

# **ATTACHMENT A**

## Gurkas, Lisa

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**From:** Gurkas, Lisa  
**Sent:** Tuesday, October 03, 2017 11:15 AM  
**To:** Gurkas, Lisa  
**Subject:** FW: Straw Proposals  
**Attachments:** Infrastructure Straw Proposal (4-26-2017).pdf; Provisional Rates Straw Proposal (4-26-17).pdf

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**From:** Gaglioti, Maria [<mailto:Maria.Gaglioti@bpu.nj.gov>]  
**Sent:** Wednesday, April 26, 2017 3:55 PM  
**To:** Stefanie Brand; Shelly Massey; [tamara.linde@pseq.com](mailto:tamara.linde@pseq.com); [joseph.accardo@pseq.com](mailto:joseph.accardo@pseq.com); [scocchi@sjindustries.com](mailto:scocchi@sjindustries.com); [smitchell@sjindustries.com](mailto:smitchell@sjindustries.com); [adembia@njng.com](mailto:adembia@njng.com); [pkeefe@southernco.com](mailto:pkeefe@southernco.com); [geisenstark@windelsmarx.com](mailto:geisenstark@windelsmarx.com); Lauren M. Lepkoski ([llepkoski@firstenergycorp.com](mailto:llepkoski@firstenergycorp.com)); [philip.passanante@pepcoholdings.com](mailto:philip.passanante@pepcoholdings.com); [westark@pepcoholdings.com](mailto:westark@pepcoholdings.com); [jmeyer@riker.com](mailto:jmeyer@riker.com); Carley, John L. - Regulatory; [jkooper@middlesexwater.com](mailto:jkooper@middlesexwater.com); [robert.brabston@amwater.com](mailto:robert.brabston@amwater.com); [dgern@gordonscornerwater.com](mailto:dgern@gordonscornerwater.com); [flwcoffice@optonline.net](mailto:flwcoffice@optonline.net); [lwaters@acsewerage.com](mailto:lwaters@acsewerage.com); [jhildabrant@aquaamerica.com](mailto:jhildabrant@aquaamerica.com); [jim.cagle@unitedwater.com](mailto:jim.cagle@unitedwater.com); [gary.prettyman@suez-na.com](mailto:gary.prettyman@suez-na.com); [james.mastrokalos@suez-na.com](mailto:james.mastrokalos@suez-na.com); [jmf1294@yahoo.com](mailto:jmf1294@yahoo.com); [movw@goes.com](mailto:movw@goes.com); [j.hosking@roxburywater.com](mailto:j.hosking@roxburywater.com); [SamSJF@verizon.net](mailto:SamSJF@verizon.net); [glorstuart@comcast.net](mailto:glorstuart@comcast.net); [dbsjr@simmonstransport.com](mailto:dbsjr@simmonstransport.com); [ahendry@njua.com](mailto:ahendry@njua.com); Goldenberg, Steven ([SGoldenberg@foxrothschild.com](mailto:SGoldenberg@foxrothschild.com)); [eliebman@aarp.org](mailto:eliebman@aarp.org); [geoffrey.gersten@dol.lps.state.nj.us](mailto:geoffrey.gersten@dol.lps.state.nj.us)  
**Subject:** Straw Proposals

Attached please find the straw proposals issued by BPU today.

Sincerely,

*Maria A. Gaglioti*

Executive Assistant  
Office of the Chief Counsel  
New Jersey Board of Public Utilities  
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## **ANNOUNCEMENT OF STAKEHOLDER PROCESS**

In recent years, the New Jersey Board of Public Utilities (“Board”) has approved in excess of \$3 billion in “Infrastructure Programs” administered by energy and water utilities related to resiliency and reliability. The Board has approved the Distributed System Improvement Charge (“DSIC”) for water companies, and separately, large Infrastructure Programs to implement repairs and replacements after Superstorm Sandy and Hurricane Irene. While each Infrastructure Program has been handled by the Board on an individual basis, the Board has nevertheless developed certain requirements and processes to protect ratepayers and facilitate replacement and repair of aging utility infrastructure.

Board Staff has been directed to establish a stakeholder process to receive comments and proposals regarding potential regulations and filing requirements for additional infrastructure projects that will not be included as part of a utility’s Capital Expenditures (“CapEx”). After consideration by the Board, this straw proposal may result in a rule applicable to a utility that wishes to establish or expand an Infrastructure Program.

The straw proposal concerning Infrastructure Programs will be the subject of a stakeholder meeting to be held on May 4, 2017 at 1:00 pm at the Board’s offices, located at 44 South Clinton Avenue, Trenton, NJ 08625. Public comments are invited. Written comments are also invited and must be submitted to Irene Kim Asbury, Secretary, New Jersey Board of Public Utilities, 44 South Clinton Avenue, 3<sup>rd</sup> Floor, Suite 314, CN 350, Trenton, New Jersey 08625, on or before May 12, 2017.

The following topics are included for discussion and comment at the stakeholder meeting and by written submissions:

1. The Infrastructure Program may be for a period of five (5) years or less.
2. The Infrastructure Programs are voluntary.

3. Any Infrastructure Program must be incremental to the Utility's average CapEx over the prior five years.
4. A filing in support of an Infrastructure Program must:
  - a) Include projected annual CapEx budgets for a five-year period, broken down by major category of expenditures;
  - b) Specify the projects, and include descriptions of project objectives and detailed cost estimates;
  - c) Include an Infrastructure Program budget establishing the maximum (or "cap") that can be spent (although year to year variations of ten percent will be allowed, and larger variations may be permitted with Board approval);
  - d) Include similar projects within the utility's CapEx budget equal to ten percent of the amount of the Infrastructure Program; and be supported with semi-annual status reports for project management oversight purposes.
5. The projects within the Infrastructure Program must be related to reliability, resiliency, and/or replacement and may include, but are not limited to:
  - a) Replacement of Gas Utilization Pressure Cast Iron mains with elevated pressure mains and associated services;
  - b) Replacement of Gas bare steel and coated steel mains and services;
  - c) Installation of Gas Excess Flow Valves where necessary;

- d) Electric distribution automation investments, for example, SCADA equipment, relays, reclosers, Volt/VAR control, communications networks, and Distribution Management System Integration;
  - e) Resiliency or Redundancy Projects; and
  - f) Projects deemed by the Board to involve critical interconnections of a utility plant.
6. The projects must be non-revenue producing. Blanket Infrastructure Programs will not be eligible.
  7. Cost recovery will be through a surcharge mechanism that will allow accelerated recovery.
  8. The Infrastructure Program must include a cost benefit analysis.
  9. The maximum annual increase in rates attributable to an Infrastructure Program will be two percent.
  10. For combination utilities, separate gas and electric Infrastructure Programs may be established, each with their own respective spending caps.
  11. Allowance for Funds Used During Construction ("AFUDC") would be allowed but not deferred accounting once facilities are in service.
  12. The utilities will be allowed to file rate recovery petitions on a semi-annual basis provided at least ten percent of the Infrastructure Program's costs were in service during the semi-annual period.

13. Rates will be provisional, with prudence to be determined in the next base rate case, which will be required to be filed no later than five years after the approval of the Infrastructure Program.
14. An annual earnings test shall be required, which shall include an unadjusted cost and revenue study.
15. If the calculated Return on Equity ("ROE") exceeds the allowed ROE from the last base rate case by fifty basis points, there will be no accelerated recovery for the next six months and until a new calculation shows no return over the fifty basis points.
16. Water utilities may use this method for infrastructure improvements or may use the Board's DSIC rules.

## **ATTACHMENT B**

**NOT FOR PUBLICATION WITHOUT THE  
APPROVAL OF THE APPELLATE DIVISION**

This opinion shall not "constitute precedent or be binding upon any court."  
Although it is posted on the internet, this opinion is binding only on the  
parties in the case and its use in other cases is limited. R.1:36-3.

SUPERIOR COURT OF NEW JERSEY  
APPELLATE DIVISION  
DOCKET NO. A-1153-14T1

IN THE MATTER OF THE BOARD'S  
REVIEW OF THE APPLICABILITY  
AND CALCULATION OF A  
CONSOLIDATED TAX ADJUSTMENT.

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Argued October 25, 2016 — Decided September 18, 2017

Before Judges Fisher, Ostrer and Vernoia.

On appeal from the New Jersey Board of Public  
Utilities, Docket No. EO12121072.

Diane Schulze argued the cause for appellant  
Division of Rate Counsel (Stefanie A. Brand,  
Director, attorney; Ms. Schulze and Christine  
M. Juarez, on the briefs).

Carolyn A. McIntosh, Deputy Attorney General,  
argued the cause for respondent New Jersey  
Board of Public Utilities (Christopher S.  
Porrino, Attorney General, attorney; Andrea M.  
Silkowitz, Assistant Attorney General, of  
counsel; Ms. McIntosh, on the brief).

Stephen B. Genzer argued the cause for  
respondent Aqua New Jersey, Inc., and United  
Water New Jersey, Inc. (Saul Ewing LLP,  
attorneys; Mr. Genzer, on the brief).

Lawrence S. Lustberg argued the cause for  
respondent Atlantic City Electric Company  
(Gibbons PC, attorneys; Mr. Lustberg and  
Amanda B. Protes, on the briefs).



Gregory Eisenstark argued the cause for respondent Jersey Central Power & Light Company (Windels Marx Lane & Mittendorf, LLP, attorneys; Mr. Eisenstark, on the brief).

Ira Megdal argued the cause for respondent New Jersey-American Water Company, Inc. (Cozen O'Connor, PC, attorneys; Mr. Megdal and Mark Lazaroff, on the brief).

James C. Meyer argued the cause for respondent New Jersey Utilities Association (Riker Danzig Scherer Hyland & Perretti, LLP, attorneys; Mr. Meyer, of counsel and on the brief; Diane N. Hickey, on the brief).

Fox Rothschild LLP, attorneys for respondent New Jersey Large Energy Users Coalition (Steven S. Goldenberg, of counsel and on the brief).

Cullen and Dykman LLP, attorneys for respondent Pivotal Utility Holdings, Inc., (Kenneth T. Maloney, on the brief).

Janine G. Bauer argued the cause for amicus curiae AARP (Szaferman, Lakind, Blumstein & Blader, PC, attorneys; Ms. Bauer, on the brief).

PER CURIAM

The Director of the Division of Rate Counsel appeals the Board of Public Utilities' final order revising its policy for calculating the consolidated tax saving adjustment (CTA) the Board utilizes in part to determine just and reasonable utility rates.

Rate Counsel and other interested parties<sup>1</sup> argue the revised CTA is not supported by adequate findings of fact, is not founded on sufficient evidence in the record, and constitutes a rule that was not enacted in accordance with the Administrative Procedure Act (APA), N.J.S.A. 52:14B-1 to -15, and due process requirements. The Board, and respondents, the New Jersey Utilities Authority and various utility companies<sup>2</sup> contend the Board's adoption of the revised CTA did not constitute rulemaking requiring compliance with the APA, is supported by the evidentiary record, and constitutes a proper exercise of the Board's discretion. Because we conclude the Board's adoption of the CTA constitutes rulemaking and the Board failed to comply with the APA's requirements, we reverse.

### I.

The Board is charged with supervising and regulating public utility companies, N.J.S.A. 48:2-13(a), and setting "just and reasonable" rates for those utilities, N.J.S.A. 48:2-21(b)(1).

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<sup>1</sup> Respondent New Jersey Large Energy Users Coalition and amicus American Association of Retired People (AARP) filed briefs supporting Rate Counsel's appeal. The Coalition participated in the proceeding before the Board. We granted AARP leave to participate in the appeal as amicus curiae.

<sup>2</sup> The respondent utility companies are Aqua New Jersey Inc., United Water New Jersey Inc., Atlantic City Electric Company, Jersey Central Power & Light Company, American Water Company, Inc., and Pivotal Utility Holdings, Inc.

The Division of Rate Counsel is a quasi-independent agency authorized by statute to represent the interests of utility ratepayers in rate-setting matters before the Board. N.J.S.A. 52:27EE-48(a); I/M/O Provision of Basic Generation Serv., 205 N.J. 339, 360 (2011).

To obtain an increase in utility rates, a utility company must petition the Board and prove that an increase is just and reasonable. N.J.S.A. 48:2-21(d). To sustain its burden of proof, a utility must establish "(1) the value of its property or the rate base, (2) the amount of its expenses, including operations, income taxes, and depreciation, and (3) a fair rate of return to investors." In re N.J. Am. Water Co., 169 N.J. 181, 188 (2001).

A company's "rate base" is "the fair value of the property of the public utility that is used and useful in [providing the regulated] public service." In re Petition of Pub. Serv. Coordinated Transport, 5 N.J. 196, 217 (1950). Reasonable rates for the service are generally set at an amount meant to "cover the utilities' expenses plus a return on the shareholders' investment," that is, an amount that permits "the public utility to earn a fair return on its rate base." Penpac, Inc. v. Passaic Cty. Utils. Auth., 367 N.J. Super. 487, 506 (App. Div.), certif. denied, 180 N.J. 457 (2004).

In an assessment of a utility's claimed expenses, a reasonable

rate shall be based only on "actual operating expenses . . . , and not for hypothetical expenses which did not and foreseeably will not occur." In re N.J. Power & Light Co., 9 N.J. 498, 528 (1952). The calculation of a utility company's tax expenses for use in the determination of its rate base is controlled "only by [its] real tax" expense, "rather than that which is purely hypothetical." Lambertville Water Co. v. N.J. Bd. of Public Util. Comm'rs, 153 N.J. Super. 24, 28 (App. Div. 1977), rev'd in part on other grounds, 79 N.J. 449, 458 (1979).

The Board has used a CTA to calculate the real tax expenses of utility companies whose federal tax returns are filed as part of the consolidated tax returns of their parent companies. The filing of a consolidated tax return permits the parent to offset the tax liability resulting from the profits of one or more of its affiliates against the losses of other affiliates. This reduces the tax obligations of each member of the group and saves each member a portion of the tax obligation they would have incurred if they filed their returns separately. Our Supreme Court has made clear that ratepayers must share in the resulting benefit to the utility. N.J. Power & Light Co., supra, 9 N.J. at 528. Otherwise, ratepayers would pay a utility's hypothetical and not real tax expenses. Ibid.

The Board has "the power and function to take into

consideration the tax savings flowing from the filing of [a] consolidated return and determin[e] what proportion of the consolidated tax is reasonably attributable to" the utility. Lambertville Water Co., supra, 153 N.J. Super. at 28. The Board is not bound by any particular methodology and may exercise its sound discretion to determine and make appropriate adjustments for a company's actual tax liability and thus ensure the reasonableness of the resultant rates. In re Revision of Rates Filed by Toms River Water Co., 158 N.J. Super. 57, 60-61 (App. Div. 1978), rev'd on other grounds, 82 N.J. 201 (1980). The Board has exercised its authority by using the CTA as the means to share with the company's ratepayers the benefits of the tax savings resulting from the consolidated tax filings.

#### The CTA Methodology

Prior to the Board's order challenged on appeal, the Board used what has been characterized as "the Rockland methodology"<sup>3</sup> to determine the CTA. Under the Rockland methodology, calculation of the CTA first requires a determination of the net taxable gains

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<sup>3</sup> The Rockland methodology was developed in a series of rate cases culminating in I/M/O The Verified Petition Of Rockland Electric Company, BPU Docket No. ER02100724 (Apr. 20, 2004) (slip op. at 62-64); see also In re Petition of Jersey Cent. Power & Light Co., BRC Docket No. ER91121820J (June 15, 1993) (slip op. at 8); In re Petition of Atlantic City Elec. Co., BRC Docket No. ER90091090J (Oct. 20, 1992) (slip op. at 6).

and losses of all of the companies on the consolidated federal tax return for each year during a review period which begins in 1991 and ends in the most recent tax year. The companies that experienced net taxable gains are grouped together and their net taxable gains are aggregated. The companies that experienced net taxable losses are grouped together and their net taxable losses are aggregated. The aggregated losses are then multiplied by the applicable federal income tax rate to determine the group's consolidated tax benefit. The amount of the consolidated tax benefit is then allocated proportionately to the companies that experienced net taxable gains based on their proportionate share of the total aggregated gains.

If application of the Rockland methodology establishes that a New Jersey utility experienced net taxable gains during the review period, its proportionate share of the consolidated tax benefit constitutes its CTA. The amount of the CTA affects the utility's rate base because the larger the tax savings adjustment under the CTA, the greater the reduction in the utility's rate base.<sup>4</sup>

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<sup>4</sup> The CTA does not result in a dollar-for-dollar reduction in the utility's tax expenses that are used to calculate the rate base. The CTA tax savings are treated as a loan from ratepayers, whose payments contributed to the profits that would otherwise have been taxed if not for the consolidated filing. Jersey Cent. Power &

### The Board Modifies the Rockland Methodology

In January 2013, the Board approved an order opening a generic proceeding to review the CTA. The Board noted that its current CTA methodology had been used for approximately twenty years and that federal tax laws and many of the companies' corporate structures had changed. The Board sought "input from stakeholders, including the utilities, customers, and . . . Rate Counsel" to determine the Board's use of the CTA, the calculation of tax savings from the filing of consolidated returns, the manner in which the savings should be shared with the utility companies and ratepayers, and if a rulemaking proceeding should be initiated. The order was posted to the Board's website and circulated to those on its generic stakeholder service list.

In March 2013, the Board posted an official Notice of Opportunity to Comment on its website and circulated it to stakeholders on its service list. The notice requested comments concerning the CTA and responses to requests for information about the stakeholders' respective positions on whether a CTA should be

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Light Co., supra, slip op. at 8. The parent company gains use of those profits earlier than it otherwise would have, and the CTA, in turn, compensates ratepayers for the time-value of their money by adjusting the company's rate base in an amount intended to prospectively credit ratepayers for the carrying costs of the loan. Petition of Atlantic City Elec. Co., supra, slip op. at 6.

utilized and what changes should be made to the CTA. The Board requested that the utility companies calculate their current CTA using the Rockland methodology and include, if applicable, the CTA included in the company's last rate base case. The notice advised that following the Board's review of the responses, it would announce a schedule of hearings to provide all interested parties with the opportunity to provide testimony on CTA issues.

The New Jersey Utilities Authority (NJUA) submitted comments on behalf of its members and various utility companies also submitted written comments. They advocated for the abolition of the CTA, arguing that the adjustment had become arbitrary due to an ever-expanding review period that used 1991 as its fixed starting point, and due to the CTA calculation's inclusion of companies that no longer participated in the consolidated income tax filings. They also asserted that application of the CTA adversely affected the utility companies' ability to attract capital and other investments necessary to ensure the safe and efficient provision of their regulated services.

The utility companies and the NJUA further noted that the relatively small CTAs that resulted from application of the methodology when it was first implemented had been replaced by a CTA that in one case was more than forty times higher. They urged the elimination of the CTA and argued that if the Board continued



its use, the review period should be reduced to as few as three years, electric company transmission assets and other operations should be removed from the analysis because they are not regulated by the Board, and companies that have been divested, dissolved, or are otherwise inactive should be excluded from the calculation.

Rate Counsel also submitted comments acknowledging that the length of the review period could result in inappropriately large adjustments and that changes in the tax code during the twenty years since the adoption of the methodology might impact the propriety of the calculation. Rate Counsel recommended that the CTA be reevaluated and adjusted based on utility specific data in fourteen different areas. Rate Counsel also urged that adoption of a revised CTA be completed through formal rulemaking.

In July 2013, the Board issued a Notice of Opportunity to Provide Additional Information, requesting that the utility companies provide data in each of the fourteen areas suggested by Rate Counsel. The notice further advised that following its review of the requested data, the Board would schedule a hearing to provide interested parties with an opportunity to testify concerning the CTA.

In November 2013, the Board issued a letter request for data concerning the taxable gains and losses for the utility companies and their affiliates for each calendar year from 1991 through

2012, and similar information from electric and gas companies broken down into gains and losses attributable to their separate electric and gas operations.

Based on the information and comments received during the process, at the Board's June 2014 meeting its staff recommended the retention of the Rockland methodology for calculation of the CTA with the following three revisions: (a) reduction of the review period to a fixed span of five calendar years; (b) an allocation of the benefits of consolidated tax savings with the utility company receiving seventy-five percent of the savings and the ratepayers receiving twenty-five percent; and (3) the exclusion of electric company transmission assets from the CTA calculation. The Board published notice of the proposed policy on its website and in the New Jersey Register, 46 N.J.R. 1657(a) (July 7, 2014), and distributed the notice to its service list, advising that public comments would be received until August 18, 2014.

The NJUA, the utility companies, Rate Counsel and the New Jersey Large Energy Users Coalition submitted comments. At its October 2014 meeting, the Board considered the recommended revisions and issued a final decision adopting them. The Board ordered that the CTA Rockland methodology would remain in effect with the following modifications:

1. The review period for the calculation shall be for five calendar years including any complete year that is included in the test year.

2. The [CTA] based on that review period shall be allocated so that the revenue requirement of the company is reduced by 25% of the adjustment; and

3. Transmission assets of the [electric distribution companies] would not be included in the calculation of the CTA.

The Board further ordered that the modified CTA would be utilized in all pending and future rate cases. The Board permitted the reopening of cases to permit recalculation of the CTA where the record was closed but the Board had not yet rendered a final decision. The Board's decision and order was entered on October 22, 2014. Corrective orders were entered on November 3, 2014 and again on December 17, 2014. Rate Counsel appealed.

## II.

Rate Counsel, the Coalition and amicus AARP assert that the Board's decision and order must be reversed because the Board was obligated to promulgate the CTA modifications through formal rulemaking in accordance with the APA. N.J.S.A. 52:14B-4. They contend the Board's order establishes a uniform policy defining the CTA methodology and, therefore, it establishes a rule that can only be adopted in accordance with the APA. In its decision, the Board found that rulemaking was not required because it had

"flexibility to determine how to proceed in matters presented to it, and [could] use its discretion to choose the most appropriate manner, including by contested case, rulemaking or informal process, based on the issues raised and the potential effects of the resolution." The Board, the NJUA and the utility companies do not dispute that the Board did not comply with the APA's procedures for rulemaking, but they contend rulemaking was not required because the CTA does not establish the rates, and application of the CTA can be adjusted in rate cases to ensure that the Board fulfills its obligation to set fair and reasonable rates. See N.J.S.A. 48:2-21(b)(1).

"Administrative agencies possess wide latitude in selecting the appropriate procedures to effectuate their regulatory duties and statutory goals." In re Auth. For Freshwater Wetlands Statewide Gen. Permit 6, Special Activity Transition Area Waiver For Stormwater Mgmt., Water Quality Certification, 433 N.J. Super. 385, 413 (App. Div. 2013); accord In re Request for Solid Waste Util. Customer Lists, 106 N.J. 508, 519 (1987). "[A]gencies enjoy great leeway when selecting among rulemaking procedures, contested hearings, or hybrid informal methods in order to fulfill their statutory mandates." Provision of Basic Generation Serv., supra, 205 N.J. at 347. However, "[a]n agency's ability to select procedures it deems appropriate is limited by 'the strictures of

due process and of the [APA].'" In re Consider Distrib. of Casino Simulcasting Special Fund, 398 N.J. Super. 7, 16 (App. Div. 2008) (quoting Request for Solid Waste Util. Customer Lists, supra, 106 N.J. at 519).

An agency's "discretion to act formally or informally is not absolute." In re N.J.A.C. 7:1B-1.1 Et Seq., 431 N.J. Super. 100, 133 (App. Div.), certif. denied, 216 N.J. 8 (2013). "If an agency determination or action constitutes an 'administrative rule,' then its validity requires compliance with the specific procedures of the APA that control the promulgation of rules." Auth. For Freshwater Wetlands Statewide Gen. Permit 6, supra, 433 N.J. Super. at 413 (quoting Airwork Serv. Div. v. Div. of Taxation, 97 N.J. 290, 300 (1984), cert. denied, 471 U.S. 1127, 105 S. Ct. 2662, 86 L. Ed. 2d 278 (1985)); accord Provision of Basic Generation Serv., supra, 205 N.J. at 347.

"Agencies should act through rulemaking procedures when the action is intended to have a 'widespread, continuing, and prospective effect,' deals with policy issues, materially changes existing laws, or when the action will benefit from rulemaking's flexible fact-finding procedures." Provision of Basic Generation Serv., supra, 205 N.J. at 349-50 (quoting Metromedia, Inc. v. Div. of Taxation, 97 N.J. 313, 329-31 (1984)). To determine if the APA

rulemaking requirements are implicated, we apply the following analysis:

[A]n agency determination must be considered an administrative rule . . . if it appears that the agency determination, in many or most of the following circumstances, (1) is intended to have wide coverage encompassing a large segment of the regulated or general public, rather than an individual or a narrow select group; (2) is intended to be applied generally and uniformly to all similarly situated persons; (3) is designed to operate only in future cases, that is, prospectively; (4) prescribes a legal standard or directive that is not otherwise expressly provided by or clearly and obviously inferable from the enabling statutory authorization; (5) reflects an administrative policy that (i) was not previously expressed in any official and explicit agency determination, adjudication or rule, or (ii) constitutes a material and significant change from a clear, past agency position on the identical subject matter; and (6) reflects a decision on administrative regulatory policy in the nature of the interpretation of law or general policy.

[Metromedia, supra, 97 N.J. at 331-32.]

"The factors need not be given the same weight, and some factors will clearly be more relevant in a given situation than others," Doe v. Poritz, 142 N.J. 1, 97 (1995), and "[n]ot all factors need be present for an agency action to qualify as an administrative rule," Provision of Basic Generation Serv., supra, 205 N.J. at 350. "The pertinent evaluation focuses on the importance and weight of each factor, and is not based on a

quantitative compilation of the number of factors which weigh for or against labeling the agency determination as a rule." Ibid.

Based on our review of the record, we are satisfied that the Board's order satisfies all of the Metromedia factors and thereby constitutes a rule requiring adoption through rulemaking in accordance with the APA. See Auth. For Freshwater Wetlands Statewide Gen. Permit 6, supra, 433 N.J. Super. at 413. With regard to the first Metromedia factor, the modified CTA applies to all of the utility companies whose tax returns are filed as part of the consolidated returns of their respective holding companies. Cf. Deborah Heart & Lung Ctr. v. Howard, 404 N.J. Super. 491, 506 (App. Div.) (finding rulemaking was not required in part because the nine of eighteen cardiac surgery facilities subject to the policy change constituted a "narrow, select group," and not a "large segment of the regulated public"), certif. denied, 199 N.J. 129 (2009). In addition, because the utility company respondents serve a significant portion of the regulated public and the CTA modifications will "impact the general public in its rate-paying capacity, the first Metromedia factor . . . support[s] closer adherence to rulemaking procedures." Provision of Basic Generation Serv., supra, 205 N.J. at 350-51; see also In re Attorney General's "Directive on Exit Polling: Media and Non-Partisan Public Interest Groups," 402 N.J. Super. 118, 134 (App. Div. 2008) (finding first

Metromedia factor supports rulemaking where the agency's order "is intended to affect a large segment of the public"), aff'd in part and modified in part on other grounds, 200 N.J. 283 (2009).

The second Metromedia factor also favors rulemaking because the modified CTA generally and uniformly applies to all regulated utilities whose tax returns are filed as part of consolidated returns. Metromedia, supra, 97 N.J. at 331. Moreover, the Board's order directs that the modified CTA applies prospectively, including in those cases that were not yet decided but where the record remained open at the time the order was entered. Thus, application of the third Metromedia factor supports a finding that the modified CTA constitutes a rule. Ibid.

As set forth in the Board's order, the modified CTA "prescribes a legal standard [and] directive that is not otherwise expressly provided by or clearly and obviously inferable from the [Board's] enabling statutory authorization." Ibid. The Board is required to set "just and reasonable rates," N.J.S.A. 48:2-21, but there is no statutory directive establishing the methodology for calculating a utility's real, as opposed to hypothetical, tax payments to determine its rate base, and no statute directs the use of a CTA. See Airwork, supra, 97 N.J. at 301 (holding rulemaking is not required for an agency order directing the form of a tax assessment where tax statute is specific concerning the



underlying tax obligation). We are therefore satisfied the fourth Metromedia factor favors a finding that rulemaking is required.

Application of the fifth Metromedia factor also favors rulemaking. Although the use of a CTA and the Rockland methodology were previously expressed in the Board's determinations in adjudicated cases, the shortened and finite review period, the allocation of the tax savings, and the elimination of electric transmission assets constitute "material and significant change[s]" to the Board's prior CTA policy. Metromedia, supra, 97 N.J. at 331. The Board never before employed a finite review period or a defined allocation, and never previously excluded a class of a utility company's assets from its CTA calculation. Further, it is not disputed that the modifications constitute material and significant changes to the CTA. Indeed, Rate Counsel, the Coalition, the NJUA and the utility companies argued before the Board that the CTA required material and significant changes, and the Board's order achieved that result.

Last, the modifications reflect the Board's decision on a regulatory policy "in the nature of an interpretation of law or general policy." Id. at 331-32. The Board acknowledges as much in its decision and order, stating that the modifications are required to recognize "the fact that a fundamental tenet of utility regulation is that any methodology used by a regulator must result

in an end result that is just and reasonable for both ratepayers and shareholders." The Board adopted the modifications based on its finding that the prior CTA methodology "may not be the appropriate means of achieving that fundamental principle." See Provision of Basic Generation Serv., supra, 205 N.J. at 352 (finding the Board's decision to "pass through" certain costs to ratepayers could be viewed as a regulatory policy which was to be applied later in individual rate-recovery hearings).

In sum, all of the Metromedia factors favor rulemaking here. The Board's order constitutes a "statement of general applicability and continuing effect that implements [and] interprets" the Board's "policy" concerning the calculation of tax adjustments to a utility company's rate base, N.J.S.A. 52:14B-2(e), and therefore is a rule within the meaning of the APA. See, e.g., Auth. For Freshwater Wetlands Statewide Gen. Permit 6, supra, 433 N.J. Super. at 413 (finding agency's adoption of a computer-based program used to determine the sufficiency of proposed nonstructural stormwater management measures constituted rulemaking); N.J. Animal Rights Alliance v. N.J. Dep't of Env't'l. Prot., 396 N.J. Super. 358, 369-70 (App. Div. 2007) (finding agency's policy detailing requirements for a public bear hunt constituted a rule requiring APA rulemaking).

Rate counsel, the Coalition and amicus AARP argue the Board's failure to comply with the APA requires reversal of the Board's order. They contend the Board's failure to engage in formal rulemaking deprived the stakeholders of APA procedural safeguards and an opportunity to present evidence and testimony at an evidentiary hearing.

For example, Rate Counsel argues the Board failed to comply with the following APA requirements: publish a proposal containing "a clear and concise explanation of the purpose and effect of the rule, the specific legal authority under which its adoption is authorized, [and] a description of the expected socio-economic impact of the rule," N.J.S.A. 52:14B-4(a)(2), and prepare and distribute "a report listing all parties offering written or oral submissions concerning the rule, summarizing the content of the submissions and providing the agency's response to the data, views, comments, and arguments contained in the submissions," N.J.S.A. 52:14B-4(a)(4). The record supports Rate Counsel's position. These APA requirements were not satisfied in the generic proceeding.

Rate Counsel also argues, and the record shows, that the Board's March 2013 Notice of Opportunity to Comment and July 2013 Notice of Opportunity to Provide Additional Information each stated that following the collection of the requested data and comments, the Board would "announce a schedule for hearings to

provide all interested parties with the opportunity to provide testimony on the CTA issues." The Board, however, never announced such hearings or conducted any hearings providing interested parties with the opportunity to present testimony.

Although agencies enjoy leeway to choose among rulemaking, adjudicatory hearings, and hybrid informal proceedings to fulfill their statutory mandates, Provision of Basic Generation Serv., supra, 205 N.J. at 347, leeway is not a license to ignore the APA's requirements. The Board has discretion to utilize various procedures to fulfill its statutory mandate, but our Supreme Court has held that "administrative action, and an agency's discretionary choice of the procedural mode of action, are valid only when there is compliance with the provisions of the [APA] and due process." Ibid.; see also Airwork, supra, 97 N.J. at 300 ("If an agency determination or action constitutes an 'administrative rule,' then its validity requires compliance with the specific procedures of the APA that control the promulgation of rules."); Consider Distrib. of Casino Simulcasting Special Fund, 398 N.J. Super. 7, 16 (App. Div. 2008) ("An agency's ability to select procedures it deems appropriate is limited by 'the strictures of due process and of the [APA] . . . .'" (quoting In re Request for Solid Waste Util. Customer Lists, supra, 106 N.J. at 519)). Where, as here, the Board promulgates an administrative rule, it is

required to comply with the APA's requirements. Provision of Basic Generation Serv., supra, 205 N.J. at 347. Because the Board failed to do so here, we are constrained to reverse the Board's order.

We are not persuaded that the Court's decision in Provision of Basic Generation Service, requires a different result. There, the Court applied the Metromedia factors to a Board order that in part allowed utility companies to pass through increased energy supplier costs to the ratepayers. Id. at 349-52. The Court found that the first five Metromedia factors supported a finding that the order constituted rulemaking and that the sixth factor "[did] not advance the analysis in any compelling way." Id. at 350-52. In weighing the factors, the Court determined that the preponderance of the "factors favor[ed] treating the [order] as akin to rulemaking" but that in adopting what the Court characterized as a "quasi-rule, the [Board] was entitled to greater flexibility with regard to procedural formalities than if this process could only have been completed by way of a strict rulemaking process." Id. at 352 (emphasis added).

Under those circumstances, the Court found the Board's use of a hybrid proceeding "which had attributes of rulemaking and adjudicative proceedings and included a legislative-type hearing, two opportunity-to-comment periods, discovery periods, and public hearings throughout the state, was sufficient to satisfy the

requirements of the . . . APA." Id. at 353 (emphasis added). But the Court expressly conditioned its conclusion upon the requirement that "evidentiary rate-setting hearings take place which apply to the cases of specific energy providers the principles to be established in" an ongoing contested case before the Board.<sup>5</sup> Ibid. Thus, the court allowed a departure from the APA's rulemaking requirements because the policy was going to be further defined in an ongoing adjudicated case.

Here, all the Metromedia factors clearly favor rulemaking. Therefore, unlike in Provision of Basic Generation Service, we address the requirements for the adoption of an actual, and not a quasi-rule, and the Board did not have the concomitant flexibility to depart from the APA's requirements. See id. at 352. Moreover, in its adoption of the modified CTA, the Board did not utilize the hybrid process the Court found provided the flexibility to abandon the requirements of formal rulemaking in Provision of Basic Generation Service.<sup>6</sup> The Board's order constitutes a general policy

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<sup>5</sup> The ongoing contested case cited by the Court was In re Provision of Basic Generation Service for the Period Beginning June 1, 2008 — BGS SREC Recovery Mechanism Proceeding, BPU Docket No. ER07060379. Ibid.

<sup>6</sup> As an alternative to acting through rulemaking, adjudication or a hybrid proceeding, an agency may act informally. Request for Solid Waste Util. Customer Lists, supra, 106 N.J. at 518. "[I]nformal action constitutes the bulk of the activity of most

that will be applied in future cases without the benefit of any of the adjudicatory proceedings the Court required in Provision of Basic Generation Service. See id. at 353.

"The purpose of APA rulemaking procedures is 'to give those affected by the proposed rule an opportunity to participate in the process, both to ensure fairness and also to inform regulators of consequences which they may not have anticipated.'" Id. at 349 (quoting In re Adoption of 2003 Low Income Hous. Tax Credit Qualified Allocation Plan, 369 N.J. Super. 2, 43 (App. Div.), certif. denied, 182 N.J. 141 (2004)). We find nothing in the Court's decision in Provision of Basic Generation Service supporting an abandonment of the well-settled principle that where an agency adopts a rule, it must proceed through formal rulemaking in accordance with the APA. Id. at 347; Airwork, supra, 97 N.J. at 300; Auth. For Freshwater Wetlands Statewide Gen. Permit 6, supra, 433 N.J. Super. at 413.

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administrative agencies," "and the line between . . . rulemaking . . . , and informal action, . . . can become blurred." Ibid. However, informal action is defined as "statutorily authorized agency action that is neither adjudication nor rulemaking." Id. at 519. "[I]nformal agency action includes investigating, publicizing, planning, and supervising a regulated industry." Ibid. Here, the Board's order did not constitute informal action because, as noted, it satisfied each of the Metromedia factors and therefore constituted a rule that required rulemaking. Metromedia, supra, 97 N.J. at 332. It is only where "the APA does not require rulemaking [that] an agency may act informally." Ibid.; N.J.A.C. 7:1B-1.1 Et Seq., supra, 431 N.J. Super. at 133.

We are also persuaded that the Board's departure from the APA requirements constituted an "irregularity or informality [that] tends to defeat or impair the substantial right or interest of the appellant." N.J.S.A. 48:2-46. In the first instance, the Board's proceeding violated the ratepayers' right to have the new CTA policy adopted in accordance with the APA.

Second, although the Board's process provided opportunities for the submission of evidence and comment and the Board made certain submissions available on its website, the Board failed to comply with the APA's requirements that it publish "a description of the expected socio-economic impact of the rule," N.J.S.A. 52:14B-4(a)(2), and prepare and distribute a report "summarizing the content of the submissions and providing the [Board's] response to the data, views, comments, and arguments contained in the submissions," N.J.S.A. 52:14B-4(a)(4). We do not consider these APA requirements to be insubstantial. They require more of the Board than merely making information available on a website and requesting comment.

Compliance with the requirements provides the stakeholders with the Board's analysis and assessment of the economic impact of a proposed rule and the Board's response to a stakeholder's data, comments and arguments before a rule is adopted. Moreover, compliance provides the stakeholders with the opportunity to



present evidence and address the Board's economic impact assessment and response to the stakeholder's data, comments and argument. In other words, the statutory requirements guarantee that Rate Counsel and the stakeholders are fully informed of the Board's position concerning a rule's economic impact and the Board's response to the submitted data, comments and arguments, thus permitting Rate Counsel and the stakeholders an opportunity to present further evidence and argument. When the requirements are ignored, the Board gathers information and comment, but Rate Counsel and the stakeholders are deprived of the right granted by the APA to consider and contest the Board's assessment of economic impact and responses to the submissions prior to the adoption of a rule.

In our view, the Board's failure to comply with the requirements deprived Rate Counsel of substantial rights and interests under the APA: the right to obtain the Board's assessment of the economic impact of the proposed modified CTA and responses to Rate Counsel and the other stakeholders' submissions, and the right to provide evidence and argument in opposition to them. The failures are of particular significance here because of the conflicting evidence presented concerning the modified CTA's potential economic impact on ratepayers. We are therefore convinced that the Board's failure to comply with the APA's

requirements in its adoption of the modified CTA constituted an irregularity that tended to defeat and impair the rights and interests of Rate Counsel and the other stakeholders.

Because we reverse the Board's order, it is unnecessary to address the arguments that the Board's decision and order lacks sufficient support in the record or is otherwise contrary to applicable law. Any remaining arguments that we have not addressed directly are without sufficient merit to warrant discussion in a written opinion. R. 2:11-3(e)(1)(E).

Reversed.

I hereby certify that the foregoing  
is a true copy of the original on  
file in my office.

  
CLERK OF THE APPELLATE DIVISION

## **ATTACHMENT C**

GAS AND ELECTRIC UTILITY INFRASTRUCTURE PROGRAMS  
LINKS TO BASE RATE PROCEEDINGS

	Utility/Program	Date Approved	Link to Base Rate Case
	<b>ORIGINAL ECONOMIC STIMULUS</b>		
1	NJNG Accelerated Energy Infrastructure Investment Program ("AIP") <sup>i</sup>	April 2009	Company's 2007 base rate case was re-opened for consideration of base rate increases associated with infrastructure investments through August 31, 2011.
2	SJG Capital Investment Recovery Tracker ("CIRT") <sup>ii</sup>	April 2009	Base rate petition to be filed on or before April 1, 2011.
3	PSE&G Capital Infrastructure Investment Program ("CIP") <sup>iii</sup>	April 2009	Base rate petition to be filed between April 3, 2009 and April 1, 2011
4	ETG Utility Infrastructure Enhancement ("UIE") Program <sup>iv</sup>	April 2009	Rate increases associated with infrastructure investments to be considered in Phase II of pending 2009 base rate case
5	ACE Infrastructure Investments Surcharge ("IIS") <sup>v</sup>	April 2009	Base rate petition to be filed on or before April 1, 2011.
	<b>ECONOMIC STIMULUS EXTENSION</b>		
6	NJNG AIP II <sup>vi</sup>	March 2011	Company's 2007 base rate case to remain open to consider infrastructure improvements through October 2012, after which the base rate case will close.
7	SIG CIRT II <sup>vii</sup>	March 2011	Company's 2010 base rate case to remain open for infrastructure investments through October 2012, with recovery for later investments to be considered in subsequent base rate or other proceeding.
8	ETG UIE II <sup>viii</sup>	May 2011	Phase II of Company 2009 base rate case to remain open to consider investments through October 2012, with recovery for later investments to be considered in a subsequent base rate or other proceeding.
9	PSE&G CIP II <sup>ix</sup>	July 2011	Company's 2009 base rate case to remain open for projects to be completed by December 2012, with recovery for later investments to be considered in the Company's next base rate case.

	<b>GAS PIPELINE SAFETY AND MODERNIZATION</b>		
10	ETG Pipeline Replacement Program ("PRP") <sup>x</sup>	Aug. 2006	Previously issued BPU Order approving Company's merger with AGLR required a base rate filing no later than March 2009.
11	NJNG Safety Acceleration and Facility Enhancement ("SAFE") Program <sup>xi</sup>	Oct. 2012	Base rate case to be filed no later than November 15, 2015
12	SJG Accelerated Infrastructure Replacement Program ("AIRP") <sup>xii</sup>	Feb. 2013	Base rate case to be filed no later than December 15, 2015.
13	ETG Accelerated Infrastructure Replacement ("AIR") Program <sup>xiii</sup>	Aug. 2013	Base rate case to be filed no later than September 1, 2016
14	PSE&G Gas System Modernization Program ("GSMP") <sup>xiv</sup>	Nov. 2015	Company previously committed to file a base rate case no later than November 1, 2017.
15	NJNG SAFE II <sup>xv</sup>	Sept. 2016	Base rate case to be filed no later than November 2019.
16	SJG AIRP II <sup>xvi</sup>	Oct. 2016	Company previously committed to file base rate case no later than October 1, 2017. Next base rate case to be filed no later than three years following the Board Order in the 2017 base rate case.
	<b>STORM HARDENING/ RESILIENCE</b>		
17	PSE&G for Approval of the Energy Strong Program <sup>xvii</sup>	May 2014	PSE&G will file its next base rate case no later than November 1, 2017.
18	JCP&L Major Storm Events in 2011 and 2012 <sup>xviii</sup>	March 2015	Company is directed to file a base rate case no later than April 1, 2017.
19	RECO Major Storm Events in 2011 and 2012 <sup>xix</sup>	May 2014	2011 and 2012 Major Storm Costs recovery to be determined in pending Base Rate Case (ER13111135).
20	RECO Storm Hardening Program <sup>xx</sup>	Jan. 2016	These costs will be subject to review in the next Base Rate Case which the Company has committed to filing by July 31, 2018.
21	ETG Natural Gas Distribution Utility Reinforcement Effort ("ENDURE") Program <sup>xxi</sup>	July 2014	Base rate case to be filed by September 1, 2016.

22	NJNG Reinvestment Enhancement Program ("RISE") <sup>xxii</sup>	July 2014	Company previously committed to file a base rate case no later than November 15, 2015.
23	SJG Storm Hardening and Reliability Program ("SHARP") <sup>xxiii</sup>	Aug. 2014	Company's 2013 base rate case pending at time program approved, and next base rate case to be filed no later than October 1, 2017.

<sup>i</sup> I/M/O the Proceeding for Infrastructure Investment and a Cost Recovery Mechanism for All Gas and Electric Utilities and I/M/O the Petition New Jersey Natural Gas Company for Approval of an Accelerated Energy Infrastructure Investment Program Pursuant to N.J.S.A. 48:2-23, and for Approval of Necessary Changes to Gas Rates and Changes in the Company's Tariff for Gas Service Pursuant to N.J.S.A. 48:2-21, BPU Dkt. Nos. EO09010049 & GO09010052 (Apr. 28, 2009).

<sup>ii</sup> I/M/O the Proceeding for Infrastructure Investment and a Cost Recovery Mechanism for All Gas and Electric Utilities and I/M/O the Petition of South Jersey Gas Company for Approval of a Capital Investment Recovery Tracker Pursuant to N.J.S.A. 48:2-21.1 and N.J.S.A. 48:2-21, BPU Dkt. Nos. EO09010049 & GO09010051 (Apr. 28, 2009).

<sup>iii</sup> I/M/O the Proceeding for Infrastructure Investment and a Cost Recovery Mechanism for All Gas and Electric Utilities and I/M/O the Petition of Public Service Electric & Gas Company for Approval of a Capital Economic Stimulus Investment Program and an Associated Cost Recovery Mechanism Pursuant to N.J.S.A. 48:2-21 and N.J.S.A. 48:2-21.1, BPU Dkt. Nos. EO09010049 & GO09010050 (Apr. 28, 2009).

<sup>iv</sup> I/M/O the Proceeding for Infrastructure Investment and a Cost Recovery Mechanism for All Gas and Electric Utilities and I/M/O the Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas for Approval of a Utility Infrastructure Enhancement Cost Recovery Rider, BPU Dkt. Nos. EO09010049 & GO09010053 (Apr. 28, 2009).

<sup>v</sup> I/M/O the Petition of Atlantic City Electric Company for Approval of Certain Energy Infrastructure Investments and Approval of a Cost Recovery For Such Projects and Related Tariff Modifications Associated Therewith Pursuant to N.J.S.A. 48:2021 and 48:21.1, BPU Dkt. No. GO09010054, Decision and Order Approving Stipulation (Apr. 28, 2009).

<sup>vi</sup> I/M/O the Petition of New Jersey Natural Gas Company for Approval of an Extension of the Accelerated Energy Infrastructure Investment Program Pursuant to N.J.S.A. 48:2-23 and for Approval of Necessary Changes in the Company's Tariff for Gas Service Pursuant to N.J.S.A. 48:2-21 et seq., BPU Dkt. Nos. GR07110889 & GR10100793 (Mar. 30, 2011).

<sup>vii</sup> I/M/O the Annual Filing of South Jersey Gas Company to Adjust its Capital Investment Recovery Tracker ("CIRT") and for Approval of an Extension of the CIRT Pursuant to N.J.S.A. 48:2-21 and N.J.S.A. 48:2-21.1 and I/M/O the Petition of South Jersey Gas Company for Approval of Base Tariff Rates and Charges for Gas Service and Other Tariff Revisions, BPU Dkt. Nos. GR10100765 & GR10010035 (Mar. 31, 2011).

<sup>viii</sup> I/M/O Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas to Extend its Utility Infrastructure Enhancement Program and Revise its Utility Infrastructure Enhancement Rate and I/M/O Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas for Approval of Increased Base Tariff Rates and Charges for Gas Services and Other Tariff Revisions, BPU Dkt. Nos. GO10120969 & GR09030195 (May 16, 2011).

<sup>ix</sup> I/M/O the Petition of Public Service Electric and Gas Company for Approval of an Extension of the Electric Capital Economic Stimulus Infrastructure Investment Program and Associated Cost Recovery Mechanism and to Roll Into Rate Base the Net Capital Investment for All the Qualifying Projects From the Initial Capital Economic Stimulus Infrastructure Investment Program Upon Completion Pursuant to N.J.S.A. 48:2-23, 48:2-21 and 48:2-21.2 and for Changes in the Tariff for Electric Service, B.P.U.N.J. No. 15 Electric, and the Tariff for Gas Service, B.P.U.N.J. No. 15 Gas Pursuant to N.J.S.A. 48:2-21 and I/M/O the

Petition of Public Service Electric and Gas Company for Approval of an Extension of the Gas Capital Economic Stimulus Infrastructure Investment Program and Associated Cost Recovery Mechanism and to Roll Into Rate Base the Net Capital Investment for All the Qualifying Projects From the Initial Capital Economic Stimulus Infrastructure Investment Program Upon Completion Pursuant to N.J.S.A. 48:2-23, 48:2-21 and 48:2-21.1 and for Changes in the Tariff for Electric Service, B.P.U.N.J. No. 15 Electric, and the Tariff for Gas Service, B.P.U.N.J. No. 15 Gas Pursuant to N.J.S.A. 48:2-21, BPU Dkt. Nos. EO11020088 & GO10110862 (Jul. 14, 2011).

<sup>x</sup> I/M/O the Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas Company to Establish a Pipeline Replacement Program Cost Recovery Rider, BPU Dkt. No. GR05040371 (Aug. 18, 2006).

<sup>xi</sup> I/M/O the Petition of New Jersey Natural Gas Company for Approval of the Safety Acceleration and Facility Enhancement Program Pursuant to N.J.S.A. 48:2-23 and for Approval of the Associated Recovery Mechanism Pursuant to N.J.S.A. 48:2-21 and N.J.S.A. 48:2-21.1, BPU Dkt. No. GO21030255 (Oct. 23, 2012).

<sup>xii</sup> I/M/O the Petition of South Jersey Gas Company to Implement an Accelerated Infrastructure Replacement Program and Associated Recovery Mechanism Pursuant to N.J.S.A. 48:2-21 and N.J.S.A. 48:2-21.1, BPU Dkt. No. GO12070670 (Feb. 20, 2013).

<sup>xiii</sup> I/M/O the Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas for Approval of an Accelerated Infrastructure Replacement Program and an Associated Cost Recovery Mechanism, BPU Dkt. No. GO12070693 (Aug. 21, 2013).

<sup>xiv</sup> I/M/O the Petition of Public Service Electric and Gas Company for Approval of a Gas System Modernization Program and Associated Cost Recovery Mechanism, BPU Dkt. No. GR15030272 (Nov. 16, 2015).

<sup>xv</sup> I/M/O the Petition of New Jersey Natural Gas Company for Approval of an Increase in Gas Base Rates and for Changes in its Tariff for Gas Service, and Approval of SAFE Extension and NJ RISE Rate Recovery Mechanism Pursuant to N.J.S.A. 48:2-21, 48:2-21.1 and for Changes to Depreciation Rates for Gas Property Pursuant to N.J.S.A. 48:2-18, BPU Dkt. No. GR15111304 (Sept. 23, 2016).

<sup>xvi</sup> I/M/O the Petition of South Jersey Gas Company to Continue Its Accelerated Infrastructure Replacement Program ("AIRP") Pursuant to N.J.S.A. 48:2-21 and N.J.S.A. 48:2-21.1 and for Approval of a Base Rate Adjustment to Reflect AIRP Investments in Base Rates, BPU Dkt. No. GR16020175 (Oct. 31, 2016).

<sup>xvii</sup> I/M/O Public Service Electric and Gas Company for Approval of the Energy Strong Program, Dkt. Nos. EO13020155 and GO13020156, Order Approving Stipulation of Settlement (5/21/14).

<sup>xviii</sup> I/M/O the Board's Establishment of a Generic Proceeding to Review the Prudence of Costs Incurred By New Jersey Utility Companies in Response to Major Storm Events in 2011 and 2012, BPU Dkt. No. AX13030196 and I/M/O the Board's Review of the Prudence of the Costs Incurred By Jersey Central Power and Light Company in Response to Major Storm Events in 2011 and 2012, BPU Dkt. No. ER13050391, Order (3/26/15).

<sup>xix</sup> I/M/O the Board's Review of the Prudence of the Costs Incurred by Rockland Electric Company in Response to Major Storm Events in 2011 and 2012, BPU Dkt. No. EO13070611, Decision and Order Approving Stipulation (May 21, 2014).

<sup>xx</sup> I/M/O the Board's Establishment of a Generic Proceeding to Review the Costs, Benefits and Reliability Impacts of Major Storm Even Mitigation Efforts, BPU Dkt. No. AX13030197 and I/M/O the Verified Petition of Rockland Electric Company for Establishment of a Storm Hardening Surcharge, BPU Dkt. No. ER14030250, Decision and Order Approving Stipulation (1/28/16).

<sup>xxi</sup> I/M/O the Board's Establishment of a Generic Proceeding to Review the Costs, Benefits and Reliability Impacts of Major Storm Event Mitigation Efforts and I/M/O the Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas for Approval of the Elizabethtown Natural Gas Distribution Utility Reinforcement Effort Program and Deferred Accounting Treatment, BPU Dkt. Nos. AX13030197 & GO13090826 (July 23, 2014).

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xxii I/M/O the Board's Establishment of a Generic Proceeding to Review the Costs, Benefits and Reliability Impacts of Major Storm Event Mitigation Efforts and I/M/O the Petition of New Jersey Natural Gas Company for Approval of the NJ RISE Program and Associated Rate Recovery Mechanism, BPU Dkt. Nos. AX13030197 & GO13090828 (July 23, 2014).

xxiii I/M/O the Board's Establishment of a Generic Proceeding to Review the Costs, Benefits and Reliability Impacts of Major Storm Event Mitigation Efforts and I/M/O the Petition of South Jersey Gas Company for Approval of a Storm Hardening and Reliability Program (SHARP) and Associated Recovery Mechanism, BPU Dkt. Nos. AX13030197 & GO13090814 (Aug. 20, 2014).



## **ATTACHMENT D**

STATE OF NEW JERSEY  
BOARD OF PUBLIC UTILITIES

IN THE MATTER OF THE PETITION :  
OF NEW JERSEY AMERICAN WATER :  
COMPANY FOR AUTHORIZATION TO :  
IMPLEMENT A DISTRIBUTION :  
SYSTEM IMPROVEMENT CHARGE :  
("DSIC") :

BPU DOCKET NO. WO08050358

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INITIAL BRIEF OF THE STAFF OF THE BOARD OF PUBLIC UTILITIES

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#### POINT I

BECAUSE NJAW HAS ESTABLISHED THAT A SUBSTANTIAL PORTION OF ITS MAINS ARE OVER 50 YEARS OLD, STAFF RECOMMENDS THAT THE BOARD IMPLEMENT A DSIC ON A PILOT BASIS AND THAT THE BOARD COMMENCE A GENERIC RULEMAKING CONSISTENT WITH APPLICABLE LAW.....	31
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## POINT II

BOARD STAFF RECOMMENDS, AMONG OTHER THINGS, THAT THE BOARD LIMIT THE DSIC ELIGIBLE PLANT TO MAINS THAT ARE OVER 50 YEARS OLD, CAP THE DSIC SURCHARGE AT 3% OF ANNUAL GROSS REVENUES BETWEEN RATE CASES, ALLOW INTEREST ON ANY OVER COLLECTION, AND REQUIRE THE COMPANY TO FILE QUARTERLY REPORTS AND ANNUAL FILINGS. ....	39
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At the Westfield Public Hearing, Mr. Tom Getzendanner, an elected official for the Town of Summit, commented that the self-implementing DSIC rate be capped at a percentage lower than 7.5%, such as at 3%, in light of the Company's recent rate increases. (Westfield Public Hearing Transcript 15-6 to 12). No members of the public spoke at the Maplewood and Westhampton public hearings.

#### STAFF'S DSIC PROPOSAL

Staff proposes that the Board adopt a DSIC mechanism that would permit NJAW to recover expenditures on the replacement of main that is at least 50 years of age, up to a total of 3% of the Company's annual gross revenues, between rate cases. Staff recommends that in order to collect a DSIC charge from ratepayers, the Company must first file a petition with the Board on or about October 2009 outlining the DSIC-eligible plant that was or is to be placed in service between December 31, 2008 and December 31, 2009. Beginning in 2010, the Company is to submit quarterly reports to reflect DSIC eligible plant that was placed in service after each period.<sup>6</sup> Staff proposes that on or about October 2010, the Company submit a petition for DSIC eligible plant that was or is to be placed in service between December 31, 2009 and December 31, 2010. The Company will also be required to file its "true up" petition which will reconcile the DSIC-eligible plant that was placed in service during the previous year up to and including December 31, 2009, along with a depreciation reserve true up for the associated plant.

Through Staff's proposal, DSIC rates would be changed annually with a filing that includes a public hearing and a Board Order. Staff recommends that the Company be required to file a base rate case no later than three years, but with rates effective no sooner than two years after the Board Order in this docket. At the conclusion of the base rate proceeding, which will

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<sup>6</sup> Staff proposes that a January 2010 quarterly report reflect eligible plant placed in service for the fourth quarter of 2009, the April 2010 report reflect activity during the first quarter of 2010, the July 2010 report reflect activity during the second quarter of 2010, and the October 2010 report reflect activity from the third quarter of 2010.

include a prudency review of all DSIC-eligible projects, all DSIC-related costs deemed just and reasonable will be made permanent, and the DSIC clause will be reset to zero. Staff also proposes all over recoveries collected under the DSIC charge be refunded to ratepayers with interest. Moreover, Staff supports the concept of an earnings test.

Additionally, Staff recommends that the implementation of the DSIC be done within the context of a pilot program for at least two years and no more than three years. Furthermore, Staff recommends that the Board begin a generic rulemaking proceeding in order to develop rules to be applied to all regulated water and wastewater utilities within the Board's jurisdiction.

Staff recommendations, including a discussion of method of calculating the DSIC charge, will be further addressed below.

#### POINT 1

BECAUSE NJAW HAS ESTABLISHED THAT A SUBSTANTIAL PORTION OF ITS MAINS ARE OVER 50 YEARS OLD, STAFF RECOMMENDS THAT THE BOARD IMPLEMENT A DSIC ON A PILOT BASIS AND THAT THE BOARD COMMENCE A GENERIC RULEMAKING CONSISTENT WITH APPLICABLE LAW.

The Board should adopt a DSIC, because the need for one is necessary to address New Jersey's aging water and wastewater infrastructure. According to NJAW, 15% or 1250 miles of its water mains will be in service for 100 years or more by the year 2020 unless they are replaced before then. (PT-2 3-21 to 22). Additionally, mains installed before 1965 account for over 50% of NJAW's water main system. Mains installed during this period pre-dates the common use of cement-lined ductile iron pipe material. (PT-2 10-2 to 8). Moreover, these mains have been subjected to years of corrosion, increased weight loading from heavier vehicles, street repavings and impacts from installation of other underground utilities. (PT-2 10-2 to 8). Further, the mains installed within the NJAW system in the 1920s and those installed between 1945 and 1955 may reach the end of their useful lives at the same time within the next 25-35 years due to factors



such as age, localized conditions, design standards and manufacturing techniques. (PT-2 5-9 to 6-3). Relative to NJAW's collection systems, Ms. Chiavari notes that these mains were constructed 50 to over 100 years ago and that they will reach the end of their useful lives within the next 5-25 years. (PT-2 3-14 to 17).

NJAW argues that traditional ratemaking alone cannot address the growing need to replace and rehabilitate aging water and wastewater infrastructure that is nearing its useful life (PT-2 16-7 to 11) and the implementation of a DSIC would relieve the uncertainty inherent in a rate case and allow the Company to pursue an aggressive replacement and rehabilitation program. (PT-2 19-10 to 13). Staff believes that a DSIC would allow the Company to accelerate its pace of infrastructure replacements at a reasonable cost, resulting in improved water quality, improved pressure and service reliability that will benefit customers. Staff also believes that the replacement and upgrade of deteriorating water and wastewater mains could reduce the number of main breaks, service interruptions, unaccounted for water; improve water quality; and enhance fire protection. Staff agrees with the Company that the DSIC will permit the Company to address its aging infrastructure on a more timely basis and that a DSIC, when properly implemented, can accelerate the replacement of older mains.

Staff notes Rate Counsel's argument that the existing ratemaking mechanism is sufficient to address an accelerated infrastructure program. (2T 94-24 to 95-3). Staff believes that the parameters set forth below address the parties's positions.

First, the Board should find that it is within its authority to order the implementation of a DSIC to customers of NJAW, a public utility under the Board's jurisdiction. Under N.J.S.A. 48:2-13, the Board has general jurisdiction over all public utilities and their "property, property rights, equipment, facilities and franchises so far as may be necessary for the purpose of carrying

out the provisions of [Title 48]." It has been stated in case law that the Board was "intended by the Legislature to have the widest range of regulatory power over public utilities," and that the provisions under N.J.S.A. 48 "are to be construed liberally." County of Bergen v. Dept. of Public Utilities of the State of N.J., 117 N.J. Super. 304, 312 (App. Div. 1971).

Moreover, the Legislature has granted the Board broad discretion to exercise its rulemaking authority to ensure just and reasonable utility rates. In re Petition of Pub. Serv. Coordinated Transp., 5 N.J. 196, 214 (1950). As stated in N.J.S.A. 48:2-21(d), "the Board, either upon written complaint or upon its own initiative, shall have power after hearing, upon notice, by order in writing to determine whether the increase, change or alteration is just and reasonable."

The BPU also has the authority to implement a DSIC because the DSIC is germane to the Board's authority delegated under the provisions of Title 48, including the power to require any public utility to provide safe, adequate and proper service under N.J.S.A. 48:2-23. In In re Petition of New Jersey American Water Co. for an Increase in Rates for Water and Sewer Service, 169 N.J. 181, 197 (2001), the Court reversed the Board's granting of a 50/50 sharing between ratepayers and shareholders of the utility's charitable contributions, because, in part, there was no nexus between utility's charitable contributions and the claimed benefits to ratepayers to justify inclusion of contributions in the utility's operating expenses. Here, the record establishes that the implementation of a DSIC will allow the Company to accelerate on an incremental basis the replacement of aging mains. This will in turn provide improved water quality, pressure and service reliability to NJAW customers. (PT-2 16-9 to 11). Because the record supports a nexus between the implementation of a DSIC and benefit to the ratepayers, and because the Board has the statutory authority to order a DSIC, the Board should find that it is within its power to implement a DSIC under its broad ratemaking authority over public utilities.

Furthermore, there is a line of case law that permits the Board, pursuant to N.J.S.A. 48:2-21.1, the "negotiation statute," to adjust rates on an interim basis pending final review within a rate case, but any such adjustments cannot be regarded as "contractual." Staff proposes that the DSIC charge be implemented under the authority of the negotiation statute. Accordingly, Staff recommends that the Company file a rate case no later than three years from the date of a Board Order approving a DSIC, but with rates to be effective no earlier than two years from the date of a Board Order in this docket, in order to ensure compliance with the N.J.S.A. 48:2-21.1.

The Board's ability to utilize the negotiation statute had been addressed in In re Industrial Sand Rates, 66 N.J. 12 (1974), in which the Court made clear that the authority granted to the Board to negotiate with the utility for an adjustment of rates is confined to interim relief pending a proceeding to determine justness and reasonableness of an existing or proposed rate, and it, therefore, set aside permanent rates negotiated by the Board with the utility without requisite rate base and rate of return findings. The Court explained that

[t]he vital justification for the "negotiation statute" and rates established under it, temporarily bypassing the establishment of rate base and fair rate of return, rests upon the legal umbilical cord which ties them to the anticipated eventual determination of the fundamentals; at which time the temporary rates, their legitimacy having been validated, merge into the [Board] judgment ordaining the final rate structure or, if and to the extent found to have been excessive, are refunded to the consumers who paid them.

[ Id. at 19-20.]

Likewise, in In re Investigation of Tele. Cos., 66 N.J. 476 (1975), the Court upheld the Board's implementation of a "comprehensive adjustment clause," which permitted the company in that matter to recover certain expenses as they increased, finding that there was a nexus to the Board's review in that company's rate case. The Court acknowledged the Court's ruling in Industrial Sand that the "legal umbilical cord" between a "temporarily increased rate and the

final adjudication of the firmly established and traditional components which enter into the determination of "just and reasonable" rates" is indispensable. Tele. Cos., 66 N.J. at 495. The Court further explained that even expenses that "flow through" to consumers must be "[t]ested in the scrutiny of final rate determination and only in that way (despite the impressive monitoring devices built into the instant clause) can such expenses be validated and become demonstrably honest components in the ascertainment of 'just and reasonable' rates." Ibid.

Consistent with the Board's statutory authority and the nexus requirements in both Tele. Cos. and Industrial Sand, the Board has the authority to implement a DSIC mechanism for NJAW in the form of a pilot program. The Board would be within its authority to implement this pilot program for a period of two years. In Communication Workers of America, AFL-CIO v. N.J. Dept. of Personnel, 154 N.J. 121 (1998), the Supreme Court found that appellant, Department of Personnel, had not exceeded its authority when it adopted new pilot programs for determining eligibility of candidates for civil service appointments without first conducting a rulemaking proceeding. The pilot program that Staff is proposing would be for an interim period with interim relief until these temporary rates in the pilot program are merged into a base rate case to be filed within three years from the final decision rendered by the Board herein. The pilot program is merely interim relief and will aid the Board and Staff in evaluating the efficacy of the processes and procedures for implementation of a DSIC. As discussed below, the Board, while evaluating this pilot program, should concomitantly institute a rulemaking procedure. Therefore, Staff recommends that the Board implement the DSIC on a pilot basis.

Based on the above case law, Staff recommends that the Board require that the Company file a rate case no later than three years from the date of a Board Order approving a DSIC, but with rates to be effective no earlier than two years from the date of a Board Order approving the

DSIC, in order to ensure that the DSIC expenses are scrutinized in a final hearing. See Tele. Cos., 66 N.J. at 496.

Staff also recommends that the general implementation of the DSIC process and procedures be promulgated pursuant to a rulemaking under the Administrative Procedure Act, N.J.S.A. 52:14B-1 et seq. (the "Act"). Under the Act, administrative rule is defined as follows:

"Administrative rule" or "rule" when not otherwise modified, means each agency statement of general applicability and continuing effect that implements or interprets law or policy, or describes the organization, procedure or practice requirements of any agency. The term includes the amendment or repeal of any rule, but does not include: (1) statements concerning the internal management or discipline of any agency; (2) intra-agency and inter-agency statements; and (3) agency decisions and findings in contested cases.

[N.J.S.A. 52:14B-2(e).]

Administrative rulemaking requirements are grounded in notions of fairness, notice and procedural due process. Crema v. New Jersey Dept. of Environmental Protection, 94 N.J. 286 (1983); Airwork Ser. Div., etc. v. Director, Div. of Taxation, 97 N.J. 290 (1984). They are designed to ensure that affected parties are provided sufficient notice with respect to actions to be taken against them prospectively or which may affect substantial rights including the rights of persons not party to the action.

The statutory definition of administrative rule has been further examined in Metromedia, Inc. v. Director, Div. of Tax'n, 97 N.J. 313 (1984). There, the Supreme Court identified six factors to be weighed in determining whether an agency action must be rendered through formal rulemaking procedures. The Court held that an agency action could be considered an administrative rule:

If it appears that the agency determination, in many or most of the following circumstances: (1) is intended to have wide coverage encompassing a large segment of the regulated or general public, rather than an individual or a narrow select group; (2) is intended to be applied generally and uniformly to all similarly

situated persons; (3) is designed to operate only in future cases, that is, prospectively; (4) prescribes a legal standard or directive that is not otherwise expressly provided by or clearly and obviously inferable from the enabling statutory authorization; (5) reflects an administrative policy that (i) was not previously expressed in any official and explicit agency determination, adjudication or rule or (ii) constitutes a material and significant change from a clear, past agency position on the identical subject matter; and (6) reflects a decision on administrative regulatory policy in the nature of the interpretation of law or general policy.

[Id. at 331-32].

The six factors "can, either singly or in combination, determine in a given case whether the essential agency action must be rendered through rule-making or adjudication." Id. at 332. The applicability of the Metromedia factors to the case at bar becomes most evident when one attempts an analysis under the six factor test.

The first Metromedia factor is whether the Board's decision to implement a DSIC is "intended to have wide coverage encompassing a large segment of the regulated or general public." Metromedia, supra at 331. The implementation of a DSIC will encompass a large segment of the general public, as it will be applicable to all water companies in New Jersey and their ratepayers.

The next factor, whether the implementation of a DSIC is "intended to be applied generally and uniformly to all similarly situated persons," is met since all water companies and their ratepayers will be generally and uniformly affected by the procedures required by the Board for implementation of a DSIC mechanism. The third factor, whether the agency policy "is designed to operate only in future cases, that is, prospectively," has been met. If adopted, the Board will be approving the implementation of a DSIC for all future cases. The application of the DSIC is, therefore, prospective in nature.

The fourth Metromedia factor is equally satisfied by the case at bar. The implementation of a DSIC mechanism is not "clearly and obviously inferable from the enabling statutory authorization." In In re Solid Waste Util. Cust. Lists, 106 N.J. 508, 518 (1987), although "all six of the Metromedia factors need not be present to characterize agency action as rulemaking," these factors "should not merely be tabulated but weighed." In that case, an order of the Board of Public Utilities was found to satisfy three of the six Metromedia criteria. Nonetheless, the New Jersey Supreme Court determined that the Board's order did not constitute an administrative rule because it was clearly inferable from the applicable enabling legislation and neither changed nor interpreted Board policy concerning solid waste utilities.

As discussed previously, there is no explicit statutory language providing for the process and procedures associated with the implementation of a DSIC. The statutory scheme does not specifically provide statutory guidance on the process and procedure for implementation of a DSIC. The Board's statutory authority allowing it to establish a DSIC is grounded in very broad and all-encompassing statutory language and the more general statutory language addressing the Board's broad discretionary power over all public utilities is applicable. Therefore, the fourth factor in Metromedia has been met, and the Board should promulgate rules in this case. Further, as discussed below, the Board will be interpreting its policies to make a determination as to the process and procedure for the DSIC.

The fifth factor considered in Metromedia is whether the policy "(i) was not previously expressed in any official and explicit agency determination, adjudication or rule or (ii) constitutes a material and significant change from a clear, past agency position on the identical subject matter." The Board has never previously addressed the DSIC in any official and explicit

agency determination, adjudication or rule. Therefore, the fifth Metromedia factor has been satisfied.

The last Metromedia factor, whether the Board's decision to implement a DSIC mechanism "reflects a decision on administrative regulatory policy in the nature of the interpretation of law or general policy," is applicable to the case at bar. Here, the Board would be making a decision in the nature of the interpretation of law or general policy. To establish the DSIC mechanism, the Board will be interpreting the law and its general policies to formulate the process and procedure for the DSIC mechanism for all water companies in the State of New Jersey.

From the foregoing, it is clear that the Board's ultimate decision to implement a DSIC mechanism in New Jersey can be readily applied to the six factor test of Metromedia and, therefore, should be written through formal rulemaking procedures.

#### POINT 2

STAFF RECOMMENDS, AMONG OTHER THINGS, THAT THE BOARD LIMIT THE DSIC ELIGIBLE PLANT TO MAINS THAT ARE OVER 50 YEARS OLD, CAP THE DSIC SURCHARGE AT 3% OF ANNUAL GROSS REVENUES BETWEEN RATE CASES, ALLOW INTEREST ON ANY OVER COLLECTION, AND REQUIRE THE COMPANY TO FILE QUARTERLY REPORTS AND ANNUAL FILINGS.

As Ms. Chiavari testified, 50% of the Company's 8,330 miles of water was installed prior to 1965 and 30% of its pipe was installed before World War II, making a substantial portion of the Company's water main system over 50 years old. (PT-2 10-2 to 5). In light of the age of main in NJAW's system and Staff's recommendation that the Board's initial implementation of a DSIC be a simple process involving one type of plant, Staff proposes that the Board allow only replacement of mains 50 years of age or older to be considered DSIC-