# PENNSYLVANIA

**PUBLIC UTILITY COMMISSION**

**Harrisburg, PA 17105-3265**

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| Public Meeting held October 6, 2016 |
| Commissioners Present:  Gladys M. Brown, Chairman  Andrew G. Place, Vice Chairman, Dissenting Statement  John F. Coleman, Jr.  Robert F. Powelson  David W. Sweet, Statement |
| Joint Application of Pennsylvania-American A-2016-2537209  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 |

**OPINION AND ORDER**

**BY THE COMMISSION:**

Before the Pennsylvania Public Utility Commission (Commission) for consideration and disposition are the Exceptions filed by Pennsylvania-American Water Company (PAWC) and the Sewer Authority of the City of Scranton (SSA) (Joint Applicants) and the Office of Consumer Advocate (OCA) on September 2, 2016, to the Recommended Decision (R.D.) of Administrative Law Judges (ALJs) David A. Salapa and Steven K. Haas, issued on August 24, 2016, in the above captioned proceeding. On September 8, 2016, the OCA, the Joint Applicants, the Office of Small Business Advocate (OSBA), and the Commission’s Bureau of Investigation and Enforcement (I&E) filed Replies to Exceptions.

**I. History of the Proceeding**

On March 30, 2016, the Joint Applicants filed their joint application requesting that the Commission, pursuant to 66 Pa. C.S. § 1102, approve PAWC’s acquisition of substantially all of the assets of SSA’s sewer system and sewage treatment works and approve PAWC’s application to render wastewater service in the areas served by SSA (Joint Application).[[1]](#footnote-1)

On April 5, 2016, the OCA filed a protest and public statement and on April 8, 2016, I&E filed a notice of appearance.

Notice of the Joint Application was published in the April 9, 2016 *Pennsylvania Bulletin* at 46 *Pa. B.* 1882, specifying a deadline of April 25, 2016, for filing protests, petitions to intervene and answers to the Joint Application.

The Joint Applicants published notice of the Joint Application in the *Scranton Times* on April 12, 2016, and April 19, 2016. On April 25, 2016, the Joint Applicants filed proofs of publication with the Commission.

On April 25, 2016, the OSBA filed an answer, notice of intervention and public statement.

On May 13, 2016, the Joint Applicants filed a motion, pursuant to 52 Pa. Code §§ 5.91 and 5.103, to amend Exhibit L of the Joint Application, involving industrial pretreatment programs (IPP-S).[[2]](#footnote-2) No answers were filed in response to the motion to amend the Joint Application. By order dated June 15, 2016, the ALJs granted the motion to amend.

On July 1, 2016, the Joint Applicants filed seven unsigned *pro forma* agreements, pursuant to 66 Pa. C.S. § 507, seeking Commission approval of the agreements. The *pro forma* agreements are between PAWC and SSA where PAWC agreed to assume contractual obligations of SSA. The contractual obligations are agreements between SSA and various entities concerning the acquisition of facilities or the provision of services by SSA.

On July 6-8, 2016, evidentiary hearings were held as scheduled. The evidentiary hearings resulted in a 168-page transcript, consisting of pages forty-nine through 217. The record also includes various statements and exhibits submitted by the Parties.

On July 19, 2016, the Parties filed Main Briefs (M.B). On July 27, 2016, the Parties, with the exception of OSBA, filed Reply Briefs (R.B.), and the record was closed on the same day.

On August 24, 2016, the Commission issued the Recommended Decision of ALJs Salapa and Haas, in which the ALJs denied the Joint Application. Exceptions were due on August 31, 2016, and Replies to Exceptions were due on September 6, 2016.

On August 31, 2016, the Joint Applicants filed an unopposed request for an extension of time to file Exceptions and Replies to Exceptions. The Joint Applicants requested an additional two days to file Exceptions and Replies, stating that the additional time was required due to the shortened Exceptions period and the ongoing conversations between the Parties regarding the issues raised in the case.

On the same day, the Joint Applicants filed a letter memorializing the Commission’s approval of the two-day extension request by telephone. Per the letter, Exceptions were due on September 2, 2016, and Reply Exceptions were due on September 8, 2016.

As previously noted, the Joint Applicants and the OCA filed Exceptions on September 2, 2016. No Exceptions were filed by I&E and the OSBA. Replies to Exceptions were filed by the OCA, I&E, OSBA and the Joint Applicants on September 8, 2016.

**II. Background**

SSA is a municipal authority organized under the laws of Pennsylvania. SSA owns and operates a wastewater collection and treatment system that provides wastewater service to the City of Scranton (City) and the Borough of Dunmore (Borough) in Lackawanna County. SSA’s wastewater collection system is a 100-year old, gravity fed, combined sewer and stormwater conveyance system. The system includes a sixty million gallons per day (60-MGD) capacity wastewater treatment plant built in 1969-1970. SSA’s wastewater collection and treatment system consists of approximately 275 miles of sewer mains, of which approximately 172 miles are combined sewers, eighty combined outflows and seven pumping stations. SSA’s wastewater treatment plant services approximately 31,229 customers for an estimated population of approximately 90,000. Approximately 95% of SSA’s wastewater customers are residential customers who account for about 85% of SSA’s revenues. Joint Application at 3-4; SSA St. 1 at 3.

PAWC is a public utility regulated by the Commission, providing water and wastewater service to the public. PAWC provides water and wastewater service to more than 400 communities in Pennsylvania. PAWC currently provides water service to the City and the Borough and operates fifteen wastewater treatment plants in Pennsylvania, including three Biological Nutrient Removal (BNR) wastewater treatment plants similar to SSA’s wastewater system. Joint Application at 3; PAWC St. 3 at 4.

The majority of SSA’s service area is currently served by combined sewers, which collect and convey a combined wastewater stream consisting of flows of sewage from homes and businesses’ infiltration and inflow and stormwater (SSA’s combined wastewater). The remainder of SSA’s combined wastewater system (not including the MS4 system, which is not part of this acquisition) [[3]](#footnote-3) consists of sanitary sewer mains which discharge wastewater into the combined sewer main. Joint Applicants’ M.B. at 1. According to the Joint Applicants, SSA’s combined wastewater system is under a consent decree between SSA, DEP, the U.S. Environmental Protection Agency (EPA) and the U.S. Department of Justice (DOJ) (Consent Decree). *Id.*

The Consent Decree, dated January 31, 2013, requires, *inter alia,* short and long term system improvements on SSA’s wastewater system and ongoing operating requirements to ensure proper treatment and control discharges that comply with applicable federal and state environmental laws. The Consent Decree commits SSA to approximately $140 million in capital improvements over a twenty-five year period ending December 1, 2037 (Long Term Control Plan or LTCP). *Id.*; SSA St. 1 at 4. In addition, SSA’s consultants estimated that to meet the financial demands of the improvements required in the Consent Decree, SSA would have to raise its customers’ wastewater rates an average of 4.75% per year over the next thirty years. SSA St. 1 at 5. Consequently, SSA considered either entering into an agreement with a third party to operate and maintain its wastewater collection and treatment system or selling the system to an entity that is capable of implementing the requirements of the Consent Decree while also maintaining reasonable wastewater rates for its customers. *Id.*

On March 3, 2015, SSA issued a Request for Proposal (RFP) soliciting proposals for a long term maintenance and operations agreement as well as proposals for the purchase of its wastewater collection and treatment system. On December 15, 2015, SSA executed a Memorandum of Understanding (MOU) with PAWC, after it selected PAWC as its preferred bidder. The MOU outlined a time period for negotiation and execution of a sales agreement between SSA and PAWC. On March 29, 2016, SSA and PAWC successfully negotiated and executed an Asset Purchase Agreement (APA). Per the APA, PAWC will purchase substantially all of the assets, properties and rights of SSA’s wastewater collection and treatment system for $195 million, subject to certain adjustments, including a variance adjustment. Joint Application; Exhibit J. Below are some of the terms of the APA:

***Purchase Price:*** PAWC agrees to pay the sum of $195 million for SSA’s wastewater assets to be transferred. This price shall be reduced by the amount necessary to bring the closing cash balance to $38,340,626. Further, at closing, there will be a cost of full defeasances of the total amount of the outstanding indebtedness as of the closing effective time. *Id.*

***1.9% Compounded Annual Growth Rate (1.9% CAGR) and Variance Adjustment:*** The purchase price of SSA’s wastewater system assets may be adjusted should the Commission approve rates that produce revenues from SSA’s wastewater customers in excess of 1.9% CAGR at the end of year ten following closing. The Parties to the APA would determine the formula for the 1.9% CAGR if there is a need to adjust the purchase price at the end of the tenth year following closing. For instance, if the revenues from SSA’s customers exceed the 1.9% CAGR after year ten following closing, PAWC would adjust the purchase price to compensate SSA for the excess amount. Section 7.07(e) of the APA states that SSA can retain the excess payment from PAWC or redistribute it to SSA’s wastewater customers. The Joint Applicants, nonetheless, indicated that the 1.9% CAGR would in no way limit the Commission’s ability to set just and reasonable rates for PAWC in a future base rate proceeding. PAWC St. 4 at 2-3, 6.

***Wastewater Rates:*** Over time, PAWC intends to adopt system wide uniform wastewater rates and to move all of its wastewater customers, including SSA’s wastewater customers’ rates to its Rate Zone 1 rates. Therefore, the APA provides that PAWC will gradually bring SSA’s wastewater customers’ rates into alignment with PAWC’s Rate Zone 1 rates. To do this, PAWC will adopt, upon closing, SSA’s current wastewater customer charge and consumption charge, as long as PAWC would be allowed to bill monthly as opposed to SSA’s current bi-monthly billing. After closing, SSA’s wastewater customers will adopt PAWC’s existing wastewater tariff on file with the Commission regarding all rates and non-related terms and conditions of service except for the customer charge and consumption charge. *Id.* at 3.

***Wastewater Rate Freeze:*** PAWC has agreed not to implement a rate increase for SSA’s customers prior to January 1, 2018, and not to implement a distribution system improvement charge (DSIC) prior to January 1, 2019. PAWC would also, in its first rate increase following closing, propose a 0% increase for SSA’s wastewater customers. The APA, nonetheless, acknowledges that the Commission has the final say on whether or not an increase in SSA’s wastewater customers’ rates will be needed. *Id.* at 4.

***Equal Increments in Wastewater Rates:*** The APA also indicates that from years eleven through thirteen following closing, PAWC would bring SSA’s customers’ rates in line with the average system rates in equal increments. Per the APA, these increments would ultimately, be decided by the Commission. *Id.* at 5.

***Employment:*** The APA also obligates PAWC to offer employment to eligible SSA employees after closing of the transaction. Joint Application, Exh. J.

**III. Discussion**

**A. Legal Standards**

As the proponent of a rule or order in this proceeding, PAWC and SSA have the burden of proof to establish that they are entitled to the relief they are seeking. 66 Pa. C.S. § 332(a). The Joint Applicants must establish their case by a preponderance of the evidence. *Samuel J. Lansberry, Inc. v. Pa. PUC*, 578 A.2d 600 (Pa. Cmwlth. 1990), *alloc. denied,* 529 Pa. 654, 602 A.2d 863 (1992). That is, the Joint Applicants’ evidence must be more convincing, by even the smallest amount, than that presented by any opposing party. *Se-Ling Hosiery, Inc. v. Margulies*, 364 Pa. 45, 70 A.2d 854 (1950). Additionally, this Commission’s decision must be supported by substantial evidence in the record. More is required than a mere trace of evidence or a suspicion of the existence of a fact sought to be established. *Norfolk & Western Ry. Co. v. Pa. PUC,* 489 Pa. 109, 413 A.2d 1037 (1980).

In this case, the Joint Applicants are seeking approval of PAWC’s acquisition of substantially all of the assets of SSA’s wastewater collection and treatment system and approval of PAWC’s application to provide wastewater service in the areas served by SSA. Accordingly, the Joint Applicants have the burden of proving that they satisfy the requirements of the Public Utility Code (Code), particularly Sections 1102 and 1103 of the Code, 66 Pa. C.S. §§ 1102 and 1103. Section 1102(a) provides that the Commission must issue a Certificate of Public Convenience (Certificate) as a legal prerequisite to a public utility offering service or abandoning service and certain property transfers by public utilities. The Code provides the following, in pertinent part:

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:

\* \* \*

(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.

66 Pa. C.S. § 1102(a)(3).

The Commission will only grant a Certificate“if the Commission shall find or determine that the granting of such certificate is necessary or proper for the service, accommodation, convenience or safety of the public.” To ensure that a transaction is in the public interest, the Commission may impose conditions in granting a Certificate that it deems to be just and reasonable. 66 Pa. C.S. § 1103(a).

In order for the Commission to approve the proposed transaction under Sections 1102 and 1103 of the Code, the Joint Applicants must demonstrate that the proposed acquisition will “affirmatively promote the ‘service, accommodation, convenience, or safety of the public’ in some substantial way.” *City of York v. Pa. PUC*, 449 Pa. 136, 141, 295 A.2d 825, 828 (1972) (*City of York*). The Pennsylvania Supreme Court explained the *City of York* standard as follows:

[T]he appropriate legal framework requires a reviewing court to determine whether substantial evidence supports the Commission’s finding that a merger will affirmatively promote the service, accommodation, convenience, or safety of the public in some substantial way. In conducting the underlying inquiry, the Commission is not required to secure legally binding commitments or to quantify benefits where this may be impractical, burdensome, or impossible; rather, the PUC properly applies a preponderance of the evidence standard to make factually-based determinations (including predictive ones informed by expert judgment) concerning certification matters.

*Popowsky v. Pa. PUC*, 594 Pa. 583, 611, 937 A.2d 1040, 1057 (2007).

Additionally, pursuant to Section 1103 of the Code, the Joint Applicants must show that PAWC is technically, legally, and financially fit to own and operate the assets it will acquire from SSA. *Seaboard Tank Lines v. Pa. PUC*, 502 A. 2d 762, 764 (Pa. Cmwlth. 1985); *Warminster Twp. Mun. Auth. v. Pa. PUC*, 138 A.2d 240, 243 (Pa. Super. 1958). As a certificated public utility, there is a rebuttable presumption that PAWC possesses the requisite fitness. *South Hills Movers, Inc. v. Pa. PUC*, 601 A.2d 1308, 1310 (Pa. Cmwlth. 1992).

In reviewing the agreements filed by PAWC and SSA, Section 507 of the Code, 66 Pa. C.S. § 507, provides the applicable standards. Pursuant to Section 507, contracts or agreements between a public utility and a municipal corporation, except contracts to furnish service at regular tariff rates, must be filed with the Commission at least thirty days prior to the effective date of the contract or agreement. In determining whether to approve such agreements, the Commission will consider the reasonableness, legality, or any other matter affecting the validity of the agreement.

**B. Commission Jurisdiction over a Combined Wastewater System**

We note at the outset that the Parties and the ALJs use the terms “sewage” and “wastewater” interchangeably. This is due to a change in the industry standard terminology from the use of the term “sewage” to the use of the term “wastewater,” the current, standard term in the industry. The Code also contains both the terms “sewer” and “wastewater.” *See* Joint Applicants’ M.B. at 15; OCA’s M.B. at 12.

**1. Positions of the Parties**

**a. OCA**

The OCA averred that the Commission has jurisdiction over wastewater services under Section 102 of the Code, but does not have jurisdiction over stormwater services. The OCA stated that the Code does not address stormwater and that wastewater and stormwater are two distinct services. OCA M.B. at 9-10, 12; OCA St. 2 at 8-9. The OCA argued that this construction is consistent with the common and approved meaning of the term “wastewater” within the industry in which wastewater and stormwater are always referred to separately. OCA M.B. at 12; OCA St. 1 at 6-8 (citing *DEP Manual* at 43.4 and 25 Pa. Code § 102.1).

The OCA also relied on *Pa. PUC v. City of Lancaster-Sewer Fund*, Docket No. R-00049862 (Order entered August 26, 2005) (*Lancaster*) and *Pa. PUC v. City of Lancaster-Sewer Fund*, Docket No. R-00049862 (Order entered September 15, 2008) (*Lancaster Remand*) (collectively, *Lancaster Decisions*) to support its position that stormwater is distinct from and not included in the definition of “wastewater” in the Code and that the costs of providing stormwater service are distinct from the costs of providing wastewater service, even when one system is providing both services. OCA M.B. at 14‑15. The OCA stated that the Commission determined in the *Lancaster Decisions* that the costs of treatment of the City of Lancaster’s stormwater could not be recovered from jurisdictional customers’ rates. The OCA contended that, not only do Pennsylvania statutes, regulations, and cases distinguish stormwater from wastewater and sewage, but water and wastewater industry standards differentiate between stormwater and sewage in terms of how these services are defined, produced, collected, treated, and billed. OCA M.B. at 19-28.

**b. Joint Applicants**

The Joint Applicants averred that, pursuant to the Statutory Construction Act of 1972, 1 Pa. C.S. §§ 1501-1991 (Statutory Construction Act), the Commission has express authority under Section 102 of the Code over combined wastewater service. Joint Applicants’ M.B. at 13-14. The Joint Applicants explained that, under Section 102 of the Code, a “public utility” includes “[a]ny person or corporations now or hereafter ***owning or operating*** in this Commonwealth ***equipment or facilities*** ***for*** . . . (vii) ***[s]ewage collection, treatment, or disposal*** for the public for compensation.” 66 Pa. C.S. § 102. (emphasis added). The Joint Applicants concluded that there was no dispute in the record that the combined wastewater system in this case consists of equipment or facilities designed for sewage collection, treatment, and disposal. The Joint Applicants described SSA’s system as an integrated wastewater system designed and operated to collect and treat pollutants in wastewater. The Joint Applicants stated that the fact that the combined wastewater system collects and transports stormwater in addition to sewage does not change the character of the lines, mains, and other facilities used for public sewage collection, treatment, or disposal services. Joint Applicants’ M.B. at 16.

The Joint Applicants averred that, assuming there is an argument that there is some question about the Commission’s express jurisdiction over a combined system that collects and treats sewage and stormwater, the Commission has necessarily implied authority over combined wastewater service. The Joint Applicants contended that the Commission has jurisdiction over combined wastewater service under accepted wastewater engineering definitions and environmental regulations, which treat sewage and stormwater or other fluids flowing within the system as “wastewaters.” *Id*. at 20-24.

**2. ALJs’ Recommendation**

Initially, the ALJs noted that resolution of this issue would depend on whether the stormwater collected by SSA’s combined system is sewage or wastewater. The ALJs stated that if the stormwater is sewage or wastewater, then the combined system is providing public utility service because it is providing sewage collection, treatment, or disposal consistent with Section 102 of the Code, 66 Pa. C.S. § 102. The ALJs determined that the stormwater collected in SSA’s combined system is sewage and, therefore, the combined system is subject to the Commission’s jurisdiction. R.D. at 19.

In reaching this determination, the ALJs did not find the Commission’s decision in *Lancaster Remand* to be controlling or persuasive because, in that case, there were no combined sewers located in the area where the jurisdictional customers resided. R.D. at 19 (citing *Lancaster*). The ALJs observed that in *Lancaster*, the Commission found that the City of Lancaster was unfairly allocating stormwater costs to jurisdictional customers, but the Commission did not address its jurisdiction over a combined sewer system. R.D. at 19.

Stating that there were no controlling Commission decisions regarding jurisdiction over combined sewer systems, the ALJs examined the provisions of the Code to determine whether the Commission has jurisdiction over a combined system under Section 102 of the Code. *Id*. The ALJs noted that the Code uses the term “sewer” in Sections 102, 510, 529, 1327, and 1526 and “wastewater” in Sections 1311, 1351, 1358, and 1403. The ALJs also noted that “wastewater utility” is defined in Section 1403 of the Code, 66 Pa. C.S. § 1403, as “[a]n entity owning or operating equipment or facilities for the collection, treatment or disposal of sewage to or for the public for compensation.” The ALJs stated that the Code does not otherwise define either “sewer” or “wastewater” and does not define or include the term “stormwater.” R.D. at 19.

In the absence of definitions for “sewage,” “sewer,” and “wastewater” in the Code or in the Commission’s Regulations, the ALJs examined the history of the inclusion of an entity operating equipment or facilities for “sewage collection, treatment, or disposal for the public for compensation” within the definition of a “public utility” under Section 102 of the Code. The ALJs stated that the definition in Section 102 is exactly the same as the definition in the previous Act of May 28, 1937, P.L. 1053, creating the Commission at 66 P.S. § 1102(17)(g), and the prior Act also did not define the term “sewage.” R.D. at 20. The ALJs noted that the Act of May 28, 1937 abolished the Public Service Commission, which had been created by the Act of July 26, 1913, P.L. 1374 (Public Service Commission Law). The ALJs also noted that the former Act of July 26, 1913, defined a public service company as including “sewage corporations” but did not define the term “sewage” or “sewage corporations.” R.D. at 21.

The ALJs found that based on their review of the history of the use of “sewage collection, treatment, or disposal” within the definition of a public utility, it was evident that, from the creation of the Public Service Commission in 1913, entities operating equipment for collection, treatment, or disposal of sewage would have been considered public service companies and, later, public utilities. R.D. at 21 (citing *Wayne Title & Trust Co. v. Wayne Sewerage Co*., 3 Pa. P.S.C. 1170 (1919) (*Wayne*); *Wayne Sewerage Co. v. Fronefield*, 76 Pa. Super. 491 (1921) (*Fronefield*); *Dickson v. Drexel*, 285 Pa. 419, 132 A. 284 (1926) (*Dickson*) (the *Wayne Sewerage Cases*)). The ALJs explained that the *Wayne* decision concerned a rate case involving the Wayne Sewerage Company, and the *Fronefield* and *Dickson* cases pertained to free sewer service provided by the Wayne Sewerage Company prior to the company’s regulation by the Public Service Commission. The ALJs further explained that the *Fronefield* and *Dickson* decisions described the Wayne Sewerage Company’s predecessors in 1883 as having constructed the town of Wayne by laying out streets and lots and constructing a gravity drainage or sewage system by laying drains or pipes in the streets and, subsequently, constructing houses and connecting the houses to the drainage system. R.D. at 21. The ALJs concluded that based on this description of the service provided by the Wayne Sewerage Company, it appeared that the company’s system was initially constructed as a combined system and handled water from the streets and sewage from the houses. *Id*. at 21-22. The ALJs observed that when the Public Service Commission exercised regulatory authority over the Wayne Sewerage Company in *Wayne*, the Commission referred to the entire system as a sewage system and, therefore, interpreted the term “sewage” in its enabling statute to include water from the streets and sewage from the houses. The ALJs determined that from the time the Public Service Commission began regulating public service companies, it appears to have regulated combined sewage systems. *Id*. at 22. The ALJs reasoned that this conclusion was supported by the testimony of PAWC’s witness, who stated that combined systems like SSA’s had been used from the mid-1800s to the mid-1900s but are no longer designed or built. SSA’s combined system, parts of which were constructed in the 1970s, continues to operate as a legacy system. *Id*. at 22 (citing Tr. at 145).

The ALJs continued that since the Public Service Commission began regulating combined sewage systems, the term “sewage” had been used in the definitions in the Act of July 26, 1913, the Act of May 28, 1937, and the current Code. The ALJs noted that the General Assembly has not substituted the term “wastewater” for the term “sewage” at 66 Pa. C.S. § 102, and the General Assembly has not defined the term “sewage” at 66 Pa. C.S. § 102, let alone defined it in a manner that excludes stormwater. The ALJs determined that in the absence of a definition in the Code for “sewage,” the General Assembly intended that the definition of “sewage” continue to have the same meaning it had in the Act of July 26, 1913. R.D. at 22. The ALJs reasoned that because the General Assembly did not alter the definition of sewage in Section 102 of the Code based on the decisions in *Wayne*, *Fronefield*, and *Dickson*, the General Assembly intended to continue regulation of combined systems as sewage systems. Accordingly, the ALJs held that SSA’s combined system is a sewage system as defined by Section 102 of the Code and is subject to Commission regulation. R.D. at 23.

**3. Exceptions and Replies**

**a. OCA’s Exceptions**

The OCA avers that the ALJ erred by finding that the Commission has jurisdiction over stormwater service. First, the OCA states that the cases regarding the Wayne system that the ALJs cited to are not dispositive. OCA Exc. at 4. The OCA argues that these cases do not conclusively show that the Wayne system was a combined system, because there may have been a sanitary sewer system and a storm water drainage system. *Id*. at 5. The OCA observes that the fact that the sewage system pipes were placed in the streets and the homes were subsequently connected to the pipes does not mean that the sewage system handled water from the streets. *Id*. (citing *Fronefield* at 494). The OCA contends that even if the system was initially constructed as a combined system, there is no indication that the system was a combined system when the Public Service Commission was created in 1913, a span covering thirty years and two owners. OCA Exc. at 5 (citing *Dickson*, 285 Pa. at 422, 132 A. at 284). According to the OCA, it is clear that only the rates for the sanitary sewer system were at issue in the Wayne cases, and there was no mention of downspout connections or lot size, roof area, or paved area that are used to set stormwater rates. OCA Exc. at 5-6 (citing *Wayne* at 1174).

Second, the OCA states that guidance on this issue can be found in other statutes promulgated by the General Assembly that address stormwater and sewer service. The OCA avers that in instances where the General Assembly has intended to include stormwater in the types of service an entity can provide, it has amended a statute to add “stormwater” when the existing statute authorized the provision of “sewer” service. OCA Exc. at 6. The OCA points to the General Assembly’s 2013 amendment of the Municipality Authorities Act to allow municipalities to operate “storm water planning management, and implementation” projects. *Id*. at 6-7 (citing 53 Pa. C.S. § 5607(a)(18)). The OCA explains that the statute already provided for municipal authorities to finance, construct, and maintain projects relating to “sewers, sewer systems or parts thereof” and “sewage treatment works.” OCA Exc. at 7 (citing 53 Pa. C.S. § 5607(a)(5) and (6)). The OCA argues that if “stormwater” were commonly understood to be included in the term “wastewater,” then adding a provision for stormwater would be redundant, and would be contrary to the rules of legislative interpretation which presume that the legislature does not intend for any provisions of a statute to be “mere surplusage.” OCA Exc. at 7 (citing *Holland v. Marcy*, 584 Pa. 195, 206 (2005)). The OCA also points to the Pennsylvania Storm Water Management Act, which defines “public utility service” to include “sewage collection, treatment or disposal” and stormwater as “drainage runoff from the surface of the land resulting from precipitation or snow or ice melt.” OCA Exc. at 7 (citing 32 P.S. § 680.4). The OCA further points to the Pennsylvania Sewage Facilities Act, which defines “sewage” in a manner that the OCA contends excludes storm water. OCA Exc. at 7 (citing 35 P.S. § 750.2).[[4]](#footnote-4)

Third, the OCA avers that the *Lancaster Remand* and *Lancaster* cases are on point. The OCA states the ALJs ignore that the City of Lancaster is the only combined stormwater/wastewater system over which the Commission exercises jurisdiction. The OCA argues that the decisions in the *Lancaster Remand* and *Lancaster* Cases depend on two findings that apply to the instant case: (1) the costs of providing stormwater service are distinct from the costs of providing wastewater service, even when one system is providing both services; and (2) the Commission-regulated customers should not pay the costs associated with stormwater service as they do not contribute to the stormwater costs. OCA Exc. at 8.

**b. Joint Applicants’ Replies to OCA’s Exceptions**

In response, the Joint Applicants aver that the ALJs properly concluded that the Commission has jurisdiction over combined wastewater service under Section 102 of the Code. First, the Joint Applicants state that the *Wayne Sewerage Cases* support a conclusion that the Commission has jurisdiction over combined system service. Joint Applicants’ R. Exc. at 2. The Joint Applicants argue that the only reasonable interpretation of the *Wayne Sewerage Cases* is that the Commission has historically exercised jurisdiction over combined systems, because the developer in those cases established a drainage system for the development and allowed abutting property owners to connect and discharge their sewage into that system. The Joint Applicants contend that the OCA ignores the fact that most community sewer systems in Pennsylvania since the 1800s and until relatively recently accepted combined stormwater and sanitary sewage, and there is substantial evidence in the record here to support such a finding. *Id*. at 3. According to the Joint Applicants, the ALJs’ rationale is consistent with court decisions that interpret the phrase “sewer system,” which was used in the *Wayne Sewerage Cases*, to include storm drains. *Id*. at 4 (citing *Medicus v. Upper Merion Twp*., 475 A.2d 918 (Pa. Cmwlth. 1984)).

Second, the Joint Applicants state that the Commission need not rely solely on the rationale in the Recommended Decision to support jurisdiction over combined wastewater service, as the rules of statutory interpretation support a conclusion that the Commission has jurisdiction over combined wastewater service. The Joint Applicants assert that the record is undisputed that the combined wastewater system at issue in this case collects and treats sewage, regardless of whether stormwater also enters that system. *Id*. at 4-5. The Joint Applicants explain that Section 1921(a) of the Statutory Construction Act, 1 Pa. C.S. § 1921(a), provides that the object of statutory interpretation is to determine the General Assembly’s intent based on the express words used in the statute. Joint Applicants’ R. Exc. at 5. The Joint Applicants also explain that when a statute’s words may not be viewed as explicit, courts and agencies may consider, among other things, the occasion and necessity for the statute, the object to be obtained, and the consequences of a particular interpretation and administrative interpretations. *Id*. (citing 1 Pa. C.S. § 1921(c)). Except for statutes subject to strict construction rules, which the Joint Applicants state is not the case here, all statutory provisions “shall be liberally construed to effect their objects and promote justice.” Joint Applicants’ R. Exc. at 5 (citing 1 Pa. C.S. § 1928(c)).

The Joint Applicants observe that the rules of statutory interpretation compel the conclusion that the Commission has jurisdiction over combined wastewater systems based on the express language of the Code, because the Commission has jurisdiction over public utilities and their facilities that collect and treat sewage under Section 102 of the Code. Joint Applicants’ R. Exc. at 4, 5. The Joint Applicants state that the terms “sewage” and “wastewater” used in the Code and the Commission’s Regulations are synonymous. *Id*. at 5. The Joint Applicants aver that, based on the accepted regulatory definitions of “sewage” and “wastewater,” any water, including stormwater, when mixed with sewage and other wastewater, becomes wastewater. *Id*. at 5-6. According to the Joint Applicants, in the wastewater engineering field, once flows from various sources are commingled, it is not possible to differentiate between the wastewaters flowing through sewerage facilities that need to be managed, treated, and discharged responsibly. *Id*. at 6. When water becomes contaminated, it becomes wastewater, which must be collected, treated, and managed responsibly by the operator of the wastewater system. *Id*. (citing PAWC St. 6-R at 6). The Joint Applicants argue that when human and animal wastes are mixed with other waters, including stormwater, the resulting flows are all “sewage” under the definitions in the Pennsylvania Clean Streams Law, 35 P.S. § 691.1, and Sewage Facilities Act, 35 P.S. § 750.2. Joint Applicants’ R. Exc. (citing PAWC St. 6-R at 5).

The Joint Applicants also argue that because the Code does not exclude combined wastewater service from the Commission’s jurisdiction, then the Commission has a duty to regulate combined systems under Section 501(a) of the Code, 66 Pa. C.S. § 501(a). Joint Applicants’ R. Exc. at 6. The Joint Applicants contend that when the General Assembly enacted Act 11 of 2012, 66 Pa. C.S. §§ 1350-1360, it could have excluded combined wastewater systems from Act 11 or from the Commission’s jurisdiction altogether, but it did not exclude combined systems from the term “sewage” under Section 102 or the more contemporary term “wastewater” in Act 11. The Joint Applicants believe that neither the Commission nor the Courts may read into a statute an express exclusion to the Commission’s jurisdiction that was not added by the legislature. Joint Applicants’ R. Exc. at 7.

Third, the Joint Applicants state that the Commission should reject the OCA’s argument that is based on other statutes. *Id*. at 8. The Joint Applicants argue that the OCA’s reliance on recent amendments to the Municipality Authorities Act is misplaced, as municipal authorities have had the authority to operate “sewer, sewer systems, or parts thereof” and “sewage treatment works” for a significant period of time. *Id*. (citing 53 Pa. C.S. § 5607(a)(5) and (6)). The Joint Applicants observe that the 2013 amendment to the Municipality Authorities Act, Act of July 9, 2013, P.L. 569, No. 2013-68, added clause (18) to 53 Pa. C.S. § 5607(a), empowering municipal authorities to undertake projects involving “stormwater planning, management, and implementation.” Joint Applicants’ R. Exc. at 8-9. According to the Joint Applicants, if, as the OCA argues, combined wastewater systems involve some aspect of stormwater systems and stormwater is not part of sewage, then the municipal authorities would not have been authorized to operate combined systems before 2013. Such an interpretation, the Joint Applicants contend, contradicts the reality that numerous municipal authorities, including the SSA, have long owned and operated combined wastewater systems under the Municipality Authorities Act. The Joint Applicants aver that the 2013 amendment clarified the power of municipal authorities to undertake pure stormwater projects and activities. *Id*. at 9. The Joint Applicants assert that any stormwater combined with sanitary sewage is wastewater based on accepted regulatory and industry definitions of “sewage” and “wastewater.” The Joint Applicants point out that the OCA is incorrect in its contention that stormwater is excluded from “sewage” based on the definition in the Sewage Facilities Act, because the definition in that Act is very broad. The Joint Applicants conclude that under the definition in the Sewage Facilities Act, when human and animal wastes are mixed with any other flow, whether it is from industrial users, groundwater, or stormwater, all of the resulting flows are considered “sewage.” Joint Applicants’ R. Exc. at 10; PAWC St. 6-R at 5.

Fourth, the Joint Applicants argue that the *Lancaster* *Decisions* are not controlling or persuasive on the issue of Commission jurisdiction over combined wastewater service. *Id*. The Joint Applicants state that the *Lancaster* *Decisions* concerned the Commission’s exercise of discretion to allocate costs in a ratemaking proceeding between jurisdictional customers who were outside of the City and did not benefit from the combined wastewater service in the City and non-jurisdictional customers within the City who benefitted from the combined wastewater service. *Id*. at 11. The Joint Applicants aver that the decisions did not address whether the Commission has jurisdiction over combined wastewater service. *Id*.; Joint Applicants’ M.B. at 32-33, R.B. at 36.

Fifth, the Joint Applicants believe that the OCA’s position on Commission jurisdiction over combined system service is contrary to the public interest. The Joint Applicants state that there are approximately 129 combined wastewater systems in Pennsylvania, many of which serve relatively small communities that are typically older and have more limited financial capabilities. Joint Applicants’ R. Exc. at 11 (citing PAWC St. 6-R at 18; PAWC Exh. JCE-3). The Joint Applicants also state that at least eleven municipalities enrolled in Act 47, known as the Municipalities Financial Recovery Act, 53 P.S. §§ 11701.101, *et seq*., are combined wastewater system communities, a number of which have limited technical and financial capabilities that present challenges in terms of addressing federal and state mandates for managing their combined sewer systems and reducing overflows. The Joint Applicants aver that these communities would benefit from the modernization of their wastewater system assets and professional operation of their systems. The Joint Applicants contend that OCA’s position on Commission jurisdiction would deprive Pennsylvania communities of the chance to pursue acquisitions of their combined wastewater systems by capable public utilities and would thwart policy efforts to regionalize wastewater services under Act 11. Joint Applicants’ R. Exc. at 12.

**4.** **Disposition**

When interpreting a statute underthe Statutory Construction Act, “[t]he object of all interpretation and construction of statutes is to ascertain and effectuate the intention of the General Assembly.” 1 Pa. C.S. § 1921(a). The clearest indication of legislative intent is generally the plain language of a statute. *Walker v. Eleby*, 577 Pa 104, 123, 842 A.2d 389, 400 (2004). “When the words of a statute are clear and free from all ambiguity, the letter of it is not to be disregarded under the pretext of pursuing its spirit.” 1 Pa. C.S. § 1921(b). When the words of a statute are not explicit, we may consider other matters in ascertaining legislative intent, including, among other things, the occasion and necessity for the statute, the circumstances under which it was enacted, the object to be attained, the former law, including other statutes on the same or similar subjects, and legislative and administrative interpretations of the statute. 1 Pa. C.S. § 1921(c). A statute is considered “ambiguous or unclear if its language is subject to two or more reasonable interpretations.” *Bethenergy Mines, Inc. v. Dep’t of Envtl. Prot*., 676 A. 2d 711, 715 (Pa. Cmwlth. 1996).

When the language of a statute is not explicit, a reviewing court must give deference to the interpretation of the legislative intent of a statute made by an administrative agency. The Supreme Court has adopted a “strong deference” standard for reviewing agency interpretations of statutes the agencies are charged to enforce. Under the “strong deference” standard, if a reviewing court determines that the precise question at issue has not been addressed by the legislature, the court will not impose its own construction on the statute, but will review the agency’s construction of the statute to determine whether that construction is permissible. *Pennsylvania Electric Co. v. Pa. PUC*, 648 A.2d 63, 78 (Pa. Cmwlth. 1994).

In this case, neither the language of Section 102 of the Code nor the language of any other Section of the Code explicitly address the Commission’s jurisdiction over a combined sewage system like the combined system operated by SSA. The ALJs engaged in a detailed and well-reasoned analysis in ascertaining the legislative intent and ultimately determining that SSA’s combined system is a sewage system under Section 102 of the Code and, therefore, that the Commission has jurisdiction over the service provided by SSA and the instant Application. As the ALJs noted, the *Wayne Sewage Cases* support the conclusion that entities operating combined sewage systems were considered public service companies and, later, public utilities. When read together, the *Wayne Sewage Cases* indicate that the Wayne Sewerage Company’s predecessors constructed the town of Wayne by laying out streets and lots and constructing a gravity drainage or sewage system by laying drains or pipes in the street. Thereafter, the predecessors constructed houses and connected the houses to the drainage system. The sewage was collected in a receiving reservoir and pumped into another reservoir on top of a hill, from which it filtered down through prepared cinder beds for the purpose of purifying it before the effluent was discharged into a creek. In 1905 after the Wayne Sewerage Company purchased the sewer system, the commissioner of health of Pennsylvania directed the Company to discontinue this discharge into the creek. As a result, the Wayne Sewerage Company constructed a sanitary system of sewage disposal by which the sewage was conveyed into tanks and filters and treated before it was discharged.

From a technical perspective, the Wayne Sewerage Company’s system represented a combined sewage system, which is currently defined as a single pipe system that collects and conveys both sewage and stormwater runoffs into a wastewater treatment plant. *See* OCA St. 1 at 5. As the ALJs noted, this factual conclusion is supported by the evidence in the record that most community sewer systems in Pennsylvania since the 1880s and until the mid-1900s were built as combined stormwater and sanitary sewage systems, similar to the system in the *Wayne Sewerage Cases*. Tr. at 145.

The *Wayne Sewerage Cases* reflect holdings that the Wayne Sewerage Company’s sewage system furnished public service and was considered a “public service company” under the Public Service Commission Law of July 26, 1913, and therefore, the rates paid by the Company’s customers were also governed by the Public Service Commission Law. *Dickson*, 285 Pa. at 424, 132 A. at 285; *Fronefield*, 76 Pa. Super. at 499; *Wayne*. The definition of a “public service company” in the Public Service Commission Law of July 26, 1913, included “sewage corporations doing business within this State.” The definition was altered by the Act of May 28, 1937, to read the same as the current definition in Section 102 of the Code, which defines a public utility as including the provision of “sewage collection, treatment, or disposal for the public for compensation.” Given that the term “sewage” was included in the definitions in the Act of July 26, 1913, the Act of May 28, 1937, and the current Code and was not altered by the General Assembly based on the decisions in *Wayne Sewerage Cases* or otherwise, we concur with the ALJs’ decision that the General Assembly intended to continue regulation of combined sewage systems.

Additionally, this Commission has provided some more recent interpretations of the meaning of the term “sewage.” In a *Final Rulemaking Order*, adopted on September 12, 1997, at Docket No. L-00950112, we stated that, in an effort to amend or delete obsolete requirements in our Regulations, we were making amendments to certain sections regarding sewer utilities and the provision of sewer service. We indicated that the words “sewer” and “sewerage” would be changed to “wastewater” as in wastewater service or wastewater facility in order to reflect current industry standard terminology. While this did not alter our jurisdictional responsibilities, it indicated an intent to use the word “wastewater” instead of “sewer.” While neither the Code nor our Regulations provide a definition of “wastewater,” our Model Tariff and PAWC’s Commission-approved tariff contain the following definition for “wastewater”: “the liquid and water-carried wastes from dwellings, commercial facilities, industrial facilities and institutions, together with any groundwater, surface water, and stormwater that may be present, whether treated or untreated, in the Company’s sewer system.” Supplement No. 2 to Tariff - Wastewater Pa. P.U.C. No. 15, 1st Revised Page No. 6C. This broad definition, which includes stormwater, provides further support for our jurisdiction over combined sewage systems. In this case, SSA’s integrated wastewater system, which includes facilities used and useful in the provision of sewage collection, treatment, and disposal, falls within our jurisdiction under Section 102 of the Code. We agree with the Joint Applicants that the fact that the combined wastewater system collects and transports stormwater, in addition to sewage, does not change the character of the lines, mains, and other facilities used for public sewage collection, treatment, or disposal.

Moreover, we agree with the ALJ that the *Lancaster Decisions* are not controlling or persuasive in deciding the issue of our jurisdiction over combined sewage systems. The City of Lancaster operated a wastewater collection system that served some customers located outside of its boundaries, and the wastewater service provided to those extraterritorial customers was subject to Commission jurisdiction. One of the main issues addressed in the *Lancaster Decisions* was whether the costs of treatment for the City’s stormwater should be passed onto the jurisdictional customers. The Commission determined that the costs associated with collecting, conveying, pumping, and treating the stormwater runoff were not properly recoverable from jurisdictional customers as those customers were not benefitting from the stormwater service. *Lancaster* at 17-18. The Commission did not address jurisdiction over a combined sewage system in those cases, because there were no combined sewers located in the areas where the jurisdictional customers resided. *Id*. at 13. The OCA relies on the *Lancaster Decisions* for its arguments that the costs of providing stormwater service are distinct from the costs of providing wastewater service, and Commission-regulated customers should not pay the costs associated with stormwater service as they do not contribute to the stormwater costs. *See* OCA Exc. at 8. Because this proceeding is an acquisition proceeding and not a rate proceeding like the *Lancaster* proceeding, allocation of stormwater costs are not properly before us at this time. Any such allocation issues are more properly addressed in a future rate proceeding. For all of these reasons, we shall adopt the ALJs’ recommendation regarding our jurisdiction in this matter and deny the OCA’s Exceptions on this issue.

**C. Reasonableness and Public Interest of the Acquisition**

**1. Positions of the Parties**

**a. Joint Applicants**

The Joint Applicants averred that PAWC is fit to acquire the combined wastewater system and begin rendering service, and that the acquisition will provide a substantial benefit to the public. According to the Joint Applicants, PAWC possesses the financial, technical, and legal fitness to own and operate the combined wastewater system, and no party challenged PAWC’s fitness in this regard. Joint Applicants’ M.B. at 38-39.

With regard to financial fitness, the Joint Applicants asserted that PAWC is the Commonwealth’s largest water and wastewater provider, with total assets of $3.9 billion and annual revenues of $613 million for 2015, including operating income of approximately $307 million and net income of approximately $143 million. Joint Applicants’ M.B. at 39-40. The Joint Applicants further asserted that PAWC: (1) has access to a $220 million line of credit through American Water Capital Corp., a wholly-owned subsidiary of American Water Works Company, which can be increased if needed; (2) has high credit ratings with both Moody’s Investor Services and Standard and Poor’s Rating Services; (3) obtains long-term debt through American Water Capital Corp. at favorable interest rates and payment terms; and (4) utilizes low-cost long-term financing through the Pennsylvania Infrastructure Investment Authority and the Pennsylvania Economic Development Financing Authority. Joint Applicants’ M.B. at 40 (citing PAWC St. 5 at 3).

With regard to technical fitness, the Joint Applicants asserted that PAWC has the experience and technical expertise to operate the combined wastewater system and implement the improvements required by the Consent Decree. Joint Applicants’ M.B. at 41-42 (citing PAWC St. 2 at 3-17; PAWC Exh. DRK-1). The Joint Applicants also pointed to PAWC’s technical expertise in operating other wastewater systems. Joint Applicants’ M.B. at 42-43 (citing PAWC St. 3 at 1, 4-7). The Joint Applicants concluded as follows:

PAWC has capable staff, facilities, and operational skills to operate the Combined Wastewater System feasibly and profitably and for the benefit of the public, including the technical capabilities to comply with the requirements of the Consent Decree and related improvements and operations, including an established track record with extensive experience delivering large, complex water and wastewater capital improvement projects, such as the [Long Term Control Plan] projects associated with [SSA’s] Combined Wastewater System.

Joint Applicants’ M.B. at 43.

With regard to legal fitness, the Joint Applicants asserted that “PAWC has a good compliance history with respect to the Code and the Commission’s rules, orders, and regulations.” Joint Applicants’ M.B. at 44 (citing PAWC St. 1 at 9). According to the Joint Applicants, there are no pending legal proceedings that would suggest that PAWC is legally unfit to provide service to SSA’s customers once the transaction is approved. Joint Applicants’ M.B. at 44 (citing PAWC St. 1 at 9).

In addition to its assertions regarding PAWC’s fitness, the Joint Applicants averred that PAWC’s ownership and operation of the combined wastewater system in SSA service territory would produce an affirmative public benefit of a substantial nature. Joint Applicants M.B. at 44. The Joint Applicants identified the following specific benefits that they alleged will be realized if PAWC is permitted to acquire and operate the combined wastewater system:

* Scranton-area customers will benefit from PAWC’s enhanced customer services relating to billing, education, and customer assistance programs. Joint Applicants’ M.B. at 45-46 (citing PAWC St. 3 at 25-27).
* PAWC has better and more varied access to capital than SSA and is well-suited to provide wastewater service in the face of substantial environmental obligations arising from the implementation of the Consent Decree, in addition to raising capital for normal operation and maintenance of the combined wastewater system. Joint Applicants’ M.B. at 46-49 (citing PAWC St. 3 at 3; PAWC St. 5 at 1-4; PAWC St. 5-R at 3-8; PAWC St. 6-R at 25-26; SSA St. 1 at 4; PAWC Exh. JSM-1; PAWC Exh. JCE-5; OCA Exh. 1; Tr. at 98, 125-26, 129-31, 200).
* Scranton-area customers will benefit from being part of a larger customer base, which will allow PAWC to leverage economies of scale, improve efficiencies, lower costs to operate the combined wastewater system, and spread costs of capital improvements across PAWC’s combined water and wastewater customer base. Joint Applicants’ M.B. at 50 (citing PAWC St. 3 at 3; PAWC St. 4 at 5-8).
* PAWC’s commitment to create 100 new jobs in the Scranton area will promote economic development. Joint Applicants’ M.B. at 50-52 (citing PAWC St. 3 at 20; PAWC St. 3-R at 2-4; PAWC St. 4-R at 14; Tr. at 117‑18).
* Proceeds from the acquisition will help ameliorate the City’s financial situation, which has been a major factor limiting economic and other development in the Scranton region for decades. Joint Applicants’ M.B. at 52-58 (citing SSA St. 2 at 2-3, 5-7; SSA St. 2-R at 5, 7; SSA St. 3-R at 4, 6‑8, 10; PAWC Exh. JCE-R at 8-13).

**b. I&E**

I&E disagreed with the Joint Applicants’ assertion that the acquisition will serve the public interest in accordance with the criteria established in Sections 1102 and 1103 of the Code. I&E M.B. at 4. I&E contended that although the Joint Applicants posited a number of benefits to SSA’s current customers and the City, they failed to identify any substantial benefit to PAWC’s existing customers. According to I&E, the benefits to SSA’s customers and the City are not relevant because SSA and the City are not properly included in the public interest consideration. I&E R.B. at 2-3. I&E asserted that the Commission, when considering a prior case involving an application filed by CMV Sewerage Company, Inc. (CMV), denied CMV’s request to transfer its wastewater assets to the North Codorus Township Sewer Authority (NCTSA), based, in part, on the fact that the public interest included only the regulated utility and its customers. I&E M.B. at 4-5 (citing *Application of CMV Sewage Company, Inc. for Approval to Transfer to North Codorus Township Sewer Authority all Assets Used and Useful in the Provision of Sewage Collection Service in North Codorus Township, York County, Pennsylvania; and Application of CMV Sewage Company, Inc. for Approval to Abandon its Provision of Sewage Service to the Public in North Codorus Township, York County, Pennsylvania,* Docket No. A-230056F2002 (Order entered December 23, 2008) *(CMV)* at 29). I&E argued that, as in *CMV*, the Commission has no explicit or implicit authority over SSA’s rates or the City’s financial issues. I&E M.B. at 5-7.

I&E also contended that the alleged economies of scale cited by the Joint Applicants are not enough to overcome the harm that will befall PAWC’s current customers if costs relating to storm water and the variance adjustment are permitted to be recovered from these customers. I&E R.B. at 3-4. I&E argued that any potential reduction in costs that PAWC’s existing customers may experience is undetermined, and may not occur for a long time, considering that “the Joint Applicants appear to recommend that the Commission disregard the rate impact for the foreseeable future.” *Id*. at 4. I&E asserted that the Commission must consider the rate impact of the acquisition on PAWC’s existing customers in the short term, and not just in the long term, as the Joint Applicants have argued. *Id*. at 5.

**c. OCA**

The OCA also questioned the Joint Applicants’ alleged benefits of the proposed acquisition. The OCA asserted that in considering whether the acquisition meets the affirmative public benefit test established by the Pennsylvania Supreme Court in *City of York*, the benefits and detriments of the transaction must be measured with respect to the impact on all affected parties, and not just on one particular group or geographic subdivision. OCA M.B. at 30 (citing *Middletown Twp. v. Pa. P.U.C.,* 482 A.2d 674 (Pa. Cmwlth. 1984) *(Middletown))*. Thus, the OCA contended that the Commission must evaluate the benefits that will accrue to the existing PAWC wastewater customers, the existing PAWC water customers, and the existing SSA customers who will be transferred to PAWC. According to the OCA, such an evaluation reveals that there is no support for concluding that existing PAWC wastewater and water customers will benefit or that the SSA customers will benefit after year ten following the transaction. OCA M.B. at 31.

The OCA asserted that an acquisition provides an affirmative benefit if the benefits of the transaction outweigh the adverse impacts of that transaction. OCA M.B. at 31 (citing *CMV*). The OCA contended that the “hypothetical benefits” claimed by the Joint Applicants “do not outweigh the certain, short-term adverse impacts on PAWC’s existing customers.” OCA M.B. at 32. Specifically, the OCA argued that PAWC’s customer base will not expand as the Joint Applicants aver, because essentially all of SSA’s 31,000 customers are already PAWC water customers. In addition, the OCA claimed that as a result of the acquisition, PAWC’s existing wastewater and water customers will (1) pay nearly $200 million of the costs of capital improvements to the SSA system under the Consent Decree; (2) pay the subsidy for keeping SSA rates lower than cost for the first ten years post-acquisition as a result of the 1.9% CAGR limitation; and (3) pay the subsidy related to not charging the DSIC rate for the first few years after the acquisition. *Id*. at 32-33.

The OCA further contended that if PAWC is required to charge cost-based rates to the SSA customers over the first ten years, then PAWC would be required to pay an enhanced purchase price as a result of the variance adjustment included in the APA. According to the OCA, this would result in the addition of $104 million to the $195 million purchase price, which the OCA contends is already more than twice the book value of SSA’s assets. The OCA asserts that this additional $104 million would then be recovered from PAWC’s existing customers. On the other hand, the OCA argues that if PAWC limits SSA rates to the level of 1.9% CAGR, the resulting revenue shortfall from SSA customers will be $104 million, which PAWC intends to recover from its existing water and wastewater customers, even though these customers would receive no benefit from the acquisition. OCA M.B. at 33-35 (citing OCA St. No. 2 at 24-27).

The OCA also objected to PAWC’s intention to seek Commission approval to spread the costs of improving SSA’s system to its existing water customers under Act 11,[[5]](#footnote-5) in accordance with the APA. The OCA argued that these existing water customers already pay for their own wastewater disposal and must pay taxes or other fees to control stormwater in their respective communities. According to the OCA, it is unfair and contrary to cost-based ratemaking to require PAWC’s existing customers to provide additional subsidies each year to help pay for wastewater disposal and stormwater control in Scranton and Dunmore. OCA M.B. at 35 (citing OCA St. 2 at 33-35; PAWC St. 4 at 4; PAWC Exh. BCG-1, Att. F, Section 7.09(x)).

Finally, the OCA criticized the Joint Applicants’ argument that the acquisition will benefit the City. Like I&E, the OCA contended that the benefit to the City is not determinative of the public interest, and that the Joint Applicants’ argument in this regard improperly ignores the impact of the proposed acquisition on the other parties affected by the transaction. OCA M.B. at 36 (citing *Middletown*; SSA St. 2-R at 3; Tr. at 94-96). According to the OCA, the Joint Applicants’ assertion that PAWC is better able to operate the SSA system and serve SSA customers is speculative and disregards the adverse impacts of the acquisition on the existing PAWC and SSA customers. OCA M.B. at 36-41.

**2. ALJs’ Recommendation**

In their Recommended Decision, the ALJs concluded that the record evidence in this proceeding supports a finding that PAWC possesses the necessary technical, financial and legal fitness to own and operate the assets it seeks to acquire from SSA, and to provide the proposed service to SSA’s customers. R.D. at 25-27. However, as discussed herein, the ALJs concluded that the variance adjustment set forth in the APA is not reasonable or in the public interest and violates the Code. According to the ALJs, the alleged benefits of the acquisition to PAWC’s customers, SSA’s customers, or the City, cannot overcome this defect. Accordingly, the ALJs recommended that the Commission deny the Joint Application. *Id*. at 42.

**3. Exceptions and Replies**

**a. Joint Applicants’ Exceptions**

In their Exceptions, the Joint Applicants assert that in addressing the variance adjustment, the ALJs failed to consider the substantial public benefits of the acquisition effectuated by the APA. According to the Joint Applicants, the acquisition will result in at least six affirmative public benefits of a substantial nature. Joint Applicants’ Exc. at 18.

First, the Joint Applicants contend that the acquisition will benefit Scranton-area customers by giving them access to the following enhanced services over those currently offered by SSA:

* Extended call center hours for customers;
* Additional bill payment options for customers;
* Enhanced customer information and education programs; and
* Access to PAWC’s customer assistance program.

Joint Applicants’ Exc. at 18-19 (citing PAWC St. 3 at 25; Joint Applicants’ M.B. at 45‑46).

Second, the Joint Applicants argue that PAWC is better positioned than SSA to address the numerous costs and obligations associated with improvements to, and operation of, SSA’s system. In support of this assertion, the Joint Applicants cite PAWC’s strong balance sheet, access to equity markets, $220 million line of credit and superior credit rating; the highly-leveraged position of SSA; and the effect of service affordability for Scranton-area customers on SSA’s access to capital through credit or otherwise. Joint Applicants’ Exc. at 19 (citing PAWC St. 5-R at 4-8; Joint Applicants’ M.B. at 46-49).

Third, the Joint Applicants aver that Scranton-area customers will benefit by being part of a larger customer base, pointing out that PAWC is the largest investor-owned water and wastewater provider in the Commonwealth. Joint Applicants’ Exc. at 19 (citing PAWC St. 3 at 3). The Joint Applicants argue that, due to its size and expertise in wastewater management and the leveraging of economies of scale, PAWC will be able to improve efficiencies and lower costs to operate the SSA system. According to the Joint Applicants, these efficiencies, along with a combined water and wastewater revenue requirement under Act 11, will act to keep rates lower for affected customers than they would be if such customers were not allowed to become part of PAWC’s customer base. Joint Applicants’ Exc. at 19-20 (citing PAWC St. 4 at 5-6; Joint Applicants’ M.B. at 50).

Fourth, the Joint Applicants assert that the acquisition will provide a substantial public benefit because PAWC has committed to create 100 new jobs in the Scranton area by the end of 2020, in addition to the SSA employees that will be utilized by PAWC after completion of the acquisition transaction. According to the Joint Applicants, PAWC anticipates that these employees will service PAWC or its parent organization to accommodate future growth. The Joint Applicants state that the costs of the new jobs will be subject to standard review for reasonableness in a subsequent rate case. Joint Applicants’ Exc. at 20 (citing PAWC St. 3 at 20; PAWC St. 3-R at 2-4; PAWC St. 4-R at 14; Tr. at 118; Joint Applicants’ M.B. at 50-52).

Fifth, the Joint Applicants contend that the acquisition will provide PAWC with SSA’s large treatment plant and the unique and specialized expertise of SSA’s skilled personnel, who are familiar with the business of treating wastewater processed at the end of a large combined system. The Joint Applicants argue that this will benefit the customers of both SSA and PAWC. Joint Applicants’ Exc. at 20 (citing SSA St. 2-R at 7, 8). In addition, the Joint Applicants state that PAWC’s experience with SSA’s treatment plant will help it in the operation of its other smaller plants. Joint Applicants’ Exc. at 20.

Finally, the Joint Applicants assert that approval of the acquisition is of critical importance to the City and its taxpayers, who are also SSA ratepayers. The Joint Applicants note that the City is a financially distressed municipality, subject to state supervision under Act 47. According to the Joint Applicants, the acquisition “is the cornerstone of the City’s economic recovery plan.” Joint Applicants’ Exc. at 21 (citing SSA St. 2 at 2-3). As the Joint Applicants further explain:

The monetization of SSA assets is necessary to put the City on the path of reducing the otherwise projected operating budget deficits through 2020. [SSA St. 2], 5:10-13; SSA St. 3-R, 10:6-14. The City’s realization of its portion of the anticipated Transaction proceeds will provide immediate relief for its 2017 budget and establish a platform for possible departure from the strictures of Act 47 for the first time in over two decades. Joint Applicants’ Main Brief, pp. 52-58; Joint Applicants’ Reply Brief, pp. 43-48.

Joint Applicants’ Exc. at 21. The Joint Applicants urge the Commission to recognize the General Assembly’s determination, as set forth in Act 47, that “addressing the financial problems of distressed municipalities is essential to protecting the health, safety and welfare of not only the citizens of the directly impacted communities, but the citizens of the Commonwealth as a whole.” Joint Applicants’ Exc. at 21 (citing 53 P.S. § 11701.102(a)).

**b. I&E’s Replies to Joint Applicants’ Exceptions**

In its Replies to the Joint Applicants’ Exceptions, I&E contends that the benefits enumerated by the Joint Applicants only apply to SSA, its customers, and the City, and that those entities are not properly included in the public interest consideration. I&E R. Exc. at 18-19 (citing I&E M.B. at 4-7; I&E R.B. at 2-5). I&E argues that historically, the public interest has been defined to include ratepayers, shareholders, and the regulated community, and that attempts to broaden this definition to include municipal authorities and their ratepayers have been rejected, especially when benefits to such entities would potentially harm the regulated utility or its customers. I&E R. Exc. at 19-20 (citing *Pa. PUC v. Bell Atlantic-Pennsylvania*, *Inc.*, 1995 Pa. PUC Lexis 193, at \*34 (*Bell Atlantic*); *CMV*)*.*

I&E also opposes the Joint Applicants’ attempt to have the Commission recognize the public interest benefits of addressing the financial plight of municipalities by “insert[ing] itself into the realm of Act 47 municipal recovery.” I&E R. Exc. at 20. I&E contends that municipal finance issues are beyond the scope of the Commission’s jurisdiction and authority as defined at Section 501 of the Code. *Id*. at 20-21 (citing 66 Pa. C.S. § 501; *CMV* at 29). According to I&E, jurisdictional utility ratepayers should not be required to bear the burden of municipal financial decisions. I&E R. Exc. at 20.

With regard to the question of whether the acquisition will benefit PAWC’s existing customers, I&E contends that “the most the Joint Applicants can offer these existing customers is some sharing of best practices with SSA’s skilled personnel.” I&E R. Exc. at 21. I&E argues that there is no evidence that such sharing is necessary for PAWC to continue providing safe and reliable service to its existing customers. Moreover, I&E asserts that “this purported benefit comes at a hefty price,” considering PAWC customers will be required to bear the burden of the purchase price of the acquisition, the cost of infrastructure improvements, and the unknown variance adjustment included in the APA. *Id*.

**c. OCA’s Replies to Joint Applicants’ Exceptions**

In its Replies to the Joint Applicants’ Exceptions, the OCA contends that the alleged benefits of the acquisition enumerated by the Joint Applicants are overstated, and that the harms will considerably outweigh the benefits. OCA R. Exc. at 11-12. The OCA asserts that there is no evidence that SSA does not possess the necessary technical, managerial, and financial fitness to operate a combined wastewater-stormwater system or to meet its obligations under the Consent Decree.  *Id*. at 13-14 (citing OCA St. 1 at 4; OCA St. 2 at 29, 31-32; Tr. at 98-100, 154; OCA M.B. at 38-40). Thus, the OCA concludes that the level and quality of service will be the same under PAWC ownership as it would be under SSA ownership. OCA R. Exc. at 14-15 (citing OCA St. 2 at 29; PAWC Exc. at 20).

The OCA also asserts that there will be no economies of scale as a result of the acquisition, as the Joint Applicants argue, because PAWC already provides water service to SSA’s customers. Moreover, the OCA claims that because of the ratemaking concessions that PAWC is seeking, the existing PAWC customers in the SSA service area will be harmed by paying rates above their cost of service so that stormwater improvements can be funded over a greater number of customers. OCA R. Exc. at 15. In addition, the OCA argues that although SSA customers may benefit from rate increase limitations in the short term, they may experience large rate increases in years eleven through thirteen following closing of the acquisition transaction. *Id*. at 15-16.

The OCA also contends that the benefits to the City described by the Joint Applicants are not determinative of the public interest. The OCA states that “[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’.” OCA R. Exc. at 16 (citing *Middletown; CMV*). According to the OCA, when the benefits to the City are weighed against the detriments to existing PAWC customers, the proposed transaction does not establish the substantial affirmative benefits necessary for approval of the acquisition. OCA R. Exc. at 16.

Finally, the OCA disputes the Joint Applicants’ assertion that customers of PAWC’s presently-owned smaller plants will benefit from the expertise PAWC will gain by operating SSA’s treatment plant. The OCA contends that there is no evidence that PAWC is not currently providing adequate service to customers it serves through smaller treatment plants. According to the OCA, any benefit to PAWC’s existing customers in this regard “is speculative at best.” OCA R. Exc. at 17.

**d. OCA’s Exceptions**

In its Exceptions, the OCA asserts that although the ALJs properly found that the variance adjustment is unreasonable, is not in the public interest, and violates the Code, they erred by not addressing the additional negative impacts of the proposed acquisition on PAWC’s existing customers. The OCA contends that there will be no affirmative benefit to these customers as the Joint Applicants aver. OCA Exc. at 16.

The OCA rejects the Joint Applicants’ claim that PAWC customers will benefit from sharing costs among a larger customer base. The OCA argues that PAWC’s customer base will not expand as a result of the acquisition as the Joint Applicants allege because all of the 31,000 customers served by SSA are already PAWC water customers. OCA Exc. at 16-17. The OCA also discounts PAWC’s claim that there will be no immediate rate impact on its existing customers. The OCA contends that PAWC plans to require its existing water and wastewater customers to begin paying between $146 and $199 million of the costs of the system improvements associated with the Consent Decree when it increases rates in its next base rate case. The OCA asserts that these costs will be in addition to the purchase price of the acquisition, which the existing water and wastewater customers will be required to pay. OCA Exc. at 17 (citing PAWC St. 4 at 4, 7; OCA St. 1 at 31; OCA St. 2 at 33). The OCA notes that PAWC’s existing customers already pay taxes or other fees to control storm water in their communities. OCA Exc. at 17-18 (citing OCA St. 2 at 34-35).

In addition, the OCA contends that the Joint Applicants failed to establish that PAWC can construct, operate and maintain SSA’s wastewater system and implement the proposed improvements associated with the Consent Decree at a lower cost and faster timeframe than SSA. The OCA argues that PAWC’s cost of capital will likely be higher compared to that of SSA, which is not required to pay income taxes or state and federal taxes on its equity earnings, and can issue tax-exempt debt. OCA Exc. at 18 (citing OCA St. 1 at 4; OCA St. 2 at 31-32; Tr. at 98; OCA M.B. at 39-40). In addition, the OCA contends that PAWC will use the same employees and follow the same time frame as SSA to meet the obligations under the Consent Decree. According to the OCA, there is no evidence that SSA is not technically or managerially fit. OCA Exc. at 18 (citing OCA St. 1 at 4; OCA St. 2 at 29; Tr. at 154; OCA M.B. at 38-39).

The OCA also maintains that there is no evidence that SSA does not possess the required financial fitness to meet its obligations under the Consent Decree as long as it continues to raise rates in accordance with its rate plan. In support of this contention, the OCA points to Standard and Poor’s determination of SSA’s healthy financial profile, strong debt service coverage, and liquidity. Moreover, the OCA opines that the cost to the public of having PAWC undertake the capital improvements is likely to be greater than the costs that would be incurred by SSA. OCA Exc. at 19 (citing Tr. at 98-100; OCA M.B. at 39).

In addition, the OCA asserts that PAWC has not shown how the level and quality of service with regard to the SSA system under PAWC ownership would improve over that under SSA ownership. OCA Exc. at 19-20 (citing OCA St. 2 at 29). The OCA contends that PAWC is unable to quantify any efficiencies or decreased operating costs that will result from the proposed transaction, or indicate when they might occur. Instead, the OCA submits that PAWC “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.’” OCA Exc. at 20 (citing PAWC St. 1 at 8; PAWC St. 4 at 5). According to the OCA, all of the risk and all of the costs relating to the acquisition are being shifted to the existing PAWC water customers. OCA Exc. at 20.

Finally, the OCA contends that the benefits of the acquisition to SSA customers are also limited. The OCA argues that although rate increases to SSA customers will be limited during the first ten years following execution of the APA, PAWC intends to move SSA customers to its Rate Zone 1 rates in years eleven through thirteen following closing of the transaction. According to the OCA, this could result in dramatic rate increases for SSA’s customers if, during the first ten years post-acquisition, PAWC proposes rate increases for Rate Zone 1 while limiting rate increases to the SSA customers in accordance with the 1.9% CAGR limitation. OCA Exc. at 20-21.

**e. Joint Applicants’ Replies to OCA’s Exceptions**

In their Replies to the OCA’s Exceptions, the Joint Applicants dispute the OCA’s contention that the addition of the 31,000 SSA wastewater customers to PAWC’s system will provide no benefit to PAWC’s customers. Quoting the testimony of PAWC witness Rod Nevirauskas, the Joint Applicants state:

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 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.

Joint Applicants’ R. Exc. at 18 (quoting PAWC St. 4-R at 4-5). According to the Joint Applicants, PAWC’s customers will benefit in the long-term from the acquisition through regionalization and the sharing of costs. Joint Applicants’ R. Exc. at 18.

The Joint Applicants also contend that the prospective rate issues raised by the OCA are beyond the scope of review for the Joint Application and should be reserved for a future PAWC base rate proceeding. The Joint Applicants assert that “the APA makes it abundantly clear that Commission approval of the Transaction would neither bind the parties nor the Commission in future PAWC base rate proceedings.” Joint Applicants’ R. Exc. at 18 (citing Joint Applicants’ R.B. at 27-28).

The Joint Applicants further argue that the OCA’s allegation that the acquisition is not in the public interest is based on a false assumption that combined wastewater service is non-jurisdictional. However, the Joint Applicants aver that the OCA’s position is incorrect as a matter of law, as the Recommended Decision concluded. The Joint Applicants maintain that PAWC is legally entitled to request that the costs of combined wastewater service be spread across PAWC’s combined water and wastewater customer base under Act 11. Joint Applicants’ R. Exc. at 18.

In addition, the Joint Applicants assert that the OCA’s contention that SSA is fit to continue to own and operate its system is irrelevant to the standard of review for the Joint Application. The Joint Applicants state that the Commission is required to evaluate whether the new owner is fit and whether there is an affirmative public benefit to the proposed transaction. According to the Joint Applicants, the fitness of the prior owner is irrelevant except to the extent that the new owner is more fit, which the Joint Applicants assert is the case, particularly with regard to PAWC’s financial ability to fund the system’s needed capital improvements. Joint Applicants’ R. Exc. at 18-10 (citing Joint Applicants’ R.B. at 38-39, 41-43).

Finally, the Joint Applicants dispute the OCA’s assertion that Scranton-area customers will be harmed by PAWC’s proposed rates in years eleven through thirteen following the closing of the acquisition transaction. According to the Joint Applicants, the APA provides for a gradual phase-in of rate increases for the Scranton-area customers in order to avoid rate shock, which will bring the customers in line with system average rates. The Joint Applicants aver that the phase-in is also intended to ensure that Scranton-area customers do not unreasonably benefit through low rates at the expense of PAWC’s other customers. Moreover, the Joint Applicants assert that according to the APA, the Commission will maintain absolute discretion to set just and reasonable rates, and that the Commission could phase in rates for Scranton-area customers over a longer period of time, if appropriate. However, the Joint Applicants contend that it is premature and inappropriate to speculate as to how the Commission may exercise its ratemaking authority in the future. Joint Applicants’ R. Exc. at 19 (citing Joint Applicants’ R.B. at 38).

**4. Disposition**

Upon our consideration of the Parties’ Exceptions, Replies to Exceptions, and the record evidence in this proceeding, we find that the Joint Applicants have met their burden of demonstrating, by a preponderance of the evidence, that the acquisition will affirmatively promote the service, accommodation, convenience, or safety of the public in a substantial way. *City of York; Popowsky v. Pa. PUC,* 594 Pa. 583, 611, 937 A.2d 1040, 1057 (2007). We have reached the conclusion that this acquisition is in the public interest based on our consideration of the impact of the acquisition on all affected parties, as required by *Middletown*, 482 A.2d at 682. Initially, we agree with the ALJs’ findings that PAWC possesses the necessary technical, financial and legal fitness to own and operate the assets it seeks to acquire from SSA and to provide the proposed service to SSA’s customers. We note that no party in this proceeding disputed the Joint Applicants’ claims or the ALJs’ findings in this regard.

In addition, we are persuaded by the evidence presented by the Joint Applicants that PAWC is better positioned to own and operate the combined wastewater system and to implement the necessary capital improvements to the system in conformance with the Consent Decree. As the Joint Applicants asserted, PAWC is the Commonwealth’s largest water and wastewater provider, with total assets of $3.9 billion and annual revenues of $613 million for 2015, including operating income of approximately $307 million and net income of approximately $143 million. Joint Applicants’ M.B. at 39-40. Also, as PAWC witness James F. Sheridan stated:

PAWC has an established track record with extensive experience delivering large, complex water and wastewater capital improvement projects, such as the Long Term Control Plan (“LTCP”) projects associated with [SSA’s] system.

PAWC has funded in excess of $1 billion in capital construction over the past five years, with expenditures expected to total $275 million to $300 million per year for the next five years. The magnitude of individual capital projects has exceeded $100 million.

PAWC St. 3-R at 4.

In addition, PAWC presented evidence that it currently operates fifteen wastewater treatment plants in Pennsylvania, including three biological nutrient removal wastewater treatment plants, similar to SSA’s system. PAWC St. 3 at 4. Moreover, as a subsidiary of American Water Works Company, Inc., PAWC has available to it the resources of American Water Works Service Company, Inc., including access to professionals with expertise in various specialized areas. *Id*. at 8. We note also that PAWC already operates water facilities in the Scranton area. *Id*. at 8-9.

PAWC also provided testimony that it currently has a $220 million line of credit through American Water Capital Corp. a wholly owned subsidiary of American Water Works Company, Inc., and that its strong credit ratings allow it to obtain additional capacity on this line. PAWC St. 5 at 3. PAWC witness James S. Merante testified that PAWC carries a corporate credit rating of “A3” from Moody’s Investors Services and an “A” rating from Standard and Poor’s Rating Services. *Id*. Mr. Merante further stated that PAWC obtains long-term debt financing through American Water Works Company, Inc. at favorable interest rates and payment terms, and also uses low-cost financing through the Pennsylvania Infrastructure Investment Authority and the Pennsylvania Economic Development Financing Authority. According to Mr. Merante, PAWC may obtain additional equity investments through American Water Works Company, Inc. *Id*. Thus, we believe PAWC’s financial resources to be superior to those of SSA with regard to its ability to meet the demands of operating and maintaining the combined system and fulfilling the requirements of the Consent Decree.

As noted above, the OCA argues that the cost of having PAWC undertake the capital improvements under the Consent Decree is likely to be greater than the cost that would be incurred by SSA, because PAWC’s cost of capital will likely be higher compared to that of SSA. OCA Exc. at 18-19. However, we find persuasive the rebuttal testimony of PAWC witness Merante, who asserted that the cost of capital analysis presented by OCA witness Scott J. Rubin, upon which the OCA relied for its conclusion, did not account for certain important limitations with regard to SSA’s financial position when compared to that of PAWC. PAWC St. 5-R at 4-6. As summarized by Mr. Merante:

Overall, Mr. Rubin’s cost of capital analysis does not properly reflect [SSA’s] limited access to equity capital (*i.e.*, limited to internally generated funds), the impact of debt issuance costs and debt covenant compliance costs, [SSA’s] debt capacity and the impact of increased leverage on [SSA’s] borrowing costs, and the impact of [SSA’s] need to obtain guarantees for its debt obligations, including guarantees provided by the City, a financially distressed city under Act 47. In light of [SSA’s] upcoming environmental compliance costs and need for significant capital investment, the focus in this proceeding should not be on [SSA’s] prior – or even current – cost of capital but instead on [SSA’s] prospective cost of capital. PAWC is, without question, better capable of meeting the future capital needs of [SSA’s] system and this is a substantial public benefit of the transaction.

*Id*. at 6.

In addition, although the OCA argues that SSA has a relatively healthy financial profile, the Joint Applicants raised a number of significant concerns regarding SSA’s ability to maintain long-term financial viability, including the following:

* Any conditions causing customers to not be able to pay for wastewater service and their current taxes are likely to lead to a higher delinquency rate for SSA, which will be noticed by SSA’s bond rating agencies;;
* Higher SSA debt costs will inevitably lead to higher rates for SSA customers;
* Increased sewer delinquencies will negatively impact SSA’s cash flow and its ability to satisfy its operating financial obligations;
* SSA is highly leveraged with an 80.4% debt to plant ratio;
* SSA will have to consider substantial rate increases on a stand-alone basis of an average of *4.57% per year* over the next thirty years to maintain its current financial profile and pay for the Consent Decree improvements;
* SSA’s existing rates consume 2.3% of its customers’ median household income;
* The combined populations of Scranton and Dunmore have been steadily declining with each ten-year census since a peak in the 1930s;
* Because median household income in the Scranton and Dunmore area has been increasing at a slower rate than the consumer price index, people continue to be unable to afford many services;
* Affordability issues plaguing Scranton area residents and SSA customers, along with SSA’s rate inflexibility and related constraints on its ability to access capital, adversely affects SSA’s future ability to raise revenue; and,
* SSA’s future incapability to raise revenue calls into question its ability to meet the capital and other spending requirements in the Consent Decree .

Joint Applicants’ R.B. at 42-43 (emphasis in original) (citations omitted).

Also, according to SSA’s witness Eugene P. Barrett, SSA estimated that the requirements of the Consent Decree, the Long Term Control Plan, and ongoing investment needs and expense requirements of SSA could result in the need for average annual rate increases to SSA’s customers of 4.57% through the year 2042. SSA determined that PAWC was better positioned than SSA to maintain wastewater rates for SSA’s customers at a level below those projected increases. SSA St. 2-R at 7. Likewise, we believe that the significantly greater size of PAWC’s customer base and substantial financial resources will allow PAWC to leverage economies of scale in providing wastewater service to SSA’s customers, which will mitigate the need for larger and more frequent rate increases that may prevail should SSA continue to own and operate the combined system.

For the reasons discussed above, we do not agree with the OCA that SSA’s technical and financial fitness is commensurate with that of PAWC, and, thus, renders SSA capable of operating, maintaining, and improving the combined wastewater system as efficiently as PAWC. Rather, we find that due to its size, its considerable experience and technical expertise in the operation and maintenance of wastewater systems, and its superior financial resources, PAWC is better positioned to efficiently operate and maintain the combined system, and to successfully fulfill the requirements of the Consent Decree in a safe and economical manner.

In addition, we agree with the testimony of Mr. Barrett that PAWC and its customers will benefit from the addition of SSA’s “large treatment plant and its skilled personnel familiar with the complex business of treating wastewater processed at the end of a large combined system.” SSA St. 2-R at 7-8. Moreover, we are of the opinion that PAWC’s existing customers also stand to benefit from enhanced economies of scale and from the additional revenues generated as a result of the addition of SSA’s 31,000 wastewater customers to PAWC’s overall customer base. PAWC St. 4-R at 4-5.

As to the concerns raised by I&E and the OCA regarding the alleged detriments of the acquisition to PAWC’s existing customers, we note that these concerns center on the potential rate effects of the acquisition. However, we are not in a position to thoroughly adjudicate ratemaking issues relating to the acquisition in this proceeding. Nor do we find that this acquisition proceeding is the appropriate context for addressing these rate issues. The record does not contain sufficient evidence to allow us to evaluate the specific effects of the acquisition on PAWC’s revenue requirement or to decide cost allocation and rate design matters. Such issues are better reserved for a future base rate proceeding.

Consistent with the above discussion, we conclude that that the acquisition will affirmatively promote the service, accommodation, convenience, or safety of the public in a substantial way. Accordingly, we will grant the Exceptions of the Joint Applicants, to the extent they argue that the Recommend Decision failed to consider the substantial public benefits of the acquisition, and we will deny the Exceptions of the OCA on this issue.

**D. Variance Adjustment of the Purchase Price**

**1. Positions of the Parties**

**a. I&E**

I&E opposed the approval of the variance adjustment in the APA and requested that the Commission deny the adjustment for the following reasons. First, I&E contended that the variance adjustment, which is an issue of first impression, is not consistent with sound ratemaking principles, would harm PAWC’s customers, is not in the public interest, and, therefore, should not be approved. I&E M.B. at 1, 8 and 15. Specifically, I&E questioned the fact that the variance adjustment is based solely on revenue growth, rather than a consideration of both revenue and expenses or net income. I&E further alleged that the variance adjustment is neither an asset purchase nor a used and useful plant, but an intangible asset or goodwill that cannot be recovered in a rate case. *Id.* at 15-18.

Second, I&E questioned the legal standing of the variance adjustment, arguing that the plain language of Section 7.07(e) of the APA regarding the adjustment violates Sections 1303 and 1304 of the Code, 66 Pa. C.S. §§ 1303 and 1304, which are, the prohibition against a utility charging any rate other than that specified in its tariff and the prohibition against a utility establishing unreasonable differences as to rates between classes of service. *Id.* at 19, citing 66 Pa. C.S. §§ 1303 and 1304. According to I&E, if PAWC decides to directly pay the adjustment to SSA’s wastewater customers ten years following closing, as highlighted in Section 7.07(e) of the APA, such payment would be considered a *de facto* rate refund to the affected customers, which ultimately results in their paying less than the prescribed rates in PAWC’s tariff. I&E M.B. at 20-21. I&E further argued that even if such a payment is not directly made by PAWC to SSA’s wastewater customers but is made through a third-party, as stipulated in Section 7.07(e) of the APA, it is still a violation of Section 1303 of the Code. Furthermore, I&E contended that although 66 Pa. C.S. § 1304 does not prohibit differences in rates, the Commonwealth Court has held that the utility must show that the differential is justified by the difference in cost required to deliver service to each class of customers, which PAWC has failed to establish in the instant proceeding. I&E asserted that the variance adjustment violates 66 Pa. C.S. § 1304, as well on the basis that I&E believes the proposed variance adjustment refund would ultimately, benefit only SSA’s wastewater customers and not PAWC’s existing customers. I&E M.B. at 21-22.

Next, I&E pointed out that the terms of the APA, which require PAWC to keep SSA’s wastewater customers’ rates low for the first ten years after closing, to increase the rates from years eleven through thirteen, and, subsequently, to bring SSA’s wastewater customers’ rates in alignment with PAWC’s Rate Zone 1 rates, may violate the concepts of gradualism and may result in rate shock. *Id.* at 22-23. I&E explained that this is even more telling in the significant gap between SSA’s residential wastewater customers’ rates and PAWC’s Rate Zone 1 residential rates.[[6]](#footnote-6)  I&E noted that while it does not oppose PAWC’s goal of moving SSA’s wastewater customers into PAWC’s Rate Zone 1 rates, PAWC’s proposed means of achieving this goal is problematic. I&E suggested that PAWC gradually increase SSA’s wastewater customers’ rates beginning with its first base rate increase filing after closing and over the entire thirteen year period. *Id.*at 23-25.

I&E also pointed out the potential problem with PAWC’s ability to claim an acquisition adjustment regarding this transaction in a future base rate proceeding. I&E noted that the instant acquisition may fall short of the requirements of Section 1327 of the Code, 66 Pa. C.S. § 1327(a), which establishes nine criteria that must be met before a utility can claim an acquisition adjustment in rate base. In particular, I&E indicated that this acquisition may be deficient in meeting the requirements in Section 1327(a)(2) and (6), because not only is the purchase price unreasonable but SSA has approximately 31,000 wastewater customers, which is higher than the 3,300 customers required for a utility to claim an acquisition adjustment in a base rate proceeding. *Id.* at 25-27.

**b. OSBA**

In its opposition to the variance adjustment, OSBA also echoed I&E’s arguments that the variance adjustment violates Section 1303 of the Code and may also violate the concepts of gradualism and rate shock. OSBA M.B. at 1-6.

**c. OCA**

The OCA also opposed the variance adjustment, alleging that based on its calculation of the revenue requirements of SSA’s wastewater system and considering the terms of the APA, in the first ten years following closing, PAWC would be required to pay SSA an additional $104 million above the purchase price of $195 million. The OCA argued that this additional cost, which is aimed at subsidizing the purchase price, should be borne by PAWC’s investors and not PAWC’s existing customers. OCA M.B. at 44‑46. The OCA argued that even if the Commission approves the variance adjustment, it should not allow PAWC to use the revenue-sharing provision of Section 1311(c) of the Code, 66 Pa. C.S. § 1311(c), for SSA’s wastewater customers for at least the first ten years following closing. The OCA also argued that an acquisition adjustment should not be approved in the instant proceeding. *Id.* at 46-47.

**d. Joint Applicants**

The Joint Applicants contended that the instant proceeding is not the appropriate forum to address ratemaking treatment of the variance adjustment. They argued that traditional ratemaking issues raised by the opposing Parties, such as recovery of the variance adjustment from ratepayers, recovery of expenses associated with new jobs, and rate gradualism, need not be addressed in this proceeding but should be reserved for a future PAWC base rate proceeding. Joint Applicants’ M.B. at 11 and 88. The Joint Applicants averred that although PAWC has committed to bringing SSA’s wastewater customers’ rates in alignment with its Rate Zone 1 rates over a reasonable period of time, nothing in the APA would deprive the Commission from making a determination of the appropriate rates for PAWC’s customers in future base rate proceedings. *Id.*

The Joint Applicants dismissed, as speculative and unfounded, I&E and OSBA’s argument regarding potential “rate shock” for SSA’s wastewater customers. According to the Joint Applicants, the rates stipulated in the APA would provide a reasonable progression of rate increases designed to bringing SSA’s wastewater customers’ rates in line with PAWC’s system-wide average rates over a thirteen year period. The Joint Applicants do not believe the “rate shock” argument is an issue because the Commission has the discretionary authority to set just and reasonable rates for the affected customers. *Id.* at 82 (citing 66 Pa. C.S. § 1301).

With regard to PAWC’s potential claim of an acquisition adjustment for SSA’s wastewater system in a future base rate proceeding, the Joint Applicants averred that following closing and prior to its next base rate filing, PAWC would prepare an original cost study of the plant-in-service, which would then be used to make a determination of the need for an acquisition adjustment claim in a future base rate proceeding. The Joint Applicants believe it is premature to speculate about PAWC’s acquisition adjustment claim for SSA’s wastewater system in the instant proceeding. Joint Applicants’ M.B. at 83-84.

The Joint Applicants also averred that it is too early to make a determination regarding the recovery of the variance adjustment through rates in the instant proceeding. They argued that the variance adjustment issue should be reserved for future base rate proceedings, stating as follows:

Because the Variance Adjustment is an adjustment to the purchase price of the SSA assets, its recovery through the rates cannot be determined until after PAWC has prepared a depreciated original cost of plant-in-service study of the SSA system and the Commission, in a base rate proceeding, has determined that the Variance Adjustment exceeds the depreciated original cost plus any allowed acquisition premium. By way of example, if the Commission determines that the depreciated original cost of the SSA system equals $195 million purchase price and that PAWC is otherwise entitled to an acquisition premium, PAWC could seek to recover the acquisition premium as the result of any Variance Adjustment that is subsequently paid. There is not a time limitation on the Commission’s ability to award an acquisition premium. After ten years of experience, the Commission could theoretically determine that PAWC’s acquisition of SSA promoted a substantial public interest and that PAWC should be rewarded by way of ate [sic] recovery of an acquisition premium.

*Id.* at 84-85.

The Joint Applicants noted that the rates outlined in the terms of the APA are not binding but are subject to Commission approval and the applicable law. *Id.*

**2. ALJs’ Recommendation**

After a thorough analysis of the positions of the Parties, the ALJs denied the variance adjustment stating that it does not represent a fixed sales price but creates an imprecise sales price that ultimately would be borne by PAWC and its customers. R.D. at 32. In their analysis, the ALJs compared this case to *Philadelphia Suburban Water Co. v. Pa. PUC*, 808 A.2d 1044 (Pa. Cmwlth. 2002) (*Philadelphia Suburban*)*.* According to the ALJs, the similarities between this case and *Philadelphia Suburban* are evident in the Court’s identification of similar issues in an asset purchase agreement in *Philadelphia Suburban*. The ALJs explained that, in *Philadelphia Suburban*, PAWC executed an asset purchase agreement with the City of Coatesville Authority (Coatesville) for the purchase of the City’s water system. The agreement, as subsequently amended, required PAWC to make an annual contribution to the Coatesville Economic Development Fund in an amount equal to Coatesville’s annual charge from PAWC for fire hydrant service. The ALJs noted that the Court found this arrangement failed to provide a fixed sales price and placed the risk of future fire hydrant service on PAWC. R.D. at 32.

The ALJs found that, because the variance adjustment is unknown and unknowable at this time, but is based on future revenues that are tied to future Commission-approved rates, the purchase price is open-ended, unreasonable and not in the public interest. *Id.* at 32-33.

The ALJs emphasized this finding, stating as follows:

In effect, PAWC and SSA are asking the Commission to approve the method for calculating the variance adjustment set forth in the APA now as reasonable and in the public interest. If the Commission approves the method for calculating the variance adjustment as reasonable and in the public interest now, it is also approving the amount that results from using that method as reasonable and in the public interest without knowing what that amount is. This is neither reasonable nor in the public interest. In addition, the 1.9% CAGR, which serves to trigger the variance adjustment, is based on arms-length negotiations between PAWC and SSA and bears no relationship to either the value of the assets that PAWC is acquiring or the estimated future revenue needs for SSA’s system based on estimated operating costs. Since the variance adjustment is open ended, bears no relationship to either the value of the assets or estimated operating costs, it is not in the public interest or reasonable as an adjustment to the purchase price.

*Id.* at 33.

The ALJs were also concerned with the fact that under the terms of the APA, the variance adjustment is only payable by PAWC and not SSA. The ALJs acknowledged that while the variance adjustment is aimed at providing a buffer for SSA’s wastewater customers against future anticipated rate increases, it is an unreasonable adjustment to the purchase price, and its payment by PAWC, which they believe is a *de facto* refund to customers or a deviation from PAWC’s tariff, violates Section 1303 of the Code, 66 Pa. C.S. § 1303.[[7]](#footnote-7) R.D*.* at 34-42.

The ALJs, however, disagreed with I&E’s argument that the variance

adjustment violates Section 1304 of the Code, 66 Pa. C.S. § 1304,[[8]](#footnote-8) because it creates an unreasonable advantage to customers in SSA’s territory. According to the ALJs, while 66 Pa. C.S. § 1304 establishes standards that a utility must follow when making rates, which are ultimately incorporated into the tariff, this case does not present a situation where the tariff itself provides an undue preference for one class of ratepayer at the expense of another because the variance adjustment is not part of the tariff applicable to SSA’s wastewater customers. R.D. at 40-42.

Having established that the variance adjustment proposed in the APA was not reasonable, not in the public interest, and violated 66 Pa. C.S. § 1303, the ALJs concluded that the Commission cannot approve the variance adjustment or the APA contained in the Joint Application. The ALJs, therefore, denied the Joint Application. *Id.* at 42-43.

**3. Exceptions, Replies and Disposition**

**a. Reasonableness and lawfulness of the variance adjustment**

**i. Joint Applicants’ Exceptions**

In their Joint Exception No. 1, the Joint Applicants dispute the ALJs’ conclusion that the purchase price, which was an arm’s-length negotiation, was unreasonable and not in the public interest due to the associated variance adjustment. According to the Joint Applicants, the variance adjustment potentially adjusts the purchase price paid by PAWC for SSA’s wastewater assets in the event that the Commission does not approve PAWC’s attempts to abide by SSA’s requirements to keep SSA’s wastewater customers’ rates at reasonable levels in the first ten years after closing. Joint Applicants’ Exc. at 2. The Joint Applicants contend that the Commission does not look at the “reasonableness” of the purchase price in an application proceeding. *Id*. at 2‑4. Citing to prior Commission-approved acquisitions containing arm’s-length negotiated purchase prices; the Joint Applicants assert that the instant proceeding is not the appropriate forum to contest the reasonableness of a purchase price.[[9]](#footnote-9) In their argument against the ALJs’ conclusion on the purchase price, the Joint Applicants state as follows:

More often, when a Code Section 1102 application warrants additional information on the purchase price of the transaction, the Commission simply orders that original cost studies be reviewed in the next general rate case to determine if the claims relating to the purchase price require further inquiry.

It is entirely appropriate, lawful and customary for the Commission to separate ratemaking issues (like the reasonableness of an acquisition’s purchase price) from the central issues presented in a Code Section 1102 evaluation, such as the legal, technical and financial fitness of the acquiring party, and the presence of affirmative public benefits in the transaction.

Joint Applicants’ Exc. at 6, 7. The Joint Applicants assert that the reasonableness of a purchase price should be reserved for a post-application rate case proceeding and should not be contested in this proceeding. Joint Applicants’ Exc. at 3-8 (citing 66 Pa. C.S. § 1301). The Joint Applicants contend that the ALJs were wrong in concluding that an approval of the APA as filed, including the variance adjustment and the methodology for its calculation, connotes a determination that the final purchase price is reasonable for ratemaking purposes. Comparing the variance adjustment to an automatic adjustment clause under Section 1307 of the Code, 66 Pa. C.S. § 1307, the Joint Applicants assert that while not an automatic adjustment mechanism by any means, the variance adjustment measures PAWC’s compliance with the 1.9% CAGR benchmark in the APA, and that the inclusion or exclusion of this adjustment in PAWC’s rates should be a matter for a subsequent proceeding similar to the automatic adjustment process.[[10]](#footnote-10) The Joint Applicants aver that the variance adjustment tracks PAWC’s level of success or failure in achieving its goal of keeping SSA’s wastewater rates reasonable compared to the benchmark of the 1.9% CAGR. Joint Applicants’ Exc. at 8-10.

Next, the Joint Applicants assert that the ALJs were wrong in their description of the distribution of the variance adjustment to be paid at the end of the tenth year following closing. *Id*. at 10 (citing R.D. at 35). They assert that the ALJs’ qualification of the distribution of the variance adjustment as a *de facto* refund to customers misses the mark, because it ignored the several other distribution methods or options proposed in the APA. The Joint Applicants averred that per the APA, they offered three options for the Commission’s review regarding the distribution of the variance adjustment. Joint Applicants’ Exc. at 11. The Joint Applicants posit that if the Commission is concerned with the distribution of the variance adjustment, it could condition approval of the APA on the removal of both distribution methods while allowing the option that SSA or its successor retain the variance adjustment payment by PAWC. The Joint Applicants allege that the ALJs ignored the fact that the APA clearly indicates that the Joint Applicants were open to receiving guidance from the Commission on the most appropriate or reasonable method of distributing the adjustment. *Id.* at 10‑12.

Finally, the Joint Applicants question the ALJs’ reliance on *Philadelphia Suburban* in reaching a conclusion that the variance adjustment payment was a *de facto* refund to customers. The Joint Applicants argue that *Philadelphia Suburban* is not applicable to this case and the variance adjustment in the APA does not violate the Court’s holding in that case. The Joint Applicants assert that *Philadelphia Suburban* is different from this case for the following reasons: (1) unlike *Philadelphia Suburban*, there is no automatic refund to customers because the APA, including the prescribed variance adjustment formula, states that SSA or its successor have the option of retaining the variance adjustment or refunding the payment to its customers; (2) while *Philadelphia Suburban* involved the utility’s constant true-up of rates set by the Commission, which could be construed as free utility service, the APA, in this case, does not reference any PAWC services used and paid for by SSA that form the basis of a PAWC payment to SSA; and (3) unlike *Philadelphia Suburban*, SSA’s wastewater customers have no right to determine how and under what circumstances the variance adjustment payment would be made. In light of the above, the Joint Applicants conclude that the ALJs erred in their reliance on *Philadelphia Suburban* in reaching a conclusion that the variance adjustment violates the Code. Joint Applicants’ Exc. at 13-15 (citing R.D. at 37; 66 Pa. C.S. § 1303; *Philadelphia Suburban*).

**ii. OCA’s Replies to Joint Applicants’ Exceptions**

In its Reply to the Joint Applicants’ Exception No. 1, the OCA avers the variance adjustment is unreasonable and unlawful. OCA R. Exc. at 2. In response to the Joint Applicants’ argument that the purchase price be reserved for a future base rate proceeding, the OCA avers that the Commission is not prohibited from reviewing the purchase price as part of an application proceeding. OCA R. Exc. at 4 (citing *Application of Pennsylvania-American Water,* 2001 Pa. PUC Lexis 10; *Application of Shenango Valley Water Co.*, 1994 Pa. PUC Lexis 110). The OCA contends that the purchase price is relevant in reviewing the merits of an acquisition and making a determination of the reasonableness of such a transaction. OCA R. Exc. at 4 (citing *Investigation of W.P. Water Co*., Docket No. I-00070114 (Order entered March 31, 2009)). The OCA further highlights the importance of a critical review prior to approval of the APA in an acquisition such as this one, which involves the purchase price of a municipal entity. OCA R. Exc. at 4 (citing *Application of West Penn Power,* 1996 Pa. PUC Lexis 32). The OCA questions the fact that while the Joint Applicants argue that rate recovery issues regarding the variance adjustment should be reserved for future rate proceedings, they are, nonetheless, requesting the Commission’s pre-approval to recover stormwater costs in the instant proceeding. OCA R. Exc. at 3-4.

Second, the OCA asserts that, contrary to the Joint Applicants’ argument that the purchase price is reasonable because it was a result of an arms-length transaction, the Commission has held that an arms-length transaction does not in itself determine the reasonableness of the purchase price. OCA R. Exc. at 5 (citing *Pa. PUC v. Citizens Utilities Water Company of Pennsylvania*, 1996 Pa. PUC Lexis 164) (*Citizens*)). According to the OCA, in *Citizens,* the Commission, in its rejection of the company’s claim that the reasonableness of the purchase price could be inferred from the fact that it was an arms-length transaction, stated that the requirement of an arms-length negotiation is a separate requirement of Section 1327 of the Code, 66 Pa. C.S. § 1327, and that “the framers of the statute recognized that an arms-length transaction, even between non-affiliated entities, could produce an unreasonable price.” OCA R. Exc. at 4-5 (citing *Citizens* at \*37). The OCA avers that, consistent with 66 Pa. C.S. § 1327 and the Commission’s policy statement at 52 Pa. Code § 69.711, the Commission must find that a negotiated arms-length purchase price is reasonable. OCA R. Exc. at 5.

The OCA also dispels the Joint Applicants’ comparison of the variance adjustment to a proceeding where an original cost study is ordered and reviewed in the next general rate case “to determine if claims relating to the purchase price require further inquiry.” *Id.* at 5. The OCA argues that because the variance adjustment, which could change the purchase price by $104 million, will not be known for ten years, requiring PAWC to conduct an original cost study in the instant proceeding will not change or impact the purchase price in any way. OCA R. Exc. at 5-6.

Next, the OCA disputes the Joint Applicants’ contention that the reasonableness of the purchase price should be separated from a Section 1102 review which involves issues such as the legal, technical and financial fitness of the acquiring utility, as well as the affirmative public benefits of the transaction. *Id.* at 6. The OCA avers that based on its assessment, the transaction would not result in an affirmative public benefit because the purchase price, which is dependent on the variance adjustment, would have a significant ratemaking impact over the first ten years after closing of this transaction. OCA R. Exc. at 6-8. The OCA states that with the addition of the variance adjustment, the purchase price could increase by up to $104 million, which means PAWC would pay more than three times the book value of the assets. *Id.* at 7. The OCA asserts that if the Commission makes a determination that it has jurisdiction over stormwater service, the Commission should protect PAWC’s existing customers from subsidizing the payment of the additional $104 million over the next ten years. *Id.* at 8.

Lastly, the OCA requests that the Commission reject the Joint Applicants’ argument that approval of the variance adjustment methodology is not the same as approving the product of the methodology. According to the OCA, the Joint Application stipulates a request for approval of both the variance adjustment and the calculation methodology of the adjustment. *Id.* at 8-9.

**iii. I&E’s Replies to Joint Applicants’ Exceptions**

In its Replies to the Joint Applicants’ Exception No. 1, I&E asserts that considering the ratemaking implications of the variance adjustment and the purchase price, the ALJs correctly denied the Joint Application based on their determination that the transaction is unreasonable and not in the public interest. I&E further asserts that if the Commission elects to reverse the ALJs’ recommendation, it must expressly reject recovery of the variance adjustment from ratepayers so that PAWC can consider other available options prior to closing of this transaction. I&E R. Exc. at 3-7. Next, I&E submits that the ALJs were correct in their conclusion that because it is impossible to determine the variance adjustment at this time, approving its calculation methodology connotes an allowance of the amount that would result from the methodology, which they believe is not in the public interest. I&E R. Exc. at 11-14. I&E disputes the Joint Applicants’ argument that the variance adjustment need not attract the same scrutiny as a Section 1102 filing because it was filed under Section 507 of the Code, 66 Pa. C.S. § 507. I&E asserts that the ALJs rightly conducted a public interest analysis of the terms of the APA and concluded that the variance adjustment set forth in the APA is not reasonable, not in the public interest and violates the Code. I&E R. Exc. at 11-12.

I&E also questions the validity of the variance adjustment, especially, because it is one-directional, *i.e.,* from PAWC to SSA. I&E asserts that the Joint Applicants have failed to make any credible argument for the appropriateness of the adjustment in a regulatory environment and how it meets the just and reasonable rates mandate of the Code. I&E R. Exc. at 14-15.

Finally, I&E disagrees with the Joint Applicants’ argument that *Philadelphia Suburban* is not controlling in this proceeding. I&E argues that the ALJs were correct in relying on *Philadelphia Suburban* because, like the ALJs in this case, the Court’s rejection of PAWC’s asset purchase agreement with Coatesville was also premised on the fact that the transaction failed to establish a fixed sales price and placed the risk of future obligations under the agreement on PAWC. I&E asserts that the Joint Applicants’ effort to distinguish this case from *Philadelphia Suburban* by highlighting the several payment options for the variance adjustment is unpersuasive and should be rejected. I&E R. Exc. at 16-18.

**iv. OSBA’s Replies to Joint Applicants’ Exceptions**

In response to the Joint Applicants’ Exception No. 1, OSBA submits that the ALJs were right in concluding that the variance adjustment in the APA was unreasonable and unlawful. OSBA asserts that irrespective of how the payment of the variance adjustment will be made by PAWC, it violates the plain language of Section 1303 of the Code. Accordingly, OSBA requests that the Commission deny the variance adjustment. OSBA R. Exc. at 3-5.

**v. OCA’s Exceptions**

In its Exception No. 3, the OCA disagrees with the ALJs’ explanation in the Recommended Decision that the potential for customer growth in SSA’s service territory could affect the revenue calculation under the variance adjustment. OCA Exc. at 14 (citing R.D. at 28-29 and 31-34). The OCA observes that the calculation of the variance adjustment proposed in Schedule 7.07(d), (e) and (f) of the APA ignoresany potential change in the number of SSA’s customers or sales over the ten-year period.[[11]](#footnote-11) OCA Exc. at 14 (citing APA §§ 7.07(d), (e), and (f)). The OCA further asserts that the calculation of the variance adjustment shows that the adjustment has nothing to do with the value of the assets being acquired by PAWC in this transaction. The OCA, nonetheless, agrees with the ALJs’ conclusion that the variance adjustment is neither reasonable nor in the public interest because it has no relationship to the value of the assets being purchased. OCA Exc. at 15.

**vi. Joint Applicants’ Replies to OCA’s Exceptions**

In their Replies to OCA Exception Nos. 3 and 4, the Joint Applicants request permission to withdraw their Exception No. 1 which defends the variance adjustment. The Joint Applicants propose that the Commission approve the Joint Application conditioned upon the Joint Applicants’ filing of an APA eliminating the variance adjustment (Proposed Amended APA). The Proposed Amended APA is attached to the Joint Applicants’ Replies to Exceptions as Appendix A. The Joint Applicants acknowledge this proposal is necessary in light of the ALJs’ denial of the Joint Application, consistent with their finding that the variance adjustment violates Section 1103 of the Code, 66 Pa. C.S. § 1103, and is not in the public interest. The Joint Applicants also believe this proposal would help streamline the Commission’s decision in this proceeding and limit potential appellate issues regarding this case. Joint Applicants’ R. Exc. at 14-15. According to the Joint Applicants, pursuant to Section 1103, the Commission has the authority to condition the issuance of a Certificate. 66 Pa. C.S. § 1103 (a). Comparing this case to *Philadelphia Suburban* and considering the fact that the ALJs relied on the latter in their denial of the Joint Application, the Joint Applicants question why the ALJs failed to recommend a conditional approval similar to that in *Philadelphia Suburban*, rather than recommending an outright denial of the Joint Application. The Joint Applicants aver that, as the ALJ in *Philadelphia Suburban* recommended an approval of the application conditioned upon the removal of a legally-offensive provision from the asset purchase agreement in that case, the ALJs should have conditioned approval of the instant proceeding on the removal of the variance adjustment from the APA. Joint Applicants’ R. Exc. at 14-16.

The Joint Applicants aver that the elimination of the variance adjustment should address the concerns raised by the ALJs and the opposing Parties to this proceeding.[[12]](#footnote-12) The Joint Applicants also highlight the urgency required in finalizing this transaction as it pertains to the City’s financial distress status. Particularly, the Joint Applicants assert that the prompt resolution of the issues in this transaction would go a long way in addressing the City’s upcoming 2016-2017 budget crisis. Further, pending issuance of a final Commission decision and in consideration of the fact that other Parties to this proceeding could appeal a Commission Order, the Joint Applicants pledge to consummate the transaction subject to the satisfaction or waiver of all other conditions to the obligations of each of the Joint Applicants. Joint Applicants’ R. Exc. at 16-17.

**vii. Disposition**

Based on our review of the record, the positions of the Parties, and the applicable law, we will grant the Joint Applicants’ request to conditionally approve the Joint Application subject to their filing of the Proposed Amended APA and the removal of the variance adjustment provisions. We acknowledge the OCA’s Exception No. 3 regarding customer growth in relation to the variance adjustment; however, based on our decision to conditionally approve the Application, we need not address this argument in detail.

Nevertheless, we note that the OCA argued that, even without the variance adjustment, the $195 million purchase price set forth in the APA is more than the book value of all of SSA’s property, plant and equipment.[[13]](#footnote-13) OCA M.B. at 33. However, the Joint Applicants have indicated that following closing and prior to its next base rate filing, PAWC would prepare an original cost study of the plant-in-service, which would then be used to make a determination of the need for an acquisition adjustment claim for this transaction in a future base rate proceeding. Joint Applicants’ M.B. at 83-84. Consequently, due to the significant difference in the book value of SSA’s wastewater plant and the purchase price of this transaction, should PAWC claim an acquisition adjustment in its next rate case filing, the original cost study may be reviewed to determine the reasonableness of the claim, consistent with Section 1327(a) of the Code, 66 Pa. C.S. § 1327(a), and the Commission’s policy statement at 52 Pa. Code § 69.721, regarding acquisitions of viable water and wastewater systems.  This review may also address any contributions-in-aid-of-construction.

We also acknowledge the concerns of some of the Parties regarding the rate impact resulting from the rate limitations applicable to SSA’s wastewater customers to which the Joint Applicants agreed in the purchase agreement. Specifically, the OCA argues that even with the removal of the variance adjustment, the “substantial detriments of the transaction outweigh the alleged benefits.” OCA R. Exc. at 18-19. Furthermore, while not recommending any changes to the ratemaking terms in the APA in this proceeding, I&E argued that the numerous ratemaking terms contained in the APA, including the rate limitations, may cause rate shock issues if not addressed starting in the first base rate case after closing. I&E M.B. at 22-25.

As we stated earlier, this proceeding is not the proper forum for addressing ratemaking issues. Therefore, we will defer *all* future rate related issues raised as a result of this transaction until PAWC’s next base rate case. This includes all valuation issues, as well as rate design issues involved in this matter.[[14]](#footnote-14) As we have indicated, disputes over future rates are not ripe for our decision at this time. At closing, PAWC will simply adopt SSA’s current customer and usage rates. R.D. at 9.[[15]](#footnote-15) It is not until the time of PAWC’s *next* base rate case that the rate issues arising from this transaction will be the subject of a full evidentiary record and ripe for decision.[[16]](#footnote-16) It is not appropriate at this juncture to prejudge those issues, even if it means that PAWC remains at financial risk for the recovery of its costs related to this transaction until the conclusion of that next base rate case when issues such as an acquisition premium and cross subsidization will be resolved.

We expect that all rate issues relating to this transaction will be fully and fairly decided in the next base rate case. Consequently, we will direct PAWC to develop and file cost of service studies regarding this transaction in its next base rate case, as will be explained in greater detail in our disposition of OCA’s Exception No. 2 involving stormwater costs allocation.

Nonetheless, as noted, pursuant to 66 Pa. C.S. § 1103(a), the Commission will only grant a Certificate“if the Commission shall find or determine that the granting of such certificate is necessary or proper for the service, accommodation, convenience or safety of the public.” 66 Pa. C.S. § 1103(a). We note that, consistent with the elimination of the variance adjustment from the purchase price, approval of this transaction is necessary for the service, accommodation, convenience or safety of the public. The record evidence indicates that SSA’s wastewater system is under a Consent Decree with regard to deficiencies that could potentially become a safety and public health issue if not adequately addressed. As we previously indicated in detail, because we have established that PAWC is technically, legally, and financially fit to operate and maintain SSA’s combined wastewater system, including making the required improvements to address the deficiencies identified in the Consent Decree, we believe this transaction meets the public interest and affirmative benefit test.

Section 1103 states that to ensure that a transaction is in the public interest, the Commission may impose conditions in granting a Certificate that it deems to be just and reasonable. 66 Pa. C.S. § 1103(a). Pursuant to the Proposed Amended APA, we will, consistent with 66 Pa. C.S. § 1103(a), grant the Joint Applicants’ request for the Commission to conditionally approve the Joint Application pending their filing of the Proposed Amended APA. We also note that our approval of the Joint Application does not connote approval of any ratemaking aspect implicated in the Proposed Amended APA.

**b. Clarification Regarding Final Acquisition Price**

**i. Joint Applicants’ Exceptions**

In their Exception No. 2, the Joint Applicants request that the Commission clarify that an absolute final purchase price is not required for approval of the Joint Application. Joint Applicants’ Exc. at 15. The Joint Applicants assert that in their denial of the Joint Application, the ALJs made overly general statements regarding their inability to determine whether the transaction is in the public interest because the total purchase price was unknown. *Id.* at 15-16 (citing R.D. at 28-33). The Joint Applicants assert that because adjustments are usually made to the purchase price between the time of execution of the asset purchase agreements and closing, there is no way to determine an absolute final purchase price during the Commission approval process of a merger or an acquisition application. The Joint Applicants further compare the variance adjustment to adjustments made to the purchase price during the normal course of business at or following closing, requesting that the Commission acknowledge and clarify that the acquisition need not have a final or absolute purchase price in order to be approved by the Commission.[[17]](#footnote-17) According to the Joint Applicants, because the final purchase price may be reviewed in the context of a future base rate proceeding, the Commission may approve the asset purchase agreement without necessarily knowing a fixed purchase price, as long as the overall transaction is in the public interest. Joint Applicants’ Exc. at 15-18.

**ii. OCA’s Replies to Joint Applicants’ Exceptions**

In its Replies to Exceptions, the OCA requests that the Commission deny Joint Applicants’ Exception No. 2 because the examples of adjustments to the purchase price identified by the Joint Applicants are made during the normal course of business. According to the OCA, contrary to the Joint Applicants’ argument, the variance adjustment, as presented in the APA, will not be made until ten years following closing, and, therefore, cannot be regarded as a normal adjustment to the purchase price. OCA R. Exc. at 10.

**iii. I&E’s Replies to Joint Applicants’ Exceptions**

In reply to the Joint Applicants’ Exception No. 2, I&E asserts that purchase price is an essential element to any contract, especially, in a public utility setting. I&E avers as follows:

[B]oth the Supreme and the Commonwealth Courts of Pennsylvania have recognized that “[p]rice is an essential term of a contract for the transfer of property and must be sufficiently definite and certain or capable of being ascertained from the contract between parties.”

I&E R. Exc. at 7-8 (citing *Portnoy v. Brown,* 430 Pa. 401, 243 A.2d 444 (1968); *Peerless Publications, Inc. v. City of Montgomery,* 656 A.2d 547, 552 (Pa. Cmwlth. 1995)). According to I&E, the emphasis placed on the potential impact of the purchase price on PAWC and on the overall transaction by the Joint Applicants should the Commission reject their request for recovery of stormwater costs, is enough reason to ensure that the purchase price is determined in this proceeding. *Id.* at 8-9.

I&E also asserts that while the variance adjustment and the several other adjustments identified by the Joint Applicants all impact the purchase price, the variance adjustment in this case, is premised on future rate cases, which would not be known for over ten years, and could result in unintended consequences for PAWC’s ratepayers. I&E, therefore, requests that the Commission reject the variance adjustment as it is an unprecedented adjustment that could have a lasting ratemaking impact on PAWC’s existing customers. *Id.* at 10-11.

**iv. OSBA’s Replies to Joint Applicants’ Exceptions**

In its Replies to the Joint Applicants’ Exception No. 2, OSBA agrees with the ALJs’ determination that because the total purchase price will be modified by the variance adjustment, it is unknown at this time. OSBA R. Exc. at 4. OSBA explains its concurrence with the ALJs’ recommendation as follows:

As correctly noted by the ALJs “[i]f the Commission were to approve the application now, the issue of the reasonableness of the variance adjustment would already be decided when the variance adjustment amount is actually calculated. In that case, the sole issue to be determined by the Commission in the future…would be whether the variance adjustment was calculated correctly, or in accordance with the formula set forth in Section 7.07 of the APA, not whether the variance adjustment, or the final purchase price is reasonable.

OSBA R. Exc. at 5-6 (citing R.D. at 30).

**v. Disposition**

As stated above, we will grant the Joint Applicants’ request to conditionally approve the Joint Application subject to their filing of the Proposed Amended APA and the removal of the variance adjustment provisions. We believe this change in circumstances renders the Joint Applicants’ Exception No. 2 moot. Consequently, we need not address it further here.

**E. Costs Associated with Stormwater**

**1. Positions of the Parties**

**a. Joint Applicants**

The Joint Applicants requested the Commission establish in this proceeding that it has jurisdiction over combined wastewater service and conclude that, pursuant to Act 11, PAWC is eligible to recover stormwater costs in future rate case proceedings. According to the Joint Applicants, a denial of this request could result in stranded costs for PAWC and significant rate increases for SSA’s customers. The Joint Applicants continued that denial of this request would be contrary to the Commission’s regionalization goals and could result in PAWC having to pay a significant variance adjustment which they believe would not be in the public interest. Joint Applicants’ M.B. at 34-38.

According to the Joint Applicants, Act 11 provides, in pertinent part, as follows:

The commission, when setting base rates, after notice and an opportunity to be heard, may allocate a portion of the wastewater revenue requirement to the combined water and wastewater customer base if in the public interest.

*Id*. at 86-87 (quoting, in part, 66 Pa. C.S. § 1311(c)).

In acknowledgement of the ratemaking component of the Act 11 language above, the Joint Applicants explained that while the extent to which PAWC may utilize Act 11 in a future base rate proceeding may not be decided now, the Commission should, at a minimum, make a determination in this proceeding that PAWC is eligible to recover combined wastewater service costs from its customer base in a future base rate proceeding. Joint Applicants’ M.B.at 86-87.

According to the Joint Applicants, Act 11 encourages capable utilities like PAWC to acquire wastewater systems in need of capital improvement because the spreading of costs helps keeps customers’ rates at reasonable levels. To emphasize this point, the Joint Applicants quoted PAWC’s witness, Mr. Nevirauskis, as follows:

Given PAWC’s size, the needed improvements to the System will not produce an unreasonable rate impact on any PAWC customer if PAWC is permitted, as allowed by Act 11, to utilize a combined water and wastewater revenue requirement. Rather, as capital improvements are made to the System, they will be reasonably spread across PAWC’s large customer base. In future years, when capital improvements are needed for some other portion of PAWC’s system not directly related to the System, those costs will again be spread across all of PAWC’s customers, including SSA’s customers.

M.B. at 34.

Next, the Joint Applicants argued that approval of this transaction is in the public interest only if the Commission concludes that it has jurisdiction over combined wastewater service and also makes a determination that PAWC is eligible to utilize Act 11 for recovery of the combined wastewater service costs. The Joint Applicants stressed that failure of the Commission to do so could significantly impact the prospective rates of Scranton-area customers as well as the financial viability of the transaction for PAWC. *Id.* at 35-37. They also contended that failure to approve the request could result in PAWC significantly exceeding the 1.9% CAGR and having to make a substantial variance adjustment payment to SSA. *Id.* at 37-38.

The Joint Applicants also disputed I&E and the OCA’s reliance on the Commonwealth Court’s decision in *City of Lancaster – (Sewer Fund) v. Pa. PUC*, No. 1968 C.D. 2005 (Pa. Cmwlth. 2006). They averred that the Commonwealth Court’s decision was not applicable in the instant proceeding for a variety of reasons: (1) the Court’s decision is unpublished and non-binding; (2) the decision predates Act 11 and deals with municipalities offering service to jurisdictional and non-jurisdictional customers; and (3) there was no evidence that the non-jurisdictional customers would have contributed through rates to the cost of serving the jurisdictional customers. The Joint Applicants noted that PAWC can request to utilize Act 11 to enable it to spread SSA’s combined wastewater service costs across its customer base. Joint Applicants’ M.B. at 32-33.

Finally, in response to I&E and the OCA’s proposal that the Commission require a cost of service study in PAWC’s next base rate case that identifies stormwater costs, the Joint Applicants averred that there is no need for such a study because the record evidence in this case does not support cost allocation among PAWC customers. The Joint Applicants continued that while PAWC is not seeking a predetermination of a rate claim for a combined water and wastewater revenue requirement under Act 11 in this proceeding, PAWC is only seeking a Conclusion of Law that because combined wastewater service is a Commission-jurisdictional wastewater service, PAWC should be allowed to utilize Act 11 for stormwater cost recovery in a future base rate proceeding. The Joint Applicants concluded that because the opposing Parties’ proposal will be adequately addressed in a future base rate proceeding, it should be rejected. *Id*. at 34-35 and 39-40.

**b. I&E**

In its opposition to the Joint Applicants’ request, I&E asserted that no jurisdictional investor-owned utility currently operates a combined wastewater and stormwater system, or has requested the recovery of stormwater costs from the Commission. I&E averred there is currently only one Commission-regulated municipal system, the City of Lancaster, that operates a combined system, and the Commission, in *Lancaster*, has determined that stormwater costs cannot be recovered from the jurisdictional customers of the municipal system. I&E M.B. at 7-10. I&E asserted that, in *Lancaster*, consistent with the OCA’s argument that the costs associated with stormwater service are not recoverable from customers residing outside the city as they are not utility costs, the ALJ determined as follows:

[S]ince stormwater enters the City’s combined sewer system through approximately 2,000 stormwater inlets and that when this stormwater is moved with wastewater to the treatment plant, increased pumping and treatment costs are the result. The ALJ further recommended that the costs associated with collecting, conveying, pumping and treating this stormwater are not properly recoverable from jurisdictional customers and must be removed before a proper allocation can be performed between jurisdictional and non-jurisdictional customers.

I&E M.B. at 10, citing *Lancaster* at 15-16. According to I&E, the Commission agreed with the ALJ, stating as follows:

We conclude that there is substantial record evidence that the City’s combined wastewater system collects stormwater runoff, and that when this stormwater is moved within the City’s system, costs related to operation of the treatment plant and pumping stations are increased.

I&E at 11 (citing *Lancaster* at 17). I&E contended that similar to *Lancaster,* PAWC’s current customers in other parts of the Commonwealth would not benefit from the City’s stormwater service and should not be made to pay for such services. I&E M.B. at 11-12.

I&E also questioned the cost-sharing benefits of this acquisition as it pertains to PAWC’s existing customers. I&E expressed concern over PAWC’s testimony regarding the benefits of cost-sharing to PAWC’s existing customers. According to I&E, PAWC’s testimony that “over time these things will even out as they [SSA’s customers] share in the costs of other wastewater systems, and ultimately other water system investment . . . ,” is concerning. I&E R.B. at 4. I&E submitted that irrespective of the fact that failure of the Commission to grant PAWC’s request may result in an increase in SSA’s wastewater customers’ rates, stranded costs for PAWC, and significant variance adjustment payment, as claimed by PAWC, if PAWC’s current customers would not benefit from the stormwater service in question, they should not be made to pay for such services. *Id.* at 8-14.

Finally, I&E concluded that to ensure stormwater costs are not spread to PAWC’s existing customers, the Commission should direct PAWC to provide a cost of service study in its next base rate case separating sanitary sewer and stormwater flows, along with the capital expense and operating costs for the two functions. [[18]](#footnote-18) I&E M.B. at 11-12; I&E R.B. at 2.

**c. OCA**

The OCA also opposed PAWC’s proposal. The OCA echoed I&E’s arguments that the Commission’s approval of the Joint Applicants’ request must be conditioned upon a requirement for PAWC to develop separate rates and charges proportional to its customers’ contribution of stormwater to the wastewater system. OCA M.B. at 41. According to the OCA, cost allocation is important in this case since a significant portion of the costs of plant improvements required in the Consent Decree will be expended on SSA’s stormwater system and the fact that PAWC’s current water and wastewater customers reside in municipalities that are providing and paying for stormwater costs.[[19]](#footnote-19) *Id.* at 42-43.

Furthermore, the OCA contended that the Joint Applicants’ reliance on Act 11 in their pre-approval request is an attempt to expand the intent and plain language of Section 1311(c) and should be denied. The OCA noted that Section 1311(c) was amended as part of Act 11 to encourage the acquisition of small failing wastewater systems with few customers by larger water utilities in order to enhance necessary improvements on the small systems. The OCA continued that the amendment of Section 1311(c) was not intended to encourage the acquisition of a large system such as SSA’s combined wastewater system. OCA R.B. at 23-24. The OCA averred that even if the Commission rules that combined wastewater service is a jurisdictional service, there is no basis for the Commission to make a determination of PAWC’s future stormwater rate recovery in the instant proceeding. *Id.* at 24-27.

**2. ALJs’ Recommendation**

The ALJs did not address PAWC’s request for pre-approval to recover stormwater costs in their Recommended Decision in light of their recommendation that the Commission deny the Joint Application.

**3. Exceptions and Replies**

**a. OCA’s Exceptions**

In its Exception No. 2, the OCA avers that the ALJs erred in failing to address the need for separate allocation of stormwater costs. The OCA asserts that if the Commission makes a determination that it has jurisdiction over the proposed acquisition, the sewage and stormwater rates must be separately allocated and that failure to do so would be harmful to PAWC’s existing customers. OCA Exc. at 8-9. The OCA argues that the Joint Applicants’ request to recover stormwater costs from PAWC’s existing customers ignores the fact that stormwater customers are not the same as wastewater customers and the Commission sets stormwater rates differently from the way it sets water and wastewater rates. Particularly, the OCA notes that pursuant to the Code, rates are set on a cost and cost-causation basis, hence, the Joint Applicants’ request to recover stormwater costs from PAWC’s existing customers is contrary to the principles of cost-causation and cost-based ratemaking. *Id.* at 10-12. According to the OCA, approval of PAWC’s request would result in PAWC’s water and wastewater customers paying for the stormwater costs of the City and the Borough, as well as the improvements required under the Consent Decree. The OCA asserts that stormwater costs make up over 85% of the capital improvement costs that are required under the Consent Decree, and are equivalent to approximately $144 million per 2012 dollars. The OCA, therefore, proposes that the Commission should, if it elects to approve the request, require PAWC to separately allocate stormwater costs so that PAWC’s customers can be properly charged for cost of service. *Id.* at 12. The OCA also suggests that the City and SSA consider charging separate stormwater fees which, according to the OCA, are employed by many municipalities including the City of Philadelphia. *Id.* at 12-13.

**b. I&E’s Replies to OCA’s Exceptions**

In response to the OCA’s Exception No. 2, I&E acknowledges that the ALJs did not address PAWC’s request to recover stormwater costs due to their denial of the Joint Application. I&E, however, states that should the Commission decide to reverse the ALJs’ recommendation and approve the Joint Application, the Commission must address this issue in the instant proceeding. I&E, like the OCA, also asserts that while it requests that the Commission deny PAWC’s pre-approval request, if the Commission elects to approve the Joint Application, it should direct PAWC to develop a separate cost of service study to isolate stormwater costs. This, according to I&E, will protect PAWC’s existing customers from paying SSA’s stormwater service costs to which they are not beneficiaries. I&E R. Exc. at 21-24 (citing I&E M.B. at 9-14 and I&E R.B. at 6‑11).

**c. Joint Applicants’ Replies to OCA’s Exceptions**

In their Replies to OCA Exception No. 2, the Joint Applicants agree with the ALJs’ decision not to address this issue. The Joint Applicants assert that the ALJs did not direct the allocation of stormwater costs as a result of their determination that combined storm/wastewater service is jurisdictional and, therefore, there is no need to differentiate wastewater from stormwater service, especially with regard to cost allocation. They further submit that the instant proceeding is not the appropriate place to address such ratemaking issues. Joint Applicants’ R. Exc. at 12-13. The Joint Applicants assert that the OCA’s arguments for cost allocation are not supported by any binding legal authority but are simply opinions of its witnesses on how they believe stormwater costs should be billed and collected. *Id.* at 13.

Additionally, in response to the OCA’s proposal regarding separate stormwater fees, the Joint Applicants aver that even in the few instances where certain municipalities or municipal authorities have been granted limited authority to impose stormwater fees, the administration of such fees tend to be complex, time-consuming, and expensive, which is in stark contrast to the Commission’s regulation of combined water/wastewater service. The Joint Applicants assert that the Commission’s regulation of combined storm/wastewater service is fair, straightforward, and permitted under Pennsylvania law. The Joint Applicants assert that the OCA’s proposal would deprive investor-owned utilities from acquiring combined storm/wastewater systems despite the fact that such acquisitions are permitted by Pennsylvania law and are in the public interest. The Joint Applicants, therefore, request that the Commission reject the OCA’s cost of service study proposal. *Id*. at 13-14.

**4. Disposition**

Based on our review of the record, the positions of the Parties, and the applicable law, we will grant, in part, OCA’s Exception No. 2 and deny the Joint Applicants’ request that the Commission pre-approve, in this proceeding, PAWC’s ability to recover stormwater costs from its combined water and sewer customer base in the future pursuant to Act 11.

Specifically, the Joint Applicants’ in their request for approval to utilize Act 11 in a future base rate proceeding stated as follows:

[T]he applicability of Act 11 to Combined Wastewater service [is] so fundamental to this Transaction that [it] must be resolved in this proceeding and cannot wait until a future PAWC base rate proceeding.

Joint Applicants’ M.B. at 35.

However, as previously noted by the Joint Applicants, Act 11 provides, in pertinent part, as follows:

The commission, when setting base rates, after notice and opportunity to be heard, *may* allocate a portion of the wastewater revenue requirement to the *combined water and wastewater* customer base if in the public interest.

66 Pa. C.S. §1311(c) (emphasis added).

The Joint Applicants, in recognition of the ratemaking language in Act 11 above, indicated they are only requesting that the Commission predetermine PAWC’s ability to, and not the extent to which it can, utilize Act 11 to recover combined stormwater and wastewater costs in a future base rate proceeding. Joint Applicants’ M.B. at 86-87. Nevertheless, it is clear that the approval requested by the Joint Applicants is a traditional ratemaking issue that should be reserved for a future base rate proceeding when the Commission is provided with a full evidentiary record on ratemaking issues. We note that what is before us in this proceeding is an acquisition application pursuant to Sections 1102 and 1103, 66 Pa. C.S. §§ 1102 and 1103. As we have stated, it would be premature for us to prejudge PAWC’s eligibility to recover the costs at issue absent a rate request from PAWC and PAWC’s presentation of a revenue requirement before the Commission. While we are cognizant of the rate recovery issues associated with utility acquisitions or mergers, the record in this case does not contain sufficient evidence to enable us to make any determination of PAWC’s eligibility to recover stormwater costs or to evaluate the specific effects of the acquisition on PAWC’s revenue requirement and rate design matters.

We also note the Joint Applicants alluded, *inter alia,* to the variance adjustment payment as a key reason for their request for the cost recovery. The Joint Applicants, in an effort to emphasize this point, stated as follows:

Likewise, if PAWC is unable to request Commission authorization to spread the costs of the Combined Wastewater service under Act 11, an important component of the Transaction would be undermined and PAWC could have to pay a significant Variance Adjustment (i.e., a purchase price adjustment based upon the 1.9% compound annual growth rate (“CAGR”) as set forth in Section 7.07 of the APA.

Joint Applicants’ M.B. at 8.

However, as we stated earlier, the Joint Applicants have proposed to amend the APA and to eliminate the variance adjustment from the purchase price in the APA. They have also proposed that the Commission conditionally approve the Joint Application pending their filing of the Proposed Amended APA. Consequently, because we will approve the Proposed Amended APA, we need not address PAWC’s request to recover stormwater costs from its existing customer base on the basis of the variance adjustment.

With regard to OCA’s Exception No. 2, both the OCA and I&E urge that stormwater costs be separately billed, apart from water and wastewater rates, to prevent the unfair burdening of existing PAWC water and wastewater customers with the capital and operating costs of treating stormwater runoff in the City and the Borough. The OCA further argues that as part of this approval, the Commission should require separated rates in order to ensure that there will be no harm to existing PAWC customers. OCA Exc. at 8-9, 10-13; OCA R.B. at 22; I&E R. Exc. at 21-24. Although, we decline to formally address specific rate issues in this proceeding, we believe that the issue of stormwater cost recovery is important and should be afforded full and complete consideration by the Commission in PAWC’s next base rate case.[[20]](#footnote-20)

The Commission has some experience with stormwater cost recovery,[[21]](#footnote-21) but not of the magnitude involved here.[[22]](#footnote-22) As with all rate design issues, the basis of rate setting is a cost of service study. The absence of a study designed with specific direction to address recovery of stormwater costs as a separate class would be an impediment to the full development of this issue in PAWC’s next base rate proceeding. As noted by I&E, “[a] separate cost of service study would provide ratemaking solutions to this stormwater issue by potentially charging SSA customers or the City for these stormwater costs.” I&E M.B. at 12.

Accordingly, we shall direct PAWC to develop and file cost of service studies in its next base rate case, pursuant to Section 53 of our Regulations, 52 Pa. Code § 53.53, Exhibit D, Section VIII, to allow both the rate limitation and stormwater costs allocation issues to be fully vetted within the nine-month time constraint of a fully litigated base rate case. First, we shall direct that PAWC include a cost of service study that fully separates the costs of providing stormwater services in the SSA service area. Moreover, PAWC shall address the pros and cons of designing stormwater rates on this separated basis.

Second, PAWC shall file a cost of service study that removes all costs and revenues associated with the SSA operations (both wastewater and stormwater) and, using the same rate design methodology it proposes be adopted in the case, develop rates that exclude the impact of the SSA acquisition included in the base rate filing. These studies will enable the parties in the next base rate case and this Commission to better evaluate the rate impacts of this transaction on PAWC’s existing customers. Both studies shall be submitted at the time of filing the next base rate case. The requirement of filing these two items is not intended to limit or affect what PAWC may propose as rates or the positions that it or any party, including the Commission, may take.

**E. Public Utility Municipal Contracts/Agreements**

**1. Positions of the Parties**

**a. Joint Applicants**

The Joint Applicants requested that the Commission should, in conjunction with its approval of the APA and the Joint Application, also approve the municipal agreements to be assumed by PAWC pursuant to the terms of the APA, and authorize PAWC to file a compliance tariff supplement consistent with the *pro forma* tariff supplement.[[23]](#footnote-23) Joint Applicants’ M.B. at 58.

On July 1, 2016, the Joint Applicants filed seven unsigned *pro forma* agreements, along with *pro forma* assignment and assumption agreements (A&A agreements), pursuant to Section 507 of the Code, 66 Pa. C.S. § 507, seeking Commission approval of the agreements. The *pro forma* agreements are agreements between PAWC and SSA in which PAWC agrees to assume contractual obligations of SSA. The contractual obligations are agreements between SSA and various entities concerning the acquisition of facilities or the provision of services by SSA. The agreements are as follows:

Interjurisdictional Agreement Between The Sewer Authority of The City of Scranton and The Borough of Dickson City, Pennsylvania, dated April 14, 2003;

Interjurisdictional Agreement Between The Sewer Authority of The City of Scranton and The Borough of Taylor, Pennsylvania, dated April 9, 2003;

Interjurisdictional Agreement Between The Sewer Authority of The City of Scranton and The Borough of Moosic, Pennsylvania, dated May 13, 2003;

Agreement for the Acceptance, Conveyance, Treatment, and Disposal of Wastewater Received from the Siniawa Enterprises Wastewater Collection System at the Scranton Wastewater Collection System and Wastewater Treatment Plant, as of June 14, 1989;

Agreement for the Acceptance, Conveyance, Treatment, and Disposal of Wastewater Received from the Montage, Inc. Wastewater Collection System at the Scranton Wastewater Collection System and Wastewater Treatment Plant, as of July 24, 2003;

Agreement Providing for Uniformity of Charges Applicable to Residents of Taylor Borough and Residents of the City of Scranton, as of January 12, 1976; and,

Agreement for the Transfer, Conveyance, and Acceptance of the Davis Street, Greenwood Avenue, and Corey Street Sanitary Sewer Conveyance Line from Moosic Borough to the Sewer Authority of the City of Scranton, as of April 16, 2008.

Joint Applicants’ M.B at 58-59.

According to the Joint Applicants, approval of the A&A agreements and the municipal agreements would help PAWC maintain existing relationships with neighboring municipalities, recognize geographic limitations on service, and improve efficiency of service. The Joint Applicants requested that the Commission issue Certificates of Filing for the agreements upon PAWC’s filing of executed versions of the A&A agreements which are substantially similar in all material respects to the *pro forma* A&A agreements. *Id.* at 59.

**b. Other Parties’ Positions**

None of the other Parties opposed the approval of the municipal agreements filed by the Joint Applicants.

**2. ALJs’ Recommendation**

The ALJs did not address the municipal agreements in their Recommended Decision consistent with their denial of the Joint Application.

**3. Exceptions and Replies**

**a. Joint Applicants’ Exceptions**

In their Exception No. 4,[[24]](#footnote-24) the Joint Applicants request that the Commission conditionally approve the Joint Application, including the municipal agreements filed pursuant to Section 507 of the Code, 66 Pa. C.S. § 507, pending PAWC’s filing of the Proposed Amended APA and PAWC’s filing of executed versions of the agreements, at which time the Commission can issue a certificate of filing for the APA and the seven agreements. The Joint Applicants assert that approval of the municipal agreements pursuant to 66 Pa. C.S. § 507 is required for closing of the transaction. The Joint Applicants further assert that the seven *pro forma* municipal agreements filed on July 1, 2016, were unsigned because PAWC was still moving the agreements through the municipal approval process.[[25]](#footnote-25) Joint Applicants’ Exc. at 22-23.

**b. OCA’s Replies to Joint Applicants’ Exceptions**

In reply to the Joint Applicants’ Exception No. 4, the OCA rejects the Joint Applicants’ request, stating that it is premised on a false assumption that the only issue with the APA and the Joint Application is the variance adjustment. OCA R. Exc. at 18. The OCA outlines several reasons it believes there are several other areas of the APA that are problematic. First and foremost, the OCA alleges that in addition to the purchase price and variance adjustment, the transaction is expected to cost PAWC’s existing ratepayers $146 million to $199 million over the next twenty years in stormwater-related capital improvements and subsidies. According to the OCA, the thirty year projection of this transaction, without adjusting for PAWC’s higher cost of capital, is in excess of $300 million. *Id.*

The OCA asserts that the benefits claimed by the Joint Applicants that would result from this acquisition are overstated and lacking. The OCA argues that eliminating the variance adjustment from the transaction does not diminish the fact that the detrimental effects of this acquisition outweigh the alleged benefits and, thus, there is no basis to approve the APA or issue Certificates of Filing for the seven agreements. *Id.* at 18-19.

**4. Disposition**

Based on our review of the record, the positions of the Parties, and the applicable law, we will grant the Joint Applicants’ Exception No. 4 and conditionally approve the municipal agreements, subject to the Joint Applicants’ filing of executed versions of all the agreements. Although the ALJs did not address the municipal agreements in their Recommended Decision, they denied the Joint Application consistent with their conclusion that the variance adjustment in the APA was unreasonable and not in the public interest. However, the Joint Applicants have proposed to eliminate the variance adjustment from the APA. They have also proposed to file executed municipal agreements with the Commission. Additionally, we note that the OCA did not find issue with the municipal agreements. Rather, the OCA’s rejection of the Joint Applicants’ Exception No. 4 is based on its disagreement with the APA. Nevertheless, we have addressed the public benefit issues of this transaction and have made a determination that pursuant to the Joint Applicants’ Proposed Amended APA, the transaction is in the public interest. We, therefore, see no reason to deny the Joint Applicants’ request for a conditional approval of the municipal agreements.

As noted, Section 507 of the Code, 66 Pa. C.S. § 507, is applicable in the review of the agreements filed by the Joint Applicants.[[26]](#footnote-26) We shall therefore, approve the subject agreements pursuant to Section 507 of the Code, 66 Pa. C.S. § 507, conditioned upon the Joint Applicants’ filing the Proposed Amended APA and the subject executed municipal agreements. Additionally, in order to enable the Commission to track future proceedings involving the municipal agreements, we will also, as a matter of administrative efficiency, direct the Joint Applicants to file the executed municipal agreements under separate “U” docket numbers.

**IV. Conclusion**

Based on our review of the record, and consistent with the foregoing discussion we shall: (1) grant, in part, the OCA’s Exceptions, (2) grant, in part, the Joint Applicants’ Exceptions; (3) modify the ALJs’ Recommended Decision; (4) conditionally grant the Joint Application, pending the Joint Applicants’ filing of the Proposed Amended APA; (5) direct PAWC to file a cost of service study in its next base rate case that fully separates the costs of providing stormwater services in the SSA service area, and to address the pros and cons of designing rates on this separated basis; (6) direct PAWC to file a cost of service study in its next base rate case that, using the same rate design methodology it proposes be adopted in the case, removes all costs and revenues associated with the SSA operations (both sewer and stormwater) from the proposed rates and develops rates that exclude the impact of the SSA acquisition; and (7) conditionally approve the *pro forma* municipal agreements, subject to the Joint Applicants’ filing of executed municipal agreements, all consistent with this Opinion and Order; **THEREFORE,**

**IT IS ORDERED:**

1. That the Exceptions filed by the Office of Consumer Advocate on September 2, 2016, are granted, in part, and denied, in part, consistent with this Opinion and Order.

2. That the Exceptions filed by Pennsylvania-American Water Company and the Sewer Authority of the City of Scranton are granted, in part, and denied, in part, consistent with this Opinion and Order.

3. That the Recommended Decision of Administrative Law Judges David A. Salapa and Steven K. Haas, issued on August 24, 2016, is modified, consistent with this Opinion and Order.

4. That the Joint Application filed by Pennsylvania-American Water Company and the Sewer Authority of the City of Scranton is conditionally granted, subject to the condition that Pennsylvania-American Water Company and the Sewer Authority of the City of Scranton file with the Commission, within ten days of the entry of this Opinion and Order, a compliance filing containing the Proposed Amended Asset Purchase Agreement, consistent with Appendix Ato the Pennsylvania-American Water Company and the Sewer Authority of the City of Scranton’s Replies to Exceptions.

5. That upon the filing of an acceptable Asset Purchase Agreement Compliance Filing, the Commission's Secretary issue a Certificate of Public Convenience evidencing Pennsylvania-American Water Company’s right under Sections 1102(a)(1) and 1102(a)(3) of the Pennsylvania Public Utility Code, 66 Pa. C.S. §§ 1102(a)(1) and 1102(a)(3), to (a) acquire, by sale, 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 (b) begin to offer or furnish wastewater service, which includes combined storm/wastewater service, to the public in the City of Scranton and the Borough of Dunmore, Lackawanna County, Pennsylvania.

6. That upon the filing of an acceptable Asset Purchase Agreement Compliance Filing, the Commission's Secretary issue a Certificate of Filing under Section 507 of the Pennsylvania Public Utility Code, 66 Pa. C.S. § 507, for the Asset Purchase Agreement By and Between The Sewer Authority of the City of Scranton, as Seller, and Pennsylvania-American Water Company, as Buyer, dated March 29, 2015.

7. That the *pro forma* municipal agreements submitted by Pennsylvania-American Water Company and the Sewer Authority of the City of Scranton are conditionally approved, subject to the filing of executed municipal agreements.

8. That upon the filing of acceptable executed versions of assignment and assumption agreements which are substantially-similar in all material respects to the *pro forma* assignment and assumption agreements filed with the Commission on July 1, 2016, the Commission’s Secretary issue Certificates of Filing under Section 507 of the Pennsylvania Public Utility Code, 66 Pa. C.S. § 507, for the following agreements:

a. Interjurisdictional Agreement Between The Sewer Authority of The City of Scranton and The Borough of Dickson City, Pennsylvania, dated April 14, 2003 (as will be assigned and assumed by an assignment and assumption agreement which is substantially-similar in all material respects to the pro forma assignment and assumption agreement filed with the Commission on July 1, 2016);

b. Interjurisdictional Agreement Between The Sewer Authority of The City of Scranton and The Borough of Taylor, Pennsylvania, dated April 9, 2003 (as will be assigned and assumed by an assignment and assumption agreement which is substantially-similar in all material respects to the pro forma assignment and assumption agreement filed with the Commission on July 1, 2016);

c. Interjurisdictional Agreement Between The Sewer Authority of The City of Scranton and The Borough of Moosic, Pennsylvania, dated May 13, 2003 (as will be assigned and assumed by an assignment and assumption agreement which is substantially-similar in all material respects to the pro forma assignment and assumption agreement filed with the Commission on July 1, 2016);

d. Agreement for the Acceptance, Conveyance, Treatment, and Disposal of Wastewater Received from the Siniawa Enterprises Wastewater Collection System at the Scranton Wastewater Collection System and Wastewater Treatment Plant, as of June 14, 1989 (as will be assigned and assumed by an assignment and assumption agreement which is substantially-similar in all material respects to the pro forma assignment and assumption agreement filed with the Commission on July 1, 2016);

e. Agreement for the Acceptance, Conveyance, Treatment, and Disposal of Wastewater Received from the Montage, Inc. Wastewater Collection System at the Scranton Wastewater Collection System and Wastewater Treatment Plant, as of July 24, 2003 (as will be assigned and assumed by an assignment and assumption agreement which is substantially-similar in all material respects to the pro forma assignment and assumption agreement filed with the Commission on July 1, 2016);

f. Agreement Providing for Uniformity of Charges Applicable to Residents of Taylor Borough and Residents of the City of Scranton, as of January 12, 1976 (as will be assigned and assumed by an assignment and assumption agreement which is substantially-similar in all material respects to the pro forma assignment and assumption agreement filed with the Commission on July 1, 2016); and,

g. Agreement for the Transfer, Conveyance, and Acceptance of the Davis Street, Greenwood Avenue, and Corey Street Sanitary Sewer Conveyance Line from Moosic Borough to the Sewer Authority of the City of Scranton, as of April 16, 2008 (as will be assigned and assumed by an assignment and assumption agreement which is substantially-similar in all material respects to the pro forma assignment and assumption agreement filed with the Commission on July 1, 2016).

9. That the executed municipal agreements shall be filed under separate “U” docket numbers.

10. That within ten days after the closing of the transaction, Pennsylvania-American Water Company shall file a compliance tariff supplement consistent with the *pro forma* tariff supplement attached as Appendix D to the Main Brief of Pennsylvania-American Water Company and the Sewer Authority of the City of Scranton, to become effective on the same date as issuance.

11. That at the time of filing its next base rate case, Pennsylvania-American Water Company shall submit a cost of service study that fully separates the costs of providing stormwater services in the service area of the Sewer Authority of the City of Scranton and addresses the pros and cons of designing rates on this separated basis, consistent with the discussion in this Opinion and Order.

12. That at the time of filing its next base rate case, Pennsylvania-American Water Company shall submit a cost of service study that removes all costs and revenues associated with the operations (both wastewater and stormwater) of the Sewer Authority of the City of Scranton and, using the same rate design methodology it proposes be adopted in that case, develop rates in its next base rate case that exclude the impact of the Sewer Authority of the City of Scranton acquisition, consistent with the discussion in this Opinion and Order.

13. That any directive, requirement, disposition or the like contained in the body of this Opinion and Order that is not the subject of an individual Ordering Paragraph, shall have the full force and effect as if fully contained in this part.

14. That upon compliance by the parties with the terms of this Opinion and Order, this matter be marked closed.

**BY THE COMMISSION,**

Rosemary Chiavetta

Secretary

(SEAL)

ORDER ADOPTED: October 6, 2016

ORDER ENTERED: October 19, 2016

1. The Joint Applicants averred that approval of the Joint Application would go a long way in addressing the long-term financial problems of the City of Scranton and the Borough of Dunmore. According to the Joint Applicants, the City has been operating under the protection of the Municipalities Financial Recovery Act, Act of 1987, P.L. 246, No. 47 (Act 47) for the past twenty-five years, during which the management of its business affairs has been under the review of an independent coordinator. Joint Application at 4. [↑](#footnote-ref-1)
2. The Joint Applicants averred that the IPP-S would not be reviewed and approved by the Commission, but would be submitted for review and approval by the Pennsylvania Department of Environmental Protection (DEP) as part of the National Pollutant Discharge Elimination System (NPDES) Permit for SSA’s wastewater system. [↑](#footnote-ref-2)
3. MS4 stands for Municipal Separate Storm Sewer System. [↑](#footnote-ref-3)
4. The Sewage Facilities Act, 35 P.S. §§ 750.1, *et seq*., provides the following:

   Sewage means 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 under the act of June 22, 1937 (P.L. 1987, No. 394), known as “The Clean Streams Law,” as amended.

   35 P.S. § 750.1. [↑](#footnote-ref-4)
5. Act 11, *inter alia*, amended 66 Pa. C.S. § 1311(c) to permit the Commission to allocate a portion of the wastewater revenue requirement to the combined water and wastewater customer base of a utility that provides both water and wastewater service, if in the public interest. [↑](#footnote-ref-5)
6. Per PAWC’s current tariff, under PAWC’s Rate Zone 1 wastewater rates, an average residential customer using 3,000 gallons of water per month pays approximately $46, while an SSA wastewater residential customer pays approximately $35. [↑](#footnote-ref-6)
7. Under the terms of the APA, PAWC will either pay the variance adjustment directly to the then customers in the SSA service area, or it will make the payment directly to the SSA which, in turn, will distribute the payment, via a third party administrator, to those customers. The ALJs agreed with I&E that both payments would violate 66 Pa. C.S. § 1303, which states as follows:

   **§ 1303. Adherence to tariffs.**

   No public utility shall, directly or indirectly, by any device whatsoever, or in anywise, demand or receive from any person, corporation, or municipal corporation a greater or less rate for any service rendered or to be rendered by such public utility than that specified in the tariffs of such public utility applicable thereto. The rates specified in such tariffs shall be the lawful rates of such public utility until changed, as provided in this part. Any public utility, having more than one rate applicable to service rendered to a patron, shall, after notice of service conditions, compute bills under the rate most advantageous to the patron.

   R.D. at 34-37 (citing 66 Pa. C.S. § 1303). [↑](#footnote-ref-7)
8. Section 1304 provides the following:

   No public utility shall, as to rates, make or grant any unreasonable preference or advantage to any person, corporation, or municipal corporation, or subject any person, corporation, or municipal corporation to any unreasonable prejudice or disadvantage. No public utility shall establish or maintain any unreasonable difference as to rates, either as between localities or as between classes of service. [↑](#footnote-ref-8)
9. *See* Joint Applicants’ Exc. at 3-8, for examples of Commission-approved acquisition applications with arms-length negotiated purchase prices. [↑](#footnote-ref-9)
10. The OCA disagrees, stating that the automatic adjustment clause is a true-up of certain expenses on an annual basis while the variance adjustment in this case is a shifting of costs from one group of customers to another. OCA R. Exc. at 8-9. [↑](#footnote-ref-10)
11. According to the OCA, Schedule 7.07(d) of the APA describes the calculation of the starting level of revenues at the time of acquisition (Year 0). It then discusses the revenue calculation in Year X, *i.e.,* a time period after the acquisition. The Year X revenue calculation is described as follows: “Calculate Wastewater Revenue from Scranton System Wastewater Customers at Year X (*based on Year 0 billing determinants* and Commission approved rates in Year X) = Year X Revenue.” OCA Exc. at 15 (emphasis added). [↑](#footnote-ref-11)
12. The Proposed Amended APA reflecting an amendment to Section 7.07(d) of the APA, stipulates as follows:

    During the ten-year period following the Closing subsequent to the first base rate case filed by Buyer after the Effective Date as described in Section 7.07(c) above, subject to Pa PUC approval and applicable Law, Buyer shall not propose any Rate Increases to be applicable to wastewater customers in the Service Area that would, taking into account all relevant facts and circumstances at such time, reasonably be expected to result in a cumulative positive difference over that ten-year period between (i) the annual revenues associated with the provision of wastewater service to customers in the Service Area calculated at PaPUC rates in accordance with Schedule 7.07(d) and (ii) a 1.9% [CAGR] Rate Increase in annual revenues associated with the provision of wastewater service to customers in the Service Area over that ten-year period relative to the starting amount of annual revenues calculated in accordance with Schedule 7.07(d). However, the Parties acknowledge that Buyer shall have the reasonable discretion to address and agree to Rate Increases for wastewater customers in the Service Area in the context of settlement of a particular Rate Increase proceeding, subject to Pa PUC approval and applicable law.

    Joint Applicants’ R. Exc., Appendix A at 57. [↑](#footnote-ref-12)
13. According to the OCA, SSA’s balance sheet as of March 31, 2015, places the book value for the wastewater plant at approximately $74 million and PAWC is not acquiring SSA’s entire assets, so the actual book value of the assets PAWC is acquiring is actually less than $74 million. OCA M.B. at 33. [↑](#footnote-ref-13)
14. Our determination in this regard, however, does not affect the requirement that PAWC file an original cost study of the acquired system’s assets consistent with the Commission’s policy statement at 52 Pa. Code § 69.721(f). [↑](#footnote-ref-14)
15. *See* Finding of Fact (FOF) No. 36. [↑](#footnote-ref-15)
16. As noted, the APA contains an agreement that PAWC will not “implement” a rate increase for SSA customers “prior to January 1, 2018.” R.D. at 9, FOF No. 40. This is a rates effective stay-out, as opposed to a rate filing stay-out. The APA also limits the magnitude of increases that *PAWC may* *propose* for SSA’s customers through a multi-year period, but does not restrict any other party’s rate case position or bind the Commission in any way. *See,* for example, R.D. at 9-10, FOF Nos. 40-42; Joint Applicants’ M.B. at 84-85. [↑](#footnote-ref-16)
17. These adjustments include cash on hand, indebtedness levels at closing and compensation changes as of closing. Joint Applicants’ Exc. at 16-17. [↑](#footnote-ref-17)
18. I&E contended that the cost of service study would provide ratemaking solutions in a future base rate case proceeding involving the recovery of stormwater related costs. I&E M.B. at 12-13. [↑](#footnote-ref-18)
19. The OCA indicated that out of the estimated $169 million investment costs needed for the LTCP, approximately $144 million, plus a significant portion of the $25 million for the wastewater treatment plant upgrade for BNR and Combined Sewer Overflow (CSO) control, is related to stormwater control. OCA M.B. at 42. [↑](#footnote-ref-19)
20. In this case, stormwater costs include costs associated with street sweeping and catch basin cleaning in the areas serviced by the combined system that PAWC has agreed to undertake in the purchase agreement. [↑](#footnote-ref-20)
21. *See* *Pa. P.U.C. v. City of Lancaster Sewer Fund*, Docket No. R-2012-2310366 (Order entered April 18, 2013) and *Lancaster Remand.*  [↑](#footnote-ref-21)
22. I&E states that this represents a case of first impression. I&E M.B. at 9. [↑](#footnote-ref-22)
23. The *pro forma* tariff supplement which incorporates the Industrial Pretreatment Program (IPP) in the Scranton Area to PAWC’s Commission-approved tariff, pursuant to the municipal agreements, was attached as Appendix D to the Joint Applicants’ Main Brief. [↑](#footnote-ref-23)
24. We note that this Exception is mistakenly labeled “Joint Applicants’ Exception No. 5” in the Joint Applicants’ Exceptions. [↑](#footnote-ref-24)
25. The Joint Applicants assert that should any of the agreements change, PAWC would file the changed agreement for the Commission to review. Joint Applicants’ Exc. at 23. [↑](#footnote-ref-25)
26. Pursuant to Section 507, contracts or agreements between a public utility and a municipal corporation, except contracts to furnish service at regular tariff rates, must be filed with the Commission at least thirty days prior to the effective date of the contract or agreement. In determining whether to approve such agreements, the Commission will consider the reasonableness, legality, or any other matter affecting the validity of the agreement. 66 Pa. C.S. § 507. [↑](#footnote-ref-26)