



# REPORT ON STEP ADJUSTMENT METHODOLOGY AND PROCESS

State of New Hampshire  
Public Utilities Commission  
Staff



# Introduction

This Report has been prepared by the Senior Advisor staff of the New Hampshire Public Utilities Commission (Commission) in response to a directive by Chairman Daniel Goldner, issued through a Procedural Order on August 31, 2023, to produce a report “summarizing the input of the participants in [this IR 22-048] investigation for the Commission’s investigation.”

The IR 22-048 investigation (Investigation) was launched by the Commission through an Order of Notice on August 26, 2022. This Order of Notice presented the following findings and parameters for examination during the Investigation:

In Order No. 26,656 (July 28, 2022) and Order No. 26,657 (July 28, 2022), the Commission made findings regarding the necessity for an investigation to examine the accounting and calculation methodologies for step adjustments presented by New Hampshire's electric and gas utilities.

Step adjustment filings have become a frequent feature of ratemaking in our State before this Commission. A high volume of step adjustment filings for utilities in the electric, gas and water industries are often under review, with these filings typically accompanied by a considerable amount of supporting accounting schedules and technical information. Furthermore, the methodologies, durations, and calculations of step adjustments amongst the regulated utilities remain inconsistent and uncoordinated. Despite the complexity involved in our review, petitioners frequently request procedural schedules consisting of an expedited and, in many cases, relatively abbreviated review by the Commission, the New Hampshire Department of Energy (DOE), and other interested persons and stakeholders.

The Commission believes that the issue of step adjustments is ripe for review, given the differences regarding the calculation methodologies used in developing step adjustment schedules, as well as the administrative challenges of adjudicating multiple step adjustment petitions each year with an abbreviated review schedule. As such, the Commission requires an investigation of all aspects of step adjustment development and process. We have determined that this investigation should embrace utilities in the electric, gas, and water industries. *See, e.g.,* Order Nos. 26,623; 26,656; 26,657; and 26,661. *See also* RSA 374:2; 374:4; 374:8; 374:10; 374:11; 374:13; 378:5; 378:7; 378:8.

## REPORT ON STEP ADJUSTMENT METHODOLOGY AND PROCESS

Following the issuance of this August 26, 2022 Order of Notice, a number of regulated utilities, from all industry groups, in New Hampshire filed written comments regarding the Investigation with the Commission. These comments are summarized below. On October 13, 2022, the Commission held an Opening Conference for the Investigation, at which representatives of the electric, gas, and Class “A” water utilities appeared. (In New Hampshire, the Class “A” water utilities, pursuant to N.H. Code Admin. Rules Puc 602.01, are those water utilities having annual water operating revenues of \$750,000 or more, and include Aquarion Water Company of New Hampshire, Inc. (owned by the Eversource holding company organization); Pennichuck Water Works, Inc.; Pennichuck East Utility, Inc.; Pittsfield Aqueduct Company, Inc.; Lakes Region Water Company, Inc.; and Hampstead Area Water Company, Inc.). Also, representatives of the DOE and the Office of the Consumer Advocate (OCA) appeared and provided oral comments to the Commission regarding the Investigation.

On March 21, 2023, the Commission issued a Procedural Order requesting that the electric and gas utilities respond to certain technical inquiries regarding their practices involving step adjustments. (The Class “A” water utilities were exempted from these requests).

Following the issuance of the Data Requests, the electric and gas utilities provided written responses to the Commission in late April 2023. Neither the DOE nor the OCA provided written input. The responses to the Commission Data Requests, and the associated written comments by the electric and gas utilities, were organized and submitted on a holding-company basis; in New Hampshire, the Eversource holding company owns an electric utility (Public Service Company of New Hampshire d/b/a Eversource), and a Class “A” water utility (Aquarion Water Company of New Hampshire, Inc.). The Liberty holding company owns an electric utility (Liberty Utilities (Granite State Electric) Corp.) and a gas utility (Liberty Utilities (EnergyNorth Natural Gas) Corp.). The Unitil holding company owns an electric utility (Unitil Energy Systems, Inc., or UES) and a gas utility (Northern Utilities Inc., or ‘Northern’).

# Executive Summary

## The Historical Contexts of Step Adjustments

The utilities agreed that step adjustments have been used in New Hampshire for at least thirty years and that they have always served as a way for utilities to recover the cost of certain necessary capital investments made between rate cases.

### 1. The step adjustment rate-making paradigm

The utilities pointed out that step adjustments are effective at mitigating the effects of earnings attrition, and therefore enable utilities to defer costly rate cases, allow for gradual, incremental increases in rates, and mitigate the effect of rate shock. The utilities believe that step increases are also essential for maintaining the financial health of a utility.

### 2. The calculation methodologies used to develop step adjustments.

The utilities calculate their non-growth post test year capital investments differently. Some use lists of individual projects and others base it on the change in net plant comprising non-growth investment in the step year. Further, the calculation or allocation of vintage depreciation expense for step increase purposes, and treatment of the Deferred Tax Balance, differs among utilities. A uniform model is preferred by some utilities.

### 3. The role of the DOE's Audit Division

The utilities agreed that DOE audits are important for examining the costs and accounting used as a basis for calculating step adjustments. They stressed the importance of receiving the audit reports early enough to conduct the needed questioning of the DOE audit staff and to reach a settlement and prepare for the hearing.

### 4. Enhancements of review proceedings

Suggestions for improvement included the Commission establishing set timelines for review of step adjustments following a rate case or rate settlement, then the petitioning company and settling parties can work the financial impact of delayed step implementation into the balance of benefits incorporated into the rate filing or settlement agreement.

The step adjustment could also be a reconciling mechanism. In this model, the utility makes a filing, and a rate could be allowed to go into effect, subject to further investigation. This provides much greater flexibility in the timeline for investigation of the prudence of capital additions addressed in the step.

Another alternative approach would be to allow the step adjustment based on a designated or agreed upon amount, for example 80 percent of the forecasted capital additions, and forego the prudence review until the next base-rate proceeding. The utility could be required to file documentation with each step adjustment to demonstrate that the forecast was met or exceeded, thereby warranting the revenue adjustment, but the prudence review would wait for the rate case.

### 5. The role of settlement agreements

The utilities uniformly favored settlements in reaching compromises in rate cases and the related step adjustments. Settlements allow for compromising multiple cost recovery issues, for establishing upper limits on step adjustments, and for delaying future rate case filings.

### 6. The qualification criteria for step adjustments

The utilities generally agreed that the current criteria for including capital investments in step adjustments are, appropriate. Those criteria include: 1) the capital investments are made after the test year, 2) are in service, 3) the costs are prudent, and 4) are not revenue producing or growth related.

### 7. The appropriateness of reconciliation adjustments

The utilities did not favor reconciling step adjustments because they are part of a rate case and adjusting rates after the fact would amount to retroactive rate making. If the Commission were to implement the step adjustments as a reconciling mechanism, the mechanics would be different than what is undertaken today. For a discussion of a possible reconciling approach see the discussion in section 4 above.

# SUMMARY OF INITIAL COMMENTS AND RECORD REQUEST RESPONSES

## The Historical Contexts of Step Adjustments

In response to record requests, utilities described the historical contexts and justifications for the introduction of step adjustments.

According to **Unitil**, Commission-approved step adjustments have been in place for Unitil companies for at least 30 years. On July 21, 1992, the Commission approved a settlement agreement proposed by the Commission Staff and Northern Utilities (DE 91-081), Inc. allowing for “step adjustments in base rates.” A decade later, the Commission approved a step adjustment mechanism allowing Northern to recover the costs associated with the installation of an Automated Reader System (DG 01-182). Those step adjustments were designed to recover costs associated with specific capital projects. The Commission approved a broader two-part step adjustment (DE 05-178) enabling Unitil Energy Systems, Inc. (“UES”) to recover prudently incurred costs related to certain large non-revenue producing capital additions placed in service as well as the acquisition of a certain parcel of land. It continued in the subsequent rate cases (RR-1 response).

**Liberty** also stated that the step adjustments first appeared in New Hampshire in the late 1990s or early 2000s. Before that time, there was no common practice for utilities to seek rate relief between rate cases.

**Eversource** stated that there is a long history of the use of “step adjustments” to address earnings attrition between base-rate proceedings. For Public Service Company of New Hampshire, the Commission addressed this issue in some detail in Docket No. DE 09-035, which was a base-rate proceeding resolved by settlement which included a series of step increases intended to “account for a return on additions to the Company's net plant as well as a return on capital additions resulting from the Company's REP-related activities.”

## Issue 1. The step adjustment rate-making paradigm

### **The advisability for continuing the step adjustment rate making paradigm in the current regulatory and economic environment in New Hampshire.**

**Unitil and Liberty** strongly support the continued use of step adjustments between rate cases to recover costs associated with certain capital investments that are placed in service after the test year.

**Unitil** pointed out that a step adjustment is effective at mitigating the effects of earnings attrition and therefore enabling utilities to defer costly rate cases, allow for gradual, incremental increases in rates, and mitigate the effect of rate shock. The Company believes that Step increases are also essential for maintaining the financial health of a utility. Referring to recent UES and Northern rate cases, the Company stated that non-growth plant additions represent a significant portion of each company's historic and forecasted investments (on average, 80% of capital spending from 2016 – 2020 and are projected to average 84.3% of capital spending through the end of 2023) which includes reliability investments, infrastructure replacement, and system improvements. The Company recognized the concerns recently expressed by the Commission regarding growth in the utility rate base relative to customer growth but stressed that there is no reason to expect a direct, proportional relationship between system investment and customer additions. UES contemplated that restricting or eliminating step adjustments would increase the frequency of full rate cases and the corresponding costs and administrative burden for all parties. Referring to RSA 378:7, which states: "The commission shall be under no obligation to investigate or hear any rate matter which it has investigated within a period of 2 years, but may do so within said period at its discretion," the company concluded that Step adjustments are an efficient method of bridging the potential gap between rate cases described in RSA 378:7.

Similarly **Liberty** stated that step adjustments: (a) allow for recovery of projects placed into service between rate cases, especially non-growth capital projects that are not offset by additional revenues; (b) allow for such interim recovery without the time and expense required of full rate cases; (c) extend the time between rate cases; (d) lessen utilities' earning attrition between rate cases; and (e) allow for the gradual adjustment of rates over the years as opposed to the potential rate shock to customers caused by rate cases filed without the benefit of intervening step adjustments.

**Eversource** Companies also recommended continuing the step adjustment ratemaking paradigm considering the current regulatory and



economic conditions facing utilities in New Hampshire. Eversource asserted that the need for increasing investment stems from numerous factors, including age and condition of distribution infrastructure; increasing expectations of customers for more reliable and resilient service due to our modern-day dependence on electricity; the benefits of installing modernized technology for reliability, resiliency, and environmental control; and the need to accommodate clean energy facilities with two-way power flows.

For both electric and water companies, **Eversource** states that the need for these investments arises primarily from the infrastructure age and the correlating deterioration and increasing customer expectations. It also pointed out that the cost of running the system is increasing, including in relation to the cost of capital projects. According to the Company, all these factors drive the need for investment not as a result of a growing customer base that would provide incremental revenues to offset the capital investment or increased O&M. In recent rate proceedings, the Eversource Companies entered into settlement agreements that included step adjustments. Those steps played an integral part in balancing the interests of all parties - the ability of the Companies to maintain sufficient revenue for a longer period, consequently avoiding the need to file a full rate case at the earliest possible opportunity and minimizing these resource-intensive administrative proceedings. Eversource also cited RSA 378:7 and argued that the 2-year restriction does not exist in neighboring jurisdictions like Massachusetts and Maine and that the step adjustment provides the opportunity for utilities to collect sufficient revenue during the interim years to avoid rate filings well beyond the two-year threshold for the filing of a new rate case.

Companies made similar arguments with more details in their responses to the Record Request (RR 1(a)). **Eversource** identified certain criteria for any alternative option to achieve the outcome of providing revenue support to mitigate earnings attrition between rate cases with differing administrative burdens.

*1. The revenue adjustment mechanism should have a cost basis so that it is adequately formulated to provide sufficient assistance in extending the time between base-rate cases, and also avoids departing from a cost basis in the interests of customers.*

*2. The revenue adjustment mechanism should encompass “guardrails” that ensure that the revenues provided by the mechanism are not over-compensating the utility, while at the same time providing the utility with sufficient revenue support to sustain the opportunity to earn the authorized return on equity (ROE). For example, an earnings sharing mechanism (ESM) that is designed to trigger a rate change in the event the utility over or under earns its authorized ROE outside a predetermined bandwidth could achieve this goal.*

*3. The revenue adjustment mechanism should encompass strong*



*incentives for the utility to control costs, while providing adequate support. This can be achieved by structuring the annual revenue adjustment to work in combination with a defined stay-out period for the next base-rate change.*

*4. The revenue adjustment mechanism should provide transparency to stakeholders and to the Commission; and*

*5. The revenue adjustment mechanism should be administratively efficient.*

### Multi-year rate plans and other solutions

**Eversource**'s written input also provided a broad-ranging legal discussion regarding the justifications for step adjustments under New Hampshire law and ratemaking standards, and advocacy for the implementation of a "**performance-based ratemaking**" approach, to replace step adjustments, in the future. Eversource also indicated at the May 9 Technical Session, in common with the other utility holding companies, that its step adjustment technical models had company-specific characteristics that would tend to make cross-holding-company granular comparisons regarding step adjustment features tenuous. (Eversource's submissions also made extensive reference to the New Hampshire Least Cost Integrated Resource Plan (LCIRP) review framework as potentially bringing fresh approaches to this area. These comments, however, were rendered obsolete by the October 7, 2023 repeal of the LCIRP statute).

**Eversource** also discussed **Periodic Rate Base Updates** used in other states. The Company has experience with stepped rate increases that occur on a periodic basis to update the rate base without any change to O&M recovery. Eversource refers to this construct as a "rate base update" and Eversource has this construct in place in Massachusetts based on a settlement process. Eversource Gas of Massachusetts entered into a settlement that allowed for two rate-base updates over a 7-year rate plan, among other rate changes. Each rate-base "update" is comprised of an update to all elements of rate base and the associated revenue requirement, including accumulated depreciation, accumulated deferred income taxes, property taxes, and return on rate base for capital additions placed in service.

**Eversource** described the **Annual Capital-Cost Recovery Mechanism** as another alternative to step adjustment. It is designed to recover the annual revenue requirement on a designated set of plant additions completed each year, subject to a later prudence review, until such time that a base-rate case occurs and recovery of the cumulative set of plant additions is rolled into rate base in base rates. The Company observed that this mechanism as implemented in Massachusetts (historical capital-cost recovery mechanism)

was severely limiting and did not eliminate the need for frequent rate cases for the utilities because of the substantial lag built into the recovery mechanism. It identified two key impediments: (1) the amount of capital expenditures allowed through the mechanism was capped at the average of three historical years, occurring prior to the last rate case, cutting off recovery of substantial amounts of plant additions cost until the next rate case; and (2) the cycle of recovery incorporated substantial lag between the in-service date and the start of recovery.

**Eversource's** electric affiliate in Connecticut operates with three revenue support mechanisms: a) a multi-year rate plan that increases the amount of allowed revenue; b) a capital tracker (the Electric Systems Improvement ("ESI") mechanism) where a revenue requirement above the new plant in service that was built into base distribution rates was included for recovery in the ESI; c) a minor Step Adjustment Provision that increased the revenue requirement in each rate year by a pre-set amount related to field operations.

**Unitil's** Massachusetts and Maine affiliates have multiple capital cost recovery adjustment mechanisms in place that allow for the recovery of costs associated with post-test year investments including –

- Capital Cost Adjustment Mechanism ("CCAM") that allows the Company to recover costs associated with post-test-year capital additions, subject to an annual spending cap and a cap on annual rate increases of 1.5% of total revenues. The amounts above the cap are deferred for recovery in a future proceeding, with carrying charges.
- An annual Grid Modernization Adjustment Factor filing to recover costs associated with incremental grid modernization investments.

**Unitil** stated that Northern's Maine division has had a Targeted Infrastructure Replacement Adjustment ("TIRA") in place. The TIRA provides for annual increases to distribution rates to recover costs associated with the company's investments in targeted operational and safety-related infrastructure replacement and upgrade projects. Unitil observed that the TIRA and the Massachusetts cost recovery adjustment mechanisms operate like step adjustments, but unlike step adjustments in New Hampshire, these mechanisms are not limited in number, though the TIRA program is expected to end in 2024.

Issue 2. The calculation methodologies used to develop step adjustments.

**The calculation methodologies used to develop step adjustments, including the treatment of depreciation and other categories of expense, rate of return, etc.**

**Liberty** supported the Commission’s review of the “methodologies used to develop step adjustments.” Liberty acknowledged that the step adjustment methods that the Commission has approved in its rates cases differ from the methods approved by the Commission for other utilities - Liberty’s step increases to recover the revenue requirement for specific capital investments made during the relevant year, whereas the other basic step adjustment mechanism looks to changes in the company’s net plant in service. The Company believes that both methods can achieve the intended goals of step adjustments. The Company calculates revenue requirements at the account-level plant addition (See Appendix 1.4). In this process, the model incorporates the Deferred Tax Balance which reduces the Rate Base, which is not the case for the Unutil or Eversource models.

**Unutil** referred to the Commission’s approval of step adjustments for UES and Northern utilizing a “change in net plant” methodology to determine eligible capital investments for inclusion in the step adjustment revenue requirement calculation. Unutil anticipated that the treatment of depreciation expense in the “change in net plant” methodology is likely to be subject to examination in this investigation. The Company uses a unique “change in non-growth net plant” methodology regarding the allocation of annual depreciation expense booked in the investment year between growth and non-growth categories of investment. Unutil maintains that the method of determining depreciation expense for the purposes of calculating revenue requirement for non-growth investment is consistent with commonly applied rate-making principles.

In response to the Commission's record request (RR-7), **Unutil** provided representative models. The Company calculates ending accumulated depreciation by netting depreciation expense against retirements, cost of removal, salvage, and transfers for both growth and non-growth categories of investment. The Company uses the proportion of the investment year’s growth and non-growth addition to allocate the annual depreciation expenses for all vintages, retirements, cost of removal, salvage, and transfers to growth and non-growth categories (See Appendix 1.2).

Citing DE 22-026, Order No. 26,656, containing the Commission’s suggestion that the “change in non-growth net plant” can be determined by

subtracting actual growth plant additions from the total change in the net plant, **Unitil** opined, that it would not result in an accurate calculation of change in the non-growth net plant. The company asserted that step adjustments will not be fully effective and achieve the purposes described in the previous section if the methodology for calculating the revenue requirement, including, inter alia, the treatment of depreciation expense, is not properly designed. Unitil appreciated the opportunity to discuss this critical issue with the Commission in the investigation.

**Eversource** favored a uniform methodology for calculating the revenue requirement change associated with the step adjustment. The Company believes that standardization of the computation of the revenue requirement change to be included in rates would be informative to all parties; would facilitate settlement discussions; and would lead to greater administrative efficiency and regulatory certainty. According to the Company, the step adjustment constitutes a proxy for the change in the rate base, so it should be calculated by updating all components of the rate base, including accumulated depreciation, incremental depreciation expense, property tax expense, the weighted cost of capital and taxes. The company concluded that the step adjustment would constitute a “roll forward” of the rate base from the most recent rate case so that all elements of the rate base maintain parity.

In response to the record request (RR 7), **Eversource** described the mechanism in detail. Unlike Unitil, Eversource excludes “new business”, to calculate Net Plant Asset value which represents the year-over-year change of cumulative capital investments placed in service, adjusted for retirements, accumulated depreciation, etc. It tracks the “new business” starting from the latest rate case separately. So essentially all assets included in the rate cases and associated annual depreciation expenses are recognized in the step adjustment revenue requirement calculations. All accumulated depreciation, and annual depreciation expenses for “New Business” since the latest rate case does not influence the step adjustment revenue requirement (See appendix 1.3).

### Issue 3: The role of the DOE’s Audit Division

#### **The role of the DOE’s Audit Division in step adjustment review proceedings**

**Unitil** expressed its openness to include any Audit Report into evidence in the step adjustments but recommended that it should be done well in advance of a hearing and make a witness available to be cross-examined on the contents of the Audit Report and the process employed to develop the conclusions contained in the Audit Report.

**Eversource** also recommended that the audit report should be subject to normal due process in a contested case consistent with RSA Chapter 541-A. It elaborated further stating that DOE is a party and to the extent that the audit does more than account for the accuracy of booked utility costs, the audit report should not be accepted as a fact in the record without allowing due process.

**Liberty** was also supportive of the Audit Division's review of step adjustments. And suggested that it may occur only after being offered into evidence and subjected to discovery and cross-examination.

### Issue 4: Enhancements of review proceedings

#### **Potential enhancements to review proceedings, including timing of step adjustment filings and proposed rate effective dates.**

**Unitil** and **Liberty** did not propose any enhancements to step adjustment review proceedings. Liberty believes steps could be taken to further streamline the step adjustment process.

**Eversource** supported potential enhancements to step adjustment review proceedings. In terms of the timing of step adjustment filings and proposed rate-effective dates, the Company stated that one objective should be to start rates on the same date to avoid the need for multiple rate changes on customers' bills and recognized the challenge of this approach.

In the RR response, **Eversource** identified three options for conducting step adjustment proceedings on a timely basis:

- 1. Continue the traditional model with longer, specified timelines for implementation following the end of a rate case, or as provided in a rate settlement. During the settlement process, trade-offs are made in devising the ultimate agreement. If the Commission has established set timelines for review of step adjustments following a rate case or rate settlement, the petitioning company and/or the settling parties can work the financial impact of delayed step implementation into the balance of benefits incorporated to the rate filing and/or settlement agreement.*
- 2. Reform the step adjustment to be a reconciling mechanism. In this model, the utility can make a filing and a rate could be allowed to go into effect, subject to further investigation. This is how many reconciling mechanisms work in other state jurisdictions. This provides much greater flexibility in the timeline for investigation of the prudence of capital*

*additions addressed in the step. If costs are disallowed as a result of the further investigation, then adjustments can be made to refund to customers any amounts that should not have been recovered.*

*3. Allow the step adjustment based on a designated or agreed upon amount, for example 80 percent of the forecasted capital additions, and forego the prudence review until the next base-rate proceeding. The utility could be required to file documentation with each step adjustment to demonstrate that the forecast was met or exceeded, thereby warranting the revenue adjustment, but the prudence review would wait for the rate case.*

**Eversource** recommended Option #2 as it removes the time pressure associated with the prudence review, but maintains the transparency of the annual process to review capital additions, and also addresses the fact that the step adjustments are heavily lagged where the base distribution rate increase and associated revenue recovery are not effective until eight months after the calendar year in which the capital projects are placed in service. With respect to applicable timeframes and methodologies for formulating step adjustment petitions, Eversource believes that the process should be linked to an enhanced LCIRP process meeting the criteria provided that the utility's LCIRP is approved in a timely manner and without excess litigation through that enhanced process. These comments on the LCIRP process are no longer relevant following repeal of the LCIRP process by the Legislature in October 2023.

### Issue 5: The role of settlement agreements

#### **The role of settlement agreements (RR-2) in full rate case proceedings in guiding step adjustment filings and criteria, including criteria related to project qualification.**

**Unitil** pointed out that its last seven rate cases have been resolved by settlement, and all included step adjustments as components of a comprehensive stipulation among the settling parties. The Company stated that Step adjustments are an essential tool in the negotiation of comprehensive rate case settlements (i.e., the number of steps, timing of the filing, eligible plant, the method of calculation, customer protections such as a cap on the incremental revenue requirement) which allows the parties additional flexibility in the negotiation of other components that comprise a potential settlement.

**Eversource** believes that the Commission should continue to encourage settlement agreements as a means to resolve contested rate case dockets. It argues that settlement agreements reflect a balance of consideration and



compromise on the key issues by the parties, and facilitate administrative efficiency, and pointed out that New Hampshire's laws and administrative rules favor settlements (RSA 541-A:31; N.H. Code of Administrative Rules Puc 203.15, 203.20). The company also stated the following:

*...If this investigation produces a standardized recommendation on the method to calculate the revenue requirement comprising the annual step adjustments, then parties to a settlement agreement in a future rate could either choose to adopt that methodology or propose an alternate methodology. If the settling parties view an alternative methodology as warranted based on the facts and circumstances of a case, then it would be their burden to support the methodology as just, reasonable and in the public interest. The Commission then has the opportunity to review the settlement and the record of the docket to find that the settlement is just, reasonable and in the public interest and therefore warrants approval...*

**Liberty** believes that agreements that settle full rate proceedings are a proper, and likely the best, forum for establishing the specific contours of the step adjustments that are to follow the rate case.

### Issue 6: The qualification criteria for step adjustments

**Unitil** and **Liberty** consider the current practice to include non-growth capital projects to be qualified for step adjustments appropriate because the revenue requirements associated with these projects are not otherwise offset by new revenues from new customers.

**Eversource** stated that setting the qualification criteria for step adjustments would be informative to all parties; would facilitate settlement discussions; and would lead to greater administrative efficiency and regulatory certainty. Referring to the settlement agreements approved in the recent rate cases of the Eversource Companies, the company finds the standard qualification is reasonable which requires that capital projects must be in service to customers to qualify for inclusion in a step adjustment, and revenue generating customer additions may not be appropriate for inclusion in the step adjustment. The Company identified that changes to the timing of review periods, capping how much may be included in a step, and subjecting all projects to a full prudence review among other measures would be a few ideas for process enhancements to facilitate the Commission's review of step adjustments.



## Issue 7: The appropriateness of reconciliation adjustments

Citing Order No. 26,656 (DE 21-030), where the Commission accepted Unitil’s “change in non-growth net plant” methodology for the purposes of calculating UES’s 2022 step adjustment revenue requirement, “subject to reconciliation,” **Unitil** cautioned that any retroactive application of a different methodology for calculating a step adjustment revenue requirement would violate the well-established rule against retroactive rate making, and “materially and arbitrarily alter the terms of settlement agreements”.

**Liberty** expressed a similar opinion that Step adjustments are not the type of costs that the Commission typically reconciles, such as cost-of-gas costs, renewable portfolio standard costs, and the like.

**Eversource** believes that if the Commission intends to implement the step adjustments as a reconciling mechanism, the mechanics would be different than what is undertaken today as base rates cannot be adjusted on a retroactive basis. Thus, to the extent that recently approved step adjustments have been incorporated into base rates, those steps cannot be reconciled.

To have a longer time period to allow for a prudence review of the capital projects (and potential O&M expense) included in the steps, **Eversource** suggests that this could be accommodated through the implementation of a “reconciling” approach outside of base rates. In that case, the Commission could approve the simultaneous implementation of the new base rates, the adjustment to temporary rates, and the step adjustment amount, with the step adjustment amount collected outside of base rates and subject to later review and reconciliation. To conduct the prudence review prior to allowing recovery to commence in rates charged to customers, then the Commission could set a standard time period of no greater than six months from the filing of the step adjustment for the prudence review; conduct that review; and then put the amount allowed for recovery into base rates (without the need for a reconciling mechanism).

**Eversource** reiterated that if step adjustments are implemented in the future as adjustments to base rates, these adjustments cannot be subject to reconciliation. This need for certainty and finality with respect to the step adjustments is important for the Company.

Issue 8. The relationship between a step increase program and a company's LCIRP planning process<sup>1</sup>

**Eversource** pointed out that the LCIRP in its current state is a forward-looking filing generally identifying a range of projects that are scheduled to be placed in service over the next five years, whereas step adjustments are limited to recovery of a capped dollar amount comprised of specific capital projects in the queue for completion in the respective step adjustment year. Eversource expressed its support for a reformation of the information provided as part of the LCIRP - a more meaningful, holistic indication of the results of the planning process applied to the New Hampshire distribution system and would demonstrate the prudence for plant additions presented in a rate proceeding, or an interim proceeding.

**Unitil** stated that a forward-looking multi-year capital plan submitted during an LCIRP proceeding may be subject to change in a subsequent year, and should not be treated as unalterable, nor should they be used to restrict a company's capital investments. Unitil argued that capital investments that depart from information provided in the LCIRP process cannot be presumptively deemed imprudent or subject to disallowance.

**Liberty** also mentioned the forward-looking characteristics of an LCIRP and the backward-looking nature of step adjustment. Like Unitil the company repeated that the prudence standard cannot be based on the LCIRP.

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<sup>1</sup> We include this section summarizing participants' comments for completeness; however, the section is no longer applicable following the repeal of the LCIRP statute in October, 2023.

# APPENDIX: WATER UTILITY INPUT

**NH Brown Law** stated that small water utilities that do not have capital cost trackers, such as the Water Infrastructure Capital Adjustment Clause or the Qualified Capital Project Adjustment Charge, have successfully used the step adjustment mechanism in the past to: (1) meet their revenue needs after the capital has been put to public use; (2) avoid an earnings or revenue deficiency shortly after processing a rate case; and (3) avoid having to process another rate case to address the newly-added capital on the heels of a recently completed rate case.

**Lakes Region Water Company** believes that Step Adjustments are a critical mechanism to improve service and maintain compliance with DES and PUC drinking water standards. Regarding the methodology and appropriateness of reconciliation adjustments, it mentioned that it has been working with the interested parties to make post-test year adjustments using traditional utility rate-making principles and will continue to do so. It stated that DOE's Audit Division plays an important role in step adjustment proceedings to reduce unnecessary delays. It believes that the qualification criteria for step adjustments should include any costs that would ordinarily be allowed in a rate case within a reasonable time period.

**Pennichuck Water Works, Inc. (PWW), Pennichuck East Utility, Inc. (PEU), and Pittsfield Aqueduct Company, Inc. (PAC)** pointed out that the existing Step Increase mechanisms in place for these companies are under the name of Qualified Capital Project Adjustment Charge (QCPAC) for both Pennichuck Water Works, Inc. and Pennichuck East Utility, Inc. Recently the Commission approved the QCPAC mechanism (replacing the Water Infrastructure and Conservation Adjustment – WICA) for PWW. The QCPAC consists of: (1) the annual principal and interest payments with respect to the applicable capital project debt, multiplied by 1.1; and (2) incremental property taxes associated with the specific capital projects, as determined in the year of the granting of the QCPAC for such projects.

The approved QCPAC process is calculated via annual filings, providing: (1) calculation of the QCPAC surcharge associated with capital investments from the previous year, for which all assets must be used and useful as of December 31 of that previous year; (2) budget information regarding proposed capital projects for the current year; and (3) a detailed forecast of anticipated capital project expenditures for the subsequent two years, for informational purposes only. The Companies believe the current QCPAC criteria, as approved for PWW and PEU are appropriate and adequate. It also emphasized the role of

DOE's Audit Division is crucial in the evaluation of the Company's QCPAC submissions, capital budgets, and projects in determining whether the projects were prudent, used, useful, and placed in service during the prior year.

# Appendix 1.1

Components included in the Company's Other Capital Cost Recovery Tracking Mechanisms in Unitil's Other Jurisdictions

Component	Maine TIRA	FGE-E CCA	FGE-E Solar	FGE-E Grid Mod	FGE-G GSEP
Pre-Tax Rate of Return	✓	✓	✓	✓	✓
Depreciation Expense	✓	✓	✓	✓	✓
Property Taxes	✓	✓	✓	✓	✓
O&M Expense			✓	✓	
O&M Savings	✓				✓
Concurrent Recovery			✓	✓	✓

# Appendix 1.2

## UES Model

IR 22-048  
 Unfil Initial  
 Comments  
 ATTACHMENT A

	<u>Rate</u>	<u>Total</u>	<u>Growth</u>	<u>Non-</u>
	<u>Growth</u>			
Plant Additions		\$ 19,929,755	\$ 3,332,692	\$ 16,597,063
		100.00%	16.72%	83.28%
Depreciation Expense		\$ 10,413,124	\$ 1,741,303	\$ 8,671,822
		100.00%	16.72%	83.28%
Cost of Removal		\$ (642,545)	\$ (40,873)	\$ (601,671)
		100.00%	6.36%	93.64%
Change in Net Plant		\$ 10,159,176	\$ 1,632,262	\$ 8,526,912
Pre-Tax Return	8.99%	\$ 913,455	\$ 146,764	\$ 766,691
Depreciation				
Plant Additions		\$ 19,929,755	\$ 3,332,692	\$ 16,597,063
Depreciation Expense	3.46%	\$ 689,570	\$ 115,311	\$ 574,258
Property Tax				
Change in Net Plant		\$ 10,159,176	\$ 1,632,262	\$ 8,526,912
Property Tax Expense	0.66%	\$ 67,051	\$ 10,773	\$ 56,278
Amortization on Post Test-Year Projects		\$ 157,739	\$ -	\$ 157,739
		100.00%	0.00%	100.00%
Revenue Requirement		\$ 1,827,814	\$ 272,848	\$ 1,554,966

# Appendix 1.3

## Eversource Model

Public Service Company of New Hampshire  
d/b/a Eversource Energy  
Docket No. DE 19-057  
Settlement Agreement - Step 1 Revenue  
Requirement

Attachment ELM/EAD-1 (Revised per TS 4-002)

Page 1 of 6

Attachment PUC 1-007(a)

**PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE**  
**CALCULATION OF STEP ADJUSTMENT #1 (EXCLUDES NEW BUSINESS)**

Line	Description	Year-Ending 12/31/2018 (A)	(effective 1/1/21) Year-Ending 12/31/2019 (B)	Reference
	Total Utility Plant in Service	\$ 2,171,045,400	\$ 2,250,917,651	Attachment ELM/EAD-1, Page 2, Line 1 Attachment ELM/EAD-1, Page 2, Line 2 Line 1 - Line 2
	Accumulated Provision for Depreciation Net Utility Plant	<u>602,426,195</u> <u>1,568,619,205</u>	<u>610,587,812</u> <u>1,640,329,840</u>	
4	Gross Plant		79,872,251	Line 1 Col. (B) - Line 1 Col. (A)
5	Change Net Plant Change		71,710,635	Line 3 Col. (B) - Line 3 Col. (A)
6	Rate of Return		6.87%	Attachment ELM/EAD-1, Page 3, Line 11
7	Gross Revenue Conversion Factor		<u>1.37142</u>	Attachment ELM/EAD-1, Page 4, Line 7
8	Return		6,755,652	Line 5 x Line 6 x Line 7
9	Depreciation Rate		3.15%	Attachment ELM/EAD-1, Page 5, Line 71
10	Depreciation		2,258,885	Line 5 x Line 9
11	Property Tax Rate		2.00%	Attachment ELM/EAD-1, Page 6, Line 3
12	Property Taxes		1,595,774	Line 4 x Line 11
13	Total Revenue Requirement		\$ <u>10,610,311</u>	(A) Line 8 + Line 10 + Line 12
14	Step 1 Revenue Requirement Cap per Settlement Agreement		\$ 11,000,000	
15	<b>Step 1 Revenue Increase (\$000s)</b>		\$ <u>10,610</u>	Line 13/1000



# REPORT ON STEP ADJUSTMENT METHODOLOGY AND PROCESS

Public Service Company of  
New Hampshire  
d/b/a Eversource Energy  
Docket No. DE 19-057  
Settlement Agreement -  
Step 1 Revenue  
Requirement

Attachment ELM/EAD-1  
(Revised per TS 4-002)

Page 2 of 6

Attachment PUC 1-007(a)

## PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE DISTRIBUTION PLANT

Line	Description	Year-Ending 12/31/2018 (A)	Year-Ending 12/31/2019 (B)	Reference
1	Total Utility Plant In Service	\$ 2,171,045,400	\$ 2,250,917,651	FERC Form 1 adj to excl New Business
2	Accumulated Provision for Depreciation	602,426,195	610,587,812	FERC Form 1 adj to excl New Business
3	Net Utility Plant	<u>1,568,619,205</u>	<u>1,640,329,840</u>	Line 1 - Line 2
4	Gross Distribution Plant Change (year over year)		<u>79,872,251</u>	Line 1 Col. (B) - Line 1 Col. (A)
5	Net Distribution Plant Change (year over year)		<u>71,710,635</u>	Line 3 Col. (B) - Line 3 Col. (A)
6	Beginning Plant Balance		2,171,045,400	Line 9 Col. (A)
7	Additions (excluding New Business)		124,926,620	FERC Form 1 adj to excl New Business, TS 4-002
8	Retirements (excluding New Business)		(45,054,369)	FERC Form 1 adj to excl New Business
9	Ending Plant Balance	<u>\$ 2,171,045,400</u>	<u>\$ 2,250,917,651</u>	Line 6 + Line 7 + Line 8

# REPORT ON STEP ADJUSTMENT METHODOLOGY AND PROCESS

## Appendix 1.4 Liberty Model

**Liberty Utilities (EnergyNorth Natural Gas) Corp. d/b/a Liberty**  
**Step 2 Adjustment - Revenue Requirement**  
(Revised per Audit Adjustments and Depreciation Study)

Line	Description	IT	Transmission Mains	Distribution Mains	Services	Meters	Transportation	GEN-Tools-Shop- Garage Equip	Total
<i>FERC Account</i>		303	367	376	380	381	392	394	
1	Capital Spending	\$ 63,515	\$ 22,551,295	\$ 511,291	\$ 605,038	\$ 2,097,505	\$ 970,393	\$ 247,679	\$ 27,046,715
2									
3	Deferred Tax Calculation								
4	Tax Method	MACRS5	MACRS20	MACRS20	MACRS20	MACRS20	MACRS5	MACRS7	
5	Tax Depreciation Rate	20.00%	3.75%	3.75%	3.75%	3.75%	20.00%	14.29%	
6									
7	Bonus Depreciation @ 0.00%	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
8									
9	Tax Basis	\$ 63,515	\$ 22,551,295	\$ 511,291	\$ 605,038	\$ 2,097,505	\$ 970,393	\$ 247,679	\$ 27,046,715
10	MACRS Depreciation	\$ 12,703	\$ 845,674	\$ 19,173	\$ 22,689	\$ 78,656	\$ 194,079	\$ 35,393	\$ 1,208,367
11									
12	Tax Depreciation - Federal	\$ 12,703	\$ 845,674	\$ 19,173	\$ 22,689	\$ 78,656	\$ 194,079	\$ 35,393	\$ 1,208,367
13	Tax Depreciation - State	\$ 12,703	\$ 845,674	\$ 19,173	\$ 22,689	\$ 78,656	\$ 194,079	\$ 35,393	\$ 1,208,367
14									
15	Book Depreciation Rate	20.00%	1.92%	1.92%	3.20%	3.33%	20.00%	5.26%	
16	Book Depreciation	\$ 12,703	\$ 432,985	\$ 9,817	\$ 19,361	\$ 69,847	\$ 194,079	\$ 13,028	\$ 751,819
17									
18	Tax over (under) Book - Federal	\$ -	\$ 412,689	\$ 9,357	\$ 3,328	\$ 8,810	\$ -	\$ 22,365	\$ 456,548
19	Tax over (under) Book - State	0	412,689	9,357	3,328	8,810	0	22,365	456,548
20	Deferred Taxes - Federal @ 21.00%	0	86,665	1,965	699	1,850	0	4,697	95,875
21	Deferred Taxes - State @ 7.60%	0	31,364	711	253	670	0	1,700	34,698
22	Deferred Tax Balance @ 0.00%	\$ -	\$ 118,029	\$ 2,676	\$ 952	\$ 2,520	\$ -	\$ 6,397	\$ 130,573
23									
24	Rate Base Calculation								
25	Plant in Service	\$ 63,515	\$ 22,551,295	\$ 511,291	\$ 605,038	\$ 2,097,505	\$ 970,393	\$ 247,679	\$ 27,046,715
26	Accumulated Depreciation	(12,703)	(432,985)	(9,817)	(19,361)	(69,847)	(194,079)	(13,028)	(751,819)
27	Deferred Tax Balance	0	(118,029)	(2,676)	(952)	(2,520)	0	(6,397)	(130,573)
28	<b>Rate Base</b>	<b>\$ 50,812</b>	<b>\$ 22,000,281</b>	<b>\$ 498,798</b>	<b>\$ 584,725</b>	<b>\$ 2,025,139</b>	<b>\$ 776,314</b>	<b>\$ 228,254</b>	<b>\$ 26,164,323</b>
29									
30	Revenue Requirement Calculation								
31	Return on Rate Base @ 8.76%	\$ 4,451	\$ 1,927,335	\$ 43,697	\$ 51,225	\$ 177,412	\$ 68,009	\$ 19,996	\$ 2,292,126
32	Depreciation Expense	12,703	432,985	9,817	19,361	69,847	194,079	13,028	751,819
33	Property Tax @ \$6.60 per \$1000	419	148,839	3,375	3,993	13,844	6,405	1,635	178,508
34	<b>Annual Revenue Requirement</b>	<b>\$ 17,574</b>	<b>\$ 2,509,158</b>	<b>\$ 56,888</b>	<b>\$ 74,579</b>	<b>\$ 261,103</b>	<b>\$ 268,492</b>	<b>\$ 34,659</b>	<b>\$ 3,222,453</b>
35									
36	Keene CNG Phase I Expansion Revenue Requirement Adjustment (per risk sharing calculation)								(21,962)
37	<b>Total Annual Revenue Requirement Related 2021 Plant Additions</b>								<b>3,200,491</b>
	Cap to Revenue Requirement per Settlement Agreement in DG 20-105								3,200,000
	Adjustment to Depreciation Expense Schedule A page 2								(660,216)
38	<b>Resulting Total Annual Revenue Requirement</b>								<b>\$ 2,539,784</b>
39									
40									
41									<b>Capped at \$3,200,000</b>
42	Rate of Return Calculation*	Capital Structure	Cost of Capital	Weighted Cost of Capital	Tax Rate	Pre-Tax WACC			
43	Equity	52.0%	9.30%	4.84%	27.004%	6.63%			
44	Debt	48.0%	4.42%	2.12%		2.12%			
45		100.0%	13.72%	6.96%		8.76%			
46	*As approved in the Settlement Agreement in Docket No. DG 20-105 with exception of the effective tax rate								