



COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
COMMONWEALTH KEYSTONE BUILDING
400 NORTH STREET, HARRISBURG, PA 17120

BUREAU OF
INVESTIGATION
&
ENFORCEMENT

March 9, 2020

Via Electronic Filing

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

Re: Pennsylvania Public Utility Commission v.
Twin Lakes Utilities, Inc.
Docket No. R-2019-3010958
I&E Reply Exceptions

Dear Secretary Chiavetta:

Enclosed for filing, please find the Bureau of Investigation and Enforcement's (I&E) **Reply Exceptions** for the above-captioned proceeding.

Copies are being served on parties as identified in the attached Certificate of Service. Should you have any questions, please do not hesitate to contact me.

Sincerely,

A handwritten signature in black ink, appearing to read "Erika L. McLain", written in a cursive style.

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Enclosure

cc: Honorable Marta Guhl (*ALJ, PUC Philadelphia*)
Office of Special Assistants (*via E-Mail only RA-OSA@pa.gov*)
Per Certificate of Service

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Pennsylvania Public Utility Commission

v.

Twin Lakes Utilities, Inc.

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Docket No. R-2019-3010958

**REPLY EXCEPTIONS
OF THE
BUREAU OF INVESTIGATION & ENFORCEMENT**

Erika L. McLain
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Dated: March 9, 2020

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I. INTRODUCTION

As explained in the I&E Exceptions filed on March 2, 2020, the ALJ issued a Recommended Decision (“RD”) on February 19, 2020 accepting all of I&E’s expense adjustments and its alternate rate of return recommendation. Although I&E agreed with the ALJ’s basis for denying Twin Lakes rate request, the crux of I&E’s Exception was that an error in Table 1 was detected and in order to accurately depict I&E’s recommendation, an adjustment must be made. Exceptions were also timely filed by Twin Lakes Utilities, Inc. (“Twin Lakes” or “Company”) and the Office of Consumer Advocate (“OCA”). I&E now files these timely Reply Exceptions in response to the Exceptions filed by Twin Lakes. I&E maintains that the Company has failed to satisfy its burden of proof with respect to its ratemaking claims; therefore, the ALJ properly accepted the I&E recommendations in this base rate proceeding.

II. REPLY EXCEPTIONS

1. **Reply to Twin Lakes Exception No. 1: The ALJ Properly Found That Twin Lakes Has Failed to Take Necessary Actions to Improve this System and Should Not Be Rewarded for its Failure to Act (Twin Lakes Exceptions, pp. 1-2; RD pp. 77-83)**

The evidence in this proceeding demonstrates that Twin Lakes is failing to provide its customers with safe and reliable service as required by the Public Utility Code. The Company reported that for the years ended December 31, 2015 through December 31, 2018, unaccounted-for water percentages averaged 80.5%.¹ Undoubtedly these levels are excessive. Excessive unaccounted-for water levels are troublesome as it increases

¹ I&E St. No. 3, p. 4.

expenses incurred by a utility for pumping, treating, and sending out water into its distribution system, thus necessitating higher rates overall.² Excessive unaccounted-for water also decreases the amount of water available to customers, especially during peak demand periods, and diminishes overall quality of service. Furthermore, as excessive unaccounted-for water levels are often related to leaks, they pose problems for customers such as service interruptions and contamination in the water lines.

Twin Lakes has repeatedly agreed to reduce unaccounted-for water and has, thus far, been unsuccessful. In the 2011 base rate proceeding, as part of the Joint Petition for Settlement, the Company agreed that it would reduce its then current 55% unaccounted for water level by 10% by September 3, 2013.³ It further agreed that over the subsequent 4 year period, it would continue to reduce unaccounted-for water levels by 10% each year.⁴ Yet, instead of decreasing, the unaccounted-for water levels continued to rise significantly over the subsequent years, ranging from 78.7% to 82.9% in 2015-2018.⁵ Once again, as part of the Joint Settlement of the 2015 base rate proceeding, the Company agreed to certain measures that would help remedy its excessive unaccounted-for water levels. As part of that Settlement, the Company agreed to a 3-year phase-in of rates. The triggering event for the year 3 rate increase was the replacement of certain older service lines.⁶ Of the 4,000 feet of mains the Company agreed to replace in the

² I&E St. No. 3, p. 4.

³ *Pennsylvania Public Utility Commission v. Twin Lakes Utilities, Inc.*, Docket No. R-2011-2246415, pp. 10, 20-21 (Recommended Decision dated January 18, 2012).

⁴ *Id.*

⁵ I&E St. No. 3, pp. 5-6.

⁶ *Pennsylvania Public Utility Commission v. Twin Lakes Utilities, Inc.*, Docket No. R-2015-2506337, pp. 9-11, 20-22 (Recommended Decision dated April 21, 2016).

2015 proceeding, the Company has only replaced 2,790 feet which has clearly not had a material impact on the unaccounted-for water levels.⁷ The amount of lost and unaccounted-for water is clearly in excess of what the Commission considers reasonable. Considering the unaccounted-for water levels along with the lead levels that have triggered DEP action, the ALJ concludes that Twin Lakes has failed to provide adequate and reasonable service.⁸

In Exceptions, Twin Lakes urges the Commission to ignore the problems identified by the ALJ and the Parties in this proceeding. Twin Lakes Exceptions note that it "...has provided adequate and reasonable service in accordance with Section 1501 of the Public Utility Code notwithstanding the extremely poor condition of the original distribution system which is the root cause of the unaccounted-for water, the excessive pumping/treating and associated costs, the loss of Well No. 1 and the threat to the continued viability of Well #2..."⁹ Twin Lakes essentially admits that in order to find it has provided safe and reliable service, this Commission would need to ignore the obvious problems with unaccounted-for water and the issues with both Wells No. 1 and No. 2. The Commission cannot, as Twin Lakes would prefer, simply pretend these issues do not exist.

The ALJ's RD explains that in 2015, Twin Lakes was granted a rate increase to be phased-in over three phases, but Twin Lakes failed to implement Phases 2 or 3.¹⁰ Phase 1

⁷ I&E St. No. 3, p. 7.

⁸ RD, p. 83.

⁹ Twin Lakes Exceptions, p. 2.

¹⁰ RD, p. 82.

of the rate increase went into effect immediately. Phase 2 was dependent on Well No. 1 being replaced and as that never occurred, Twin Lakes was unable to implement Phase 2 of its rate increase. Additionally Phase 3 of the rate increase was dependent on specific mains being replaced; once again, Twin Lakes failed to achieve these replacements leaving Twin Lakes unable to implement Phase 3 of its rate increase. Twin Lakes has a demonstrable history of failing to implement measures that would reduce unaccounted-for water on this system. In its Exceptions, Twin Lakes states that "...Twin Lakes perceived 'inaction' has no basis in fact or in the record."¹¹ This is a wholly inaccurate. The evidentiary record shows that there is concrete evidence that Twin Lakes was unable to implement either Phase 2 or Phase 3 of its prior rate request because this utility has failed to act to remediate the high levels of unaccounted-for water. In 2015, Twin Lakes affirmatively agreed to an amount of money it apparently believed was sufficient to replace Well No. 1 and certain mains, however, even when that increase was approved by this Commission, the utility still failed to replace the well or the mains. Understandably, I&E remains unpersuaded that even if the full increase was granted in this proceeding Twin Lakes would successfully reduce unaccounted-for water.

Granting a rate request has not, thus far, incentivized Twin Lakes to make the necessary upgrades to its system. Therefore, the ALJ's determination that Twin Lakes "...has failed to provide adequate and reasonable service in the matter in accordance with Section 1501 of the Public Utility Code," and, as such, "...Twin Lakes is not entitled to is

¹¹ Twin Lakes Exceptions, p. 2.

full requested rate increase¹² is appropriate. Requiring ratepayers to pay higher rates when history has shown a reluctance on Twin Lakes part to make the necessary upgrades to its system is contrary to the public interest. Twin Lakes failure to provide safe and reliable service necessitates that this Commission grant less than its full requested increase. Accordingly, I&E requests that the Commission reject Twin Lakes Exception No. 1 and accept the ALJ's recommendation that Twin Lakes has failed to provide adequate and reliable service and, thus, mitigate the rate increase accordingly.

2. Reply to Twin Lakes Exception 2: The ALJ Properly Found that Affordability of Rates is a Factor in Setting Just and Reasonable Rates (Twin Lakes Exceptions pp. 2-4; RD pp. 83-87)

The Recommended Decision correctly states that the Commission is charged with setting just and reasonable rates.¹³ As explained in I&E's Main Brief, the Commission must adhere to the Public Utility Code and as such, the Code mandates adequacy of service must be taken into account when determining the level at which to set rates.¹⁴ In the Recommended Decision, ALJ Guhl appropriately determined that Twin Lakes failed to provide its customers with adequate and reasonable service.¹⁵ The Company's failure to provide adequate service while at the same time requesting a significant rate increase (the current average monthly bill would increase from \$94.59/month to \$248.34/month under the Company's proposed rates) is not in the public interest.¹⁶

¹² RD, p. 83.

¹³ 66 Pa.C.S. §1301.

¹⁴ 66 Pa.C.S. 523(a); I&E MB, pp 41-42.

¹⁵ RD, pp 82-83.

¹⁶ I&E St. No. 2, p. 25. I&E M.B., p. 53.

Twin Lakes erroneously claims that the ALJ violated the regulatory compact by considering affordability.¹⁷ Twin Lakes goes on to state that by violating the regulatory compact and disallowing companies to earn an adequate return on capital, the Commission would send a clear, chilling message to Pennsylvania utilities.¹⁸ This argument is nonsensical given that Twin Lakes disregards the fact that the ALJ accepted I&E's alternate proposal allowing Twin Lakes to earn a 9.23% return on equity. I&E's alternate recommendation was based upon a traditional ROE analysis that employed the Discounted Cash Flow ("DCF") method and utilized the Capital Asset Pricing Model ("CAPM") as a check to the DCF results. In contrast, Twin Lakes did not offer any evidence to support its proposed 11.00% return on equity claim. It did not conduct a DCF or CAPM analysis and failed to use a water utility proxy group to establish a benchmark of comparable risk. Accordingly, the RD's recommendation to accept I&E's alternate return on equity recommendation was based upon traditional rate of return calculations, which result in just and reasonable rates.

In its Exceptions, Twin Lakes questions OCA witness Sherwood's qualifications to provide expert testimony regarding affordability.¹⁹ This objection is inappropriate at this stage of litigation. Twin Lakes had an opportunity to either attempt to strike OCA's testimony or cross-examine Ms. Sherwood at the hearing set for this matter; however, Counsel for Twin Lakes did neither. It is improper for Twin Lakes' Counsel to argue the credibility of Ms. Sherwood's testimony at this stage of the rate proceeding given that the

¹⁷ Twin Lakes Exceptions, pp. 3-4.

¹⁸ Twin Lakes Exceptions, p. 3.

¹⁹ Twin Lakes Exceptions, p. 4.

Company failed to file a motion to strike and waived the opportunity to cross-examine Ms. Sherwood on her experience with affordability issues or object to the introduction of Ms. Sherwood's testimony regarding affordability.

Lastly, Twin Lakes cites to *Pennsylvania Public Utility Commission v. Pennsylvania Gas & Water Company*²⁰ which concluded that affordability should not be a factor in setting just and reasonable rates. However, as mentioned above, the Commission is charged with setting rates that are just and reasonable and 66 Pa.C.S. § 523(a) requires the Commission to take into account the efficiency, effectiveness, and adequacy of service. The RD found that Twin Lakes is not providing adequate service to its customers and therefore, the rates should be set at a reasonable level calculated to reflect the level of service.²¹ As the RD correctly points out if rates are set too high not only would it violate the basic principles of rate setting, such as gradualism and avoiding rate shock, but it would also result in customers not being able to afford water service.²²

I&E requests that the Commission reject Twin Lakes Exception No. 2 and accept the ALJ's recommendation and find that Twin Lakes has failed to support its claim that the ALJ erred when considering affordability.

3. Reply to Twin Lakes Exception 3: The ALJ Properly Found that Twin Lakes Has Failed to Provide Safe and Adequate Service (Twin Lakes Exceptions pp. 5-6; RD pp. 77-83)

As explained in detail in the I&E Reply to Twin Lakes Exception No. 1, the ALJ correctly found that Twin Lakes is not providing safe and adequate service. In

²⁰ *Pennsylvania Public Utility Commission v. Pennsylvania Gas & Water Company*, 1993 Pa PUC Lexis 61.

²¹ RD, pp 82-83.

²² RD, p. 87.

Exceptions, counsel for Twin Lakes notes, “[t]he core issue in this matter is that Twin Lakes operates a system that is in poor condition, a Well No. 1 that has failed, a Well No. 2 that requires replacement, significant UFW losses, all of which will require Twin Lakes to, of necessity, invest at least an additional \$3.1 million of capital improvements.”²³ I&E agrees that the system is in poor condition given that Well No. 1 failed Well No. 2 is in danger of failing and needs replaced, and unaccounted-for water levels are excessively high. However, even when given the opportunity to implement rate increases, the utility did not carry out the measures it agreed to carry out to curb the unaccounted-for water problems.²⁴ Additionally, the Company has failed to proactively remedy these concerns. Despite being aware of its ongoing service issues, the Company waited until August 2019 to apply for a PENNVEST loan to fund system improvements.²⁵ I&E questioned the Company’s delay in testimony but the Company failed to respond; therefore, the reasons for the delay are still unknown. To assert now that Twin Lakes will remedy the problems if simply given a higher level of rate relief is, at best, speculative considering past history has shown an unwillingness to correct these problems even when provided with rate relief.

Twin Lakes, in its Exceptions, joins OCA in encouraging the Commission to initiate a Section 529 proceeding as part of the Final Order of this current rate proceeding.²⁶ I&E would not oppose a Section 529 proceeding be initiated for Twin

²³ Twin Lakes Exceptions, p. 5.

²⁴ RD, p. 82.

²⁵ I&E M.B., pp. 52-53.

²⁶ Twin Lakes Exceptions, p. 6.

Lakes as I&E stated in Testimony it would be within the public interest to keep rates affordable for Twin Lakes' customers and explore other possibilities such as a sale to another investor-owned utility or a Section 529 proceeding.²⁷

The Commission should reject Twin Lakes' Exception No. 3 as the evidence in the record overwhelmingly proves that Twin Lakes has failed to provide its customers with adequate and reasonable service.

4. Reply to Twin Lakes Exception No. 4: The ALJ Properly Concluded that Twin Lakes Should Not Be Allowed to Claim its Acquisition Adjustment into Perpetuity (Twin Lakes Exceptions pp. 6-7, RD pp. 15-20).

In the instant proceeding the Company claimed a \$54,406 positive acquisition adjustment related to it being acquired by Middlesex Water Company in 2009. By way of background, in November of 2009 when Middlesex Water Company acquired Twin Lakes the purchase price was \$99,410 while the net book value was \$79,726 thus resulting in a \$19,684 positive acquisition adjustment. While the Commission approved the acquisition itself, it never specifically approved any acquisition adjustment.²⁸ In its 2011 rate case, the Company recalculated the original acquisition adjustment because it failed to include accumulated depreciation, which resulted in a revised acquisition adjustment of \$71,440.²⁹ In its 2015 rate case, Twin Lakes appropriately amortized this amount to reflect that four years lapsed between the 2011 and 2015 rate cases, which resulted in a \$54,406 claim. However, in this rate proceeding, the Company has failed to

²⁷ I&E St. No. 2, p. 39.

²⁸ I&E St. No. 3, p. 14.

²⁹ I&E St. No. 3, p. 15.

continue to amortize the adjustment to reflect that another four years has lapsed since the 2015 case and contends that it is entitled to an acquisition adjustment of \$54,406, which the ALJ properly denied. Instead, the ALJ appropriately accepted I&E's recommended acquisition adjustment of \$36,018, a reduction of \$18,388 to the Company's claim, to appropriately reflect that this adjustment should be amortized since the Company's 2015 rate proceeding.

As was explained in both Testimony and the I&E Main Brief, I&E does not dispute the \$71,440 acquisition adjustment claim that was updated in the 2011 rate case; however, to determine an appropriate amount for recovery, that \$71,440 claim must be amortized from the date of the acquisition in November 2009 to this 2019 rate case. It seems evident that Twin Lakes was aware at some point that it needed to properly amortize this acquisition adjustment as between the Company's 2011 and 2015 base rate cases a proper amortization was reflected and the amount claimed was reduced from \$71,440 in 2011 to \$54,406 in 2015.³⁰ In the RD, ALJ Guhl agrees with I&E that this acquisition adjustment should not be allowed to continue in perpetuity noting that "[i]t would be improper not to reflect a reduction to the value of the acquisition adjustment because to do so would necessarily allow the Company to earn a return on the overpayment for this system in perpetuity."³¹ The ALJ then explains that the "...annual amortization expense is properly reflected under operation and maintenance expense

³⁰ I&E St. No. 3-SR, p. 11; I&E MB, p. 8.

³¹ RD, p. 20.

adjustments in I&E's recommendation. As such, it is recommended that the Company be allowed a residual \$36,018 acquisition adjustment as of September 30, 2019."³²

Twin Lakes claims, in its Exceptions, that a corresponding acquisition adjustment should be included as an O&M expense item.³³ Twin Lakes raised the same argument in its Main Brief.³⁴ I&E responded to Twin Lakes in Reply Brief where it was explained that the annual amortization expense of \$3,572 was properly reflected under operation and maintenance adjustments in I&E's recommendation tables in Appendix D of its Main Brief.³⁵

Lastly, Twin Lakes now requests in Exceptions, that the annual amortization occur over one of two timeframes; either the 24-month timeframe it projects for a subsequent base rate case, or the 39-month period proposed by I&E as the timeframe over which rate case expense should be normalized.³⁶ This proposal must be rejected as it is wholly inappropriate for Twin Lakes to propose an amortization period for the first time in the Exception phase of litigation. In contrast, I&E provided testimony³⁷ stating that a 20-year amortization period beginning in November 2009 was appropriate as it was the same amortization schedule used in the Company's 2015 rate proceeding. The Company failed address I&E's 20-year amortization recommendation in its responsive testimony, through cross-examination at hearings, or in its briefs. Therefore, the Company's attempt to

³² *Id.*

³³ Twin Lakes Exceptions, p. 6.

³⁴ Twin Lakes MB, p. 7.

³⁵ I&E MB, p. 5.

³⁶ Twin Lakes Exceptions, p. 7.

³⁷ I&E St. No. 3, p. 19; I&E St. no. 3-SR, pp. 6, 11.

argue for an abnormally short 24-month or 36-month amortization period for the first time in Exceptions is unsupported, improper and must be rejected.

The Commission should reject Twin Lakes Exception No. 4 because it fails to raise valid arguments challenging the RD. I&E requests that the Commission accept the ALJ's recommendation and find that the Company's claim for acquisition adjustment be reduced by \$18,388 resulting in a total positive acquisition adjustment allowance of \$36,018.

III. CONCLUSION

For the reasons stated herein, the Bureau of Investigation & Enforcement respectfully requests that the Commission deny the exceptions of Twin Lakes Utilities, Inc. and adopt the Recommended Decision of the Administrative Law Judge Guhl with only the limited modification to Table 1 addressed in the I&E Exceptions.

Respectfully submitted,



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Prosecutor

PA Attorney ID No. 320526

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Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg PA 17120

Dated: March 9, 2020

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Pennsylvania Public Utility Commission :
 :
 v. : Docket No. R-2019-3010958
 :
 Twin Lakes Utilities, Inc. :

CERTIFICATE OF SERVICE


I hereby certify that I am serving the foregoing **Reply Exceptions** dated March 9, 2020 in the manner and upon the parties listed below in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a party):

Served via First Class and Electronic Mail

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