

**BEFORE THE PUBLIC SERVICE COMMISSION**  
**OF THE STATE OF DELAWARE**

IN THE MATTER OF THE APPLICATION OF )  
ARTESIAN WATER COMPANY, INC., CONCERNING )  
THE ESTABLISHMENT OF A DISTRIBUTION SYSTEM ) PSC DOCKET NO. 05-188  
IMPROVEMENT CHARGE UNDER THE PROVISIONS OF )  
26 DEL. C. § 314 TO BE EFFECTIVE JULY 1, )  
2005 (FILED MAY 31, 2005) )

**ORDER NO. 6940**

This 25<sup>th</sup> day of July, 2006, the Commission determines and Orders the following:

1. In May 2005, Artesian Water Company, Inc. ("Artesian") filed to adjust its "Distribution System Improvement Charge" ("DSIC") rate in order to recover the DSIC costs for various "eligible" capital improvements made by it between July 1, 2004 and April 30, 2005.<sup>1</sup> This DSIC filing (to be effective July 1, 2005) came while Artesian's general rate case filing (PSC Dckt. No. 04-42) was pending before the Commission.<sup>2</sup> In addition, the May 2005 filing sought to recover costs for "eligible" plant placed in service over a prior ten-month period. In contrast, the provisions of 26 Del. C. § 314(b)(5) speak of semi-annual adjustments to DSIC rates for improvements "placed in service during the period ending two months prior to the effective date of changes to the DSIC rates." The Commission saw in these two circumstances some questions that could not be adequately addressed under the time constraints for review imposed by the DSIC statutory

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<sup>1</sup>See 26 Del. C. § 314 (2004 Supp.) ("§ 314").

<sup>2</sup>Artesian's DSIC rate had earlier been reset to zero when (on April 6, 2004) it placed rates in effect (under bond) in its general rate case filing.

provision. Consequently, it decided to allow the DSIC surcharge adjustment to go forward on July 1, 2005. At the same time, it asked Artesian to respond to several questions focusing on the timing of the DSIC filing (during a pending general rate case) and the scope of DSIC costs recovered (those coming over a 10-month rather than a 6-month "look back" period). See PSC Order No. 6663 (June 21, 2005).

2. Artesian filed its responses.<sup>3</sup> On the issue of collecting a DSIC charge while a general rate case is pending, Artesian emphasized that § 314(a)(4)c. allows a water utility to recover DSIC costs for currently used and useful "eligible" plant that was "not included in the public utility's rate base in its most recent general rate case." All the improvements underlying its July 1, 2005 filing, Artesian said, had been placed in service after July 1, 2004, past the close of the "rate base" period that was being utilized in the general rate case.<sup>4</sup> As such, all the plant constituted "eligible distribution system improvements." Moreover, nothing in § 314 specifically precludes the filing for a DSIC adjustment when a general rate case is being considered. Thus, in the utility's view, its July 2005 filing was appropriate to recover its DSIC costs that otherwise would not be recovered until the filing of another general rate case. On the issue of the ten-month "look-back" period, Artesian offered two responses. First, in the company's view, the 6-month temporal period described in § 314(b)(5) is directive, not prescriptive. It describes what plant

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<sup>3</sup>Artesian Response (filed July 21, 2005).

<sup>4</sup>Artesian reported that in the general rate case, the utility sought recovery on a rate base reflecting plant-in-service as of June 30, 2004.

(and related costs) can be recovered in a semi-annual filing; it does not require the utility to make every such semi-annual filing. If a utility might choose to forego filing at that first available time, there is nothing that bars it from including the DSIC costs from its earlier improvements in its DSIC rate when it might later file for a DSIC rate adjustment. Second, according to Artesian, even if the temporal terms in § 314(b)(5) might impose a restraint in the case of a DSIC rate "adjustment," such timing limitation does not apply when a DSIC rate is re-initiated after having been earlier "zeroed" out. The Commission had earlier ruled that in the case of a first (or initial) DSIC rate filing by a utility, the only temporal restraint on DSIC costs is that the improvements could not have been in the rate base in the utility's last-concluded rate case.<sup>5</sup> To Artesian, its July 2005 filing was a similar "initial" filing, coming after its earlier DSIC rate charge had been extinguished. Therefore, the only limit was that the improvements could not have been in the rate base considered in any prior rate case, whether concluded or pending. If so, it appropriately could look back not just six months but ten months to be able to include all otherwise eligible improvements not recognized in the rate base in the then pending rate case.

3. Artesian further adjusted its DSIC rate upward on January 1, 2006. But now, its DSIC rate has once more been reset to zero.<sup>6</sup> Staff has submitted a memorandum related to its investigation

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<sup>5</sup>See Order No. 6283 (Oct. 7, 2003).

<sup>6</sup>See PSC Order No. 6948 (June 20, 2006). That happened when (on July 10, 2006) Artesian put new rates into effect under bond in its general rate case filing made in Dckt. No. 06-158.

of the July 1, 2005 DSIC filing and the reconciliation of actual DSIC costs and surcharge recoveries over the 2005 calendar year.<sup>7</sup> Staff reports that - laying aside the two issues identified by the Commission - the DSIC improvements qualified as "eligible" improvements<sup>8</sup> and the 2005 DSIC revenues substantially matched the properly-calculated annual DSIC costs.

4. The Commission will now confirm the DSIC rate allowed to go into effect by PSC Order No. 6663 (June 21, 2005). As set out more fully below, the Commission still has significant concerns about the concurrent collection of a DSIC charge while a general rate case is pending and a water utility's ability to "look back" beyond the "six-month" window set forth in § 314(b)(5) for DSIC costs to justify a DSIC rate adjustment. However, as Artesian correctly asserts, the text of § 314 does not unequivocally speak to the first issue. Nor has the Commission earlier made any formal pronouncement on the issue. Similarly, while § 314(b)(5) speaks of "adjustments" to the DSIC rate for costs of DSIC improvements coming on-line within a defined window, the Commission has, previously, found that such provision does not apply to a utility's "first" DSIC rate submission after the enactment of § 314. But before now, the Commission has not had an occasion to speak (even tentatively) to whether such "exemption" for "initial" filings applies to DSIC rate filings after a previous DSIC rate has been reset to "zero." In light of the absence of any prior clear articulations on the issues, the Commission sees no reason to reach

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<sup>7</sup>See 26 Del. C. § 314(b)(8) (2004 Supp.).

<sup>8</sup>See 26 Del. C. § 314(a)(4) (2004 Supp.).

back to reject, or modify, Artesian's July 2005 DSIC rate, particularly given that it was relatively small and prevailed for a rather short time.

5. Even so, the Commission believes it might be appropriate to now put forward some thoughts on how it might scrutinize future DSIC rate filings that might come during a rate case or that might seek to recover DSIC costs for facilities put in service outside the six-month window set forth in § 314(b)(5). What follows are neither binding rules nor binding definitive judgments: this docket is not a rule-making proceeding and no traditional formal adjudication has occurred. Rather, the comments represent tentative views, subject to be later revisited and reviewed with an open mind in any later individual proceeding. The Commission believes that by now articulating its tentative views, it will not only clarify what it sees as the legal and policy issues in this context but will also narrow the issues in any such later proceeding and thus allow for a better focused final resolution. This narrowing of issues is particularly appropriate given the short time that the DSIC provision allots to the Commission to act on a particular semi-annual DSIC filing.<sup>9</sup>

A. DSIC Rate Filings During the Time  
a General Rate Case Remains Pending

6. Artesian is correct that § 314(b)(5) does not explicitly say that a utility cannot collect a DSIC rate surcharge during the

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<sup>9</sup>See 26 Del. C. § 314(b)(4) (2004 Supp.). This Order can be viewed as somewhat akin, but not identical to, non-binding "Statements of General Policy," issued by federal agencies under the federal Administrative Procedures Act. See, e.g., Pacific Gas & Electric Co. v. FPC, 506 F.2d 33 (D.C. Cir. 1974).

time it might have a general rate case pending. So too, given the Commission's rules defining "test year" for rate cases, it is entirely possible that during a general rate proceeding a utility might have in service DSIC eligible improvements that are not recognized in the "test year" and hence (at least for "test year" calculations) would "not [be] included in the public utility's rate base in its most recent general rate case."<sup>10</sup> Indeed, the longer a general rate case remains pending, the greater the possibilities that the rate base utilized in that pending case will not capture all DSIC improvements that might have come on-line since the rate case filing. Thus, a utility has a significant position that it should be allowed to timely recover, via a DSIC surcharge rate filing, the costs for these non-revenue producing improvements that fall outside the general rate case's "rate base."<sup>11</sup>

7. The difficulties that the Commission sees arise on the practical side. The DSIC costs (and the DSIC rate) are keyed to the

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<sup>10</sup>See 26 Del. C. § 314(a)(4)c. (2004 Supp.). See "Minimum Filing Requirements for All Regulated Companies Subject to the Jurisdiction of the Commission" ("MFRs"), Part A Rate Increase Application - Major Utilities, I.B.1 "Test Year Defined." The MFRs allow the filing utility to choose (with some restraints) the test year and the test period to govern the general rate application. MFR, Part A: I.A, B.1-2, C.

<sup>11</sup>Indeed, one might suggest that if concurrent DSIC filings are not allowed, the greater the possibility that the utility will follow the present general rate case with another, so as to be able to begin recovering the costs of the post-rate base DSIC eligible plant. On the other hand, if concurrent DSIC filings are allowed, there would be no need for such a later rate case filing to recover those costs. Thus concurrent rate case and DSIC proceedings would seem to be consistent with one of the goals of the DSIC provision: to reduce the frequency of rate cases (and rate expenses). Whether concurrent DSIC filings will in fact avoid having a second general rate case follow on the heels of a first one is not clear. For example, here, Artesian was able to recover a DSIC rate during its earlier (recently-concluded) rate case. Yet, it has now filed another general rate case.

utility's weighted cost-of-capital "as established in the most recent general rate proceeding."<sup>12</sup> When the DSIC filing comes during the time when a general rate case is ongoing, what is that "established" weighted cost-of-capital? Is it the "weighted cost-of-capital" declared by the Commission in the last rate Order prior to the present general rate filing? Or, if the utility has put its new rates into effect under bond, is the "established" weighted cost-of-capital that proposed by the utility in its recent filing to support those now "effective" bonded rates? And if the "last rate case" or "bonded" cost of capital is deemed the "established" one for the concurrent DSIC filing, what happens if later in the current (pending) rate case the Commission might determine that a differing capital structure or rate of return is appropriate? Would such a ruling require retroactive adjustments to the recoverable DSIC costs?

8. Then too there is a risk of subscriber confusion when a DSIC rate emerges while a general rate case is pending. Utility managers and rate analysts might understand the concepts of test year and test periods, as well as DSIC improvements, costs, and surcharges. But the only thing subscribers will understand is that the utility has filed for a rate increase; that it has been allowed to put all, or some portion, of those new higher rates in effect, and that now it is adding an additional surcharge on top of the recently increased rates.

9. All this suggests to the Commission that DSIC surcharges during a pending general rate case should be the extreme exception, rather than the routine. By this Order, the Commission does not bar

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<sup>12</sup>See 26 Del. C. § 314(a)(5)a. (2004 Supp.).

the filing for such a DSIC adjustment during a rase case. As noted earlier, this is not a rule-making proceeding. Rather, the Commission expects that if a water utility wants to adjust its DSIC rate during the time its general rate case is moving forward, the utility should accompany its DSIC application with a full and complete explanation why such DSIC filing is necessary.

10. A statement that the DSIC improvements are not included in the "test year" or "test period" chosen by the utility in its rate case would be a necessary recital but probably not an adequate explanation. The Commission's Minimum Filing Requirements grant a degree of flexibility in the parameters for a "test period" and the submission of supporting materials. MFR, Part A: I.C. Moreover, DSIC improvements, by definition, must be non-revenue producing and, in some cases, will replace existing plant (presumably recognized in the rate base used in the general case). Thus, it is likely that dates for placing DSIC plant-in-service and the DSIC capital costs will be "known and measurable." Similarly, given that such improvements are non-revenue producing, inclusion of such plant in a "test period" would not seem to skew the principle of temporarily matching costs and revenues. Thus, the Commission would expect that the explanation demonstrate why the utility could not include such DSIC improvements in its rate base in the proffered general rate case under the flexibility granted for "test periods."<sup>13</sup> Absent an explanation about

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<sup>13</sup>For example, the explanation could report that the utility sought to include such DSIC improvements in its rate base but Staff, the Public Advocate, or another party objected, or that the Hearing Examiner ruled against the recognition of such DSIC improvement costs in rate base.

why DSIC improvement costs cannot be subsumed in the general rate case, the Commission will be inclined to carefully scrutinize any concurrent filing for a DSIC rate adjustment.

B. DSIC Rate Adjustments for Improvements  
Outside the § 314(b)(5) Timing Window

11. The second issue raised by Artesian's July 1, 2005 DSIC adjustment filing is whether a DSIC rate can be "adjusted" to collect DSIC costs placed in service at a time earlier than the six-month window described in § 314(b)(5). In other words, does § 314(b)(5) obligate the utility to file semi-annually to recover its DSIC costs for improvements placed in service within the preceding six-month window, or forfeit (until the next general rate case) its ability to recover the DSIC costs for those improvements? Artesian suggests that § 314(b)(5) was not intended to impose such a "use or lose" regime. Instead, § 314(b)(5) only defines when a utility might begin recovering its DSIC costs for a given improvement. It was not to forbid a utility from foregoing the first opportunity to recover such costs and lumping those costs with later DSIC costs - linked to later improvements - in a subsequent DSIC rate filing.

12. The Commission, on a tentative basis, reads the text of § 314(b)(5) as undercutting Artesian's view. Section 314(b)(5) clearly speaks in terms of a specific temporal limit on what improvements can be looked to for semi-annual adjustments to a DSIC rate: "[the DSIC rate shall be adjusted semi-annually for eligible distribution system improvements placed in service during the 6-month period ending 2 months prior to the effective date of changes in the DSIC rate." If the scheme was meant to allow a utility to accumulate

DSIC costs between general rate cases and allow the utility to decide when to begin recovering those DSIC costs, why include such a temporal limit in § 314(b)(5)? Rather, the statute would have simply declared the time frames for filings (§ 314(b)(3)) and set forth a single criteria: the DSIC costs have to arise from "eligible" improvements not recognized in the last general rate case or any prior DSIC filing.<sup>14</sup> There would not have been any need to describe a shorter window for when the improvements were placed in service. Yet, § 314(b)(5) imposes narrow timing limitations as to eligible improvements and hence eligible costs.

13. The Commission recognizes that if one reads § 314(b)(5) as imposing time limits on what additional DSIC costs can be recovered in a particular DSIC filing, the result may be more frequent DSIC filings. A utility would not be able to forego a DSIC filing to presently recover costs in favor of a later submission that would include these earlier additional costs with the costs of later DSIC improvements. The Commission is normally loathe to tilt to a procedure that requires a utility to collect monies from consumers earlier than when the utility might otherwise seek recovery. But the entire DSIC regime is set-up as a fast-track process. Filings for

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<sup>14</sup>Indeed, in the proceedings leading to Order No. 6283, the parties appearing before the Hearing Examiner apparently assumed that § 314(b)(5) imposes temporal limitations on the costs that can be recovered in a particular DSIC rate adjustment filing. See Order No. 6283, Exhibit A (HE Rpt.) at 6 n. 2. See also Memo. of United Water Delaware Inc. submitted in PSC Dckts. Nos. 02-173 & 02-176 at pg. 3 (July 24, 2003) ("This section [314(b)(5)] of the statute places a substantive limit on the time period for investments included in the DSIC rate only for adjustments to the DSIC rate. It does not place the same substantive limit on the utility's initial DSIC filing.").

DSIC rate adjustments based on recent improvements are easier to verify than those where the improvements, and costs, arose a year or more before. In addition, a regime which not only allows, but might mandate, prompt DSIC filings encourages utilities to make DSIC-type improvements to their distribution systems.

14. Artesian has also suggested that even if § 314(b)(5) imposes temporal limits for DSIC rate "adjustments," those limitations do not apply to "initial" DSIC rate filings. And the category or "initial" filings includes not only those "first" filings made by a utility after the enactment of the DSIC provisions, but the "initial" filing made by a utility after its earlier DSIC rate had been reset to zero because of a general rate case submission. In order No. 6283, the Commission did determine that several utilities, in making their first DSIC rate applications after the enactment of the provision, were not bound by the temporal limitations of § 314(b)(5) and could reach back and include in those first filings the present DSIC costs of all otherwise eligible improvements they had placed in service since their last (pre-DSIC) general rate case. However, the Commission has a significant question whether the "exemption" from the § 314(b)(5) temporal limits that was recognized in Order No. 6283 carries over to the situation where the utility has had its pre-existing DSIC rate "reset to zero" but then later files for an increased DSIC charge. In the situations under consideration in the Order No. 6283 proceeding, the utilities had never previously filed for a DSIC rate. There was - in literal terms - no "pre-existing" DSIC rate. In contrast, in the situation here, the utility had

earlier DSIC rates, but, in the words of § 314(b)(9), that DSIC rate had been "reset to zero" when it placed in effect general rate increases. Pointedly, § 314(b)(9) does not speak in terms of a DSIC rate "ending," "lapsing," or "terminating" when "effective" new general rates now recover prior DSIC costs. Rather, the statutory language speaks in terms of the DSIC rate remaining, but being "reset" at "zero." If so, when a utility later files for a differing DSIC surcharge, one could say it is seeking to "adjust" the previous DSIC rate - to change it from "zero" to the new DSIC percentage.<sup>15</sup> And § 314(b)(5) would apparently cover such "adjustments" to DSIC rates.

15. The Commission emphasizes that it is not making any definitive binding rulings on either of the above issues. It simply sets forth its initial, tentative views. If hereafter a utility wishes to implement a DSIC rate adjustment during the time it has a rate case pending, it should file an explanation of why such filing is necessary. If the utility shows necessity, then the Commission can make a final determination whether such a filing is legally permissible. Similarly, if a utility hereafter seeks to recover DSIC costs arising from improvements placed in service outside the temporal window set forth in § 314(b)(5), that utility should anticipate that the matter will be subject to scrutiny in a full-blown proceeding. The utility should be fully prepared to show why the statutory provision (and good policy) support allowing recovery of such type of "banked" DSIC costs.

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<sup>15</sup>"Adjust" is defined as "[t]o change so as to match or fit; cause to correspond." The American Heritage Dictionary at pg. 79 (2d ed. 1982).

Now, therefore, **IT IS ORDERED:**

1. That, for the reasons set forth in the body of this Order, the Distribution System Improvement Charge rate for Artesian Water Company, Inc., allowed to go into effect by PSC Order No. 6663 (June 21, 2005), is hereby confirmed.

2. That the Secretary shall send a copy of this Order to all water utilities subject to the jurisdiction of this Commission.

3. That the Commission reserves the jurisdiction and authority to enter such further Orders in this matter as may be deemed necessary or proper.

BY ORDER OF THE COMMISSION:

/s/ Arnetta McRae  
Chair

/s/ Joann T. Conaway  
Commissioner

/s/ Dallas Winslow  
Commissioner

/s/ Jaymes B. Lester  
Commissioner

/s/ Jeffrey J. Clark  
Commissioner

ATTEST:

/s/ Karen J. Nickerson  
Secretary