COMMONWEALTH OF PENNSYLVANIA

November 18, 2019

E-FILED

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

Re: Joint Application of Aqua America, Inc., Aqua Pennsylvania, Inc., Aqua Pennsylvania Wastewater, Inc., Peoples Natural Gas Company LLC and Peoples Gas Company LLC for all of the Authority and the Necessary Certificates of Public Convenience to Approve a Change in Control of Peoples Natural Gas Company LLC and Peoples Gas Company LLC by Way of the Purchase of All of LDC Funding LLC's Membership Interests by Aqua America, Inc. / Docket Nos. A-2018-3006061, A-2018-3006062, A-2018-3006063

Dear Secretary Chiavetta:

Enclosed please find the Exceptions to the Recommended Decision, on behalf of the Office of Small Business Advocate ("OSBA"), in the above-captioned proceedings.

Copies will be served on all known parties in these proceedings, as indicated on the attached Certificate of Service.

If you have any questions, please do not hesitate to contact me.

Sincerely,

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Attorney ID No. 312245

Enclosures
cc: Brian Kalcic
Parties of Record

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EXCEPTIONS TO THE RECOMMENDED DECISION ON BEHALF OF THE OFFICE OF SMALL BUSINESS ADVOCATE

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Date: November 18, 2019

I. Introduction

On November 13, 2018, Peoples Natural Gas Company LLC ("Peoples Natural Gas"), and Peoples Gas Company LLC ("Peoples Gas") (collectively, "Peoples") together with Aqua America, Inc. ("Aqua America"), Aqua Pennsylvania, Inc. ("Aqua PA"), and Aqua Pennsylvania Wastewater, Inc. ("Aqua PA WW") (collectively, with Peoples, the "Joint Applicants") filed a Joint Application requesting approval from the Pennsylvania Public Utility Commission ("Commission") for a change in control of Peoples by means of Aqua America's purchase of all of LDC Funding LLC's membership interests pursuant to Sections 1102(a)(3) and 2210(a)(1) of the Public Utility Code, 66 Pa. C.S. §§ 1102(a)(3) and 2210(a)(1) ("*Joint Application*").[1]

On January 18, 2019, a prehearing conference was held before Administrative Law Judge ("ALJ") Mary D. Long.

On April 2, 2019, the Office of Small Business Advocate ("OSBA") submitted the direct testimony and exhibits of Mr. Robert D. Knecht.

On May 21, 2019, the OSBA submitted the surrebuttal testimony and exhibits of Mr. Knecht.

An evidentiary hearing was held before ALJ Long on June 11, 2019, at which time the testimony of witness Mr. Knecht was moved into the evidentiary record.

On June 26, 2019, the Joint Applicants filed a *Joint Petition for Approval of Non-Unanimous, Complete Settlement Among Most Parties* ("*Non-Unanimous Settlement*"), which was opposed by the OSBA and the Commission's Bureau of Investigation and Enforcement ("I&E").

[1] The acquisition is hereafter referred to as the "Proposed Transaction."

On July 10, 2019, the OSBA, I&E, and the Joint Applicants submitted Main Briefs (respectively, "OSBA MB," "I&E MB," and "J.A. MB").

On July 25, 2019, the OSBA, I&E, the Joint Applicants, the Office of Consumer Advocate ("OCA"), and the Coalition for Affordable Utility Services and Energy Efficiency in Pennsylvania ("CAUSE-PA") submitted Reply Briefs (respectively, "OSBA RB," "I&E RB," "J.A. RB," "OCA RB," and "CAUSE-PA RB").

On October 28, 2019, ALJ Long issued her Recommended Decision ("RD").

The OSBA submits the following Exceptions in response to the RD.

II. Exceptions

Exception No. 1: The ALJ erred in finding that access to equity will be even greater in the future after Aqua America becomes a larger public utility. (RD, at 6)

There is no evidence in the record that the SteelRiver[2] entities ever experienced difficulty raising capital. (OSBA MB, at 16; OCA St. No. 2, at 27, fn. 14). Additionally, the Joint Applicants never quantified their bald claim that Aqua America will have better access to equity markets post-transaction. (OSBA MB, at 16). Rather, the testimony of I&E witness John Zalesky contradicts this finding: "While this merger may *slightly* improve bond ratings and access to affordable capital, it is likely that due to the large size of both Companies, the merger will not provide any significant benefit to the Peoples Companies in seeking capital." (I&E St. No. 1, at 5) (emphasis added). That the Proposed Transaction has had a material and sustained negative influence on the market price for Aqua America's equity also demonstrates that the

[2] Peoples Gas and Peoples Natural Gas are wholly-owned subsidiaries of PNG Companies LLC, indirectly owned by SteelRiver Infrastructure Fund North America LP ("SRIFNA") and an affiliated fund. These funds are managed by SteelRiver Infrastructure Associates LLC and its affiliated management entities (collectively, "SteelRiver"). (*Joint Application*, at 7, ¶15; 9, ¶18). LDC Funding LLC is a wholly-owned direct subsidiary of LDC Parent LLC, which is indirectly owned by SRIFNA and an affiliated fund managed by Steel River. (*Joint Application*, at 10, ¶22).

equity markets do not consider the Proposed Transaction to be financially beneficial. (OSBA St. No. 1-S, at 9). Therefore, the ALJ's finding that Aqua America will have more access to equity post-transaction is unsubstantiated and in fact contradicted by the evidence in this matter.

Exception No. 2: The ALJ erred in concluding that there was no reason to delve into the purchase price of the Proposed Transaction because ratepayers were "adequately protected from recovery of the purchase price." (RD, at 33)

The ALJ's conclusion ignores the negative ratepayer impact that completion of the Proposed Transaction will have by increasing the riskiness of Aqua America debt, and therefore increasing the costs and risk to customers. (OSBA MB, at 14). The ALJ offers no explanation as to how ratepayers are protected against the negative impacts on both Aqua America's debt rating and its equity value that have already occurred in anticipation of the Proposed Transaction. Standard & Poor's and Moody's recognized that the Proposed Transaction will increase the riskiness of Aqua America debt. (OSBA MB, at 14; OSBA RB, at 12). The stock market reaction to the Proposed Transaction was consistent with the conclusion that the Proposed Transaction will increase risk. (OSBA MB, at 14). In the three days following the announcement of the Proposed Transaction, Aqua America's stock price fell approximately 11 percent relative to the Dow Jones utility Index. (OSBA MB, 14-15). The initial negative impact of the Proposed Transaction announcement on Aqua America's market cap was about $720 million, and in late March 2019 it was $450 million. (OSBA MB, at 15). Lower credit ratings for the debt will serve to lower the value of that debt, which will lead to higher interest rates. (OSBA, MB at 14; OSBA RB at 12-13). Higher interest rates will be passed on to ratepayers. (OSBA MB, at 14). Therefore, contrary to the ALJ's decision, it is appropriate for the Commission to examine the purchase price of the Proposed Transaction and whether it has a

negative impact on ratepayers. The evidence in the record conclusively demonstrates that the Proposed Transaction's purchase price does negatively impact ratepayers.

Exception No. 3: The ALJ erred in concluding that the consideration paid as part of the Proposed Transaction is reasonable. (RD, at 34)

The Proposed Transaction contemplates a purchase price of $4.275 billion, of which $1.3 billion is existing Peoples debt being assumed by Aqua America, and $2 billion is a "goodwill" asset, which produces no revenue. (OSBA MB, at 12-13). The purchase price substantially exceeds the book value of the companies being purchased. (OSBA MB, at 13, OSBA St. No. 1-S, at 5, fn. 3). While the Joint Applicants relied on a Fairness Opinion authored by Moelis & Company LLC ("Moelis Opinion") to justify the exorbitant amount being paid in the Proposed Transaction, the record evidence demonstrates that the Moelis Opinion was not authored by an independent, unbiased entity. (OSBA MB, at 11-12). Moreover, the ALJ's price premium analysis does not cite to any record evidence supporting the price premium, and appears to rely entirely on the ALJ's observation regarding Aqua's share price and book value. The OSBA observes that the supporting evidence provided by Aqua America, in the form of Exhibits DJS-2R and DJS-5R, do not present comparable market to book ratios. In addition, the OSBA respectfully reminds the Commission that the Proposed Transaction involves the purchase of a natural gas utility and not a Pennsylvania water utility. The high market to book ratio observed by the ALJ for Aqua America may result from many factors that do not apply to a natural gas distribution company, including more favorable regulatory treatment in Pennsylvania. Therefore, the ALJ's conclusion that the consideration paid as part of the Proposed Transaction is reasonable is unsubstantiated by record evidence.

Exception No. 4: The ALJ erred in concluding that the Joint Applicants demonstrated that the amount paid above the book value would not be financially destabilizing to Aqua America. (RD, at 34)

"The inflated purchase price of $2 billion, combined with the market's reaction to the Proposed Transaction announcement, demonstrates that the Proposed Transaction will be financially destabilizing for the combined entity." (OSBA MB, at 15). The $2.0 billion that will be paid to SteelRiver for a non-revenue producing asset will be financed in part by new debt. (OSBA MB, at 14). As the "goodwill" does not produce revenue, the new debt simply adds to the overall riskiness of the combined company, equating to higher interest rates. (OSBA MB, at 14). If new equity is raised to pay the $2 billion, the new equity will serve to dilute the existing earnings of the independent companies, as, once combined, the same earnings will need to be spread over a larger equity base. (OSBA MB, at 14). Such dilution will likely negatively impact the combined company's ability to raise equity in the future. (OSBA MB, at 14). The difficulty raising equity, combined with the lower credit ratings for debt (which result in higher interest rates), will, contrary to the ALJ's conclusion, be financially destabilizing for Aqua America post-transaction.

As an ancillary consideration, it appears that the ALJ also erred in setting too low a standard for evaluating the financial impact of the purchase price, in concluding that, as long as the acquisition was not "financially destabilizing" and is not "shocking or unusual," the Proposed Transaction should be acceptable to the Commission. The Proposed Transaction does not need to be destabilizing or shocking for it to have a negative impact on ratepayers. The standard for this acquisition is one of an affirmative public benefit; it is not one that merely requires a determination that the Proposed Transaction is not disastrously bad.

Exception No. 5: The ALJ erred by concluding that the OSBA objects to the *Non-Unanimous Settlement* "because it fails to adhere to any of the commitments agreed upon in the 2013 Equitable Settlement."[3] (RD, at 49)

This ALJ is simply mistaken. Specifically, the OSBA objects to the *Non-Unanimous Settlement* provisions related to the Goodwin and Tombaugh Gathering Systems ("G/T Systems") because the proposed resolution for addressing a known safety hazard is an uneconomic project that will be unreasonably funded almost entirely by ratepayers. (OSBA MB, at 25; *See* OSBA RB, at 19-22). Moreover, the OSBA's discussion of the 2013 Equitable Settlement, and the continuing obligation of Peoples/SteelRiver to comply with the terms it committed to in that settlement, served to provide background on the G/T Systems and to remind the ALJ and Commission that, in the nearly six years of ownership, little had been done to address the rehabilitation of these systems. (OSBA MB, at 21-23). This is evidenced by the fact that ALJ found that "[l]ost and unaccounted for gas levels remain a significant concern on these systems. These levels were very high in 2012, and they remain high today." (RD, at 54) (internal citations omitted).

Additionally, the 2013 Equitable Settlement established a process whereby Peoples would (1) conduct economic evaluations of the G/T Systems, (2) complete system-wide assessments of the G/T Systems, and (3) present a plan to the Commission estimating the additional funds necessary to provide safe and reliable service on the G/T Systems. (OSBA MB, at 22-23). The terms of the *Non-Unanimous Settlement* eradicate that process. (OSBA MB, at 25). The OSBA suggested that "Peoples and its parent, SteelRiver, should be required by the

[3] In 2013, Peoples acquired the G/T Systems in the acquisition/merger proceeding with Equitable Gas Company, LLC ("Equitable") at Docket Nos. A-2013-2353647, A-2013-2353649, and A-2013-2353651 ("Equitable Merger"). A process was established in the partial settlement reached in the Equitable Merger ("2013 Equitable Settlement"), whereby Peoples agreed to undertake various economic evaluations related to the G/T Systems. As part of the 2013 Equitable Settlement, Peoples agreed that if the economic test was not satisfied, that Peoples would recommend not investing further in the G/T Systems. The Commission approved the 2013 Equitable Settlement by Order on November 14, 2013.

Commission to satisfy the terms of [the Commission Order approving the 2013 Equitable Settlement], and to do so on an expedited basis." (OSBA RB, at 19). This suggestion is not an insistence on blindly adhering to the results of the economic test from the 2013 Equitable Settlement; rather, it is a request for the Commission to hold signatories of Commission-approved settlements to their commitments and to not reward calculated delay on projects that pose safety risks to the public. The *Non-Unanimous Settlement* rewards SteelRiver for stalling on fulfilling its obligations until the G/T Systems became "someone else's problem" and creates dangerous policy by signaling to Pennsylvania public utilities that they can avoid complying with Commission decisions if doing so would involve addressing politically difficult problems. (OSBA RB, at 23). If the *Non-Unanimous Settlement* is approved as recommended by the ALJ, SteelRiver will receive $4 billion while a system-wide net cost of at least $79 million is imposed on its former customers to rehabilitate the G/T Systems – systems which SteelRiver knew were a safety hazard and did nothing to fix. (OSBA RB, at 19). Such a result would be unjust and unreasonable, and the OSBA respectfully requests the Commission to reject the ALJ's recommendation.

As noted in the OSBA's Reply Brief, "it is the OSBA's position that remediation of the G/T Systems as contemplated in the *Non-Unanimous Settlement* is an uneconomic project that will be funded almost entirely by ratepayers." (OSBA RB, at 19). Under the terms of the *Non-Unanimous Settlement*, ratepayers will be responsible for paying at least $79 million in net costs for systems that will create an additional rate base investment supported by revenues of $17 million. (OSBA MB, at 24-25; OSBA RB, at 19). The *Non-Unanimous Settlement* terms will negatively impact customers for approximately sixty-seven years and that negative impact will be up to $10 million a year. (OSBA RB, at 21-22). It is the OSBA's position that "it is unjust

and unreasonable to ask ratepayers to make such an enormous contribution [1] when the overall project so miserably fails an economic test" and [2] when Aqua is paying SteelRiver $2.0 billion for goodwill assets, which produce no revenue. (OSBA MB, at 13, 25; OSBA RB, at 20) (emphasis added). "Finding a reasonable, cost-effective solution that balances the public interest regarding the G/T Systems and the effects on associated customers remains the responsibility of the Commission." (OSBA MB, at 25-26). The OSBA has numerous objections to the *Non-Unanimous Settlement* (*See* OSBA MB, at 13-31; OSBA RB, at 9-25); however, the ALJ's conclusion that the OSBA objects to the *Non-Unanimous Settlement* because it does not adhere to the 2013 Equitable Settlement is erroneous.

Exception No. 6: The ALJ erred by concluding that the OSBA believes that the economic test in the 2013 Equitable Settlement should be used to resolve the problem of the G/T Systems. (RD, at 50)

The RD summarized the OSBA's argument as follows: "It is unjust and unreasonable to ask ratepayers to make such an enormous contribution when the overall project fails the economic test." (RD, at 50). The RD again incorrectly asserts that the OSBA's position on this issue is a rigid insistence that the economic test outlined in the 2013 Equitable Settlement must be used in analyzing the G/T Systems. (RD, at 51). The 2013 Equitable Settlement economic test permits the G/T Systems to be transferred to Peoples if the amount of additional investment necessary to provide safe and reliable service from those systems is equal to or less than the sum of the remaining portion of the $5 million fund provided by Equitable to assess the system, the estimated $12 million to convert customers, and the estimated $6 million that would be supported by revenues from the G/T Systems. (RD, at 43-44). Nowhere in the record is there support for the conclusion that OSBA insists that this is the only proper analysis of how to address the G/T Systems.

To be clear, the OSBA's argument is that it is unjust and unreasonable to ask ratepayers to make such an enormous contribution because it is uneconomic under any analysis to have ratepayers pay at least $120 million in cost for systems that will produce revenues which justify an investment of $17 million and avoid some $10 million in customer conversion costs, even with the $13 million rate incentive in the *Non-Unanimous Settlement*. (OSBA MB, at 25; *See* OSBA RB, at 19-22, J.A.Exhibit JAG-3R). On its face, the proposal has customers paying more than 7 times as much as these systems will produce. Furthermore, approving the *Non-Unanimous Settlement* when the proposed resolution of the G/T Systems is so clearly uneconomic under any test would encourage reactive, unreasonable, and imprudent spending by Companies to the detriment of customers; due process requires that this argument be rejected.

The OSBA's legal position is that when a Company (or the Commission) is looking to commit ratepayer money for a project (in this case, at least $120 million), an analysis of whether the expenditures are reasonable and prudent is necessary, as this is the basis of public utility law. (OSBA MB, at 25-26; OSBA RB, at 19-20). Unreasonable and imprudent expenditures may be permitted if the funding source is shareholder money, but when ratepayer money is to be used for system rehabilitation, there must be a showing of reasonableness and prudency of expenditures. (OSBA MB, at 25-26; OSBA RB, at 20-21). In short, it is the OSBA's view that the process specified in the 2013 Equitable Settlement should have been followed for a proper airing of the issues in this matter, rather than having the first step in that process introduced in the rebuttal stage of an acquisition proceeding. (OSBA MB, at 25-26). Moreover, to the extent this issue is going to be resolved in this proceeding, it should not be done in a manner that is extraordinarily favorable to the SteelRiver entity which has so egregiously dragged its feet in addressing a matter of public safety. The ALJ's conclusion that the OSBA supports an arbitrary imposition of

the results of the economic test specified in the 2013 Equitable Settlement as the way to resolve the G/T Systems issues is erroneous and contrary to the record.

Exception No. 7: The ALJ erred in improperly inserting the issue of abandonment of customers on the G/T Systems when such issue is not before the Commission and not at issue in these proceedings. (RD, at 51)

The RD concludes that OSBA's insistence on the 2013 Equitable Settlement economic test requires abandonment of customers. (RD, at 51). The ALJ is simply wrong. The OSBA has never argued for abandonment in this proceeding.

The RD further noted that the OSBA did not consider the social, litigation, and economic costs of abandoning customers served by the G/T Systems. (RD, at 51). Of course, the OSBA did not argue those issues -- abandonment is not at issue in this proceeding.

There is no proposal to abandon G/T Systems customers before the Commission. The position that the only two options are abandoning customers or accepting the *Non-Unanimous Settlement* contradicts the record evidence. Specifically, in response to questioning by ALJ Long, Joint Applicants' witness Joseph Gregorini testified as follows:

> Q: Now, if the Commission does not approve the transaction, is it Peoples' intent to pitch the Scenario 3 to remediate what's going on in the line?
> A: Well, as Mr. –
> Q: So that's the most likely outcome?
> A: Well, I think it would be part of a process that would start with getting together with the state parties and reviewing some of the options there.
>
> It was our intent that we would certainly submit as part of that plan in compliance with the 2013 settlement, but because of the abandonment issues and some of the complications there, you know, it was out intent to explore other options. (Transcript, at 150-151).

The ALJ inserts a non-existent binary choice into her RD: either approve the *Non-Unanimous Settlement* or abandon customers on the G/T System. (RD, at 51). To the contrary, as set forth in the OSBA Main and Reply Briefs, there are more options to address the G/T Systems than just the two proffered by the ALJ. (OSBA RB, at 23). Furthermore, I&E's Main and Reply Briefs demonstrate that there are a multitude of options to address the G/T Systems which do not involve approving uneconomic plans, abandoning customers, or penalizing general ratepayers by forcing them to pay exorbitant amounts of money for the G/T System remediation, while rewarding SteelRiver by allowing it to take its $4 billion and forget about these systems. (I&E MB, at 33-35; I&E RB, at 18). In fact, the ALJ explicitly acknowledges that there are more than two unappealing solutions, by concluding "the Commission nevertheless has discretion to impose conditions which it deems to be just and reasonable" even where it determines that the granting of a certificate of public convenience is necessary or proper for the service, accommodation, convenience, or safety of the public without imposing any conditions. (RD, at 20, *citing* 66 Pa.C.S. § 1103(a)).[4]

Examples of the various options available to the Commission are listed as follows:

- Require $127 million be set aside by SteelRiver to facilitate remediation of the G/T Systems, and that any portion of the $127 million not spent be returned to SteelRiver, or, if the costs are higher than $127 million, then the amounts above $127 million be borne by Aqua America's shareholders. (I&E MB, at 34; I&E RB, at 18).[5]

[4] I&E's RB provides a list of examples where the Commission has imposed conditions on utilities as part of its approval. (I&E RB, at 29).

[5] *See* I&E RB, at 19-25, for a discussion of why requiring SteelRiver to forgo a portion of its profit in order for customers to receive safe and reliable service is consistent with prior Commission decisions and is in the public interest.

- Require Peoples and SteelRiver to begin repair of the G/T Systems immediately, with the cost of repair primarily borne by SteelRiver. (OSBA RB, at 23).
- Require a portion of the purchase price to be set aside and held in a restricted account to pay for the uneconomic cost to replace the G/T Systems. (I&E MB, at 33).
- Evaluate whether SteelRiver/Peoples should be fined under Section 501 of the Pennsylvania Public Utility Code, 66 Pa. C.S. §501(a), for delaying meaningful progress on its commitments under the 2013 Equitable Settlement, for allowing the G/T Systems to deteriorate, and for failing to address the safety issues on the G/T Systems of which it had full knowledge. (OSBA RB, at 23).
- Reject the provisions related to the G/T Systems in the *Non-Unanimous Settlement*. (I&E RB, at 29-30).

The OSBA agrees with I&E that, "if the Joint Applicants are going to knowingly…make the financially irresponsible choice to replace the entirety of the Goodwin and Tombaugh Systems, then…the financial burden should lie squarely on the shoulders of the Joint Applicants." (I&E MB, at 33).

The Commission has the authority to impose conditions on the Proposed Transaction to protect customers and ensure that customers are not paying for imprudent investment decisions by the Joint Applicants. It would be contrary to Commission precedent to approve a wholly uneconomic project such as the G/T System remediation plan proposed by the *Non-Unanimous Settlement*. Considering the safety, economics, and history of the G/T Systems, approving the *Non-Unanimous Settlement* would be unconscionable and lacks substantial record evidence showing its reasonableness to customers. The RD was incorrect to suggest that the only two choices available are approval of the *Non-Unanimous Settlement* or abandonment of customers.

The Commission has the power to do more; there are numerous options available to the Commission to facilitate the protection of Pennsylvania utility customers.

Exception No. 8: The ALJ erred in concluding that the commitments in the *Non-Unanimous Settlement* to replace the G/T Systems are in the public interest and that it is in the public interest to approve the *Non-Unanimous Settlement* terms addressing the G/T Systems. (RD, at 53, 55)

The RD correctly indicates that the essence of the regulatory compact is that "utilities are mandated to provide safe and reliable utility service, and in return they may earn a return on their prudent investment." (RD, at 60 *citing Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591 (1944)). If the Commission approves the *Non-Unanimous Settlement*, "it may ultimately be forced to allow the recovery of imprudent costs from ratepayers." (I&E MB, at 32). Replacing the G/T Systems at the expense of customers with (nearly) full recovery of and on the assets is not in the public interest as it will harm existing ratepayers. (I&E MB, at 32).

Peoples estimates that the full replacement cost of the G/T Systems is $120 million which, if adjusted for investment supported by revenues, avoided conversion costs, and remaining Equitable funds, will, under the *Non-Unanimous Settlement*, force customers to pay a present value of $91.7 million. (OSBA RB, at 19). The one-time rate credit of $13 million promised in the *Non-Unanimous Settlement* results in existing customers being required to pay approximately $79 million in net cost. (OSBA RB, at 19). Under the *Non-Unanimous Settlement's* proposal, customers will be negatively impacted by this project for approximately sixty-seven years. (OSBA RB, at 21). As will be discussed *infra*, the full replacement cost is an estimate, not a cap, and I&E's estimate for full replacement cost is significantly higher. (OSBA RB, at 19-20). However, assuming that $120 million is accurate for full replacement cost, the

maximum annual impact to customers is $10.2 million per year in Year 5, $8.9 million in Years 11 through 15, and $8.7 million in years 16 through 20. (OSBA RB, at 21 *citing* J.A. Exhibit JAG-2R). Adding $10 million a year to rates is a substantial detriment to customers and not in the public interest. (OSBA RB, at 21-22).

Furthermore, it is not in the public interest to approve the *Non-Unanimous Settlement* terms pertaining to the G/T Systems. Doing so will create bad policy for customers, the Commonwealth of Pennsylvania, and the Commission. SteelRiver signed the 2013 Equitable Settlement in October 2013 that required it to evaluate the G/T Systems which were experiencing unaccounted-for gas rates in the 60 to 80 percent range. (OSBA RB, at 22). Beginning in 2014, Peoples mowed rights-of-way, leak surveyed the lines throughout the G/T Systems, walked the G/T Systems to GPS-locate facilities and meter locations, placed the facilities into the GIS mapping system, replaced and installed line markers, established eight new odor inspection sites, initiated quarterly odor inspections, placed the facilities into the PA OneCall System, and incorporated facilities into the Peoples' damage prevention program. (RD, at 44). Peoples added all lines to a three-year cycle inspection program and claimed to have been classifying, grading, and repairing leaks according to its leak management program. (RD, at 45).

The Goodwin System ***currently*** **loses 82%** of its gas. (I&E RB, at 15).

The Tombaugh System ***currently*** **loses 44%** of its gas. (I&E RB, at 15).

After six years of ownership and *knowing* that the G/T Systems were leaking gas at an alarming rate, SteelRiver did nothing with these systems. (OSBA RB, at 22). Conveniently, at the moment SteelRiver has the opportunity to make billions of dollars and can wash its hands of the G/T Systems, Peoples wants to remediate the G/T Systems as soon as possible, at the cost of ratepayers. The OSBA views the steps that Peoples has taken since 2014 to be *de minimis*

considering the amount of gas the G/T Systems are leaking. Therefore, the OSBA asks that the Commission not reward SteelRiver for its inaction. (OSBA RB, at 22). Approval of the *Non-Unanimous Settlement* would signal to utilities that it is acceptable to the Commission for the bare minimum steps to be taken to address known dangerous conditions, that it is appropriate for utilities to avoid taking steps to repair dangerous systems because the political implications of doing so are unpleasant, that there is a profit to be made for inaction, and that it is the preferred method of the Commission to have customers bear the responsibility of payment for uneconomic and imprudent investments. (OSBA RB, at 22-23). The Commission has not taken this stance in the past.

The OSBA respectfully requests that the Commission decide this matter consistent with its previous decisions to protect customers, allow utilities to earn a return only on their prudent investments, and to force utilities to maintain safe and adequate service for its customers. It is not in the public interest to approve the *Non-Unanimous Settlement* terms addressing the G/T Systems without corrective modification.

Exception No. 9: The ALJ erred in dismissing I&E's concern that replacement of the G/T Systems could cost significantly more than the $120 million estimate, which would negatively impact ratepayers. (RD, at 53)

The ALJ concluded that the full replacement cost estimate of $120 million of the G/T Systems in the *Non-Unanimous Settlement* was accurate. (RD, at 53). I&E estimated that the replacement cost is more accurately in the range of $184 million to $368 million. (I&E MB, at 27, *citing* I&E St. No. 2-SR, at 11). The RD seemed to rest its finding on testimony from Joint Applicant witness Mr. Gregorini that I&E's replacement cost figures reflected the replacement costs for pipeline in urban areas, whereas the G/T Systems were in rural areas where per mile replacement costs were lower. (RD, at 53). However, I&E based its estimate on a replacement

cost of $500,000 to $1,000,000 per mile, which is actually far less than what Peoples reported in its most recent Long-Term Infrastructure Improvement Plan ("LTIIP") (*i.e.*, $1,273,000 per mile in 2017, $1,323,000 per mile in 2018, and $1,317,000 per mile in 2018).[6] (I&E MB, at 27 *citing* I&E St. No. 1-SR, at 17). Simply put, the estimate used by I&E was significantly lower than Peoples' *actual* most-recent per mile replacement cost, and it did not even attempt to account for the obvious trend increase in pipeline replacement costs. In addition, because the long-delayed analysis of the G/T systems was not introduced until the rebuttal stage of an acquisition proceeding, the analysis could not be subjected to a rigorous review by the parties.

Furthermore, the RD's conclusion that the $120 million cost is accurate appears to assume that conditions will be same as in testimony. As noted by the OSBA, "Aqua has never remediated a natural gas gathering system because it is a **water and wastewater utility**," and there may be unexpected conditions encountered in the remediation process which would increase the cost. (OSBA MB, at 25). The failure of the RD to account for Aqua America's inexperience in accepting the accuracy of *Non-Unanimous Settlement's* cost estimate of remediation is an error.

Additionally, the RD's dismissal of I&E's concern that the cost estimates for remediation of the G/T Systems are inaccurate sweeps aside another important point raised by I&E: there is no cap on the contributions from ratepayers, and anything over the rate credit from Aqua America can be passed onto ratepayers under the *Non-Unanimous Settlement*. (I&E MB, at 27, I&E RB, at 17). The OSBA shares this concern. (OSBA MB, at 25; OSBA RB, at 21). In fact, the *Non-Unanimous Settlement* itself observes that the final total cost of remediating the G/T Systems may exceed the $120 million. (*Non-Unanimous Settlement*, at 6-7, ¶33).

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[6] *See* Peoples' LTIIP for January 1, 2017 through December 31, 2021, at Docket Nos. P-2013-2342745, P-2013-2344596, Appendix A, p. 7. ("Peoples LTIIP").

As set forth above, the Commission has the power to impose additional conditions on the Proposed Transaction. (66 Pa. C.S. § 1103(a)). The OSBA, I&E, and all signatories to the *Non-Unanimous Settlement* acknowledge that remediation of the G/T Systems may cost more than $120 million. Therefore, if the Commission approves the Proposed Transaction, the OSBA respectfully submits that the Commission should invoke Section 1103(a) and add appropriate conditions so that ratepayers are not required to pay for the repair of the G/T Systems.

Exception No. 10: The ALJ erred in concluding that the OSBA did not address Mr. Gregorini's testimony regarding all the "actions had been taken" by the Company with respect to the G/T Systems in its argument that approving the *Non-Unanimous Settlement* would reward SteelRiver for doing nothing with natural gas gathering systems that it knew had serious problems. (RD, at 55)

The ALJ is simply wrong. The OSBA addressed Mr. Gregorini's testimony when it observed that SteelRiver did nothing to repair the G/T Systems which, throughout its ownership, have always leaked natural gas at unacceptably high levels. The OSBA reached the obvious conclusion that the actions taken by Peoples, which Mr. Gregorini listed, were wholly ineffective in addressing the many well-known problems in the G/T Systems. (OSBA RB, at 22).

The OSBA rejects the conclusion that mowing rights-of-way adequately addressed the leaking gas on the G/T Systems. (RD, at 44). The OSBA rejects the conclusion that leak surveying the systems adequately addressed the leaking gas on the G/T Systems. (RD, at 44). The OSBA rejects the conclusion that walking the G/T Systems adequately addressed the leaking gas on these systems. (RD, at 44). The OSBA does not agree that putting the facilities into the GIS mapping system or replacing and installing line markers adequately addressed the leaking gas on these systems. (OSBA, at 44). The OSBA does not agree that establishing eight new odor inspection sites and initiating quarterly odor inspections adequately addressed the G/T

Systems that were leaking between 60% and 80%. (RD, at 44). The OSBA does not agree that placing facilities into the PA OneCall System and incorporating the facilities in Peoples' damage prevention program adequately addressed these leaking systems. (RD, at 44). The OSBA does not agree that adding all lines to a three-year cycle inspection program and classifying, grading and repairing leaks on the line according to Peoples leak management program adequately addressed the leaking gas on the G/T Systems. (RD, at 44). Finally, the OSBA does not agree that these extremely modest actions would represent a serious effort at addressing this problem if they had been done over a one-year period, much less over a six-year period. The simple fact is that the G/T Systems were leaking at an alarming and unsafe rate in 2012, and they continue to do so today. (RD, at 54)

Accordingly, the OSBA did consider Mr. Gregorini's testimony, and found that the steps that SteelRiver/Peoples took are designed to simply measure just how poor the system performance actually was rather than to make serious repairs or to meaningfully comply with the 2013 Equitable Settlement. Thus, Mr. Gregorini's testimony is insufficient to change the OSBA's opinion that, after six years of ownership, SteelRiver/Peoples did *nothing* to address the G/T Systems that leak unacceptably high levels of gas.

The Commission-approved 2013 Equitable Settlement required Peoples and SteelRiver to begin to address the G/T Systems beginning ***six years ago***. It is now late-2019 and both Systems continue to leak an absurd amount of gas (82% and 44%, respectively), are a known safety hazard, and must be addressed.

Exception No. 11: The ALJ erred in concluding that the *Non-Unanimous Settlement* terms addressing the G/T Systems are a significant public benefit. (RD, at 55)

The OSBA has consistently argued that the Proposed Transaction does not have a net affirmative public benefit. (OSBA MB, at 2, 6, 7, 13-28, 30-31; OSBA RB, at 3, 9-26). To the extent that there are some specific items that have come out of the feeding frenzy that are deemed to be a public benefit, the OSBA concludes that these benefits are outweighed by the negative implications of the increased financial risk to Aqua America which will be borne by ratepayers (both water and gas). Moreover, the OSBA has argued that the terms set forth in the proposed *Non-Unanimous Settlement,* including the proposed solution for the G/T Systems (a seven-year repair plan paid for by all Peoples ratepayers), also do not include any affirmative public benefits, but instead inflict significant public harm. The record evidence is explicit: (1) Peoples is currently bound, by the terms of the 2013 Equitable Settlement, to address the G/T Systems, (Transcript, at 103-104); (2) the *Non-Unanimous Settlement* proposes to remediate the entirety of the G/T Systems and will produce "marginal revenues" (OCA RB, at 19); (3) the Peoples' companies concede remediation of the entirety of the G/T Systems is uneconomic (Joint Applicants Statement No. 3-R, at 8); and (4) the *Non-Unanimous Settlement* proposes to fully remediate the G/T Systems at the expense of ratepayers by imposing on them at least $79 million in net cost, with substantial upside risk (OSBA RB, at 19-20; *Non-Unanimous Settlement*, at 6-7. ¶¶ 29, 30, 33).

One additional, final fact: if the Proposed Transaction, as conditioned by the *Non-Unanimous Settlement,* is approved without modification, SteelRiver is rewarded with a premium of $2 billion on its book asset value, while having avoided addressing the G/T Systems

as it committed to in the 2013 Equitable Settlement. (*See* OSBA RB, at 22-23). This result would be unconscionable.

Therefore, the OSBA, a statutory advocate charged with the duty of protecting Pennsylvania ratepayers, respectfully submits that based upon the record evidence, the ALJ erred by concluding that the *Non-Unanimous Settlement* terms addressing the G/T Systems are a significant public benefit.

Exception No. 12: The ALJ erred in her analysis of the *Non-Unanimous Settlement* terms by improperly weighing the burden on the G/T Systems customers who may be subject to abandonment against the impact of socializing the costs of remediation to other ratepayers. (RD, at 55)

As set forth above, the ALJ once again improperly determined that only two possible resolutions of the G/T Systems exist. Addressing the issues posed by the G/T Systems cannot be viewed as an either/or paradigm, as there is no evidence in the record to support such a conclusion. As explained *supra*, the issue of abandonment is not before the Commission and insertion of abandonment considerations is improper in this proceeding.

Furthermore, as also set forth above, the Commission should invoke Section 1103(a) and exercise its ability to impose conditions on the Proposed Transaction to mitigate the negative impacts on ratepayers, especially in the context of the G/T Systems. I&E and the OSBA have suggested numerous conditions that the Commission may impose on the Proposed Transaction and *Non-Unanimous Settlement* to prevent customers from bearing the financial burden of paying for the majority of the uneconomic full rehabilitation of the G/T Systems. (OSBA RB, at 23; I&E MB, at 33-34; I&E RB, at 18, 29-30).

To be clear, the OSBA <u>is not</u> in favor of wholesale abandonment of customers served by the G/T Systems; (2) the OSBA <u>is</u> in favor of solving the issues posed by the G/T Systems in an

expedient, economic, and safe manner; and (3) the OSBA concludes that the *Non-Unanimous Settlement,* by forcing customers to pay for such a large percentage of the rehabilitation of these Systems, is unreasonable and imprudent.

Exception No. 13: The ALJ erred in concluding that commitment in the *Non-Unanimous Settlement* to increase spending to levelize the replacement of pipeline in the Peoples' system is an important and significant public benefit. (RD, at 60)

The Joint Applicants commit to filing a modified LTIIP to accelerate LTIIP spending in the amount of $30 million per year as part of the *Non-Unanimous Settlement*. (*Non-Unanimous Settlement*, at 13-14, ¶ 69). This "commitment" is simply to file a modified LTIIP, which is not an affirmative public benefit. (OSBA MB, at 22). It was an error for the ALJ to conclude that increased LTIIP spending is a significant public benefit of the Proposed Transaction. (RD, at 60).

Furthermore, I&E witness Matthew Matse's testified that acceleration of LTIIP spending would be "difficult if not impossible." (OSBA MB, at 19; OSBA RB, at 16-17, *citing* I&E St, No. 3, at 8-9). The Joint Applicants did not offer any detailed analysis of the impact the proposed acceleration in LTIIP spending would have on cost efficiency, rate stability, the obsolescence of the plan in place, safety concerns, and number of affected customers. (OSBA MB, at 19). Aqua America did not undertake any systematic evaluation of the high cost of mains replacement in Pennsylvania or the feasibility of accelerating replacement infrastructure given the limited availability of qualified workers. (OSBA MB, at 20).

When viewed from a customer perspective, this commitment is proposing to impose higher costs on customers, in a shorter amount of time, to replace old pipe which Peoples is

already committed to and is required to do; effectively, this commitment is a penalty to ratepayers not a public benefit. (OSBA MB, at 21).

The Commission should heed the testimony of I&E witness Mr. Matse and reject this "commitment" as an affirmative public benefit.

Exception No. 14: The ALJ erred in concluding that the broader sources of capital available to Aqua America creates an enhanced ability to finance infrastructure improvements and to meet the commitments for more ambitious infrastructure replacement as set forth in the *Non-Unanimous Settlement*. (RD, at 63)

The ALJ improperly concluded that public ownership provides Aqua America with an enhanced ability to meet its *Non-Unanimous Settlement* commitments. (RD, at 63). The Joint Applicants did not offer evidence that SteelRiver experienced any difficulty raising capital needed by Peoples. The Joint Applicants also offered no record evidence demonstrating the claim of Aqua America's "enhanced ability." (OSBA MB, at 16).

Additionally, the ALJ's conclusion assumes that investors are unwilling or unable to invest in private ventures, which the OSBA witness Mr. Knecht testified is untrue. (OSBA MB, at 16-17, *citing* OSBA St. No. 1-S, at 10). Finally, the ALJ appears to imply that any such increased access to equity capital will somehow be a public benefit. The OSBA can locate no evidence on the record which demonstrates that this alleged improvement will result in a lower cost of equity that must be borne by ratepayers. Therefore, the ALJ's conclusion is not supported by record evidence and must be rejected.

Exception No. 15: The ALJ erred in concluding that additional transparency (by virtue of public ownership) is a positive characteristic of Aqua America that will enhance the Commission's ability to evaluate the operations of the regulated utility subsidiaries. (RD, 64)

It was an error for the ALJ to conclude that additional transparency will enhance the Commission's ability to evaluate the operations of Peoples post-transaction. (RD, at 64). All Pennsylvania public utilities are required to share information with the Commission and are an "open book" to regulators. (OSBA MB, at 17). The Joint Applicants did not provide any record evidence that additional information concerning Peoples will be provided under Aqua America's ownership. (OSBA MB, at 17-18). While the ALJ noted that additional transparency is not the most substantial benefit offered by the Proposed Transaction, it was an error to conclude there is any benefit due to "additional" transparency. (RD, at 64).

Exception No. 16: The ALJ erred in concluding that there will be new jobs created to execute the planned infrastructure replacement. (RD, at 71)

The OSBA agrees with the concept that creating new jobs is an affirmative public benefit. However, no such job creation has been committed to by the Joint Applicants.

Specifically, the commitment made by the Joint Applicants in the *Non-Unanimous Settlement* is to file a modified LTIIP; ***there is no commitment by the Joint Applicants to create new jobs or to hire additional employees*** related to the LTIIP. (OSBA MB, at 22; I&E RB, at 14).

The Joint Applicants have not undertaken a systematic evaluation of the feasibility of accelerating replacement infrastructure. (OSBA MB, at 20). The Joint Applicants' discussions with local labor unions regarding the availability of a work force is no guarantee that jobs will be added. (OSBA RB, at 25; I&E RB, at 14). Moreover, the rapid rise in the cost per mile for mains replacement shown in Peoples' LTIIP, combined with the testimony of Mr. Matse, provide

substantial evidence that there is significant tightness in the markets for qualified contractors to perform this work. (I&E St, No. 3, at 8-9, Peoples LTIIP at Appendix A, p. 7). The ALJ's conclusion that the Joint Applicants will add new jobs to execute the LTIIP is unsupported by the evidence and must be rejected by the Commission.

Exception No. 17: The ALJ erred in finding that the implementation of SAP into Aqua America's computer system is a clear public benefit resulting from the Proposed Transaction. (RD, at 74)

The SAP platform can be added to Aqua America's existing systems at any time. Adding the SAP platform to Aqua America's systems has nothing, whatsoever, to do with the Proposed Transaction. The SAP platform is generally considered superior to Aqua America's existing antiquated system, so it is hardly surprising that Aqua America would be moving toward implementing the SAP platform regardless of the existence of the Proposed Transaction. (OSBA MB, at 27).

Of course, nothing prevents Aqua America from adopting the SAP platform today. Aqua America does not need to spend $4 billion buying Peoples in order to justify upgrading its old systems to the SAP platform. (I&E MB, at 36, *citing* CAUSE-PA St. No. 1, at 9).

The ALJ was in error to conclude that implementation of the SAP platform by Aqua America is a in any way an affirmative public benefit of the Proposed Transaction.

Exception No. 18: The ALJ erred in rejecting the OSBA's argument that commitments for low-income customers and universal service are not affirmative public benefits because they only benefit one class of ratepayers. (RD, at 78)

The *Non-Unanimous Settlement* contains an array of provisions related to low-income assistance and universal service. (*See Non-Unanimous Settlement*, at ¶¶98 – 111). Many of these commitments are mere continuations of the status quo, and thus do not qualify as benefits

as the ALJ correctly concludes. (RD, at 69). Others simply represent expansions of the aid to low-income customers, that will be paid for by ratepayers. Under *Middletown Township*, these changes do not represent a benefit because it is a benefit to some customers at the expense of others.

Targeting a specific class with benefits (in this case, low-income ratepayers) does not satisfy the *City of York*[7] standard, as explained in the *Middletown Township*[8] case. (OSBA MB, at 28). The ALJ rejects the OSBA's argument and insists that the *Middletown Township* case does not support the OSBA's position; the ALJ explains that the Commission rejected the proposed acquisition in the *Middletown Township* case because the acquisition would only benefit residents of Middletown Township and would have an adverse effect on the utility's remaining customers. (RD, at 78). However, that is exactly the factual scenario presented in the instant case. The *Middletown Township* case is precisely on point and supports the OSBA's position.

The *Non-Unanimous Settlement* contains numerous commitments concerning low-income service programs, but also contains numerous provisions that would have an adverse effect on all Aqua America and Peoples ratepayers. The *Non-Unanimous Settlement* will result in the completion of the Proposed Transaction, which will dilute earnings for Aqua America's shareholders, increase financial risk for the combined entity, and likely will result in higher interest costs for ratepayers. (OSBA MB, at 6). Additionally, the *Non-Unanimous Settlement*

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[7] *City of York et al. v. Pennsylvania Public Utility Commission*, 295 A.2d 825 (Pa. 1972). This case holds that a finding that the proposed transaction will affirmatively promote the service, accommodation, convenience, or safety of the public in some substantial way is required to satisfy the standard under Section 1103(a) of the Public Utility Code (66 Pa. C.S. § 1103(a)) that a certificate of public convenience may be issued only upon a finding or determination that granting such certificate is necessary or proper for the service, accommodation, convenience or safety of the public. *City of York*, 295 A.2d at 828.

[8] *Middletown Township v. Pennsylvania Public Utility Commission*, 482 A.2d 674 (Pa. Cmwlth. 1984).

results in ratepayers being burdened with significantly more costs than they would be in the absence of the Proposed Transaction. (OSBA MB, at 19-26; OSBA RB, at 15-22).

Therefore, the OSBA respectfully submits that that the ALJ mis-applied the *Middletown Township* case. The Commonwealth Court has decided that class-specific benefits do not satisfy the *City of York* standard. Consequently, the low-income program commitments included in the *Non-Unanimous Settlement* are not affirmative public benefits.

Finally, the *Non-Unanimous Settlement* includes a commitment from Aqua America shareholders to contribute an additional $100,000 per year to Dollar Energy (*Non-Unanimous Settlement*, at ¶100) for four years, a commitment from Peoples to contribute an additional $75,000 per year to Low Income Usage Reduction Program ("LIURP") for three years (*Non-Unanimous Settlement*, at ¶ 101), and a commitment from Aqua America shareholders to contribute $50,000 per year to the Helping Hand program for four years (*Non-Unanimous Settlement*, at ¶109). The OSBA acknowledges that these items represent benefits to the residential class, but respectfully submits they are *de minimis* in the context of the Proposed Transaction. The Proposed Transaction involves a purchase price of $4.275 billion, and SteelRiver is being paid some $3 billion for $1 billion in book equity. (OSBA MB, at 12-13; OSBA St. 1, at 3). By OSBA's count, the incremental shareholder commitments to low income customers come to less than $1 million total, spread over three to four years. The OSBA respectfully submits that such miniscule benefits to the residential class do not offset the substantial negative impacts of the Proposed Transaction on ratepayers, including the increased financial risk and the G/T funding requirements.

Exception No. 19: The ALJ erred in concluding that the commitments made by the Joint Applicants to improve customer service and related metrics constitute affirmative public benefits. (RD, at 85)

The Joint Applicants commit to "ensure that the Peoples Companies continue to provide safety and reliable service to their customers, at a level that meets or exceeds current performance." (J.A. MB, at 47). In the case of Peoples, there is no commitment to affirmatively improve customer service. Continuation of the status quo does not constitute a public benefit. (RD, at 69).

In the case of Aqua America, it is in all utilities' interests to continuously improve customer service and the improvement of Aqua PA's customer service and related metrics is not dependent on the Proposed Transaction. (OSBA RB, at 24). Additionally, as noted by I&E, it is questionable whether these commitments are viewed by the Joint Applicants as firm commitments that must be met. A more realistic interpretation of the language of the Non-Unanimous Settlement would be that Aqua PA views these commitments as mere goals in which case there is zero benefit, let alone a significant public benefit. (I&E RB, at 30-31). Illusory benefits will not satisfy the *City of York* standard.[9] *Popowsky v. Pa. P.U.C.*, 937 A.2d 1040, 1057-1058 (Pa. 1972).

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[9] The Pennsylvania Supreme Court stated the following, when addressing the issue of affirmative public benefits in a telecommunications merger proceeding between Verizon Communications, Inc. and MCI, Inc.:

> In summary, as indicated in *City of York*, the 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, 937 A.2d at 1057 (emphasis added).

As the Non-Unanimous Settlement does not contemplate any penalties for non-compliance, it is difficult to believe that these commitments will be any more effective than the status quo in encouraging Aqua PA to improve its customer service.

Exception No. 20: The ALJ erred in finding that the provisions in the *Non-Unanimous Settlement* related to enhancing operational practices in the competitive retail gas market are affirmative public benefits. (RD, at 90)

The ALJ notes that the *Non-Unanimous Settlement* adopts many of the proposals by the natural gas supplier parties[10] to maintain and enhance the existing choice and transportation programs of the Peoples Companies. (RD, at 87). When analyzing whether an affirmative benefit will result from the Proposed Transaction, the relevant inquiry whether the Proposed Transaction results in an affirmative public benefit when compared to the status quo. (OSBA MB, at 12). Agreeing to *maintain* programs that are already in place (*i.e.*, the status quo) is not an affirmative public benefit. (RD, at 69). Regarding the proposed changes to existing practices, the *Non-Unanimous Settlement* is generally silent as to which entities will be required to bear the costs for those changes. Absent any such commitment from the Joint Applicants, it is reasonable to conclude that the costs will be passed on to ratepayers or the natural gas suppliers. In any event, the Joint Applicants fail to meet their burden to demonstrate that these changes represent

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The Supreme Court found evidence of affirmative public benefits in the proposed merger between Verizon and MCI:

> Indeed, even from a lay perspective, bearing in mind today's technological advances affecting all segments of business and personal life, there is much force to the Commission's conclusion that a combination of Verizon's and MCI's assets and strengths has substantial potential to create an integrated infrastructure supporting delivery of innovative, high-speed data and video services via the fiber-optic network, as well as deployment of mobile devices freeing workers from fixed workstations.

Popowsky, 937 A.2d at 1058.

[10] Dominion Energy Solutions, Inc. and Shipley Choice LLC d/b/a Shipley Energy ("NGS Parties"), Retail Energy Supply Association ("RESA"), and Direct Energy Business Marketing, LLC and Direct Energy Small Business, LLC ("Direct Energy").

public benefits. In addition, no party has made any effort to quantify the impacts of the changes contemplated in the *Non-Unanimous Settlement*. As such, there is no evidence that these changes represent a material affirmative public benefit.

Exception No. 21: The ALJ erred in finding that the one-time $10 million rate credit in the *Non-Unanimous Settlement* is an affirmative public benefit. (RD, at 92)

The $10 million rate credit cannot be analyzed on a standalone basis. That rate credit must be analyzed in the context of the Proposed Transaction as whole. When considering the entirety of the Proposed Transaction, the $10 million rate credit will barely make a dent in the rate increases that will result from the merger. The Commission must consider the $30 million annual increases in rate base which would result from accelerated LTIIP spending. The Commission must consider the $79 million (and possibly more) in net costs associated with the G/T Systems remediation. The Commission must consider the possible increase in financial risk associated with the Proposed Transaction. Consequently, any benefit from a one-time rate credit of $10 million is eclipsed by the negative effects of the Proposed Transaction. (OSBA RB, at 25). Moreover, the "one-time" nature of the rate credit highlights the fact that is readily admitted by the Joint Applicants, namely that this Proposed Transaction contains no operating synergies. (OSBA St. No. 1 at 11). Thus, while a near-term credit is welcome, there are no longer-term cost savings or rate credits to offset the negative impacts of the Proposed Transaction.

As the Proposed Transaction will cost customers much more than they are currently paying, a one-time rate credit is not an affirmative public benefit of the Proposed Transaction. (OSBA RB, at 25).

Exception No. 22: The ALJ erred in finding that the charitable contribution commitments made in the *Non-Unanimous Settlement* are affirmative public benefits. (RD, at 97)

The *Non-Unanimous Settlement* includes two commitments regarding charitable contributions. First, Aqua America agrees to contribute a minimum of one-half of one percent of net earnings. (*Non-Unanimous Settlement*, at ¶113). Thus, if Aqua America earns 8.00 percent on rate base, it will make a minimum charitable contribution of 0.04 percent. The *Non-Unanimous Settlement* also indicates that Aqua America will set a goal of increasing that level to 1 percent of net income in five years, but no commitment is offered. (*Non-Unanimous Settlement*, at ¶113). The OSBA is unable to locate any evidence regarding the current level of charitable contributions by Aqua America, and none is cited by the ALJ in the RD. The OSBA submits that there is no evidence indicating that the one-half of one percent represents an increase at all. Second, Peoples agrees to a minimum charitable commitment of $2.7 million per year. (*Non-Unanimous Settlement*, at ¶113). As shown in OCA witness Ralph Smith's exhibits, the 2018 contribution from Peoples was $3.6 million, and the average over the past four years was just under $3.0 million per year. (OCA St. No. 2, Attachment RCS-3, at p. 49 of 120). As such, the *Non-Unanimous Settlement* commitment actually falls short of the status quo. Therefore, the ALJ's finding that an affirmative public benefit of the Proposed Transaction is Aqua America's commitment to increasing the percentage of pre-tax net income provided as charitable contributions over present levels is serious error. (RD, at 97).

Furthermore, if adopted by the Commission, the ALJ's finding again creates bad policy. The Proposed Transaction will force ratepayers to pay $30 million more a year in increased LTIIP spending and to pay for the majority of the G/T Systems rehabilitation project. However, as part of the Proposed Transaction, Aqua America chooses to increase its charitable

contributions – rather than alleviate the financial burden it is placing on its customers. (OSBA MB, at 30). It is an error for the ALJ to conclude that increasing charitable contributions is an affirmative public benefit of the Proposed Transaction when the Proposed Transaction forces customers to pay much more than they would absent the merger.

Exception No. 23: The ALJ erred in finding that it is only the concern for cost to ratepayers which inform the objections of OSBA to the Proposed Transaction. (RD, at 102)

The OSBA concedes that cost to ratepayers is a primary concern that informs its objections to the Proposed Transaction. After all, the OSBA is tasked with representing the interests of small business customers of utility services before the Commission.

Nevertheless, the OSBA's objections to the Proposed Transaction are also based on the Joint Applicants' failure to meet its burden of proving that the Proposed Transaction will affirmatively promote the service, accommodation, convenience, or safety of the public in some substantial way as required by the *City of York,* 295 A.2d 825, 828 (Pa. 1972). (OSBA MB., at 6; OSBA RB, at 3). The OSBA expressed a significant concern that adding a massive non-revenue-producing goodwill asset to Aqua PA's books, with a significant increase in associated debt, will materially increase the financial riskiness of Aqua America, and thus the riskiness of its two Pennsylvania utility subsidiaries. (OSBA MB at 12-15). While the OSBA's primary concern associated with this risk is, understandably, its impact on ratepayers, increasing the overall riskiness of two large Pennsylvania utilities may also have a negative impact on other stakeholders, notably workers and suppliers, as well as potential impacts on government tax revenues.

Therefore, while it would be correct to say that the cost of the Proposed Transaction informs the OSBA's objections to it, the ALJ is wrong that cost to ratepayers is the only basis for the OSBA's objections to the Proposed Transaction.

Exception No. 24: The ALJ erred in finding that the Proposed Transaction and *Non-Unanimous Settlement* are in the public interest and supported by substantial evidence. (RD, at 103, 105)

Neither the Proposed Transaction nor the *Non-Unanimous Settlement* are in the public interest. Aqua America is paying $2 billion in goodwill to SteelRiver, which is an enormous price premium that will be detrimental to ratepayers. (OSBA MB, at 30). The *Non-Unanimous Settlement* proposes to increase LTIIP spending by $30 million a year, to be paid by ratepayers, and to replace the G/T Systems, the cost of which will be largely borne by ratepayers (at least $79 million net). (OSBA MB, at 30, OSBA RB, at 20).

In its Main Brief, I&E correctly stated the issue, as follows:

> The costs associated with the commitments reflected in the [*Non-Unanimous Settlement*], all or most of which will ultimately be borne by ratepayers, appear to have gone unreviewed…it is certainly not in the public interest to also view ratepayers as a never-ending funding source. (I&E MB, at 14).

Contrary to the ALJ's finding, the Proposed Transaction and *Non-Unanimous Settlement* are only in SteelRiver and the Aqua America shareholders' interests – not in the public interest. (OSBA MB, at 6, 13,15, 25, 30; OSBA RB, at 10-12,18, 20-21, 22, 25).

Exception No. 25: The ALJ erred in concluding that the Joint Applicants have demonstrated that the Proposed Transaction, as conditioned by the *Non-Unanimous Settlement*, will affirmatively promote the service accommodation, convenience or safety of the public in some substantial way as required by *City of York* and *Popowsky*. (RD, at 104)

The Proposed Transaction does not provide any net quantifiable or verifiable benefits, and many of the commitments the Joint Applicants claim are affirmative public benefits are in fact vague, illusory, unenforceable, or a continuation of the status quo operations of the current Peoples companies, Aqua PA, and Aqua PA WW. (OSBA MB, at 6). To the extent there are modest public benefits in the *Non-Unanimous Settlement*, they are far outweighed by the negative impacts of the Proposed Transaction that are identified by the OSBA and are exacerbated by some of the commitments in the *Non-Unanimous Settlement* and the substantial harm associated with the Proposed Transaction. (OSBA RB, at 9).

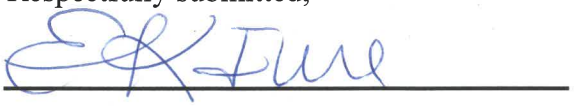
As repeatedly argued by the OSBA, the Proposed Transaction increases the financial risk of the combined resulting entity by increasing the riskiness of Aqua America debt. (OSBA MB, at 14). Lower credit ratings for debt lowers the value of that debt, which negatively impacts existing bondholders and can lead to higher interest rates. (OSBA MB, at 14). Customers will be negatively impacted by higher interest rates because the financial impact of those higher rates will be passed on to ratepayers. (OSBA MB, at 14). The *Non-Unanimous Settlement* commits to filing a modified LTIIP which, if approved, would result in customers paying for an additional $30 million annually in rate base. (OSBA RB, at 10). Ratepayers will be required to provide a return of and return on that capital through the Distribution System Improvement Charge mechanism, and they will presumably be asked to continue to do so in future base rate cases. (OSBA RB, at 10). Customers are responsible for paying the lion's share of the G/T Systems remediation under the *Non-Unanimous Settlement*; "the ratepayer impact of the *Non-Unanimous*

Settlement under the Company's calculations is up to $10 million per year, the negative impact will extend for more than 60 years, the capital costs could credibly be more than three times as high as those estimated by the Joint Applicants, and the ratepayers are fully responsible for all costs except for a one-time $13 million credit." (OSBA RB, at 22). The Proposed Transaction will significantly increase the costs for customers well beyond what they are currently paying, and these costs far outweigh any modest benefit offered by the Proposed Transaction. As such, the ALJ erred in concluding that the Proposed Transaction, as conditioned by the *Non-Unanimous Settlement*, will affirmatively promote the service accommodation, convenience or safety of the public in some substantial way.

V. Conclusion

Wherefore, the OSBA respectfully requests that the Commission adopt the OSBA's Exceptions, as set forth above, and revise the Recommended Decision accordingly.

Respectfully submitted,



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Office of Small Business Advocate
555 Walnut Street, 1st Floor
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Dated: November 18, 2019

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Joint Application of Aqua America, Inc., Aqua Pennsylvania, Inc., Aqua Pennsylvania Wastewater, Inc., Peoples Natural Gas Company LLC and Peoples Gas Company LLC for all of the Authority and the Necessary Certificates of Public Convenience to Approve a Change in Control of Peoples Natural Gas Company LLC and Peoples Gas Company LLC by Way of the Purchase of All of LDC Funding LLC's Membership Interests by Aqua America, Inc.	:	**Docket No. A-2018-3006061** **Docket No. A-2018-3006062** **Docket No. A-2018-3006063**

CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing have been served via email and/or First-Class mail (*unless other noted below*) upon the following persons, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).

The Honorable Mary D. Long
The Honorable Emily DeVoe
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