

**STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH**

DOCKET NO. W-354, Sub 399

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application by Carolina Water Service, Inc.)
of North Carolina for a Certificate of)
Convenience and Necessity to Provide)
Water Utility Service to the Carteret County)
Water System, and for Approval of Rates)
ORDER GRANTING CERTIFICATE
OF PUBLIC CONVENIENCE AND
NECESSITY, APPROVING RATES,
AND REQUIRING COMPLIANCE
FILING, BOND, AND CUSTOMER
NOTICE

HEARD: Tuesday, October 18, 2022, at 7:00 p.m., in the Commission Board Room,
Carteret County Courthouse, 2nd Floor, 302 Courthouse Square, Beaufort,
North Carolina 28516

Tuesday, June 20, 2023, at 10:00 a.m., in Commission Hearing Room 2115,
Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27603

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

APPEARANCES:

For Carolina Water Service, Inc. of North Carolina:

Jo Anne Sanford, Sanford Law Office, PLLC, 721 North Bloodworth Street,
Raleigh, North Carolina 27604

For Carteret County:

Claud R. Wheatly, III, Wheatly Law Group, PA, 710 Cedar Street, Beaufort,
North Carolina 28516

For the Using and Consuming Public:

William E.H. Creech, James Bernier, Public Staff - North Carolina Utilities
Commission, 4326 Mail Service Center, Raleigh, North Carolina 27699-
4300

BY THE COMMISSION: On June 25, 2018, N.C. Gen. Stat. § 62-133.1A (Fair Value Statute) became law. It authorizes water and wastewater public utilities to elect to use a fair value determination for rate-making purposes when acquiring utilities owned by counties, municipalities, and other government utilities.

On July 26, 2022, Carolina Water Service, Inc. of North Carolina (CWSNC or the Company) filed an Application for Determination of Fair Value of Utility Assets Pursuant to N.C.G.S. § 62-133.1A and Establishing Rate Base for Acquisition of the Carteret County Water System (Fair Value Application) in Docket No. W-354, Sub 398 (the Fair Value Proceeding).

On August 2, 2022, CWSNC filed an Application for Certificate of Public Convenience and Necessity and for Determination of Rates, pursuant to N.C.G.S. § 62-110, with respect to its planned acquisition of the Carteret County Water System (the System) in the above-referenced docket (as subsequently revised and supplemented, the CPCN Application).

On August 25, 2022, the Public Staff notified CWSNC by letter filed with the Commission that it deemed additional enumerated information was necessary to complete the CPCN Application. On August 26, 2022, CWSNC filed a response to the Public Staff's questions and statements, including a revised Application. On September 2, 2022, CWSNC made a Supplemental filing.

On September 13, 2022, the Commission issued an Order Scheduling Hearings, Establishing Discovery Guidelines, and Requiring Customer Notice. This Order applied to both the Fair Value Proceeding and the above-captioned proceeding on the CPCN Application.

On October 18, 2022, at 7:00 p.m. in the Carteret County Courthouse, the Commission held a public witness proceeding to hear from customers both with respect to the Fair Value Proceeding and the CPCN Application. Seven witnesses testified.

On November 22, 2022, CWSNC filed in both dockets its Response to Customer Concerns from the October 18, 2022, Beaufort North Carolina Public Hearing. On December 16, 2022, the Staff filed its Response to CWSNC's Response to Customer Concerns. CWSNC filed a Supplemental Response to Customer Concerns on January 17, 2023.

On February 10, 2023, in the Fair Value Proceeding, the Commission issued its Order Establishing Rate Base of Water System Acquired from Carteret County (Fair Value Order) in which the Commission granted CWSNC's Fair Value Application to establish rate base by the fair value method. The Commission also held that the reasonable and appropriate fair value of the System assets being acquired by CWSNC, as adjusted in the public interest, is \$8,416,000; that the reasonable fees and transaction

and closing costs are \$312,039; and that the resulting rate base value of the System assets is \$8,728,039 as of the date of the acquisition.

The Public Staff testimony of Lynn Feasel and Charles Junis was filed on March 10, 2023. On March 27, Carteret County (County) filed the testimony of Carteret County witnesses Denise Meshaw and Tommy Burns, along with a Petition to Intervene. On March 29, 2023, the Company filed rebuttal testimony of Donald H. Denton III and Matthew P. Schellinger II.

The County's Petition to Intervene was granted on April 4, 2023.

CWSNC filed revised exhibits on May 9, 2023, which updated information about the rates that had been ordered by the Commission in Docket No. W-354, Sub 400, the Company's recent Multi-Year Rate Plan case. In response, the Public Staff updated its testimony on June 13, 2023.

On June 20, 2023, the evidentiary hearing took place in the Commission Hearing Room, 2d floor of the Dobbs Building, at 430 North Salisbury Street, Raleigh, NC 27603. During the hearing and without objection, the Commission took judicial notice of the entire record created in the Fair Value Proceeding.

On July 7, 2023, the Public Staff filed Public Staff Late-Filed Exhibits Nos. 1 and 2.

Based on the entire record in this proceeding and in the Fair Value Proceeding, the Commission makes the following:

FINDINGS OF FACT

1. CWSNC is a corporation duly organized under the laws of and is authorized to do business in the State of North Carolina. It is a franchised public utility providing water and sewer utility service to customers in North Carolina, pursuant to Chapter 62 of the North Carolina General Statutes. CWSNC is a wholly owned subsidiary of Corix Regulated Utilities, Inc.

2. CWSNC is properly before the Commission for approval of its Application for a CPCN under N.C.G.S. § 62-110 to own and operate the System, which it has contracted to purchase from the County.

3. The System, owned by Carteret County, a county established under Chapter 162A of the General Statutes, is a "Local Government Utility" as defined by Commission Rule R7-41(b)(1).

4. The System consists of the two water systems, North River/Mill Creek and Merrimon, and serves approximately 1,250 water utility customers.

5. Since at least 2019, the County has been looking for another entity to take over ownership of the System.

6. Following a series of public meetings and a public upset bid process, on September 20, 2021 the Carteret County Board of Commissioners accepted CWSNC's \$9.5 million bid to purchase the System.

7. On October 18, 2021, CWSNC, as buyer, and Carteret County, as seller, entered into a Utility Asset Purchase Agreement (as subsequently amended, the APA) pursuant to which CWSNC agreed to purchase the assets of the System for a purchase price of \$9.5 million.

8. CWSNC and the County entered into an operation and maintenance oversight agreement dated January 24, 2022. Under the agreement, CWSNC provides an Operator in Responsible Charge and consultation services to the County staff.

9. The System currently is well maintained and provides adequate, safe, reliable, and compliant service to customers.

10. It is not possible on the present record to accurately quantify the impact of CWSNC's purchase of the System on CWSNC's future rates charged to customers.

11. The Public Staff has taken the position that if the Commission grants the CPCN, the Commission should require the APA to be amended to provide that the proceeds from the sale shall either (a) be held by the County in trust for the benefit of the System customers as a hardship fund or to subsidize CWSNC customer bills on a pro rata basis or (b) credited to CWSNC as a direct reduction in rate base of the System.

12. The water rates reflected in CWSNC's Revised Form Application Exhibit 12 to the Fair Value Application are the existing Carteret County rates. CWSNC has agreed with Carteret County that the customers of the System will remain at Carteret County's current water rates four years from the date the sale of the System is closed.

13. CWSNC requests that the going forward depreciation rates shall be equal to that of the CWSNC Uniform Water rate division as a reasonable approximation of the remaining service lives of the utility assets of Carteret County, rather than the 4.00% depreciation rate proposed by the Public Staff.

14. CWSNC requests that the Purchase Acquisition Adjustment amortization rate be set at 3.22% consistent with the expected remaining useful lives of the acquired assets.

15. CWSNC requests the amortization rate for due diligence and transaction costs be set at 2.50% consistent with CWSNC Uniform Water rate division's rate and that such costs be recorded in the Organization plant account.

APPLICABLE LEGAL STANDARD

CWSNC seeks a CPCN pursuant to N.C.G.S. § 62-110(a), which provides, in relevant part:

[N]o public utility shall hereafter begin the construction or operation of any public utility plant or system or acquire ownership or control thereof, either directly or indirectly, without first obtaining from the Commission a certificate that public convenience and necessity requires, or will require, such construction, acquisition, or operation....

The Commission has considerable discretion in making the determination as to whether approval of a CPCN application is justified by public convenience and necessity, as described by the North Carolina Supreme Court:

The doctrine of convenience and necessity has been the subject of much judicial consideration. No set rule can be used as a yardstick and applied to all cases alike. This doctrine is a relative or elastic theory rather than an abstract or absolute rule. The facts in each case must be separately considered and from those facts it must be determined whether or not public convenience and necessity require [the action].

State ex rel. Utils. Comm'n v. Casey, 245 N.C. 297, 302, 96 S.E.2d 8, 12 (1957) (citation and quotation marks omitted). This Commission has noted that “the decision of whether to grant or deny a CPCN must rest upon substantive evidence; it cannot rest on speculation or sentiment.” Order Denying Certificate of Public Convenience and Necessity for Merchant Generating Facility, No. EMP-105, Sub 0 at 7-8 (N.C.U.C. June 11, 2020) (citing *Howard v. City of Kinston*, 148 N.C. App. 238, 246, 558 S.E.2d 221, 227 (2002)). The burden is on the applicant to provide this substantive evidence and demonstrate that the CPCN should be granted. *Id.*

The Public Staff takes the position that the Commission should apply the three-part test for determining public convenience and necessity that it has traditionally applied to mergers. See, e.g., Tr. vol. 2, 78. Under this test, in order to determine whether a proposed utility merger is justified, the Commission considers:

(1) whether the merger would have an adverse impact on the rates and services provided by the merging utilities; (2) whether ratepayers would be protected as much as possible from potential costs and risks of the merger; and (3) whether the merger would result in sufficient benefits to offset potential costs and risks.

Order Approving Merger Subject to Regulatory Conditions and Code of Conduct, Nos. E-2, Sub 1095; E-7, Sub 1100; and G-9, Sub 682 at 68 (N.C.U.C. Sept. 29, 2016). The Company

does not concede that this test applies; however, it believes that application of the three-part merger test would result in approval of the CPCN. Tr. vol. 3, 105, 128.

The Company does not concede that this test applies, but it does not offer an alternative formulation or ask the Commission to explicitly reject the Public Staff's position. The Commission notes that the standard advocated by the Public Staff was developed in connection with cases governed by N.C.G.S. 62-111(a). The present transaction is not governed by that statute since Carteret County is not the holder of a franchise approved under Chapter 62. The Commission therefore finds it unnecessary to address whether the Public Staff's position should or should not be applied as a general matter to transfers subject to N.C.G.S. § 62-133.1A, since the general jurisprudence applicable under N.C.G.S. 62-110 is sufficient to decide the case at hand. Moreover, the Commission notes that the Company, while not conceding the correctness of the Public Staff's position, contends that the evidence supporting its application is sufficient to satisfy even the standard advocated by the Public Staff. Tr. vol. 3, 105, 128.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1-4

Jurisdiction

The evidence supporting these findings of fact is found in the verified CPCN Application, the testimony and exhibits of the witnesses, the Commission record, the General Statutes and Commission Rules, and the entire record in this proceeding. These findings are informational, procedural, and jurisdictional in nature and are not contested by any party.

It is undisputed that CWSNC is a utility company that provides water and sewer service for compensation to the public in North Carolina under the jurisdiction of Chapter 62 of the General Statutes and that it is regulated by the Commission. Likewise, Carteret County's status as a Local Government Utility under the Fair Value Statute and its authority to sell the System has not been questioned. CWSNC and the County have executed a contract for the sale of the Carteret System to CWSNC, and CWSNC has applied for a CPCN in this docket in order to provide service to the customers on the System.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 5-7

County Desire to Sell

The evidence for these findings is found in the testimony of Public Staff witness Charles Junis in the Fair Value Proceeding, the APA, and the testimony and exhibits of County witnesses Denise Meshaw and Tommy Burns.

In the Fair Value Proceeding, Public Staff witness Junis summarized the County's efforts to divest itself of ownership of the System beginning with obtaining a State Water

System Merger Grant in 2019 in an unsuccessful attempt to entice the Town of Beaufort to take over the System. Fair Value Proceeding Tr. vol. 3, 131. Upon receiving expressions of interest from public water utilities, the County next initiated a public upset bid process, *id.* at 134, which culminated in the County Board of Commissioners voting to accept CWSNC's bid on September 20, 2021, and entering into the Asset Purchase Agreement with CWSNC on October 18, 2021. *Id.* at 135.

County residents registered opposition to the transaction both with the County Board of Commissioners, *see e.g.*, Tr. vol. 1, 63-64, by filing Consumer Statements of Position with this Commission and by testifying at the public hearing held jointly in this proceeding and the Fair Value Proceeding.

County witnesses Burns and Meshaw—respectively, the County Manager and the Chief Financial Officer—testified as to the reasons the County sought a buyer for the System. Witness Burns called the System a “fledgling system” and testified that it is hard for the County to justify keeping the System at all costs. Tr. vol. 3, 42. He emphasized that it is a low-density system, and thus there are not enough ratepayers to spread the user charges to fully fund the system. *Id.* He testified that “lack of development, environmental limitations, and permitting regulations will prevent large parts of the water system area from being developed now or in the future.” *Id.* at 44. Witness Burns asserted that the Local Government Commission favors merger, regionalization, and other means of transferring systems to other providers who can provide economies of scale to distressed systems. *Id.* at 43. Witness Meshaw added that being named a distressed system by the Local Government Commission places requirements on the County to attend training and take other actions. *Id.* at 58. She testified that the County can never overcome being small and rural merely by funding and that the long-term viability issues are part of the consideration that led to the sale. *Id.* at 59.

In the Fair Value Order, based on the evidentiary record in the Fair Value Proceeding, the Commission found that the System “was not financially self-sufficient on customer rates alone” and had been funded at times from the County's General Fund and, additionally, was “regularly supported with taxes collected from property owners within the boundary of a special water taxing district (the Water District).” Fair Value Order at 6. The Commission further found that “[t]he System customers represent less than half of the parcels within the Water District, and they are only a small fraction of the County population.” *Id.*

Public Staff witness Junis testified that the County was able to manage the System both operationally and financially. He stated that, to his knowledge, the County provides safe, reliable, and compliant service to the System. Tr. vol. 2, 68. Further, Witness Junis asserts that the County's management is capable and has shown the ability to improve the Water Fund's financial outlook, including by accessing public grants and low-cost loans. *Id.*

The Commission concludes that the County's decision to sell the System is a factor in favor of granting CWSNC's petition for a CPCN.

North Carolina law vests boards of county commissioners with the authority to exercise each power, right, duty, function, privilege, and immunity of the county. N.C.G.S. § 153A.12. County citizens, including those who are customers of the System, were and are able to exercise their political and civil rights with respect to this decision. Further, the Fair Value Statute provides a ratemaking tool that facilitates county- or municipality-owned water and wastewater systems to be acquired by public utilities. There is nothing in the language of the Fair Value Statute suggesting that a county or municipality must be failing to provide adequate service in order for this Commission to grant a CPCN to a public utility to acquire and operate its water or wastewater system. Under the facts presented here, the Commission sees no reason to substitute its judgment for that of the Carteret County Board of Commissioners as to what is in the best interest of the County and its citizens.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 8-9

CWSNC Service

The evidence for these findings is the CPCN Application; customer testimony at the public witness hearing; consumer statements of position filed in this docket; CWSNC's Response to Customer Concerns; Public Staff's Response to CWSNC's Response to Customer Concerns; CWSNC's Supplemental Response to Customer Concerns; the testimony of Company witness Donald H. Denton III in in both this proceeding and the Fair Value Proceeding; the testimony and exhibits of Company witness Matthew Schellinger II in this proceeding; and the testimony of Public Staff witness Charles Junis in both this proceeding and the Fair Value Proceeding.

CWSNC has been operating the System as the Operator In Charge since January 22, 2022. Tr. vol. 2, 83. During the public witness hearing on October 18, 2022, seven customers testified in opposition to the transaction, including some who expressed quality concerns about water pressure and discoloration. Tr. vol. 1, 39, 56, 74, 76. Additionally, some consumers who filed statements with the Commission expressed water quality concerns. Consumer Position of Lynda Phillips, filed October 3, 2022; Consumer Position of Beth Thompson, filed November 1, 2022; Consumer Position of Lisa Lauren Camp, filed November 1, 2022. CWSNC described in detail how it addressed these service complaints, both in its Response to Customer Concerns and in its Supplemental Response to Customer Concerns.

Public Staff witness Junis met with System staff in April 2022 for a site visit and visual inspection of the System assets. Tr. vol. 2, 66. Witness Junis testified that he found the System assets to be in acceptably good condition and well-maintained. *Id.* at 67. He testified that utility service to existing System customers would be the same or better following an acquisition by CWSNC. *Id.* at 83. He stated that "CWSNC's record of service

is satisfactory and CWSNC has the technical, managerial, and financial capacity” to provide water utility service to the System. *Id.*

In response to Commissioner questions, Company witness Denton described CWSNC’s existing operations in the vicinity of Carteret County and how those operations will benefit the System. *Id.* at 29-32. He explained that CWSNC would be using its existing operators to service and maintain System operations. *Id.* at 31-32. Witness Denton also described the Storm Response Team that is available to augment local staff during storm conditions. *Id.* at 30-31.

On cross-examination, Company witnesses Denton and Schellinger acknowledged that System customers would no longer have the option to pay their bills in person but instead would interface with customer service and billing offices located outside of the County. *Id.* at 14-19.

The Commission concludes that CWSNC is well-qualified to assume operations and ownership of the System. The Company is a public utility in good standing in the State of North Carolina. It had been operating the System for over a year at the time of the expert hearing in this matter, and no evidence was introduced suggesting that it was providing anything less than professional and competent service. CWSNC responded appropriately to customer service complaints made during this proceeding and the Fair Value Proceeding. The minor changes in how accounts will be serviced under new ownership is an insignificant consideration.

CWSNC’s demonstrated ability to operate the System in such a way as to provide adequate, safe, reliable, and compliant service to customers is a factor that strongly weighs in favor of granting CWSNC’s petition for a CPCN for the System.

EVIDENCE AND CONCLUSIONS OF LAW FOR FINDINGS OF FACT NOS. 10-11

Impact on Rates

The evidence supporting these findings of fact is contained in the record in the Fair Value Proceeding, the Fair Value Order, the Company’s CPCN Application, the testimony and exhibits of Company witnesses Schellinger and Denton, County witnesses Burns and Meshaw, and Public Staff witnesses Feasel and Junis.

CWSNC has indicated that in its next rate case, likely to be filed in 2026 for rates effective in 2027, it will seek to move the System customers into CWSNC uniform water rates. Tr. vol. 2, 44.

The primary risk that the Public Staff identified in connection with granting the CPCN is a risk of increased rates for existing System customers and/or existing uniform rate CWSNC customers above the rate increases that could be expected if the CPCN were denied.

CWSNC witness Schellinger testified as to the customer benefits of the transaction, including the economies of scale created by the transaction. Tr. vol. 3, 114-15.

With respect to rate impacts, witness Schellinger testified as follows:

The Company concludes from these calculations that the Uniform Water customers would benefit from the acquisition of Carteret, whether the Carteret customers are included in the Uniform Water rate division in the next MYRP case or not. However, the best outcome for all customers – which would generate savings for all customers – is to include Carteret customers in the Uniform Water rate division in the next rate case, as that provides savings to existing customers, while providing the best rate outcome for the Carteret customers. . . . The drivers for the Carteret monthly bill results show that lower O&M costs, from both a more cost efficient operation of Carteret by CWSNC and larger scale afforded by the acquisition, outpace the higher rate base per customer of Carteret as a stand-alone system. In addition, the Uniform Water customers benefit from the added customers, which spreads fixed costs across a larger customer base. Although not yet calculated by CWSNC, the Company believes non-Uniform Water rate division customers would also benefit from the acquisition of Carteret, due to the Carteret customers absorbing a portion of overall CWSNC fixed costs.

Id. at 119-20.

The Public Staff disputed these conclusions.

The Public Staff Panel questioned the non-incremental expense adjustments, specifically the accuracy of removing corporate allocation expenses that are passed down on a per customer basis. Tr. vol. 2, 150-51.

Public Staff witness Junis testified that the Sub 384 Uniform Water rate base per customer was \$2,337 and the fair value with associated fees rate base was \$6,835 per System customer. Tr. vol. 2, 79. CWSNC witness Schellinger testified on rebuttal that the Sub 400 Rate Year 3 Uniform Water rate base per equivalent residential connections (ERC) is \$3,072 and the Carteret County year 4 rate base per ERC is \$5,185. Tr. vol. 3, 116-17. CWSNC witness Schellinger concluded that this rate base per ERC metric does not contemplate the eventual inflection point as the System continues to amortize and depreciate through the future while CWSNC continues to invest in its existing aging systems and infrastructure. *Id.*

The Public Staff points out that the Company's calculations show that uniform customers will pay more in average monthly bills (uniform rates of \$77.58 from line 50 of Revised Rebuttal Exhibit MPS-4) if the Carteret County customers are rolled into

CWSNC's uniform rates as opposed to the Carteret County customers being charged standalone rates (uniform rates of \$76.89 from line 49 of Revised Rebuttal Exhibit MPS-4). The Public Staff concludes that CWSNC uniform rate customers would benefit from shared costs being allocated to the System customers if the System customers are charged standalone rates.

Moreover, the Public Staff Panel testified that Merrimon customers will have a larger rate impact when the four-year freeze ends, as their rates are currently lower than the North River/Mill Creek system rates. Tr. vol. 2, 125.

Witness Junis provided evidence that many of the County's costs are lower than CWSNC's costs. He testified that the County does not pay federal or state income taxes on System receipts. Tr. vol. 3, 83. In the Fair Value Proceeding, CWSNC witness Denton acknowledged that the County's cost of debt is substantially lower than CWSNC's. Fair Value Order at 20. In the Sub 400 Rate Case, a debt cost rate of 4.64% was found to be just and reasonable for setting CWSNC rates. Tr. vol. 2, 45. The County enjoys an embedded cost of debt of only 2.61%. Fair Value Proceeding Tr. vol. 2, 70-71.

Public Staff witness Junis suggested in direct testimony that either CWSNC or Carteret County, or both, could voluntarily agree to mitigate the impact of the sale on System customers beyond a temporary rate freeze, such by using the sales proceeds to reduce the rate base or create a hardship fund. *Id.* at 85. Public Staff witness Junis noted a reference to such mitigation in the Fair Value Order and steps taken by other utilities. *Id.*, citing Fair Value Order at 24-25; tr. vol 3, 32. Neither CWSNC nor the County has proposed such mitigation measures.

County witness Meshaw testified that unless the County Commission levied taxes, System rates would need to increase by 40% if the County continued to own the System.

In response to the Public Staff's suggestion that a hardship fund be created for System customers, County witness Burns questioned whether that would be an appropriate public purpose for the funds and noted that there are existing hardship programs through the County Department of Social Services and other groups. Tr. vol. 3, 45-46.

Based upon competent, substantial, and material evidence in the record, the Commission concludes that the potential for increased customer rates in CWSNC's next rate case is insufficient grounds on which to deny CWSNC's CPCN to acquire the System in light of the following three considerations.

First, as described in detail above, the Public Staff and CWSNC have reached very different conclusions as to the impact the transaction will ultimately have on rates in CWSNC's next rate case, expected in three years. As this Commission indicated in the Fair Value Order, "[t]he System assets will not be added to rate base for rate setting purposes until CWSNC's next rate case, which is anticipated to be in four years. As a

result, it is difficult to predict the impact of granting the Application on future rates.” Fair Value Order at 8. There are numerous factors that can impact rates in the future, and the Commission will not rest its decision on this foundation. Further, as the Commission noted in the Fair Value Order, the Fair Value Statute explicitly gives the Commission discretion to classify the System as a separate entity for ratemaking purposes, consistent with the public interest. N.C.G.S. § 62-133.1A(e).

Second, while the evidence does suggest that System customers are likely to see at least some increase of their rates at the end of the four-year rate freeze and that this is particularly true with respect to the Merrimon system customers, this is a risk that was inherent in the decision the Carteret County Board of Commissioners made on behalf of its constituents. The County is in a better position than the Commission to weigh the overall risks and benefits to its citizens of the change in ownership of the System. Moreover, there are undeniable rate benefits to the System customers in the form of the four-year rate freeze and the benefit of having rates that are regulated by this Commission pursuant to established law and procedure. Under County management, there has been a history of significant rate increases, and County witnesses projected significant future increases if the CPCN were not granted.

Third, in the Fair Value Order, the Commission adjusted the fair value of the System, as determined by an average of three appraisers, to a lower number in the public interest, thus setting the rate base for the System assets at \$8,416,000. Fair Value Order at 33. It would be inconsistent with that determination, on the facts presented, for the Commission to now deny a CPCN on the grounds that the System rate base would result in rates that are unacceptably high.

The Commission does not agree with the Public Staff’s position that because the fair value of the System was determined in accordance with N.C.G.S. § 62-133.1A instead of under N.C.G.S. § 62-133(b)(1), the difference in those two methods creates an “acquisition adjustment,” i.e., a purchase price difference above the depreciated original cost of the acquired assets, which is normally not included in rate base pursuant to Commission policy. See Tr. vol. 2, 74-75 (citing Order Approving Transfer and Denying Acquisition Adjustment in Docket No. W-1000, Sub 5 (Jan. 6, 2000)). Quite to the contrary, N.C.G.S. § 62-133.1A explicitly provides the method for determining rate base.

The Commission is likewise not persuaded that a CPCN should be conditioned on apportioning part of the sales proceeds to either reduce the rate base of the System assets or to create a hardship fund for System customers. Such actions could certainly be a positive contribution to the public convenience and necessity, but the Commission declines to order them in this proceeding.

Conclusion as to CPCN

The Commission has carefully considered and weighed all the evidence and arguments presented in this proceeding. On balance and based upon competent,

substantial, and material evidence in the record, the Commission determines that granting the CPCN for CWSNC to operate the System serves the public convenience and necessity.

EVIDENCE AND CONCLUSIONS OF LAW FOR FINDING OF FACT NO. 12

Approved Rates

The evidence for this finding of fact is contained the Fair Value Docket and the testimony of Company witness Denton.

In the Fair Value Proceeding, the Company filed Revised Exhibit 12 to its Fair Value Application, which reflected the existing System rates with two minor changes to conform the rates to CWSNC's standard tariff terms relating to meter testing fees and charges for late payment. Fair Value Tr. vol. 4, 132-33. The Company has agreed to maintain these rates for System Customers for four years following the closing of the sale of the System. Tr. vol. 2, 33.

EVIDENCE AND CONCLUSIONS OF LAW FOR FINDING OF FACT NO. 13

Depreciation rates

The evidence for this finding of fact is contained in the original CPCN Application and the updates thereto, the Fair Value Docket, the testimony of CWSNC and the Public Staff witnesses in this proceeding, and in the Commission's records.

Public Staff witness Feasel testified that she calculated depreciation expense based on the depreciation rates recommended by Public Staff witness Junis. Tr. vol. 2, 45. In response to questions from the Commission witness Junis stated that the Public Staff believes that 25 years would be a reasonable estimated remaining life of these assets going forward. Concerning the Public Staff's determination of a 4.00% depreciation rate for the acquired assets and the amortization of the acquisition adjustment, witness Junis responded that "we're looking at essentially that sum as a whole when looking at a[n] acquisition adjustment and any remaining undepreciated balance of plant on the County's books." *Id.* at 163-164. Witness Junis stated that the County was utilizing a depreciation rate of 30 years and that a majority of these assets would be fully depreciated in nine years. Witness Junis commented that CWSNC, by using its uniform depreciation rates, extends some of these plant assets to a useful life of 100 years. He testified that the Public Staff is "just not comfortable with that as a reasonable expectation of the estimated life going forward." *Id.* at 164. Witness Junis further testified that if the acquisition is approved by the Commission, CWSNC would potentially file a new depreciation study in a future rate case that may modify some of the Company's depreciation rates. Witness Junis commented that CWSNC has not completed a depreciation study in multiple rate cases. *Id.* at 162.

In prefiled testimony, witness Junis testified that on March 3, 2023, CWSNC provided in its response to Public Staff Data Request No. 6, an updated addendum to its application for transfer of public utility franchise and for approval of rates (Updated Addendum). On May 25, 2023, witness Junis stated that CWSNC provided a modified version of the Updated Addendum incorporating the Commission decisions in the Sub 400 Rate Case. Witness Junis expressed concerns about the Updated Addendum, including, among other things, that (1) CWSNC's rate base calculations do not include contributions in aid of construction (CIAC), which would reduce the original cost plant and increase the amount of the purchase acquisition adjustment, and (2) the depreciation rates are modified to CWSNC's lower rates, which result in longer estimated lives and reduce the benefit of the four-year rate freeze. Tr. vol. 2, 55.

Witness Junis testified that as of June 30, 2022, the County's audited financial records indicate total capital assets less depreciation in the amount of \$5,402,027. *Id.* at 73. Witness Junis contended that because 56.83% of the capital funding is CIAC (either in the form of grants or developer contributions) the original cost less depreciation and amortization of CIAC would be approximately \$2,332,055. *Id.* Witness Junis testified that the significance of CIAC is that it offsets associated plant in service, thereby reducing the return on rate base and depreciation expense for ratemaking purposes. In response to questions from the Commission, witness Junis maintained that if CIAC is factored into the calculation of rate base, the plant balances are significantly reduced resulting in the majority of the rate base amount being an acquisition adjustment. *Id.* at 162. Witness Junis commented that CWSNC witness Schellinger presents an acquisition adjustment of approximately \$3.0 million in his rebuttal testimony. *Id.* at 162-163. Witness Junis testified that the Public Staff utilizes the 4.00% depreciation rate on the entirety of the \$8.7 million rate base because "we're trying to estimate the impact in this proceeding." *Id.* at 163.

In rebuttal testimony, CWSNC witness Schellinger disagreed with the Public Staff's proposal to depreciate and amortize the entirety of the allowed rate base at 4.00% per year. He testified that the 4.00% rate that the Public Staff is proposing is not a reasonable approximation of the remaining useful service lives of the assets of the System. Tr. vol. 3, 111. Witness Schellinger explained that Carteret County has depreciated its assets to date based on a flat 30-year useful service life for all asset categories, except vehicles, without regard for how long those assets generally or usually last, which has resulted in a number of plant categories being over-depreciated as a percent of their remaining useful life. *Id.* He commented that the primary categories of assets in the System are Water Treatment Plant, Distribution Reservoirs and Standpipes, and Transmission and Distribution Mains, for which CWSNC is authorized to depreciate over 50 years, 50 years, and 100 years, respectively. *Id.* Witness Schellinger provided Rebuttal Exhibit MPS-1 which contained a capital asset listing provided by Carteret County as of June 30, 2022, which ties to the plant and accumulated depreciation amounts listed in Carteret County's audited annual report. *Id.*

Witness Schellinger testified that utilizing CWSNC's current Uniform Water depreciation rates, the going forward composite depreciation rate on Carteret's plant in service would be 1.40% and the acquired assets will fully depreciate over 31 years. *Id.* at 112. He provided Rebuttal Exhibit MPS-2 which presents a breakdown of the Carteret County water plant and accumulated depreciation at June 30, 2022; the implied accumulated depreciation amount at December 31, 2022 based on the County's depreciation rates; the age of the assets by NARUC account category; CWSNC's Uniform Water rate division service lives and depreciation rates; the National Association of Regulatory Commissioners (NARUC) recommended service lives for each asset account for comparison; the annual amount of depreciation expense utilizing CWSNC's depreciation rates; and the fair value rate base approved by the Commission in the Fair Value Docket. Witness Schellinger commented that the NARUC service lives all point to considerably longer service lives for assets than the 30-year life that Carteret County has been using.

In rebuttal testimony, witness Schellinger explained how CWSNC proposes to account for the FMV transaction in compliance with, and using guidance from, Generally Accepted Accounting Procedures (GAAP) and National Association of Regulatory Utility Commissions (NARUC) Uniform System of Accounts (USOA). Tr. vol. 3, 109. He stated that specific guidance from the NARUC USOA for Class A Water Utilities that is helpful for determining the accounting for FMV transactions is Accounting Instructions #17C and #18 (pages 19-20), and Balance Sheet Account #114 – Utility Plant Acquisition Adjustments (pages 59-60). *Id.* at 110.

Utilizing this guidance, witness Schellinger stated that CWSNC understands that the proper way to account for this transaction on closing is as shown in Table 1 below:

Table 1

<u>Balance Sheet Account</u>	<u>Debit</u>	<u>Credit</u>	<u>NARUC Account</u>
Plant	12,195,043		101
Accumulated Depreciation		6,992,436 ¹	108
Cash - Purchase		9,500,000	131
Acquisition Project		312,039 ²	101
Goodwill	1,084,000		114
Purchase Acquisition			114
Adjustment	3,525,432		
Total	<u>16,804,475</u>	<u>16,804,475</u>	
	<u>Debit</u>	<u>Credit</u>	<u>Total</u>
Rate Base	15,720,475	6,992,436	8,728,039 ³

¹ Implied Accumulated Depreciation as of 12/31/2022 based on the Water Fund Capital Assets Report dated 06/30/2022.

² Reasonable fees paid to the utility valuation experts, reasonable transaction and closing costs as ordered by the Commission.

³ Reasonable and appropriate fair value of the Carteret County Water system as ordered by the Commission.

Id.

Witness Schellinger further stated that the Public Staff does not appear to have outlined a position on how a fair value transaction should be accounted for but has made certain assumptions regarding depreciation and amortization expenses in the Public Staff's cost of service assumptions. *Id.* at 109.

During the expert witness hearing, Public Staff witness Feasel testified in response a question from the Commission concerning whether the Public Staff agreed with the accounting set forth in CWSNC witness Schellinger Table 1 that "I'm fine with how they categorize that." Tr. vol. 2, 160. Witness Feasel stated that "[t]he main issue is just the depreciation rate difference." *Id.* Witness Feasel further stated that the Public Staff considers the \$8.7 million fair value rate base "as a whole group that is related to the Carteret County system and when we depreciate it in order to have everything including plant PAA and due diligence depreciate the same time like when we fully depreciate everything, every component stop at the same time." *Id.* at 162.

In response to questions from the Commission, witness Schellinger explained how the 1.40% composite depreciation rate based on CWSNC's current depreciation rates and the remaining service life of the acquired assets resulted in a PAA amortization period of 31 years, a rate of 3.22%. Tr. vol. 3, 135. During his response, witness Schellinger referenced his Rebuttal Exhibit MPS-2 filed on March 29, 2023. Witness Schellinger stated that the acquired assets will be largely depreciated at the time CWSNC acquires

the System as a result of the depreciation expense recorded under County ownership plus his estimation of the amount of accumulated depreciation at a date near the expected closing date. *Id.* at 135-36. He testified that NARUC USOA guidance provides that CWSNC should continue to depreciate the plant in service, that is, the approximately \$12.195 million on the County's current financial accounting books while taking into account the accumulated depreciated recorded by the County on these assets. *Id.* Witness Schellenger explained that using CWSNC's current depreciation rates on a going forward basis to calculate depreciation expense on the acquired assets results in an effective rate of 3.22% on a going forward basis because when you take into account the accumulated depreciation, the acquired assets will be fully depreciated in 31 years. *Id.*

For purposes of determining the depreciation and amortization rates to utilize in this fair value transaction, the Commission acknowledges that CWSNC seeks to categorize the various components of the fair value rate base as set forth in Table 1 of the rebuttal testimony of CWSNC witness Schellinger whereas the Public Staff views the rate base in totality. The Commission agrees with CWSNC that it is appropriate to account for the fair value transaction as shown in Table 1 above as supported by NARUC USOA guidance and GAAP. The Public Staff did not provide an alternative accounting of the fair value transaction upon closing other than to state that if CIAC is factored into the calculation of rate base, the plant balances are significantly reduced resulting in the majority of the rate base amount being an acquisition adjustment. This appears to be a primary reason the Public Staff utilizes a single depreciation/amortization rate on the total rate base amount to calculate the Public Staff's recommended depreciation/amortization expense. Further, the Commission acknowledges that the Public Staff testified at the expert witness hearing that the Public Staff accepts the categorization of the fair value rate base presented by CWSNC but takes issue with the depreciation/amortization rates the Company utilizes.

The Commission disagrees with the Public Staff's rationale that CIAC should be factored into the calculation of rate base because the Fair Value Statute sets forth in N.C.G.S. § 62-133.1A (b)(1)d. that "[t]he original source of funding for all or any portions of the water and sewer assets being acquired is not relevant to an evaluation of fair value." Thus, the Commission's determination of the fair value rate base in the Fair Value Proceeding did not set forth whether any of the original source of funding for the System was in the form of grants or developer contributions. The Commission agrees with CWSNC's proposed recording of this fair value transaction on its books and notes that it is not appropriate to record any CIAC related to the transaction. Therefore, the Commission concludes that it is reasonable and appropriate to establish different depreciation and amortization rates for the following rate base components: (1) plant in service, (2) purchase acquisition adjustment, and (3) transaction and due diligence costs as requested by CWSNC.

For the various NARUC plant in service asset accounts, CWSNC proposes to utilize the depreciation rates equal to that of the CWSNC Uniform Water rate division as a reasonable approximation of the remaining service lives of the utility assets of Carteret

County. CWSNC states that this would result in a going forward effective composite depreciation rate of 3.22% on the acquired assets when taking into consideration the accumulated depreciation because these assets would fully depreciate in 31 years. CWSNC provided the NARUC service lives for the various categories of acquired assets for reference to emphasize that the NARUC service lives are considerably longer than the 30-year life that Carteret County has utilized in its financial accounting. In contrast, the Public Staff recommends a remaining service life of 25 years for the net book value of the acquired assets, the purchase acquisition adjustment, and the transaction and due diligence costs.

Based upon competent, substantial, and material evidence in the record, the Commission gives weight to the testimony of CWSNC witness Schellinger and concludes that depreciation rates for the acquired Carteret County water plant should be set on a going forward basis at rates equal to that of CWSNC's Uniform Water rate division. By using the depreciation rates requested by CWSNC and taking into account the accumulated depreciation on the acquired assets at the time of closing (which was estimated at December 31, 2022), the acquired assets will fully depreciate in approximately 31 years. The Commission finds the remaining useful life of 31 years for these assets to be reasonable based on a review of the information set forth in witness Schellinger's Rebuttal Exhibit MPS-2. This rebuttal exhibit contains a column which provides the approximate age of the acquired assets at December 31, 2022. The Commission finds, for example, that the acquired transmission and distribution assets, NARUC account 331.4, which is stated as having an approximate age of 18.87 years, would depreciate for an additional 31 years under CWSNC ownership, resulting in a total estimated service life when fully depreciated of 49.87 years. The Commission finds a total estimated service life of 49.87 years for the acquired transmission and distribution assets to be reasonable. Witness Junis expressed concern that by using the depreciation rates approved for CWSNC's Uniform Water rate division that the useful life of some of these acquired assets would be extended to 100 years. The Commission disagrees. The Commission concludes that the total useful lives for all of the categories of acquired assets presented on Schellinger's Rebuttal Exhibit MPS-2 based on approximately 31 years of additional depreciation under CWSNC ownership are reasonable. Consequently, the Commission concludes that the going forward depreciation rates for the assets acquired from the County should be equal to that of the CWSNC Uniform Water rate division which results in the acquired assets becoming fully depreciated in approximately 31 years when taking into account the accumulated depreciation recorded by the County at the time of closing on the sale.

EVIDENCE AND CONCLUSIONS OF LAW FOR FINDING OF FACT NO. 14

PAA amortization rate

The evidence for this finding of fact is contained in the original CPCN Application and the updates thereto, the Fair Value Docket, the testimony of CWSNC and the Public Staff witnesses in this proceeding, and in the Commission's records.

In rebuttal testimony CWSNC witness Schellinger disagreed with the Public Staff's proposal to depreciate and amortize the entirety of the allowed rate base at 4% per year without distinction for the portion of rate base that will be amortized. Witness Schellinger testified that CWSNC is proposing to amortize the PAA over the composite remaining useful life of the acquired assets, or 3.22%, as shown in Rebuttal Exhibit MPS-2. Tr. vol. 3, 113. Witness Schellinger explained that CWSNC has a number of past Purchase Acquisition Adjustments amortizing on its books and that it has been the Public Staff's position that this PAA rate changes in each rate case in order to amortize over the remaining useful life of CWSNC's plant. He commented that the PAA amortization rate was recently reset in the Sub 384 rate case to 2.73% for the Uniform Water rate division. He stated that due to resetting, the amortization rate is no longer correlated with any particular original underlying acquisition. *Id.* at 113. Witness Schellinger maintained that the PAA amortization rate associated with the System is a rate that is wholly within the discretion of the Commission to set and as such is a significant portion of the eventual cost to serve that as of yet has not been determined. *Id.* at 112-13.

Witness Schellinger recommended that the PAA amortization rate for the System be set at the remaining useful life of the underlying plant, 31 years, which results in an amortization rate of 3.22%. This would have the effect of syncing the entire FMV of the acquisition – and the depreciation of the acquired assets and the PAA – to the same timeline.

Based upon competent, substantial, and material evidence in the record, the Commission concludes that the PAA amortization rate for the System should be set at the remaining useful life of the underlying plant, or 3.22%. Use of the 3.22% amortization rate would result in the purchase acquisition adjustment of approximately \$3.213 million related to this fair value transaction being amortized over a period of approximately 31 years.

EVIDENCE AND CONCLUSIONS OF LAW FOR FINDING OF FACT NO. 15

Due Diligence and Transaction Costs

The evidence for this finding of fact is contained in the original CPCN Application and the updates thereto, the Fair Value Docket, the testimony of CWSNC and the Public Staff witnesses in this proceeding, and in the Commission's records.

Based upon the recommendation of Public Staff witness Junis, Public Staff witness Feasel calculated depreciation and amortization expense on the entirety of the Commission-allowed rate base for the Carteret County fair value acquisition at a rate of 4.00% per year.

CWSNC witness Schellinger requested that the Commission set the amortization of the due diligence and transaction costs of \$312,039 at 2.50% and place them into the Organization plant account, similar to that of the Public Staff's recommendation in Docket

No. W-354, Sub 364, a general rate case proceeding related to CWSNC's acquisitions of Riverbend Estates Water Systems, Inc. (Docket Nos. W-390, Subs 13 and 14 and W-354, Sub 358) and Pace Utilities Group, Inc. (Silverton subdivision-Docket No. W-354, Sub 361 and W-1046, Sub 5), and consistent with the CWSNC Uniform Water rate division's rate.

The Commission determines that, consistent with the ratemaking treatment granted to CWSNC in the Sub 364 general rate case proceeding for the due diligence and transaction costs related to the acquisitions of the Riverbend Estates and Silverton service areas, it is reasonable and appropriate to set the amortization of the due diligence and transaction costs of \$312,039 for the System at 2.50% and record the asset amount into the Organization plant account. Further, the Commission finds that the 2.50% amortization rate requested by CWSNC in this proceeding is consistent with the amortization rate for this category of plant for CWSNC's Uniform Water rate division. The Public Staff did not provide any persuasive evidence in the present proceeding to deviate from this asset classification or amortization rate previously approved by the Commission for CWSNC.

IT IS, THEREFORE, ORDERED as follows:

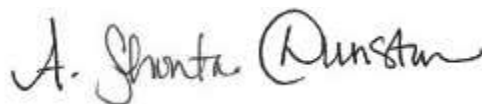
1. That CWSNC is hereby granted a certificate of public convenience and necessity to provide water utility service in North River/Mill Creek and Merrimon service areas in Carteret County, North Carolina effective upon the date CWSNC provides the Commission notice of closing of the sales transaction;
2. That Appendix A, attached hereto, constitutes the Certificate of Public Convenience and Necessity;
3. That at the earlier of 30 days of this Order or the closing of the sale of the System, CWSNC shall file for Commission approval a rate schedule that complies with this Order, said rates to apply for four years after the date of the closing, unless otherwise ordered by this Commission;
4. That the going forward depreciation rates on the acquired assets shall be equal to that of the CWSNC Uniform Water rate division, which results in the assets becoming fully depreciated in approximately 31 years;
5. That the amortization rate for the due diligence and transaction costs is set at 2.50% and such costs shall be placed into the Organization plant account;
6. That the Purchase Acquisition Adjustment amortization rate is set at 3.22%, consistent with the expected remaining useful lives of the acquired assets;
7. That the Public Staff and CWSNC shall work together to recommend an appropriate bond, which shall be approved by further order of the Commission; and

8. That CWSNC shall submit a proposed customer notice to the Commission for review and approval, and upon approval of the notice by the Commission, shall give appropriate notice of the approved rate increase by mailing the notice to each of the System customers during the billing cycle following the closing of the sale of the System.

ISSUED BY ORDER OF THE COMMISSION.

This the 29th day of August, 2023.

NORTH CAROLINA UTILITIES COMMISSION

A handwritten signature in black ink that reads "A. Shonta Dunston". The signature is written in a cursive style with a large, stylized "D" at the end.

A. Shonta Dunston, Chief Clerk

DOCKET NO. W-354, SUB 399

Commissioner Floyd B. McKissick, Jr., concurring:

I dissented from the Order in the companion case to this one, Docket No. W-354 Sub 398, in which Carolina Water Service Inc. of North Carolina (Carolina Water) sought and received approval to establish the rate base for the Carteret County Water System (System) pursuant to the fair value method set out in N.C. Gen. Stat. § 62-133.1A (Fair Value Proceeding). I had several significant concerns about granting that application, including the fact that the System was constructed in part with \$6,491,452 in federal and state grants which may or may not be repaid; that it seems that System customers will face higher rates than they otherwise would have under continued County ownership; that the appraisals were deficient; that the rate base requested was unjustified and excessive, among many other factors; therefore I did not find the evidence supporting the fair value determination to be probative.

Now that the Fair Value Proceeding is resolved and the rate base of the System established, the Commission evaluates different variables in deciding whether to grant a Certificate of Public Convenience and Necessity (CPCN) to Carolina Water for the System. Carolina Water's ability to operate the System is uncontested. While I continue to have serious concerns relating to the rate impacts of the transaction on System customers, when next called upon to set retail rates for Carolina Water, the Commission will set rates that are just and reasonable under the facts and circumstances as revealed by the evidentiary record at that time. Accordingly, I concur in the Commission's decision to grant a CPCN.

\s\ Floyd B. McKissick, Jr.
Commissioner Floyd B. McKissick, Jr.

**STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH**

DOCKET NO. W-354, SUB 399

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION
CAROLINA WATER SERVICE, INC. OF NORTH CAROLINA

is granted this

CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

to provide water utility service in

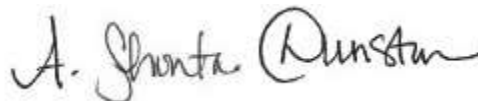
NORTH RIVER/MILL CREEK AND MERRIMON SERVICE AREAS

Carteret County, North Carolina,
subject to any orders, rules, regulations,
and conditions now or hereafter lawfully made
by the North Carolina Utilities Commission.

ISSUED BY ORDER OF THE COMMISSION.

This the 29th day of August, 2023.

NORTH CAROLINA UTILITIES COMMISSION

A handwritten signature in black ink that reads "A. Shonta Dunston". The signature is written in a cursive, flowing style.

A. Shonta Dunston, Chief Clerk