

COMMONWEALTH OF PENNSYLVANIA



OFFICE OF CONSUMER ADVOCATE

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February 5, 2019

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

Re: Application of Pennsylvania -American Water
Company Pursuant to Sections 507, 1102, and
1329 of the Public Utility Code for approval
of its Acquisition of the Water Assets of
Steelton Borough Authority
Docket No. A-2019-3006880

Dear Secretary Chiavetta:

Attached for electronic filing please find the Office of Consumer Advocate's Protest and Public Statement in the above-referenced proceeding.

Copies have been served per the attached Certificate of Service.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Erin L. Gannon".

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

Attachment

cc: Office of Administrative Law Judge
Office of Special Assistants (e-mail only: ra-OSA@pa.gov)
Bureau of Technical Utility Services (email only)
Certificate of Service

*266082

CERTIFICATE OF SERVICE

Re: Application of Pennsylvania-American :
Water Company Pursuant to Sections :
507, 1102, and 1329 of the Public Utility : Docket No. A-2019-3006880
Code for approval of its Acquisition of :
the Water Assets of Steelton Borough :
Authority :

I hereby certify that I have this day served a true copy of the following document, the Office of Consumer Advocate's Protest and Public Statement 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 5th day of February 2019.

SERVICE BY E-MAIL & INTER-OFFICE MAIL

Scott B. Granger
Bureau of Investigation & Enforcement
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor
Harrisburg, PA 17120

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

John Evans, Esquire
Small Business Advocate
Office of Small Business Advocate
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Susan Simms Marsh, Esquire
Elizabeth Rose Triscari, Esquire
Pennsylvania-American Water Company
800 West Hersheypark Drive
Hershey, PA 17033

Kathy L. Pape, Esquire
Adeolu A. Bakare, Esquire
Alessandra L. Hylander, Esquire
McNees Wallace & Nurick LLC
100 Pine Street, P.O. Box 1166
Harrisburg, PA 17108-1166

/s/ Erin L. Gannon

Erin L. Gannon

Senior Assistant Consumer Advocate

PA Attorney I.D. # 83487

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Office of Consumer Advocate

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5th Floor, Forum Place

Harrisburg, PA 17101-1923

Phone: (717) 783-5048

Fax: (717)783-7152

Dated: February 5, 2019

*266081

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

In re: Application of Pennsylvania-American Water Company Pursuant to Sections 507, 1102 and 1329 of the Public Utility Code for Approval of its Acquisition of the Water Assets of Steelton Borough Authority : : : : Docket No. A-2019-3006880

PROTEST OF THE
OFFICE OF CONSUMER ADVOCATE

The Office of Consumer Advocate (OCA) files this Protest in the above-captioned Application pursuant to the provisions of the Rules of Practice and Procedure of the Pennsylvania Public Utility Commission (PUC or Commission), 52 Pa. Code §§ 5.51-5.53, and Chapter 11 and Section 1329 of the Public Utility Code, 66 Pa. C.S. § 1101, *et seq.* and 66 Pa. C.S. § 1329. Through this Application, filed on January 2, 2018, Pennsylvania-American Water Company (PAWC or Company) seeks Commission approval for the acquisition of the water treatment, transportation, and distribution facilities of Borough of Steelton (Steelton or Borough), and the right of PAWC to provide water service to the areas served by Steelton in the Borough of Steelton and in a portion of Swatara Township, Dauphin County, Pennsylvania. PAWC also seeks approval of the ratemaking rate base of the assets as determined under Section 1329(c)(2) of the Public Utility Code, as well as approval of the collection of a Distribution System Improvement Charge (DSIC) prior to the Borough's first post-acquisition rate case, accrual of Allowance for Funds Used During Construction (AFUDC) for post-acquisition projects not recovered through the DSIC for book and ratemaking purposes, and deferral of

depreciation related to post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. Application at ¶ 2. PAWC also requests the approval of the Asset Purchase Agreement (APA) with Steelton as well as other municipal agreements pursuant to Section 507 of the Public Utility Code. Application at ¶ 3. The Borough provides water service to 2,472 customers, including 2,289 residential, 124 commercial, 34 industrial, 11 municipal, and one bulk sales customer connection.¹ Application at ¶ 8.

The OCA files this Protest in order to ensure that the application is approved only if (1) it is found to be in the public interest; (2) it provides substantial, affirmative benefits to the public, and (3) it is in accordance with the Public Utility Code and applicable Commission rules and regulations.

Specifically, the OCA avers as follows:

1. The Protestant is Tanya J. McCloskey, Acting Consumer Advocate, 555 Walnut Street, 5th Floor, Forum Place, Harrisburg, PA 17101-1923. Protestant's attorney for the purpose of receiving service of all documents in this proceeding is Erin L. Gannon, Senior Assistant Consumer Advocate.

2. The OCA is authorized by law to represent the interests of utility ratepayers in all proceedings before the Commission. 71 P.S. §§ 309-1, *et seq.* This Protest is filed by the OCA to ensure that the interests of PAWC's existing and acquired customers are protected.

3. Section 1102 of the Public Utility Code requires that the Commission issue a Certificate of Public Convenience as a legal prerequisite to an entity offering service, abandoning service and certain property transfers by public utilities or their affiliated interests. 66 Pa. C.S. §1102(a)(1)-(3).

¹ The OCA notes that the customer numbers provided in the referenced Application paragraph are more recent than the customer numbers provided in Appendix A-17-a.

4. The Code further requires that a certificate shall only be granted upon findings 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). See City of York v. Pa. P.U.C., 449 Pa. 136, 141, 295 A.2d 825, 828 (1973); see also Popowsky v. Pa. P.U.C., 594 Pa. 583; 937 A.2d 1040 (2007).

5. Section 1103 explicitly allows the Commission to impose conditions upon the issuance of a Certificate of Public Convenience. 66 Pa. C.S. § 1103(a). Section 1103(a) of the Code provides: “The Commission, in granting such a certificate, may impose such conditions as it may deem to be just and reasonable.” The OCA submits that the Commission may wish to consider the imposition of conditions in order to ensure that the public interest standard is met.

6. An increase in rates involves a substantial property right and ratepayers are entitled to notice of a Commission’s administrative proceeding in which a decision is made regarding rates. The notice provided with PAWC’s Application does not meet the fundamental requirements under the 14th Amendment of the United States Constitution (U.S. Const. amend. XIV, § 1), 52 Pa. Code Section 53.45(b)(1-4) and the order entered in McCloskey v. Pa. P.U.C., 1624 CD 2017 (Oct. 11, 2018) (New Garden).

7. Section 1329 of the Public Utility Code, *inter alia*, enables a public utility to use fair market valuation to determine whether the fair market valuation or the purchase price, whichever is less, will be reflected in rate base. 66 Pa. C.S. § 1329(c)(2). This recently added provision is an alternative to the use of original cost, less depreciation for ratemaking purposes, when a public utility acquires municipal water and wastewater assets. PAWC proposes to pay \$22,500,000 per the Asset Purchase Agreement of November 14, 2018. Appendix A-24-a. The original cost of the assets is

\$19,739,906, and the original cost less depreciation is \$14,433,434.76. Appendix A-5.1.

8. The Borough of Steelton Utility Valuation Expert's (UVE) appraisal conducted by ScottMadden was \$21,459,590. Appendix A-5.2. The PAWC UVE's appraisal conducted by Associated Utility Services, Inc. (AUS) was \$23,221,800. Appendix A-5.1. The average of the fair market value appraisals of the buyer's UVE and the seller's UVE is \$22,340,695. PAWC St. 3 at 6. The valuation experts were paid \$33,152 to date to AUS and \$40,965 to ScottMadden for the Fair Market Value Appraisals. Appendix A-8. PAWC estimates that it will incur transaction and closing costs of \$137,500 to \$225,000. Appendix A-12.

9. Preliminarily, the OCA has identified the following areas that require further consideration by the Commission and must be resolved prior to Commission approval of this application pursuant to Chapter 11 and Section 1329 of the Public Utility Code, and the 14th Amendment to the Constitution of the United States.

a. The OCA submits that the notice included in the revised Application does not comply with the 14th Amendment of the Constitution of the United States, 52 Pa. Code Section 53.45, and the Commonwealth Court's decision in New Garden.

b. The valuation information provided with the Application is not sufficient to determine whether PAWC's ratemaking proposals are reasonable. The data and information provided in support of each valuation must be analyzed on the record to determine if the Company's proposals are properly supported. In addition, PAWC's proposed rates, and any proposed rate stabilization plan, must be adequately supported and result in rates that are just and reasonable.²

² PAWC states that it is not proposing a rate stabilization plan. Application at ¶ 13, footnote 2.

c. PAWC would charge the following rates to all customers in the acquired service territory with 5/8-inch and 3/4-inch meters:

Borough of Steelton	
Service Charge per month including first 1,700 gallons	\$ 14.78
Usage Charge over initial 1,700 gallons per 100 gallons	\$ 0.826

Appendix A-13. These rates are equivalent to the pre-acquisition rates charged by Steelton. Application at ¶ 32. As PAWC proposes to bill Steelton customers monthly, PAWC's proposed rates reflect the conversion of the quarterly rates currently charged by Steelton to monthly rates. The proposed rates and tariffs require further examination to determine if they are just, reasonable, and in accord with the Public Utility Code.

d. Information is provided regarding the estimated costs of planned investment in the system. PAWC estimates that the capital costs for the 10-year capital plan for the Steelton system will be \$35.735 million. PAWC St. 3 at 8; PAWC Exh. DRK-1. The impact that the costs will have on the rates of existing and acquired customers must be determined to assess the benefits and detriments of the acquisition. Preliminarily, the OCA notes that if the application is approved, and the rate increase related to the \$22,340,695 ratemaking rate base requested by PAWC were applied only to the Steelton customers, the rates charged to Borough customers would increase approximately 47% over the pro forma revenues in the first year of ownership. See Attachment A to this Protest at 3, Revised Affidavit of Ashley E. Everette (correcting the Affidavit dated January 24, 2019 – Attachment C to the OCA's Petition for Appeal of Staff Action and/or

a Determination of Finality – to reflect that the proposed ratemaking rate base is \$22.34 million, not \$22.5 million). The OCA further notes that if the rate increase were applied equally to Steelton Borough and PAWC water customers, the rates charged would increase approximately 0.2% over the pro forma 2018 sales revenues. Id. at 4. Moreover, if the increase were applied only to existing PAWC water customers, the rates charged to PAWC water customers would increase approximately 0.2% over the pro forma 2018 sales revenues. Id. Thus, if the revenue requirement to existing PAWC water customers includes the cost of ownership of the Steelton system, existing PAWC water customers' rates could increase approximately 0.2% due to this acquisition. Id.

10. The OCA submits that additional information is necessary to determine if the proposed rates and PAWC's request for an approved rate base of \$22,340,695 for the Steelton acquisition are reasonable. The OCA reserves the right to raise additional issues as the case proceeds and further information is obtained from the Applicant.

11. The OCA submits that PAWC's notice to ratepayers must be amended and that additional information is necessary to determine how the transaction will substantially and affirmatively benefit PAWC's existing customers.

WHEREFORE, the Office of Consumer Advocate respectfully requests that the Pennsylvania Public Utility Commission not approve this Application at this time due to the issues raised above and the need for additional information. The Office of Consumer Advocate further requests that the Pennsylvania Public Utility Commission investigate and hold full hearings regarding the Application.

Respectfully submitted,



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Acting Consumer Advocate

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555 Walnut Street 5th Floor, Forum Place
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(717) 783-5048

Dated: February 5, 2019
265923

PUBLIC STATEMENT OF THE
OFFICE OF CONSUMER ADVOCATE
PURSUANT TO 71 P.S. SECTION 309-4(e)

Act 161 of the Pennsylvania General Assembly, 71 P.S. § 309-2, as enacted July 9, 1976, authorizes the Consumer Advocate to represent the interests of consumers before the Pennsylvania Public Utility Commission (Commission). In accordance with Act 161, and for the following reasons, the Acting Consumer Advocate determined to file a Protest and participate in proceedings before the Commission involving the proposed acquisition by Pennsylvania-American Water Company (PAWC) of the Borough of Steelton (Steelton) water assets.

The objective of the Acting Consumer Advocate in filing a Protest in this matter is to protect the interests of PAWC's current customers and the Steelton customers. The Acting Consumer Advocate will endeavor to prevent ratepayers from paying costs that are unreasonable or unduly discriminatory, or otherwise violative of the Public Utility Code. The Acting Consumer Advocate will ensure that the ratepayers receive proper notice in accordance with the Public Utility Code and public policy. The Acting Consumer Advocate will investigate the proposed acquisition to determine if there are substantial affirmative public benefits and request the Public Utility Commission order all necessary and proper customer protections which are justified, reasonable, and in accordance with sound ratemaking principles.

As of November 30, 2018, PAWC serves approximately 659,930 water customers in Pennsylvania. The Borough provides water service to 2,472 customers, including 2,289 residential, 124 commercial, 34 industrial, 11 municipal, and one bulk sales customer connection.

Attachment A
Everette Affidavit
Revised 2/5/2019

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

In re: Application of Pennsylvania- :
American Water Co. Pursuant to Sections :
507, 1102, and 1329 of the Public Utility : Docket No. A-2019-3006880
Code for Approval of its Acquisition of the :
Water Assets of Steelton Borough Authority :

**REVISED AFFIDAVIT OF
ASHLEY E. EVERETTE**

FEBRUARY 5, 2019

1. My name is Ashley E. Everette. I am a Regulatory Analyst employed by the Pennsylvania Office of Consumer Advocate. My business address is 555 Walnut Street, Forum Place, 5th Floor, Harrisburg, Pennsylvania 17101.
2. I have testified as an expert witness on accounting and finance issues in water, wastewater, electric and natural gas cases, including each Section 1329 proceeding that has been filed with the Commission to date.
3. Steelton Borough Authority revenues from water charges in 2017 were \$2,664,325. Appendix A-19-a, 2017 Financial Report, page 4.
4. PAWC estimates annual revenues in the first year of ownership of \$2,794,000. Appendix K of the Application.
5. The annual revenue requirement is calculated as the sum of the return on net rate base, operation and maintenance expenses, annual depreciation expense, and taxes.

6. PAWC claims that its 2018 capital structure for water operations is 44.89% long-term debt, 0.17% preferred stock, and 54.94% common equity. See Docket No. R-2017-2595853, PAWC Statement No. 13, Exhibit No. 13-A, Schedule 12.
7. PAWC claims that its 2018 cost rate for long-term debt is 5.25% and its 2018 cost rate for preferred stock is 8.66%. See Docket No. R-2017-2595853, PAWC Statement No. 13, Exhibit No. 13-A, Schedule 12.
8. The cost of equity for Distribution System Improvement Charge (DSIC) purposes shown in the most recent Quarterly Earnings Report for water utilities was 9.95%. See Docket No. M-2018-3006643.
9. Using the above capital structure and cost rates, PAWC's total cost of capital is estimated to be 7.84%, as shown in the chart below:

	<u>Capital Structure</u>	<u>Cost Rate</u>	<u>Weighted Cost</u>
Long-Term Debt	44.89%	5.25%	2.36%
Preferred Stock	0.17%	8.66%	0.01%
Common Equity	54.94%	9.95%	<u>5.47%</u>
			7.84%

10. PAWC proposes a fair market value ratemaking rate base of \$22,340,695. Appendix A-11 of the Application.
11. The estimated net operating income requirement on the \$22.341 million rate base is \$1,752,000 (\$22.341 million x 7.84%).
12. PAWC estimates operation and maintenance expense associated with the Steelton system to be \$1,391,000. Appendix K of the Application.

13. The estimated amount of taxes other than income is \$92,000. Appendix K of the Application.
14. PAWC estimates annual depreciation expense in the first year of ownership to be \$364,000. Appendix K of the Application. If this is the depreciation expense on the \$22.341 million rate base, it represents a depreciation rate of 1.63% per year.
15. For calculating the estimated income tax liability, the estimated amount of tax-deductible interest associated with the acquisition is \$527,000, calculated as the weighted cost of debt (2.36%) times the \$22.341 million purchase price.
16. The current Pennsylvania corporate income tax rate is 9.99%.
17. The current federal corporate income tax rate is 21%.
18. Based on the levels of the net operating income requirement, operation and maintenance expenses, taxes other than income, and depreciation expense outlined above, the estimated total revenue requirement associated with PAWC ownership of the Steelton water system is \$4,096,000. This revenue requirement includes a provision for state income taxes of \$172,000 and federal income taxes of \$325,000.
19. A revenue requirement of \$4,096,000 would require an increase of \$1,302,000 over the pro forma Year-1 revenues of \$2,794,000.
20. If the \$1,302,000 increase were applied only to the Steelton customers, the rates charged to Steelton customers would increase approximately 47% over the pro forma revenues in the first year of ownership ($\$1,302,000 / \$2,794,000$).

21. PAWC's pro forma 2018 sales revenues from Water Operations are \$667,585,862.
Joint Petition for Settlement of Docket No. R-2017-2595853, Summary Proof of Revenues.
22. If the \$1,302,000 increase were applied only to existing PAWC water customers, the rates charged to PAWC water customers would increase approximately 0.2% over the pro forma 2018 sales revenues ($\$1,302,000 / \$667,585,862$).
23. The combined revenues from Steelton water customers and existing PAWC water customers is approximately \$670,379,862 ($\$2,794,000 + \$667,585,862$).
24. If the \$1,302,000 increase were applied equally to Steelton and PAWC water customers, the rates charged to these customers would increase approximately 0.2% over the pro forma 2018 sales revenues ($\$1,302,000 / \$670,379,862$).
25. Thus, if the revenue requirement to existing PAWC water customers includes the costs of ownership of the Steelton system, existing PAWC water customers' rates could increase approximately 0.2% due to this acquisition.

266083

COMMONWEALTH OF PENNSYLVANIA :
 : SS
Dauphin County :

Ashley E. Everette, Regulatory Analyst for the Office of Consumer Advocate, being duly sworn (affirmed) according to law, deposes and says that the facts contained in the foregoing Revised Affidavit in the matter of In re: Application of Pennsylvania-American Water Co. Pursuant to Sections 507, 1102, and 1329 of the Public Utility Code for Approval of its Acquisition of the Water Assets of Steelton Borough Authority, at Docket No. A-2019-3006880, are true and correct; or are true and correct to the best of her knowledge, information and belief and she expects to be able to prove the same at the hearing hereof.

Ashley E. Everette
Ashley E. Everette
Regulatory Analyst
Office of Consumer Advocate

Sworn and subscribed
before me this 5th day
of February, 2019.

My Commission
Expires 8/14/2020

Heather R Yoder
Signature of Official
Administering Oath

Commonwealth of Pennsylvania
NOTARIAL SEAL
Heather R Yoder, Notary Public
Harrisburg City, Dauphin County
My Commission Expires August 14, 2020