

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Pennsylvania Public Utility Commission	:	R-2017-2624240
Office of Consumer Advocate	:	C-2017-2626954
	:	
v.	:	
	:	
Newtown Artesian Water Company	:	

RECOMMENDED DECISION ON REMAND

Before
Christopher P. Pell
Deputy Chief Administrative Law Judge

I. INTRODUCTION

The Public Utility Commission remanded this matter to the Office of Administrative Law Judge for the purposes of allowing the parties to introduce relevant evidence addressing the single issue of whether Newtown Artesian Water Company has exceeded its DSIC cap and will continue to exceed it, and whether this justifies the requested increase to a 7.5% cap. This decision determines that the Company has exceeded its 5% DSIC in two consecutive quarters and is likely to continue to exceed the 5% DSIC cap if it continues to move forward with its capital improvement program and its Commission-approved LTIP. However, this decision recommends that the Company’s request to increase its DSIC cap from 5% to 7.5% should be denied since it did not meet its burden of demonstrating that an increase to the DSIC cap is necessary and in the public interest.

II. HISTORY OF THE PROCEEDING

On September 1, 2017, Newtown Artesian Water Company (Newtown Artesian, NAWC or Company), Utility Code 212070, filed Supplement No. 126 To WATER-PA. P.U.C.

No. 9 (Supplement No. 126) to become effective November 1, 2017. Supplement No. 126 proposes to increase NAWC's existing Distribution System Improvement Charge (DSIC) cap from 5% to 7.5%.

On September 29, 2017, the Office of Consumer Advocate (OCA) filed a Public Statement, a Notice of Appearance on behalf of Christine Maloni Hoover, Esq., and Erin L. Gannon, Esq., and a formal Complaint. The Complaint was docketed at C-2017-2626954.

By Order entered October 5, 2017, the Pennsylvania Public Utility Commission (Commission) instituted an investigation into the lawfulness, justness, and reasonableness of the rates, rules, and regulations contained in NAWC's proposed Supplement No. 126 To WATER-PA. P.U.C. No. 9. The Commission ordered that the Company's proposed Supplement No. 126 To WATER-PA. P.U.C. No. 9 be suspended by operation of law until May 1, 2018, unless otherwise directed by Order of the Commission. The Commission further ordered that the investigation shall include consideration of the lawfulness, justness, and reasonableness of the existing rates, rules, and regulations of NAWC. The matter was assigned to the Office of Administrative Law Judge for the prompt scheduling of hearings culminating in the issuance of a Recommended Decision.

In accordance with the Commission's October 5, 2017, Order, the matter was assigned to Deputy Chief Administrative Law Judge Christopher P. Pell.

A Prehearing Conference was held on November 8, 2017. Counsel for NAWC and OCA participated.

By Prehearing Order dated November 17, 2017, I identified the parties of record and established the procedural schedule and the procedures applicable to this proceeding.

On November 6, 2017, Newtown Artesian served the following Direct Testimony: the Direct Testimony of Harold Walker, III, NAWC Statement No. 1; and the Direct Testimony of George Forsyth, NAWC Statement No. 2.

On November 20, 2017, OCA served the Direct Testimony of Jerome D. Mierzwa, OCA Statement No. 1.

On November 29, 2017, Newtown Artesian served the Rebuttal Testimony of Harold Walker, III, NAWC Statement No. 1R.

On December 6, 2017, OCA served the Surrebuttal Testimony of Jerome D. Mierzwa, OCA Statement No. 1-SR.

On December 6, 2017, I emailed the parties the cross-examination matrix for the hearings in this proceeding. I directed the parties to complete the cross-examination matrix and return it to me by the close of business on December 7, 2017. The parties completed the matrix as requested.

The evidentiary hearing was held as scheduled in Philadelphia on December 11, 2017. During the hearing, NAWC presented the rejoinder testimony of Harold Walker, III, and made Mr. Walker available for cross-examination by the OCA. NAWC Witness George Forsyth was excused from appearing at the hearing as OCA did not request to cross-examine him, and also because I did not have any questions for him. OCA also presented its witness, Jerome D. Mierzwa, for cross-examination. NAWC and OCA both moved to have their witnesses' testimony and exhibits entered into the record. As there were no objections, all testimony and exhibits were admitted into the record during the hearing.

In accordance with my November 17, 2017, Prehearing Order, the parties filed Main Briefs on January 4, 2018, and Reply Briefs on January 16, 2018.

I issued a Recommended Decision on February 9, 2018. NAWC filed Exceptions to my Recommended Decision on March 1, 2018. OCA filed Reply Exceptions on March 12, 2018.

By Commission Order dated April 26, 2018 (April 26, 2018 Order), the Commission recognized that after the record closed in this matter, NAWC filed its DSIC

quarterly update stating that it had exceeded the 5% cap and that its expenditures had already reached 5.44%. The Commission determined that this information may prove relevant to the disposition of this matter and gave NAWC the opportunity to voluntarily file an extension of its rate suspension, set to expire on May 1, 2018, for an additional 90 days. The Commission noted that if NAWC filed this extension, then the matter would be remanded to the Office of Administrative Law Judge to reopen the record for proceedings necessary for the introduction of additional relevant evidence, subject to the examination of the OCA and the introduction of its own evidence. The Commission further noted that a remand would be limited to the single issue of whether NAWC has exceeded its DSIC and will continue to exceed it, and whether this justifies the requested increase to a 7.5% cap.

On April 26, 2018, NAWC filed Supplement No. 133 to Tariff Water Pa. P.U.C. No. 9 to voluntarily extend the effective date of Supplement No. 126 to Water Pa. P.U.C. No. 9 from May 1, 2018 until July 30, 2018.

By email dated April 27, 2018, I provided the parties with a proposed schedule for hearings and briefs and directed that they develop and submit, for my consideration, a procedural schedule for this matter. I directed the parties to submit this proposed schedule no later than the close of business on April 30, 2018.

On April 30, 2018, the parties provided me with their proposed schedule.

By Prehearing Order Setting Procedural Schedule On Remand dated May 1, 2018, I adopted the parties' proposed schedule.

On May 4, 2018, Newtown Artesian served the following testimony: the Testimony on Remand of Harold Walker, III, NAWC Statement No. 1 Remand; and the Testimony of George Forsyth, NAWC Statement No. 2 Remand.

On May 11, 2018, OCA served the Testimony on Remand of Jerome D. Mierzwa, OCA Statement No. 1-RM.

On May 15, 2018, Newtown Artesian served the Rebuttal Testimony On Remand of Harold Walker, III, NAWC Statement No. 1R Remand.

On May 15, 2018, I emailed the parties the cross-examination matrix for the hearing in this proceeding. I directed the parties to complete the cross-examination matrix and return it to me by 12:00 p.m. on Thursday, May 17, 2018. The parties subsequently informed me that they had agreed to waive cross-examination of all witnesses and were prepared to stipulate to the admission of testimony and exhibits into the record.

The evidentiary hearing was held as scheduled on May 18, 2018. During that hearing, counsel for NAWC and OCA stated on the record that they agreed to waive cross-examination of the other party's witnesses and moved to have their pre-served testimony and exhibits admitted into the record. Accordingly, all parties' testimony and exhibits were admitted into the record during the hearing.

In accordance with my May 1, 2018, Prehearing Order, the parties filed Main Briefs on Friday, May 25, 2018, and Reply Briefs on May 31, 2018. The parties' Main and Reply Briefs on Remand are made a part of the record through this Recommended Decision.

The record in this proceeding consists of the transcripts of the prehearing conference and both evidentiary hearings, and the statements and exhibits sponsored by the parties during the December 11, 2017, and May 18, 2018, hearings. The record closed on May 31, 2018, after I received the parties' Reply Briefs.

III. FINDINGS OF FACT

1. Newtown Artesian Water Company is a public utility that provides water service to 10,554 customers in Newtown Borough, Newtown Township, and the northern portion of Middletown Township, Bucks County. NAWC St. No. 2 at 1-2; NAWC Exh. 1, Supporting Information for Supplement No. 126 at 1-2 and 5.

2. NAWC's water distribution system includes approximately 130 miles of mains, 1,000 hydrants, 3,200 valves and 10,300 meters. NAWC Exh. 1, Supporting Information for Supplement No. 126 at 2.
3. NAWC's DSIC is currently capped at 5%. NAWC St. 1 at 2.
4. On January 22, 2018, NAWC filed a DSIC quarterly update with a February 1, 2018, effective date (January 2018 DSIC filing). NAWC Exh. HW-1 Remand, Sch. 1 at 2.
5. NAWC's January 2018 DSIC filing calculated a DSIC rate of 5.44%. NAWC Exh. HW-1 Remand, Sch. 1 at 2.
6. NAWC did not include Private Fire Protection customer revenues in its January 2018 calculations. NAWC St. 1 Remand at 3.
7. Including Private Fire Protection customer revenues would reduce the February 2018, DSIC rate to 5.25 %. OCA St. 1RM at 2; NAWC Exh. HW-1 Remand, Sch. 3 at 1.
8. On April 20, 2018, NAWC filed a DSIC quarterly update with a May 1, 2018, effective date (April 2018 DSIC filing). NAWC Exh. HW-1 Remand, Sch. 2 at 2.
9. NAWC's April 2018 DSIC filing calculated a DSIC rate of 5.71%. NAWC Exh. HW-1 Remand, Sch. 2 at 2.
10. NAWC did not include Private Fire Protection customer revenues in its April 2018 calculations. NAWC St. 1 Remand at 3.
11. Including Private Fire Protection customer revenues would reduce the May 2018 DSIC rate to 5.48%. OCA St. 1RM at 4; NAWC St. 1 Remand at 3.

12. NAWC's Long Term Infrastructure Improvement Plan (LTIIIP) related capital improvement program expenditures are projected to be approximately \$4,251,000 between 2017, and 2021. NAWC St. No. 1 at 3; NAWC St. 2, Att. 1 at 12; NAWC St. No. 1R at 3.

13. The capital expenditures projected in NAWC's Annual Asset Optimization Plan (AAOP) and in the Company's LTIIIP for the years 2019, 2020, and 2021 project that the Company's DSIC will increase to 6.3% after 2018, to 8.87% after 2019, to 10.47% after 2020, and to 11.49% after 2021. NAWC St. No. 1 Remand at 6.

14. NAWC's projected DSIC rates through 2021 are based on the assumption that NAWC will not file a base rate case before 2021. OCA St. 1RM, Sch. JDM-1.

15. NAWC has not filed a base rate case since 2011. OCA St. 1 at 5.

16. Filing a base rate case will reset the Company's DSIC rate to zero. 66 Pa.C.S. § 1358(b)(1); NAWC Exh. HW-1 Remand, Sch. 7.

17. A base rate case will change the ratio of LTIIIP expenditures to rate base value and the total customer bill to which the DSIC is applied will likely be higher. OCA St. 1RM at 5; OCA St. 1SR at 5.

18. The Company's Purchased Water Adjustment Clause and the Fully Projected Future Test Year are alternates available to NAWC to address the potential regulatory lag in the financing of LTIIIP improvements. OCA St. 1 at 6; OCA St. 1SR at 7; 66 Pa.C.S. § 315(e).

IV. DISCUSSION

A. Applicable Legal Standards

1. Burden of Proof

The public utility bears the burden of proof to establish the justness and reasonableness of its requested rate increase. As set forth in Section 315(a) of the Public Utility Code, 66 Pa.C.S. § 315(a):

Reasonableness of rates – In any proceeding upon the motion of the Commission, involving any proposed or existing rate of any public utility, or in any proceedings upon the complaint involving any proposed increase in rates, the burden of proof to show that the rate involved is just and reasonable shall be upon the public utility.

The Commonwealth Court has stated:

Section 315(a) of the Public Utility Code, 66 Pa.C.S. § 315(a), places the burden of proving the justness and reasonableness of a proposed rate hike squarely on the utility. It is well-established that the evidence adduced by a utility to meet this burden must be substantial.¹

The Pennsylvania Supreme Court has stated that the party with the burden of proof has a formidable task to show that the Commission may lawfully adopt its position. Even where a party has established a prima facie case, the party with the burden of proof must establish that “the elements of that cause of action are proven with substantial evidence which enables the party asserting the cause of action to prevail, precluding all reasonable inferences to the contrary.”² Furthermore, it is well-established that the “degree of proof before administrative tribunals as well as before most civil proceedings is satisfied by establishing a preponderance of the evidence.”³ Additionally, the evidence must be substantial and legally

¹ *Lower Frederick Twp. v. Pa. Pub. Util. Comm’n*, 48 Pa. Commw. 222, 226-27, 409 A.2d 505, 507 (1980) (citations omitted). See also, *Brockway Glass v. Pa. Pub. Util. Comm’n*, 63 Pa. Commw. 238, 437 A.2d 1067 (1981).

² *Burleson v. Pa. Pub. Util. Comm’n*, 461 A.2d 1234, 1236 (Pa. 1983).

³ *Lansberry v. Pa. Pub. Util. Comm’n*, 578 A.2d 600, 602 (Pa.Cmwlth. 1990).

credible, and cannot be mere “suspicion” or a “scintilla” of evidence.⁴ Thus, a utility has an affirmative burden to establish the justness and reasonableness of its rate request.

2. Act 11 Statutory Provisions

Act 11 of 2012, effective April 16, 2012, (Act 11) amended Chapters 3, 13 and 33 of the Public Utility Code (Code). 66 Pa.C.S. chs. 3, 13, 33. Act 11, in part, establishes a DSIC mechanism that allows certain utilities, including electric distribution companies; natural gas distribution companies (NGDCs); city natural gas operations; and water and wastewater companies, with distribution or collection systems, upon Commission approval, to recover the costs related to the repair, improvement, and replacement of eligible property outside of a rate case. 66 Pa.C.S. §§ 1350-1360.

Section 1351 of the Code sets forth the definitions for “eligible property” for each utility type, including water utilities.

For water utilities, eligible property shall include:

- (i) Utility service lines, meters and hydrants installed as in-kind replacements for customers.
- (ii) Mains and valves installed as replacements for existing facilities that have worn out, are in deteriorated condition or are required to be upgraded to meet under 52 Pa. Code Ch. 65 (relating to water service).
- (iii) Main extensions installed to eliminate dead ends and to implement solutions to regional water supply problems that present a significant health and safety concern for customers currently receiving service from the water utility.
- (iv) Main cleaning and relining projects.
- (v) Unreimbursed costs related to highway relocation projects where a water utility must relocate its facilities.
- (vi) Other related capitalized costs.

66 Pa.C.S. § 1351.

⁴ *Id.*

As a precondition to the implementation of a DSIC, Act 11 requires that a utility must file a long-term infrastructure improvement plan (LTIP) with the Commission and specifies the information to be included in the LTIP. 66 Pa.C.S. § 1352.

Section 1353(a) of the Code specifically provides as follows:

(a) Authority.—Except as provided under this subchapter, after January 1, 2013, a utility may petition the commission, or the commission, after notice and hearing, may approve the establishment of a distribution system improvement charge to provide for the timely recovery of the reasonable and prudent costs incurred to repair, improve or replace eligible property in order to ensure and maintain adequate, efficient, safe, reliable and reasonable service.

66 Pa.C.S. § 1353(a).

Section 1358 of the Code provides various customer protections. Section 66 Pa.C.S. § 1358(a)(2), establishes a general rate cap. Under this section, a DSIC granted to a water utility under former section 1307(g) . . . or this subchapter may not exceed 7.5% of the amount billed to customers. Under certain circumstances, Section 1358(b) requires that a DSIC rate be reset to zero. After a reset, only fixed costs of new eligible property not previously reflected in base rates may be reflected in a quarterly DSIC update. The DSIC rate is reset to zero if new base rates are established. 66 Pa.C.S. § 1358(b)(1). For investor-owned utilities, a reset is also required if, in any quarter, data filed with the Commission in the utility's most recent annual or quarterly earnings report show that the utility will earn a rate of return that would exceed the allowable rate of return used to calculate its fixed costs under the DSIC.

66 Pa.C.S. § 1358(b)(3).

Section 1358(c) of the Code, 66 Pa.C.S. § 1358(c), provides that, absent an express limitation on existing ratemaking authority, the Commission retains its full and existing ratemaking authority. Accordingly, the Commission has the full power and authority under the Code to examine, investigate, and audit any and all aspects regarding the data, operation, and implementation of the DSIC to the same extent that it would review a non-DSIC rate matter. In

exercising its ratemaking authority, Section 1301 of the Code mandates that the Commission determine “[e]very rate made, demanded, or received by any public utility ... shall be just and reasonable, and in conformity with regulations or orders of the commission.” This mandate applies to the DSIC rate in this proceeding. 66 Pa.C.S. § 1301. Finally, Section 1358(e) requires that all DSICs shall be subject to audits by the Commission and annual reconciliation based on a period consisting of the twelve months ending December 31 of each year. 66 Pa.C.S. § 1358(e)(1)(i), (ii).

On August 2, 2012, the Commission entered its Order in *Implementation of Act 11 of 2012*, Docket Number M-2012-2293611 (*Final Implementation Order*), which established procedures and guidelines necessary to implement Act 11 and included a Model Tariff for DSIC filings.

B. Whether the Company Has Exceeded Its 5% DSIC Cap.

1. Newtown Artesian’s Position.

The Commission recognized, in its April 26, 2018 Order, that NAWC had filed its *January 2018 DSIC Quarterly Filing*. The January 2018 DSIC Quarterly Filing, which was submitted to the Commission on January 22, 2018, with an effective date of February 1, 2018, was assigned to Docket No. M-2018-2643814. Following the filing of the January Quarterly DSIC, NAWC submitted its *April 2018 DSIC Quarterly Filing*. The April 2018 DSIC Quarterly Filing, which was submitted to the Commission on April 20, 2018, with an effective date of May 1, 2018, was assigned to Docket No. M-2018-3001339. NAWC asserts that its Quarterly DSIC filings effective February 1, 2018, at M-2018-2643814 and effective May 1, 2018, at M-2018-3001339 exceed the current 5.0% cap. The DSIC calculation also increased from the February submission to the May submission. (NAWC MB at 6).

NAWC acknowledges that its DSIC rates effective February 1, 2018 and May 1, 2018 were calculated exclusive of private fire protection service, and that subsequent to the submission of the February and May calculations, the Commission concluded in its April 26,

2018 Order that private fire protection customers should be charged the DSIC. NAWC asserts that the inclusion of private fire protection service in the DSIC calculations has no material impact on the February and May calculations. As shown in Exhibit HW-1 Remand, Schedule 3, the Company's DSIC rate of 5.44%, effective February 1, 2018, would have been 5.25% if the Company included private fire protection service in the calculation. Also, as shown in Exhibit HW-1 Remand, Schedule 4, the Company's DSIC rate of 5.71%, effective May 1, 2018, would have been 5.48% if the Company included private fire protection service customers in the calculation. NAWC asserts that its DSIC surcharge remains above 5.0% even with private fire protection service included in the DSIC calculations. The Company further asserts that with the inclusion of private fire protection service, the DSIC calculation would have increased from 5.25% to 5.48% from February 1, 2018, to May 1, 2018. (NAWC MB at 7-8).

NAWC also notes that it considered The Tax Cuts and Job Act of 2017 ("TCJA") in preparing its February 2018 and May 2018 DSIC calculations, and that it did not include the new TCJA federal tax rate in the February DSIC calculation since all the investment and related expenses occurred in 2017, before the TCJA went into effect. NAWC asserts that its use of the pre-TCJA federal tax rate in the February calculation is consistent with Section 1357(b)(1) of the Public Utility Code which directs that the pre-tax return will be calculated using the federal income tax rate "as of the last day of the three-month period ending one month prior to the effective date of the DSIC." The pre-TCJA federal tax rate was in effect on December 31, 2017, the last day of the three-month period ending one month prior to the February 1, 2018 effective date of the January 2018 DSIC filing. (NAWC MB at 8; NAWC RB 3).

NAWC notes that it did include the new TCJA federal tax rate in the May calculation of 5.71% as shown on Schedule 2 of Exhibit HW-1 Remand. All the investment and related expenses for the May calculation occurred in 2018, after the TCJA went into effect. The new TCJA federal tax rates were in effect on March 31, 2018, the last day of the three-month period ending one month prior to the May 1, 2018, effective date of the April 2018, DSIC filing. (NAWC MB at 8-9).

In response to OCA's witness Mierzwa's contention that a prior period DSIC undercollection of 0.07% should have been excluded from the January 2018 DSIC calculation, NAWC maintained that the prior period undercollection must be included in the DSIC calculation since it is required by Commission approved tariff language. The Commission's approved formula for the DSIC calculation, which includes the "e" reconciliation factor (in this case an undercollection) is presented at page 28 of the Company's tariff:

The formula for calculation of the DSIC surcharge is as follows:

$$\text{DSIC} = \frac{(\text{DSI} \times \text{PTRR}) + \text{Dep} + e}{\text{PQR}}$$

Where:

DSI = the original cost of eligible distribution system improvement projects.

PTRR = the pre-tax return applicable to eligible distribution system improvement projects.

Dep = Depreciation expense related to eligible distribution system improvement projects.

e = the amount calculated under the annual reconciliation feature as described below.

PQR = Projected quarterly revenue including any revenue from acquired companies that are new being charged the rates of the acquiring company.

NAWC asserts that it is incorrect and misleading for the OCA to attempt to characterize a required component of the Commission approved DSIC formula as an "upward adjustment." (NAWC MB at 10; NAWC RB at 3, 6).

NAWC further notes that the OCA now acknowledges that "the facts now show that NAWC exceeded the [5%] DSIC cap" in its most recent quarterly DSIC filings effective February 1, 2018 and May 1, 2018.⁵ Even with the inclusion of private fire protection service

⁵ OCA Main Brief on Remand at 5.

revenue, the DSIC calculations at 5.25% as of February 1 and 5.48% as of May 1 were above 5%. (NAWC RB at 3).

In sum, NAWC posits that there is substantial evidence of record to demonstrate that the Company's DSIC is above 5%. The current DSIC calculation, effective May 1, 2018, is 5.48%, excluding short term debt, using the actual cost of long term debt, including private fire protection service and reflective of the new TCJA federal tax rate. (NAWC MB at 9; NAWC RB at 4).

2. OCA's Position.

In the underlying proceeding, the Commission determined that NAWC had not shown that increasing the DSIC cap was necessary or in the public interest.⁶ The evidence showed, *inter alia*, that NAWC had not exceeded a 5% DSIC rate since implementing a DSIC in 1998. After the record closed, NAWC filed two quarterly updates indicating that absent a 5% cap, its DSIC rate would be 5.44% and 5.71%, respectively. OCA disputes the amount by which NAWC exceeded the DSIC cap but acknowledges that the facts now show that NAWC exceeded the DSIC cap in those two quarters. The question before the Commission, however, is whether NAWC has shown that an increase to the DSIC cap is necessary and in the public interest. OCA asserts that exceeding the DSIC cap in two quarters does not outweigh the substantial evidence against waiving the statutory cap. (OCA MB at 5).

While NAWC calculated a DSIC rate above 5% in two quarters, OCA notes that it introduced evidence in this proceeding on remand showing it was by a smaller margin than the Company claimed. In the underlying proceeding, the Commission found that NAWC had not properly calculated the DSIC rate and ordered the Company to recalculate its DSIC rate for the four-year period ending November 2017, and to change its calculation going forward.⁷ According to OCA, NAWC made some but not all of those corrections in its DSIC rate for the first two quarters of 2018. With respect to the January 2018, DSIC Filing, the Company did not

⁶ April 26, 2018, Order at 32.

⁷ April 26, 2018, Order at 42-43.

include Private Fire Protection customers in the calculation of the DSIC rate. OCA witness, Mr. Mierzwa provided the following explanation:

A comparison of the revenues shown on Schedule 5, page 1, and Schedule 3, page 1, attached to Mr. Harold Walker, III's testimony indicates private fire protection revenues of \$46,575 should have been included in NAWC's January 2018 DSIC calculation. Reflecting these private fire protection revenues would have reduced NAWC's DSIC by [sic] to 5.25 percent, or by 0.19 percent.⁸

Accordingly, OCA asserted in its Main Brief that the calculated DSIC rate for February 1, 2018 should have been 5.25% rather than 5.44%, and that for the May 1, 2018, DSIC the correction for Private Fire Protection reduced the calculated rate from 5.71% to 5.48%. OCA MB at 5-6. In its Reply Brief, OCA noted that the Company now acknowledges and agrees with the rates as calculated by OCA if the calculations include Private Fire Protection.⁹ OCA asserted that this downward revision to the NAWC's DSIC is significant in that the Company's DSIC rates for these two quarters exceeded 5% by a smaller margin than originally claimed by the Company, and that this does not support a waiver of the statutory 5% cap. OCA RB at 3-4.

Additionally, according to OCA, both 2018 DSIC Filings contain upward adjustments that are not reflective of the Company's actual DSIC expenses/expenditures and will change in future DSIC filings. The pretax rate of return used by the Company to calculate the January 2018, DSIC Filing did not reflect the changes resulting from the TCJA of 2017. OCA posits that, while this is consistent with the statutory DSIC calculation,¹⁰ the Company may have over collected DSIC revenues for that quarter because the revenues will be taxed at the new, lower federal corporate tax rate. As stated by OCA witness Mierzwa:

Because the revenues from the February 1, 2018, DSIC rate will accrue to the Company in 2018, the Company will actually be taxed on that income at the 21 percent federal income tax rate.

⁸ OCA St. 1RM at 2 (footnote omitted); *see also* NAWC Exh. HW-1 Remand, Schs. 3 at 1, 5 at 1.

⁹ NAWC MB at 7.

¹⁰ Section 1357(b)(1) of the Public Utility Code provides that pre-tax return will be calculated using the state and federal income tax rates "as of the last day of the three-month period ending one month prior to the effective date of the DSIC and subsequent updates." 66 Pa. C.S. § 1357(b)(1).

Therefore, based on the tax change calculations provided by Mr. Walker, the February 1, 2018, DSIC rate has a built-in overcollection of 0.48 percent that is not reflective of NAWC's current DSIC-related income tax liability.¹¹

Also, the calculated February 2018 DSIC rate includes an upward adjustment of 0.07% due to prior period undercollections.¹² Prior period undercollections also raised the May 2018 DSIC rate by 0.25% (or 0.24% if you include Private Fire Protection revenues).¹³ These adjustments for prior period undercollections do not reflect NAWC's current DSIC capital expenditures. In future quarters, the adjustments could be larger, smaller, or even serve to reduce the DSIC rate if there is a prior period overcollection. But for the possible tax-related overcollection in the January 2018 DSIC Filing and the prior period undercollections reflected in both quarters, the calculated February and May 2018 DSIC rates would be closer to 5%. OCA maintains that this does not support a waiver of the 5% DSIC cap. (OCA MB at 6-7; OCA RB at 4-5).

3. Discussion and Conclusions

The Commission remanded this matter to the OALJ to determine, in part, whether NAWC has exceeded its current 5% DSIC cap. This was in response to NAWC's *January 2018 DSIC Quarterly Filing* stating that it had exceeded the 5% cap and that its expenditures had already reached 5.44%. The evidence of record demonstrates, and the parties agree, that the Company exceeded its 5% DSIC cap in two consecutive quarters. Although OCA disputes the proper calculation of the DSIC, it acknowledges that "the facts now show that NAWC exceeded the DSIC cap in those two quarters by some amount."¹⁴

The dispute in the calculation of the DSIC stems from the fact that, initially, NAWC did not include private fire protection customers in its calculation of the DSIC rate. NAWC acknowledged that its February 1, 2018, and May 1, 2018, DSIC rates (5.44% and 5.71% respectively) were calculated exclusive of private fire protection customers as these rates

¹¹ OCA St. 1RM at 3 (citing NAWC Exh. HW-1 Remand, Sch. 5 at 1).

¹² NAWC Exh. HW-1 Remand, Sch. 1 at 7.

¹³ NAWC Exh. HW-1 Remand, Sch. 2 at 3, Sch. 4 at 1.

¹⁴ OCA MB at 5.

were calculated and submitted prior to the Commission's April 26, 2018 Order that private fire protection customers should be charged the DSIC. NAWC further acknowledged that its February 1, 2018 and May 1, 2018 DSIC rates would have been 5.25% and 5.48% respectively if the Company had included private fire protection. When including private fire protection, as is required, NAWC's calculation of the DSIC coincides with the OCA's calculation.

Regarding the OCA's assertion that both 2018 DSIC filings contain upward adjustments that are not reflective of NAWC's current expenditures, it is important to remember that the Commission remanded this matter to determine, in part, whether NAWC exceeded its 5% DSIC cap. The Commission did not place any caveats or limitations on that directive, such as removing overcollections from the calculation. Upon review of the record, I find that the Company calculated its DSIC in accordance with statutory provisions regarding the DSIC and its Commission-approved DSIC formula, as well as in accordance with the Commission's April 26, 2018 Order. These calculations demonstrate that the Company's DSIC did, in fact, exceed the 5% DSIC cap in two consecutive quarters in 2018.

C. Whether the Company Will Continue to Exceed Its 5% DSIC Cap.

1. Newtown Artesian's Position

NAWC notes that Section 1356 of the Public Utility Code provides that a utility with an approved distribution system improvement charge and LTIIP shall file an AAOP. NAWC filed its AAOP for the year ended December 31, 2017 on April 3, 2018. A copy of the AAOP is included in the evidentiary record as Attachment A to NAWC Statement No. 2 Remand and as Schedule 6 to NAWC Statement No. 1 Remand, Exhibit HW-1. The projected expenditures for 2018 presented in the AAOP demonstrate that the Company's DSIC related investment will continue to exceed its current DSIC rate cap of 5% given the fact the Company's current DSIC calculation as of May 1, 2018 is already in excess of 5%. Stated differently, NAWC asserts that its calculated DSIC will continue to increase and exceed the current 5% cap as the Company continues to make further DSIC eligible capital improvements. (NAWC MB at 12).

NAWC Statement No. 1 Remand, Exhibit HW-1, Schedule 7 presents the estimated year end DSIC rate assuming the Company makes the DSIC related capital expenditures projected for 2018 in the AAOP and for 2019, 2020, and 2021, assuming the Company makes the projected DSIC related capital expenditures in its approved LTIIP. The DSIC rate calculations shown on Schedule 7 include private fire protection service customers. NAWC asserts that, per Schedule 7, the Company's current DSIC rate of 5.48% is projected to increase to 6.30% after the 2018 DSIC related infrastructure is completed, to 8.87% after the 2019 DSIC related infrastructure is completed, to 10.47% after the 2020 DSIC related infrastructure is completed, and to 11.49% after the 2021 DSIC related infrastructure is completed. NAWC maintains that the information shown on Schedule 7 demonstrates that the Company's DSIC related investment will continue to exceed its current DSIC rate cap of 5%. (NAWC MB at 12).

In response to OCA's perceived uncertainties as to whether the DSIC will continue to exceed 5% because projected capital expenditures may be overstated, NAWC asserts that it is certain that the DSIC will continue to exceed 5%. With the current DSIC calculation in excess of 5%, the DSIC will continue to be above 5% as NAWC continues to move forward with its capital improvement program and its Commission approved LTIIP. NAWC asserts that, even if projects are completed under budget, the additional dollars of DSIC eligible investment will continue to cause the DSIC, which is already above 5%, to increase further. (NAWC MB at 13; NAWC RB at 5-6).

2. OCA's Position

In addition to submitting evidence that the Company has exceeded a 5% DSIC rate in the first half of 2018, the Company provided a schedule intended to show that its DSIC rate will be higher than 5% through 2021 if NAWC does not file a base rate case before 2021 and its actual expenditures meet or exceed its projected expenditures.¹⁵ OCA maintains, however, that having a DSIC rate higher than 5% does not entitle a utility to a cap waiver. Each

¹⁵ NAWC St. 1 Remand, Sch. 7.

utility's request is evaluated on a case by case basis, based on review of the complete record, to determine whether a cap waiver is necessary and in the public interest.¹⁶ (OCA MB at 7).

According to OCA, NAWC's arguments that it will continue to exceed a 5% DSIC rate are based on assumptions that do not support a waiver of the DSIC cap. First, the DSIC rate projections contained in Schedule 7 assume that NAWC will not file a base rate case before 2021. OCA notes that it has already been seven years since the Company filed a base rate case. Lengthening that interval by waiving the DSIC cap is not consistent with the policy of the Commission or the intent of the statutory cap waiver provision. The DSIC cap serves to prevent extended periods between base rate proceedings.¹⁷ As stated by the Commission in its denial of Columbia Gas' Petition to increase its DSIC cap:

We agree that the 5% DSIC cap underscores the function of the DSIC, which is to supplement, rather than replace base rate proceedings.¹⁸

The OCA's witness testified regarding the value of base rate proceedings:

[Base rate proceedings] provide the opportunity for simultaneous review of all aspects of a utility's revenues, expenses and capital costs for the same period of time.¹⁹

(OCA MB at 7-8).

Second, OCA notes that the projections in Schedule 7 assume that the Company will spend the annual amounts forecasted in the remaining years of its LTIP (2018 through 2021). However, in 2017, which was the first year of its LTIP, the Company substantially overstated its LTIP projections. The Company's AAOP for Year Ended December 31, 2017, attached to NAWC witness Walker's testimony on remand, shows that projected LTIP expenditures for 2017 were \$1.03 million, but actual expenditures were only \$0.705 million.²⁰

¹⁶ April 26, 2018, Order at 33-34.

¹⁷ 66 Pa. C.S. § 1358(a); *Petition of PAWC to Establish a DSIC*, P-00961031, 1996 Pa. PUC LEXIS 182 at *21 (Aug. 26, 1996) (*PAWC 1996*).

¹⁸ *Petition of Columbia Gas of Pa., Inc.*, P-2016-2521993, Opinion and Order at 50 (Dec. 22, 2016).

¹⁹ OCA St. 1 at 5.

²⁰ NAWC St. 2 Remand, Att. 1 at 3.

This is a difference of \$324,374, or more than 30%. OCA posits that it is equally possible that the Company's projected expenditures in other years of the LTIIP will be overstated. (OCA MB at 9).

If NAWC begins to spend as much as projected and exceeds a 5% DSIC rate, it has the ability to file a base rate case, roll its DSIC into base rates for recovery and reset the DSIC rate to zero.²¹ A base rate case will also change the ratio of LTIIP expenditures to rate base value and the total customer bill to which the DSIC is applied will likely be higher. OCA maintains that this will increase the amount the Company can recover with a 5% DSIC cap. (OCA MB at 9; OCA RB at 6).

Lastly, the OCA notes that in any quarter, the DSIC rate is subject to adjustment for prior period undercollections or overcollections. In the latter case, this would have the effect of reducing the Company's DSIC rate below projections. Any resulting overcollections will have a downward effect of the DSIC rate in future quarters. Moreover, OCA argues that if the Company's LTIIP expenditures are below budget, then the Company's actual DSIC rates will be less than projected, and closer to 5%. (OCA MB at 9; OCA RB at 5).

Accordingly, OCA maintains that NAWC's Schedule 7 does not show with certainty that the Company's DSIC rates will continue to exceed the 5% cap. Considered with all the evidence in the record, the possibility that NAWC could exceed a 5% rate prospectively is not sufficient to warrant an increase to the Company's DSIC cap. (OCA MB at 9-10; OCA RB at 6).

3. Discussion and Conclusions

In addition to determining whether NAWC has exceeded its current 5% DSIC cap, the Commission remanded this matter to determine, in part, whether NAWC will continue to exceed its 5% DSIC cap. In addressing this portion of the remanded issue, the parties considered the option of the Company filing a base rate case in lieu of an increase to the DSIC

²¹ 66 Pa. C.S. § 1358(b)(1).

cap. Any discussion of whether the Company should file a base rate case in lieu of receiving an increase to the DSIC cap is more appropriately addressed in the final section of this decision, where the Commission has directed that a determination be made as to whether current and future DSIC rates justify the requested increase to 7.5%.

As previously noted, the Company has demonstrated, and the parties agree, that NAWC's DSIC exceeded the 5% DSIC cap in two consecutive quarters in 2018. Upon review of the record, and specifically upon NAWC Statement No. 1 Remand, Exhibit HW-1, Schedule 7, I find that if the Company continues to move forward with its capital improvement program and its Commission-approved LTIP, the Company will continue to exceed the 5% DSIC cap. I am persuaded by NAWC that, even if OCA is correct that NAWC has over estimated its projected expenditures for these projects, the additional dollars of DSIC eligible investment will continue to cause the DSIC to exceed the 5% DSIC cap.

Regarding OCA's concern that the DSIC rate is subject to adjustment for prior period undercollections/overcollections and that an overcollection would have a downward effect of the DSIC rate in future quarters, I would note that OCA indicated that if the Company's LTIP expenditures are below budget, then its actual DSIC rates will be less than projected and closer to 5%. While I agree that this is a possibility, the Commission remanded this matter for a determination, in part, as to whether NAWC will continue to exceed its 5% DSIC cap. If, as I have noted, the Company continues to move forward with its capital improvement program, I believe that the Company will continue to exceed the 5% DSIC cap.

D. Whether the Company's Requested DSIC Cap Increase Should Be Approved.

1. Newtown Artesian's Position

The Commission, in its April 26, 2018 Order, remanded this matter seeking assurances that NAWC's DSIC exceeds 5% and will continue to exceed 5%. NAWC asserts that it has provided the sought for assurances and, thus, NAWC submits that the increase of the DSIC cap to 7.5% is justified. With the DSIC capped at 5% and a current DSIC calculation greater

than 5%, NAWC maintains that it is under recovering costs incurred in furtherance of its Commission approved LTIP. NAWC submits that this under recovery is neither just nor reasonable, and that the DSIC cap should be increased to 7.5%. (NAWC MB at 13; NAWC RB at 7).

In further support of the requested increase, NAWC notes that the Commission issued a press release on May 3, 2018 addressing “Drinking Water Week” in Pennsylvania, a copy of which is included as Schedule 8 to Exhibit HW-1 Remand. Citing Commissioner Sweet, the press release explains that "water is far too valuable a resource to be taken for granted - after all, it is the only utility commodity that we physically ingest. ... From prudent ratemaking, to daily oversight, to working with utilities to strengthen water system viability, the Commission is continually taking an active role to ensure safe and reliable service." Continuing to cite Commissioner Sweet, the press release comments specifically on the DSIC mechanism:

“The PUC’s Distribution System Improvement Charge (DSIC) mechanism has proven to be a valuable tool in accelerating the replacement of existing aging facilities. ... Needed replacement projects that would be put on hold until a future base rate proceeding can now be jumpstarted by using a DSIC surcharge on customers’ bills to accelerate the replacement.”

(NAWC MB at 13-14).

NAWC maintains that the recent press release and Commissioner Sweet’s comments are consistent with legislative intent and the benefits of a DSIC as historically recognized by the Commission. NAWC referenced Commissioner Fitzpatrick’s comments about the DSIC mechanism when the Commission approved Pennsylvania-American Water Company’s request for a 7.5% cap in 2007:

I support the well-reasoned Motion of Chairman Holland in this case. As the Motion recognizes, both Pennsylvania and the United States face a major problem with aging infrastructure. The General Assembly created a tool to combat this problem in the water industry when it authorized water companies to institute a distribution system improvement charge (DSIC). Based upon the record in this proceeding, it is clear that allowing Pennsylvania

American Water Company to raise its DSIC cap from 5% to 7.5% of billed revenues is consistent with the purpose of the General Assembly in establishing a DSIC.

The parties that opposed raising the DSIC cap in this proceeding used logic that is inconsistent with establishing a DSIC in the first place--they plainly do not favor allowing a utility to collect expenditures outside of base rate proceedings. While the policy that utility expenditures will only be recovered in setting base rates still applies in most situations, the General Assembly has created an exception for expenditures by water utilities for distribution system infrastructure. Our decision today is consistent with the legislative intent in establishing the DSIC mechanism.²²

NAWC notes that the exception now provides for a maximum DSIC of 7.5% for water utilities that are pursuing a Commission approved LTIP.²³ (NAWC MB at 14-15; NAWC RB at 8-9).

Subsequent to the PAWC proceeding, the General Assembly enacted Act 11 of 2012 including Section 1358(a)(2). Unlike the statutory circumstances in 2007, current statutory law expressly allows a DSIC cap of 7.5% for water utilities.²⁴ Moreover, the Commission has approved and allowed United Water Pennsylvania Inc. (“United”),²⁵ Aqua Pennsylvania, Inc. (“Aqua”)²⁶ and Pennsylvania-American Water Company (“PAWC”)²⁷ to increase their DSIC caps from 5.0% to 7.5%. NAWC maintains that there is no basis upon which these requests of other Pennsylvania water utilities to increase their DSIC cap, ultimately approved by the Commission, can continue to be distinguished from the request of NAWC to increase its DSIC cap. NAWC asserts that the evidence it has presented in this remand proceeding demonstrates that NAWC’s DSIC exceeds 5% and will continue to exceed 5%. (NAWC MB at 15; NAWC RB at 8).

²² *Petition of Pennsylvania-American Water Company*, Docket No. P-00062241 (Opinion and Order adopted July 11, 2007, and entered August 14, 2007, concurring statement of Commissioner Terrance J. Fitzpatrick).

²³ Section 1358(a)(2) of the Public Utility Code, 66 Pa. C.S. § 1358(a)(2).

²⁴ Section 1358(a)(2) of the Public Utility Code, 66 Pa. C.S. § 1358(a)(2).

²⁵ *Petition of United Water Pennsylvania Inc. for Approval of a Tariff Supplement to Revise its Maximum Distribution System Improvement Charge to 7.5% of Billed Revenues*, Docket No. P-2013-2389331 (Order entered December 19, 2013).

²⁶ *Pa. Pub. Util. Comm’n, et al. v. Aqua Pennsylvania, Inc.*, Docket No. R-2008-2079310 (Opinion and Order entered July 23, 2009).

²⁷ *Petition of Pennsylvania-American Water Company*, Docket No. P-00062241 (Opinion and Order adopted July 11, 2007, and entered August 14, 2007).

NAWC has a Commission approved LTIIIP with projected DSIC eligible capital expenditures of \$4,251,000 for 2017 through 2021, totaling approximately 41% of existing rate base. Compliance with the approved LTIIIP will be facilitated by increasing the DSIC cap to 7.5%. It will do this by allowing the Company to recover the fixed costs (depreciation and pre-tax return) of completed DSIC eligible LTIIIP projects until they, ultimately, are reflected in base rates in the Company's next base rate case. The evidence presented by NAWC in this remand proceeding demonstrates that NAWC's DSIC exceeds 5% and will continue to exceed 5% as NAWC moves forward with its Commission approved LTIIIP. (NAWC MB at 15-16; NAWC RB at 7-8).

The Company notes that Section 1301 of the Public Utility Code provides that all rates must be just and reasonable. Consistent with this statutory objective, the Company is entitled to the opportunity to earn a fair rate of return.²⁸ The Company asserts that under present circumstances it is being unreasonably denied the opportunity to recover the fixed costs (depreciation and pre-tax return) of completed DSIC eligible LTIIIP projects until they, ultimately, are reflected in base rates in the Company's next base rate case. (NAWC RB at 8).

NAWC asserts that the benefits to increasing the DSIC cap are not one-sided. As presented in the Commission approved LTIIIP, the Company has pipe in need of replacement in the near-term future. Customer benefits include a decline in the number of main breaks and service interruptions, increased fire protection and an improvement in water quality through replacement, lining, cleaning and tie-ins. Increasing the DSIC cap to 7.5% will jumpstart these needed replacement projects as the Commission recognized in its recent press release discussed above. (NAWC MB at 16).

In response to the OCA's contention that a further acceleration of infrastructure replacement is required to justify the proposed increase to the DSIC cap,²⁹ the Company submits that this contention is contrary to the April 26, 2018 Order. In remanding this matter to address a single limited issue, the Commission noted, citing its Order entered July 12, 2017, at Docket No.

²⁸ *Bluefield Water Works and Improvement Co. v. Public Service Comm'n of West Virginia*, 262 U.S. 679 (1923).

²⁹ OCA Main Brief on Remand at 11.

P-2017-2594725, that it has already determined that NAWC has “fulfilled sixth [sic] of the eight elements required in an LTIP filing that the replacement of aging infrastructure is or will be accelerated.”³⁰ The Commission is not looking for a further acceleration of infrastructure replacement to justify the increase to the DSIC cap. The Public Utility Code, in any event, does not require a further acceleration to justify the proposed DSIC cap increase. (NAWC RB at 9).

In response to OCA’s contention that the Company could file a base rate case to address regulatory lag, NAWC maintains that this argument ignores the fact that the Company will continue to under recover the costs of its Commission approved LTIP program while the base rate case moves along from preparation and filing through statutory suspension and final Commission order. The under recovery as a result of this regulatory lag is neither just nor reasonable, and the DSIC cap should instead be increased to 7.5% until the next base rate case. (NAWC RB at 6, 9).

In response to OCA’s contention that lengthening the rate case interval by “waiving” the DSIC cap is not consistent with the policy of the Commission or the intent of the statutory cap “waiver” provision, NAWC submits that this is not what the Commission directed the parties to address on remand. NAWC asserts that the Commission’s decision remanding this matter to address a limited single issue and a recent Commission press release emphasizing the benefits of the water DSIC suggest that the Commission is inclined to allow the proposed cap increase if NAWC’s DSIC exceeds 5% and will continue to exceed 5%. (NAWC RB at 4).

NAWC further argues that there is no Commission “policy” limiting the number of years between base rate proceedings. Moreover, NAWC argues that there is no statutory cap “waiver” provision associated with a water DSIC of 7.5%. The statutory “waiver” provision in Section 1358(a)(1) of the Public Utility Code applies to utilities other than water utilities. For water utilities the statutory cap enacted by the General Assembly in Section 1358(a)(2) is 7.5%. (NAWC RB at 5).

³⁰ April 26, 2018 Order at 35.

Increasing the DSIC cap to 7.5% will occur without impeding existing customer safeguards. The General Assembly has included legislated safeguards within the DSIC process to ensure that the DSIC is appropriately monitored and that ratepayers are adequately protected. Safeguards assure that NAWC's DSIC is reflecting only DSIC eligible projects and that NAWC is not over-earning. Ultimately, the DSIC represents only the dollar-for-dollar recovery of prudent expenses incurred for improving reliability to customers. Moreover, the DSIC eligible projects projected as part of the Commission approved LTIP will further the continued provision of reasonable and adequate service while jumpstarting needed replacement projects. NAWC maintains that increasing the DSIC cap to 7.5% is justified so that these LTIP expenditures may continue to be reflected in the DSIC calculation until the next base rate case. NAWC MB at 16.

With the DSIC capped at 5% and a current DSIC calculation greater than 5%, NAWC maintains that it is not recovering depreciation and pre-tax return that it would otherwise be able to recover if the DSIC cap were increased to 7.5%. Accordingly, NAWC submits that it is just, reasonable and appropriate that the Company be allowed to recover these costs, and that it has justified the proposed increase of the DSIC cap to 7.5%. (NAWC RB at 9-10).

2. OCA's Position

As stated in its recent Order, the Commission agreed "with the ALJ and the OCA that Section 1358(a)(2) does not establish that a 7.5% DSIC for all water utilities is presumptively reasonable."³¹ The Commission further stated that, "approval of a DSIC cap waiver is done on a case-by-case basis after consideration of all the evidence in the record."³² OCA notes that the ALJ elaborated on this point in the Recommended Decision, stating:

Although Act 11 does provide a mechanism for a water utility's DSIC cap to be increased from 5% to 7.5%, it is not an automatic entitlement and does come with limitations... It is significant that the Commission noted water utilities who were previously granted a waiver up to 7.5% had demonstrated that they had accelerated

³¹ April 26, 2018 Order at 32.

³² *Id.* at 33-34.

their rate of infrastructure replacement and that an increase over the then-current DSIC cap was ‘necessary and in the public interest.’³³

The OCA submits that the evidence adduced by NAWC here does not change these conclusions and does not satisfy the Company’s burden of showing that an increase to the DSIC cap is necessary and in the public interest. (OCA MB at 10).

Based on the totality of evidence in this record, OCA asserts that the Company’s position is materially different from other water utilities that have been granted a waiver of the 5% DSIC cap. Each of those utilities repeatedly and frequently exceeded the 5% cap. Contrary to those utilities, NAWC has exceeded its DSIC cap in only two quarters since the Company implemented a DSIC in 1998.³⁴ (OCA MB at 10).

OCA further asserts that with a 5% DSIC cap, NAWC has not filed a base rate case for 7 years and, historically, has averaged 5 years between base rate filings. In contrast, Aqua, PAWC and United Water were filing base rate cases approximately every two years to three years with a 5% cap.³⁵ OCA notes that, in the underlying proceeding, the ALJ recognized the distinction between NAWC’s situation and that of other water utilities in rejecting the Company’s argument that increasing the DSIC cap to 7.5% will lengthen its rate case filing frequency.³⁶ The ALJ stated that this argument lacked merit based on the infrequency of NAWC’s historical base rate filings, which at the time, averaged five years in between base rate cases.³⁷ The Commission agreed that lengthening the time between NAWC’s base rate case filings was not reason to waive the 5% DSIC cap.³⁸ (OCA MB at 11; OCA RB at 8).

³³ R.D. at 26-27; *see also Implementation of Act 11 of 2012*, M-2012-2293611, Final Implementation Order at 42 and n.5 (Aug. 2, 2012,) (*Final Implementation Order*).

³⁴ *See* OCA St. 1 at 3, 5; NAWC Exh. HW-1 Remand, Schs. 1, 2.

³⁵ *See Pa. Pub. Util. Comm’n v. Aqua Pennsylvania, Inc.*, R-2008-2079310, 2009 Pa. PUC LEXIS 263 at 27-28 (July 23, 2009) (*Aqua*); *Petition of Pennsylvania-American Water Co. for Approval to Implement a Tariff Supplement to Tariff Water – Pa. P.U.C. No. 4 Revising the DSIC*, P-00062241, 2007 Pa. PUC LEXIS 42 at 30-32 (July 11, 2007) (*PAWC 2007*); *Petition of United Water Pa., Inc. for Approval of a Tariff Supplement to Revise its Maximum DSIC To 7.5% of Billed Revenues*, P-2013-2389331, Order at 6 (Dec. 19, 2013) (*United Water*).

³⁶ R.D. at 29-30.

³⁷ *Id.*

³⁸ April 26, 2018 Order at 33.

In response to NAWC's reliance on Commissioner Sweet's recent remarks in a press release promoting the DSIC as a valuable tool to jumpstart needed replacement projects that would be put on hold until a future base rate proceeding, OCA posits that the Company is attempting to compare its position by stating that a DSIC cap increase will jumpstart needed replacement projects. While the Commission noted in its April 26, 2018 Order that infrastructure replacement is or will be accelerated in NAWC's LTIP filing,³⁹ NAWC has not shown that infrastructure replacement will be accelerated by increasing the DSIC cap. To the contrary, NAWC has stated that it will not further accelerate infrastructure replacement and it will comply with its approved LTIP regardless of whether the DSIC cap increase is approved.⁴⁰ OCA notes that the other water utilities provided evidence that the increase to the DSIC cap was necessary to accelerate infrastructure replacement.⁴¹ For this reason, OCA submits that NAWC's position is materially different from prior water utility proceedings where the Commission approved an increase to the DSIC cap. Therefore, approval of NAWC's proposal will not serve to jumpstart infrastructure replacement and is not necessary to ensure and maintain the level of infrastructure investment approved in the Company's LTIP. (OCA MB at 11; OCA RB at 8-9).

OCA maintains that NAWC already has other means to address regulatory lag in recovering its LTIP investment:

We agree with the OCA that the Company has other means to address the potential regulatory lag in the financing of the LTIP improvements. The OCA notes that NAWC has a Purchased Water Adjustment Clause through which it automatically recovers approximately one-third of its annual operating expenses without filing a base rate case. The OCA also suggests that the Company can utilize a fully forecasted future test year, which allows for prospective inclusion of distribution system improvement costs in rate base.⁴²

³⁹ *Id.* at 35.

⁴⁰ Tr. at 36; *see also* NAWC St. 1 at 3.

⁴¹ *See Aqua* (holding that an increase to the DSIC cap would allow Aqua to accelerate replacement of 1,500 miles of critical pipe); *PAWC 2007* at *6, 24 (approving an incremental increase to PAWC's DSIC cap based, *inter alia*, on PAWC's claim that the increase would support its efforts to accelerate replacement of its older small-diameter mains); *United Water* at 3 (determining that an increase of the DSIC cap "will enable UWPA to accelerate further its main replacement program").

⁴² April 26, 2018, Order at 33.

For example, utilizing the Fully Projected Future Test Year (FPFTY) in a base rate case filed in 2018 would allow the Company to collect expenditures for an additional year after the end of the future test year.⁴³ Doing so would allow NAWC to recover a larger portion of its projected LTIIP expenditures through base rates and lessen reliance on DSIC recovery. Based on the Company's DSIC rate history, it is possible that filing a base rate case and using a FPFTY could allow NAWC to recover the costs associated with its DSIC-eligible investment for years without reaching a 5% cap. (OCA MB at 12).

Moreover, and in response to NAWC's assertion that increasing the 7.5% cap will not impede existing customer safeguards, OCA argues that the Company's position is without merit since the Company anticipates that increasing the cap could prolong the already lengthy intervals between base rate cases from 7 years to 10 years.⁴⁴ This would impede the primary safeguard provided by the DSIC cap, which is to prevent utilities from evading base rate review for extended periods.⁴⁵ (OCA RB at 9).

OCA notes that, if simply exceeding the cap were sufficient justification for a waiver, the cap would not serve any purpose within the legislation. It would simply be a placeholder until the utility exceeds that level of spending. OCA maintains that this is inconsistent with the rules of statutory construction, which dictate that all provisions of a statute should be given effect.⁴⁶ The very fact that there is a statutory cap on the amount that can be recovered through the surcharge is an indication that the General Assembly intended the Commission to require additional evidence to establish the necessity of a waiver.⁴⁷ (OCA RB at 7).

OCA further argues that granting an increase solely due to exceeding the existing 5% cap would also be inconsistent with Commission precedent. In prior DSIC cases, the Commission has made clear that inclusion of projects in an LTIIP is not dispositive of whether

⁴³ 66 Pa. C.S. § 315(e).

⁴⁴ See NAWC M.B. Remand at 16; *see also* OCA St. 1RM, Sch. JDM-1.

⁴⁵ 66 Pa. C.S. § 1358(a)(1); *see also* *Petition of PAWC to Establish a DSIC*, P-00961031, 1996 Pa. PUC LEXIS 182 at *21 (Aug. 26, 1996); *PAWC 2007* at *32.

⁴⁶ 1 Pa. C.S. § 1921(a).

⁴⁷ 66 Pa. C.S. § 1358(a)(1).

the utility will be permitted to recover the costs of those projects through a DSIC.⁴⁸ Thus, all water utilities that make LTIP expenditures at levels that exceed the amount recoverable with a 5% DSIC cap are not automatically entitled to a higher DSIC cap.⁴⁹ In each case decided under Section 1358(a)(2), OCA notes that the Commission required additional evidence to show that waiver of the cap is necessary and in the public interest.⁵⁰ (OCA RB at 7).

In conclusion, if reaching the 5% DSIC cap is the only evidence required for waiver, the cap would function as a trigger, rather than a limitation. Instead, the Commission has recognized that a 7.5% DSIC for all water utilities is not presumptively reasonable.⁵¹ There must be sufficient evidence showing that waiver is necessary and in the public interest. The totality of evidence continues to weigh heavily against increasing NAWC's cap. The DSIC cap is the primary consumer safeguard to ensure that utilities cannot evade base rate review for extended periods.⁵² OCA submits that NAWC has not shown that a higher DSIC cap is necessary and in the public interest, and that consistent with the Commission's initial conclusion, the Company's DSIC should remain capped at 5%. OCA MB at 13.

3. Discussion and Conclusions

The Commission remanded this matter in order to determine whether NAWC has exceeded its current 5% DSIC cap and will continue to exceed it, and whether this justifies the requested increase to a 7.5% DSIC cap. The record demonstrates, and both parties agree, that NAWC's DSIC has exceeded its 5% DSIC cap for two consecutive quarters. The record further demonstrates that, if the Company continues to move forward with its capital improvement program, it is likely that the Company will continue to exceed the 5% DSIC cap. However, although the Company has presented evidence to answer both of these questions in the affirmative, the Company is still not automatically entitled to its requested DSIC cap increase to 7.5%. The Commission, in remanding this issue, indicated that the Company's introduction of

⁴⁸ See, e.g., *Petition of Columbia Gas of Pa., Inc. for Approval of its LTIP*, Docket No. P-2012-2338282, Order at 10-11, 27, (Mar. 14, 2013); *Petition of UGI Penn Natural Gas, Inc. for Approval of its LTIP*, Docket No. P-2013-2398835, Order at 24 (Sept. 11, 2014); *Petition of Peoples Natural Gas Co. LLC for Approval of its LTIP*, Docket No. P-2013-2344596, Order at 43 (May 23, 2013).

⁴⁹ April 16, 2018, Order at 32; R.D. at 26.

⁵⁰ *Aqua, PAWC 2007, United Water*.

⁵¹ April 26, 2018 Order at 33.

⁵² 66 Pa. C.S. § 1358(a)(1); see also *PAWC 1996* at *21.

relevant evidence was “subject to the examination of the OCA and the introduction of its own evidence.”⁵³

The Company has argued that, with its DSIC capped at 5% and a current DSIC calculation greater than the 5% cap, it is under recovering costs incurred in furtherance of its Commission-approved LTIIP, and that this under recovery is neither just nor reasonable and its DSIC cap should be increased to 7.5%. However, I agree with the OCA that if solely exceeding the cap constituted justification for a waiver of the DSIC cap, then the cap would not serve any purpose. Clearly, the Company must show that an increase to the DSIC cap is necessary and in the public interest.

The Company noted that the Commission, in its April 26, 2018, Order, stated “[w]e note that the Commission has already determined that NAWC fulfilled sixth [sic] of the eight elements required in an LTIIP filing that the replacement of aging infrastructure is or will be accelerated.”⁵⁴ Based on this, the Company asserts that the Commission is not requiring further acceleration of infrastructure replacement to justify the increase to the DSIC cap, nor does the Public Utility Code require further acceleration. Although I previously found that the Company had not presented any evidence to establish that it would accelerate its rate of infrastructure replacement, since the Commission specifically noted that it already determined that the replacement of aging infrastructure is or will be accelerated in the April 26, 2018 Order, I must conclude that the Commission is satisfied with NAWC’s rate of replacement as it relates to the DSIC cap increase request. Therefore, I will not address the OCA’s argument that other water utilities provided evidence that the increase to the DSIC cap was necessary to accelerate infrastructure replacement.

The Company also argued that the Commission has approved and allowed United Water Pennsylvania, Aqua Pennsylvania, Inc. and Pennsylvania-American Water Company to increase their DSIC caps from 5% to 7.5%, and that there is no basis upon which these requests of other Pennsylvania water utilities to increase their DSIC cap, ultimately approved by the

⁵³ April 26, 2018 Order at 35.

⁵⁴ *Id.*

Commission, can continue to be distinguished from NAWC's request to increase its DSIC cap. I must disagree with NAWC. Each of the utilities mentioned had not only regularly exceeded their DSIC cap and accelerated their infrastructure improvement, they had also filed regular base rate increase requests, on an average of every two to three years. In contrast, the Company has not filed a base rate case in seven years, the last occurring in 2011.⁵⁵ Moreover, the Company has acknowledged that it is seeking an increase to the DSIC cap so that it can begin to recover fixed costs through the DSIC while postponing a base rate proceeding.⁵⁶

The Company has argued against filing a base rate case, stating that the suggestion that it could file a base rate case ignores the fact that NAWC will continue to under recover the costs of its Commission approved LTIP throughout the duration of the base rate proceeding. Instead, the Company asserts that under recovery as a result of this regulatory lag is neither just nor reasonable, and that the DSIC cap should instead be increased to 7.5% until it files its next base rate case. Again, I must disagree with NAWC, mainly as the Commission addressed and disagreed with this argument in its April 26, 2018 Order:

We disagree with the Company's argument regarding the filing of a base rate case. NAWC last filed a rate case in 2011. We agree with the OCA that the Company has other means to address the potential regulatory lag in the financing of the LTIP improvements. The OCA notes that NAWC has a Purchased Water Adjustment Clause through which it automatically recovers approximately one-third of its annual operating expenses without filing a base rate case. The OCA also suggests that the Company can utilize a fully forecasted future test year, which allows for prospective inclusion of distribution system improvement costs in rate base.⁵⁷

I agree with the OCA that utilizing a FPFTY in a base rate case filed this year would allow NAWC to collect expenditures for an additional year after the end of the future test year, and that it would also allow the Company to recover a larger portion of its projected LTIP

⁵⁵ NAWC St. 1-R at 5.

⁵⁶ NAWC St. 1-R at 3-4; Tr. at 30.

⁵⁷ April 26, 2018 Order at 3.

expenditures through base rates and lessen reliance on DSIC recovery. Accordingly, I must conclude that the Company's concerns regarding regulatory lag are without merit.

Each of the aforementioned water companies whose request to increase the DSIC cap from 5% to 7.5% was granted by the Commission had demonstrated that an increase to their DSIC was necessary and in the public interest. Each of these companies consistently exceeded their 5% DSIC cap even when filing base rate cases on regular intervals. In contrast, NAWC is seeking to further delay a base rate filing by increasing its DSIC. As previously noted, NAWC's concerns regarding regulatory lag are unfounded, and filing a base rate increase request, which the Company has not done in seven years, is a viable alternative to the requested DSIC cap increase. While I do believe that NAWC's determination to improve its infrastructure is laudable, the Company has failed to present evidence to demonstrate that an increase to the DSIC cap is necessary and in the public interest. Accordingly, I shall recommend that NAWC's request for an increase to the DSIC cap from 5% to 7.5% be denied.

V. CONCLUSIONS OF LAW

1. The Commission has jurisdiction over the subject matter and the parties to this proceeding pursuant to 66 Pa.C.S. §§ 1350-1360.
2. In any proceeding upon the motion of the Commission, involving any proposed or existing rate of any public utility, or in any proceeding upon complaint involving any proposed increase in rates, the burden of proof to show that the rate involved is just and reasonable shall be upon the public utility. 66 Pa.C.S. § 315(a).
3. A party proposing an adjustment to a ratemaking claim bears the burden of presenting some evidence or analysis tending to demonstrate the reasonableness of the adjustment. *See, e.g., Pa. Pub. Util. Comm'n v. PECO Energy Co.*, Docket No. R-891364, *et al*, 1990 Pa. PUC LEXIS 155 (Order entered May 16, 1990); *Pa. Pub. Util. Comm'n v. Brezewood Telephone Co.*, Docket No. R-901666, 1991 Pa. PUC LEXIS 45 (Order entered January 31, 1991).

4. Every rate made, demanded, or received by any public utility, or by any two or more public utilities jointly, shall be just and reasonable, and in conformity with regulations or orders of the Commission. 66 Pa.C.S. § 1301.

5. Absent an express limitation on existing ratemaking authority, the Commission retains its full and existing ratemaking authority. 66 Pa.C.S. § 1358(c).

6. Section 1358(a)(2) provides that a distribution system improvement charge granted to a water utility . . . may not exceed 7.5% of the amount billed to customers. 66 Pa.C.S. § 1358(a)(2).

7. The burden of proving that an increase of the Company's DSIC cap from 5% to 7.5% is on Newtown Artesian Water Company. 66 Pa.C.S. § 315(a).

8. Newtown Artesian Water Company has failed to sustain its burden of proving that an increase of the DSIC cap from 5% to 7.5% is just and reasonable.

VI. ORDER

THEREFORE,

IT IS RECOMMENDED:

1. That Newtown Artesian Water Company's proposal, contained in Supplement No. 126 To WATER-PA. P.U.C. No. 9, to increase its DSIC cap from 5% to 7.5% of billed revenue be denied;

2. That the Complaint filed by the Office of Consumer Advocate at Docket No. C-2017-2626954 be sustained; and

3. That this proceeding be marked closed.

Date: June 12, 2018

_____/s/
Christopher P. Pell
Deputy Chief Administrative Law Judge