

COMMONWEALTH OF PENNSYLVANIA



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April 8, 2022

Rosemary Chiavetta, Secretary
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Re: Application of Aqua Pennsylvania Wastewater, Inc.
pursuant to Sections 507, 1102 and 1329 of the Public
Utility Code for Approval of its Acquisition of the
Wastewater System Assets of East Whiteland Township
Docket No. A-2021-3026132

Dear Secretary Chiavetta:

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

Copies have been served per the attached Certificate of Service.

Respectfully submitted,

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Certificate of Service

*326765

CERTIFICATE OF SERVICE

Re: Application of Aqua Pennsylvania Wastewater, :
Inc. pursuant to Sections 1102, 1329, 507, and :
2102 of the Public Utility Code for Approval of its : Docket No. A-2021-3026132
Acquisition of the Wastewater System Assets :
of East Whiteland Township :

I hereby certify that I have this day served a true copy of the following document, the Office of Consumer Advocate's Main Brief, upon parties of record in this proceeding in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

Dated this 8th day of April 2022.

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Application of Aqua Pennsylvania Wastewater, :
Inc. pursuant to Sections 507, 1102, 1329 and :
2102 of the Public Utility Code for Approval of its : Docket No. A-2021-3026132
Acquisition of the Wastewater System Assets :
of East Whiteland Township :

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I. STATEMENT OF THE CASE

A. Procedural History

On August 3, 2021, Aqua Pennsylvania Wastewater, Inc. (Aqua, Applicant, or Company) filed an Application under Sections 507, 1102, 1329 and 2102 of the Public Utility Code requesting that the Public Utility Commission (Commission) (1) approve the acquisition of the wastewater system assets of East Whiteland Township (East Whiteland or Township), Chester County; (2) approve the right of Aqua to provide wastewater service in the requested territory; and (3) include, in its Order approving the acquisition, the ratemaking rate base of the assets as determined under Section 1329(c)(2) of the Public Utility Code. Application at ¶ 3; 66 Pa. C.S. §§ 507, 1102, 1329 and 2102. Aqua also requests approval of the Asset Purchase Agreement (APA) dated January 8, 2021 as well as other municipal agreements, pursuant to Section 507 of the Public Utility Code, and requests that the Commission issue an Order and Certificate of Public Convenience approving and addressing the items requested in this Application. Application at ¶ 5. Aqua provides wastewater service to approximately 45,000 customers throughout Pennsylvania. East Whiteland owns a sanitary wastewater collection system which provides direct wastewater service to 3,895 customers in East Whiteland Township, who will become Aqua customers if the Application is approved. Application at ¶ 8.

On August 26, 2021, the Office of Small Business Advocate filed a Notice of Intervention, and Public Statement. The OCA filed a Protest and Public Statement on September 17, 2021. On October 4, 2021, I&E entered its appearance in the matter. On February 3, 2022, East Whiteland

Township filed a Notice of Intervention. On February 4, 2022, Richard Gage filed a Protest to the Application.

By Secretarial Letter dated December 20, 2021, the Commission conditionally accepted the Application for filing. The Commission directed Aqua to provide individual notice to Aqua's potentially affected existing water and wastewater customers, ensure concurrent notice is provided to all current East Whiteland wastewater customers and that newspaper notice be provided in the East Whiteland area. Upon completion, Aqua was directed to file proof of publication of the newspaper notice with the Commission. The Commission informed Aqua that it had accepted the Application for filing on February 4, 2022. Administrative Law Judge (ALJ) Marta Guhl issued a Prehearing Conference Order on February 23, 2022 directing the parties to submit a prehearing conference memorandum on or before March 4, 2022.

A prehearing conference was held on March 8, 2022. On March 11, 2022, the OCA served the direct testimony of David J. Garrett¹ and Noah D. Eastman.² I&E and OSBA also served direct testimony on March 11, 2022. Both the Company and East Whiteland Township served rebuttal testimony on March 18, 2022. I&E, OSBA, and the OCA served surrebuttal testimony on March 25, 2022. An evidentiary hearing was held on March 31, 2022, where the OCA and other parties

¹ Mr. Garrett is the managing member of Resolve Utility Consulting, LLC. He is an independent consultant specializing in public utility regulation. Mr. Garrett has represented numerous consumer groups and state agencies in utility regulatory proceedings, primarily in the areas of cost of capital and depreciation. He is a Certified Depreciation Professional with the Society of Depreciation Professionals. He is also a Certified Rate of Return Analyst with the Society of Utility and Regulatory Financial Analysts. Mr. Garrett's background and qualifications are attached as Exhibit DJG-1 to OCA Statement 1.

² Mr. Eastman is a Regulatory Analyst at the Office of Consumer Advocate. He regularly analyzes the financial, economic, rate of return, and policy issues relevant to ratemaking filings and presents written testimony on behalf of the OCA. He has submitted testimony in *McCloskey v. Hidden Valley Utility Services* - C-2014-2447138, C-2014-2447169; *Application of Pennsylvania American Water Co.* - A-2020-3019634; *Pa. PUC v. Duquesne Light Co.* - R-2021-3024750; *Pa. PUC v. PECO Energy Co.* - Electric Division - R-2021-3024601; *Pa. PUC v. Community Utilities of Pennsylvania* - R-2021-3025206, R-2021-3025207; *Application of Aqua Pennsylvania Wastewater, Inc.* - A-2021-3026132. A more complete description of Mr. Eastman's education and experience may be found at Appendix A to OCA Statement 2.

submitted their testimony and associated exhibits into the record. Pursuant to the schedule, the OCA files this Main Brief in support of its position.

B. Overview of the Proposed Transaction

In accordance with Section 1102 of the Public Utility Code, Aqua is requesting a Certificate of Public Convenience to acquire the East Whiteland Township wastewater system and provide wastewater service within the municipal boundaries of the Township. Application at ¶ 3. Aqua proposes to pay \$54,930,000 for East Whiteland Township's assets. Application at ¶ 21. Aqua also chose to file its application under Section 1329 of the Public Utility Code. Aqua requests that the purchase price of \$54,930,000 be approved for ratemaking purposes as it is lower than the average of the two appraisals provided within its application. *See* 66 Pa. C.S. § 1329(c)(2). In addition, Aqua seeks approval from the Commission for several other municipal agreements pursuant to Section 507 of the Public Utility Code. Application at ¶¶ 69, 70. Aqua also requests that if the East Whiteland acquisition is completed, the Commission also approve the subsequent assignment of the Wastewater Conveyance Agreement from East Whiteland to Aqua under Section 2102 of the Public Utility Code. Application at ¶¶ 71-72.

II. BURDEN OF PROOF

Under Sections 315(c) and 332 of the Public Utility Code, the burden of proof rests with the Applicant. Section 332 states:

Burden of proof. - Except as may be otherwise provided in section 315 (relating to burden of proof) or other provisions of this part or other relevant statute, the proponent of a rule or order has the burden of proof.

66 Pa. C.S. § 332. Section 315(c) places the burden of proof upon the Applicant. It states that:

In any proceeding upon the motion of the commission, involving the service or facilities of any public utility, the burden of proof to show that the service and facilities involved are adequate, efficient, safe, and reasonable shall be upon the public utility.

66 Pa. C.S. § 315(c). Therefore, it is Aqua that has the burden of demonstrating by a preponderance of the evidence that its proposed acquisition of East Whiteland meets the requirements of Pennsylvania law. *See Lansberry v. Pa. PUC*, 578 A.2d 600, 602 (Pa. Cmwlth. Ct. 1990) (*Lansberry*). More precisely, the Applicant's case must be more convincing than the case presented by the challenger. *Se-Ling Hosiery, Inc. v. Margulies*, 70 A.2d 845, 856 (1950).

The Pennsylvania Supreme Court has stated that the party with the burden of proof has a formidable task to show that the Commission may lawfully adopt its position. Even where a party established a prima facie case, the party with the burden of proof must establish that “the elements of that cause of action are proven with substantial evidence which enables the party asserting the cause of action to prevail, precluding all reasonable inferences to the contrary.” *Burleson v. Pa. PUC*, 461 A.2d 1234, 36 (1983). Additionally, the evidence must be substantial and legally credible, and cannot be mere “suspicion” or a “scintilla” of evidence. *Lansberry* at 602. Finally, the Applicant has the burden of proving that the acquisition will “affirmatively promote the ‘service, accommodation, convenience, or safety of the public’ in some substantial way.” *City of York v. Pa. PUC*, 295 A.2d 825, 28 (Pa. Cmwlth. Ct. 1972); 66 Pa. C.S. § 315(c) (*City of York*).

III. STATEMENT OF QUESTIONS INVOLVED

Q. Whether the proposed transaction establishes affirmative public benefits?

Suggested Answer: No.

Q. If the Commission approves the application under Section 1102, are any conditions necessary?

Suggested Answer: Yes.

Q. Whether the valuations provided pursuant to Section 1329 are reasonable under Chapter 13 of the Public Utility Code and accepted financial and ratemaking principles?

Suggested Answer: No.

IV. SUMMARY OF ARGUMENT

Aqua's request for approval of its proposed purchase of the East Whiteland wastewater system was filed under Section 1102 of the Public Utility Code. 66 Pa. C.S. § 1102. Aqua failed to show that the transaction would provide the required substantial affirmative public benefits under Section 1102. The averred benefits of the transfer do not outweigh the substantial adverse impact on Aqua's existing wastewater customers (and likely, its water customers) and on the East Whiteland customers under Aqua ownership. East Whiteland's average rate base per Equivalent Dwelling Unit (EDU) is slightly higher than that of Aqua's existing customers. Aqua calculated a \$5.011 million annual revenue deficiency to support the East Whiteland system if the proposed \$54.9 million rate base is approved. Aqua St. 1, App. A. If the costs are applied only to East Whiteland's customers, it would require a 132% increase to their current rates. If not, the additional revenue requirement will be recovered from existing Aqua wastewater customers and likely Aqua water customers. The evidence shows no meaningful change in quality or conditions of service will result from changing ownership from East Whiteland to Aqua. Thus, the OCA recommends that the Commission deny the proposed transaction.

As it pertains to Section 1329, the appraisal process is not a simple formulaic mathematical exercise. Review of the appraisals provided by Aqua and East Whiteland demonstrate that judgments made in each type of analysis as well as in how much weight is given to each approach. In this case, the appraisals for the Seller and Buyer must be adjusted to reflect accepted ratemaking and regulatory principles. As a result of these necessary and reasonable adjustments, the average of the two appraisals is \$46.5 million. As this is less than the purchase price of \$54.9 million, the appropriate amount for ratemaking purposes is \$46.5 million. Even at this lower level of ratemaking rate base, the OCA submits that there are not

substantial affirmative public benefits. Should the Commission determine to approve the proposed transaction under Section 1102, the OCA identified several conditions that are necessary, in addition to the adjusted ratemaking rate base, to protect the public interest and should be adopted as part of such determination.

V. ARGUMENT

A. Sections 1102/1103

1. Introduction

As discussed in Section V.A.3 below, based on a weighing of the known harms and claimed future benefits, Aqua has failed to establish that the proposed transaction is in the public interest.

The Public Utility Code authorizes the Commission to permit a regulated public utility to begin to offer service in an additional territory and to acquire property used and useful in the public service, as is requested in this application. 66 Pa. C.S. § 1102(a)(1), (3). The statutory standard for the Commission's review of the application is set forth in Section 1103, which states:

A certificate of public convenience shall be granted by order of the commission, only if the commission shall find or determine that the granting of such certificate is necessary or proper for the service, accommodation, convenience, or safety of the public.

66 Pa. C.S. § 1103. The seminal case addressing the Commission's review under Section 1103 is *City of York*, where the Pennsylvania Supreme Court addressed a proposed merger of three telephone companies. The Court specifically cited Section 203, the predecessor statute to Section 1103, and set forth the standard as follows:

Section [1103] of the Public Utility Law requires that those seeking approval of a utility merger demonstrate more than the mere absence of any adverse effect upon the public. Section [1103] requires that the proponents of a merger demonstrate that the merger will affirmatively promote the "service, accommodation, convenience, or safety of the public" in some substantial way.

City of York at 828 (quoted in *Application of Pennsylvania-American Water Co.*, Docket No. A-2016-2537209, Order at 11 (Oct. 19, 2016)). This is the standard by which all acquisitions of Pennsylvania utility companies must be judged.

This standard was addressed by the Commonwealth Court in *Middletown Township v. Pa. PUC*, 482 A.2d 674 (Pa. Cmwlth. Ct. 1984) (*Middletown*). In *Middletown*, to acquire part of the

facilities of the Newtown Artesian Water Company, Middletown Township filed an application for a Certificate of Public Convenience. The Commission adopted the ALJ's determination that the acquisition would be a benefit to some customers but would have an adverse impact on other customers and, thus, it denied the application. *Id.* at 679. The Township appealed and, in hearing the appeal, the Commonwealth Court considered the *City of York* standard applicable through Section 1102 and Section 1103. The Court affirmed the Commission's decision rejecting the application stating, *inter alia*, that "when the 'public interest' is considered, it is contemplated that the benefits and detriments of the acquisition be measured as they impact on all affected parties, and not merely on one particular group or geographic subdivision as might have occurred in this case." *Id.* at 682 (emphasis in original). The Court added that "the primary objective of the law in this area is to serve the interests of the public." *Id.*; *see also Popowsky v. Pa. PUC*, 937 A.2d 1040 (Pa. 2007).

An acquisition provides an affirmative benefit if the benefits of the transaction outweigh the adverse impacts of that transaction. *Application of CMV Sewage Co., Inc.*, 2008 PaPUC LEXIS 950, *30 (*CMV*). To determine whether benefits meet this standard, the Commission may consider: "(1) the legal and technical fitness of the purchasing entity to provide service; (2) the public need for service; (3) the inadequacy of the existing service; and (4) any other relevant evidence." *Application of North Heidelberg Water Co.*, 2010 PaPUC LEXIS 919, *20.

This application fails to meet the appropriate legal standard, whether calculated at the \$54.93 million rate base proposed by Aqua or the \$46.5 million rate base calculated by OCA, because it would harm existing and acquired ratepayers and would not provide substantial affirmative public benefit. As discussed below, the benefits identified by Aqua are mere generalizations that do not address the corresponding harm to existing Aqua wastewater and water

customers, and to the East Whiteland customers after acquisition. For this reason and to serve the public interest, the Commission should deny the application.

2. Fitness

The OCA did not present any evidence regarding Aqua's fitness.

3. Substantial Affirmative Public Benefits

To approve the application, the Commission must determine that there are affirmative public benefits. As an integral part of that review the Commission must fully consider the harms of this acquisition on three specific groups with respect to the traditional *City of York* affirmative public benefits test: (1) the existing Aqua wastewater customers, (2) the existing Aqua water customers – who may potentially bear costs of the East Whiteland system, if the Commission permits costs to be shifted under 66 Pa. C.S. § 1311(c), and (3) the existing East Whiteland Township customers who will be transferred to Aqua. *City of York* at 828.

In its review of the Commission's approval of Aqua's acquisition of the New Garden system, the Commonwealth Court determined that the Commission is required to consider the rate impact in Section 1329 fair market value acquisitions in order to determine if there is a substantial public benefit, as required under Section 1102. The Commonwealth Court stated as follows:

Simply, by approving the sale and then putting off the consideration of the impact on rates to a later rate base proceeding, the Commission cannot do the balancing test required by Section 1102 of the Code to weigh all the factors for and against the transaction, including the impact on rates, to determine if there is a substantial public benefit. It is in this proceeding that the Commission is charged with deciding whether the impact on rates based on the OCA's undisputed evidence was outweighed by the other positive factors that the acquisition served a substantial public benefit. Because it did not do so, this matter is remanded to the Commission to make that determination, including the propriety of the rate restriction on New Garden ratepayers set forth in the APA.

McCloskey v. Pa. PUC, 195 A.3d 1055, 1067 (Pa. Cmwlt. Ct. 2018) (*New Garden Appeal*).

It is well-established that the Township's balance sheet will benefit from the proposed transaction. As proposed, East Whiteland Township will receive \$54.93 million or 64% more than the net book value³ of the system. OCA St. 2 at 9. Aqua anticipates spending \$16.92 million for capital improvements to the East Whiteland system during the next 10 years. *Id.* at 6.

There is, however, no support for concluding that existing Aqua wastewater and water customers will receive any net benefit or that the East Whiteland customers will see a net benefit after the East Whiteland rate freeze ends. To the contrary, the record shows that customers will experience substantial harm that is outweighed by any purported benefits. As such, Aqua has failed to demonstrate the necessary public benefits required for approval of this Application.

a. Harm to Existing Aqua Wastewater and Water Customers

Aqua claims that its existing wastewater customers will benefit from the proposed transaction because, at some unknown time in the future, customers will benefit from regionalization and consolidation. OCA St. 2 at 2. Aqua has not provided any evidence that shows when, or if, existing customers will see the benefit that Aqua claims will arrive at some time in the future. What is certain is that the acquisition will increase rates for customers in the short term.

The proposed ratemaking rate base and planned system investment in conjunction with the current level of East Whiteland rates means the system will not generate revenue sufficient to cover its cost of service under Aqua ownership. Aqua calculates that the acquisition would create an **annual** revenue deficiency of \$5.011 million that will be recovered from either Aqua's existing customers, East Whiteland customers, or both. OCA St. 2 at 3; Aqua St. 1, App. A. As Aqua has structured the transaction, its existing water customers are also at risk for supporting the costs of

³ Book value under Section 1329 does not reflect an offset for contributed plant or capital as is done in ratemaking. 66 Pa. C.S. § 1329(d)(5). The net book value of the Township's assets is \$33.4 million. OCA St. 2 at 9.

acquiring the East Whiteland customers because Aqua will seek approval under 66 Pa. C.S. § 1311(c) to allocate a portion of its wastewater revenue requirement to the combined water and wastewater customer base. It must be recognized that every other Aqua water customer already must pay for wastewater disposal either to another provider, to Aqua, or with their individual wastewater system.

Aqua estimates that recovering 50% of the East Whiteland revenue deficiency from Aqua wastewater customers would increase its wastewater customers' monthly rates by \$4.62 or 4.67%. *Id.* Aqua also provides a calculation of an assignment to its water customers under Section 1311(c) and under that scenario, the existing Aqua water customers would be allocated about 44% of the total East Whiteland revenue deficiency. *Id.* This would result in an estimated increase of \$0.33 per month or 0.41% for existing residential water customers.⁴ *Id.*

Regarding the certain rate increase to existing Aqua customers, this proposed transaction is not occurring in a vacuum. Aqua has other Section 1329 acquisitions pending or approved since its last base rate case, like Willistown Township, Lower Makefield Township and DELCORA, for which it also projects revenue requirement deficiencies that would put upward pressure on rates for acquired or existing customers in the short term and push the timing for customers to realize any benefits from cost sharing further into the future.⁵

Aqua proposes a three year rate freeze for Township customers in its application. OCA St. 2 at 4. Under Section 1329, a rate stabilization plan is defined as “[a] plan that will hold rates

⁴ Here, Aqua assumed that, instead of Aqua wastewater customers paying \$2,505,000 of the revenue deficiency, about 88% of that amount (\$2,505,000) would be shifted to Aqua water customers. OCA St. 2 at 3. The actual percentage of any shift of revenue requirement from wastewater to water customers will be determined in the next rate case. As such, the rates for existing wastewater or water customers could be different than estimated. *Id.* at 3-4.

⁵ See *Application of Aqua Pennsylvania Wastewater, Inc.*, Docket No. A-2021-3027268 (*Willistown Township*); *Application of Aqua Pennsylvania Wastewater, Inc.*, Docket No. A-2021-3024267 (*Lower Makefield Township*); *Application of Aqua Pennsylvania Wastewater, Inc.*, Docket No. A-2019-3015173 (*DELCORA*).

constant or phase rates in over a period of time after the next base rate case.” 66 Pa. C.S. § 1329. It is not known whether Aqua will file a base rate case within three years of closing. Aqua’s proposal to freeze rates for the East Whiteland customers for three years after closing is, thus, a rate stabilization plan because it has the potential to hold rates constant or phase rates in over a period of time after its next base rate case.

The Commission has required that “if a rate stabilization is proposed, the applicant will be required to provide testimony, schedules, and work papers that establish the basis for the plan and its impact on existing customers who need to cover the revenue requirement that would be shifted to them under the plan.” *Implementation of Section 1329 of the Public Utility Code*, Docket No. M-2016-2543193, Final Implementation Order at 27 (Oct. 27, 2016). No such plan was provided in this proceeding. This has the effect of depriving the Commission and the parties the ability to fully evaluate the benefits and harms of the proposed transaction. OCA St. 2 at 5. The OCA notes that Aqua has provided this type of information in a previous Section 1329 application where a rate freeze was proposed. *Id.* Its failure to do so in this proceeding was not adequately explained by Aqua.

Whether or not the Commission finds that the rate freeze is a rate stabilization plan, the Commission should not approve a rate freeze that attempts to remove the Commission’s discretion in setting rates and should reject any rate freeze for East Whiteland customers that extends beyond the effective date of new rates in Aqua’s next base rate case. This would help to protect existing Aqua customers from covering the revenue deficiency. OCA St. 2 at 4. If the East Whiteland acquisition is approved, existing Aqua customers would already be at risk to cover the revenue requirement required to keep East Whiteland rates lower than cost. They should not also have to

subsidize the revenue requirement required to keep East Whiteland rates lower than the new rates established for East Whiteland in a base rate case.

For all these reasons, Mr. Eastman concluded that the proposed transaction is neither fair to customers nor consistent with principles of cost-based ratemaking. The terms of the transaction would harm Aqua's existing customers and provide nothing other than speculative benefit at some unknown point in the future.

b. Harm to East Whiteland Customers

The record also demonstrates that East Whiteland customers not will affirmatively benefit from the proposed transaction. As discussed above, during the first three years post-acquisition, Aqua proposes to freeze rates for Township customers and continue to charge East Whiteland customers their present sewer rate of approximately \$33 per month. APA, ¶ 7.03(a); OCA St. 2 at 3. At the conclusion of the rate freeze, however, Aqua projects those rates would need to be increased by an additional \$77.64 per month, or by **132.93%**, if the entire revenue deficiency is applied to East Whiteland rates. OCA St. 2 at 3. Thus, East Whiteland customers will experience significant rate increases if the system is acquired by Aqua. Even if East Whiteland customers bear only 50% of the revenue requirement related to the Aqua-proposed ratemaking rate base, East Whiteland customers would see rates increased by 66.47%. *See* Aqua St. 1, App. A. In that scenario, Aqua's existing wastewater and water customers would subsidize the remaining revenue requirement.

If the rate freeze extends beyond Aqua's next base rate proceeding, the East Whiteland rates will fall behind the increased rates for Aqua's existing water and wastewater customers, further exacerbating the amount of the subsidy going forward. OCA St. 2 at 4. To catch up,

Township customers will see higher rate increases than currently forecasted in order to move towards the rates of the main rate zone and their cost of service. *Id.* at 5-6.

There has also been public opposition to the acquisition, as evidenced by the individuals who provided testimony at the public input hearing as to the harms that may occur. For example, Mr. Gilbert testified that East Whiteland has provided safe and adequate service for decades and that ratepayers were not asked if the wastewater system should be sold. Tr. 50-52. Mr. Fasano similarly expressed his concern that Aqua would significantly increase the cost of sewer management over time for East Whiteland homeowners. Tr. 59. Ms. Frissora, Ms. Arranz and Mr. Gage testified as to their concerns as Aqua water customers that their water rates will increase because of the sale of East Whiteland's wastewater system to Aqua. Tr. 45-48, 55, 65. Additionally, Ms. Frissora noted that East Whiteland is already regionalized as sewage from East Whiteland's collection system is already treated at the Valley Forge Sewer Authority regional treatment plant. Tr. 47.

c. The Adverse Impacts on Aqua's Existing Customers and the East Whiteland Customers Outweigh the Claimed Benefits of the Proposed Transaction.

In the *CMV* case discussed above, the Commission concluded that the adverse impacts of the proposed transaction for the existing customers outweighed the benefits. *CMV* at *30. The customers proposed to be acquired were currently receiving service from a system that complied with applicable environmental laws and regulations. While the *CMV* system might have required upgrades to comply with stricter environmental requirements at an unknown future date, there was no certain evidence on that point. The Commission stated:

The advantages alleged by NCTSA do not outweigh the certain, immediate adverse impacts of this transaction. The proposed transaction will result in an immediate \$1,800 cost for Colonial Crossings customers, which is in addition to an average rate increase of approximately \$70 per quarter, or 54% compared to existing rates.

We find that the ALJ correctly weighed the evidence before him, and concluded that the costs of the proposed transaction for the Colonial Crossings customers outweigh the benefits for those customers.

Id. As in *CMV*, the alleged benefits of acquiring the East Whiteland system are disputed and the adverse impacts of the proposed acquisition outweigh any claimed benefits.⁶

Although Aqua references economies of scale, the Company has not provided any showing of cost reductions or efficiencies that will be produced by the acquisition of the East Whiteland customers. OCA St. 2 at 8. Additionally, the evidence of record shows that both Aqua's existing customers and East Whiteland's customers will likely experience rate increases if the proposed transaction is approved. Economies of scale exist "when a firm's average cost curve decreases as output increases." OCA St. 2 at 7 citing Charles F. Phillips, Jr., *The Regulation of Public Utilities: Theory and Practice*, p. 52. This can also be understood as a reduction in cost per unit of output as that output increases. OCA St. 2 at 7. Generally, for utilities, acquisitions produce economies of scale because fixed costs can be spread to more customers. However, since East Whiteland customers will not even be covering their full cost of ownership at the proposed \$54.93 million rate base, they will not share the costs of infrastructure improvements for other parts of Aqua's service territory until some unknown, speculative date in the future. Additionally, there has been no showing that economies of scale would make rates more affordable in the long-term. OCA St. 2 at 13. To the contrary, Aqua witness Packer calculates that the East Whiteland rate base per EDU is greater than the Aqua rate base per EDU. Aqua St. 1 at 17. Specifically, Aqua would pay \$200 more per EDU than its average cost per EDU of \$7,000, which means no reduction in total costs for providing service.

⁶ In *CMV*, the Commission was not persuaded that potential economies of scale provided a benefit that outweighed the known adverse impacts of the transaction. As the OCA pointed out in *CMV*, there is no guarantee that savings resulting from any economies of scale will be reflected in the rates charged to customers. *Id.* at *29-30.

Aqua claims that the acquisition will reduce the cost of capital investment; however, closer review invalidates this claim. Aqua estimates that capital investments in the East Whiteland system over 10 years, on a per customer basis, will be lower than Aqua's and will decrease the future per customer cost of capital investments for Aqua from \$5,111 per customer to \$5,050, or by \$61. *Id.* (citing Aqua response to OCA-IV-2). For existing Aqua customers, this decrease is small (\$61 over an entire decade) and fully negated by the rate increase of \$554.40 that Aqua projects for its wastewater customers for the same period. For East Whiteland customers, it means the per customer costs for capital investment will increase from \$4,344 to \$5,050 or by \$706. OCA St. 2 at 8. Again, either the existing Aqua customers or the acquired Township customers, or both, will pay increased rates because of this transaction.

Additionally, Aqua states that the current operating expenses of the Township are approximately \$2.8 million, and the Company projects operating expenses of \$2.0 million (\$800,000 less) under Aqua ownership. OCA St. 2 at 8. Viewed in isolation, this is a positive result for Township customers, but when coupled with the fact that the overall increase to costs under Aqua's ownership that will produce an annual revenue deficiency of \$5.011 million and increase rates for the acquired East Whiteland or existing Aqua customers, this positive result is completely negated. *Id.* at 9.

Further, the cost of ownership is significantly higher if the East Whiteland Township system is acquired by Aqua because those costs include nearly \$4 million for return to Aqua shareholders. OCA St. 2 at 9. There is no cost of equity for East Whiteland Township as its cost of capital is limited to repaying debts at a much lower interest rate (about 3.7%). *Id.* Aqua is required to pay taxes, whereas East Whiteland Township is not. *Id.* Additionally, the acquisition of East Whiteland is a Section 1329 acquisition, and as such, the entirety of the purchase price can

be incorporated into Aqua's rate base without recognizing offsets for contributed plant or capital, as is done in traditional ratemaking. There is no evidence of substantial cost savings or quantified efficiencies for this proposed acquisition that would offset Aqua's higher cost of ownership. In combination with all the other adverse financial impacts of the proposed acquisition, the known harms outweigh the claimed long-term and unsubstantiated benefits.

Moreover, the evidence does not support the claimed short-term benefits, such as Aqua's claim that East Whiteland customers will benefit from Aqua's 24/7/365 customer service is also not supported by record evidence. Sewer problems during normal business hours can be directed to the sewer department directly, while outside of normal business hours the police department will direct calls to the sewer department on-call staff. OCA St. 2 at 10. Again, at the public input hearing there was no indication that ratepayers had any concerns with East Whiteland's customer service. The Township already has the ability to address emergencies.

Aqua also argues that Chapter 14 of the Public Utility Code is an affirmative public benefit of the transaction. OCA St. 2 at 10. While the OCA acknowledges that protections provided by the Public Utility Code are a benefit, standing alone they are not sufficient to outweigh the harms. If the existence of Chapter 14 of the Public Utility Code were enough to satisfy the *City of York* standard for affirmative public benefits, any acquisition by an entity regulated by the Public Utility Commission would meet the standard.

The Township's testimony on the alleged affirmative public benefits also does not meet the *City of York* standard. Township witness Nagel claimed that there are two key benefits to the proposed transaction from the perspective of the Township and its residents:

1. Permit the Township to exit the business of providing sanitary sewer service and instead focus on its core governmental functions while simultaneously ensuring that our residents would have safe and reliable service at affordable rates, and;

2. The sale proceeds will allow the Township to address improvements and projects throughout the Township and benefit the Township's overall financial position.

OCA St. 2 at 12.

The alleged benefits that are claimed by Mr. Nagel would occur under any sale of any system by a municipality to Aqua. The proposed transaction, however, must affirmatively promote the service, accommodation, convenience or safety of the public in some substantial way. It must reflect benefits to the ratepayers of Pennsylvania that are substantial, and the various risks and harms that could result from the acquisition must be mitigated.

There is no evidence that the sale would provide an affirmative public benefit by ensuring that East Whiteland customers have safe and reliable service any more so than they have under the current East Whiteland Township ownership. East Whiteland is not a troubled system. Indeed, based on the information provided by Aqua and the Township, the current service provided by the Township is safe and reliable. *See* East Whiteland St. 3R at 3; OCA St. 2SR at 9. This is uncontroverted.

Aqua acknowledged that the Township's system has the capacity to meet the demands of current and future customers, does not have any sanitary system overflows in 2020, and is not currently under a Corrective Action Plan or Connection Management Plan with DEP. *See* Aqua St. 2 at 14; OCA St. 2 at 14. Simply put, the Township is already providing service that is at least as safe and reliable as the service that Aqua provides, and the continuation of safe and reliable service is not an affirmative public benefit.

The evidence shows that the Township is financially fit to complete any necessary improvements and upgrades given that it has cash and cash equivalents exceeding \$29 million. OCA St. 2 at 6. In the year 2020 alone, the Sewer Fund had an increase to cash and cash equivalents of more than \$500,000. *Id.*; Aqua Exh. J2 at 42. While Aqua currently estimates that

it will invest approximately \$16.92 million in capital improvements over the next 10 years, the evidence regarding East Whitefield's financial position indicates the Township could make necessary improvements and upgrades to the system, equal to what Aqua has proposed, and it would not present an unreasonable financial burden for the Township. OCA St. 2 at 6. Thus, there is no showing that acquisition by Aqua would improve current or future service received by East Whiteland customers or that the Township is not currently or would not in the future be able to continue its current level of service.

In summary, the record does not bear out Aqua's contention that East Whiteland customers will receive a benefit that outweighs the detriment of dramatically increased rates. The proposed transaction would produce a revenue deficiency that would increase East Whiteland rates by more than **132%** if applied to those customers, more than double their current sewer rates. OCA St. 2 at 13. To the extent that East Whiteland rates are not increased to cover their cost of service, then existing Aqua customers will make up the difference in the rates they pay for service. *Id.* Even if the East Whiteland customers were to simply experience rate increases that would bring them close to Aqua's current rate zone 1 rates, Township customers would see their rates go up by more than 60%.⁷ OCA St. 2 at 11. Rates and overall costs for existing Aqua customers would also increase. OCA St. 2 at 11. Moreover, the evidence shows that East Whiteland customers will receive no meaningful change in service from the transfer of ownership.

4. Conclusion

The averred benefits of Aqua acquiring the East Whiteland system are vague and unquantified. The harms are known and significant. The Joint Applicants have failed to show that

⁷ The current monthly bill for an average Aqua residential wastewater customer using 3,020 gallons per month (Aqua Exhibit I1, pg. 2) with a \$31 customer charge is \$53.95 ($\$31 + (\$7.60 \times 3.02)$) (Aqua Tariff Sewer-Pa P.U.C. No. 2, pg. 8.1 (rate zone 1)). Aqua has requested to increase those rates effective May 2022 (R-2021-3027386).

the proposed transaction would result in any substantial, affirmative public benefits to Aqua's existing water and wastewater customers or the acquired East Whiteland customers. The OCA submits, therefore, that the Commission must deny the Application.

B. Section 1329

1. Introduction

Section 1329 was enacted in April 2016 and became effective on June 29, 2016. Act 2016-12 (HB 1326). Section 1329 provides, *inter alia*, that when a regulated water or wastewater utility acquires a municipal water or wastewater provider, the regulated utility can ask for ratemaking treatment of the acquired utility's assets using fair market value. 66 Pa. C.S. § 1329. As set forth in Section 1329(a) and (b), the process for determining the fair market value is based on two separate appraisals, each using the Cost, Market, and Income approaches. 66 Pa. C.S. §§ 1329(a)(3), (b). The appraisals are then averaged to determine the fair market value, 66 Pa. C.S. § 1329(g), and the lesser of the purchase price or the fair market value is what the acquiring utility will present as the proposed rate base. 66 Pa. C.S. § 1329(c)(2). This is not a simple mathematical exercise. The appraisals reflect the judgments and choices made by each utility valuation expert as will be discussed below.

In this proceeding, the two appraisal values for the East Whiteland Township assets were \$55.7 million (Gannett Fleming) and \$57.8 million (AUS Consultants). OCA St. 1 at 2; Aqua Exh. X at 13; Aqua Exh. Y at 3. The average of these two appraisals is \$56.7 million. Aqua and the Township have negotiated a purchase price of \$54,930,000. OCA St. 1 at 2. As discussed below, Aqua's proposed rate base is overstated due to errors, flaws, and unreasonable subjectivity by the UVEs making the appraisals. If the Commission approves the proposed acquisition, the

correct ratemaking rate base amount is \$46,500,000 for the Township’s system. OCA St. 1 at 6 and 46; OCA Exh. DJG-2.

2. Legal Principles

As discussed above, pursuant to Section 1329, upon agreement by the acquiring public utility and the selling entity, “two utility valuation experts shall perform two separate appraisals of the selling utility for the purpose of establishing its fair market value” and each “shall determine fair market value” in compliance with the Uniform Standards of Professional Appraisal Practice (USPAP) based on the Cost, Market, and Income approaches. 66 Pa. C.S. § 1329(a). “The ratemaking base shall be the lesser of the purchase price negotiated by the acquiring public utility . . . and selling utility or the fair market value of the selling utility.” 66 Pa. C.S. § 1329(c)(2).

The Applicant must provide to the Commission copies of the appraisals, the purchase price, the ratemaking rate base, the closing costs, and, if applicable, a tariff and rate stabilization plan. 66 Pa. C.S. § 1329(d)(1). Regardless of whether the Applicant meets the requirements of Section 1329, the Applicant also has the burden of proving that it satisfies the requirements of Sections 1102 and Section 1103 of the Public Utility Code as well. *See New Garden Appeal* at 1064 (citing *City of York*); 66 Pa. C.S. §§ 1102, 1103. Moreover, the Commission has determined that UVEs are required to apply jurisdictional exceptions under the valuation approaches, to establish appropriate guidelines and consistent assumptions for Section 1329 Fair Market Value appraisals, to comply with Commission precedent, and to reduce variances in the appraisals for the same property. *Application of Aqua Pennsylvania Wastewater, Inc.*, Docket No. A-2019-3008491, Order at 6-7 (Nov. 5, 2019) (*Cheltenham*).

3. Aqua's Application

The Company and the Township commissioned FMV appraisals from Gannett Fleming and AUS Consultants. Harold Walker, III of Gannett Fleming estimated an FMV of \$55.7 million for the East Whiteland wastewater system assets and Jerome C. Weinert of AUS Consultants estimated an FMV of \$57.8 million. Aqua Exh. X at 13; Aqua Exh. Y at 3. Gannett Fleming and AUS Consultants provided these appraisals using the Cost, Income, and Market approaches, as set forth in Section 1329(a)(3).

Gannett Fleming's appraisals are summarized as follows:

Approach	Base Value	Weight	Weighted Value
Market	\$ 46,741,589	33.3%	\$ 15,583,646
Cost	59,118,924	33.3%	19,704,337
Income	61,147,544	33.3%	20,380,476
Total			\$ 55,668,460

OCA St. 1 at 3.

AUS Consultants appraisals are summarized as follows:

Approach	Base Value	Weight	Weighted Value
Market	\$ 56,178,539	10.0%	\$ 5,617,854
Cost	59,847,171	50.0%	29,923,586
Income	55,600,045	40.0%	22,240,018
Total			\$ 57,781,457

Id.

These estimates are influenced by several unreasonable assumptions. As the above tables show, Gannett Fleming and AUS Consultants apply different weightings to each approach, indicating that judgment plays a role in the UVEs determinations about the FMV of the Township's

assets. Both UVEs used the same three approaches to calculate FMV, and both came up with different results overall and under each individual approach. OCA St. 1 at 4. As such, the OCA submits that the Commission should carefully consider the assumptions informing each UVE’s appraisal results, the flaws in those assumptions that are identified in the OCA’s testimony, and the Commission should accept the adjustments proposed by the OCA to more properly reflect financial and ratemaking principles.

OCA witness Garrett calculated that with the appropriate adjustments discussed below, the adjusted Gannett Fleming appraisal result would be \$45.7 million, and the adjusted AUS Consultants appraisal would be \$47.2 million. OCA St. 1 at 6; OCA Exh. DJG-2. The average of these two appraisal results is \$46.5 million, which is the amount that Mr. Garrett recommends be used by the Commission for establishing rate base under Section 1329 rather than the \$54.9 million proposed by Aqua. *Id.* These recommendations are summarized in the following chart:

OCA’s Recommended Rate Base:

	Appraiser Results	OCA Adjusted
Gannett Fleming	\$ 55,668,460	\$ 45,748,213
AUS Consultants	57,781,457	47,200,091
Average	\$ 56,724,958	\$ 46,500,000
Purchase Price	\$ 54,930,000	\$ 54,930,000
Proposed Ratebase	\$ 54,930,000	\$ 46,500,000

OCA St. 1 at 6.

4. Challenges to UVE Appraisals

The issue of whether parties can challenge Utility Valuation Expert (UVE) appraisals has already been decided by the Commission. The Commission found that “Section 1329 permits the Commission and the Parties to develop a record pertaining to the review and analysis of the fair

market value appraisals of the UVEs.” *Application of Aqua Pennsylvania Wastewater, Inc.*, Docket No. A-2016-2580061, Order at 35 (June 29, 2017) (internal citations omitted) (*New Garden*). The ratemaking approvals of Section 1329 must be reconciled with the requirement of Section 1301 of the Public Utility Code, 66 Pa. C.S. § 1301, requiring each rate to be just and reasonable and the requirements of Section 1102 that acquisitions provide substantial affirmative benefits.

In a subsequent Section 1329 proceeding, the Commission reiterated that Section 1329 contains no prohibitions on the ability of parties to review the UVE appraisals as to their reasonableness and stated as follows:

We agree that Section 1329 does not prevent a review of the UVE assumptions for reasonableness, and for the reasons discussed below, we find that the ALJ appropriately considered several of the recommendations to the fair market appraisals of the Limerick system.

Application of Aqua Pennsylvania Wastewater, Inc., Docket No. A-2017-2605434, Order at 36 (Nov. 29, 2017) (*Limerick*). Thus, it would be inconsistent with the requirements of the Public Utility Code and prior Commission orders to permit Aqua to simply present a rate base number, show that the appraisers chose numbers to fill in all the blanks in the formulas, and not permit any review or challenges of those inputs.

a. Cost Approach

Under the Cost Approach, appraisers consider direct and indirect costs associated with reproduction or replacement of plant assets, as well as any loss of value due to functional or economic obsolescence or reduced life expectancy.⁸ The American Society of Appraisers, *ASA Business Valuation Standards* at 20. In this case Gannett Fleming’s appraisal under the cost

⁸ https://www.appraisers.org/docs/default-source/5---standards/bv-standards-feb-2022.pdf?sfvrsn=5c9e5ac0_3 (last accessed Mar. 9, 2022).

approach relied on the reproduction cost method, and AUS Consultant's appraisal relied on the replacement cost method. Aqua Exh. X at 16; Aqua Exh. Y at 6. Both UVEs estimated accumulated depreciation as a reduction to their respective cost estimates, also known as depreciation "reserve." *Id.*; OCA St. 1 at 14. To arrive at their respective depreciation reserve estimates, both Mr. Walker for Gannett Fleming and Mr. Weinert for AUS Consultants relied in part on Iowa curves to estimate the remaining lives of the Township's depreciable accounts. OCA St. 1 at 14. While the OCA is not proposing adjustments to either UVE's estimates for replacement or reproduction cost, the OCA does propose several adjustments to the depreciation parameters assumed by the UVEs. *Id.*

i. Iowa Curves

When utilities have records about asset placements and retirements by vintage year, depreciation experts can analyze the historic retirement patterns in each account to estimate depreciation rates. OCA St. 1 at 14. Depreciation experts most commonly use the retirement rate method to conduct this analysis. *Id.* at 14-15. This method involves displaying historical retirement patterns graphically in the form of original survival curves, and depreciation experts then use visual and mathematical curve fitting techniques and their own personal judgement to select an Iowa curve that best fits the original survival curve. *Id.* at 15. The Iowa curve that the expert ultimately selects is then used to calculate the average remaining life and depreciation rate for each account. *Id.*; OCA St. 1, App. A (providing a detailed explanation of Iowa curves).

In this case, the Township did not have the requisite records about asset placements and retirements by vintage year for the UVEs to conduct a more objective, empirical analysis when selecting the most appropriate Iowa curve and remaining life. OCA St. 1 at 15. The UVEs still chose to use Iowa curves to estimate the average remaining life and accumulated depreciation of

the Township's assets, and relied on their subjective judgment to determine which Iowa curves were the best fit. *Id.* For example, Mr. Weinert selected a best-fitting Iowa curve based on AUS Consultant's "experience in preparing depreciation studies for the water and wastewater industry...." Aqua Exh. Y at 9. Mr. Walker similarly selected a best-fitting Iowa curve "based on [Gannett Fleming's] experience...." Aqua Exh. X at 18. Thus, both UVEs primarily relied on subjective factors, such as "experience," in support of their proposed service lives, without company-specific empirical support.

Like the UVEs, Mr. Garrett's used his experience to develop recommended service lives for East Whiteland assets from depreciation studies for other utilities. OCA St. 1 at 20-23. Unlike the UVEs, however, Mr. Garrett's recognizes that the lack of utility-specific actuarial data is best represented by life estimates that are more conservative and, thus, more reasonable. OCA St. 1SR at 10-11. As discussed below, the OCA proposed adjustments to the Iowa curves used by Gannett Fleming and AUS Consultants in the following accounts: Accounts 354 (Structures and Improvements), 360 (Collection Sewers – Force Mains), 361 (Collection Sewers – Gravity Mains), and 363 (Services to Customers).

ii. Gannett Fleming's Cost Approach

To reach his conclusion about the valuation of the Township's assets under the cost approach valuation, Mr. Walker used the replacement cost method which involved estimating accrued depreciation using his subjectively selected Iowa curves, and then subtracting that depreciation from estimated reproduction cost to reach an FMV appraisal of \$59.1 million. OCA St. 1 at 18; OCA Exh. DJG-6. Mr. Walker also conducted a FMV analysis using the original cost method. The original cost method estimates the cost of the assets in question when those assets were "new" or first constructed, based on information contained in the Engineering Assessment.

Aqua Exh. X at 14. Mr. Walker's analysis under the original cost method produced an indicated value of \$33 million. OCA St. 1 at 18; Aqua Exh. Q at 24. Mr. Walker inexplicably excluded his analysis under the original cost method from his recommended FMV under the cost approach, and instead only proposed the \$59.1 million valuation from the replacement cost method. OCA St. 1 at 18-19. Still, Mr. Walker notes, and the OCA agrees, that the original cost method can "provide meaningful metric to evaluate the reasonableness of other indications of value produced by other valuation methods." Aqua Exh. Q at 26; OCA St. 1 at 18-19. For that reason, the OCA used Mr. Walker's original cost method as part of its adjustment to Mr. Walker's FMV proposal under the cost approach. OCA St. 1 at 19.

Given that FMV result of the original cost method is more comparable to the FMV results of the various other approaches being used to estimate the value of the East Whiteland system, in this case Mr. Garrett based his adjustments on Mr. Walker's cost approach valuation on replacement cost. OCA St. 1 at 18-19. Further, the OCA did not proposed adjustments to Mr. Walker's replacement cost estimates in this case. Instead, the OCA's proposed adjustments to the service lives for certain accounts impact accumulated depreciation and result in a FMV of \$56.3 million, which is about \$2.8 million less than Mr. Walker's proposed cost approach valuation of \$59.1 million. OCA St. 1 at 22; OCA Exh. DJG-2.

The OCA's adjustments to Mr. Walker's Iowa Curve calculations are outlined in the following table and summarized below:

Proposed Iowa Curve and Accrued Depreciation Adjustments:

Account	Description	Gannett Fleming Position		OCA Adjustments	
		Iowa Curve	Accrued Depreciation	Iowa Curve	Accrued Depreciation
354.30	STRUCTURES AND IMPROVEMENTS - PUMPING	60-R3	2,769,664	45-R3	3,478,958
354.40	STRUCTURES AND IMPROVEMENTS - TREATMENT	65-R2.5	1,392,486	55-R2.5	1,553,425
360.10	COLLECTION SEWERS - FORCE - MAINS	70-R2.5	2,493,840	60-R2.5	2,821,192
361.10	COLLECTION SEWERS - GRAVITY - MAINS	65-R2.5	15,386,808	60-R2.5	16,282,307
363.20	SERVICES TO CUSTOMERS	55-R2.5	4,368,034	45-R2.5	5,055,324

OCA St. 1 at 20.

First the OCA recommends using service lives of 45 and 55 years for the Township’s pumping and treatment structures and improvements accounts, respectively. *Id.* The curves proposed by OCA witness Garrett for these accounts are the same as those proposed by Mr. Weinert of AUS Consultants, and they are consistent with Mr. Garrett’s proposed Iowa curves for these accounts in prior Section 1329 proceedings. *Id.* For the force and gravity collection mains accounts, the OCA proposes a 60-year average life, just as Gannett Fleming proposed for those accounts in a wastewater case in front of the Indiana Utility Commission.⁹ *Id.* Finally, the OCA recommends using a 45-R3 curve for the Account 363.20 (Services) to estimate a reasonable range for that account. OCA St. 1 at 20.

Mr. Walker criticizes OCA witness Garrett’s proposed Iowa curves as being inconsistent with Iowa curves that he has proposed in other cases. Aqua St. 4R at 8-9. As OCA witness Garrett notes, the utilities in the cases referenced by Mr. Walker produced far more historical retirement data to support their proposed service lives than Aqua or the Township has produced in this case. OCA St. 1SR at 9. The Iowa curves proposed by the OCA here are the most reasonable given the

⁹ See OUCC Prefiled Testimony of David J. Garrett – Public’s Exhibit No. 1, filed June 22, 2018 in Cause No. 45039 before the Indiana Utility Regulation Commission, at <http://www.resolveuc.com/representative-engagements>.

lack of historical retirement data that the Township has available. *Id.* As such, it appears that neither of the UVEs in this case performed the type of statistical analysis that Mr. Walker references. OCA St. 1SR at 9. Further, Mr. Walker and Mr. Weinert proposed different Iowa curves and service lives under their respective cost approaches, highlighting that experts frequently have different opinions regarding the appropriate service lives for calculating FMV under Section 1329.

After making the adjustments outlined in the above table, OCA witness Garrett used the same process as Mr. Walker to calculate depreciation, with the only difference being that Mr. Garrett used shorter Iowa curves and thus came to a lower cost approach estimate. OCA St. 1 at 21. Applying Mr. Garrett's proposed Iowa curves and accrued depreciation, the OCA recommends an adjusted cost approach valuation of \$56.3 million, which is about \$2.8 million less than Mr. Walker's proposed cost approach valuation of \$59.1 million. *Id.* at 22.

iii. AUS Consultant's Cost Approach

Mr. Weinert of AUS Consultants used the replacement cost method to determine a FMV for the East Whiteland system under the cost approach valuation. OCA St. 1 at 23. Mr. Weinert also estimated accrued depreciation to calculate "replacement cost less depreciation" values for each account. *Id.*

The OCA's recommended adjustments to AUS Consultant's proposals are based on using the same average service lives that the OCA recommended in its adjustments to the Gannett Fleming cost approach. *Id.* These adjustments are summarized as follows:

Proposed Iowa Curve Adjustments to AUS Consultants:

Account	Description	AUS Iowa Curve	OCA Iowa Curve
360.21	COLLECTION SEWERS - FORCE - MAINS	75-R3	60-R3
361.21	COLLECTION SEWERS - GRAVITY - MAINS	80-R2.5	60-R2.5
361.23	COLLECTION SEWERS - GRAVITY - MANHOLES	80-R2.5	60-R2.5

Id.

Mr. Weinert disagrees with many of the OCA’s proposed service lives. Aqua St. 5R at 8-12. In support of his own recommendations, Mr. Weinert relies on the Gannett Fleming depreciation studies for Aqua Pennsylvania, Inc. and Pennsylvania American Water Company (PAWC). OCA St. 1SR at 10. This is problematic for several reasons. First, these depreciation studies were not conducted on the assets at issue in this proceeding. *Id.* Second, Mr. Weinert notes that his service life proposals in this case are similar to those proposed by Gannett Fleming in *other cases*, but Mr. Weinert does not explain the discrepancy between his and Gannett Fleming’s proposed service lives in *this case*. *Id.*

Mr. Weinert also asserts that OCA witness Garrett failed to support the service lives that he proposed in this proceeding with data specific to the East Whiteland assets, but he fails to recognize that he too based his proposed service lives on data obtained from other cases. OCA St. 1SR at 10-11. Since the Township does not maintain the requisite data for a utility-specific actuarial analysis, a comparative analysis is the only way to calculate these proposed service lives, and so that is what *both* Mr. Garrett and Mr. Weinert did. *Id.* Mr. Weinert contends that his comparative analysis is more credible than Mr. Garrett’s because it relies on the most recent depreciation studies conducted by Aqua and PAWC, but this argument only highlights that similar data was not available about the Township’s assets in this case. Aqua St. 5R at 12; OCA St. 1SR at 10-11. Therefore, both Mr. Weinert and Mr. Garrett used their own judgment to evaluate the

appropriate service lives for various accounts of the Township. OCA St. 1SR at 10-11. The only material difference between the two analyses is that Mr. Garrett's average estimates assumed shorter lives than those proposed by AUS Consultants, and consequently Mr. Garrett estimated a lower FMV under the cost approach than AUS Consultants. OCA St. 1SR at 11-12. Mr. Weinert's comparative analysis is not more correct than Mr. Garrett's simply because it results in a higher FMV. Rather, Mr. Garrett's comparative analysis should be adopted because it is more conservative. In this case, the longer life estimates used by the UVEs and resulting increase to FMV are not reasonable in the absence of utility-specific actuarial data to provide empirical support.

Based on the above adjustments, the OCA's calculation for Renewed Cost New Less Depreciation (RCNLD) came to approximately \$53.1 million, which is about \$6.7 million less than AUS Consultants' calculation of \$59.8 million. OCA St. 1 at 24; OCA Exh. DJG-12. Using this lower RCNLD and Mr. Garrett's proposed Iowa curves and accrued depreciation adjustments discussed above, the OCA calculated a cost approach valuation of \$53.1 million for the East Whiteland system, which is about \$6.7 million less than AUS Consultant's proposed cost approach valuation of \$59.8 million. OCA St. 1 at 24; OCA Exhs. DJG-12, DJG-13.

b. Market Approach

The Market Approach, also called the Sales Comparison Approach by The American Society of Appraisers, is "a general way of determining a value indication...by using one or more methods that compare the subject to similar businesses [or assets] that have been sold."¹⁰ The American Society of Appraisers, *ASA Business Valuation Standards* at 12. To evaluate whether a

¹⁰ https://www.appraisers.org/docs/default-source/5---standards/bv-standards-feb-2022.pdf?sfvrsn=5c9e5ac0_3 (last accessed Mar. 9, 2022).

reasonable basis for comparison exists, the American Society of Appraisers recommends considering whether the assets in question have similar qualitative and quantitative characteristics and whether there is a comparable amount of data known about each asset. *Id.* As described below, both Gannett Fleming and AUS Consultants used incomparable transactions to the proposed acquisition in this case to calculate the FMV of the East Whiteland System under the Market Approach, causing both UVEs to arrive at unreasonably high values.

i. Gannett Fleming Market Approach

Gannett Fleming estimated a market approach valuation of \$46.7 million for the East Whiteland system assets and AUS Consultants estimated a market approach valuation of \$56.1 million. Aqua Exh. X at 13; Aqua Exh. Y at 3. Aqua witness Walker used the Market Multiples Method and the Selected Transactions method in his market approach valuation. Aqua Exh. X at 13. Mr. Walker’s Selected Transactions method estimated the value of the Township’s system using financial and demographic statistics from other acquired systems. *Id.* Specifically, Mr. Walker used investor capital statistics, gross property statistics, and plant and equipment (PP&E) statistics from other acquired systems to calculate appropriate corresponding values for the East Whiteland system. OCA St. 1 at 7. An example of this can be seen here:

Township / Acquired System	Purchase Price and Capital Statistic	Price / Statistic Ratio	Adjusted Statistic
East Whiteland			
Investor Capital	\$ 42,513,245		
Gross PP&E	43,447,309		
Net PP&E	32,955,596		
New Garden (INT)	\$ 29,500,000		
Investor Capital	23,001,140	1.28	\$ 54,525,155
Gross PP&E	25,988,330	1.14	49,318,121
Net PP&E	17,967,319	1.64	54,108,801

Id. The OCA proposes a few adjustments to Mr. Walker's selected transactions method. Specifically, the OCA proposes excluding integrated wastewater transactions to assess the FMV of the East Whiteland system. OCA St. 1 at 8-9.

Regarding the market value estimate, Mr. Walker criticized the OCA's proposal to use the ratemaking rate bases approved by the Commission for each transaction, rather than the purchases prices (as proposed by Mr. Walker). Aqua St. 4R at 19-20; OCA St. 1SR at 2-4. Mr. Walker also disagrees with the OCA's proposal to use Original Cost New Less Depreciation (OCNLD) data rather than financial statement data in the selected transactions method. Aqua St. 4R at 18-19; OCA St. 1SR at 4-5. In response, OCA witness Garrett explained that:

By establishing a ratemaking rate base based on fair market value that is lower than the winning bid / purchase price in any particular case, the Commission is essentially determining that the winning bid does not comport with the fair market value of a particular transaction. For example, the purchase price in the Limerick transaction was \$75.1 million; however, the ratemaking rate base based on fair market value, as determined by the Commission, was \$64.4 million. Suppose the winning bid had been even higher at \$90 million – even further divergent from the fair market value. Yet this is still the figure Mr. Walker would have presumably relied on in his selected transaction analysis, despite the fact that it would be grossly excessive relative to the Commission's ultimate determination. We are using the selected transactions method (and all other models in the case) for the sole purpose of helping the Commission determine the fair market value in this proceeding. It only makes sense that we would incorporate that same figure from comparable transactions as part of the selected transactions method to help the Commission determine the fair market value in this proceeding.

Id. at 3-4. The same line of reasoning supports the use of OCNLD determinations rather than financial statement data. *Id.* at 4. Relying on OCNLD, or ex-post data, should not be disregarded as irrelevant simply because it was obtained after the transaction purchase price was determined.

Id. Moreover, Aqua witness Walker acknowledges that using only OCNLD (without ex-ante data)

would not have significantly changed his valuation (less than \$1 million). Aqua St. 4R at 18; OCA St. 1SR at 4.

Mr. Walker also criticized the OCA's exclusion of 7 (seven) of the 13 (thirteen) transactions he included as part of his analysis under the selected transactions method. Aqua St. 4R at 20-21; OCA Exh. DJG-4. However, OCA Witness Garrett explained in direct testimony why he did not include transactions involving integrated treatment and collection systems. The Township owns only one wastewater treatment plant. OCA St. 1 at 9-10; OCA St. 1SR at 5. Wastewater treatment in the Township is mainly provided by another entity, so East Whiteland's system may be properly characterized as a collection-only system. OCA St. 1 at 9. Thus, the OCA's market analysis only includes transactions involving collection/distribution systems. Mr. Walker's analysis included integrated systems which in turn produced FMV results that are unreasonably high. For example, the Kane and Limerick transactions produced indicated valuations as high as \$69 million and \$62 million, respectively. OCA St. 1 at 9; OCA Exh. DJG-4. These results are higher than any of the valuation estimates produced by either appraiser, and they are notably higher than the average adjusted result of \$46.5 million from the OCA's analysis. *Id.*

OCA witness Garrett's adjustments to Gannett Fleming's market approach result in a market approach valuation estimate of \$39.5 million, which is about \$7.1 million less than Gannett Fleming's market approach valuation of \$46.7 million. OCA St. 1 at 11. This number is far more reasonable than Gannett Fleming's result because Mr. Garrett excluded integrated systems because the Township is not an integrated system and Mr. Garrett found that the analysis including integrated systems produced several results that are unreasonably high. *Id.* This calculation is summarized below:

	<u>Gannett Fleming Market Approach Results</u>			<u>OCA Adjusted Market Approach Results</u>		
	Amount	Weight	Result	Amount	Weight	Result
Market Multiples	\$ 49,340,713	50%	\$ 24,670,357	\$ 49,340,713	50%	\$ 24,670,357
Selected Transactions	44,142,464	50%	<u>22,071,232</u>	29,756,954	50%	<u>14,878,477</u>
Total			\$ 46,741,589			\$ 39,548,833

Id.

ii. AUS Consultants Market Approach

To determine his estimate of FMV of the East Whiteland system, Aqua witness Weinert considered the purchase price and Reproduction Cost New Less Depreciation (RCNLD) data from comparable acquisitions in Pennsylvania. OCA St. 1 at 11. Mr. Weinert reviewed the price-to-RCNLD ratios for each of these comparable acquisitions and then applied his ratio to the RCNLD amount estimated for the Township, in order to find the implied market valuation for the Township. *Id.* Using this approach, Mr. Weinert estimated the market value of the East Whiteland system to be \$56.2 million. *Id.*; OCA Exh. DJG-2.

The OCA proposes three adjustments to Mr. Weinert’s market approach valuation. First, the OCA proposes that, instead of using the purchase price for each transaction selected by Mr. Weinert, it would be more appropriate to use the Commission’s approved ratemaking rate base, since that is the statutorily determined, Commission approved fair market value as defined by Section 1329. OCA St. 1 at 11-12; 66 Pa. C.S. § 1329. The entire point of the appraisal process is to determine a fair market value for the Township under Section 1329 and as noted above, in some prior acquisitions the negotiated purchase price and the Commission-approved ratemaking rate base have been different. OCA St. 1 at 12. Thus, to determine fair market value under the market approach, it makes the most sense to consider actual Commission-approved rate base amounts. *Id.*

In rebuttal testimony, Mr. Weinert argues that using rate base instead of the agreed upon purchase price is not appropriate under the definition of “market approach,” because the actual agreed upon rate base does not represent a market transaction. Aqua St. 5R at 5. This is incorrect. Commission-approved rate base represents a market transaction. OCA St. 1SR at 6-7. Once the Commission determines a FMV under Section 1329, both the buyer and seller have the option not to proceed with the transaction. *Id.* When they agree to proceed, however, the Commission’s approved FMV is not only what the ratemaking rate base for a transaction, but it is also the number that both buyer and seller must necessarily agree to so as to proceed with the transaction. *Id.* Thus, the Commission-determined rate base is a market sale that must be agreed to by both buyer and seller. It is not a hypothetical value, and its use is acceptable to determine the value of the Township’s assets under the market approach.

Mr. Weinert’s argument that “purchase price” is the best indicator of FMV in Section 1329 cases fails to consider that Section 1329 transactions are not comparable to purely market-driven transactions. OCA St. 1 at 11-12. Of course, even by the plain terms of Section 1329, this is only true if the purchase price is lower than the UVE appraisal amounts. 66 Pa. C.S. § 1329. In competitive marketplace transactions, both parties have an incentive to maximize their value, with the buyer seeking the lowest price and the seller seeking the highest price. OCA St. 1SR at 7. These incentives are not present in Section 1329 transactions, as indicated by the very existence of the Section 1329 regulation. *Id.* The ultimate FMV of a Section 1329 transaction as determined by the Commission and as agreed to by both buyer and seller provides the best indicator of what FMVs for other Section 1329 transactions should be, and thus, the Commission approved ratemaking rate base should be used in the market approach valuation to estimate the FMV of the East Whiteland system.

The OCA also recommends against using the weightings that Mr. Weinert applied to his FMV/RCNLD ratios. OCA St. 1 at 12. Mr. Weinert's weightings caused the ratios resulting from higher purchase price/FMV transactions to have more influence than lower-priced transactions, because Mr. Weinert divided the sum of all purchase price amounts by the sum of all RCNLD amounts. *Id.*; OCA St. 1SR at 7-8. This is unreasonable in this case, where a transaction such as McKeesport (with a purchase price of \$159 million) cannot be reasonably compared to a transaction with a purchase price of only \$54.9 million. *Id.*

For example, Mr. Weinert's weightings give the McKeesport transaction the greatest statistical weighting, when that transaction is the *least comparable* to the proposed sale of the East Whiteland system. OCA St. 1SR at 7-8. The OCA recommends giving equal weight to each transaction, unless there is a compelling reason not to do so for a particular transaction. *Id.* Further, the Commission has rejected the use of a weighted average when, as is the case here, its use would allow larger acquisitions to influence the resulting FMV more than the smaller, more comparable transactions. *Cheltenham* at 69. That is certainly the case here, where the inclusion of a transaction such as McKeesport would drive the purchase price up so drastically. OCA St. 1 at 7-8.

After using the Commission's approved ratemaking rate bases instead of purchase price to determine fair market value, and after using more reasonable weightings than those proposed by Mr. Weinert, the OCA finds the adjusted AUS market approach fair market value of the East Whiteland system to be approximately \$40.9 million. OCA St. 1 at 14. This number is far more reasonable than Gannett Fleming's proposed FMV for the following reasons: (1) the negotiated purchase price and the Commission-approved ratemaking rate base have been different amounts, therefore, it is preferable to consider actual Commission-approved rate base amounts, rather than

purchase prices; (2) Mr. Garrett did not apply weightings to his FMV / RCNLD ratios since it results in certain un-relatable transactions being given the greatest weight; and (3) Mr. Garrett only included transactions involving only collection/distribution systems, like the Township, and not transactions involving integrated treatment and collection systems. *Id.* at 11-12. This represents an adjustment of \$15.2 million to Mr. Weinert's market approach valuation.

c. Income Approach

The OCA presented the testimony of David J. Garrett to address the Income Approach analyses presented by East Whiteland witness Weinert from AUS and Aqua witness Walker from Gannett Fleming. Mr. Walker and Mr. Weinert estimate income approach valuations of \$61.1 million and \$55.6 million, respectively. OCA St. 1 at 24. Mr. Garrett recommended several adjustments to the Income Approach analyses as discussed in OCA Statements 1 and 1SR. Mr. Garrett's adjustments to Mr. Walker's and Mr. Weinert's Income Approach analysis reduce the valuations to \$41,357,255 or by \$19.8 million and \$14.2 million, respectively. OCA St. 1 at 24; OCA Exh. DJG-2. As set forth below, Mr. Garrett's adjustments are reasonable and consistent with public utility principles and should be adopted.

The theory behind Income Approach valuation is that the value of a business is the future economic benefit that ownership will provide. The Income Approach is a procedure to value a business based on the anticipated value the business creates in over time. The American Society of Appraisers, *ASA Business Valuation Standards* at 10-11.¹¹

OCA witness Garrett's income approach adjustment recognizes that assets that are expected to generate cash flows over time can be valued with various discounted cash flow models.

¹¹ https://www.appraisers.org/docs/default-source/5---standards/bv-standards-feb-2022.pdf?sfvrsn=5c9e5ac0_3 (last accessed Mar. 25, 2022).

OCA St. 1 at 25. This basic premise also underlies the approach taken by the UVEs in their income approach valuations. *Id.* OCA witness Garrett described the Income Approach models utilized by the UVEs and the reasoning for the OCA's proposed adjustments in this proceeding as follows:

Under this valuation method, the value of an asset (the Township's wastewater system assets in this case), is equal to the present value of its future cash flows. This model also requires estimates for a growth rate and discount rate. For publicly traded assets, we can use the dividend discount model. A derivation of this model that solves for the discount rate is called the Discounted Cash Flow ("DCF") model in regulatory proceedings. However, since the Township is not publicly traded and does not issue dividends, we must consider its estimated free cash flow from operations, rather than dividends, as part of the valuation model. I also proposed adjustments to the UVEs' long-term growth rate and discount rate, which are both key inputs to the DCF Model. Under the DCF Model used for the valuation adjustment in this case, the discount rate is the asset's estimated cost of capital. My adjustment is the result of applying these reasonable estimates to the UVE income approaches.

OCA St. 1 at 25 (internal citations omitted). The key differences between the OCA and UVE positions then, are the OCA's use of a constant growth rate DCF model based on cash flow or dividends from the current period and use of a more reasonable estimated long-term growth rate and discount rate (cost of capital).

First, OCA witness Garrett adjusted the Township's free cash flows from operations. OCA St. 1 at 26. In formulating this adjustment, OCA witness Garrett utilized the average amount of operating revenues, earnings before interest and taxes (EBIT), depreciation, and capital expenditures for years 2018, 2019, and 2020 to calculate free cash flow from operations presented by Mr. Walker to use as the basis for discounted cash flow analysis. *Id.* OCA witness Garrett selected average amounts obtained from these three years in this proceeding because using the amounts from any single year could have produced an inaccurate indicated valuation.¹² OCA St.

¹² Had OCA witness Garrett utilized free cash flow calculation obtained from 2018 alone in this proceeding, it would have produced an indicated value of \$307 million. OCA St. 1 at 26. On the other hand, using 2020 figures alone would have produced a negative valuation for the system assets. *Id.*

1 at 26. As such, OCA witness Garrett determined that averaging the figures from all three years ultimately produced an indicated valuation that was much more reflective of the results obtained from the other valuation approaches.¹³ *Id.*

Next, OCA witness Garrett adjusted the cost of capital for the Township as follows:

Figure 1: Cost of Capital Adjustment

Capital Component	Proposed Ratio	Cost Rate	After-Tax Rate	Weighted Cost
Long Term Debt	50%	3.9%	2.8%	1.39%
Equity	50%	6.1%	6.1%	3.06%
Total	100%			4.45%

OCA St. 1 at 28. The capital composition and rates contemplated in this calculation produce a cost of capital estimate of 4.45%. *Id.* By comparison, Mr. Walker utilized a capital structure of 23.9% debt and 76.1% equity, a market cost of debt of 3.37% and a range of market cost of equity of 7.87% to 9.47%. Aqua Exh. Q at 29. Mr. Weinert utilized a capital structure of 29% debt and 71% equity, and a market cost of debt of 2.79% with an after-tax rate of 0.58%. Aqua Exh. R at 39. As discussed below, Mr. Walker and Mr. Weinert’s capital structures and cost of capital are not reasonable for use in their Income Approach analyses.

The weighted cost of capital essentially involves several key components, including the cost of debt, the cost of equity, and the capital structure. In terms of estimation, the most critical of these components is the cost of equity. OCA St. 1 at 27. OCA witness Garrett considered a proxy group of water utilities substantially similar to the proxy group considered by the UVEs. *Id.*

¹³ The OCA notes that the indicated valuation adjustment of \$41.3 million under the adjusted income approach valuation is almost identical to the adjusted valuation of \$41 million to Mr. Weinert’s market approach. OCA St. 1 at 26.

The figures in the above table were utilized as inputs for the discount rate for Mr. Garrett's discounted cash flow adjustment for the Township. OCA St. 1 at 28. OCA witness Garrett's adjusted cost of capital of 4.45% is less than the estimates of both UVEs (Mr. Walker estimates a range of a cost of capital of 6.57% to 7.79% while Mr. Weinert estimates a cost of capital of 7.57%). OCA St. 1 at 28. As shown above, the differences between cost of capital estimates stem from the differences between the various components of the cost of capital – primarily the UVEs' unreasonable capital structures of more than 70% equity and the cost of equity. *Id.* at 27.

In estimating the Township's cost of equity, OCA witness Garrett utilized the two most widely used financial models: the Discounted Cash Flow Model (DCF) and the Capital Asset Pricing Model (CAPM). OCA St. 1 at 29. Mr. Garrett utilized these models because, unlike the known, contractual and embedded cost of debt, there is not any explicitly quantifiable "cost" of equity. Instead, the cost of equity must be estimated through various financial models, such as the DCF and CAPM. OCA St. 1 at 29.

OCA witness Garrett's DCF model, which is based on the average DCF result for each company in the proxy group, results in a 5.5% cost of equity estimate for the Township. OCA St. 1 at 36. OCA witness Garrett's Direct Testimony provides an extensive discussion on the DCF model. *Id.* at 30-36. The most critical input in the DCF Model is the growth rate. Unlike the stock price and dividend inputs in the DCF, the growth rate input must be estimated. OCA St. 1 at 32. Before future cash flows are discounted by the cost of equity, however, they must be "grown" into the future by a long-term growth rate. *Id.* One of the inherent assumptions of the DCF is that these cash flows in the form of dividends grow at a constant rate forever. Thus, the growth rate term in the constant growth DCF model is often called the "constant" or "stable" growth rate. OCA St. 1 at 32.

A fundamental concept in finance is that no firm can grow forever at a rate higher than the growth rate of the economy in which it operates. OCA St. 1 at 33. As such, the constant growth rate used in the DCF Model should not exceed the aggregate economic growth rate. This is especially true when the DCF Model is conducted on public utilities because these firms have defined service territories. *Id.* The following table shows three long-term growth detriments discussed in OCA witness Garrett’s testimony:

Constant Growth Rate Determinants

Constant Growth Determinants	Rate
Nominal GDP	3.8%
Real GDP	1.8%
Inflation	2.0%
Risk Free Rate	2.0%
Highest	3.8%

OCA St. 1 at 35. For the long-term growth rate, OCA witness Garrett selected the maximum, reasonable long-term growth rate of 3.8%. *Id.*

As OCA witness Garrett utilized the utility proxy group to estimate the cost of equity, he used the same proxy group to estimate the cost of debt and capital structure. OCA St. 1 at 44. To estimate cost of debt, OCA witness Garrett considered the interest expense and long-term debt reported for each of the proxy companies. To estimate the capital structure, OCA witness Garrett considered the long-term debt ratios for each proxy company. *Id.* As such, OCA witness Garrett considered substantially the same proxy group of companies as both UVEs as well as their consideration of Value Line as a source for some of the pertinent financial data used in their analyses, including the debt ratios.

OCA witness Garrett's average, adjusted cost of debt (pre-tax) and debt ratio for the proxy group is 3.9% and 50%, respectively. OCA St. 1 at 45. In comparison, Mr. Walker utilized a debt ratio of only 23.9% and Mr. Weinert utilized a debt ratio of only 29%. *Id.* These debt ratios are significantly lower than the average reported debt ratio of the proxy group (50%), which is what OCA witness Garrett based his capital structure adjustment on. OCA St. 1 at 45.

Based on the cost of equity and cost of capital components discussed above, OCA witness Garrett's adjustments to the UVEs' appraisals resulted in an Income Approach valuation of \$41.4 million. OCA St. 1 at 44. The OCA's adjustment resulted in an Income Approach valuation that is \$19.8 million less than Gannett Fleming's valuation of \$61.1 million, and it is \$14.2 million less than AUS Consultants' valuation of \$55.6 million. *Id.* Mr. Garrett's adjustments to the Gannett Fleming and AUS income approach valuations are reasonable and should be adopted.

5. Conclusion

Mr. Garrett's recommended adjustments to Mr. Walker's Cost, Income and Market approaches modify the Gannett Fleming appraisal result from \$55,668,460 to \$45,748,213. OCA St. 1 at 3-4. Mr. Garrett's recommended adjustments to Mr. Weinert's Cost, Income and Market approaches modify the AUS appraisal result from \$57,781,457 to \$47,200,091. *Id.* at 3-5. The OCA averaged the two OCA adjusted appraisal results, which resulted in an average of \$46,500,000. OCA St. 1 at 5-6. Because this amount is less than the \$54,930,000 purchase price, the OCA submits that the amount approved for ratemaking rate base pursuant to Section 1329 must be no more than \$46,500,000, rather than \$54,930,000 as proposed by Aqua.

C. Recommended Conditions

As set forth above, the OCA recommends that the Commission deny the relief requested in the Application. If, however, the Commission approves the proposed acquisition, the OCA recommends the following conditions:

1. *The Commission should adopt the OCA's proposed adjustments to the appraisals, resulting in an overall ratemaking rate base of \$46,500,000 (prior to closing and transaction costs).*

The average of the adjusted appraisal results is less than the purchase price and thus, pursuant to 66 Pa. C.S. § 1329(c)(2), should be adopted as the ratemaking rate base. *See discussion supra* at 23-44. Also, the lower ratemaking rate base will reduce the revenue deficiency created by the acquisition and the resulting rate increases for customers.

2. *The rate freeze provision should be rejected. OCA St. 2 at 4. If the Commission does not reject the rate freeze provision, the Commission should condition its approval on the recognition that the Commission retains the ultimate authority to set rates, including but not limited to, the authority to allocate revenues, if appropriate, to the East Whiteland Township customers that are different from the restrictions contained in Section 7.03 of the Asset Purchase Agreement.*

The proposed three-year rate freeze could hold East Whiteland rates constant after Aqua's next base rate case. Existing Aqua customers should not be at risk to cover the revenue requirement required to keep East Whiteland rates lower than rates set for those customers in a base rate case. OCA St. 2 at 15-16; *New Garden* at 42; *Limerick* at 31; *see discussion supra* at 12-14. If the Commission does not reject the rate freeze provision, the Commission should condition its approval on the recognition that the Commission retains the ultimate authority to set rates, including but not limited to, the authority to allocate revenues, if appropriate, to the East Whiteland Township customers that are different from the restrictions contained in Section 7.03 of the Asset Purchase Agreement. OCA St. 2 at 15-16.

3. *Aqua should be required to provide a separate Cost of Service Study for the East Whiteland system, in the first base rate case which includes the Township's assets.*

This condition will provide information to establish rates that reflect the costs for the East Whiteland system. OCA St. 1 at 46. Parties in the next Aqua base rate case would have the opportunity to propose that the resulting rates for the Township customers should differ, as appropriate, from rates proposed by Aqua.

4. *The proposed projects reflected in the revised LTIP should be in addition to, and not reprioritize, any capital improvements that Aqua was already committed to undertake for existing customers.*

Reprioritization of capital improvements would disadvantage existing Aqua customers. OCA St. 2 at 15. This condition helps to ensure that projects and expenditures already planned for existing Aqua wastewater customers will not be given less priority as a result of the East Whiteland Township acquisition. *Id.*

5. *Rates claims related to the accrual of AFUDC for non-DSIC eligible, post-acquisition improvements should be made in the next Aqua base rate case following the plant additions.*

This condition would ensure that the AFUDC would be claimed at the same time as the improvements are included in rates. OCA St. 2 at 15.

D. Section 507 Approvals

The OCA did not present any evidence regarding the Section 507 approval aspects of the proposed transaction.

E. Section 2102 Approval

The OCA did not present any evidence regarding the Section 2102 approval aspects of the proposed transaction.

F. Other Approvals, Certificates, Registrations and Relief, If Any, Under the Code

The OCA did not present any evidence regarding other approvals, certificates, registrations, and relief under the Pennsylvania Public Utility Code concerning the proposed transaction.

VI. CONCLUSION WITH REQUESTED RELIEF

For the reasons stated above, if the Commission approves the application under Sections 507, 1102, 1329 and 2102 of the Public Utility Code, the Office of Consumer Advocate's proposed conditions should be adopted, including the OCA's proposed adjustments to the appraisals.

Respectfully Submitted,

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List of OCA Sponsored Testimony and Exhibits

- OCA Statement 1, Direct Testimony of David J. Garrett
 - Appendix A: Iowa Curves
 - Appendix B: Discounted Cash Flow Model Theory
 - Appendix C: Capital Asset Pricing Model Theory
 - OCA Exhibits DJG-1 through DJG-22
- OCA Statement 1SR, Surrebuttal Testimony of David J. Garrett
- OCA Statement 2, Direct Testimony of Noah D. Eastman
 - Appendix A: Background and Qualifications of Noah D. Eastman
- OCA Statement 2SR, Surrebuttal Testimony of Noah D. Eastman

OCA Proposed Findings of FactSection 1102/1103

1. As proposed, East Whiteland Township will receive \$54.93 million or 64% more than the net book value of the system. OCA St. 2 at 9.
2. The net book value of the Township's assets is \$33.4 million, which does not reflect an offset for contributed plant or capital. OCA St. 2 at 9.
3. Aqua anticipates spending \$16.92 million for capital improvements to the East Whiteland system during the next 10 years. OCA St. 2 at 6.
4. Aqua calculates that the acquisition would create an annual revenue deficiency of \$5.011 million that will be recovered from either East Whiteland customers, Aqua's existing customers, or both. OCA St. 2 at 3; Aqua St. 1, App. A.
5. Aqua estimates that by recovering 50% of the East Whiteland revenue deficiency from East Whiteland's customers and 50% from Aqua wastewater customers would increase its wastewater customers' monthly rates by \$4.62 or 4.67%. OCA St. 2 at 3; Aqua St. 1, App. A.
6. Aqua also provides a calculation of an assignment to its water customers under Section 1311(c) and under that scenario, the existing Aqua water customers would be allocated about 87.61% of the \$2,505,500 revenue deficiency and subsidize 44% of the total revenue deficiency for East Whiteland. OCA St. 2 at 3; Aqua St. 1, App. A.
7. This would result in an estimated increase of \$0.33 per month or 0.41% for existing residential water customers. OCA St. 2 at 3; Aqua St. 1, App. A.
8. Aqua proposes a three year rate freeze for Township customers in its application. OCA St. 2 at 4.
9. During the first three years post-acquisition, Aqua proposes to freeze rates for Township customers and continue to charge East Whiteland customers their present sewer rate of approximately \$33 per month. APA, ¶ 7.03(a); OCA St. 2 at 3.
10. At the conclusion of the rate freeze, Aqua projects that East Whiteland rates would need to be increased by an additional \$77.64 per month, or by 132.93%, if the entire revenue deficiency is applied to East Whiteland rates. OCA St. 2 at 3.
11. East Whiteland customers will experience significant rate increases if the system is acquired by Aqua. Even if East Whiteland customers bear only 50% of the revenue requirement related to the Aqua-proposed ratemaking rate base, East Whiteland customers would see rates increased by 66.47%. See Aqua St. 1, App. A.

12. If the rate freeze extends beyond Aqua's next base rate proceeding, the East Whiteland rates will fall behind the increased rates for Aqua's existing water and wastewater customers, further exacerbating the amount of the subsidy going forward. OCA St. 2 at 4.
13. To catch up, Township customers will see higher rate increases than currently forecasted in order to move towards the rates of the main rate zone and their cost of service. OCA St. 2 at 5-6.
14. Economies of scale exist "when a firm's average cost curve decreases as output increases." OCA St. 2 at 7 citing Charles F. Phillips, Jr., *The Regulation of Public Utilities: Theory and Practice*, p. 52.
15. Economies of scale can also be understood as a reduction in cost per unit of output as that output increases. OCA St. 2 at 7.
16. There has been no showing that rates would become more affordable in the long-term due to economies of scale. OCA St. 2 at 13.
17. The Company has not provided any showing of cost reductions or efficiencies that will be produced by the acquisition of the East Whiteland customers. OCA St. 2 at 8.
18. Aqua estimates capital investments in the East Whiteland system over 10 years, on a per customer basis, are lower than Aqua's and will decrease the future per customer cost of capital investments for Aqua from \$5,111 per customer to \$5,050, or by \$61. OCA St. 2 at 8.
19. For existing Aqua customers, this decrease in the future per customer cost of capital investments is small (\$61 over an entire decade) and fully negated by the rate increase of \$554.40 that Aqua projects for its wastewater customers for the same period. OCA St. 2 at 8.
20. For East Whiteland customers, acquisition means their per customer costs for capital investment will increase from \$4,344 to \$5,050 or by \$706. OCA St. 2 at 8.
21. Aqua witness Packer calculates that the East Whiteland rate base per EDU is greater than the Aqua rate base per EDU. Aqua St. 1 at 17.
22. The cost of ownership is significantly higher if the East Whiteland Township system is acquired by Aqua because those costs include nearly \$4 million for return to Aqua shareholders. OCA St. 2 at 8.
23. There is no cost of equity for East Whiteland Township as its cost of capital is limited to repaying debts at a much lower interest rate (about 3.7%). OCA St. 2 at 8.
24. Aqua is required to pay taxes, whereas East Whiteland Township is not. OCA St. 2 at 9.
25. Sewer problems during normal business hours can be directed to the sewer department directly, while outside of normal business hours the police department will direct calls to the sewer department on-call staff. OCA St. 2 at 10.
26. The current service provided by the Township is safe and reliable. See East Whiteland St. 3R at 3; OCA St. 2SR at 9.

27. The Township's system has the capacity to meet the demands of current and future customers, does not have any sanitary system overflows in 2020, and is not currently under a Corrective Action Plan or Connection Management Plan with DEP. See Aqua St. 2 at 14; OCA St. 2 at 14.
28. The Township is financially fit to complete any necessary improvements and upgrades given that it has cash and cash equivalents exceeding \$29 million. OCA St. 2 at 6.
29. In the year 2020 alone, the Sewer Fund had an increase to cash and cash equivalents of more than \$500,000. OCA St. 2 at 6; Aqua Exh. J2 at 42.
30. The Township could make necessary improvements and upgrades to the system, equal to what Aqua has proposed, and it would not present an unreasonable financial burden for the Township. OCA St. 2 at 6.
31. If the East Whiteland rates increase to Aqua's current rate zone 1 rates, Township customers would see their rates go up by more than 60%. OCA St. 2 at 11.
32. The current monthly bill for an average Aqua residential wastewater customer using 3,020 gallons per month with a \$31 customer charge is \$53.95 ($\$31 + (\$7.60 \times 3.02)$). Aqua Exh. I1 at 2; Aqua Tariff Sewer-Pa P.U.C. No. 2, at 8.1 (rate zone 1)).
33. Aqua has requested to increase its rates effective May 2022. Pa. PUC v. Aqua Pennsylvania Wastewater, Inc., Docket No. R-2021-3027386.

Section 1329

34. In this proceeding, the two appraisal values for the East Whiteland Township assets were \$55.7 million (Gannett Fleming) and \$57.8 million (AUS Consultants). OCA St. 1 at 2; Aqua Exh. X at 13; Aqua Exh. Y at 3.
35. Aqua and the Township have negotiated a purchase price of \$54,930,000. OCA St. 1 at 2.
36. If the Commission approves the proposed acquisition, the correct ratemaking rate base amount is \$46.5 million for the Township's system. OCA St. 1 at 5, 6, 46; OCA Exh. DJG-2.

Cost Approach

37. When utilities have records about asset placements and retirements by vintage year, depreciation experts can analyze the historic retirement patterns in each account to estimate depreciation rates. OCA St. 1 at 15-16.
38. In this case, the Township did not have the requisite records about asset placements and retirements by vintage year for the UVEs to use the more empirical curve techniques involved in the retirement rate method. OCA St. 1 at 15.
39. The UVEs chose to use Iowa curves to estimate the average remaining life and accumulated depreciation of the Township's assets, and the UVEs relied on their subjective judgment to determine which Iowa curves were the best fit. OCA St. 1 at 15-16.

40. To reach his conclusion about the valuation of the Township's assets under the cost approach valuation, Mr. Walker used the replacement cost method which involved estimating accrued depreciation using his subjectively selected Iowa curves, and then subtracting that depreciation from estimated reproduction cost to reach an FMV appraisal of \$59.1 million. OCA St. 1 at 18-19; OCA Exh. DJG-6.
41. The original cost method estimates the cost of the assets in question when those assets were "new" or first constructed, based on information contained in the Engineering Assessment. Aqua Exh. X at 14.
42. Mr. Walker's analysis under the original cost method produced an indicated value of \$33 million. OCA St. 1 at 18; Aqua Exh. Q at 24.
43. Mr. Walker excluded his analysis under the original cost method from his recommended FMV under the cost approach, and instead only proposed the \$59.1 million valuation from the replacement cost method. OCA St. 1 at 18-19.
44. The OCA used Mr. Walker's replacement cost method analysis as part of its adjustment to Mr. Walker's FMV proposal under the cost approach. OCA St. 1 at 19.
45. The OCA recommends certain adjustments to the Mr. Walker's replacement cost method which would result in a FMV of \$56.3 million. OCA St. 1 at 22.
46. Mr. Walker and Mr. Weinert proposed different Iowa curves and service lives under their respective cost approaches. OCA St. 1SR at 8.
47. The OCA recommends using a service life of 45 years for the Township's pumping improvement account and 55 years for the Township's treatment improvement account. OCA St. 1 at 20.
48. The curves proposed by OCA witness Garrett for the Township's pumping and treatment structures and improvements accounts are the same as those proposed by Mr. Weinert of AUS Consultants, and they are consistent with Mr. Garrett's proposed Iowa curves for these accounts in prior Section 1329 proceedings. OCA St. 1 at 20.
49. For the force and gravity collection mains accounts, the OCA proposes a 60-year average life, just as Gannett Fleming proposed for those accounts in a wastewater case in front of the Indiana Utility Commission. OCA St. 1 at 20.
50. The OCA recommends using a 45-R3 curve for the Services account which is consistent
51. with Mr. Garrett's proposal for this account in prior Section 1329 proceedings and is a reasonable range for that account. OCA St. 1 at 20.
52. The utilities in the cases referenced by Mr. Walker produced far more historical retirement data to support their proposed service lives than Aqua or East Whiteland Township has produced in this case. OCA St. 1SR at 9.
53. The Iowa curves proposed by the OCA here are the most conservative and, thus, most reasonable given the absence of utility-specific actuarial data. OCA St. 1SR at 11.

54. OCA witness Garrett used the same process as Mr. Walker to calculate accrued depreciation, with the only difference being that Mr. Garrett used shorter Iowa curves and thus came to a lower cost approach estimate. OCA St. 1 at 21.
55. Applying Mr. Garrett's proposed Iowa curves and accrued depreciation, the OCA recommends an adjusted cost approach valuation of \$56.3 million, which is about \$2.8 million less than the Gannett Fleming's cost approach valuation. OCA St. 1 at 22.
56. Mr. Weinert of AUS Consultants used the replacement cost method to determine a FMV for the Township system under the cost approach valuation. OCA St. 1 at 23.
57. Mr. Weinert estimated accrued depreciation in order to calculate "replacement cost less depreciation" values for each account. OCA St. 1 at 23.
58. The OCA's recommended adjustments to AUS Consultant's proposals are based on using the same average service lives for the collection sewers mains accounts that the OCA recommended in its adjustments to the Gannett Fleming cost approach. OCA St. 1 at 23.
59. In support of his own recommendations, Mr. Weinert relies on the Gannett Fleming depreciation studies. OCA St. 1SR at 10.
60. Mr. Weinert's depreciation studies were not conducted on the assets at issue in this proceeding. OCA St. 1SR at 10.
61. Both Mr. Walker and OCA witness Garrett base their proposed service lives on data obtained from other cases. OCA St. 1SR at 10-11.
62. The Township does not maintain the requisite data for a utility-specific actuarial analysis. OCA St. 1SR at 11.
63. The OCA's calculation for Renewed Cost New Less Depreciation (RCNLD) came to approximately \$53.1 million, as opposed to Mr. Weinert's calculated value of \$56.2 million for RCNLD. OCA St. 1 at 13.
64. Using this RCNLD, the OCA calculated a cost approach valuation of \$40.9 million for the East Whiteland system, which is about \$15.2 million lower than the AUS Consultant's proposed cost approach valuation. OCA St. 1 at 13; OCA Exh. DJG-5.

Market Approach

65. Gannett Fleming estimated a market approach valuation of \$46.7 million for the East Whiteland system assets and AUS Consultants estimated a market approach valuation of \$56.1 million. Aqua Exh. X at 13; Aqua Exh. Y at 3.
66. Mr. Walker multiplied certain Township metrics such as gross and net PP&E (property, plant and equipment) and the number of customers by the ratio of enterprise value to the same metric

- for a group of publicly traded water utilities referred to as the Comparable Group. OCA St. 1 at 7.
67. Mr. Walker increased the Comparable Group ratios (called “multiples”) by adjustments which he indicates are intended to reflect growth, risk, and contributions. After this calculation for each metric, Mr. Walker averaged some of the results and determined a Market Approach valuation of \$49.3 million. OCA St. 1 at 7.
 68. The OCA proposes excluding integrated wastewater transactions to assess the FMV of the East Whiteland system. OCA St. 1 at 9.
 69. The Township owns only one wastewater treatment plant. OCA St. 1 at 9.
 70. Wastewater treatment in the Township is mainly provided by another entity, so East Whiteland’s system may be properly characterized as a collection-only system. OCA St. 1 at 9.
 71. Mr. Walker’s analysis included integrated systems which in turn produced FMV results that are unreasonably high, especially when using demographic statistics such as population and number of customers to indicate fair market value. OCA St. 1 at 9.
 72. When using population as a relative adjustment to purchase price, the Limerick and Kane 1329 transactions would indicate FMVs of \$62 million and \$69 million, respectively. OCA St. 1 at 9.
 73. OCA Witness Garrett excluded transactions from his proposed Gannett Fleming adjustments only when the transactions did not contain the data necessary to make the relevant calculations under the selected transactions approach, or when the transactions involved integrated systems. OCA St. 1SR at 5.
 74. Mr. Walker stated in his appraisal report that he gave “additional weight to the collection/distribution assets selected transactions multiples.” OCA St. 1 at 9; Aqua Exh. Q at 41.
 75. Mr. Walker also noted in one instance that one of the assets that he referenced, Connecticut Water, was a fully integrated system and thus “may overstate the value of the [East Whiteland] Wastewater System.” OCA St. 1 at 9-10; Aqua Exh. Q at 42.
 76. OCA witness Garrett’s adjustments to exclude Section 1329 transactions involving integrated systems from Mr. Walker’s Selected Transactions method of determining FMV yielded an FMV estimate of \$39.5 million for the East Whiteland system. OCA St. 1 at 10.
 77. Mr. Weinert estimated the market value of the Township system to be \$40.9 million. OCA St. 1 at 10.
 78. The point of the appraisal process is to determine a fair market value for the Township under Section 1329, and in some prior acquisitions, the negotiated purchase price and the Commission-approved ratemaking rate base have been different. OCA St. 1 at 12.
 79. Once the Commission determines a FMV under Section 1329, both the buyer and seller still have the option not to proceed with the transaction. OCA St. 1SR at 6.

80. A transaction regulated under Section 1329 fair market valuation is clearly different from a transaction within a competitive market. OCA St. 1SR at 7.
81. The Section 1329 process is used for determining the ratemaking rate base, which will be used for setting rates for utility customers in future cases. OCA St. 1SR at 7.
82. While the use of the “purchase price” may be appropriate in an open and competitive market, it is not a reasonable substitute for the Commission oversight within a fair market value utility appraisal. OCA St. 1SR at 7.
83. After using the Commission’s approved ratemaking rate bases, instead of purchase price, to determine fair market value, and after using more reasonable weightings than those proposed by Mr. Weinert, the OCA finds the adjusted AUS market approach fair market value of the East Whiteland system to be approximately \$59.8 million. OCA St. 1 at 24.

Income Approach

84. Mr. Walker and Mr. Weinert estimate income approach valuations of \$61.1 million and \$55.6 million, respectively. OCA St. 1 at 24.
85. Mr. Garrett’s adjustments to Mr. Walker’s and Mr. Weinert’s Income Approach analysis reduce the valuations to \$41,357,255 or by \$19.8 million and \$14.2 million, respectively. OCA St. 1 at 24; OCA Exh. DJG-2.
86. The Income Approach is a procedure to value a business based on the anticipated value the business creates in over time. The American Society of Appraisers, ASA Business Valuation Standards at 10-11.
87. OCA witness Garrett’s income approach adjustment recognizes that assets that are expected to generate cash flows over time can be valued with various discounted cash flow models. OCA St. 1 at 25.
88. OCA witness Garrett adjusted the Township’s free cash flows from operations. OCA St. 1 at 26.
89. OCA witness Garrett utilized the average amount of operating revenues, earnings before interest and taxes (EBIT), depreciation, and capital expenditures for years 2018, 2019, and 2020 to calculate free cash flow from operations presented by Mr. Walker to use as the basis for discounted cash flow analysis. OCA St. 1 at 26.
90. OCA witness Garrett selected average amounts obtained from these three years in this proceeding because using the amounts from any single year could have produced an inaccurate indicated valuation. OCA St. 1 at 26.
91. The capital composition and rates contemplated by Mr. Garrett produce a cost of capital estimate of 4.45%. OCA St. 1 at 26.
92. OCA witness Garrett considered a proxy group of water utilities substantially similar to the proxy group considered by the UVEs. OCA St. 1 at 27.

93. OCA witness Garrett's adjusted cost of capital of 4.45% is less than the estimates of both UVEs (Mr. Walker estimates a range of a cost of capital of 6.57% to 7.79% while Mr. Weinert estimates a cost of capital of 7.57%). OCA St. 1 at 28.
94. In estimating the Township's cost of equity, OCA witness Garrett utilized the two most widely used financial models: the Discounted Cash Flow Model (DCF) and the Capital Asset Pricing Model (CAPM). OCA St. 1 at 29.
95. OCA witness Garrett's DCF model, which is based on the average DCF result for each company in the proxy group, results in a 5.5% cost of equity estimate for the Township. OCA St. 1 at 36.
96. Unlike the stock price and dividend inputs in the DCF, the growth rate input must be estimated. OCA St. 1 at 32.
97. Before future cash flows are discounted by the cost of equity, they must be "grown" into the future by a long-term growth rate. OCA St. 1 at 32.
98. The growth rate term in the constant growth DCF model is often called the "constant" or "stable" growth rate. OCA St. 1 at 32.
99. A fundamental concept in finance is that no firm can grow forever at a rate higher than the growth rate of the economy in which it operates. OCA St. 1 at 33. This is especially true when the DCF Model is conducted on public utilities because these firms have defined service territories. *Id.*
100. For the long-term growth rate, OCA witness Garrett selected the maximum, reasonable long-term growth rate of 3.8%. OCA St. 1 at 35.
101. As OCA witness Garrett utilized the utility proxy group to estimate the cost of equity, he used the same proxy group to estimate the cost of debt and capital structure. OCA St. 1 at 44.
102. To estimate the capital structure, OCA witness Garrett considered the long-term debt ratios for each proxy company. OCA St. 1 at 44.
103. OCA witness Garrett's average, adjusted cost of debt (pre-tax) and debt ratio for the proxy group is 3.9% and 50%, respectively. OCA St. 1 at 45.
104. The UVEs debt ratios are significantly lower than the average reported debt ratio of the proxy group (50%). OCA St. 1 at 45.

OCA Proposed Conclusions of Law

1. Aqua Pennsylvania Wastewater, Inc. is a public utility as defined in Section 102 of the Public Utility Code. 66 Pa. C.S. § 102.
2. The Commission has jurisdiction over the parties and subject matter of this proceeding. 66 Pa. C.S. § 101, *et seq.*
3. Aqua Pennsylvania Wastewater, Inc. has the burden of proof to show that its proposed acquisition of the East Whiteland system is adequate, efficient, safe, and reasonable under Section 315(c). 66 Pa. C.S. § 315(c).
4. Aqua Pennsylvania Wastewater, Inc. has the burden of proof to show that its proposed purchase of the East Whiteland wastewater system would provide substantial affirmative benefits under Section 1102 of the Public Utility Code. 66 Pa. C.S. § 1102.
5. Aqua Pennsylvania Wastewater, Inc. has not established that the proposed transaction would provide the required substantial affirmative benefits to existing Aqua customers or to the acquired East Whiteland customers under Section 1102. 66 Pa. C.S. § 1102.
6. The Commission has the authority to grant a certificate of public convenience to a utility only when doing so is necessary or proper for the service, accommodation, convenience, or safety of the public. 66 Pa. C.S. § 1103(a).
7. Aqua Pennsylvania Wastewater, Inc. has not established that the proposed transaction is necessary or proper for the service, accommodation, convenience, or safety of the public. 66 Pa. C.S. § 1103(a).
8. The Commission can, under Section 1103(a), impose conditions that it deems just and reasonable. 66 Pa. C.S. § 1103(a).
9. If the proposed transaction is approved, the Company may ask for ratemaking treatment of the East Whiteland system's assets using fair market value. 66 Pa. C.S. § 1329.
10. If the proposed transaction is approved, the correct ratemaking rate base amount is \$46.5 million for the Township's system.

OCA Proposed Ordering Paragraphs

It is hereby ORDERED THAT:

1. The Application of Aqua Pennsylvania Wastewater, Inc. pursuant to Sections 507, 1102 and 1329 of the Public Utility Code for Approval of its Acquisition of the Wastewater System Assets of East Whiteland Township, is denied.

Or, in the alternative to the Application's denial:

1. The Application is approved conditioned on the following requirements:
 - 1) The OCA's proposed adjustments to the UVE appraisals, resulting in an overall ratemaking rate base of \$46,500,000 (prior to closing and transaction costs) are adopted.
 - 2) The proposed rate freeze provision contained in Section 7.03 of the Asset Purchase Agreement is denied.
 - 3) In the first base rate case which includes the Township's assets, Aqua shall provide (1) a cost of service study that removes all costs and revenues associated with the operations of the East Whiteland wastewater system and (2) a separate cost of service study for the East Whiteland system.
 - 4) The proposed reflected in the revised LTIP shall be in addition to, and not reprioritize, any capital improvements that Aqua was already committed to undertake for existing customers,
 - 5) Rate claims related to the accrual of AFUDC for non-DSIC eligible, post-acquisition improvements should be made in the *next* Aqua base rate case following the plant additions.