

COMMONWEALTH OF PENNSYLVANIA



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March 15, 2018

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

Re: Petition of Pennsylvania-American Water  
Company for Approval of Tariff Changes  
and Accounting and Rate Treatment Related  
to Replacement of Lead Customer-Owned  
Service Pipes  
Docket No. P-2017-2606100

Dear Secretary Chiavetta:

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

Copies have been served per the attached Certificate of Service.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "P. D. Demanchick".

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Enclosures

cc: Honorable Elizabeth Barnes, ALJ  
Certificate of Service

\*245093

## CERTIFICATE OF SERVICE

Petition of Pennsylvania-American Water :  
Company for Approval of Tariff Changes :  
and Accounting and Rate Treatment Related : Docket No. P-2017-2606100  
to Replacement of Lead Customer-Owned :  
Service Pipes :

I hereby certify that I have this day served a true copy of the following document, the Office of Consumer Advocate's Reply Brief, 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 15th day of March 2018.

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BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of Pennsylvania-American Water	:	
Company for Approval of Tariff Changes	:	
and Accounting and Rate Treatment Related	:	Docket No. P-2017-2606100
to Replacement of Lead Customer-Owned	:	
Service Pipes	:	

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REPLY BRIEF  
OF THE OFFICE OF CONSUMER ADVOCATE

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Dated: March 15, 2018

## **TABLE OF CONTENTS**

I.	INTRODUCTION .....	1
A.	Procedural History .....	3
II.	REPLY ARGUMENT .....	3
A.	The Commission Should Deny the Company’s Proposal to Capitalize Lead Service Pipe Replacement Costs and Recover a Return on and a Return of Such Costs. ....	3
1.	Customer-owned property cannot be capitalized and cannot be recorded in the Company’s Account 333 – Services. ....	3
a.	The Company’s proposal is not similar to previous Commission decisions allowing gas utilities to capitalize the cost of replacing customer-owned service lines. ....	4
b.	The OCA does not consider the York Water proceeding to be binding in this matter. It is an example of a reasonable approach to replacing customer-owned lead Service Pipes.....	7
c.	The costs of replacing customer-owned lead Service Pipes are not similar to the restoration costs incurred when accessing Company property. ....	8
d.	The costs of replacing customer-owned lead Service Pipes are akin to jobbing expenses and should be booked to the Company’s Account 416. ....	11
2.	Lead Service Pipe replacement costs are not eligible for inclusion in the Company’s DSIC.....	12
B.	The Commission Should Adopt the OCA’s Deferred Regulatory Accounting Recommendation. ....	12
C.	The Commission Should Adopt the OCA’s Additional Recommendations.....	16
1.	Five-Year Warranty.....	16
2.	Partial Compensation Plan .....	16
3.	Education and Outreach .....	17
IV.	CONCLUSION WITH REQUESTED RELIEF .....	19

## TABLE OF AUTHORITIES

**Page(s)**

### **Administrative Decisions**

<u>In the Matter of an Application by Halifax Regional Water Commission for an Order Approving Amendments to its Regulations to Provide for the Repair and Replacement of Lead Service Pipes in the Provision of Water Service, Matter No. M07891, 2017 NSUARB 138, Decision (Nova Scotia Utility and Review Board Aug. 22, 2017) .....</u>	7-8, 14
<u>Klossman v. Duquesne Light Co.,</u> Docket No. C-00945802, 1995 Pa. PUC LEXIS 136, Initial Decision (Dec. 22, 1995), aff'd 1996 Pa. PUC LEXIS 112, Order (July 24, 1996).....	10
<u>Pa. PUC v. Pennsylvania Power and Light Co.,</u> Docket No. R-84265, 1985 Pa. PUC LEXIS 56 (Apr. 26, 1985) .....	15
<u>Petition of Columbia Gas of Pennsylvania, Inc. for Limited Tariff Waivers of Certain Tariff Rules Related to Customer Service Line Replacement,</u> Docket No. P-00072337, 2008 Pa. PUC LEXIS 344 (May 19, 2008) .....	4, 5, 6, 10, 18
<u>Petition of Pennsylvania-American Water Company for Approval of Tariff Changes and Accounting and Rate Treatment Related to Replacement of Lead Customer-Owned Service Pipes,</u> Docket No. P-2017-2606100, Procedural Order (Aug. 9, 2017) .....	3
<u>Petition of Peoples Natural Gas Co. LLC for Approval of Limited Waivers of Certain Tariff Rules Related to Customer Service Line Replacement,</u> Docket No. P-2013-2346161, 2013 Pa. PUC LEXIS 543 (May 23, 2013) .....	4, 5, 6, 10, 18
<u>Petition of The York Water Company for an Expedited Order Authorizing Limited Waivers of Certain Tariff Provisions and Granting Accounting Approval to Record Costs of Certain Customer-Owned Service Line Replacements to the Company's Service Account,</u> Docket No. P-2016-2577404, Order (Mar. 8, 2017).....	7, 8, 15
<u>Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of New York American Water Co. for Water Service, Case No. 16-W-0259, Order (NY PSC May 18, 2017).....</u>	7

**Statutes**

66 Pa.C.S. § 1351.....1, 12

66 Pa.C.S. § 1357.....1

66 Pa.C.S. §1510.....5

## **I. INTRODUCTION**

The Office of Consumer Advocate (OCA) submits this Reply Brief in response to the Main Brief of Pennsylvania-American Water Company (PAWC or Company). The OCA's Main Brief contained a comprehensive discussion of the evidence and its position on all issues. Thus, in this Reply Brief, the OCA will respond only to those matters raised by PAWC that the OCA did not previously address or that require clarification.

The issue in this proceeding is whether the Commission should allow PAWC to revise its tariff in order to replace customer-owned lead service lines (Service Pipes, pursuant to Section 2.16 of the Company's existing Tariff) in accordance with PAWC's Replacement Plan. Specifically, PAWC requests the Commission (1) allow the Company to replace customer-owned lead Service Pipes at its sole cost, subject to the specific accounting and rate recovery treatment proposals contained in its Petition, (2) authorize the Company to capitalize such costs incurred and to record those costs in Account No. 333 – Services (Services Account) for accounting purposes, and (3) affirm that the costs are “eligible property” for water utilities under Section 1351, which means the Company can recover a return on and a return of the costs through its Distribution System Improvement Charge (DSIC) pursuant to 66 Pa.C.S. § 1357.

As stated in the OCA's Main Brief, the OCA agrees substantially with PAWC's request to replace customer-owned lead Service Pipes. OCA M.B. at 12. As noted by PAWC, however, the primary disagreement between the Company and the statutory advocates is the proposed accounting and ratemaking treatment proposals. OCA M.B. at 18-24, PAWC M.B. at 8. The OCA disagrees with the Company's proposal to earn a return on customer property that is not devoted to the public use because it violates basic ratemaking principles. OCA M.B. at 18-19. Moreover, the Company's proposed capitalization and treatment of these extraordinary, non-recurring costs

under Account 333 of the Uniform System of Accounts (USOA) will allow the Company to improperly recover depreciation and pre-tax return on customer pipes for a period of approximately fifty-seven years, realizing profits well exceeding the cost to install the pipes. OCA M.B. at 19-23. For this reason, the OCA submits that the Commission should deny the Company's proposed accounting and ratemaking treatment proposals.

The OCA submits, rather, that these costs are extraordinary, non-recurring, one-time expenses. OCA M.B. at 14-18. These expenses are extraordinary because of the effects lead exposure can have on customers as seen in the recent tragedy in Flint, Michigan. OCA M.B. at 5-8. In light of this, PAWC will attempt to replace remaining customer-owned lead Service Pipes pursuant to its Replacement Plan over a one-time, ten-year period. OCA St. 1 at 20. Accordingly, the OCA submits that the Commission allow PAWC to establish a regulatory asset through which it can track the costs and recover the reasonable and prudent expenses over an amortization period to be determined in PAWC's next base rate proceeding. OCA M.B. at 14-18.

Furthermore, the OCA has made several recommendations that the Commission should adopt for the Company's program. OCA M.B. at 24-29. First, the Company should provide a five-year warranty on all customer-owned lead Service Pipes that it replaces pursuant to the Replacement Plan. Id. at 24-26. Secondly, the Company should offer a partial compensation plan to customers that have recently replaced their lead Service Pipe in the past four years. Id. at 26-27. Such compensation would be a percentage of the total cost to the customer or a percentage of \$3,500, whichever is less, with the percentage decreasing on a pro rata basis depending on the year the customer replaced the lead Service Pipe. Id. at 26. Lastly, the Company should work with the statutory advocates to develop a comprehensive education and outreach program. OCA M.B. at 28-29.



The OCA respectfully submits this Reply Brief in support of its position.

**A. Procedural History**

The procedural history in this matter is addressed in detail in the OCA's Main Brief. OCA M.B. at 1-2. On March 1, 2018, the OCA, the Bureau of Investigation and Enforcement (I&E), the Office of Small Business Advocate (OSBA), and PAWC filed Main Briefs. The OCA files this Reply Brief on March 15, 2018 in accordance with the procedural schedule adopted in the Procedural Order. Petition of Pennsylvania-American Water Company for Approval of Tariff Changes and Accounting and Rate Treatment Related to Replacement of Lead Customer-Owned Service Pipes, Docket No. P-2017-2606100, Procedural Order at 2 (Aug. 9, 2017) (Procedural Order).

**II. REPLY ARGUMENT**

**A. The Commission Should Deny the Company's Proposal to Capitalize Lead Service Pipe Replacement Costs and Recover a Return on and a Return of Such Costs.**

The Company seeks permission from the Commission to include in the Company's rate base in a subsequent base rate proceeding and/or the Company's existing DSIC, costs it incurs during its proposed Replacement Plan. PAWC M.B. at 16. In other words, the Company seeks to earn a return of and a return on the cost of replacing customer-owned lead Service Pipes. The Company advances several arguments for its proposed accounting and ratemaking treatment. The Company's arguments are flawed and must be rejected. The OCA will deal with each in turn.

1. Customer-owned property cannot be capitalized and cannot be recorded in the Company's Account 333 – Services.

In this proceeding, the OCA and I&E have argued that the Company cannot capitalize costs incurred when replacing customer-owned lead Service Pipes, or book the costs to the Company's

Services Account, because PAWC does not own or control the customer Service Pipes. OCA M.B. at 18-19, I&E M.B. at 9-15. PAWC makes several arguments that are without merit.

- a. The Company's proposal is not similar to previous Commission decisions allowing gas utilities to capitalize the cost of replacing customer-owned service lines.*

PAWC argues that the Commission has not established a *per se* rule against capitalizing investments in customer-owned property. PAWC M.B. at 18. In support of this argument, PAWC states that the Commission previously determined that it was appropriate to capitalize costs incurred when replacing customer-owned gas service lines where the lines were made of a vulnerable material and posed safety concerns. Id.; see Petition of Columbia Gas of Pennsylvania, Inc. for Limited Tariff Waivers of Certain Tariff Rules Related to Customer Service Line Replacement, Docket No. P-00072337, 2008 Pa. PUC LEXIS 344 (May 19, 2008) (Columbia Gas), Petition of Peoples Natural Gas Co. LLC for Approval of Limited Waivers of Certain Tariff Rules Related to Customer Service Line Replacement, Docket No. P-2013-2346161, 2013 Pa. PUC LEXIS 543 (May 23, 2013) (Peoples) (collectively Gas Service Line Cases). PAWC attempts to compare the two by stating that the 'inherent danger' associated with the vulnerable gas service lines is no different than the 'insidious effects' of lead exposure. PAWC M.B. at 20.

While the OCA acknowledges the public health risks of lead exposure, the OCA submits that the Commission should reject PAWC's comparison of its proposal and the Commission's decision to allow Columbia Gas of Pennsylvania, Inc. (Columbia Gas) and Peoples Natural Gas Company, LLC (Peoples) to capitalize and earn a return on the costs of replacing customer-owned gas service lines.

In the Columbia Gas and Peoples proceedings, the Commission granted requests by both utilities to capitalize the costs of replacing customer-owned gas service lines largely because replacing those service lines was physically necessary for replacing its own gas mains. See

Columbia Gas, 2008 Pa. PUC LEXIS 344, at \*4, Peoples, 2013 Pa. PUC LEXIS 543, at \*9. For example, Columbia Gas stated that it began a program to replace all of its own unprotected bare steel and cast iron mains over the next twenty years, which would permit the utility to operate its distribution system at higher pressures than currently could be employed. Columbia Gas, 2008 Pa. PUC LEXIS 344, at \*2. The utility sought a tariff waiver to replace customer-owned bare steel gas service lines in the course of its program because failure to do so would result in customer service lines being incapable of handling the new system pressures and losing service until the customer could afford to replace it. Id., at \*4. The Commission agreed stating that the Company be allowed to replace at its expense “certain customer-owned service lines when the lines *must* be replaced as a result of Columbia’s main replacement and upgrade program. Columbia Gas, 2008 Pa. PUC LEXIS 344, at \*8 (emphasis added).<sup>1</sup> Similarly, in Peoples, the Commission granted the Petition as filed stating that:

Peoples further believes that it is proper for the Company’s costs to be capitalized, and presumably recouped through rates, because the service line replacements are necessary to complete the project and the project has overall benefits to all Peoples customers.

2013 Pa. PUC LEXIS 543, at \*14.

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<sup>1</sup> The Commission also based its decision on Section 1510 of the Public Utility Code, which states:

When connecting the premises of the customer with the gas utility distribution mains, the public utility shall furnish, install and maintain the service line or connection according to the rules and regulations of the filed tariff. A public utility shall not be authorized or required to acquire or assume ownership of any customer’s service line. A public utility shall not be authorized or required to acquire or assume ownership of any pipe or appurtenances installed after the effective date of this section between its main and the meter unless the utility would have been authorized or required to do so according to the rules and regulations of its filed tariff if the pipe or appurtenances had been installed on or before the effective date of this section. Maintenance of service lines shall be the responsibility of the owner of the service line.

66 Pa.C.S. §1510; see also Columbia Gas, 2008 Pa. PUC LEXIS 344, at \*7-8. The water utility industry does not have a similar statutory provision.

In this proceeding, however, PAWC has failed to show evidence that the replacement of customer-owned lead Service Pipes is physically necessary. As stated above, the customer gas service lines that the gas utilities replaced would not have been operational otherwise. The gas service lines would have been unable to handle the additional pressure, forcing the customer to have to pay for the replacement. In this instance, the Company asserts that it will undertake partial service line replacements in circumstances where a customer refuses to allow the Company to replace its lead Service Pipe. The Company states that it will use a dielectric coupling to separate the dissimilar metals of the replaced Company-owned Service Line (copper) and the customer-owned lead Service Pipe. PAWC St. 1R at 6, PAWC M.B. at 16.

Another material difference between PAWC's situation and the Gas Service Line Cases, is that natural gas distribution companies (NGDCs) may, in certain areas, own and maintain the entire service line from the main to the customers' premises. Accordingly, NGDCs already have a mechanism in base rates to recover the costs associated with gas service lines on the customer's premises. Columbia Gas and Peoples, however, are the exception to the rule wherein some customers own their portion of the service line. See Columbia Gas, 2008 Pa. PUC LEXIS 344 at \*3, Peoples, 2013 Pa. PUC LEXIS 543, at \*8. For that reason, both gas utilities had to seek a tariff waiver to replace those lines. Within the water utility industry, however, it is not common to own the customer portion of the service line. Accordingly, PAWC does not own any customer Service Pipes and does not presently include any customer-owned Service Pipes in rate base.

For these reasons, PAWC's proposal to replace customer-owned lead Service Pipes is not similar to the situation in Columbia Gas and Peoples for ratemaking purposes. Accordingly, the Commission should reject PAWC's reliance on the two cases.

- b. The OCA does not consider the York Water proceeding to be binding in this matter. It is an example of a reasonable approach to replacing customer-owned lead Service Pipes.*

The Company remarks that I&E and the OCA improperly rely on the precedential effect of the settlement adopted by the Commission regarding York Water Company's (York Water) proposal to replace customer-owned lead service lines as reason not to allow PAWC to capitalize the costs of replacing customer-owned Service Pipes. PAWC M.B. at 21; see Petition of The York Water Company for an Expedited Order Authorizing Limited Waivers of Certain Tariff Provisions and Granting Accounting Approval to Record Costs of Certain Customer-Owned Service Line Replacements to the Company's Service Account, Docket No. P-2016-2577404, Order (Mar. 8, 2017) (York Water).

The OCA, however, has not relied on York Water to the extent the Company claims. Rather than treat it with precedential effect, the OCA submits that York Water provides an example to the Commission of how a Pennsylvania water utility was permitted to treat the costs of customer-owned lead service line replacements. The OCA has not argued that the Commission is **required** to follow the same treatment. Rather, the OCA has argued that its proposed regulatory asset treatment is reasonable for the reasons presented in this case.

York Water's approach also contains a cost sharing mechanism by requiring the utility to bear some of the costs through deferred accounting treatment. This is consistent with the replacement of customer-owned lead service lines in other jurisdictions. See Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of New York American Water Co. for Water Service, Case No. 16-W-0259, Order (NY PSC May 18, 2017), In the Matter of an Application by Halifax Regional Water Commission for an Order Approving Amendments to its Regulations to Provide for the Repair and Replacement of Lead Service Pipes in the Provision of

Water Service, Matter No. M07891, 2017 NSUARB 138, Decision (Nova Scotia Utility and Review Board Aug. 22, 2017).

PAWC further attempts to differentiate its position from York Water by claiming that York Water needed to correct pre-existing violations of the Lead and Copper Rule in accordance with DEP and EPA mandated deadlines. PAWC M.B. at 21. To meet these deadlines, PAWC states York Water agreed to forego earning a return or other carrying charge, which allowed for a quick settlement and the ability to make the replacements to meet the deadlines. Id.

The OCA submits that the Company is not in a position to state the reasons why York Water entered into a settlement and why it might have chosen to forego its original position. Many factors go in to the decision to settle. Moreover, PAWC was not involved in the negotiations between York Water and opposing counsel. PAWC and its experts, therefore, have no firsthand knowledge of what occurred during these discussions. As such, the argument by PAWC should be disregarded.

*c. The costs of replacing customer-owned lead Service Pipes are not similar to the restoration costs incurred when accessing Company property.*

PAWC claims that the costs associated with the replacement of customer-owned lead Service Pipes is similar to roadway restoration costs incurred when undergoing work on Company-owned mains, services, and appurtenances. PAWC M.B. at 22. The Company explains that every time the Company excavates a public street to install, replace, or rehabilitate its mains, service, or appurtenances, it incurs substantial roadway restoration costs. Moreover, PAWC argues that these costs include restoration work performed on the customer premises that were damaged in the course of such replacement. PAWC M.B. at 22. PAWC states that these restoration costs are capitalized and booked to the utility's property account for the underlying capital project, even though the Company does not own the property. Id. PAWC further reasons that just as the

excavation needed to undergo main replacement impacts the serviceability of municipally-owned property (roadways), the excavation of Company-owned Service Lines directly affects the serviceability of the customer-owned lead Service Pipe. PAWC M.B. at 22-23.

As stated in the OCA's Main Brief, roadway restoration costs are not comparable to replacing customer-owned lead Service Pipes. OCA M.B. at 22-23. Roadway restoration costs represent an unavoidable expense that results from the Company having to access its own property. OCA St. 1SR at 5; OCA M.B. at 23. Additionally, the Company has a right-of-way to access those mains, which presumably includes the ability to disturb the property above.

In this proceeding, the Company has shown no evidence that the replacement of a customer-owned lead Service Pipe is an unavoidable consequence of replacing a Company-owned lead Service Line. The Company rejected the OCA's recommendation that the Company not undertake any partial lead service line replacements, unless there is no feasible alternative stating, "PAWC may need to replace its Service Line, even if a customer-owned LSP cannot be replaced at the same time, to avoid conflicts with other utilities to complete important main replacement work..." PAWC M.B. at 16. Additionally, the Company has stated that it must obtain permission to conduct this work because it has no right of way. PAWC M.B. at 5. Accordingly, the Company cannot compare replacement of lead Service Pipes to roadway restoration work.

Additionally, I&E distinguished between customer-owned lead Service Pipe replacements and roadway restoration costs on the basis that the former only benefits the individual customer, whereas main and service replacement underlying the restoration work benefits all customers. I&E M.B. at 11-12. PAWC rejects this distinction, arguing that it routinely makes expenditures that benefit a small number of customers that are capitalized and included in rate base, such as main extensions benefiting an individual homeowner. PAWC M.B. at 23.

The OCA, however, disagrees with PAWC's argument. While the Company may make expenditures benefitting a small number of customers and earn a return on those expenses, the Company only gives an example of installing its own property, *i.e.* main extension benefitting only one customer. PAWC M.B. at 23. The OCA acknowledges that where the Company installs property that it owns, the costs are prudent and reasonable, and the property is used and useful, it may earn a return on those costs regardless of the number of customers connected. In a situation where the Company intends to earn a profit from capitalizing customer property, however, it matters whether the benefits extend to all customers, or only a few. See Columbia Gas, 2008 Pa. PUC LEXIS 344, at \*6, Peoples, 2013 Pa. PUC LEXIS 543, at \*9.

The Company claims that the Replacement Plan will benefit all customers because it will allow the Company to expand its main replacement program into areas it has delayed because of the risks of partial lead service line replacements in these areas. This reason is insufficient, however, because the Company has delayed its plan voluntarily and indeed stated that "infrastructure rehabilitation in those areas is necessary and must be undertaken." Petition at 7. The Company, therefore, intends to finish the main replacement program whether or not customers allow it to replace their Service Pipes. Moreover, the Commission has stated that customer-owned service line extensions are a customer specific cost:

Costs incurred at the request of an individual customer which are beyond the standard service supplied to other customers, in the same rate class, are considered to be customer-specific. Such non-standard service requests include private property service line extensions...

Klossman v. Duquesne Light Co., Docket No. C-00945802, 1995 Pa. PUC LEXIS 136, at \*20, Initial Decision (Dec. 22, 1995), *aff'd* 1996 Pa. PUC LEXIS 112, at \*43-44, Order (July 24, 1996).

For these reasons, the OCA submits that the Company cannot argue that the costs of replacing customer-owned lead Service Pipes are an unavoidable cost similar to roadway



restoration work, or that it is similar to the installation of company-owned property that benefits a small number of customers, or that replacement of Service Pipes are beneficial to all customers.

- d. The costs of replacing customer-owned lead Service Pipes are akin to jobbing expenses and should be booked to the Company's Account 416.*

As stated in the OCA's Main Brief, the costs of replacing customer-owned property are properly considered a jobbing expense, which is an expense resulting from work the Company performs on behalf of a third-party on an incidental or contract basis. OCA M.B. at 19-20. The Company rejects this interpretation because under the Company's proposal these costs will be included in its overall, regulated cost of service, which is not directly charged to the customers whose LSP is being replaced. PAWC M.B. at 24. For this reason alone, PAWC argues that the Replacement Program is conceptually far different from the relationship between the utility and counter-parties envisioned by Account 416. PAWC M.B. at 24.

The OCA submits that whether or not the Company collects the costs of replacing lead Service Pipes from all ratepayers or specific customers is immaterial to whether the Company should treat these costs as a special category of jobbing expenses under Account 416. The USOA defines Accounts 415 and 416 as follows:

415. Revenues from Merchandising, Jobbing, and Contract Work

416. Costs and Expenses of Merchandising, Jobbing, and Contract Work

A. These accounts shall include respectively, all revenues derived from the sale of merchandise and jobbing or contract work, including any profit or commission accruing to the utility on jobbing work performed by it as agent under contracts whereby it does jobbing work for another for a stipulated profit or commission, and all expenses incurred in such activities.

Uniform System of Accounts for Class A Water Utilities, National Association of Regulatory Utility Commissioners, Account 416 (1996). Simply put, if the Company performs work for another for payment of expenses incurred, it must include all costs and expenses from such work

in Account 416. The definition of Account 416 does not exclude jobbing expenses recovered from all ratepayers.

For this reason, the Company's argument against treatment of these costs as a jobbing expense should be rejected. The OCA submits that the Company book these costs as a special category of a jobbing expense under Account 416 of the USOA.

2. Lead Service Pipe replacement costs are not eligible for inclusion in the Company's DSIC.

The Company requests affirmation from the Commission that the costs of replacing customer-owned lead Service Pipes constitutes eligible property under 66 Pa.C.S. Section 1351. PAWC M.B. at 30. Specifically, the Company argues that once the Commission determines that Service Pipe replacements costs should be capitalized, that these costs are squarely within the definition of 'other capitalized costs' under Section 1351 of the Public Utility Code. Id.

As stated in the OCA's Main Brief, the Commission should not allow the Company to capitalize these costs and include them in rate base. OCA M.B. at 18-19. The ordinary treatment of utility expense on third-party property is to expense such cost as it is incurred and not recover it. See pgs. 13-14, infra. Moreover, these expenses cannot be booked to the Company's Services Account because it constitutes costs on property existing on the customer's premises, which is outside the definition of the –Services Account. OCA M.B. at 21-23. For these reasons, the OCA submits that these costs should not be considered 'eligible property' under Section 1351 of the Public Utility Code.

**B. The Commission Should Adopt the OCA's Deferred Regulatory Accounting Recommendation.**

In the OCA's Main Brief, it recommended to the Commission that the Company should be allowed to recover the prudent and reasonable expenses incurred when replacing customer-owned lead Service Pipes over an amortization period to be determined in PAWC's next base rate

proceeding. OCA M.B. at 14-18. To that end, the OCA recommended that the Commission allow the Company to establish a deferred regulatory asset through which it can track the costs incurred in between base rate proceedings. Id. The OCA noted that rather than require the Company to expense 100 percent of the costs and not be allowed recover any of it, as would normally be done with such expenses, these extraordinary and substantial, non-recurring expenses warrant special ratemaking treatment.

The Company disagrees with this approach for several reasons. First, the Company claims that the amortization method does not compensate the Company for committing capital for an extended period, similar to cash working capital. PAWC M.B. at 26. The OCA submits, however, that its recommendation allows the Company to recover expenses that it would otherwise be required to expense immediately with no recovery. OCA St. 1 at 7. As stated by the OCA's witness:

[T]he Company is proposing a program that is likely to last for ten years or more. The typical ratemaking treatment for such a program would be to expense the costs as they are incurred. When the Company files a base rate case then the costs would be eligible for inclusion in the test year. In April 2017, PAWC filed a base rate case with a calendar year 2018 projected test year (Docket No. R-2017-2595853). PAWC, however, did not include costs associated with customer-owned service lines in its rate-case projections, and it never updated its case to include such costs. Thus, we have a situation where a utility is proposing to incur an on-going expense beginning in the projected test year that it did not include in the test year projections in the rate case. The typical ratemaking treatment for such an expenditure would be to ignore it until the next base rate case. Many things change between cases -- some costs increase, others decrease; new projects are implemented, others are terminated; and so on. Base rates are set based on an overall level of projected costs synchronized with projected levels of sales, customer counts, investment levels, and other costs. Base rates are not meant to track each particular project or specific expenditure amounts. Recovery is not dollar-for-dollar.

As such, the normal approach to this program would be to require the Company to expense the cost and treat it as one of those items that changes between rate cases. Because of the important public-health implications of the project, however, I am proposing special ratemaking treatment that provides the Company with the opportunity to recover most of its costs from customers. My proposed deferral and amortization would enable the Company to eventually recover from customers the costs it otherwise would be required to expense immediately. While Mr. Cox views this as a "glass half empty" because it does not provide perfect compensation to the

Company, I view it as a "glass half full" because it provides the Company with compensation that it otherwise would not be entitled to receive.

OCA St. 1 at 6-7. Under ordinary circumstances, PAWC would not be able to recover any of its expenses associated with the replacement of customer-owned lead Service Pipes. Given the nature of lead exposure, however, the OCA does recommend that the Company recover the reasonable and prudent expenses associated with the Replacement Plan. This treatment provides some compensation to the Company and is sufficient to support its efforts.

The Company further argues that these expenses cannot be characterized as 'atypical' and 'non-recurring' because these expenses require regular annual expenditures for ten years. PAWC M.B. at 27. The OCA submits, however, that the costs of replacing customer-owned lead Service Pipes constitutes a non-recurring expense justifying the use of a deferred accounting treatment. As explained by OCA witness Scott Rubin:

I consider this to be a one-time, extraordinary expenditure, even though the "one time" may last as long as 10 years due to the time-consuming nature of the work and the need to schedule it in conjunction with other projects. In short, the work will be performed at a few thousand properties, it is essential for the work to be performed in order to protect public health, it will be performed once, and there will be no need to repeat it once this program is finished.

OCA St. 1 at 20.

Lastly, the Company argues that the OCA's position on 'cost sharing' does not support the OCA's regulatory asset recommendation. PAWC M.B. at 28. More specifically, the Company argues that the cases the OCA's witness cited to does not demonstrate the cost sharing the OCA proposes in this proceeding. PAWC M.B. at 28-30. The OCA agrees that the approaches taken in other jurisdictions differ from what the OCA proposes in this proceeding. By way of example, Halifax Water's program does allow the Company to include 25% of the costs of replacing customer-owned lead service lines in rate base as an unplanned or emergency circumstance.

The OCA has not suggested that its recommendation matches exactly the approaches taken in other jurisdictions. Rather, the OCA is stating that in other proceedings dealing with the replacement of customer-owned lead service lines, there is an element of cost sharing between ratepayers and investors. As Scott Rubin makes clear, “[t]he details of the cost sharing differ, but in no instance are all utility customers being required to pay a return of and return on 100% of the costs of replacing customer-owned lead service lines.” OCA St. 1SR at 8. Moreover, the OCA points specifically to York Water as an approach that the Commission may find reasonable, which itself includes a cost-sharing mechanism, *i.e.* the use of a deferred regulatory asset. OCA St. 1 at 15. Such cost sharing has been recognized by the Commission, where expenses are not the fault of either the investors or customers.

For the purposes of this proceeding we agree with the judge that the sudden burden of this new plant investment on the company’s customers was no fault of Penn Power or of its investors; but neither was it the fault of ratepayers. Under these circumstances there must be some sharing of the risk associated with bringing large plants on line.

See e.g. Pa. PUC v. Pennsylvania Power and Light Co., Docket No. R-84265, 1985 Pa. PUC LEXIS 56, at \*23 (Apr. 26, 1985).

For the reasons above and in the OCA’s Main Brief, the Commission should allow the Company to establish a deferred regulatory asset through which it can track expenses it incurs during its Replacement Plan and book any offsetting state or federal grant money it receives. Additionally, PAWC should be allowed to recover the reasonable and prudent expenses it incurs over an amortization period to be determined in PAWC’s next base rate proceeding.

**C. The Commission Should Adopt the OCA's Additional Recommendations**

1. Five-Year Warranty

The Company objects to the OCA's recommendation that PAWC provide a five-year warranty for Service Pipe replacements, stating that a one year limited workmanship warranty is sufficient. PAWC M.B. at 16.

A one year limited warranty, however, is an inadequate period to determine whether there are issues with the installation of the Service Pipe and the materials the Company used. OCA M.B. at 24-16; OCA St. 1SR at 3. The Commission should allow enough time to ensure that the Company installed the line properly. One way to determine the integrity of the newly installed Service Pipe is to subject the line to extreme weather conditions, such as freezing and thawing or heavy rain. OCA St. 1SR at 3. If the Company only provides a one-year limited warranty, it is unlikely that a newly installed Service Pipe will experience sufficient weather disturbances in order to ensure the line is not defective. Id.

Additionally, it is highly unusual for a service line to fail in the first few years of its service life. As the OCA's witness stated "if a line failed in its first five years, there would be a strong likelihood that something was wrong, either with the materials used in the pipe or in the way it was installed." Id. Accordingly, a five-year period would allow sufficient time to determine that the Company properly installed the pipe and that it is functioning correctly.

2. Partial Compensation Plan

The Company has opposed the OCA's recommendation that it implement a sliding scale of reimbursement for customers that have replaced their lead Service Pipe in the past four years on the basis that it would be administratively complex and that the proper focus of this proposal is on customer-owned Service Pipes that remain in service and pose a health risk. PAWC M.B. at 15.

As stated in the OCA's Main Brief,

There is little evidence to suggest, however, that this reimbursement program would be administratively complex. The Company stated that it "anticipates a small number of customers would qualify for reimbursement." PAWC St. 1R at 18. Moreover, the OCA's recommendation limits the reimbursement period to four years prior to the enactment of the Replacement Plan. This is "consistent with the general limitation on refunds of customer bills under the Public Utility Code (Section 1312(a))." OCA St. 1SR at 4. The administration of this program, therefore, should not pose a burden to PAWC.

Additionally, the OCA's recommendation provides sufficient protection for the Company. Under the OCA's proposal, the Company would verify the customer's lead Service Pipe replacement by visiting the customer site to confirm, as well as require a paid invoice, a certification from a verified plumber, and other documentation as determined by the Company. OCA St. 1 at 23-24.

OCA M.B. at 26-27. The OCA would reiterate that there are equity concerns involved if the Company fails to reimburse customers that have recently replaced their lead Service Pipe and at the same time require them to pay for the replacement of another customer's lead Service Pipe replacement under the Replacement Plan. See OCA M.B. at 27.

### 3. Education and Outreach

PAWC addresses its public education efforts stating that its "efforts regarding lead service lines are consistent with the National Drinking Water Advisory Council's recommendations."

PAWC M.B. at 5. To that end, the Company's communications plan includes:

Direct mailings to notify potentially affected customers of the Replacement Plan, press releases, bill inserts, information on the Company's website regarding health effects of lead, and a lead information pamphlet to be distributed to all customers. In addition, PAWC plans to release an educational video about lead and notify customers when lead is encountered on the customer-owned segment of the service line.

PAWC M.B. at 5.

The OCA supports the Company's efforts to be consistent with the National Drinking Water Advisory Council's recommendations concerning public outreach and education. OCA M.B. at 28-29. The OCA does submit, however, that the Company should work with the statutory

advocates to further develop PAWC's comprehensive outreach and education program. Id. The Commission has previously encouraged the statutory advocates to work with the utility to develop a proper education and communication plan where the utility seeks to replace customer-owned service lines. See Peoples, 2013 Pa. PUC LEXIS 543, at \*15 ("We commend OCA in this approach, and urge Peoples to collaborate with OCA in keeping its customers fully and properly informed as to the costs and benefits of their service line replacements."), Columbia Gas, 2008 Pa. PUC LEXIS 344, at \*9.

By recommending PAWC work with the statutory advocates the Commission will ensure the development of a robust and informative program ensuring that PAWC consumers (1) are fully informed about lead contamination, (2) know how to identify if their Service Pipes is made of lead, (3) have information about the Company's Replacement Plan, and (4) have the ability to contact representatives of the Company in order to evaluate whether the consumer should be placed on the service line replacement list.



#### IV. CONCLUSION WITH REQUESTED RELIEF

For the reasons set forth above, and in the OCA's Main Brief, the OCA submits that the Commission approve the Company's tariff revision to allow it to replace, at its expense, customer-owned lead Service Pipes. The Commission, however, should reject the Company's proposed accounting and ratemaking treatment as the Company has not proven by a preponderance of the evidence that it be allowed to capitalize the costs and include them in rate base. Alternatively, the OCA asks the Commission to allow the Company to book such costs into a deferred regulatory asset in which it may recover the prudent and reasonable expenses over an amortization period to be decided in the Company's next base rate proceeding. Additionally, the OCA requests that the Company provide a 5-year warranty for replaced Service Pipes, partial compensation to customers that replaced their lead Service Pipe prior to this proposal, and work with the statutory advocates to develop a comprehensive education and outreach program.

Respectfully submitted,



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