

COMMONWEALTH OF PENNSYLVANIA



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July 7, 2010

Honorable Charles E. Rainey, Jr.
PA Public Utility Commission
801 Market Street, Suite 4063
Philadelphia, PA 19107

Re: Pa. Public Utility Commission, *et al.*

v.

Pennsylvania-American Water Company
Clarion Wastewater Operations, R-2010-2166208
Claysville Wastewater Operations, R-2010-2166210
Coatesville Wastewater Operations, R-2010-2166212
Northeast Wastewater Operations, R-2010-2166214

Dear Judge Rainey:

Enclosed please find an original and one copy of the Prehearing Memorandum of the Office of Consumer Advocate.

Copies have been served upon all parties of record as shown on the attached Certificate of Service.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Shaun A. Sparks".

Shaun A. Sparks
Assistant Consumer Advocate
PA Attorney I.D. #87372

Enclosures

cc: Secretary's Office of the PUC
Certificate of Service

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four above-referenced rate increase requests. While PAWC filed four unconsolidated cases, PAWC generally employs the same witnesses in the filings and the filings raise similar issues. The OCA supports consolidation of the cases if consolidation avoids scheduling difficulties. Regarding consolidation, this Prehearing Memorandum will address issues common to all four filings in a unified fashion and will address the particulars of each case to the extent necessary. The OCA would also point out that the Parties should agree on the organization of testimony, exhibits, and schedules (as well as evidentiary hearings) to accommodate the four cases and some parties' limited participation in the four cases.

Coatesville Wastewater Operations

On 23 April 2010, Pennsylvania-American Water Company, Coatesville Wastewater Operations, d/b/a Pennsylvania American Water (PAWC-Coatesville) filed Supplement No. 2 to Tariff Wastewater Pa. P.U.C. No. 8 to become effective 22 June 2010. Through this Tariff Supplement, PAWC-Coatesville seeks Commission approval increased rates for providing wastewater service to its ratepayers.

The Coatesville Wastewater Operations of Pennsylvania American Water serves approximately 6,030 customers, consisting of residential, commercial, industrial and municipal customers in the City of Coatesville, the Borough of Parkesburg, and the following Townships: West Sadsbury, East Fallowfield, Caln, West Caln, West Brandywine, Valley, Sadsbury and Highland, in Chester County

If the proposed tariff supplement becomes effective, PAWC-Coatesville would benefit from an opportunity to recover an estimated increase in its total annual operating revenues of \$8,156,652, which is an overall increase of approximately 158%. The bill of a typical residential customer would increase from \$27.43 per month to \$90.26 per month, an approximate increase of 229%. A typical commercial customer bill would increase from \$83.54 to \$243.18, an approximate increase of 191%.

Clarion Wastewater Operations

On 23 April 2010, Pennsylvania-American Water Company, Clarion Wastewater Operations, d/b/a Pennsylvania American Water (PAWC-Clarion) filed Original Tariff Wastewater - Pa. P.U.C. No. 10 to become effective 22 June 2010. Through this tariff filing, PAWC-Clarion seeks Commission approval of increased rates for providing wastewater service to its ratepayers.

The Clarion Wastewater Operations of Pennsylvania American Water serves approximately 2,200 customers, consisting of residential, commercial industrial and municipal customers in Clarion Borough and portions of the Townships of Clarion and Monroe in Clarion County.

If the proposed tariff becomes effective, PAWC-Clarion would benefit from an opportunity to recover an estimated increase in its total annual operating revenues of \$968,817, which is an overall increase of approximately 84%. The bill of a typical residential

customer would increase from \$21.52 per month to \$40.37 per month, an approximate increase of 88%. A typical commercial customer bill would increase from \$110.66 to \$209.83, an approximate increase of 90%.

Claysville Wastewater Operations

On 23 April 2010, Pennsylvania-American Water Company, Claysville Wastewater Operations, d/b/a Pennsylvania American Water (PAWC-Claysville) filed Original Tariff Wastewater - Pa. P.U.C. No. 11 to become effective 22 June 2010. This original tariff would cancel Tariff Wastewater-Pa. P.U.C. No. 6 and seeks Commission approval of increased the rates for providing wastewater service to its ratepayers.

The Claysville Wastewater Operations of Pennsylvania American Water serves approximately 496 customers, consisting of residential, commercial industrial and municipal customers in Claysville Borough, Washington County and portions of the Township of Donegal in Washington County.

If the proposed tariff becomes effective, PAWC-Claysville would benefit from an opportunity to recover an estimated increase in its total annual operating revenues of \$487,486, which is an overall increase of approximately 158%. The bill of a typical residential customer would increase from \$38.30 per month to \$92.75 per month, an approximate increase of 142%. A typical commercial customer bill will increase from \$74.95 to \$241.60, an approximate increase of 222%.

Northeast Wastewater Operations

On 23 April 2010 Pennsylvania-American Water Company, Northeast Wastewater Operations, d/b/a Pennsylvania American Water (PAWC-Northeast) filed Tariff Wastewater Pa. P.U.C. No. 9 to become effective 22 June 2010. Through this tariff filing, PAWC-Northeast seeks Commission approval of increased rates for providing service to its ratepayers.

Three separate divisions constitute PAWC's Northeast operations. The Northeast Wastewater Operations of Pennsylvania American Water serves nearly 3,200 residential customers in its Lehman Pike system, over 700 residential customers in its Blue Mountain Lake system and approximately 100 residential customers in its Winona Lakes system. The Northeast customers reside in portions of Lehman Township, Pike County and portions of Smithfield and Stroud Townships in Monroe County.

If the proposed tariff supplement becomes effective, PAWC-Northeast would benefit from an opportunity to recover an estimated increase in its total annual operating revenues of \$2,099,490, which is an overall increase of approximately 240%. The bill of a typical Lehman Pike system customer would increase from \$16.90 per month to \$57.70 per month, an approximate increase of 241%. The bill of a typical Blue Mountain system customer would increase from \$23.05 per month to \$80.02 per month, an approximate increase of 247%. The bill of a typical Winona Lake system customer would increase from \$27.33 per

month to \$69.03 per month, an approximate increase of 153%.

The OCA filed its Formal Complaints and Public Statements in these matters on 29 April 2010. Since that time, the OCA has engaged with PAWC and the Parties in matters concerning the rate increase request, as the OCA will discuss below.

II. PREHEARING MEMORANDUM

A. Required Matter

The OCA will follow seriatim the ALJ's requirements for Prehearing Memoranda found at pages 1 and 2 of the 29 June Prehearing Conference Order.

1. Settlement status

While the OCA has been in contact with PAWC over the preceding months, the OCA has not participated in settlement discussions. While the OCA is receptive to reasonable settlement discussions, the OCA has not yet completed its review of the filings and the Company has not yet responded to all OCA discovery. In addition, the OCA requires a complete review of all information provided in this matter to guide any positions it may take in settlement discussions.

2. Discovery status

To date, the OCA has served thirty-one sets of discovery for the four cases in total. In anticipation of consolidation of the filings, and to aid in administrative management, the OCA labeled its discovery sets sequentially. Thus, there is only one OCA Set 1, Set 2, etc.

across the four cases. At present, PAWC is steadily responding to OCA discovery. Regarding discovery, the OCA would emphasize that the magnitude of the proposed increases has triggered a very close examination of PAWC's support for its requests. Nevertheless, the OCA anticipates that the current cooperative exchange of information will continue.

In addition to written interrogatories, OCA expert witness Terry Fought, P.E., is performing a physical inspection of the PAWC facilities that underlie the rate increase requests and, while scheduled, has yet to complete the Northeast system inspections.

3. Proposed discovery rules

The OCA proposes that the ALJ modify the Commission's discovery rules in accord with the attached Appendix A. These modifications are particularly important given the very compressed schedule in these proceedings.

4. Proposed discovery schedule

The OCA also requests that discovery close with the end of evidentiary hearings scheduled in this matter, allowing for matters properly developed during evidentiary hearings.

5. Admissions or stipulations

The Parties have not yet developed any admissions or stipulations. The OCA is amenable to reasonable stipulations.

6. Factual issues to be addressed

Based upon its preliminary analysis of PAWC's filings, the OCA has compiled a list of issues that it anticipates will be included in its investigation of the proposed rate increase requests. While the OCA has been as thorough as possible, the OCA anticipates that discovery responses may raise additional issues.

The OCA has served extensive interrogatories, toured and inspected most of the PAWC facilities, and has obtained information related to both. When the Company has responded to all interrogatories, and OCA has had the opportunity to review responses to OCA discovery (and the discovery of other Parties), the OCA anticipates that further discovery meetings and potential settlement discussions may take place. The OCA will also be better able to quantify its specific recommendations when it develops and files its direct testimony.

The list of issues and sub-issues set forth below will be analyzed and presented as appropriate by the OCA with the assistance of its expert witnesses.

A. Rate of Return

1. Cost of Common Equity: The OCA will perform a detailed analysis of the cost of common equity claimed by PAWC. The OCA will examine PAWC's barometer group of companies to assess the Company's claimed cost of common equity. Also, the OCA will carefully examine the Company's methodologies and supporting data used to

develop its final cost of common equity claim. The OCA will show that the various upward adjustments sought by PAWC are without merit.

2. Capital Structure: The OCA will examine whether the capital structure claimed by PAWC is representative of the similar companies and consistent with the period in which rates will be in effect and is otherwise appropriate for ratemaking purposes.

3. Embedded Cost of Debt: The OCA will examine the embedded cost of debt claimed by PAWC.

4. Interest Coverage Ratios: The OCA will perform an analysis of the reasonableness of the interest coverage ratios as a test for rate of return recommendations.

B. Rate Base/Measure of Value

1. The OCA will examine the reasonableness and accuracy of the projections of PAWC related to the water utility plant in service at the time relevant to this proceeding including, but not limited to, whether the test year plant will be completed as claimed and whether retirements are accurately reflected.

2. The OCA will review PAWC's claim for plant additions during the future test year to determine if PAWC has prudently incurred all such costs.

3. The OCA will investigate whether PAWC's adjustment to rate base for depreciation reserve is appropriate with a particular emphasis on the Coatesville system.

4. The OCA will examine PAWC's projections of non-investor supplied

funds, including but not limited to, customer advances for construction and contributions in aid of construction.

5. The OCA will examine PAWC's claim for materials and supplies.

6. The OCA will examine PAWC's calculation and amount of cash working capital, including the impacts of changing to monthly billing.

7. The OCA intends to examine the reasonableness and accuracy of PAWC's claimed valuation of its investment.

C. Revenues And Expenses

1. The OCA will examine whether the number of customers projected on PAWC's system at the times relevant to this proceeding is reasonable and accurate.

2. The OCA will examine whether PAWC's estimates of the volume of wastewater to be treated during future periods is reasonable and accurate.

3. The OCA will examine whether PAWC's projection of revenues in the future test year is reasonable and accurate.

4. The OCA will examine whether the salary and wage annualizations and increases included by PAWC in the pro forma test year are reasonable and accurate including, but not limited to, whether PAWC will fill vacancies and new positions as claimed.

5. The OCA will review the costs associated with the accrual of

retirement benefits other than pensions for PAWC's employees.

6. The OCA will examine whether PAWC's general inflation adjustment is just and reasonable.

7. The OCA intends to examine the appropriateness of PAWC's pro forma claim for rate case expense.

8. The OCA will examine the reasonableness of PAWC's projected price increases for electric power purchased.

9. The OCA will evaluate the miscellaneous other expense items which appear to be based upon company projections of future price levels.

10. The OCA will review PAWC's request for depreciation expenses to determine whether it is just and reasonable.

D. Taxes

The OCA may raise issues related to the calculation of taxes including, but not limited to, calculation of federal and state income taxes and the amount of those taxes included as expenses for ratemaking purposes, including an adjustment for consolidated tax savings.

E. Rate Structure/Cost of Service/Rate Design

1. The OCA will examine PAWC's proposed distribution of the revenue increase among customer classes and ratemaking regions and its proposed capacity charge.

2. The OCA will examine whether the rate design changes proposed by PAWC are reasonable and appropriate.

3. The OCA will examine PAWC's cost of service study, including the methodology used and the reasonableness of the allocation.

4. The OCA will examine the reasonableness and appropriateness of PAWC's proposed tariff changes.

F. Quality of Service

1. The OCA will examine whether PAWC's collection main extension and other quality of service rules and regulations are enforced and applied in a fair and equitable manner.

2. The OCA will examine whether PAWC is providing its current and future residential customers with adequate, efficient, safe and reasonable service.

G. Other Issues

1. The OCA will examine any relevant environmental issues that arise because of the PAWC's operations.

2. The OCA will investigate to ensure that the Company is complying with prior Commission orders.

7. Legal Issues To Be Addressed

The OCA is currently examining the legal issues raised by PAWC's proposed tariff

changes. While not yet complete, the OCA analysis raises legal issues related to cost allocations and plant in service. The OCA will present factual issues related to this in testimony, and will present fully-developed argument on these issues in briefs.

8. Names, Titles and Business Addresses of Witnesses

The OCA will present the following witnesses in this proceeding:

Accounting/Regulatory Policy: Mr. Ralph Smith
Larkin & Associates
15728 Farmington Road
Livonia, MI 48154
RSmithLA@aol.com
msdady@gmail.com
dawn.bisdorf@gmail.com

Rate of Return: J. Randall Woolridge
Penn State University
120 Hammaker Circle
State College, PA 16801
IRW@psu.edu

Rate Design/Cost of Service: Mr. Scott Rubin, Esq.
333 Oak Lane
Bloomsburg, PA 17815
scott.j.rubin@gmail.com

Quality of Service: Mr. Terry Fought, P.E., Consulting Engineer
780 Cardinal Drive
Harrisburg PA 17111
tlfengr@comcast.net

The OCA reserves the right to call additional witnesses. The OCA will notify the ALJ and all parties of record immediately should the need for additional witnesses arise.

9. Issues Each Witness Will Address

Mr. Rubin will address cost of service and rate design issues. Mr. Smith will address accounting and revenue requirement issues. Mr. Woolridge will address issues relating to rate of return. Mr. Fought will address issues related to quality of service. The OCA has described each of these subject areas in detail above.

10. Proposed Date For Second Prehearing Conference

The OCA does not propose that the ALJ conduct a second prehearing conference in this matter at this time. The OCA will nevertheless be available at the convenience of the ALJ and the Parties should a second prehearing conference or settlement hearing be requested or required.

11-13. Proposed Schedule

Please see Appendix B for the OCA proposed schedule. The OCA has included dates beyond the reply brief for the convenience of the Parties. The OCA has one conflict regarding its witness Scott Rubin. The OCA would propose to file Mr. Rubin's direct on 2 August 2010 with other parties responding to Mr. Rubin on 23 August 2010. Mr. Rubin would then provide surrebuttal on 27 August 2010.

In support of its proposed schedule, the OCA requires 90 days from the date of filing to prepare its direct case. While the Company has ostensibly had well over a year to prepare its case, the OCA is reasonably entitled to 90 days to perform its request for

proposal contracting process, hire consultants, perform discovery, review and analyze the filing, and develop direct testimony. Here, the end of the suspension period for the PAWC filings is Friday, 21 January 2011 and there is a Commission public meeting on Thursday, 13 January 2011. The ALJ has also directed that the Parties provide reply briefs no later than Thursday, 30 September 2010. Considering these dates, and in particular the 30 September date, the OCA proposes schedule in Appendix B. The OCA has been in contact with the Parties and is working to develop a schedule for these proceedings. The OCA points out that PAWC can alleviate any scheduling difficulty associated with its method of filing these cases. It is PAWC's option to move from the January 13, 2011 public meeting to the January 27, 2011 public meeting to allow for more time for litigation. The ALJ should take PAWC's willingness to exercise this option into consideration in setting the procedural schedule.

14. Other Pertinent Information.

The number of protests and formal complaints indicates significant public interest in these proceedings. The following table shows the OCA's approximate to-date tally of combined formal complaints, rate protests, and letters voicing opposition to the proposed rate increase in each division.

Coatesville -	445
Clarion -	14
Claysville -	169
Northeast -	21

Based on this expression of public concern, the OCA respectfully requests that the Commission conduct public input hearings in each of the affected service areas. The OCA will work with the Commission, the Company, and the other Parties to locate accommodations for these hearings. The OCA also requests that the Commission direct PAWC to advertise these public input hearings in media outlets serving each service area. The OCA would also request the opportunity to review the announcements prior to publication.

As the service area descriptions show, the four divisions are in far-flung and discrete areas. For this reason, combined public input hearings would be inappropriate. Regarding Coatesville, the OCA would request two public input hearings - one afternoon and one evening hearing. Regarding the Northeast division, the OCA has received a telephonic request for a hearing in or near the Saw Creek development. The OCA would request at least one in-person public input hearing in Claysville, and to accommodate scheduling issues, the OCA is amenable to conducting a telephonic public input for the Clarion division.

B. SERVICE ON OCA

Senior Assistant Consumer Advocate Dianne E. Dusman and Assistant Consumer Advocate Shaun A. Sparks will represent the OCA in this matter. Parties should serve two copies of all documents on the OCA as follows:

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Respectfully submitted,

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Senior Assistant Consumer Advocate

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DATED: July 7, 2010
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APPENDIX A

OCA Proposed Order For Expedited Discovery

Discovery must be conducted according to the Commission's rules and regulations, subject to the following modifications for an expedited discovery period. Because the time for discovery is limited, a shortened discovery response period is appropriate. Therefore, the following modifications will apply:

- A. Responding parties to provide answers to written interrogatories in-hand within ten (10) calendar days of service of the interrogatories.
- B. Respondents will orally communicate objections to interrogatories to the propounding party within three (3) days of service; respondents will provide written objections to the propounding party within five (5) days of service.
- C. Propounding parties will file motions to dismiss objections and/or direct the answering of interrogatories with the ALJ within three (3) days of service of written objections.
- D. Respondents will answer to motions to dismiss objections and/or direct the answering of interrogatories within three (3) days of service of such motions.
- E. Rulings over such motions will be issued, if possible, within seven (7) days of filing of the motion.
- F. Responses to requests for document production, entry for inspection, or other purposes will be served in-hand within ten (10) calendar days.
- G. Requests for admission will be deemed admitted unless answered within ten (10) days or objected to within five (5) days of service
- H. Answers to on-the-record data requests will be served in-hand within three (3) calendar days of the request.

APPENDIX B

OCA Proposed Schedule

	<i>Day and Date</i>	<i>Day Interval</i>
Filing	Friday, April 23, 2010	
		60
Suspension Required By	Tuesday, June 22, 2010	
		76
Prehearing	Thursday, July 08, 2010	
		21
Public Input Hearings Begin	Thursday, July 29, 2010	
		90
Intervenor Direct (from filing)	Thursday, July 22, 2010	
		21
Company Rebuttal	Thursday, August 12, 2010	
		14
Intervenor Surrebuttal	Thursday, August 26, 2010	
		3
Evidentiary Hearings Begin	Monday, August 30, 2010	
		21
Initial Brief	Monday, September 20, 2010	
		10
Reply Brief	Thursday, September 30, 2010	
		45
Recommended Decision	Thursday, November 04, 2010	
		20
Exceptions	Wednesday, November 24, 2010	
		10
Reply Exceptions	Monday, December 06, 2010	
		38
Commission Public Meeting	Thursday, January 13, 2011	
End of Suspension Period	Friday, January 21, 2011	

CERTIFICATE OF SERVICE

Re: Pennsylvania Public Utility Commission

v.

Pennsylvania-American Water Company –
Clarion Wastewater Operations
Claysville Wastewater Operations
Coatesville Wastewater Operations
Northeast Wastewater Operations

Docket No. R-2010-2166208
Docket No. R-2010-2166210
Docket No. R-2010-2166212
Docket No. R-2010-2166214

I hereby certify that I have this day served a true copy of the foregoing document, Prehearing Memorandum of the Office of Consumer Advocate 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 7th day of July 2010.

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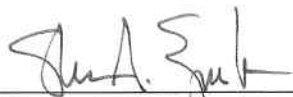
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