

**NORTH CAROLINA
PUBLIC STAFF
UTILITIES COMMISSION**

December 1, 2023

Ms. A. Shonta Dunston, Chief Clerk
North Carolina Utilities Commission
4325 Mail Service Center
Raleigh, North Carolina 27699-4300

Re: Docket No. W-100, Sub 67
Investigation Regarding Consolidation of Water and Wastewater Utilities
and the Utilization of Uniform Rates

Dear Ms. Dunston:

Pursuant to the Order Scheduling Technical Conference issued in the above referenced docket on September 18, 2023, and the Order Rescheduling issued October 18, 2023, please find enclosed the Public Staff's presentation materials for the technical conference set for Wednesday, December 6, 2023. Charles M. Junis, Director of the Public Staff's Water, Sewer, and Telephone Division will participate in the technical conference on behalf of the Public Staff.

By copy of this letter, I am serving all parties of record.

Sincerely,

Electronically submitted
/s/ Megan Jost
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**Docket No. W-100, Sub 67
Uniform Rates**

December 6, 2023

**Charles M. Junis, PE
Director, Water, Sewer, and Telephone
Public Staff - NCUC**

Commission Directive

1. Whether the uniform rate paradigm continues to serve the public interest in North Carolina.

What is the uniform rate paradigm?

USEPA – NARUC at page 1:

“Consolidated rates or single-tariff pricing is the use of a unified rate structure for multiple water (or other) utility systems that are owned and operated by a single utility, but that may or may not be contiguous systems or physically interconnected. Under a system of single-tariff pricing, all customers of the utility pay the same rate for service, even though the individual systems providing service may vary in terms of the number of customers served, operating characteristics, and stand-alone costs. Single-tariff pricing essentially allows for allocating the average costs of combined systems in the course of ratemaking.”

Simply put, uniform rates serve the public interest on a case-by-case basis. Uniform rates come in different shapes and sizes. There are potential benefits and detriments associated with the uniform rate paradigm that should be considered.

Potential Benefits

From page 2 of the Commission's Order in this docket:

“First, the Commission has recognized that consolidating the costs associated with many systems into a single rate division spreads those costs over a larger customer base, which provides downward pressure on rates. The uniform rate paradigm spreads risks across customers to their benefit, as, while customers share in the risk of the need for significant investment in one system or the occurrence of significant unexpected costs by one system, that risk is borne by a much larger body of customers. Second, the ability to spread costs over a larger customer base has encouraged and enabled larger, well-capitalized utilities like Aqua North Carolina, Inc. (Aqua) and Carolina Water Service, Inc. of North Carolina (CWSNC) to acquire financially or operationally troubled water and wastewater systems in North Carolina that are in need of significant investment and to make that necessary investment in the acquired systems. Third, the Commission has recognized the administrative and regulatory efficiencies that arise from the uniform rate paradigm. As a consequence, both Aqua and CWSNC have uniform rate divisions for both water and sewer service.” (Emphasis added).

Rate stability – smoothing of rate impacts from necessary expenditures such as replacements and improvements or new testing requirements.

Rate parity – equalizing rates between low- and high-cost systems, including when costs contributing to rates are beyond the utility's and customers' control.

Rate equality – customers pay the same price for comparable service.

Potential Detriments

Desensitization – dulling cost impacts and justifying paying a premium or for infrastructure twice, inflating spending on capital projects and expenses, or obscuring unreasonable executive compensation.

Disincentive – failing to promote innovation and cost controls.

Erosion – undermining the cost-of-service matching principle.

The case study of Hampton Roads Sanitation District “shows how financial impacts can be uneven and, in some cases, individual communities and ratepayers may even be worse-off financially with full consolidation even if the region as a whole is better off.” US Water Alliance, at page 29.

USEPA – NARUC

Summary of Select Arguments in Favor and Against Single-Tariff Pricing

Select Arguments in Favor of Single-Tariff Pricing	Select Arguments Against Single-Tariff Pricing
<ul style="list-style-type: none"> <input type="checkbox"/> Mitigates rate shock to utility customers (17) <input type="checkbox"/> Lowers administrative costs to the utilities (16) <input type="checkbox"/> Provides incentives for utility regionalization and consolidation (15) <input type="checkbox"/> Physical interconnection is not considered a prerequisite (13) <input type="checkbox"/> Addresses small-system viability issues (13) <input type="checkbox"/> Improves service affordability for customers (12) <input type="checkbox"/> Provides ratemaking treatment similar to that for other utilities (10) <input type="checkbox"/> Facilitates compliance with drinking water standards (9) <input type="checkbox"/> Overall benefits outweigh overall costs (9) <input type="checkbox"/> Promotes universal service for utility customers (8) <input type="checkbox"/> Lowers administrative cost to the commission (8) <input type="checkbox"/> Promotes ratepayer equity on a regional basis (6) <input type="checkbox"/> Encourages investment in the water supply infrastructure (5) <input type="checkbox"/> Promotes regional economic development (3) <input type="checkbox"/> Encourages further private involvement in the water sector (2) <input type="checkbox"/> Other: Can be consistent with cost-of-service principles (1) and found to be in the public interest (1) 	<ul style="list-style-type: none"> <input type="checkbox"/> Conflicts with cost-of-service principles (14) <input type="checkbox"/> Provides subsidies to high-cost customers (12) <input type="checkbox"/> Not acceptable to all affected customers (10) <input type="checkbox"/> Considered inappropriate without physical interconnection (8) <input type="checkbox"/> Distorts price signals to customers (7) <input type="checkbox"/> Fails to account for variations in customer contributions (6) <input type="checkbox"/> Justification has not been adequate in a specific case (or cases) (6) <input type="checkbox"/> Discourages efficient water use and conservation (4) <input type="checkbox"/> Encourages growth and development in high-cost areas (4) <input type="checkbox"/> Undermines economic efficiency (3) <input type="checkbox"/> Provides unnecessary incentives to utilities (2) <input type="checkbox"/> Not acceptable to other agencies or governments (2) <input type="checkbox"/> Insufficient statutory or regulatory basis or precedents (2) <input type="checkbox"/> Overall costs outweigh overall benefits (2) <input type="checkbox"/> Encourages overinvestment in infrastructure (1)

Source: Author's construct. See Tables E3 and E4. Numbers in parentheses represent number of mentions (out of 21 applicable survey responses).

Commission Directive

2. Whether the path to uniformity should or must change in light of the challenges faced by the water and wastewater utilities in North Carolina.

Is there a defined “path to uniformity” that has been created and followed consistently?



“Uniform” Rates for Water and Sewer Utilities

Aqua

- Five rate divisions
- 24 purchased service rates
- Approximately 738 water systems and 59 sewer systems

Carolina Water Service

- Four rate divisions
- 14 purchased service rates
- Approximately 93 water systems and 38 sewer systems

Old North State Water Company

- One water rate division
- Two purchased service rates
- Approximately 44 water systems and 8 sewer systems

Red Bird Utility Operating Company

- System specific rates
- Approximately two water systems and five sewer systems
- 10 pending CPCN and transfer dockets

What are the challenges? From page 2 of the Commission's Order in this docket:

“Water and wastewater systems in North Carolina face an increasing number of challenges to their provision of safe, adequate, reliable, and affordable service. Replacing aging or failing infrastructure, complying with environmental regulations, addressing secondary water quality issues, planning for and implementing treatment for PFOS/PFOA3 and other chemicals of emerging concern, protecting against physical and cyber threats to infrastructure, and generally responding to customer expectations regarding service quality are but several of these challenges.”





The regulatory framework has changed considerably over the past 10 years. How and where growth is occurring is also changing. While there continue to be satellite communities, we are also seeing infill and municipal expansion. These changes in light of the challenges should be considered.

We must be careful not to create new problems that outweigh the benefits. For example, a high cost, low supply system whose customers do not receive price signals that reflect the cost of service may see discretionary demand increase and prompt costly investment in expansion. This scenario could negatively impact other customers, despite their efforts to limit usage to essential purposes.

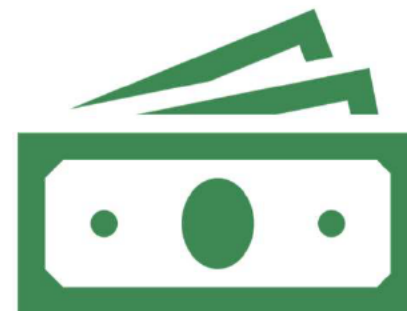
Commission Directive

2.a. Whether the availability of the Water and Sewer Investment Plan (WSIP) ratemaking mechanism, N.C.G.S., § 62-133.1B, affects the analysis of whether uniform rates or stand-alone rates are appropriate at the time of approval of a request to transfer a utility franchise.

Yes, the WSIP affects the analysis of whether uniform rates or stand-alone rates are appropriate at the time of approval of a request to transfer a utility franchise.

How would a newly acquired system be incorporated into an existing WSIP? Is incorporation feasible? Key considerations include, but are not limited to, the following:

- Size of the acquired system
- Rates (revenue requirements and rate design)
- Capital improvement plan (additional projects)
- Performance metrics (timing and benchmarks)
- Earnings test (timing)



Commission Directive

2.b. How rate shock and rate gradualism should be balanced during any migration to uniform rates in a rate case proceeding or WSIP for systems acquired since the last rate case proceeding or WSIP.

If the revenue requirement per acquired customer is greater than the revenue requirement per existing uniform customer, mitigating rate shock and implementing rate gradualism to benefit the acquired customers requires uniform customers to subsidize them.

Is there a time when that would be appropriate? Acceptable?

If the revenue requirement per acquired customer is less than the revenue requirement per existing uniform customer, mitigating rate shock and implementing rate gradualism to benefit acquired customers slows benefits to uniform customers but may be fair and reasonable.

Other factors would include benefits such as quality and reliability of service.

N.C.G.S. § 62-133.1B.(b) requires that “the plan and associated rates are just, reasonable, and in the public interest, and the plan reasonably ensures the provision of safe, reliable, and cost-effective service to customers.”

Commission Directive

2.c. Whether, and under what circumstances, the commitment of resources, both utility and Public Staff/Commission, to reviewing and maintaining a stand-alone rate paradigm for regulatory treatment is justified.

Yes, on a case-by-case basis. Under certain circumstances stand-alone rates will be more likely justified, including, but not limited to, the following:

- Fair value acquisitions where the cost of service is higher than the existing uniform cost of service;
- Systems where the level of service is significantly greater than adequate; and
- Systems with materially different infrastructure and operations and socioeconomic conditions.

Commission Directive

2.d. Whether, and under what circumstances, the justification for uniform rates in a transfer proceeding should deviate from a traditional historical cost-of-service analysis.

Ideally, customers shouldn't pay more than the cost of service. If the traditional historical cost-of-service analysis results in rates lower than the uniform rates, there is not a clear justification for approval of the uniform rates.

N.C.G.S. § 62-111 subsection (a) states transfer "approval shall be given if justified by the public convenience and necessity" and subsection (f) requires approval "upon finding that the proposed grant or transfer. . . is in the public interest."

Regarding consolidation, the US Water Alliance states, "Assessing, estimating, and quantifying benefits may be daunting, but doing so is essential to know whether benefits outweigh the costs and challenges." It goes without saying that "assessing, estimating, and quantifying" costs is essential, too.

Commission Directive

2.e. Whether and how those situations where a system to be acquired has rates that do not fully reflect the cost to provide utility service impact the consideration of whether a uniform rate paradigm is appropriate.

Yes, a larger rate increase is justified when the system's rates generate revenues lower than the cost of service.

But if the fully reflected cost of service still generates rates below uniform rates, then uniform rates are not warranted at transfer.

Commission Directive

2.f. Whether, and under what circumstances, stepped-in rate increases to[wards] the acquiring utility's uniform rates should be considered when uniform rates are not supported by the historical cost-of-service analysis [of the acquired system] at the time of transfer.

Yes, on a case-by-case basis depending on how you define “stepped-in rates.”

One example is the Aqua acquisition of Clear Meadows water system in Docket No. W-218, Sub 420. The hearing was held open briefly for Aqua to make initial capital improvements, Public Staff audit, and incorporation of those costs for recovery in increased rates from the seller's present rates, which were both less than the proposed uniform rates.

Commission Directive

2.f.i. Whether the Commission is authorized to consider planned capital improvements over the stepped-in rate period under N.C.G.S. § 62-133.

No, stepped-in rates under N.C.G.S. § 62-133 cannot change after the record has closed or between rate cases.

§ 62-133. How rates fixed.

(b)(1) Ascertain the reasonable original cost or the fair value under G.S. 62-133.1A of the public utility's property **used and useful, or to be used and useful within a reasonable time after the test period**, in providing the service rendered to the public within the State, less that portion of the cost that has been consumed by previous use recovered by depreciation expense. (Emphasis added).

§ 62-133. How rates fixed.

(c) The original cost of the public utility's property, including its construction work in progress, shall be determined as of the end of the test period used in the hearing and the probable future revenues and expenses shall be based on the plant and equipment in operation at that time [. . .] The test period shall consist of 12 months' historical operating experience prior to the date the rates are proposed to become effective, but the Commission shall consider such relevant, material and competent evidence as may be offered by any party to the proceeding tending to show actual changes in costs, revenues or the cost of the public utility's property used and useful, or to be used and useful within a reasonable time after the test period, in providing the service rendered to the public within this State, including its construction work in progress, **which is based upon circumstances and events occurring up to the time the hearing is closed.** (Emphasis added).

Commission Directive

2.f.ii. If so, whether the acquiring utility should be required to provide supporting documentation to the Public Staff and Commission of in-service dates prior to stepping up the rates to the next level.

If the Commission is authorized to consider planned capital improvements over the stepped-in rate period under N.C.G.S. § 62-133, then the acquiring utility should be required to provide supporting documentation to the Public Staff and Commission of the in-service dates, actual costs incurred, and be subject to investigation, including reasonableness and prudence, prior to stepping up the rates to the next level.

Alternatively, stepped-in rates could be provisional and subject to refund, but at some time would require supporting documentation and true-up.

Commission Directive

2.g. Whether and how the existing stand-alone rate divisions currently in place for Aqua, CWSNC, and any other intervenor would eventually be consolidated into one unified rate structure.

Depends on the policy goals of the Commission, cost of service analysis, and whether the result is just and reasonable rates. N.C.G.S. § 62-130-32 and 140.

Aqua Uniform Water and Brookwood rates are trending toward each other, and Aqua Uniform Sewer and Fairways Sewer rates are trending toward each other. The outlier has been Fairways Water.

CWSNC rates would likely need to be consolidated with a phased approach due to the disparity between the rates of its rate divisions.

Other Relevant Matters

- Affordability
 - How much can customers pay?
- Equality v. Equity
 - Is paying the same price fair?
 - “Equality means each individual or group of people is given the same resources or opportunities. Equity recognizes that each person has different circumstances and allocates the exact resources and opportunities needed to reach an equal outcome.”
<https://onlinepublichealth.gwu.edu/resources/equity-vs-equality/>
- Customer Assistance Programs
 - How can financially vulnerable customers get help?
 - UNC – EFC conducted baseline research on CAPs and evaluated options for OWASA.
- Essential v. Discretionary Usage
 - What are the cost impacts of demand? What is adequate service?



QUESTIONS

Resources

Consolidated Water Rates: Issues and Practices in Single-Tariff Pricing. EPA. 1999. <https://nepis.epa.gov/Exe/ZyPURL.cgi?Dockkey=200027XN.TXT> (USEPA – NARUC)

Strengthening Utilities Through Consolidation: The Financial Impact. Report. US Water Alliance and University of North Carolina, School of Government, Environmental Finance Center. 2019. https://efc-prod-dept-sogtesting.cloudapps.unc.edu/sites/default/files/2019/Published_Final_Utility%20Consolidation%20Financial%20Impact%20Report_022019.pdf (US Water Alliance)

Evaluating Customer Assistance Programs: Orange Water and Sewer Authority. Report. University of North Carolina, School of Government, Environmental Finance Center. 2023. https://efc.sog.unc.edu/wp-content/uploads/sites/1172/2023/10/OWASA-Evaluating-Customer-Assistance-Programs-Final-Report_updated-10_18_23.pdf (UNC – EFC)

Additional Resources

Clean Water Act Financial Capability Assessment Guidance

<https://www.epa.gov/system/files/documents/2023-01/cwa-financial-capability-assessment-guidance.pdf>

Water and Sewer Affordability Tool

<https://efc.sog.unc.edu/resource/water-and-wastewater-affordability-tool-videos/>

Water Affordability Business Case Downloadable Tool

<https://www.nrdc.org/resources/water-affordability-business-case-downloadable-tool>

CERTIFICATE OF SERVICE

I certify that a copy of the foregoing has been served on all parties of record or their attorneys, or both, in accordance with Commission Rule R1-39, by United States mail, first class or better; by hand delivery; or by means of facsimile or electronic delivery upon agreement of the receiving party.

This the 1st day of December, 2023.

Electronically submitted
/s/ Megan Jost
Staff Attorney