Post & Schell P.C.
ATTORNEYS AT LAW

17 North Second Street
12th Floor
Harrisburg, PA 17101-1601
717-731-1970 Main
717-731-1985 Main Fax
www.postschell.com

Michael W. Hassell

mhassell@postschell.com
717-612-6029 Direct
717-731-1985 Direct Fax
File #: 182321

February 28, 2022

VIA ELECTRONIC FILING

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor North
P.O. Box 3265
Harrisburg, PA 17105-3265

Re: PA Public Utility Commission v. Aqua Pennsylvania, et al.
Docket Nos. R-2021-3027385, et al.

Dear Secretary Chiavetta:

Attached are the Exceptions to the Recommended Decision of Aqua Pennsylvania, Inc. and Aqua Pennsylvania Wastewater, Inc. ("Aqua PA") in the above-referenced proceeding.

Copies will be provided as indicated on the Certificate of Service.

Respectfully submitted,

Michael W. Hassell

Michael W. Hassell

MWH/kls
Attachment

cc: Honorable Mary D. Long (*w/att.*)
Office of Special Assistants (*w/att.*)
Certificate of Service

CERTIFICATE OF SERVICE
(R-2021-3027385 and R-2021-3027386)

I hereby certify that a true and correct copy of the foregoing has been served upon the following persons, in the manner indicated, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), and the Prehearing Order dated October 19, 2021 (establishing the list of fully active parties in this proceeding).

VIA E-MAIL ONLY

Scott B. Granger, Esquire
Bureau of Investigation & Enforcement
Commonwealth Keystone Building
400 North Street, 2nd Floor West
Harrisburg, PA 17105-3265
sgranger@pa.gov

Christy M. Appleby, Esquire
Harrison W. Breitman, Esquire
Erin L. Gannon, Esquire
Lauren E. Guerra, Esquire
Mackenzie C. Battle, Esquire
Office of Consumer Advocate
555 Walnut Street
Forum Place, 5th Floor
Harrisburg, PA 17101-1923
cappleby@paoca.org
hbreitman@paoca.org
egannon@paoca.org
lguerra@paoca.org
mbattle@paoca.org

Steven C. Gray, Esquire
Office of Small Business Advocate
555 Walnut Street
Forum Place, 1st Floor
Harrisburg, PA 17101
sgray@pa.gov

John W. Sweet, Esquire
Ria M. Pereira, Esquire
Elizabeth R. Marx, Esquire
Lauren Berman, Esquire
Pennsylvania Utility Law Project
118 Locust Street
Harrisburg, PA 17101
PULP@pautilitylawproject.org

Adeolu A. Bakare, Esquire
Charis Mincavage, Esquire
McNees Wallace & Nurick LLC
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166
Abakare@mcneeslaw.com
Cmincavage@mcneeslaw.com
Counsel for Aqua Large Users Group

George A. Bibikos, Esquire
GA BIBIKOS LLC
5901 Jonestown Road, Suite 6330
Harrisburg, PA 17112
gbibikos@gabibikos.com

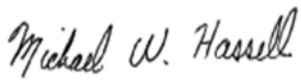
Robert Rosenthal
R.A. Rosenthal Inc.
524 Strathmore Dr.
Mechanicsburg, PA 17050
ask-rosey@comcast.net

Brian Kalcic
Excel Consulting
225 S. Meramec Avenue, Suite 720-T
St. Louis, MO 63105
excel.consulting@sbcglobal.net

Richard J. Gage
120 Treaty Drive
Wayne, PA 19087
brittagage@aol.com

Francine Weiner
1903 2nd Street
Langhorne, PA 19047
fhwhome@gmail.com

John Day
614 Runyon Avenue
Piscataway, NJ 08854
john@johnday.us



Date: February 28, 2022

Michael W. Hassell

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission, *et al.*	:	
	:	
v.	:	Docket Nos. R-2021-3027385, *et al*.
	:	
Aqua Pennsylvania, Inc.	:	
Pennsylvania Public Utility Commission, *et al.*	:	
	:	
v.	:	Docket Nos. R-2021-3027386, *et al*.
	:	
Aqua Pennsylvania Wastewater, Inc.	:	

EXCEPTIONS OF
AQUA PENNSYLVANIA, INC. AND AQUA PENNSYLVANIA WASTEWATER, INC.

Kimberly A. Joyce, Esq. (ID # 86605)
Mary McFall Hopper, Esq. (ID # 60118)
Alexander R. Stahl, Esq. (ID # 317012)
762 W. Lancaster Ave
Bryn Mawr, PA 19010
Phone: 610-645-1077
Phone: 610-645-1170
Phone: 610-645-1130
E-mail: kajoyce@essential.co
E-mail: mmhopper@aquaamerica.com
E-mail: astahl@aquaamerica.com

Michael W. Hassell, Esq. (ID # 34851)
Garrett P. Lent, Esq. (ID # 321566)
Post & Schell, P.C.
17 North Second Street, 12th Floor
Harrisburg, PA 17101
Phone: 717-731-1970
E-mail: mhassell@postschell.com
E-mail: glent@postschell.com

Dated: February 28, 2022

Counsel for Aqua Pennsylvania, Inc., and Aqua Pennsylvania Wastewater, Inc.

Table of Contents

Page

TABLE OF AUTHORITIES

Page

United States Supreme Court Decisions

Pennsylvania Appellate Court Decisions

Pennsylvania Administrative Agency Decisions

Pennsylvania Statutes

Pennsylvania Regulations

I. INTRODUCTION

Aqua Pennsylvania, Inc. and Aqua Pennsylvania Wastewater, Inc. (collectively, "Aqua PA," "AP" or the "Company") hereby file these Exceptions to the Recommended Decision dated February 18, 2022 (the "RD"), and issued by Administrative Law Judge Mary D. Long (the "ALJ"). Through this proceeding, Aqua PA requested that the Pennsylvania Public Utility Commission ("Commission") approval of 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"). The Company filed this combined water and wastewater case in accordance with the provisions of Section 1311(c) of the Public Utility Code. 66 Pa.C.S. § 1311(c). The requested increase is based upon a fully projected future test year ending March 31, 2023 ("FPFTY") and is designed to provide the Company with an opportunity to earn a 7.64% overall rate of return on rate base, including a 10.75% return on common equity, resulting in a claimed increase in water revenues of approximately $86.118 million or 16.9%, and a claimed increase in wastewater revenues of approximately $11.566 million or 31.2%.

In the RD, the ALJ recommends that the Commission grant Aqua PA a maximum water revenue increase of approximately $15.2 million and a maximum wastewater revenue increase of approximately $16.7 million, which produces only a 6.45% overall rate of return and an 8.90% return on common equity. However, the RD reaches these conclusions based upon several errors that Aqua PA submits should be carefully reviewed and adjusted by the Commission in order to reflect record evidence and controlling precedent. In each of these instances, the RD adopted adjustments proposed by the Commission's Bureau of Investigation and Enforcement ("I&E") and/or the Office of Consumer Advocate ("OCA"), which failed to follow controlling precedent and/or were based on clearly erroneous factual findings.

The page limit on these Exceptions, *see* 52 Pa. Code § 5.533(c), constrains Aqua PA's

ability to fully explain its positions. The Company requests that the Commission review its Main Brief ("MB") and Reply Brief ("RB") for further explanations of its positions as noted herein.

II. EXCEPTIONS

A. EXCEPTION NO. 1 – THE RD'S PROPOSED 8.9% RETURN ON COMMON EQUITY MUST BE SUBSTANTIALLY INCREASED OR IT WILL CALL INTO QUESTION THE COMMISSION'S COMMITMENT TO SUPPORTING INFRASTRUCTURE INVESTMENT. RD AT 77-81.

Aqua PA excepts to the RD's recommendation that the Commission adopt I&E's recommended return on common equity ("ROE") of 8.9%. If adopted, this ROE will represent a watershed moment for the end of the Commission's longstanding commitment to supporting infrastructure investment, made doubly worse in a period of rising capital costs. The RD ROE would signal to the utilities and the credit rating agencies that Pennsylvania regulation has ceased to support investment in the state at a time of critical capital investment needs.

The RD initially recognizes the need to employ informed judgment in determining the allowed ROE. RD at 77. However, the RD immediately foregoes undertaking a reasoned analysis of the various methodologies for determining the cost rate for common equity presented by the parties, the components inherent in each of those methodologies, and information regarding the current environment of rising capital costs that are not adequately addressed by the use of one single methodology to the exclusion of all others. Instead, the RD simply decides that the "method employed by I&E which results in an 8.9% ROE is the most reasonable." RD at 77.

This approach of selecting the middle number of three ROE recommendations does not reflect a reasoned analysis of the evidence of record. Moreover, in selecting I&E's recommended ROE, the RD is implicitly endorsing an approach that rejects the application of informed judgment. Rather, as explained in Aqua PA's RB, I&E's recommendation is based upon its rote, formulaic application of a single approach to determining ROE, *i.e.*, the Discounted Cash Flow ("DCF")

method. In so doing, I&E declares that ROE determinations have become "less controversial", and that the DCF "should be established by mathematical formulation." *See* AP MB at 45. Such an approach is contrary to prior Commission observations:

> A fair rate of return for a public utility, however, is not a matter which is to be determined by the application of a mathematical formula. It requires the exercise of informed judgment based upon an evaluation of the particular facts presented in each proceeding. There is no one precise answer to the question as to what constitutes the proper rate of return.

Pa. PUC v. Pennsylvania Power Co., 55 Pa. P.U.C. 552, 559 (1982) (emphasis added).

If adopted by the Commission, an ROE of 8.9% will signal to investors that the Commission is no longer supportive of infrastructure investment, which will drive up future capital costs for Pennsylvania utilities through corporate downgrades. These concerns were described in detail by Aqua PA's rate of return consultant, Mr. Moul:

> The investment community would be very concerned if the Commission were to adopt either of the positions of the I&E or OCA. If it were to do so, investors would see Pennsylvania regulation as less supportive of the Company at a time of high levels of capital investment. Over the next five years, AP expects capital expenditures to be nearly $1.5 billion. At present, Pennsylvania regulation is currently ranked Above Average/3 by Regulatory Research Associates ("RRA"), which reflects an upgrade that occurred on May 10, 2017. The rating system used by RRA includes three principal categories (*i.e.*, Above Average, Average and Below Average with more refined positions within the categories designated by the numbers 1, 2 and 3). If the Commission were to follow the proposals of I&E or the OCA, the regulatory ranking of Pennsylvania would certainly be jeopardized. The return on equity used by the Commission to set rates embodies in a single numerical value a clear signal of regulatory support for the financial strength of the utilities that it regulates. Although cost allocations, rate design issues, and regulatory policies relative to the cost of service are important considerations, the opportunity to achieve a reasonable return on equity represents a direct signal to the investment community of regulatory support (or lack thereof) for the utility's financial strength. In a single figure, the return on equity utilized to set rates provides a common and widely understood benchmark that can be compared from one company to another and

> is the basis by which returns on all financial assets (stocks – both utility and non-regulated, bonds, money market instruments, and so forth) can be measured. So, while varying degrees of sophistication are required to interpret the meaning of specific Commission policies on technical matters, the return on equity figure is universally understood and communicates to investors the types of returns that they can reasonably expect from an investment in utilities operating in Pennsylvania.

AP St. 7-R at 4-5. Critically, the ROE established in this case will be used for Distribution System Improvement Charge ("DSIC") purposes for Aqua PA for the two years following the Commission's Order. 66 Pa.C.S. § 1357(b). A deficient ROE here will not only harm the Company now but will also discourage future infrastructure investment not only for the Company, but the utility industry generally throughout Pennsylvania.

In order for Aqua PA, and other utilities, to continue to be able to raise the capital necessary to finance these investments, it is critical that the Commission demonstrate that Pennsylvania remains a constructive and supportive regulatory environment, through a fair rate of return. As the Commission observed in *Pa. PUC v. PPL Electric Utilities Corp.*, Docket No. R-2012-2290597, at p. 81 (Order entered Dec. 28, 2012) ("*PPL Electric 2012*"):

> Furthermore, we note that the setting of the proper return on equity is even more critical in this proceeding as our Pennsylvania jurisdictional utilities implement plans to accelerate the greatly needed replacement of aging infrastructure. Attracting capital to Pennsylvania at reasonable rates to accomplish this infrastructure replacement has never been more important to PPL, its customers and the Commonwealth of Pennsylvania.

As will be explained further below, there are a number of specific errors in the RD's recommendation of an 8.9% ROE. These include the RD's failure to correct inadequacies in the I&E DCF formula, failure to give recognition to a DCF leverage adjustment accepted by the Commission in prior proceedings where the unadjusted DCF calculation produces an inadequate result, failure to take into account clear and substantial rises in inflation that will increase capital

costs, failure to consider the higher Capital Asset Pricing Model ("CAPM") results and the results of other methodologies which demonstrated clear inadequacies in the I&E's DCF result, failure to consider the Commission's recent ROE determinations, including its DSIC determination, in establishing a fair return, and failure to recognize Aqua PA's superior management performance in the ROE allowance.

Aqua PA demonstrated that an ROE of 10.75%, inclusive of a management performance adder, was appropriate in this proceeding. *See* AP MB at 107-140; AP RB at 45-56. In particular, Aqua PA witness Mr. Moul demonstrated, using multiple methods of evaluating the cost of common equity, that the zone of reasonableness for Aqua PA ranged from 10.5% (using a risk premium analysis) to 13.40% (comparable earnings result). *See* AP St. 7 at 7. Mr. Moul's recommendation accounted for both the inherent infirmities associated with the various methodologies used by the parties in this proceeding and used informed judgment to reflect relevant aspects of the current financial climate, including conservative estimates of rising interest rates. *See* AP RB at 46-48 (discussing the necessity of using multiple methodologies and informed judgment); *see also PUC v. UGI Utilities, Inc. – Electric Division*, Docket No. R-2017-2640058, at pp. 104-105 (Order entered October 25, 2018) ("*UGI Electric*") (recognizing "sole reliance on one methodology without checking the validity of the results of that methodology with other cost of equity analyses does not always lend itself to responsible ratemaking" and concluding that "where evidence based on other cost of equity methods indicates that the DCF-only results may understate the utility's current cost of equity capital, we will consider those other methods, to some degree."). Based upon these facts, Aqua PA's recommended a 10.75% cost of common equity is reasonable and appropriate.

1. I&E's DCF Calculation Adopted By The RD Is Understated. RD at 77-78.

The initial components of a DCF calculation include a dividend yield and a growth rate.

AP St. 7 at 22. The RD undertakes no analysis of either of these components, but simply adopts the I&E recommendation. This failure results in an understated DCF.

I&E derived a dividend yield for its proxy group of 1.75%, using an average of spot stock price and a 52-week average. I&E St. 2 at 22. The result is less than Aqua PA witness Mr. Moul's dividend yield recommendation of 1.94%. AP St. 7 at 24. One reason for I&E's lower dividend yield is its selection of spot prices, which were near the 52-week high of stock prices for each of the barometer group companies. I&E Ex. No. 2, Sch. 4. Otherwise, the 52-week average dividend yield of 1.87% is quite close to Mr. Moul's six-month average dividend yield.

I&E relied upon five-year projected earnings growth rates for its proxy group, taken from four sources. I&E St. 2 at 23. I&E used an unadjusted average of all projected earnings growth rate data for its proxy group to produce a growth rate of 7.15%. I&E St. 2 at 23.

I&E's growth rate is unreasonable because it improperly includes an extremely low 3.6% growth rate for Middlesex Water. As explained in the Recommended Decision issued in Columbia Gas of Pennsylvania, Inc.'s 2020 rate case, I&E excluded a high data point from its growth rate calculation on the basis that it was outside the norm and distorted the results. *See Pa. PUC v. Columbia Gas of Pennsylvania, Inc.*, Docket Nos. R-2020-3018835, et al., at p. 133 (Recommended Decision dated Dec. 4, 2020). The Commission adopted the I&E DCF recommendation in its final order. *Pa. PUC v. Columbia Gas of Pennsylvania, Inc.*, Docket Nos. R-2020-3018835, et al., at p. 131 (Order entered Feb. 19, 2021) ("*Columbia 2020*"). If high-end growth rates can be excluded, as I&E has done in the past, then low-end growth must be also excluded from the DCF calculation. Here, the growth rate for Middlesex Water is 210 basis points lower than the next lowest growth rate included by I&E. I&E Exhibit 2, Sch. 5. If the RD had removed the unreasonably low 3.6% growth rate for Middlesex Water from the growth rate

calculation, the resulting growth rate would have been 7.74%. AP MB at 124.

The Commission should revise the RD, adopt Mr. Moul's dividend yield result, and correct the I&E growth rate as explained above. These corrections alone will increase the DCF to 9.68%.

2. The RD Erroneously Rejects Any Leverage Adjustment To The DCF Result. RD at 78-79.

The RD concludes that Aqua PA failed to justify the appropriateness of adding a leverage adjustment to the DCF result. The RD fails to consider that the Commission has included an adjustment for leverage in instances, like the present, where the DCF result understates the cost of common equity.

A leverage adjustment is designed to adjust the DCF cost rate for the different percentage of debt in the capital structure calculated at market values of equity and long-term debt (*i.e.*, the values used by investors in the DCF analysis) as compared to the percentage of debt in the capital structure at book value (*i.e.*, the values used in the ratemaking process). AP St. 7 at 26-27. For example, a utility that has a stock price above its book value and has an embedded cost of debt different from the marginal cost of debt, has a market value or capitalization of its equity that is greater than the book value of its equity. When an investor purchases that equity at the market price (*i.e.*, the price used in the DCF model), the percentage of equity in the market capitalization is greater than the percentage of equity at book value. Under such circumstances, the DCF cost rate based on market prices should be adjusted upward to reflect the greater financial risk associated with a higher debt ratio when that cost rate is applied to a book value capitalization in utility proceedings. *Id.*; AP St. 7-R at 23-25.

The Commission has been selective in its adoption of a leverage adjustment to the DCF.

A leverage adjustment has been adopted in a number of prior cases.[1] However, in other cases, the Commission has rejected the addition of a leverage adjustment.[2]

What is most apparent from the decisions that have not adopted a leverage adjustment is that the Commission has concluded the unadjusted DCF results in those cases do not understate the cost of common equity. For example, in *Aqua 2008* the Commission explained:

> In the cases cited by Aqua in support of its leverage adjustment, it is obvious that the DCF results in those cases were not as high as the unadjusted DCF result we have in this proceeding, since the final cost of equity in those cases was no higher than 10.6% with the leverage adjustment. The unadjusted DCF results presented by the Parties in this case are generally higher than the DCF recommendations from the earlier cases cited by Aqua. When viewed in the context of the other methodologies, we conclude that there is no need to have an upwards adjustment to compensate for any perceived risk related to Aqua's market-to-book ratio. Accordingly, we reject the ALJ's recommendation to allow a 65-basis point leverage adjustment.

Aqua 2008, at *46-47. Importantly, while the Commission declined to adopt Aqua PA's proposed leverage adjustment, it ultimately approved an 11.0% cost of common equity, which was also inclusive of a 22-basis point adjustment for managerial performance. *Aqua 2008*, at *68-69.

Here, there is substantial evidence demonstrating that the unadjusted DCF results understate the cost of common equity in the current economic environment. *See* Sections II.A.3-5 *infra*. For these reasons, and those explained in Aqua PA's briefs, the Commission should conclude that an adjustment to the DCF results is needed. AP MB at 112-117; AP RB at 50-51.

---

[1] *See, e.g., Popowsky v. Pa. PUC*, 868 A.2d 606, 612-13 (Pa. Cmwlth. 2004) ("*PA American*"); *Pa. PUC v. Pa. American Water Co.*, Docket No. R-0001639 (Order dated Jan. 10, 2012) (approving 60 basis point adjustment); *Pa. PUC v. PPL Gas Utilities Corp.*, Docket No. R-00061398, 2007 Pa. PUC LEXIS 2 (Order entered Feb. 8, 2007) (approving 70 basis point adjustment); *Aqua 2004 Order*, at *85-87 (adopting 60 basis point adjustment); *Pa. PUC v. PPL Electric Utilities Corp.*, Docket No. R-00049255 (Order dated Dec. 6, 2004) (approving 45 basis point adjustment).

[2] *See Columbia 2020*, at p. 131; *UGI Electric*, at p. 93; *PPL Electric 2012*, at p. 91; *Pa. PUC v. City of Lancaster Bureau of Water*, Docket Nos. R-2010-2179103, et al., at p. 79 (Order dated July 14, 2011) ("*City of Lancaster 2011*"); *Pa. PUC v. Aqua Pa., Inc.*, Docket No. R-00072711, 2008 Pa. PUC LEXIS 50, at *46-47 (Order dated July 17, 2008) ("*Aqua 2008*").

3. The RD Fails To Take Into Account The Effects Of Rising Inflation On Capital Costs.

The RD completely fails to address the substantial increases to the rate of inflation that have been experienced subsequent to the preparation of rate of return recommendations by the parties. As Aqua PA witness Mr. Moul testified in rejoinder testimony, the inflation rate reported in December was 6.8%, a 39-year high. AP St. 7-RJ at 5. That inflation shows no signs of abating. Further, the Federal Open Market Committee ("FOMC") has made clear that it is ending its policies designed to maintain low interest rates. As Mr. Moul explained:

> A forward-looking assessment of the capital markets is especially relevant here because the Company's rates will be based on a fully projected future test year ("FPFTY"). Higher inflation expectations are a contributing factor that points to higher interest rates. Indeed, higher inflation today is revealed by a 5.9% increase in social security payments announced on October 13, 2021, the largest one-year increase in nearly four decades. FOMC has signaled that it plans to taper its bond buying program (i.e., quantitative easing) in November 2021 and to end it completely by mid-2022. The Fed Funds rate is also likely to increase from very low levels that existed during the pandemic. Higher interest rates clearly point to higher capital costs prospectively.

AP St. 7-R at 6. Increasing inflation will continue to increase interest rates and capital costs:

> As a preliminary matter, interest rates, and indeed all capital cost rates, are influenced by investor expectations associated with inflation. It has been reported recently that inflation has reached a 39-year high of 6.8%. A rate not seen since 1982. Future capital costs will be influenced by this fact and, hence, interest rate forecasts must be considered.

AP St. 7-RJ at 5. Thus, capital cost rates in the FPFTY will be higher than earlier data may have indicated.

It is important to recognize that the DCF formula does not directly measure changes in interest rates. Moreover, the DCF components presented in this case—dividend yield and growth rate—reflect data compiled before the recent substantial rises in inflation and, therefore, the DCF

results are understated and fail to capture the current cost of equity. For this reason, the Commission should adjust the ROE recommendation to include a leverage adjustment and/or explicitly recognize the results from other measures of the cost of common equity.

4. The RD Fails To Properly Consider The Results Of Methodologies Other Than The DCF To Establish A Reasonable ROE. RD at 79.

As explained previously, the RD adopts the I&E's proposed DCF of 8.9%. The RD asserts that I&E used the DCF method and the CAPM method to arrive at its recommended ROE of 8.9%. RD at 78. However, this is inaccurate. Although I&E did prepare a CAPM analysis, in reality, I&E ignored its 9.89% CAPM result in deriving its recommendation. AP MB at 121.

Aqua PA recognizes that the Commission has long considered the results of DCF analyses as important inputs into determining ROE. However, the Commission also recognizes the importance of informed judgment and the information provided by other models. For example, the Commission expressed its position on the sole use of DCF results in *PPL Electric 2012*:

> In this case, we will rely upon the DCF methodology and informed judgment in arriving at our determination of the proper cost of common equity. In particular, we note that the evidence presented in this case based on the CAPM and RP methods produced a range of results that was consistently higher than the results produced by a DCF-only approach. This suggests that, while properly computed in the abstract, the DCF-only results understate the current cost of equity for PPL and that consideration should be given to the CAPM and RP evidence in determining the appropriate range of reasonableness.

PPL Electric 2012, at p. 81; *see also UGI Electric*, at pp. 104-105.

The use of informed judgment to temper the reliance on DCF results is necessary to ensure the utility has the opportunity to earn a reasonable return on its investment, consistent with long-standing ratemaking standards. *See, e.g., Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944); *Bluefield Waterworks and Imp. Co. v. P.S.C. of West Virginia*, 262 U.S. 679, 690 (1923).

The RD ignores the many flaws associated with the DCF method. Mr. Moul explained:

> While the results of a DCF analysis should certainly be given weight, the use of more than one method provides a superior foundation for the cost of equity determination. Since all cost of equity methods contain certain unrealistic and overly restrictive assumptions, the use of more than one method will capture the multiplicity of factors that 26 motivate investors to commit capital to an enterprise (i.e., current income, capital appreciation, preservation of capital, level of risk bearing). The simplified DCF model makes the assumption that there is a single constant growth rate, there is a constant dividend payout ratio, that price – earnings multiples do not change, and that the price of stock, earnings per share, dividends per share and book value per share all have the same growth rate. We know from experience that those assumptions are not realistic, because the stock market reveals performance that is very different from the assumptions of the DCF.[3] The use of multiple methods provides a more comprehensive and reliable basis to establish a reasonable equity return for AP.

AP St 7-R at 10-11. As explained above, one of the flaws of the DCF in a rising interest rate environment is that it lags in taking into account interest rate changes.

In contrast, other methods, particularly the CAPM and the Risk Premium ("RP") method, are important to consider in a time of rising interest rates because both methods directly reflect forecasts of interest rates and bond yields. As Mr. Moul observed:

> [The RP] is particularly useful when investors expect changes in the cost of debt prospectively, which is currently the expectation of investors, as I have explained above and in AP St. No. 7, pages 35-39. Indeed, the Risk Premium approach provides for direct reflection of prospective interest rates in the model and therefore should be given weight in determining the equity cost rate in this case.

AP St. 7-R at 23-24.

As was the case in *PPL Electric 2012*, the CAPM and RP produce results that are higher

[3] The growth rate variables shown on Schedules 8 and 9 of AP Exhibit 4-A show that the assumption associated with the simplified DCF model are not reasonable.

than a DCF-only approach. I&E's CAPM approach, while understated,[4] produces an ROE of 9.89%. Aqua PA's CAPM result is 13.4%, inclusive of a 1.02% size adjustment, and 12.38% exclusive of the size adjustment. AP St. 7 at 43. Aqua PA's RP result is 10.5%, reflecting a conservative interest rate for A-rated public utility bonds of 3.75%. AP St. 7 at 39.

The RD's sole reliance upon I&E's DCF result should be rejected. The Commission should specifically consider and reflect in its ROE determination the results of other methods more attuned to rising interest rates.

5. The RD Fails To Reconcile Its Recommendation To The Commission's Recent Determinations On ROE.

The determination of proper ROE should not be made in a vacuum. Regulatory consistency requires that the Commission not adopt widely divergent results when faced with contemporaneous data.

In this case, the RD's recommendation of an 8.9% ROE is well outside the norm of recent Commission determinations. For example, in the past year, the Commission granted a 9.86% ROE for Columbia Gas, and a 10.24% for the Gas Division of PECO Energy. AP MB at 97. These returns were granted in a period of substantially lower inflation and interest rates than are now being experienced. It is not rational to believe that the cost rate for common equity has dropped 100 basis points or more since those cases were decided.

Also instructive is the Commission's recent determination of the ROE to be applied for water utilities' DSICs. At its Public Meeting of January 13, 2022, at Docket No. M-2021-3030045, the Commission issued its most recent Quarterly Earnings Report. In that report, the Commission determined that the allowed DSIC ROE for water utilities would be 9.80%. That determination

[4] As explained in AP MB at 125-26, one of the flaws of I&E's CAPM is it fails to give appropriate weight to projected, increasing, Treasury yields. A 1.98% risk-free rate, in the current inflationary environment, is inadequate. Correcting for various errors in the I&E CAPM produces an ROE of 11.11%, inclusive of a 1.02% size adjustment.

was based upon data derived as of December 2021, which is a period comparable to that considered in this proceeding.

Importantly, the Commission's calculations reflected a barometer group DCF calculation of 8.49%. The Commission also provided a CAPM calculation of 9.85%. Thus, for DSIC purposes, it is clear that the Commission considers the DCF result to be understated, and "has been guided by the results of other models and other factors aside from DCF when setting the DSIC return." AP St. 7-R at 11.[5]

The allowed DSIC provides an important guide to the ROE that should be set in contemporaneous base rate proceedings. DSIC recoveries are reconciled, and therefore the 9.80% ROE is guaranteed. In contrast, in a base rate case, the ROE is only an opportunity rate and therefore should be greater than the ROE for DSIC purposes. AP St. 7-R at 5.

The allowed DSIC return rate is further evidence that the 8.90% ROE recommended in the RD is seriously deficient and will not provide Aqua PA with the opportunity to earn its investor-required cost of capital for the FPFTY. The Commission should not be reducing ROE when there is a continuing, compelling need for capital investment to rehabilitate aging infrastructure.

6. The RD Inappropriately Disregards The Requirements Of Section 523 Of The Public Utility Code. RD at 79-81.

The RD errs in failing to consider Aqua PA's effective management in setting an ROE.[6] The failure to give recognition to Aqua PA's effective management is contrary to the provisions of Section 523 of the Public Utility Code, which provides in relevant part:

> The commission shall consider, in addition to all other relevant evidence of record, the efficiency, effectiveness and adequacy of service of each utility when determining just and reasonable rates

[5] Aqua PA notes that, as shown on page 28 of the Quarterly Earnings Report, the gap between the calculated DCF result and the CAPM has been growing over the past year. This provides a further demonstration that the CAPM is showing that DCF results are understated.

[6] Evidence of Aqua PA's effective management performance is detailed at pages 129-140 of AP MB.

> under this title. On the basis of the commission's consideration of such evidence, it shall give effect to this section by making such adjustments to specific components of the utility's claimed cost of service as it may determine to be proper and appropriate.

66 Pa.C.S. § 523(a) (emphasis added).[7]

The RD acknowledges that the Company "has been a strong partner with the Commission in acquiring troubled water systems." RD at 79. Taking on systems like North Heidelberg, Belle Aire Acres, and others is a significant undertaking that requires management resources for systems that will never be viable (financially or service reliability) on their own. However, the RD then proceeds to discount the Company's efforts by asserting that the Company also has acquired systems that were not troubled and has asked existing customers to pay for those acquisitions. RD at 79-80. However, the two items are unrelated. Aqua PA includes in rate base only those amounts permitted by law. Incentives to encourage acquisitions and regionalization to reduce the number of troubled water systems in the Commonwealth should not be denied simply because the Company also undertakes acquisitions of some entities that may not be classified as "troubled."

The RD also asserts that providing additional basis points for effective management may offset cost savings, that would "defeat the purpose of cutting expenses to benefit ratepayers." RD at 80. However, such contention ignores the statutory directive of Section 523, quoted above, and the Commission's own Policy Statement to encourage use of rate of return premiums to encourage the acquisition of troubled water systems. The Commission has previously rejected contentions that utilities should not be provided additional basis points for quality utility service, and should similarly reject such contentions here. *See, e.g.*, *UGI Electric*, at p. 119; *PPL Electric 2012*, at pp. 98-99; *Aqua 2008*, at *63; *Pa. PUC v. West Penn Power Co.*, Docket Nos. R-00942986, et al.,

[7] *See also* the Commission's Policy Statement for incentives to acquire small, troubled water system at 52 Pa. Code § 69.711, which provides: "The rate of return premium as an acquisition incentive may be the most straightforward and its use is encouraged."

1994 Pa. PUC LEXIS 144, *147 (Order dated Dec. 29, 1994).

7. Conclusion As To The Cost Of Common Equity.

As explained above, the RD errs by recommending an ROE of 8.9%. This result is contrary to the weight of the evidence, as briefed by Aqua PA. *See* AP MB at 107-140; AP RB at 45-56. In the face of rising capital costs, this recommendation, if adopted, would provide a chilling effect upon investors in Pennsylvania utilities. The Commission should substantially revise the RD's recommendation to recognize the Company's proposed 10.75% ROE.

B. EXCEPTION NO. 2 – THE RD ERRS BY DISALLOWING AP'S WATER RATE BASE CLAIM RELATED TO THE ACQUISITION OF THE BOROUGH OF PHOENIXVILLE WATER SYSTEM. RD AT 44.

The RD concludes that the Commission should disallow $2,437,305 from Aqua PA's rate base, related to the Company's proposed positive acquisition adjustment for the Borough of Phoenixville ("Phoenixville") water system. RD at 44.[8] The proposed positive acquisition adjustment reflects the fact that the Company paid more than depreciated original cost ("DOC") for the asset. RD at 39. As such, the Company has requested a return on and return of the purchase price in this proceeding consistent with Section 1327 of the Public Utility Code, 66 Pa.C.S. § 1327, which is reflected in the positive acquisition adjustment as of the end of the FPFTY of $2,315,440 set forth in AP Exhibit 1-A, Schedule G-3. AP MB at 19.

The RD reasons that "I&E and OCA successfully rebutted the presumption of the reasonableness of the excess paid for the Phoenixville system." RD at 43. The RD further explains

[8] The acquisition of the subject water system assets was approved by the Commission in *Joint Application of Aqua Pennsylvania, Inc. and the Borough of Phoenixville for approval of 1) the acquisition by Aqua of the water system assets of Phoenixville used in connection with the water service provided by Phoenixville in East Pikeland and Schuylkill Townships, Chester County, and Upper Provide Township, Montgomery County, PA; 2) the right of Aqua to begin to supply water service to the public in portions of East Pikeland Township, Chester County, and Upper Provide Township, Montgomery County, PA; and 3) the abandonment of Phoenixville of public water service in East Pikeland Township, Chester County, and Upper Provide Township, Montgomery County, and certain locations in Schuylkill Township, Chester County, PA*, Docket Nos. A-2018-2642837, A-2018-3642839, et al. (Recommendation Decision dated Sept. 13, 2019), *adopted as final* (Order entered Oct. 24, 2019) ("*Aqua-Phoenixville Order*").

that: (a) there is no evidence that Phoenixville was failing to render reasonable and adequate service to its extraterritorial customers at the time of the acquisition; (b) Aqua PA completed a thorough analysis of the system prior to making and offer and closing; (c) the problems identified by Aqua PA constitute "ongoing maintenance and investment"; and (d) the unaccounted for water ("UFW") level identified by the Company was not indicative of a failure of facilities. RD at 43.

Aqua PA's proposed positive acquisition adjustment should be approved, and the Commission should reverse the RD. As an initial matter, Aqua PA notes that the RD fails to analyze, or even acknowledge, the Commission's prior findings that (a) recognized Phoenixville's inside-the-borough customers were subsidizing the service provided to outside-the-borough customers, and the defense of a base rate filing had deterred it from seeking rate relief to invest in its system,[9] (b) the Commission had previously ***directed*** Phoenixville to avail itself of an acquisition to alleviate these burdens,[10] and (c) Aqua PA's acquisition of the system is consistent with the regulatory requirement established in the *Phoenixville Petition Order*.[11] The RD ignores the regulatory requirements imposed by the Commission which prompted the acquisition.

The RD is also incorrect that there is no evidence that Phoenixville was failing to render reasonable and adequate service at the time of this acquisition. As explained by Aqua PA, the provider was manually reading meters, the system experienced high levels (*i.e.*, 68%) of non-revenue or unaccounted for water ("UFW"), and 30% of the system fire hydrants required repair or replacement at the time of the acquisition. AP MB at 24-25. While the RD attempts to sidestep

[9] AP MB at 21 (quoting *Petition of the Borough of Phoenixville for a Declaratory Order that the Provision of Water and Wastewater Service to Isolated Customers in Adjoining Townships Does Not Constitute the Provision of Public Utility Service Under 66 Pa. C.S. § 102*, Docket No. P-2013-2389321, at 3-4 (Opinion and Order entered May 19, 2015) ("*Phoenixville Petition Order*")).

[10] AP MB at 21-22 (quoting *Phoenixville Petition Order* at 7-8).

[11] AP MB at 21-22, 25-26. The Commission also previously concluded as a matter of law that, through the *Phoenixville Petition Order*, the Commission had "encouraged the Borough to pursue a sale of its water system assets." *Aqua-Phoenixville Order* at 19, Conclusion of Law ¶ 14.

these facts by arguing that these matters reflect ongoing maintenance and investment requirements, and that high levels of UFW were not indicative of system failure, it does so by divorcing the existence of these conditions from the reasons why Phoenixville was unable to address them during its ownership. Phoenixville did not address these issues because, as the Commission noted in the *Phoenixville Petition Order*:

> In past years, the disproportionate cost of rate filings compared to the minimal revenues recovered from the Borough's small extraterritorial customer base has deterred the Borough from seeking rate relief and created cost subsidies flowing from inside-borough customers to outside-borough customers.

Phoenixville Petition Order at 3 (quoting the petition) (emphasis added); AP MB at 29-30.

The RD's conclusion that Aqua PA completed a thorough analysis of the system prior to making an offer and closing on the acquisition similarly misses the point. Aqua PA addressed this very argument, raised by I&E, in its Reply Brief as follows:

> First, the fact that poor conditions are known or knowable at the time of the acquisition is not the test; and if it was, it would completely undermine the purpose of Section 1327. Second, the assertion that the conditions were "known or knowable" actually supports the fact that the system was troubled at the time it was acquired, and that Aqua PA has satisfied the requirements of Section 1327(a)(3), which is to encourage acquisition of troubled systems.

AP RB at 13. If it were the case that a public utility's showing under Section 1327 could be rebutted by the claim that the poor conditions of the system were "known or knowable" at the time of the acquisition, or that the public utility conducted a thorough investigation of the system prior to acquiring it, Section 1327 would be a legal nullity.[12] Indeed, it would be impossible to identify a troubled system for acquisition consistent with Section 1327 and Commission policy, because

[12] Pennsylvania statutes are to be construed presuming "[t]hat the General Assembly does not intend a result that is absurd, impossible of execution or unreasonable" and "[t]hat the General Assembly intends the entire statute to be effective and certain." 1 Pa.C.S. § 1922(1)-(2). The interpretation of Section 1327 advanced by the RD violates both of these rules of construction.

the identification of the poor conditions that would satisfy Section 1327 would also render it ineligible for the rebuttable presumption established by this section.

Finally, the RD ignores that the Commission's policy encourages regionalization and the acquisition of smaller troubled systems by larger capable public utilities. *See* 52 Pa. Code § 69.711. Aqua PA presented credible testimony that "[t]he Phoenixville acquisition was a prime candidate for using this policy," AP St. 2-R at 8, and that the Commission's policy encourages regionalization and the acquisition of smaller troubled systems by larger capable public utilities is served. AP MB at 30; *see also* AP RB at 13.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should reject the RD's disallowance of the positive acquisition adjustment claimed for Phoenixville, and permit Aqua PA to recover the $2,437,305 that is the excess of DOC associated with this system. AP MB at 19-31; AP RB at 10-14.

C. EXCEPTION NO. 3 – THE RD ERRS BY DIRECTING AP TO CANCEL THE CONTRACTS BETWEEN AP AND CERTAIN RIDER DRS CUSTOMERS, AND CHARGE THOSE CUSTOMERS FULL TARIFFED RATES. RD AT 49, 50.

The RD directs the Company to cancel certain contracts negotiated in good faith, in some cases, many years ago. This action could likely negatively impact current Aqua PA customers, create unnecessary litigation, and force local governments to build unnecessary infrastructure they had relied upon not having to build at certain point in time. As explained in Aqua PA's Main Brief, "Rider DRS – Demand Based Resale Service" permits Aqua PA to enter into customer-specific contracts at prices designed to maintain sales that would otherwise be lost to water service alternatives, for customers that can satisfy the requirements of this rider. AP MB at 38-40. Focused on the requirement that such customers must have a "competitive alternative," I&E recommended that contracts between Aqua PA and the Borough of Sharpsville ("Sharpsville"),

Schwenksville Borough Authority ("Schwenksville"), Chemung County Industrial Development Authority ("Chemung"), Horsham Water and Sewer Authority ("Horsham"), and New Wilmington Municipal Authority ("New Wilmington") (I&E St. 4-SR at 18) be cancelled. AP MB at 40. I&E also proposed that, until the contract with Aqua Ohio's Masury Division ("Masury") is approved, Masury should be billed at full tariff rates. AP MB at 40.

The RD adopts I&E's recommendations with respect Chemung, Horsham, New Wilmington and Sharpsville, and recommends that the Commission cancel these contracts and require these customers to pay full tariff rates. RD at 48-49. The RD similarly concludes that the application of discounted rates for Masury is "premature." RD at 49-50.

Each of these recommendations is in error and should be reversed by the Commission. Critically, the RD ignores the specific language of Rider DRS, which provides that:

> The Company shall require documentation to establish, to the Company's satisfaction, the existence of a competitive alternative. Such documentation may include, but is not limited to, an affidavit of the customer or, if the customer is a corporation, an affidavit of one or more of its officers.

Tariff Water No. 3, Original Page 20 (emphasis added). Aqua PA is required to adhere to its tariff.[13] 66 Pa.C.S. § 1303. By concluding that "[i]t is not reasonable for Aqua to be satisfied" by information satisfies the unambiguous language of its tariff, and that "[i]t should not be burdensome for a customer" to provide additional information, the RD undermines Aqua PA's ability to adhere to its tariff as it is obligated to do under the Public Utility Code.

Moreover, the RD disregards the basis upon which the parties entered into these contracts and undermines the benefits these contracts provide to other customers. AP MB at 41-42. By adopting I&E's recommendations, the RD supports I&E second guessing of documentation,

[13] Importantly, I&E, nor any other party, has asserted that the language of Rider DRS is unjust and unreasonable or provided any evidence in support of this position.

contracts and decisions made by entities in the past. The RD errs by ignoring the realities of these long-term contracts and seeks to analyze them in a vacuum, divorced from the specific facts and circumstances that existed at the time the contracts were entered into. AP MB at 41. As a result, the RD fundamentally alters the good faith, arms-length negotiations of the parties when they entered into these contracts over a decade ago, AP MB at 42, and ultimately eliminates approximately $974,405 in benefits to other existing Aqua PA customers. AP MB at 38-39 (sum of the benefits of the contracts associated with the applicable entities).

The recommendations specific to each of the contracts with Chemung, Horsham, Sharpsville, New Wilmington, and Masury are discussed further below.

1. The RD Errs By Concluding The Rider DRS Contracts With Chemung, Horsham, and New Wilmington Are Not Adequately Supported.

The RD's recommends that the Rider DRS contracts with Chemung, Horsham and New Wilmington should be cancelled. It concludes that the documentation provided by Chemung and Horsham is only "a self-serving statement that competitive alternatives exist" and that "[i]t is not reasonable for Aqua to be satisfied by so little information." RD at 48. The RD further concludes that the contract with New Wilmington does not comply with Rider DRS and recommends this municipality should be subject to full tariff rates. RD at 48.

Contrary to the RD's conclusion, the statement in the Chemung contract is not "self-serving." Rather, it is a legally binding representation by this municipality, that forms the basis for the contract itself. AP MB at 47. Effectively, the RD appears to insinuate that the representations of a municipal entity that binds itself to a long-term contract based upon those representations is not to be trusted. There is no support for such a finding in the record.

Similarly, Aqua PA demonstrated that Horsham has existing interconnections with the Company and another water provider, as well as wells located throughout its own system. AP MB

at 48. The RD ignores these alternative supplies, and further disregards the undisputed fact that Horsham could supply 100% of its water through sources other than the Company. AP MB at 48.

Aqua PA also demonstrated that the wheeling agreement with New Wilmington provides important benefits, including enabling Aqua PA to provide service to a noncontiguous area of its service territory at low cost. AP MB at 48-49. As such, it is reasonable for the Company to conclude that such a wheeling agreement does not require a competitive alternative.

2. The RD Errs By Retroactively Concluding That The Alternative Identified And Considered By The Borough of Sharpsville At The Time It Entered Into Its Contract Is Not Viable.

Regarding Sharpsville, the RD concludes that "the only competitive alternative identified in the documentation supporting the discounted sale rate was the potential construction of an expensive new water treatment plant. There is no evidence that this alternative is financially viable or that Sharpsville could purchase water from other sources." RD at 48-49. This reasoning completely ignores further representations in the agreement—*i.e.*, representations made at the time the contract was entered into regarding the then-existing source of supply. AP MB at 44-45 (citing HIGHLY CONFIDENTIAL I&E Exhibit No. 4 at 154). This evidence conclusively demonstrates that Sharpsville was not only contemplating a new alternative to obtaining water service from Aqua PA, but also had an existing alternative at the time it entered into the contract. *See* AP MB at 44-45. Moreover, Sharpsville subsequently provided an affidavit that satisfies Rider DRS. AP MB at 45-46. The Commission should not cancel a long-term DRS contract mid-term where the alternative does not now exist precisely because of the DRS contract. Sharpsville has provided documentation required by Aqua PA's tariff, and Aqua PA is obligated to adhere to its tariff.

3. The RD's Recommendation Regarding The Contract Between Aqua PA And Aqua Ohio's Masury Division Misunderstands The Facts.

Finally, the RD recommends that a determination on the rates paid by Masury is

"premature." RD at 49-50. It reasons that the agreement between Aqua PA and Masury was filed as an affiliated interest agreement on November 30, 2021, and that no determination has yet been made on this agreement. RD at 50. The RD disregards the fact that Aqua PA currently provides water to Aqua Ohio's Masury Division under a special tariff rate.[14] Moreover, this specific agreement contains a competitive alternative analysis, as well as a sworn affidavit from Masury that it would select the alternative in the absence of the new contract. AP MB at 49-50. If it is to be concluded that the Masury contract is not approved, then, rather than impute over $1 Million in additional revenues from Masury as proposed by the RD, the Commission should remove $258,000 in revenues that will not be received from Masury. AP MB at 50.

D. EXCEPTION NO. 4 – THE RD ERRS BY INCREASING THE COMPANY'S SPECIAL CONTRACT REVENUE ASSOCIATED WITH CERTAIN NEGOTIATED WATER RATE CONTRACTS TO REFLECT ESCALATION RATES CALCULATED BY THE OCA. RD AT 53.

The RD erroneously adopts the OCA's proposed adjustment to increase water revenues associated with certain special contract revenues, based upon the use of a different escalation factor for these contracts. RD at 53-54. The RD attempts to justify this recommendation by explaining that revenues tied to a contractual escalation factor "should be increased based upon a reasonable estimate of the amount of that escalation factor." RD at 54. It goes on to adopt an escalation factor prepared by the OCA which reflects the average of the forecasted inflation rates used by the Consumer Price Index, Office of Management and Budget, and Federal Reserve for 2021, 2022 and 2023. RD at 54. In addition, the RD accepted the OCA's "higher inflation for 2021 through a November 2021 government publication containing information up to October 2021 from the Bureau of Labor Statistics." RD at 54.

[14] *See* Tariff Water – Pa. P.U.C. No. 2, Third Revised Page 12.4.

This recommendation is flawed and should be rejected. Importantly, each of the contracts that would be subject to this adjustment contain an escalation provision as a part of their terms. AP MB at 51. These provisions further specify how the rate of inflation is to be calculated for determining the annual escalation of each contract. AP MB at 51. OCA's recommendation, adopted by the RD, effectively substitutes a different escalation rate into each contract than the one that was agreed to by the parties. This is unreasonable and inappropriate.

Moreover, the Company demonstrated the inflation rates calculated by OCA were overstated. AP MB at 52-53. Indeed, OCA includes inflation rates for 2023 which disregards that "this rate case is based upon a FPFTY ending March 31, 2023, and 2023 inflation rates will not affect most of the contract rates." AP MB at 52. The RD simply repeats this mistake, and calculates an adjustment based upon inflation rates that will not affect the Company's revenues during the FPFTY.

Aqua PA further submits that, to the extent that the Commission determines that OCA's adjustment is appropriate due to OCA's use of more current inflation rates, the Commission should consider such inflation rates with respect to the Company's proposed General Price Level Adjustment. *See* Section II.G. *infra*. As explained in the exception on this issue below, existing macroeconomic conditions demonstrate that increases in inflation are subjecting the Company to increased expenses. While the RD asserts that the revenues the Company obtains under its negotiated water rate contracts must be increased to reflect inflation, it disregards the effects of inflation on other aspects of the Company's revenue requirement that would necessitate a higher revenue increase than what was recommended. This is an inconsistent and arbitrary approach.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should reject the RD's recommended water revenue increase of $236,777 as a result

of its flawed analysis of the escalation provisions of certain negotiated water contracts. AP MB at 51-53; AP RB at 19.

E. EXCEPTION NO. 5 – THE RD ERRS BY DISALLOWING A PORTION OF THE COMPANY'S PROPOSED GENERAL LIABILITY INSURANCE EXPENSE. RD AT 59.

The RD recommended that the Commission adjust the Company's claimed General Liability Insurance Expense consistent with the recommendations of I&E. RD at 59. In this regard, Aqua PA's claim for insurance expense for water operations would be decreased by $340,945 and for wastewater operations would be increased by $29,967. RD at 59. The RD reasoned that these adjustments were necessary because Aqua PA "failed to provide adequate documentation in support of its treatment" of this expense, and that Aqua PA did not justify its "mixing of calculation elements…for the purposes of projecting expense increases." RD at 59.

This recommended adjustment should be rejected. Aqua PA fully explained how it calculated its projection of general liability insurance expense for the FPFTY. AP MB at 74-75. In response to criticisms raised by I&E and OCA, the Company updated its insurance claim to reflect actual general liability expense information for the Year 2022 that became available after the case had been filed. AP MB at 75. The Company then used I&E's proposed three-year average percentage increase to this expense to adjust the final quarter of the FPFTY. AP MB at 75-76 (citing and quoting AP St. 4-R at 6-7).

Although the RD claims that the Company improperly mixed calculation elements, there is nothing unusual or improper in updating the claim to reflect known, actual information for FY 2022, or in developing the FPFTY claim using three quarters of that actual data and one quarter of projected data using the same adjustment factor (4.38%) proposed by both the OCA and I&E witnesses in their direct testimony. There is also no evidence of record to support I&E's concerns regarding the reliability of this information; its testimony is pure conjecture. AP RB at 30.

Aqua PA's approach in calculating its updated expense in rebuttal followed the same approach proposed by I&E to compute this expense. It started with known cost and adjusted it to the FPFTY level, using the same escalation factor proposed by I&E. AP RB at 30. The only difference is that Aqua PA updated its claim to reflect more recent actual data as the starting point. AP RB at 30. In this regard, the RD inconsistently accepts I&E's calculation as credible, but asserts that Aqua PA's calculation, which uses the same method updated with the most recent data available, is not credible. The Commission should reject this reasoning.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should reject the RD's adjustment to the Company's claim for general liability insurance expense, and adopt the Company's updated general liability insurance expense for water and wastewater operations. *See* AP MB at 74-77; AP RB at 29-30.

F. EXCEPTION NO. 6 – THE RD ERRS BY DISALLOWING RECOVERY OF THE COMPANY'S SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN. RD AT 63.

The RD recommends disallowing the cost of the Company's Supplemental Executive Retirement Plan ("SERP"). RD at 63. The RD improperly applies incentive compensation recovery criteria to a post-employment retirement benefit to reach its incorrect recommendation.

The SERP is a legacy retirement program, similar to the Company's pension plan but limited to certain senior level employees who did not qualify under the Company's former pension plan due to Internal Revenue Code limitations. RD at 63. Thus, the SERP provides replacement retirement benefits for the limited number of present and retired employees and their spouses who are not eligible for the Company's qualified pension plan.

Like other employee benefits such as medical insurance and the qualified pension plan, eligibility for benefits each year under the SERP is not based upon performance criteria, but upon employment. Like the pension plan, the SERP was closed to new participants starting in April

2003.[15] However, like the pension plan, the benefits to be received pursuant to the terms of the SERP were not taken away from then-existing employees at the time the plan was closed; rather, pre-April 2003 employees continue to be entitled to receive their promised benefits upon retirement. Thus, like the pension plan, the Company continues to incur costs under this legacy plan. As participants/eligible spouses pass away, the cost of the program will phase out.

The RD reasons that the SERP is not associated with retaining or recruiting executive talent, nor is it connected to employee performance metrics. RD at 63. The RD contrasts the SERP to the Company's incentive compensation plan, and concludes that the SERP is not associated with cost-containment or maintenance of high-quality service. RD at 63. Based upon these conclusions, the RD recommends that the SERP costs be disallowed. This is a flawed analysis. As a post-employment benefit, recovery of the costs of the program in rates should not be measured by whether it serves as a current recruiting tool, or whether the recipient retirees have met an incentive compensation target. Such an approach would disincentivize utilities from changing or eliminating post-employment benefits, if the ongoing costs of a discontinued program may no longer be recoverable. For the reasons explained above, and in Aqua PA's briefs, the cost of the SERP should be allowed. AP MB at 72-74; AP RB at 28-29.

G. EXCEPTION NO. 7 – THE RD ERRS BY REMOVING THE COMPANY'S GENERAL PRICE LEVEL ADJUSTMENT THAT REFLECTS THE ANTICIPATED EFFECT OF INFLATION ON EXPENSES THAT WERE NOT OTHERWISE SPECIFICALLY ADJUTED. RD AT 70-71.

The RD concludes that the Commission should remove the Company's proposed General Price Level Adjustment for several reasons. RD at 70-71. At the outset, it should be emphasized that the Company has made this type of inflationary adjustment for a limited portion of its expenses

[15] In order to control costs for the benefit of customers, the defined benefit SERP and pension plan were replaced by a defined contribution 401(k) program. AP MB at 73.

for decades. With that background, it is particularly concerning the RD agrees with the OCA in the case based on the current economic environment. The RD claims that the adjustment was not justified, and further asserts that "[w]hile it may be simpler for Aqua to simply use a general inflation factor for a block of expenses, its simplicity belies the fact that Commission precedent requires specificity if an inflation factor is utilized." RD at 70. The RD goes on to explain that a large, sophisticated utility should not be permitted to use a general adjustment, such as the General Price Level Adjustment used by the Company, because it would "incentivize less accurate tracking of expenses and would disincentivize Aqua from controlling its costs." RD at 70. Finally, the RD reasons that the adjustment should be rejected because "Aqua has not demonstrated that tracking the changes in these expenses individually is unduly burdensome." RD at 70. These recommendations are incorrect and inconsistent with the law, and should therefore be rejected.

Aqua PA first notes that the RD ignores the test enunciated by the Commission regarding the evaluation of an inflation adjustment to expenses not otherwise specifically adjusted. Importantly, the Commission has repeatedly held that general price adjustment factors may be applied to expenses not separately adjusted, where the utility has demonstrated the adjustments are adequately supported and relatively conservative. AP MB at 61-62 (citing authorities). More specifically, the Commission has "consistently accepted inflation adjustments where supported by historic data demonstrating that the utility has experienced cost increases that exceed the claimed inflation increases." AP MB at 62 (quoting *Pa. PUC v. Philadelphia Suburban Water Company*, Docket Nos. R-00016750, 2002 Pa. PUC LEXIS 55, at *55 (Order entered July 8, 2002)).

The RD incorrectly supplants this precedent based upon its concern that the adjustment "requires specificity." RD at 70. Even if this were the correct test, and it is not, such specificity was provided by Aqua PA. Aqua PA's Main Brief is instructive on this point:

> Aqua PA witness Mr. Manning testified that the expenses subject to this adjustment are directly affected by inflation and that "[t]he expenses that the Company is requesting be increased under this general inflation adjustment have all historically grown at rates that far exceed the requested inflation factor that the Company is applying to them, which is 1.75% in the FTY and 1.70% in the FPFTY." AP St. 3-R at 3. He went on to provide specific examples related to expense categories subject to this adjustment as follows:
>
> > Supplies expense, which falls under this adjustment, has grown at an average rate of 8.19% over the last three years. Lab Testing expenses, which also fall under this adjustment, have grown at an average rate of 11.13% over the last three years. Outside accounting expenses, also under this adjustment, have grown at an average rate of 3.38% over the last three years as well.
>
> AP St. 3-R at 3-4. In each case, Aqua PA's proposed General Price Level Adjustment utilizes an inflation factor well below the historical cost increases the Company has experienced.

AP MB at 63. Mr. Manning's testimony on this point was not rebutted by any other party.

Furthermore, it is not disputed, nor does the RD consider, that the macro conditions in which the world is currently operating support the Company's position that the inflation factor proposed by the Company is conservative. AP MB at 63-64. Indeed, the proposed General Price Level Adjustment is surpassed by both actual inflation rates experienced in the latter months of 2021 and more recent projected inflation rates. AP St. 3-R at 4.[16]

The RD's further basis for rejecting the proposed adjustment, *i.e.*, the adjustment would incentivize less accurate tracking of expenses and would disincentivize cost controls, is also without merit. No evidence has been presented that demonstrates an adjustment—which has been used by the Company and accepted by the Commission in rate proceedings for over 25 years,

[16] Other Aqua PA witnesses specifically addressed the rising projections of inflation, which affect the Company's revenue requirement. *See* AP St. 1-R at 5-6 (explaining that "the [inflation] factor is higher today than it was just six months ago, and the Company expects the factor to be sustained well into 2022" but that the Company was maintaining its proposed 1.70% inflation factor); AP St. 7-R at 6 (identifying economic indicators that inflation rates are expected to rise).

including in Aqua PA's last fully litigated base rate proceeding (AP MB at 60, 62-63)—has resulted in inaccurate tracking of expenses or a failure to control costs. Rather, record evidence demonstrates that the adjustment is in fact conservative in light of substantially rising inflation costs, and that the Company did not seek to update the inflation factor used for its General Price Level Adjustment based upon these conditions. *See* AP MB at 64.

In addition, the RD's conclusion that the General Price Level Adjustment should be rejected because "Aqua has not demonstrated that tracking the changes in these expenses individually is unduly burdensome" is erroneous. RD at 70. General Price Level Adjustment have been accepted by the Commission precisely because it is unreasonable to expect the Company to individually analyze thousands of relatively minor dollar invoices to compute hundreds of separate cost adjustments. As explained above, the test applied by the Commission to evaluate an inflation based adjustment is where the adjustment is adequately supported and relatively conservative. In each instance where Aqua PA applied the General Price Level Adjustment, this showing was made. AP MB at 63. The RD's attempt to ignore these facts by applying an incorrect legal standard should be rejected.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should not adopt the RD's recommendation regarding the General Price Level Adjustment, and should approve the Company's proposed adjustment without modification. AP MB at 59-64; AP RB at 22-24.

H. EXCEPTION NO. 8 – THE RD ERRS BY ORDERING AQUA PA TO PREPARE A SEPARATE COST OF SERVICE STUDY FOR EACH SYSTEM ACQUIRED UNDER 66 PA.C.S. § 1329 THAT IS INCLUDED IN THE NEXT BASE RATE PROCEEDING FOLLOWING SUCH ACQUISITION. RD AT 83.

The RD also adopts the recommendation advanced by I&E that Aqua PA be required to prepare separate cost of service studies and revenue requirements in its next base rate proceeding.

RD at 82-83. This would require Aqua PA to prepare a cost of service study and revenue requirement for (a) combined Wastewater Zones 1 through 6 (consisting of the Company's legacy systems), (b) combined Wastewater Zones 7-11 (representing the systems acquired under Section 1329 of the Public Utility Code prior to this base rate proceeding), and (c) each additional system acquired after this proceeding under Section 1329. RD at 82-83. The RD justifies this recommendation upon the importance of tracking the implications of the acquisition of water and wastewater systems and the effects on rates and cost of service, and explains that "I&E's proposals are reasonable and sensible and well within the Commission's mandate to assure that a utility's rates are just and reasonable." RD at 83.

Aqua PA initially notes that the RD ignores applicable appellate precedent. The Commonwealth Court has specifically affirmed a prior Commission order that declined to condition a water utility's proposed consolidation of rate districts upon the maintenance of separate records for each district. *See Pittsburgh v. Pa. PUC*, 526 A.2d 1243 (Pa. Cmwlth. 1987), *pet. for allowance of appeal denied*, 538 A.2d 880 (Pa. 1988). Consistent with this case, Aqua PA should not be required to maintain and prepare separate cost of service studies and revenue requirements in its next base rate proceeding.

Furthermore, the RD disregards the impacts of imposing this requirement on Aqua PA relative to other water and wastewater utilities in Pennsylvania. This requirement will result in significant accounting, tracking, operational and rate impacts, that would also frustrate the Commission's policy supporting single tariff pricing and consolidation. AP MB at 219. In turn, the increased costs and complications associated with preparing separate cost allocation studies would likely put the Company at a competitive disadvantage from other bidders in future acquisition opportunities. AP MB at 219.

Moreover, Aqua PA submits that, for new acquisitions, the recommended requirement should be analyzed in the context of future Section 1329 acquisition proceedings, and not in this base rate case. AP MB at 219-220. The Commission should not require Aqua PA to indefinitely prepare separate costs of service and revenue requirements for future acquired systems, where it is not known whether and when further systems will be acquired.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should not adopt the RD's recommendation that would require the Company to maintain and prepare separate costs of service and revenue requirements associated with its various wastewater systems. AP MB at 93-94.

I. EXCEPTION NO. 9 – THE RD ERRS BY RECOMMENDING THAT THE COMMISSION ACCEPT I&E'S METHODOLOGY FOR ALLOCATING WASTEWATER REVENUE AND DESIGNING WASTEWATER RATES, INCLUDING I&E'S PROPOSED ACT 11 ALLOCATION. RD AT 87-91, 96.

Aqua PA proposed to allocate a portion of the wastewater revenue requirement to its water customers in order to provide a path for gradualism for the subject systems, as this is the first case in which the Commission will consider increases to the rates for these systems. AP St. 1-R at 23-24. The RD rejected the Company's proposed Act 11 revenue allocation, which proposed to allocate approximately 30% or $21 Million of the Company's proposed revenue requirement from wastewater to water rates, and recommended that the Commission adopt the revenue allocation proposed by I&E of approximately $10 Million instead. *See* RD at 91. Each of the bases advanced by the RD in support of its recommendation should be rejected.

First, the RD correctly acknowledges that public utility regulation involves the socialization of costs that benefit a subset of customers to a larger group of customers, and that this premise underlies Act 11. RD at 89. However, the RD errs by reasoning that Aqua PA's proposed allocation of wastewater revenues is not equitable to water customers because Aqua PA

and the selling municipalities should know, at the time of a subject wastewater system acquisition, rates would increase as wastewater customers were likely paying rates that were well below the cost of service. RD at 89-90. In this regard, the RD effectively restates the justifications advanced by I&E, which Aqua PA demonstrated were not reasonable and unsupported by recorded evidence.

Aqua PA specifically explained that I&E's testimony, which implies that municipal governments believed the cost of acquiring the subject systems would be borne solely by the Company's existing customers, ignores the fact that the Company explains how the purchase price will impact future customer rates as a part of the Section 1329 process. AP MB at 218-219. Furthermore, Aqua PA demonstrated that the Company engages with and educates municipal leaders on the ratemaking process, which further belies I&E's arguments. AP MB at 218-219.

Next, the RD reasons that "[w]here the community representatives opted to sell their system in order to forgo increasing taxes or utility rates or both, they cannot now escape the consequences of that decision." RD at 90. It further explains that "[t]he communities of the Acquired Systems achieved some benefit from the revenue generated by the sale of their wastewater systems." RD at 90.

While the RD cites to Aqua PA's testimony to support this point (RD at 90, n.163), it takes this testimony out of context. Specifically, Aqua PA witness Mr. Packer's cited testimony was provided in response to the proposed Act 11 revenue allocation advanced by OCA. AP MB at 217-218. Although Mr. Packer did "not disagree that there is a benefit to customers in these systems as far as local tax savings" he clearly goes on to testify that "the principles of gradualism should prevail and be utilized to mitigate these first in rate increases." AP St. 1-R at 25. He further explained his reasoning as follows:

> All of these acquisitions were approved individually by the PUC and deemed in the public interest. <u>That determination was not a short</u>

> term only assessment. The PUC understands that these systems will be owned and operated by the Company for many years and there will be plenty of opportunity to adjust the rate design for these systems to balance the recovery of the cost of utility service. As the Company builds a larger wastewater footprint, the ability to adjust the rates between zones and systems will only be enhanced, as we have seen for many years on the water utility side. It is for these reasons that I believe the adjustments to reduce the Act 11 allocation should be rejected.

AP St. 1-R at 25-26 (emphasis added). The RD ignores the fact that each of these acquisitions is a "long-term" proposition, where the Commission will have plenty of opportunities to adjust the rate design for each acquired system in the years to come. Rather, it appears to reason that, because some immediate benefit was obtained by the communities that sold these systems to Aqua PA, each system should be subjected to a more significant and immediate rate increase than under Aqua PA's proposal. Aqua PA submits this reasoning highlights that I&E's proposal will result in rate shock and is therefore unreasonable.

The RD further claims that "Aqua's approach of simply allocating 30% of the proposed wastewater revenue requirement to water customers is arbitrary." RD at 90. While the RD cites to a passage from *Lloyd*, which rejected the definition of gradualism as limiting a rate increase to 10% of the total bill as "the magic number that will prevent rate shock," *Lloyd v. Pa. PUC*, 904 A.2d 1010, 1020 (Pa. Cmwlth. 2006), Aqua PA does not assert that its proposed 30% allocation is magic number and fully explained why its proposal was just and reasonable. *See* AP MB at 216-225; *see also* AP RB at 95-99. Indeed, given the number and size of the acquired systems since the Company's last base rate case, it is appropriate for the initial allocation of revenues to be higher in order to mitigate the impacts of the initial rate increase for these systems while still moving each towards the cost of service. AP St. 1-R at 24; *see also* AP MB at 216. Each of the alternatives advanced by the other parties disrupts this balanced approach, and would immediately subject the customers of the acquired systems to more significant rate increases.

Finally, Aqua PA notes that the RD also adopts the wastewater revenue allocation and rate design proposed by I&E, which were proposed to obtain I&E's Act 11 revenue allocation proposal. *See* RD at 91. Aqua PA fully explained why each of the Rate Zone specific rate design proposals advanced by I&E were inappropriate. *See* AP MB, Section IX.C.2.b. Moreover, Aqua PA explained the basis for designing its proposed wastewater rates in detail. AP MB at 237-238. The RD fails to conduct any meaningful analysis of the Company's proposed wastewater rate design, except to determine that I&E's proposed rate design should be adopted as a part of its adoption of I&E's proposed Act 11 revenue allocation. The Commission should reject this recommendation, and take into consideration that actual rate design proposals advanced by the Company.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should reverse RD's recommended allocation of wastewater revenues under Act 11, and adopt the Company's proposed Act 11 revenue allocation. AP MB at 213-225; AP RB at 95-99. In addition, the Commission should adopt Aqua PA's proposed design of wastewater rates.

J. EXCEPTION NO. 10 – THE RD ERRS BY RECOMMENDING THAT AQUA PA BE REQUIRED TO STUDY THE REASONABLENESS OF UNMETERED RATES. RD AT 98.

OCA and several customers that participated in the public input hearings raised concerns regarding Aqua PA's unmetered wastewater rates. RD at 96. Due to these concerns, OCA recommended that Aqua PA should be ordered to study the reasonableness of its unmetered rates, and to provide the results of such study in its next base rate case. RD at 98. The RD agreed with the OCA, and ordered Aqua PA to conduct the recommended study, explaining that the Company's average monthly usage of 4,000 gallons may not result in fair rates where there is a significant mix in types of housing and that there may be areas in Aqua's service territory where unique circumstances suggest a different method of calculating a flat rate is more reasonable. RD at 98.

The RD's recommendation should be rejected. As an initial matter, Aqua PA notes that the RD does not find or conclude that the Company's use of unmetered rates or use of an average monthly usage of 4,000 gallons is unreasonable. *See* 66 Pa.C.S. § 1301. Rather, the RD only finds that the use of a 4,000 gallon average monthly usage rate may not result in fair rates, and that there may be areas where a different method of calculating a flat rate is more reasonable. RD at 98.

Aqua PA demonstrated that its existing unmetered rates and method for calculating them is reasonable, and is consistent with the standard in the industry and for other water utilities across Pennsylvania. AP MB at 243-244. Aqua PA witness Mr. Duerr credibly testified that the average usage of 4,000 gallons was substantiated by the pre-COVID pandemic average residential usage shown in Aqua PA's last base rate case, and that its average usage amount was consistent with the average usage used by other water utilities such as Pennsylvania-American Water Company. AP St. 9-R at 14-15. As such, despite OCA's claims to the contrary, Aqua PA has adequately explained and justified the differences between metered and unmetered rates.

The recommendation also presumes that Aqua PA has access to usage data to assess average usage in areas without metered water service. Many of these areas have individual customer wells, and usage cannot be determined. Any such study results will thus be doomed to challenge as "speculative."

For these reasons, and the reasons more fully explained in Aqua PA's briefs, the Commission should not adopt the RD's recommendation to require Aqua PA to further study unmetered rates and to report on the results of this study in its next base rate proceeding. AP MB at 243-244; AP RB at 103-104.

K. EXCEPTION NO. 11 – THE RD ERRS BY REJECTING THE COMPANY'S PROPOSED ENERGY COST ADJUSTMENT MECHANISM AND PURCHASED WATER ADJUSTMENT CLAUSE. RD AT 99-104.

The RD recommends that the Company's proposed Energy Cost Adjustment Mechanism

("ECAM") and its Purchased Water Adjustment Clause ("PWAC") be rejected. RD at 99-104. The RD concludes that Aqua PA failed to demonstrate that it cannot adequately control its energy and purchased water costs through normal mechanisms, each cost category does not constitute a significant amount of Aqua PA's cost of service. RD at 101-102, 104. In addition, the RD concludes that energy costs are not likely to decline in this climate, so customers are not likely to benefit from the ECAM. RD at 102. The RD further finds that the ECAM constitutes impermissible single-issue ratemaking. RD at 102. The RD's findings regarding the ECAM and PWAC should be rejected, and each of these reconcilable riders should be approved.

Aqua PA demonstrated that both the ECAM and PWAC satisfies the requirements for approval of reconcilable riders under Pennsylvania law and Section 1307(a) of the Public Utility Code, 66 Pa.C.S. § 1307(a). AP MB at 245-259; AP RB at 105-106. Aqua PA demonstrated that both the ECAM and the PWAC satisfy the well-recognized exception to the prohibition against single-issue ratemaking; each rider seeks to recover an expense that is easily identifiable and beyond the Company's control. AP MB at 245-246.

With specific respect to the RD's finding that energy costs are not likely to decline, the RD cites no evidence of record to support this finding. Rather, this unsupported assertion appears to be an attempt to undermine Aqua PA's otherwise unrebutted testimony that any energy cost savings would be timely passed through to customers. AP MB at 255-256.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should reject the RD's findings and conclusions regarding the ECAM and PWAC, and approve these proposed reconcilable riders. AP MB at 235-258; AP RB at 105-107.

L. EXCEPTION NO. 12 – THE RD ERRS BY REJECTING THE PROPOSED FEDERAL TAX ADJUSTMENT SURCHARGE. RD AT 104-106.

The RD recommends that the Commission reject the Company's proposed automatic

adjustment clause to adjust its water and wastewater base rates for changes in federal corporate income tax rates, called the Federal Tax Adjustment Surcharge ("FTAS"). RD at 106. Importantly, the RD did not find or conclude that the proposed method of calculation, mechanics or safeguards set forth in the Company's proposed FTAS were unreasonable. *See* AP MB at 261 (noting that no parties contested these aspects of the FTAS). Rather, the ALJ concludes that the FTAS is "premature" because there is "no pending legislation proposing an increase to the federal corporate income tax rate" and "[e]ven if legislation was being considered in Congress, there is no way of knowing if or when and in what form the tax change would be implemented." RD at 106.

Aqua PA addressed the parties' arguments that the FTAS was premature and demonstrated that those concerns should be rejected. AP MB at 262; *see also* AP St. 8 at 15 and AP St. 8-R at 9. The concern, adopted by the ALJ, that a change in the federal corporate income tax rate is uncertain is irrelevant to the determination of whether the FTAS is just and reasonable. Indeed:

> If no change occurs, the FTAS has no impact upon customers. AP St. 8-R at 9. If/when a change does occur, the FTAS will act as a temporary mechanism if/when a change occurs between a utility's base rates and will more-timely ensure that the impacts of the change are reflected in the utility's rates. AP St. 8-R at 9.

AP MB at 262.

Aqua PA further demonstrated that any change in the federal corporate income tax rate would have a significant impact upon tax expense, and the Company's rates. AP St. 8 at 1 (calculating a $14 million increase in revenue requirement associated with an increase from 21% to 28% in the federal corporate income tax rate). This calculation is unrebutted and, therefore, it is reasonable to infer that changes in the federal corporate income tax rate, whether it be an increase or a decrease, will significantly impact the Company's base rates.

Finally, Aqua PA demonstrated that the FTAS is analogous to the State Tax Adjustment Surcharge ("STAS"). AP MB at 261. Just as the STAS provides for adjustments to base rates for

changes in state tax rates (and more specifically for changes under the Pennsylvania Corporate Net Income Tax), so too does the FTAS provide for adjustments to base rates for changes in federal corporate income tax. AP St. 8 at 18.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should reject the RD's findings and conclusions regarding the FTAS, and it should approve the proposed FTAS without modification. AP MB at 259-263: AP RB at 107.

M. EXCEPTION NO. 13 – THE RD ERRS BY REQUIRING AQUA PA TO DEVELOP AN ISOLATION VALVE INSPECTION AND EXERCISE PROGRAM. RD AT 125.

During this proceeding, OCA recommended that the Company be required to establish a 5-year inspection cycle for non-critical isolation valves. While the RD correctly concluded that "OCA has not sustained its burden of proving that imposing a 5-year inspection cycle for non-critical valves is necessary or will derive a benefit to Aqua's system commensurate with the cost to implement the program," it recommended that Aqua PA "develop an isolation and inspection exercise program, to be implemented no later than 180 days from the effective date of rates" set in this proceeding. RD at 125. The RD further recommends that the inspection and exercise program establish a defined schedule to exercise each of its non-critical vales and maintain records of attempts to inspect and exercise isolation valves. RD at 125.

The RD's recommendation that Aqua PA develop and implement a non-critical isolation valve inspection and exercise program should be rejected. Aqua PA submitted unrebutted testimony that:

> All non-critical valves have been identified in the Aqua GIS asset registry…An analysis has been completed to ensure the exercising of these valves is completed over a 12-year period. Internal staff used GIS analysis techniques to identify valve proximity to major roadways to determine staffing requirements needed for traffic control measures. The Company is developing a timeline to

> determine which non-critical valves are scheduled in year one, two, etc.

AP St. 9-R at 13-14. As explained in its testimony and Main Brief, Aqua has already developed an appropriate inspection and exercise program. AP MB at 172.

Moreover, the Company has already made commitments through its 2020 management audit relating to the inspection of non-critical valves. AP MB at 172; AP St. 9-R at 13. As stated above, the Company committed to ensure the exercising of these valves is completed over a 12-year period. As stated above, the Company committed to ensure the exercising of these valves is completed over a 12-year period. The recommendation advanced by the RD is simply duplicative of Aqua PA's existing program and commitments.

For these reasons and the reasons more fully explained in Aqua PA's briefs, the Commission should reject the RD's recommendation that Aqua PA develop and implement an isolation and inspection exercise program.

III. CONCLUSION

WHEREFORE, and for all of the foregoing reasons, Aqua Pennsylvania, Inc. and Aqua Pennsylvania Wastewater, Inc., respectfully request that the Pennsylvania Public Utility Commission (1) grant these exceptions, (2) revise the Recommended Decision of Administrative Mary D. Long, and (3) approve the rate increase and other proposals contained in Tariff Water – Pa. P.U.C. No. 3 and Tariff Sewer – Pa. P.U.C. No. 3, consistent with the modifications set forth herein.

Respectfully submitted,

Michael W. Hassell

_____

Kimberly A. Joyce, Esq. (ID # 86605)
Mary McFall Hopper, Esq. (ID # 60118)
Alexander R. Stahl, Esq. (ID # 317012)
762 W. Lancaster Ave
Bryn Mawr, PA 19010
Phone: 610-645-1077
Phone: 610-645-1170
Phone: 610-645-1130
E-mail: kajoyce@essential.co
E-mail: mmhopper@aquaamerica.com
E-mail: astahl@aquaamerica.com

Michael W. Hassell, Esq. (ID # 34851)
Garrett P. Lent, Esq. (ID # 321566)
Post & Schell, P.C.
17 North Second Street, 12th Floor
Harrisburg, PA 17101
Phone: 717-731-1970
E-mail: mhassell@postschell.com
E-mail: glent@postschell.com

Dated: February 28, 2022

Counsel for Aqua Pennsylvania, Inc., and Aqua Pennsylvania Wastewater, Inc.