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December 21, 2018

RE: Hidden Valley Foundation, Inc.
-Pa. Public Utility Commission
v. Hidden Valley Utility Services, L.P.
(Docket Nos. R-2018-3001306 and
R-2018-3001307)
Our File 5996

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

Dear Secretary Chiavetta:

Enclosed for filing is Hidden Valley Foundation, Inc.'s Reply Brief in the above-referenced proceeding.

Copies have been served on the parties as indicated on the enclosed Certificate of Service.

Sincerely yours,

VUONO & GRAY, LLC

William H. Stewart III

Enclosures
cc: Hidden Valley Foundation, Inc.
Honorable Mark A. Hoyer
Honorable Katrina L. Dunderdale
Per Certificate of Service

/00215705.1

CERTIFICATE OF SERVICE

Re:	Pennsylvania Public Utility Commission	:	
	v.	:	Docket Nos. R-2018-3001306
	Hidden Valley Utility Services, L.P.	:	R-2018-3001307
	Water and Wastewater	:	

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

Dated this 21st day of December 2018.

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY COMMISSION	:	
	:	DOCKET NO. R-2018-3001306
v.	:	
HIDDEN VALLEY UTILITY SERVICES, L.P. – WATER	:	
PENNSYLVANIA PUBLIC UTILITY COMMISSION	:	
	:	DOCKET NO. R-2018-3001307
v.	:	
HIDDEN VALLEY UTILITY SERVICES, L.P. – WASTEWATER	:	

REPLY BRIEF OF HIDDEN VALLEY FOUNDATION, INC.

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I. INTRODUCTION AND SUMMARY OF ARGUMENT

In its main brief, Hidden Valley Utility Services, L.P. ("HVUS" or the "Company") characterizes this case as a classic "Catch-22" situation, arguing that the Company must be granted rate relief in order for it to be able to comply with the Commission's decisions in *McCloskey v. Hidden Valley Utility Services, L.P.*, Docket Nos. C-2014-2447138 and C-2014-2447169 ("*McCloskey*" or "*McCloskey* Decisions"), which require HVUS to make extensive costly improvements to its water and wastewater systems within a limited time frame. What HVUS fails to acknowledge, is that the "Catch-22" situation the company finds itself in today is completely self-inflicted and that the Company has no one to blame but its own management for its current predicament.

Had HVUS complied with the Commission's Order in the 2004 application proceeding ("2005 Order")[1], instead of waiting until 2018 to finally comply with the 2005 Order, the Company would not be in this situation. Had HVUS raised rates gradually through prior rate proceedings (instead of waiting until 2018 to file rate proceedings) and used the proceeds from those rate increases to comply with the terms of the 2005 Order, the Company would not be in this situation. Had Mr. Kettler decided not to make significant distributions to himself over the last decade and instead invested those Company funds into appropriate repairs and improvements to the Company's water and wastewater systems during that time period, HVUS would not be in this situation.

The fact that the Company now appears to be finally making a good faith effort to comply with the *McCloskey* Decisions, after effectively ignoring the Commission's 2005 Order

[1] *In the Matter of: Application of Hidden Valley Utility Services, LP – Water; Application of Hidden Valley Utility Services, LP – Wastewater, for Approval to Offer, Render, Furnish, or Supply Wastewater Services to the Public in Hidden Valley, PA* (Order entered July 15, 2005) (2004 Application); *see* McCloskey Case ALJ Exh. 2 ("2005 Settlement").

which addressed the very same issues, is a positive development, but the Commission should not ignore HVUS' long-term and chronic failure to address its quality of service issues just because it has finally begun to address them in 2018. The fact remains that HVUS continues to fail to provide safe, adequate, and reliable water and wastewater service to its customers, and its requested rate increases should be denied for that reason. This case is not a "Catch-22" situation; it is a case of the Company doing too little, too late, with respect to its obligation to provide safe, reasonable and adequate water and wastewater service to its customers, and the Commission should not reward the Company's long-term negligence and delinquency in this regard by approving the Company's rate increases at the expense of its customers, who still suffer from inadequate water and wastewater service, as they have from the time that the Company first began to provide service.

II. BACKGROUND AND PROCEDURAL HISTORY

The Foundation addressed the background and procedural history of this case in its Main Brief, where the Foundation adopted the Background and Procedural History sections of the Main Brief of the Office of Consumer Advocate. Hidden Valley Foundation Main Brief, p. 2; OCA Main Brief, pp. 5-13.

III. LEGAL STANDARD

The Foundation addressed the legal standard in its Main Brief. Hidden Valley Foundation Main Brief, pp. 2-4.

IV. REPLY TO HVUS QUALITY OF SERVICE ARGUMENT

HVUS argues that, although the Commission has the discretion pursuant to Sections 523(a) and 526(a) of the Public Utility Code to reduce a utility's rate request, in part or in whole, based on the quality of service it is providing to customers, the Commission should not exercise such discretion because the non-unanimous settlement between the Bureau of Investigation and Enforcement ("I&E") and HVUS (the "Settlement") properly balances the interests of customers and the utility. Based on that position, HVUS argues that a further "reduction" of its rate request (beyond the "reduction" from the Company's initial proposed rates to the lesser rates stipulated in the non-unanimous Settlement, which remain significant increases over the current rates for both water and wastewater) is not warranted. The Company is focused on the wrong issue—the question is not whether a further "reduction" of its rate request is warranted; the question is whether the Company has provided sufficient evidence that it is entitled to any rate increase at all.

A. The McCloskey Decisions Support Denial of HVUS' Requested Rate Increases.

HVUS argues that the fact that the Commission ordered the Company to complete certain tasks, within stated timeframes, to bring its water and wastewater systems into compliance with Section 1501, is "critically important" in view of the Commission's decision in *Pa. Pub. Util. Com'n v. Clean Treatment Sewage Company*, Docket No. R-2009-2121928, 2010 Pa. PUC LEXIS 671 (Opinion and Order entered April 22, 2010), where the Commission denied a public utility's request for rate relief on the basis that the utility failed to provide adequate and reasonable service.[2] HVUS focuses on language from the Commission in *Clean Treatment*

[2] In *Clean Treatment*, the Commission stated: "We fully realize that improvements to the Company's service and facilities will require a rate increase, but we have seen nothing in this filing that indicates that any improvements will be forthcoming." 2010 Pa. PUC LEXIS at *33.

stating that nothing in the rate filing in that case indicated that any improvements will be forthcoming, contrasting that scenario with the *McCloskey* Decisions, where the Commission gave HVUS a plan for improvements that included milestones. As HVUS and its customers know, a plan for improvements, even one with milestones that is ordered by the Commission, means nothing with respect to whether the improvements will *actually be completed.*

The plan for improvements in the 2005 Settlement required that HVUS find a solution that would "permanently solve the problems caused by the levels or iron and manganese in its water" (Paragraph C.20 of the 2005 Settlement) but those problems remain an issue today in 2018 and will remain an issue going forward until they are resolved (if ever). HVUS' position that this is "not a case in which the Company is demonstrating a disregard for, flouting, or defiance of the Code and the Commission's Orders and regulations" is demonstrably false. If failing to address issues that remained outstanding from the settlement of the 2004 Application Proceeding until ordered (again) to address such issues in the *McCloskey* Decisions in 2018 is not disregarding or flouting the Commission's Orders, what is?

The Commission has specifically addressed the issue of what a utility must do to show that it has addressed a prior finding of inadequate service in *Pennsylvania Pub. Utility Commission v. Pennsylvania Gas & Water Co.*, 61 Pa. PUC 496 (1986): "PG&W must show actual results of service improvements as opposed to optimistic plans for the future. On this point, we again state that every customer is entitled to water that is fit for the basic, domestic purposes." *Id.* at 502. To this point, HVUS has failed to show actual results of service improvements (or any service improvements at all); as in 2005, all that HVUS has promised is optimistic plans for the future, plans the customers of HVUS have no reason to believe will come to fruition based on their experience over the last decade and a half. HVUS has never been able

to provide its customers with water that is fit for basic domestic purposes and there is no reason to believe that will change until the Company can demonstrate that it has actually done so.

HVUS believes that withholding rate relief until the Company has fully complied with the improvement plan established in *McCloskey* is not necessary to enforce that plan. But that is not the question at issue in this matter; the question is, given the Commission's prior finding of inadequate service, has HVUS shown the actual results of service improvements necessary to qualify it for rate relief? In the *PG&W* cases, the Commission found that the evidence did not demonstrate actual results of service improvements to the substandard quality of service. *Pa. P.U.C. v. Pa. Gas & Water Co.*, 68 Pa. PUC 191, 1988 Pa. PUC LEXIS 457 (Sept. 29, 1988).[3] Based on the finding that the Company failed to demonstrate that its ratepayers were currently receiving adequate service, the Commission denied the 1987 rate increase request in its entirety. *Id.*

Here, likewise, the Company has failed to demonstrate that its ratepayers are currently receiving adequate service and has failed to provide any evidence of actual results of any alleged service improvements made by the Company. The best that the Company can offer is that there is no evidence that the service issues at Hidden Valley have become *worse* since the *McCloskey* decisions. *See* HVUS' Main Brief at p. 27. While that may be the case (and one wonders how the service issues could possibly even get worse), there is also no evidence that the service issues have become any *better* since the Commission's finding in *McCloskey* that the Company is not providing reasonable and adequate water and wastewater service as required by 66 Pa. C.S. §

[3] In the 1987 rate case, a new water filtration plant had become operational, a system monitoring program had been implemented, a corrosion control program was put in place, 60 percent of Company-owned lead and lead-lined services had been replaced and a formal main flushing program had been established. *See* 68 Pa. P.U.C. 191 at 415-15.

1501. Accordingly, the Company has not demonstrated that it has satisfactorily addressed the Commission's prior finding of inadequate service, and the Company's rate requests must be denied for this reason.

B. The Company's Wastewater Service Remains Seriously Deficient.

While HVUS largely acknowledges its continuing failure to provide adequate water service, the Company has demonstrated a concerning unwillingness to acknowledge the severity of the issues with the wastewater system and the Company's failure to provide adequate wastewater service to its customers. HVUS takes the position that, because the Commission's finding of inadequate wastewater service in the *McCloskey* decisions was based on the record in a hearing held in November of 2015, that finding does not reflect the current state of the Company's wastewater service, noting that improvements have been made in the three intervening years. That might be a reasonable position if the improvements completed since 2015 had resulted in a wastewater system with no or few service issues remaining in 2018. But that is not the case at all. In response to the Commission's Order in *McCloskey* that the Company obtain and file with the Commission a written report from an independent Pennsylvania licensed water and wastewater engineer concerning the adequacy of the wastewater system (January 2018 Order at 62-63), HVUS obtained such a report, and it recommended seventy-five projects to be completed by HVUS in connection with the Commission's directive that HVUS ensure that customers shall receive adequate and reasonable wastewater service on or before January 31, 2019. OCA St. 3S (WW) at 3; Exh. TLF-1.

As of July 27, 2018, there were eight projects that were completed, three that were started and sixty-four that had not yet been started. OCA St. 3S (WW) at 3. At this time, 40 days out from the Commission's deadline for the Company to "comply with all recommendations from

the engineer with regard to wastewater services in order to ensure that customers shall receive adequate and reasonable wastewater service, on or before January 31, 2019" (Ordering Paragraph 11 of the Commission's May 3, 2018 Opinion and Order in *McCloskey*), it is clear that the Company cannot and will not comply with the Commission's Order with respect to wastewater service.[4] Given these facts, it is obvious that the Company continues to have serious deficiencies in its wastewater service and that such service will remain deficient until such time as all of the recommendations in the engineer's report have been completed, if that date ever comes. This means that the Company's wastewater system remains in violation of Section 1501 based on the facts that currently exist in 2018, just as it was in violation in November 2015.

The minor improvements since that time have not resulted in any demonstrable wastewater service improvement; they were merely the first steps made by the Company towards addressing the long-neglected significant problems with the wastewater service, a service that will remain inadequate until all of the recommendations in the engineer's report are completed. Then, and only then, will the Company be able to seriously argue that it is providing reasonable and adequate wastewater service and that a rate increase is proper. To characterize evidence of Company's deficient wastewater service as "stale" is misleading and disingenuous given the recency and scope of the engineer's report. OCA St. 3 (WW) at 5-6; Exh. TLF-1. The Company is effectively asking the Commission to ignore its deficient wastewater service because no potential "disaster scenarios" have been realized (yet) and because the Company's water service

[4] On October 18, 2018, HVUS filed a Petition for Amendment of the Commission's May 2018 Order. HVUS has asked the Commission to amend paragraph 8 of the Order, which requires HVUS to "comply with all recommendations from the engineer, in order to correct any identified deficiencies..." within one year from the date of the engineer's report, asking that the one year deadline (April 30, 2019) be replaced with a series of milestones related to the option HVUS chooses or, in the alternative, change the one-year deadline to a four-year deadline. Petition at 8-9.

is even more deficient than its wastewater service, resulting in more customer complaints about the water service.

As the Company spins it, (1) the Commission's finding in *McCloskey* that the Company's wastewater system is in violation of Section 1501 and (2) the current deficiencies in the wastewater system identified in the engineer's report, which the Company cannot correct in time to meet the Commission's January 31, 2019 deadline, constitute "limited evidence in the record regarding the quality of service presently provided by Hidden Valley's wastewater system." This position is blatantly and willfully ignorant of the current reality of the quality of the Company's wastewater service. The record shows that the quality of the Company's wastewater service was not adequate and reasonable it 2015, it is not adequate and reasonable now, it will not be adequate and reasonable on or before January 31, 2019, and the Company does not know if or when the quality of its wastewater service will ever become reasonable and adequate.

C. A Complete Denial of the Company's Requested Rate Relief is Supported by Prior Commission Authority

The Company argues that the Commission's complete denial of any rate relief in this case would "destroy the Company," "virtually guaranteeing that improvements will not be made." HVUS Main Brief at p. 35. Here again, the Company and its management fails to take responsibility for its role in the fate of the Company since it obtained its authority from the Commission as a water and wastewater utility in 2005. In arguing that this case is similar to *Pa. Pub. Util Comm'n v. Lake Latonka Water Company*, 1989 Pa. PUC LEXIS 231 (Recommended Decision dated November 28, 1989, Final Order entered October 16, 1989)[5] because there the

[5] *Lake Latonka* also holds that a utility provides inadequate water service even when the water "has non-health, aesthetic quality problems." 71 Pa. PUC at 22. The Commission has held in other cases that water was inadequate despite being safe to drink. *See Ashbaugh v. Fitz Henry Water Co.*, 51 Pa. PUC 287 (1977), where the Commission ruled that the water was inadequate because of the water's "unpleasant taste, sediment, and unsuitability for laundry purposes" and held that the utility had violated its statutory obligation. *Id.* at 291.

Commission approved a non-unanimous settlement in a rate case against a property owners association's argument against a rate increase based on inadequate service, the Company misses the main distinguishing factor between the cases—the settlement agreement in *Latonka*, which gave the company modest rate relief, coupled with conditions designed to improve service, is analogous to the 2005 Settlement that resulted from the Company's 2004 applications to provide service and approved the initial water and wastewater rates, while also imposing significant conditions on the Company, which the Commission gave the Company until July 2014 (over 9 years!) to complete, and which the Company did not come close to completing; it is not analogous to the Company's current situation where it is asking the Commission for approval of a new non-unanimous settlement agreement after completing flouting the prior 2005 Settlement ordered by the Commission.

This case most resembles the *Clean Treatment* case, where the Commission denied a rate increase in its entirety and instituted a Section 529 proceeding because it had serious concerns regarding the financial, technical and managerial ability of the utility to make the necessary improvements. 2010 Pa. PUC LEXIS at *4-5. Those same exact concerns exist with respect to HVUS today and they have existed for the entire course of the Company's existence. The most important factor and reason for denying the Company's requested rate increases, is that the Company's quality of service issues have been present since day one and have never improved to the point where HVUS has provided adequate and reasonable water and wastewater service to its customers. The destruction of HVUS has been caused by its mismanagement since its inception and the Company should not now receive a bail out from the Commission in order to allow it to maybe, someday provide adequate and reasonable service. The Company should be forced to come up with its own capital to make the improvements required by the *McCloskey* Order. If it

cannot do so, then the Commission should enforce the remedies provided for in *McCloskey*, including the Section 529 proceeding. *See* January 2018 Order at 66; 66 Pa. C.S. § 529 provides authority to the Commission to order a takeover of a small troubled system by a larger capable public utility. 66 Pa. C.S. § 529(a).

Furthermore, a utility is not entitled to rate increases simply because it exists and provides some service, without regard to whether that service is adequate. As the Commission has stated, "a utility is not *guaranteed* rate increases necessary for a return on its property; it is only entitled to rates sufficient to earn a fair return if it provides adequate service. This is the essence of the regulatory bargain. The Legislature has specifically made it part of the Public Utility Code, which we are bound to administer:

> Every public utility shall furnish and maintain adequate, efficient, safe, and reasonable service and facilities, and shall make all such repairs, changes, alterations, substitutions, extensions, and improvements in or to such service and facilities as shall be necessary or proper for the accommodation, convenience, and safety of its patrons, employees, and the public. Such service also shall be reasonably continuous and without unreasonable interruptions or delay. Such service and facilities shall be in conformity with the regulations and orders of the commission. Subject to the provisions of this part and the regulations or orders of the commission, every public utility may have reasonable rules and regulations governing the conditions under which it shall be required to render service.
>
> 66 Pa. C.S. §1501."

Pennsylvania Pub. Util. Comm'n v. Pa. Gas & Water Co., 68 Pa. P.U.C. 191 (Sept. 29, 1988).

Importantly, the Commonwealth Court of Pennsylvania has affirmed the Commission's authority to deny rate increases because of inadequate service, even where the utility argued that without the increase, it would not have enough revenue to continue operating:

> While we recognize that to starve NUI of a rate increase may hinder its abilities to upgrade its systems, we also recognize that a public utility is not entitled to a rate increase when its service is so inadequate. As the D.C. Court of Appeals observed, a utility's fulfillment of its service commitment is a *sine quo non* to constitutional protection under confiscation principles. **To hold otherwise would mean that**

> **regardless of the level of service provided by a utility, or if the utility provided no service, the PUC would be required to give the utility a reasonable rate of return solely because it exists**. In this case, there was ample evidence of an inadequate level of service that did not justify any increase in rates.

Nat'l Utilities, Inc. v. Pennsylvania Pub. Util. Comm'n, 709 A.2d 972, 979 (Pa. Commw. Ct. 1998) (Emphasis added.) The Commonwealth Court rejected NUI's alternative argument that it needed the rate increase to pay its loans, noting the ALJ's finding that the company had sufficient funds available to pay its loans but chose to pay other expenses, some of which were excessive and unnecessary. *Id.* at 979, footnote 13. Although the Company has not made the argument that it needs the rate increases to pay its loans, the Company has significant loan debt and no plan to repay it, and the Company's situation is analogous to NUI's because it has chosen to make excessive and unnecessary expenditures in lieu of the spending on repairs and improvements required to put the Company in a position to provide adequate service, specifically significant distributions to its owner while the Company has remained (1) unprofitable and (2) unable and unwilling to provide reasonable and adequate service to its customers. Along with failing to request a rate increase since 2005, these distributions are a major reason that the Company is in its current financial position and that the Company cannot afford to make the costly improvements required by the *McCloskey* Order. It goes without saying that the scope and cost of the improvements necessary today would not be nearly as great if the Company had made some effort to properly maintain its water and wastewater systems over the last thirteen years in compliance with the 2005 Settlement and 2005 Order. If HVUS is destroyed, it will have been the actions of the Company that destroyed it, not the failure of the Commission to bail it out after many years of mismanagement and neglect of its water and wastewater service, not to mention its customers.

D. Denial of the Company's Requested Rate Increases Does Not Deny the Company's Constitutional Rights.

The Supreme Court long ago recognized that the value of service could be considered in determining whether a rate resulted in the confiscation of utility property, finding no due process violation or denial of rights to a utility company where the Commission was influenced by considerations of the value of the service in this case. *Market Street Railway Co. v. Railroad Commission of California*, 324 U.S. 548, 563-64.

Moreover, a series of Pennsylvania cases have held that, until the quality of service improved, it would be impermissible for the effective rates to provide a return that might be considered to be confiscatory:

> The making of repairs and improvements to meet the duty to render reasonable and adequate service is not necessarily dependent on the profit which may reasonably be expected therefrom; in proper cases such repairs and improvements may be ordered though the immediate result thereof would be a financial loss to the utility.

Colonial Prod. Co. v. Pa. P.U.C., 188 Pa. Super. 163, 172–73, 146 A.2d 657, 663 (1958); See *Sherman v. Public Service Commission*, 90 Pa.Super. 523, 526; *Ridley Township v. Pennsylvania Public Utility Commission*, 172 Pa.Super. 472, 478, 479, 94 A.2d 168; see also *National Util. Inv. v. Pa. P.U.C.*, 709 A.2d 972, 977-980 (Pa. Commw. 1998) (NUI 1998) (holding that the Fifth and Fourteenth Amendments to the U.S. Constitution are not violated when a public utility is denied an increase in rates when it fails to provide adequate service to the public, even if the result is a rate of return less than it would otherwise be entitled to receive).

Further, in *Nat'l Utilities, Inc.*, the Commonwealth Court held that the Fifth and Fourteenth Amendments to the Constitution are not violated when a public utility is denied an increase in rates when it fails to provide adequate service to the public, even if the result is a rate of return less than it would otherwise be entitled to receive. *Nat'l Utilities, Inc.*, 709 A.2d at 979.

The Company's position that denying a rate increases denies the Company any constitutional rights is wholly without merit.

V. REPLY TO HVUS' INDEPENDENT AUDIT ARUGMENT

HVUS takes the patently absurd and gratuitously self-serving position that the results of an independent audit ordered by the Commission should be proprietary and confidential, with the Company's management having the discretion to select an auditor. Even by the Company's standards of operating with no apparent regard for the adequacy of its water and wastewater systems, financial records, or its service to customers, arguing that the Company should not be required to share the results of the audit with the parties (while the audit would be financed by the ratepayers the Company has failed to serve for over a decade!) after the Company's consistent and chronic failure to prepare and file accurate financial records over the course of its existence, is particularly brazen. The reason for this proposed requirement seems obvious—the prospect of the parties learning about the actual financial position of the Company today and over the course of its existence, as opposed to the false picture of the finances painted by the inaccurate financial statements filed with the Commission, is too damaging for the Company to reveal. This transparent attempt to continue to hide the true state of the Company's finances while the customers of the Company are told that rate increases are necessary to fund the improvements required by *McCloskey* because the Company cannot otherwise afford them, is completely unacceptable to the Foundation and its members, the ratepayers who have undergone many years of substandard service by the Company. They have a right to review the results of the independent financial audit ordered by the Company prior to having their bills increase one cent while they continue to receive inadequate water and wastewater service from the Company, and they demand nothing less than an independent audit by an auditor with no prior relationship to the Company and who is not chosen by the Company. To order an audit under any other

conditions would send the message that there are no consequences for the Company's consistent failure to file accurate financial reports with the Commission.

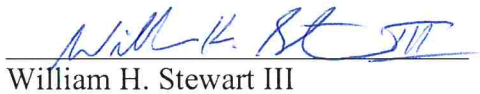
VI. REPLY TO HVUS' NON-UNANIMOUS SETTLEMENT PETITION AND JOINT STIPULATION

Like the Office of Consumer Advocate ("OCA"), the Foundation did not join in the Non-Unanimous Settlement Petition and is opposed to the agreement between HVUS and the Bureau of Investigation and Enforcement therein. Accordingly, the Foundation adopts the OCA's position and arguments with respect to the Non-Unanimous Settlement Petition and Joint Stipulation in OCA's reply brief.

VII. CONCLUSION

For the foregoing reasons, Hidden Valley Utility Services, L.P.'s proposal to increase rates for water and wastewater customers should be denied. The Foundation opposes the Joint Petition of Non-Unanimous Settlement as being against the public interest, and the Foundation respectfully requests that Administrative Law Judges Mark A. Hoyer and Katrina L. Dunderdale recommend, and the Commission deny, the terms and conditions contained in the Joint Petition of Non-Unanimous Settlement. The Foundation further respectfully requests that Administrative Law Judges recommend, and the Commission adopt the findings of fact, conclusions of law and ordering paragraphs proposed by the Commission in its Main Brief.

Respectfully submitted,



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