

COMMONWEALTH OF PENNSYLVANIA



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March 18, 2024

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

Re: Implementation of Section 1329 of the
Public Utility Code
Docket No. M-2016-2543193

Dear Secretary Chiavetta:

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

Copies have been served as indicated on the enclosed Certificate of Service.

Respectfully submitted,

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Certificate of Service

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CERTIFICATE OF SERVICE

Implementation of Section 1329 of the : Docket No. M-2016-2543193
Public Utility Code :

I hereby certify that I have this day served a true copy of the following documents, the Office of Consumer Advocate's Comments, upon parties of record in this proceeding in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

Dated this 18th day of March 2024.

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Valuation of Acquired Municipal Water and :
Wastewater Systems – Act 12 of 2016 : Docket No. M-2016-2543193
Implementation of Section 1329 :
of the Public Utility Code :

**COMMENTS OF
THE OFFICE OF CONSUMER ADVOCATE
TO THE TENTATIVE SUPPLEMENTAL
IMPLEMENTATION ORDER**

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ATTACHMENT

I. INTRODUCTION

The Office of Consumer Advocate (OCA) appreciates the opportunity to provide comments to the Public Utility Commission's (Commission or PUC) Tentative Supplemental Implementation Order addressing Valuation of Acquired Municipal Water & Wastewater Systems under Section 1329 of the Public Utility Code (2024 Tentative Supplemental Implementation Order or 2024 TSIO). The Tentative Supplemental Implementation Order was entered on February 7, 2024 and published in the Pennsylvania Bulletin on February 17, 2024 at 54 Pa.B. 906. The OCA welcomes the additional guidance provided by the 2024 TSIO. As set forth below, there are a number of areas where the OCA has provided suggested additions or modifications to the Commission's proposals.

The OCA filed comments on August 11, 2016 in response to the Commission's first Tentative Implementation Order entered on July 21, 2016. The Final Implementation Order was entered on October 27, 2016 (*2016 Final Implementation Order or 2016 FIO*). The OCA filed comments and reply comments to the Commission's second Tentative Supplemental Implementation Order Entered September 20, 2018. The Final Supplemental Implementation Order was entered on February 28, 2019. (*2019 Final Supplemental Implementation Order or 2019 FSIO*).

Since the enactment of Section 1329, there have been twenty-seven applications filed pursuant to Sections 1329 and 1102 of the Public Utility Code.¹ The OCA has participated in each filing. The proceedings to date have provided valuable experience in understanding how applications filed under Sections 1329 and 1102 develop and proceed and how to work within the

¹ Of the twenty-seven applications filed, there is one that has not closed and six that are pending before the Commission.

very short time frame provided for the development of the record and the litigation and briefing of the case. There have been two appellate decisions that frame the understanding of what the Commission must consider. The first decision was in the first case filed pursuant to Sections 1329 and 1102. *See McCloskey v. Pa. PUC*, 195 A.3d 1055 (Pa. Commw. Oct. 11, 2018) (*McCloskey*). The second appellate decision was in *Cicero v. Pa. P.U.C.*, 300 A.3d 1106 (Pa. Cmwlth. Ct. 2023), *reh'g denied*, *Cicero v. Pa. PUC*, 2023 Pa. Commw. LEXIS 150 (Sept. 26, 2023). The OCA supports many of the concepts contained in the 2024 TSIO and submits these comments in response to the Commission's invitation to comment.

II. COMMENTS

A. Introduction

The OCA's comments to the TSIO address the proposed public hearings, including the notice and additional information that the OCA recommends be included in the rate impact information. The OCA also provides recommendations regarding the notices that are sent to the customers of the buyer and seller after the application is filed with the Commission. The OCA provides feedback on the Reasonableness Review Ratio and proposes an alternative fixed guidepost for consideration. Finally, it has been more than four years since Section 1329 issues were addressed in an implementation order so the OCA's comments provide additional areas for the Commission's consideration during this proceeding.

B. Public Hearings

The TSIO requires at least two in-person public hearings before executing the asset purchase agreement. 2024 TSIO at 3. The public hearings are to address the proposed acquisition, describe the potential rate impacts, provide an opportunity for public comments and be held within the municipal boundaries of the selling entity. *Id.* The Commission's TSIO requires the acquiring

utility to provide notice to the selling utility's customers and provides examples of notice, including direct notice. *Id.*

The OCA supports the requirement of at least two in-person hearings **before** the execution of the asset purchase agreement, and the Commission's notice and substantive requirements for the hearings. There are a few areas where the OCA would propose changes to ensure uniformity for the public and all stakeholders.

1. Notice

The OCA encourages several notice methods to effectively reach as many of the stakeholders as possible and to ensure people are aware of the two public hearings. Specifically, it is the OCA's position that the direct notification of the selling utility's customers should be done by direct outreach, including phone call, text, letter, or email. This direct notice by the acquiring utility would need to be made in cooperation with the selling utility to ensure the customers of the selling utility are properly identified and receive the direct notice.

The OCA suggests that the public meetings at which the proposed sale is to be discussed should be scheduled separately from the regular business meetings of the selling municipality. The use of a regularly scheduled public meeting held by the municipal government in which the proposed transaction is on the agenda is problematic and should not be an option used to fulfill the requirement of two public hearings. The nature of the regularly scheduled meetings is that they often include many topics on the agenda and may restrict the opportunity for the public to comment and ask questions about the transaction. The opportunity for the public to address concerns about a proposed sale and to ask questions of the public officials and the acquiring utility is often limited to very short time frames due to the other municipal business that needs to be addressed at the regularly scheduled meeting of the municipality. Of course, the municipality can include the

proposed transaction on any of its public meeting agendas. The OCA's position is that those meetings should not be used to comply with the two public hearings contemplated in the Commission's TSIO.

2. Rate Impact

The TSIO proposes public hearings to address the proposed acquisition, describe the potential rate impacts, and provide an opportunity for public comments. 2024 TSIO at 3. Regarding the potential rate impacts, or more accurately the potential bill impacts, the information provided to customers of the selling utility and to the customers of the acquiring utility is critical for all of the customers to understand the impact of the proposed sale. The bill impact information needs to be clear and complete.

The basis for the bill impact information should be the revenue requirement associated with the ratemaking rate base, calculated by the acquiring utility. That information is provided in the Section 1329 Application (see example in Attachment A) but could be provided earlier as part of the bill impact information provided at the public hearings. Using the revenue requirement calculation that is based on the proposed purchase price would provide important information to the seller's customers. The initial revenue requirement can be compared to the revenues to be collected from the seller's customers using the rates at closing. If the current rates do not collect enough revenue to cover the buyer's revenue requirement using the ratemaking rate base, then there would be an annual revenue shortfall. That shortfall and the future impact on the seller's rates and bills are important to address at the public hearings because it would provide clear information about what the rate impact will be from the purchase price.²

² Section 1329 provides that the ratemaking rate base, i.e., the value used for setting rates, is the lower of the purchase price or the average of the two appraisals. 66 Pa. C.S. §§ 1329(c)(2) and (g). For these comments generally, the OCA is making a simplifying assumption that the purchase price is the lesser of the two numbers. For purposes of the public

Generally, the OCA recommends that the bill impact information be in plain language without unnecessary information or legal information. The calculation of the bill impact should be designed to provide meaningful information to the seller's customers and the buyer's customers. The bill impact should be shown without accounting for any rate freeze that the buyer and seller have proposed because those freezes are not binding on the PUC when setting rates and they have led to significant confusion, anger, and frustration by affected customers. The use of the existing Section 1329 notices is not recommended because that notice does not provide full and complete information that would fulfill the requirement that customers, who are learning about a potential sale, receive information about the bill impacts of that proposed transaction. The OCA has three specific recommendations, discussed below, about what information should be included in the bill impact provided to the seller's customers.

Wastewater acquisitions: The bill impact for a wastewater acquisition should reflect the full impact of the revenue requirement calculated by the buyer that identifies the shortfall, if any, between the revenues collected through the seller's rates and the calculated revenue requirement. The full bill impact should not be reduced by any proposed Section 1311(c) shift that the buyer may propose in future rate cases. Using the full bill impact information provides a realistic picture of what the seller's customers may face if the sale is approved at the acquiring utility's then-current rates. Another component of describing the potential rate impacts would be to show the rate impact if all of the revenue requirement were collected from the selling utility customers. In an acquisition of a wastewater provider, there also could be information about the possible shift of wastewater revenue requirement to water customers pursuant to a request by the acquiring utility filed under

hearings, presumably the possible purchase price would be the only number that would be available because an asset purchase agreement has not yet been executed, and the utility valuation experts (UVE) have not been retained to produce appraisals as described in the process to be followed after an agreement is reached. 66 Pa. C.S. § 1329(a).

Section 1311(c) in a future rate case but it should be emphasized that it is within the Commission’s discretion as to whether any shift would be approved and in what amount. 66 Pa. C.S. § 1311(c). In other words, any request by the acquiring utility under Section 1311(c) should not be portrayed or implied as relieving the seller’s customers from ever paying the revenue requirement that results from the sale of the utility assets. This recommendation is consistent with the Commission’s directive regarding the verifications that the Commission is requiring in the Rate Impact Notice section, as discussed below. 2024 TSIO at 4-5.

Bill impact at different usage levels: The bill impact information should provide information for customers at different usage levels, not just for a “typical” customer’s usage level. For example, a customer using 5,000 gallons of water per month (perhaps a small family) would see a different bill impact. A customer using 10,000 gallons of water per month (perhaps a larger family) would see a different impact.

The chart below is an example of what could be used in the notice to provide the bill impacts for additional usage levels. The numbers are simply for illustration.

| Gallons per month | Current Bill | Proposed Bill |
|-------------------|--------------|---------------|
| 3,200 | \$72.45 | \$87.65 |
| 5,000 | \$102.45 | \$127.65 |
| 10,000 | \$183.79 | \$234.25 |

The use of 5,000 and 10,000 gallons per month represents a reasonable estimate that falls at or near the middle of a range of usage for 2 and 4-person households and a range of daily usage of 5-100 gallons per day (gpd). This range is based on information contained in Penn State Extension:

Estimating Water Needs.³ Although this paper is based on designing water systems, using 50 gallons per day per person (gppd) as the minimum and 100 gppd for a 30-day month would equal 3,000 to 6,000 gallons per month for a 2-person household and 6,000 to 12,000 gallons per day for a 4-person household. Choosing a level close to the middle of each range is a reasonable approach to show the impact of the transaction on customers at different usage levels. The OCA recommends the same approach be used for a notice of a potential wastewater acquisition.

Capital Expenditures Agreed to in the APA: The calculations of the rate impact should include any capital expenditure commitments that the acquiring utility is committing to in the APA and the related revenue requirement. For example, if the acquiring utility commits to invest a minimum amount of capital expenditures for a number of years in the service area of the selling utility, that additional revenue requirement impact should be included in the rate impact calculation to understand the impact of the capital expenditure commitments in the APA. An example of capital investment information that could be presented is illustrated below:

| | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 |
|---------------------|-----------|-------------|-------------|-------------|-------------|
| Capital Investments | \$710,100 | \$3,438,600 | \$2,205,500 | \$1,793,000 | \$3,976,500 |

| | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
|---------------------|-------------|-------------|-------------|-------------|-------------|
| Capital Investments | \$3,629,500 | \$1,738,000 | \$1,870,000 | \$1,892,000 | \$1,947,000 |

³³ <https://extension.psu.edu/water-system-planning-estimating-water-needs>

If there are capital investment commitments being negotiated as part of the proposed acquisition, the bill impact calculations should reflect the agreed-upon capital investments. This information would assist in understanding the relationship between the capital expenditure commitments in the APA and the future rate impacts of those commitments. An example of the revenue requirement calculation at closing and including Year 1 capital expenditures is provided as Attachment A.

C. Rate Impact Notice

The TSIO requires the acquiring utility and the selling utility to verify, or declare under affidavit, three items with the initial application that would be a prerequisite to a perfected application. 2024 TSIO at 4. Those required areas are that 1) both parties are aware of the potential rate impacts the transaction may have on the selling utility's customers, including the overall dollar and percentage impact from stand-alone rates from the transaction price, 2) the selling utility has publicly communicated those rate implications through notice to its customers, and 3) both parties understand that the Commission may shift rate allocations in a different manner than what the buyer and seller commit to in the application. In its discussion, the Commission acknowledges that the current requirements include notice to the selling utility's customers, stating:

[W]e believe it is prudent to fortify the public notice requirements with this additional information. This information should prove particularly informative for the selling utility and its customers, as it will make it more certain both have a clear and informed understanding of the stand-alone rate implications from the transaction.

2024 TSIO at 5. The OCA agrees with the Commission and its stated intent to fortify the public notice requirements. As discussed in the public hearings section and the required bill impact information, *supra*, the OCA has proposed specific information that should be included in the rate impacts discussion at the public hearings **and** should be included in the notices that are included

with the filed application and directly provided to the customers of the buyer and the seller pursuant to *McCloskey*. Specifically, the notices should include clear information about the bill impacts of the proposed ratemaking rate base, at different usage levels, and including the first year capital expenditures. In a wastewater application, the notice to the seller's customers should also show the bill impact at the full revenue requirement of the ratemaking rate base, without any proposed shift under Section 1311(c). In that same wastewater application, the notice to the buyer's customers should reflect the impact if there is a full shift of the revenue requirement for the acquisition from the seller's customers to the water customers. This approach will provide the full potential impact to each set of customers.

D. Default Weights for Appraisals

In its TSIO, the Commission addresses the default weights for the three appraisal methods used by the utility valuation experts (UVEs). 2024 TSIO at 5-6. The OCA's comments address the Commission's proposal of equal weighting which OCA supports. The OCA also provides a recommendation regarding which analysis should be used in the cost approach.

1. Equal Weighting

The appraisal methods are set out in Section 1329(a)(3) which states that each UVE shall determine fair market value using the Uniform Standards of Professional Appraisal Practice (USPAP) employing the cost, market and income approaches. 66 Pa. C.S. § 1329(a)(3). The vast majority of the UVE appraisals use an even weighting of the three approaches however, there are some that weigh the appraisals unevenly. 2024 TSIO at 5. The Commission's directive is that the three approaches be weighed evenly, or one-third for each of the three approaches, noting that these default weights "will eliminate the ability of any UVE to artificially inflate or deflate the results of any appraisals that come in high or low, respectively." *Id.* The OCA fully supports the

Commission’s recognition of the strategy that is employed as well as the Commission’s proposed solution to have the default be equal weighting. The opportunity to seek authority to vary from these default weights “for good cause shown” would need to be included in the application when filed. 2024 TSIO at 5-6. The OCA supports this approach. It has been clear that the uneven weighting is not supported by any analysis and the use of uneven weighting should be eliminated or strictly limited by the Commission’s approach.

2. Cost Approach

The OCA supports an additional refinement related to the cost approach. Section 1301’s mandate for just and reasonable rates *must be given effect* when valuing utility property pursuant to Section 1329. *See Application of Aqua Pennsylvania Wastewater, Inc. Pursuant to Sections 1102, 1329 & 507 of the Public Utility Code for Approval of its Acquisition of the Wastewater System Assets of Cheltenham Twp. & Contracts between Aqua Pennsylvania Wastewater, Inc. & Cheltenham Twp., A-2019-3008491, Order at 37-18 (Nov. 5, 2019) (Cheltenham).* Thus, the “fair market value” of utility property for ratemaking rate base under Section 1329 must reflect rates that are “just and reasonable” under Section 1301 of the Code.

As discussed above Section 1329(a)(3) requires each UVE to “determine *fair market value* in compliance with [USPAP], employing the cost, market and income approaches.” 66 Pa. C.S. § 1329(a)(3) (emphasis added).⁴ The term “fair market value” is defined under Section 1329 as “the

⁴ USPAP Rule 7-4 does *not* require an appraiser to use all three approaches – cost, income and market – in an appraisal. Rather, Rule 7-4(a)-(c) states that “*when a [sales comparison/cost approach/income approach] is necessary for credible assignment results,*” an appraiser must follow the guidance set forth therein relating to each respective approach. The Rule essentially leaves it to the discretion of the appraiser to determine which approach is necessary for credible assignment results. It is Section 1329 that requires the UVEs to utilize all three approaches. Thus, in order for a UVE to give “credible assignment results” for an appraisal conducted pursuant to Section 1329, all three approaches must be used. Thus, it is only by reading USPAP Rule 7-4 consistently with Section 1329’s mandate to use all three approaches that the UVEs utilize all three approaches in their fair market value appraisals.

average of the two utility valuation expert appraisals conducted under subsection (a)(2).” The PUC has broad discretion under Section 1329, which it has not exercised to this point and that it should exercise going forward starting with this 2024 TSIO. Specifically, Section 1329 does not direct which method must be used by a UVE under the cost approach. The Commission has discretion, and it can and should exercise it in the TSIO or in regulations, to prescribe the method that should be used under the cost approach.

USPAP does not specify which method must be used under the Cost Approach. There are 4 different methods that can be used under the cost approach:

- Original cost new (OCN) less depreciation (OCNLD) method;
- trended original cost (TOC) less depreciation (TOCLD) method;
- reproduction cost method (RCN) less depreciation (RCNLD); and
- replacement cost (COR) less depreciation (CORLD) method.

USPAP defines the term “cost” as “the actual or estimated amount required to create, reproduce, replace, *or obtain* a property.” USPA Definitions. Standards Rule 1-4(b) and (g) govern appraisals of real property and Rule 7-4(b) explains the cost approach. In general terms, the cost approach measures value by determining the cost new of the property minus applicable depreciation. USPAP Rule 7-3 requires the appraiser in appraising personal property (i.e., the utility plant), as follows:

1467 **STANDARD RULE 7-3**

1468 **In developing a personal property appraisal, when necessary for credible assignment results, an appraiser**
1469 **must:**

1470 **(a) analyze the property's current use and alternative uses as relevant to the type and definition of value and**
1471 **intended use of the appraisal;**

1472 Comment: In the context of personal property, value can be a function of the choice of the appropriate
1473 market or, in some cases, market level for the type of item, the type and definition of value, and the intended
1474 use of the appraisal.

1475 The appraiser must consider the various uses of the property when viable alternative uses exist and when
1476 those alternative uses may result in a different value.

1477 **(b) define and analyze the appropriate market consistent with the type and definition of value; and**

1478 Comment: The appraiser must recognize that there are distinct levels of trade (measurable marketplaces)
1479 and each may generate its own data. For example, a property may have a different value at a wholesale level
1480 of trade, retail level of trade, or under various auction conditions. Therefore, the appraiser must analyze the
1481 subject property within the correct market context.

1482 **(c) analyze the relevant economic conditions that exist on the effective date of the valuation, including**
1483 **market acceptability of the property and supply, demand, scarcity or rarity.**

Under USPAP Rule 7-3, the appraiser “must analyze the relevant economic conditions that exist on the effective date of the valuation.” The PUC should require the UVEs to set forth the economic conditions of the sale in their appraisals. In the public utility/ muni-owned /muni-authority-owned system context, the “economic conditions” *are natural monopoly-owned systems* for which consumers have already paid for and/or are paying for the existing infrastructure in rates. *There does not exist a competitive market for these assets. These assets are invested in and paid for under rate regulation and government control.*

Given these undisputable *economic conditions*, as required to be considered by USPAP Rule 7-3, the PUC should require that a UVE’s cost approach analysis use only the OCNLD method as the appropriate valuation method under the cost approach. The PUC previously stated in the *2019 FSIO*, Appendix C, Additional Guidelines, that the OCNLD method of valuation can be utilized under the USPAP cost approach.

The PUC should consider the intention of Section 1329(a)(4)’s mandate that a licensed engineer conduct an assessment of the tangible assets of the selling utility and that such assessment

be incorporated into UVE appraisal under the cost approach. Section 1329(a)(4)'s mandate requires a rejection of the CORLD (replacement cost) method because the CORLD method does not require an estimate of costs of identical utility property under present prices but rather permits the assumption of the replacement of existing property with similar new property having the nearest equivalent utility to the property being valued (*i.e.*, it permits the hypothetical creation of the most efficient system for wastewater collection utilizing contemporary materials for pipe and plant).⁵ Contrast the CORLD method with the RCNLD method, which requires a valuation of existing utility property under present prices.

Based on this, when considering Section 1329(a)(4)'s mandate to incorporate the Engineer's Assessment of existing seller property into the UVEs' cost approach, it focuses the cost approach on only three methods – OCNLD, TOCLD and RCNLD.

For 35 years, it has been settled law through the statutory mandate under 66 Pa. C.S. § 1301(b) that utility property is to be valued solely under original cost new less accumulated depreciation. 66 Pa. C.S. § 1311(a), (b). The OCNLD method of valuation of utility property was developed after years of litigation under the prior statutory standard of "fair value." Prior to 1984, the relevant statute provision required utility property in rate base to be valued under a "fair value."⁶ The prior statutory standard of "fair value" was developed more fully as a doctrine through Commission decisions and case law. Typically, the valuation methods used to determine the "fair

⁵ Acknowledging that this is a departure from the general guidance adopted in the 2019 FSIO, Appendix C, Additional Guidelines, which expressly permitted the replacement cost method under the cost approach. However, given the reasoning offered here, the PUC should reach a different conclusion from before.

⁶ Specifically, prior to 1984, the Public Utility Law (1937, May 28, PL 1053, Art 1, §1; 66 PS 1151), provided, in part:

The commission may, after reasonable notice and hearing, ascertain and fix the *fair value* of the whole or any part of the property of any public utility, insofar as the same is material to the jurisdiction of the commission, and may make revaluations from time to time and ascertain the fair value of all new construction, extension, and additions to the property of the public utility.

See Pa. PUC v. Philadelphia Elec. Co., 31 PUR 4th 15 (Pa. PUC Order Dec. 28, 1978) (*PECO 1978*).

value” of utility property moved between three cost valuation methods – OCN, TOC and RCN. From these cost valuation methods, to determine the appropriate measure of value, the Commission would typically deduct accrued depreciation and depletion, resulting in the OCNLD, TOCLD and RCNLD valuations. *See e.g. City of Pittsburgh v. Pa. PUC*, 90 A.2d 607, 611 (Pa. Super. 1952) (*City of Pittsburgh*).⁷

- Relating to these three cost-based valuation methods, the PUC has explained as follows:

The proper valuation of utility property has had a controversial history in the Commonwealth, toggling between hybrids of “original cost” and “reproduction cost” techniques. Reproduction value, as the name implies, is an appraisal of the utility’s property under present prices. Advocates argue that this method recognizes inflation and the resultant loss of money’s purchasing power. Proponents of original cost, on the other hand, argue that the use of reproduction cost resulted in a windfall to investors by compensating them beyond their original investment and point to the difficulty of establishing a proper trending technique. *Rates can vary substantially depending upon the valuation technique used.*

For many years, the [Commission] employed a composite of the two methods labeled “trended original cost,” which was neither original nor reproduction cost, but something in between. In practice, the Commission calculated cases on an original cost basis and then backed into the fair value and rate of return findings that replicated the original cost result. In 1981, the Commission successfully convinced the Pennsylvania Supreme Court that the statutorily required “fair value” could include strictly original cost valuation and the burdensome reproduction cost standard was abandoned. [Citing *Pennsylvania Gas, supra.*] The practice of using original cost exclusively was codified thereafter under Act 153 of Sept. 27, 1984 (P.L. 721). [Citing 66 Pa. Code § 1311(b).] This statutory prescription modified the previous version of Section 1311, which [mandated the fair value standard.] [Citation omitted]. Original cost is now the law of Pennsylvania.

See James H. Cawley & Norman J. Kennard, A Guide to Utility Ratemaking, 116 (Pa. PUC 2018) (emphasis added).⁸

⁷ *See also, e.g., Solar Electric Co. v. Pa. PUC*, 9 A.2d 447 (Pa. Super. 1939); *Peoples Natural Gas Co. v. Pa. PUC*, 34 A.2d 375 (Pa. Super. 1943); *Equitable Gas Co. v. Pa. PUC*, 51 A.2d 497 (Pa. Super. 1947).

⁸Available at, http://www.puc.pa.gov/General/publications_reports/pdf/Ratemaking_Guide2018.pdf.

As the PUC acknowledged in its *Guide to Utility Ratemaking*, rates can vary substantially depending upon the cost valuation method used. This acknowledgement is particularly relevant here to this analysis given the Commonwealth Court’s decision in *McCloskey*, which stated that “the Commission must take into consideration the effect of rates if the sale is approved.” *McCloskey*, 195 A.3d at 1066.

The PUC must recognize that among the four cost-based methods, OCNLD, TOCLD, RCNLD and CORLD, the OCNLD method is the method least likely to overvalue or undervalue utility property. The PUC must not overlook the Commonwealth’s long history of controversy prior to 1984 over which method was to be used in order to fix just and reasonable rates. The PUC also must not overlook the fact that the General Assembly settled that controversy by enacting, in 1984, Section 1311(b) to require cost-based valuation of utility property for ratemaking using the OCNLD method. The PUC also must recognize that Section 1311(b) is still existing law today. Indeed, in 2018, the General Assembly amended Section 1311, under Act 120 of 2018, 2018, Oct. 24, P.L. 738, No. 120 § 1, to include an additional subsection (b)(2) to Section 1311.⁹ In amending Section 1311(b) to add this new subsection, the General Assembly reaffirmed the OCNLD standard under Section 1311(b)(1), without any caveat or carveout for Section 1329’s required cost approach for valuation of utility property.

The rules of statutory construction require that every statute be construed, if possible, to give effect to all its provisions. 1 Pa. C.S. § 1921(a). Thus, the question before the PUC is whether it is possible to give effect to Section 1311(b) when determining the ratemaking rate base under

⁹ The amendments under Act 120 of 2018 to Section 1311 govern the rate base treatment of a public utility providing water or wastewater service that replaces a customer-owned lead water service line or a customer-owned damaged wastewater lateral, performed concurrent with a scheduled utility main replacement project or under a commission-approved program, notwithstanding that the customer shall hold legal title to the replacement water service line or wastewater lateral.

Section 1329 under the cost approach. The OCA posits that it is, especially when considering, as discussed above, the long and contentious history leading up to the enactment of Section 1311(b) and the General Assembly's recent reaffirmation of the OCNLD standard under this Code provision.

As the Commonwealth Court explained with regard to Section 1329:

Section 1329 allows a private utility to acquire a government utility's assets at its fair market value rather than at the original cost of assets minus the accumulated depreciation and then add that amount to the rate base. Valuing the assets at fair market value rather than cost will usually result in a higher price for the assets added to the rate base than the one previously used.

McCloskey, 195 A.3d at 1066.

Section 1311(b) can be construed to be given effect under Section 1329(a)(3)'s mandate to use the cost approach and Section 1329(a)(4)'s mandate to incorporate the Engineer's Assessment of existing system assets into the cost approach. Under this statutory construction approach, the Commission is able to construe Code Sections 1329, 1301, and 1311(b) in a way that gives meaning to all provisions, while remaining consistent with USPAP Rule 7-4, which the PUC has previously concluded permits the use of the OCN method.

Based on this analysis, the PUC can and should find that the OCNLD is the appropriate method of valuation under the cost approach required under Section 1329(a)(3). However, the cost approach is not the sole method of valuing utility property under Section 1329. The UVEs determine the value of the property also using the income and market approaches, which by necessity, resulted in a higher valuation of the system assets added to the rate base than compared to the valuation produced under the OCNLD method alone. It is recognized that valuing the assets at fair market value rather than original cost alone will usually result in a higher price for the assets added to the rate base.

This position constitutes reasoning that appropriately considers, rather than dispels in wholesale fashion, 35 years of well-settled utility ratemaking law. It is consistent with the rules of statutory construction, which require that every statute be construed, if possible, to give effect to all its provisions.¹⁰

Utilizing the OCNLD valuation method under the cost approach is supported when considering the resulting rate impact to the customers. *McCloskey*, 195 A.3d at 1066 (“the Commission must take into consideration the effect of rates if the sale is approved.”). As indicated in the *Guide to Utility Ratemaking*, rates can vary substantially depending upon the cost-based valuation method used.

E. Reasonableness Review Ratio

The Commission proposes a reasonableness review ratio (RRR) that it would publish annually, and would be used as a guidepost to make a final determination on the overall prudence of the Section 1329 applications but would not be binding. 2024 TSIO at 6. The TSIO describes the inputs and how the annual calculation of the RRR would be done. 2024 TSIO at 6-8.

¹⁰ As the Pennsylvania Supreme Court has explained, the approach to questions of statutory construction is well-settled:

The object of all interpretation and construction of statutes is to ascertain and effectuate the intention of the General Assembly. Every statute shall be construed, if possible, to give effect to all its provisions.” 1 Pa. C.S. § 1921(a); *Commonwealth v. McCoy*, 599 Pa. 599, 962 A.2d 1160, 1167–68 (2009). A statute’s plain language generally provides the best indication of legislative intent. *McCoy*, 962 A.2d at 1166; *Ephrata Area Sch. Dist. v. County of Lancaster*, 595 Pa. 111, 938 A.2d 264, 271 (2007); *Pennsylvania Fin. Responsibility Assigned Claims Plan v. English*, 541 Pa. 424, 664 A.2d 84, 87 (1995) (“Where the words of a statute are clear and free from ambiguity the legislative intent is to be gleaned from those very words.”). Only where the words of a statute are not explicit will we resort to other considerations to discern legislative intent. *Ephrata Area Sch. Dist.*, *supra*; *see also* 1 Pa. C.S. § 1921(c); *In re Canvass of Absentee Ballots of Nov. 4, 2003 Gen. Election*, 577 Pa. 231, 843 A.2d 1223, 1230 (2004). Moreover, in this analysis, “[w]e are not permitted to ignore the language of a statute, nor may we deem any language to be superfluous.” *McCoy*, 962 A.2d at 1168. Governing presumptions are that the General Assembly intended the entire statute at issue to be effective and certain, and that the General Assembly does not intend an absurd result or one that is impossible of execution. *See* 1 Pa. C.S. § 1922(1)-(2). *Board of Revision of Taxes, City of Philadelphia v. City of Philadelphia*, 607 Pa. 104, 4 A.3d 610, 622 (Pa. 2010).

Wayne M. Chiurazzi Law Inc. v. MRO Corp., 97 A.3d 275, 292 (Pa. 2014) (citations contained in original).

As explained below, the OCA supports the intent of the RRR to provide a guidepost to assist in determining the prudence of the applications. It is clear that the RRR should not be considered a test of presumptive reasonableness or a determination that the application is in the public interest if the transaction meets this guidepost. The OCA understands that the RRR would be one factor among many considered by the Commission. It also is clear that the RRR cannot override *McCloskey* and *Cicero* that clearly require the Commission to consider the rate impact of the transaction as part of the overall consideration of whether there are substantial affirmative public benefits from the proposed transaction.

The need for a guidepost, with the stated understanding that the guidepost is one factor among many, is clear as the OCA will discuss below given the rate impact of Section 1329 acquisitions that proceeded without any guideposts. The OCA prefers a fixed value guidepost of 1.25x because the use of the RRR raises concerns of variability and timing, as discussed below.

1. Rate Impact After Seven Years of Section 1329 Acquisitions

Over the first seven years of Section 1329, there have been twenty-seven applications filed, with twenty acquisitions receiving a final order approving the acquisition and subsequently closing on the transaction.¹¹ The twenty-one acquisitions that have final orders have added more than \$1.09 billion of ratemaking rate base to the rate bases of Aqua Pennsylvania, Pennsylvania-American Water, and Veolia. As the chart below shows, the ratemaking rate bases are almost all multiples over the depreciated original cost.

¹¹ Of the twenty-one applications listed in the chart, one has not closed (PAWC's acquisition of Butler Area Sewer Authority).

Table 1: Summary of Section 1329 (Ratemaking Rate Base vs. Depreciated Original Cost)¹²

| Seller | Buyer | Type of System | Ratemaking Rate Base | Depreciated Original Cost |
|---|---------|----------------|-------------------------|---------------------------|
| New Garden | Aqua PA | Wastewater | \$ 29,500,000 | \$ 18,567,728 |
| Limerick | Aqua PA | Wastewater | \$ 64,373,378 | \$ 46,153,867 |
| McKeesport | PAWC | Wastewater | \$ 158,000,000 | \$ 80,085,602 |
| East Bradford | Aqua PA | Wastewater | \$ 5,000,000 | \$ 5,473,948 |
| Sadsbury | PAWC | Wastewater | \$ 8,300,000 | \$ 7,480,573 |
| Mahoning | SUEZ | Water | \$ 4,734,800 | \$ 3,507,138 |
| Mahoning | SUEZ | Wastewater | \$ 4,765,200 | \$ 3,234,859 |
| Exeter | PAWC | Wastewater | \$ 92,000,000 | \$ 40,057,634 |
| Steelton | PAWC | Water | \$ 20,500,000 | \$ 14,433,435 |
| Cheltenham | Aqua PA | Wastewater | \$ 44,558,259 | \$ 15,408,458 |
| East Norriton | Aqua PA | Wastewater | \$ 20,750,000 | \$ 8,407,007 |
| Kane | PAWC | Wastewater | \$ 17,560,000 | \$ 12,070,455 |
| Royersford | PAWC | Wastewater | \$ 13,000,000 | \$ 5,173,559 |
| Valley | PAWC | Water | \$ 7,325,000 | \$ 5,370,438 |
| Valley | PAWC | Wastewater | \$ 13,950,000 | \$ 9,214,738 |
| Upper Pottsgrove | PAWC | Wastewater | \$ 13,750,000 | \$ 8,970,325 |
| Lower Makefield | Aqua PA | Wastewater | \$ 53,000,000 | \$ 19,808,274 |
| East Whiteland | Aqua PA | Wastewater | \$ 54,413,635 | \$ 33,403,972 |
| City of York | PAWC | Wastewater | \$ 231,500,000 | \$ 97,106,105 |
| Shenandoah | Aqua PA | Water | \$ 12,000,000 | \$ 10,784,743 |
| Butler Area Sewer | PAWC | Wastewater | \$ 228,000,000 | \$ 93,409,083 |
| TOTAL | | | \$ 1,096,980,272 | \$ 538,121,941 |
| ¹ Depreciated original cost is shown without considering the "original source of funding" pursuant to Section 1329; i.e. contributions have not been deducted. | | | | |

Cumulatively, the \$1.09 billion ratemaking rate base valuation is 2.04 times the depreciated original cost of the acquired systems of approximately \$538 million. This valuation impacts rates.

Setting the ratemaking rate base at multiples over depreciated original cost plus the increased cost of ownership of an investor-owned utility caused a combined annual revenue requirement shortfall of \$85,218,654 at the time of closing on the twenty transactions. The shortfall in revenue requirement is due to the difference between the revenues collected from the acquired customers and the revenue requirements for the acquired customers using the ratemaking

¹² Two of the acquisitions above that have been approved by the Commission are subject to ongoing appeals. The Commonwealth Court reversed the Commission's approval of the East Whiteland Township acquisition in *Cicero*, but the Commission, Aqua, and East Whiteland Township all have requested review by the Pennsylvania Supreme Court. The Butler Area Sewer Authority, while approved by the Commission, has been appealed by Center and Summit Townships.

rate base created by the fair market valuation.¹³ The revenue requirement shortfall at closing or Commission approval for each of the twenty-one approved and closed transactions is shown in the table below.

Table 2: Annual Revenue Requirement Deficiency of Approved and Closed Transactions

| REVENUE REQUIREMENT SHORTFALL | | | | | |
|--|-----------------|--------------|------|------------------|----------------------|
| Aqua | New Garden | \$ 1,662,142 | PAWC | McKeesport | \$ 16,737,759 |
| Aqua | Limerick | \$ 7,778,000 | PAWC | Sadsbury | \$ 94,062 |
| Aqua | East Bradford | \$0 | PAWC | Exeter | \$ 5,378,000 |
| Aqua | Cheltenham | \$ 2,772,000 | PAWC | Steelton | \$ 1,117,000 |
| Aqua | East Norriton | \$ 1,155,000 | PAWC | Kane | \$ 1,265,000 |
| Aqua | Lower Makefield | \$ 2,828,000 | PAWC | Royersford | \$ 1,210,343 |
| Aqua | East Whiteland | \$ 5,011,000 | PAWC | Upper Pottsgrove | \$ 1,002,000 |
| Aqua | Shenandoah W | \$ 865,031 | PAWC | Valley W | \$ 1,697,000 |
| Veolia | Mahoning W | \$ 492,666 | PAWC | Valley WW | \$ (1,413,000) |
| Veolia | Mahoning WW | \$ 114,651 | PAWC | City of York | \$ 17,557,000 |
| | | | PAWC | BASA | \$ 17,895,000 |
| TOTAL ANNUAL REVENUE DEFICIENCY | | | | | \$ 85,218,654 |

This means that consumers are paying at least \$85 million more each year for water and wastewater service due to the valuation under Section 1329. The impact of the revenue requirement shortfall is usually viewed in the context of each application. However, from existing customers' perspective, the layered impact of each revenue requirement shortfall is what they see as part of each rate filing. The impact of just twenty 1329 acquisitions has already been felt by the buyers' customers, including some of the acquired customers in rate cases after acquisition. The chart below shows that pending applications would add another \$18.8 million of annual revenue deficiencies.

¹³ The revenue requirement shortfall is calculated as of the closing on each transaction (and Commission approval for the one transaction that has not closed) and grows in each subsequent rate case under the ownership of the investor-owned utility.

Table 3: Annual Revenue Requirement Deficiency of Pending Transactions

| | | | | | |
|--|------------------|--------------|------|------------|---------------------|
| Aqua | DELCORA | \$ 4,553,000 | PAWC | Towamencin | \$7,731,000 |
| Aqua | Beaver Falls | \$ 4,288,000 | | | |
| Aqua | Greenville Sewer | \$ 2,230,000 | | | |
| TOTAL PENDING ANNUAL REVENUE DEFICIENCY | | | | | \$18,802,000 |

Looking at the rate impact from another perspective, the chart below shows the cumulative increase that the acquisitions have had on the average rate base per customer. For example, the average rate base per customer for both Aqua Pennsylvania (Aqua) and for Pennsylvania American Water Company (PAWC) have grown significantly since 2016 as reflected in the tables below.

Table 4: Aqua’s Average Rate Base Per Customer

| Average Rate Base per Customer 2016 | | Average Rate Base per Customer 2022 | | Percentage Increase 2016 to 2022 |
|-------------------------------------|---------|-------------------------------------|---------|----------------------------------|
| Aqua Pa Wastewater: | \$3,795 | Aqua Pa Wastewater | \$9,449 | 249% |
| Aqua Pa Water: | \$7,177 | Aqua Pa Water: | \$9,812 | 137% |

Table 5: PAWC’s Average Rate Base Per Customer

| Average Rate Base per Customer 2016 | | Average Rate Base per Customer 2022 | | Percentage Increase 2016 to 2022 |
|-------------------------------------|---------|-------------------------------------|----------|----------------------------------|
| PAWC Wastewater: | \$7,162 | PAWC Wastewater: | \$12,458 | 174% |
| PAWC Water: | \$5,565 | PAWC Water: | \$7,423 | 133% |

Increases in rate base will generally increase revenue requirements (any projected operation and maintenance costs savings identified by the buyer have already been reflected in the buyer’s calculation of the revenue requirement). The average rate base per customer for Section 1329 acquisitions approved to date is shown below.

Table 6: Average Rate Base Per Customer

| Average Rate Base per Customer | | | | |
|--------------------------------|---|------------------------|---------------------|--------------------------------|
| | Acquired Utility | 1329 Allowed Rate Base | Number of Customers | Average Rate Base per Customer |
| Aqua Purchases | New Garden A-2016-2580061 | \$29,500,000 | 2,106 | \$14,008 |
| | Limerick A-2017-2605434 | \$64,373,378 | 5,434 | \$11,846 |
| | East Bradford A-2018-3001582 | \$5,000,000 | 1,248 | \$4,006 |
| | Cheltenham A-2019-3008491 | \$44,558,259 | 10,219 | \$4,360 |
| | East Norriton A-2019-3009052 | \$20,750,000 | 4,966 | \$4,178 |
| | Lower Makefield A-2021-3024267 | \$53,000,000 | 11,151 | \$4,753 |
| | East Whiteland A-2021-3026131 | \$54,413,635 | 3,895 | \$13,970 |
| | Shenandoah (Water) A-2022-3034143 | \$12,000,000 | 2,899 | \$4,139 |
| | Total | \$283,595,272 | 41,918 | \$7,658 |
| PAWC Purchases | McKeesport A-2017-2606103 | \$158,000,000 | 12,780 | \$12,363 |
| | Sadsbury A-2018-3002437 | \$8,300,000 | 998 | \$8,317 |
| | Exeter A-2017-3004933 | \$92,000,000 | 9,015 | \$10,205 |
| | Steelton (Water) A-2019-3006880 | \$20,500,000 | 2,415 | \$8,489 |
| | Kane A-2019-3014248 | \$17,560,000 | 2,019 | \$8,697 |
| | Royersford A-2020-3019634 | \$13,000,000 | 1,620 | \$8,025 |
| | Upper Pottsgrove A-2020-3021460 | \$13,750,000 | 1,447 | \$9,502 |
| | Valley (Water) A-2020-3019859 | \$7,325,000 | 1,670 | \$4,386 |
| | Valley (Wastewater) A-2020-3020178 | \$13,950,000 | 3,125 | \$4,464 |
| | City of York A-2021-3024681 | \$231,500,000 | 13,747 | \$16,840 |
| | Butler Area Sewer A-2022-3037047 | \$228,000,000 | 14,792 | \$15,414 |
| | Total | \$803,885,000 | 63,628 | \$9,700 |
| Veolia Purchases | Mahoning (Water) A-2018-3003519 | \$4,734,800 | 1,186 | \$3,992 |
| | Mahoning (Wastewater) A-2018-3003517 | \$4,765,200 | 1,620 | \$2,941 |
| | Total | \$9,500,000 | 2,806 | \$3,467 |
| Overall Total | | \$1,096,980,272 | 108,352 | \$11,125 |

It is important to clarify that the OCA takes no position on the price a buyer can or should pay or a seller can or should sell its utility plant. The issue is what amount can be put into rate base and paid for by customers versus what amount should be paid for by the acquiring utility.¹⁴ As Consumer Advocate Cicero stated in testimony before the Senate Democratic Policy Committee in a January 2024 hearing on Section 1329:

All the data paints an increasingly grim picture that Section 1329 created an incentive for investor-owned water and wastewater utilities to purchase municipal utilities at significantly inflated prices to the detriment of consumers. In short, Act 12 has been a financial disaster for customers and has not materially or substantially improved service.

<https://www.senatormuth.com/wp-content/uploads/2024/01/Patrick-Cicero-Testimony.pdf>

As will be discussed in the next section, one way for the rate impact of future Section 1329 valuations to be lessened is to have a fixed cap on what can be proposed to be collected from customers.

2. A Fixed Guidepost

The cumulative rate impact of the seven year history of fair market valuation has been grim for customers, as discussed above. Moving forward, having a fixed guidepost or cap on what can be collected from customers is an important step and an additional factor that will be reviewed in an application under Section 1103 of the Public Utility Code. 66 Pa. C.S. § 1103. The OCA recommends a fixed guidepost of 1.25x, as discussed below.

The OCA has concerns that having a guidepost that is not fixed could cause issues during the relatively long time that it might take from public hearings discussed above to the filing of the

¹⁴Utilities have often paid more than book value to acquire systems. For example, when Essential Utilities, the parent company of Aqua Pennsylvania purchased Peoples Gas in March 2020 (PUC Order entered January 24, 2020), it paid \$2 billion over book value, or 87% over the net book value of the company at the time, but it was only allowed to put into ratemaking rate base the net book value of the Company. It did not get to recover from ratepayers that amount above net book value.

application with the Commission. During that time, a variable guidepost might change. The OCA also addresses other concerns with the RRR below.

The OCA prefers 1.25x as the fixed guidepost for the Commission to consider in its analysis – recognizing, as stated below, that the overall standard remains under Sections 1102 and 1103 of the public utility code that an affirmative public benefit is required before the Commission can approve an acquisition. The use of 1.25 fixed guidepost would, where the acquisition otherwise meets the legal standard, still permit the buyer to include 25% more than depreciated original cost in rate base, even if the system acquired is not troubled. Moreover, this approach maintains the higher calculation for depreciated original cost, as defined in Section 1329(d)(5).¹⁵ This change would make a significant difference for consumers but would still permit buyers and sellers to know the maximum that could be proposed to be included in rates. Nothing would prevent a utility for paying anything it wants for another utility, but in so doing it would have to make more informed and strategic choices because its shareholders would bear the costs associated with the acquisition above a certain threshold.

The table below is an example of what a maximum multiple would do to constrain the fair market value. This example uses 1.25x as the maximum that would be allowed for ratemaking rate base and adds columns C and D to Table 1 shown above.

¹⁵ Section 1329(d)(5) is a departure from existing ratemaking because the original source of funding is not considered which means that contributions and grants that might have been used to build the system are not subtracted from depreciated original cost.

Table 7: Ratemaking Rate Base vs. Dep. Orig. Cost vs. 125% of Dep. Orig. Cost

| | | | A | B | C | D |
|-------------------|---------|----------------|-------------------------|---------------------------|--------------------------------|-------------------------|
| Seller | Buyer | Type of System | Ratemaking Rate Base | Depreciated Original Cost | 125% Depreciated Original Cost | Lesser of Column A or C |
| New Garden | Aqua PA | Wastewater | \$ 29,500,000 | \$ 18,567,728 | \$ 23,209,660 | \$ 23,209,660 |
| Limerick | Aqua PA | Wastewater | \$ 64,373,378 | \$ 46,153,867 | \$ 57,692,334 | \$ 57,692,334 |
| McKeesport | PAWC | Wastewater | \$ 158,000,000 | \$ 80,085,602 | \$ 100,107,003 | \$ 100,107,003 |
| East Bradford | Aqua PA | Wastewater | \$ 5,000,000 | \$ 5,473,948 | \$ 6,842,435 | \$ 5,000,000 |
| Sadsbury | PAWC | Wastewater | \$ 8,300,000 | \$ 7,480,573 | \$ 9,350,716 | \$ 8,300,000 |
| Mahoning | SUEZ | Water | \$ 4,734,800 | \$ 3,507,138 | \$ 4,383,923 | \$ 4,383,923 |
| Mahoning | SUEZ | Wastewater | \$ 4,765,200 | \$ 3,234,859 | \$ 4,043,574 | \$ 4,043,574 |
| Exeter | PAWC | Wastewater | \$ 92,000,000 | \$ 40,057,634 | \$ 50,072,043 | \$ 50,072,043 |
| Steelton | PAWC | Water | \$ 20,500,000 | \$ 14,433,435 | \$ 18,041,794 | \$ 18,041,794 |
| Cheltenham | Aqua PA | Wastewater | \$ 44,558,259 | \$ 15,408,458 | \$ 19,260,573 | \$ 19,260,573 |
| East Norriton | Aqua PA | Wastewater | \$ 20,750,000 | \$ 8,407,007 | \$ 10,508,759 | \$ 10,508,759 |
| Kane | PAWC | Wastewater | \$ 17,560,000 | \$ 12,070,455 | \$ 15,088,069 | \$ 15,088,069 |
| Royersford | PAWC | Wastewater | \$ 13,000,000 | \$ 5,173,559 | \$ 6,466,949 | \$ 6,466,949 |
| Valley | PAWC | Water | \$ 7,325,000 | \$ 5,370,438 | \$ 6,713,048 | \$ 6,713,048 |
| Valley | PAWC | Wastewater | \$ 13,950,000 | \$ 9,214,738 | \$ 11,518,423 | \$ 11,518,423 |
| Upper Pottsgrove | PAWC | Wastewater | \$ 13,750,000 | \$ 8,970,325 | \$ 11,212,906 | \$ 11,212,906 |
| Lower Makefield | Aqua PA | Wastewater | \$ 53,000,000 | \$ 19,808,274 | \$ 24,760,343 | \$ 24,760,343 |
| East Whiteland | Aqua PA | Wastewater | \$ 54,413,635 | \$ 33,403,972 | \$ 41,754,965 | \$ 41,754,965 |
| City of York | PAWC | Wastewater | \$ 231,500,000 | \$ 97,106,105 | \$ 121,382,631 | \$ 121,382,631 |
| Shenandoah | Aqua PA | Water | \$ 12,000,000 | \$ 10,784,743 | \$ 13,480,929 | \$ 12,000,000 |
| Butler Area Sewer | PAWC | Wastewater | \$ 228,000,000 | \$ 93,409,083 | \$ 116,761,354 | \$ 116,761,354 |
| TOTAL | | | \$ 1,096,980,272 | \$ 538,121,941 | \$ 672,652,426 | \$ 668,278,346 |

As can be seen from this Table, under the current paradigm, \$1.097 billion was added to rate base. Using a 1.25x cap on what can be included would have resulted in \$668,278,346 being added, or \$428,701,926 or 39% less. Having a cap of 1.25x would have saved ratepayers tens of millions of dollars each year while still allowing the utility to recover amounts above net book value. The OCA recommends this fixed guidepost be adopted and used as one of many factors that are considered in determining whether a proposed transaction meets the legal requirements under Section 1103 of the Public Utility Code.

3. Variable Guidepost

Regarding the RRR index, the OCA has concerns regarding the variability of the index. For example, the RRR index calculated in Appendix A of the TSIO used data through the third quarter of 2023 resulting in an RRR index of 1.68. 2024 TSIO at 7. If the index is updated, to include the fourth quarter of 2023 through first quarter of 2024, for example, the RRR index would

change. It is the OCA's position that this injects too much variability to serve as a guidepost, even recognizing the Commission's intent to update annually, not quarterly.

The use of a variable guidepost like the RRR also raises the issue of which calculation would be used to determine whether a particular proposed transaction is under the RRR. For example, if an APA is signed on January 1, 2024, the application is filed on October 1, 2024, and the Commission order is scheduled to vote on the application on May 1, 2025, it is not clear which RRR calculation would be used. The 2023 RRR would be available on the date the APA is signed, the 2024 calculation would be available on the date the application was filed and the 2025 calculation would be available at the time of the Commission vote. This uncertainty about which RRR calculation should be used would reduce the effectiveness of the RRR. It also creates complications for notice to customers as the metrics change and since the Commission correctly wants the acquiring utility and selling utility to be as accurate as possible in their notices, the OCA submits that a fixed metric would create more of the certainty that the Commission desires to instill in this process.

F. Timing to Effectuate Proposed Changes

At page 8 of the TSIO the Commission addresses the timing of the proposed changes. The minimum of two public hearing requirement, the rate impact notice, and the default appraisal weight revisions would go into effect 30 days after the issuance of a final order.¹⁶ 2024 TSIO at 8. Applications filed after 30 days would need to include the revised materials and comply with the public hearing, rate impact notice and default appraisal weights. *Id.* The OCA supports the prompt implementation of the changes.

¹⁶ The OCA is considering "issuance" to be the same as entry of a final order.

Regarding the RRR, the initial calculation would be published 30 days after the issuance of the final order in this proceeding and then published annually in April. 2024 TSIO at 8. The OCA does not object to the timing of the publication of the RRR, with consideration of its comments above.

G. Other Issues Not Addressed in the Tentative Supplemental Implementation Order

The OCA has a number of other issues that arise during the course of every application that is filed under Section 1329, as will be discussed below. The OCA submits that these additional modifications are reasonable, provide certainty to the participants, result in more efficient proceedings, and should be adopted by the Commission in its Supplemental Implementation Order.

1. Notice to Customers of the Buyer and Seller

The notices provided to the customers of the buyer and seller as part of the application proceeding before the Commission should include the information OCA recommended above for the bill impact information provided at the public hearings before an APA is executed. Specifically, the different usage levels and the projected Year 1 capital expenditures at a minimum should be incorporated into the notices sent after the Commission provides conditional acceptance. Providing meaningful information about the transaction to the impacted customers is an important part of fulfilling the notice requirement.

2. Conditional Acceptance Should Permit the Case to Move Forward For Protests, Intervention, Discovery, and Other Procedural Issues

In the 2019 FSIO, the Commission stated that “a docket will remain inactive until a Section 1329 application under that docket number has been formally accepted by the Commission. Filings in an inactive docket will not be considered until the time at which the docket becomes active.” 2019 FSIO at 42. The OCA recommends changing the current approach of designating

the docket as an “inactive” docket until final acceptance. If the case is able to move forward while notices are being provided to the customers, interested parties would be able to file protests and petitions to intervene, pursue discovery, and requests for public input hearings, along with addressing procedural issues. Having that 30 to 35 day period of time available for these actions would be an important step to providing a meaningful opportunity for parties to participate in the proceeding.

A brief review of what happens during the period between the filing and final acceptance is important to understand the impact the current practice has on parties. Currently, when an application checklist is determined by Technical Utility Services (TUS) to be complete, a Secretarial Letter is issued to conditionally accept the application. At that time, the notices are sent, or begin to be sent to the customers of the acquiring utility and the selling utility. During that approximately 30-day period, the docket continues to be treated as an inactive docket. The inactive docket designation prevents parties who have filed protests or sought to intervene from proceeding with discovery, seeking discovery modifications, presenting requests for public input hearings and any procedural matters that may need to be addressed. The docket does not become active until the notices are provided to all customers of the buyer and seller, the buyer provides information to the Secretary’s Office that the notices have been provided to all customers, and the Secretary’s office issues a letter stating that the application is finally accepted. At that point, the application will be published in the Pennsylvania Bulletin that will include a deadline for protests. A prehearing conference is set for a short time after the protest deadline. At that prehearing conference, it is likely that the testimony for non-applicant parties will be due **within a few days**. It would be practically impossible for a party that has not been involved since at least the time of the filing of the application to appear at a prehearing and then file testimony a few days later.

By permitting the docket to be “active” even if not finally accepted, protests can be filed, the parties can proceed with discovery, request discovery modifications earlier through access to an Administrative Law Judge, and proceed with developing positions for litigation. This would be similar to what happens when a formal complaint is filed against a rate filing and the parties proceed with discovery even before the suspension of the case for investigation.¹⁷ The only addition is that with the even more expedited litigation schedules in Section 1329 applications, the OCA would recommend that the ALJ, who will be assigned to the case, would be available to address procedural issues, including moving forward with the scheduling process for public input hearings that would be held after the protest period is over.

3. Modified Discovery Periods Should Be Considered the Default Discovery Periods and Be Effective as Soon as the Application Is Conditionally Accepted

In cases filed under Section 1329, at the time of filing, the Commission’s existing regulations for discovery apply. Pursuant to 52 Pa. Code § 5.342(d) and (e), answers to discovery are due 20 days after service, and objections are due 10 days after service of the interrogatories. In its *2019 FSIO* the Commission rejected I&E and OCA’s requests for standard modified discovery periods but encouraged applicants to propose discovery rule modifications and parties to enter into mutually agreeable discovery schedules. *2019 FSIO* at 51.

While parties often have agreements and ALJs grant modified discovery periods that are significantly shorter than the standard discovery period for applications due to the short time period for the litigation, the necessity of working through these issues in each case should not be required of any of the parties and the ALJs after seven years and twenty-seven applications. Moreover, as

¹⁷ The Commission has the authority to reject an application or similar document when it is of the opinion that it does not sufficiently set forth required material or is otherwise insufficient. 52 Pa. Code § 1.4(d).

discussed above, the delay in being before an ALJ due to the inactive docket designation as well as waiting for a final acceptance of the application slows down the entire process. Recognizing that the testimony of the parties (not buyer and seller) are due within a very short period of time after the prehearing conference, the OCA submits it is reasonable to adopt modified discovery time frames as part of the filing of an application using Section 1329. The OCA's proposed discovery modifications are:

- A. Answers to interrogatories and responses to requests for document production, entry for inspection, or other purposes shall be served within five (5) calendar days of service of the interrogatories or requests for production.
- B. Objections to interrogatories and/or requests for production shall be communicated orally to the propounding party within two (2) calendar days of service; unresolved objections shall be served on the propounding party in writing within three (3) calendar days of service of the interrogatories and/or requests for production.

The OCA submits that these discovery modifications be adopted for use in each application that is filed using Section 1329.

4. The Six Month Suspension Period Should Be Extended Automatically by the Commission to Ensure a Full Six Months for the Proceeding

Section 1329 provides that a final order shall be issued within six months of the filing date of an application that is filed using fair market valuation. 66 Pa. C.S. § 1329(d)(2).¹⁸ The six month period begins after notice has been provided to both the buyer and seller's customers and the final acceptance of the application is issued. The Commission has recognized that the six-month suspension period is directory and not mandatory and that it has the discretion to extend the time period to permit appropriate due process to all parties. Section 1329 does not trump or

¹⁸ House Bill 1863 would remove the six-month statutory requirement that the Commission issue a final order from the date an application is submitted that meets the requirements of Section 1329. The OCA fully supports this bill as drafted.

eliminate the Commission's adjudicatory discretion to provide appropriate due process to all parties. *County of Delaware v. Pa. PUC*, 286 A.3d 397 (Pa. Cmwlth. Ct. 2022) (unpublished).

There are still proceedings where the six-month suspension period does not line up well with a Commission public meeting.¹⁹ The OCA submits that the Commission should include, as part of the Supplemental Implementation Order, that it will automatically extend the suspension period to a public meeting date that ensures that there is at least a full six months for the litigation of the proceeding. By making this scheduling adjustment, it will address the issue at the beginning of the proceeding and will remove that issue from one that needs to be addressed by the ALJ and the parties at the prehearing conference.

¹⁹ In its 2019 *FSIO* at 39-40, the Commission addressed the approach to the six month deadline:

We first direct applicants to consider the effect of a particular filing date on the length of the consideration period, including the ten-day review of the Application Filing Checklist by TUS, the timeframe for publication in the *Pennsylvania Bulletin*, and the Public Meeting schedule. Applicants should consider these factors with the goal of attaining a consideration period of 170 to 180 days. We agree with Aqua that it is feasible for applicants to back into a Public Meeting date that will maximize the use of the six-month consideration period and we expect all applicants to make a good faith effort to do so.

If an applicant nonetheless files an application such that the consideration period is less than 170 days, TUS will encourage the applicant to voluntarily extend the consideration period to between 170 and 180 days. If the applicant declines, TUS is permitted to hold acceptance of the application one to five additional calendar days to achieve a consideration period of 170 to 180 days.

III. CONCLUSION

The OCA appreciates this opportunity to provide comments to the Commission's Tentative Supplemental Implementation Order. The OCA respectfully requests that the Commission carefully consider the points and issues raised in the OCA's comments and respectfully requests that the Commission adopt the OCA's comments in its final order.

Respectfully Submitted,

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Appendix A

Aqua Pennsylvania Wastewater, Inc.
LOWER MAKEFIELD Wastewater Authority

| | | | | |
|-----|--|-----------|------------------|--------------------------------------|
| 1.) | LOWER MAKEFIELD Wastewater Authority | | Year 1 | Notes |
| | Revenue | \$ | 10,038,836 | |
| | O&M | | 6,194,610 | |
| | Depreciation | | 1,454,181 | ***2.72% Composite Depreciation Rate |
| | Taxes Other | | 214,905 | |
| | Income Taxes | \$ | 314,667 | *****21% Federal & 9.99% State |
| | Operating Income | \$ | 1,860,472 | |
| | Rate Base at Fair Market Value | \$ | 53,000,000 | |
| | Capital Investments (Year 1) | \$ | 462,550 | |
| | Rate Base (Including Capital Investments less depreciation year 1) | \$ | 52,008,369 | |
| | Interest Expense ^ | | 1,086,322 | |
| | ^ Includes Interest Expense synchronized with rate base | | | |
| | Required Operating Income (Rate Base x Rate of Return) | \$ | 3,834,964 | |
| | Operating Income Deficiency | \$ | 1,974,492 | |
| | Gross Revenue Conversion Factor | | 1.432171 | |
| | Revenue Deficiency (Excess) \$ | \$ | 2,828,000 | |
| | Revenue Deficiency (Excess) % | | 28.17% | |
| | Increase applied to Acquired (Authority) customers 100% | \$ | 2,828,000 | |
| | Increase % | | 28.17% | |
| | Increase applied to Acquired (Authority) customers 50% | \$ | 1,414,000 | |
| | Increase % | | 14.09% | |
| | Increase applied to Existing (Company Wastewater) customers 50% | \$ | 1,414,000 | |
| | Increase % | | 3.82% | |
| | Increase applied to Existing (Company Water) customers (Act 11) | \$ | 3,216,709 | |
| | Increase % | | 0.74% | |

| | Avg. Usage / Kgal | Estimated Monthly Increase | Estimated Monthly Increase | Estimated Percentage Increase |
|--|-------------------|----------------------------|----------------------------|-------------------------------|
| Impact Existing (Lower Makefield) Residential 100% | 4.69 | \$ 20.94 | | 28.17% |
| Impact Existing (Lower Makefield) Commercial 100% | 4.69 | \$ 30.32 | | 28.17% |
| Impact Existing (Lower Makefield) Residential 50% | 4.69 | \$ 10.47 | | 14.09% |
| Impact Existing (Lower Makefield) Commercial 50% | 4.69 | \$ 15.16 | | 14.09% |
| Impact Existing Customers (Company Wastewater) - Residential - 50% | 3.02 | \$ 2.61 | | 3.82% |
| Impact Existing Customers (Company Wastewater) - Commercial - 50% | 21.94 | \$ 8.20 | | 3.82% |
| Impact Existing Customers (Company Wastewater) - Industrial - 50% | 3.20 | \$ 2.11 | | 3.82% |
| Impact Existing Customers (Company Water) - Residential | 4.08 | \$ 0.48 | | 0.74% |
| Impact Existing Customers (Company Water) - Commercial | 37.05 | \$ 3.02 | | 0.74% |
| Impact Existing Customers (Company Water) - Industrial | 211.51 | \$ 14.24 | | 0.74% |

| | | | | |
|-----|-----------------------|---------|-----------|-------|
| 2.) | Rate of Return | | | |
| | Debt | Ratio | Cost Rate | WACC |
| | Equity | 47.15% | 4.43% | 2.09% |
| | | 52.85% | 10.00% | 5.29% |
| | | 100.00% | | 7.37% |

| | | | |
|-----|--|----------|---------------|
| 3.) | Gross Revenue Conversion Factor | | |
| | Dollar of Revenue | | 1.0000 |
| | Less: Gross Receipts (Revenue) Tax | 0.00% | 0.0000 |
| | Less: Reg Assessments | 0.62% | 0.0062 |
| | Less: Bad Debts | 1.17% | 0.0117 |
| | State Taxable Income | | 0.982053 |
| | State Income Tax | 9.9999% | 0.0982 |
| | Federal Taxable Income | | 0.883848772 |
| | Federal Tax Rate | 21.00% | |
| | Federal Income Tax | | 0.185608 |
| | Net Revenue Dollar | | 0.69824052992 |
| | Gross Revenue Conversion Factor | | 1.43217123 |
| | EFT | 28.8999% | |