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January 11, 2022

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor
Harrisburg, PA 17120

VIA ELECTRONIC FILING

RE: Pennsylvania Public Utility Commission v. Aqua Pennsylvania, Inc.;
Docket No. R-2021-3027385

Dear Secretary Chiavetta:

Attached for filing with the Pennsylvania Public Utility Commission is the Main Brief of the Aqua Large Users Group ("Aqua LUG") in the above-referenced proceeding.

As evidenced by the attached Certificate of Service, all parties to this proceeding are being duly served with a copy of this document. Thank you.

Very truly yours,

A handwritten signature in blue ink, appearing to read 'A. Bakare', written over a light blue horizontal line.

Adeolu A. Bakare
MCNEES WALLACE & NURICK LLC

Counsel to the Aqua Large Users Group

Attachment

c: Administrative Law Judge Mary D. Long (via E-Mail and First Class Mail)
Certificate of Service

CERTIFICATE OF SERVICE

I hereby certify that I am this day serving a true copy of the foregoing document upon the participants listed below in accordance with the requirements of 52 Pa. Code Section 1.54 (relating to service by a participant).

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Counsel to the Aqua Large Users Group

Dated this 11th day of January, 2022, at Harrisburg, Pennsylvania.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission, *et al.* :
 :
 v. : R-2021-3027385, *et al.*
 :
 Aqua Pennsylvania, Inc. :

Pennsylvania Public Utility Commission, *et al.* :
 :
 v. : R-2021-3027386, *et al.*
 :
 Aqua Pennsylvania Wastewater, Inc. :

**MAIN BRIEF OF THE
AQUA LARGE USERS GROUP**

Building Owners & Managers Association (BOMA) of Philadelphia
Swarthmore College
Thomas Jefferson University

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Dated: January 11, 2021

I. INTRODUCTION

On August 20, 2021, Aqua Pennsylvania, Inc. ("Aqua" or "Company"), filed Tariff Water-Pa. P.U.C. No. 3 ("Tariff Water No. 3") and Tariff Sewer-Pa. P.U.C. No. 3 ("Tariff Sewer No. 3") with the Pennsylvania Public Utility Commission ("PUC" or "Commission"). Collectively, Aqua proposes to implement an approximate \$97.7 million base rate increase for water and sewer customers.

On October 14, 2021, the Aqua Large Users Group ("Aqua LUG") filed a Complaint in this proceeding. Aqua LUG is an ad hoc association of large volume end-users receiving water service from Aqua. Aqua LUG members require substantial volumes of water in their operations, and water costs comprise a significant element of their respective costs of operation. Because any change in Aqua's rates would impact the price Aqua LUG members pay for service, Aqua LUG is an active party to this proceeding. Current Aqua LUG membership is listed on the cover page of this Main Brief.

On October 15, 2021, Administrative Law Judge ("ALJ") Mary D. Long convened a Prehearing Conference, in which the procedural schedule for this proceeding was developed. Pursuant to the procedural schedule, Aqua LUG submitted the Direct Testimony of Richard A. Baudino on November 10, 2021. Aqua LUG also received Direct Testimony on or around November 10, 2021, from the Office of Consumer Advocate ("OCA"); Bureau of Investigation and Enforcement ("I&E"); Office of Small Business Advocate ("OSBA") (collectively, "State Advocates"); Citizens for Affordable Utility Services and Energy Efficiency in Pennsylvania ("CAUSE-PA"); and the Masthope Mountain Community Association ("Masthope"). Aqua LUG received Rebuttal Testimony from the Company and the OSBA on November 19, 2021. On December 14, 2021, Aqua LUG received Surrebuttal Testimony from Aqua, OCA, OSBA, I&E, Masthope, and CAUSE-PA.

Evidentiary Hearings in this proceeding were held on December 20, 2021, during which Aqua LUG stipulated the testimony of Mr. Baudino into the record. Pursuant to the procedural schedule and 52 Pa. Code Section 5.502, Aqua LUG now files this Main Brief.

II. SUMMARY OF ARGUMENT

In this Main Brief, Aqua LUG addresses three specific issues raised in this proceeding. First, Aqua LUG argues against Aqua's requested \$97.7 million rate increase as unjust and unreasonable in light of evidence presented by the State Advocates indicating that a lower overall rate increase would provide the Company with sufficient revenues, while ensuring just and reasonable rates for Aqua's customers. See Section III.A¹, infra. Notably, Aqua LUG is not proposing specific expense or revenue requirement adjustments, but supports consideration of the adjustments proposed by OCA and I&E. Second, Aqua LUG submits that the Purchased Water Adjustment ("PWA") and Energy Cost Adjustment ("ECA") riders proposed by the Company in this proceeding must be denied as inappropriate single-issue ratemaking. See Section V.A, infra. Finally, Aqua LUG opposes the Company's proposed revenue allocation for failure to achieve sufficient progress towards cost of service and recommends that the Commission either adopt the revenue allocation proposed by OSBA witness Brian Kalcic and supported by Mr. Baudino or alternatively adopt the revenue allocation proposed by Mr. Baudino. See Section VI.A, infra.

¹ Because Aqua LUG has not addressed every topic identified in the Common Briefing Outline, the section numbering in this Main Brief differs from the Common Briefing Outline. However, each header shows the respective numbering in the Common Briefing Outline set forth in the Prehearing Order of October 19, 2021.

III. EXPENSES
(Section V of Standard Brief Outline)

A. Aqua Should Be Granted the Minimal Rate Increase Necessary, if Any, in Order to Ensure Just and Reasonable Rates for the Company's Customers.

Pursuant to the Pennsylvania Public Utility Code, "[e]very rate made, demanded, or received by any public utility ... shall be just and reasonable." 66 Pa. C.S. § 1301. In order to ensure that Aqua's rates meet these criteria, the PUC should grant the Company the minimal rate increase necessary to allow it to provide adequate service to its customers, while still maintaining just and reasonable rates. Aqua LUG is not proposing an independent revenue requirement recommendation, but rather recommends that any rate increase awarded for Aqua fall within the parameters recommended by the State Advocates.

Both the OCA and I&E have offered substantial evidentiary support, based on detailed analyses of Aqua's Rate of Return ("RoR") and claimed expenses, to reduce the overall rate increase proposed by the Company. See generally OCA Statement No. 1, Direct Testimony of Ralph C. Smith (hereinafter, "OCA St. 1"); OCA Statement No. 1-SR, Surrebuttal Testimony of Ralph C. Smith (hereinafter, "OCA St. 1-SR"); OCA Statement No. 3, Direct Testimony of David J. Garrett (hereinafter, "OCA St. 3"); OCA Statement No. 3-SR, Surrebuttal Testimony of David J. Garrett (hereinafter, "OCA St. 3-SR"); I&E Statement No. 1, Direct Testimony of Christine Wilson (hereinafter, "I&E St. 1"); I&E Statement No. 1-SR, Surrebuttal Testimony of Christine Wilson (hereinafter, "I&E St. 1-SR"); I&E Statement No. 2, Direct Testimony of Anthony Spadaccio (hereinafter, "I&E St. 2"); and I&E Statement No. 2-SR, Surrebuttal Testimony of Anthony Spadaccio (hereinafter, "I&E St. 2-SR").

For example, both the OCA and I&E findings suggest significant adjustments to the Company's proposed expenses in several areas, including cash working capital, pension expense, and payroll. See generally OCA St. 1, pp. 19-62; and I&E St. 2 pp. 8-43. Similarly, both the

OCA and I&E support a significantly lower ROR and Return on Equity ("ROE") than those offered by the Company. See OCA St. 2, p. 3; and I&E St. 1, p. 6. As part of this analysis, the OCA places more emphasis on the Discounted Cash Flow ("DCF") methodology, while I&E claims Aqua failed to support its proposed size adjustment to its Capital Asset Pricing Model results. See OCA St. 3, p. 3; and I&E St. 2, pp. 49-50. Based upon these findings, the OCA and I&E both propose a total rate increase significantly below that requested by the Company.

The Commission must consider the evidence presented by both the OCA and I&E as guidance for determining the necessary rates applicable to Aqua. Specifically, the Commission must deny Aqua's request for a \$97.7 million rate increase and modify this request based upon review of the reasonable adjustments offered by the OCA and I&E.²

IV. RATE OF RETURN (Section VII of Standard Brief Outline)

See Section III, infra.

V. MISCELLANEOUS ISSUES (Section VIII of Standard Brief Outline)

A. Aqua Should Not Be Permitted to Implement a Purchased Water Adjustment or an Energy Cost Adjustment, as Such Mechanisms Would Constitute Inappropriate and Impermissible Single-Issue Ratemaking.

As part of this proceeding, Aqua is proposing to implement a PWA to "capture changes in its cost to purchase water caused by changes in the rates charged by non-affiliated suppliers from whom the Company purchases water." Aqua Statement No. 4, Direct Testimony of Christopher M. Henkel (hereinafter, "Aqua St. 4"), p. 2. According to Aqua, the PWA would automatically adjust customer bills, at the Company's option, any time one or more of its water

² As Aqua LUG is not proposing specific adjustments to Aqua's proposed expense or revenue requirement, this Main Brief omits the rate schedules referenced in the Prehearing Order issued on October 19, 2021.

suppliers changes rates for sales to the Company. Id. at 3-4. Aqua also proposes to implement an Energy Cost Adjustment Mechanism to "recover the costs of energy [electric and natural gas] used to provide water services to its customers and only those costs." Because such adjustments are nothing more than an unjust and unreasonable attempt at single-issue ratemaking, these mechanisms should be rejected by the Commission.

The Commission has a long-standing policy disfavoring rate mechanisms that would adjust rates based on a single issue. See, e.g., I&E St. 3, p. 14. Under this policy, single-issue ratemaking is prohibited if it "impacts on a matter that is normally considered in a base rate case." Pa. Indus. Energy Coalition v. Pa. Pub. Util. Comm'n., 653 A.2d 1336, 1350 (Pa. Commw. 1995). This prohibition is "based on the rate maker's obligation to consider all of a utility's revenues and costs in the balancing process to achieve just and reasonable rates." Pub. Util. Comm'n. v. Philadelphia Gas Works, Docket No. P-00042090, Order (July 8, 2004), p. 7. Otherwise, such a "review of expense items in isolation could result in confiscatory rates," in part by ignoring the fact that a utility "may have a sufficient over-collection in another matter to adequately compensate the company" for any undercollection it may experience in the matter that is the subject of the rate. Id.

The proposed PWA and Energy Cost Adjustment Mechanism ("ECAM") would violate this long-standing policy by permitting adjustments to customer rates that would be based solely on the cost of purchased water and energy, which are simply a single item of Aqua's cost to serve that is normally and properly included in base rate proceedings. See OCA St. 4, p. 24. The PWA and ECAM would circumvent the normal process of filing a base rate increase for these expenses and would thereby ignore important and potentially offsetting capital and expense

factors that would otherwise be included in base rate calculations. See id.; and I&E St. 3, pp. 15-16, & 21.

Additionally, Aqua's circumstances with relation to purchased water and energy expenses simply do not warrant the implementation of an automatic recovery mechanism, as the costs to Aqua for its purchases of water supplies do not constitute significant expenses that require adjustments between base rate cases. In fact, Aqua's purchased water and purchased energy expenses collectively constitute less than 5% of the Company's overall cost of service. See I&E St. 3, pp. 16 & 23; and OCA St. 4, p. 25. This percentage sharply contrasts with the other situations where the Commission has approved automatic recovery mechanisms for commodity purchase expenses under the Section 1307 statutory exception to single-issue ratemaking, such as with the Purchase Gas Cost ("PGC") mechanism for natural gas utilities where the costs of acquiring natural gas supply regularly constitutes 70% of O&M expenses. See I&E St. 3, pp. 15-16.

Accordingly, no reason exists to believe that the Company's regular base rate proceedings are or will be inadequate to reconcile these recurring and anticipated expenses. Moreover, Aqua has simply not demonstrated the need for this exception to the Commission's long-standing policy against single-issue ratemaking. Thus, the Commission should reject the proposed PWA and ECAM as inappropriate, impermissible, and unsubstantiated.

VI. RATE STRUCTURE **(Section IX of Standard Brief Outline)**

A. The Commission Should Modify the Revenue Allocation proposed by Aqua and Require a Proportional Scale Back in Case of an Overall Rate Increase that is Less than Aqua has Requested.

In this proceeding, Aqua has prepared and presented a Cost of Service Study ("COSS"), which the Company utilized to allocate the requested rate increase among the various ratepayer

classes. See generally Aqua Statement No. 5, Direct Testimony of Connie Heppenstall (hereinafter, "Aqua St. 5"). As detailed in the Direct Testimony of Aqua LUG witness Mr. Baudino, as well as OSBA witness Mr. Kalcic, Aqua's proposed revenue allocation fails to sufficiently move the customer classes towards cost of service. To achieve reasonable progression towards cost-based rates, the Commission should modify Aqua's proposed revenue allocation to reflect the adjustments proposed by Mr. Kalcic and supported by Mr. Baudino. Alternatively, the Commission should approve the adjustments proposed by Mr. Baudino.

One of the primary principles of ratemaking is that customers' rates should reflect the cost of service. Specifically, the Commonwealth Court and the Commission have repeatedly held that a utility's cost of providing service must be the guiding principle – or "polestar" – in utility ratemaking. See Lloyd v. Pa. Pub. Util. Comm'n, 904 A.2d 1010, 1020 (Pa. Commw. Ct. 2006; see also, e.g., Pa. Pub. Util. Comm'n v. Philadelphia Gas Works, Docket No. R-2008-2073938, 2009 WL 884424 *5 (Order entered Mar. 26, 2009) (upholding natural gas utility rates as consistent with Lloyd by reason of the rates being properly derived from a cost of service analysis and subject to cost of service review in future base rate case). The Commission has since applied the Court's directive in Lloyd by recognizing that, while other factors may be considered, cost of service should be the primary consideration for ratemaking purposes. See, e.g., Pa. Pub. Util. Comm'n v. PPL Elec. Utilities Corp., Docket No. R-00049255, 2007 WL 2198189 *7-10 (Order entered Jul. 25, 2007) (PUC order citing Lloyd in support of settlement of distribution rate increase based on cost of service principles). In circumstances where immediately moving a particular customer class to cost of service would produce an extremely disproportionate increase for a particular class of customers, then the rate-making principle of "gradualism" can be applied to move rates towards cost of service over a period of time. See

Barash v. Pa. Pub. Util. Comm'n, 101 Pa. Commw. 76, 515 A.2d 651 (1986). These are the relevant considerations to be applied in reviewing the revenue allocation proposals in this proceeding.

To examine the progress towards cost of service in this proceeding, Aqua LUG witness Mr. Baudino reviewed the Relative Rate of Return ("RROR") resulting from the Company's proposed revenue allocation. Mr. Baudino explains the principles underlying this analysis in the below excerpt from his Direct Testimony:³

The relative rate of return ("RROR") shows how close a customer class rate of return is to the system average rate of return. For example, if a customer class rate of return is 5.5% and the system average rate of return is 6.5%, then that class RROR is 0.85 (5.5% divided 6.5%). Because the 0.85 RROR is below 1.0, the class is earning less than the system average rate of return. A class RROR of 1.0 indicates that the class return is the same as the system average rate of return. A class RROR greater than 1.0 indicates that the class RROR is greater than the system average rate of return.

Based on these principles, Mr. Baudino examined the customer class RROR from Aqua's 2018 rate case as well as the current and proposed RROR from the 2021 rate filing. The results of this analysis are shown below:⁴

³ Aqua LUG Statement No. 1 – Direct Testimony of Richard Baudino ("Aqua LUG St. 1"), at 3.

⁴ *Id.* at 4.

	(1)	(2)	(3)
	2018	Current	AP
	<u>Case</u>	<u>Case</u>	<u>Proposed</u>
			<u>RROR</u>
Residential	0.95	0.96	0.96
Commercial	1.04	1.07	1.05
Industrial	0.84	0.93	1.00
Public	1.21	1.18	1.18
Other Water Utilities	5.12	15.77	14.74
Private Fire	1.76	1.25	1.27
Public Fire	0.98	0.97	1.00

The comparison of the RROR from Aqua's 2018 rate case to the current 2021 rate case shows the Company's proposed revenue allocation makes entirely inadequate progress towards cost of service for the Residential, Commercial and Public customer classes. As observed by Mr. Baudino:

The proposed RROR for the Residential class made no movement towards the system average increase in Ms. Heppenstall's proposed revenue allocation. The Commercial class RROR declined only slightly.

To achieve movement consistent with the directives from *Lloyd*, Mr. Baudino proposes that the Commission adopt the revenue allocation set forth in Exhibit__(RAB-2) to Aqua LUG St. 1. Adopting Mr. Baudino's adjustments to the Company's proposed revenue allocation would move most customer classes closer to cost of service in the manner set forth below:⁵

- Move the Residential class from a RROR of 0.96 to 0.98.

⁵ Aqua LUG St. 1, at 5.

- Move the Commercial class from a RROR of 1.07 to 1.02.
- Move the Industrial class from a RROR of 0.93 to 0.99.
- Move the Public class from a RROR of 1.18 to 1.15.

Mr. Baudino recognizes that adjustment of the revenue allocation will have an impact on the Company's proposed rate structure. In particular, Mr. Baudino recognizes that adjusting the customer class revenue allocations could impact revenues assigned to Industrial customer usage at blocks 5 and 6. Consistent with the principles of gradualism, Mr. Baudino recommends the Commission allocate any excess revenue requirement above the Industrial customer cost of service to the Residential customer class. Aqua LUG St. 1, at 6.

Importantly, OSBA witness Brian Kalcic also addressed Aqua's lack of movement towards cost of service. To illustrate the Company's lack of movement, Mr. Kalcic analyzed the interclass revenue subsidies for all customer classes, including the Private Fire and Other Water Utility customer classes. The results of Mr. Kalcic's adjustments to Aqua's revenue allocation are set forth in Schedule BK-4W to OSBA Statement No. 1, Direct Testimony of Brian Kalcic ("OSBA St. 1"). Mr. Kalcic's adjusted revenue allocation achieves additional movement towards cost of service for the Residential, Commercial, Public, Other Water Utility, and Private Fire customer classes in comparison to Mr. Baudino's analysis. *See* OSBA Statement No. 1-R, Rebuttal Testimony of Brian Kalcic ("OSBA St. 1-R") at 11-12. Accordingly, Mr. Baudino subsequently testified in support of Mr. Kalcic's recommendation. Aqua LUG Statement No. 1-S, Surrebuttal Testimony of Richard Baudino ("Aqua LUG St. 1S"), at 3.

In response, Aqua witness Connie Heppenstall acknowledges the reasonableness of the revenue allocation proposed by both Mr. Baudino and Mr. Kalcic. In response to Mr. Baudino's proposed revenue allocation, Ms. Heppenstall concludes "I have no philosophical problem with

Mr. Baudino's recommendation." Aqua Statement No. 5-R, Rebuttal Testimony of Connie Heppenstall ("Aqua St. 5-R"), at 25. In response to Mr. Kalcic's proposed revenue allocation, Ms. Heppenstall concurred that the recommendation is "reasonable". Aqua St. 5-R, at 5. Notwithstanding the acknowledged reasonableness of the Aqua LUG and OSBA proposals, Ms. Heppenstall continues to support Aqua's as-filed revenue allocation.

The evidence cited in support of Ms. Heppenstall's adherence to the as-filed revenue allocation is not compelling. In declining to adopt the revenue allocation of Mr. Baudino, Ms. Heppenstall claims it would result in a RROR for the Residential and Industrial class between 0.98 and 0.99. Aqua St. No. 5-R, at 25. It is not clear why this is viewed as an unreasonable outcome given that the RROR for the Residential and Industrial customer classes at current rates are 0.96 and 0.93 respectively. Aqua LUG St. No. 1, at 5. Similarly, Ms. Heppenstall declines to adopt Mr. Kalcic's revenue allocation on grounds that the Company's proposed revenue allocation reflects the Act 11 allocation of wastewater revenue to water customers. However, Mr. Kalcic presented the results of this proposed revenue allocation both with and without an Act 11 allocation. OSBA St. No. 1, at 19. Accordingly, Aqua has failed to provide a compelling basis adoption of its proposed revenue allocation over the alternative revenue allocations achieving more reasonable progress towards cost of service.

For the reasons set forth above, Aqua requests that the Commission deny the revenue allocation proposed by Aqua for failure to achieve sufficient movement towards costs of service and adopt the revenue allocation proposed in OSBA St. No. 1, Schedule BK-4W, and supported by Aqua LUG. Alternatively, and at minimum, Aqua LUG requests that the Commission deny Aqua's proposed revenue allocation for failure to achieve sufficient movement towards costs of service and adopt the revenue allocation proposed in Aqua LUG St. No. 1, Exhibit (RAB_2). To

the extent the Commission approves a revenue increase lower than the proposed revenue increase, the approved revenue allocation should be scaled back proportionately as set forth in Mr. Baudino's Direct Testimony. Aqua LUG St. 1, p. 6.

VII. CONCLUSION
(Section X of Standard Brief Format)

WHEREFORE, the Aqua Large Users Group respectfully requests that the Pennsylvania Public Utility Commission:

(a) grant Aqua the minimal rate increase necessary to ensure just and reasonable rates for the Company's ratepayers;

(b) deny Aqua's request to recover purchased water and energy costs through Purchased Water Energy Cost Adjustment Mechanisms; and,

(c) approve the revenue allocation proposed in OSBA Statement No. 1 or, at minimum, approve the revenue allocation proposed in Aqua LUG Statement No. 1.

Respectfully submitted,

McNEES WALLACE & NURICK LLC

By 

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Counsel to the Aqua Large Users Group

Dated: January 11, 2021

APPENDIX A

PROPOSED CONCLUSIONS OF LAW

1. Pursuant to the Pennsylvania Public Utility Code, "[e]very rate made, demanded, or received by any public utility ... shall be just and reasonable." 66 Pa. C.S. § 1301.
2. Single-issue ratemaking is prohibited if it "impacts on a matter that is normally considered in a base rate case." Pa. Indus. Energy Coalition v. Pa. Pub. Util. Comm'n., 653 A.2d 1336, 1350 (Pa. Commw. 1995).
3. Single-issue ratemaking is disfavored "based on the rate maker's obligation to consider all of a utility's revenues and costs in the balancing process to achieve just and reasonable rates." Pub. Util. Comm'n. v. Philadelphia Gas Works, Docket No. P-00042090, Order (July 8, 2004), p. 7.
4. A "review of expense items in isolation could result in confiscatory rates," in part by ignoring the fact that a utility "may have a sufficient over-collection in another matter to adequately compensate the company" for any undercollection it may experience in the review of the isolated matter. Pub. Util. Comm'n. v. Philadelphia Gas Works, Docket No. P-00042090, Order (July 8, 2004), p. 7.
5. A utility's cost of providing service must be the guiding principle – or "polestar" – in utility ratemaking. See Lloyd v. Pa. Pub. Util. Comm'n., 904 A.2d 1010, 1020 (Pa. Commw. Ct. 2006); see also, e.g., Pa. Pub. Util. Comm'n v. Philadelphia Gas Works, Docket No. R-2008-2073938, 2009 WL 884424 *5 (Order entered Mar. 26, 2009).
6. While other factors may be considered, cost of service should be the primary consideration for ratemaking purposes. See, e.g., Pa. Pub. Util. Comm'n v. PPL Elec. Utilities Corp., Docket No. R-00049255, 2007 WL 2198189 *7-10 (Order entered Jul. 25, 2007) (PUC order citing Lloyd in support of settlement of distribution rate increase based on cost of service principles).

APPENDIX B

PROPOSED ORDERING PARAGRAPHS

IT IS ORDERED:

1. Tariff Water-Pa. P.U.C. No. 3 and Tariff Sewer-Pa. P.U.C. No. 3 are approved as modified by this Order adopting expense, rate of return, revenue allocation and rate design adjustments proposed by various parties;
2. Aqua's proposals to recover purchased water and energy costs through Purchased Water and Energy Cost Adjustment Mechanisms are denied; and
3. The rates set forth in Tariff Water-Pa. P.U.C. No. 3 reflect the revenue allocation proposed in OSBA Statement No. 1; or, at minimum, the revenue allocation proposed in Aqua LUG Statement No. 1.