

COMMONWEALTH OF PENNSYLVANIA



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February 4, 2019

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

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

Dear Secretary Chiavetta:

Attached for electronic filing please find the Office of Consumer Advocate's Exceptions in the above-referenced proceedings.

Copies have been served per the attached Certificate of Service.

Very truly yours,

A handwritten signature in blue ink that reads "Christine Maloni Hoover".

Christine Maloni Hoover
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Enclosures:

cc: Honorable Mark A. Hoyer
Honorable Katrina L. Dunderdale
Office of Special Assistants (e-mail only: ra-OSA@pa.gov)
Certificate of Service

*265728

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 Office of Consumer Advocate's Exceptions, 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 4th day of February 2019.

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY	:	
COMMISSION, et al.	:	Docket Nos. R-2018-3001306
	:	R-2018-3001307
v.	:	C-2018-3001841
	:	C-2018-3001843
HIDDEN VALLEY UTILITY	:	
SERVICES – WATER	:	
	:	
HIDDEN VALLEY UTILITY	:	
SERVICES – WASTEWATER	:	

EXCEPTIONS OF THE OFFICE
OF CONSUMER ADVOCATE

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Table of Contents

I. INTRODUCTION 1

II. EXCEPTIONS 3

OCA Exception No. 1: The Inadequate Water And Wastewater Service Provided By HVUS Supports A Denial Of the Revenue Requirements Agreed To In The Non-Unanimous Settlement. R.D. at 33-34, 46-53; OCA M.B. at 18-46; OCA R.B. at 6-22.3

A. Introduction.....3

B. Rate Relief Does Not Include Funding for Improvements Required By McCloskey 4

OCA Exception No. 2: Additional Revenue Requirement When Service Remains Inadequate Is Inconsistent With The Requirements of the Public Utility Code. R.D. at 33-34, 46-53; OCA M.B. at 18-46; OCA R.B. at 6-22.....7

III. CONCLUSION..... 10

TABLE OF AUTHORITIES

Cases	Page(s)
<u>Market Street Railway Co. v. Railroad Commission of California,</u> 324 U.S. 548 (1945).....	8
 Administrative	
<u>McCloskey v. Hidden Valley Utility Services,</u> Docket Nos. C-2014-2447138 and C-2014-2447169 Order (January 17, 2019).....	6
<u>McCloskey v. Hidden Valley Utility Services,</u> Docket Nos. C-2014-2447138 and C-2014-2447169 Order (January 18, 2018).....	<i>passim</i>
<u>Pa. P.U.C. v. Pa. Gas & Water Co.,</u> 68 Pa. PUC 191, 1988 Pa. PUC LEXIS 457 (Sept. 30, 1988).....	4, 5, 7
<u>Pa. P.U.C. v. Pennsylvania Gas and Water Co.,</u> 61 Pa. PUC 409, 74 PUR4th 238 (1986)	3, 4, 7
 Statutes	
66 Pa. C.S. § 523.....	2, 8
66 Pa. C.S. § 526.....	2, 8
66 Pa. C.S. § 1301.....	2, 8
66 Pa. C.S. § 1501.....	2, 7, 8
 Other Authorities	
52 Pa. Code § 5.533	1

I. INTRODUCTION

On January 25, 2019, the Office of Administrative Law Judge issued the Recommended Decision of Deputy Chief Administrative Law Judge Mark A. Hoyer and Administrative Law Judge Katrina L. Dunderdale (ALJs) addressing proposed rate increase requests of Hidden Valley Utility Services, L.P. (HVUS or the Company) regarding its water and wastewater services. The ALJs concluded that HVUS is providing inadequate water and wastewater service to its customers. The ALJs, however, recommended that HVUS receive an increase of \$65,557 (46.6%) in water revenues and an increase of \$82,227 (28%) in wastewater revenues because HVUS needs additional sums in order to comply with the Public Utility Commission's (Commission) order in McCloskey v. Hidden Valley Utility Services, Docket Nos. C-2014-2447138 and C-2014-2447169 Order (January 18, 2018) and McCloskey v. Hidden Valley Utility Services, Docket Nos. C-2014-2447138 and C-2014-2447169 Order on Reconsideration (May 3, 2018) (McCloskey or 2018 Complaint Cases)

The ALJs correctly recognized that HVUS is providing inadequate water and wastewater service. The ALJs also correctly recognized that the inadequate service needed to be addressed. Unfortunately, the ALJs based their recommendation on information that is not supported by the record or the facts. The ALJs also erred in requiring ratepayers to pay any increase in rates in light of the inadequate service being provided by HVUS. The Company's continuing inadequate service and failure to comply with the 2005 Settlement and the 2018 Complaint Case Orders require a denial of the proposed increases. Therefore, pursuant to 52 Pa. Code § 5.533, the OCA files the following exceptions for the Commission's consideration.

The Company's proposed rate increase for water was an increase of 105% and for wastewater an increase of 63%. Under the Non-Unanimous Settlement increase, customers

would face substantial increases: water rates would increase by 46.6% and wastewater rates would increase by 28% in Phase I and by an additional 49.7% under the Non-Unanimous Settlement. The ALJs recommended that the Non-Unanimous Settlement be approved with modifications. As set forth below and in the OCA's Main and Reply Briefs, HVUS should not receive any increase in revenues due to the ongoing inadequate service that it provides to its customers. Despite the ALJs' characterization that denying the rate increases would satisfy Hidden Valley's customers and OCA, the reason to deny the rate increases is to recognize that the rates that are paid today, and have been paid since 2005, were set to reflect adequate service which customers never received. Moreover, the rate increase is premised on customers receiving adequate service, which the record clearly establishes they are not receiving and will not receive in the future test year and beyond. Given the inadequate service that the ALJs found, it is inconsistent with the requirements of the Public Utility Code and is not legally supportable to increase rates above the current level. 66 Pa. C. S. §§ 523, 526, 1301, and 1501.

II. EXCEPTIONS

OCA Exception No. 1: The Inadequate Water And Wastewater Service Provided By HVUS Supports A Denial Of the Revenue Requirements Agreed To In The Non-Unanimous Settlement. R.D. at 33-34, 46-53; OCA M.B. at 18-46; OCA R.B. at 6-22.

A. Introduction

The ALJs rely on assertions that HVUS needs “additional sums” in order to comply with the totality of the requirements in McCloskey. R.D. at 33. The reliance on these assertions is not supported by the record evidence and is not consistent with the requirements of the Public Utility Code. Ratemaking requires that the utility provide adequate service, and the ALJs found that HVUS is not providing adequate service.

The Commission has explained the relationship between rates and service:

It is our opinion that in exchange for the utility’s provision of safe, adequate, and reasonable service, the ratepayers are obligated to pay rates which cover the cost of service which includes reasonable operation and maintenance expenses, depreciation, taxes and a fair rate of return to the utility’s investors. Thus, as the OCA contends, a quid pro quo relationship exists between the utility and its ratepayers.

Pa. P.U.C. v. Pennsylvania Gas and Water Co., 61 Pa. PUC 409, 415-16, 74 PUR4th 238, 245 (1986) (PG&W 1986). In PG&W 1986, the Commission also addressed the timing of rate increases related to actual improvements versus plans for the future:

Finally, we point out that customers are entitled to adequate and reasonable service at the time they are paying their bills, not some optimistic point in the future.

61 Pa. PUC at 416. In this case, the current rates that the HVUS customers are paying are based on a legal presumption that they are receiving safe, adequate and reliable water and wastewater service. The ALJs found that HVUS is not providing adequate service, which is consistent with the Commission’s finding in McCloskey. Thus, there is no basis for an increase in water or

wastewater rates given the inadequate service provided by HVUS.

B. Rate Relief Does Not Include Funding for Improvements Required By McCloskey

The ALJs state that HVUS will use the additional revenue requirement that they recommend to comply with the Commission's order in McCloskey. There is no evidence that the additional revenue requirements recommended by the ALJs will be used to comply with McCloskey. In fact, as discussed below, the evidence shows that the rate relief sought by HVUS did **not** include funding for the improvements required in McCloskey.

In PG&W 1986 and Pa. P.U.C. v. Pa. Gas & Water Co., 68 Pa. PUC 191, 1988 Pa. PUC LEXIS 457 (Sept. 30, 1988) (PG&W 1988), the Commission specifically addressed the issue of what the utility must do to show that it has addressed a prior finding of inadequate service. Specifically, PG&W's 1985 rate increase request was denied in its entirety. PG&W 1986, 61 Pa. PUC at 426-27. The Commission explicitly stated what PG&W was required to demonstrate in order to qualify for rate relief:

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.

PG&W 1986 Order on Reconsideration, 61 Pa. PUC at 502 (emphasis in original). In reviewing the record in PG&W's next base rate case filed in 1987, the ALJs found and the Commission agreed, that the evidence "did not demonstrate actual results of service improvements to the substandard quality of service, existing at the time that the Commission acted upon the Company's last rate request." 68 Pa. PUC at 502(emphasis in original).¹ The Commission found that the Company failed to demonstrate that its ratepayers were currently receiving

¹ In the 1987 rate case, PG&W had constructed a new water filtration plant, and initiated a number of other programs related to flushing and corrosion control. PG&W argued that it had made substantial progress since the 1985 rate filing. See 68 Pa. PUC at 414-15.

adequate service and denied the 1987 rate increase request in its entirety. PG&W 1988, 68 Pa. PUC at 421.

The current case does not contain any expenses or capital projects related to improving the service HVUS provides to its customers, so the revenue requirement agreed to by HVUS and I&E will not be used to make any improvements that will solve the iron and manganese problems, or address the long list of issues in the engineer's report for wastewater. HVUS has not asked for any capital expenditures or other expenses related to making improvements in the water and wastewater service. As Ms. Sherwood explained:

This rate case utilizes a 2017 historical test year and does not include any claims regarding expenditures related to the options shown in the April 2018 engineer's report. The requested rate increase would address increased expenses incurred since rates were implemented in 2005, but it would not provide the revenue needed to recover any expenditures related to service improvements. Furthermore, at the time of the rate case filing, the Company had not chosen which options it would implement from the April 2018 engineer's report.

OCA St. 1 (W) at 1-2; OCA St. 1 (WW) at 1-2. According to HVUS's engineer's report, the cost of the wastewater improvements is \$227,900 and the cost of the water improvements is between \$852,000 and \$2,389,000. HVUS M.B. at 35. Those costs do not include additional requirements such as testing and replacing water meters. Id. There is no evidence that HVUS has chosen an option for the water system (treatment or alternate source). There is no evidence that HVUS has sought and secured financing for any of these improvements or that it will be able to secure financing for these improvement. There is no assurance that the improvements will be made by HVUS, especially given the experience with its delayed compliance with the 2005 Settlement Agreement. See OCA M.B. at 7-8. There is no evidence that HVUS will be able to comply with the directives in McCloskey, even if it receives the increase in the Non-

Unanimous Settlement or even if it had received its originally proposed revenue increase.² OCA R.B. at 12-13. There is no evidence of actual service improvements now or in the future.

Regarding the likelihood of HVUS making the improvements that are necessary, the Commission looked at that when it considered the Petition for Amendment filed by HVUS:

Adhering to the process outlined in our prior Orders is preferential to the amendments suggested by HVUS because the requested modifications **would result in further delays without any assurances that subsequent compliance deadlines could be met or that proposed improvements could be adequately funded.** Such an indeterminate approach would appear to be detrimental to the interest of the Company's customers who have suffered from the long term water service problems. Thus, we shall deny the Second Petition.

McCloskey, slip op. at 31 (Jan. 17, 2019) (McCloskey January 2019 Order) (emphasis added). Moreover, the Commission determined that it should proceed to a Section 529 case:

As expressed in the *January 2018 Order*, we viewed any further delays in complying with the deadlines of this long-standing proceeding as possibly indicative of the Company's lack of competency to operate and of its ability to provide reasonable and adequate service. Considering the Company's admission that it will not be able to comply with the deadline set forth in Ordering Paragraph No. 8 of the *May 2018 Order*, and in light of the possible evidentiary questions related to the estimated schedules provided by the Company's engineer and the financing plans for any of such proposals, we find that it would be appropriate to proceed to the hearing procedures set forth in the *May 2018 Order*.

McCloskey January 2019 Order at 31.³ There is no evidence that establishes that the revenue requirements recommended by the ALJs will be used by HVUS to make any

² In fact, as discussed in the OCA's Main Brief, HVUS filed a Petition for Amendment in McCloskey, and asked for relief from the deadlines imposed to comply with the requirement to resolve the water quality of service issues by April 30, 2019. OCA M.B. at 11. The Commission denied the Petition. McCloskey January 2019 Order. In addition, the engineer's report, although filed by April 30, 2018 deadline, did not comply with the Commission's Order because it did not contain a recommendation but rather contained a number of options. Id.; OCA St. 3 (W) at 5-6.

³ It is clear that the Commission did not make any determination regarding whether a mandatory takeover was appropriate in the context of the McCloskey complaint proceedings, contrary to the ALJs' characterization regarding HVUS. See R.D. at 32. The Commission specifically stated that a Section 529 proceeding, in which it would

improvements required by McCloskey. There is no evidence that HVUS will be able to secure financing to make the improvements. The Commission's January 2019 Order recognized this by recommending moving to the hearing procedures set forth in the May 2018 Order.

OCA Exception No. 2: Additional Revenue Requirement When Service Remains Inadequate Is Inconsistent With The Requirements of the Public Utility Code. R.D. at 33-34, 46-53; OCA M.B. at 18-46; OCA R.B. at 6-22.

Even if the revenue requirement results in a zero return on equity⁴, the Public Utility Code requires that the utility invest in the capital needed to provide adequate service and then receive rates that reflect the utility's used and useful, prudent investments before receiving rate increases related to the investments. This ensures that rates are not increased while service is inadequate and ensures that the utility will actually make the investments and improve service before receiving additional revenues. See PG&W 1986 and PG&W 1988. To do otherwise would increase rates to customers while service remains inadequate and would permit a utility to receive additional revenues without making any additional investments. That scenario would be in conflict with the Public Utility Code.

In PG&W 1988, the Commission cited to judicial precedent that "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" and found that this regulatory

investigate whether a mandatory takeover was appropriate, would be the next step if HVUS did not comply with the McCloskey Orders.

⁴The OCA would note that the resulting rate of return is not provided with the Non-unanimous settlement, but the revenue increases permitted by the Non-unanimous settlement are higher than the revenue increases indicated by I&E's primary litigation position (0% return on equity). I&E's calculated revenue increases using a 0% return on equity were \$57,753 for water and \$69,175 for wastewater. I&E St. No. 1 (W) at 3; I&E St. No. 1 (WW) at 3. Because the Non-unanimous settlement allows for increases greater than these it appear that the revenue requirements provide a positive return on equity for HVUS. OCA M.B. at 50.

bargain has been codified in Section 1501 of the Public Utility Code. 66 Pa. C.S. § 1501. 68 Pa.

PUC at 197. That Section requires:

every public utility shall furnish and maintain adequate, efficient, safe, and reasonable service and facilities, and shall make such repairs, changes, alterations, substitutions, extensions, and improvements in or to such service and facilities as shall be necessary and 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.

The linkage between the setting of just and reasonable rates and the quality of service is well-established in case law. In Market Street Railway Co. v. Railroad Commission of California, 324 U.S. 548 (1945), the United States Supreme Court affirmed a Railroad Commission order that reduced the fare to be charged by the railway company for providing inadequate service. Legal standards which protect utility investors from the confiscation of their property do not take precedence over the utility's obligation to provide safe, adequate and reasonable service. The Railroad Commission, during an investigation into the rates and service of the Market Street Railway Company, found that it was reasonable to reduce the fare being charged because *inter alia*, service had deteriorated, there was evidence of long-term neglect and inadequate inspection and maintained stock. 324 U.S. at 556. The Supreme Court, in responding to the railway company's arguments that the order was confiscatory under Hope, and that the company was entitled to a sufficient return rejected the argument that the railway company was entitled to a return "sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital" and to "enable the company to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for the risks assumed." Id. at 566. The Supreme Court found those considerations concerned a company which had the advantage of an economic position which promised to yield what was held to be an excessive return on its investment and that was inapplicable to a company

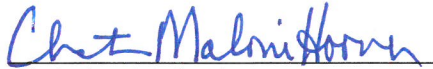
“whose financial integrity already is hopelessly undermined, which could not attract capital on any possible rate, and where investors recognize as lost a part of what they have put in.” Market St. Railway, 324 U.S. at 566. Hidden Valley has provided no evidence that it can attract capital, where it has never ended an operating year without a loss and where despite collecting rates set as if it were providing adequate service, it has not provided adequate service to its customers.

As the ALJs correctly found, the Company is failing to comply with Section 1501 of the Public Utility Code, 66 Pa. C.S. § 1501. The applicable constitutional and legal standards establish this Commission’s authority and obligation to set rates which reflect service inadequacies, including denying the rate increases proposed by HVUS. 66 Pa. C.S. § 523, 526, 1301, and 1501. There is no support for increasing the rates charged by HVUS when it is not providing adequate service.

III. CONCLUSION

For the foregoing reasons, the OCA respectfully accepts to the portions of Deputy Chief Administrative Law Judge Hoyer and Administrative Law Judge Dunderdale's Recommended Decision as discussed above. The OCA submits that rate increases should be denied and the Non-Unanimous Settlement's revenue requirement provisions should be rejected.

Respectfully Submitted,



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