

STATE OF NEW YORK  
PUBLIC SERVICE COMMISSION

CASE 16-W-0259 - Proceeding on Motion of the Commission as to  
the Rates, Charges, Rules and Regulations of  
New York American Water Company, Inc. for Water  
Service.

ORDER ESTABLISHING RATES FOR WATER SERVICE

Issued and Effective: May 18, 2017

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STATE OF NEW YORK  
PUBLIC SERVICE COMMISSION

At a session of the Public Service  
Commission held in the City of  
Albany on May 18, 2017

COMMISSIONERS PRESENT:

Gregg C. Sayre, Interim Chairman  
Diane X. Burman

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BY THE COMMISSION:

INTRODUCTION

This order establishes a four-year rate plan for water service by New York American Water Service, Inc. (the Company or NYAW), for the period April 1, 2017 through March 31, 2021. The order adopts the terms of a Joint Proposal (or JP) executed by the Company and the New York State Department of Public Service Staff (Staff), with modifications. LI Clean Air Water & Soil Ltd. (CAWS)<sup>1</sup> and North Merrick Community Association (NMCA)<sup>2</sup> oppose the JP. Public Utility Law Project of New York, Inc. (PULP) neither supports nor opposes the JP.<sup>3</sup>

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<sup>1</sup> CAWS states that it is a not-for-profit organization formed in 2016 to protect and preserve Long Island's natural resources.

<sup>2</sup> NMCA states it is a not-for-profit civil association covering parts of Merrick in Long Island.

<sup>3</sup> The New York State Department of State, Division of Consumer Protection's Utility Intervention Unit (UIU) also is a party to, but has not participated in, this rate proceeding.

BACKGROUND

NYAW is a wholly-owned subsidiary of American Water Works Company, Inc. (AWW) that provides residential and non-residential metered and other water services as well as public and private fire protection services to approximately 124,000 customers in parts of Nassau, Putnam, Sullivan, Ulster, Washington and Westchester Counties. Due to various acquisitions of other water companies, NYAW currently operates under four tariffs covering the following water supply districts and service areas: Lynbrook, Merrick, Sea Cliff, Cambridge, Kingsvale, Dykeer, Waccabuc, Wild Oaks, Mill Neck Estates, Mt. Ebo, Spring Glen Lake, and Lucas Estates.

Company Acquisitions and Prior Rate Plans

NYAW, then operating as the Long Island Water Corporation (LIWC), last requested a base rate increase for its Lynbrook Water District in 2011.<sup>4</sup> The Commission thereafter adopted a three-year rate plan commencing April 1, 2012, pursuant to which LIWC received annual base rate increases of approximately \$3.0 million (6.0%), \$1.4 million (2.6%), and \$1.2 million (2.2%) in the first, second, and third rate years, respectively.<sup>5</sup> The rate plan included procedures to capture, for LIWC customers' benefit, synergy savings that would accrue if the Commission approved AWW's acquisition of Aqua New York, Inc. (Aqua NY), which was then the subject of a petition filed in Case 11-W-0472.

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<sup>4</sup> Case 11-W-0200, Long Island Water Corporation d/b/a Long Island American Water - Water Rates. Rate request filed April 29, 2011.

<sup>5</sup> Case 11-W-0200, Long Island Water Corporation d/b/a Long Island American Water - Water Rates, Order Determining Revenue Requirement and Rate Design (issued March 20, 2012).

In 2012, the Commission approved AWW's acquisition of Aqua NY and its wholly-owned subsidiaries, New York Water Service Corporation (NYWS) and Aquarian Water Company of Sea Cliff, Inc. (Sea Cliff),<sup>6</sup> and thereafter approved a petition to merge Aqua NY, NYWS, Sea Cliff and LIWC into a single corporation, NYAW.<sup>7</sup> In the Acquisition Order, the Commission approved a rate increase moratorium whereby AWW would be precluded from filing for rate increases for NYWS (which provided service to the Merrick water district), Sea Cliff, and Aqua NY's five upstate service districts (Cambridge, Kingsvale, Dykeer, Waccabuc and Wild Oaks) until March 31, 2015. The Commission also directed AWW to consider establishing, upon expiration of the rate increase moratorium, consolidated, uniform rates for the same rate classifications for customers of all its service territories. In addition, the terms and conditions of NYWS's rate plan remained in effect,<sup>8</sup> as modified by the acquisition order, and the acquired companies became or continued to be subject to a Revenue Adjustment Clause (RAC), Property Tax Reconciliation (PTR) provision, and an earnings sharing mechanism (ESM). The Cambridge district remained subject to its existing System Improvement Charge (SIC).

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<sup>6</sup> Case 11-W-0472, American Water Works Co., Inc., et al. - Acquisition of Aqua New York, Inc., Order Approving Stock Acquisition (issued April 20, 2012) (Acquisition Order).

<sup>7</sup> Case 12-W-0217, Aqua of New York of Sea Cliff, Inc. et al. - Merger, Order Approving Merger (issued August 17, 2012).

<sup>8</sup> NYWS was subject to a three-year rate plan ending February 5, 2013, under which it received annual base rate increases of approximately \$1.90 million (8.5%), \$.42 million (1.57%) and \$.53 million (1.95%), in the first, second, and third rate years, respectively. Case 09-W-0237, New York Water Service Corp. - Water Rates, Order Establishing Three-Year Rate Plan (issued January 29, 2010).

The last base rate increase for Sea Cliff was in 2003 when the Commission approved a rate plan for the three years ending September 30, 2004, 2005, and 2006, with base rate increases of \$142,354 (6.6%), \$138,586 (6%), and \$0, respectively.<sup>9</sup> The last base rate increase for Aqua NY's five upstate service districts was in 2008 when the Commission approved an increase of approximately \$173,600 (117%) for Cambridge, \$30,000 (32%) for Kingsvale, \$70,500 (99.7%) for Dykeer, \$26,000 (54.6%) for Waccabuc, and \$15,500 (11.1%) for Wild Oaks.<sup>10</sup> In doing so, the Commission began "the process of developing a consolidated rate structure" for those upstate service districts.<sup>11</sup>

In 2014, the Commission approved NYAW's acquisition of Mt. Ebo Water Works, Inc., the merger of that company into NYAW, and the replacement of all non-revenue terms of Mt. Ebo's tariff with those used in NYAW's Lynbrook Water District tariff.<sup>12</sup> The last base rate increase for Mt. Ebo was in 2012 when the Commission approved an increase of \$109,105 (50%) in its annual revenues.<sup>13</sup>

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<sup>9</sup> Case 02-W-1564, Sea Cliff Water Company - Water Rates, Order Establishing Rates and Authorizing Surcharge Mechanism, Name Change, and Other Tariff Revisions (issued October 22, 2003).

<sup>10</sup> Case 08-W-0107, Aqua New York, Inc. - Water Rates, Order Approving Modified Rate Increase (issued December 23, 2008).

<sup>11</sup> Id., p. 18.

<sup>12</sup> Case 14-W-0067, New York American Water Company, Inc. - Acquisition of Mt. Ebo Water Works, Inc., Order Approving Stock Sale and Acquisition (issued June 13, 2014).

<sup>13</sup> Case 12-W-0210, Mt. Ebo Waterworks - Water Rates, Order Approving Rates (issued November 27, 2012).

Thereafter, the Commission approved NYAW's acquisition of Lucas Estates Water Company, Inc.,<sup>14</sup> Spring Glen Lake Water Company LLC,<sup>15</sup> and the Mill Neck Estates Water System,<sup>16</sup> and the replacement of their tariffs with the terms used in NYAW's Lynbrook Water District tariff, including its rates. In 2015, the Commission adopted the terms of a Joint Proposal that, among other things, provided that NYAW's existing rate structure would be continued with certain modifications and that NYAW would not file for a rate increase with an effective date before March 31, 2017.<sup>17</sup>

#### Current Rate Filing

On April 29, 2016, NYAW filed tariff revisions designed to increase revenues by approximately \$8.5 million, or 8.3%, for the rate year ending March 31, 2018. NYAW also sought to consolidate its service territories into two service areas, with a proposed increase in revenues for Service Area 1 (SA1)<sup>18</sup>

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<sup>14</sup> Case 14-W-0148, New York American Water Company, Inc. - Acquisition of Lucas Estates Water Company, Inc., Order Approving Sale and Acquisition (issued July 25, 2014).

<sup>15</sup> Case 15-W-0375, New York American Water Company, Inc. - Acquisition of Spring Glen Lake Water Company LLC, Order Approving Sale and Acquisition (issued October 15, 2015).

<sup>16</sup> Case 15-W-0639, New York American Water Company, Inc. - Acquisition of Mill Neck Estates Water System, Order Approving Sale and Acquisition (issued February 25, 2016).

<sup>17</sup> Case 14-W-0489, American Water Company, Inc. Petition for an Update to its System Improvement Charge, Order Adopting Terms of Joint Proposal (issued August 14, 2015).

<sup>18</sup> SA1 includes the Lynbrook District, the five upstate water districts from the former Aqua NY (Cambridge, Dykeer, Kingsvale, Waccabuc and Wild Oaks), and the service areas formerly covered by the Mt. Ebo, Lucas Estates, Mill Neck Estates, and Spring Glen Lake water systems (Exh. 41, Joint Proposal, at 1 n.1). Ninety-eight percent of the SA1 customers are located in Lynbrook.



of \$5.8 million or 8.4% and for Service Area 2 (SA2)<sup>19</sup> of \$2.7 million or 8.1%. In addition, NYAW proposed that the general terms and conditions and tariffs currently in effect for its various service territories be consolidated in order to reduce administrative expenses, reduce customer confusion, and blend the rate effect of necessary capital investments across multiple service areas.

The Commission has suspended NYAW's rate filing and initiated this proceeding to examine the merits of the Company's proposals. The suspension period currently extends through June 23, 2017.<sup>20</sup>

Pursuant to the schedule established for the case,<sup>21</sup> Staff, CAWS and NMCA filed testimony and exhibits in response to NYAW's rate filings on September 2, 2016. Staff was the only party to offer alternative revenue requirement recommendations to NYAW's proposal. Staff recommended that the revenue requirements be increased by \$43,188 for SA1 and decreased by \$891,340 for SA2.<sup>22</sup>

On September 23, 2016, NYAW filed rebuttal testimony and exhibits.<sup>23</sup> NYAW revised its proposed revenue increase upward to approximately \$8.7 million, reflecting proposed

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<sup>19</sup> SA2 includes the Merrick and Sea Cliff Districts (Exh. 41, Joint Proposal, at 1 n.2). Ninety-one percent of the SA2 customers are located in Merrick.

<sup>20</sup> Order Approving Extension of Maximum Suspension Period of Major Rate Filing (issued March 9, 2017).

<sup>21</sup> Ruling on Schedule (issued June 14, 2016).

<sup>22</sup> Exh. 71, Luthringer Testimony, p. 5.

<sup>23</sup> CAWS also filed rebuttal testimony on September 23, 2016. On October 25, 2016, Administrative Law Judge Moreno granted NYAW's motion to exclude that testimony from the evidentiary record on the ground that it was unauthorized supplemental direct testimony.

increases for SA1 in the approximate amount of \$6.7 million and for SA2 in the approximate amount of \$2 million.<sup>24</sup>

NYAW filed a notice of impending settlement negotiations on September 26, 2016. Administrative Law Judge (Judge) Ashley Moreno advised us that the notice complied with our rules and regulations (16 NYCRR 3.9(2)). Based on the parties' continued efforts to reach a settlement, the evidentiary hearing, initially scheduled to commence on October 13, 2016, was postponed multiple times.<sup>25</sup> NYAW also consented to extensions of the suspension period in these proceedings through June 23, 2017, subject to a "make whole" provision.<sup>26</sup>

On January 9, 2017, NYAW filed a Joint Proposal executed by NYAW and Staff. Pursuant to the schedule adopted thereafter,<sup>27</sup> on February 8, 2016, NYAWS and Staff filed statements in support of the Joint Proposal, CAWS filed a statement in opposition to the Joint Proposal, and PULP filed a statement indicating that it neither supports nor opposes the Joint Proposal. On February 21, 2017, NYAW, Staff and CAWS filed reply statements.

An evidentiary hearing on the Joint Proposal was held in Albany on March 8, 2017, before Judges Costello and Moreno.<sup>28</sup> A total of 114 exhibits were admitted into the record. NYAW and

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<sup>24</sup> Exh. 40, FXS-8R, FXS-8.1R and FXS-8.2R.

<sup>25</sup> Ruling Postponing Hearing (issued October 6, 2016), Ruling Further Postponing Hearing (issued November 10, 2016), and Third Ruling Postponing Hearing (issued December 7, 2016).

<sup>26</sup> See NYAW Letters dated September 27, November 9 and December 5, 2016.

<sup>27</sup> Ruling on Schedule and Discovery Motion (issued January 24, 2017).

<sup>28</sup> Notice of Evidentiary Hearing (issued February 23, 2017).

Staff sponsored a panel at the hearing in support of the JP. CAWS and NMCA jointly cross-examined the witnesses. The panel also responded to questions from the ALJs regarding various provisions of the JP.

Pursuant to a schedule established for post-hearing briefing,<sup>29</sup> CAWS filed an initial post-hearing brief and NYAW filed a letter in lieu of an initial post-hearing brief on April 17, 2017. On April 24, 2017, NYAW and Staff each filed a post-hearing brief replying to CAWS's brief.

#### PUBLIC NOTICE AND COMMENTS

##### Public Notice

Pursuant to State Administrative Procedure Act (SAPA) §202(1), a Notice of Proposed Rulemaking was published in the State Register on July 13, 2016 [SAPA No. 16-W-0259SP1]. In addition, on June 16, 2016, the Commission issued a Notice of Public Statement Hearings on Proposed Water Rate Increase, which described the Company's rate filing and scheduled information sessions followed by public statement hearings in the afternoons and evenings on July 6, 2016 in Brewster, New York, and on July 13, 2016 in Oceanside, New York. The notice stated that NYAW representatives would provide a brief overview of the Company's rate proposal during the information session and provide a brief opportunity for questions and answers. The notice also stated that comments could be made by internet, mail or the Commission's toll-free Opinion Line. A copy of the notice was published in The Eagle and The Putnum County Courier on June 30, 2016; The Journal News on June 30 and July 5, 2016; the Sullivan County Democrat on July 1 and 5, 2016; The Daily Freeman on July 1 and 5, 2016; the Putnam County News and

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<sup>29</sup> Ruling on Post-Hearing Briefing (issued April 10, 2017).

Recorder on July 6, 2016; and the Nassau edition of Newsday on July 4 and 11, 2016.

On October 6, 2016, a similar notice was issued, which, among other things, explained that the parties had filed testimony with respect to the rate proposal and scheduled a public statement hearing on October 26, 2016 in Malverne, New York, during the afternoon, and in Wantagh, New York, during the evening. A copy of the notice was published in the Nassau, Suffolk and Queens editions of Newsday on October 12 and 19, 2016. The public statement hearings in Malverne and Wantagh were scheduled in response to requests by NYAW's customers on Long Island.

Public Statement Hearing Comments<sup>30</sup>

Pursuant to the notices discussed above, a total of six public hearings were held on NYAW's rate filing. No comments were made at the hearings in Brewster. Comments were made by ten individuals at the Oceanside hearings, 20 individuals at the Malverne hearing, and 31 individuals at the Wantagh hearing. Over 30 of those individuals spoke on their own behalf. Others commented on behalf of PULP, CAWS, NMCA, the Oceanside Civic Association, the Oceanside Fire Department, the Baldwin Civic Association, the Wantagh Seaford Homeowners Association, the Forest City Community Association, and several private businesses. Elected officials from the New York State Senate and Assembly, the Nassau County Legislature, and the Village of Malverne also commented at the hearings.

Commenters generally opposed the requested rate increases in light of the economy and the high cost of living on

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<sup>30</sup> This section summarizes the comments made at the public statement hearings. Transcripts of the public statement hearings appear in their entirety on the Department's website.

Long Island and because they believed they already paid too much for water, especially when compared to nearby residents who received water from public water authorities or municipal water districts. They stated that they paid three times more than customers of public water authorities, assertedly because NYAW was allowed to recover high profits and 100% of its property taxes from customers. Many maintained that such rate recovery for NYAW was unconstitutional in that it treated customers of public and private water companies unequally. Several commenters stated that they also would prefer to be served by a public water authority. Some commenters stated that the cost of service for fire hydrants also was too high and that such service cost approximately ten times more than that charged by nearby public water authorities. A few statements indicated that the requested increase in rates was too high when viewed in the context of the State's two percent property tax cap.

Various speakers complained about the quality of their water, stating that it was brown or contained sediment, which they attributed to iron in the water or rust from NYAW's pipes. Some stated they could not use NYAW's water for drinking, bathing, washing clothes or washing dishes, and that they had to either filter their water or use bottled water instead. Other commenters complained about low water pressure, various water main breaks, and poor customer service. A few speakers raised concerns about the contamination of water supplies by groundwater plumes containing industrial solvents from a superfund site in Bethpage, New York. They questioned whether they were being charged in rates for related clean-up costs, and suggested that NYAW aggressively seek to recover such costs from the parties responsible for the contamination.

A few speakers stated their view that NYAW was seeking an increase in rates for projects that had already been funded

in prior rate cases. Some of them also asserted that NYAW should have made infrastructure improvements with the money it used for construction of an office building in Merrick, which they maintained was not needed and should not be paid for in rates. Some commenters stated that they should not have to pay research and development costs for NYAW's geothermal pilot project on Long Island because they would not benefit from the project. A few of them also complained about the salaries paid to NYAW executives and about being solicited by another subsidiary of AWW to buy insurance for their privately-owned water pipes.

State Senator Todd Kaminsky stated concerns with the cost of living on Long Island, especially for the elderly, and maintained that no increase was justified given the common occurrence of brown water. Assembly Member Brian Curran expressed similar concerns about the increasing cost of living on Long Island and stated that NYAW has not improved its water quality over the past several years. Assembly Member Michaelle Solages stated that NYAW should look to save money and follow the two percent property tax cap rather than seeking a large increase in rates. Nassau County Legislator Steven D. Rhoads stated that NYAW should not get an increase in rates because it merely acts as a delivery system for the water that citizens already own, the requested increase would only widen the disparity between the costs paid by NYAW customers and customers of public water districts, and NYAW should first be required to seek alternative sources of funding and reduce operating costs through efficiencies. Nassau County Legislator Siela Bynoe indicated that many customers could not use NYAW's water and had to use bottled water and that NYAW should not get an increase in rates until it made further infrastructure improvements and released its budget to show the improvements it planned to make.

Village of Malverne Mayor Patricia McDonald stated that NYAW had an aging water distribution system that has resulted in discolored water and that NYAW should find alternative sources to fund necessary upgrades to its system.

PULP and a few other speakers raised concerns with the impact that increased rates would have on customers with low or fixed incomes. They were in favor of implementing a low-income rate reduction program to address the issue, but believed that the administrative costs for the program that NYAW proposed were too high. PULP indicated that it would work with NYAW and Staff to find a better solution.

PULP and several other speakers also raised concerns about the potential for lead in the water. PULP suggested that the replacement of lead service lines be addressed on a statewide basis and that NYAW advise non-English speaking customers in their native language about the existence of lead service pipes and the health risks posed by lead. Other commenters stated that lead had been found in the water of certain schools and that NYAW had no plans to address whether residential customers also had a lead problem.

A few commenters supported the infrastructure improvements NYAW proposed and stated that the capital projects proposed by NYAW were needed to improve water quality and replace an aging infrastructure. One commenter noted that cost savings ultimately would be realized through the appropriate funding of capital projects.

Written Comments and Opinion Line Comments

In addition to the notices discussed above, the Commission issued a Notice Seeking Public Comment on the Joint Proposal on February 3, 2017, requesting comments by internet, mail or telephone by March 6, 2017. A copy of the notice was published in the Daily Freeman and the Nassau, Suffolk and

Queens editions of Newsday on February 12 and 16, 2017; The Eagle on February 9 and 16, 2017; the Sullivan County Democrat on February 14 and 17, 2017; and the Putnam County Courier on February 14 and 21, 2017. Six telephone comments were received on the Commission's opinion line and 1,379 written comments were filed with the Commission, over 500 of which were made after the Joint Proposal was filed.<sup>31</sup> The vast majority of the written and opinion line comments opposed NYAW's proposed rate increases for the same reasons offered in the public statement hearings.

A few individuals also stated that they did not understand how the cost of their water could be so high since it is a basic human necessity produced for free by nature and provided to others by nearby public water authorities or municipal water districts at a significantly lower cost and better quality. Various individuals questioned whether NYAW was making excessive profits because, they said, NYAW charged approximately four times more than nearby municipal water districts. Several individuals said their rates already were the highest in New York or the nation, they could not afford yet another increase, and they wanted the option to choose between competing water companies. Some also stated that their water was "clouded" at times or had an unpleasant smell or taste. A few individuals stated that various surcharges included on their

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<sup>31</sup> By letter dated March 6, 2017, Nassau County Legislator Steven D. Rhoads expressed concern regarding many of the terms of the Joint Proposal, including the proposed rate increases and Earnings Sharing Mechanism under which NYAW would retain 100% of earnings attributable to an average actual return on equity up to and including 9.75%. Legislator Rhoads requested the Commission to extend the public comment period and ultimately to reject the Joint Proposal. In response, the Commission issued a notice reopening the public comment period on the Joint Proposal through April 7, 2017. Further public comments received pursuant to that notice are discussed in the text.



water bills added to the already high cost of water. Some also commented that NYAW should not be allowed to recover any money when it successfully challenges its property tax assessments. Finally, several individuals stated that the Commission has merely acted as a "rubber stamp" to the Company's rate increase requests.

ANALYSIS OF JOINT PROPOSAL

The Public Service Law (PSL) establishes the Commission's broad supervisory jurisdiction over the furnishing or distribution of water for domestic, commercial or public uses and to those persons and entities operating the systems in New York State.<sup>32</sup> The Commission is charged with their regulation to ensure that the services provided to customers and the public will be safe and adequate and that all charges made for those services are just and reasonable.<sup>33</sup> Setting just and reasonable rates requires a balancing of the customers' interests with those of the utility's investors.<sup>34</sup> We may consider such factors and assign the weight to those factors as is deemed appropriate in setting utility rates, and our decision will not be set aside unless it is made without a rational basis or reasonable support in the record.<sup>35</sup>

In evaluating the terms of a joint proposal submitted for our consideration, we must determine if the joint proposal, considered as a whole, produces a result that is in the public interest. Our Settlement Guidelines set forth factors to be

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<sup>32</sup> PSL §§ 2(26), (27), 4(1), 5(1)(f) and 89-c(1).

<sup>33</sup> PSL §89-b(1).

<sup>34</sup> Abrams v Public Serv. Commn., 67 NY2d 205, 212 (1986).

<sup>35</sup> Id.

used in conducting that analysis.<sup>36</sup> They include consideration of whether the terms of the joint proposal are consistent with the environmental, social and economic policies of the Commission and the State; produce results within the range of outcomes that might result if the issues in the case were fully litigated; appropriately balance the interests of the utility's ratepayers, its investors and the long-term viability of the utility; and provide a rational basis for our ultimate decision. Consideration is also given to whether the record is complete and the extent to which the settlement is contested.

Here, the parties were provided a fair and adequate opportunity to conduct discovery and submit testimony and exhibits in response to NYAW's testimony and exhibits. In addition to Staff, two parties filed testimony and exhibits in response to the Company's filings. Consistent with our rules of procedure,<sup>37</sup> the parties also were notified about planned settlement negotiations and given the opportunity to fully participate in those negotiations.

After the filing of the Joint Proposal, entered into by NYAW and Staff, the parties were permitted to submit initial and reply statements in support of or opposition to the JP. A total of 114 exhibits were admitted into the record at the evidentiary hearing, consisting of the parties' pre-filed testimony and exhibits, Joint Proposal and Appendices, parties' responses to written questions from the Administrative Law Judge, and the Company's responses to certain discovery requests. The 388 page transcript of the evidentiary hearing includes cross examination by CAWS and NMCA and responses by

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<sup>36</sup> Cases 90-M-0255, et al., Procedures for Settlements and Stipulation Agreements, Opinion 92-2 (issued March 24, 1992) (Settlement Guidelines).

<sup>37</sup> 16 NYCRR 3.9.

NYAW and Staff to questions by the ALJs. The parties also filed post-hearing briefs to further address issues raised at the evidentiary hearing. We find that the record compiled in this case is complete and provides an adequate basis for our decision.

The record demonstrates that the parties have conducted a thorough examination and analysis of NYAW's historic and proposed capital and operating expenditure levels and that the provisions of the JP address the legitimate concerns and interests of the parties, the Company and the Company's customers. The record also establishes the broad range of outcomes that could have been pursued in litigation and that the terms of the JP fall well within the range of potential litigated outcomes. The Joint Proposal is the product of negotiation and consensus between NYAW and Staff, and we acknowledge the difficult work and compromise necessarily involved in the process.

In addition, the terms of the Joint Proposal are consistent with current State policies. The JP includes an inclining block rate structure designed to foster water conservation, the first lead pipe removal pilot program for a regulated water utility in New York, and a water main replacement program that will reduce non-revenue water. At the same time, the JP includes several provisions to protect ratepayers from circumstances that otherwise would impose an unfair burden. Ratepayers are protected by an earnings sharing mechanism, downward-only Utility Plant in Service (UPIS) and main replacement reconciliation mechanisms, SIC provisions, and the Revenue, Production Costs and Property Tax Reconciliation (RPCPTR) mechanism.

Ratepayers also benefit by the levelization of the rate increases over the term of the rate plan and the

efficiencies created by consolidation of NYAW's water districts into two service areas. As discussed in the next section, the four-year term of the rate plan benefits both ratepayers and the Company. We find that the rate plan that we are adopting strikes an appropriate balance between the interest of ratepayers and the long-term viability of the Company.

We generally summarize and discuss below several provisions of the Joint Proposal. The discussion of these provisions is not an exhaustive discourse on each issue. Nevertheless, we have considered all of the terms set forth in the Joint Proposal, the evidentiary record, and the parties' arguments in support of or opposition to our adoption of the provisions of the JP.

#### Rate Plan Term

Section III.A of the Joint Proposal provides for a four-year rate plan that would begin on April 1, 2017, and continue through March 31, 2021. Rate Year 1 consists of the twelve-month period ending on March 31, 2018. Rate Years 2 through 4 consist of the twelve-month periods ending March 31, 2019, 2020 and 2021, respectively. The Company asserts that the multi-year plan is in the public interest because it provides customers and the Company with rate certainty and will allow the Company to focus on operating its water system rather than expending substantial resources to prepare and litigate annual rate filings.<sup>38</sup> Noting its general policy position that rate plans should be for no more than a one-year period, PULP expresses concern with the term of the rate plan based upon its view that, although multi-year rate plans arrived by settlement "theoretically" can provide better results for ratepayers than single-year rate plans arrived through litigation, "settlement

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<sup>38</sup> NYAW Statement in Support, p. 5; NYAW Reply Statement, p. 9.

outcomes providing better public benefits than litigated outcomes are far less common than New York's preference for rate case settlements would tend to imply."<sup>39</sup>

PULP offers no evidentiary support for the proposition that customers actually benefit more from annually litigated rate filings than from multi-year rate plans resulting from settlement, and we agree with the Company that the multi-year rate plan provides various benefits to customers and the Company that are not otherwise available. For example, the Company, and in turn ratepayers, will avoid incurring costs for rate filings for at least the next three years. Long-term rate certainty also assists NYAW's customers in budgeting the funds needed to cover their water bills. Moreover, multi-year rate plans strengthen incentives for efficiency gains, which benefit ratepayers in the long-term, and as discussed below, the multi-year rate plan provides for the levelization of rates, significantly mitigating the economic impact of the rate increase on customers in Rate Year 1. Finally, a long-term plan allows utility management to focus on effectively running their business, making capital investments and developing programs with the best overall long-term benefits rather than focusing on annual rate case filings.

#### Revenue Increases

Section III.B of the Joint Proposal sets forth NYAW's annual revenue requirements for each of the four rate years. When compared to amounts the Company would have been entitled to recover through base rates and surcharges under current rate plans, the JP provides NYAW with an incremental revenue increase in Rate Year 1 of approximately \$3.6 million or 3.5%, divided into an increase of approximately \$3.26 million or 4.8% for SA1

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<sup>39</sup> PULP Statement on the Joint Proposal, p. 3 (footnote omitted).

and \$0.33 million or 1% for SA2. The incremental revenue increases proposed over the course of the rate plan are set forth in the chart below.

<b>Unlevelized Incremental Revenue Increases (\$ millions)</b>				
<b>Rate Year</b>	<b>SA1 Revenue Increase</b>	<b>SA1 Percent Increase</b>	<b>SA2 Revenue Increase</b>	<b>SA2 Percent Increase</b>
<b>1</b>	\$3.26	4.82%	\$0.33	0.98%
<b>2</b>	\$3.10	4.38%	\$1.82	5.31%
<b>3</b>	\$2.71	3.68%	\$2.02	5.62%
<b>4</b>	\$4.34	5.69%	\$3.63	9.58%

Under existing SIC provisions, NYAW was already entitled to recover approximately \$3.0 million for SA1 and \$0.16 million for SA2, which otherwise would be collected from customers through a surcharge.<sup>40</sup> Also as a surcharge under current rate plans, for the rate year ending March 31, 2018, the Company would be allowed to collect approximately \$5.16 million for SA1 and \$0.22 million for SA2 and through Revenue Adjustment Clause (RAC) provisions and approximately \$8.65 million for SA1 and \$3.63 million for SA2 under Property Tax Reconciliation (PTR) provisions.<sup>41</sup> Including those amounts, which are revenue neutral because NYAW could collect them under existing rate plans, the JP recommends total revenue increases for Rate Year 1 of approximately \$20.10 million or 39.55% for SA1 and \$4.34 million or 14.43% for SA2.<sup>42</sup> Taking these previously approved amounts into consideration the JP recommends the following total unlevelized annual base revenue increases for NYAW, by service area:

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<sup>40</sup> Exh. 41, Joint Proposal, Appendix A-1.1, p. 1 and Appendix A-2.1, p. 1.

<sup>41</sup> Id.

<sup>42</sup> Id.

<b>Unlevelized Annual Base Revenue Increases (\$ millions)</b>				
<b>Rate Year</b>	<b>SA1 Revenue Increase</b>	<b>SA1 Percent Increase</b>	<b>SA2 Revenue Increase</b>	<b>SA2 Percent Increase</b>
<b>1</b>	\$20.10	39.55%	\$4.34	14.43%
<b>2</b>	\$3.10	4.38%	\$1.82	5.31%
<b>3</b>	\$2.71	3.68%	\$2.02	5.62%
<b>4</b>	\$4.34	5.69%	\$3.63	9.58%

To mitigate the impact of the Rate Year 1 revenue increases, the Joint Proposal recommends levelization of the increases, as shown below.

<b>Levelized Base Revenue Increases (\$ millions)</b>				
<b>Rate Year</b>	<b>SA1 Levelized Revenue Increase</b>	<b>SA1 Percent Increase</b>	<b>SA2 Levelized Revenue Increase</b>	<b>SA2 Percent Increase</b>
<b>1</b>	\$10.14	19.94%	\$3.07	10.20%
<b>2</b>	\$10.14	16.67%	\$3.07	9.29%
<b>3</b>	\$10.14	14.33%	\$3.07	8.53%
<b>4</b>	\$10.14	12.56%	\$3.07	7.88%

The proposed revenue increases are driven in substantial part by significant increases in property taxes, declining sales, and increases to rate base, largely due to increases in net plant and depreciation.<sup>43</sup> In general, the increases in net plant are needed to improve water quality and system reliability, including the expansion of the Company's water main replacement program to address an aging distribution system, tank and well replacements or improvements, replacement of pH adjustment systems, and various system upgrades to improve the small water systems recently acquired by the Company. The increased revenue requirements resulting from those factors are partially offset by a productivity adjustment, refunds to

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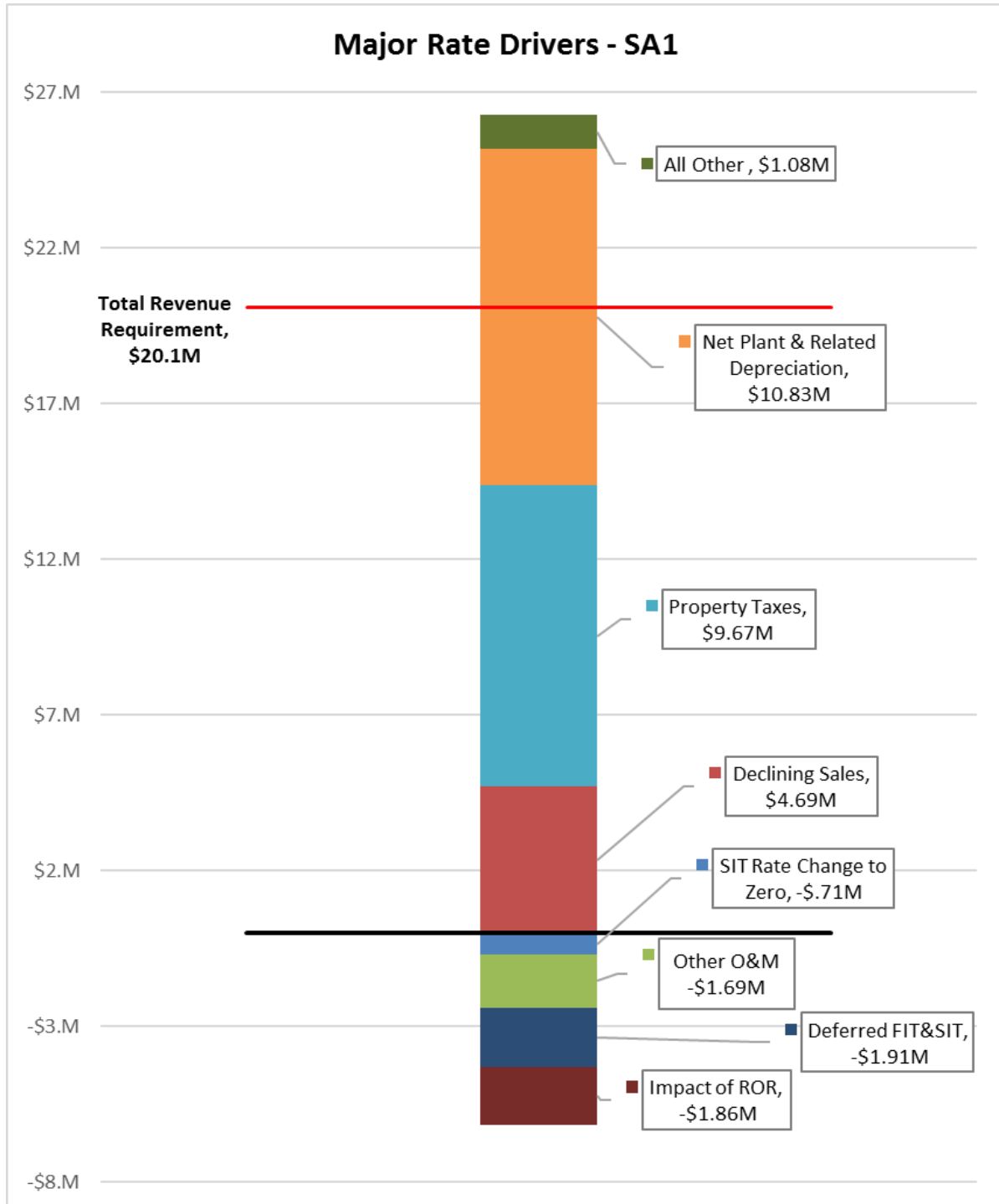
<sup>43</sup> Exh. 4, Bruce Direct Testimony, pp. 9, 20; Exh. 41, Joint Proposal, Appendix A, Schedule A-1.1 - A-1.4, p. 5 and Schedule A-2.1 - A-2.4, p. 5, and Appendix D; Exh. 42, Response to ALJ Question 4; Tr. 282-283.

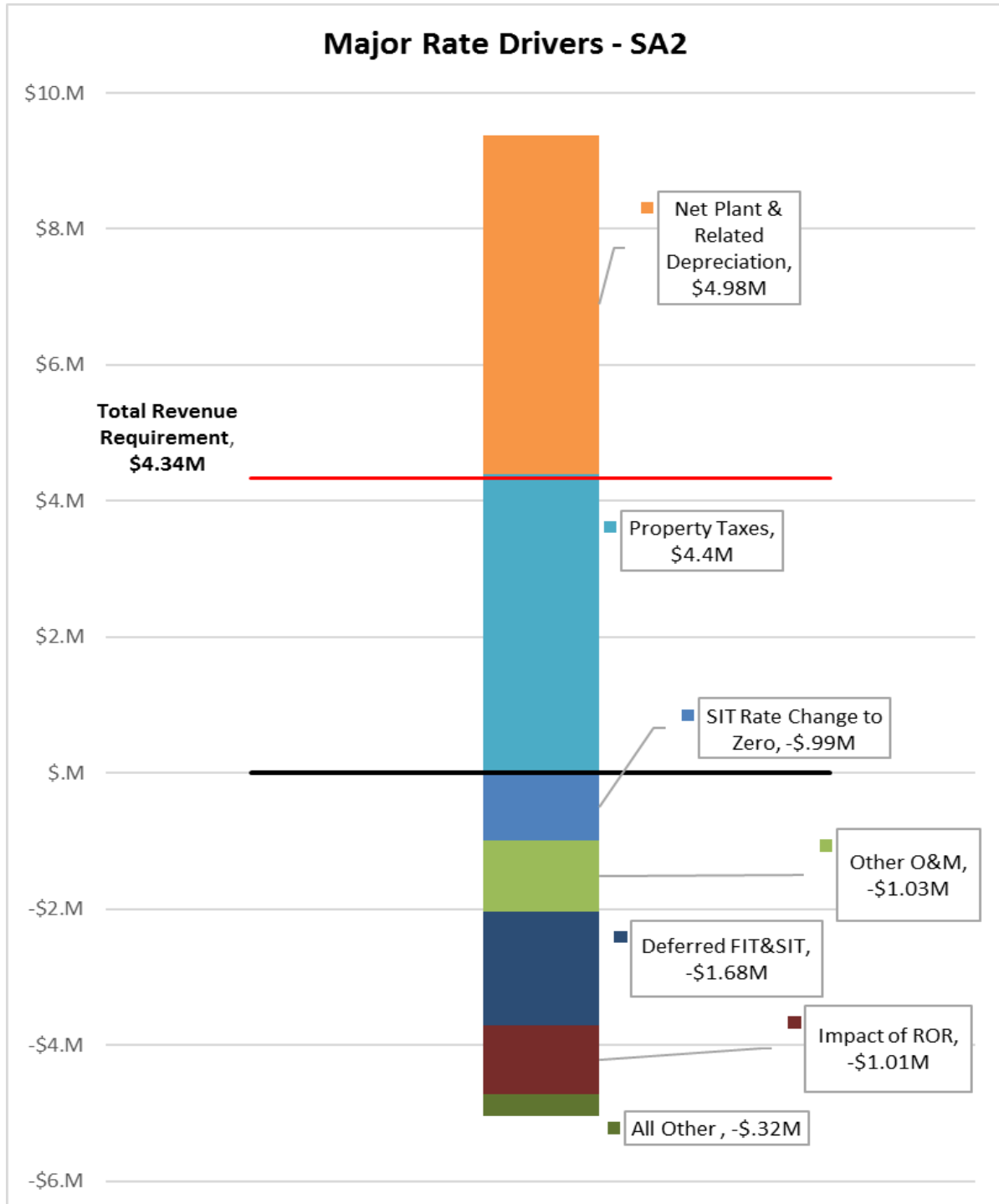
ratepayers resulting from NYAW's designation as a Qualified New York Manufacturer (QNYM), and reductions to operations and maintenance (O&M) expenses, the cost of capital, and State income tax liability.<sup>44</sup> The major rate drivers are summarized by service area in the charts below.

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<sup>44</sup> As explained further in the section addressing the QNYM credit, the revenue requirement impact resulting from recent legislation amending certain provisions of the tax law will be addressed in a separate proceeding under Case 17-W-0232.







In pre-filed testimony, NYAW treated its revenue requirement request as incremental to any amounts previously authorized for recovery under current rate plans through base rates, SIC surcharges, and surcharges allowed under existing RAC and PTR provisions. The Company originally forecasted that it would be entitled under current rate plans to collect as surcharges, for the rate year ending March 31, 2018, RAC deferrals in the approximate amount of \$5.4 million for SA1 and \$111,000 for SA2, and PTR deferrals in the approximate amount of \$8.74 million for SA1 and \$3.68 million for SA2.<sup>45</sup> NYAW's request of a total incremental revenue requirement increase of approximately \$8.5 million (8.3%), representing an incremental increase of approximately \$5.8 million (8.4%) for SA1 and \$2.7 million (8.12%) for SA2, thus excluded those forecasted RAC and PTR surcharges, the accrued SIC surcharge amounts discussed earlier, and the amounts previously authorized for recovery through base rates under current rate plans.<sup>46</sup>

After Staff proposed various adjustments to NYAW's requests, Staff initially recommended an overall revenue requirement increase for SA1 of approximately \$43,000 and an overall revenue requirement decrease for SA2 of approximately \$891,000.<sup>47</sup> In its Statement in Support of the Joint Proposal, Staff now notes that, with certain corrections and updates to its direct case, its one-year litigation position would be to recommend revenue requirement increases in the approximate amount of \$2.59 million representing \$1.73 million for SA1 and \$864,000 for SA2.<sup>48</sup>

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<sup>45</sup> Exh. 22, FXS-9.1 and 9.2.

<sup>46</sup> Exh. 22, FXS-9, FXS-9.1 and FXS-9.2.

<sup>47</sup> Exh. 72, GRL-2, Schedule A, p. 8, and Schedule I, p. 8.

<sup>48</sup> Staff Statement in Support, p. 8.

In rebuttal, NYAW revised the amounts it asserted it would have been entitled to recover under current rate plans, changing its total incremental revenue requirement increase to approximately \$8.7 million, representing an increase of approximately \$6.7 million for SA1 and \$2 million for SA2.<sup>49</sup> In doing so, NYAW modified the forecasted amounts that it would be entitled to collect as surcharges under its current rate plans for RAC deferrals to approximately \$5 million for SA1 and \$735,000 for SA2, and for PTR deferrals to approximately \$8.65 million for SA1 and \$3.63 million for SA2.<sup>50</sup>

The JP includes those forecasted PTR deferral amounts and modified forecasted RAC deferral amounts of approximately \$5.15 million and for SA1 and \$0.22 million for SA2. Therefore, as stated above and as noted by both the Company and Staff, when compared to the amounts NYAW would have been entitled to recover through base rates and surcharges under rate plans, the JP provides NYAW with a total incremental revenue requirement increase in Rate Year 1 of approximately \$3.6 million or 3.5%. That number represents the portion of base revenue increases that do not relate to the revenue neutral shift of SIC surcharges into base rates or amounts previously authorized for recovery under current rate plans.

The Company notes that the proposed incremental increases are significantly lower than it sought originally but higher than the total amount recommended by Staff for both service areas combined. Stating that the JP adopts many of the adjustments proposed by Staff in testimony, the Company maintains that the proposed revenue requirement increases reflect a reasonable compromise that provides customers with a

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<sup>49</sup> Exh. 39, FXS-1R.

<sup>50</sup> Exh. 39, FXS-2.1R and FXS-2.2R.

significant value and the Company with the funds necessary to allow it to continue to provide safe, adequate and reliable service.<sup>51</sup> While Staff acknowledges that the base rate increases recommended for NYAW are substantial, it agrees with the Company that rates should be increased to allow the Company to continue to appropriately serve its customers.<sup>52</sup>

CAWS, NMCA and others through written and public comments oppose the proposed rate increases. Their main assertions in this regard are that (1) the Company does not provide the quality of water or service that warrants an increase; (2) rates already are too high, especially when compared to rates of nearby municipal water systems; (3) allowing the Company to recover property taxes through rates is unconstitutional because nearby municipal water systems do not recover property taxes from their customers; and (4) the Company's proposed property tax expenses do not reflect reductions to property taxes resulting from successful property tax challenges.

As discussed later in this order, property taxes are a typical cost of providing utility service. Moreover, the JP includes a number of projects to address water quality and pressure concerns, including investments in water treatment and delivery systems and the replacement of lead service lines and aging water mains. The JP also addresses customer service concerns by including a customer service performance incentive mechanism, which subjects NYAW to potential negative revenue adjustments for poor customer service. We find that the proposed annual increases are needed for the Company to maintain safe and reliable service and earn a reasonable return on its

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<sup>51</sup> NYAW Statement in Support, pp. 7-8.

<sup>52</sup> Staff Statement in Support, p. 7.

investments. We also find the JP's recommended levelization of the annual increases will moderate the resulting customer rate increases to the maximum extent practicable.

Operations and Maintenance Costs

The JP would provide the following amounts for O&M expenses:

<b>O&amp;M Expenses (\$ millions)</b>		
<b>Rate Year</b>	<b>SA1</b>	<b>SA2</b>
<b>1</b>	\$21.27	\$10.83
<b>2</b>	\$21.56	\$10.93
<b>3</b>	\$21.79	\$11.07
<b>4</b>	\$23.78	\$13.09

For the rate year ending March 31, 2018, NYAW had proposed O&M expenses of approximately \$22.62 million for SA1 and \$12 million for SA2.<sup>53</sup> According to the Company, the total of those projected O&M expenses were "approximately \$1.9 million less than the last authorized levels for all districts combined."<sup>54</sup> NYAW also explained the steps it has taken to manage O&M expenses, including volume purchasing; reducing its fleet of vehicles; as well as various energy, water and labor efficiency measures.<sup>55</sup> After making certain adjustments to NYAW's proposed amounts, Staff recommended O&M expenses of approximately \$21.33 million for SA1 and \$10.67 million for SA2.<sup>56</sup> In rebuttal, NYAW reduced its requested O&M expenses to

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<sup>53</sup> Exh. 22, FSX-8.1, p. 2 and FSX-8.2, p. 2.

<sup>54</sup> Exh. 4, Bruce Direct Testimony, p. 11.

<sup>55</sup> Exh. 4, Bruce Direct Testimony, pp. 12-17 and Exh. 8, Kern Direct Testimony, pp. 5-8.

<sup>56</sup> Exh. 72, GRL-2, Schedule A, p. 2 and GRL-2, Schedule A, p. 2.

approximately \$21.99 million for SA1 and \$10.94 million for SA2.<sup>57</sup>

The O&M expenses provided for in the JP for Rate Year 1 are less than the amounts proposed in testimony by NYAW and Staff for SA1 and within the range of the amounts NYAW and Staff proposed for SA2. Moreover, as compared to the O&M expenses approved under the Company's existing rate plans, the O&M expenses proposed in the JP reflect a decrease of approximately \$1.69 million for SA1 and \$1.03 million for SA2. The O&M expenses included in the Joint Proposal are unopposed, more favorable than or within the range of potential litigated outcomes, appear reasonable, and will mitigate the proposed revenue increases in Rate Year 1. We therefore adopt the proposed O&M expenses.

#### Productivity Adjustment

Under the Joint Proposal, the forecast budget for labor, pensions, other post-employment benefits (OPEBs) and payroll tax on which rates are set is reduced by a two percent productivity adjustment in all four rate years.

Initially, NYAW did not include a productivity adjustment in its revenue requirement. Staff recommended a two percent productivity adjustment, consisting of the "standard 1% productivity adjustment... imputed to reflect gains from unidentified sources" and an additional one percent adjustment to reflect savings and efficiencies expected from the consolidation of NYAW's various water districts and other programs and initiatives NYAW proposed.<sup>58</sup> Applying the two percent adjustment against each district's total rate year labor, employee benefits, pensions, OPEBS and payroll tax

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<sup>57</sup> Exh. 40, FSX-3.1R and FSX-3.2R.

<sup>58</sup> Exh. 67, Keymel Testimony, pp. 6-7.

expenses, Staff recommended a downward adjustment to O&M expenses for SA1 in the amount of \$183,161 and for SA2 in the amount of \$76,863.<sup>59</sup> In rebuttal, NYAW maintained that a productivity adjustment was not warranted, because not all potential efficiencies from new programs would “necessarily equate to a reduction in costs.”<sup>60</sup> Further, NYAW asserted that, rather than being subject to a productivity adjustment, it should be given an incentive to encourage it to continue to acquire and manage “small and troubled water systems.”<sup>61</sup>

NYAW now states in support of the JP that the proposed two percent productivity adjustment represents a “direct benefit to customers” in helping to reduce the rate increase that would otherwise result.<sup>62</sup> No other party addresses the productivity adjustment proposed in the JP.

Although the Commission has generally imputed a one percent productivity adjustment, the higher percentage here is unopposed and not without precedent.<sup>63</sup> Moreover, the two percent adjustment is appropriate given the consolidation of NYAW’s nine water districts and various capital projects proposed here. As NYAW points out, the two percent productivity adjustment

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<sup>59</sup> Id., p. 9.

<sup>60</sup> Exh. 39, Simpson Rebuttal Testimony, p. 16.

<sup>61</sup> Id., pp. 17-18.

<sup>62</sup> NYAW Statement in Support, p. 8.

<sup>63</sup> Cases 16-G-0058 et al., KeySpan Gas East Corporation et al. - Rates, Order Adopting Terms of Joint Proposal and Establishing Gas Rate Plans (issued December 16, 2016), pp. 39-40; Case 08-E-0539, Consolidated Edison Company of New York - Rates, Order Setting Electric Rates (issued April 24, 2009), pp. 36-38; Case 93-E-1123, Long Island Lighting Company - Rates, Order Adopting Recommended Decision with Modifications (issued July 6, 1995), pp. 27-29.



proposed in the JP benefits customers by reducing the Company's O&M expenses by approximately \$184,385 for SA1 and \$77,434 for SA2 in Rate Year 1, with further reductions to the Company's O&M expenses in the remaining rate years.<sup>64</sup> Accordingly, we adopt the two percent productivity adjustment.

Capital Structure, Return on Equity and Overall Rate of Return

Pursuant to Section III.C of the Joint Proposal, the revenue requirements for each of the four years of the proposed rate plan would be based on a hypothetical capital structure with a 46% common equity ratio and a 9.1% return on equity (ROE), with an overall rate of return (ROR) of 6.56%.

In pre-filed testimony, NYAW had proposed that its common equity ratio used for rate-setting be increased from the actual amount of 45.66% as of December 31, 2015 to 48% based upon its pro forma stand-alone capital structure for the rate year ending March 31, 2018.<sup>65</sup> Noting that NYAW was not adequately ring-fenced from its parent company AWW and other AWW affiliates, a necessary condition in order to allow for consideration of NYAW's stand-alone capital structure, Staff recommended a 45.1% common equity ratio based on AWW's consolidated capital structure.<sup>66</sup> Staff asserted that the recommended 45.1% common equity ratio was reasonable and that together with the other elements of Staff's recommendations would produce financial metrics consistent with an investment-grade bond rating.<sup>67</sup> In rebuttal, NYAW disagreed with Staff's

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<sup>64</sup> Exh. 41, Joint Proposal, Appendix A, Schedules A-1.1, p. 2, A-1.2, p. 2, A-1.3, p. 2, A-1.4, p. 2, A-2.1, p. 2, A-2.2, p. 2, A-2.3, p. 2 and A-2.4, p. 2.

<sup>65</sup> Exh. 21, Simpson Direct Testimony, p. 24; Exh. 22, FXS-10, p. 1.

<sup>66</sup> Exh. 59, Duah Testimony, pp. 18-23.

<sup>67</sup> Id., p. 28.

recommendation, maintaining that it was appropriate for it to rely on its stand-alone capital structure to arrive at a proposed common equity ratio of 48%.<sup>68</sup>

Although the common equity level proposed in Section III.C is slightly higher than Staff's one-year litigated position, Staff maintains that the proposal is reasonable given that AWW may find it necessary to modestly strengthen its balance sheet as it embarks on substantial infrastructure investments over the next four years. Staff also supports the 46% level because it is identical to the 46% common equity ratio recently approved for Suez Water New York Inc., which is a similarly-situated water company in Staff's view.<sup>69</sup> NYAW points out that the proposed capital structure represents a fair compromise between the litigation positions taken by it and Staff in pre-filed testimony.

No party objects to the proposed 46% common equity ratio. As Staff notes, it is proper and consistent with the Commission's practice to focus the development of the equity ratio on the parent's capital structure given the lack of ring-fencing. In the context of this four year settlement, the 0.9% modest upward adjustment to the equity ratio is appropriate. The proposed common equity ratio is comparable to equity ratios approved by the Commission for similarly-situated water companies and would produce lower overall revenue requirements than the common equity level initially proposed by NYAW. We find the proposed capital structure containing the 46% equity ratio to be reasonable.

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<sup>68</sup> Exh. 39, Simpson Rebuttal Testimony, pp. 21-27.

<sup>69</sup> Staff's Statement in Support, pp. 10-11, citing Case 16-W-0130, Suez Water New York Inc. - Rates, Order Establishing Rate Plan (issued January 24, 2017).

The Joint Proposal's 9.1% ROE is significantly lower than NYAW's proposed ROE of 10.75%<sup>70</sup> and modestly higher than Staff's recommended ROE of 8.55%.<sup>71</sup> NYAW states that the 9.1% ROE "reflects the current low interest rate environment, which may not continue in the future."<sup>72</sup> It also asserts that it agreed to the 9.1% ROE in the interests of settlement and because such an ROE is "sufficiently high to attract necessary capital" and adequately compensate investors for the additional business and financial risks presented by a multi-year rate plan, while remaining sufficiently low enough to protect ratepayer interests. Staff similarly states that the proposed ROE includes an upward adjustment to Staff's litigated position to account for the higher risk to the utility inherent in a multi-year rate plan.<sup>73</sup>

CAWS argues that NYAW does not deserve a "9.75% profit," asserting that shareholders are not subjected to any increased risk as a result of this multi-year rate plan.<sup>74</sup> However, the Commission has consistently recognized the increased risk to utilities inherent in multi-year rate plans and have endorsed appropriate adjustments to ROEs to reflect

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<sup>70</sup> Exh. 12, Moul Direct Testimony, p. 1.

<sup>71</sup> Exh. 57, Ahmed Testimony, p. 3.

<sup>72</sup> NYAW Statement in Support, pp. 8-9.

<sup>73</sup> Staff Statement in Support, p. 10.

<sup>74</sup> CAWS Reply Statement in Opposition, p. 3. CAWS's reference to a "9.75 profit" appears to relate to the JP's proposed Earnings Sharing Mechanism discussed later in this order, rather than to the 9.1% ROE and 6.56% ROR discussed in the text above.

such risks.<sup>75</sup> As Staff points out, "investors reasonably require higher returns for locking up their investment for an extended period of time," given the additional financial risk that economic and utility operating conditions may change during a four-year rate plan.<sup>76</sup>

In this case, we determine that the proposed 9.1% ROE is appropriately adjusted to reflect the increased risk to NYAW as a result of the longer term rate plan that is proposed here. The ROE was derived by relying on our well-established methodology of employing two-third/one-third weighting of the discounted cash flow model and the capital asset pricing model applied to a surrogate group of companies. In light of the additional business risk and the need to compensate investors for additional financial risk when entering into a multi-year agreement, the agreed to 9.1% ROE is a reasonable outcome relative to Staff's initial proposal, and underscores NYAW's willingness to compromise in the context of a comprehensive settlement. Overall, the ROR is reasonable in light of the

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<sup>75</sup> Case 16-W-0130, Suez Water New York Inc. - Rates, Order Establishing Rate Plan (issued January 24, 2017), pp. 81-83 (approving a 9.0% ROE in a three-year rate plan); Cases 16-G-0058, KeySpan Gas East Corporation et al. - Rates, Order Adopting Terms of Joint Proposal and Establishing Gas Rate Plans, p. 33 (approving a joint proposal that established rates reflecting a 9.0% ROE); Case 15-G-0382, St. Lawrence Gas Company, Inc. - Rates, Order Establishing Multi-Year Rate Plan (issued July 15, 2016) (adopting a 9.0% ROE in a three-year rate plan); Cases 15-E-0283, et al., New York State Electric & Gas Corp. - Rates, Order Approving Electric and Gas Rate Plans in Accord with Joint Proposal (issued June 15, 2016) (adopting 9.0% ROE in a three-year rate plan); 11-W-0200, Long Island Water Corporation - Rates, Order Determining Revenue Requirement and Rate Design (issued March 20, 2012), pp. 15-16 (approving a 9.65% ROE in a three-year rate plan).

<sup>76</sup> Staff Statement in Support, p. 10.

risks faced by the Company, current investor requirements, and the need to keep rates as low as possible while ensuring that the Company can provide safe, adequate and reliable service.

Capital Expenditures

Capital improvements to utility plant are one of the major rate drivers in this proceeding. Over the course of the proposed four-year rate plan, there will be a net increase, taking into consideration plant retirements, of \$117,650,560 of utility plant in service with a net investment of \$75,802,709 in SA1 and \$41,847,853 in SA2.<sup>77</sup> Investments in capital expenditures and associated depreciation represent approximately 37 percent of the revenue increase in Rate Year 1, 62 percent in Rate Year 2, 59 percent in Rate Year 3 and 29 percent in Rate Year 4.

The Joint Proposal provides a list of utility plant additions that the Signatory Parties anticipate to be put into service over the course of the rate plan.<sup>78</sup> Such projects include investments in water production, treatment and delivery systems as well as investment in building improvements, vehicles, equipment and software systems. The Joint Proposal

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<sup>77</sup> Exh. 41, Joint Proposal, Appendix D, pp. 1-3. This amount excludes projects associated with the proposed System Improvement Charge.

<sup>78</sup> Exh. 41, Joint Proposal, Appendix D.

provides annual targets for UPIS. The UPIS targets for reconciliation are shown on the table, below.<sup>79</sup>

Rate Year	SA1	SA2
1	\$313,230,941	\$136,840,850
2	\$335,318,842	\$147,327,545
3	\$354,073,674	\$159,522,319
4	\$371,682,831	\$169,359,594

If, at the end of the rate plan, NYAW has not met the cumulative UPIS targets identified, the revenue requirement impact of the Company's underspending would be deferred for the benefit of customers.<sup>80</sup> If NYAW spends in excess of these amounts, there would be no deferral; ratepayers would not be responsible for any capital investments above the cumulative target levels during the rate plan.

The terms of the Joint Proposal would also require NYAW to maintain an average annual level of investment in main replacements and associated infrastructure of \$14.287 million during the course of the rate plan. Like the UPIS reconciliation mechanism described above, if NYAW has not met its cumulative required spending level on main replacements at the end of the rate plan, the revenue requirement impact of the shortfall would be deferred for the benefit of customers.<sup>81</sup> Should NYAW spend more than the target amounts on main replacements, there would be no deferral.

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<sup>79</sup> Exh. 41, Joint Proposal, p. 6 and Tr. 297.

<sup>80</sup> Exh. 41, Joint Proposal, pp. 6-7 and Tr. 301. Projects associated with the proposed System Improvement Charge would not count toward target and actual UPIS.

<sup>81</sup> Exh. 41, Joint Proposal, p. 7 and Tr. 303-304.

The proponents of the Joint Proposal anticipate NYAW will make further acquisitions of water systems during the proposed rate plan. Pursuant to the Joint Proposal terms, newly acquired systems, and any capital investments made to any newly acquired systems, would be excluded from the calculation of actual UPIS and the UPIS targets.<sup>82</sup> The provisions of the Joint Proposal would authorize NYAW to request recovery of capital investments in an acquired system in the context of an acquisition petition. In that instance, NYAW would request to delay recording depreciation expense relating to the capital investments until the next base rate case proceeding. In the interim, carrying costs would be applied to the capital investment at the Other Customer Provided Capital Rate established by the Commission.<sup>83</sup> Thus, existing ratepayers would not pay for any capital investment in a newly acquired system over the course of the rate plan.<sup>84</sup>

In support of the proposal, NYAW heralds the benefits of additional capital spending on infrastructure to improve its system, specifically noting benefits of the accelerated main replacement program. The Company opines that proactively replacing aging infrastructure will benefit ratepayers in improved water quality, reductions in leakage and avoided costs of repairing main breaks.<sup>85</sup> According to Staff, UPIS and the main replacement reconciliation mechanisms will protect ratepayers from paying for projected capital expenditure

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<sup>82</sup> Tr. 306.

<sup>83</sup> Exh. 41, Joint Proposal, p. 8.

<sup>84</sup> Tr. 306.

<sup>85</sup> NYAW Statement in Support, pp. 9-10.

projects that are not realized by NYAW during the course of the rate plan.<sup>86</sup>

For its part, CAWS contends that infrastructure improvements in the last base rate proceeding were not implemented, but that rates were not reduced as a result. It disputes that infrastructure improvements included in the Joint Proposal will be implemented.<sup>87</sup> CAWS opines that capital improvements are needed, but, pursuant to the terms of the Joint Proposal, there is no assurance to ratepayers that specific projects will be implemented.<sup>88</sup>

Staff and NYAW argue that CAWS's concerns are ill-founded, because the UPIS reconciliation mechanism protects ratepayers from any underspending on capital projects.<sup>89</sup> The Signatory Parties state that the list of identified capital projects are those that are anticipated, not proscribed. Staff argues that NYAW must be afforded flexibility in prioritizing capital projects to address water supply or infrastructure issues as they arise.<sup>90</sup>

We find that the capital expenditure plan included in the budget is reasonable and will allow NYAW continue to make strides in improving NYAW's system to the benefit of customers, both in the form of improved water quality and service. In the litigated case, with the exception of the geothermal project, there were no great disputes with regards to capital spending.

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<sup>86</sup> Staff Statement in Support, p. 18.

<sup>87</sup> CAWS Statement in Opposition, pp. 2, 6-8, and 12-13.

<sup>88</sup> Ibid., p. 13. CAWS's assertions related to the DeMott Avenue water tank project are discussed in the SIC Section of this order.

<sup>89</sup> Staff Statement in Support, pp. 17-18; Staff Reply Statement p. 5; NYAW Statement Reply Statement, pp. 6-7.

<sup>90</sup> Staff Reply Statement, p. 5.



With the exceptions of the increased spending for main replacement and the adjustment to exclude the geothermal project, Staff was supportive of the Company's proposed capital budget for the rate year and found the proposed projects necessary for the continued safety and reliability of NYAW's system.<sup>91</sup> Based on this record, we find that the level of investment included in the Joint Proposal is sufficient to allow NYAW to continue to implement necessary improvements to its system.

The rate plan also includes sufficient protections to ensure that ratepayers will not be harmed if NYAW fails to make the level of improvements included in the proposed rate plan. While NYAW initially recommended reconciliation in both under- or over-spending,<sup>92</sup> the UPIS reconciliation mechanism recommended by the Joint Proposal is consistent with Staff's litigation position that recommended a downward-only adjustment.<sup>93</sup> While CAWS raised concerns that ratepayers may be harmed by underspending, we find that the UPIS reconciliation will protect ratepayers from this situation. This mechanism ensures that NYAW is making the investment that it commits to in the Joint Proposal or, if it does not, that ratepayer funds are put aside, earning interest, for future disposition by the Commission. CAWS points out that needed projects may not be constructed, or may be delayed, over the course of the rate plan. However, NYAW should be afforded the ability to adjust to unforeseen circumstances over the course of the rate plan and use its judgment to triage projects to ensure the most needed projects

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<sup>91</sup> Exh. 63, Staff Infrastructure Panel Testimony, pp. 8-9.

<sup>92</sup> Exh. 21, Simpson Direct Testimony, p. 9.

<sup>93</sup> Exh. 63, Staff Infrastructure Panel Testimony, pp. 4-5.

are addressed, whether or not they are at the front of the planning queue.

We also find the target level of spending for main replacements contained in the Joint Proposal to be reasonable. Customers and parties to this proceeding have voiced concerns with aspects of NYAW's service,<sup>94</sup> including the inconvenience and costs related to main breaks and frustration with water pressure and quality. The capital improvement plan will make strides in addressing those concerns. The level of spending on main replacements is consistent with the recommendation of Staff in its testimony that was supported by NYAW.<sup>95</sup> A dedicated budget for mains within the capital program will ensure that NYAW is focused on addressing this component of its system that will have an impact on customers in the form of improved water service. Focus on mains and services will reduce levels of lost water from deteriorated pipes, lower costs associated with emergency repairs or replacement and should also improve water pressure.

The provisions of the Joint Proposal that exclude investment in newly acquired water systems from the UPIS balance is in the interest of ratepayers. The Commission's Statement of Policy on Acquisition Incentive Mechanisms for Small Water Companies (AIM Policy) encourages larger water utilities to acquire small, non-viable water systems.<sup>96</sup> We encourage large, more stable water companies to continue to procure troubled systems to ensure that ratepayers of those systems receive safe

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<sup>94</sup> Exh. 91, Borecky Testimony, pp. 7-8.

<sup>95</sup> Exh. 63, Staff Infrastructure Panel Testimony, p. 12; Exh. 30, Kilpatrick Rebuttal Testimony, p. 2.

<sup>96</sup> Case 93-W-0962, Small Water Utilities - Acquisition and Merger, Statement of Policy on Acquisition Incentive Mechanisms for Small Water Companies (issued August 8, 1994).

and adequate service at just and reasonable rates. The provisions of the Joint Proposal would foster NYAW's efforts to pursue such acquisitions, advancing our policy goals, while at the same time maintaining rate stability during the rate plan.<sup>97</sup> This ensures that existing customers will not face additional costs while they are adjusting to the new rate plan, which, for some customers, will represent significant bill impacts.

In sum, the proposed capital improvement plan balances the needs of ratepayers and NYAW, is reasonable and is in the public interest.

Revenue, Production Costs and Property Tax Reconciliation Mechanisms

Section III.E of the Joint Proposal includes provisions that would create a combined Revenue, Production Costs and Property Tax Reconciliation Mechanism.<sup>98</sup> NYAW currently has such mechanisms in its three largest water districts.<sup>99</sup> NYAW would continue the mechanisms, and implement them across its service areas, updated for new target levels, shown on the table, below.

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<sup>97</sup> Tr. 306.

<sup>98</sup> The property tax reconciliation is discussed in detail in the Property Tax Section of this order.

<sup>99</sup> Tr. 310-311.

Rate Year 1	Metered Revenues	\$55,223,985	SA 1
		30,455,665	SA 2
	Fuel, Power and Chemicals	4,645,605	SA 1
		2,029,824	SA 2
	Property Taxes	22,226,002	SA 1
		10,382,025	SA 2 - Merrick
3,298,216		SA 2 - Sea Cliff	
Rate Year 2	Metered Revenues	\$64,664,943	SA 1
		33,275,164	SA 2
	Fuel, Power and Chemicals	4,833,388	SA 1
		2,041,756	SA 2
	Property Taxes	23,115,042	SA 1
		10,797,306	SA 2 - Merrick
3,430,145		SA 2 - Sea Cliff	
Rate Year 3	Metered Revenues	\$69,560,986	SA 1
		36,089,101	SA 2
	Fuel, Power and Chemicals	4,865,415	SA 1
		2,053,753	SA 2
	Property Taxes	24,039,644	SA 1
		11,229,198	SA 2 - Merrick
3,567,351		SA 2 - Sea Cliff	
Rate Year 4	Metered Revenues	\$73,099,385	SA 1
		38,441,850	SA 2
	Fuel, Power and Chemicals	4,845,464	SA 1
		2,065,531	SA 2
	Property Taxes	25,001,230	SA 1
		11,678,366	SA 2 - Merrick
\$3,710,045		SA 2 - Sea Cliff	

The differences between the levels of actual revenues and production costs and property taxes and the forecasted target amounts, identified above, would be deferred and the difference recovered or refunded through the RPCRC on an annual basis. At the conclusion of each rate year, NYAW would file a reconciliation within 60 days, along with implementing tariff leaves. The net surcharge or credit would then go into effect 45 days following the submittal, unless Staff submits a letter

to NYAW advising that the reconciliation amounts require adjustment.

The surcharge or surcredit would be applied to all metered customers' bills through a percentage surcharge or credit based on the projected revenues from metered water sales in the succeeding rate year. To calculate the surcharge or surcredit, NYAW would divide the net of the metered revenues and production costs for the prior year by the projected meter revenues for the following rate year and then the resulting percentage applied to metered bills.<sup>100</sup> The recovery or refund associated with a rate year target would be fully recovered or refunded in the succeeding rate year.

The provisions of the Joint Proposal would continue these mechanisms beyond the term of the proposed rate plan at the Rate Year 4 targets, until new levels are set by the Commission in its next rate proceeding. If NYAW does not seek rate relief to be effective by April 1, 2021, monthly target levels would be established for calculating the RPCRC for any period of time not equivalent to a 12-month rate year. In that instance, monthly target levels would be set using the monthly averages of metered revenue for the most recent five years applied to the Rate Year 4 target level.

In pre-filed testimony, NYAW and Staff had agreed that having adjustment mechanisms pertaining to revenues, production costs and property taxes in each of the service areas is appropriate.<sup>101</sup> They also agreed that the return or recovery of any funds pursuant to a reconciliation be returned over the

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<sup>100</sup> Tr. 313-314.

<sup>101</sup> Exh. 6, DeStefano Direct Testimony, p. 19 and Exh. 77, Staff Rates Panel Testimony, pp. 39-40.

course of one rate year.<sup>102</sup> The main point of contention between the parties in their litigated cases, with regards to the mechanism, related to production costs and how they should be recovered if the actual production costs came in above the forecasted level. In that instance, Staff recommended that NYAW recover 95 percent of costs over the target from ratepayers, rather than full recovery. According to Staff, this would motivate the Company to keep costs down.<sup>103</sup> NYAW maintained that production costs are largely out of its control and that, if less than full recovery of costs were authorized, it should coincide with the implementation of a conservation plan, citing customer usage as the main driver of variations in production cost levels.<sup>104</sup> NYAW also suggested that it should be authorized to retain any demonstrated savings in production costs.<sup>105</sup>

In its pre-filed case, Staff also recommended that, for purposes of the reconciliation filing, NYAW be directed to reduce its actual treatment costs for power and chemicals by the treatment costs associated with the volume of water lost due to the geothermal project's water usage. According to Staff, its recommendation would ensure that NYAW does not receive recovery of the incremental water treatment costs of the geothermal project from ratepayers.<sup>106</sup> While the parties took opposing positions regarding the geothermal pilot, as discussed in this order, this recommendation was not addressed by the Company in its rebuttal.

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<sup>102</sup> Exh. 6, DeStefano Direct Testimony, p. 19 and Exh. 77, Staff Rates Panel Testimony, p. 40.

<sup>103</sup> Exh. 77, Staff Rates Panel Testimony, pp. 40-41.

<sup>104</sup> Exh. 26, DeStefano Rebuttal Testimony, p. 15.

<sup>105</sup> Id.

<sup>106</sup> Exh. 75, Staff Policy Panel Testimony, pp. 8-10.

With regards to the targets themselves, the targets fall between the Signatory Parties' litigation positions for metered revenues and fuel, power and chemicals. In pre-filed testimony NYAW and Staff put forth competing methodologies for projecting customer usage.<sup>107</sup> This calculation would factor into both the forecast of metered revenues as well as production costs. Both parties agreed usage is declining. However, they disputed the rate of declining consumption.<sup>108</sup>

In its initial testimony, NYAW projected the proposed rate year metered consumption revenue for SA1 as approximately \$69 million and SA2 as \$33.6 million.<sup>109</sup> These projections were based on present rate year sales forecasts totaling \$45.8 million in SA1 and \$27 million in SA2.<sup>110</sup> Of those operating revenues, fuel, power and chemical costs were projected for the rate year at approximately \$4.7 million for SA1 and \$2 million for SA2.<sup>111</sup>

Staff disputed those amounts in its testimony. With regard to metered consumption revenues, Staff agreed with the Company's forecasted customer count;<sup>112</sup> however, it argued that the Company erred in its calculation of projected usage.<sup>113</sup> It faulted NYAW's declining usage methodology, which applied NYAW's

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<sup>107</sup> Exh. 19, Roach Direct Testimony, pp. 5-27 and Exh. 77, Staff Rates Panel Testimony, pp. 7-23.

<sup>108</sup> Exh. 37, Roach Rebuttal Testimony, pp. 1-20 and Exh. 77, Staff Rates Panel Testimony, pp. 7-18.

<sup>109</sup> Exh. 6, DeStefano Direct Testimony, pp. 3-6; Exh. 22, FXS-9.1 and FXS-9.2.

<sup>110</sup> Exh. 22, FXS-9.1 and FXS-9.2.

<sup>111</sup> Exh. 7, Hawn Direct Testimony, pp. 4-5 and Exh. 22, FXS-8.1, p. 2 and FXS-8.2, p. 2.

<sup>112</sup> Exh. 77, Staff Rates Panel Testimony, p. 6.

<sup>113</sup> Ibid., pp. 7-18.

analysis of the Lynbrook district to its entire service territory and argued that the analysis should be based on actual data.<sup>114</sup> Staff presented an alternate methodology.<sup>115</sup> As a result, Staff recommended adjustments to sales revenues that would decrease sales revenues in SA1 by approximately \$186,000 and increase sales revenues in SA2 by approximately \$963,000.<sup>116</sup> For SA1, Staff argued present rate year sales should be forecast at \$45.6 million and, for SA2, \$30 million.<sup>117</sup> With regards to production costs, Staff generally agreed with the Company's methodology but recommended several changes that resulted in a combined increase to the forecast power, fuel and chemical costs of approximately \$420,000.<sup>118</sup>

In its rebuttal testimony, NYAW argued that Staff's analysis on declining consumption was flawed on a variety of bases and maintained that NYAW's original position should be maintained.<sup>119</sup> With regards to production costs, NYAW agreed with some aspects of Staff's adjustment, but disagreed with the application of a by-district non-revenue water percentage.<sup>120</sup> NYAW recommended applying a three-year average non-revenue water percentage by service area.<sup>121</sup> The Company also disputed Staff's position regarding fuel costs.<sup>122</sup>

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<sup>114</sup> Ibid., p. 9.

<sup>115</sup> Exh. 77, Staff Rates Panel Testimony, pp. 18-20 and Exh. 78, SRP-2.

<sup>116</sup> Exh. 78, SRP-5.

<sup>117</sup> Exh. 78, SRP-6.

<sup>118</sup> Exh. 77, Staff Rates Panel Testimony, pp. 26-30 and Exh. 78, SRP-3.

<sup>119</sup> Exh. 37, Roach Rebuttal Testimony, p. 1-18.

<sup>120</sup> Exh. 28, Hawn Rebuttal Testimony, p. 3.

<sup>121</sup> Id.

<sup>122</sup> Ibid., pp. 4-5.



At the evidentiary hearing, the Signatory Parties indicated that the Joint Proposal represented a compromise of the Staff and Company position with regards to declining consumption and, therefore, the sales forecast and resulting revenue targets. While they characterized their analyses as using different methodologies, they recognized the Joint Proposal as reaching a mid-point between the parties' positions.<sup>123</sup> The Signatory Parties also reached compromise with regards to production, chemical and fuel costs.

The mechanism put forth in the Joint Proposal memorializes the agreements reflected in the Signatory Parties' litigated cases and reaches compromise on disputed aspects. With the exception of the property tax element, separately addressed in this order, the mechanism is unopposed by the parties. We find that the mechanism, as now proposed, balances both the needs of the Company and its ratepayers. Customers can be assured that, if revenues exceed what was expected, they receive a benefit. If production costs are less than forecasted, customers will be compensated the savings. For the Company, its financial health is protected over the course of the rate plan by ensuring that it is compensated for projected revenues and it can be sure that production costs, prudently incurred, are recovered.

A particular benefit of this mechanism is the expediency of prompt recovery of the under or over-collected amounts, avoiding a prolonged deferral on NYAW's books until rates are next set. We also find this mechanism to be equitable in that, by surcharging or crediting any amounts quickly, the mechanism fairly distributes amounts to customers, drastically reducing the likelihood of intergenerational inequities. For

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<sup>123</sup> Tr. 277.

the reasons stated, we find that the revenue and production cost reconciliation mechanism is reasonable and in the public interest.

System Improvement Charge

NYAW currently has a SIC mechanism in place with respect to certain of its water districts.<sup>124</sup> Section III.F of the Joint Proposal would allow NYAW to continue the use of the SIC mechanism and extend its application throughout NYAW's service territory. The mechanism would allow NYAW to use a surcharge to recover carrying costs (the return and depreciation expense) related to specific capital improvement projects that are identified and authorized by this order. Recovery of costs through the SIC mechanism would begin only after those projects are placed in service in Rate Years 2, 3, 4 and beyond, and after their costs have been reviewed and approved by Staff. The SIC surcharge would be assessed on customer bills and calculated pursuant to a formula set forth in the Joint Proposal, which includes a pre-tax rate of return of 8.81% applied to the net

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<sup>124</sup> Case 11-W-0472, American Water Works Co., Inc., et al. - Acquisition of Aqua New York, Inc., Order Approving Stock Acquisition (issued April 20, 2012) (continuing SIC surcharge mechanism previously approved for the former Cambridge Water Company), pp. 11-12; Case 11-W-0200, Long Island Water Corporation - Rates, Order Determining Revenue Requirement and Rate Design (issued March 20, 2012) (continuing SIC in place for the Lynbrook district), pp. 19-20; Case 07-W-0177, Aqua New York, Inc., et al.-Acquisition of Aquarion Water Company of Sea Cliff, Order Instituting Surcharge to Recover Costs Associated with New Elevated Tank (issued December 22, 2009); see also, Case 14-W-0489, American Water Company, Inc. Petition for an Update to its System Improvement Charge, Order Adopting Terms of Joint Proposal (issued August 14, 2015) (extending the SIC in place for the Lynbrook district and updating it to include six additional capital projects); Case 02-W-1564, Sea Cliff Water Company - Water Rates, Order Establishing Rates and Authorizing Surcharge Mechanism, Name Change, and Other Tariff Revisions (issued October 22, 2003).

rate base increase resulting from the projects plus annual depreciation expense.

The SIC mechanism would include the following nine projects, the first eight located in SA1 and the last in SA2:

<b>PROJECT</b>	<b>COST (\$ millions)</b>
Plant No. 20 - Portable Iron Removal Facility	\$1.5
Plant No. 22 - Portable Iron Removal Facility	\$1.9
Plant No. 4 - Iron Removal Facility	\$8.8
Plant No. 7 - Tank Roof Replacement	\$1.6
Plant No. 1 - Iron Removal Facility	\$9.0
Plant No. 6 - Iron Removal Facility	\$6.8
Submarine Crossing	\$2.0
Transmission Main - Baldwin Plant 12-13	\$4.0
Demott Tank and Booster Station	\$3.0
<b>TOTAL</b>	<b>\$38.6</b>

NYAW would have to make a compliance filing with the Secretary to the Commission regarding a project's in-service status within 30 days after the project has been placed in service. It also would conduct an annual reconciliation between authorized collections and actual collections related to the SIC surcharge, which would be filed with the Commission within 60 days after the end of each rate year. The filing will update the SIC surcharge rate to reflect adjustments to under-collections or over-collections. The submitted surcharge would go into effect 60 days after the submittal unless Staff submits a letter to the Company indicating that the surcharge should be adjusted. The SIC surcharge mechanism would remain in place until rates are reset, at which time all costs previously collected through the SIC would be fully accounted for and included in base rates, instead of being recovered in a SIC surcharge.

In pre-filed testimony, NYAW had requested that previously accrued revenues due under existing SIC provisions be “rolled into base rate recovery.”<sup>125</sup> As updated on rebuttal, NYAW requested that accrued SIC revenues of approximately \$3.03 million for SA1 and \$159,000 for SA2 be included in base rates for Rate Year 1.<sup>126</sup> NYAW further requested that, going forward, the SIC mechanism be “reset” and expanded to apply to its other water districts to allow for increased construction of large capital projects needed throughout its service territory at a manageable cost to customers.<sup>127</sup> NYAW proposed that the carrying costs related to ten specific capital improvement projects be subject to the SIC.<sup>128</sup>

Staff did not contest the amounts NYAW sought to include in base rates for accrued SIC revenues, which have been approved by Staff under the SIC mechanism approved in prior cases. Recognizing that the “SIC mechanism allows NYAW the financial flexibility to do necessary and substantial plant construction beyond the rate year without the need to file for a base rate increase,” Staff agreed to the continued application of the SIC mechanism and to the Company’s project construction cost estimates.<sup>129</sup>

Staff, however, recommended that the Company’s construction cost estimates be used to establish the maximum levels of capital costs allowed to be recovered under the SIC.<sup>130</sup> Staff also recommended that the Company be required to make

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<sup>125</sup> Exh. 6, DeStefano Direct Testimony, p. 20.

<sup>126</sup> Exh. 40, FXS-2.1R and FXS-2.2R.

<sup>127</sup> Exh. 6, DeStefano Direct Testimony, p. 20.

<sup>128</sup> Exh. 10, Kirkpatrick Direct Testimony, p. 21.

<sup>129</sup> Exh. 63, Staff Infrastructure Panel Testimony, pp. 18-20.

<sup>130</sup> Ibid., p. 21.

certain SIC compliance filings, and that various other provisions be added to the proposed SIC.<sup>131</sup> Staff determined that the Newbridge Well Filter Plant project should not be subject to the SIC mechanism because a feasibility study was still being conducted on that project.<sup>132</sup> Moreover, noting that each of the two service areas proposed by the Company has its own revenue requirement, rate base, capital budgets and forecasts, Staff disagreed with NYAW's proposal to have all of its service territory subject to a single SIC mechanism, recommending that each service area have its own designated SIC projects and surcharge.<sup>133</sup> On rebuttal, NYAW agreed with all of Staff's recommendations except for the recommendation that the Company use separate SIC mechanisms for each service area.<sup>134</sup>

Although the Joint Proposal does not explicitly state so, NYAW and Staff now agree that each service area will be subject to separate surcharges based upon the projects that occur within the particular service area.<sup>135</sup> The Joint Proposal would include in base rates accrued SIC surcharge revenues of approximately \$3.03 million for SA1 and \$159,000 for SA2. The Joint Proposal also contains the compliance filing requirements and other provisions recommended by Staff, and includes the nine capital improvement projects on which NYAW and Staff agreed in pre-filed testimony.

CAWS and NMCA object to the inclusion of the Demott Tank and Booster Station Project on the ground that funding was

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<sup>131</sup> Ibid., pp. 21-23.

<sup>132</sup> Ibid., pp. 19-20.

<sup>133</sup> Ibid., pp. 23-24.

<sup>134</sup> Exh. 30, Kilpatrick Rebuttal Testimony, p. 15.

<sup>135</sup> Tr. 325.

provided in a prior case,<sup>136</sup> which, they maintain, should have been used to construct the booster pump station now proposed in this JP.<sup>137</sup> However, as the Company explained in pre-filed testimony and at the evidentiary hearing, the Demott Well and Elevated Storage Tank Project approved in Case 09-W-0237 and the Demott Tank and Booster Station proposed here are two different projects.<sup>138</sup> The Company constructed the Demott well but, due to community opposition, not the elevated tank, which was intended to address water pressure issues. The amounts allocated for the elevated storage tank were applied to other infrastructure improvements.<sup>139</sup> The project proposed in this JP involves the addition of a ground storage tank and booster station so that minimum pressure requirements can be satisfied during peak hour demands.<sup>140</sup>

CAWS and NMCA also argue that the project amounts included in the SIC surcharge provision are really rate increases and should be identified as such. However, a good reason exists to include those project amounts under the SIC mechanism. SIC surcharges cannot be imposed until Staff verifies that all work on a project is completed. Accordingly, the SIC mechanism allows the Company to undertake capital projects needed to ensure safe and adequate service while protecting ratepayers against the possibility of slippage or

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<sup>136</sup> Case 09-W-0237, New York Water Service Corp. - Water Rates, Order Establishing Three-Year Rate Plan (issued January 29, 2010).

<sup>137</sup> CAWS Statement in Opposition, p. 7.

<sup>138</sup> Exh. 30, Kilpatrick Rebuttal Testimony, pp. 12-13; Tr. 210-215, 220-221.

<sup>139</sup> Case 11-W-0472, American Water Works Co., Inc., et al. - Acquisition of Aqua New York, Order Approving Stock Acquisition (issued April 20, 2012), p. 13.

<sup>140</sup> Exh. 30, Kilpatrick Rebuttal Testimony, p. 13.

delay in scheduled construction and by setting a cap on the cost of SIC projects.

The capital construction projects proposed in the SIC also will help to address customer concerns over discolored water associated with the presence of iron, improve water pressure, and make necessary infrastructure improvements. In addition, Staff testimony supports the view that the costs of the proposed construction projects are reasonable when compared to the historic costs of similar projects previously authorized by the Commission and recovered through past SICs.<sup>141</sup> Accordingly, the SIC provisions are in the public interest and are adopted.

#### Revenue Allocation and Rate Design

Pursuant to Section III.G of the Joint Proposal, NYAW would consolidate its four existing PSC tariffs into one new tariff, PSC No. 5, which would establish uniform terms, conditions and fees over NYAW's service territory. Existing minimum usage allowances, which require Merrick and Sea Cliff customers to pay for a set volume of water regardless of usage, would be terminated and NYAW would move all metered customers to a monthly billing cycle.<sup>142</sup> Public and Fire Service customers would be billed quarterly in arrears. The plan would eliminate the existing winter/summer rate structure and implement a year-round, inclining four-block, fixed-volume rate structure. The tariff would establish separate residential and non-residential rate structures within SA1 and SA2.

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<sup>141</sup> Exh. 63, Staff Infrastructure Panel Testimony, p. 20.

<sup>142</sup> In Case 11-W-0472, the Commission directed NYAW, in its next rate filing, to consider and propose consolidated, uniform rates for customers of the same rate classification, conversion to monthly billing and elimination of the currently applicable minimum usage allowances. Acquisition Order, pp. 9-10.

The proponents of the Joint Proposal state that the rate increase is allocated using the distribution of revenues at current rates, by service classification, with two exceptions. The first exception is to private and public fire service customers. Those customers would experience a revenue increase that is half of the increase of the other service classes in each of the service areas. The second exception to the standard revenue allocation concerns Sea Cliff property taxes which are exceptionally high. The proponents of the Joint Proposal would apply a special formula to allocate, within SA2, a portion of Sea Cliff property tax responsibilities to customers in the Merrick district. NYAW would first calculate the per-customer property tax burden in each of the two districts. Comparing the two, NYAW would isolate the amount by which the per customer property tax burden of Sea Cliff exceeds that of Merrick. That total for all Sea Cliff customers would then be equally divided between the customers of the Sea Cliff and Merrick districts.<sup>143</sup> Because of the significantly larger number of customers in Merrick, the per-customer effect of that sharing would still fall disproportionately on Sea Cliff customers. Pursuant to the terms of the Joint Proposal, the Company would be required to include a Cost of Service Study in its next rate filing to assess the cost recovery in revenues across its customer classes.

In their pre-filed cases, NYAW and Staff agreed on many issues related to rate design and allocation. Both parties supported a new tariff that would be applicable to all

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<sup>143</sup> Tr. 329-332.



customers,<sup>144</sup> the consolidation of the service territory into the two service areas described in the Joint Proposal,<sup>145</sup> the use of an inclining four-usage block rate design,<sup>146</sup> the elimination of usage allowances<sup>147</sup> and the move to monthly billing.<sup>148</sup> While the Signatory Parties agreed on these aspects, they differed with respect to the appropriate level of meter charge and rate design and allocation methodology.

In its initial testimony, NYAW proposed establishing an equalized meter charge for all residential and non-residential customers across the districts.<sup>149</sup> It proposed a \$15 meter charge for residential and non-residential customers with a 5/8" meter.<sup>150</sup> While Staff agreed with the application of monthly meter charges across all districts, it disputed the amount of the meter charges, particularly for 5/8" meters, arguing the charge should be set the lower existing Lynbrook rate of \$10.44.<sup>151</sup> Staff argued that the Lynbrook district has the largest customer base, its customers were accustomed to the charge, and moving the majority of costs to the volumetric

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<sup>144</sup> Exh. 21, Simpson Direct Testimony, pp. 17-19, Exh. 6, DeStefano Direct Testimony, pp. 21-22 and Exh. 75, Staff Policy Panel Testimony, pp. 14-16.

<sup>145</sup> Exh. 21, Simpson Direct Testimony, pp. 17-19, Exh. 6, DeStefano Direct Testimony, pp. 16 and Exh. 75, Staff Policy Panel Testimony, pp. 14-16.

<sup>146</sup> Exh. 6, DeStefano Direct Testimony, pp. 14-15 and Exh. 77, Staff Rates Panel testimony, pp. 37-38.

<sup>147</sup> Exh. 6, DeStefano Direct Testimony, pp. 14-15 and Exh. 77, Staff Rates Panel Testimony, p. 35.

<sup>148</sup> Exh. 5, Claase Direct Testimony, pp. 3-4 and Exh. 77, Staff Rates Panel Testimony, p. 38.

<sup>149</sup> Exh. 6, DeStefano Direct Testimony, pp. 14-15.

<sup>150</sup> Exh. 22, FXS-12, Tab 3.

<sup>151</sup> Exh. 77, Staff Rates Panel Testimony, p. 35 and Exh. 78, SRP-7.

portion of the bill would send a strong price signal for conservation.<sup>152</sup> NYAW rejected Staff's lower recommended meter charge, arguing that it would add volatility to the annual revenue adjustment clause which could lead to significant surcharges.<sup>153</sup>

To allocate the revenue increase, NYAW recommended first allocating a portion of the revenue increase to private and public fire customers. NYAW allocated revenues equal to a 3.5 percent increase to public fire service for both SA1 and SA2. It allocated revenues equal to a 2.02 percent and 15 percent increase to private fire service in SA1 and SA2, respectively.<sup>154</sup> NYAW explained the comparatively modest increase in SA1 for private fire service was attributable to the significantly higher tariff rates for private fire service in Lynbrook compared to other districts. The Company then allocated the remaining revenue increase for each service area based on the proportion of pro forma present revenues for the year ending March 31, 2018 for the residential, non-residential and sprinkler classes. The resulting revenue increase allocation would be applied to the fixed and volumetric charges with the intent of balancing the bill impacts to customers and the desired movement towards full consolidation.<sup>155</sup> The lawn sprinkler service rate (SC No. 4) in the Lynbrook district was proposed at NYAW's proposed third block rate for residential customers in SA1.<sup>156</sup>

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<sup>152</sup> Exh. 77, Staff Rates Panel Testimony, pp. 34-37.

<sup>153</sup> Exh. 26, DeStefano Rebuttal Testimony, p. 17.

<sup>154</sup> Exh. 6, DeStefano Direct Testimony, p. 16.

<sup>155</sup> Exh. 6, DeStefano Direct Testimony, pp. 16-17.

<sup>156</sup> Exh. 22, FXS-12, Tab 3, p. 10.

Staff took issue with NYAW's revenue allocation, contending that it arbitrarily allocated revenues between service classifications. Staff recommended revenue increases be evenly allocated across service classifications, including fire protection and sprinklers.<sup>157</sup> Staff avowed that any changes in allocation should be supported by a cost of service study.<sup>158</sup> It also recommended that the bill impacts be considered at different usage points to determine the timeline for changes in rate design; a design that, it said, would soften impacts to customers.<sup>159</sup> Staff further rejected a full consolidation of rates within SA2. It stated that the disparity in property taxes between the Sea Cliff and Merrick districts was too significant to integrate their rates. Staff recommended the Sea Cliff property tax expenses incremental to those of Merrick should be collected through a rate applicable only to customers in the Sea Cliff district, thereby keeping the property taxes with customers of Sea Cliff. Staff suggested those costs be recovered from Sea Cliff customers on a volumetric basis through the use of a Rate Adjustment Mechanism (RAM).<sup>160</sup>

NYAW was generally supportive of Staff's proposed allocation method of incremental revenue requirement adjustments in its rebuttal testimony but disagreed with its allocation calculation, noting an error in the calculated late payment rate and Staff's failure to consider existing surcharge revenues being moved into base rates.<sup>161</sup> NYAW opposed Staff's proposal to implement a RAM specific to Sea Cliff customers, arguing that

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<sup>157</sup> Exh. 77, Staff Rates Panel Testimony, p. 31.

<sup>158</sup> Ibid., pp. 31-32.

<sup>159</sup> Ibid., pp. 38-39.

<sup>160</sup> Exh. 77, Staff Rates Panel Testimony, pp. 41-42.

<sup>161</sup> Exh. 26, DeStefano Rebuttal Testimony, p. 16.

the proposal would slow progress towards a consolidated rate and revenue design.<sup>162</sup> The Company maintained it would undercut the goal of the rate consolidation. It claimed that the move towards consolidation should be made in the context of this proceeding, where considerable revenue requirement reductions are available to offset bill impacts to customers.<sup>163</sup> NYAW further contended delay could make consolidation more challenging at a later time, particularly if property taxes continue to climb. It argued that, in consideration of the RAM, Sea Cliff customers would experience significant bill impacts.<sup>164</sup>

The rate design and revenue allocation espoused in the Joint Proposal incorporates the areas of agreement within the Signatory Parties' litigated cases and reflects a compromise of the areas in contention. The proposal put forth by the Signatory Parties also addresses previous Commission directives that required consideration of consolidation, conversion to monthly billing and elimination of the currently applicable minimum usage allowances for customers in the Merrick and Sea Cliff districts.<sup>165</sup>

We find that most aspects of the recommended rate design and allocation will provide benefits both to ratepayers and the Company and will promote our policy goals. By moving all customers to one tariff and bringing all metered customers onto the same billing cycle, the Company will capture administrative efficiencies and, by virtue of a more streamlined approach, customers should experience improved service. Moreover, the rate design, with its four-block inclining

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<sup>162</sup> Ibid., p. 18.

<sup>163</sup> Ibid., pp. 18-19.

<sup>164</sup> Id.

<sup>165</sup> Acquisition Order, pp. 9-10.

structure, will encourage conservation by its price signaling. A regular billing cycle will allow customers to better understand their usage and it may assist in identifying leaks on the customer's property.

The proposed allocation, on the other hand, raises some concern. In particular, the three areas where the allocation deviates from the existing allocation of revenues among the service classes warrant scrutiny, namely, with regard to lawn sprinklers, fire service and the treatment of Sea Cliff property taxes. After evaluating these areas, we remain concerned with the treatment of Sea Cliff property taxes.

First, it appears that the lawn sprinkler rate in Lynbrook reflects the rate applicable to the third block of the residential rate in SA1. Although this was not specifically identified by the parties, the sprinkler rate was a matter in dispute in the litigated case. Here, the proposed rate appears consistent with NYAW's litigation position that the sprinkler rate to be set at the third block level of the SA1 residential rate. As a consequence, the allocation of revenues to that classification is higher than it would otherwise be. We find that applying this rate to the lawn sprinkler tariff is reasonable to encourage conservation.

Second, as proposed in the Joint Proposal, public and private fire protection customers would experience half of the increase provided to the other services classes. This approach balances the concerns raised by NYAW and Staff in their litigated cases. NYAW indicated some concern in applying the same increase to public and private fire service customers, given the differences in their existing rates. We also note that during the pendency of this proceeding we heard from several individuals at public statement hearings who raised concerns regarding the affordability of rates relating to public

and private fire service and NMCA and CAWS reiterated those concerns in their testimony.<sup>166</sup> Here, we find that the proposal strikes a balance between the parties' positions by allocating a portion of the increase to those customers pending a full cost of service study. Through the cost of service study, we will be provided with better guidance as to how costs should be allocated to this class of customers. Until that time, it is appropriate that these customers absorb some of the increase, to minimize the situation in which other customers pay more than they should.

Finally, we must reject the Joint Proposal's approach of sharing a portion of Sea Cliff's property tax burden with customers of the Merrick district. The property taxes associated with the Sea Cliff district are considerable, for several reasons identified by NYAW. First, the Company pointed out that a large energy supplier is decommissioning its plant in Sea Cliff.<sup>167</sup> NYAW is taxed in a special utility class. The taxing jurisdictions within Sea Cliff have been allocating lost revenues from the decommissioning energy supplier to other customers in that class to make up the lost revenue.<sup>168</sup> Second, NYAW identified Sea Cliff as a relatively high-valued property area with higher than average assessments compared to other parts of its system.<sup>169</sup> Finally, the Company explained that taxes are increasing due to capital improvements it is making to its system. As more capital improvements are added to its system, the value of assets and assessments increases.<sup>170</sup>

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<sup>166</sup> Exh. 91, Borecky Testimony, p. 6 and Exh. 107, Denenberg Testimony, pp. 5-7.

<sup>167</sup> The referenced energy supplier is the Glenwood Power Station.

<sup>168</sup> Tr. 332.

<sup>169</sup> Tr. 332-333.

<sup>170</sup> Tr. 332.

NYAW, and the preceding owners of the Sea Cliff district, have experienced a significant increase in property taxes over the last ten years. Since 2006, actual property taxes have almost quadrupled, and since 2013, property taxes have more than doubled. The result of these increases has been significant surcharges to Sea Cliff customers through the existing Property Tax Reconciliation mechanism. For the first two years of the rate plan, Sea Cliff customers will continue to pay these surcharges which will result in significant bills.

The problem with the JP's proposal to share a portion of Sea Cliff's property tax burden with Merrick customers arises because of the system of taxation applicable in Nassau County. Unlike other parts of New York State, New York City and Nassau County have the authority to create a utility and special franchise class for taxing purposes. A result of this is that taxing jurisdictions can charge the utility and special franchise class a higher rate than all other real property owners. Thus, instead of spreading any revenue shortfalls over a broader class of real property owners, some taxing jurisdictions have charged the utility and franchise class magnitudes above the rate of that for other real property classes. Because these taxes are business expenses of regulated utilities, the taxes are passed along to the Company's ratepayers.

Specifically, our concern is that by allowing some sharing of Sea Cliff's property tax with the Merrick district, we may encourage taxing jurisdictions to continue to disproportionately target the utility and special franchise class to make up revenue shortfalls. That is an untenable outcome. We are mindful of the concerns raised by NYAW, that consolidation may be more difficult in the future. However, we can only authorize full rate consolidation where we believe it

is in the best interest of ratepayers. Sea Cliff utility property taxes are roughly 55% of Sea Cliff's revenues. Merrick property taxes are roughly 37% of Merrick's revenues. Moreover, the Merrick and Sea Cliff districts are not interconnected and there are no discernable benefits flowing to Merrick customers from the properties generating the taxes. Under these unique circumstances, we cannot support the socialization of Sea Cliff's property taxes with Merrick. Instead, NYAW is directed to surcharge Sea Cliff customers, on a volumetric basis, for the incremental per customer property tax burden above that of the per customer property tax responsibility of Merrick customers.

Earnings Sharing Mechanism

Section III.H of the Joint Proposal would establish an ESM governing distribution between customers and shareholders of earnings above certain stated thresholds of the average of NYAW's achieved ROEs for the four rate years. The common equity ratio used in each year's calculation of the actual ROE would be the lesser of NYAW's actual rate year common equity ratio or 46%.<sup>171</sup> Actual ROEs would be determined for each rate year and, at the end of the four-year rate plan, the average of the four ROEs would be compared against the earnings sharing threshold

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<sup>171</sup> At the evidentiary hearing, Staff explained that the 46% common equity ratio cap is provided in the calculation to protect ratepayers in case the Company's actual common equity ratio is higher than the 46% common equity ratio used in the JP to determine the Company's hypothetical capital structure for purposes of determining the Company's revenue requirements (Tr. 336-337).



percentages discussed below. A sample ESM calculation for the rate plan is set forth in Appendix E of Joint Proposal.<sup>172</sup>

Under the ESM, NYAW would retain 100% of earnings attributable to an average actual ROE up to and including 9.75%. Earnings attributable to an average actual ROE above 9.75% and up to 10.50% would be shared 50% to customers and 50% to shareholders. Earnings attributable to an average actual ROE above 10.5% would be shared 90% to customers and 10% to shareholders. Any earnings shared with customers would earn interest at the Commission-determined Other Customer Provided Capital Rate in effect on April 1, 2019 (the mid-point of the four-year rate plan). Interest would be earned on the net-of-tax balance that would exist until any over-earnings were fully passed back to customers. The customers' share of any excess earnings would be deferred for the benefit of customers in NYAW's next rate case or as otherwise directed by the Commission. The ESM would continue until rates are reset by the Commission.

NYAW and Staff maintain that the ESM is a critical part of this four-year rate plan that provides distinct benefits to both ratepayers and investors. They assert that the multi-tiered ESM thresholds allow the Company to earn a fair return, incent the Company to control costs and improve productivity, and allow ratepayers to share in the Company's financial benefits, while also ensuring that the Company does not receive

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<sup>172</sup> Under Section III.H, the ESM calculation would exclude any revenue adjustments resulting from the Customer Service Performance Incentive Mechanism, NYAW's share of property tax refunds, any other Commission-approved ratemaking incentives or adjustments in effect during the applicable rate year; revenues not generated from utility operations and related deductions and taxes; and changes in accounting not contemplated in setting the revenue requirements.

a windfall through excessive overearnings due to unforeseen events or large errors in financial projections.<sup>173</sup> NYAW further states that the ESM thresholds are comparable to those in other Commission-approved rate plans.<sup>174</sup>

PULP states that it is concerned with the proposed ESM based on its opposition to ESMs in general and to ESMs with generous "dead bands" in particular, although it does not advocate the use of a different dead band.<sup>175</sup> PULP maintains that, in its experience, dead bands have resulted only in over-earnings for the utility rather than a proper balance of benefits between the utility and ratepayers. As stated in the discussion on the JP's proposed ROE and ROR, CAWS argues that NYAW should not be entitled to a "9.75% profit."

The Commission has endorsed the use of ESMs in the multi-year rate plans of many utilities, including NYAW.<sup>176</sup> As the Commission recently explained, such "mechanisms encourage a

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<sup>173</sup> NYAW Statement in Support, p. 14; Staff Statement in Support, p. 12.

<sup>174</sup> NYAW Statement in Support, p. 14, citing Cases 15-E-0283 et al., New York State Electric & Gas Corporation - Rates, Order Approving Electric and Gas Rate Plans in Accord with Joint Proposal (issued June 15, 2016); Cases 16-E-0060 et al., Consolidated Edison Company of New York, Inc. - Rates, Order Approving Electric and Gas Rate Plans (issued January 25, 2017), pp. 26-27, as corrected by erratum notice issued January 25, 2017.

<sup>175</sup> PULP Statement on the Joint Proposal, pp. 3-4.

<sup>176</sup> Case 14-W-0489, American Water Company, Inc. Petition for an Update to its System Improvement Charge, Order Adopting Terms of Joint Proposal (issued August 14, 2015), pp. 5, 8; Case 11-W-0200, Long Island Water Corporation - Rates, Order Determining Revenue Requirement and Rate Design (issued March 20, 2012), pp. 16-17, 26; Case 11-W-0472, American Water Works Co., Inc., et al. - Acquisition of Aqua New York, Inc., Order Approving Stock Acquisition (issued April 20, 2012), pp. 11-12.

utility to cut its costs, while providing ratepayers protection if actual financial results are dramatically different than had been forecast.”<sup>177</sup> Indeed, the ESMS previously authorized for NYAW have been effective in making NYAW seek to achieve cost savings, as shown by the significant decreases in NYAW’s O&M expenses, which, as discussed earlier, benefit ratepayers as an offset to NYAW’s annual revenue requirement increases.

The 65 basis point dead band proposed here resulting from the difference between the 9.1% ROE reflected in rates and the actual ROE of 9.75% above which sharing begins is consistent with prior decisions of the Commission and fosters our interest in encouraging cost efficiencies.<sup>178</sup> The proposed ESM strikes a reasonable balance among the interests of ratepayers and shareholders, will provide critical protection to ratepayers over the term of the multi-year rate plan, and is adopted.

### Property Taxes

#### Property Tax Reconciliation Provisions

Section III.I of the JP provides for the Company’s property taxes to be partially reconciled to specific target levels for each year of the rate plan, with separate target levels set for each service area. The proposed property tax reconciliation (PTR) provisions are discussed in this section. The proposed property tax target levels are discussed in the next section.

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<sup>177</sup> Cases 16-E-0060 et al., Consolidated Edison Company of New York, Inc. – Rates, Order Approving Electric and Gas Rate Plans (issued January 25, 2017), p. 27, as corrected by erratum notice issued January 25, 2017.

<sup>178</sup> Case 16-W-0130, Suez Water New York Inc. – Rates, Order Establishing Rate Plan (issued January 24, 2017), pp. 83-84 (approving a 65 basis point dead band and noting that the Commission has approved numerous dead bands with sharing beginning anywhere “from 40 to 75 basis points above the ROE allowed in the case”).

In Rate Years 1 and 2, ratepayers would be responsible for 85% of any property tax expense in excess of the target levels for those years and NYAW would be responsible for the remaining 15%. In Rate Years 3 and 4, ratepayers would be responsible for 90% of any property taxes in excess of the target levels for those years and NYAW would be responsible for the remaining 10%. Variances between actual and forecasted property tax amounts for which ratepayers are liable would be collected through the RPCPTR in the next rate year. If actual property taxes are below target levels, ratepayers would be entitled to collect 100% of the difference through the RPCPTR, unless NYAW demonstrates that the reduction in the property tax expense was a direct result of its intervention and action, in which case NYAW would be allowed to retain 15% of the difference in Rate Years 1 and 2 and 10% of the difference in Rate Years 3 and 4. The disposition of any property tax refunds NYAW might receive would be addressed in separate proceedings initiated pursuant to Public Service Law § 113 and 16 NYCRR § 89.3.

In pre-filed testimony, NYAW noted that it currently has PTR provisions for its Lynbrook, Merrick and Sea Cliff districts, under which ratepayers are responsible for either 85% (in Merrick and Sea Cliff) or 90% (in Lynbrook) of property taxes in excess of target levels and are credited 100% of property tax amounts falling below target levels.<sup>179</sup> NYAW maintained that such asymmetrical PTR provisions were unwarranted, "given the Company's record and aggressiveness on tax challenges and the extent of the Commission's active oversight of the Company's tax challenge activities and status."<sup>180</sup> NYAW proposed that the PTR mechanism be extended to

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<sup>179</sup> Exh. 6, DeStefano Direct Testimony, p. 27.

<sup>180</sup> Id., p. 28.

all of its districts, but modified to make ratepayers responsible for 100% of property tax costs in excess of forecasted target amounts.<sup>181</sup>

Staff recognized that a PTR provision was needed to protect both the Company and ratepayers from incorrect property tax forecasts.<sup>182</sup> In Staff's view, ratepayers should be responsible for 85% and the Company for 15% of property tax amounts in excess of forecasted levels, with the Company allowed to retain 15% of property tax amounts below target levels only where it demonstrates that the property tax reduction was a direct result of its intervention and efforts.<sup>183</sup> Staff rejected the Company's proposal to hold ratepayers 100% responsible for property taxes because, in its view, that would remove the Company's incentive to aggressively challenge property tax assessments.<sup>184</sup> In rebuttal, NYAW disagreed with Staff's recommendation and adhered to its original proposal.<sup>185</sup>

NYAW now asserts that the PTR provisions recommended in the JP represent "a reasonable compromise that is in line with the treatment of property taxes in other recent rate cases and is within the range of likely outcomes had this case been fully litigated."<sup>186</sup> Staff states that the proposed PTR mechanism provides NYAW with an appropriate incentive to pursue property tax reductions while protecting it from the financial impact that increasing property taxes present to "an enterprise for which approximately 31 percent of total revenues for SA1 and

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<sup>181</sup> Id.

<sup>182</sup> Exh. 65, Jagadish Testimony, pp. 5-6.

<sup>183</sup> Ibid., p. 7.

<sup>184</sup> Ibid., pp. 7-8.

<sup>185</sup> Exh. 27, DeStefano Rebuttal Testimony, p. 3.

<sup>186</sup> NYAW Statement in Support, p. 15.

nearly 40 percent of total revenues for SA2 [are] paid to the taxing authorities for property and school taxes.”<sup>187</sup> Staff further posits that the proposed PTR mechanism will benefit customers because they would avoid paying all of the property taxes above forecasted levels and recover all or a major share of the funds resulting where actual property taxes are below forecasted levels.<sup>188</sup>

Noting that NYAW recovers from customers through rates 100% of forecasted property tax levels, CAWS and NMCA argue that ratepayers should likewise recover 100% of the funds resulting when actual property taxes paid are below forecasted levels. They maintain that allowing the Company to retain a portion of those funds improperly allows the Company to earn a higher “profit” than allowed under the rate plan and provides the Company with an incentive to improperly inflate its forecasted property tax levels.

We disagree. The record contains no evidence showing that NYAW has improperly inflated its property tax forecasts. To the contrary, the record shows that NYAW used its past actual property tax liability to establish the forecasted tax levels. Moreover, those forecasts are independently reviewed by Staff as part of the rate-setting process. In addition, the ROE applicable to the Company is not set in isolation but as part of a complete rate plan, which includes reconciliation provisions to account for variations between forecasted and actual expenses to ensure the continued financial viability of the utility while protecting customers. Therefore, contrary to the assertions by CAWS and NMCA, application of such reconciliation provisions do not result in earnings higher than allowed by the rate plan and

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<sup>187</sup> Staff Statement in Support, p. 14.

<sup>188</sup> Id.

do not encourage inflated forecasts. Indeed, the Company's property tax forecasts historically have been low as compared to its actual property tax liability. As Staff points out, the adjustments to property tax forecast levels in this JP are designed to more appropriately align the forecasted levels with the Company's actual property tax liability.

Furthermore, if actual property taxes are below forecasted levels, the proposed PTR provisions provide that ratepayers are entitled to recover 100% of the difference through the RPCPTR. The only circumstance under which the Company can receive any portion of that amount is where the Company establishes that it took action that directly resulted in the reduction of property tax expense. As Staff points out, allowing the Company to share in a certain percentage of savings in that circumstance provides the Company with an incentive to pursue property tax reductions. If 100% of the property tax reductions were to be returned to ratepayers, that incentive would be diminished. The proposed sharing of the variance between property tax expenses and property tax targets therefore benefits ratepayers because they are entitled to recover the major portion of such property tax savings. We have approved PTR provisions in other cases for those very reasons, as well as because PTR provisions also benefit ratepayers when actual property tax expenses are greater than forecasted because the Company is responsible for paying a portion of the difference.<sup>189</sup>

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<sup>189</sup> See, e.g., Cases 16-E-0060 et al., Consolidated Edison Company of New York, Inc. - Rates, Order Approving Electric and Gas Rate Plans, as corrected by Erratum Notice issued January 25, 2017; Cases 13-W-0539 et al., United Water New Rochelle, Inc. - Rates, Order Approving Merger and Adopting Multi-Year Rate Plan (issued November 14, 2014), pp. 31-33; Case 11-W-0472, American Water Works Co., Inc., et al. - Acquisition of Aqua New York, Inc., Order Approving Stock Acquisition (issued April 20, 2012), pp. 10-11.

CAWS also argues that the JP provides NYAW with an incentive to challenge property taxes judicially, rather than administratively before an Assessment Review Committee or the Nassau County Assessor before assessments are finalized, and to delay resolution of the judicial tax challenges in an effort to increase the amount recovered against which it could seek to retain the 15% or 10% provided for in the JP. While CAWS points out that specific tax challenges have been pending for a number of years, it offers only unsupported allegations that NYAW somehow was responsible for delaying resolution of the tax challenges in order to increase the amount it could recover under a PTR provision. In addition, NYAW explains that the consolidation of several years of property tax challenges into a single litigation is a reasonable strategy that allows for its efficient use of legal and other expert resources and results in maximum refunds, with interest, for the benefit of ratepayers.<sup>190</sup> Moreover, although the witnesses at the evidentiary hearing stated that they were unaware of an "Assessment Review Commission" or of any meetings between NYAW and the Nassau County Assessor regarding property tax assessments, those witnesses also repeatedly informed CAWS that they did not have that information because such matters would be "handled by the legal team, internal and external legal consultants."<sup>191</sup> NYAW has since pointed out that, pursuant to Real Property Tax Law §706,<sup>192</sup> it has filed protests every year with the Nassau County Assessment Review Commission.<sup>193</sup>

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<sup>190</sup> NYAW Reply Post-Hearing Brief, p. 7.

<sup>191</sup> Tr. 139.

<sup>192</sup> RPTL 706(2) requires a petition challenging a property tax assessment to show that a "complaint was made in due time to the proper officers to correct such assessment."

<sup>193</sup> NYAW Reply Post-Hearing Brief, p. 6.



Accordingly, we conclude that the PTR provisions proposed here are in the public interest, strike an appropriate balance between the interests of the Company and ratepayers, and they are adopted.

Forecasted Property Tax Levels

Section III.I of the Joint Proposal sets forth the following forecasted property tax levels for each of the four rate years:

<b>Forecasted Property Tax Levels (\$ millions)</b>					
<b>Rate Year</b>	<b>SA1 Total</b>	<b>SA2 Merrick</b>	<b>SA2 Sea Cliff</b>	<b>SA2 Total</b>	<b>Combined Total</b>
<b>1</b>	\$22.2	\$10.4	\$3.3	\$13.7	\$35.9
<b>2</b>	\$23.1	\$10.8	\$3.4	\$14.2	\$37.3
<b>3</b>	\$24.0	\$11.2	\$3.6	\$14.8	\$38.8
<b>4</b>	\$25.0	\$11.7	\$3.7	\$15.4	\$40.4

In pre-filed testimony, NYAW initially forecasted its total property tax liability for Rate Year 1 to be in the amount of \$36.09 million,<sup>194</sup> an increase of \$7.12 million or 24.58% over the historic test year.<sup>195</sup> NYAW's actual tax liability increased by eight percent from 2013 to 2014 (from \$25.112 million to \$27.125 million) and by 6.8 percent from 2014 to 2015 (from \$27.125 million to \$28.969 million).<sup>196</sup> NYAW asserted that its property tax expense increased substantially in recent years and that it expected the variance between its actual property tax liability and the property tax targets established in current rate plans to continue to grow.<sup>197</sup> As later adjusted to reflect

<sup>194</sup> Exh. 22, FXS-12, Tab 24, p. 1; Exh. 65, p. 4.

<sup>195</sup> The historic test year covers the twelve months ending December 31, 2015.

<sup>196</sup> Exh. 22, FXS-4.

<sup>197</sup> Exh. 6, DeStefano Direct Testimony, pp. 27, 29.

certain updated actual tax liability, Staff agreed with NYAW's forecasted property tax liability in the amount of \$35.9 million, based upon an "evaluation of the Company's actual historical property taxes."<sup>198</sup>

The Joint Proposal adopts the \$35.9 million property tax level for Rate Year 1, an increase of approximately \$9.69 million or 77% for SA1 and \$4.37 million or 47% for SA2 over property tax levels allowed under the Company's existing rate plans.<sup>199</sup> In addition, property taxes are forecasted to increase by 4% in both service areas for each of the succeeding three rate years. The increases in the forecasted property tax levels are largely due to significant increases to net utility plant, which is projected to increase in Rate Year 1 by \$89.6 million, or 36 percent, as compared to the historic test period.<sup>200</sup> The JP includes separate forecasted property tax levels for the Merrick and Sea Cliff Water Districts for setting rates within SA2.

CAWS and NMCA apparently argue that the forecasted property tax levels are too high given NYAW's success in past

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<sup>198</sup> Exh. 65, Jagadish Testimony, pp. 4-5.

<sup>199</sup> Exh. 42, Responses to ALJ Questions, pp. 3-4.

<sup>200</sup> Tr. 281-282; Exh. 22, FSX-12, Tab 24, pp. 3-5; Exh. 41, Joint Proposal, Appendix A, Schedule A-1.1, p. 5 and Schedule A-2.1, p. 5.

property tax challenges<sup>201</sup> and New York State's Property Tax Cap Law (Chapter 97 of the Law of 2011). That law, effective January 1, 2012, generally limits the annual growth of the total property taxes levied by local governments and school districts to two percent or the rate of inflation, whichever is less, subject to certain exceptions. CAWS and NMCA maintain that those factors should have reduced the Company's property tax liability going forward but are not accounted for in the JP.<sup>202</sup>

That argument lacks merit. The Company explained in pre-filed testimony that, for the former Aqua New York five upstate service districts (Cambridge, Kingsvale, Dykeer, Waccabuc and Wild Oaks), it used a three-year (2015, 2016 and 2017) average percentage change increase/decrease for town/general taxes, school taxes and village property taxes in projecting its property tax expense for those areas.<sup>203</sup> For Mt. Ebo, the Company used "the increase between the 2014 and 2015 tax year bills as the projected year-over-year increase for each tax class."<sup>204</sup> For the Lynbrook, Merrick and Sea Cliff districts, NYAW relied on utility plant in service, construction

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<sup>201</sup> The Company discussed past and pending property tax challenges in its pre-filed testimony and noted that it has refunded approximately \$20.5 million to ratepayers as a result of successful property tax challenges (Exh. 6, DeStefano Direct Testimony, pp. 23-27). In addition, a Joint Proposal filed January 9, 2017 is currently before the Commission concerning the distribution of a tax refund in the approximate amount of \$984,000, resulting from NYAW's successful challenges to *ad valorem* taxes for garbage collection and disposal services charged to special franchise and utility property imposed in the Town of Oyster Bay, Syosset Sanitation District and Glenwood Garbage District, in Case 16-W-0384.

<sup>202</sup> CAWS Statement in Opposition, p. 5.

<sup>203</sup> Exh. 6, DeStefano Direct Testimony, p. 22.

<sup>204</sup> Id.

work in progress, and franchise tax assessments to calculate its property tax forecasts for those areas.<sup>205</sup> The reduced property tax burden resulting from past property tax challenges and any property tax cap effects necessarily would have been reflected in the Company's tax bills used in those calculations. To the extent those factors may further affect the Company's actual tax liability during this rate plan, they would be captured in the PTR mechanism.

CAWS makes much of the fact that the Company and Staff testified at the evidentiary hearing that they did not specifically consider the State tax cap in determining the Company's forecasted tax levels.<sup>206</sup> In making that argument, CAWS ignores the fact that the State's property tax cap effects necessarily would have been reflected in the tax bills used to make those forecasts, as discussed above. Moreover, Staff specifically explained that the property tax forecasts were not otherwise based on any potential future changes to tax rates, but were instead based on historic tax rates and bills as applied to forecasted increases to utility plant.<sup>207</sup> That the percentage increase to NYAW's forecasted tax liability exceeds the two percent property tax cap is not surprising given the large increases in current and projected utility plant. It also makes sense in light of NYAW's historical tax liability, which, as stated, increased by eight percent from 2013 to 2014 and by 6.8 percent from 2014 to 2015, despite the existence of the property tax cap during those years.

Investor-owned utilities like NYAW are required to pay property taxes to school districts, villages and towns on the

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<sup>205</sup> Ibid., pp. 22-23.

<sup>206</sup> CAWS Post-Hearing Brief, pp. 2-3.

<sup>207</sup> Tr. 71.

buildings and plant used to provide water service. In this case, although the Company forecasts large increases to its property tax levels, which is designed to lessen the disparity that has existed between the Company's forecasted and actual property tax liability, we find that the proposed property tax levels are reasonable. Accordingly, they are adopted.

Other Property Tax Issues

CAWS and NMCA argue that allowing NYAW to recover property tax expenses from ratepayers is unconstitutional under the Due Process and Equal Protection Clauses of the Federal Constitution because nearby municipal water systems do not recover property taxes from their customers. They maintain that, although property tax expenses are included in NYAW rates, the ratepayers are not paying a fee for water usage but are actually paying property taxes that those Nassau County residents served by municipal water systems do not have to pay. In making that argument, CAWS and NMCA misunderstand the differences between municipal and privately owned water systems, the costs that privately owned water systems are entitled to recover in providing water service, and the role the Commission plays in the rate setting process.

In establishing a three-year rate plan for NYWS in Case 09-W-0237, the Commission rejected arguments urging the Commission to facilitate municipalization of a privately owned water system by denying it the revenues needed to match the reasonable costs of providing its water service.<sup>208</sup> In doing so, the Commission recognized certain fundamental differences between municipal and privately owned water systems. As stated in that case, the chief advantages of municipal systems is that

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<sup>208</sup> Case 09-W-0237, New York Water Service Corporation - Rates, Order Establishing Three-Year Rate Plan (issued January 29, 2010), p. 22.

they "can usually avoid paying property taxes, income taxes, and other taxes, and obtain needed capital at a lower cost." By contrast, privately-owned water companies are subject to property and income taxes, which are a legitimate part of their cost to provide water service and, thus, properly recoverable from customers.

Despite the differences between the two systems, which necessarily involve different costs and different rates, current laws and policies allow water service to be provided by either municipal or privately owned water companies.<sup>209</sup> The Commission did not establish that dual system, has no jurisdiction over taxing authorities or municipal water systems, cannot force municipalization of privately-owned water companies, and lacks jurisdiction to determine whether the existence of municipal and privately-owned water systems within the same tax district creates any constitutional problems. In rate cases, our jurisdiction extends to whether a privately-owned water company provides safe and adequate service at just and reasonable rates.<sup>210</sup> In doing so, we cannot prohibit such water companies from recovering property tax expenses in rates, as that would be "unlawful under the Public Service Law and contrary to our responsibility to set just and reasonable rates that would ensure the Company can provide safe, reliable and adequate water service."<sup>211</sup>

Next, we reject CAWS's contentions that NYAW and Staff failed to provide sufficient information explaining the effect

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<sup>209</sup> Ibid., p. 21.

<sup>210</sup> Public Service Law §§ 2(26)(27), 4(1), 5(1)(f) and 89-c(1).

<sup>211</sup> Case 09-W-0237, New York Water Service Corporation - Rates, Order Establishing Three-Year Rate Plan (issued January 29, 2010), p. 23.

of certain property tax payments on the proposed rate plan.<sup>212</sup> In response to one of CAWS's discovery requests, NYAW stated upon information and belief, and subject to certain objections, that Aqua NY paid taxes to school districts outside of its operating territory. NYAW further explained that it discontinued paying those taxes when it acquired Aqua NY in 2012 and that any resulting savings would have been passed under the applicable existing PTR mechanism.<sup>213</sup> Because NYAW no longer pays those taxes, they would not be included in the property tax forecasts contained in this JP. Moreover, to the extent CAWS wishes to know whether NYAW brought any challenges seeking a refund for Aqua NY's property tax payments, NYAW discussed all of its property tax challenges in pre-filed testimony and its property tax witness stated at the evidentiary hearing that he was unaware of any pending property tax case regarding those school districts.<sup>214</sup> Finally, contrary to CAWS's position, the reason why NYAW stopped paying property taxes to school districts outside its service territory is clear from the record: NYAW stopped paying those taxes because the school districts were outside of its service territory.<sup>215</sup>

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<sup>212</sup> CAWS Statement in Opposition to the Joint Proposal, pp. 2, 4 and 11.

<sup>213</sup> Exh. 114, CAWS-4, pp. 1-2.

<sup>214</sup> Exh. 6, DeStefano Direct Testimony, pp. 24-27; Tr. 161.

<sup>215</sup> To the extent that CAWS complains that NYAW or Staff did not respond to CAWS's third set of interrogatories, the ALJ denied CAWS's motion to compel responses to those interrogatories. Ruling on Schedule and Discovery Motion (issued January 24, 2017). To the extent that CAWS is dissatisfied with NYAW's or Staff's responses to other interrogatories, CAWS never moved to compel further responses.

Finally, CAWS takes issue with the percentage of tax refunds that NYAW is allowed to retain in proceedings brought pursuant to Public Service Law §113-2 and 16 NYCRR 89.3, and requests that the portion of past tax refunds allocated to the Company be turned over to ratepayers. However, past Commission orders allocating tax refunds to the Company and ratepayers are not subject to challenge in this separate rate case. To the extent that CAWS wishes to contest the future allocation of tax refund awards, the challenge should be asserted in the context of a specific tax refund proceeding, as CAWS has done in connection with the tax refund at issue in Case 16-W-0384.<sup>216</sup>

New York Qualified Manufacturer Credit

Section III.J of the Joint Proposal states that NYAW and its outside accounting firm have determined that NYAW is a Qualified New York Manufacturer, which results in a regulatory liability for the benefit of NYAW's customers and a current 0% state income tax rate for NYAW.<sup>217</sup> The JP provides that the target amount of the regulatory liability to be used for ratemaking purposes will be approximately \$3 million for SA1 and \$2.1 million for SA2, or a total of \$5.1 million, and that NYAW will amortize those amounts over the first three years of the proposed rate plan. If NYAW loses its QNYM status during this rate plan or beyond for any reason, NYAW will defer the revenue requirement impact associated with such a change for future recovery from ratepayers.

NYAW originally estimated the QNYM credit to be in the amount of \$5.8 million.<sup>218</sup> Although Staff initially agreed with

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<sup>216</sup> See CAWS Statement in Opposition to Sanitation Refund Proposal, filed February 6, 2017.

<sup>217</sup> See Tax Law §210(1)(a)(vi).

<sup>218</sup> Exh. 22, FXS-12, Tab 26.



that amount,<sup>219</sup> NYAW updated the amount in rebuttal testimony to reflect the actual QNYM credit balance through July 2016 of \$5.1 million.<sup>220</sup> Staff agrees that section III.J of the Joint Proposal "reflects the correct amounts to be amortized and passed back to customers,"<sup>221</sup> with the \$5.1 million QNYM credit to be amortized over three years. Although CAWS maintains that NYAW has failed to show how the QNYM credit "was realized" by ratepayers,<sup>222</sup> the Commission previously approved NYAW's use of a portion of the regulatory liability as an offset to reduce amounts owing under the Company's Revenue, Production Costs and Property Tax Reconciliation mechanisms for the rate year ending March 31, 2015.<sup>223</sup> Moreover, the Joint Proposal establishes that NYAW would refund the remaining regulatory liability to ratepayers in the amount of \$723,835 per year for SA1 and \$988,260 per year for SA2 in Rate Years 1, 2 and 3.<sup>224</sup> The QNYM credit provision of the Joint Proposal appears both reasonable and in the public interest. It benefits customers by crediting to them the savings resulting from the 0% state income tax rate.

We note that the budget bill signed by the Governor on April 10, 2017 amends certain provisions of the tax law,<sup>225</sup> which

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<sup>219</sup> Exh. 71, Luthringer Testimony, pp. 11-12.

<sup>220</sup> Exh. 39, Simpson Rebuttal Testimony, p. 9; Exh. 40, FXS-13R.

<sup>221</sup> Staff Statement in Support, p. 19.

<sup>222</sup> CAWS Statement in Opposition, p. 7.

<sup>223</sup> Cases 15-W-0437 et al., Petition of NYAW for Approval to Offset the RAC/PTR Surcharge, PSC 1, Order Authorizing Use of Funds (issued October 21, 2015).

<sup>224</sup> Exh. 41, Joint Proposal, Appendix A-1.1, p. 2; A-1.2, p. 2 and A-1.3, p. 2; Appendix A-2.1, p. 2, A-2.2, p. 2, and A-2.3, p. 2.

<sup>225</sup> Senate Bill No. 2009-C, Part P, amending Tax Law §210-B(1)(b)(i), which, pursuant to Tax Law §210(1)(a)(iv), describes the property that qualifies a manufacturer as a QNYM.

appears to make water companies ineligible to be considered as QNYMs and, therefore, ineligible for a 0% state income tax rate. Under the JP, the revenue requirement impact associated with such a change in the law would be deferred for future recovery. However, because this issue would also affect other water utilities in New York, and to mitigate the rate impacts that a deferral would otherwise cause, we direct the Secretary to issue a notice instituting a proceeding, for NYAW and any other affected water company, that quantifies the ratemaking impacts of this change in law, and proposes a recovery mechanism to avoid the rate pressure a deferral would cause in the Company's next rate filing.

Pension and OPEBs

Section III.K of the Joint Proposal states that NYAW remains subject to the Commission's policy statement regarding accounting and ratemaking treatment for pensions and OPEBs.<sup>226</sup> NYAW would continue to reconcile its actual pension and OPEB expenses to the levels allowed in rates and defer the difference. For each of the four rate years, after deducting the portion allocated to capital, NYAW's net pension rate allowances would be \$852,199 for SA1 and \$531,417 for SA2, or a total of \$1,383,616; and its net OPEB rate allowances would be \$388,688 for SA1 and \$(321,642) for SA2, or a total of 67,046.

The JP mirrors the numbers presented by NYAW in its pre-filed testimony, to which Staff had agreed.<sup>227</sup> In addition, NYAW requested that it be allowed to earn interest on its

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<sup>226</sup> Case 91-M-0890, Statement of Policy Concerning the Accounting and Ratemaking Treatment for Pensions and Postretirement Benefits Other Than Pensions (issued September 7, 1993) (Pension and OPEB Policy Statement).

<sup>227</sup> Exh. 22, FXS-8.1, p. 2 and 8.2, p. 2; Exh. 71, Luthringer Testimony, p. 6.

projected debit balance of its pension and OPEB internal reserves and to reduce the interest rate applied against its internal reserve credit balance to the Other Customer Provided Capital Rate.<sup>228</sup> As to the latter request, NYAW maintained that the lower interest rate provided by the customer capital rate was consistent with the interest rate used on other deferrals, such as the Revenue Adjustment Clause and Property Tax Reconciliation Clause, and with the rate used to calculate interest on its property tax refund cases.

Noting that NYAW's request to earn interest on the projected debit balance of its pension and OPEB internal reserves was the subject of a pending proceeding in Case 15-W-0325,<sup>229</sup> Staff stated that the issue would be addressed in that proceeding.<sup>230</sup> Staff disagreed with NYAW's request to have the Other Customer Provided Capital Rate, which was then 2.6%, applied against its internal reserve credit balance. Staff pointed out that the Pension and OPEB Policy Statement requires "that the interest rate applied on an internal reserve balance be the pretax rate of return that the utility is currently allowed in its base rates," which was above 9% for the Lynbrook and Sea Cliff districts.<sup>231</sup> Staff explained that because NYAW did not invest the rate allowance funds in an external fund, but retained the funds within the Company, it "has the use of these ratepayer provided funds, and ratepayers should be compensated for the use of these funds at the same rate of return the

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<sup>228</sup> Exh. 21, Simpson Direct Testimony, pp. 28-29.

<sup>229</sup> Petition of New York American Water Company, Inc. Requesting Authority to Accrue interest on the Debit Balances of its Internal Reserves (Petition filed June 16, 2015).

<sup>230</sup> Exh. 71, Luthringer Testimony, p. 7.

<sup>231</sup> Id.

Company in authorized to earn on capital invested in the utility.”<sup>232</sup>

The JP does not adopt NYAW’s proposals to which Staff disagreed, but adopts the agreed-upon amounts for pension and OPEB rate allowances, which are not opposed and appear reasonable.

Customer Service Performance Incentive Mechanism

The Commission adopted the first Customer Service Performance Incentive (CSPI) mechanism for a New York water utility, for NYWS, one of NYAW’s predecessor companies, in 2010.<sup>233</sup> Section III.L of the JP continues that mechanism and makes it applicable to the Company’s entire service territory, with certain modifications to make the mechanism more stringent. As set forth in the chart below, the proposed CSPI mechanism would subject the Company to certain negative revenue adjustments (NRAs) based upon its annual “escalated complaint” rate per 100,000 customers, with any NRAs to be deferred and returned to ratepayers as determined by the Commission.

<b>Annual Escalated Complaint Rate Per 100,000 Customers</b>	<b>Negative Revenue Adjustment<sup>234</sup></b>
Less than 3	\$0
Greater than or equal to 3	\$194,946
Greater than or equal to 3.4	\$292,420
Greater than or equal to 4	\$389,893

Any customer of a regulated utility may contact the Department of Public Service, Office of Consumer Services (OCS),

<sup>232</sup> Id., p. 8 (citing Pension and OPEB Policy Statement, pp. 19-20 and Appendix A thereto, p. 6).

<sup>233</sup> Case 09-W-0237, New York Water Service Corporation - Rates (issued January 29, 2010), pp. 44-46.

<sup>234</sup> The JP notes that these NRAs are roughly equivalent to 10, 15, and 20 basis points, respectively.

with a complaint about the utility.<sup>235</sup> OCS closely monitors the number and types of all such complaints, which are referred in the first instance to the utility for resolution directly with the customer. If the utility does not resolve that initial complaint to the customer's satisfaction, the customer may again contact OCS, which then considers the matter an "escalated complaint." OCS investigates all escalated complaints and provides a written determination to the customer. As stated, the CSPI mechanism tracks only escalated complaints.

Escalated complaints under the CSPI mechanism would include "those that Staff determines involve situations where the Company has not provided a reasonable level of customer service and/or its actions are deemed to be not in compliance with the Commission's regulations or the Company's tariff."<sup>236</sup> Examples of complaints that would not be counted in the CSPI mechanism as an escalated complaint include complaints about "water quality where the water supplied is in compliance with water quality standards" and "complaints involving a minor disruption to a customer's water service due to necessary system maintenance."<sup>237</sup> In addition, the Company may request that the Commission waive or amend the escalated complaint thresholds and NRAs.

The number of escalated complaints would be calculated on a 12-month rolling average starting on January 1, 2018.<sup>238</sup> The JP explains that the delayed implementation of the CSPI mechanism "will allow the monthly billing program to go into effect while supporting administrative ease and reporting

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<sup>235</sup> 16 NYCRR Part 12.

<sup>236</sup> Exh. 41, Joint Proposal, p. 20.

<sup>237</sup> Id.

<sup>238</sup> Id., p. 19; see also Tr. 354.

consistency by establishing a calendar year start date.”<sup>239</sup> The potential revenue adjustments would be determined during the succeeding rate years after the Company files its annual performance report, which shall include the Company’s escalated complaint rate, any revenue adjustments, complaints the Company asserts should be excluded from the CSPI mechanism, and the reasons supporting such exclusions. The Company is required to file its annual performance report within 60 days after the end of each Rate Year, beginning with Rate Year 2. Accordingly, the first time the Company would be subject to potential NRAs under the CSPI mechanism would be for the 12-month period from January 1, 2018 to December 31, 2019, which would be determined based upon the Company’s annual performance report to be filed no later than May 30, 2019. The proposed CSPI mechanism would remain in place until changed by the Commission.

Staff had proposed in pre-filed testimony that the CSPI mechanism established for NYWS in Case 09-W-0273 be applied to the Company’s entire service territory, with lowered escalated complaint thresholds and higher potential NRAs.<sup>240</sup> Specifically, Staff recommended that the Company be subject to an NRA of approximately \$374,000, or 20 basis points, for an escalated complaint rate greater than or equal to 2.1 complaints per 100,000 customers; an NRA of approximately \$468,000, or 25 basis points, for an escalated complaint rate greater than or equal to 2.5 complaints per 100,000 customers; and an NRA of approximately \$561,000, or 30 basis points, for an escalated complaint rate greater than or equal to 2.9 complaints per 100,000 customers.<sup>241</sup> Staff recommended making the CSPI

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<sup>239</sup> Id., p. 19.

<sup>240</sup> Exh. 73, O’Dell-Keller Testimony, pp. 4-8.

<sup>241</sup> Exh. 74, EOK-3, p. 1.

mechanism more stringent due to the significant growth in the Company's customer base and revenues, as well as to address the increase in the Company's 12-month rolling average escalated complaint rates from 0.7 in 2013 to 1.6 in April 2016. Staff also recommended that the Company be required to file annual reports with the Commission regarding its performance on the CSPI mechanism.

In rebuttal testimony, NYAW maintained that Staff lacked support for recommending NRAs of 20, 25 and 30 basis points.<sup>242</sup> It stated that it had satisfied the CSPI mechanism thresholds previously set for NYWS and that a more appropriate mechanism should be designed to create proper incentives and avoid disincentives for the Company. NYAW therefore offered to work with Staff to craft a CSPI mechanism "that properly balances Company incentives and customer benefits."<sup>243</sup>

The CSPI mechanism proposed in the JP is more stringent than the one currently applicable to NYWS but not as rigorous as that originally proposed by Staff. NYAW asserts that this CSPI mechanism is consistent with other Commission-approved rate plans and provides the Company with an appropriate added incentive to continue to provide high-quality water service and respond promptly and effectively to consumer complaints.<sup>244</sup> Staff similarly maintains that the proposed CSPI mechanism "is an appropriate and reasonable means to incent NYAW to provide a high-level of customer service to ratepayers, by

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<sup>242</sup> Exh. 26, DeStefano Rebuttal Testimony, p. 9.

<sup>243</sup> Ibid., p. 10.

<sup>244</sup> NYAW Statement in Support of JP, p. 18, citing Cases 13-W-0539 et al., United Water New Rochelle Inc. - Rates (issued November 14, 2014), pp. 43-44.

proper response to customer complaints about their service.”<sup>245</sup> PULP asserts that the JP’s retention of the CSPI is in the public interest and underscores the importance to NYAW “of quality service and attention to maintaining and growing the partnership between the Company and its ratepayers.”<sup>246</sup>

CAWS opposes the CSPI mechanism as ineffective because it does not include complaints made to the Company, initial complaints made to OCS, and complaints made about the Company to elected officials. CAWS also asserts that NYAW intentionally deceives the public as to the real reasons for water quality issues and does not prominently display the Commission’s contact information on customer bills.

CAWS’s arguments lack merit, and suggest misunderstandings of both how Commission complaints are handled, and the principles of customer service measurement. When a customer initially complains to the Commission, the utility has a final opportunity to satisfy the customer’s concerns. If it is able to do so, the matter is considered resolved and such a complaint is not counted for the purpose of the CSPI mechanism. By contrast, where the customer indicates that the utility’s response is not satisfactory, the complaint is then “escalated.” Regardless of how the matter is resolved thereafter, such an escalated complaint is counted against the utility for purposes of measuring customer performance, because it is clear that the Company has failed to satisfy the customer. Such counting of escalated complaints is routinely used for measuring utilities’ customer service performance for purposes of imposing NRAs. The accumulation of escalated complaints beyond the target level is evidence that the quality of the Company’s service has

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<sup>245</sup> Staff Statement in Support of JP, p. 20.

<sup>246</sup> PULP Statement on the Joint Proposal, p. 3.



deteriorated, and it is appropriate to subject the utility to potential negative financial impacts in such cases.

Moreover, we reject CAWS's position that customers are not adequately notified about their right to make an initial or escalated complaint to the Commission. Indeed, whenever a utility resolves a customer complaint "wholly or partially in the utility's favor, the utility must inform the customer of the commission's complaint handling procedures, including the commission's address and phone number."<sup>247</sup> In addition, NYAW is required to provide customers annually with a brochure that describes the rights and responsibilities of residential customers.<sup>248</sup> NYAW's customer bills also clearly inform customers of their right to contact the Commission and provide a toll-free number for that purpose.<sup>249</sup> Furthermore, when OCS initially refers a customer complaint back to a utility, it informs the customer by letter that the customer may contact OCS at a toll-free number contained in the letter if dissatisfied with the company's response, at which point OCS would initiate an investigation and then report its findings to the customer.

CAWS also takes issue with the CSPI mechanism's exclusion from consideration as an escalated complaint water quality complaints where the water involved complies with "water quality standards." The same provision was contained in the CSPI mechanism adopted for NYWS in Case 09-W-0273. As Staff correctly points out, water quality standards do not fall within

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<sup>247</sup> 16 NYCRR 14.19(a)(4).

<sup>248</sup> 16 NYCRR 14.16(a)(1).

<sup>249</sup> The Commission's contact information and a copy of the rights and responsibilities brochure mentioned in the text also are available on NYAW's website at <https://amwater.com/nyaw/customer-service-billing/rights-responsibilities>.

our jurisdiction.<sup>250</sup> Accordingly, we agree with NYAW and Staff that the proposed CSPI mechanism appropriately does not subject the Company to NRAs for water quality complaints regarding water that satisfies applicable water quality standards. Of course, we recognize that discolored, unpalatable and/or odiferous water is undesirable for drinking, bathing or washing even when it passes testing by the State and/or County Departments of Health. However, we also note that the Company has taken and will be taking various steps to address water quality issues, including construction of portable and permanent iron removal treatment plants to address discoloration due to the iron that naturally occurs in Long Island groundwater.<sup>251</sup>

We find the proposed CSPI mechanism to be reasonable and in the public interest. Accordingly, the CSPI mechanism is adopted.

#### Low-Income Program

Section III.M of the Joint Proposal would establish a low-income program for residential customers within 60 days of the effective date of new rates. Customers who receive Medicaid or Home Energy Assistance benefits would be eligible to enroll in the program, once their status is verified with a third-party program administrator. Approved customers would then receive a monthly bill credit equal to their meter charge (up to the 1" price) on 12 monthly bills. Those customers would be required to re-certify their eligibility status annually to continue to receive benefits.

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<sup>250</sup> Although OCS does not investigate water quality complaints, it does track the number of consumers who raise concerns about water quality and maintains a written file of those concerns for review by engineering staff assigned to the utility.

<sup>251</sup> Exh. 8, Kern Direct Testimony, pp. 13-14; Exh. 11, Kilpatrick Direct Testimony, pp. 3-19.

The budget for the low-income program is proposed to be capped at \$80,000 annually and recovered in base rates. Any program funds not expended during any rate year would be carried over for use in the following rate year. The low-income program, and the budget associated with it, is proposed to continue beyond the term of the rate plan.

Initially, NYAW had proposed a low-income program similar to the program described above.<sup>252</sup> However, as initially proposed, the administration and customer communication costs associated with its initial program were estimated at \$55,000 annually, while the program was estimated to serve approximately 98 customers and provide approximately \$17,574 in direct benefits to customers in Rate Year 1.<sup>253</sup> Staff opposed NYAW's proposed program, contending that it was not cost-effective.<sup>254</sup> Both parties indicated their willingness to discuss modifications to the program.<sup>255</sup>

The low-income program offered in the Joint Proposal addresses the concerns raised by Staff in its testimony. The program also has the support of PULP as the first low-income rate reduction program for a regulated water company in New York.<sup>256</sup> While PULP opines that it would have preferred a larger budget for the low-income program, it maintains the program is a reliable financial assistance program that will aid low-income customers.<sup>257</sup>

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<sup>252</sup> Exh. 6, DeStefano Direct Testimony, p. 21.

<sup>253</sup> Exh. 22, FXS-12, Tab 16 and FXS-12, Tab 1, p. 29.

<sup>254</sup> Exh. 73, O'Dell-Keller Testimony, p. 13.

<sup>255</sup> Exh. 73, O'Dell-Keller Testimony, pp. 14-15; Exh. 26, DeStefano Rebuttal Testimony, p. 8.

<sup>256</sup> PULP Statement on Joint Proposal, pp. 2-3.

<sup>257</sup> Ibid., p. 2.

While we recognize that the bill impact of the rate changes for some customers will be significant, we do not find that incurring the costs associated with the proposed low-income program are advisable at this time. We recently directed Suez Water New York Inc. to work with Staff and interested stakeholders to design a program to deliver low-income discounts to income-eligible customers.<sup>258</sup> A collaborative process began on May 15, 2017. Because that process has not been completed, and the results have not yet been presented to or considered by us, the Commission does not support instituting a low-income discount program for NYAW as proposed. However, and as we previously discussed, a recent change in law may render NYAW no longer qualified for a State income tax exemption. The result of the change in law will be additional charges to ratepayers. We find that the \$80,000 program budget, proposed to be allowed in rates, will better serve customers to offset those costs. Therefore, we disapprove the low-income program and direct NYAW to defer, for the benefit of ratepayers, the amount allowed in rates for the low-income program. The net deferral will accrue interest at the Other Customer Provided Capital Rate established by the Commission.

#### Lead Pipe Removal Program

Section III.N of the Joint Proposal would establish a lead pipe removal pilot program. Pursuant to the terms of the Joint Proposal, shareholders would fund the pilot program in Rate Year 1 only, up to an amount of \$75,000. Through the pilot program, NYAW would gather information regarding the accuracy of available data on the extent and location of lead pipe on its system and on customer premises connecting with its system, collect additional aggregate data on lead pipe locations, and

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<sup>258</sup> Case 16-W-0130, Suez Water New York Inc. - Rates, Order Establishing Rate Plan (issued January 24, 2017), pp. 93-94.

replace, at NYAW's incremental cost, a customer's lead service line where NYAW is replacing mains and services that connect to the customer's lead service line. NYAW also committed to participate in a collaborative, should one be convened by Staff, to discuss lead pipe replacement issues and concerns. The proponents of the Joint Proposal argue that the pilot program will facilitate the Commission's policy of main and service replacements, support public health and welfare, and assist customers in addressing customer-owned lead service line replacement in coordination with NYAW's replacement of its facilities.<sup>259</sup>

As further clarified by the Signatory Parties, the budget associated with this program is dedicated to cover the incremental cost of replacing customer lead service lines. Program funds will not be applied to any costs associated with research.<sup>260</sup> NYAW estimates that the program will cover the replacement of between 15 and 30 service lines during its one-year term, anticipating that the incremental cost of replacing a customer's lead service line is between \$2,500 and \$5,000.<sup>261</sup> According to the Company, this is within the range of customer-owned lead services that it would encounter while replacing mains over the course of one year.<sup>262</sup>

As further explained at the evidentiary hearing, replacement of a customer's lead service pipe interconnected to a NYAW main is desirable where the Company is replacing its main to avoid a potentially unhealthy condition referred to as

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<sup>259</sup> Exh. 41, Joint Proposal, pp. 22-23; NYAW Statement in Support, pp. 18-19.

<sup>260</sup> Tr. 371.

<sup>261</sup> Tr. 368.

<sup>262</sup> Tr. 368-369.

partial lead service line replacement.<sup>263</sup> According to the Company, if it cuts into a customer's lead service line during construction, and the service line is not subsequently thoroughly flushed, the result may be an increase in lead concentrations, according to research it reviewed.<sup>264</sup> NYAW reported that its field staff is qualified to identify lead service mains where it is conducting work,<sup>265</sup> and to avoid a cut into a customer's lead service line, NYAW's preference, through the pilot program, is to replace customers' service lines in lieu of a partial lead service line replacement.<sup>266</sup> NYAW also advised that it is developing a targeted notice to customers with lead service lines.<sup>267</sup>

To implement this program, NYAW would first select mains for replacement, based on its analysis of several factors, including main age, leaks and breaks, availability of coordination with local municipalities, and concentrations of lead service lines.<sup>268</sup> Once NYAW has identified the mains it intends to replace, the Company would review its records to determine whether interconnected customers may have lead service lines. In order to be certain of the composition of a customer's service line, NYAW would make an appointment with the customer.<sup>269</sup> After determining a customer's service line is lead, NYAW would then enter into a legal agreement with a

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<sup>263</sup> Tr. 372.

<sup>264</sup> Tr. 372-373.

<sup>265</sup> Tr. 382.

<sup>266</sup> Tr. 373.

<sup>267</sup> Tr. 383-384.

<sup>268</sup> Tr. 377-378.

<sup>269</sup> Tr. 378-379.

customer, install the new NYAW main, and replace the customer's lead service line.<sup>270</sup>

According to NYAW, data and experience learned through the course of the pilot program would inform discussions in a collaborative.<sup>271</sup> The collaborative, envisioned to be convened by Staff, is anticipated to consider the legality, availability, costs, benefits and feasibility of on-bill financing for replacement of customer-owned lead services, among other topics.<sup>272</sup>

The presence of lead in the water system was raised over the course of this proceeding by the Company, parties and members of the public. In its initial testimony, the Company acknowledged that it had no proposal to establish a customer assistance program related to lead service lines, but it would further pursue the issue with Staff during the proceeding.<sup>273</sup> It later proposed an expansive program to Staff, to be paid for in base rates, which, it argued, would proactively address lead service lines.<sup>274</sup> Staff and NYAW agreed to continue discussing such a program.<sup>275</sup>

Both NMCA and CAWS raised concerns during the course of the proceeding about the potential for lead in the water distribution system and in customers' homes.<sup>276</sup> They argued that

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<sup>270</sup> Id.

<sup>271</sup> Tr. 370.

<sup>272</sup> Exh. 41, Joint Proposal, p. 23.

<sup>273</sup> Exh. 4, Bruce Direct Testimony, p. 32.

<sup>274</sup> Exh. 64, SIP-1 (DPS-290).

<sup>275</sup> Exh. 63, Staff Infrastructure Panel Testimony, p. 30 and Exh. 30, Kilpatrick Rebuttal Testimony, pp. 11-12.

<sup>276</sup> Exh. 91, Borecky Testimony, p. 10; Exh. 107, Denenberg Testimony, p. 10.

health risks associated with lead may be significant, and that NYAW should take more aggressive steps to address both company-owned and customer-owned lead pipes.<sup>277</sup>

NYAW responded to these concerns by stating that it is in compliance with the Environmental Protection Agency's Lead and Copper Rule requirements, it does not produce water containing lead, and it takes protective measures, such as adding corrosion inhibitors to its water, to reduce any potential for lead to leach from pipes into its drinking water.<sup>278</sup> NYAW stressed that it does not own, operate or control services or facilities such as indoor plumbing or service lines in private residences, commercial buildings or public facilities and that these services and facilities are the responsibilities of the owners.<sup>279</sup> NYAW identified the program it proposed to Staff as its effort to accelerate removal of both Company-owned and customer-owned service lines and to address affordability of making such improvements by a customer.<sup>280</sup>

PULP is supportive of the Joint Proposal's pilot program, calling it "groundbreaking."<sup>281</sup> It states that municipal water systems have access to financial assistance for removal of lead pipes, but private systems, like NYAW's, have not had such assistance.<sup>282</sup> Until such time that assistance is available, PULP asserts that the proposed lead pipe removal

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<sup>277</sup> Id.

<sup>278</sup> Exh. 31, Kilpatrick Rebuttal Testimony, pp. 10-11.

<sup>279</sup> Id.

<sup>280</sup> Ibid., pp. 11-12.

<sup>281</sup> PULP Statement on the Joint Proposal, p. 3.

<sup>282</sup> Id.



program will help to address a serious public health issue immediately.<sup>283</sup>

The lead pipe replacement program recommended in the Joint Proposal makes strides to address an issue that is important to the health and well-being of NYAW's customers. We are supportive of NYAW's efforts to engage customers where the Company is conducting work and to be proactive to inform customers about customer-side lead service lines. We appreciate NYAW's pursuit of this issue throughout the proceeding and its willingness to utilize shareholder funds to assist in the replacement of a customer's lead service line, although it is ordinarily the responsibility of the customer to do so.

The New York State Legislature has recognized the issue of customer-owned lead service lines. The capital projects bill earmarked \$2.5 billion dollars for spending on clean water infrastructure projects.<sup>284</sup> Of those funds, \$20 million are dedicated to addressing lead service lines. The process established by the Legislature envisions municipalities requesting monies from the Department of Health.<sup>285</sup> The Department of Health will administer a Lead Service Line Replacement Grant Program that will allocate funds, giving priority to municipalities that have a high percentage of elevated childhood blood lead levels and considering whether the community is low income and the number of lead service lines in need of replacement.<sup>286</sup>

We are hopeful that the stakeholder collaborative envisioned by the Signatory Parties will include municipalities,

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<sup>283</sup> Id.

<sup>284</sup> Laws of 2017, Chapter 54.

<sup>285</sup> Laws of 2017, Chapters 54 and 57. See Public Health Law (PHL) §1114.

<sup>286</sup> PHL §1114.

so that NYAW and Staff may make those municipalities aware of the availability of these funds and familiarize them with the application process, for the benefit of municipal constituents and NYAW ratepayers. This collaborative will lay the groundwork for finding a long-term solution for addressing customer-owned lead service lines within NYAW's service territory. We hereby direct our Staff to establish the collaborative within 60 days of the issuance of this order.

As noted above, at the evidentiary hearing, NYAW identified partial lead service line replacements as posing a potential risk to customers. In order to protect customers from any potential risk, we direct NYAW to advise a customer, where the Company discovers a customer has a lead service line, that the customer's line is lead. In addition, NYAW should provide customers with sufficient notice whereby the customer might mitigate any potential health risks where the Company is conducting work on an interconnected main or service. The notice should include, at a minimum, the customer's option to replace its service line and the Company's recommended flushing protocols where it encounters a partial lead service line replacement.

#### Geothermal Pilot Project

The Joint Proposal contains several provisions relating to the geothermal pilot heating/cooling system in the William S. Buck Elementary School located in Valley Stream. NYAW installed this system, at its cost, in 2014. It utilizes the constant temperature geothermal energy available from water delivered by NYAW's water distribution mains as the ground loop in the system.

Pursuant to the terms of the Joint Proposal, no recovery of or on the geothermal pilot program would be

authorized.<sup>287</sup> However, NYAW would retain its right to petition the Commission for recovery of the pilot program in the future.<sup>288</sup> No non-revenue water production costs associated with the geothermal project would be permitted recovery from ratepayers and those costs would be adjusted out of the production cost reconciliation mechanism that was previously discussed.<sup>289</sup> Finally, the Joint Proposal would allow \$130,608 associated with the geothermal pilot as a research and development cost, to be recovered in Rate Year 1.<sup>290</sup>

In its testimony, NYAW sought recovery for the full cost of the \$4.55 million dollar pilot project.<sup>291</sup> NYAW contended that it should be allowed recovery of the costs associated with the geothermal pilot, asserting the project is compatible with the Commission's Reforming the Energy Vision (REV) proceeding<sup>292</sup> as a "water for REV" project.<sup>293</sup>

NMCA and CAWS opposed recovery of these costs. They argued that customers outside the school district would not realize any social, economic or environmental benefits from the pilot.<sup>294</sup> Moreover, they asserted that customers should not

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<sup>287</sup> Exh. 41, Joint Proposal, p. 8.

<sup>288</sup> Id.

<sup>289</sup> Exh. 41, Joint Proposal, p. 11.

<sup>290</sup> Exh. 41, Joint Proposal, Appendix A, Schedule A-1.1, p. 2 and Schedule A-2.1, p. 2.

<sup>291</sup> Exh. 4, Bruce Direct Testimony, p. 30; Exh. 11, Kilpatrick Direct Testimony, pp. 24-28.

<sup>292</sup> Case 14-M-0101, Reforming the Energy Vision.

<sup>293</sup> Exh. 4, Bruce Direct Testimony, pp. 29-30.

<sup>294</sup> Exh. 91, Borecky Testimony, p. 8 and Exh. 113, Poretsky Testimony, p. 1-2.

shoulder any research and development costs associated with the program.<sup>295</sup>

For its part, Staff maintained that the geothermal project was not appropriate for traditional rate base recovery.<sup>296</sup> Staff claimed project costs should be excluded from rate year plant additions and that no depreciation expense associated with the project should be authorized,<sup>297</sup> with the exception of the Horton Avenue Main, a segment of the project that Staff supported as necessary for system reliability and water quality, regardless of the geothermal pilot project.<sup>298</sup> Staff regarded the pilot as having uncertain benefits and suggested the pilot be classified as a research and development project.<sup>299</sup> Staff opined that the project's research and development value would benefit NYAW's parent company, American Water Works Company, Inc., and suggested that costs of the project should be shared with the parent. It posited that research and development costs associated with the project should be limited to NYAW's share of total revenues of its parent, three percent, and recommended the Commission allocate three percent of the total net geothermal pilot project costs, or \$130,608, to NYAW.<sup>300</sup> It further recommended that non-revenue water associated with the geothermal project and any treatment costs associated with the volume of water lost due to the

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<sup>295</sup> Exh. 91, Borecky Testimony, p. 8.

<sup>296</sup> Exh. 75, Staff Policy Panel Testimony, p. 4.

<sup>297</sup> Exh. 75, Staff Policy Panel Testimony, pp. 6-7; Exh. 63, Infrastructure Panel Testimony, p. 16; Exh. 64, SIP-3 and SIP-4.

<sup>298</sup> Exh. 75, Staff Policy Panel Testimony, p. 6-7.

<sup>299</sup> Ibid., p. 4.

<sup>300</sup> Ibid., pp. 7-8.

project's water usage be excluded from rates.<sup>301</sup> Staff noted that the pilot is unique and its effectiveness is yet unproven, but that NYAW could consider a variety of business models that may benefit ratepayers and shareholders.<sup>302</sup>

NYAW disputed Staff's position, arguing that Staff failed to consider the project's benefits as a result of its contribution toward REV goals.<sup>303</sup> NYAW asserted that full recovery should be authorized,<sup>304</sup> that the Commission should support research and development costs of water utilities, and that such costs should not be allocated to its parent.<sup>305</sup>

Staff maintains that the treatment of the geothermal pilot project in the Joint Proposal is reasonable and should be adopted.<sup>306</sup> It asserts that the treatment of the geothermal pilot is consistent with its litigation position.<sup>307</sup>

We find that the recovery of \$130,607 as research and development costs strikes the right balance between ratepayers and shareholders. We are tasked with carefully scrutinizing any proposal that would seek recovery of ratepayer funds to ensure it provides demonstrable and sufficient benefits to water customers. Pursuant to the proposal, ratepayers will not pay for project costs whose benefits have not yet been quantified. At the same time, NYAW is provided some recovery of its investment as a research and development cost. If the Company's project is a success and it develops a viable business model as

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<sup>301</sup> Ibid., pp. 8-9.

<sup>302</sup> Ibid., pp. 10-14.

<sup>303</sup> Exh. 30, Kilpatrick Rebuttal Testimony, p. 8.

<sup>304</sup> Id., p. 8.

<sup>305</sup> Ibid., p. 9.

<sup>306</sup> Staff Statement in Support, p. 22-23.

<sup>307</sup> Ibid., p. 23.

a result of its efforts, both ratepayers and shareholders may benefit. Given the costs associated with this project, and the uncertain benefits, we find that allocating research and development costs between NYAW and its parent is appropriate, particularly in that, if successful, NYAW's parent may replicate the program nationwide amongst its subsidiaries to its benefit.

Agreements Between Parties

The Joint Proposal contains several provisions implementing agreements between the parties, which do not require our adoption. Those provisions, enumerated in the ordering clauses below, are not disapproved, but their terms are not adopted as part of this order.

CONCLUSION

The record compiled in this case is complete and supports our decision to adopt the terms of the Joint Proposal as proposed by the signatory parties, with one modification. Notwithstanding the opposition discussed in this order, we conclude that the Joint Proposal provides a fair balancing of the interests of ratepayers and the Company and its investors. It provides sufficient funding for NYAW to maintain safe and reliable service and attract necessary capital to ensure the long-term viability of the Company, while mitigating the ratepayer impact through levelization of the revenue increases. The Joint Proposal provides reasonable resolutions for the issues raised in this case and recommends funding levels and programs that are within the reasonable range of outcomes that might be expected as a result of the case being fully litigated. Finally, the terms of the JP also evidence its consistency with our environmental, social and economic policies and those of the State.

Accordingly, we find that the rate plan established herein will provide just and reasonable rates and is in the public interest.

The Commission orders:

1. The rates, terms, conditions, and provisions of the Joint Proposal dated January 9, 2017, filed in this proceeding and attached hereto as Attachment 1, with the exception of the implementing provisions set forth in Section III, Paragraphs S, U, V, W and X, are adopted and incorporated herein to the extent consistent with the discussion herein. An officer of New York American Water Company, Inc. is directed to file with the Commission a letter confirming its unconditional acceptance of the Multi-Year Rate Plan established in this Order by noon on May 23, 2017.

2. New York American Water Company, Inc. is directed to file a cancellation supplement, effective on not less than one day's notice, on or before May 23, 2017, cancelling the tariff amendments and supplements listed in Attachment 2.

3. New York American Water Company, Inc. is authorized to file, on not less than one day's notice, to become effective on June 1, 2017, on a temporary basis, such tariff changes in PSC No. 5 as are necessary to effectuate the terms of this Order for the rates in the rate year ending March 31, 2018.

4. New York American Water Company, Inc. shall serve copies of its filings on all active parties to these proceedings. Any party wishing to comment on the tariff amendments may do so by filing its comments with the Secretary to the Commission and serving its comments upon all active parties within ten days of service of the tariff amendments. The amendments specified in the compliance filings shall not become effective on a permanent basis until approved by the

Commission and will be subject to refund if any showing is made that the revisions are not in compliance with this Order.

5. New York American Water Company, Inc. is directed to file such further tariff changes as are necessary to effectuate the rates for Rate Year 2 ending March 31, 2019, Rate Year 3 ending March 31, 2020, and Rate Year 4 ending March 31, 2021. Such changes shall be filed on not less than 30 days' notice to be effective on a temporary basis.

6. New York American Water Company, Inc. is directed to file cancellation supplements on not less than one day's notice, effective June 1, 2017, cancelling its tariff schedules, PSC Nos. 1 through 4, and the supplements and statements contained in those schedules.

7. The requirement of the Public Service Law §89-c(10) and 16 NYCRR 720-8.1 that newspaper publication be completed prior to the effective date of the amendments for Rate Year 1 are waived and New York American Water Company, Inc. is directed to file with the Secretary to the Commission, no later than six weeks following the effective date of the amendments, proof that a notice to the public of the changes set forth in the amendments and their effective date had been published once a week for four consecutive weeks in one or more newspapers having general circulation in the service territory. The requirements of Public Service Law §89-c(10) and 16 NYCRR 720-8.1 are not waived with respect to Rate Year 2, Rate Year 3, and Rate Year 4.

8. In the Secretary's sole discretion, the deadlines set forth in this Order may be extended. Any request for an extension must be in writing, include a justification for the extension, and be filed at least one day prior to the affected deadline.



9. This proceeding is continued.

By the Commission:

(SIGNED)

KATHLEEN H. BURGESS  
Secretary