



COMMONWEALTH OF PENNSYLVANIA  
PENNSYLVANIA PUBLIC UTILITY COMMISSION  
P.O. BOX 3265, HARRISBURG, PA 17105-3265

IN REPLY PLEASE  
REFER TO OUR FILE

February 22, 2010

James J. McNulty, Secretary  
Pennsylvania Public Utility Commission  
P.O. Box 3265  
Harrisburg, PA 17105-3265

Re: Pennsylvania Public Utility Commission v. Newtown Artesian Water  
Company

Docket No. R-2009-2117550

Dear Secretary McNulty:

Enclosed please find an original and nine (9) copies of the Office of Trial Staff's  
(OTS) **Exceptions** in the above-captioned proceeding.

Copies are being served on all active parties of record.

Sincerely,

Adeolu A. Bakare  
Prosecutor  
Office of Trial Staff  
PA Attorney I.D. #208541

Enclosure  
AAB/edc

cc: Parties of record  
Chairman Cawley  
Vice Chairman Christy  
Commissioner Pizzigrilli  
Commissioner Gardner  
Commissioner Powelson  
Chief Counsel Pankiw  
Director Davis

SECRETARY'S BUREAU  
PA PUC

2010 FEB 22 PM 1:15

RECEIVED



## TABLE OF CONTENTS

I.	INTRODUCTION .....	1
II.	EXCEPTIONS .....	2
	1. OTS Exception No. 1: The ALJ Erroneously Concluded that Single Issue Ratemaking is Inapplicable to Commission Review of a Proposed Section 1307 Surcharge .....	2
	2. OTS Exception No. 2: The ALJ Failed to Distinguish NAWC’s PWAC from the Surcharge at Issue in <i>Pennsylvania Indus.</i> on the grounds that NAWC’s PWAC is a Section 1307 Surcharge Seeking to Recover Expenses Normally Considered in a Base Rate Case .....	5
	3. OTS Exception No. 3: The ALJ Erroneously Concluded that the Commission Approved an Automatic Adjustment Clause Permitting Recovery of Purchased Water Expense for United Water Bethel, Inc. ....	8
	4. OTS Exception No. 4: The ALJ Erroneously Concluded that the Proposed Purchased Water Adjustment Clause is Lawful Without Addressing the Question of Public Interest .....	10
III.	CONCLUSION .....	14

**TABLE OF CITATIONS**

**Cases**

*Pennsylvania Indus. Energy Coalition v. Pennsylvania Public Utility Commission*,  
653 A.2d 1336, 1347, 1349-50 (1996)..... 3, 4, 6

**Commission Decisions**

*Pennsylvania Public Utility Commission v. United Water Bethel, Inc.*  
Docket No. R-00963804 (Order entered December 19, 1996) ..... 8, 9

**Statutes**

66 Pa. C.S. § 1307 ..... *passim*

66 Pa. C.S. § 1307(a)..... 4, 5

66 Pa. C.S. § 1308 ..... 9

66 Pa. C.S. § 1308(b) ..... 1

## I. INTRODUCTION

The Office of Trial Staff (“OTS”) respectfully submits these instant Exceptions to the Recommended Decision of Administrative Law Judge Ky Van Nguyen (“ALJ”) issued by cover letter from the Office of Administrative Law Judge (“OALJ”) on February 1, 2010, in this fully litigated proceeding. Newtown Artesian Water Company (“NAWC” or “Company”) initiated the case on July 1, 2009, by filing Supplement No. 68 to Tariff Water – Pa. P.U.C. No. 9, with an effective date of August 31, 2009.<sup>1</sup> The tariff supplement proposes to implement a purchased water adjustment clause (“PWAC”) pursuant to Section 1307 of the Public Utility Code, 66 Pa. C.S. § 1307.<sup>2</sup> The Office of Consumer Advocate (“OCA”) filed a Formal Complaint, Public Statement and Notice of Appearance on July 24, 2009. OTS filed a Notice of Appearance on August 10, 2009.

On September 1, 2009, in accordance with Public Utility Code Section 1308(b), the filing was suspended by operation of law until March 1, 2010. The parties convened for a Prehearing Conference on October 9, 2009. ALJ Nguyen issued a Prehearing Order memorializing the hearing schedule on October 13, 2009.

Following the schedule set forth in the Prehearing Order, OTS distributed

---

<sup>1</sup> NAWC initially filed Supplement No. 67 to Tariff Water – Pa. P.U.C. No. 9 on July 1, 2009 and subsequently received notice from Commission staff that the filing should have been filed as Supplement No. 68. Pursuant to Commission staff directive, NAWC filed Supplement No. 68 on July 16, 2009. For briefing purposes, Supplement No. 68 is referred to as if filed on July 1, 2009.

<sup>2</sup> NAWC Exhibit No. 1, Supporting Information, p. 3.

OTS Statement No. 1, the Direct Testimony of Jeremy Hubert on October 23, 2009, OTS Statement No. 1-SR, the Surrebuttal Testimony of Jeremy Hubert and accompanying OTS Exhibit No. 1-SR on December 8, 2009. The evidentiary hearing was held on December 15, 2009, at which time the OTS testimony and exhibits were entered into the record. Additionally, ALJ Nguyen entered OTS Cross-Examination Exhibit Nos. 1-3 into the record.

In the Recommended Decision, the ALJ rejects or fails to address positions advanced in the OTS Main and Reply Briefs. These OTS Exceptions therefore respectfully urge the Commission to reject the ALJ's recommendations and recognize the legitimacy and value of incorporating each of the OTS recommendations into the final Order resolving this proceeding.

## **II. EXCEPTIONS**

### **OTS EXCEPTION NO. 1**

#### **The ALJ Erroneously Concluded that Single Issue Ratemaking is Inapplicable to Commission Review of a Proposed Section 1307 Surcharge**

Recommended Decision, pp. 7-9.

OTS Main Brief, pp. 4-6.

OTS Reply Brief pp. 4-8.

The ALJ improperly expanded the scope of a Commonwealth Court holding and erroneously concluded that single issue ratemaking is inapplicable to the Commission's review of NAWC's purchased water adjustment clause. In reaching this conclusion, the ALJ relied on the Commonwealth Court's decision in

Pennsylvania Indus. Energy Coalition v. Pa. PUC.<sup>3</sup> However, as propounded in the OTS Reply Brief, the Commonwealth Court never addressed the issue of whether the doctrine of single issue ratemaking is applicable to the Commission's review of a proposed Section 1307 automatic adjustment clause. The ALJ failed to recognize the limited scope of the Commonwealth Court's review and improperly characterized its holding as a limitation upon the Commission's consideration of single issue ratemaking.

In *Pennsylvania Indus.*, the Commonwealth Court addressed the question of whether the doctrine of single issue ratemaking is applicable to its decision to affirm or reverse a Commission approved surcharge. In this case, the Pennsylvania Industrial Energy Coalition ("Industrial Coalition"), petitioned the Commonwealth Court for review of Commission orders requiring implementation of demand side management ("DSM") programs. The Industrial Coalition, *inter alia*, opposed the cost recovery methods approved by the Commission, contending that "that each method of recovering program costs approved by the PUC, the balancing account recovered in later base rates and the annually adjusted surcharge, violates the Code."<sup>4</sup> As part of its argument, the Industrial Coalition claimed that "permitting a surcharge" is single issue ratemaking.<sup>5</sup>

---

3 *Pennsylvania Indus. Energy Coalition v. Pennsylvania Public Utility Commission*, 653 A.2d 1336, 1349-50 (1995) [Pennsylvania Indus.].

4 *Id.* at 1347.

5 *Id.* at 1349.

Before reaching the Commonwealth's Court's disposition of this issue, it must be noted that the question before the Court concerned only the use of single issue ratemaking as a justification for reversing a Commission action. As emphasized in the Recommended Decision, the Commonwealth Court found the doctrine of single issue ratemaking to be inapplicable "[b]ecause the surcharge is permitted under the Code." RD, p. 9. As stated in the OTS Main Brief, Section 1307(a) places the approval of a surcharge within the discretion of the Commission. Therefore, as was the case in *Pennsylvania Indus.*, a surcharge is "permitted under the Code" only upon the Commission's approval. This observation clarifies the distinction between the Commonwealth Court's use of the doctrine of single issue ratemaking to reverse a Commission approved surcharge and the Commission's consideration of the doctrine of single issue ratemaking in evaluating a surcharge currently before it.

The Commonwealth Court's finding that single issue ratemaking is inapplicable as a defense to a Commission approved surcharge does not disturb the Commission's authority to balance the negative effects of single issue ratemaking against any benefits that might accrue from a proposed 1307 surcharge. Again, in *Pennsylvania Indus.*, the Commonwealth Court addressed the allegation of the Industrial Coalition that "permitting a surcharge" is single issue ratemaking. By answering the question in the negative, the Court essentially held that it will not apply the doctrine of single issue ratemaking to reverse a Commission decision

permitting a surcharge.<sup>6</sup> The Commonwealth Court did not express an opinion regarding the Commission's consideration of the doctrine of single issue ratemaking in exercising its discretionary authority under Section 1307(a). Consequently, the Commission should grant the OTS Exception to the ALJ's conclusion that the doctrine of single issue ratemaking is inapplicable to a Section 1307 surcharge.

## OTS EXCEPTION NO. 2

**The ALJ Failed to Distinguish NAWC's PWAC from the Surcharge at Issue in *Pennsylvania Indus.* on the grounds that NAWC's PWAC is a Section 1307 Surcharge Seeking to Recover Expenses Normally Considered in a Base Rate Case.**

Recommended Decision, p. 9.  
OTS Reply Brief pp. 6-7.

As described in the above Exception, the ALJ relied upon *Pennsylvania Indus.* to find that single issue ratemaking is inapplicable to the Commission's review of NAWC's PWAC. However, this finding contradicts the Commonwealth Court's implicit assertion that single issue ratemaking is applicable where a party requests recovery of expenses normally considered in a base rate case. In addition to the reasons offered in OTS Exception No. 1, the ALJ's finding should be rejected because the Commonwealth Court limited its holding in *Pennsylvania*

---

<sup>6</sup> "Indeed, in determining the inapplicability of the doctrine to its review, the court noted that 'the PUC applied Section 1307's authorization to specifically allow an automatic adjustment of rates outside of the rate-making procedures.' The Commonwealth Court has simply recognized that, as established in the OTS Main Brief, Section 1307 empowers the Commission to permit single issue ratemaking. When the Commission properly invokes its statutory powers to allow single issue ratemaking through an automatic adjustment clause, the nature of the single issue cost recovery becomes inapplicable to the Commonwealth[sic] Court review of the Order." OTS Reply Brief, p. 6.

*Indus.* to cases where no party seeks to recover a line item that would normally be considered in a base rate case.

In finding that the doctrine of single issue ratemaking is inapplicable to appellate review of the DSM surcharge proposed in *Pennsylvania Indus.*, the Commonwealth Court predicated its decision on the fact that DSM costs are not typically recovered through base rate cases. The excerpt from the Court's opinion in the Recommended Decision demonstrates the emphasis placed upon this distinction:

Single issue ratemaking is similar to retroactive ratemaking and, in general, is prohibited if it impacts on a matter that is normally considered in a base rate case. This is, however, not a base rate case. No party has asked for specific recovery of a line item that traditionally would be requested in a rate-making procedure. RD, p. 9.

Assuming, *arguendo*, that the Commonwealth Court intended to declare single issue ratemaking inapplicable to the Commission's review of a Section 1307 surcharge, the ALJ's recommendation must still fail because the costs recovered through NAWC's proposed PWAC are traditionally considered in base rate cases. As stated by the ALJ, "the financial impacts of all regulatory lag on utilities are considered by the Commission in establishing an appropriate rate of return." RD, p. 4.

Allowing recovery of increased purchased water expenses outside of a base rate case would enable NAWC to recover such expenses regardless of any

simultaneous decreases in other line items that might serve to offset any portion of the increased purchased water expenses.<sup>7</sup> This is not a result contemplated by *Pennsylvania Indus.* as the Commonwealth Court specifically exempted surcharges recovering costs typically considered in base rate cases from its finding that single issue ratemaking is inapplicable to Section 1307 surcharges. RD, p. 9. By exempting surcharges designed to recover costs typically considered in base rate cases from its finding that single issue ratemaking is inapplicable to Section 1307 surcharges, the Commonwealth court implicitly stated that single issue ratemaking is applicable in those cases where a Section 1307 surcharge recovers costs typically considered in a base rate case.

Therefore, OTS requests that the Commission grant this OTS Exception to the ALJ's finding that single issue ratemaking is inapplicable to NAWC's proposed PWAC.

---

<sup>7</sup> This is in contrast to the holistic process undertaken in a Section 1308 base rate case. The OTS Main Brief presented a description of this process through the following recounting of NAWC's 2008 settlement: "In reaching a settlement of a base rate case, the parties do not approve individual expenses. Rather, each party individually reviews the revenue and expense items and determines an overall revenue number that, considering all factors, is sufficient to provide the utility with an opportunity to earn a just and reasonable return. OTS Main Brief, p. 18.

### OTS EXCEPTION NO. 3

**The ALJ Erroneously Concluded that the Commission Approved an Automatic Adjustment Clause Permitting Recovery of Purchased Water Expense for United Water Bethel, Inc.**

Recommended Decision, p. 12.

OTS Reply Brief pp. 10-11.

In justifying the use of Section 1307 to recover NAWC's increased purchased water expenses, the ALJ erroneously found that the Commission approved a similar clause for another large water utility, United Water Bethel, Inc. ("Bethel Inc."). In the Recommended Decision, the ALJ states that "the Commission has approved an automatic adjustment clause for recovery of purchased water expense for Bethel Inc., a water utility, like Newtown Artesian, with annual revenue greater than \$250,000." RD, p. 12. This observation is based upon a misunderstanding of the Commission Order Entered December 19, 1996 at Docket No. R-00963804 ("1996 Bethel Order")<sup>8</sup>. Bethel Inc. neither requested nor received an automatic adjustment clause for recovery of purchased water expense. As demonstrated in the OTS Reply Brief, the Commission granted Bethel Inc.'s request to recover a specific and identifiable purchased water increase through a surcharge, a markedly different mechanic from a purchased water adjustment clause.

In the 1996 Bethel Order, the Commission granted Bethel Inc.'s request for a purchased water pass-through to be recovered through a surcharge. Bethel, Inc.

---

8 NAWC Exhibit No. 2

had filed a purchased water pass-through to recover \$102,092 in additional revenues pursuant to notice from its suppliers of increases in purchased water rates effective in November and October of 1996. OTS RB, p. 10. The Commission approved the purchased water pass-through, but “unlike the procedures attendant to an automatic adjustment clause, the Company was not granted leave to further adjust the surcharge in the event of any subsequent increases in purchased water rates.” OTS RB, p. 10. In fact, the Commission explicitly required the Company to file a base rate case upon the next subsequent rate increase. OTS RB, p. 10-11.

As explained in the OTS Main Brief, “a PWAC is a perpetual mechanism enabling the Company to recover the amount of any subsequent purchased water increase through a Section 1307 proceeding.” OTS MB, p. 12. Indeed, even as NAWC seeks to implement the proposed PWAC, it has no scheduled purchased water rate increases. As observed by the ALJ, BCWSA, NAWC’s sole supplier of purchased water, intends to hold NAWC’s current rates through 2012. RD, p. 6. Accordingly, NAWC’s PWAC is designed to recover future purchased water rate increases. The Commission did not grant such an open ended clause in the 1996 Bethel Order. OTS MB, p. 10-11. The surcharge granted to Bethel, Inc. was limited to recovery of the specific dollar amount requested in that Section 1308 proceeding; no provision for additional future recovery was made. OTS MB, p. 10. Therefore, OTS requests that the Commission grant this Exception to the

ALJ's finding that United Water Bethel, Inc. was granted an automatic adjustment clause for the recovery of purchased water expense.

#### **OTS EXCEPTION NO. 4**

##### **The ALJ Erroneously Concluded that the Proposed Purchased Water Adjustment Clause is Lawful Without Addressing the Question of Public Interest.**

Recommended Decision, pp. 12.

OTS Main Brief, pp. 13-22.

OTS Reply Brief pp. 11-14.

The ALJ found that NAWC's proposed PWAC is "lawful" without making a determination as to whether it is in the public interest. The OTS Main Brief provided a lengthy discussion concerning the Commission's authority to grant NAWC's proposed PWAC. In the Main Brief, we concluded that approval or disapproval of NAWC's proposed PWAC is entirely a discretionary matter subject to the Commission's judgment. OTS subsequently provided evidence showing that the Company's interests are adequately protected by currently available remedies and that the proposed PWAC could potentially harm ratepayers. Accordingly, OTS submits that the proposed PWAC is not in the public interest and respectfully Excepts to the ALJ's failure to address the issue.

The ALJ's analysis of the application of Section 1307 established only that NAWC's proposed PWAC is not among the class of costs prohibited from recovery under Section 1307, such a determination, in and of itself, does not justify approval of the proposed PWAC. As stated in the Recommended Decision, OTS

opines that “the Commission has authority to grant an automatic adjustment clause for a non-capital expense which is easily determined and beyond a utility’s control, or required by government entity.” RD, p. 10. NAWC’s proposed PWAC fits the criteria but, as noted by the ALJ, “OTS recommends that the Commission reject Newtown Artesian’s proposed purchased water adjustment charge.” RD, p. 10. In testimony and in brief, OTS offered several arguments demonstrating that the PWAC is not in the public interest and should be rejected.

Nevertheless, the Recommended Decision does not provide a discussion regarding the balancing of Company and ratepayer interests. NAWC argued, in testimony and in its brief, that the Company suffers adverse financial effects due primarily to the absence of a PWAC. Specifically, NAWC argued that it is unable to earn a reasonable rate of return due to its large lost purchased water expense (“LPWE”) and that it averages a disproportionately low return on common equity. NAWC MB, p. 32-33. In the OTS Main and Reply Briefs, we provided a detailed record refuting NAWC’s claims of business hardship and evidencing the harms that would likely befall ratepayers upon approval of the proposed PWAC.

In the Main Brief, OTS argued that NAWC cannot arbitrarily attribute the shortfall from its settled base rate cases to LPWE as the parties reached an overall revenue number satisfactory to all but “did not negotiate or communicate every revenue or expense item that they might have considered individually amongst themselves.” OTS MB, p. 20. OTS also noted that NAWC’s comparison of its

actual return on equity to the *authorized* returns granted to other utilities constitutes and “apples to oranges” comparison. OTS MB, 20-21. Additionally, OTS argued that NAWC’s claims of unduly inflated base rate case expenses ring hollow because the Company has never filed to increase rates exclusively for recovery of purchased water rate increases. OTS MB, p. 21. In fact, the Company’s 2008 base rate filing for increased revenues of \$695,802 included \$410,802 of non-purchased water expenses. OTS MB, p. 22.

The OTS Reply Brief outlined the ratepayer harm that would likely flow from the proposed PWAC. OTS argued that parceling out large expenses from the base rate review process subjects the ratepayers to potentially confiscatory rates.<sup>9</sup> As stated in the Reply Brief, “[t]his is particularly important because NAWC’s proposed PWAC does not incorporate a check upon expenses to be recovered through the automatic adjustment clause. OTS RB, p. 13. However, the Recommended Decision did not address the merits of these arguments regarding the alleged adverse financial effects suffered by the Company or the potential harm to ratepayers.

Neither did the Recommended Decision address the available remedy of a purchased water pass-through. In the OTS Reply Brief, we averred that any adverse financial consequences that may flow from regulatory lag following increased purchased water expenses could be cured by a purchased water pass-

through. Paradoxically, NAWC argues that its recent base rate cases were filed primarily to recover increased purchased water rates, yet the Company has not sought relief through a purchased water pass-through. As demonstrated by the record of United Water Bethel, Inc., purchased water pass-through filings are an effective methodology for permitting accelerated recovery of increased purchased water costs without perpetually removing such costs from the traditional ratemaking process. OTS RB, p. 13.

Based on the evidence that NAWC has overstated the adverse financial effects suffered in the absence of a PWAC, the potential for harm to ratepayers following the granting of the proposed PWAC and the availability of an alternative remedy through the traditional ratemaking process, OTS recommends that the Commission grant this Exception to the ALJ's failure to discuss the public interest implications of NAWC's proposed PWAC and reject the proposed PWAC as against the public interest.

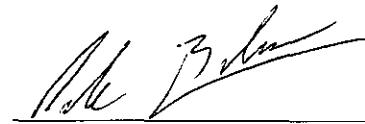
---

<sup>9</sup> OTS is cognizant of the modifications to NAWC's proposed PWAC recommended by the ALJ and submits that the 3% cap on the proposed PWAC and the one directional interest payments mitigate, but fails to eliminate the potential for unduly burdensome rates. *See* RD, p. 13, 18-19.

### III. CONCLUSION

For the reasons set forth above, the Office of Trial Staff hereby maintains that the Commission should issue an Order concluding this proceeding that incorporates all OTS Exceptions submitted herein.

Respectfully submitted,



---

Adeolu Bakare  
Prosecutor  
PA Attorney I.D. # 208541

Office of Trial Staff  
Pennsylvania Public Utility Commission  
P.O. Box 3265  
Harrisburg, PA 17105-3265  
(717) 783-6155

Dated: February 22, 2010

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission :  
v. : Docket No. R-2009-2117550  
Newtown Artesian Water Company :

**CERTIFICATE OF SERVICE**


I hereby certify that I am serving the foregoing **Exceptions**, dated February 22, 2010, either personally, by first class mail, electronic mail, express mail and/or by fax upon the persons listed below, in accordance with the requirements of § 1.54 (relating to service by a party):

Honorable Ky Van Nguyen  
Office of Administrative Law Judge  
Pennsylvania Public Utility Commission  
801 Market Street, Room 4063  
Philadelphia, PA 19107

Jennedy S. Johnson, Esquire  
Dianne E. Dusman, Esquire  
Office of Consumer Advocate  
555 Walnut Street  
5<sup>th</sup> Floor Forum Place  
Harrisburg, PA 17101-1923

William R. Lloyd, Esquire  
Office of Small Business Advocate  
300 North Second Street  
Suite 1102 Commerce Building  
Harrisburg, PA 17101

Thomas T. Niesen, Esquire  
Thomas, Long, Niesen & Kennard  
212 Locust Street, Suite 500  
P.O. Box 9500  
Harrisburg, PA 17108-9500

  
Adeolu A. Bakare  
Prosecutor  
Office of Trial Staff  
PA Attorney I.D. #208541

RECEIVED  
2010 FEB 22 PM 1:15  
SECRETARY'S BUREAU