconciliation calculation than proposed by Aqua.

On April 8, 2022, Aqua filed its response to the Public Staff's Notice, consisting of a second affidavit of Dean M. Gearhart, Manager, Rates and Planning for Aqua. Aqua asserted that the calculations proposed in the Public Staff's Notice are inconsistent with the Commission's finding in the Sub 526 Rate Case Order that a revenue reconciliation process "as set forth by the Company" is integral to the pilot program.

The Public Staff planned to present this matter to the Commission at its April 18, 2022, Staff Conference. However, at the request of the Commission, this matter was removed from the Staff Conference agenda.

On May 4, 2022, the Commission issued its Order Scheduling Oral Argument and Requiring Verified Responses by the Parties. This order scheduled oral argument for May 16, 2022, and required the parties to respond in writing by May 11, 2022, to questions set out by the Commission.

On May 11, 2022, both parties filed their verified written responses to the Commission's questions. On May 16, 2022, oral argument was held as scheduled. On June 14, 2022, both parties filed their respective proposed orders.

Based on the Reconciliation Request, the records of the Commission, the filed Notice of the Public Staff, the filed Aqua response to the Public Staff's Notice,

the verified responses of both parties to the Commission's written questions, the parties' positions presented at the May 16, 2022, oral argument, the Sub 526 Rate Case Order, and the applicable statutes and Commission Rules, the Commission makes the following:

FINDINGS OF FACT

1. Aqua is a corporation duly organized and authorized to do business under the laws of the State of North Carolina. Aqua is a franchised public utility providing water and sewer utility service to customers in North Carolina, and is subject to the Commission's jurisdiction.

2. In the Sub 526 rate case, Aqua proposed to implement a Conservation Pilot Program for residential customers in five of the Company's service areas in North Carolina, including a revenue reconciliation process. The Public Staff opposed the Conservation Pilot Program. The Commission approved the Conservation Pilot Program for four of the five service areas in the Aqua proposal.

3. The purpose of the revenue reconciliation process is to assure that Aqua will receive its full authorized revenue requirement, no more and no less, for the water systems included in the pilot program, consistent with N.C.G.S. § 62-133.12A and "as set forth by the Company" in the Sub 526 rate case.

4. As set forth in the Sub 526 rate case by Aqua witness Thill, "the proposed revenue reconciliation calculation is based on 'average per customer usage.'" (T 4, p 37) Aqua witness Thill's Direct Exhibit 4 in the Sub 526 rate case provided revenue reconciliation sample calculations for illustrative purposes.

Those sample calculations all use the “Average per Customer Usage Excess/Deficit” to determine surcredits and surcharges.

5. In the Sub 526 rate case, the pilot program-annualized billing determinants were 81,972 bills and 562,713,732 gallons, resulting in a monthly average consumption per bill of 6,865 gallons. The pilot program service revenue requirement authorized by the Commission in the Sub 526 rate case was \$5,482,975, comprised of \$1,696,820 for base facility charges and \$3,786,155 for consumption charges.

6. During the 12 months of 2021, Aqua issued 83,550 bills for 579,753,300 gallons, resulting in a monthly average consumption per bill of 6,939 gallons in the pilot service areas. The actual pilot program service revenue was approximately \$5,691,105, comprised of \$1,729,485 for base facility charges and \$3,961,620 for consumption charges.

7. In its Reconciliation Request, Aqua compared the monthly average bill amount for consumption charges utilizing the number of bills and total consumption from the Sub 526 rate case (\$46.19) to the actual 12 months of 2021 (\$47.42). This resulted in a revenue excess of \$1.23 per bill. Aqua initially proposed to refund a total of \$102,766.50, which is the revenue excess of \$1.23 per bill multiplied by the 83,550 actual bills issued, to customers in the pilot program service areas. In subsequent filings, Aqua corrected its calculation to track the methodology set forth in witness Thill’s Sub 526 rate case testimony and in the Sub 526 Rate Case Order, resulting in a proposed refund of \$102,226.19 before

interest. The corrected refund amount of \$102,226.19 before interest is reasonable and appropriate.

8. The Public Staff recommended that the entire \$208,130 (\$5,691,105 minus \$5,482,975) of service revenue in excess of the revenue requirement approved by the Commission in the Sub 526 rate case be refunded. At oral argument, the Public Staff suggested an alternative refund of all service revenue in excess of the revenue requirement approved by the Commission in the Sub 526 except for Basic Facility Charge revenues from customer growth. The Public Staff's recommendation is not appropriate because it differs from the reconciliation methodology based on average per customer usage, as proposed by witness Thill in the Sub 526 rate case and approved in the Sub 526 Rate Case Order. It is also inappropriate because it would result in a mismatch of customer growth revenues to customer growth expenses.

9. In the Sub 526 rate case, Aqua witness Thill proposed issuing monthly flat rate bill credits over several months. However, the Reconciliation Request proposed issuing a one-time, flat rate bill credit to the number of pilot program customers' existing as of December 2021. Aqua's corrected amount of refund, before interest, is \$14.48 per customer. A one-time bill credit of \$14.48 per customer, before interest, is reasonable and will benefit customers. The bill credit should be made in the next possible billing cycle following issuance of this order.

10. To the extent the number of customers receiving refunds is different from the 7,059 customers at the end of 2021, future reconciliations shall account

for the difference so that ultimately the refund for excess revenue for 2021 will be \$102,226.19 before interest.

11. Aqua initially proposed that there should not be interest added to the excess revenue to be refunded to customers, or in the alternative that the interest rate match the Company's authorized overall rate of return of 6.81%. At oral argument Aqua withdrew its proposal of zero interest, and recommended that it pay an interest rate of 6.81% to customers on the refund. The Company reasoned that this rate would not force it to pay an interest rate greater than the return it was authorized to earn. The 6.81% interest rate on refunds is reasonable and appropriate.

12. It is also reasonable and appropriate for Aqua's authorized overall rate of return to be used to determine interest on surcharges and credits in future reconciliations, as proposed by Aqua.

DISCUSSION AND CONCLUSION

Aqua's status as a North Carolina corporation duly authorized to provide water and sewer service to specified service areas, as approved by and regulated by the Commission, is a matter of record and not contested.

In the Sub 526 Rate Case Order, the Commission approved a Conservation Pilot program with inclining block rates for the Arbor Run, Merion, Pebble Bay, and Bayleaf Master System service areas. An annual revenue reconciliation is an integral part of the Conservation Pilot program.

On February 14, 2022, Aqua filed its first annual revenue reconciliation request (February 14 Request) for the Conservation Pilot program. The

February 14 Request included an affidavit showing that 2021 actual revenue for the pilot service areas was \$1.23 per bill higher than used for rate design in the Sub 526 rate case. Aqua multiplied the \$1.23 excess revenue per bill times actual 2021 bill count of 83,550 to equal an excess revenue amount for 2021 of \$102,766.50. Aqua proposed to refund \$14.56 per customer based on dividing the excess revenue (\$102,766.50) by the number of year-end customer count (7,059).

On April 1, 2022, the Public Staff filed a notice (April 1 Notice) that challenged the revenue reconciliation methodology of the Company and made different recommendations. The Public Staff recommended that the entire service revenue excess of \$208,130 for the pilot service areas be refunded. They reasoned that the Sub 526 Rate Case Order provided that the purpose of the revenue reconciliation was to assure that Aqua receive its authorized revenue requirement, no more and no less. They noted that Thill Direct Exhibit 4 in the Sub 526 rate case assumed no customer growth.

On April 8, 2022, Aqua filed a response (Aqua April 8 Response) to the Public Staff's April 1 Notice. The Company argued that the Sub 526 Rate Case Order approved a revenue reconciliation methodology "as set forth by the Company" in the Sub 526 rate case. Aqua cited the Sub 526 Rate Case Order as finding that the methodology set forth by the Company is based on the average per-customer use, not on the gross level of revenue. Aqua observed that the Public Staff's recommendation would impose a cap on actual revenue based on the revenue requirement used in the Sub 526 rate case, thereby requiring refund of all revenues from customer growth in addition to refund of revenues from increased

per customer usage. The Aqua April 8 Response did revise the calculation methodology from the February 14 Request to more accurately track the methodology set forth in witness Thill's testimony in the Sub 526 rate case. Aqua stated that its method based on average per customer usage, including the usage from 2021 customer growth, would comply with the Sub 526 Rate Case Order (Finding number 33) that the Company "receive its full authorized revenue requirement, no more and no less."

On May 4, 2022, the Commission issued an order that required the parties to file verified responses to nine questions, and set the matter for oral argument. Among those questions, the Commission observed there was a math error in the Aqua April 8 Response.

Aqua filed its verified responses to the Commission questions on May 11, 2022 (Aqua May 11 Responses). The Company agreed that it had a math error in the Aqua April 8 Response, and it submitted revised affidavits to show the corrected refund amount of \$102,226.19. The Aqua May 11 Responses included the following sentence-by-sentence revenue reconciliation method set forth in witness Thill's testimony in the Sub 526 rate case, as quoted by the Commission in the Sub 526 Rate Case Order, and added the numerical calculations for the 2021 data, as follows:

1. Dividing the volumetric revenue requirement by the number of bills used in determining rates provides Aqua NC with the Revenue per Bill - as Authorized. [$\$3,786,155$ in block revenue / $81,972$ bills = $\$46.19$ per bill]
2. Aqua NC would perform a similar calculation using actual data in the 12 full months following implementation of rates to determine the Revenue per Bill - Actual. [$\$3,961,620$ in block revenue / $83,550$ bills = $\$47.42$ per bill]

3. The difference between those actual and authorized averages would define the Company's Average per Customer Usage Excess or Deficit. [$\$47.42 - \$46.19 = \$1.23$]
4. Dividing that Excess or Deficit by the Revenue per Bill as Authorized provides Aqua NC Excess or Deficit Rate. [$\$1.23 / \$46.19 = 2.7\%$]
5. The Rate is then multiplied by the originally authorized volumetric revenue to determine the value of the excess or deficit. [$\$3,786,155 \times 2.7\% = \$102,226.19$]

The Public Staff also filed its verified responses to Commission questions on May 11 (Public Staff May 11 Responses). The Public Staff argued that Aqua's revenue reconciliation was inconsistent with the methodology of witness Thill in three respects.

First, Aqua rounded its excess rate to 2.7%, whereas Thill Direct Exhibit 4 used two decimal places. Using Thill's rounding convention would mean an excess rate of 2.66%, and therefore under the Aqua calculation the refund amount would be \$100,711.72.

Second, Aqua divided the excess revenue amount by year-end bill count to get a one-time bill credit amount per customer, whereas the Thill Direct Exhibit 4 divided excess revenue by the actual bill count (bills over twelve months).

Third, Aqua's revenue reconciliation recognized that there was customer growth in 2021, whereas Thill Direct Exhibit 4 assumed no growth in the number of customer bills between the rate case and the hypothetical year of actual pilot experience.

The Public Staff May 11 Responses further argued that the Aqua reconciliation request was not based on average per customer use, but instead

was based on average per bill revenue, and that it was appropriate to cap Aqua's revenues at the level used in the rate case.

The parties supported their respective positions in oral argument on May 16, 2022. The Company maintained the Public Staff's methodology would be a disincentive to conservation rates because the utility would have to refund revenues from growth, in addition to any revenue difference caused by under- or over-conservation by each customer, while still paying for the additional costs of serving a larger number of customers. The Public Staff maintained that revenue reconciliation lowered the Company's risk, so it was reasonable to require a refund of revenues from customer growth.

At oral argument, each party offered a modification to its filed position. Aqua stated that it proposed to pay 6.81% interest on the refunds, and withdrew its prior zero interest position. The Public Staff conceded that the Commission could allow Aqua to retain the Basic Facility Charge revenue from customer growth (T pp. 34-35) but that there still should be a refund of volumetric service revenues from customer growth.

Having reviewed the filings and oral arguments of the parties, the Commission makes the following conclusions.

A Revenue Reconciliation Based on Average Per Customer Usage, as Recommended by Aqua, is Proper

Finding of Fact No. 44 in the Commission's Sub 526 Rate Case Order states in relevant part: "It is reasonable and appropriate that a revenue reconciliation process *as set forth by the Company* be integral to the pilot program...." (Emphasis added)

The process set forth by the Company is a reconciliation based on average per customer usage. In contrast, the Public Staff recommended a process that would refund all actual revenues in excess of the revenue requirement set in the Sub 526 rate case.

The Aqua methodology was set forth in the testimony of Company witness Thill, and quoted at page 105 of the Sub 526 Rate Case Order. The parties agree as to the volumetric revenue requirement and number of bills used in the rate case, the actual volumetric revenue requirement and number of bills in 2021, and the year-end number of customers in the pilot service areas. The uncontested numbers in the methodology set forth by the Company in the rate case produce the calculation quoted above from the Aqua May 11 Responses. It results in excess 2021 volumetric revenue of \$102,226.19. When divided by the 7,059-year end number of customers, a one-time bill credit of \$14.48 before interest is proper.

The Public Staff relies in part on wording from the Sub 526 Rate Case Order to support its argument that revenues should be capped at the revenue requirement set in the rate case. In particular, Finding of Fact No. 33 states “According to Aqua NC, the purpose of the proposed revenue reconciliation process is to assure that the Company will receive its full authorized revenue requirement, no more and no less.” Finding of Fact No. 43 states “A revenue reconciliation mechanism is appropriate to support the Company’s reasonable opportunity to recover its full Commission-approved revenue requirements despite implementation of a Conservation Pilot Program.” These statements must be interpreted in light of the full Sub 526 Rate Case Order, not in isolation. The

Commission intended, consistent with Aqua’s testimony, to protect both the customers and the Company from unexpected revenue impacts due specifically to the implementation of conservation rates. This conclusion is supported by the following portions of the Sub 526 Rate Case Order:

...as a general matter of fairness there must be a settlement process to ensure that neither the pilot customer group (as a whole) nor the Company is unduly harmed or enriched *by this program*. The intent of the revenue reconciliation is that the Company should receive its full authorized revenue requirement, no more and no less.

(pp. 123; emphasis added) Thus the reconciliation process is intended to limit Aqua to its full revenue requirement with respect to the impacts of the pilot conservation rates (“by this program”). It is not intended to be a true-up for unrelated variables that affect gross revenue, such as customer growth. The “full authorized revenue requirement” wording is qualified in the preceding sentence by the focus on impacts of over- or under-consumption from that predicted to result from the conservation pilot rates.

The Commission understands that average per customer consumption is not solely a measure of conservation. Average per-customer consumption could be greater than the level anticipated in the rate case due to drought or other factors beyond rate-induced conservation. (T pp. 17) The Commission expects Aqua to provide analysis, after acquiring more experience, to distinguish how much conservation rates as opposed to other factors affected usage. (T pp. 19)

In any event, the Commission concludes that average per customer usage is a better approach to revenue reconciliation than capping the gross revenues to the rate case level because the cap on gross revenues incorporates the effect of

customer growth. The presence or absence of customer growth is different from the impact of conservation rates, and thus outside the intended purpose of the Conservation Pilot and its revenue reconciliation.

The issue of capping revenues in the reconciliation was directly addressed in the Sub 526 rate case:

Witness Thill testifies that customer growth is not included in the revenue reconciliation computation. Consistent with the explicit language of House Bill 529 (Session Law 2019-88) which was signed into law on July 8, 2019, the proposed revenue reconciliation calculation is computed based on “average per customer usage.” To compute the reconciliation adjustment at a gross level of revenue, rather than at a per customer average level, would ignore that a portion of future revenue may be attributed to customers added after the test year....

(Sub 526 Rate Case Order pp. 105) The testimony of Aqua’s witness is critical to the Commission’s decision because the Commission approved the reconciliation method “as set forth by the Company.” The method set forth by witness Thill in the Sub 526 rate case involves:

1. Dividing the volumetric revenue requirement by the number of bills used in determining rates provides Aqua NC with the Revenue per Bill - as Authorized.
2. Aqua NC would perform a similar calculation using actual data in the 12 full months following implementation of rates to determine the Revenue per Bill - Actual.

What witness Thill meant, and the Commission approved, is that the refund amount should be based on average per customer consumption and not include excess revenues due to customer growth.

The Public Staff argued that the examples in Thill Direct Exhibit 4 in the Sub 526 Rate Case showed no customer growth, and therefore the reconciliation calculation should refund revenues based on total revenue requirement and not

on average per customer usage. The Commission does not agree. First, witness Thill made clear throughout his testimony that he was recommending a calculation based on average per customer usage, and the Commission approved that methodology. The Public Staff's interpretation of Thill Direct Exhibit 4 would be inconsistent with the need for a reconciliation based on average per customer usage. Second, the Public Staff errs in reasoning that Thill Direct Exhibit 4 shows the Company proposed a method that requires refund of all growth revenues. Thill Direct Exhibit 4 shows in Scenario 2 an example where actual average per customer usage is 1% greater than anticipated in the rate case, without customer growth. It would be a complete misreading of that exhibit to conclude that any increase in actual revenue requirement above the amount anticipated in the rate case should be refunded because the hypothetical example in the exhibit does not assume customer growth. The assumptions in the exhibit do not preclude actual experience that is different; indeed, it would be virtually impossible for an example provided at the time of the rate case to exactly predict the actual experience that will occur in the year after the rate case.

In the Sub 526 rate case, the Commission noted that N.C.G.S. § 62-133.12A authorized adoption of a rate adjustment mechanism to “track and true up variations in *average per customer usage*.” That observation was immediately followed with: “The Commission concludes that it is reasonable and appropriate that a revenue reconciliation process *as set forth by the Company* be integral to the pilot program....” (Sub 526 Rate Case Order pp. 124; emphasis added) The connection between these two sentences in the Sub 526 Rate Case Order

recognizes that the statutory approval for reconciliations based on average per customer usage is the methodology proposed by the Company.

The issue of whether to reconcile pilot service area revenues on average per customer usage or on total revenue requirement was disputed by the parties and decided by the Commission in the Sub 526 rate case. Clearly, the Commission did not impose a cap of the nature proposed by the Public Staff in the Sub 526 rate case. The Public Staff did not file exceptions to the Sub 526 Rate Case Order, did not appeal that Order, and has not shown a compelling change of circumstances that might support reconsideration of that Order. The issue was litigated once, and should not be relitigated in the same proceeding with the same parties. The Commission stands by its Sub 526 Rate Case Order.

The Public Staff Recommendation Would be a Disincentive to Conservation Rates and Undermine Public Policy

At oral argument, Aqua indicated that a revenue reconciliation that capped the pilot area revenues to the revenue requirement set in the rate case, as proposed by the Public Staff, would be a disincentive to conservation rates. The reason is that customer growth creates additional revenues and additional costs. If the Company must refund the additional revenues but still incur the additional costs, it will necessarily realize a lower rate of return than authorized, at least with regard to the customer growth. Water utilities that expect customer growth simply are not going to support conservation rates where the reconciliation method reduces the rate of return below the level authorized by the Commission.

The Commission has sought to advance public policy by seeking comments on “rate design proposals that may better achieve revenue sufficiency and stability

while also sending appropriate efficiency and conservation signals to consumers.” Docket No. W-100, Sub 59, March 20, 2019, Order Establishing Generic Proceeding and Requiring Comments. Aqua’s Conservation Pilot and revenue reconciliation proposal in the Sub 526 rate case are a positive response to the Commission’s public policy interest in exploring effective conservation rates. A reconciliation that refunds revenues from customer growth in addition to any excess revenues caused by change in average per customer usage would burden Aqua with a financial loss separate and apart from the purpose of the pilot conservation rates. Utility support for conservation rates, which the Commission seeks to promote as a matter of public policy, would be undermined if the Commission requires the utility to accept a lower rate of return as part of the conservation rate reconciliation. Additionally, the message to customers receiving an unrelated refund for growth revenues would undermine the intended purpose of the usage behavior expected to drive conservation patterns from the installation of tiered rates.

Retroactive Ratemaking

The 2021 revenues in Aqua’s pilot service areas result from (1) average per customer usage higher than expected in the Sub 526 rate case, and (2) customer growth.¹ Customer growth revenues are separate from the impact of conservation

¹ This is shown in the February 14, 2022, affidavit of Dean Gearhart, Aqua’s Manager of Rates and Planning. That affidavit shows the Sub 526 rate case annual bill count for the Conservation Pilot Program service areas was 81,972, with an average usage of 6,865 gallons per bill. It shows the actual 2021 annual bill count was 83,550, meaning customer growth occurred, and also an average usage of 6,939 gallons per bill, meaning there was less conservation than projected.

rates. Customer growth revenue is not normally refunded; to do so would be retroactive ratemaking.

To avoid unlawful retroactive ratemaking, a true up or reconciliation of actual revenues to the revenue requirement in a rate case would have to be grounded in specific statutory authority or in a lawful rate case mechanism. Neither exists for a total revenue reconciliation that would include customer growth. There is no such rate case mechanism because the Commission approved a reconciliation method based on average per customer usage, not total revenues. There is no statutory authority because the one applicable statute, N.C.G.S. § 62-133.12A, provides for adjustment based on average per customer usage. Indeed, the Sub 526 Rate Case Order links the mechanism approved by the Commission to that statute:

The Commission acknowledges that N.C.G.S. § 62-133.12A allows the Commission to “adopt, implement, modify, or eliminate a rate adjustment mechanism for one or more of the company’s rate schedules to track and true-up variations in average per customer usage from levels approved in the general rate case proceeding” upon a finding that such mechanism is appropriate to track and true-up variations in average per customer usage and is in the public interest. The Commission concludes that it is reasonable and appropriate that a revenue reconciliation process as set forth by the Company be integral to the pilot program....

(Sub 526 Rate Case Order pp. 123-24) The Commission does not approve of a refund based on total revenues that would be unlawful retroactive ratemaking. The Commission does approve a reconciliation methodology, as proposed by the Company, that complies with N.C.G.S. § 62-133.12A truing up variations in actual average per customer usage from levels approved in the general rate case proceeding.

Mismatch of Revenues and Expenses

The Public Staff recommendation would also violate the regulatory principle of matching revenues to expenses. This principle was alluded to in the Sub 526 rate case testimony of Aqua witness Thill:

To compute the reconciliation adjustment at a gross level of revenue, rather than at a per customer average level, would ignore that a portion of future revenue may be attributed to customers added after the test year.... [U]sing a prospective customer count *without also incorporating future cost increases should not be permitted.*

(Sub 526 Rate Case Order pp. 105; emphasis added) The Commission does not approve a reconciliation method that would violate the matching principle.

A reconciliation that capped revenues for the pilot areas at the level set in the Sub 526 rate case would result in refund of revenues generated by customer growth in addition to revenues generated by greater average per customer usage. Customer growth does not occur without additional costs to the utility. To force Aqua to refund the customer growth revenues while incurring the customer growth costs would result in a “mismatch” that is improper in the ratemaking framework.

Refund Modifications Proposed by the Parties

While the methodology for calculating excess revenue to be refunded was established in the Sub 526 rate case through the testimony of Aqua witness Thill, and approved in the Sub 526 Rate Case Order, there nonetheless are reconciliation matters raised by the parties that are appropriate for Commission review and decision.

First is the question of whether Aqua should pay interest on the refunds to customers. Initially, Aqua initially proposed zero interest, with a secondary proposal

of interest at 6.81%. The Public Staff proposed 10% interest. At oral argument Aqua withdrew its zero-interest recommendation and proposed 6.81%. The Company noted that a 10% interest rate would force it to pay an interest rate higher than the rate of return it was authorized to earn. The Public Staff argued that a 10% interest rate is commonly approved by the Commission for customer refunds, although at oral argument they also stated, “we can understand how the Commission could end up at a 6.81 percent.” (T pp. 35) The Commission notes that under N.C.G.S. § 62-130(e), it may, but is not required, to approve an interest rate up to 10% per annum. A 6.81% rate is reasonable in the present case because it treats the parties even-handedly: Aqua must pay interest equal to the return that the Company was given the opportunity to earn in the Sub 526 rate case.

Second is the offer by the Public Staff at oral argument to modify its proposal so that Aqua would refund only the volumetric portion of the revenue from customer growth (approximately \$175,465) and would retain the base facilities charge revenue from customer growth (approximately \$32,665). While the Commission appreciates the spirit of compromise that this represents, the offer would still be inconsistent with the reconciliation methodology approved in the Sub 526 Rate Case Order, inconsistent with the matching principle and public policy as discussed above, and unlawful.

Third is the Public Staff position that Aqua departed from the methodology set forth in the Sub 526 rate case by calculating the excess revenue rate at 2.7% instead of carrying it out an additional decimal place as was shown on Thill Direct Exhibit 4. As set forth in the Public Staff May 11 Responses, the use of an

additional decimal place would reduce the Company's excess revenue calculation from \$102,226.19 to \$100,711.72. In other words, the discrepancy noted by the Public Staff would mean \$1,514.47 less to refund to customers. At oral argument, Aqua agreed that Thill Direct Exhibit 4 used an additional decimal place that was omitted in the rounding of the Company's refund calculation, and stated that it did not have a position on how the Commission should resolve that difference. The Commission concludes that the calculation by Aqua resulting in an excess revenue amount of \$102,226.19 is reasonable, notwithstanding the rounding that was not in Thill Direct Exhibit 4, because (a) the difference is immaterial, and (b) the rounded amount used by Aqua actually favors customers in this instance.

Fourth, as the Public Staff pointed out, Thill Direct Exhibit 4 recommended refunds spread across several months whereas the Aqua revenue reconciliation proposed a one-time bill credit. The Public Staff is correct that the Company recommendation is a discrepancy from the process "as set forth by the Company" in the rate case. However, the Commission concludes this discrepancy is reasonable because (a) it was recommended by the Public Staff and accepted by Aqua, and (b) it will result in the full refund being credited to customers sooner than the approach in Thill Direct Exhibit 4.

On May 4, 2022, the Commission issued an order that posed certain questions to the parties regarding the reconciliation methodology. Question No. 1 includes the following inquiry: "Is the correct calculation $\$3,786,155 \times 2.7\% = \$102,226.19$ which would then be divided by the year-end 2021 bill count of 7,059 to equal a one-time refund of \$14.48 per customer before interest, if any?" Aqua

answered “yes.” However, the customers who are in the pilot service areas at the time refunds will be made are not entirely the same as the 7,059 customers who were in the pilot service areas on December 31, 2021. Consequently, the amount of refund issued as bill credits to the customers in the pilot service areas could be more or less than the \$102,226.19 of excess revenues. This situation was anticipated by witness Thill’s testimony in the Sub 526 rate case: “Any over or under recovery as a result of fluctuations between the actual components of the calculation and the assumed components in determining the surcredits/surcharges would roll into the subsequent period’s calculation of the excess/deficit.” (Sub 526 Rate Case Order, p 105) The Commission concludes that to the extent the number of customers receiving refunds is different from the 7,059 customers at the end of 2021, future reconciliations shall account for the difference so that ultimately the refund for excess revenue for 2021 will be \$102,226.19 before interest. This conclusion is consistent with the methodology proposed by witness Thill in the Sub 526 rate case, and it is reasonable.

SUMMARY

For the reasons set forth herein, and based on the facts of record in this case regarding the implementation of a Conservation Pilot Program revenue reconciliation, the Commission concludes that that the revenue reconciliation methodology proposed by Aqua is reasonable and appropriate; that the correct amount to refund by one-time bill credit is \$102,226.19 plus interest at the rate of 6.81% per annum; and the bill credit should be made in the next available billing cycle.

IT IS, THEREFORE, ORDERED as follows:

1. That Aqua shall implement the recommended Conservation Pilot Program refund set forth herein, to be issued as part of Aqua’s next billing cycle; and

2. That Aqua shall mail to each of the customers in the Conservation Pilot Program service areas with the next regularly scheduled customer billing a copy of the attached Customer Notice, and Aqua shall file the attached Certificate of Service, properly signed and notarized, not later than 45 days after the issuance of this Order.

ISSUED BY ORDER OF THE COMMISSION.

This the ____ day of _____, 2022.

NORTH CAROLINA UTILITIES COMMISSION

A. Shonta Dunston, Chief Clerk

STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH

DOCKET NO. W-218, SUB 526A

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

| | | |
|-------------------------------------|---|------------------------|
| In the Matter of |) | |
| Application by Aqua North Carolina, |) | |
| Inc., 202 MacKenan Court, Cary, |) | NOTICE TO CUSTOMERS OF |
| North Carolina 27511, for Approval |) | CONSERVATION PILOT |
| of Annual Adjustment to |) | PROGRAM REFUND |
| Conservation Pilot Program |) | |
| Revenue Reconciliation |) | |
| Charge/Credit |) | |

NOTICE IS HEREBY GIVEN that the North Carolina Utilities Commission has issued an Order authorizing Aqua North Carolina, Inc. to issue a one-time bill credit in the amount of \$14.48 plus interest to each water utility customer in the Arbor Run, Merion, Pebble Bay, and Bayleaf Master System service areas. The purpose of this bill credit is to refund surplus revenues received by Aqua North Carolina, Inc., due to greater average per customer usage than anticipated under the Conservation Pilot Program.

The Commission’s Order setting forth its findings and conclusions concerning this proceeding can be viewed on the Commission’s website at www.ncuc.net, under the “Docket Search” feature, utilizing Docket No. W-218, Sub 526A.

ISSUED BY ORDER OF THE COMMISSION.

This the ____ day of _____, 2022.

NORTH CAROLINA UTILITIES COMMISSION

A. Shonta Dunston, Chief Clerk

CERTIFICATE OF SERVICE

I, _____, mailed with sufficient postage or hand delivered to all affected customers copies of the attached Order issued by the North Carolina Utilities Commission in Docket No. W-218, Sub 526A, and the Order was mailed, or hand delivered by the date specified in the Order.

This the ____ day of _____, 2022.

By: _____
Signature
Aqua North Carolina, Inc.

The above-named applicant, _____, personally appeared before me this day and, being first duly sworn, says that the Commission's Order dated _____ issued in Docket No. W- 218, Sub 526A, was mailed or hand delivered to all affected customers as required by the Order.

Witness my hand and notarial seal, this the ____ day of _____, 20____.

Notary Public

Printed or Typed Name

(SEAL) My Commission Expires: _____
Date