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November 9, 2023

Via Electronic Filing

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

Re: Columbia Water Company; 2023 General Base Rate Increase Filing; Docket No. R-2023-3040258; **COLUMBIA WATER COMPANY'S REPLY EXCEPTIONS**

Dear Secretary Chiavetta:

Enclosed for filing with the Commission are Columbia Water Company's Reply Exceptions in the above-referenced matter.

A word copy of these Reply Exceptions are being provided to the Office of Special Assistants under separate cover.

If you have any questions concerning this filing, please contact me.

Very truly yours,

/s/ Whitney E. Snyder

Whitney E. Snyder
Thomas J. Sniscak
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Counsel for Columbia Water Company

WES/das
Enclosure

cc: ra-OSA@PA.GOV
Per certificate of service

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket No. R-2023-3040258
	:	
	:	
Columbia Water Company	:	

COLUMBIA WATER COMPANY REPLIES TO EXCEPTIONS

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Dated: November 9, 2023

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I. <u>INTRODUCTION AND SUMMARY OF REPLIES TO EXCEPTIONS</u>

Columbia Water Company ("Columbia Water" or "Company") files with the Pennsylvania Public Utility Commission ("PUC" or "Commission) these Replies to Exceptions of the Office of Consumer Advocate ("OCA") and the Bureau of Investigation and Enforcement ("I&E"), and the Office of Small Business Advocate ("OSBA") to the October 23, 2023 Recommended Decision ("RD") of Administrative Law Judges Mary D. Long and Charece Z. Collins.

The law dictates that the Commission must provide the Company with a fair return of and on its investment. Otherwise, the Commission's decision would run afoul of the principles set forth in *Bluefield Waterworks & Improvement Company v. Public Service Commission*, 262 U.S. 679 (1923) and *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 592 (1944):

> Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility of its property in violation of the Fourteenth Amendment.[1]
>
> From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.[2]

Thus, rate of return is determined on financial investment standards considering risk of similar companies and the ability to maintain credit and attract capital. ***Without adequate credit and capital, a utility cannot obtain the resources it needs to serve customers safely and reliably***.

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1 *Bluefield Waterworks & Imp. Co. v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679, 690 (1923) (*Bluefield*).

2 *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (*Hope*).

Despite the well-developed law on return of and on utility property, I&E and OCA justify their respective Exceptions with arguments that boil down to rates should be lower to save ratepayers money.[3] These arguments would have the Commission violate the tenets of *Hope and Bluefield* discussed above and encourage the Commission to engage in arbitrary decision-making. Moreover, OCA and I&E's arguments based on mitigating alleged impacts to customers lack any evidentiary support.

Even if considering customer impacts was the legal standard here, which it is not, ***there is absolutely no evidence in the record that the proposed rate increase of 14.2% will have any negative impact on any single Columbia Water customer or Columbia Water customers as a whole***. No customers testified at the public input hearings. No party presented evidence[4] of any actual negative impact on ratepayers. No party presented evidence that customers are having trouble paying bills at current or proposed rates. No party presented evidence that the pandemic or inflation have impacted customers such that the proposed rate increase would create a hardship to any specific ratepayer or ratepayers as a whole.

Moreover, the Company exercised its discretion to provide significant mitigation of rate increase impacts in its rate request. The proposed rate increase was already mitigated with a Black Box Customer Discount at the discretion of the Company. The Black Box Customer Discount resulted in the Company discounting its rate increase request by 294,928, or 23%, for the benefit of customers. The Company further mitigated the rate increase because it is not seeking to recover from customers in this proceeding any of the negative impact that the pandemic had on the

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3 *See, e.g.* OCA Exceptions at pp. 3, 6, 9, 11, 16-18; I&E Exceptions at p. 6.

4 While two pro se complaints were filed, *pleadings are not evidence* and the Complainants failed to submit any evidence into the record.

Company.[5] This is another mitigation to the benefit or ratepayers that the Company chose at its discretion. There is no evidentiary basis to make any decision to approve lower than requested rates due to alleged impacts on customers particularly where, as here, the Company has already exercised its discretion to significantly mitigate the impact of rates on its customers.

The record evidence clearly demonstrates not only that the Company's proposed rate increase is just and reasonable, but that the Company needs the rate increase it has requested to continue to provide excellent quality of service, continue making capital improvements, and attract investors to provide ready access to capital.[6] OCA and I&E's arguments, if adopted, will have serious negative impacts including potential loss of investors and inability to raise adequate amounts of capital to provide excellent quality of service and continued capital improvements.

For example, the OCA and I&E's penal hypothetical capital structure recommendation, in combination with their respective unreasonably low return on equity ("ROE") recommendations,[7] violates the tenets of *Hope and Bluefield* and thus violates the tenants of traditional ratemaking. Both OCA and I&E base their arguments on alleged impacts to ratepayers.[8] But there is no evidence of such alleged impacts and, thus, these arguments cannot be relied upon. As stated by the Commonwealth Court regarding rate of return:

> Although the Commission, within the limits of the statute, has certain discretionary powers (*Philadelphia v. Pennsylvania Public Utility Commission*, 164 Pa.Super. 96, 103, 63 A.2d 391), it is not justified in making any finding as to rate of return to be allowed a

[5] *Pa. Pub. Util. Comm'n v. Philadelphia Gas Works*, Docket Nos. R-2023-3037933 *et al.,* Opinion and Order at 68 (Order entered November 9, 2023) (approving PGW recovery over next three years of over $30 million in pandemic related costs).

[6] *See generally* Columbia Water MB and RB.

[7] Under I&E's recommended rate of return, the Company would receive an overall cost of capital of 5.5%. I&E M.B. at 14. Under the OCA's recommended rate of return, the Company would receive an overall cost of capital of 6.31%. OCA M.B. at 34.

[8] I&E Exceptions at p. 6; OCA Exceptions at pp.

> utility without substantial and competent evidence presented to support it.[9]

Moreover, as discussed by the Commission in a recent Order, the Commission should not engage in arbitrary decision-making to justify an end result but must weigh the evidence before using traditional ratemaking methodologies in setting just and reasonable rates consistent with *Bluefield* and *Hope*.[10] From a practical standpoint, an insufficient return would harm the Company's ability to attract investors, force the Company to take on additional debt to finance Company operations, and potentially cause a default of the Company's loan obligations, resulting in higher interest rates and higher costs to customers.

If the Commission is going to consider impacts to ratepayers, it should carefully weigh what is in fact best for ratepayers. Adopting OCA and I&E arguments may save ratepayers money in the short-term but will place ratepayers' provider of essential water utility in financial jeopardy, negatively impact the ability to attract adequate capital to provide and thus receive excellent quality of service, and result in higher debt costs in the future. History makes clear that arbitrarily low rates result in delay of necessary and policy driven infrastructure maintenance and improvements and, ultimately, unsafe service. What is best for the long-term benefit of both ratepayers and the Company is to apply traditional ratemaking methodologies to the actual record evidence and grant the Company's requested rate increase so it can continue providing excellent quality of service.

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[9] *U.S. Steel Corp. v. Pa. Pub. Util. Comm'n*, 390 A.2d 849, 863 (Pa. Cmwlth. 1978) (quoting *Pittsburgh v. Pa. Pub. Util. Comm'n*, 126 A.2d.777, 785 (Pa. Super. 1956)).

[10] *Pa. Pub. Util. Comm'n v. PECO Energy Co. – Gas Division, et al.*, Docket Nos. R-2020-3018929, *et al.*, 2021 WL 2645922, at *21-23 (Opinion and Order entered Jun. 22, 2021).

II. REPLIES TO EXCEPTIONS

A. The RD Correctly Found Columbia Water's Actual Capital Structure should be used. Reply to OCA Exception 4 and I&E Exception 2.

The Commission should reject OCA and I&E's proposals to utilize a hypothetical capital structure. OCA and I&E's positions are contrary to Commission precedent and fail to distinguish the Commission's correct decisions in prior Columbia Water base rate proceedings and ask the Commission to make an arbitrary decision that, if adopted, would be detrimental to not just the Company but also its customers.[11] Moreover, contrary to the OCA's assertions the RD did not improperly shift any burdens. As explained at length in the Company's briefs, the Company presented substantial evidence to show that its actual capital structure is reasonable and in fact benefits ratepayers.[12]

The Commission found in two previous Columbia Water cases that its capital structure was not too heavily weighted on the equity side.[13] In both cases, the Company had a capital structure that was similar to, but slightly ***more equity rich*** than Company's requested capital structure here,[14] yet, in both instances the Commission held that the Company's "capital structure is not

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11 Columbia Water M.B. at 56; R.B. at 35, 36.

12 Columbia Water M.B. at Section VII.B.; R.B. at Section VII.B.

13 *Pa. Pub. Util. Comm'n v. Columbia Water Co.*, Docket Nos. R-2008-2045157, *et. al.*, 2009 WL 1708836 (Opinion and Order entered Jun. 10, 2009) (*CWC* 2009); *see also Pa. Pub. Util. Comm'n, et. al. v. Columbia Water Co.*, Docket Nos. R-2013-2360798, *et al.*, 2014 WL 316891, at *25 (opinion and Order entered Jan. 23, 2014) (*CWC 2013*).

14

Comparison of Columbia Water's Capital Structure		
Year	Debt	Common Equity
2008	35.8%	64.2%
2013	35.6%	64.4%
2023	36.66%	63.34%

unreasonable or uneconomical under the rationale of the *Carnegie* decision."[15] The *Carnegie* decision explains:

> [t]he Commission has the duty to regulate utilities in a manner which provides customers with reliable service at reasonable cost. This is not to say that we may mandate to regulated utilities the proportion of debt and equity contained in their capital structures. Rather, the actual capital structure is a matter within the discretion of corporate management; however, this does not preclude the commission from determining that a particular utility's capital structure is unreasonable and uneconomical when balancing the goals of safety, prudent management, and economy and utilize a hypothetical capital structure for rate-making purposes.[16]

In both the 2008 and 2013 Columbia Water rate cases, the Commission found that the Company's capital structure did not violate the *Carnegie* decision, as the capital structure was not found to be unreasonable or uneconomic.

The OCA and I&E both fail to make any valid argument distinguishing these prior decisions or rebutting the Company's substantial evidence that its capital structure is reasonable.[17] Neither the OCA or I&E have provided any evidence suggesting that the Company abused its managerial discretion in obtaining the present capital structure, nor have they shown or even alleged that Columbia Water's capital structure is unreasonable and uneconomical when balancing the goals of safety, prudent management, and economy. Thus, the Company's financing is largely unchanged from prior years and prior Commission decisions and the Company should receive the same treatment from the Commission in this proceeding.

Nonetheless, both parties again ask the Commission to engage in arbitrary decision-making based on alleged costs to ratepayers, including broad and unsupported arguments that the pandemic

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[15] *CWC 2009*, 2009 WL 1708836 (citing *Pa. Pub. Util. Comm'n v. Carnegie Natural Gas Company*, Docket Nos. R-79100977, *et al*., 1980 WL 140939, at *11 (Opinion and Order entered Jul. 25, 1980) (*Carnegie*)).

[16] *Carnegie*, 1980 WL 140939, at *11 (citing Garfield and Lovejoy, "Public Utility Economics." Prentis-Hall, 1964, p.130).

[17] Columbia Water M.B. at 51-52; R.B. at 35-36

and inflationary pressures merit use of a hypothetical capital structure. These arguments fail for three reasons. First, these arguments misconstrue the law, logic and reason. Per *Carnegie* that the Commission is to balance "the goals of safety, prudent management, and economy."[18] Economy cannot mean, as I&E and OCA posit, greater costs to customers because a higher equity ratio obviously results in higher rates, so under I&E and OCA's version of the "economy" any equity would be uneconomic. That is obviously incorrect. The end result of a higher rate due to equity to debt ratio is not the definition of uneconomic. This argument should be denied.

Second, there is no record evidence that the proposed rate increase will negatively impact consumers or that consumers are negatively impacted by the pandemic and/or inflationary pressures such that the rate increase would cause a hardship.

Third, the Commission has already rejected these arguments in the Company's 2008 and 2013 rate cases.

> The OCA and the OTS concluded that their recommended 50%/50% hypothetical capital structure is reasonable for Columbia and avoids burdening Columbia's ratepayers with the excessive rates that would result from using Columbia's atypically high common equity ratio.[19]

And, as I&E argued in the Company's 2013 rate case:

> In its Reply Exceptions, I&E reiterates that the capital structure utilized by Columbia is not in line with its historical capital structure, but is in fact more heavily weighted toward equity than the Company has been in any of the past five years. I&E also contends that Columbia's actual capital structure is not in line with the industry average, and places an unfair financial burden upon customers.[20]

In both instances, the Commission rejected these arguments, finding in the Company's 2013 rate case that "adopting a hypothetical 50/50 capital structure, rather than the Company's

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18 *Carnegie*, 1980 WL 140939, at *11.
19 *CWC 2009*, 2009 WL 1708836.
20 *CWC 2013*, 2014 WL 316891, at *24.

actual capital structure, would be somewhat arbitrary, and would fail to recognize the benefits to ratepayers of the Company having ready access to capital markets due to its strong capital structure."[21]

The practical impacts of utilizing a hypothetical capital structure will be detrimental to ratepayers and the Company. Adopting a hypothetical capital structure would be akin to providing an investor with a debt return for a portion of their investment. To satisfy the investor's expectations, the Company would then be required to give the investor a higher return on the equity portion of its investment, which the Company certainly would not achieve under the ROE proposals of the OCA and I&E.[22] This would leave Columbia Water as an unattractive investment leading to investors walking away.[23] As Mr. D'Ascendis testified this could be problematic because it would require the Company to increase its financial risk and obtain more debt financing at higher, detrimental interest rates:

> As mentioned on page 6 of my Rebuttal Testimony, CWC's relatively strong capital structure provided financing flexibility and access to capital when required, and that was evidenced by relatively low interest rates as compared to my Utility Proxy Group. The Opposing Witnesses' proposed hypothetical capital structures put CWC's current financing flexibility and access to capital at reasonable terms in danger. As discussed in more detail in Company Witness David T. Lewis' rejoinder testimony, the Opposing Witnesses' hypothetical capital structure would cause the Company to default on at least one debt covenant, which would then trigger several other defaults due to cross default provisions in that financing instrument and their other financing instruments. Because of this, it could be assumed that cost of marginal debt (if the Company could raise any) would be consistent with below investment grade, or "junk" bonds. As the Company's 2023 debt issuances already indicate a BB credit rating, the Company's increased debt to equity ratio would lead to further credit degradation. As shown on CWC Exhibit No. DWD-2RJ, the yield on single B and CCC utility bonds non-investment grade bond yields

21 *Id.* at *25.
22 CWC St. 1-RJ at 4:1-5.
23 CWC St. 4-RJ at 8:5-11.

> range from 10.59% to 13.38% on July 31, 2023. These yields both exceed the Opposing Witnesses' recommended ROEs in this proceeding.[24]

As further explained by Company witness Lewis:

> In fact, Mr. Garrett goes so far as to suggest the Company should take on more debt. However, despite Mr. Garrett's myopic and ill-informed suggestion, the reality is the Company cannot take on any significant amount of additional debt because the Company's Loan Agreement with M&T Bank, which covers all of the Company's loans with the bank, constrains the Company's ability to take on more debt. I have included the Loan Agreement as **CWC Exhibit DTL-1RJ.** Specifically, the loan agreement has a cash flow to debt service coverage ratio requirement and a maximum debt to capitalization ratio requirement. CWC has taken out two debt issuances in 2023 and CWC is already very close to the cash flow to debt service coverage ratio limitation, and taking on additional debt would more likely than not cause a default on these loans. I have included the calculations for the debt limitations associated with the loan agreements as **CWC Exhibit DTL-2RJ**. This default would have a domino effect as most, if not all, of the Company's loans have cross default provisions, meaning default on one loan results in defaults on the Company's other loans. Witness Garrett's suggestion to take on more debt would likely place the Company in financial ruin to the detriment of customers, not just shareholders. This is also a reason it is so important to have shareholders and investors that are incentivized to provide the necessary capital when such capital cannot be reasonably raised in the debt market.
>
> Based on my experience as President and General Manager of a successful water company, Mr. Garrett's suggestions are not an appropriate, prudent, or reasonable approach to managing a water company's capital.[25]

Thus, employing a hypothetical capital structure would be to the detriment of the Company's customers, not to their benefit. Contrary to the OCA and I&E's claims, the Company's current capital structure is a significant benefit to customers providing Columbia Water access to low-cost financing. The OCA and I&E's Exceptions should be denied.

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24 CWC St. 4-RJ at 6:5-21.

25 CWC St. 1-RJ at 4:11 – 5:11 (emphasis in original).

B. The RD Correctly Rejected I&E's Proxy Group. Reply to I&E Exception 1.

The RD correctly agreed with both the Company's and the OCA's expert witness testimony that Essential Utilities Inc. ("Essential") is appropriate to include in the proxy group. I&E witness Keller's proxy group was an outlier because he excluded Essential where Mr. D'Ascendis' and OCA Witness Garrett's respective proxy groups included Essential. I&E witness Keller excluded Essential "because it violated his criteria that 50% or more of the company's revenues be generated from regulated water utility operations." I&E M.B. at 19. As the RD correctly found, Essential is appropriate to include in Mr. D'Ascendis' proxy group because the better measure is earnings, not revenue as Mr. Keller suggests.[26] Measures of income are far more likely to be considered by the financial community in making credit assessments and investment decisions than are measures of revenue.[27]

I&E now argues for the first time that the Commission has set a "standard" for determining whether a company should be included in a proxy group based on percentage revenues from water utility operations.[28] I&E has waived this argument by not previously raising it in testimony or briefs and it should be rejected for this reason.[29]

I&E's Exception should be denied.

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26 Columbia Water M.B. at 61-62.

27 CWC St. 4-R at 85:3-11.

28 I&E Exceptions at pp. 4-5.

29 *Pa. Pub. Util. Comm'n v. Columbia Gas of Pennsylvania, Inc.*, Docket Nos. R-2021-3024296 *et. al.*, (Order entered December 16, 2021) ("By failing to preserve the issue in briefs, Mr. Culbertson has denied the ALJ the opportunity to provide his position for our consideration. Thus, …we also find that by failing to seek interlocutory review of the issue as our Regulations allow, and then ***by failing to brief the issue as our Regulations require***, ***Mr. Culbertson has not preserved it for our review***."); *see also* 52 Pa. Code § 5.533(c) ("Statements of reasons supporting exceptions must, insofar as practicable, incorporate by reference and citation, relevant portions of the record and passages in previously filed briefs."); *Wilson v. Columbia Gas of Pennsylvania, Inc.,* Docket No. C-2013-2367375 2013 WL 6835138 at *5 (Opinion and Order entered Dec. 19, 2013) ("[N]ew arguments may not be raised at the exception stage of a proceeding, as it deprives parties of the opportunity to respond.") (citing *Application of PPL Electric Utilities Corporation*, Docket No. A-2011-2267349 (Order entered July 16, 2013)).

C. The RD Correctly Rejected I&E's DCF and CAPM Results. Reply to I&E Exception 3.

Based on the correct finding that I&E's proxy group was an outlier because it did not include Essential, the RD correctly rejected I&E's DCF and CAPM results. As explained at length in the Company's briefs, the RD was correct to reject I&E's common equity recommendation on this basis.[30]

In its Exceptions, I&E now argues that the RD was incorrect to give weight to CAPM results based on an extremely misleading argument that cases decided in 2017 and 2018 support the notion that "[j]ust recently, the Commission affirmed reliance primarily on the DCF and rejected giving weight to the other methodologies."[31] This argument lacks any credibility because it wholly ignores what the Commission has in fact decided in the ***recent*** past. Specifically, the Commission in 2022 recognized that multiple methodologies of calculating return on equity are necessary for responsible ratemaking.[32] The Commission utilizes the Capital Aset Pricing Model ("CAPM") as a check on the Discounted Cash Flow ("DCF") to make upward adjustments to the cost of common equity set quarterly for the Distribution System Improvement Charge ("DSIC") surcharge purposes, most recently finding an average DCF of 8.0 and a CAPM of 10.42 to order a 9.65% return on equity for water companies.[33] In selecting 9.65%, which is beyond the midpoint between the DCF and CAPM and much closer to the CAPM that the DCF, the Commission clearly gave more weight to the CAPM. This decision was just last month (October 2023) when setting return on equity for the DSIC.

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[30] Columbia Water M.B. at Section VII.D.1; R.B. at Section VII.C.

[31] I&E Exceptions at pp.7-8.

[32] RD at 59-60 (quoting *Pa. Pub. Util. Comm'n v. Aqua Pa., Inc.*, Docket No. R-2021-3027385 at 154 (Opinion and Order entered May 16, 2022) ("*Aqua*")

[33] *Bureau of Technical Utility Services Report to the Commission Regarding Quarterly Earnings of Pennsylvania Utilities for the Year ended June 30, 2023*, Docket No. M-2023-3042679, Report at 27 (issued October 19, 2023).

I&E's argument not to give weight to CAPM results also lacks any credibility because on the one hand, I&E argues for lower rates due to alleged impacts of the pandemic and inflation on ratepayers that has no evidentiary support,[34] but ignores that the Commission has specifically recognized the resulting interest rate hike and volatility have impacts return on equity that require consideration of the CAPM.[35]

I&E's Exception should be denied.

D. <u>The Company's Cost of Equity Should Not Be Set Any Lower Than 9.55%. Reply to OCA Exceptions 5 and 6.</u>

In Exception 5, OCA argues at length that its ROE position should be accepted, and the Company's ROE position should be rejected, and that the ALJs erred in using the Company's ROE position. These contentions are all incorrect. As the Company has explained at length in its briefs, Company Witness D'Ascendis presented substantial evidence that the Company's ROE recommendation is most reasonable.[36] The Company has also explained at length based on Mr. D'Ascendis testimony that OCA's ROE recommendation is completely unreasonable and confiscatory.[37] The Company excepted to the RD's ROE analysis and determination and stands by that exception. However, the RD's ROE determination is certainly more reasonable than OCA's position and a much more balanced approach. Under no circumstances should the Commission order an ROE for the Company lower than 9.55%.

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[34] I&E Exceptions at p. 7.

[35] *Pa. Pub. Util. Comm'n v. Aqua Pa., Inc.*, Docket No. R-2021-3027385 (Opinion and Order entered May 16, 2022) ("We are persuaded by the arguments of Aqua that the ALJ erred by concluding I&E used its DCF and CAPM results to determine Aqua's ROE. In this regard, we note that although I&E did use its CAPM as a comparison to its DCF result, *it made no CAPM based adjustment to its final ROE recommendation*. I&E M.B. at 47. As Aqua points out, infra, the U.S. economy is currently in a period of high inflation. To help control rising inflation, the Federal Open Market Committee has signaled that it is ending its policies designed to maintain low interest rates. Because the DCF model does not directly account for interest rates, consequently, it is slow to respond to interest rate changes. However, I&E's CAPM model uses forecasted yields on ten-year Treasury bonds, and accordingly, its methodology captures forward looking changes in interest rates.").

[36] Columbia Water M.B. at Section VII.D.1; RB at Section VII.C.

[37] Columbia Water M.B. at 80-83; RB at 45-46.

In Exception 6, OCA makes several meritless arguments about why an ROE of 9.55% is too high. These arguments defy logic and reason and seek the Commission to engage in arbitrary decision-making.

First, the OCA believes the RD should have lowered the ROE because it adopted an actual capital structure which makes the Company less risky. The RD was correct not to make a downward adjustment due to capital structure-based risk (financial risk) because the RD also refused to make an upward adjustment for business risk. Moreover, the RD was correct in finding that use of an appropriate capital structure extinguishes the need to adjust for financial risk.[38] If (and only if) the Commission grants the Company's Exception that ROE should be adjusted upward for business risk, the Company also agrees that, as Mr. D'Ascendis testified, it would be appropriate to make a downward adjustment to ROE of .11%.[39] The Commission cannot, as OCA would have it, only make adjustments for financial risk without consider business risk. Reason and logic dictate that if the Commission makes a downward adjustment for financial risk, it should likewise make an upward adjustment for business risk of 1.0%.[40]

Next, the OCA makes various statements clearly intended to convince the Commission to make arbitrary decisions to lower rates. For example, OCA states: [t]he return on equity recommended by the ALJs, as applied to the Company's capital structure ratios, contributes significantly to the ALJs' overall recommendation that CWC be permitted to increase base rates by $944,893, or 95% of CWC's filed request."[41] There is absolutely no basis in the law or traditional ratemaking principles to make a ROE determination based on how much the ROE impacts the overall rate increase or what percentage of the requested increase is granted. This is OCA asking the Commission to make an ROE recommendation based on the impact of overall

38 RD at 64.
39 Company MB at 74-75.
40 Company MB at 69-74.
41 OCA Exceptions at p. 17.

increased rates to ratepayers. Again, there is absolutely no evidence of negative impacts to ratepayers. The Commission must base its decisions on evidence and make reasoned decisions and thus should reject OCA's argument.

OCA also erroneously argues that because a hypothetical capital structure results in higher rates and because the chosen cost of equity results in higher rates, the capital structure and cost of equity are therefore uneconomic and unreasonable.[42] No equity percentage would ever be economical or reasonable under this flawed reasoning. So too regarding the OCA's arguments regarding the percentage of the increase in the Company's revenues attributable to return on equity. How a revenue requirement is developed and cost of equity determined has nothing to do with how much of a rate increase is associated with cost of equity. These arguments have no merit.

Finally, OCA argues that a 9.55% cost of equity will unreasonably burden consumers. But there is absolutely no evidence that rates will burden any customer, let alone an unreasonable burden. The Commission cannot make arbitrary decisions with no record support. The OCA's Exceptions should be denied.

E. <u>The RD Correctly Rejected OCA's Proposal to Average Materials and Supplies Expense. Reply to OCA Exception 1.</u>

The OCA's comparison to cost data from as early as 2018 through 2021 is inappropriate and should not be a valid basis to conclude that the level of materials and supplies expense during the Historic Test Year ("HTY") is abnormal. As Company witness Shambaugh testified, cost data from 2020 no longer represents the costs to operate the Company.[43] This statement is likewise applicable to cost data from 2018 and 2019. The Company proved prices have been substantially increased by the general conditions of the economy since 2020, having been plagued by historic inflation levels and supply chain pressures.[44] Moreover, the Company provided explicit evidence

42 OCA Exceptions at p. 18.
43 CWC St. 2-RJ at 9:12-15.
44 CWC St. 2-RJ at 7:15 – 8:10.

that the Company is on pace to (1) substantially exceed HTY materials and supplies expense and (2) even *exceed* its Future Test Year ("FTY") claim in this case:

> Moreover, the Company has taken a conservative approach in setting its claimed level of materials and supplies expense. The Company is already on track to exceed the claimed level of materials and supplies expense based on current levels of spend. For example, for the period January 1, 2023 through August 7, 2023, the total expensed was $293,841. That is an average of $1,348 per day ($293,841 / 219 days = $1,342 per day). Annualized, that works out to $489,830 ($1,348 x 365 days = $489,830). The $489,830 is about $112,440 more than the HTY 2022 amount of $377,390 and $57,430 more than the FTY 2023 amount of $432,400.[45]

As the record evidence demonstrates, the Company's claimed level of materials and supplies expense of $432,400 actually understates the Company's actual, going-forward costs for materials and supplies.[46]

Where, as here, the Company has provided reasonable evidence that costs represent a normal level of cost going forward, averaging costs from previous years is not appropriate. For example, in *Pennsylvania Public Utility Commission v. Columbia Water Co.*, the Office of Trial Staff ("OTS") recommended that the Commission average the Company's claim for office expense and utilities over a period of three years.[47] In rejecting OTS' recommendation and adopting the Company's claim, the Commission stated, "Columbia's rebuttal claim is known and measurable, using actual 2008 figures."[48]

Conversely, the OCA makes vague and speculative judgments about the future of the economy without any compelling evidence. As the Company indicated in its Main Brief, the little evidence the OCA provided either does not support the OCA's position or is merely a politically

45 CWC St. 2-R at 15:14-21.
46 Columbia Water M.B. at 29.
47 *CWC 2009*, 2009 WL 1708836.
48 *Id*.

motivated report designed to reinforce a biased narrative about current supply chain pressures.[49] Ms. Rogers certainly is not qualified to make such general claims about the future of the economy,[50] nor has the OCA presented any independent study or analysis that could lead a decision maker to reasonably conclude the OCA is correct. The OCA's suggestion that cost data that pre-dates the worst economic effects of the pandemic now represent a 'normal' level of expense strains credulity and is not reasonable. OCA's Exception should be denied.

F. <u>The RD Correctly Rejected OCA's Proposed Adjustment to Normalize Other – Maintenance Expense. Reply to OCA Exception 2.</u>

Based upon the same flawed reasons it recommends an adjustment to the Company's materials and supplies expense, the OCA argues that the Company's claim for other-maintenance expense should be averaged over the years 2020, 2021, and 2022. The OCA reasons that an average adjustment is necessary to prevent overcollection from customers due to high costs in 2022, that the Company did not provide any analysis to show the actual impact of inflation and supply chain shortages, and that the burden of proof should lie with the Company to demonstrate recovery of these costs.

The OCA's arguments fail for the same reasons set forth above in response to the OCA's materials and supplies adjustments. However, there are some additional points the Commission should consider. First, it is well-settled that the Company is entitled to recover known and measurable changes to reasonably incurred and prudent expenses from its customers.[51] Here, the Company has shown that its increased costs to other-maintenance expense and its other expenses are known and measurable. The OCA has not and cannot challenge the level of expense that was incurred by the Company in the HTY. Such costs are consistent with and currently understate

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[49] Company M.B. at 27-28.
[50] OCA M.B. at 2-3; *see also* OCA St.1, App. A.
[51] *UGI Corp. v. Pa. Pub. Util. Comm'n*, 410 A.2d 929, 931 (Pa. Cmwlth. 1980).

what the Company is currently incurring to provide service to its customers in the FTY. Utilizing actual costs is not a guarantee of recovery of historic costs, but the most reasonable and accurate basis for the FTY.

Even the OCA's Exceptions show that the Company's costs have increased over the years.[52] This chart makes clear that while costs may fluctuate over the short term, it is clear that over the long term, costs continue to increase, so there is absolutely no basis to make an average based on historical costs to set future rates given what the actual cost data shows. The Company's actual cost data reflects increases that are the result of systemic economic inflation and supply chain shortages.[53] To suggest the Company's evidence of it actual costs during the HTY and to date in the FTY is insufficient proof is inconsistent with Commission precedent acknowledging that evidence of actual costs is sufficient.[54]

G. <u>The RD Correctly Rejected OCA's Proposal to Utilize a State Income Tax Rate Not In Effect During the Test Year. Reply to OCA Exception 3.</u>

The OCA opposes the use of an 8.99 percent state income tax rate because the Company's rate increase request is suspended until January 27, 2024 and, once new rates go into effect, the 8.49 percent rate will be the applicable tax rate.[55] However, the Company continues to support the use of a state income tax rate of 8.99% because that is the rate currently in effect throughout the duration of the FTY in this proceeding.[56] The OCA's concerns are also ameliorated by the Commission's requirement that future state income tax reductions be flowed-through annually

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52 OCA Exceptions at p. 5.
53 CWC St. 1-R at 3:4-19; *see also* CWC Exhibit DTL-1R.
54 *CWC 2009*, 2009 WL 1708836.
55 CWC St. 2-R at 23:3-6.
56 CWC St. 2-R at 23:6-10.

through the State Tax Adjustment Surcharge ("STAS").[57] The Company has complied and will continue to comply with these requirements.[58]

If the Commission grants OCA's exception, which is should not, the Company requests the Commission expressly hold that the Company is not required to make an adjustment for 2024 through the STAS.

H. The RD Correctly Found the Company's COSS is Adequate. Reply to OSBA Exception 2.

The Company disagrees with OSBA's arguments that the Company's Cost-of-Service Study ("COSS") was inadequate or incomplete. OSBA apparently believes the Company should incur significant and unnecessary rate case expense to have a COSS prepared that provides a customer-class demand study. Incurring this significant rate case expense is completely unreasonable for a Company of Columbia Water's size. This is particularly unreasonable where, as here, the RD and the OCA fail to provide opportunity for the Company to recover existing rate case expense in rates.[59] Requiring a customer-class demand study is also unreasonable because it is unnecessary. As the RD correctly found, the COSS and expert witness testimony sponsored by David Fox of Raftellis was adequate for parties to make class allocation recommendations and for the RD to make a decision on class allocation. The OSBA's Exception should be rejected.

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[57] *See* 52 Pa. Code § 69.52.

[58] *State Tax Adjustment Columbia Water Company*, Docket No. R-2023-3037555 (Secretarial Letter issued Jan. 11, 2023), available at https://www.puc.pa.gov/pcdocs/1770225.pdf).

[59] Columbia Water Exceptions at pp. 19-23.

III. **CONCLUSION**

WHEREFORE, for the reasons stated above, Columbia Water Company respectfully requests that the Commission deny the Exceptions of the OCA, I&E, and OSBA.

Respectfully submitted,

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Dated: November 9, 2023

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the foregoing document upon the parties, listed below, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a party).

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