



Rate Making 101
Those seeking CLE credit
must sign in.

MACRUC 2026

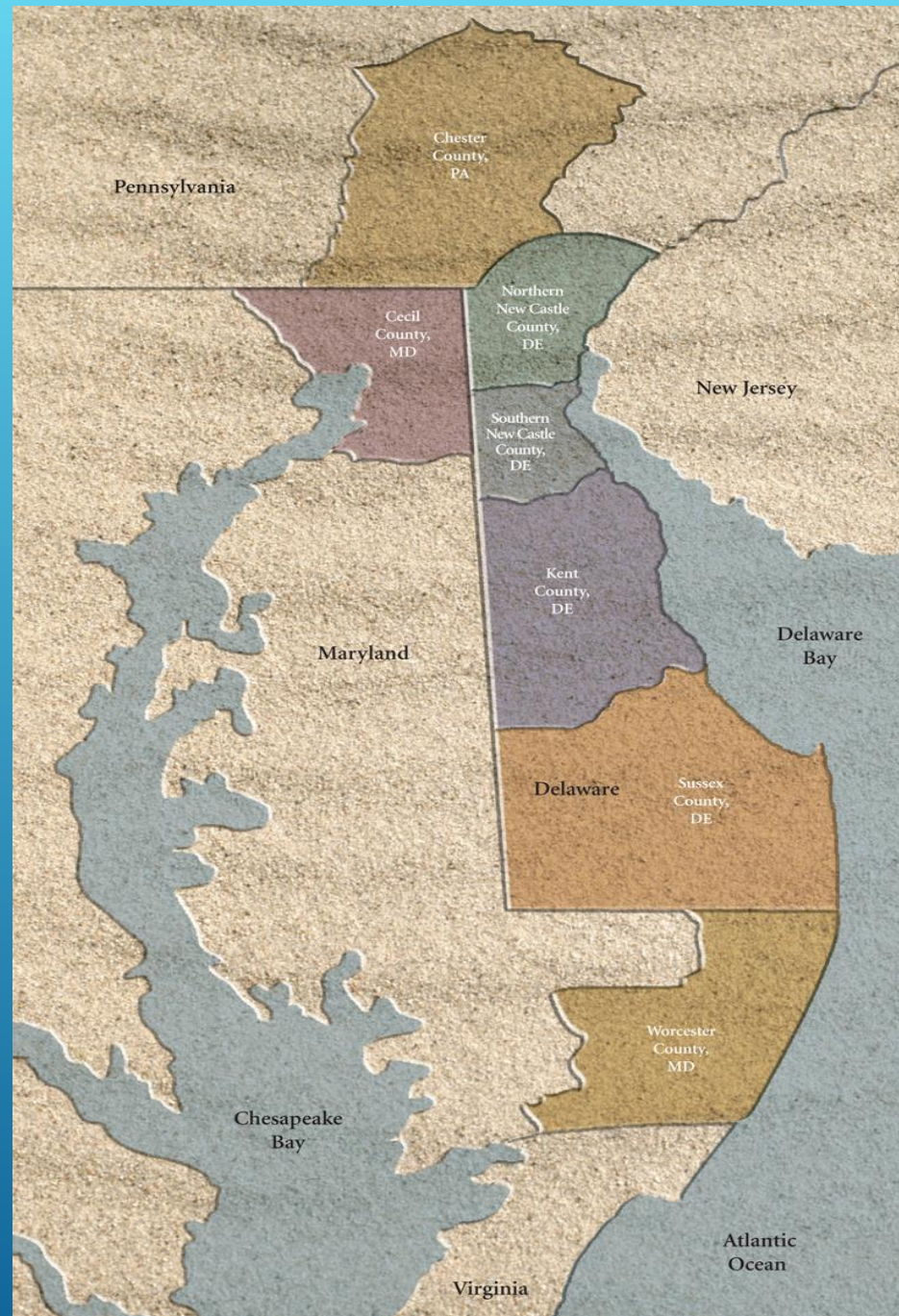
31ST ANNUAL EDUCATION CONFERENCE

Rate Making 101

David Spacht, CFO

Artesian Water Company Inc.

Artesian Water Company, Inc on the Delmarva Peninsula



WATER SERVICE FACTS

Population Served – approximately 301,000

Metered Customers – 101,900

Annual Production – 9.3 billion gallons

Miles of main – 1,515

Active Wells- 232

Treatment Facilities – 73

Storage Capacity – 178 million gallons

Average Cost Per Day - \$1.78

Wastewater Service:

Customers – 9,100

Treatment Capacity – 1 mgd (permit/const add. 1.25 mgd)

REGULATORY COMPACT

- What is the Regulatory Compact
 - The State Confers Monopoly Status – Created by State Legislature
 - In Exchange for Obligation to Serve
 - Regulation as a Surrogate for Competition
 - Public Utility/Service Commissions are delegated the power - Quasi-Judicial power supported by state and federal courts

REGULATORY COMPACT

- Constitutional Right to Fair Return
 - Fifth and Fourteenth Amendment – Hope & Bluefield
 - (Bluefield v West Virginia 1923)
 - “Rates which are not sufficient to yield a reasonable return on the value of the property used in public service at the time it is being so used to render the service are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property, in violation of the Fourteenth Amendment of the Constitution.” **(Takings Clause)**
 - “Under the due process clause of the Fourteenth Amendment of the Constitution...a waterworks company is entitled to the independent judgment of the court as to both law and facts, where the question is whether the rates fixed by a public service commission are confiscatory.” **(Due Process Clause)**


REGULATORY COMPACT

- Federal Power Commission v. Hope Natural Gas (1944)
- “The rate-making function...involves the making of pragmatic adjustments, and the Commission is not bound to the use of any single formula or combination of formulae in determining rates.”
- “The fixing of just and reasonable rates by the Commission involves a **balancing of the investor and consumer interests.**”
- “As respects rates from the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business, and by such standard the return to the equity owner...**should be sufficient to assure confidence in the financial integrity of the enterprise so as to maintain its credit and attract capital.**”

REGULATORY COMPACT

- Utilities are allowed the “**opportunity**” to earn a **Fair Rate of Return on** their investments.
 - Investors are Stockholders and Bondholders
 - In order to provide “**opportunity**”, Utilities must also be allowed to recover **fair and reasonable** expenses associated with providing the service.
- 

RATE SETTING - PROCESS

- The Rate Case
 - Formal Process Held before a Commission
 - Commission generally delegates fact finding to a Hearing Examiner or Administrative Law Judge
 - “Generally” initiated by filing a rate change petition by the Utility – Statutes also provide the power for Commissions to initiate rate adjustments (i.e. changes in tax law significantly effecting expenses paid by consumers)
 - Parties to a Rate Case
 - The Utility
 - State Commission Staff
 - The Ratepayer Advocate
 - Intervenors (large users, municipalities, etc.)
 - Public Hearings
 - Evidentiary Hearings
 - Hearing Examiner/ALJ Initial Decision
 - State Utility Commission Final Decision
- 

RATE SETTING - THE FORMULA

$$\frac{\text{A: Net Operating Income}}{\text{B: Rate Base}} = \text{C: Rate of Return (ROR)}$$

DETERMINING A UTILITIES REVENUE REQUIREMENT



Artesian Water Company, Inc.
YTD Statement of Income
December 31, 2025

	2025 YTD	% of Revenue	2024 YTD	% of Revenue	Increase (Decrease)	% Incr/(Decr)
Revenue						
Water Sales	89,277,517	97.9%	86,266,438	97.9%	3,011,079	3.5%
Other Utility Operating Rev	1,879,368	2.1%	1,847,471	2.1%	31,897	1.7%
Non-Utility Operating Revenue	0	0.0%	2,229	0.0%	(2,229)	(100.0%)
Gain or Loss on Sale of Land	0	0.0%	0	0.0%	0	0.0%
	<u>91,156,886</u>	<u>100.0%</u>	<u>88,116,139</u>	<u>100.0%</u>	<u>3,040,747</u>	<u>3.5%</u>
Expense						
Utility Operations and Maintenance Expenses	44,111,955	48.4%	42,557,937	48.3%	1,554,018	3.7%
Non-Utility Operations and Maintenance Expenses	0	0.0%	0	0.0%	0	0.0%
Total Operations and Maintenance Expenses	<u>44,111,955</u>	<u>48.4%</u>	<u>42,557,937</u>	<u>48.3%</u>	<u>1,554,018</u>	<u>3.7%</u>
Depreciation and Amortization	12,890,956	14.1%	12,686,922	14.4%	204,035	1.6%
Federal and State Taxes	5,372,453	5.9%	5,154,775	5.8%	217,678	4.2%
Taxes-Property and Other	5,436,742	6.0%	5,606,465	6.4%	(169,723)	(3.0%)
	<u>67,812,106</u>	<u>74.4%</u>	<u>66,006,098</u>	<u>74.9%</u>	<u>1,806,008</u>	<u>2.7%</u>
Operating Income	<u>23,344,780</u>	<u>25.6%</u>	<u>22,110,040</u>	<u>25.1%</u>	<u>1,234,739</u>	<u>5.6%</u>
AFUDC	568,322	0.6%	429,863	0.5%	138,459	32.2%
Miscellaneous Income	1,222,948	1.3%	1,233,847	1.4%	(10,900)	(0.9%)
Total Income	<u>25,136,050</u>	<u>27.6%</u>	<u>23,773,751</u>	<u>27.0%</u>	<u>1,362,298</u>	<u>5.7%</u>
Interest Charges						
Long-Term Debt Interest	7,619,735	8.4%	7,689,110	8.7%	(69,375)	(0.9%)
Short-Term Debt Interest	64,178	0.1%	281,914	0.3%	(217,736)	(77.2%)
Amortization of Debt Expense	345,888	0.4%	346,643	0.4%	(755)	(0.2%)
Customer Deposit Int and Other	124,140	0.1%	129,319	0.1%	(5,179)	(4.0%)
	<u>8,153,942</u>	<u>8.9%</u>	<u>8,446,986</u>	<u>9.6%</u>	<u>(293,044)</u>	<u>(3.5%)</u>
Net Income	<u>16,982,108</u>	<u>18.6%</u>	<u>15,326,765</u>	<u>17.4%</u>	<u>1,655,342</u>	<u>10.8%</u>
Preferred Dividend Requirement	0	0.0%	0	0.0%	0	0.0%
Earnings Applicable to Common Stock	<u>16,982,108</u>	<u>18.6%</u>	<u>15,326,765</u>	<u>17.4%</u>	<u>1,655,342</u>	<u>10.8%</u>

RATE SETTING – THE FORMULA

A: Net Operating Income = C: Rate of Return
B: Rate Base (ROR)



Utility Plant paid for by investors

Investor is defined as having provided the Company with capital for which the only benefit received is a “return on” its investment

RATE SETTING

BASIS FOR SETTING RETURN ON AND OF ASSETS

B: Rate Base =

Cost of Utility Plant

Less: Accumulated Depreciation

Less: **Utility Plant Adjustments:**

Contributions in Aid of Construction

Advances in Aid of Construction

Deferred Tax Normalization

Add: **Other Investment Adjustments:**

Construction Work in Progress

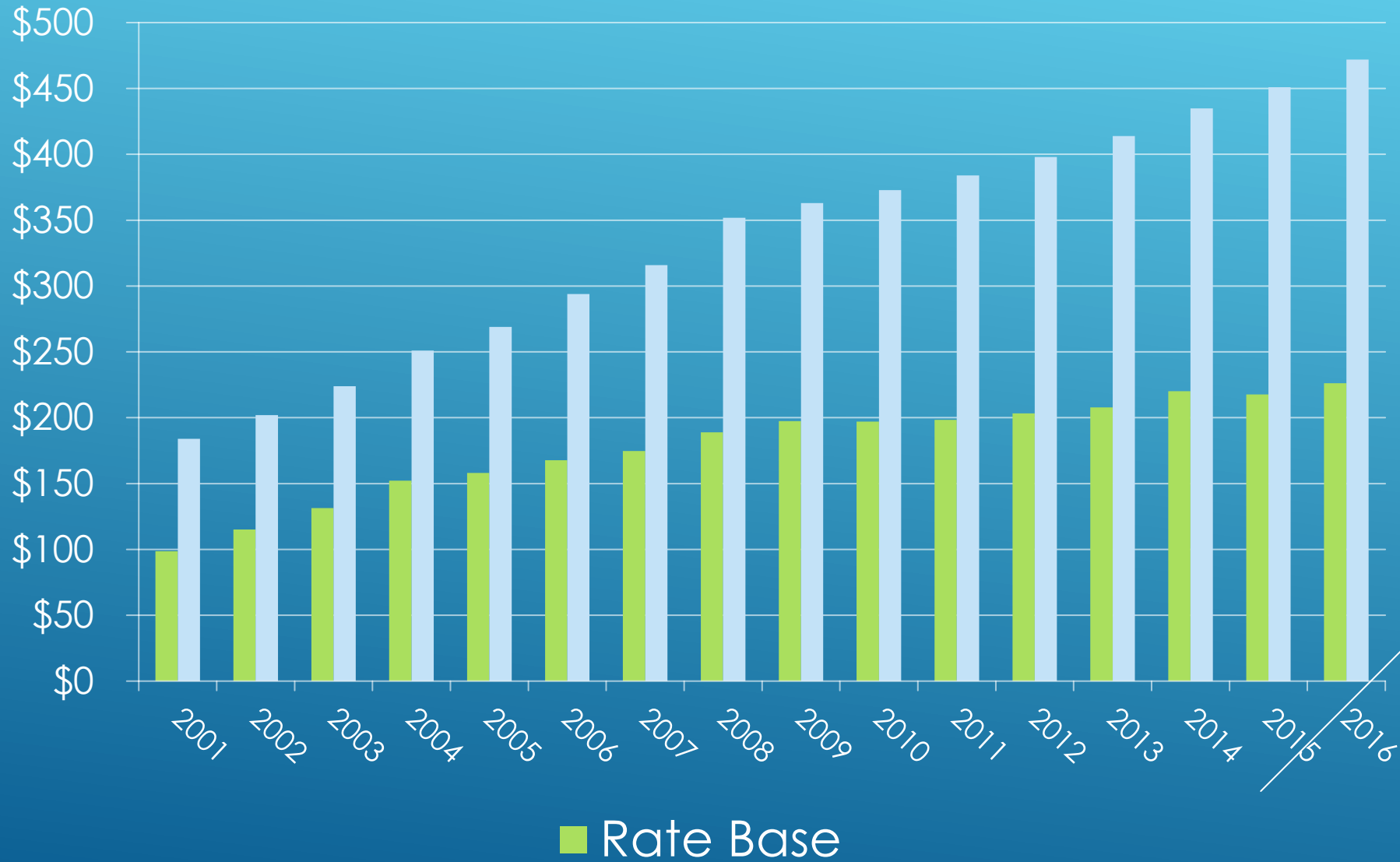
Materials and Supplies

Working Capital Allowance

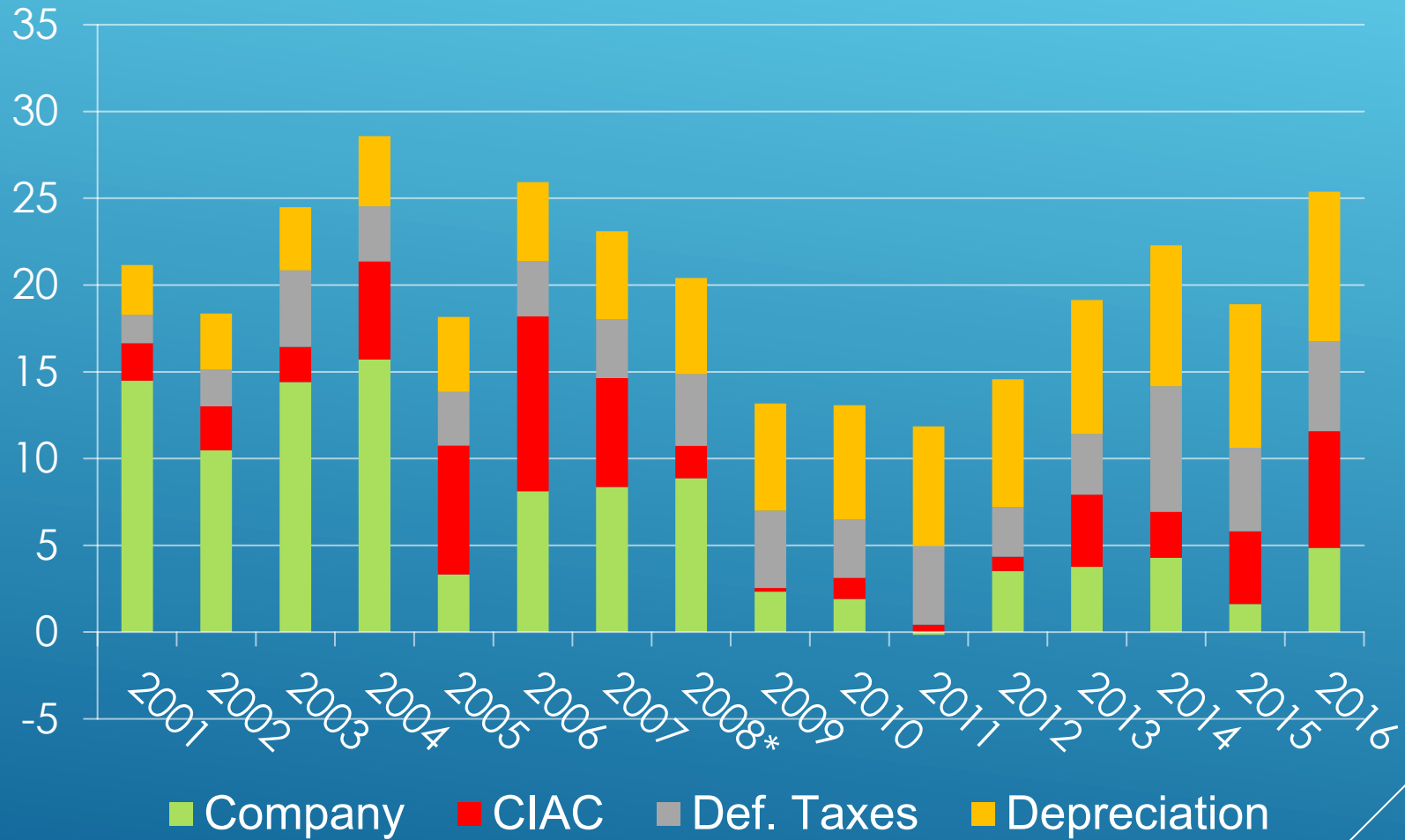
Special Amortizations

UTILITY PLANT / RATE BASE

(IN MILLIONS)



ANNUAL INVESTMENT IN PLANT



RATE SETTING - THE FORMULA

$$\frac{\text{A: Net Operating Income}}{\$ 359,183,000} = \text{C: Rate of Return (ROR)}$$

Return on Rate Base expected
by investors



C: COST OF CAPITAL

CAPITAL STRUCTURE AND RATE OF RETURN

GUASTELLA WATER COMPANY

Rate of Return Summary


Schedule D-1

(000's omitted)


Explanation and Comments

	<u>Reference Schedule</u>	<u>Amount</u>	<u>Percent</u>	<u>Cost Rate</u>	<u>Cost of Capital</u>
Long-term Debt	D-2	\$176,000	50.27%	5.24%	2.63%
Common Equity	D-3	\$174,126	49.73%	10.75%	5.35%
		<u>\$350,126</u>	100.00%		<u>7.98%</u>

Cost of Equity –What is it?

- A measure of expected return on an equity investment
 - In ratemaking process, the cost of equity is expressed as a percentage –profits relative to an equity investment
 - Should be from the vantage point of a rational investor
 - Long term horizon
 - Cost of equity cannot be measured –must be estimated
 - Typically expressed as a range of reasonableness
 - Several formulas which rely on financial markets' data available to help estimate the expected return
 - Still requires the use of a lot of judgement
- 

ROE BY THE NUMBERS

- Consultants Develop the range
 - DCF
 - CAPM
 - Risk Premium
 - Comparable Investments?
 - Water Utilities
 - Gas Utilities
- 

C: COST OF CAPITAL

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RATE SETTING - THE FORMULA


$$\frac{\text{A: Net Operating Income}}{\$ 359,183,000} = 7.98\% \text{ (ROR)}$$

Annual Revenue Requirement
and Net Income required to pay
expenses and a return expected by
investors



A: NET OPERATING INCOME

“THE INCOME STATEMENT”

- ▶ Historical - Represents the fiscal (annual) results of operation; revenues received, expenses paid or accrued, including taxes (income or other) as required.
- ▶ Rate Making - Represents the amount of money necessary to pay expenses, taxes and everything necessary to provide utility service to customers including a fair return to the utilities investors EVERY YEAR.

“DURING THE RATE EFFECTIVE PERIOD”



A: NET OPERATING INCOME

“THE INCOME STATEMENT”

Gross Operating Revenue

Less:

Operation Expenses

Maintenance Expenses

Depreciation Expense

Taxes-Other Than Income

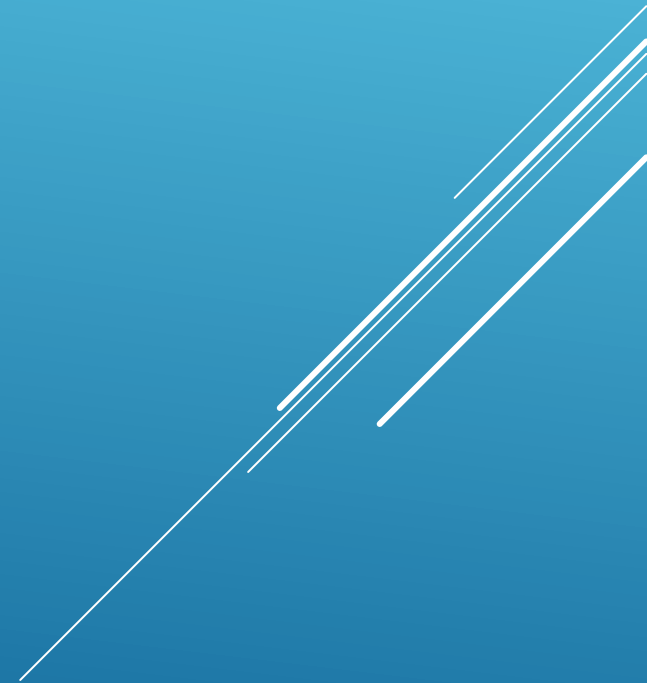
Income Taxes

Net (Utility) Operating Income

Return to Investors



“The Line”



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TYPES OF ADJUSTMENTS

- **Accounting Corrections**
 - Errors
 - Out-of-period entries
(E.g., thirteen months of rent recorded in the historical base year)
- **Regulatory accounting adjustments**
 - Expenses OK for GAAP, but not allowed for ratemaking
(E.g., lobbying, charitable donations)
 - Non-utility operations
- **Proforma adjustments -for changes that are expected to happen for the test year**
 - Estimates
 - Normalization
 - Annualization
 - Attrition
 - Deferred expenses (reg assets)
 - Historical costs requested to be recovered in the future

INCOME STATEMENT

GUASTELLA WATER COMPANY Operating Income Statement Schedule C-1 (S000's omitted)

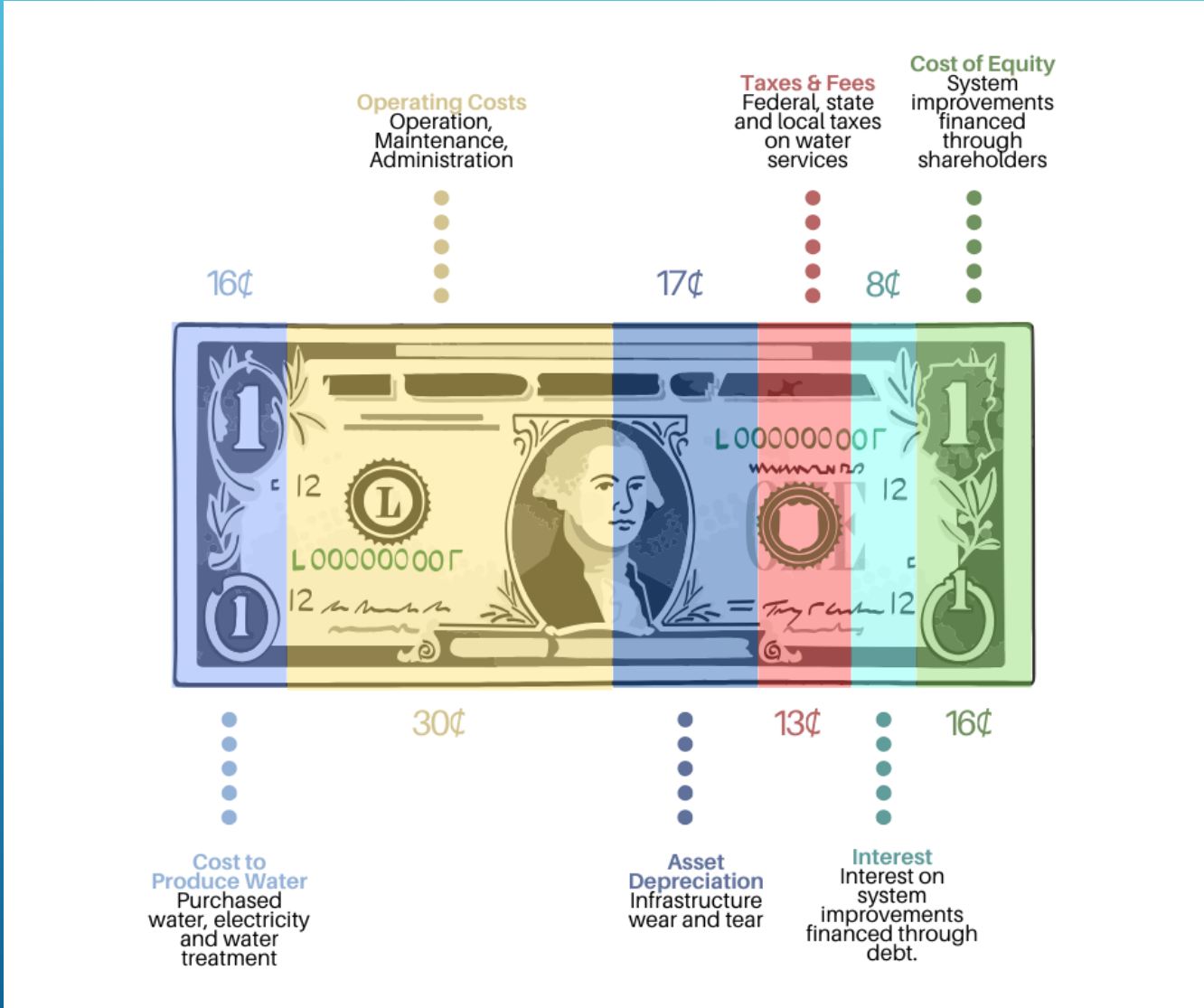
	2025		Present		2027
	<u>Actual</u>	<u>Sch</u>	<u>Adjustments</u>	<u>No.</u>	<u>Rate</u>
					<u>Proposed</u>
					<u>Rates</u>
					<u>Increase</u>
Operating Revenues	\$78,119	C-2	2,628	(1)	\$78,237
			(1,467)	(2)	\$18,123
			(1,043)	(3)	\$96,360
Expenses:					
Labor		C-3	2,108	(4)	
Fringe Benefits		C-4	843	(5)	
Locate Curb Boxes		C-5	130	(6)	
Power		C-6	700	(7)	
Chemicals		C-7	159	(8)	
Rate Case Expenses		C-8	500	(9)	
SDWA Studies		C-9	62	(10)	
Tank Painting		C-10	42	(11)	
Lobbying Expense		C-11	100	(12)	
Productivity		C-12	(28)	(13)	
Filtration Repairs		C-13	15	(14)	
Storm Damage Costs		C-14	450	(15)	
Inflation		C-15	1,476	(16)	
Total O & M	<u>37,084</u>		<u>6,557</u>		<u>43,641</u>
Depreciation	11,734	C-16	1,076	(17)	12,810
Taxes Other Than Income	5,226	C-17	265	(18)	5,491
Federal Income Taxes	3,518	C-18	(2,033)	(19)	1,486
Total Expenses	57,562		5,865		63,428
Operating Income	20,557		(5,747)		14,809
Interest Expense	7,040	C-19	2,180	(20)	9,220
Net Income	<u>\$13,517</u>		<u>(7,927)</u>		<u>\$5,589</u>
Rate Base	<u>\$315,808</u>	B-1			<u>\$359,183</u>
Return on Rate Base	<u>6.51%</u>	D-1			<u>4.12%</u>
					<u>7.98%</u>

RATE SETTING - THE FORMULA

$$\frac{\text{A: } \$ 19,441,000}{\text{B: } \$359,183,000} = \text{C: } 7.98\%$$

(ROR)

What Each Rate Dollar Represents to Utility



Allocating Costs to Customer Rates

Artesian Water Company Inc.			Total System						
Functionalization of Expenses	Functional Factor	Test Year Period	Base	Maximum Day	Peak Hour	Meters and Services	Billings and Accounting	Hydrants	
O&M Expenses									
Source of Supply Expense									
602.000 Purchased Water	Base	\$ 1,605,106	\$ 1,605,106	\$ -	\$ -	\$ -	\$ -	\$ -	
603.000 Miscellaneous Expenses	Base / MaxDay	-	-	-	-	-	-	-	
604.000 Rents - Source of Supply	Base / MaxDay	27,720	20,000	7,720	-	-	-	-	
614.000 Maintenance of Wells (Labor)	Base / MaxDay	42,096	30,372	11,724	-	-	-	-	
614.000 Maintenance of Wells	Base / MaxDay	248,708	179,442	69,267	-	-	-	-	
614.001 Wk Pay - Monitoring Wells	Base / MaxDay	-	-	-	-	-	-	-	
Total Source of Supply Expense		\$ 1,923,629	\$ 1,834,919	\$ 88,711	\$ -	\$ -	\$ -	\$ -	
Pumping Expenses									
623.000 Purchased Power	Base	\$ 3,838,092	3,838,092	-	-	-	-	-	
624.000 Pumping Labor and Expenses (Labor)	Base / MaxDay / PeakHr	1,313,644	563,058	217,347	533,238	-	-	-	
624.000 Pumping Labor and Expenses	Base / MaxDay / PeakHr	100,540	43,094	16,635	40,811	-	-	-	
626.000 Miscellaneous Expenses - Pumping (Labor)	Base / MaxDay / PeakHr	382,417	163,913	63,272	155,232	-	-	-	
626.000 Miscellaneous Expenses - Pumping	Base / MaxDay / PeakHr	40,766	17,473	6,745	16,548	-	-	-	
630.000 Other Pumping Equipment	Base / MaxDay / PeakHr	91,811	39,352	15,191	37,268	-	-	-	
631.000 Maint of Structures (Labor)	Base / MaxDay / PeakHr	572,257	245,282	94,682	232,292	-	-	-	
631.000 Maint of Structures	Base / MaxDay / PeakHr	175,442	75,198	29,028	71,216	-	-	-	
632.000 Maint of SCADA - Parts & Supply	Base / MaxDay / PeakHr	12,156	5,210	2,011	4,934	-	-	-	
633.000 Maint of Pumping Equipment (Labor)	Base / MaxDay / PeakHr	2,795,472	1,198,203	462,522	1,134,747	-	-	-	
633.000 Maint of Pumping Equipment	Base / MaxDay / PeakHr	329,567	141,260	54,528	133,779	-	-	-	
Total Pumping Expenses		\$ 9,652,164	\$ 6,330,137	\$ 961,961	\$ 2,360,066	\$ -	\$ -	\$ -	
Water Treatment									
641.000 Chemicals	Base	\$ 2,085,298	\$ 2,085,298	\$ -	\$ -	\$ -	\$ -	\$ -	
642.000 Chemicals - Labor and Expenses (Labor)	Base / MaxDay	649,073	468,303	180,771	-	-	-	-	
642.000 Chemicals - Labor and Expenses	Base / MaxDay	707,140	510,197	196,942	-	-	-	-	
643.000 Chemicals - MISC	Base / MaxDay	256,759	185,250	71,509	-	-	-	-	
652.000 Maint Of Water Treatment Equip	Base / MaxDay	2,088,504	1,506,844	581,661	-	-	-	-	
Total Water Treatment Expenses		\$ 5,786,775	\$ 4,755,892	\$ 1,030,883	\$ -	\$ -	\$ -	\$ -	
Transmission & Distribution Expense									
663.000 Meter Expenses (Labor)	Meters & Services	933,324	-	-	-	933,324	-	-	
663.000 Meter Expenses	Meters & Services	146,151	-	-	-	146,151	-	-	
665.000 T&D - MISC Expenses (Labor)	Other T&D	649,327	45,786	-	186,116	377,199	-	40,227	
665.000 T&D - MISC Expenses	Other T&D	7,237	510	-	2,074	4,204	-	448	
670.000 Biwk Pay-Maint Supr T&D Main (Labor)	Other T&D	95,305	6,720	-	27,317	55,363	-	5,904	
672.000 Maint of Distribution Reservoirs	Peak Hour	996,743	-	-	996,743	-	-	-	
673.000 Maint of T&D Mains (Labor)	Base / Peak Hour	0	0	-	0	-	-	-	
673.000 Maint of T&D Mains	Base / Peak Hour	851,245	364,863	-	486,382	-	-	-	
675.000 Maint of T&D Services (Labor)	Meters & Services	1,569,317	-	-	-	1,569,317	-	-	
675.000 Maint of T&D Services	Meters & Services	131,849	-	-	-	131,849	-	-	
676.000 Maint of Meters (Labor)	Meters & Services	163,986	-	-	-	163,986	-	-	
676.000 Maint of Meters	Meters & Services	61,211	-	-	-	61,211	-	-	
677.000 Maint of Hydrants (Labor)	Hydrants	264,219	-	-	-	-	-	264,219	
677.000 Maint of Hydrants	Hydrants	56,341	-	-	-	-	-	56,341	
678.000 Maint of Misc Plant	Other T&D	12,005	847	-	3,441	6,974	-	744	
Total T&D Expense		\$ 5,938,261	\$ 418,727	\$ -	\$ 1,702,073	\$ 3,449,578	\$ -	\$ 367,883	


Allocating Costs to Customer Rates

Artesian Water Company Inc. Total System Allocation	Total System Test Year Total	Residential	All Other	CCH	Misc. Other Use	Fire Capacity	Fire Hydrants
Rate Base							
Total Rate Base							
Base	\$ 150,176,608	\$ 91,949,598	\$ 44,282,949	\$ 2,137,215	\$ 96,662	\$ 1,620,082	\$ -
Maximum Day	27,866,983	14,947,039	6,274,390	440,833	13,696	2,080,692	-
Peak Hour	130,851,926	69,998,776	30,630,612	1,938,432	66,862	27,236,237	-
Meters and Services	50,882,765	39,284,653	5,633,262	20,932	-	5,826,339	-
Billings and Accounting	294,326	278,773	13,098	6	-	2,449	-
Hydrants	5,970,847	-	-	-	-	-	5,970,847
Total Total Rate Base	\$ 366,043,456	\$ 216,458,839	\$ 86,834,312	\$ 4,537,417	\$ 177,220	\$ 36,765,799	\$ 5,970,847
Required Income							
Base	\$ 11,128,737	\$ 6,813,863	\$ 3,281,558	\$ 158,377	\$ 7,163	\$ 120,055	\$ -
Maximum Day	2,065,064	1,107,640	464,959	32,668	1,015	154,188	-
Peak Hour	9,696,694	5,187,212	2,269,861	143,646	4,955	2,018,323	-
Meters and Services	3,770,633	2,911,163	417,449	1,551	-	431,757	-
Billings and Accounting	21,811	20,658	971	0	-	181	-
Hydrants	442,466	-	-	-	-	-	442,466
Total Required Income	\$ 27,125,405	\$ 16,040,537	\$ 6,434,798	\$ 336,242	\$ 13,133	\$ 2,724,505	\$ 442,466

Allocating Costs to Customer Rates

Artesian Water Company Inc.							
Class Cost of Service Summary	Test Year Total	Residential	All Other	CCH	Misc. Other Use	Fire Capacity	Fire Hydrants
Rate Base	\$ 366,043,456	\$ 216,458,839	\$ 86,834,312	\$ 4,537,417	\$ 177,220	\$ 36,765,799	\$ 5,970,847
Rate of Return	7.4104%	7.4104%	7.4104%	7.4104%	7.4104%	7.4104%	7.4104%
Required Operating Income	\$ 27,125,405	\$ 16,040,537	\$ 6,434,798	\$ 336,242	\$ 13,133	\$ 2,724,505	\$ 442,466
Operating Expenses							
O&M	\$ 48,387,061	\$ 31,284,631	\$ 9,946,411	\$ 476,776	\$ 18,971	\$ 3,402,576	\$ 930,606
Depreciation	13,001,378	7,923,908	2,869,325	141,568	5,502	1,299,507	254,023
Taxes	11,595,901	6,960,311	2,634,118	135,038	5,258	1,136,552	250,453
Total Operating Expenses	\$ 72,984,339	\$ 46,168,849	\$ 15,449,854	\$ 753,381	\$ 29,732	\$ 5,838,635	\$ 1,435,081
Total Revenue Requirement	\$ 100,109,744	\$ 62,209,387	\$ 21,884,653	\$ 1,089,623	\$ 42,865	\$ 8,563,140	\$ 1,877,547
Other Revenues	1,840,070	1,143,441	402,251	20,028	788	157,395	34,510
Sales Revenue Requirement	\$ 98,269,674	\$ 61,065,945	\$ 21,482,401	\$ 1,069,595	\$ 42,077	\$ 8,405,745	\$ 1,843,037
Functional Breakdown							
Base	\$ 38,948,195	\$ 23,650,702	\$ 11,390,184	\$ 549,721	\$ 24,863	\$ 416,707	-
Maximum Day	8,075,552	4,608,685	1,934,610	135,924	4,223	641,549	-
Peak Hour	25,896,478	13,600,416	5,951,377	376,628	12,991	5,291,866	-
Meters and Services	17,505,820	13,523,680	1,939,242	7,206	-	2,005,708	-
Billings and Accounting	6,000,593	5,682,462	266,989	117	-	49,914	-
Hydrants	1,843,037	-	-	-	-	-	1,843,037
Sales Revenue Requirement	\$ 98,269,674	\$ 61,065,945	\$ 21,482,401	\$ 1,069,595	\$ 42,077	\$ 8,405,745	\$ 1,843,037
Current Revenues	\$ 87,419,753	\$ 54,613,782	\$ 19,149,986	\$ 490,940	\$ 75,399	\$ 9,575,673	-
Increase \$	\$ 10,849,921	\$ 6,452,163	\$ 2,332,415	\$ 578,655	\$ (33,322)	\$ 673,108	-
Increase %	12.4%	11.8%	12.2%	117.9%	-44.2%	7.0%	-
Wholesale Increase %	24.1%	-	-	-	-	-	-

Alternative Ratemaking

- Alternative Rate Mechanisms
 - Distribution System Improvement Charge (DSIC)
 - Expense Adjustment Clauses (purchased water, electric)
 - Revenue Stabilization
 - Forecasted Test Years
 - Water Revenue Adjustment Mechanism (WRAM) Connecticut
 - Extended Projected Test Periods – California 3yr
 - Multi-year rate increase plans – Phase-in or Investment recog.
 - Inclining Block Rates, Low-income Rates, Economic Development Rates
 - Implementation of Advanced Metering Infrastructure – will allow more intuitive pricing (i.e. demand, time of day use)
- 

NARUC Board of Directors Resolution Supporting Consideration of Regulatory Policies Deemed as “Best Practices”

“...Due to the massive capital investment required to meet current and future water quality and infrastructure requirements, adequately adjusting allowed equity returns to recognize industry risk in order to provide a fair rate of return on invested capital was recognized as crucial...”

MACRUC 2026

31ST ANNUAL EDUCATION CONFERENCE

Rate Making 101

David Spacht, CFO

Artesian Water Company Inc.



Rate Making 101