

COMMONWEALTH OF PENNSYLVANIA



OFFICE OF CONSUMER ADVOCATE

555 Walnut Street, 5th Floor, Forum Place
Harrisburg, Pennsylvania 17101-1923
(717) 783-5048
800-684-6560

FAX (717) 783-7152
consumer@paoca.org

July 19, 2016

Rosemary Chiavetta, Secretary
PA Public Utility Commission
Commonwealth Keystone Bldg.
400 North Street
Harrisburg, PA 17120

Re: Joint Application of Pennsylvania-American Water Company and the Sewer Authority of the City of Scranton for Approval of (1) the transfer, by sale, of substantially all of the Sewer Authority of the City of Scranton's Sewer System and Sewage Treatment Works assets, properties and rights related to its wastewater collection and treatment system to Pennsylvania-American Water Company, and (2) the rights of Pennsylvania-American Water Company to begin to offer or furnish wastewater service to the public in the City of Scranton and the Borough of Dunmore, Lackawanna County, Pennsylvania.
Docket No. A-2016-2537209

Dear Secretary Chiavetta:

Attached for electronic filing please find the Office of Consumer Advocate's Main Brief in the above-referenced proceeding.

Copies have been served per the attached Certificate of Service.

Respectfully submitted,

/s/ Erin L. Gannon

Erin L. Gannon
Senior Assistant Consumer Advocate
PA Attorney I.D. # 83487
E-Mail: EGannon@paoca.org

Enclosures

cc: Honorable David A. Salapa, ALJ
Honorable Steven K. Haas, ALJ
Certificate of Service

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Joint Application of Pennsylvania-American :
Water Company and the Sewer Authority :
of the City of Scranton for Approval of :
(1) the transfer, by sale, of substantially all :
of the Sewer Authority of the City of Scranton's :
Sewer System and Sewage Treatment Works : Docket No. A-2016-2537209
assets, properties and rights related to its :
wastewater collection and treatment system to :
Pennsylvania-American Water Company, and :
(2) the rights of Pennsylvania-American Water :
Company to begin to offer or furnish wastewater :
service to the public in the City of Scranton and :
the Borough of Dunmore, Lackawanna County, :
Pennsylvania.

I hereby certify that I have this day served a true copy of the following document, the Office of Consumer Advocate's Main Brief, upon parties of record in this proceeding in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

Dated this 19th day of July 2016.

SERVICE BY E-MAIL AND INTER-OFFICE MAIL

Allison C. Kaster, Esquire
Gina L. Lauffer, Esquire
Bureau of Investigation & Enforcement
Pennsylvania Public Utility Commission
400 North Street
Harrisburg, PA 17120

SERVICE BY E-MAIL AND FIRST CLASS MAIL, POSTAGE PREPAID

Sharon Webb, Esquire
Office of Small Business Advocate
Suite 202, Commerce Building
300 N. Second Street
Harrisburg, PA 17101

Alan Michael Seltzer, Esq.
John F. Povilaitis
Buchanan Ingersoll &Rooney PC
409 North Second Street, Suite 500
Harrisburg, PA 17101

David P. Zambito, Esq.
D. Troy Sellars
Cozen O'Connor
17 North Second Street, Suite 1410
Harrisburg, PA 17101

Susan Simms Marsh, Esquire
Pennsylvania American Water
800 West Hersheypark Drive
Hershey, Pennsylvania 17033

SERVICE BY FIRST CLASS MAIL, POSTAGE PREPAID

Jeffrey J. Belardi, Esquire
The Sewer Authority of the
City of Scranton
410 Spruce Street, 4th Floor
Scranton, PA 18503

Paul J. Walker, Esquire
The Sewer Authority of the
City of Scranton
205 North Washington Ave. #1
Scranton, PA 18503

/s/ Erin L. Gannon
Erin L. Gannon
Senior Assistant Consumer Advocate
PA Attorney I.D. # 83487
E-Mail: EGannon@paoca.org

Christine Maloni Hoover
Senior Assistant Consumer Advocate
PA Attorney I.D. # 50026
E-Mail: CHoover@paoca.org

Counsel for
Office of Consumer Advocate
555 Walnut Street
5th Floor, Forum Place
Harrisburg, PA 17101-1923
Phone: (717) 783-5048
Fax: (717) 783-7152
223873

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Pennsylvania.

MAIN BRIEF OF THE
OFFICE OF CONSUMER ADVOCATE

Christine Maloni Hoover
Senior Assistant Consumer Advocate
PA Attorney I.D. # 50026
E-Mail: CHoover@paoca.org

Erin L. Gannon
Senior Assistant Consumer Advocate
PA Attorney I.D. # 83487
E-Mail: EGannon@paoca.org

Counsel for:
Tanya J. McCloskey
Acting Consumer Advocate

Office of Consumer Advocate
555 Walnut Street
5th Floor, Forum Place
Harrisburg, PA 17101-1923
Phone: (717) 783-5048
Fax: (717) 783-7152
Dated: July 19, 2016

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I. INTRODUCTION

Pennsylvania-American Water Company, Inc. and the Sewer Authority of the City of Scranton, seek approval for PAWC to acquire the combined stormwater and wastewater collection and treatment assets of SSA and serve its existing 31,000 customers in the City of Scranton and Borough of Dunmore. The Public Utility Commission must deny the Application if it finds that it does not have jurisdiction over the assets being transferred, which provide wastewater and stormwater services. Also, the Commission must deny the Application if it finds that the acquisition by PAWC is not in the public interest and does not provide a substantial, affirmative benefit. 66 Pa. C.S. §§ 1102(a)(2), 1103(a); City of York v. Pa. P.U.C., 449 Pa. 136, 141, 295 A.2d 825, 828 (1972). The OCA respectfully submits that the Application fails on both counts and must be denied.

The Public Utility Code does not authorize the acquisition of stormwater facilities and provision of stormwater service to and by a regulated public utility. 66 Pa. C.S. §§ 102, 1102. The fact that stormwater service and wastewater service are provided in a combined system does not make them a single service subject to Commission regulation; much as the fact that when electric distribution services and electric supply service or local telephone, long distance telephone and television services are provided over the same physical facilities, they do not become a single service subject to Commission regulation. Tr. 97. As such, the Commission is unable to authorize the proposed acquisition and provision of stormwater service by PAWC.

The Office of Consumer Advocate (OCA) also submits that the harms of this transaction outweigh any alleged benefit provided by the agreement between PAWC and the Authority, and the proposed transfer is not in the public interest. The proposed transaction will only increase costs for PAWC's wastewater and water customers with no benefits in the short or long term.

For these reasons, the Commission must reject the Application. In the alternative, the Commission has the authority to impose conditions on its approval of the acquisition and should ensure that stormwater costs are separately allocated to Scranton customers.

A. Description of the System

The Sewer Authority of the City of Scranton's (SSA) system consists of 317 miles of collection sewers and large interceptors, 80 combined sewer overflows (CSOs), seven pumping stations, and a wastewater treatment plant (WWTP). Fifty-four percent of the collection sewers, *i.e.* 172 miles, are "combined sewers" which convey both stormwater and wastewater. OCA St. 1 at 2. When the total flow of wastewater and stormwater in the combined sewers exceeds the capacity of the interceptor sewers, pumping stations and/or treatment plant, partially treated or untreated flow is discharged to the Lackawanna River and nearby streams via CSOs. Id.

Other portions of the City and the Borough are served by separate wastewater sewers and MS4 storm sewers. PAWC intends to acquire the combined stormwater/wastewater facilities owned by SSA including the wastewater sewers in the MS4 area but excluding the storm sewers in the MS4 area. OCA St. 1 at 3.

In the Combined Sewer System (CSS), there are 80 permitted CSO discharge points including the WWTP headworks bypass, and 4 pumping station overflow outlets. Under the Federal CSO Policy, the SSA entered into a consent decree under which, among other things, the SSA adopted a 25-year Long Term Control Plan (LTCP) in 2012. The Authority is also implementing an approved Nine Minimum Controls (NMC) program.¹ Id.

¹ Improvements to the combined sewer system and the wastewater treatment plant must be made to reduce CSO discharges to no more than 4 overflow events year during the typical year for outfalls that discharge into non-channelized, tributary streams and no more than 9 overflow events during the typical year for CSO outfalls that discharges to either channelized tributary streams or to the Lackawanna River. OCA St. 1 at 3. Based on a hydraulic model of the combined sewer system, implementation of these

B. Overview of the Proposed Transaction

Pennsylvania-American Water Company is proposing to purchase most of the assets of the Authority for a stated purchase price of \$195 million subject to various adjustments at closing.² The purchase price includes the transfer of more than \$38 million in cash balances from the Authority to PAWC, so the net purchase price for the SSA's physical assets is approximately \$157 million. The SSA assets have a net book value of less than \$74 million.³

The assets to be purchased constitute the Authority's CSS, which includes facilities that are used for the collection, transmission, retention, and treatment of both wastewater and stormwater for approximately 31,000 customers in the City of Scranton and Borough of Dunmore.⁴

The Asset Purchase Agreement contains a number of other terms and conditions. Among the most important is a requirement that PAWC either limit the amount that it charges to SSA customers for the next 10 years or pay an enhancement to the purchase price at the end of the 10 years.⁵

C. Procedural History

On March 30, 2016, PAWC and SSA jointly filed an Application to transfer all the assets of the Authority's sewer system and sewage treatment works to PAWC and for PAWC to render wastewater service in the areas served by Scranton. On April 9, 2016, Notice of the Application was published in the Pennsylvania Bulletin establishing an April 25, 2016 deadline for submission of protests and petitions to intervene. On April 5, 2016, the OCA filed a Protest to

improvements and the NMC measures will result in at least 90 percent system-wide wet weather capture in a typical year. Id.

² PAWC Exh. BCG-1, Att. F (Section 3.01).

³ OCA St. 2 at 25 (citing SSA Annual Report, Balance Sheet as of Mar. 31, 2015).

⁴ PAWC Exh. BCG-1 at 3-4.

⁵ PAWC Exh. BCG-1, Att. F (Section 7.07(d)).

the Joint Application. The Bureau of Investigation and Enforcement filed a Notice of Appearance on April 8, 2016.

The matter was assigned to the Office of Administrative Law Judge and was further assigned to Administrative Law Judge (ALJ) Ember S. Jandebour. A Hearing Notice was issued on April 20, 2016, and an in-person Prehearing Conference was scheduled for May 10, 2016 at 10:00 a.m. in Scranton. On April 25, 2016, the Office of Small Business Advocate filed an Answer, Notice of Intervention and Public Statement.

A Hearing Notice was issued on April 27, 2016, scheduling a telephonic Prehearing Conference on May 10, 2016 at 10:00 a.m. and the case was then reassigned to ALJ David Salapa and ALJ Steven K. Haas. A Prehearing Conference Order was issued on April 27, 2016, directing the parties to provide Prehearing Memorandum by May 6, 2016.

On May 10, 2016, a Prehearing Conference was held, at which time a procedural schedule was established. PAWC and Scranton filed a Motion to amend Exhibit L of their Joint Application on May 13, 2016 and no Answers were filed to the Motion.

Direct Testimony was submitted by the Joint Applicants on May 13, 2016. The OCA, I&E and OSBA submitted Direct Testimony on June 14, 2016.⁶ Rebuttal Testimony was

⁶ The OCA presented testimony by two expert witnesses. A list of all OCA-sponsored exhibits is attached as Appendix A, hereto.

Terry L. Fought is a consulting engineer with more than forty years' experience as a civil engineer. Mr. Fought is a registered Professional Engineer in Pennsylvania, New Jersey and Virginia and is a Professional Land Surveyor in Pennsylvania. Mr. Fought has prepared studies related to and designed water supply, treatment, transmission, distribution and storage for private and municipal wastewater agencies. He has also served as a consultant to the OCA for numerous water and sewer matters since 1984. Mr. Fought's background and qualifications are attached to OCA St. 1, as Appendix A.

Scott J. Rubin is an independent attorney and public utility industry consultant under contract with the OCA who has testified as an expert witness before utility commissions and courts in seventeen states and the District of Columbia and province of Nova Scotia. OCA St. 2 at 1-2. Since 1984, Mr. Rubin has provided legal and consulting services to a variety of parties interested in public utility regulatory proceedings. Id., App. A.

submitted by the Joint Applicants on June 24, 2016. Evidentiary hearings were held on July 6-8, 2016, where the OCA submitted Surrebuttal Testimony, the Joint Applicants provided Rejoinder Testimony and all parties had the opportunity to conduct cross-examination.

The OCA now files this brief presenting its recommendations to the ALJ and the Commission in this proceeding.

II. BURDEN OF PROOF

Under Sections 315(c) and 332 of the Public Utility Code, the burden of proof rests with the Joint Applicants. Section 332 states:

(a) Burden of proof. - Except as may be otherwise provided in section 315 (relating to burden of proof) or other provisions of this part or other relevant statute, the proponent of a rule or order has the burden of proof.

66 Pa. C.S. § 332. Section 315(c) places the burden of proof upon the Joint Applicants. It states that:

In any proceeding upon the motion of the commission, involving the service or facilities of any public utility, the burden of proof to show that the service and facilities involved are adequate, efficient, safe, and reasonable shall be upon the public utility.

66 Pa. C.S. § 315(c). Therefore, it is the Joint Applicants that have the burden of demonstrating by a preponderance of the evidence that the proposed acquisition by PAWC meets the requirements of Pennsylvania law.

III. SUMMARY OF ARGUMENT

The Public Utility Code does not authorize the proposed acquisition by PAWC of the Scranton Sewer Authority's stormwater assets and the provision of stormwater service to the public by a public utility for compensation. The fact that stormwater service and wastewater service are provided in a combined system does not make them a single service subject to Commission regulation; much as the fact that when electric distribution services and electric supply service or local telephone, long distance telephone and television services are provided over the same physical facilities, they do not become a single service subject to Commission regulation. Also, it is not consistent with public policy in Pennsylvania for a privately-owned utility to provide stormwater service to the public.

In addition to the legal and policy issues presented by the proposed acquisition of a combined stormwater/wastewater system, the proposed transfer has not been shown to provide affirmative public benefits. The purchase price is a total of \$260 million or more for SSA assets with a net book value of less than \$74 million which is not reasonable. In addition, PAWC expects its existing water customers to provide nearly one half of the purchase price, or at least \$104 million over the next 10 years. There is additional detriment to the public due to the lack of any significant savings in the cost to own and operate the SSA system. Further, PAWC's existing customers would not receive any benefit from the proposed transaction because the total customer count is not increasing. It is likely that the existing customers will see substantial detriment because of the proposed ratemaking treatment related to revenue sharing of wastewater costs onto water customers. These provisions of the transaction result in no benefits to the public from the proposed transaction and a very high likelihood that there will be a substantial detriment to the public. For these reasons, the Commission must reject the Application.

If the Commission determines to permit the Application to proceed, and permit an investor-owned public utility to provide stormwater service to the public, it must condition the approval by requiring the utility to develop separate rates and charges for the stormwater service to its customers and other entities who may not be wastewater customers. This separation requirement should include a plan by the Company to determine how it will identify and bill the responsible parties for stormwater service. In addition, the Commission must condition its approval to prevent PAWC's existing customers from paying at least \$104 million over the next 10 years to subsidize the purchase price. Further, the Commission must condition its approval to prohibit the Company from using the revenue sharing provision of Section 1311(c) for the SSA purchase for at least 10 years after closing.

IV. ARGUMENT

A. The PUC Has Jurisdiction Over Wastewater Services But Not Stormwater Services.

PAWC seeks Commission approval to (1) acquire the SSA sewer system and sewage treatment works related to, or used in connection with, its wastewater collection and treatment system (2) begin providing wastewater service in the areas served by the Authority and (3) begin charging rates for that service. Application at 1, Exh. L. The SSA system, however, provides two distinct services. It is a “combined sewer system,” which provides wastewater service and stormwater service. PAWC seeks approval to recover all costs associated with the combined system through rates. The PUC, however, does not have jurisdiction over the provision of stormwater service and cannot authorize PAWC to provide stormwater service for compensation.

The Public Utility Code defines a “public utility” as “[a]ny person or corporations now or hereafter owning or operating in this Commonwealth equipment or facilities for . . . sewage collection, treatment, or disposal for the public for compensation.” 66 Pa. C.S. § 102(1)(vii). The Public Utility Code does not address stormwater.

Wastewater and stormwater are distinct services. The United States Environmental Protection Agency (USEPA) defines a combined sewer system as a network that “collects rainwater runoff, domestic sewage, and industrial wastewater into one pipe.”⁷ OCA St. 1 at 5; OCA St. 2 at 7. OCA witness Rubin explained the three types of flows:

Domestic sewage (the more common term now is domestic wastewater) is perhaps the easiest to understand: it is the waste that flows from indoor drains (sinks, showers, toilets, etc.) in residential buildings. It also includes similar types of wastewater from sinks and toilets in commercial and industrial buildings.

Industrial wastewater is liquid waste from industrial processes that may have chemical, biological, and/or physical characteristics that are very different from domestic wastewater. Those differences have led to numerous legal and

⁷ USEPA, Combined Sewer Overflows, <https://www.epa.gov/npdes/combined-sewer-overflows-csos>.

regulatory requirements that require the pretreatment of industrial wastewater before it can be introduced into a system designed to treat domestic sewage. Domestic wastewater and industrial wastewater usually are referred to in the industry by the generic term wastewater.

Rainwater runoff, which is more commonly referred to by the broader label of stormwater (since it can include both rainwater runoff and water from the melting of snow and ice) is water that falls on streets, roofs, driveways, parking lots, bare soil, and other surfaces. In order to prevent flooding of properties and roadways, the water is collected and transported, usually through a series of culverts, storm drains, and pipes, to a nearby waterway (stream, river, lake, or ocean). Stormwater usually is not subject to treatment (unless it is combined with wastewater), but it may be subject to various restrictions and limitations under discharge permits. Indeed, those stormwater discharge requirements have become more stringent during the past 20 to 25 years which has led to a separate focus on the way in which stormwater removal costs are collected by the stormwater service provider.

OCA St. 2 at 8-9. The collection of “domestic sewage” and “industrial wastewater” is wastewater service, which is regulated under the Public Utility Code. The “rainwater runoff” is stormwater, which is not a service under the Public Utility Code.

As recognized by PAWC witness Elliot, current engineering practice for sewer systems involves the design of separate systems for wastewater and stormwater runoff. Tr. 145 (“They are – well, combined sewer systems are no longer designed”). In these separate systems, “[w]astewater is conveyed to a wastewater treatment plant and stormwater is generally discharged without treatment to a receiving water.” OCA St. 1 at 5-6. This is consistent with the Pennsylvania Department of Environmental Protection’s (PaDEP) position, as of 1997:

In general, the Department will approve plans for new sewer systems or extensions to systems only when designed as separate sanitary sewers in which water from roof drains, streets, and other areas and groundwater from foundation drains are excluded. Sewers which are designed to carry both sanitary wastewater and stormwater will not normally be approved.

OCA St. 1 at 6 (citing Domestic Wastewater Facilities Manual, A Guide for the Preparation of Applications, Reports and Plans, Bureau of Water Quality Protection, Commonwealth of PA,

Dept. of Envir. Protection, at 15 (Oct. 1997) (DEP Manual). The Long Term Control Plan (LTCP) explains the origin and purpose of the SSA combined system:

Under accepted engineering practice at that time, the Sewer System was designed to serve the dual purpose of removing both sanitary sewage and storm water from developed areas of the community. These portions of the Sewer System are a combined sewer system (CSS), designed to convey a combination of storm water and sanitary sewage downstream directly to area streams, where the combined sewage was discharged without any treatment prior to 1972.

OCA Exh. TLF-10. All Pennsylvania municipalities are responsible for providing stormwater service within their borders with some exceptions of Federal and State lands and right-of-ways. OCA St. 1S at 3. Scranton and Dunmore have delegated that responsibility to the SSA and have agreed with how the stormwater costs in the combined sewer system are allocated to their residents.

There are other combined sewer systems in Pennsylvania, however, none of them are owned or operated by a privately-owned public utility. OCA St. 1 at 5. They are owned by municipal authorities or corporations and the Commission has no jurisdiction over their rates and service, with one exception. The Public Utility Commission regulates the rates and service of the portion of customers residing outside the city limits served by the City of Lancaster Sewer Fund. The Lancaster system is a combined sewer system. The PUC has ruled, and the Commonwealth Court affirmed, that costs of treatment of the City's stormwater cannot be recovered from jurisdictional customers' rates. Pa. P.U.C. v. City of Lancaster Sewer Fund, Docket No. R-0004986, Remand Order at 3 (Sept. 15, 2008) (Lancaster 2004); City of Lancaster v. Pa. P.U.C. v. City of Lancaster Sewer Fund, Docket No. R-2012-2310366, Order (Apr. 18, 2013) (Lancaster 2012).

Because stormwater service is not a regulated utility service under the Public Utility Code, PAWC's application must be denied as proposed. The following sections discuss the legal, policy, and engineering distinctions between wastewater and stormwater.

1. Public Utility Code and City of Lancaster

The Commission cannot authorize PAWC to provide stormwater service to the City of Scranton for compensation because stormwater service is distinct from sewage, or wastewater, service under the Public Utility Code. The Public Utility Code refers to sewer and wastewater; "wastewater" is the current, standard terminology in the industry. See 66 Pa. C.S. §§ 102, 510, 529, 1526 ("sewer"); 66 Pa. C.S. §§ 1311, 1327, 1329, 1351, 1358, 1403 (wastewater). The Public Utility Code does not contain the term "stormwater."

As discussed above, Section 102 of the Public Utility Code defines a wastewater utility to include "[a]ny person or corporations now or hereafter owning or operating in this Commonwealth equipment or facilities for . . . sewage collection, treatment, or disposal for the public for compensation." 66 Pa. C.S. § 102(1)(vii). PAWC argues, however, that the provision of stormwater service by a privately-owned utility for compensation is permissible under the Public Utility Code where the system providing the stormwater service is a combined system. PAWC St. 4-R at 15-16. The Company argues that the Public Utility Code's definition of "wastewater" should be construed to include wastewater with regard to combined systems. PAWC St. 6-R at 4-6, 8-9.

This construction is inconsistent with the common and approved meaning of the term "wastewater," which is not used in the industry to refer to both wastewater and stormwater, rather "stormwater" is always referred to separately. OCA St. 1 at 6-8; 1 Pa. C.S. § 1903(a). As Mr. Fought explained, it is generally understood that:

- “wastewater” (previously sewage) includes domestic wastewater, industrial wastewater, and infiltration/inflow within the sewer system, and
- “stormwater” is defined as water that falls on streets, roofs, driveways, parking lots, and other impervious and pervious surfaces such as grass and bare soil.

OCA St. 1 at 6 (citing DEP Manual at 43.4 and 25 Pa. Code §102.1).

The Joint Applicants point to the PUC’s changes to its regulations to use the term “wastewater” rather than “sewage” as support for their position that wastewater includes stormwater.⁸ PAWC St. 6-R at 4; see OCA St. 1S at 4. However, the Commission specified in its 1997 rulemaking order promulgating the change that the purpose of the wording change was to update its terminology. See OCA Exh. TLF-2, Att. ID-4B, p. 2. Moreover, the Public Utility Code was not modified. There is no basis to support the Joint Applicants’ position that this terminology change expanded the PUC’s wastewater jurisdiction to include stormwater.

Further, where the General Assembly has intended to include stormwater in the types of service an entity can provide, it has amended the statute to add “stormwater” where the existing statute already authorized the provision of “sewer” service. Specifically, in 2013, the General Assembly amended the Municipal Authorities Act to allow municipal authorities to operate “storm water planning, management and implementation” projects. 53 Pa. C.S. § 5607(a)(18). The statute already provided for municipal authorities to finance, construct and maintain projects relating to “sewers, sewer systems or parts thereof” as well as “sewage treatment works.” 53 Pa. C.S. § 5607(a)(5), (a)(6). If “stormwater” were commonly understood to be included in the term “wastewater,” then adding a provision for stormwater would be redundant. Because a statute should be interpreted so as to “give effect to all its provisions,” 1 Pa. C.S. § 1921(a), it is presumed that the legislature does not intend for any provisions of a statute to be “mere

⁸ The wording change from sewer and sewerage to wastewater in the PUC regulations is shown in OCA Exhibit TLF-2.

surplusage,” see, e.g., Holland v. Marcy, 584 Pa. 195, 206 (2005); Burdick v. Erie Ins. Group, 946 A.2d 1106, 1108 (Pa. Super. Ct. 2008).

The Pennsylvania Storm Water Management Act also supports a statutory distinction between “stormwater” and “sewage.” 32 P.S. § 680.4. The Act defines “public utility service” to include “sewage collection, treatment or disposal.” Id. Stormwater is separately defined as “drainage runoff from the surface of the land resulting from precipitation or snow or ice melt.” 32 P.S. § 680.4.

In addition, the Pennsylvania Sewage Facilities Act explicitly defines “sewage” as “any substance that contains any of the waste products or excrement or other discharge from the bodies of human beings or animals and any noxious or deleterious substances being harmful or inimical to the public health, or to animal or aquatic life, or to the use of water for domestic water supply or for recreation, or which constitutes pollution . . .” 35 P.S. § 750.2. This definition excludes stormwater.

Pennsylvania case law likewise shows that “stormwater” is distinct from and not included within the definition of “wastewater” in the Public Utility Code. For the one utility in the Commonwealth operating a combined system and serving customers within the Commission’s jurisdiction – City of Lancaster Sewer – the Commission has approved rates for jurisdictional customers that exclude stormwater costs. The Commission ruled, and the Commonwealth Court affirmed, that all costs associated with stormwater service must be paid solely by City customers; that is, that stormwater service was not jurisdictional to the Commission. Lancaster 2004; Lancaster 2012. Specifically, the Commonwealth Court stated:

After a review of the record, we conclude that the Commission did not err in accepting the OCA’s overall cost allocation methodology, which is premised on the theory that the collection of both storm water and sewage in the City’s combined sewer system, increases the cost of sewage treatment and that the costs

of treatment of the City's stormwater should not be passed on to the jurisdictional customers....

Lancaster 2004 at 3. Not only did the Court recognize that PUC-jurisdictional customers should not pay the costs associated with stormwater service to non-jurisdictional customers, the Court recognized that the costs of providing stormwater service are distinct from the costs of providing wastewater service, even where one system is providing two services.

In the natural gas and petroleum context, the Commonwealth Court recently held that the jurisdiction of the Federal Energy Regulatory Commission (FERC) and the Pennsylvania PUC is not mutually exclusive. In re Condemnation of Sunoco Pipeline, L.P., 2016 PaLEXIS 326 (Sunoco). The Court relied on Amoco Pipeline Co., which held that commingling of shipments in the pipeline is not determinative of jurisdiction.

As the cases demonstrate, the commingling of oil streams is not a factor in fixing jurisdiction under the [Interstate Commerce Act].

Commingling does not alter the jurisdictional nature of the shipments, and as Sinclair has stated, the question of jurisdiction arises only in the context of the facts relevant to individual shipments.

Sunoco at *5-7; Amoco Pipeline Co., 62 FERC ¶ 6119, at 61803-04, 1993 FERC LEXIS 120, *10-11. These decisions rebut PAWC's contention that the physical commingling of stormwater and water within the Authority's CSO does not expand the Commission's jurisdiction to stormwater service.

2. Other States' Case Law and Statutes Support the Proposition That "Stormwater" and "Sewage" Are Distinct Concepts Unless Otherwise Specified.

Pennsylvania statutes, regulations, and case law are consistent with the conclusion that "wastewater" and "stormwater" are distinct terms and distinct services under the Public Utility Code, because the Legislature did not explicitly include the provision of stormwater service in the definition of wastewater (sewage) service and defines the terms separately in the Sewage

Facilities Act. 32 P.S. § 680.4; 35 P.S. § 750.2. This is consistent with the treatment of wastewater service and stormwater service in other states.

The Ohio Supreme Court recently held that the terms “sewer” or “waste water” do not include “storm water” unless the relevant statute explicitly defines “sewer” or “waste water” to include stormwater. Northeast Ohio Reg’l Sewer Dist. v. Bath Twp., 144 Ohio St. 3d 387, 388-89, 44 N.E.3d 246, 248-51 (Bath Twp.). The Ohio Revised Code expressly includes “stormwater” within its definition of “wastewater” and, therefore, the Ohio Supreme Court concluded that the Sewer District was able to implement the stormwater program. Bath Twp., 144 Ohio St. 3d at 389, 44 N.E.3d at 251; Ohio Rev. Code Ann. § 6119.011(K). Similarly, Vermont’s statute states that “sewage” includes “stormwater.” Vt. Stat. Ann. tit. 24. § 3672 (3) (West). See also D.C. Code Ann. § 34-2202.01(8) (West) (defining “sewage collection” as the collection of both sanitary sewage and stormwater); N.J. Stat. Ann. § 58:11B-3 (West) (defining “wastewater” to include sewage and stormwater).

Unlike Ohio, Vermont, the District of Columbia, and New Jersey, the Pennsylvania Legislature does not explicitly include “stormwater” in its definition of sewage or wastewater. Instead, Pennsylvania statutes and regulations define “storm water” and “sewage” separately, similar to a number of other states. See N.H. Rev. Stat. § 149-I:6 (discussing the rulemaking processes in municipalities where sewage is pumped separately from the processes in municipalities where stormwater is collected); W.Va. Code St. R. § 150-5-1 (explaining the rules governing sewage utilities, as opposed to the rules governing stormwater utilities found in W.Va. Code St. R. § 150-36-2).

3. I/I Is Not The Same as Stormwater Service.

The Joint Applicants argue that I/I is the same as stormwater and because I/I is part of a wastewater system, the PUC has authority over stormwater. This position would greatly expand

the PUC's jurisdiction. As discussed above, there is no support in the Public Utility Code for the Joint Applicants' position regarding stormwater being included in the Public Utility Code's definition of sewer. Further, as discussed below, there is no support in engineering or public policy to support the Joint Applicants' position that I/I is the same as stormwater or that stormwater should be subject to PUC jurisdiction. The OCA submits that the PUC should not expand its jurisdiction in the manner proposed by the Joint Applicants.

Wastewater or sewage includes domestic wastewater, industrial wastewater and infiltration/inflow (I/I) within the collection system. OCA St. 1 at 6. DEP's domestic wastewater facilities manual describes the wastewater that is received at the treatment plant as being made up of domestic wastewater⁹, industrial wastewater¹⁰ and the infiltration/inflow within the sewer system. Id.

I/I consists of: (1) groundwater infiltrating into the joints and cracks in sewer pipes and manholes and (2) surface/stormwater flowing into the sewers from manhole covers and prohibited connections from roof drains, street inlets, etc. OCA St. 1S at 5. I/I is to be reduced to the extent practicable and cost-effective in comparison to the costs if I/I is not reduced, *i.e.* extra operation and maintenance, adding capacity to sewers, pumping stations and treatment plants. Id.

Thus, the inflow of surface/stormwater is not a deliberate design decision to introduce surface/stormwater into the collection system. As Mr. Fought noted, a wastewater plant is not designed to and does not replace any municipal stormwater facilities. OCA St. 1S at 4. The presence of I/I in a wastewater system does not mean that system is providing stormwater

⁹ Domestic wastewater consists of flow from residential, commercial, institutional, and recreational establishment. OCA St. 1 at 6, n.5.

¹⁰ Industrial wastewater includes wastewater generated by employees and any process or cooling water discharged to the sewer system. OCA St. 1, n.5.

service. As Mr. Fought noted, stormwater connections are prohibited in wastewater systems regulated by the PUC. OCA St. 1S at 4-5.

In contrast, the Authority's use of 10,000-14,000 stormwater catch basins and inlets designed to capture stormwater and introduce it into the SSA combined system is a stormwater service. OCA St. 1 at 9. The stormwater catch basins are not operationally equivalent to the I/I that may leak into a system around manhole covers; the impact of I/I compared to 10,000-14,000 stormwater catch basins on the operation of a wastewater system is very different. The inflow around manholes of surface/stormwater into a wastewater collection system is a minor part of the overall system, whereas the design, and upkeep related to 10,000-14,000 stormwater catch basins drives the design and operation of a stormwater or combined system. Id. at 9-11.

Further, I/I is not a service that is provided to customers. Rather it is part of operating a wastewater system. The PUC routinely deals with wastewater systems that have I/I and has not considered the systems to be providing stormwater service or to be a combined wastewater/stormwater system. The PUC has recognized that there are systems with higher I/I flows that may be contributing to additional treatment flows, but has not considered that to be a combined system as the Joint Applicants argue should be done in this case. In fact, PAWC witness Elliott testified that in the PAWC Northeast rate case, in a study conducted by Gannett Fleming, the I/I costs were treated as one of several costs of operating the wastewater system. See Tr. 141. That is exactly the point that the Joint Applicants' position ignores. I/I has always been dealt with as one of several costs of operating a wastewater system. He also admitted on cross examination that sanitary sewer systems do not have stormwater catch basins as a stormwater system or a combined system would have. There is no basis for the Joint Applicants' position that I/I found in a wastewater system is the same as stormwater that is specifically

collected through catch basins. Thus, the Joint Applicants' attempt to expand the PUC's jurisdiction by equating I/I with stormwater should be rejected.

4. The PUC Should Not Expand Its Jurisdiction to Include Stormwater Service.

In addition to legal arguments regarding why the PUC should not expand its jurisdiction to include stormwater service, there are strong policy and engineering reasons why the Commission should not do so. OCA witnesses Fought and Rubin distinguish wastewater and stormwater because they are produced, collected, and billed in different manners, regardless of whether the services are provided by combined or separate sewer systems.

a. Stormwater and Wastewater Are Fundamentally Different Services.

Wastewater utility service requires running pipes from each property to a wastewater treatment plant where the wastewater is treated prior to being discharged into a receiving water, such as a lake, stream, and river. OCA St. 2 at 9. Mr. Rubin noted that the customer controls its wastewater production and disposal, collects the wastewater produced in a building into a wastewater service line or pipe that connects to the wastewater main. Id. "Throughout the process, wastewater is produced and controlled by the customer then transferred to the utility at a specific point." Id.

Stormwater service is not directly controlled by customers or contained in pipes throughout the process. OCA St. 2 at 9. Stormwater is rain, snow, and ice melt. Some stormwater falls on pervious ground that can absorb some of the stormwater. Id. Other stormwater falls on roofs, streets, sidewalks, frozen ground and other impervious surfaces where it is not absorbed and it flows downhill. Id. Thus, as noted by Mr. Rubin, most stormwater does not begin as controlled, piped flow of water. Id. A stormwater control system directs the flow

of the runoff so that it does not create flooding on private property or on public property. Id. at 9-10. Stormwater flow is controlled by designing streets to direct the flow, grading properties, parking lots, and driveways to control the flow, maintaining streets (cleaning streets, repairing curbs, cleaning storm drains) so that stormwater enters storm drains and is collected in a network of pipes. OCA St. 2 at 10.

When there is a separate stormwater system, the stormwater is directly discharged to a body of water with little or no treatment. OCA St. 2 at 10; OCA St. 1 at 8. In a system that combines storm sewers and sanitary sewers, stormwater flows commingle with wastewater flows and should be directed to a wastewater treatment plant. Id. In some older combined systems, like the SSA system, the flow exceeds the capacity of the pipes, which results in combined sewer overflows (CSO) that divert some of the combined flow before it reaches the wastewater treatment plant and discharges untreated wastewater and stormwater into a receiving water. Id. Mr. Rubin noted that one of the important clean water initiatives of the past two decades is to reduce or eliminate the use of CSOs. Id. Stormwater control involves catch basins, streets and curbs, storm drains, stormwater pipes, if there is a separate system, and CSO control facilities in a combined stormwater-wastewater system. Id.

In summary, Mr. Rubin found that the biggest difference between stormwater and wastewater is that a customer does not create stormwater, but may have some ability to control it, and most stormwater flows above ground until it reaches a storm drain. OCA St. 2 at 10. A wastewater customer directly creates and controls all wastewater flows and all of those flows are piped directly into the wastewater system. OCA St. 2 at 11.

b. Stormwater Service Is Intertwined With Other Municipal Functions.

As Mr. Rubin testified, “the nature of stormwater service is such that it is intertwined with other municipal functions, such as the maintenance of streets.” OCA St. 2 at 19. Mr. Rubin noted that a significant part of the stormwater removal system in a developed area are the streets, culverts, and drainage ditches that are in the public right of way and that are designed, operated, and maintained by local (or state) government. Id.

Mr. Rubin explained further:

The movement of stormwater through a city depends in significant measure on the network of streets, drainage ditches, and culverts that are part of the public right-of-way and that are designed, constructed, and maintained by the government. It is not feasible to separate control of these facilities from control of the remainder of the stormwater management system.

In other words, stormwater does not begin at the storm drain; it must get to the storm drain over a properly maintained network of streets. While the storm drains and the pipes underneath them theoretically could be separated from the streets in which the drains are located, doing so would be poor public policy. The essential elements of the system should remain under common ownership and control. It simply is not possible to move stormwater through a city without having streets. If the purported “stormwater utility” has no ability to manage the streets (repairing potholes, keeping curbs functional, cleaning streets to keep debris from clogging storm drains, etc.), then the so-called utility is not able to provide the service it purports to provide. A pothole filling with water and flooding a street or a damaged curb failing to contain stormwater leading to a flooded basement are failures in the stormwater system. We do not want to create a system where the so-called “stormwater utility” can point a finger at the city and say “the damaged curb is not my responsibility” while the city points a finger at the utility and says “stormwater is not my responsibility” or where it is not clear which entity is responsible for street sweeping and cleaning. There should be one entity that is responsible for stormwater and that entity must be under the control of local government.

Q. Are there other reasons why stormwater utilities should be government-owned?

Yes. Some municipalities (such as Philadelphia) have found that it is more cost effective to use stormwater management solutions that do not involve new pipes or larger detention basins, particularly when the stormwater and wastewater systems are combined. For example, increasing vegetation (tearing up unused

paved areas and planting trees or planting roof gardens), using porous paving materials, and encouraging property owners to reduce the size of paved areas are a few examples of what is termed “green infrastructure.” These types of measures can significantly reduce the amount of stormwater that flows into the system, but they cannot be mandated by a privately owned utility; they must be undertaken (and enforced) by local government.

Other non-structural measures can include building and land use codes that encourage or mandate the use of stormwater-reduction efforts on properties. When such measures are employed, local governments are responsible for legislating, inspecting, and enforcing such requirements.

Finally, a privately owned stormwater utility lacks any meaningful enforcement method to collect stormwater bills from a property owner. With all other utility services, the service can be disconnected if the customer does not pay. That is not true with stormwater; it is not possible to stop the rain from falling on a property. Under Authority ownership, the Authority has the ability to place liens on properties that have not paid the bills; PAWC would not have that ability. This is yet another important, practical reason why stormwater utilities should be government-owned.

OCA St. 2 at 20-22. It is clear that an investor-owned utility should not be providing stormwater service. The Joint Applicants have not rebutted the OCA’s evidence on this issue.

c. Stormwater and Wastewater Are Treated as Different Services for Engineering Purposes.

From an engineering perspective, stormwater services are different from wastewater services and stormwater is not the same as I/I. OCA St. 1 at 6. The Joint Applicants position is that the SSA combined system constitutes wastewater service. To support its position, the Joint Applicants provided excerpts from professional engineering manuals and PUC regulations. See OCA St. 1 at 7; Exhibit TLF-2. As Mr. Fought testified, none of the three excerpts support the Joint Applicants’ position. In the first excerpt, the definition of wastewater from an engineering manual titled Design and Construction of Sanitary and Storm sewers,” includes the phrase “together with any groundwater, surface water and stormwater that may be present.” OCA St. 1

at 7. Mr. Fought testified that the phrase relied on by the Joint Applicants referred to I/I but did not define wastewater as including stormwater. Id.

In the second excerpt, from a manual titled “Wastewater Engineering” it states that a combined sewer includes domestic wastewater, industrial wastewater, I/I plus stormwater, but never states that stormwater is wastewater. Id. He also noted that the definition of sewage did not include unpermitted connections of stormwater – only I/I. The third excerpt, which is a page from a manual titled “Glossary Water and Wastewater Control Engineering” does not contain a definition for wastewater. It defines storm wastewater and stormwater. Mr. Fought concluded that the terms and definitions were not commonly used and may not be industry standard definitions. He also noted that the Glossary was no longer available from any of the publishers. OCA St. 1 at 7-8. Thus, none of the definitions provided by the Joint Applicants supports their position that wastewater is defined as including stormwater. Mr. Fought provided various relevant definitions of wastewater in Exhibit TLF-3. As he noted, stormwater is always referred to separately from wastewater. Id. at 8. Mr. Fought’s experience with wastewater for the last 30 years is consistent with the definitions in Exhibit TLF-3 which make it clear that wastewater and stormwater “have distinct definitions that are not interchangeable.” Id.

Mr. Fought also noted that PAWC’s current wastewater tariff prohibits any stormwater from being introduced into its sanitary sewer. Under the tariff provision, no stormwater from “pavements, areas ways, runoff basins, roof runoff water, foundation drains, subsurface drains, water from springs, cooling water, basement sump pumps, unpolluted industrial or commercial process water or other sources...” If stormwater was included in wastewater, as the Joint Applicants argue, this provision would not be necessary.

d. Stormwater and Wastewater Are Treated as Separate Services for Economic Regulation.

The Joint Applicants' position is that stormwater and wastewater should continue to be a combined system, even under PUC regulations. That position is based on PAWC's plan to shift stormwater costs onto its water customers, as discussed below. However, it is the OCA's position that there are legal issues that would prevent that. Moreover, there are relevant policy reasons why stormwater and wastewater are treated as separate utility services for purposes of economic regulation.

Mr. Rubin discussed the different economic regulation of stormwater service compared to wastewater service. He noted that he has served as a consultant in two rate cases involving stormwater service. OCA St. 2 at 11-14. He stated that it has become increasingly common over the past 20 years for state or local governments to create separate stormwater utilities or to have separate stormwater operations within larger public works departments. Id. at 11. The Water Environment Federation (WEF) found that in 1994 there were only a few local government agencies with separate fees for stormwater. Id. By 2014, there were approximately 1,500 stormwater utilities in the United States and Canada. Id. Importantly, whether and how a jurisdiction can establish a stormwater utility is subject to state legal and constitutional requirements. Id.

Mr. Rubin noted that fees for separate stormwater service have been set with a separate stormwater removal system as well as in those communities with combined stormwater wastewater systems. OCA St. 2 at 12.

Regarding a combined stormwater/wastewater system, Mr. Rubin described a federal decision that upheld the imposition of a separate stormwater fee. Vandergriff v. Chattanooga, 44 F. Supp. 2d (E.D. Tenn.), aff'd per cur., 182 F.3d 918 (6th Cir. 1999). In that case, the court rejected the argument that the CSO is a sewage facility, not a stormwater facility. Id. at 934.

OCA St. 2 at 12. In 2013, a court in Maine upheld a cost allocation methodology used by a municipal utility that separated stormwater and wastewater costs for its CSS. Hallowell v. Greater Augusta Util. Dist., 2013 Me. Super. LEXIS 34 (Mar. 18, 2013); OCA St. 2 at 12. In that system, separate charges were developed for stormwater customers (residents of Augusta), while non-residents and residents alike paid separate charges for wastewater service. Mr. Rubin also explained how the rates are set in Philadelphia:

[T]he City of Philadelphia is one of the few Pennsylvania municipalities with a stormwater utility. Approximately two-thirds of Philadelphia is served by a CSS. The charges for providing stormwater service are separate from the charges for wastewater service. Specifically, in Philadelphia wastewater charges are based in part on water consumption while stormwater charges are based on the characteristics of the property (all residential properties pay a flat rate for stormwater; non-residential properties pay a stormwater charge based on the gross area and impervious surface area of the property). Interestingly, the charges for stormwater service do not vary depending on whether a property is served by Philadelphia's separate stormwater system or by the combined system.

OCA St. 2 at 12-13. Mr. Rubin testified that there are strong public policy reasons to have a separate stormwater fee and that the failure to have a separate charge for stormwater service may result in stormwater costs being considered a tax or not being reasonable which can have important consequences for a service provider and its customers. Id. at 13.

Mr. Rubin noted that not only are the services different, the facilities are different, and the appropriate methods for charging customers, even determining customers, are different for stormwater and wastewater. OCA St. 2 at 15. He provided the following examples:

[S]ewage (or wastewater) service often is based on water consumption while stormwater service usually is charged based on a property's size and/or impervious surface area. Similarly, in a multi-unit building, each unit might be a separate water and wastewater customer, but the building as a whole (that is, the owner of the building) would be the stormwater customer. Indeed, an individual apartment in a building or single office in a professional building would have no responsibility for, and no ability to control, stormwater emanating from the building's roof, parking lot, and other outdoor surfaces.

...

Several years ago, some federal government agencies had objected to bills they were receiving for stormwater charges. For many decades, federal agencies have been required to pay bills for utility services they receive (including wastewater service), but the new stormwater charges were different and, they argued, not the same as charges for wastewater service. As a consequence, Congress amended the federal Clean Water Act to add a special provision that required federal agencies to pay “reasonable service charges” for stormwater service, so long as the charge is “based on some fair approximation of the proportionate contribution of the property or facility to stormwater pollution ... and used to pay or reimburse the costs associated with any stormwater management program (whether associated with a separate storm sewer system or a sewer system that manages a combination of stormwater and sanitary waste)”

That is, this statute recognized that stormwater service was fundamentally separate from wastewater service and that federal agencies should be responsible for paying reasonable charges for stormwater service. Those charges, however, must be proportionate to the federal building's contribution of stormwater to the system. This is true whether the stormwater system is a stand-alone system or part of a CSS.

OCA St. 2 at 15-16.

In rebuttal, PAWC provided the testimony of an engineering witness who focused on the engineering approach to the treatment and processing of combined stormwater and wastewater. PAWC witness Elliott’s testimony did not address the issue presented in this case, which is whether the PUC has jurisdiction over stormwater service. Rather, PAWC witness Elliott’s position is focused on the definition of wastewater after stormwater and wastewater mix. See OCA St. 1S at 3; PAWC St. 6-R at 4-6. As Mr. Rubin explained in surrebuttal, the PUC regulates services provided by a utility, and to some extent facilities. Tr. 96. The PUC does not regulate water quality, like the issuance of discharge permits. Id. Just as water and wastewater are distinct services, wastewater and stormwater are distinct services. Id. Mr. Rubin noted that there are different customers, different ways in which the services are measured, regulated, and so on. Id. PAWC witness Elliott’s testimony does not rebut Mr. Rubin’s testimony regarding those fundamental differences.

Mr. Rubin explained that the fact that wastewater and stormwater ultimately come together in common facilities and there is a physical commingling is not important in looking at the PUC's jurisdiction. Tr. 96-97. He provided examples of similar instances where the same facilities are used but only a segment of the service is under PUC jurisdiction. Specifically, he stated:

We have, for example, in the energy industry, we have electric distribution services and electric supply service that are both provided in part over the same physical facilities. The PUC regulates distribution. It does not regulate supply. We have something very similar in the natural gas industry, at least for certain types of customers. And in the telecommunications industry, you have the same wires being used to provide services that are regulated at the state level, services that are regulated at the federal level and services that are completely unregulated, and basically local telephone, long distance telephone and television services all being provided over the same physical facility, but three distinct services regulated or unregulated in three distinct ways from an economic perspective.

Tr. 97. Mr. Rubin concluded by noting that PAWC witness Elliott's testimony does not address the issue of how these distinct services are provided and whether they are regulated by the PUC.

Id. Mr. Rubin's position is consistent with the Sunoco case, discussed *supra*, where the Commonwealth Court determined that the FERC does not have authority to regulate intrastate shipments of products on the basis that those products are shipped on the same pipeline as interstate shipments. Sunoco at *9.

The Court stated:

[T]he record shows that pipeline service operators in Pennsylvania, such as Sunoco, can be, and frequently are, simultaneously regulated by both FERC and PUC through a regulatory rubric where FERC jurisdiction is limited only to interstate shipments, and PUC's jurisdiction extends only to intrastate shipments.

Id.

In rejoinder, PAWC witness Elliott repeated his direct testimony regarding the operational processes to handle a combined stormwater/wastewater system. See Tr. 135-136.

His focus remains on the operations of the treatment facility and the stormwater facilities. See Tr. 137-38. However, he then states, “It’s all one set of customers. All of the costs are billed to the same set of customers.” Tr. 137-38. He fails to acknowledge that there is no basis under the Public Utility Code for that approach. He also fails to distinguish between the SSA, which is not regulated by the PUC, and PAWC, which is. He also does not recognize that there is no requirement that the economic regulation be done in that manner. Mr. Elliot also fails to acknowledge that combined systems exist that have separate rates for separate customer groups. He continues to ignore the legal and policy issues why the economic regulation may differ from the environmental regulation of combined systems, *e.g.*, National Pollutant Discharge Elimination System permit program.

During cross-examination, PAWC witness Elliott acknowledged that sanitary systems do not have stormwater catch basins or area drains on road surfaces. Tr. 179. He also acknowledged that many entities without water connections, including parking lots, a city park, streets, contribute to stormwater are not wastewater customers under the current SSA and would not currently pay anything related to the costs of stormwater service. Tr. 180. He acknowledged that those costs are currently collected from the SSA wastewater customers based on their water usage. Tr.183.

e. Summary

Not only do Pennsylvania statutes, regulations, and cases distinguish stormwater from sewage and wastewater, but water and wastewater industry standards differentiate between stormwater and sewage in terms of how these services are defined, produced, collected, treated, and billed. Accordingly, although the Commission has jurisdiction over sewage services, it does not have jurisdiction over stormwater services, because stormwater is not sewage. The OCA

submits that these policy reasons for separate regulation of stormwater and wastewater services should be considered by the PUC and should lead to a denial of the application.

B. The Application Should Be Denied Because There Is No Affirmative Public Benefit.

A regulated public utility cannot provide stormwater service for compensation because, as discussed above, stormwater service is distinct from wastewater service and is not included in the services regulated by the Public Utility Code. Therefore, the OCA submits that the Commission must deny PAWC's application for a Certificate of Public Convenience. If, however, the Commission determines that its jurisdiction over wastewater service allows it to consider this Application, then PAWC's application should be denied for another reason – because the proposed transaction will not provide the required affirmative benefit.

The Public Utility Code authorizes the Commission to permit a regulated public utility to begin to offer service in an additional territory and to acquire property used and useful in the public service, as is requested in this application.¹¹ 66 Pa. C.S. § 1102(a)(1), (3). The merits of

¹¹ Section 1102(a)(1) provides:

(a) General Rule. Upon the application of any public utility and the approval of such application by the commission, evidenced by its certificate of public convenience first had and obtained, and upon compliance with existing laws, it shall be lawful:

(1) For any public utility to begin to offer, render, furnish or supply within this Commonwealth service of a different nature or to a different territory than that authorized by:

(i) A certificate of public convenience granted under this part...

...

(3) For any public utility... to acquire from, or to transfer to, any person or corporation, including a municipal corporation, by any method or device whatsoever, including the sale or transfer of stock and including a consolidation, merger, sale or lease, the title to, or the possession or use of, any tangible or intangible property used or useful in the public service.

Id. Section 1103 states that a certificate of public convenience will be granted only where necessary or proper for the service, accommodation, convenience or safety of the public. 66 Pa. C.S. § 1103(a).

applications arising under Section 1102 are measured by the standards set forth in the City of York case. City of York, 449 Pa. 136 at 141, 295 A.2d 825 at 828. In City of York, the Supreme Court addressed a proposed merger of three telephone companies. The Pennsylvania Supreme Court specifically cited Section 203, the predecessor statute to Section 1103, and set forth the standard as follows:

Section [1103] of the Public Utility Law requires that those seeking approval of a utility merger demonstrate more than the mere absence of any adverse effect upon the public. Section [1103] requires that the proponents of a merger demonstrate that the merger will affirmatively promote the “service, accommodation, convenience, or safety of the public” in some substantial way.

449 Pa. at 141, 295 A.2d at 828. This is the standard by which all mergers of Pennsylvania utility companies must be judged.

This standard was addressed by the Commonwealth Court in Middletown Township v. Pa. P.U.C., 482 A.2d 674 (Pa. Commw. Ct. 1984) (Middletown). In Middletown, in order to acquire part of the facilities of the Newtown Artesian Water Company, Middletown Township filed an application for a Certificate of Public Convenience. The ALJ determined that the acquisition would be a benefit to some customers, but would have an adverse impact on other customers. Id. at 679. The ALJ, therefore, denied the application. Id. The Commission adopted the ALJ’s Initial Decision and the Township appealed. In hearing the appeal, the Commonwealth Court considered the City of York standard applicable through Section 1102 and Section 1103. The Court affirmed the Commission’s decision to reject the merger stating, *inter alia*, that “when the ‘public interest’ is considered, it is contemplated that the benefits and detriments of the acquisition be measured as they impact on all affected parties, and not merely on one particular group or geographic subdivision as might have occurred in this case.” Id. at 682 (emphasis in original). The Court added that “the primary objective of the law in this area is

to serve the interests of the public.” Id.; see also Popowsky v. Pa. P.U.C., 937 A.2d 1040 (Pa. 2007).

In this proceeding, three specific groups should be evaluated with respect to the traditional City of York affirmative public benefits test: (1) the existing PAWC wastewater customers, (2) the existing PAWC water customers – who may potentially bear costs of the Scranton combined sewer system, if the Commission permits costs to be shifted under 66 Pa. C.S. § 1311(c), and (3) the existing SSA customers who will be transferred to PAWC. As discussed in the testimony of OCA witness Rubin, it is well-established that the City of Scranton will benefit from the proposed transaction. There is, however, no support for concluding that existing PAWC wastewater and water customers will benefit or that the SSA customers will benefit after year 10. The record shows that the Joint Applicants have failed to demonstrate the necessary public benefits required for approval of this Application.

1. Detriment to Existing Wastewater and Water Customers

An acquisition provides an affirmative benefit if the benefits of the transaction outweigh the adverse impacts of that transaction. Application of CMV Sewage Co., Inc., 2008 PaPUC LEXIS 950, *30 (CMV). In order to determine whether benefits meet this standard, the Commission may consider: “(1) the legal and technical fitness of the purchasing entity to provide service; (2) the public need for service; (3) the inadequacy of the existing service; and (4) any other relevant evidence.” Application of North Heidelberg Water Co., 2010 PaPUC LEXIS 919, *20.

In this proceeding, the Joint Applicants allege that PAWC’s existing wastewater customers will benefit from the proposed transaction because, at some unknown future date, they will benefit from sharing costs among a larger customer base. PAWC St. 1 at 8; PAWC St. 4-R at 4-5. PAWC witness Nevirauskas stated:

While Scranton-area customers may benefit from the sharing of costs initially, PAWC's other customers will undoubtedly benefit from the revenues generated from Scranton-area customers in the future as the systems servicing those other customers require capital improvement. Indeed, the Commission should analyze the rate impact of this Transaction not from a 13-year perspective but from a 100-year perspective and recognize that other PAWC customers will benefit from the addition of over 31,000 wastewater customers.

PAWC St. 4-R at 4-5. The Company also notes that there will be no "immediate" rate impact on PAWC's existing customers. PAWC St. 1 at 8.

These claimed hypothetical benefits do not outweigh the certain, short-term adverse impacts on PAWC's existing customers. First, the PAWC customer base is not expanding. While SSA serves approximately 31,000 customers, essentially all of those customers are already PAWC water customers. OCA St. 2 at 34. PAWC's total customer count would not increase.

Second, while PAWC does not propose to increase rates for existing wastewater and water customers in this Application proceeding, the Company does plan for its existing wastewater and water customers to begin paying between \$146 and \$199 million of the costs of improvements to the SSA system when it increases rates in its next base rate case – as soon as January 1, 2018. PAWC St. 4 at 4, 7. The large, long-term capital improvements under the consent decree will have a major impact on the rates of existing customers. According to a rate study prepared for SSA in 2012, stormwater-related capital investments are projected to total between \$146 million and \$199 million (in 2011 dollars) over the next 20 years. OCA St. 1 at 31 (citing PAWC Response to OCA II-6, Att. B, Table 2). At the same time, PAWC proposes a zero percent increase in rates for the SSA customers in the Application proceeding and has agreed that it will not propose to increase the SSA customer rates by more than 1.9% compound annual growth rate (CAGR) over the 10 years post-acquisition. PAWC St. 4 at 3-4; Tr. 115-16. As a result, over the next 20 years, PAWC's wastewater and water customers will pay for nearly

\$200 million of improvements to the SSA system. PAWC also intends to continue charging the Distribution System Improvement Charge (DSIC) to existing wastewater customers' bills between base rate cases, but will not seek to charge the DSIC to the SSA customers before January 1, 2019. PAWC St. 4-R at 2. The result of these provisions is that PAWC's existing wastewater and water customers will be required to support nearly \$200 million in capital improvements just to the SSA system, plus the subsidies for keeping SSA rates lower than cost for the first 10 years post-acquisition, plus the subsidy related to not charging the DSIC rate for the first few years after acquisition. Further, as discussed below, the impact of the purchase price will be layered on top of all of these costs that are proposed to be borne by the existing wastewater and water customers.

Further, under the terms of Section 7.07 of the Asset Purchase Agreement (PAWC Exh. BJK-1, Exh. F), if PAWC is required to charge cost-based rates to the SSA customers over the first 10 years, then PAWC would be required to pay SSA at least an additional \$104 million as an enhanced "purchase price." OCA St. 2 at 24-25. PAWC then plans to recover that additional cost from its wastewater and water customers.

It is not reasonable or consistent with the public interest for the purchase price to be at least \$104 million higher than the \$195 million purchase price as set forth in the Asset Purchase Agreement. OCA St. 2 at 25. As Mr. Rubin explained, the \$195 million purchase price is already more than 2x the book value of the SSA's assets.¹² Specifically, SSA's balance sheet as of March 31, 2015 shows that the book value of all of SSA's property, plant, and equipment is \$74,660,819. Id. It is important to understand that not all of SSA's assets (the stand-alone stormwater assets) are being acquired by PAWC, so the actual book value of the acquired assets

¹² Even with the cash and equivalents of \$38,340,626 that SSA is required to provide, the net purchase price would be approximately \$156.66 million, still more than 2x the book value of all SSA assets. OCA St. 2 at 25.

is something less than \$74,660,819. Id. PAWC has not provided any evidence to show that it is reasonable for the company to acquire these assets at more than 2x book value. By adding another \$104 million on top of the purchase price, it would mean that PAWC would be paying more than 3x book value, or \$260 million for assets with a book value of less than \$74 million. OCA St. 2 at 26.

On the other hand, PAWC's investors are not agreeing to absorb \$104 million over the next 10 years in exchange for agreeing to keep the rate increases artificially low for the SSA customers. Rather, the Asset Purchase Agreement is predicated on PAWC being able to charge that \$104 million (or more) to PAWC's existing water customers. OCA St. 2 at 26. Section 7.09(x) of the Asset Purchase Agreement states that in PAWC's first base rate proceeding following closing, PAWC shall include a request to combine partially, under Section 1311(c), water and wastewater revenue requirements for ratemaking purposes "to ensure the System's customers benefit from Act 11 in the same manner as its other customers throughout Pennsylvania." OCA St. 2 at 26; Asset Purchase Agreement, PAWC Exh. BJG-1, Exh. F. Mr. Rubin concluded that PAWC is attempting to obligate its existing customers to pay an additional \$104 million for the addition of the SSA customers, in addition to the purchase price of \$195 million and the \$144 to \$199 million of improvements that will be necessary.

Mr. Rubin summarized the issue as follows:

I conclude that the real purchase price for SSA's assets is \$260 million: \$156.66 million paid for the assets and \$104 million provided in guaranteed rates below the cost of service over the next 10 years. If PAWC's shareholders were willing to pay that purchase price, I might question their business judgment, but that in itself would not make the proposed transaction contrary to the public interest, as long as they did not expect to include the entire purchase price in rate base.

That, however, is not how the transaction is structured. Rather, the Company expects its existing water customers to provide nearly one-half of the purchase price: at least \$104 million over the next 10 years. That is despite the fact that existing customers would receive essentially no benefit from the proposed

transaction. No new customers are being acquired (all SSA customers are already water customers of PAWC), so there is no meaningful reduction in overhead or back-office costs per customer resulting from the proposed transaction.

OCA St. 2 at 27.

Fourth, PAWC intends to seek Commission approval to spread the costs of improving SSA's system to its existing water customers. OCA St. 2 at 33-35; PAWC St. 4 at 4; PAWC Exh. BCG-1, Att. F, Section 7.09(x). As explained by OCA witness Rubin:

The Company intends to ask the Commission to allow the Company to collect a significant portion of SSA's revenue requirement from PAWC water customers. The Company provided two projections of the level of subsidy it might request from PAWC water customers. In response to I&E-10, Attachment A, PAWC shows that in 2017 it plans to collect just \$23.2 million of its \$31.4 million revenue requirement from SSA customers, a shortfall of \$8.2 million. The amount by which SSA would be subsidized by other customers would increase each year through 2024 before declining for the next few years. In total, the response to I&E-10 projects subsidies from other PAWC customers totaling in excess of \$120 million over a 13-year period.

The Company's response to OCA II-6, Attachment C, is even more telling. This response projects the difference in revenue requirement and revenue collections for 30 years. That response shows a total subsidy from existing PAWC water customers of more than \$360 million over the 30-year period.

OCA St. 2 at 33.

It must be recognized that every other PAWC water customer already has to pay for wastewater disposal and must pay taxes or other fees to control stormwater in his/her community. Mr. Rubin provided the following example:

PAWC customers in Mount Lebanon, PA, currently pay PAWC for water, pay the Borough of Mount Lebanon \$4.05 per 1,000 gallons for wastewater disposal and \$8.00 per month for stormwater control. Now PAWC suggests that a Mount Lebanon customer -- who already is paying for her own wastewater disposal and stormwater control -- must provide additional subsidies each year to help pay for wastewater disposal and stormwater control in Scranton and Dunmore.

OCA St. 2 at 34-35. For all of these reasons, Mr. Rubin concluded that the proposed transaction is neither fair to customers nor consistent with principles of cost-based ratemaking.

2. The Benefit to the City of Scranton Is Not Determinative of the Public Interest.

A determination of the public interest involves examining the impact of the proposed acquisition on all parties that would be affected by the transaction, as opposed to only considering “one particular group or geographic subdivision.” Middletown Twp. v. Pa. P.U.C., 85 Pa. Commw. 191, 202; 482 A.2d 674, 682 (1984). Application of CMV Sewage Co., Inc., 2008 Pa. PUC LEXIS 950, *43. Therefore, while the Commission is statutorily charged with the regulation of public utilities and the protection of their customers and must consider the adverse impacts of a proposed transaction on these parties, the Commission has explicitly chosen not to “expand [the] previous definition of the public interest to include the interests of municipal authorities” Id. at *43-44; Tr. 94-96. Thus, while SSA witness Barrett explains that the sale is expected to benefit the City, the benefit to Scranton does not determine whether the proposed transaction will benefit the existing PAWC and SSA customers. SSA St. 2-R at 3.

3. Detriment to Scranton Customers after Year 10

The record clearly shows that SSA customers will receive a substantial benefit from the proposed transaction during the first ten years post-acquisition, *e.g.*, PAWC will not propose to increase rates for SSA customers by more than 1.9% CAGR over the 10-year period, SSA customers will not pay a DSIC prior to January 1, 2019, the substantial costs of improving the system will be subsidized by PAWC’s existing wastewater customers and, if the Commission allows, by its water customers.¹³ PAWC St. 4-R at 2; PAWC Exh. BCG-1, Att. F (Section

¹³ WHEREAS, pursuant to the terms of the APA, the customers of the System will experience in the first ten years after the transaction a significant reduction in the Authority’s currently planned sewer rates, meaning that, as per the terms of the APA, the sewer rates will not increase to the extent that the Authority, acting on its own, would require; and

7.09(x)); PAWC Exh. BCG-1, Att. J at 3. PAWC indicates, however, that it intends to move the SSA customers to its system rates in equal increments in years 11 through 13 following closing of the transaction. PAWC St. 4 at 3; PAWC St. 4-R at 2. If approved as proposed, PAWC would charge an SSA customer using 3,000 gallons of water per month \$34.50 compared to charging an existing Rate Zone 1 customer \$46.14 for the same usage.^{14,15} In the 10 years post-acquisition, the rate disparity will grow if PAWC proposes rate increases for Rate Zone 1 that exceed the rate increases proposed for SSA customers due to the CAGR limitation. This means that moving SSA customers to system rates in years 11 through 13 could require severe or unaffordable increases.

Section 7.07(d) of the Asset Purchase Agreement provides that, if at the end of 10 years the actual increases exceed a compound average of 1.9% per year, then PAWC must pay an additional “purchase price” equal to the difference. PAWC Exh. BCG-1, Att. F (Section 7.07(d)); OCA St. 2 at 23. The Authority has sole discretion whether PAWC will distribute this amount to its current wastewater customers in the City of Scranton and Borough of Dunmore or pay the adjustment directly to the Authority with no limitation on how the funds are used. PAWC Exh. BCG-1, Att. F (Section 7.07(e)). Even if the adjustment is paid to wastewater customers in the Scranton area, it will be partly recovered from the same customers in their water

WHEREAS, the APA sets forth that during the first ten years of ownership PAWC may not raise the sewer rates more than an average of 1.9% compound annual growth rate (“CAGR”) per year; and

WHEREAS, the APA will shift to PAWC the obligations of Consent Decree compliance and Long Term Control Plan implementation currently estimated to be at or near \$140,000,000; and

WHEREAS, the purchase price for the sale, transfer, assignment conveyance and delivery of the assets shall be One Hundred Ninety-Five Million Dollars (\$195,000,000.00) subject to the adjustments contemplated in the APA. . . .

PAWC Exh. J at 3.

¹⁴ \$19.50 service charge + (\$0.50 usage charge per 100 gallons x 30) = \$34.50 per month. PAWC Exh. BCG-1, Att. L.

¹⁵ \$7.50 customer charge + \$1.2880 usage charge per 100 gallons x 30) = \$46.14 per month. See App. B attached to this brief (Supp. 2, PAWC Tariff-Wastewater Pa. P.U.C. No. 15 at 4).

rates. Id., Section 7.09(x). As such, there is no certainty that the adjustment will offset the rate increases for SSA customers in years 11 through 13.

4. The Adverse Impacts on PAWC’s Existing Customers and the Scranton Customers after Year 10 Outweigh the Benefits of the Proposed Transaction.

In the CMV case discussed above, the Commission concluded that the adverse impacts of the proposed transaction for the existing customers outweighed the benefits. 2008 Pa. PUC LEXIS 950, * 32. The customers proposed to be acquired were currently receiving service from a system that was in compliance with applicable environmental laws and regulations. While that system might have required upgrades to comply with stricter environmental requirements at an unknown future date, there was no certain evidence on that point. The PUC stated:

The advantages alleged by NCTSA do not outweigh the certain, immediate adverse impacts of this transaction. The proposed transaction will result in an immediate \$ 1,800 cost for Colonial Crossings customers, which is in addition to an average rate increase of approximately \$70 per quarter, or 54% compared to existing rates. We find that the ALJ correctly weighed the evidence before him, and concluded that the costs of the proposed transaction for the Colonial Crossings customers outweigh the benefits for those customers.

Id. at *32. As in CMV, the alleged benefits of acquiring the SSA system are “speculative”¹⁶ and the adverse impacts of the proposed acquisition of the SSA system outweigh any claimed benefits.

Although the Joint Applicants contend that the receipt of service from PAWC versus SSA is a benefit, there is no evidence that the current owner is not technically or managerially able to operate the existing system and perform the proposed improvements. Tr. at 154; OCA St.

¹⁶ The Commission has deemed benefits to be “speculative” where the buyer’s system was more technologically advanced but customers were already receiving service that complied with all applicable federal and state regulations. See CMV at * 29-31. Likewise, the Commission was not persuaded that potential economies of scale provided a benefit that outweighed the known adverse impacts of the transaction. As the OCA pointed out in CMV, there is no guarantee that savings resulting from any economies of scale will be reflected in the rates charged to customers. Id. at *29-30.

1 at 4. Indeed, as a term of the transaction, PAWC will offer employment to SSA staff. PAWC Exh. BCG-1, Att. F (Section 7.04(b)). Financially, the record shows that SSA has an A- bond rating (compared to PAWC's A) and that SSA adopted a Long-Term Control Plan in 2012, with full knowledge of the associated costs. OCA St. 1 at 3-4; PAWC St. 6-R at 25; Tr. 126, 154; PAWC Exh. JCE-5.

Although PAWC witness Merante claimed that PAWC is in a much stronger financial position than SSA, Mr. Rubin pointed out that Standard & Poor's noted SSA's healthy financial profile, its strong debt service coverage and liquidity. Tr. 98-99. He also testified that there is no reason to believe that SSA could not finance the capital improvements over the next 20 years that it agreed to implement in its consent decree with the federal and state governments. Tr. 99-100. Mr. Rubin also observed that Standard & Poor's noted that, assuming SSA can implement reasonable rate increases over time, it will be able to finance the obligations it has agreed to. Id. at 100.

The Joint Applicants provided no documentation that PAWC can construct, operate and maintain the existing SSA system and proposed LTCP improvements at a lesser cost than SSA. OCA St. 1 at 4; OCA St. 2 at 32. As stated by OCA witness Rubin:

Q. In your opinion, are there compelling reasons why PAWC should be allowed to acquire the Authority's CSS and become the first privately owned provider of stormwater service in Pennsylvania?

A. No. OCA's engineering witness, Mr. Fought, explains in his testimony that there are no advantages to the public (or to the environment) from having PAWC own the Scranton-Dunmore system. PAWC is not committing to undertake any physical construction or studies that the Authority is not already required to undertake. PAWC does not claim that it has significant expertise in the operation of a combined wastewater-stormwater utility and, in fact, it appears that it would rely on existing Authority employees for most of that expertise. In other words, it appears that the level and quality of service will be the same under PAWC ownership as it would be under SSA ownership.

Q. Can the public expect substantial cost savings under PAWC ownership as compared to continued Authority ownership?

A. No. From the documents that the Company and SSA have provided, it appears that PAWC will undertake the same projects on the same time-frame as the Authority. Moreover, the cost to the public of having PAWC undertake those projects is likely to be substantially greater than the costs that would be incurred by the Authority.

OCA St. 2 at 29. Mr. Rubin testified that PAWC's cost of capital will likely be higher compared to SSA, which does not have to pay income taxes and state and federal taxes on its equity earnings and has the advantage of being able to issue tax exempt debt. *Id.* at 30-31; Tr. 98.

PAWC is unable to "precisely quantify" any efficiencies or decreased operating costs resulting from the proposed transaction or indicate when they might occur. PAWC St. 4 at 5. It relies on the vague supposition that at some unknown time efficiencies "will inevitably be realized because of the size of PAWC's water and wastewater operations." PAWC St. 1 at 8; PAWC St. 4 at 5.

In contrast, the adverse impacts on PAWC's existing wastewater and water customers are known and measurable. Pursuant to the Asset Purchase Agreement, PAWC will pay an initial net cash payment of \$157 million and take responsibility for the required \$140 to \$199 million in investments in the SSA system, which are costs that will be recovered from its existing customers. PAWC Exh. BCG-1, Att. F (Sections 2.04, 3.01, 3.02(a)); OCA St. 2 at 31 (citing PAWC Response to OCA II-6, Attach. B, Table 2). Further, PAWC will request Commission approval to shift the costs of the acquisition to its existing water customers, at least \$104 million over the next 10 years. PAWC Exh. BCG-1, Att. F (Section 7.09(x)).

For these reasons, and those discussed above, the Joint Applicants have failed to show that the terms of the proposed transaction would result in any substantial, affirmative public

benefits to PAWC's existing water and wastewater customers or the acquired SSA customers after year 10. The OCA submits, therefore, that the Commission must deny the Application.

C. If The Commission Finds Affirmative Public Benefits, It Needs To Ensure That Certain Protections Are In Place Or All Benefits Will Be Lost.

If the Commission finds affirmative public benefits and that PAWC can acquire a stormwater system and operate it as a regulated service under the Public Utility Code, then it needs to ensure certain protections are put in place now or any benefits the Commission identifies will be lost. Specifically, the Commission needs to require that stormwater costs are separately allocated to Scranton customers and Scranton area entities that contribute to stormwater in the system. In addition, the Commission should find that the 1.9% CAGR provision is not reasonable because it improperly shifts costs to the existing PAWC wastewater and water customers. Also if any additional costs are due to the City of Scranton because of the variance adjustment that will be calculated 10 years after the transaction closes, these costs should not be collected from ratepayers but instead should be the PAWC shareholder's responsibility. For the reasons discussed below, these issues need to be addressed as part of the Commission Order in this proceeding to allow the Joint Applicants to determine whether the transaction will move forward.

1. Stormwater Costs Need To Be Separately Allocated to Scranton Customers.

If a PUC-regulated utility is ever to be permitted to provide stormwater service to the public, then the utility would need to develop separate rates and charges that were proportional to a customer's contribution of stormwater to the system. OCA St. 2 at 19-20. Mr. Rubin also concluded that it would be necessary to levy stormwater charges on the entities that contribute to the stormwater but are not wastewater customers. For example, building owners, but not tenants in a multi-unit building would need to be charged for the stormwater contribution of the building.

The tenants would not have any control over the stormwater management for the building and thus would not be charged a stormwater fee from PAWC. Id. at 19-20. Regarding the development of separate charges, Mr. Rubin stated:

[I]n my opinion such separate proportional charges would be necessary to pass muster as “just and reasonable” rates under Pennsylvania law and as being “based on some fair approximation of the [customer's] proportionate contribution” to stormwater under federal law.

OCA St. 2 at 20.

The estimated costs of the LTCP are \$169 million in August 2012 dollars. OCA St. 1 at 3; Exh. TLF-1. Approximately \$144 million plus a significant portion of the \$25 million for the wastewater treatment plant upgrade for BNR and CSO control is related to stormwater control. OCA St. 1 at 4. These amounts are in addition to the \$195 million that is the initial acquisition price under the proposed transaction.¹⁷

Stormwater costs are the majority of the costs that need to be expended under the consent decree. Thus, if PAWC is permitted to provide stormwater service to the public, it would need to develop separate rates and charges that were proportional to a customer’s contribution of stormwater to the system. OCA St. 2 at 19. As Mr. Fought explained, PAWC proposes that all of its water and sewer customers will pay a portion of the costs based on each customer’s water usage. OCA St. 1 at 11. PAWC’s proposal should be rejected.

First, there is no correlation between the volume of water used by a customer and stormwater runoff. Id. The stormwater runoff is based on the lot size, ground cover, soil type, ground slope, roof area, paved area, etc. Id. Mr. Fought recommended that the original cost, operation and maintenance costs of the SSA combined system be allocated between stormwater and wastewater, with the allocated wastewater costs from the combined system being added to

¹⁷ The impact of the variance adjustment on the final purchase price will not be known until 10 years after the transaction closes. OCA St. 2 at 23.

the wastewater costs from the customers located in the MS4 system. OCA St. 1 at 11-12. This procedure has been used in the City of Lancaster Sewer Fund's 2004 and 2012 rate cases. Id. at 12. The allocated stormwater costs could then be billed to either the City and the Borough or an Authority that could bill residents for stormwater costs. OCA St. 1 at 12.

Second, separately allocating the stormwater costs addresses the issues raised with the additional duties that PAWC has agreed to undertake, namely street sweeping and catch basin cleaning in the areas serviced by the combined system. OCA St. 1 at 12. Based on the relative areas of the MS4 system and the combined system as shown on Exhibit TLF-9, it is clear that the majority of the street sweeping and catch basin cleaning in the City of Scranton and the Borough of Dunmore will be the responsibility of PAWC, an investor-owned utility, rather than the municipalities. Id. Mr. Fought noted that PAWC does not provide those services in any other of its wastewater systems. Mr. Fought was unaware of any other PUC regulated utility, other than Lancaster, that is responsible for sweeping the streets and cleaning the catch basins of the municipalities it serves. Id.

Further, it is important to recognize that present PAWC water and wastewater customers reside in municipalities that are providing for and paying the costs of their stormwater handling. Id. Thus it would not be appropriate to allocate those costs, normally borne by municipalities, to PAWC's existing water and sewer customers outside of the Scranton and Dunmore areas. OCA St. 1 at 13. Mr. Fought noted that stormwater costs could be billed to the City of Scranton and the Borough of Dunmore or an Authority because it is the municipalities' responsibility to provide for the handling of stormwater within its borders.

2. The Costs Related To The Variance Adjustment Should Not Be Borne By Ratepayers.

Section 7.07(d) of the Asset Purchase Agreement limits the amount that PAWC can increase rates for wastewater and stormwater service over the next 10 years. If at the end of the 10 years, the actual increases exceed compound average of 1.9% per year, then PAWC must pay SSA an additional “purchase price” equal to the difference between the actual increases and the compound average of 1.9% per year. OCA St. 2 at 23. Mr. Rubin calculated the effect of the proposed rate increase limitation, compounded over 10 years to be equal to a total increase of 20.7% over the 10 year period. Id.

Mr. Rubin found that the 1.9% Compound Annual Growth Rate (CAGR) limitation was also not reasonable in light of the known capital investments that would be made in the SSA system during that same time. He provided an example of the impact on the purchase price that could be expected, using the SSA’s most recent annual report for the 12 months ending March 31, 2015.¹⁸ OCA St. 2 at 23-24.

For the year ending 3/31/15, SSA had total operating revenues of \$22,694,320. A 20.7% increase, as would be the result of the 1.9% CAGR, would mean total allowable revenues of \$27,392,000, or an increase of \$4.7 million over 10 years. Id. at 24.

SSA has projected its revenue requirement in 2026 (i.e., when the 10 year CAGR period would end) would be \$45 million. OCA St. 2 at 24. So, in 2026, the 20.7% rate increase limitation would result in a shortfall of \$17.7 million in revenues in just that one year. Id. Mr. Rubin calculated the shortfall in each of the first 10 years. Schedule SJR-1. His calculations, using the SSA numbers, shows that the total 10 year shortfall would be \$104 million. OCA St. 2 at 24; Sch. SJR-1.

¹⁸ First document in Schedule 4.05 to the Asset Purchase Agreement. PAWC Exh. BJG-1, Exh. F.

Under the terms of Section 7.07 of the Asset Purchase Agreement (PAWC Exh. BJK-1, Exh. F), if PAWC is required to charge cost-based rates to the SSA customers over the first 10 years, then PAWC would be required to pay SSA an additional \$104 million as an enhanced “purchase price.” OCA St. 2 at 24-25.

Mr. Rubin also looked at the impact that PAWC’s higher cost of capital will have on the possible adjustment to the purchase price. As discussed above, there are two factors that significantly affect the cost of PAWC ownership. OCA St. 2 at 29. The first is the differences in the cost of capital between PAWC and SSA. Id. The second is difference in the tax structure of PAWC and SSA. Id. In order to understand the relative impact of the cost of capital differences, Mr. Rubin used PAWC’s most recent annual report for the period ending 12/31/15¹⁹ and SSA’s most recent available annual report for the year ending 3/31/15. OCA St. 2 at 30. He used actual results for the respective accounting period and did not reflect any pro forma adjustments or cost projections that might be made in a rate case. Id. Mr. Rubin’s review estimates that the cost of capital for PAWC is about 60% higher than the Authority’s cost of capital due to higher debt costs and the requirement that PAWC pay federal, state, and local income taxes. Id. PAWC’s overall cost of capital is 11.72% while SSA’s cost of capital is 7.38%. Id. Mr. Rubin indicated that difference means that if a \$1 million investment is needed in the system, it would cost the Authority about \$74,000 per year to finance that capital while it would cost PAWC, and ultimately its customers almost \$120,000 per year to finance the same investment. The impact this has on the revenue requirement that PAWC proposes to shift to its existing water customers in order to keep SSA customers at or below the 1.9% CAGR is to increase the subsidy from about \$104 million to closer to \$150 million over the first ten years. OCA St. 2 at 33. Over 30

¹⁹ Mr. Rubin used the water operations report because the wastewater report did not include information on the full capital structure.

years, that subsidy would go from \$360 million under SSA cost rates to \$500 million at PAWC's cost rate. Id.

In rebuttal, PAWC presented a new witness who criticized Mr. Rubin's calculation of the cost of capital analysis. PAWC St. 5-R at 4-6. In surrebuttal, Mr. Rubin restated that his calculation used reported financial information to determine the difference in what it costs each entity to finance their operations. Tr. 97-98. He did not claim to be calculating a fair rate of return for either entity. Id. Rather he used the publicly available information to show relative costs of capital while noting that PAWC has to pay income taxes, state and federal taxes on its equity earnings while the Authority does not have to do that. Id. He also noted that the Authority has the advantage of being able to issue tax exempt debt, which typically has a lower cost rate than debt that PAWC would issue. Id.

It is not reasonable for PAWC's existing customers to pay such a large subsidy. While Section 1311(c), 66 Pa. C.S. § 1311(c) gives the PUC discretion to shift some wastewater costs to water customers under the same corporate umbrella, it does not apply to stormwater costs, which are the bulk of the SSA costs that would be shifted to the water customers. OCA St. 2 at 34. As noted previously, every other water customer has to pay for wastewater disposal and must pay taxes or other fees to control stormwater in their community. Id.

Mr. Rubin recommended that the Commission must prevent PAWC's existing customers from paying \$104 million over the next 10 years to subsidize the purchase price. OCA St. 2 at 27-28. He recommended that if PAWC wants to agree to the 10-year rate limitation, in lieu of an increase in the purchase price, then PAWC's investors must assume the cost of that investment. Id. By preventing PAWC from transferring cost responsibility away from SSA customers, the Commission would require PAWC to be responsible for the entire purchase price to which it

agreed: the initial net cash payment of \$156.66 million as well as an additional \$104 million (or more) payable either through reduced revenue collections from customers or a one-time payment in 10 years. OCA St. 2 at 28.

3. Recommended Conditions

As summarized in the testimony of OCA witness Rubin, the OCA recommends that the Commission deny the relief requested in the Joint Application. OCA St. 2 at 4-5. If, however, the Commission permits a privately-owned utility to provide stormwater service for compensation through a combined wastewater/stormwater system, the OCA recommends the following conditions:

1. PAWC must develop separate rates and charges that are proportional to a customer's contribution of stormwater to the system. PAWC will levy stormwater charges solely on building owners, rather than tenants, particularly for multi-unit buildings where the tenants have no control over stormwater management for the buildings.
2. PAWC's investors, rather than existing customers, will assume the costs of subsidizing the purchase price adjustment of \$104 million.
3. PAWC will not use the revenue-sharing provision of Section 1311(c) of the Public Utility Code for SSA for at least the first 10 years post-closing.
4. Any claim by the Company that its acquisition price should be higher than book value, or that any increment above book value should be included in rates as an acquisition adjustment should be addressed in a future proceeding, *i.e.* no acquisition adjustment is approved in this proceeding.

OCA St. 2 at 4-5. The evidentiary record and legal discussion herein supports a Commission decision to deny the Application by a privately-owned utility to provide wastewater and stormwater service for compensation. The record also shows the proposed transaction will

provide no affirmative benefit and will cause detriment to PAWC's existing wastewater and water customers and the SSA customers in years 11 through 13 post-acquisition. If the Commission approves the proposed acquisition, however, then the OCA submits that its recommended conditions should be adopted.

V. CONCLUSION


The OCA's recommendation that the Commission deny PAWC's application for a Certificate of Public Convenience to purchase the SSA wastewater and stormwater assets and provide wastewater and stormwater service is consistent with applicable law, under which a regulated public utility cannot provide stormwater service for compensation. The OCA's recommendation is also intended to prevent PAWC's existing water and wastewater customers from bearing the costs of a transaction that provides no affirmative benefit. For both reasons, the agreement struck by PAWC and SSA must be denied. In the alternative, the Application should be conditioned so that PAWC's existing water and wastewater customers are not penalized by paying rates that reflect PAWC's provision of stormwater service to the residents of Scranton and the Borough of Dunmore.

For the reasons set forth above, the Office of Consumer Advocate urges the Commission to find that the Application of PAWC and SSA does not satisfy the standards set forth in Section 1103(a) of the Public Utility Code and City of York. The OCA submits that the Commission must reject the proposed Application and that it would be appropriate to do so without prejudice. In the alternative, the OCA respectfully requests that the Commission condition its approval on the requirements that the existing PAWC water and wastewater customers are not burdened with paying costs attributable to the provision of stormwater service.

Respectfully submitted,



Christine Maloni Hoover
Senior Assistant Consumer Advocate
PA Attorney I.D. No. 50026
Email: CHoover@paoca.org



Erin L. Gannon
Senior Assistant Consumer Advocate
PA Attorney ID No. 83487
Email: EGannon@paoca.org

Counsel for:
Tanya J. McCloskey
Acting Consumer Advocate

Office of Consumer Advocate
555 Walnut Street 5th Floor, Forum Place
Harrisburg, PA 17101-1923
(717) 783-5048

Dated: July 19, 2016
223875

OCA Proposed Finding of Facts

1. The Sewer Authority of the City of Scranton's (SSA) system consists of 317 miles of collection sewers and large interceptors, 80 combined sewer overflows (CSOs), seven pumping stations, and a wastewater treatment plant (WWTP). OCA St. 1 at 2.
2. Fifty-four percent of the collection sewers, *i.e.* 172 miles, are "combined sewers" which convey both stormwater and wastewater. OCA St. 1 at 2.
3. When the total flow of wastewater and stormwater in the combined sewers exceeds the capacity of the interceptor sewers, pumping stations and/or treatment plant, partially treated or untreated flow is discharged to the Lackawanna River and nearby streams via CSOs. OCA St. 1 at 2.
4. Other portions of the City and the Borough are served by separate wastewater sewers and MS4 storm sewers. OCA St. 1 at 3.
5. PAWC intends to acquire the combined stormwater/wastewater facilities owned by SSA including the wastewater sewers in the MS4 area but excluding the storm sewers in the MS4 area. OCA St. 1 at 3.
6. In the Combined Sewer System (CSS), there are 80 permitted CSO discharge points including the WWTP headworks bypass, and 4 pumping station overflow outlets. OCA St. 1 at 3.
7. The assets to be purchased constitute the Authority's CSS, which includes facilities that are used for the collection, transmission, retention, and treatment of both wastewater and stormwater for approximately 31,000 customers in the City of Scranton and Borough of Dunmore. PAWC Exh. BCG-1 at 3-4.
8. Under the Federal CSO Policy, the SSA entered into a consent decree under which, among other things, the SSA adopted a 25-year Long Term Control Plan (LTCP) in 2012. The Authority is also implementing an approved Nine Minimum Controls (NMC) program. OCA St. 1 at 3.
9. Improvements to the combined sewer system and the wastewater treatment plant must be made to reduce CSO discharges to no more than 4 overflow events year during the typical year for outfalls that discharge into non-channelized, tributary streams and no more than 9 overflow events during the typical year for CSO outfalls that discharges to either channelized tributary streams or to the Lackawanna River. OCA St. 1 at 3.
10. Based on a hydraulic model of the combined sewer system, implementation of these improvements and the NMC measures will result in at least 90 percent system-wide wet weather capture in a typical year. OCA St. 1 at 3.

11. Pennsylvania-American Water Company is proposing to purchase most of the assets of the Authority for a stated purchase price of \$195 million subject to various adjustments at closing. PAWC Exh. BCG-1, Att. F (Section 3.01).
12. The purchase price includes the transfer of more than \$38 million in cash balances from the Authority to PAWC, so the net purchase price for the SSA's physical assets is approximately \$157 million. OCA St. 2 at 25.
13. The SSA assets have a net book value of less than \$74 million. OCA St. 2 at 25 (citing PAWC Exh. BCG-1, Att. F (Section 3.02(a))).
14. Pursuant to the Asset Purchase Agreement, PAWC is required to either limit the amount that it charges to SSA customers for the next 10 years or pay an enhancement to the purchase price at the end of the 10 years. PAWC Exh. BCG-1, Att. F (Section 7.07(d)).
15. The SSA system provides wastewater service and stormwater service.
16. The United States Environmental Protection Agency (USEPA) defines a combined sewer system as a network that "collects rainwater runoff, domestic sewage, and industrial wastewater into one pipe."¹ OCA St. 1 at 5; OCA St. 2 at 7.
17. Domestic sewage (the more common term now is domestic wastewater) is perhaps the easiest to understand: it is the waste that flows from indoor drains (sinks, showers, toilets, etc.) in residential buildings. It also includes similar types of wastewater from sinks and toilets in commercial and industrial buildings. OCA St. 2 at 8.
18. Industrial wastewater is liquid waste from industrial processes that may have chemical, biological, and/or physical characteristics that are very different from domestic wastewater. Those differences have led to numerous legal and regulatory requirements that require the pretreatment of industrial wastewater before it can be introduced into a system designed to treat domestic sewage. Domestic wastewater and industrial wastewater usually are referred to in the industry by the generic term wastewater. OCA St. 2 at 8.
19. Rainwater runoff, which is more commonly referred to by the broader label of stormwater (since it can include both rainwater runoff and water from the melting of snow and ice) is water that falls on streets, roofs, driveways, parking lots, bare soil, and other surfaces. OCA St. 2 at 8.
20. In order to prevent flooding of properties and roadways, the water is collected and transported, usually through a series of culverts, storm drains, and pipes, to a nearby waterway (stream, river, lake, or ocean). OCA St. 2 at 8-9.

¹ USEPA, Combined Sewer Overflows, <https://www.epa.gov/npdes/combined-sewer-overflows-csos>.

21. Stormwater usually is not subject to treatment (unless it is combined with wastewater), but it may be subject to various restrictions and limitations under discharge permits. OCA St. 2 at 9.
22. Stormwater discharge requirements have become more stringent during the past 20 to 25 years which has led to a separate focus on the way in which stormwater removal costs are collected by the stormwater service provider. OCA St. 2 at 9.
23. Current engineering practice for sewer systems involves the design of separate systems for wastewater and stormwater runoff. Tr. 145. Combined sewer systems are no longer designed. Id.
24. In these separate systems, “[w]astewater is conveyed to a wastewater treatment plant and stormwater is generally discharged without treatment to a receiving water.” OCA St. 1 at 5-6; OCA St. 1 at 6 (citing Domestic Wastewater Facilities Manual, A Guide for the Preparation of Applications, Reports and Plans, Bureau of Water Quality Protection, Commonwealth of PA, Dept. of Envir. Protection, at 15 (Oct. 1997).
25. The SSA system was designed to serve the dual purpose of removing both sanitary sewage and storm water from developed areas of the community. OCA Exh. TLF-10. These portions of the Sewer System are a combined sewer system (CSS), designed to convey a combination of storm water and sanitary sewage downstream directly to area streams, where the combined sewage was discharged without any treatment prior to 1972. Id.
26. Scranton and Dunmore have delegated the responsibility for providing stormwater service within their borders to the SSA and have agreed with how the stormwater costs in the combined sewer system are allocated to their residents. OCA St. 1 at 3.
27. There are other combined sewer systems in Pennsylvania, however, none of them are owned or operated by a privately-owned public utility. OCA St. 1 at 5.
28. All combined stormwater/wastewater systems in Pennsylvania are owned by municipal authorities or corporations and the Commission has no jurisdiction over their rates and service, with the one exception. OCA St. 1 at 5.
29. The Public Utility Commission regulates the rates and service of the portion of customers residing outside the city limits served by the City of Lancaster Sewer Fund. OCA St. 1 at 5.
30. The Public Utility Code does not contain the term “stormwater.” 66 Pa. C.S. § 101-3316.
31. The common and approved meaning of the term “wastewater,” is not used in the industry to refer to both wastewater and stormwater. OCA St. 1 at 6.

32. It is generally understood that “wastewater” (previously sewage) includes domestic wastewater, industrial wastewater, and infiltration/inflow within the sewer system. OCA St. 1 at 6 (citing DEP Manual at 43.4 and 25 Pa. Code §102.1).
33. It is generally understood that “stormwater” is water that falls on streets, roofs, driveways, parking lots, and other impervious and pervious surfaces such as grass and bare soil. OCA St. 1 at 6 (citing DEP Manual at 43.4 and 25 Pa. Code §102.1).
34. Where the General Assembly has intended to include stormwater in the types of service an entity can provide, it has amended the statute to add “stormwater” where the existing statute already authorized the provision of “sewer” service.
35. In 2013, the General Assembly amended the Municipal Authorities Act to allow municipal authorities to operate “storm water planning, management and implementation” projects. 53 Pa. C.S. § 5607(a)(18).
36. I/I consists of: (1) groundwater infiltrating into the joints and cracks in sewer pipes and manholes and (2) surface/stormwater flowing into the sewers from manhole covers and prohibited connections from roof drains, street inlets, etc. OCA St. 1S at 5.
37. I/I is to be reduced to the extent practicable and cost-effective in comparison to the costs if I/I is not reduced, *i.e.* extra operation and maintenance, adding capacity to sewers, pumping stations and treatment plants. OCA St. 1S at 5.
38. The inflow of surface/stormwater is not a deliberate design decision to introduce surface/stormwater into the collection system. OCA St. 1S at 5.
39. As Mr. Fought noted, a wastewater plant is not designed to and does not replace any municipal stormwater facilities. OCA St. 1S at 4.
40. Stormwater connections are prohibited in wastewater systems regulated by the PUC. OCA St. 1S at 4-5.
41. The Authority uses 10,000-14,000 stormwater catch basins and inlets designed to capture stormwater and introduce it into the SSA combined system. OCA St. 1 at 9.
42. The stormwater catch basins are not operationally equivalent to the I/I that may leak into a system around manhole covers; the impact of I/I compared to 10,000-14,000 stormwater catch basins on the operation of a wastewater system is very different. OCA St. 1 at 9-10.
43. The inflow around manholes of surface/stormwater into a wastewater collection system is a minor part of the overall system, whereas the design, and upkeep related to 10,000-14,000 stormwater catch basins drives the design and operation of a stormwater or combined system. OCA St. 1 at 9-10.

44. In the PAWC Northeast rate case, in a study conducted by Gannett Fleming, the I/I costs were treated as one of several costs of operating the wastewater system. See Tr. 141.
45. Sanitary sewer systems do not have catch basins designed to collect stormwater. OCA St. 2 at 10.
46. Wastewater utility service requires running pipes from each property to a wastewater treatment plant where the wastewater is treated prior to being discharged into a receiving water, such as a lake, stream, and river. OCA St. 2 at 9.
47. The customer controls its wastewater production and disposal, collects the wastewater produced in a building into a wastewater service line or pipe that connects to the wastewater main. OCA St. 2 at 9.
48. Stormwater service is not directly controlled by customers or contained in pipes throughout the process. OCA St. 2 at 9.
49. Stormwater is rain, snow, and ice melt. OCA St. 2 at 9. Some stormwater falls on pervious ground that can absorb some of the stormwater. Id. Other stormwater falls on roofs, streets, sidewalks, frozen ground and other impervious surfaces where it is not absorbed and it flows downhill. Id.
50. A stormwater control system directs the flow of the runoff so that it does not create flooding on private property or on public property. OCA St. 2 at 9-10. Stormwater flow is controlled by designing streets to direct the flow, grading properties, parking lots, and driveways to control the flow and maintaining streets (cleaning streets, repairing curbs, cleaning storm drains) so that stormwater enters storm drains and is collected in a network of pipes. OCA St. 2 at 10.
51. When there is a separate stormwater system, the stormwater is directly discharged to a body of water with little or no treatment. OCA St. 2 at 10; OCA St. 1 at 8.
52. In a system that combines storm sewers and sanitary sewers, stormwater flows commingle with wastewater flows and should be directed to a wastewater treatment plant. OCA St. 2 at 10; OCA St. 1 at 8.
53. In some older combined systems, like the SSA system, the flow exceeds the capacity of the pipes, which results in combined sewer overflows (CSO) that divert some of the combined flow before it reaches the wastewater treatment plant and discharges untreated wastewater and stormwater into a receiving water. OCA St. 2 at 10; OCA St. 1 at 8.
54. Mr. Rubin noted that one of the important clean water initiatives of the past two decades is to reduce or eliminate the use of CSOs. OCA St. 2 at 10; OCA St. 1 at 8.
55. Stormwater service is intertwined with other municipal functions, such as the maintenance of streets. OCA St. 2 at 19.

56. A significant part of the stormwater removal system in a developed area are the streets, culverts, and drainage ditches that are in the public right of way and that are designed, operated, and maintained by local (or state) government. OCA St. 2 at 19.
57. The movement of stormwater through a city depends in significant measure on the network of streets, drainage ditches, and culverts that are part of the public right-of-way and that are designed, constructed, and maintained by the government. OCA St. 2 at 20.
58. Some municipalities (such as Philadelphia) have found that it is more cost-effective to use stormwater management solutions that do not involve new pipes or larger detention basins, particularly when the stormwater and wastewater systems are combined. OCA St. 2 at 21.
59. For example, increasing vegetation (tearing up unused paved areas and planting trees or planting roof gardens), using porous paving materials, and encouraging property owners to reduce the size of paved areas are a few examples of what is termed “green infrastructure.” OCA St. 2 at 21. These types of measures can significantly reduce the amount of stormwater that flows into the system, but they cannot be mandated by a privately owned utility; they must be undertaken (and enforced) by local government. Id.
60. A privately owned stormwater utility lacks any meaningful enforcement method to collect stormwater bills from a property owner. OCA St. 2 at 22.
61. With all other utility services, the service can be disconnected if the customer does not pay. OCA St. 2 at 22. That is not true with stormwater; it is not possible to stop the rain from falling on a property. Id.
62. Under Authority ownership, the Authority has the ability to place liens on properties that have not paid the bills; PAWC would not have that ability. OCA St. 2 at 22.
63. Stormwater services are different from wastewater services and stormwater is not the same as I/I. OCA St. 1 at 6.
64. PAWC’s current wastewater tariff prohibits any stormwater from being introduced into its sanitary sewer. OCA St. 1 at 9. Under the tariff provision, no stormwater from “pavements, areas ways, runoff basins, roof runoff water, foundation drains, subsurface drains, water from springs, cooling water, basement sump pumps, unpolluted industrial or commercial process water or other sources shall be admitted to the Company Sanitary Sewer.”
65. It has become increasingly common over the past 20 years for state or local governments to create separate stormwater utilities or to have separate stormwater operations within larger public works departments. OCA St. 2 at 11.

66. The Water Environment Federation (WEF) found that in 1994 there were only a few local government agencies with separate fees for stormwater. OCA St. 2 at 11. By 2014, there were approximately 1,500 stormwater utilities in the United States and Canada. Id.
67. Fees for separate stormwater service have been set with a separate stormwater removal system as well as in those communities with combined stormwater wastewater systems. OCA St. 2 at 12.
68. The City of Philadelphia is one of the few Pennsylvania municipalities with a stormwater utility. Approximately two-thirds of Philadelphia is served by a CSS. The charges for providing stormwater service are separate from the charges for wastewater service. OCA St. 2 at 12-13.
69. Specifically, in Philadelphia wastewater charges are based in part on water consumption while stormwater charges are based on the characteristics of the property (all residential properties pay a flat rate for stormwater; non-residential properties pay a stormwater charge based on the gross area and impervious surface area of the property). OCA St. 2 at 13. The charges for stormwater service do not vary depending on whether a property is served by Philadelphia's separate stormwater system or by the combined system. Id.
70. Sewage (or wastewater) service often is based on water consumption while stormwater service usually is charged based on a property's size and/or impervious surface area. OCA St. 2 at 15.
71. In a multi-unit building, each unit might be a separate water and wastewater customer, but the building as a whole (that is, the owner of the building) would be the stormwater customer. OCA St. 2 at 15. An individual apartment in a building or single office in a professional building would have no responsibility for, and no ability to control, stormwater emanating from the building's roof, parking lot, and other outdoor surfaces. Id.
72. Congress amended the federal Clean Water Act to add a special provision that required federal agencies to pay "reasonable service charges" for stormwater service, so long as the charge is "based on some fair approximation of the proportionate contribution of the property or facility to stormwater pollution ... and used to pay or reimburse the costs associated with any stormwater management program (whether associated with a separate storm sewer system or a sewer system that manages a combination of stormwater and sanitary waste)" OCA St. 2 at 16.
73. In the energy industry, electric distribution services and electric supply services are both provided in part over the same physical facilities. The PUC regulates distribution. It does not regulate supply. The natural gas industry is similar. Tr. 97.
74. In the telecommunications industry, the same wires are used to provide services that are regulated at the state level, services that are regulated at the federal level and services that are completely unregulated, and basically local telephone, long distance telephone and

television services all being provided over the same physical facility, but three distinct services regulated or unregulated in three distinct ways. Tr. 97.

75. Sanitary systems do not have stormwater catch basins or area drains on road surfaces. Tr. 179.
76. Many entities without water connections, including parking lots, a city park, streets, contribute to stormwater are not wastewater customers under the current SSA and would not currently pay anything related to the costs of stormwater service. Tr. 180.
77. Those costs are currently collected from the SSA wastewater customers based on their water usage. Tr.183.
78. The PAWC customer base is not expanding. While SSA serves approximately 31,000 customers, essentially all of those customers are already PAWC water customers. OCA St. 2 at 34. PAWC's total customer count would not increase. Id.
79. PAWC plans for its existing wastewater and water customers to begin paying between \$146 and \$199 million of the costs of improvements to the SSA system when it increases rates in its next base rate case – as soon as January 1, 2018. PAWC St. 4 at 4, 7.
80. According to a rate study prepared for SSA in 2012, stormwater-related capital investments are projected to total between \$146 million and \$199 million (in 2011 dollars) over the next 20 years. OCA St. 1 at 31 (citing PAWC Response to OCA II-6, Att. B, Table 2).
81. PAWC proposes a zero percent increase in rates for the SSA customers in the Application proceeding and has agreed that it will not propose to increase the SSA customer rates by more than 1.9% compound annual growth rate (CAGR) over the 10 years post-acquisition. PAWC St. 4 at 3-4; Tr. 115-16.
82. Over the next 20 years, PAWC's wastewater and water customers will pay for nearly \$200 million of improvements to the SSA system.
83. PAWC also intends to continue charging the Distribution System Improvement Charge (DSIC) to existing wastewater customers' bills between base rate cases, but will not seek to charge the DSIC to the SSA customers before January 1, 2019. PAWC St. 4-R at 2.
84. PAWC's existing wastewater and water customers will be required to support nearly \$200 million in capital improvements just to the SSA system, plus the subsidies for keeping SSA rates lower than cost for the first 10 years post-acquisition, plus the subsidy related to not charging the DSIC rate for the first few years after acquisition.
85. Under the terms of Section 7.07 of the Asset Purchase Agreement (PAWC Exh. BJK-1, Exh. F), if PAWC is required to charge cost-based rates to the SSA customers over the first 10 years, then PAWC would be required to pay SSA at least an additional \$104

- million as an enhanced “purchase price.” OCA St. 2 at 24-25. PAWC then plans to recover that additional cost from its wastewater and water customers.
86. The \$195 million purchase price is already more than 2x the book value of the SSA’s assets. OCA St. 2 at 5.
 87. Even with the cash and equivalents of \$38,340,626 that SSA is required to provide, the net purchase price would be approximately \$156.66 million, still more than 2x the book value of all SSA assets. OCA St. 2 at 25.
 88. SSA’s balance sheet as of March 31, 2015 shows that the book value of all of SSA’s property, plant, and equipment is \$74,660,819. OCA St. 2 at 25.
 89. Not all of SSA’s assets (the stand-alone stormwater assets) are being acquired by PAWC, so the actual book value of the acquired assets is something less than \$74,660,819. OCA St. 2 at 25.
 90. Section 7.09(x) of the Asset Purchase Agreement states that in PAWC’s first base rate proceeding following closing, PAWC shall include a request to combine partially, under Section 1311(c), water and wastewater revenue requirements for ratemaking purposes “to ensure the System’s customers benefit from Act 11 in the same manner as its other customers throughout Pennsylvania.” OCA St. 2 at 26; Asset Purchase Agreement, PAWC Exh. BJG-1, Exh. F.
 91. No new customers are being acquired (all SSA customers are already water customers of PAWC), so there is no meaningful reduction in overhead or back-office costs per customer resulting from the proposed transaction. OCA St. 2 at 27.
 92. PAWC intends to seek Commission approval to spread the costs of improving SSA’s system to its existing water customers. OCA St. 2 at 33-35; PAWC St. 4 at 4; PAWC Exh. BCG-1, Att. F, Section 7.09(x).
 93. PAWC plans to collect just \$23.2 million of its \$31.4 million revenue requirement from SSA customers, a shortfall of \$8.2 million. The amount by which SSA would be subsidized by other customers would increase each year through 2024 before declining for the next few years. In total, the response to I&E-10 projects subsidies from other PAWC customers totaling in excess of \$120 million over a 13-year period. OCA St. 2 at 33.
 94. The total subsidy from existing PAWC water customers is more than \$360 million over the 30-year period. OCA St. 2 at 33.
 95. Every other PAWC water customer already has to pay for wastewater disposal and must pay taxes or other fees to control stormwater in his/her community. OCA St. 2 at 34-35.

96. PAWC customers in Mount Lebanon, PA, currently pay PAWC for water, pay the Borough of Mount Lebanon \$4.05 per 1,000 gallons for wastewater disposal and \$8.00 per month for stormwater control. OCA St. 2 at 34-35.
97. During the first ten years post-acquisition, PAWC will not propose to increase rates for SSA customers by more than 1.9% CAGR over the 10-year period, SSA customers will not pay a DSIC prior to January 1, 2019, the substantial costs of improving the system will be subsidized by PAWC's existing wastewater customers and, if the Commission allows, by its water customers. PAWC St. 4-R at 2; PAWC Exh. BCG-1, Att. F (Section 7.09(x)); PAWC Exh. BCG-1, Att. J at 3.
98. PAWC indicates intends to move the SSA customers to its system rates in equal increments in years 11 through 13 following closing of the transaction. PAWC St. 4 at 3; PAWC St. 4-R at 2.
99. If approved as proposed, PAWC would charge an SSA customer using 3,000 gallons of water per month \$34.50 compared to charging an existing Rate Zone 1 customer \$46.14 for the same usage. PAWC Exh. BCG-1, Att. L; App. B (Supp. 2 PAWC Tariff-Wastewater Pa. P.U.C. No. 15 at 4).
100. Section 7.07(d) of the Asset Purchase Agreement provides that, if at the end of 10 years the actual increases exceed a compound average of 1.9% per year, then PAWC must pay an additional "purchase price" equal to the difference. PAWC Exh. BCG-1, Att. F (Section 7.07(d)); OCA St. 2 at 23.
101. The Authority has sole discretion whether PAWC will distribute the variance adjustment to its current wastewater customers in the City of Scranton and Borough of Dunmore or pay the adjustment directly to the Authority with no limitation on how the funds are used. PAWC Exh. BCG-1, Att. F (Section 7.07(e)).
102. Even if the adjustment is paid to wastewater customers in the Scranton area, it will be partly recovered from the same customers in their water rates. PAWC Exh. BCG-1, Att. F, Section 7.09(x).
103. There is no evidence that the current owner is not technically or managerially able to operate the existing system and perform the proposed improvements. Tr. at 154; OCA St. 1 at 4.
104. As a term of the transaction, PAWC will offer employment to SSA staff. PAWC Exh. BCG-1, Att. F (Section 7.04(b)).
105. SSA has an A- bond rating (compared to PAWC's A) and that SSA adopted a Long-Term Control Plan in 2012, with full knowledge of the associated costs. OCA St. 1 at 3-4; PAWC St. 6-R at 25; Tr. 126, 154; PAWC Exh. JCE-5.

106. Standard & Poor's noted SSA's healthy financial profile, its strong debt service coverage and liquidity. Tr. 98-99.
107. There is no reason to believe that SSA could not finance the capital improvements over the next 20 years that it agreed to implement in its consent decree with the federal and state governments. Tr. 99-100.
108. Standard & Poor's noted that, assuming SSA can implement reasonable rate increases over time, it will be able to finance the obligations it has agreed to. Id. at 100.
109. The Joint Applicants provided no documentation that PAWC can construct, operate and maintain the existing SSA system and proposed LTCP improvements at a lesser cost than SSA. OCA St. 1 at 4; OCA St. 2 at 32.
110. PAWC will undertake the same projects on the same time-frame as the Authority. Moreover, the cost to the public of having PAWC undertake those projects is likely to be substantially greater than the costs that would be incurred by the Authority. OCA St. 2 at 29.
111. PAWC's cost of capital will likely be higher compared to SSA, which does not have to pay income taxes and state and federal taxes on its equity earnings and has the advantage of being able to issue tax exempt debt. OCA St. 2 at 30-31; Tr. 98.
112. PAWC is unable to "precisely quantify" any efficiencies or decreased operating costs resulting from the proposed transaction or indicate when they might occur. PAWC St. 4 at 5.
113. Pursuant to the Asset Purchase Agreement, PAWC will pay an initial net cash payment of \$157 million and take responsibility for the required \$140 to \$199 million in investments in the SSA system, which are costs that will be recovered from its existing customers. PAWC Exh. BCG-1, Att. F (Sections 2.04, 3.01, 3.02(a)); OCA St. 2 at 31 (citing PAWC Response to OCA II-6, Attach. B, Table 2).
114. PAWC will request Commission approval to shift the costs of the acquisition to its existing water customers, at least \$104 million over the next 10 years. PAWC Exh. BCG-1, Att. F (Section 7.09(x)).
115. Stormwater costs are the majority of the costs that need to be expended under the consent decree. OCA St. 2 at 19.
116. There is no correlation between the volume of water used by a customer and stormwater runoff. OCA St. 2 at 19.
117. Separately allocating the stormwater costs addresses the issues raised with the additional duties that PAWC has agreed to undertake, namely street sweeping and catch basin cleaning in the areas serviced by the combined system. OCA St. 1 at 12.

118. The majority of the street sweeping and catch basin cleaning in the City of Scranton and the Borough of Dunmore will be the responsibility of PAWC, an investor-owned utility, rather than the municipalities. OCA St. 1 at 12. PAWC does not provide those services in any other of its wastewater systems. Id.
119. The effect of the proposed rate increase limitation, compounded over 10 years to be equal to a total increase of 20.7% over the 10 year period. OCA St. 2 at 23.
120. For the year ending 3/31/15, SSA had total operating revenues of \$22,694,320. A 20.7% increase, as would be the result of the 1.9% CAGR, would mean total allowable revenues of \$27,392,000, or an increase of \$4.7 million over 10 years. OCA St. 2 at 24.
121. In 2026, the 20.7% rate increase limitation would result in a shortfall of \$17.7 million in revenues in just that one year. OCA St. 2 at 24.
122. Under the terms of Section 7.07 of the Asset Purchase Agreement (PAWC Exh. BJK-1, Exh. F), if PAWC is required to charge cost-based rates to the SSA customers over the first 10 years, then PAWC would be required to pay SSA an additional \$104 million as an enhanced “purchase price.” OCA St. 2 at 24-25.
123. The cost of capital for PAWC is about 60% higher than the Authority’s cost of capital due to higher debt costs and the requirement that PAWC pay federal, state, and local income taxes. OCA St. 2 at 30. PAWC’s overall cost of capital is 11.72% while SSA’s cost of capital is 7.38%. Id.
124. That difference means that if a \$1 million investment is needed in the system, it would cost the Authority about \$74,000 per year to finance that capital while it would cost PAWC, and ultimately its customers almost \$120,000 per year to finance the same investment. OCA St. 2 at 30-31.

Proposed Conclusions of Law

1. The Public Utility Commission must deny the Application if it finds that it does not have jurisdiction over the assets being transferred, which provide wastewater and stormwater services.
2. The Public Utility Commission has jurisdiction over sewer service. 66 Pa. C.S. §§ 102(1)(vii),
3. The Public Utility Commission does not have jurisdiction over stormwater service and the assets being transferred from Scranton Sewer Authority to PAWC.

If the Commission determines that it has jurisdiction:

1. The Joint Applicants did not meet their burden of proving by a preponderance of the evidence that the proposed acquisition of the Scranton Sewer Authority assets and the proposed ratemaking terms will affirmatively promote the “service, accommodation, convenience, or safety of the public in some substantial way. 66 Pa. C.S. § § 316(c), 332.
2. The acquisition by PAWC is not in the public interest and does not provide a substantial affirmative benefit. 66 Pa. C.S. §§ 1102(a)(2), 1103(a); City of York v. Pa. P.U.C., 449 Pa. 136, 141, 295 A.2d 825, 828 (1972).
3. The acquisition as proposed would result in the harm outweighing any benefits and the proposed transfer is not in the public interest.

If the Commission determines that it has jurisdiction and that there are affirmative public benefits:

1. The Public Utility Commission has the authority to impose conditions on the grant of a certificate of public convenience. 66 Pa. C.S. § 1103.
2. The Application is found to provide affirmative public benefits with the following conditions:
 - a. PAWC must develop separate rates and charges that are proportional to a customer's contribution of stormwater to the system. PAWC will levy stormwater charges solely on building owners, rather than tenants, particularly for multi-unit buildings where the tenants have no control over stormwater management for the buildings.
 - b. PAWC’s investors, rather than existing customers, will assume the costs of subsidizing the purchase price adjustment of \$104 million.
 - c. PAWC will not use the revenue-sharing provision of Section 1311(c) of the Public Utility Code for SSA for at least the first 10 years post-closing.
 - d. Any claim by the Company that its acquisition price should be higher than book value, or that any increment above book value should be included in rates as an acquisition adjustment should be addressed in a future proceeding, *i.e.* no acquisition adjustment is approved in this proceeding.

Proposed Ordering Paragraphs:

IT IS ORDERED:

1. PAWC and SSA’s Joint Application is hereby denied because the Commission does not have jurisdiction over stormwater.

If the Commission determines that it has jurisdiction:

1. PAWC and SSA’s Joint Application is hereby denied because the Application does not affirmatively promote the service, accommodation, convenience or safety of the

public in some substantial way.

If the Commission determines that it has jurisdiction and that there are affirmative public benefits:

1. PAWC and SSA's Joint Application is hereby approved, subject to the following conditions that are intended to create an affirmative public benefit:
 - a. PAWC must develop separate rates and charges that are proportional to a customer's contribution of stormwater to the system. PAWC will levy stormwater charges solely on building owners, rather than tenants, particularly for multi-unit buildings where the tenants have no control over stormwater management for the buildings.
 - b. PAWC's investors, rather than existing customers, will assume the costs of subsidizing the purchase price adjustment of \$104 million.
 - c. PAWC will not use the revenue-sharing provision of Section 1311(c) of the Public Utility Code for SSA for at least the first 10 years post-closing.
 - d. Any claim by the Company that its acquisition price should be higher than book value, or that any increment above book value should be included in rates as an acquisition adjustment should be addressed in a future proceeding, *i.e.* no acquisition adjustment is approved in this proceeding.

Appendix B

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Joint Application of Pennsylvania-American :
 Water Company and the Sewer Authority :
 of the City of Scranton for Approval of :
 (1) the transfer, by sale, of substantially all :
 of the Sewer Authority of the City of Scranton’s :
 Sewer System and Sewage Treatment Works : Docket No. A-2016-2537209
 assets, properties and rights related to its :
 wastewater collection and treatment system to :
 Pennsylvania-American Water Company, and :
 (2) the rights of Pennsylvania-American Water :
 Company to begin to offer or furnish wastewater :
 service to the public in the City of Scranton and :
 the Borough of Dunmore, Lackawanna County, :
 Pennsylvania.

Testimony, Schedules and Exhibits of the
Office of Consumer Advocate

1. OCA Statement No. 1 – The Direct Testimony of Terry L. Fought dated June 14, 2016, Appendix A – Background and Qualifications of Terry L. Fought and Exhibits TLF-1 through TLF-9 (admitted into the record on July 6, 2016).
2. OCA Statement No. 2 – The Direct Testimony of Scott J. Rubin dated June 14, 2016, Appendix A – VITAE of Scott J. Rubin, and Schedule SJR-1 (admitted into the record on July 6, 2016).
3. OCA Statement No. 1S – The Surrebuttal Testimony of Terry L. Fought dated July 6, 2016, and Exhibit TLF-10 (admitted into the record on July 6, 2016).
4. OCA Exhibit No. 1 – Standard & Poor’s May 7, 2015 Report on American Water Works Co., Inc. (admitted into the record on July 8, 2016).

Pennsylvania-American Water Company

PART I:

- The rates as set forth below will be in effect for all Coatesville, Claysville and Clean Treatment wastewater customers. (C)

Metered Charges (Based on Water Usage or Sewage Flows, determined at PAWC's discretion)

All metered customers shall be subject to a monthly service per equivalent dwelling unit (EDU).

A. Residential ***

Service Charge per month: \$ 7 50
per 100 gallons \$1.2880 (D)

B. Commercial

Service Charge per month: \$20 00

Service Charge per month Coatesville only:

5/8" meter \$ 7.50

3/4" - 1 1/2" meter \$10.00

2" meter and up \$20.00

Usage Charge per 100 gallons \$1.1194 (D)

C. Industrial

Service Charge per month: \$20.00

Usage Charge per 100 gallons \$1.1194

D. Municipal

Service Charge per month: \$20 00

Usage Charge per 100 gallons \$1.1194