STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH

Docket No. W-1300, Sub 92

In the Matter of Blue Heron Asset Management, LLC and Liberty Senior Living , LLC, Complainants v. Old North State Water Company, Inc. Respondent	)	Post Hearing Brief of Respondent in Support of Motion to Dismiss and in Opposition to Motion for Judgement on the Pleadings

In accordance with the Commission's procedural orders in this docket Old North State Water Company, Inc. ("Old North State") submits this post hearing brief in support of its positions as addressed comprehensively in its Proposed Order submitted simultaneously herewith.

A. Complainants made concessions in oral argument on October 4, 2023 supporting Old North State's Motion to Dismiss.

At the oral argument on October 4, 2023 the positions and allegations of the Complainants, Blue Heron Asset Management ,LLC ("Blue Heron") and Liberty Senior Living LLC ("Liberty Senior") confronted challenges from Old North State and probing questions from the Commission panel. In that context the fallacy and lack of persuasiveness of Complainants' positions were laid bare. Following, are examples from the transcript illustrating these points. In addition, this brief repeats the analysis of the Commission's determinations in Docket No. W-354, Sub 118 explaining the distinction between a negotiated connection fee and a uniform connection fee. This brief addresses Complainants' arguments that Commission decisions on the taxability of contributions in aid of construction have relevance to this dispute. The brief

addresses Complainants' arguments that laws subsisting at the time of a contract provide terms missing in the documents allegedly constituting a contract.

At the oral argument on October 4, 2023 Counsel for Blue Heron was asked (transcript p. 85. l. 9),

> The Application states: "The customer agrees to promptly pay the application fee, service fees, late fees and after hour fees, et cetera, at the utility's standard rate as set forth by the utility."
>
> How do you interpret "promptly" and are you -- and is your client in violation of the requirement of promptly making that payment?

Counsel responded (transcript p. 85, l. 18):

> So, you know, when I look at the language, it says "application fee, service fee, late fees, after hours fees." It's not clear that they are -- it doesn't specifically say "tap fees" or "connection fees," which are terms that Old North State has used in its instructions. So it's not clear that it applies to connection fees.
>
> Here, I also -- I think, to the extent that prompt payment of connection fees was expected, it seems like it was waived by Old North State since they didn't say, you know, "there's no contract because you didn't pay it quickly."
>
> You know, they accepted the fact that there are some issues in terms of the construction of the facilities and when we can connect. They seemed to accept the fact that they can wait a little while till you pay us until the facilities are ready, which is what the parties did.

Significantly, this response inaccurately leaves out the essential phrase in the portion of the application addressed by the Commission and Counsel for Complainants. The language from the application is "application fee, service fees, late fees, after hours fees, **and all other charges and fees."** Emphasis added. Under no interpretation of the application form can it be concluded that the requirement to make prompt payment failed to address connection fees or tap fees. Moreover, the response by Counsel underscores that Blue Heron bases its claim for an express, binding contract before April 19, 2021 on a single provision in the application form submitted and ignores this and other provisions in the form, which contradict the reliance upon

the single sentence and obviates the conclusion that no agreement as to the amount of connection fee to be paid existed on April 19, 2021.

At the October 4, 2023 argument Counsel for Complainants was asked to address Old North State's argument drawing a distinction between a negotiated rate and a uniform rate. (transcript pp. 86-88).

Counsel for Complainants responded (transcript p. 87, l. 5):

> So I think, with the Sub 9 Order, and really with the Sub 0 Order, they started with a negotiated rate in a contract.
>
> But then what happened is one of those parties, the utility, came to the Commission and said, "Will you make this negotiated rate that we negotiated as part of an asset purchase agreement? Will you make this the uniform connection rate that will apply to everybody going forward?"
>
> And the Commission said, "Yes. We approve that. The rate you're requested is reasonable. We're going to make that the rate.
>
> And so the Sub 0 Order did that for BCU, and BCU started charging that to customers as the connection fee.
>
> And the Sub 9 Order did that for Old North State, right? It said, "We see there is an asset purchase agreement. We understand you're asking to make that a uniform tariff. We are making that the uniform tariff going forward." And that's the tariff that my clients are asking to be applied to them.
>
> It's not a negotiated tariff. It may have originated as a negotiated tariff, but once the parties came to the Commission and, said, "Will you make this part of the tariff order?" It became a uniform tariff applied to everyone. And that's what we're asking to be applied to us.
>
> Commissioner Duffley: Okay. And what about the position that the parties are not similarly situated? The developers were not similarly situated.
>
> Counsel for Complainants:
>
> So I -- in candor, I don't fully understand the nuances of that argument that Old North State is making.

None of Complainants' recitations, paraphrasing and interpretations of the Commission's orders in Sub 0 or Sub 9 find any support whatsoever in this rather obvious misinterpretation and disinterpretation. The only reference to the Asset Purchase Agreement was the one sentence that indicated that the Asset Purchase Agreement established the purchase price between Newland and Old North State. Likewise, the orders made clear that the connection fees collected would be remitted to Newland, the developer that contributed the facilities at no cost. The order in Sub 0 addressed an initial application. The Commission had no operating experience on which to establish a rate. The rate base was $0.0. There was no finding that any rate or tariff was based on any legitimate cost of service principles. The connection fees were negotiated, so the Commission was not called on to establish them independently. In Sub 9, the only case involving Old North State, the Commission made no finding or conclusion as to the reasonableness of connection fees beyond that they were negotiated fees and that the connection fees so established would be remitted to Newland. No tariff or fees were changed. The Commission was not called upon to address the reasonableness of the tariff or fees going forward in Sub 9 as the parties had requested no change. Sub 9 was a transfer case, not a case for adjustment of rates. Complainants are in error in reading into the Commission's two orders findings and conclusions that are not there.

Old North State spent pages in its initial brief addressing the orders of the Commission in Docket No. W-354, Sub 118 addressing the distinction between a negotiated fee between the initial developer contributing the facilities to the utility and a uniform fee to be applied where no contract between a subsequent builder not contributing systems existed. The orders are a matter of public record. This distinction is a fundamental one clearly understood and applied in scores of wastewater service areas in North Carolina. It has been the black letter law in North Carolina for more than 25 years. It is repeated below. If Counsel for Blue Heron cannot understand the distinction, or, which is more likely, simply is unable to address the distinction, this fact should go far in persuading the Commission that Complainants' complaint should be dismissed.

The following dialogue appears at the October 4, 2023 argument, (transcript pp. 95 and 96):

> Maybe I've misunderstood the facts of the case, but I thought I heard Mr. Finley state there's an e-mail where it's saying: Let's figure out and settle what those tap these are.
>
> So could it be that they didn't pay the tap fee because they were still negotiating the tap fees versus they just didn't --were not sophisticated enough to calculate the tap fees?
>
> Counsel for Complainants :
>
> So what we're doing is we're now talking about two different sets of communications.
>
> So the Blue Heron communication, Blue Heron's the group that submitted the application, had an agreement, didn't mention tap fees. They asked for an invoice, right? That's an agreement on March 23rd.
>
> We're now moving into Liberty Senior.
>
> ***
>
> So Liberty Senior said -- they were aware of the tap fees, right?

This response by Counsel clearly and obviously misstates the facts. The e-mail to which the Commission's question was addressed was an e-mail on behalf of Kevin Wade, an employee of Blue Heron, not Liberty Senior. The e-mail was repeated verbatim in Respondent's verified answer. (pages 8-9). The e-mail was repeated verbatim in Respondent's initial brief. (page 5) The e-mail was cited by Counsel for Respondent only minutes before the question to Counsel for Complainants at the oral argument on October 4 (transcript p. 26, l. 18). The e-mail was recited verbatim several minutes after Counsel for Complainants misstated what the e-mail had said. (transcript p.118, l.16). The e-mail graphically disproves Blue Heron's claim that it had a binding, express contract as to the amount of connection fees to be paid before April 19, 2021. Pretending that the e-mail does not exist or through sleight of hand attributing the authorship of the e-mail to Liberty Senior instead of Blue Heron only drives home the point that Blue Heron's case is not supported by the facts and must be dismissed.

At the October 4, argument Counsel for Complainants states, (transcript p. 110, l. 8)

> Well, so that's why we take the position that the Sub 9 order, even though it doesn't explicitly incorporate the Asset Purchase Agreements, it does clearly implicitly incorporate the agreements by acknowledging them and acknowledging the history that led to the $1,500 per REU.

Any accurate reading of the Sub 9 order makes clear that the Commission did not incorporate any asset purchase agreement explicitly, implicitly, or otherwise. Even if an order had implicitly incorporated an agreement, an implicit incorporation cannot be enforced. Moreover, this answer by Counsel for Complainants is clearly at odds with the earlier statement that the terms of the Asset Purchase Agreement were approved and made a portion of the tariff.

At the October 4, 2023 argument the following statement appears, (transcript p. 106, l 3):

> the [handout] makes the argument for me at the top. The Sub 9 order incorporates the agreement's definition of REU.

Any accurate reading of the Commission's Sub 9 order refutes without question Counsel's argument that it incorporates the Asset Purchase Agreement's definition of REU for any customer other than a single family residential customer, which is not a customer to which any issue in this case relates whatsoever.

At the October 4, 2023 argument the following statement from Counsel appears. (pp. 108 & 109):

> And so, in other words, at the time that the Commission entered its Sub 9, Order, there was a prior BCU agreement where it said, "Can we please collect the fees as defined in the agreement?" And the Commission said yes in Sub 0?.

> Then Old North State shows up in 2014 and says, "Hey, can we continue to collect the exact same fee that BCU asked for in Sub 0?
>
> And, by the way, you know from the Asset Purchase Agreement the calculation of REU is the exact same.
>
> In the Commission's actual order, it acknowledges that Old North State is trying to continue to collect the exact same fee as BCU first wanted to collect back in 2009.
>
> And the Commission says, "We know that these fees are going to. These fees are going to go right back to BCU, part of the Asset Purchase Agreement, to pay what is owed.

In this inaccurate and misleading paraphrase Counsel for Complainants attempts twice to slip in references to the Asset Purchase Agreement addressing non-single family residence buildings such as paragraph 1.27 that simply do not appear in the Commission's orders.

> At the October 4, 2023 argument the following appears (p. 75, l. 23):
>
> And what he seems to say-- and I'm not sure this is accurate-- is he seemed to say, "Well, if you don't side with Old North State, ratepayers are going to be punished here."
>
> And I'm not sure that's the case. Because my understanding is that, to the extent Old North State needs to collect more for the fact that it's not collecting enough from these two developers, it needs to come to the Commission and ask for a rate increase.
>
> And that rate increase is gonna be based on the expectation that it prudently managed its construction operations and the collection of fees.
>
> And I would say that if a utility miscalculated what it should be charging to developers to the point that it now needs to collect more from others to pay for it, maybe the utility shouldn't be able to collect that from the ratepayers.
>
> Maybe that's something that's on the utility for not properly managing how it estimates costs, how it comes to the Commission to ask for rate increases, and how it manages construction.
>
> So I'm not willing to accept as, you know, the gospel that ratepayers are going to have-- be forced to pay for the increased cost of the construction if the Commission honors the prices that we believe it should be honoring for complainants.

The undisputed, verified evidence in this case is that Old North State is required to incur the cost to expand its facilities including expanding the sewage treatment plant and constructing a lift station and force main to be able to provide service to Blue Heron and Liberty Senior. (Old North State Response, pp. 4, 8-9, 11, 12, 15). The undisputed, verified evidence in this case is that to the extent that Old North State is not permitted to recover the costs for the expansion of the sewage treatment plant and the lift station and the force main through connection fees, Old North State must recover those costs from consumers through usage rates. (Response pp. 5, 12, 18, 28). Counsel for Complainants' musings and speculations are nothing more than musings and speculations. Complainants have made no allegation and have presented no verified pleading that the facilities to which Old North State refers were caused by any cost causer other than builders such as Blue Heron and Liberty Senior. Likewise, there is no evidence and no supported verified allegation that Old North State has mismanaged its planning of additions to the sewage treatment system in Briar Chapel that would justify a disallowance of costs. The verified evidence submitted by Old North State at the request of the Commission is that the timing of the additions Old North State must undertake to serve Blue Heron and Liberty Senior was based upon the timing of expansion of the spray irrigation facilities by Newland. There is no allegation or verified evidence that Old North State has been imprudent or unreasonable in incurring the costs it seeks to recover from Blue Heron and Liberty Senior. Old North State justified the increase in connection fees, which the Commission approved in Sub 71, based on the filing that Old North State made that was audited by the Public Staff and that resulted in a Public Staff recommendation that the increase be approved. Consequently, the argument by Complainants that should the Commission allow them to interconnect at a cost less than that approved in Sub 71 the shortfall would not be recovered from other customers who did not cause the costs must be rejected. Complainants have moved for judgment on the pleadings. The argument Counsel makes here cannot be found in any of Complainants' pleadings. The arguments Old North State makes are in the verified pleading and verified submissions.

At the October 4 argument the following took place, (transcript p. 77, l. 8):

> Commissioner Duffley: Mr. Schauer, before you move on, you made a comment that - that a developer has a choice: either let the utility build themselves or they would build the facilities.
>
> And how can you make that choice if you don't know the price?
>
> Mr. Schauer:
>
> So I don't think you can. Which is why -- which is why they were asked-- you know, my clients were asking for the price at the time and which is why I think that the price can't change once it's agreed to.

Blue Heron submitted its application to Old North State on March 23, 2021. Old North State responded to the application with respect to price on that same date by saying that Old North State would submit an invoice in the future. 27 days later, on April 19, 2021, immediately after the Commission issued its order in Sub 71 increasing the connection fees to $4,000 per REU, Old North State, as promised, submitted the invoice. On March 23, 2021 and April 19, 2021, Blue Heron was well under way with its project. No evidence exists that Blue Heron owned any land on which to construct a wastewater treatment facility. It had no permit from DEQ to discharge effluent from any wastewater treatment plant it might have contemplated. It had no contractor to construct a wastewater treatment facility. It had no permission from Chatham County to proceed with its construction on the assumption that Blue Heron would construct and operate a self-owned sewage treatment system. For Blue Heron to suggest that based on its unsupported conclusion that it could interconnect to the Old North State system for $69,000 based on its March 23 application, having been forewarned that an invoice would be submitted that would make no reference to $69,000 so that Blue Heron forewent a decision within those 27 days to build its own sewage treatment facilities, exceeds credibility.

On April 19, 2021 Blue Heron was in receipt of Old North State's invoice. Blue Heron was aware at that time of what Old North State intended to charge for interconnection. Blue Heron

had 17 months to choose not to interconnect with Old North State but to construct its own sewage treatment facilities. Blue Heron's argument that Old North State's delay of 27 days deprived Blue Heron of an opportunity to self-build sewage treatment facilities for its multi-unit apartment complex is feckless

At the October 4, 2023 argument the following statements of Counsel for Complainants took place, (transcript pp. 78 and 79)

page 78, line 2:

> So I think there was a clear meeting of the minds on compensation. There's not a defined number, because interpretation is required, but both parties agree: However the Commission interprets it, that's what the Complainants are gonna pay.

***

Page 79, line 13:

> They're both saying, "Commissioners, please tell us what it is, and that's gonna resolve the dispute. We disagree what it is. We can't resolve it ourselves. Please tell us what it is."

Page 80, line 17:

> And I would reiterate that we do strongly believe that there was a meeting of the minds for the reasons set forth.

Page 81, line 2 :

> It's like, "Well, no. You understood that the Commission sets rates. They determined that." So long as the rates are calculated consistent with the Commission, there was a meeting of the minds. It's just that it wasn't precise on that one term.

Page 81, line 15 :

> And so, what they did is they said, "We're going to pay the tariffed rates under Sub 9."

But there's-- you know, it turns out there's a disagreement on how exactly that applies in this context, and we leave it to the Commission to decide.

And so I do think there was a meeting of the minds on all essential terms.

Page 84 line 19:

So where those terms aren't set by law, I think there may not be a meeting of the minds.

But when the law says these are the terms, you cannot negotiate them, then there doesn't need to be a meeting of the minds on those terms. Because in some ways maybe they're not essential because they're already -- they've already been dictated.

Respectfully, Old North State is at a loss to comprehend the arguments Complainants are making and what position Complainants are taking with respect to the issue of whether or not there was a meeting of the minds. All of this inconsistent argumentation illustrates that there was no agreement or meeting of the minds between Blue Heron and Old North State. By arguing that the law, as established and implemented by the Commission, provides the missing agreement and missing meeting of the minds, Blue Heron is left with an argument that the 2014 Asset Purchase Agreement provides the missing element. The fallacy of this argument is that the Commission has never approved or endorsed any provision of the 2014 Asset Purchase Agreement to which Blue Heron points. Blue Heron's arguments simply fall apart under their own weight.

Page 88, line 20:

But Old North State came to the Commission and said, "Please approve our ability to charge every developer and new resident who wants to connect $1,500 per REU."

And once they did that, they're saying, we don't care if you're not similarly situated, Blue Heron and" -- I'm referring to my clients back here-- Blue Heron and Liberty Senior, because the Commission said we can charge you the same rate. So the fact that you're not similarly situated no longer matters. The Commission says we apply the $1,500 per REU rate to everybody going forward. It's the uniform tariff. "

Once again, Complainants are attributing to Old North State's request and to the Commission's order provisions that do not exist. The Sub 9 order refers to the 2014 Asset Purchase Agreement only to the extent the agreement refers to the purchase price. The Sub 9 order states that connection fees established thereunder will be remitted to Newland. Blue Heron and Liberty Senior contributed no facilities as did Newland. Collection fees collected by Old North State from Blue Heron will not be remitted to Newland because the facilities for which the connection fees serve as reimbursement were not built by Newland. They are financed initially by Old North State. Old North State came to the Commission and sought $4,000 per REU to recover the costs of the facilities to serve Blue Heron. All this is clearly set forth in the terms of the Commission's order and the verified response of Old North State. There is no evidence in the record to the contrary. Blue Heron and Newland are clearly distinguishable.

The $1,500 connection fee approved in Sub 9 was a rate negotiated with Newland, the developer, which installed the initial facilities and contributed them to Old North State. The connection fee established by the Commission in Sub 71 was the uniform rate to be charged builders like Blue Heron and Liberty Senior for which no agreement existed addressing contributed facilities and the rate the utility should charge through which to reimburse the initial developer.

At the October 4, 2023 argument the following took place, (transcript p. 106, l. 2):

> And if you could look at the handout that says-- and it makes the argument for me at the top. The Sub 9 Order incorporates the agreement's definition of REU.

The Sub 9 order in no respects incorporates any provision of the 2014 Asset Purchase Agreement addressing the calculation of a billing determinant through reference to a provision such as section 1.27. There is only one reference to the Asset Purchase Agreement in the Sub 9 order. That reference is to the fact that the Asset Purchase Agreement establishes the purchase

price. No decretal paragraph or tariff provision suggests in any way that the definition of REU incorporates the provisions of the 2014 Asset Purchase Agreement.

Page 106, line 23:

> and BCU shows up and says, "we would like the ability to collect the $1,500 per REU that we're obligated to collect per our purchase agreement."
>
> So there's no question. I don't think there's any question that BCU, when it was asking for a $1,500 per REU connection fee, was asking for a connection fee as calculated by the purchase agreement that it had signed, and the purchase agreement that obligated it to ask for the ability to collect the connection fee.

There is no provision in the Sub 0 order that in any respect supports Counsel's paraphrase of the order and that reads into that order provisions that are not there.

Page 108, line 21:

> and so, in other words, at the time that the Commission entered the Sub 9 order, there was a prior BCU agreement where it said, can we please collect the fees as defined in the agreement? And the Commission said yes in Sub 0.

Nowhere in the Sub 0 or Sub 9 orders does the Commission say the connection fee approved or the billing determinant approved is based on the Asset Purchase Agreement. While it is correct that the $1,500 per REU approved and Sub 0 and Sub 9 are the same rate negotiated by the parties in various Asset Purchase Agreements, the Commission in no respect examines the reasonableness of the agreements or bases its determinations in the two orders on any other cost of service justifications. It did not do so because the connection fees were negotiated because after collected by the utility they would be remitted to Newland as partial reimbursement for the facilities Newland contributed to the utility.

Below Old North State repeats for the Commission's convenience in full the portion of Old North State's references in its reply to the Commission's orders in Docket No. W-354, Sub 118. These orders address the distinction between a negotiated connection fee between the developer that installs and contributes sewer facilities to the utility and receives reimbursement through subsequent tap fee remittances and new developers or builders, like Blue Heron and Liberty Senior, that contributed no facilities and with which the utility has no contract and for which a uniform tariff is necessary.

B. **Distinction between asset reimbursement remitted to the initial developer that contributes facilities and asset reimbursement from subsequent builders that do not.**

1. **Commission Precedent Addressing Connection Fees Established in Asset Purchase Agreements as Part of the Compensation to the Seller of a Wastewater System and Connection Fees Based on Traditional Cost of Service Principles Demonstrates that Complainants' Allegations Must Be Dismissed.**

In a number of dockets involving the connection fees charged by Carolina Water Service the issue arose as to whether the Company was required to charge its tariffed uniform connection fees or was authorized to charge a different level of connection fees upon certain acquisitions and whether connection fees the Company collected and then passed through to developers that sold systems to the Company should be reflected as contributions in aid of construction and thereby reduce the rate base.

The Commission was required to address situations such as those addressed in this docket in which the level of connection fees was established in Asset Purchase Agreements negotiated between the developer of systems that had incurred the initial expense in installing the systems and the utility acquirer of the systems. The Commission was required to address situations in which the level of connection fees assessed by the utility that factored into the purchase price and that was not based on traditional cost of service principles was lawful and appropriate. The Commission carefully examined this issue and determined that the Company had acted prudently, appropriately and with the best interest of its customers in mind in negotiating

contracts calling for connection fees forming an essential component of the purchase price and not based upon traditional cost of service principles. The Commission likewise endorsed the process through which the utility, subsequent to acquisition, assessed connection fees from new builders and passed the fees through to the developer/seller. The Commission found the practice prudent, appropriate and in the best interest of customers. In opposition to Public Staff and Attorney General recommendations to the contrary, the Commission determined that connection fees so collected and passed through to the developer did not constitute contributions in aid of construction that should be subtracted from rate base. By contrast, connection fees assessed under tariffs based on cost of service principles and approved in advance by the Commission that are retained by the utility to finance system improvements constitute contributions in aid construction and reduce rate base.

a. Connection Fees Established As Part of the Purchase Price Between a Developer and the Public Utility Are Based On Competitive Market Considerations and Receive Treatment by the Commission Different from Connection Fees Established in More Traditional Contexts.

This issue was addressed extensively by the Commission in its orders dated March 22, 1994 and February 27, 1998 in Docket No. W-354, Sub 118 , *In the Matter of Carolina Water Service Inc of North Carolina - Investigation of Tap and Plant Modification Fees.*

> The evidence in this case indicates that CWS has utilized two primary methods over its 22-year history in North Carolina to acquire new systems and expand into new areas. One method has been the purchase of existing utility systems. The other method has been to contract with developers of areas contiguous to an already certificated CWS system for the authority to provide water and or sewer utility service. The systems generally are constructed by others in order to facilitate the construction of residential subdivisions. In obtaining systems during the time it has operated in North Carolina, CWS has followed a consistent pattern. CWS has entered into contracts with the sellers of systems through which the Company has sought to minimize development risk for CWS and its ratepayers. CWS's objective has been to maximize contributions in aid of construction (CIAC) collected from developers of new areas and to obtain existing systems at a reasonable cost per connection. CWS asserts that it has sought to obtain systems where there was an opportunity to expand in the future and take advantage of economies of scale.

Each contract CWS enters into when it acquires systems contains provisions addressing the mechanism through which CWS accomplishes its investment objectives. The consideration exchanged by CWS and the developer or builder is established through contractual provisions identifying facilities the seller conveys and setting forth the compensation, if any, CWS pays for such facilities.

This pattern of compensation and facility transfer differs with each CWS system acquisition. Each service area is unique; each seller, developer or builder has different needs and objectives. The varying competitive market forces dictate what compensation the seller requires for the facilities conveyed in an arms-length transaction to CWS and the price CWS is willing to pay for those facilities. The sales price for the systems are not regulated per se, for there is no tariff or Commission rule controlling the price of utilities CWS acquires. However, regulation does exist in the form of oversight in certificate of public convenience and necessity proceedings or subsequent general rate cases.

Issues such as the level of connection fees, whether connection fees are waived or collected, the timing of collection of such fees, and whether the fees are retained by CWS or remitted to a third party, are necessarily tied to the agreed upon compensation paid for the facilities conveyed. For the reasons outlined above, CWS has negotiated contracts that call for many different approaches to the timing, mechanics, and the level of compensation, reflecting the different risks and the circumstances of each situation. This has caused different mechanisms and levels of connection fees to be charged to builders. CWS asserts that the delicate balance between the purchase price paid for utility facilities and CIAC collected has resulted in a reasonable and appropriate investment per connection and that the reasonableness of the Company's investment is evidenced by the approvals granted in general rate case and certificate of public convenience and necessity orders issued over a long period of time. According to CWS, accomplishment of its investment goal has resulted in a reasonable rate base and the payment of a reasonable amount as return on the rate base through rates paid by customers. CWS takes the position that the evidence of this conclusion is found not only in the record of this proceeding but in the orders entered by the Commission during the Company's 22-year history.

An examination of CWS's investment practices over its history in North Carolina reveals that the Company's practices have been consistent and that the mechanism of connection fees has been used to obtain funds from or convey funds to sellers of systems. Where CWS has a contract establishing connection fees, the Company has relied upon those contractual terms as dictating and subsequent activities regarding the connection fees.

...

> As explained above, in the excerpts from the Docket No. W-354, Sub 118 order, the contract defined connection fees are based upon an arms-length transaction between CWS and the seller. Each transaction is based upon its own unique circumstances and, therefore, such details as connection fees may be unique and vary from transaction to transaction. Connection fees defined in a contract approved by and on file with the Commission, for a given subdivision shall be the governing connection fees in that subdivision. Otherwise the approved uniform connection fees shall apply in the absence of a contract.
>
> Based upon the foregoing, the Commission finds that the Public Staff request that CWS should be required to provide justification where it has varied in its uniform connection fee should be denied. The presence of a contract approved by the Commission and on file with the Commission, provides CWS the justification it needs to charge a connection fee that varies from its uniform connection fee. As noted above, in the case where the different connection fees are specified in an approved contract, the contract governs. In the absence of the approved contract, the uniform connection fees govern.

Emphasis added.

The practice the Commission addressed with respect to the Carolina Water Service acquisitions from developers is the same practice followed by the Briar Chapel Utilities and Old North State that acquired the systems at issue in this docket from the developer, NNP. The connection fees of $1,500 and the REUs representing the billing determinants used to calculate the multiples of the $1,500 for individual connections were negotiated between the developer that built, financed, and installed the sewage treatment facilities that it sold to Briar Chapel Utilities and Old North State and that NNP agreed to install through an Asset Purchase Agreement. As part of the transaction set forth in the Asset Purchase Agreement, Briar Chapel Utilities/Old North State would assess the connection fees at the $1,500 level and remit them to the developer. In this fashion, the connection fees served as a delayed method of compensation to the developer that had conveyed the facilities to Old North State at a 0 cost. This was all in accord with typical financial arrangements occurring scores of times where developer owned systems are acquired by public utilities in North Carolina.

Blue Heron and Senior Liberty are not privy to nor a successor in interest to previous Asset Purchase Agreements between NNP and Old North State. While there has been a transfer of facilities providing wastewater services in the Briar Chapel service area, that transfer was based upon an Asset Purchase Agreement in which the rate base to the acquirer, the

connection fees to be charged and the REUs serving as billing determinants for calculating the connection fees for each connection were interdependent. Each of those variables was negotiated between the seller and the acquirer and determined the rate base in the hands of the acquirer, the connection fees to be charged and the REU's serving as billing determinants for calculating the connection phase for each connection or interdependent. Each of those variables was negotiated between the seller and the acquirer and determined the rates in the hands of the acquirer. The seller knew the acquirer would bear responsibility to finance in some measure through connection fees. The acquirer agreed to collect and pass through the connection fees to the seller. The NCUC approved the transfer and did not question the usage rate requested, the rate base established in the transfer of the collection fees or REUs in the Asset Purchase Agreement.

With respect to Briar Chapel the situation changed in 2021. The developer had received or was receiving appropriate remuneration through the connection fees passed through at the $1,500 level. Old North State, having acquired the systems from Briar Chapel Utilities, faced the responsibility of expanding the sewage treatment plant by 250,000 gpd and installing a force main and lift station to serve structures such as those being built by Blue Heron. The cost of this expansion was not one borne by NNP, the developer, but would be borne initially by Old North State. The $4,000 connection fee and the REUs were based on traditional cost of service principles and were calculated to reimburse Old North State over time for the cost of facilities such as the 250,000 gpd expansion, the construction of the force main and the lift station.

In the Sub 71 docket Old North State supported its request for an increase in the connection fees to $4,000 per connection on an exhibit setting forth in detail the estimated cost of the 250,000 gpd expansion needed to serve builders such as Blue Heron. The $4,000 supported by this evidence and approved by the Commission supplanted the $1,500 per connection and the REU calculations set forth in the Asset Purchase Agreement with NNP. The REU relied upon by Old North State enabled Old North State to collect from builders like Blue Heron an appropriate level of funds at $4,000 per connection to pay at least in part for the facilities such as the expansion, the force main and the lift station. Should the Commission agree with Blue Heron that the builder, Blue Heron, should be assessed a connection fee less

than the $4,000 and based on an REU lower than that relied upon by Old North State, the investment such as that Old North State represented to the Commission it would offset by the connection fees will not be offset, rate base will not be offset by the contributions in aid of construction, and end use customers will bear the cost of the expansion in contradiction to the Commission's intent in approving the request in Sub 71.

With reference to the Carolina Water Service example, the $4,000 connection fee is equivalent to the uniform connection fee.

b. Builders That Do Not Install Facilities and Have No Contract Addressing Connection Fees Must Pay Connection Fees Established by the Commission on Terms the Commission Approves Based On Cost of Service Principles.

This situation within Brier Chapel was likewise addressed by the Commission in its 1994 and 1998 orders in Docket No. W-354, Sub 118.:

> Although CWS relies primarily upon its contracts with the seller to determine the connection fees charged within a service area, occasions arise where the connections are made that are not covered by any contract. For example, the developer may complete the sales of homes within the subdivision and leave a number of lots without new homes. Subsequently someone else will buy the lots and construct homes in situations not covered under the contract with the original developer. In other situations, a portion of the subdivision will be sold by the original developer to a third party before homes are constructed. CWS may have no contract with the subsequent developer of the new section.
>
> Without a provision in the Company's tariff authorizing it to assess connection fees in those situations, CWS would have difficulty collecting any connection fees at all. Consequently, in 1981, CWS requested uniform system-wide rates in the Sub 16 docket and at that time sought a tariffed set of connection fees. In its filing, CWS clearly indicated that the tariffed tap fees established by the Commission were to apply only where no contract existed for a different fee.

Emphasis added

This situation addressed in the Carolina Water Service orders is comparable to the one in Briar Chapel at issue here. The buildings Blue Heron seeks to connect are not those built by NNP, with whom the Asset Purchase Agreement addressed in Sub was negotiated. Without the

order in Sub 71 it would be inappropriate and contrary to the public interest to charge a connection fee not based on the cost to construct the facilities such as the 250,000 GPD expansion, the lift station and the force main and remit the fees to the developer that will not finance these expenditures. The fees addressed in Sub 9 were not intended to apply to the property Blue Heron bought from NNP and not covered by any Asset Purchase Agreement between the original developer and the utility. If Blue Heron's theory is correct and the terms of the Asset Purchase Agreement and the Commission's orders in Subs 0 and 9 control, for any connection assessed at the time of the Blue Heron application was accepted, Old North State must remit these collections to NNP. NNP would conclude that it had won the lottery without even purchasing a ticket.

Old North State applied to the Commission to increase its tariffed connection fees to $4,000 per REU. The expansion of the facilities such as the sewage treatment plant, the lift station and the force main were necessary to serve builders such as Blue Heron and Liberty Senior. The connection fees established at $4,000 per REU from Blue Heron were not to be remitted to the developer, NNP, because the developer bore no responsibility to pay for that expansion and the construction of these facilities. Had the situation been otherwise the Commission would never have approved the request. The $4,000 per REU collected from builders such as Blue Heron would not be remitted to the developer but would be retained by Old North State. These connection fees would constitute contributions in aid of construction and would reduce rate base and thereby benefit the end use customers in the Briar Chapel service territory.

c. Connection Fees Approved By The Commission For Builders Not Addressed in Asset Purchase Agreements and Not Remitted To The Developer Constitute Contributions In Aid Of Construction.

The Commission in its orders in Docket No. W-354, Sub 118 confronted arguments by the Public Staff and the Attorney General that where Carolina Water Service entered into contracts calling for the Company to remit to the developer connection fees, the Commission should attribute to the Company the connection fees so remitted as reductions to rate base. The Commission rejected those arguments.

> The penalty the Public Staff urges the Commission to employ is to reduce rate base by $3 million, or by approximately 20%. The theory of this penalty is that CWS should have charged its uniform, tariffed connection fees, and had it done so, cash CIAC would have increased by $3 million. Notwithstanding the many harsh admonitions and reprimands the Commission has delivered over the years to CWS regarding its connection fee practices and procedures, there is no reasonable basis, legal or equitable, upon which to adopt the ratemaking adjustment through the imputation of connection fees proposed in this case by the Public Staff and Attorney General.

Sub 118 Order, NCUC Orders & Decisions, 1994, p. 653.

When Old North State remits to NNP connection fees obtained upon interconnection by structures constructed by NNP covered by the Asset Purchase Agreement between NNP, Briar Chapel Utilities and Old North State and addressed in Subs 0 and 9, the connection fees so remitted do not reduce rate base. NNP had contributed to the utility the facilities to serve structures from which those connection fees were collected. Blue Heron has contributed nothing. Blue Heron is a builder that acquired property from NNP. Old North State must expand the sewage treatment plant and construct other facilities initially at its own expense. Old North State is charging Blue Heron that builder's pro rata share of the cost to be reimbursed to make these improvements. Old North State will not remit to NNP any of the connection fees assessed to Blue Heron. The full amount of the fees collected from Blue Heron will constitute contributions in aid of construction, will reduce rate base, and will inure to the ultimate benefit of the end use consumers in the Briar Chapel subdivision.

C. Commission orders addressing the payment of taxes on contributions in aid of construction and the party responsible for the payments are not relevant to the issues in this docket.

Blue Heron was forced to submit a 20 page reply brief in its feeble effort to rebut Old North State's responsive brief in this docket. Old North State submitted no reply brief because Blue Heron submitted nothing requiring a reply in its initial brief. On page 6 of the Blue Heron reply brief under the heading "The contract formed on March 23, 2021 was a 'sale' under Rule R10-20," Blue Heron meanders into a discussion of contributions in aid of construction. It is

unclear the relevance of the discussion of a contribution in aid of construction to Blue Heron's argument with respect to a sale. It is relevant however that finally after Old North State has stressed from the beginning of this dispute that the connection fees paid by Blue Heron constitute a contribution in aid of construction so as to reduce rates and reduce rate base upon which Old North State earns a return that Blue Heron mentions for the first time contributions in aid of construction. These undisputed facts nullify Blue Heron's allegations that Old North State is engaged in a scam or other of the alleged nefarious actions asserted by Blue Heron.

Blue Heron acknowledges, as if there were any dispute, that Blue Heron's connection fees constitute a contribution in aid of construction. Blue Heron cites *In Re: Matter of Application by Aqua North Carolina Inc,...*, Docket No. W-218, Sub 396 for the proposition that connection fees are contributions in aid of construction. Blue Heron cites *In the Matter of Carolina Water Service Inc. of North Carolina - Investigation of Tap and Plant Modification Fees,* Docket No. W-354, Sub 118, stating "when a utility contracts with a developer to collect the connection charges ... from the developer in several payments, a liability to pay taxes on CIAC is incurred upon the execution of the contract." Blue Heron also cites *In the Matter of Impact of the Federal Tax Cuts and Jobs Act on Contributions In Aid of Construction for Water and Wastewater Companies* - Docket No. W-100, Sub 57, addressing the Commission's determination of when the federal income tax on contributions in aid of construction is to be borne by the contributing developer or the utility.

None of this discussion and none of Blue Heron 's citations have anything to do with any dispute in this docket. The issue in this docket is whether it is Old North State or Blue Heron that is in violation of N.C. Gen. Stat. § 62-139. There is no issue with respect to the assessment of federal or state income taxes on the collection of a contribution in aid of construction. The issue is when a service is rendered under N.C. Gen .Stat. § 62-139. Under any interpretation the Commission might employ in this docket, unless the connection fees are remitted to Newland, they will be a contribution in aid construction. The extent of which an issue might arise as to when the taxes are due and who owes them is not an issue in this docket. Blue Heron's belated effort to address the issue of contributions in aid of construction is a red herring and a rather

obvious effort to engage in yet another frolic and detour to divert the Commission's attention from the relevant issues in this docket.

D. Complainants' arguments that the law which subsists at the time and place of making a contract rectifies the missing elements in the Old North State - Blue Heron contract are unavailing.

Blue Heron argues on pages 9 and 10 of its Brief Supporting Judgment on the Pleadings:

> Old North State contends that Blue Heron's tender of the application could not be an offer because the application did not state the applicable connection fee, and an offer missing the material term is not a valid offer. *See*, Resp. at 7. North Carolina law says otherwise. Laws which subsist at the time and place of the making of a contract ... enter into and form a part of it, as if they were expressly referred to or incorporated by its terms. *N.C. Ass'n of Educators Inc. v. State*, 368 N.C. 777, 789, 786 S.E.2d 255, 264 (2016) (quoting *Home Builders & Loan Association v. Blaisdell*, 290 U.S. 398, 429-30 (1934)). The rates for connection service were prescribed as a matter of law by the Commission. *See,* N.C. Gen. Stat § 62-139(a). The application did not need to state the prescribed rates in order for the rates to be incorporated into the offer and subsequent contract.

The N.C. Ass'n of Educators case addressed the constitutionality of changes to the State's Career Status Law that purported to eliminate or reduce the tenure rights of teachers who had entered into valid contracts of employment with their employers.

Blue Heron cites the Court's discussion on page 789:

> We conclude the Career Status Law did not itself create any vested contractual rights.
>
> However, our analysis does not end here. Laws which subsist at the time and place of the making of a contract... enter into and form a part of it, as if they were expressly referred to or incorporated in its terms . (Citation omitted) Before receiving career status, plaintiffs entered individual contracts with local school boards. Implied as a part of each of these contracts was the Career Status Law. As the State concedes in its brief, the applicable statutory terms must be read into the contracts and the contracts incorporated the statutory body of school law applicable to plaintiffs as teachers. The statutory system that was in the background of the contract between the teacher and the board set out the mechanism through which the teachers could obtain career status. A teacher's career status rights under the Career Status Law become vested only upon completion of several consecutive years as a probationary teacher and then receiving approval from the school board. Thus, vesting stems not from the Career Status Law, but from the teacher's entry into an individual contract with the local school

> system. At the time the parties made the contract, the right to career status vested. At that point, the General Assembly no longer could take away vested rights retroactively in a way that would substantially impair it.

The issue in the N.C. Ass'n of Educators case is not one addressing any dispute arising under Chapter 62 of the General Statutes. The statute Blue Heron asserts as the law which subsists at the time and the place of the making of the Blue Heron contract is N.C. Gen. Stat. § 62-139. As addressed at length by the parties, while Blue Heron asserts that its right to service under that statute arose at the time of the alleged contract, Old North State maintains that the statute addresses obligations of the parties at the time service is rendered, which took place 17 months subsequent to the entering of the alleged contract. The holding of the N.C. Ass'n of Educators case does nothing to aid the Commission in resolving that fundamental dispute.

The N.C. Ass'n of Educators case did not address a contract between teachers and their school boards with missing essential terms such as the length of the contract, the terms of compensation or terms outlining tenure. There was no issue of failure of the contracting parties to have a meeting of the minds as is the case before the Commission here. The Court addressed reading into valid and consummated contracts statutory context addressing tenure. The N.C. Ass'n of Educators case is not in any respect on all fours with the case the Commission must address here. Moreover, the Court ruled that changes in the Career Status Law purporting to limit rights under the employment contracts could not be enforced retroactively.

Blue Heron's real argument is that section 1.27 of the 2014 Asset Purchase Agreement and the Commission's order in Sub 9 establishing rates for connection fees of $1,500 provide the missing information absent from the alleged March 23, 2021 contract between Old North State and Blue Heron. Section 1.27 of the 2014 Asset Purchase Agreement and the Commission's order in sub 9 are not laws in any respect equivalent to the State's Career Status Law.

More to the point, N.C. Gen. Stat.§ 139(a) cited by Blue Heron addresses enforceability of utility rates in effect at the time of service. As discussed in great detail by Old North State in its filings in this docket, the date service was provided to Blue Heron was August 31, 2022, not March 23, 2021 when Blue Heron submitted it incomplete application.

Respectfully submitted, this 29 day of November, 2023.

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/s/ Edward S. Finley, Jr.
Counsel for Old North State
Water Company

CERTIFICATE OF SERVICE

I hereby certify that a true and exact copy of the foregoing Post Hearing Brief was duly served upon parties of record either by depositing same in a depository of the United States Postal Service, first class postage prepaid, or by electronic delivery.

This the 29th day of November 2023

Edward S. Finley, Jr.,

/s/ Edward S. Finley, Jr.

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