

**PENNSYLVANIA
PUBLIC UTILITY COMMISSION
Harrisburg, PA 17120**

Commissioners Present:

Gladys Brown Dutrieuille, Chairman
John F. Coleman, Jr., Vice Chairman
Ralph V. Yanora

Application of Aqua Pennsylvania Wastewater, Inc., pursuant to 66 Pa. C.S. §§ 1102 and 1329 for: (1) approval of the acquisition by Aqua Pennsylvania Wastewater, Inc. of the wastewater assets of East Whiteland Township situated within the Township of East Whiteland, Chester County, Pennsylvania; (2) approval of the right of Aqua Pennsylvania Wastewater, Inc. to begin to offer, render, furnish and supply wastewater service to the public in portions of East Whiteland Township, Chester County, Pennsylvania; and (3) an order approving the acquisition that includes the ratemaking rate base of the East Whiteland Township wastewater system assets pursuant to Section 1329(c)(2) of the Public Utility Code

A-2021-3026132

Request for Approval of Contracts, including Assignments of Contracts, between Aqua Pennsylvania Wastewater, Inc. and East Whiteland Township, Pursuant to Section 507 of the Public Utility Code

Request for Approval of a Contract between Affiliated Interests, Pursuant to Section 2102 of the Public Utility Code

OPINION AND ORDER

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BY THE COMMISSION:

Before the Pennsylvania Public Utility Commission (Commission) for consideration and disposition are the Exceptions to the Recommended Decision (R.D.) of Administrative Law Judge (ALJ) Marta Guhl, issued on May 10, 2022, in the above-captioned proceeding, which were filed by the following Parties on May 20, 2022: Aqua Pennsylvania Wastewater, Inc. (Aqua, the Company, or the Applicant); East Whiteland Township (EWT or the Township); and the Commission's Bureau of Investigation and Enforcement (I&E). On May 27, 2022, the Office of Consumer Advocate (OCA) filed Replies to Exceptions.¹ For the reasons stated, *infra*, we shall: (1) grant, in part, and deny, in part, the Exceptions of Aqua and the Township, and grant the Exception of I&E; (2) adopt the Recommended Decision, as modified; and (3) approve the Application, as modified; all consistent with this Opinion and Order.

I. Procedural History

On July 26, 2021, Aqua filed an Application under Sections 1102, 1329, 507, and 2102 of the Public Utility Code (Code), 66 Pa. C.S. §§ 1102, 1329, 507, 2102, seeking approval of: (1) the acquisition, by Aqua, of the wastewater system assets of EWT; (2) the right of Aqua to begin to offer, render, furnish and supply wastewater service to the public in the requested territory; and (3) an order approving the acquisition that includes the ratemaking rate base of the Township's wastewater system assets

¹ The Office of Small Business Advocate (OSBA) also participated in this proceeding. A customer, Richard J. Gage, also filed a protest to the Application as discussed *infra*. All of the participating entities will be known collectively as the Parties.

pursuant to Section 1329(c)(2) of the Code, 66 Pa. C.S. § 1329(c)(2).² Application at ¶ 3. Aqua also requested approval of the Asset Purchase Agreement (APA) dated January 8, 2021, as well as other municipal agreements and contracts, pursuant to Sections 507 and 2102 of the Code, 66 Pa. C.S. §§ 507, 2102, and requested that the Commission issue an order and Certificate of Public Convenience (Certificate) approving and addressing the items requested in its Application. Application at ¶¶ 5, 69-72.

On December 20, 2021, the Secretary's Bureau issued a Letter conditionally accepting Aqua's Application.

On February 4, 2022, the Secretary's Bureau issued a Letter accepting the Application of Aqua to acquire EWT. Also on February 4, 2022, Aqua customer, Richard Gage, filed a Protest to the Application.

On March 4, 2022, Prehearing Conference Memoranda were filed by the Parties.

A prehearing conference in this matter was held on March 8, 2022. Counsel for Aqua, I&E, the OCA, the OSBA, and EWT participated.

The procedural schedule discussed at the Prehearing Conference on March 8, 2022, was memorialized in Prehearing Order #1 dated March 16, 2022.

² Under 66 Pa. C.S. § 1329, *inter alia*, Aqua sought to establish a ratemaking rate base of \$54,930,000 for EWT's wastewater system assets based on the negotiated purchase price, as the negotiated purchase price of \$54,930,000 is less than the average of the fair market value appraisals, which is \$56,724,729 (determined by \$55,668,000 presented in the appraisal of Gannett Fleming Valuation and Rate Consultants, LLC (Gannett Fleming) and \$57,781,458 presented in the appraisal of AUS Consultants, Inc. (AUS)). Application at 18.

On March 22, 2022, a Public Input Hearing was held telephonically. Six people presented on-the-record statements.

On March 31, 2022, the evidentiary hearing was held in this matter. The Parties waived cross-examination of all witnesses and moved to have their pre-served testimony and exhibits entered into the record. As there were no objections, all documents and exhibits were entered into the record at the time of the hearing.

Main Briefs were filed on April 8, 2022. On April 15, 2022, Reply Briefs were filed. On the same date, Aqua, I&E, the OCA, the OSBA, the Township, and Mr. Gage filed a Stipulation which covered certain issues if the Commission approved the Application that the Parties agreed to as conditions of the approval. The record closed on April 15, 2022.

In the Recommended Decision issued on May 10, 2022, ALJ Guhl found that Aqua had not established that the proposed purchase of the EWT system would provide substantial affirmative benefits under Section 1102 of the Code. The ALJ also found that the proposed transaction was not necessary or proper for the service, accommodation, convenience, or safety of the public under 66 Pa. C.S. § 1103. Thus, ALJ Guhl recommended that the proposed transaction be denied. R.D. at 1, 59-60.

As noted above, Aqua, EWT, and I&E filed Exceptions on May 20, 2022. On May 27, 2022, the OCA filed Replies to Exceptions.

II. Transaction Overview

Aqua is a certificated provider of wastewater service, duly organized and existing under the laws of the Commonwealth of Pennsylvania. Aqua provides wastewater service to approximately 45,000 customer accounts in various counties throughout Pennsylvania, including parts of Chester County and within the Township itself, and currently operates thirty-nine wastewater treatment plants. Application at ¶ 7; Aqua St. 1 at 8-9.

EWT is a Pennsylvania Second Class township, which owns the sanitary wastewater collection system (the System) providing sanitary wastewater service to approximately 3,895 customers in EWT. Application at ¶ 8. Although EWT owns the Malvern Hunt Wastewater Treatment Plant (WWTP), wastewater treatment is mainly provided by the Valley Forge Sewer Authority (VFSA).³ Application at ¶ 15.

On January 8, 2021, Aqua and EWT entered into an APA for the sale of the assets, properties, and rights related to the Township's System at an agreed-upon price of \$54,930,000. Thereafter, Aqua and the Township agreed to use the process presented in Section 1329 of the Code to determine the fair market value (FMV) of the System assets and the ratemaking rate base. As required by Section 1329, Aqua and EWT jointly retained the services of Pennoni Associates, Inc. (Pennoni) to complete the engineering assessment and original cost estimate of the System (Engineering Assessment).

³ In the Application, Aqua stated that Malvern Hunt WWTP was in the process of being decommissioned and converted to a pump station. Following the decommissioning, all wastewater flows will be treated at the VFSA WWTP. EWT, in addition, collects/conveys flow to/from its system from the Borough of Malvern, Tredyffrin Township, Charlestown Township, and Willistown Township, which then flows for treatment at the VFSA. EWT also has several areas of its system that are on the border between EWT and East Goshen Township. While EWT owns the facilities within its borders, flows from these customers are sent to the East Goshen Municipal Authority (EGMA) WWTP. Aqua St. 2 at 5-6.

Aqua St. 1 at 10, 20; Application at ¶ 11. Aqua selected Gannett Fleming, and the Township selected AUS, as their respective UVEs to prepare FMV appraisals of the System. Application at ¶ 53. Gannett Fleming’s FMV report concluded that the value of the System was \$55,668,000; AUS’ FMV was \$57,781,458. Application Exhs. Q and R, respectively.^{4, 5} Both appraisals were prepared in compliance with the Uniform Standards of Professional Appraisal Practice (USPAP) standards. Application at ¶ 61; Application Exhs. T1 and T2.

In its Application, Aqua proposed a ratemaking rate base of \$54,930,000 based on the agreed-to purchase price of \$54,930,000. This amount is less than the average of the two UVE appraisals for the System ($(\$55,668,000 + \$57,781,458)/2 = \$56,724,729$). Application at ¶ 56; *See* 66 Pa. C.S. § 1329(c)(2).

In addition, Aqua is seeking approval of the APA with EWT. Application Exh. B. The APA requires Aqua to implement the Township’s existing rates for the acquired customers upon closing, and for at least three years thereafter. The APA also provides that Aqua’s tariff rules and regulations will apply following closing, and EWT customers will be converted from annual or quarterly to monthly billing. Application Exh. B at Section 7.03. Moreover, in accordance with Section 1102 of the Code, Aqua is requesting a Certificate in order to provide wastewater services to the Township customers. Application at ¶ 5. In addition, Aqua is seeking approval for several other municipal agreements pursuant to Section 507 of the Code. Application at ¶¶ 69, 70. Aqua is also requesting that if the EWT acquisition is completed, the Commission also approve the subsequent assignment of the Wastewater Conveyance Agreement from EWT to Aqua under Section 2102 of the Code. Application at ¶¶ 71, 72. Separate

⁴ Application Exhibit Q, Gannett Fleming Fair Market Value Appraisal Report (hereinafter “Application Exh. Q” or “Gannett Fleming FMV Appraisal”).

⁵ Aqua Application, Exhibit R, AUS Fair Market Value Appraisal Report (hereinafter “Application Exh. R” or “AUS FMV Appraisal”).

customer notices were sent to the Township customers and current Aqua customers informing them of the proposed transaction and the potential rate impact.

III. Public Input Hearing

One public input hearing was conducted telephonically to give the public an opportunity to be heard regarding the acquisition of the Township System by Aqua. The public input hearing was held on March 22, 2022, at 6 p.m., at which six individuals testified in opposition to the acquisition. R.D. at 14-16. We refer to the Recommended Decision for a detailed summary describing the positions of the witnesses who testified at the public input hearing, and which is incorporated herein. *See Id.*

IV. Legal Standards

A. Burden of Proof, 66 Pa. C.S. § 332(a)

As the proponent of a rule or order in this proceeding, Aqua has the burden of proof to establish that it is entitled to the relief it is seeking. 66 Pa. C.S. § 332(a). The Applicant must establish its case by a preponderance of the evidence. *Samuel J. Lansberry, Inc. v. Pa. PUC*, 578 A.2d 600 (Pa. Cmwlth. 1990), *alloc. denied*, 529 Pa. 654, 602 A.2d 863 (1992). That is, the Applicant's evidence must be more convincing, by even the smallest amount, than that presented by any opposing party. *Se-Ling Hosiery, Inc. v. Margulies*, 364 Pa. 45, 70 A.2d 854 (1950). Additionally, this Commission's decision must be supported by substantial evidence in the record. More is required than a mere trace of evidence or a suspicion of the existence of a fact sought to be established. *Norfolk & Western Ry. Co. v. Pa. PUC*, 489 Pa. 109, 413 A.2d 1037 (1980).

B. Certificate of Public Convenience, 66 Pa. C.S. §§ 1102, 1103

Section 1102(a)(1)(i) of the Code requires a utility to first obtain a Certificate prior to beginning to offer or supply utility service to a different territory than that previously authorized by the Commission. 66 Pa. C.S. § 1102(a)(1)(i).

Section 1102(a)(3) of the Code requires a utility to first obtain a Certificate from the Commission prior to a utility or an affiliated interest of a utility to acquire or transfer, to any person or corporation by any method, property used or useful in the public service. 66 Pa. C.S. § 1102(a)(3).

Section 1103(a) of the Code establishes the standard for granting a Certificate required under Section 1102:

A certificate of public convenience shall be granted . . . 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.* The commission, in granting such certificate, may impose such conditions as it may deem to be just and reasonable.

66 Pa. C.S. § 1103(a) (emphasis added); *see also Seaboard Tank Lines v. Pa. PUC*, 502 A.2d 763, 764-65 (Pa. Cmwlth. 1985).

According to the Pennsylvania Supreme Court, satisfying the standard of Section 1103(a) requires the Commission to find that the proposed transaction will “affirmatively promote the service, accommodation, convenience, or safety of the public in some substantial way.” *City of York v. Pa. PUC*, 449 Pa. 136, 141, 295 A.2d 825, 828 (1972) (*City of York*). In establishing this precedent, the Court held that the statute’s clear command is that the Commission must find that the granting of a certificate “will

affirmatively benefit the public.” *Id.* (overruling in part, *Northern Pennsylvania Power Co. v. Pa. PUC*, 333 Pa. 265, 267, 5 A.2d 133, 134).

The Supreme Court further held:

In conducting the underlying inquiry, the Commission is not required to secure legally binding commitments or to quantify benefits where this may be impractical, burdensome, or impossible; rather, the PUC properly applies a preponderance of the evidence standard to make factually-based determinations (including predictive ones informed by expert judgment) concerning certification matters.

Popowsky v. Pa. PUC, 594 Pa. 583, 611, 937 A.2d 1040, 1057 (2007) (*Popowsky*).

Further, the Court explained that demonstration of the affirmative public benefit does not require that every customer receive a benefit from the proposed transaction.

Id. at 617-618, 937 A.2d at 1061. In addition, “in some circumstances conditions may be necessary to satisfy the Commission that public benefits sufficient to meet the requirement of Section 1103(a) will ensue.” *Id.* at n.21. The Commission can, under Section 1103(a), impose conditions that it deems just and reasonable. 66 Pa. C.S. § 1103(a).

One of the factors that the Supreme Court identified in the *City of York* for the Commission to consider, in determining whether there is an affirmative public benefit is:

[A]t least in a general fashion, the effect that a proposed merger is likely to have on future rates to consumers. Along with the likely effect of a proposed merger upon the service that will be rendered to consumers, the probable general effect of the merger upon rates is certainly a relevant criteria of whether the merger will benefit the public.

City of York, 295 A.2d at 829.

In applying this specific factor, the Pennsylvania Commonwealth Court recently held that the Commission must perform “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.” *McCloskey v. Pa. PUC*, 195 A.3d 1055, 1066-1067 (Pa. Cmwlth. 2018), *appeal denied*, 207 A.3d 290 (Pa. 2019) (*McCloskey*) (emphasis added). While *McCloskey* held that rate impact must be addressed, it recognized that “the Commission is charged with deciding whether the impact of rates...is outweighed by ... other positive factors that...served [as] a substantial public benefit.” 195 A.3d at 1067.

The Commission and the courts have held that granting a certificate need not be “absolutely necessary” in order to be in the public interest. *See Hess v. Pa. PUC*, 107 A.3d 246, 262 (Pa. Cmwlth. 2014). The Commonwealth Court reasoned, “[n]ot only would this approach be impractical and unrealistic, it would actually pose a danger to the health, safety and welfare of the public.” *Id.* In addition, when considering the public interest, the Commission may consider how the benefits and detriments impact “*all affected parties*, and not merely one particular group or geographic subdivision.” *Middletown Twp. v. Pa. PUC*, 482 A.2d 674, 682 (Pa. Cmwlth. 1984) (emphasis in original); *see also, Dunk v. Pa. PUC*, 232 A.2d 231, 234-35 (Pa. Super. 1967), *aff’d*, 252 A.2d 589 (1969) (where public benefit included companies and customers other than the proponent utility).

To obtain a Certificate, the acquiring public utility has the burden, by a preponderance of the evidence, to establish that it is technically, legally, and financially fit to provide the proposed service. *McCloskey*, 195 A.3d at 1058. An existing certificate holder is entitled to a “continuing presumption regarding its fitness to operate,” which includes a presumption that the certificate holder has a propensity to operate legally. *Lehigh Valley Transp. Servs., Inc. v. Pa. PUC*, 56 A.3d 49, 58 (Pa. Cmwlth. 2012) (*Lehigh Valley Transp.*); *South Hills Movers, Inc. v. Pa. PUC*, 601 A.2d 1308, 1310

(Pa. Cmwlth. 1992). It is the protestant's burden to rebut that presumption. *Lehigh Valley Transp.* Where an Applicant is both presumed fit and sets forth affirmative evidence demonstrating fitness, this burden is particularly heavy. *Id.*

C. Ratemaking Rate Base Value, 66 Pa. C.S. § 1329

Section 1329 of the Code establishes a process for ratemaking purposes to value the plant of municipal-owned water and wastewater systems to be acquired by certificated public utilities. 66 Pa. C.S. § 1329.⁶ Under Section 1329, the value of water and wastewater system assets to be included in the acquiring utility's rate base for ratemaking purposes will be the lesser of the purchase price negotiated by the acquiring utility and seller or the "fair market value" of the selling utility's system. 66 Pa. C.S. § 1329(c)(2).

The FMV process under Section 1329 where the acquiring utility and the seller must elect and agree to have the FMV of the seller's assets established through separate, independent appraisals conducted by Utility Valuation Experts (UVEs) is voluntary. 66 Pa. C.S. § 1329(a). The Commission maintains a list of qualified UVEs from which the acquiring utility and seller must choose their respective appraisers. 66 Pa. C.S. §§ 1329(a)(1), (2).

The UVEs must prepare an appraisal of the seller's system assets in compliance with the USPAP, employing the Cost, Market and Income Approaches. 66 Pa. C.S. § 1329(a)(3). The FMV of the system is defined as the average of the two separate UVE appraisals conducted in compliance with Section 1329(a)(3). 66 Pa. C.S. § 1329(g).

⁶ Governor Wolf signed into law Act 12 of 2016 (Act 12) on April 14, 2016. This Act amended Chapter 13 of the Code by adding a new section, Section 1329, which became effective on June 13, 2016. 66 Pa. C.S. § 1329.

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).

D. Utility-Municipal Contracts, 66 Pa. C.S. § 507

Section 507 of the Code provides as follows regarding a utility's contract with a municipal corporation:

Except for a contract between a public utility and a municipal corporation to furnish service at the regularly filed and published tariff rates, no contract or agreement between any public utility and any municipal corporation shall be valid unless filed with the commission at least 30 days prior to its effective date. Upon notice to the municipal authorities, and the public utility concerned, the Commission may, prior to the effective date of such contract or agreement institute proceedings to determine the reasonableness, legality or any other matter affecting the validity thereof. Upon the institution of such proceedings, such contract or agreement shall not be effective until the Commission grants its approval thereof.

66 Pa. C.S. § 507. Thus, pursuant to Section 507, the Commission has discretionary power to institute proceedings to determine the reasonableness, legality and validity of the contracts between a municipality and a public utility. *Id.*; *see also County of Allegheny v. Pa. PUC*, 159 A.2d 227, 233 (Pa. Super. 1960).

E. Affiliated Interest Agreements, 66 Pa. C.S. § 2102

Regarding a utility's contract with an affiliated interest, as defined in 66 Pa. C.S. § 2101, Section 2102 of the Code states, in pertinent part, as follows:

a) . . . No contract or arrangement for the purchase, sale, lease or exchange of any property, right or thing or for the furnishing of any service, property, right or thing . . . made or entered into after the effective date of this section between a public utility and any affiliated interest shall be valid or effective unless and until such contract or arrangement has received the written approval of the commission

(b) . . . The commission shall approve such contract or arrangement made or entered into after the effective date of this section only upon investigation that it is reasonable and consistent with the public interest. . . .

66 Pa. C.S. § 2102. Therefore, pursuant to Section 2102, the Commission shall review contracts between a utility and an affiliated interest to determine whether it is legal, reasonable and consistent with the public interest.

F. Settlements in the Public Interest

Pursuant to our Regulations at 52 Pa. Code § 5.231, it is the Commission's policy to promote settlements. A full settlement of all the issues in a proceeding eliminates the time, effort and expense that otherwise would have been used in litigating the proceeding, while a partial settlement may significantly reduce the time, effort and expense of litigating a case. A settlement, whether whole or partial, benefits not only the named parties directly, but, indirectly, all customers of the public utility involved in the case. *Pa. PUC, et al. v. Columbia Gas of Pennsylvania, Inc.*, Docket Nos. R-2015-2468056, *et al.* (Order entered December 3, 2015) at 6-7. Despite this policy, the Commission does not simply rubber stamp settlements without determining whether the terms are in the public interest. *Pa. PUC v. Philadelphia Gas Works*, Docket No. M-00031768 (Order entered January 7, 2004); *Pa. PUC v. CS Water and Sewer Assoc.*, 74 Pa. P.U.C. 767 (1991); *Pa. PUC v. Philadelphia Electric Co.*, 60 Pa. P.U.C. 1 (1985).

G. General Standards

In the Recommended Decision, ALJ Guhl made fifty-nine Findings of Fact and reached twenty-seven Conclusions of Law. *See* R.D. at 5-14, 59-63. The Findings of Fact and Conclusions of Law are incorporated herein by reference and are adopted without comment unless they are either expressly or by necessary implication rejected or modified by this Opinion and Order.

As we proceed in our review of the various positions of the Parties in this proceeding, we are reminded that the Commission is not required to consider expressly or at length each contention or argument raised by the parties. *Consolidated Rail Corp. v. Pa. PUC*, 625 A.2d 741 (Pa. Cmwlth. 1993); *also see, generally, University of Pennsylvania v. Pa. PUC*, 485 A.2d 1217 (Pa. Cmwlth. 1984). Exceptions that we do not specifically address shall be deemed to have been duly considered and denied without further discussion.

V. Discussion

A. Section 1102/1103 Analysis

1. Substantial Affirmative Public Benefits

a. Positions of the Parties

Aqua claimed that the proposed transaction will provide substantial affirmative public benefits to both existing Aqua customers and the acquired EWT customers. In support, the Company asserted that it provides utility service to approximately 45,000 wastewater customers; has years of experience operating wastewater treatment and collection systems in a safe, reliable and efficient manner; has

the managerial, technical, and financial resources to continue to operate, maintain and improve the EWT System; and has acquired sixteen wastewater systems over the past ten years, many of which required significant investment to correct service and environmental issues. Aqua M.B. at 10.

Aqua also cited the Commission's long-standing record of support for consolidation and regionalization of water and wastewater systems. The Company submitted that the Commission understands that in doing so, the utility industry will realize the benefits of better management practices, economies of scale, and resulting in greater customer, environmental, and economic benefits. According to Aqua these types of acquisitions will enhance the quality of ratepayers' daily lives, promote community economic development, and provide environmental enhancements. *Id.* at 11.

Regarding the benefits to the Township, Aqua argued that EWT's customers will become part of a larger scale, efficiently operated, wastewater utility and the operational overlap between water and wastewater utility operations will provide the opportunity for better coordination of capital activities throughout the EWT service area. The Company projected lower operation and maintenance (O&M) costs under Aqua's ownership that will likely be realized through reductions in costs for wastewater maintenance, as well as efficiencies in administrative and general costs, such as insurance, auditing and legal, among others. Specifically, referencing the EWT 2020 Financial Statements, Aqua noted that the Sewer Fund Operating Expenses were approximately \$2.8 million whereas the Company is projecting annual expenses of approximately \$2.0 million. In addition, Aqua estimated that it will invest approximately \$16.92 million in the System over the next ten years, including upgrades to pump stations, force mains and gravity collection systems based on conditions observed, facility age and safety; resulting in benefits to Township customers. Aqua M.B. at 12.

Aqua further asserted that the acquisition will provide enhanced customer service for EWT customers by providing customer service through a toll-free number from 8 a.m. to 5 p.m. EST for regular business and 24/7/365 emergency response. The Company proffered that Township customers will be able to take advantage of Aqua's online bill payment option, including payment by text message, the ability to sign up for notifications and alerts to be sent to their email address or phone, allowing them to stay informed of events impacting their service, as well as having access to Aqua's customer assistance programs. Aqua M.B. at 12.

Aqua contended that the acquisition will provide enhanced customer billing and payment protections under Chapter 14 of the Code that provide for billing, payment, collection, termination and reconnection of service, payment arrangements, medical certifications, and formal and informal complaint procedures. The Company also noted that its customer care teams would be available to help resolve service and billing issues and has an established procedure for addressing formal and informal complaints. *Id.*

Regarding benefits to existing Aqua customers, the Company argued that the acquisition of the System will provide an approximate 9% increase in Aqua's customer base. By virtue of the Company's larger customer base, Aqua submitted that future infrastructure investments across the state will be shared at a lower incremental cost per customer for all of Aqua's customers; and that, based on Township records, EWT has approximately 7,658 equivalent dwelling units (EDU), which equates to approximately \$7,200 purchase price per connection and is almost equal to the Company's existing rate base per EDU, projected at approximately \$7,000. Given the similarities in purchase price per connection to rate base per EDU, combined with lower operating cost, Aqua proffered that the EWT System will provide economies of scale that can be achieved as a result of this acquisition. *Id.* at 12-13.

Aqua contended that the acquisition will not have an adverse effect on the service provided to existing customers of Aqua; and that the acquisition will not have any immediate impact on the rates of either existing customers of Aqua or existing customers of EWT. The Company also noted that it will implement the existing Township base rates upon closing, but will apply existing miscellaneous fees and charges in the Company's tariff. *Id.* at 13.

Aqua further submitted that any hypothetical rate impact is outweighed by affirmative public benefits. The Company stated that the current average monthly bill of an EWT residential customer is approximately \$33.33 per EDU. Applying 100% of the revenue deficiency of \$5,011,000 associated with the proposed rate base addition to the existing Township rates, Aqua asserted that the average EWT bill would increase to approximately \$77.64 per month or an 132.93% increase. However, Aqua argued that the calculation and percentage increase is a point in time estimate reflective of revenue deficiency upon year one ownership, and although there is an expectation of increased rates going forward, Aqua asserted it is not proposing any change in rates to EWT customers as part of this transaction. Aqua indicated that the proposed rate changes for EWT customers will be presented in an Aqua base rate proceeding subsequent to the closing of the acquisition. *Id.* at 13-14.

Aqua argued that the hypothetical rate impact is outweighed by other positive benefits. The Company submitted that, although the rates of the EWT System are reasonably expected to increase, either on their own, or after acquisition by the Company, the proposed transaction provides more flexibility and opportunity to deal with those impacts over a much larger customer base. In further support, Aqua submitted that the EWT System has characteristics that demonstrate that economies of scale can be achieved as a result of this acquisition; and that the transaction furthers a recognized legislative objective and is consistent with the Commission's policy in favor of consolidation and regionalization policy. *Id.* at 14-15.

EWT supported the arguments of Aqua and asserted that the Township's customers will benefit from the expertise and experience of a regulated public utility such as Aqua. The Township added that the up-front proceeds from the proposed transaction will enable EWT to reduce its debt and fund other projects in the Township. EWT M.B. at 9-10.

Although the Township acknowledged that it currently provides adequate service to its residents, EWT asserted that this service takes a significant amount of time and attention of the Township's staff. In support, EWT noted that the Township's Director of Public Works Department currently dedicates approximately 50% of his time operating and managing the System, leaving about half of his time to tend to his various other responsibilities as Director of Public Works such as maintenance of EWT's roads, parks, and traffic. *Id.* at 10.

I&E argued that, in order to ensure that the Company's asserted benefits will materialize, the Commission should approve Aqua's Application subject to I&E's recommended conditions. I&E M.B. at 7-10.⁷

The OCA asserted that the Application fails to meet the appropriate legal standard, because it would harm existing and acquired ratepayers and would not provide substantial affirmative public benefit. Specifically, the OCA noted that the Township's balance sheet will benefit from the proposed transaction and that the Township will receive 64% more than the net book value of the System. Further, the OCA acknowledged Aqua's anticipated spending of \$16.92 million for capital improvements to the EWT System during the next ten years. However, the OCA argued that there is no

⁷ As discussed *infra*, I&E proposed several conditions pertaining to a separate cost of service study for the EWT System, rejection of the three-year rate freeze proposal, and identification of missing easements and other transaction requirements related to such easements. I&E M.B. at 9-10.

support for concluding that existing Aqua wastewater and water customers will receive any net benefit or that the EWT customers will see a net benefit after their rate freeze ends. Accordingly, the OCA contended that Aqua failed to demonstrate the necessary public benefits required for approval of the Application. OCA M.B. at 11.⁸

In its Main Brief, the OSBA took no position on the issue of substantial affirmative public benefits. OSBA M.B. at 13.

b. Recommended Decision

The ALJ found a lack of evidence to establish that the System under Aqua's ownership would affirmatively promote the service, accommodation, convenience, or safety of the public. In addition, the ALJ determined that the evidence did not establish that any benefit to be realized from the proposed transaction would outweigh the harms to current Aqua water and wastewater customers or existing EWT sewer customers. Accordingly, the ALJ recommended that the Application be denied. R.D. at 59.

As an initial matter, the ALJ noted that in order to determine if the proposed transaction provides a substantial affirmative benefit, it is necessary to consider the fitness of the purchasing entity to provide the service, the adequacy of the existing service and any other relevant evidence. According to the ALJ, the evidence clearly established the public need for the service and Aqua's fitness to provide the proposed service. The ALJ explained that no Party presented a substantial challenge to Aqua's fitness and the Company outlined in detail the evidence to support its claim that it

⁸ For a summary of the OCA's briefing arguments in opposition to the Company's position on substantial affirmative public benefits, see pages 35-44 of the Recommended Decision.

possesses the legal, financial, technical and managerial fitness to provide the service provided proposed in its Application. R.D. at 51, 53.

Regarding affirmative public benefits, the ALJ addressed the following five areas of consideration: (1) harm to existing Aqua wastewater and water customers; (2) harm to EWT customers; (3) whether the adverse impacts to the existing customers of Aqua and EWT outweigh the benefits of the transaction; (4) economies of scale; and (5) volume discounts and cost sharing. R.D. at 53-59.

Under the first consideration, the ALJ determined that Aqua's existing water customers are at risk in the short term of being required to support the costs of acquiring the EWT customers in this transaction. The ALJ noted that all Aqua water customer are already required to pay for wastewater disposal either to another provider, to Aqua, or with their individual wastewater system. In addition, the ALJ rejected Aqua's characterization of an anticipated rate increase as hypothetical. According to the ALJ, a rate increase to existing Aqua customers, at least in the short term, is a certainty. R.D. at 53-54.

In support, the ALJ noted other Section 1329 acquisitions pending or approved since Aqua's last base rate case.⁹ The ALJ considered these other Section 1329 acquisitions, for which the Company projects revenue requirement deficiencies, as likely resulting in increased rates for acquired or existing customers in the short term and

⁹ Here, the ALJ is referring generally to the acquisitions of Lower Makefield Township, the Delaware County Regional Water Quality Authority (DELCORA), and Willistown Township. *See generally, Application of Aqua Pennsylvania Wastewater, Inc. Pursuant to Sections 1102 and 1329 of the Public Utility Code for Approval of its Acquisition of the Wastewater System Assets of Lower Makefield Township*, Docket No. A-2021-3024267 (Order entered January 13, 2022) (*Lower Makefield*); *Application of Aqua Pennsylvania Wastewater, Inc. (DELCORA)*, Docket No. A-2019-3015173; and *Application of Aqua Pennsylvania Wastewater, Inc. (Willistown)*, Docket No. A-2021-3027268.

delaying any potential benefits to customers from cost sharing further into the future. The ALJ added that Aqua's proposed three-year rate freeze for EWT customers would compound the expected harm to the Company's customers. Acknowledging Aqua's uncertainty whether or not it will file a base rate case within three years of closing, the ALJ determined that Aqua's customers would be at risk to cover the revenue requirement required to keep EWT rates lower than cost for the first three years following the closing of this transaction. R.D. at 54.

Regarding the second consideration of affirmative public benefits, the ALJ emphasized that approximately six Aqua or EWT customers testified at the public input hearing regarding anticipated harms resulting from the proposed acquisition. The ALJ reasoned that existing EWT customers testified that the Township's System is operating well and does not have any issues providing service to its existing customers. Also, the ALJ highlighted Aqua customers testified that Aqua's service to water customers had not been adequate. The ALJ stated that EWT acknowledged that it has the means to service its existing and future customers and complete needed upgrades in the future. *Id.*

Regarding the third consideration, the ALJ found that the purported benefits of acquiring the Township's System did not outweigh the adverse impacts of the proposed transaction. Rather, the ALJ concluded that the proposed acquisition would detrimentally impact wastewater customers in EWT due to anticipated increased rates without providing any substantial or necessary benefits to Township customers. The ALJ also determined that the proposed transaction increased costs for Aqua's customers until and unless the EWT customers' rates increase to cover the \$5,011,000 revenue deficiency estimated by Aqua. R.D. at 57.

In support, the ALJ cited the current average monthly bill of an EWT residential customer as approximately \$33.00 per month. Applying 100% of the revenue deficiency of \$5,011,000 associated with the proposed rate base addition to the existing

EWT rates, the ALJ emphasized that the average EWT bill would increase to approximately \$77.64 per month or an 132.93% increase. Thus, the ALJ noted EWT customers will experience significant rate increases if the System is acquired by Aqua. R.D. at 54-55.

According to the ALJ, Aqua did not establish that the purported benefits of acquiring the EWT System outweigh the adverse impacts of the proposed transaction and that the potential rate impact outweighs the various positive benefits asserted by Aqua. Although Aqua references economies of scale, the ALJ opined the Company has not established the existence of net cost reductions or efficiencies that will be produced by the acquisition of the EWT customers. Further, the ALJ stated that EWT customers would not even be covering their full cost of ownership at the proposed \$54.93 million rate base, and would not share the costs of infrastructure improvements for other parts of Aqua's service territory. Additionally, the ALJ found no evidence that rates would become more affordable in the long-term due to economies of scale. R.D. at 55.

Furthermore, the ALJ found that any advantages realized by Aqua's billing systems and services and protections under Chapter 14 of the Code are outweighed by the costs ratepayers would bear based on the transaction. Moreover, the ALJ rejected the argument that EWT customers would have safer and more reliable service under Aqua's ownership. Here, the ALJ stated that EWT is not a troubled system and the Township's current service is safe and reliable. R.D. at 56-57.

The ALJ noted that the Township's System has the capacity to meet the demands of current and future customers, did not have any sanitary system overflows in 2020, and is not currently under a Corrective Action Plan or Connection Management Plan with the Pennsylvania Department of Environmental Protection (DEP). Additionally, the ALJ credited the financial fitness of the Township and its ability to

complete any necessary improvements or upgrades noting that EWT has over \$29 million in cash and cash equivalents. *Id.*

Regarding the fourth consideration pertaining to economies of scale, the ALJ reasoned that an individualized analysis of every system is necessary to ensure that each acquisition complies with the Code, particularly Section 1102. According to the ALJ, a showing of only technical, managerial, financial ability to acquire and operate a system is insufficient to support a finding furthering the public interest. The ALJ reiterated that it is necessary to show that the benefits substantially outweigh the harms and that Aqua did not establish such a showing. R.D. at 57-58.

In the fifth and final consideration, the ALJ examined volume discounts and sharing of costs. The ALJ concluded that many of the arguments of the Company were anticipated general benefits unsupported by the record. Although the ALJ acknowledged that Aqua's size creates the potential for volume discounts and cost sharing, the ALJ highlighted the Company's higher cost of capital. The ALJ reasoned that the Township has the ability to make any necessary improvements to the System at a more attractive financing cost than Aqua could obtain and that the Township would not have to raise rates for an equity return on a \$54.93 million purchase price because the Township already owns the System. In addition, the ALJ stated that the Township rates do not include dividends for shareholders, depreciation expense, Pennsylvania sales tax, or Pennsylvania or Federal taxes on revenues and that the Township's financing cost would be approximately two to three times lower than Aqua's financing cost. R.D. at 58-59.

Further, the ALJ reasoned that Aqua failed to establish that it can improve on the Township's quality of service, operations, convenience, and safety. The ALJ cited the Company's ability to terminate service subject to the Commission's Regulations and protections and noted that such a result could not occur under Township ownership. The

ALJ also found that the evidence also failed to establish that Aqua's operation of the System will be safer than the Township's operations as no real difference was demonstrated regarding Aqua or the Township's ability to bring skilled experienced resources to the operation of the Township's System. *Id.* at 60.

c. Exceptions and Replies

In its Exception No. 1, Aqua excepts to the conclusion that it failed to establish an affirmative public benefit to the acquisition of the EWT System. Aqua argues its acquisition of the EWT System is supported by substantial affirmative public benefits, including those cited by the Commonwealth Court in *McCloskey*. To support this position, Aqua maintains *McCloskey* focused on two Commission findings as substantial evidence sufficient to support a conclusion that there is a public benefit to an Aqua Section 1329 transaction:

- 1) Aqua, as the owner of numerous water and wastewater systems has sufficient operational expertise and ability to raise capital to support system operations; and
- 2) The Commission has a policy of consolidation/regionalization of wastewater system assets that allows for increased maintenance, upgrade and expansion of public sewer and water facilities.

Aqua contends substantial evidence supports these same findings in this proceeding and a conclusion that there are substantial affirmative public benefits to this Transaction. Further, the Company asserts no more needs to be determined to support Commission approval of this Section 1329 acquisition. Aqua Exc. at 4-5.

Aqua claims the Recommended Decision failed to properly apply the *Popowsky* standard by requiring a quantification of public benefits that is not required by *Popowsky*. The Company avers:

Popowsky explains that, in certification matters, the Commission properly applies a preponderance of the evidence standard to make factually based determinations (including predictive ones informed by expert judgment) and that the Commission is not required to secure legally binding commitments or to quantify benefits where this may be impractical, burdensome or impossible.

Aqua Exc. at 8.

Aqua states the Commission should apply a preponderance of the evidence standard as explained in *Popowsky*, recognizing its authority to make factually based determinations (including predictive ones informed by expert judgment). The Company asserts quantification of public benefits or legally binding commitments are not required. Aqua claims the benefits presented in the record are substantial evidence in support of the Transaction. Therefore, Aqua proclaims the Commission should reject the Recommended Decision and approve the Transaction. Aqua Exc. at 13.

Finally, Aqua addressed the ALJ's analysis of harms of the Transaction on three specific groups: (1) existing Aqua wastewater customers, (2) existing Aqua water customers, and (3) EWT customers who will be transferred to Aqua. The Company claims that neither existing Aqua customers nor EWT customers will be harmed by the acquisition. Aqua states any perceived harm to customers is offset by benefits resulting from the transaction and is fully addressed in its Exception No. 2. Aqua Exc. at 13.

In its Exception No. 2, Aqua excepts to the conclusion that adverse impacts on its existing customers and the EWT customers outweigh the benefits of the proposed transaction. The Company argues that the ALJ departs from the balancing test

recognized in *Cheltenham*,¹⁰ citing *McCloskey* and *Popowsky*. Aqua states, rather than a weighing of all factors for and against a transaction, including the impact on rates, the ALJ concentrates on short-term rate impact. Aqua states the ALJ's decision:

...accepts that the transaction will result in a revenue deficiency of \$5.011 million and then looks for counterbalancing dollar benefits in either economies of scale or volume discounts / sharing costs, requiring, in effect, a dollars-and-cents, cost-benefit type analysis.

Aqua Exc. at 17.

Aqua excepts to the conclusion that the evidence did not establish that any benefit to be realized from the proposed transaction would outweigh the harms to current Aqua and EWT customers and the dispositive effect given to potential short-term rate impact. *Id.* at 17-18.

The Company claims the ALJ erred by accepting the OCA's argument that individualized analysis of every system is in the public interest and required by Section 1102. Aqua contends that by increasing its customer base, it provides more service to more customers for less incremental cost. The Company states this is a recognized public benefit consistent with the Commission's policy supporting regionalization/consolidation and single tariff pricing. Contrary to the ALJ, Aqua states an individualized economic analysis of the EWT System is inconsistent with the public interest and adverse to the basic public utility model. Aqua Exc. at 18.

¹⁰ *Application of Aqua Pennsylvania Wastewater, Inc. Pursuant to Sections 1102, 1329 & 507 of the Public Utility Code for Approval of its Acquisition of the Wastewater System Assets of Cheltenham Twp. & Contracts between Aqua Pennsylvania Wastewater, Inc. & Cheltenham Twp.*, Docket No. A-2019-3008491 (Order entered November 5, 2019) at 39 (*Cheltenham*).

Next, Aqua claims that the ALJ erred by determining Aqua's higher cost of capital would not offset savings realized through volume discounts and cost sharing. The Company notes *Popowsky* does not require the Commission to quantify benefits where this may be impractical, burdensome, or impossible. In this case, Aqua asserts that the long-term cost benefits of the acquisition cannot be currently quantified. The Company notes it provided specific, tangible examples of short-term economies of scale and benefits, showing a 29% decrease in expenses with Aqua ownership. Aqua Exc. at 19.

Finally, the Company believes the ALJ erred, after determining a rate deficiency, by finding that EWT customers will not receive a benefit that outweighs the estimated rate increase. Aqua notes the amount of a rate increase will be determined in an Aqua base rate case and will be dependent on how the Commission chooses to apportion an increase among Aqua's acquired and existing customers. However, contrary to *Popowsky*, Aqua argues the ALJ's focus on rate impacts minimizes or fails to account for the aspirational and other public benefits of the Transaction. Further, the Company notes that "[w]hile *McCloskey* concludes that rate impact should be addressed, it recognizes that it is not dispositive in the Commission's determination of substantial affirmative benefits." Aqua Exc. at 20-23.

Therefore, Aqua states the Commission should reject the ALJ's decision and approve the Transaction. Aqua Exc. at 23.

In its Replies to Aqua Exc. No. 1, the OCA claims the ALJ properly determined that Aqua has failed to demonstrate the necessary public benefits required for approval of a Section 1329 transaction. Based on the *City of York*, the OCA states Aqua must show that benefits will substantially outweigh the harms for each transaction. The OCA argues Aqua cannot use *McCloskey* to claim that only two Commission findings, Aqua's expertise and the Commission's policy of consolidation/regionalization, are needed to support a conclusion that there is a public benefit to its Section 1329

transaction. In *McCloskey*, the OCA points out the Commonwealth Court reversed the Commission for failing to consider rate impact in its determination. OCA R. Exc. at 1-2.

The OCA contends the ALJ correctly applied the *Popowsky* standard and Aqua incorrectly surmises the ALJ demanded a quantification of benefits. Consistent with *Popowsky*, the OCA asserts the ALJ considered and reached a determination based on the record evidence about the benefits claimed by Aqua in both the short and long term. OCA R. Exc. at 5.

In its Replies to Aqua Exc. No. 2, the OCA rejects Aqua's claim the ALJ gave too much weight to the short-term rate impact of the Transaction. The OCA states the ALJ correctly followed the precedent in *McCloskey* by considering rate impact along with all of the record evidence provided by Aqua regarding claimed benefits of the transaction, including economies of scale, volume discounts, quality of service, billing and payment options and EWT's interest in selling its System for \$54.93 million. OCA R. Exc. at 6-7.

In its Exception No. 1, EWT excepts to the ALJ's conclusion that the Application should be denied because Aqua failed to establish that the Transaction will affirmatively promote the service, accommodation, convenience, or safety of the public and the evidence did not establish any benefit to be realized from the Transaction would outweigh the harms to current Aqua water and wastewater customers or existing EWT wastewater customers. The Township considers the only identified harm of the Transaction is a potential rate increase. However, EWT disagrees that the record evidence does not illustrate that the potential rate impacts are outweighed by the various benefits of the Transaction. In support of benefits to its customers, the Township asserts that there are numerous examples of benefits that would be realized under Aqua ownership. Therefore, EWT believes when considering both qualitative and quantitative

benefits of the Transaction, Aqua has satisfied its burden under section 1102 of the Code. EWT Exc. at 2-5.

In its Exception No. 2, EWT argues the ALJ created a precedent that municipal systems must be in dire circumstances in order to be sold under the Code. EWT reiterates its assertion that Aqua has satisfied its burden to prove that the Transaction on the whole will affirmatively promote the service, accommodation, convenience or safety of the public. Even though the Township is financially sound and provides reliable customer service, it notes the Code does not require a system to be distressed or residents to suffer from poor operational management before a municipality is permitted to sell its system. Consequently, EWT disagrees with the ALJ's recommended denial of the Transaction based on the Township's financially sound position and excellent service. EWT Exc. at 6-7.

The OCA's Replies to EWT Exception No. 1 are unified and incorporated in its Replies to Aqua Exception No. 2. OCA R. Exc. at 6.

In its Replies to EWT Exception No. 2, the OCA claims EWT misinterprets the ALJ's decision. Based on the record evidence, the OCA states the ALJ determined that the Township does not operate a troubled system. Therefore, to meet the *City of York* standard, the OCA argues Aqua needed to establish that other benefits would result from the transaction and that those benefits are substantial enough to outweigh the harms. The OCA concurs with the ALJ's decision that Aqua did not meet this burden and does not create a new precedent requiring a municipal system to be in dire circumstances in order to sell its system. OCA R. Exc. at 13-15.

d. Disposition

Upon review of the evidentiary record and after application of the balancing test required under Section 1102 of the Code, we find that Aqua has proven that it is technically, legally, and financially fit to acquire the Township's System, and has demonstrated that the acquisition has substantial affirmative public benefits that outweigh the purported harms asserted by the OCA.

As set forth in the Commonwealth Court's decision in *McCloskey*, our obligation in performing "the balancing test under Section 1102 of the Code [is] to weigh all the factors for and against the transaction, including the impact on rates, to determine if there is a substantial public benefit." *McCloskey*, 195 A.3d at 1066 (applying *City of York*). We are further "charged with deciding whether the impact of rates ... is outweighed by ... other positive factors that ... served [as] a substantial public benefit." *Id.* at 1067. Moreover, the Pennsylvania Supreme Court has explained that "in some circumstances conditions may be necessary to satisfy the Commission that public benefits sufficient to meet the requirement of Section 1103(a) will ensue." *Popowsky*, 937 A.2d at 1061, n.21. The Commission has consistently applied this balancing test for evaluating whether to issue Certificates in Section 1329 proceedings. *See, e.g., Cheltenham, Application of Pennsylvania-American Water Company – Valley Township*, Docket Nos. A-2020-3019859 and A-2020-3020178 (Order entered October 28, 2021), and *Lower Makefield*.

As summarized above, the ALJ recommended rejection of the Application due to the Company's failure to show that its ownership of the Township's System would affirmatively promote the service, accommodation, convenience, or safety of the public. The ALJ concluded that no benefits to the proposed transaction would outweigh the harms to current Aqua water and wastewater customers or existing EWT customers. In addition, the ALJ rejected the Company's contention that the acquisition would create

economies of scale and that Aqua's size creates the potential for volume discounts and cost sharing. R.D. at 53-59.

In their respective Exception Nos. 1 and 2, Aqua and the Township each object to the ALJ's conclusions and argue that the proposed transaction is supported by substantial affirmative public benefits. In support, Aqua proffers that it has presented evidence similar to the public benefits recognized by the Commission and the Commonwealth Court in *McCloskey*. That is, the Company asserts that: (1) Aqua, as the owner of numerous water and wastewater systems has sufficient operational expertise and ability to raise capital to support system operations; and (2) the Commission has a policy of consolidation/regionalization of wastewater system assets that allows for increased maintenance, upgrade and expansion of public sewer and water facilities. In addition to the public interest benefits recognized in *McCloskey*, Aqua cites to testimony pertaining to the following: benefits to existing Aqua customers; benefits to EWT's customers; enhanced customer service for EWT customers; enhanced customer billing and payment protections; no adverse effect to the transaction; and the Township's desire to sell its System. Aqua Exc. 5-23.

In its Replies to Exceptions, the OCA objects that the Company's Application merely relies on the Commission's promotion of regionalization and consolidation and circumvents the Commission's review process. Moreover, as summarized above, the OCA relies heavily on the anticipated rate impact on Aqua's and the Township's customers which they contend outweighs any purported benefits to the transaction. For example, the OCA emphasizes the ALJ's rationale that the proposed transaction could increase rates as much as 133% for EWT customers, 5% for existing Aqua wastewater customers, and 0.4% for existing Aqua water customers depending on how the \$5.011 million revenue shortfall is apportioned between customers. OCA R. Exc. at 3 (citing R.D. at 36-37, 39).

Overall, the OCA supports the weighing of evidence conducted by the ALJ regarding the harms and benefits specific to the EWT acquisition and the conclusion that it would not serve the public interest. In particular, the OCA argues that the existing EWT customers would receive no detectable improvement in their service and, in many cases, lose existing benefits. It references, in part, the ALJ's rationale as follows:

- Aqua has not established that it can improve on the Township's quality of service, operations, convenience or safety;
- Aqua can terminate water service for non-payment of wastewater service subject to Commission Regulations, whereas the Township cannot;
- The Township already has the ability to address emergencies and there was no evidence that EWT customers have any problems with their current billings and payments to the Township;
- The Township is financially fit with more than \$29 million in cash and cash equivalents, including a Sewer Fund increase to cash and cash equivalents of \$500,000 in 2020 alone, and thus it could make the anticipated capital improvements over the next ten

years without an unreasonable financial burden for the Township.

See OCA R. Exc. at 10-11 (citing R.D. at 56-57, 59).¹¹

In the seminal Section 1329 case in *McCloskey*, the Commonwealth Court considered the Commission’s findings that Aqua, as the Applicant in that proceeding and as owner of numerous water and wastewater systems, had sufficient expertise and ability to raise capital to support system operations. The Court also acknowledged the finding that the Commission has a policy in support of consolidation and regionalization of wastewater system assets that allows for increased maintenance, upgrade and expansion of public sewer and water facilities. In its rationale, the Court stated that these Commission findings were of the type that the Pennsylvania Supreme Court in *Popowsky* held were sufficient to meet the Section 1103 public benefit standard. “As per [*Popowsky*], these *aspirational statements are substantial evidence* to support the notion that there is a public benefit for the merger.” *McCloskey*, 195 A.3d at 1065 (emphasis added).

¹¹ In its Replies to the Exceptions, the OCA argues that “Aqua must show that benefits will *substantially* outweigh the harms.” OCA R. Exc. at 2 (emphasis added) (citing *City of York*). Although the Applicant in a Section 1329 proceeding must establish that there are substantial public benefits pursuant to the Section 1102 balancing test, the Applicant is not required to establish that the benefits *substantially* outweigh the harms. Rather, the burden of proof requires the Applicant to establish its case by a preponderance of the evidence, *see* 66 Pa. C.S. § 332(a) and *Lansberry*; that is, the evidence in this and in all Commission-related proceedings requires the evidence to be more convincing, by even the smallest amount, than that presented by the other Parties, *see Se-Ling Hosiery*. Our consideration, therefore, is whether the evidence demonstrates that the proposed transaction will affirmatively promote the service, accommodation, convenience, or safety of the public in some substantial way. *City of York*, 295 A.2d at 828. This does not require us to determine whether the benefits substantially outweigh the harms, nor could such a requirement be practically measured in light of the directive that the Applicant is not required to quantify benefits if impracticable, burdensome, or impossible. *Popowsky*, 937 A.2d at 1057.

Regarding its ownership of wastewater systems and operational expertise, Aqua cited its record of acquiring and improving wastewater systems by establishing that:

- The Company provides utility service to approximately 45,000 wastewater customers and has years of experience operating wastewater treatment and collection systems in a safe, reliable, and efficient manner. Additionally, Aqua has the managerial, technical, and financial resources to continue to operate, maintain and improve the EWT System. Aqua St. 1 at 14 and Aqua Exh. 1, Application ¶ 52.d.
- Aqua has acquired sixteen wastewater systems over the past ten years with many of these systems requiring significant investment to correct service and environmental issues.¹² The Company testified that the inherent diversification of systems and customers provides a foundation of stability in that, they are all not requiring major capital investments at the same time, and thereby, spreading the financial impacts over the long-term operations of the acquiring utility as a whole. Aqua St. 1 at 14.

Moreover, no Parties credibly disputed Aqua's fitness to become a certificated provider of the Township's System. Indeed, as an existing certificated utility, Aqua's fitness is presumed. Regarding financial fitness specifically, Aqua established that it is a Class A wastewater utility with total assets of \$350 million, annual revenues of \$32 million, and, as subsidiary of the Aqua Pennsylvania Water, Inc. (Aqua Water), has access to Aqua Water's financing capabilities. Aqua St. 1 at 9-11. Accordingly, Aqua

¹² Aqua referenced the following systems which it has acquired: New Garden, East Norriton (2020); Cheltenham (2019); East Bradford, Limerick (2018); Tobyhanna, Avon Grove (2017); Emlenton, Honeycroft (2016); Bunker Hill (2015); Penn Township (2014); Treasure Lake (2013); and Sage Hill, Kidder Township, Beech Mountain, Village at Valley Forge (2012). Aqua M.B. at 13.

has provided substantial evidence pertaining to its ability to raise capital to support system operations.

Additionally, Aqua established that it is able to provide seamless management, customer service, regulatory compliance, engineering, financial, and ancillary services from the Company's Southeastern Division Office in Bryn Mawr. Moreover, the Company plans to hire three additional operators to address day-to-day operations of the EWT System and may be used in other Aqua systems in the area. Currently, Aqua has twenty-seven wastewater operators, with many holding dual water and wastewater certifications who may be called upon to assist in the operation of the system. Aqua St. 2 at 15-16.

In support of its operational and technical expertise, Aqua emphasized its work with the Commission and the statutory advocates to acquire and improve troubled wastewater systems, citing Washington Park Wastewater, Docket No. A-230550F2000. The Company also highlighted its appointment as receiver of the North Heidelberg Sewer Company in Berks County and its oversight of daily wastewater operations of the facility serving approximately 274 customers on March 5, 2018. Aqua St. 2 at 17-18.

As to the Commission policy of consolidation and regionalization of wastewater system assets, Aqua testified that if it were permitted to acquire only non-viable systems, rather than a mix of viable and non-viable systems, such a directive would have a significant impact on its existing customers' rates and service. According to the Company, both types of systems, viable and non-viable, are consistent with the Commission's policy statements regarding acquisitions. Aqua proffered that the acquisition of the EWT System will continue to address the Commission's supported policy of consolidation and regionalization. Aqua St. 1 at 14-15.

In support, Aqua cited to the Commission's long-standing record of support for consolidation and regionalization of water and wastewater systems. Aqua St. 1 at 13-14 (citing, *Final Policy Statement on Acquisitions of Water and Wastewater Systems*, Docket No. M-00051926 (Order entered August 17, 2006) (*2006 Final Policy Statement*)). There, we stated:

[A]cquisitions of smaller systems by larger more viable systems will likely improve the overall long-term viability of the water and wastewater industry. Additionally, these types of acquisitions will also enhance the quality of ratepayers' daily lives, promote community economic development and provide environmental enhancements. We strongly believe that these types of acquisitions generally serve public policy goals.

2006 Final Policy Statement at 18.

More recently, and after enactment of Section 1329, we emphasized similar public policy goals. We explained that Section 1329 reflects a determination by the General Assembly that fair market value acquisitions of municipal water and wastewater systems further the public interest. *See, generally, Implementation of Section 1329 of the Public Utility Code – Tentative Implementation Order*, Docket No. M-2016-2543193 (Order entered July 21, 2016) (*TIO*); and *Implementation of Section 1329 of the Public Utility Code – Tentative Supplemental Implementation Order*, Docket No. M-2016-2543193 (Order entered September 20, 2018) (*TSIO*). Specifically, we noted there are a number of water and wastewater systems owned by municipal corporations or authorities throughout the Commonwealth where sale to an investor-owned public utility can facilitate necessary infrastructure improvements and ensure the continued provision of safe, reliable service to customers at reasonable rates. *TIO* at 2. Additionally, we explained that:

[t]he development of water and wastewater service throughout the Commonwealth over the years has led to the creation of large numbers of geographically dispersed water and wastewater systems owned by municipal corporations or authorities. For these systems, sale to a larger, well-capitalized and well-run regulated public utility or entity can be prudent because it can facilitate necessary infrastructure improvements and access to capital markets, and, ultimately, it can ensure the long-term provision of safe reliable service to customers at reasonable rates.

TSIO at 4.

Aqua argued that the proposed transaction with EWT is no exception to these principles and that the analysis in *McCloskey* is equally applicable in this proceeding and constitutes substantial evidence sufficient to support the public benefit of the transaction. Aqua St. 1 at 15. We agree. However, we shall further evaluate whether Aqua has established whether there are additional affirmative benefits to support the acquisition. Our evaluation will consider whether Aqua has satisfied the preponderance of the evidence standard with the understanding that it is not required to secure legally binding commitments nor quantify benefits if impracticable, burdensome, or impossible. *Popowsky*, 937 A.2d at 1057.

In addition to the public interest benefits recognized in *McCloskey*, Aqua provided testimony pertaining to the following: benefits to existing Aqua customers; benefits to EWT customers; enhanced customer service for EWT customers; enhanced customer billing and payment protections; no adverse effect to the transaction; and EWT's desire to sell its System.

Regarding benefits to existing Aqua customers, we recognize that the transaction would result in an approximate nine percent increase in the Company's customer base. We agree with Aqua's testimony that, as a result of the Company's larger

customer base, future infrastructure investments across the Commonwealth will be shared at a lower incremental cost per customer for all of Aqua's customers. *See* Aqua St. 1 at 17. In support, Aqua cites to a Commonwealth Court decision recognizing the many benefits of single tariff pricing as follows:

- (1) A larger rate and revenue base ameliorates the impact of major capital additions needed from time to time in every service area;
- (2) A larger revenue base promotes flexibility in timing and financing major capital additions;
- (3) The impact of instability resulting from changes in sales volumes is mitigated when the effect of such volumetric factors is spread over a larger economic base; and
- (4) The reduction of the number of accounting units and the number of individual rate filings results in administrative efficiency with a potential to reduce costs to ratepayers.

Aqua Exc. at 14 (citing *Pittsburgh v. Pa. PUC*, 560 A.2d 889, 893 (Pa. Cmwlth. 1989)). We agree that through single tariff pricing EWT and all of Aqua's water and wastewater customers will benefit from the sharing of financial and infrastructure risks over time. As discussed below, EWT will likely need future infrastructure improvements and through the proposed transaction will be able to share financial and infrastructure risks with other customers within a larger customer base. *See* Aqua St. 2 at 10-11; Aqua St. 2-R at 2-3.

Additionally, the Township's 7,658 customer connections equate to a \$7,200 purchase price per connection which is approximately equal to Aqua's existing base rate per EDU projected at \$7,000. These similarities combined with Aqua's lower operating cost demonstrate that economies of scale can be achieved through the proposed

acquisition. *Id.* Moreover, the ability to share costs among a large customer base is a recognized benefit and a basic tenet of ratemaking. *See* Aqua St. 1 at 17.

As to the benefits for the Township's customers, we note that the Company is already the owner and operator of the EWT water system and has key operations in nearby service areas. This proximity will facilitate the assumption of the operation and incorporation of EWT's System within Aqua's system which will likely result in further long-term operating efficiencies. For example, operational overlap between water and wastewater utility operations provides opportunities for coordinating capital activities involving road openings and restorations thereby minimizing disturbances within the Township. Aqua St. 1 at 16.

Significantly, EWT customers will also benefit from an approximate 29% reduction in operating expenses under Aqua's ownership when comparing the Township's 2020 budget expenses of approximately \$2.8 million with Aqua's expense projection of \$2 million. Aqua St. 1 at 16. This comparison indicates a tangible, quantifiable savings as a result of the acquisition.

Further, Aqua will invest approximately \$16.92 million in the acquired System over ten years which will include upgrades to pump stations, force mains and gravity collection systems due to observed conditions, facility ages, and safety. Aqua St. 2 at 10-11. The planned capital improvements include safety related electrical Arc-Flash studies for protection of operations personnel. Aqua's witness Mark J. Bubel, Sr., testified that during Aqua's due diligence visit to the pump station locations, there was no obvious indication that Arc-Flash study work was conducted due to the absence of appropriate Arc-Flash safety alert stickers on electrical control panels. The Company asserted that its Arc-Flash safety study work will result in a significant public benefit of Aqua ownership. Aqua St. 2-R at 2.

Aqua also testified that its capital improvement projection includes funds to address Inflow and Infiltration (I&I).¹³ In addition to impacting the Township's allocation for treatment within the VFSA wastewater treatment plant, I&I impacts Township treatment costs and the VFSA plant itself in terms of the plant's available hydraulic capacity for the Township and member municipalities. Further, Aqua asserted that I&I impacts conveyance capacity and cost within the Valley Creek Trunk Sewer system for EWT and member municipalities. Aqua submitted that the targeting of capital to investigate I&I and undertake remediation as appropriate is a significant benefit of the Company's ownership.¹⁴ The Company also emphasized that reductions in I&I can reduce conveyance and treatment costs. Aqua St. 2-R at 3.

¹³ The Environmental Protection Agency defines I&I as follows:

(20) Infiltration. Water other than wastewater that enters a sewer system (including sewer service connections and foundation drains) from the ground through such means as defective pipes, pipe joints, connections, or manholes. Infiltration does not include, and is distinguished from, inflow.

(21) Inflow. Water other than wastewater that enters a sewer system (including sewer service connections) from sources such as, but not limited to, roof leaders, cellar drains, yard drains, area drains, drains from springs and swampy areas, manhole covers, cross connections between storm sewers and sanitary sewers, catch basins, cooling towers, storm waters, surface runoff, street wash waters, or drainage. Inflow does not include, and is distinguished from, infiltration.

40 C.F.R. § 35.2005(b)(20) and (21).

¹⁴ In his testimony, Aqua witness Mr. Bubel cited to the DEP 2019 Chapter 94 Report (2019 DEP Report) to support his belief that there is I&I within the EWT System. Aqua St. 2-R at 2-3; MJB 2-R Exh. 1.

Aqua also proffered that the EWT System has experienced Sanitary Sewer Overflows (SSOs).¹⁵ Aqua witness Mr. Bubel testified that the 2019 DEP Report indicated that the System experienced capacity related by-passing, SSOs or surcharging during the 2019 DEP Report year. The Company submitted that certain system improvements that are targeted within Aqua’s ten-year capital estimate would mitigate the SSOs and is indicative of a further significant benefit of Aqua ownership. Aqua St. 2 at 3.

In the Recommended Decision, the ALJ stated that the Township could make necessary improvements and upgrades to the System equal to what Aqua has proposed without imposing an unreasonable financial burden on the Township. Although it may be possible for EWT to borrow funds or use cash on hand to make capital improvements similar to the capital expenditures outlined by Aqua, it is not certain from the record that the Township will in fact do so within the short term or long term given the multitude of other services the Township must allocate to address the needs of their citizens. Here, EWT has determined that it is in the best interest of its constituents to stop providing wastewater service. Further, we acknowledge that Aqua has a history of infrastructure improvements and is committed to investing in the capital improvements noted above, which represents a substantial benefit weighing in favor of the transaction. Aqua St. 1-R at 14.

In further support of the benefits to EWT’s customers, Aqua testified to its ability to deal with complex environmental regulations. Aqua explained that its facilities are operated by DEP licensed operators or are closely monitored by a designated operator under the direction of the licensed operator. Additionally, the Company’s operational

¹⁵ SSO is defined as: “[a]n intermittent overflow of wastewater, or other untreated discharge from a separate sanitary sewer system (which is not a combined sewer system), which results from a flow in excess of the carrying capacity of the system or from some other cause prior to reaching the headworks of the plant.” 25 Pa. Code § 94.1.

staff is supported by in-house engineers who assist with capital planning to improve system efficiencies and are immediately available for system troubleshooting and to ensure with environmental regulations. Aqua St. 2-R at 4.

In addition, the Company asserted that it has a staff of in-house environmental compliance experts who monitor changing regulatory requirements and work closely with engineering and operational staff to implement changes to system processes. Aqua also has an in-house laboratory that can process samples obtained from the Township System to assist in quickly identifying potential substances that degrade the treatment process at the VFSA plant. Further, the Company highlighted its formal emergency preparedness plans for its systems and a business continuity plan if a significant emergency were to occur. *Id.*

EWT's customers will also benefit from a variety of customer service and customer billing and payment protection enhancements. These include Aqua's:

- Toll-free customer service number for regular business hours and a 24/7/365 emergency response line to address wastewater emergencies and to direct emergency calls to field service personnel;¹⁶
- Online bill payment options including a pay-by-text feature and email and phone notifications for service impact events;
- Compliance with Chapter 14 of the Code with the added oversight of the billing process;
- Access to customer assistance low-income programs.

See Aqua St. 1 at 17-18 and Aqua St. 1-R at 19.

¹⁶ At present, after hours emergency calls must be directed through the Township's police department. OCA St. 2 at 10.

Regarding customer billing and payment protections, Aqua has procedures and processes in place to comply with the Chapter 14 provisions for billing, payment, collection, termination and reconnection of services, payment arrangements, medical certifications, and informal and formal complaint procedures. The Company also has customer care teams available to help resolve such service and billing issues. Aqua St. 1 at 18.¹⁷

Aqua submits that the transaction will have no adverse effect on its customers and contends that there will be no immediate impact on the rates of either the Company's customers or existing customers of EWT. The Company asserts that, consistent with Section 1329(d)(1)(v) of the Code, Aqua will implement the existing Township base rates upon closing. However, existing miscellaneous fees and charges in the Company's tariff will be applied. Aqua Exh. 1, Application at ¶ 52.g, and Aqua St. 1 at 11-12.

As a final area of public benefit, Aqua emphasizes that the Township wants to sell its System. According to the Company, the public interest will be served by allowing Aqua to provide wastewater service in the requested territory and to address the issues of regulatory requirements and capital expenditures. Aqua submits that the Township will benefit from the support of wastewater professionals throughout the Company's organization. Aqua Exh. 1, Application at ¶ 52.b.

¹⁷ The Commission recently acknowledged in another Section 1329 proceeding, the public benefits of the Commission's comprehensive regulatory oversight of rates and quality of service for newly-acquired customers and their access to the Commission's complaint procedures. *See Application of Pennsylvania-American Water Company – York City Sewer Authority*, Docket No. A-2021-3024681 (Recommended Decision issued February 28, 2022; Final Order entered April 14, 2022).

The Township also credits the following affirmative benefits of the transaction for its customers and residents generally:

- (1) the Township can exit the sanitary sewer business and instead focus its resources on other core government functions while ensuring safe, reliable service at affordable rates for its residents;
- (2) the Township's customers will benefit from the expertise and experience of a regulated public utility like Aqua; and
- (3) the up-front proceeds from the Proposed Transaction will allow for various redevelopment opportunities in EWT.

EWT Exc. at 4 (citing Aqua St. 3 at 8).

When weighing all the factors, including the impact on rates, the ALJ focused on the harms resulting if Aqua were to apply 100% of the revenue deficiency of \$5.011 million associated with the proposed rate base addition to the existing Township rates. Under that scenario, the average Township customer bill would increase to an additional \$77.64 per month or 132.93% above the current rate of \$33 per month. The ALJ also noted that even if EWT customers were to bear 50% of the revenue requirement related to Aqua's proposed rate base, Township customers would experience a 66.47% rate increase. R.D. at 54-55.

However, the rate deficiency emphasized by the ALJ is only a preliminary analysis of the potential rate impact on the Township's customers. This figure is a non-binding estimate of the incremental rate effect of the proposed rate base increase and is used as part of the notice procedure to customers in Section 1329 proceedings. *See FSIO, supra*. As we previously explained "the Section 1329 valuation could have a highly unlikely rate effect of \$0. Equally unlikely is the full allocation of all costs – acquisition

and perhaps others – to a rate division consisting of only the customers of the acquired municipal system. The more likely *outcome* is indeterminate; it will be found somewhere between possible extremes.” *FSIO* at 32 (emphasis in original).

All of the Parties acknowledge that some level of a rate increase is expected as a result of the transaction. Indeed, there is a reasonable expectation that rates for the Township’s customers will increase even if the Commission were to reject the Application given the level of capital expenditures considered to be necessary over the next ten years. However, we agree with Aqua and the Township that, if the transaction is approved, there will be more flexibility to address rate impact and to allocate costs over a much larger customer base. *See, e.g.*, Aqua St. 1-R at 15-16 (examining five years of capital investments on the Company’s acquired wastewater systems).

When considering all the factors, including the impact on rates, we find that the benefits of Aqua’s ownership outweigh the purported harms outlined by the OCA. Aqua’s expertise and ability to raise and deploy capital and to spread costs over a larger customer base, the Township’s decision to exit the wastewater business, and the transaction’s furtherance of the policy objectives of the General Assembly in enacting Section 1329, as well as the additional factors discussed above, are all substantial affirmative benefits weighing in favor of granting the Application. Accordingly, we shall grant Aqua Exception Nos. 1 and 2 and EWT Exception No. 1.¹⁸

¹⁸ In EWT Exception No. 2, the Township argues that the Recommended Decision creates a precedent that a municipality cannot sell its assets under the Code unless or until dire circumstances warrant the sale. EWT Exc. at 6. Because we are granting Aqua Exception Nos. 1 and 2 and EWT Exception No. 1, the arguments in EWT Exception No. 2 are deemed moot and we shall decline to address them.

B. Ratemaking Rate Base

Finding that Aqua's proposal to acquire the EWT System should not be approved pursuant to Section 1102 of the Code, as discussed *supra*, the ALJ presumably did not find it necessary to address the FMV of the Township's System in her Recommended Decision, nor provide conditional recommendations on this issue or the other remaining issues in this proceeding should the Commission not agree with her primary recommendation.

Thus, regarding the issue of the appropriate ratemaking rate base under the instant Section 1329 transaction, Aqua raises a single, but broad exception. Specifically, in its Exception No. 3, "Aqua excepts to the failure of the Recommended Decision to address the fair market value of the System and submits that, pursuant to Section 1329(c)(2), the fair market value ratemaking rate base is \$54,930,000." Aqua Exc. at 23. In reply, the OCA maintains that the ALJ properly determined that the proposed transaction would not provide affirmative public benefits; nonetheless, the OCA continues by providing reiterated arguments from its testimonies and briefs that the recommended ratemaking rate base of \$46.5 million, in lieu of the Company's proposed FMV ratemaking rate base amount of \$54.93 million, properly reflects reasonable adjustments to the UVE appraisals under Section 1329 of the Code. OCA R. Exc. at 15-25.

Having granted Aqua's Exception No. 1, finding that the instant Section 1329 transaction meets the statutory requirement to provide, substantial, affirmative public benefits, we, accordingly, shall grant, in part, Aqua's Exception No. 3 to the extent that the Parties' arguments pertaining to each of the OCA proposed adjustments to the UVE appraisals will be addressed within the context of those issue below.

Additionally, for future Section 1329 proceedings, we encourage the Office of Administrative Law Judge to issue a Recommended Decision, as contemplated by our Regulations and Section 334(a) of the Code, 66 Pa. C.S. § 334(a), providing conditional recommendations on all pending issues, even if the presiding officer recommends denial of an application on the basis that the proposed transaction lacks the existence of substantial affirmative benefits. In order for the Commission to prepare a comprehensive disposition, it would be beneficial for the presiding officer, who is present for the reception of evidence, to prepare a full recommendation on all pending issues including the appropriate FMV of the wastewater system being acquired.

Furthermore, as the Commission has previously made the determination in other Aqua Section 1329 acquisitions, such as *New Garden*,¹⁹ *Limerick*,²⁰ *Cheltenham*, and *Lower Makefield*, that challenges to UVE appraisals are permissible, we continue with our discussion and consideration of the Parties' positions regarding the OCA's proposed adjustments to several of the UVE appraisal approaches.

1. Aqua's Application

As previously indicated, UVEs, Gannett Fleming and AUS, found appraised values of approximately \$55.668 million and \$57.781 million, respectively, for an average appraised value of approximately \$56.725 million. The purchase price of \$54.93 million is below the average appraised value; consequently, Aqua proposed the

¹⁹ *Application of Aqua Pennsylvania Wastewater, Inc. Pursuant to Sections 1102 and 1329 of the Public Utility Code for Approval of its Acquisition of the Wastewater System Assets of New Garden Township and the New Garden Township Sewer Authority*, Docket No. A-2016-2580061 (Order entered June 29, 2017) (*New Garden*).

²⁰ *Application of Aqua Pennsylvania Wastewater, Inc. Pursuant to Sections 1102 and 1329 of the Public Utility Code for Approval of its Acquisition of the Wastewater System Assets of Limerick Township*, Docket No. A-2017-2605434 (Order entered November 29, 2017) (*Limerick*).

\$54.93 million purchase price amount be included in rate base, if the transaction is approved. Application at ¶ 56; 66 Pa. C.S. § 1329(c)(2).

The two appraisals provided by Gannett Fleming and AUS were prepared in accordance with the USPAP, employing the Cost, Income, and Market Approaches to arrive at the FMV of the System. Both firms were pre-certified as authorized UVEs. Aqua M.B. at 6. In arriving at its estimate, Gannett Fleming considered all three approaches, assigning an equal weight to the result of each approach. AUS primarily relied on the Cost Approach, with the Income and Market Approaches being utilized to confirm the overall value of the System’s operation.²¹ The results of each are summarized as follows:

Summary of Results Prepared by Gannett Fleming			
	<u>Indicated Value</u>	<u>Weight</u>	<u>Weighted Value</u>
Cost Approach	\$59,118,924	33.33%	\$19,704,337
Income Approach	\$61,147,544	33.33%	\$20,380,476
Market Approach	\$46,741,589	33.34%	\$15,583,646
Total		100%	\$55,668,459
Conclusion	→		\$55,668,000

See Aqua St. 4 at 13. In summary, the results from the original cost method form the basis for Gannett Fleming’s replacement cost method, and both methods form the basis for its Cost Approach. Its Income Approach utilized the capitalization of earnings (cash flow) method and considers the results of two types of discounted cash flow (DCF)

²¹ In preparation of their FMV estimates, specifically in the Cost Approach, Gannett Fleming and AUS utilized the Engineering Assessment provided by Pennoni. Aqua St. 4 at 16; Application Exh. R, Narrative Report at 2.

analyses, the EBIT and EBITDA terminal value model (Market Multiple DCF) and the capitalization of terminal value model (Capitalization DCF) (collectively referred to as the DCF methods).²² Gannett Fleming’s Market Approach is supported by the market multiples method and selected transaction method. Aqua St. 4 at 14-15.

Summary of Results Prepared by AUS			
	<u>Indicated Value</u>	<u>Weight</u>	<u>Weighted Value</u>
Cost Approach	\$59,847,171	50%	\$29,923,586
Income Approach	\$55,600,045	40%	\$22,240,018
Market Approach	\$56,178,539	10%	\$5,617,854
Total		100%	\$57,781,458
Conclusion	→		\$57,781,458

See Aqua St. 5 at 3. In summary, AUS’ Cost Approach is supported by the results from the replacement cost method less accrued depreciation. The results from the DCF method formed the basis for AUS’ Income Approach. AUS’ Market Approach is supported by the comparable sales method. Aqua St. 5 at 6, 14, 19.

As can be seen by the results of each consultant’s analyses, as summarized above, it is clear that judgment is involved in the inputs used, the weighting given to each approach, and the FMV determinations. That is why two UVEs have reached different FMV results for the Township’s System. As discussed below, OCA witness David J.

²² EBIT is earnings before interest and taxes and EBITDA is earnings before interest, tax, depreciation, and amortization.

Garrett proposed adjustments under all three valuation approaches in this proceeding.²³ The tables below outline the OCA's adjustments to Gannett Fleming's and AUS' appraisals under all three approaches:

Summary of OCA Adjustments to Gannett Fleming's Appraisal					
Approach	Gannett Fleming Indicated Value	OCA Adjustment	OCA Adjusted Value	OCA Weight	OCA Weighted Value
Cost	\$59,118,924	(\$2,780,373)	\$56,338,551	33.3%	\$18,779,517
Income	\$61,147,544	(\$19,790,289)	\$41,357,255	33.3%	\$13,785,752
Market	\$46,741,589	(\$7,192,756)	\$39,548,833	33.3%	\$13,182,944
Total				100%	\$45,748,213

Summary of OCA Adjustments to AUS' Appraisal					
Approach	AUS Indicated Value	OCA Adjustment	OCA Adjusted Value	OCA Weight	OCA Weighted Value
Cost	\$59,847,171	(\$6,722,100)	\$53,125,071	50%	\$26,562,536
Income	\$55,600,045	(\$14,242,790)	\$41,357,255	40%	\$16,542,902
Market	\$56,178,539	(\$15,232,008)	\$40,946,531	10%	\$4,094,653
Total				100%	\$47,200,091

See OCA Exh. DJG-2.

²³ I&E has not challenged the UVE's appraisals in this proceeding; however, as explained below in the Recommended Conditions section of this Opinion and Order, I&E contended that the UVE's reliance on the fact that all easements and real property rights will be transferred to Aqua by EWT prior to closing may invalidate the accuracy of their appraisals. I&E M.B. at 9. The OSBA did not assert specific challenges to the UVE appraisals.

In summary, the culmination of the OCA’s proposed adjustments results in a \$8.43 million reduction to Aqua’s requested rate base of \$54.93 million, as illustrated below.²⁴

Summary of OCA's Recommended Rate Base		
	UVE Results	OCA Adjusted
Gannett Fleming	\$55,668,460	\$45,748,213
AUS	\$57,781,458	\$47,200,091
Average	\$56,724,958	\$46,500,000
Purchase Price	\$54,930,000	\$54,930,000
Proposed Rate Base	\$54,930,000	\$46,500,000

See OCA Exh. DJG-2.

2. Cost Approach – Service Lives

a. Positions of the Parties

Aqua provided that the estimation of service lives is an important part of the valuation of depreciable plant assets under the Cost Approach. Aqua explained that shorter service lives, as recommended by the OCA witness Mr. Garrett, result in lower

²⁴ The OCA calculated that the adjusted Gannett Fleming appraisal result would be \$45,748,213, and the adjusted AUS appraisal result would be \$47,200,091, in order to properly reflect financial and ratemaking principles. OCA Exh. DJG-2. The recalculated average of the two appraisal results is approximately \$46,500,000, which is the amount the OCA recommended be used by the Commission for establishing ratemaking rate base under Section 1329 because this amount is less than the \$54,930,000 purchase price. OCA M.B at 44.

values under the Cost Approach. Aqua explained further that Mr. Garrett recommended shorter service lives for five plant accounts in the Gannett Fleming Cost Approach. Aqua argued that Mr. Garrett's recommendations are not supported by statistical analysis and should not be adopted. Aqua M.B. at 28 (citing Aqua St. 4-R at 4).

Gannett Fleming explained the general concept of service lives and the use of Iowa curves as follows:

Depreciation represents the loss in property value from: physical deterioration; functional obsolescence; and external obsolescence. The accrued depreciation represents the sum of the annual depreciation amounts that would have been charged for depreciation at a point in time. Accrued depreciation is a calculated amount that would be in the book reserve account at a point in time using the current depreciation parameters (i.e., average service life).

The average service lives of depreciable assets are based on the materials used for construction and how long the depreciable assets are likely to meet service demands. The range of survivor characteristics usually experienced by utility and industrial properties is encompassed by a system of generalized "survivor curves" known as the Iowa type curves.

The accrued depreciation ratio from a survivor curve is a concept that is used to estimate the consumed service capacity of plant at a point in time. The survivor curve is used to find the applicable accrued depreciation factors of the assets to result in the total accumulated depreciation.

Application Exh. Q at 23.

The OCA argued that the Township did not have asset placement and retirement records by vintage year for the UVEs to use to select Iowa curves to calculate the average remaining life and estimate depreciation. OCA M.B. at 26 (citing OCA St. 1 at 15). The OCA averred that without the asset placement and retirement records, the

OCA’s proposed adjustments to service lives are more conservative and more reasonable. OCA M.B. at 27.

(1) Gannett Fleming

The OCA made the following adjustments to Gannett Fleming’s Iowa curve calculations:

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 M.B. at 29 (citing OCA St. 1 at 20).

The OCA provided that it used the same values to adjust the Gannett Fleming Cost Approach as those proposed by Mr. Jerome C. Weinert of AUS for Account No. 354.30 (Structures and Improvements – Pumping) and Account No. 354.40 (Structures and Improvements – Treatment). For Accounts 360.10 (Collection Sewers – Force Mains) and Account No. 361.10 (Collection Sewers – Gravity Mains), the OCA proposed a 60-year average life, arguing that Gannett Fleming used the 60-year life for these accounts in a wastewater case in front of the Indiana Utility Commission.²⁵ The

²⁵ 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>. OCA M.B. at 31, n. 13.

OCA recommended a 45-year life for the Services to Customers Account to estimate a reasonable range for that account. OCA M.B. at 29 (citing OCA St. 1 at 20).

(2) AUS

Aqua provided that in the AUS appraisal, the Cost Approach is based on Cost of Replacement New less Depreciation (CORLD). Aqua noted that Mr. Garrett accepted the AUS Cost of Replacement but adjusted depreciation by reducing the estimated service lives for several plant categories. The impact of Mr. Garrett's adjustments reduced the AUS Cost Approach result from \$59.8 to \$53.1 million. Aqua M.B. at 31 (citing Aqua St. 5-R at 8; OCA St. 1 at 23-24; Aqua St. 5-R at 18-19). Aqua submitted that Mr. Garrett provided no apparent basis for his recommended service lives for the AUS Appraisal. According to Aqua, Mr. Garrett simply stated that he made the AUS service lives the same as those he used for Gannett Fleming's Cost Approach. Aqua noted that Mr. Garrett maintained that AUS did not provide support for the service lives it selected. Aqua M.B. at 32 (citing Aqua St. 5-R at 10-11, referencing pages 15-16 of Mr. Garrett's direct testimony).

Aqua disagreed with Mr. Garrett's assertion that AUS did not provide support for its service lives determinations. According to Aqua, Mr. Weinert detailed how AUS determined service lives and depreciation with specific reference to depreciation studies presented by Pennsylvania-American Water Company (PAWC) and Aqua in general rate proceedings.²⁶ Aqua averred that the PAWC and Aqua depreciation studies show a service life in a range of 75-80 years for Gravity Collection Mains demonstrating that the 80-year service life used in the AUS appraisal is reasonable. Mr. Garrett's 60-year service life is not reasonable, as Aqua argued, as it clearly understates the actual service life for gravity mains constructed and serving Pennsylvania

²⁶ PAWC and Aqua General Rate Cases can be found at Docket Nos. R-2017-2595853, R-2020-3019371, and R-2018-3003561.

customers and it should not be adopted. Aqua M.B. at 32-33 (citing Aqua St. 5-R at 12-13).

The OCA recommended adjustments to the AUS Cost Approach using the same average service lives that it recommended in its adjustments to the Gannett Fleming Cost Approach. OCA M.B. at 30.

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

OCA St. 1 at 23.

The OCA noted that Mr. Weinert disagreed with the OCA’s proposed service lives. While Mr. Weinert relied on the Gannett Fleming depreciation studies, the OCA offered that these studies were not conducted on the assets at issue in this proceeding. Although Mr. Weinert noted that his service life proposals in this case are similar to those proposed by Gannett Fleming in other cases, according to the OCA, he does not explain the differences between his and Gannett Fleming’s proposed service lives here. OCA M.B. at 31 (citing OCA St. 1SR at 10).

The OCA claimed that 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 that is what both Mr. Garrett and Mr. Weinert did. *Id.* While Mr. Weinert claimed that his comparative analysis is more credible than Mr. Garrett’s because it relied on the most recent depreciation studies conducted by Aqua

and PAWC, the OCA averred that this argument only highlights that similar data was not available about the Township's assets in this case. OCA M.B. at 31 (citing Aqua St. 5-R at 12; OCA St. 1SR at 10-11). The OCA reasoned that both Mr. Weinert and Mr. Garrett used their own judgment to evaluate the appropriate service lives for various accounts of the Township. OCA M.B. at 31-32 (citing OCA St. 1SR at 10-11).

The Township endorsed, adopted, and incorporated by reference the section of Aqua's Main Brief relating to the challenges to UVE appraisals. EWT M.B. at 14.

I&E did not challenge the UVEs appraisals with the exception of the issue regarding easements and real property rights as discussed *infra* in Section V.D. Recommended Conditions. I&E M.B. at 9.

The OSBA took no position on this issue. OSBA M.B. at 15.

b. Recommended Decision

The ALJ did not address the issue of service lives for the Township System assets.

c. Aqua Exception No. 3 and Replies

In its Exception No. 3, Aqua excepts to the failure of the Recommended Decision to address FMV and ratemaking rate base which includes the service lives issue. Aqua Exc. at 23.

(1) Gannett Fleming Cost Approach – Service Lives

Aqua provides that the OCA witness Mr. Garrett recommended shorter service lives for five plant accounts in the Gannett Fleming Cost Approach. Aqua notes that the Commission has not accepted Mr. Garrett’s proposed service lives in prior Section 1329 proceedings. According to Aqua, it is the Gannett Fleming service lives that are consistent with the service lives approved by the Commission in prior fully litigated 1329 proceedings, such as *Limerick*, *Cheltenham*, and *Lower Makefield*. Aqua avers that Mr. Garrett’s shorter service lives are not reasonable and not suitable for the EWT System assets. Aqua Exc. at 25-26 (citing Aqua St. 4-R at 6-7).

Aqua provides that Mr. Garrett’s recommended service lives for Account No. 354.30 (Structures and Improvements – Pumping) and Account No. 354.40 (Structures and Improvements – Treatment) are based on the AUS appraisal. Aqua submits that Mr. Garrett also claimed that his service lives for these two accounts are consistent with his “proposed Iowa curves for these accounts in prior Section 1329 proceedings.” Aqua Exc. at 26 (citing Aqua St. 4-R at 4).

Aqua notes that Mr. Garrett’s recommended service lives for Account No. 360.10 (Force Mains) and Account No. 361.10 (Gravity Mains) are based on a 2016 depreciation study in the state of Indiana (*Indiana Study*). Aqua also notes that Mr. Garrett claimed that his recommended service life for Account No. 363.20 (Services to Customers) is consistent with his proposal for this account in prior 1329 proceedings. *Id.*

Aqua contends that the *Indiana Study* included information for Citizens Energy Group - Citizens Wastewater (CWW) and Citizens Energy Group – Westfield Wastewater (WWW) which is not statistically significant. *Id.* Aqua explains that the data for CWW’s Force Mains account included only seven years of accounting data, with

no retirements and the data for WWW's Force Mains account included only three years of accounting data, with a total of \$15,000 of retirements. Similarly, Aqua submits that the Gravity Mains data for CWW and WWW were also limited. Aqua Exc. at 26, n. 61 (citing Aqua St. 4-R at 4-5; Cause No. 45039 before the Indiana Utility Regulation Commission). According to Aqua, along with the lack of statistical significance, Mr. Garrett provided no evidence that the assets of CWW and WWW are comparable to the Township assets. Aqua notes that the CWW system is a combined sewer system, while the Township is not. Aqua Exc. at 26 (citing Aqua St. 4-R at 5; Aqua M.B. at 29-30).

Aqua notes that Mr. Garrett recommended service lives that are between 18% and 22% shorter for Accounts 354.30, 354.40 and 363.20 than those he recommended in the *Indiana Study*. Aqua Exc. at 27 (citing Aqua St. 4-R at 7; Aqua M.B. at 30).

Aqua claims that Mr. Garrett chose the shortest service life available – whether based on the *Indiana Study*, the AUS appraisal or the Gannett Fleming appraisal for each of his adjusted five accounts. Aqua argues that the use of shorter service lives reduces the appraised value under the Cost Approach. Aqua Exc. at 27 (citing Aqua St. 4-R at 9).

(2) AUS Cost Approach – Service Lives

Aqua contends that Mr. Garrett provided no apparent basis for his recommended service lives for the AUS Appraisal other than that he made the AUS lives the same as those he used for Gannett Fleming. Aqua claims that Mr. Garrett argued that AUS lacked support for the service lives it selected. Aqua Exc. at 27-28 (citing Aqua St. 5-R at 11; Aqua M.B. at 27).

Aqua avers that Mr. Weinert used depreciation studies in PAWC and Aqua general rate cases which were the result of analysis of the companies' historical survival and retirement experience over a wide span of years, representing actual service life experience of wastewater plant. Aqua Exc. at 28 (citing Aqua St. 5-R at 11; Aqua M.B. at 27).

In its Reply to Aqua Exception No. 3, the OCA first responds to the Aqua Exception regarding the Gannett Fleming Cost Approach. The OCA argues that Mr. Garrett's use of the *Indiana Study* to inform his service life recommendations in the present case was reasonable. The OCA notes that as discussed in its Main Brief and in testimony, the Township did not maintain the requisite records about asset placements and retirements, so the UVEs used their subjective judgment to calculate service lives. OCA Exc. at 16 (citing OCA M.B. at 29-20; OCA St. 1SR at 10-11). The OCA avers that like Mr. Garrett, both UVEs support their subjectively selected service lives by comparing them to other utilities. Aqua Exc. at 16 (citing Aqua St. 4 at 8; Aqua St. 5 at 9).

The OCA notes that Aqua criticizes Mr. Garrett for proposing service lives in this case that differ from those he proposed in other cases where he addressed service lives for grouped depreciable assets. OCA Exc. at 16 (citing Aqua Exc. at 26-27). The OCA explains that Mr. Garrett recognized that in those cases the utilities produced significant historical retirement data to support their proposed service lives that was not available for EWT. OCA Exc. at 16 (citing OCA St. 1SR at 9). The OCA explains further that for the Gannett Fleming pumping account and treatment account, Mr. Garrett accepted the Iowa curves that Mr. Weinert used in this case and prior Section 1329 proceedings. OCA Exc. at 16-17 (citing OCA St. 1 at 20). The OCA notes that Mr. Garrett's proposed service lives for the force and gravity mains accounts are the same as what Gannett Fleming proposed for a wastewater utility in Indiana. Additionally, the OCA notes that Mr. Garrett's proposed service life for the services

account is consistent with his proposal for this account in prior Section 1329 proceedings (which were settled) and it is with a reasonable range for this account. *Id.*

The OCA argues that Mr. Garrett’s service life recommendations are appropriately conservative, given the need to rely on comparative analyses in lieu of utility-specific data. The OCA reasons that Aqua has failed to justify using longer proposed service lives in this proceeding, which would only serve to increase the values under the cost approach. OCA Exc. at 17 (citing OCA St. 1 at 20, 22; OCA M.B. at 28-30).

Regarding the AUS Cost Approach adjustments, the OCA avers that both Mr. Garrett and Mr. Weinert from AUS selected their service lives based on data from other cases. OCA Exc. at 17 (citing OCA M.B. at 31-32; OCA St. 1SR at 10-11). The OCA argues that there is no utility-specific actuarial data available for the Township System assets, so it is more reasonable to be conservative when calculating the appropriate service lives for various accounts. *Id.*

d. Disposition

(1) Gannett Fleming Cost Approach – Service Lives

Mr. Walker provided that he viewed or observed the Township’s facilities on June 15, 2021. He stated that he also relied on the Engineering Assessment prepared by Pennoni, the System’s Chapter 94 reports, the System’s 537 Plan, the System’s Municipal Wasteload Management Program Reduction Plan, and the APA, to confirm the condition of the System’s property and equipment. Aqua St. 4-R at 3. Mr. Garrett did not observe the Township’s assets and has not valued a utilities property. Aqua St. 4-R at 2-3, Aqua Exh. HW-1 at 1-2. We find that Mr. Walker has relied on more information

than Mr. Garrett in developing the service lives used in the Gannett Fleming Cost Approach.

Mr. Garrett proposed the use of shorter service lives for five separate accounts. We note that Mr. Garrett chose the shortest service lives available – whether based on the *Indiana Study*, the AUS appraisal or the Gannett Fleming appraisal for each of his five recommended adjustments to the Gannett Fleming Cost Approach. Mr. Garrett selected the *Indiana Study* values for Accounts 360.10 and 361.10 but for the other accounts he chose whatever value was lowest. Mr. Garrett recommended using longer service lives for Account No. 354.30 and Account No. 354.40 in the *Indiana Study* than the values he recommended here for the Township system assets. Instead, he used values from the AUS appraisal for these two accounts. Aqua St. 4-R at 8-9. We must agree with Aqua that Mr. Garrett’s approach is unreasonable here. If Mr. Garrett believed the *Indiana Study* results to be appropriate for use for EWT’s assets, it would be more reasonable to expect him to use the values from the study for all five accounts in question. Accordingly, we are not persuaded to accept the OCA’s recommendations to adjust (downward) the service lives in the Gannett Fleming Cost Approach.

(2) AUS Cost Approach – Service Lives

AUS recommends a 75-year service life for Account No. 360.21 (Collection Sewers - Force Mains) and an 80-year service life for Account No. 361.21 (Collection Sewers - Gravity Mains). The 80-year service life for gravity sewer mains was found excessive for the sewer gravity mains in *Lower Makefield*. In that case, a longer 80-year service life as recommended for lined vitreous concrete pipe (VCP) was not appropriate as the system was mostly unlined VCP and only a small portion of the system was lined. In *Lower Makefield* a value of 65-years was recommended. *Lower Makefield* at 44-45. While AUS avers that the gravity mains in the Township are mostly plastic with an expected service life of 80 years, the Engineering Assessment indicates

that only approximately 50% of the gravity mains are plastic. Similarly, approximately 50% of the force mains in the Township are also plastic. *See* Application Exh. D.

Mr. Weinert testified that he determined the service lives for the Township assets using depreciation studies filed by PAWC and Aqua Pennsylvania Wastewater, Inc. in their General Rate Cases (R-2017-2595853, R-2020-3019371, and R-2018-3003561) and AUS' experience in preparing depreciation studies and appraisal experience for the water and wastewater industries. Aqua St. 5 at 9. We note that an 80-year service life for Account No. 361.23 (Collection Sewers – Gravity Manholes) appears to be much greater than what was proposed for this account in the depreciation studies AUS relied on for Account No. 361.23. The depreciation studies used a 50-year service life for this account. Application Exh. R at 30. It is unclear as to why Mr. Weinert selected an 80-year service life for the Account No. 361.23 (Gravity Manholes) when the depreciation studies used a 50-year service life. AUS has not provided a justification for using a service life that is thirty years longer than what was proposed by the depreciation studies.

We find that the 80-year service lives proposed by AUS for Accounts 361.21 and 361.23 are not reasonable. We also find that the 75-year service life for Force Mains is too high here. While AUS maintains that both the force mains and gravity mains in the EWT System are plastic, which it contends justifies the 75-year service life, the mains are approximately 50% plastic. We note that Gannett Fleming used a 65-year life for gravity mains. Application Exh. Q, Exh. 7 at 3. We are persuaded that the OCA's recommended 60-year service life is reasonable for these three accounts. The OCA's adjustments led to a Cost Approach valuation of \$53.1 million for the EWT System, which is approximately \$6.7 million less than the AUS proposed Cost Approach valuation of \$59.8 million. OCA M.B. at 32 (citing OCA St. 1 at 21; OCA Exhs. DJG-12, DJG-13).

3. Income Approach

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 over time. OCA M.B. at 39 (citing *ASA Business Valuation Standards* at 10-11. American Society of Appraisers accessed March 25, 2022, https://www.appraisers.org/docs/default-source/5---standards/bv-standards-feb-2022.pdf?sfvrsn=5c9e5ac0_3).

Gannett Fleming's DCF methods use two different assumptions for EWT system operations over the next twenty years: (1) a municipal-owned (MUNI) scenario;²⁷ and (2) an investor-owned utility (IOU) scenario.²⁸

Under the MUNI ownership scenario, the results of the Capitalization DCF show a range of value for the Township's System of \$68.3 million to \$70.7 million, and the results of the Market Multiple DCF show a value of \$63.6 million. Application Exh. Q, Exh. 15 at 6.

Under the IOU scenario, results of the Capitalization DCF show a range of value for the Township's System of \$44.4 million to \$53.7 million, and the results of the Market Multiple DCF show a range of value of \$56.5 million to \$67.2 million. Application Exh. Q, Exh. 16 at 6.

As shown in the following table, the results of Gannett Fleming's DCF methods based on the MUNI ownership scenario indicated a value of approximately

²⁷ Application Exh. Q, Exh. 15.

²⁸ Application Exh. Q, Exh. 16.

\$67.1 million for the Township’s System. The results of its DCF methods based on the IOU scenario indicated a value of approximately \$55.1 million for the Township’s System. Collectively, Gannett Fleming’s DCF methods indicate a value of approximately \$61.1 million based on the Income Approach.

<u>MUNI Ownership Scenario</u>	
Ref.: Application Exh. Q, Exh. 15 at 6.	
DCF with Capitalization of Terminal Value Model @ 2.89%	\$70,673,661
DCF with EBIT & EBITDA Terminal Value Model	\$63,625,249
Median	<u>\$67,149,455</u>
<u>IOU Scenario</u>	
Ref: Application Exh. Q, Exh. 16 at 6.	
DCF with Capitalization of Terminal Value Model @ 6.37%	\$53,747,255
DCF with Capitalization of Terminal Value Model @ 7.59%	\$44,579,501
DCF with EBIT & EBITDA Terminal Value Model - Discount Rate of 6.57%	\$67,233,718
DCF with EBIT & EBITDA Terminal Value Model - Discount Rate of 7.79%	\$56,544,009
Median	<u>\$55,145,632</u>
<u>Conclusion</u>	
MUNI DCF	\$67,149,455
IOU DCF	<u>\$55,145,632</u>
Median	<u>\$61,147,544</u>

The Income Approach analysis presented by the Township’s witness, Mr. Weinert from AUS, also utilized the DCF technique, indicating a value of approximately \$55.6 million. Application Exh. R, Narrative Report at 11.

a. Positions of the Parties

The OCA's witness, Mr. Garrett substituted his own Income Approach for both UVEs' appraisals, resulting in several recommended adjustments to the Income Approach analyses as discussed in OCA Statements 2 and 2SR. Mr. Garrett's proposed adjustments are based on his use of a capitalization of earnings method and different cash flows to value. Mr. Garrett also disagreed with the discount rates used by Gannett Fleming and presented what he believed to be a more appropriate discount rate. The Income Approach utilized by Mr. Garrett was based on the average of EWT's 2018 through 2020 financials as follows:²⁹

²⁹ Mr. Garrett explained that he selected an average of 2018-2020 cash flow data as the basis of his cash flow analysis because it is more appropriate to base an Income Approach FMV analysis on current ownership and cash flow metrics, rather than future ownership. OCA St. 1SR at 17. Mr. Garrett further testified as follows:

In my view, the value of an asset is primarily based on its present value. I am not suggesting that projecting future cash flows should entirely ignore future ownership, however, the various and numerous assumptions Mr. Walker has made in his discounted cash flow model indicate a much different (and higher) value than if the analysis is based on a reasonable projected growth (and discount) of known cash flow metrics under current ownership.

OCA St. 1SR at 14.

Annual Free Cash Flow Calculation				
	Year 0	2018	2019	2020
Operating Revenues	\$ 4,734,652	\$ 5,372,388	\$ 4,444,567	\$ 4,387,000
EBIT	1,116,178	2,246,182	596,544	505,808
Tax (28.89%)	322,464	648,922	172,342	146,128
EBIT (1-t)	793,714	1,597,260	424,202	359,680
Depreciation	756,089	718,700	774,783	774,783
Capital Expenditures	1,290,442	393,256	740,070	2,738,000
Free Cash Flow from Operations	\$ 259,361	\$ 1,922,704	\$ 458,915	\$ (1,603,537)

See Exhibit Q - Gannett Fleming FMV Appraisal, Exhibit 13.
*Year 0 figures are averages of 2018-2020 figures

See OCA Exh. DJG-15. Based on the above financial information, Mr. Garrett performed a direct capitalization of similar cash flows from operations to perpetuity as follows:³⁰

Income Approach Adjustment Summary	OCA Exhibit DJG-14	
Cash Flow	259,361	[1]
Cash Flow		
Constant Growth Rate	0.038	[2]
Discount Rate	0.045	[3]
Multiplier	159.4585	[4]
Value	41,357,255	[5]
[1] From OCA Exhibit DJG-15		
[2] From OCA Exhibit DJG-17		
[3] From OCA Exhibit DJG-16		
[4] Multiplier = (1+[2])/([3]-[2])		
[5] Value = [1] * Multiplier		

³⁰ The capitalization of earning method converts a single base economic income number to a value by dividing it by a capitalization rate.

See OCA Exhs. DJG-14, 15. Based on Mr. Garrett's Income Approach valuation of \$41,357,255, his recommended reductions to Gannett Fleming's and AUS' Income Approach analyses were \$19,790,289 (\$61,147,544 - \$41,357,255) and \$14,242,790 (\$55,600,045 - \$41,357,255), respectively. OCA St. 1 at 24.

Mr. Walker of Gannett Fleming, and Mr. Weinert of AUS disagreed with Mr. Garrett's use of the Township's average financial information for 2018-2020 as the basis for his Income Approach analysis and his discount rate. Aqua M.B. at 39-43. Mr. Walker specifically noted that Gannett Fleming has applied the DCF method as its Income Approach to valuation in fourteen Section 1329 proceedings and submitted that the Commission has not adjusted Gannett Fleming's DCF recommendation in any one of those prior proceedings. Aqua St. 4-R at 12. Aqua argued that Mr. Garrett's recommendations do not meet a standard of value of FMV and are in direct violation of Section 1329. Aqua St. 4-R at 10.

Mr. Walker presented five specific reasons why Mr. Garrett's use of "free cash flow from operations" of \$259,361 is not appropriate to determine the value of the EWT System: (1) the revenues (\$4,734,652) and the EBIT (\$1,116,178) amounts reflect current ownership, current rates, and current operations, which do not reflect the anticipation of future benefits of a hypothetical buyer's ownership; (2) the revenue and EBIT used reflect current ownership, current rates, and current operations, which does not include income taxes nor a fair rate of return; (3) the depreciation expense (\$756,089) is based on the original cost of the assets, not a current value of the assets; (4) the subtraction of income taxes (\$322,464) is not consistent with the current ownership as the Township is a non-income tax paying entity (*i.e.*, municipality); (5) the EBIT (\$1,116,178) amount used by Mr. Garrett is equivalent to a before income tax overall rate of return of only 1.9% to 2.0% on the value of net plant, based on Gannett Fleming's Cost Approach (\$59,118,924) or Mr. Garrett's Cost Approach (\$56,338,551), and is

clearly below the zone of reasonable returns for public utility assets. Aqua St. 4-R at 13; Aqua M.B. at 41; Aqua R.B. at 12-13.

Mr. Walker also presented five specific reasons why Mr. Garrett's discount rate of 4.5% shown on OCA Exhibit DJG-14 and developed on OCA Exhibit DJG-16 is not appropriate: (1) the rate was not determined based on a standard of value of FMV, as is appropriate when used in the Income Approach to valuation, but rather on methods used by witnesses who provide testimony before the Commission concerning fair rate of return on original cost rate base; (2) since Mr. Garrett's capitalization of earnings method reflects current ownership, current rates, and current operations as a municipality, the discount rate should have been based on a municipality's discount rate, not an investor-owned discount rate, so that cash flows and discount rates are coordinated; (3) since Mr. Garrett used book capitalization ratios, commonly used in base rate proceedings, the rate is not reflective of market value capitalization ratios at the valuation date in accordance with accepted valuation practice; (4) for a municipality, the appropriate debt cost rate is the current municipal revenue bond rate at the valuation date, not the embedded cost of debt, as used by Mr. Garrett; and (5) Mr. Garrett's equity cost rate was not determined at the valuation date (*i.e.*, May 20, 2021) in accordance with accepted valuation practices and used for market valuation purposes.³¹ Aqua St. 4-R at 15-17; Aqua M.B. at 41; Aqua R.B. at 13.

Similarly, AUS consultant, Mr. Weinert disagreed with Mr. Garrett's single year's "free cash flow from operations" used in his recommended capitalization of earnings model, contending that Mr. Garrett erroneously assumes that revenues and expenses as reported in EWT's financial information will be the operating results of the

³¹ The OCA argued that Mr. Garrett's equity cost rate, calculated over a period from January 18, 2022 to March 1, 2022, does not comport with the requirements of 66 Pa. C.S. § 1329 nor comply with the USPAP. A fair market value appraisal is determined on a stated valuation date, not for a period of time. Aqua St. 4-R at 17.

buyer. Aqua M.B. at 42. Aqua submitted that expenses and rate base will change as a result of the sale, and that Mr. Garrett's estimated cost of equity at 6.0% is far below what the Commission regularly assumes is the cost of equity, which was 9.85% based on the Bureau of Technical Utility Services Report on Quarterly Earnings, of Jurisdictional Utilities for the Year Ending December 31, 2020. Aqua St. 5-R at 21; Aqua M.B. at 50.

In response to Mr. Garrett's proposed adjustments, Mr. Weinert presented an adjusted OCA model in his rebuttal testimony. Aqua submits, when adjusted for the transition of the Township wastewater operation to a rate regulated utility, the OCA model produces an Income Approach indicator of \$62,117,860 which is significantly higher than the AUS Income Approach indicator of \$55,600,045. Aqua M.B. at 42. Since the AUS result of \$55,600,045 is conservative in comparison to the result of \$62,117,860 when the OCA model is properly adjusted as presented by Mr. Weinert, Aqua contended that the Commission should reject the OCA adjustment to the AUS Income Approach. *Id.*

b. Recommended Decision

The ALJ did not address either Gannett Fleming's or AUS' Income Approach in her Recommended Decision.

c. Aqua Exception No. 3³² and Replies

Although the ALJ did not make a determination regarding the Income Approach, nevertheless, as part of its Exception No. 3 Aqua reiterates several of its positions and arguments previously presented in its testimony and briefs. Aqua Exc.

³² It is noted that EWT stated in its Exceptions that it adopts and incorporates by reference all of Aqua's Exceptions related to Gannett Fleming's and AUS' Income Approaches. EWT Exc. at 8.

at 32-35. Additionally, Aqua explains that the Income Approach to valuation used in Gannett Fleming's appraisal is based on the DCF method, which values the potential for profit in an investment and reflects future events. Aqua Exc. at 33 (citing Pratt, Shannon P. *Defining Standards of Value*. Valuation 34, no. 2, June 1989. <http://www.appraisers.org/docs/default-source/college-of-fellows-articles/defining-standards-of-value.pdf>). Aqua argues that Gannett Fleming used the DCF method to be consistent with the required standard of value of FMV.³³ The DCF method "is based on the principle of anticipation - *i.e.*, value is created by the anticipation of future benefits. DCF analysis reflects investment criteria and requires the appraiser to make rational and supportable assumptions." Aqua Exc. at 33 (citing Appraisal Standards Board, *First Exposure Draft of proposed new Advisory Opinions and Advisory Opinion Revisions in conjunction with the 2016-17 edition of the Uniform Standards of Professional Appraisal Practice* at 6).

Conversely, Aqua argues that the OCA's capitalization of earnings or cash flow method, which converts a single base economic income number to a value by dividing it by a capitalization rate, has never been accepted by the Commission in a Section 1329 proceeding. Aqua Exc. at 33.

Aqua further argues that, although Mr. Garrett stated that the single cash flow that he utilized is from the Gannett Fleming appraisal, he failed to disclose that the single cash flow was not used in the Income Approach to valuation used in Gannett Fleming's appraisal. Specifically, the Income Approach to valuation used in the Gannett Fleming appraisal is based on projected cash flows beginning in 2022 and thereafter. Aqua Exc. at 34.

³³ Aqua maintains that since the Commission has not adjusted Gannett Fleming's DCF recommendation, pertaining to its Income Approach, in any of the prior fourteen Section 1329 proceedings in which it was utilized, it should, likewise, not be adjusted in this proceeding. Aqua Exc. at 32-33.

Similarly, in relation to AUS' appraisal, Aqua maintains its disagreement with Mr. Garrett's single year's "free cash flow from operations" used in his recommended capitalization of earnings model, contending that Mr. Garrett erroneously assumes that revenues and expenses as reported in EWT's financial information will be the operating results of the buyer. Aqua Exc. at 35.

In reply, the OCA maintains that it is more appropriate to base an income approach FMV analysis under Section 1329 on current ownership and cash flow metrics, rather than future ownership. OCA R. Exc. at 24. The OCA avers that the importance of basing the Income Approach on present ownership under Section 1329 has been recently discussed by the Commission in *Lower Makefield* as follows:

As previously indicated, the Income Approach is based on the premise that the value of a property is the *present* value of the future net benefits of owning the property.

Id. (citing *Lower Makefield* at 69) (emphasis by the OCA).

The OCA argues that Mr. Walker, Mr. Weinert, and the OCA's witness, Mr. Garrett, all utilized a process which involves discounting projected cash flows to arrive at their respective Income Approach valuations; however, the difference between Mr. Garrett's and the UVEs' valuation using the Income Approach is that Mr. Garrett based his FMV analysis on current ownership and cash flow metrics, rather than future ownership. The OCA maintains that Mr. Garrett's approach of using actual data is a reasonable approach to valuation, whether or not Mr. Walker has proposed it in a previous Section 1329 proceeding. Further the OCA contends that Aqua's statement that the Commission "has never accepted the capitalization of earnings method recommended by Mr. Garrett in a Section 1329 fair market value proceeding" is misleading, given that most of those proceedings were settled, and due to that, the Commission has not yet

reviewed the adjustments recommended by the OCA's witness, Mr. Garrett.
OCA R. Exc. at 22-23.

d. Disposition

We must agree with Aqua that the OCA did not establish that its proposed adjustments to the Gannett Fleming and AUS Income Approach results, based on Mr. Garrett's use of a single year cash flow utilizing an average of the Township's 2018 through 2020 financials, are appropriate in this proceeding. We agree with Aqua's reasoning that the OCA's formulation of the income from operations and the resultant value erroneously assumes that revenues and expenses as reported in EWT's financials will be the operating results of the buyer. As the ownership and operation migrates to the buyer, Aqua in this case, several changes will occur; namely there will be a new rate base determined by the Commission based on their findings in this Application and the buyer, Aqua, will be allowed to earn a Commission authorized return on rate base. Operating expense, including taxes, will be incorporated along with the allowed return on rate base in determining the ongoing EWT revenue requirement. Mr. Garrett's model does not factor in these changes to the Township's operations as a rate-regulated wastewater utility.

Further, we agree with Aqua that Mr. Garrett's use of the original cost plant value as the basis for his Income Approach is not reasonable. The circularity of this recommendation defeats or eliminates the need to appraise plant assets since the indicated value of net cost of the plant assets is simply the net original cost of the plant assets under Mr. Garrett's recommendation. If this were the appropriate or correct method to value assets, then an original cost less depreciation analysis would be the only method needed to value assets. However, the value of the investment in plant and equipment for the Township's System assets is being determined in these proceedings based upon a standard of value of fair market value, not a standard of value of original cost.

To be consistent with the standard of value of FMV, the UVEs used the DCF method, which is based on the principle of anticipation, *i.e.*, value is created by the anticipation of future benefits. Accordingly, we are not persuaded to accept the OCA's recommended Income Approach valuation of approximately \$41.4 million, which effectively would reduce Gannett Fleming's and AUS' Income Approach valuations by \$19,790,289 (\$61,147,544 - \$41,357,255) and \$14,242,790 (\$55,600,045 - \$41,357,255), respectively.

4. Market Approach

a. Gannett Fleming

(1) Positions of the Parties

Gannett Fleming's Market Approach to value, which was prepared under the direction of Mr. Walker of Gannett Fleming, was based on the Market Multiples Method and the Selected Transactions Method.³⁴

The general assumptions used for the Market Multiples Method are listed on page 1 in Exhibit 17 to the Application's Exhibit Q. The Market Multiples Method resulted in an indicated value of \$49,340,713. *Id.* None of the Parties in this proceeding objected to Gannett Fleming's Market Multiples Method under the Market Approach. However, as discussed, below, the OCA objected to Gannett Fleming's Selected Transactions Method.

³⁴ Details on Gannett Fleming's development of the Market Multiples Method and the Selected Transactions Method are described in Application Exhibit Q on pages 35-38 and 38-42, respectively. *Also see* Aqua St. 4 at 24.

In determining the selected transactions used in this evaluation, Mr. Walker limited his search to: (1) those that occurred in 2016 or later; (2) purchases involving water or wastewater systems; (3) the assets being purchased; and (4) those that did not discount “cost free” capital/customer contributions in the valuation. Application Exh. Q at 40. Based on the above criteria, Mr. Walker ultimately selected thirteen Section 1329 transactions to use in the study.³⁵

In the next step, Mr. Walker calculated sales price multiples of selected transactions involving the purchase or sale of business that met the state selection criteria. The calculated sales price multiples included transactions multiples of: Investor Provided Capital (ICAP); Gross Property, Plant and Equipment (GPPE); Net Property, Plant and Equipment (NPPE); Revenue; EBITDA; EBIT; Customers; and Population. Application Exh. Q at 40.

Mr. Walker noted that the Selected Transactions Method relies on and reflects information that was known, *i.e.*, *ex-ante*, at the time the winning purchase bid (price) was offered, and the metrics used are time-period sensitive (*e.g.*, bids made in

³⁵ The selected transactions used by Gannett Fleming are: (1) Sale of the City of McKeesport Wastewater system to Pennsylvania-American Water Company in 2017; (2) Sale of New Garden Township Sewer Authority to Aqua Pennsylvania in 2017; (3) Sale of Limerick Township Wastewater system to Aqua Pennsylvania in 2017; (4) Sale of East Bradford Township Wastewater system to Aqua Pennsylvania in 2018; (5) Sale of Mahoning Township Water system to Suez Water Pennsylvania in 2018; (6) Sale of Mahoning Township Wastewater system to Suez Water Pennsylvania in 2018; (7) Sale of Sadsbury Township Wastewater system to Pennsylvania-American Water Company in 2018; (8) Sale of Exeter Township Wastewater system to Pennsylvania-American Water Company in 2019; (9) Sale of Steelton Borough Authority Water system to Pennsylvania-American Water Company in 2019; (10) Sale of Cheltenham Township Wastewater system to Aqua Pennsylvania in 2019; (11) Sale of East Norriton Township Wastewater system to Aqua Pennsylvania in 2019; (12) Sale of Kane Borough Authority Water system to Pennsylvania-American Water Company in 2020; and (13) Sale of Royersford Borough Authority Water system to Pennsylvania-American Water Company in 2021. *See* Aqua St. 4 at 25-26; Application Exh. Q, Exh. 18 at 2-3.

2016 only reflect metrics from 2015 since the results of 2016 could not be known at the time of the bids). *Id.* The resulting *ex-ante* metrics are included on page 2 of Exhibit 18 to Application Exhibit Q. Since complete information only existed for a few of the transactions using *ex-ante* data, Gannett Fleming supplemented the *ex-ante* data with *ex-post* information of GPPE and NPPE (collectivity called “Asset Items”). Application Exh. Q at 40-41. The *ex-post* metrics are included on page 3 of Exhibit 18 to Application Exhibit Q.

In the next step, Mr. Walker applied the selected transactions multiples of the selling utilities to develop an indicated value of the EWT’s System. Application Exh. Q at 41; OCA St. 1 at 7. This was accomplished by multiplying the EWT System’s financial and operating data by the selling utilities’ transactions multiples.³⁶ *Id.* The results of Gannett Fleming’s Selected Transactions Method, which are included on page 1 of Exhibit 18, range in value from \$35.5 million to \$63.2 million when all transactions are considered, and a range in value of \$19.2 million to \$58.7 million when mostly collection/distribution assets are solely considered. Application Exh. Q at 41. After giving additional weight to the selected transactions multiples for the collection/distribution assets, Gannett Fleming’s selected transactions method resulted in an indicated value of \$44,142,464 million. *Id.*, Application Exh. Q, Exh. 18.

Collectively, Gannett Fleming’s Market Multiples Method value of \$49,340,713 and the Selected Transactions Method value of \$44,142,464, which were both given a weighting of 50%, resulted in a total Market Approach value of \$46,741,589. Application Exh. Q, Exh. 19.

The OCA witness, Mr. Garrett, made several adjustments to Mr. Walker’s Selected Transaction Method in which he: (1) excluded all integrated treatment and

³⁶ See pages 2 and 3 of Exhibit 18 to Application Exhibit Q.

collection systems (integrated systems) from his analysis and only considered collection/distribution companies (OCA St. 1 at 8-9; OCA M.B. at 34, 35); (2) excluded *ex-ante* data from his analysis and only considered the use of OCNLD, or *ex-post* data (OCA M.B. at 34); and (3) substituted the Commission's FMV rate bases in lieu of the purchase prices paid for each transaction. *Id.*

Regarding the OCA's first adjustment that removed all the selected transactions involving integrated systems from Gannett Fleming's FMV Appraisal,³⁷ Mr. Garrett testified that although he does not believe it is necessarily unreasonable to include integrated systems when assessing the fair market value of a collection-only system under the Selected Transactions Method or similar type of market analysis, in this case, including integrated systems in the analysis produced several results that are unreasonably high. *Id.* at 9.

With regard to the OCA's second adjustment in which Mr. Garrett relies on OCNLD, or *ex-post* data, rather than both *ex-ante* and *ex-post* data as used by Mr. Walker, Mr. Garrett testified that his approach, which relies on OCNLD data, is consistent with the OCA's approach in prior Section 1329 proceedings, and it should not be disregarded simply because the data was obtained after the transaction purchase price was determined. OCA St. 1SR at 4.

In the OCA's third adjustment that used FMV rate bases approved by the Commission for each of the selected transactions in lieu of the negotiated purchase prices of the selected transactions paid by the buyers, Mr. Garrett testified that since the Selected Transactions Method is being used for the sole purpose of helping the

³⁷ Mr. Garrett noted that although the Township owns one wastewater treatment plant that treats water for another small community system, the Township's wastewater treatment is provided primarily by another entity such that the EWT System is properly characterized as a collection-only system for purposes of analysis. Aqua St. 1 at 10.

Commission determine the fair market value in this proceeding, “[i]t 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.” OCA St. 1SR at 3-4. Mr. Garrett asserted that when the Commission establishes a ratemaking rate base based on FMV in any particular Section 1329 proceeding, “the Commission is essentially determining that the winning bid does not comport with the fair market value of a particular transaction.” OCA St. 1SR at 3.

Aqua’s witness, Mr. Walker, argued that Mr. Garrett’s adjustments to Gannett Fleming’s Selected Transaction analysis do not meet a standard of value of fair market value and are in direct violation of Section 1329. Aqua St. 4-R at 17-18, 24. Mr. Walker specifically contended that Mr. Garrett’s choice of selected transactions represents an unreliably small sample size that should not be accepted for a Selected Transaction analysis. Aqua M.B. at 35-37. Mr. Walker also contended that Mr. Garrett’s use of only *ex-post* data in his analysis should be rejected because the Selected Transactions Method relies on and reflects information that was known, *ex-ante*, at the time the winning purchase bid (price) was given, and the winning purchase bid (price) could not have reflected *ex-post* information that was not available when it was made. Aqua St. 4-R at 19. Finally, Mr. Walker disagreed with Mr. Garrett’s proposal to use the ratemaking rate bases approved by the Commission for each transaction rather than the purchase prices used in the Gannett Fleming analysis because the Commission-approved, FMV rate base is not representative of a market transaction. Aqua St. 4-R at 19.

In summary, Gannett Fleming’s uncontested Market Multiples Method, as shown in Exhibit 17 of Application Exhibit Q, results in an indicated value of \$49,340,713. Gannett Fleming’s Selected Transactions Method, as shown on Exhibit 18 of Application Exhibit Q, results in an overall indicated value of \$44,142,464. After applying 50% weightings to the indicated results from the Market Multiples Method and the Selected Transactions Method, Gannett Fleming FMV of the EWT’s System under

the Market Approach is \$46,741,589 as summarized in the table below. Application Exh. Q, Exh. 19.

As noted, the OCA agreed with Gannett Fleming’s Market Multiples Method analysis that resulted in an indicated value of \$49,340,713. However, the OCA’s adjustments to the Gannett Fleming’s Selected Transactions Method resulted in an overall indicated value of \$29,756,954. The OCA also agreed with Gannett Fleming’s 50% weightings for the Market Multiples Method and Selected Transactions Method. After applying the 50% weightings to the OCA’s indicated results from the Market Multiples Method and the Selected Transactions Methods, the OCA adjusted FMV of the Township’s System under the Market Approach is \$39,548,833 as summarized in the table below.

	[1]	[2]	[3]	[4]	[5]	[6]
	Gannett Fleming Market Approach Results			OCA Adjusted Market Approach Results		
	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

[1], [2], [3] Gannett Fleming FMV Appraisal, Exhibit 18
 [4] Adjusted amounts from OCA Exhibit DJG-4
 [5] Applied weighting
 [6] = [4] * [5]

OCA Exhibit DJG-3.

(2) Recommended Decision

The ALJ did not address Gannett Fleming’s Market Approach in her Recommended Decision.

(3) Aqua Exception No. 3,³⁸ Replies, and Dispositions

(a) Selected Transaction Method – *Ex-Ante* and *Ex-Post* Data

In its Exceptions, Aqua first takes issue with Mr. Garrett’s reliance only upon *ex-post* data in his analysis instead of Gannett Fleming’s use of both data from financial statements (*i.e.*, *ex-ante* data) and OCNLD data used in the respective proceeding (*i.e.*, *ex-post* data). Aqua Exc. at 29. Aqua submits that the OCA recommended an identical approach to exclude *ex-ante* data (financial statements) in *Cheltenham*,³⁹ and that approach was rejected by the Commission. Aqua Exc. at 29 (citing Aqua St. 4 at 18-19).

Aqua contends that had Mr. Garrett applied only *ex-post* data to all the collection/distribution systems Selected Transactions used in the Gannett Fleming appraisal, Mr. Garrett’s methodology would indicate a value of \$47,693,222, or 60% more than his \$29,756,954 recommendation for the Selected Transactions Method. Aqua Exc. at 30 (citing Aqua St. 4-R at 22-23).

³⁸ It is noted that EWT stated in its Exceptions that it adopts and incorporates by reference all of Aqua’s Exceptions related to Gannett Fleming’s and AUS’ Market Approaches.

³⁹ *Cheltenham* at 73-74.

Aqua also asserts that Mr. Walker emphasized in his testimony that Mr. Garrett's Selected Transactions Method result of \$29,756,954 is less than the system's depreciated original cost (OCNLD) of \$32,955,596, which suggests a multiple of OCNLD of 0.90-times ($\$29,756,954 \div \$32,955,596$). Mr. Walker testified that the FMV for \$32,955,596 OCNLD cannot be as low as 0.90-times, and Mr. Garrett presented no evidence that would support an OCNLD multiple of 0.90. Aqua Exc. at 30 (citing Aqua St. 4-R at 23-24; Aqua M.B. at 36).

The OCA rejoins that Mr. Garrett's reliance on *ex-post* data in this proceeding is consistent with the OCA's recommendations in prior Section 1329 proceedings. OCA R. Exc. at 18 (citing OCA St. 1SR at 4; OCA M.B. at 34-35). The OCA maintains its position that 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. OCA R. Exc. at 18 (citing OCA St. 1SR at 4). The OCA notes that Aqua's witness, Mr. Walker, acknowledged that using only OCNLD, or *ex-post* data, would have changed his valuation only by less than \$1 million. OCA R. Exc. at 18 (citing OCA St. 1 SR at 4; Aqua St. 4R at 18).

We agree with Aqua's arguments in its Exceptions that using only *ex-post* data in the Selected Transactions Method Analysis is not appropriate. As Aqua noted in its Exceptions, in *Cheltenham*, the OCA recommended an identical approach in its Selected Transactions Method analysis to exclude *ex-ante* data which was rejected by the Commission. Aqua Exc. at 29 (citing *Cheltenham* at 73-74).

In this proceeding, as explained, *supra*, Mr. Garrett, *inter alia*, excluded all *ex-ante* data and included only *ex-post* data as part of his adjustments to Mr. Walker's Selected Transactions Method. In *Cheltenham*, we denied similar *ex-post* adjustments by the OCA to Gannett Fleming's Market Approach based on our conclusion that "the metrics used in the Market Approach are those metrics known by the bidder at the time

the winning purchase price (bid) is given.” *Cheltenham* at 73. In this proceeding, Aqua used *ex-ante* data supplemented by *ex-post data* in those instances where limited *ex-ante* data existed, whereas the OCA relied exclusively on *ex-post* data. Similar to his argument in *Cheltenham* that favored using *ex-ante* data, Aqua’s witness, Mr. Walker, presented the following argument in his testimony against the sole use of *ex-post* data:

The Selected Transaction[s] Method relies on and reflects information that was known, *ex-ante*, at the time the winning purchase bid (price) was given. After all, the winning purchase bid (price) could not have reflected *ex-post* information that was not available when it was made. The metrics (property, plant and equipment, Customers, etc.) used in the Selected Transaction[s] Method are relative to the time period the bid (price) was made. That is, the metrics are time period sensitive. For example, a 2016 bid would likely reflect metrics from 2015 since the results of 2016 would not be known at the time. It is unrealistic and unreasonable for Mr. Garrett to suggest, by omission, that only *ex-post* data that **becomes available only after a bid is made** is more appropriate than *ex-ante* financial information in the Market Approach.

Aqua St. 4-R at 19.

We agree with Mr. Walker’s argument against the OCA’s exclusive use of *ex-post* data in the Selected Transactions Method analysis. Also, as noted, the OCA is proposing similar adjustments to its Selected Transactions Method analysis in this proceeding that it also proffered in *Cheltenham* and that we rejected. Furthermore, we note that the OCA did not respond to Mr. Walker’s observation as to how the Township’s System valuation could be less than its depreciated original cost. Accordingly, consistent with our ruling in *Cheltenham* and Mr. Walker’s arguments against using only *ex-post* data, we shall grant Aqua’s Exception on this matter.

**(b) Selected Transaction Method – Use of FMV
Ratemaking Rate Base Value instead of the
Purchase Price Paid**

Next, in its Exceptions, Aqua objects to Mr. Garrett's substitutions of the purchase prices paid for the selected transactions with the fair market value rate bases approved by the Commission. Aqua Exc. at 29. Aqua submits that the same approach was recommended by the OCA and rejected by the Commission in *Cheltenham*. *Id.* Aqua further contends that there is no authoritative source, nor Commission precedent, to support the use of Commission-directed ratemaking rate base values in the Market Approach. Aqua Exc. at 29-30 (citing Aqua St. 4-R at 20).

In reply, the OCA submits that Mr. Garrett's use of Commission-approved rate base to make a valuation under the Market Approach is acceptable because a Commission-approved rate base represents a market transaction. OCA R. Exc. at 18 (citing OCA St. 1 at 3-4; OCA M.B. at 34). The OCA notes that in *Cheltenham*, the Commission expressed concern that using purchase prices to determine fair market values has the potential to create a circular pattern that rewards utilities for paying excessive purchase prices. OCA R. Exc. at 18 (citing *Cheltenham* at 57). The OCA avers that using Commission-approved rate base here will help address the concerns that the Commission expressed in *Cheltenham* about allowing UVEs to use purchase prices that are higher than the Commission-determined ratemaking value when assessing an asset's fair market value. OCA R. Exc. at 18. The OCA states that the only reason the Commission ultimately accepted the UVE's use of purchase prices instead of Commission-determined rate bases in *Cheltenham* was because the Commission was concerned that Commission-determined rate base represented a hypothetical assumption of market value rather than an actual indication of market value. OCA R. Exc. at 19 (citing *Cheltenham* at 58). However, the OCA explains that Mr. Garrett testified in this proceeding that once the Commission determines a rate base, both parties still have the

freedom to choose not to move forward with the proposed transaction. OCA R. Exc. at 19 (citing OCA St. 1SR at 6). Thus, the OCA is of the opinion that the Commission-determined rate base is acceptable to determine a valuation of EWT's assets under the Market Approach because it is not a hypothetical value, but rather represents a market sale because it must be agreed to by both buyer and seller. *Id.*

We do not agree with the OCA's analysis that uses the Commission's FMV rate bases instead of the purchase prices paid for each of the transactions it used in its adjustments to the Selected Transactions Method analysis under Gannett Fleming's Market Approach. Our determination here is similar to our ruling in *Cheltenham*. In *Cheltenham*, the OCA similarly argued, as it did in this proceeding, that the selected transactions under the Market Approach should use the Commission-determined fair market value rate bases in lieu of the purchases prices agreed upon by the buyer and seller because using purchase prices that are higher than Commission-determined ratemaking rate base values will overstate the fair market value of an acquisition. *Cheltenham* at 58.

In *Cheltenham*, the Company's and Cheltenham Township's UVE's, Gannett Fleming and AUS, respectively, used negotiated purchase prices for market comparables and/or selected transactions under the Market Approach. *Cheltenham* at 57. In that proceeding, Aqua argued, and the presiding officer, ALJ Angela Jones agreed, that using Commission-determined ratemaking rate base values as market comparables would represent hypothetical assumptions that would be contrary to USPAP. *Cheltenham* at 58. In that proceeding, we adopted the rationale of ALJ Jones in her Recommended Decision where she determined that AUS' use of negotiated purchase prices cannot be found to be unreasonable "because the purchase price is the price paid in the market, not the ratemaking rate base determination of the Commission." *Cheltenham* at 58; *Cheltenham* R.D. at 38.

It is noted however, that in *Cheltenham*, ALJ Jones shared some concern with the OCA that “accepting the use of higher [negotiated] purchase prices would result in greater ratemaking rate base values, which would appear to create a circular pattern that would reward utilities for paying excessive purchase prices.” *Id.* Accordingly, although ALJ Jones rejected the OCA’s position to use Commission-determined ratemaking rate base values, she did recommend “that the Commission consider issuing a jurisdictional exception in a future Section 1329 supplemental implementation order to require UVEs to use ratemaking rate base values in place of purchase prices for market approach valuation purposes.” *Id.*

However, we disagreed with ALJ Jones’ jurisdictional exception recommendation in *Cheltenham*. *Cheltenham* at 61. But we did agree with the ALJ’s recommendation that rejected the use of the Commission-determined rate bases because using Commission-determined ratemaking rate base values as market comparables would represent hypothetical assumptions that would be contrary to USPAP. *Cheltenham* at 60-61. Since a Commission-determined ratemaking rate base value is not a reflection of what willing buyers will ultimately pay in a market and does not change the price bid and paid by a buyer, we maintain our policy position in this proceeding that the proper transaction inputs under the Market Approach valuation are based on the purchase prices of those transactions determined by the buyers and sellers prior to the valuation dates rather than the Commission-determined fair market values of the ratemaking rate bases.

In view of the above, the OCA has not offered any new arguments in this proceeding that would convince us to reverse our policy established in *Cheltenham*. Accordingly, Aqua’s Exception on this matter is granted.⁴⁰

⁴⁰ We note, as will be discussed, *infra*, that Aqua made the same arguments in its Exceptions to reject the OCA’s use of the Commission’s FMV rate bases in lieu of the purchase prices for each of the transactions the OCA used in its adjustments to the Comparable Market Sales Method analysis under the AUS Market Approach.

(c) Selected Transaction Method – Choice of Selected Transactions

Finally, in its Exception No. 3, Aqua submits that unlike Gannett Fleming's analysis, which includes information for thirteen selected transactions, Mr. Garrett's analysis was based on only three of the thirteen transactions after he excluded various selected transactions that were not solely collection/distribution systems.⁴¹ Aqua Exc. at 30. According to Aqua, this is an unreliably small sample size that Mr. Garrett compounded by excluding results or indications of value he viewed as too high or too low. Aqua Exc. at 30 (citing Aqua St. 4-R at 22; Aqua M.B. at 35).

Aqua contends that had Mr. Garrett not subjectively removed the indicated values that he determined were too high or too low, his result for the Selected Transactions Method would be \$38,072,212, or 28% more than his \$29,756,954 recommendation. Aqua Exc. at 30 (citing Aqua St. 4-R at 22).

In reply, the OCA asserts that Mr. Garrett did explain his decision to include only those transactions involving collection/distribution systems in his market approach analysis in his testimony. OCA R. Exc. at 19 (citing OCA St. 1 at 9-10; OCA St. 1SR at 5). The OCA submits that Mr. Garrett testified that, because EWT owns only one small wastewater treatment plant, the Township System may be properly characterized as a collection-system only, and therefore, it is not reasonable to include integrated systems in the Market Approach analysis. OCA St. 1 at 9-10.

⁴¹ The three transactions that Mr. Garrett ultimately used in his Selected Transactions Method are: (1) East Bradford Township Wastewater Collection System; (2) Mahoning (combination of Mahoning Township Water system and Mahoning Township Wastewater System); and (3) PAWC/Upper Pottsgrove Wastewater Collection. See OCA Exh. DJG-4.

The OCA claims that Mr. Garrett's adjustment, which resulted in a valuation estimate of \$39.5 million, or about \$7.1 million less than Gannett Fleming's Market Approach valuation of \$46.7 million, is far more reasonable than Gannett Fleming's result in view of the fact that Mr. Garrett excluded integrated systems because the Township is not an integrated system and also because Mr. Garrett found that including integrated systems in his analysis produced several results that are unreasonably high. OCA R. Exc. at 19-20 (citing OCA St. 1 at 11; OCA M.B. at 35).

Based on our review and comparison of the transactions used by Gannett Fleming and the OCA in their analyses, we are of the opinion that the sixteen transactions selected and used by Gannett Fleming to determine the FMV appraisal of the Township's System results is a better approximation to the FMV of the EWT System than the three transactions ultimately selected by the OCA.

We have several concerns with Mr. Garrett's selections that convinces us that Gannett Fleming's selected transactions provide a more realistic approach. As noted, Mr. Garrett's analysis included only three Collection/Distribution (C/D) as opposed to Gannett Fleming's thirteen transactions. Mr. Garrett explained that his decision in choosing his transactions was because the Township's System is more appropriately classified as a "collection-only" system since the Township owns only one small wastewater treatment plant. OCA St. 1 at 9, n.11. Therefore, Mr. Garrett chose to exclude the seven integrated systems that were included in Gannett Fleming analysis so that his resulting transactions would just include collection/distribution systems. Aqua St. 4-R at 21. After excluding the seven selected transactions, Mr. Garrett further reduced his sample size by excluding transactions that he determined to be too high. OCA St. 1 at 9. Ultimately, Mr. Garrett's recommendation regarding Gannett Fleming's Selected Transactions Method based was based on only three selected C/D transactions. Aqua St. 4-R at 20-22. As noted, the three C/D transactions are East Bradford, Mahoning and Upper Pottsgrove. *See* OCA Exh. DJG-4. Furthermore, for unknown reasons,

Mr. Garrett combined the two separate transactions for the Township of Mahoning Water System Assets and the Township of Mahoning Sewer System Assets as a single transaction in his analysis (Aqua St. 4-R at 20). Again, without any explanation, Mr. Garrett added the Upper Pottsgrove transaction – a transaction which was not included in Gannett Fleming’s analysis and also is not a valid transaction since it was filed after the May 20, 2021 valuation date. Aqua St. 4-R at 21. If Upper Pottsgrove were eliminated, the number of Mr. Garrett’s transactions remaining for analysis would be reduced to two, assuming there was a valid reason that Mr. Garrett combined the Mahoning Water and Mahoning Wastewater transactions as a single transaction. Thus, we are persuaded that the adjustments proposed by the OCA to Gannett Fleming’s Selected Transactions Method would not result in a reliable appraisal of EWT’s System under the Market Approach.

In consideration of the above, we shall grant Aqua’s Exception on this issue and approve Gannett Fleming’s Selected Transactions Method without any adjustments.

b. AUS

(1) Positions of the Parties

AUS’ Market Approach to value, which was prepared by Mr. Weinert of AUS Consultants, was based on: (1) the Financial Market Ratios Method which considered various market-to-book value ratios for nine investor-owned water utilities⁴²

⁴² The nine companies selected were: (1) American States Water; (2) American Water; (3) Aqua America; (4) California Water Company; (5) Consolidated Water Company; (6) Middlesex Water; (7) Middlesex Water; (8) SJW Corp; and (9) York Water Company.

as reported in the January 8, 2021 *Value Line Investment Survey*;⁴³ and (2) the Comparable Market Sales Method that used eighteen sales transactions of Pennsylvania municipal water and wastewater systems to investor-owned water/wastewater utilities.⁴⁴ Aqua M.B. at 36; Application Exh. R at 12, 42.

Under the Financial Market Ratios Method, Mr. Weinert analyzed market financial ratios for nine water industry companies as reported in the January 2021 edition of *Value Line Investment Surveys*. In the analysis, the companies' stock (market) and debt (book) per share are compared as a ratio to the book value per share. Mr. Weinert determined that an accurate result depends on using the weighted mean of the ratio of the

⁴³ Details on AUS' development of the Market Multiples Method and the Selected Transactions Method are described in AUS' Fair Market Value Appraisal Report on pages 12-15 (Executive Summary) and pages 41-52 in Application Exhibit R. *Also see* Aqua St. 5 at 14-18.

⁴⁴ Mr. Weinert used the following comparable sales transactions in his Comparable Sales Method analysis: (1) Sale of City of McKeesport Wastewater Collection and Treatment System to Pennsylvania-American Water Company in 2016; (2) New Garden Township Wastewater Collection and Paid For and Owned Treatment System to Aqua Pennsylvania in 2016; (3) Limerick Township Wastewater Collection and Treatment System to Aqua Pennsylvania; (4) East Bradford Township Wastewater Collection and Paid For Treatment System to Aqua Pennsylvania in 2017; (5) Mahoning Water Distribution System to Suez Pennsylvania in 2018; (6) Mahoning Wastewater Collection System to Suez Pennsylvania in 2018; (7) Cheltenham Wastewater Collection System in 2018; (8) Steelton Water Distribution and Treatment System to Pennsylvania-American Water Company in 2018; (9) Sadsbury Wastewater Collection System to Pennsylvania-American Water Company in 2017; (10) Exeter Wastewater Collection and Treatment System to Pennsylvania-American Water Company in 2018; (11) East Norriton Wastewater Collection System to Aqua Pennsylvania in 2018; (12) McKean Wastewater Collection and Treatment System in 2018; (13) Royersford Wastewater Collection and Treatment System in 2019; (14) Valley Water Treatment and Distribution System to Pennsylvania-American Water Company in 2019; (15) Valley Wastewater Collection System to Pennsylvania-American Water Company in 2019; (16) Delaware County Regional Wastewater Collection and Treatment System to Aqua Pennsylvania in 2019; (17) Upper Pottsgrove Wastewater Collection System to Pennsylvania-American Water Company; and (18) Lower Makefield Wastewater Collection and Purchased Treatment Capacity System to Aqua Pennsylvania in 2020. Aqua St. 5 at 18.

market debt and equity to book debt and equity. This method resulted in an estimated market value of \$70,482,381 as shown in the table below. Aqua St. 5 at 14; Application Exh. R at 49.

Financial Basis¹		Market Value per Share to Book Value per Share	
Financial Markets			
Market to Book (equity)		3.40	
Market to Book (equity and debt)		2.11	
Use (equity and debt)		2.11	AUS Input
East Whiteland Township's Wastewater Collection System and Purchased Treatment Capacity OCLD		33,403,972	Cost Approach - OCLD
Market Value Indication		70,482,381	

In order to arrive at a measure of comparability under the Comparable Market Sales Method, Mr. Weinert analyzed the Section 1329 purchase prices of the eighteen Pennsylvania municipal water and wastewater systems in relationship to their: (1) depreciated original cost (OCLD); (2) depreciated replacement cost (RCNLD or CORLD); (3) customers; and (4) cashflows (EBITDA) for both, average five-year and thirteen-year periods.⁴⁵ He also analyzed the stock (market) and debt (book) per share as a ratio to the book value per share of each of the nine investor-owned water utilities companies he selected.⁴⁶ The table below summarizes the results of the Financial Market Ratios Method and Comparable Market Sales Method used by Mr. Weinert in his Market Approach analysis.

⁴⁵ Tables containing the details of the Purchase Price to OCLD, Purchase Price to CORLD, Purchase Price to Customers, Purchase Price to Cash Flows (EBITDA) (5 and 13-year periods) are included in Application Exh. R on pages 44-48.

⁴⁶ A summary of the measures of comparability are included in the table on page 50 of Application Exhibit R.

Market Approach			
Market Comparables (to)			
OCLD	65,048,584		
CORLD	56,178,539		
Customers	34,298,172		
Cash Flows (EBITDA)	43,140,348		
Market Financials (to)			
OCLD	70,482,381		
Market Approach Conclusion	56,178,539	10%	5,617,854

Application Exh. R, Valuation Summary at 2 of 28.

Mr. Weinert ultimately decided that the ratio of the purchase prices to the properties' depreciated replacement cost (*i.e.*, RCNLD or CORLD) was the best indicator to determine the appraised value of the physical assets of EWT's wastewater collection system under this method. Mr. Weinert then applied that ratio to the Township's RCNLD to determine its implied market valuation. Using this approach, Mr. Weinert estimated the market value of the EWT System to be \$56,178,539 as shown in the table below. Aqua St. 5 at 3, 4, 14-18; Application Exh. R at 18, 50; OCA St. 1 at 11.

Market Sales Analysis - PP/CORLD			
	Simple	Weighted	
Mean	0.8087	0.9337	
Standard Deviation	0.1746	0.1695	
Median	0.8229	0.7558	
Mode	0.6918	0.6918	
Conclusion		0.9387	AUS Input
East Whiteland Township's Wastewater Collection System and Purchased Treatment Capacity CORLD		59,847,171	Cost Approach - CORLD
Market Value Indication		56,178,539	

The OCA's witness, Mr. Garrett, made three adjustments to Mr. Weinert's analysis in which he: (1) included only collection/distribution systems from the list of the

eighteen comparable sales transactions used by AUS (OCA St. 1 at 12);⁴⁷ (2) substituted the Commission’s FMV rate bases in lieu of the purchase prices paid for each transaction (OCA St. 1 at 11-12); and (3) used a simple average of the purchase price to RCNLD ratios rather than the weighted average used by AUS.⁴⁸ OCA St. 1 at 11, 13.

Mr. Garrett’s proposed adjustments reduced the AUS Market Approach by \$15,272,234, from \$56,178,539 to \$40,906,304, as shown in the table below (OCA St. 1 at 14; OCA M.B. At 38):⁴⁹

Appraisal Approach	AUS Consultants Appraisal			OCA Adjustment	OCA Garrett Adjustment to AUS Appraisal		
	Value Indicator	Weight	Wtd Value Indicator		Value Indicator	Weight	Wtd Value Indicator
Market	56,178,539	10%	5,617,854	(15,232,008)	40,946,531	10%	4,094,653

Aqua St. 5-R at 1.

⁴⁷ Mr. Garrett explained that although the Township owns one wastewater treatment plant, which treats wastewater to a small community system, “wastewater treatment is mainly provided by another entity such that the East Whiteland system is properly characterized as a collection-only system for purposes of analysis.” OCA St. 1 at 9, n.11. Thus, the resulting comparable sales transactions used by Mr. Garrett are: (1) SUEZ/Mahoning Water Distribution System, (2) SUEZ/Mahoning Wastewater Collection; (3) Aqua/East Bradford Wastewater Collection and Paid For Treatment Capacity; (4) PAWC/Sadsbury Wastewater Collection; (5) PAWC Steelton Water Distribution and Treatment; (6) Aqua/Cheltenham Wastewater Collection; (7) PAWC/Valley Water Treatment and Distribution System; (8) PAWC/Valley Wastewater Collection System; (9) PAWC/Upper Pottsgrove Wastewater Collection; (10) PWAC/Royersford Wastewater Collection and Treatment; (11) PWAC/Lower Makefield Wastewater Collection and Purchased Treatment Capacity; and (12) Aqua/East Norriton Wastewater Collection. *See* OCA Exh. DJG-5 attached to OCA St. 1.

⁴⁸ OCA St. 1 at 11-13.

⁴⁹ *See* OCA St. 1 at 13. It is noted that the difference between the OCA’s indicated value of \$40,906,304 here compared to the \$40,946,531 in the table is due to rounding the FMV/RCNLD ratios to two decimal places and four decimal places, respectively.

In response to Mr. Garrett's adjustments, Mr. Weinert further noted that, in addition to the three adjustments, *supra*, Mr. Garrett used different values of CORNLD values for the PWAC/McKeesport and Aqua/Limerick transactions, and did not include the DELCORA Wastewater Collection and Treatment System \$276,500,000 transaction in his analysis. Aqua St. 5-R at 2-3.

With regard to Mr. Garrett's first adjustment, above, to use only wastewater collections systems as opposed to all the Section 1329 transactions reviewed by the Commission that were included in AUS' analysis, Mr. Weinert noted that although Mr. Garrett eliminated wastewater transactions that included wastewater treatment facilities for comparability purposes, his analysis also included transactions that involved three water distribution transactions. Mr. Weinert asserted that if wastewater treatment facilities should be eliminated on comparability issues, then water distribution properties should be eliminated as well. Aqua St. 5-R at 5-6. Mr. Weinert provided testimony on the effects his adjustment would have on Mr. Garrett's proposal which we shall discuss in more detail in Aqua's Exceptions and our disposition below.

With regard to Mr. Garrett's second adjustment that substituted the Commission-determined rate bases in place of the agreed-upon purchase prices, Mr. Weinert asserted, *inter alia*, that the use of the Commission-determined rate base as opposed to the agreed-upon purchase price invalidates the analysis as a market-comparable approach because the conditions under which the resultant rate bases were derived in the various Section 1329 applications do not represent market transactions in accordance with the definition of definition of "Market Value" as defined in *The Appraisal of Real Estate* (14th Edition at 58). Aqua St. 5-R at 5.

With regard to Mr. Garrett's third adjustment, in which he relied upon using the purchase price simple average as opposed to the transaction size weighted average, Mr. Weinert asserted that the use of a transaction-size weighted average is more

accurate because it produces a more reliable market-comparable indicator based on the standard deviation which is nearly twice a closer fit to the data than the simple mean. Aqua St. 5-R at 6-8.

In his surrebuttal testimony, Mr. Garrett was not persuaded to change his adjustments based on Mr. Weinert's assertions. OCA St. 1SR at 6-8.

(2) Recommended Decision

The ALJ did not address the AUS Market Approach in her Recommended Decision.

(3) Aqua Exception No. 3, Replies, and Dispositions

(a) Comparable Market Sales Method – Use of FMV Ratemaking Rate Base Value Instead of the Purchase Price Paid

In its Exceptions, Aqua maintains its position that none of the adjustments proposed by Mr. Garrett are appropriate and none should be adopted. Aqua first argues that Mr. Garrett wrongfully substituted Commission-determined rate base for purchase price in his adjustments to the AUS Market Approach. Aqua Exc. at 31-32. In support of this Exception, Aqua refers to Mr. Weinert's rebuttal testimony where he asserted that the use of Commission-determined rate bases under Section 1329 applications, as opposed to the agreed-upon purchase prices, is not an appraisal market comparable approach as it does not represent a market transaction because the Commission's determination of ratemaking rate base under Section 1329 applications does not meet the definition of

Market Value in terms of an agreed-upon price between a buyer and seller neither being under duress. *Id.* (citing Aqua St. 5-R at 5; Aqua M.B. at 37).

The OCA replies that Aqua's argument, that the use of Commission-determined rate base is not an appraisal market-comparable approach because it does not represent a market transaction, is flawed because Section 1329 transactions are not comparable to purely market-driven transactions. OCA R. Exc. at 20 (citing OCA St. 1SR at 7; OCA M.B. at 37). The OCA contends that the incentives that are present in competitive marketplace transactions between buyers and sellers are not present in Section 1329 transactions, which is, in part, why the Section 1329 regulations exist at all. *Id.*; 66 Pa. C.S. § 1329. The OCA cites to Mr. Garrett's surrebuttal testimony in which he explained that when the Commission establishes a ratemaking rate base that is lower than the purchase price of any given transaction, the Commission is finding that the purchase price does not comport with the fair market value for that transaction. In this regard, Mr. Garrett stated:

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 [and Mr. Weinert] 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.

OCA R. Exc. at 20 (citing OCA St. 1SR at 3). In view of the above, the OCA submits that once the Commission establishes the appropriate FMV, both parties have the freedom not to go forward with the transaction, or to agree to go forward with a higher agreed-upon purchase price. The OCA notes that the Commission-determined rate base only establishes the amount of the transaction that is fair to recover from ratepayers and

that the Parties do not agree to Commission-determined FMV under “duress.” OCA R. Exc. at 20-21 (citing Aqua Exc. at 31). The OCA further notes that since both buyers and sellers in past proceedings mostly agree to move forward with the Commission-determined rate base in a transaction, the Commission-determined rate base is the best indication in determining the FMV under the Market Approach. OCA R. Exc. at 20-21.

Inasmuch as Aqua’s Exceptions here are materially the same as those it made against the OCA’s adjustments to Gannett Fleming’s Selected Transactions Method analysis under the Market Approach, *supra*, where the OCA substituted the Commission FMV rate bases in lieu of purchase prices paid, we shall similarly grant Aqua’s Exception in this matter and reject the OCA’s adjustments to use the Commission’s FMV rate bases in lieu of the purchase prices.

(b) Comparable Market Sales Method – Use of Simple Average of Price to RCNLD Ratio Instead of Weighted Price to RCNLD Ratio

In its Exceptions, Aqua explains that the market comparable statistic being measured in the market analysis is the ratio of the purchase price to the RCNLD or CORLD, not the size of the transaction. Aqua Exc. at 32. For this reason, Aqua asserts that the use of a transaction-size weighted average produces a weighted average with statistics far superior to a simple mean as demonstrated by the weighted mean and its standard deviation shown in the Table presented on page 7 of Mr. Weinert’s rebuttal testimony. Aqua Exc. at 32 (citing Aqua St. 5-R at 6-7). Therefore, Aqua is of the opinion that its purchase price weighted average should be approved because it is more accurate than Mr. Garrett’s simple average that has a less reliable market-comparable indicator. Aqua Exc. at 32 (citing Aqua St. 4 at 8).

The OCA replies that although Aqua argues that Mr. Garrett’s use of a simple average is a “less reliable market comparable indicator” than Mr. Weinert’s use of a weighted average, Mr. Weinert’s weightings allow transactions with higher purchase prices to have more influence than lower-priced transactions. OCA R. Exc. at 21 (citing OCA St. 1 at 12; OCA M.B. at 38). For Mr. Weinert’s weightings to be acceptable, the OCA submits he would have to demonstrate in this case that it is more appropriate for larger transactions to influence his market approach under Section 1329 than smaller transactions. OCA R. Exc. at 21 (citing *Cheltenham* at 69). The OCA asserts that Mr. Weinert failed to put forth any evidence in this proceeding to support his use of the weighted average other than his own unexplained assertion that it is more “reliable.” OCA R. Exc. at 21 (citing Aqua St. 5-R at 7-8). On the other hand, the OCA submits that it has demonstrated that using the weighted average causes large transactions, such as the \$159 million McKeesport transaction, to have the greatest statistical weighting in this proceeding, when the McKeesport transaction cannot reasonably be compared to the EWT assets. OCA R. Exc. at 21 (citing OCA St. 1 at 7-8; OCA M.B. at 38).

We shall deny Aqua’s Exception on this matter. In prior cases, we ruled similarly because AUS had not demonstrated that it is appropriate for larger transactions to influence the Market Approach under Section 1329 more than smaller transactions. *See, e.g., Cheltenham* at 67, 69. However, it is noted, as will be addressed in more detail in our disposition of Aqua’s next Exception below pertaining to Mr. Garrett’s selection of market comparables, that based on our adjustment to exclude all integrated and water distribution transactions from Mr. Garrett’s analysis, the outlier transactions consequently will be eliminated from Mr. Garrett’s analysis. This eliminates Mr. Garrett’s concerns about Mr. Weinert’s use of a weighted average giving a greater statistical weighting to the outlier transactions. Nevertheless, in this proceeding, we shall continue to use the simple average, proposed by the OCA, in lieu of the weighted average proposed by the Company’s witness, Mr. Weinert.

(c) Comparable Market Sale Method – Selection of Market Comparables

In its Exception No. 3, Aqua maintains its objection to Mr. Garrett's exclusion of those Section 1329 wastewater system transactions which included treatment facilities from his analysis. Aqua contends that if wastewater property transactions that include treatment facilities should be eliminated because of a lack of comparability, then Mr. Garrett also should have excluded the three transactions that included water distribution properties in his Market Approach analysis.⁵⁰ Aqua Exc. at 31-32. According to Aqua, if the three water distributions properties were eliminated, Mr. Garrett's Market Approach would increase from \$40,946,531 (\$40,906,305 if FMV/RCNLD ratios are rounded to two decimal places) to \$42,616,932. Aqua Exc. at 32 (citing Aqua St. 5-R at 5-6).

Aqua further contends that Mr. Garrett's adjustment that removed treatment facilities from the wastewater transactions results in an underestimation of the value of the Township's System because Mr. Garrett failed to include the value of the purchased treatment capacity at the Valley Forge Treatment Plant. According to Aqua, had Mr. Garrett included Section 1329 transactions of wastewater properties with collection and treatment assets to account for the value of purchased treatment capacity while excluding collection only systems, his Market Approach conclusion would have been \$44,901,310 instead of \$40,946,531. Aqua Exc. at 32 (citing Aqua St. No. 5-R at 6).

In its Reply Exception to Aqua's Exception No. 3, the OCA incorporates the same arguments it made on this issue in the Gannett Fleming Market Approach where Mr. Garrett excluded integrated systems from the selected transactions, *supra*. The OCA

⁵⁰ The three transactions that include water distribution systems are: (1) SUEZ/Mahoning Water Distribution System; (2) PAWC/Steelton Water Distribution and Treatment, and (3) PAWC/Valley Water Treatment and Distribution System.

asserts that Mr. Garrett's exclusion of integrated systems produces a far more reasonable result under the AUS Market Approach as well. OCA R. Exc. at 21.

After reviewing the arguments raised by Aqua and the OCA on this matter, we agree with the OCA that, for comparability purposes, integrated systems should be removed from the list of transactions used by AUS in its Market Approach. However, we also agree with Aqua, that if integrated systems are excluded, it is also proper to exclude those transactions involving water distribution systems, because, as noted, *supra*, although the Township owns one wastewater treatment plant that treats water for another small community system, there is general agreement among the parties that because the Township's wastewater treatment is provided primarily by another entity, the EWT System is properly characterized as a collection-only system for analysis purposes. *See* Aqua St. 1 at 10; OCA St. 1 at 9, n.11. The elimination of those transactions with integrated systems and water distribution systems will leave nine comparable market transactions that are solely wastewater collection systems and are most similar in operations to the EWT System.⁵¹

As noted, Mr. Weinert testified that his adjustment to the OCA's proposal, which removes both integrated and water distribution systems, while maintaining the OCA's proposal to use the Commission-determined fair-market rate base transactions in the price to RCNLD ratios, would increase the value under Mr. Garrett's Market

⁵¹ The resulting eight wastewater collection systems are: (1) SUEZ/Mahoning Wastewater Collection; (2) Aqua/East Bradford Wastewater Collection and Paid For Treatment Capacity; (3) PAWC/Sadsbury Wastewater Collection; (4) Aqua/Cheltenham Wastewater Collection; (5) PAWC/Valley Wastewater Collection System; (6) PAWC/Upper Pottsgrove Wastewater Collection; (7) PWAC/Lower Makefield Wastewater Collection and Purchased Treatment Capacity; (8) Aqua/Lower Makefield; and (9) Aqua/East Norriton Wastewater Collection.

Approach from \$40,946,531 (\$40,906,305 if FMV/RCNLD ratios are rounded to two decimal places) to \$42,616,932.⁵² Aqua St. 5-R at 5-7.

Since Mr. Weinert's adjustments were made using calculations based on Mr. Garrett's original inclusion of FMV transactions in the price to RCNLD ratio (see table on page 7 of Aqua St. 5-R), we have modified Mr. Weinert's adjustment by replacing the FMV/RCNLD ratios with Purchase Price/RCNLD ratios in the calculations. Our final adjustment to the OCA's proposal excludes both integrated systems and water distribution systems from AUS' original transactions and uses a Purchase Price/RCNLD ratio. Accordingly, our adjustment will reduce AUS' Market Approach value by \$12,615,981, from \$56,178,539 to \$43,562,558, or an approximate 22.5% reduction. A summary of our adjustments in addition to those made by Mr. Weinert to Mr. Garrett's proposal is shown in the table below.⁵³

⁵² To be consistent with Mr. Weinert's use of two decimal places to demonstrate his adjustments in Aqua St. 5-R, this amount would be \$42,618,113.

⁵³ Our adjustment to AUS' Market Approach value has a corresponding adjustment to reflect our adjustment to AUS' RCNLD from approximately \$59.8 million to \$53.1 million reflecting the adjusted services lives of Account Nos. 360.21, 361.21, and 361.23 as described in the AUS Cost Approach discussion, *supra*.

Property Acquired	Type of System	FMV (OCA-Proposed)	Purchase Price (AUS-Proposed)	RCNLD	FMV/RCNLD	PP/RCNLD	OCA-Proposed	AUS-Adjusted	PUC-Adjusted
							(Garrett) FMV/RCNLD without Integrated Systems	(Weinert) FMV/RCNLD without Integrated & Dist Systems	PP/RCNLD without Integrated & Dist Systems
Aqua/New Garden Twp.	Int	\$29,500,000	\$ 29,500,000	\$ 30,615,410	0.9636	0.9636			
PAWC/City of McKeesport	Int	\$158,000,000	\$ 159,000,000	\$160,301,491	0.9856	0.9919			
Aqua/Limerick Township	Int	\$64,373,378	\$ 64,373,378	\$ 86,086,756	0.7478	0.7478			
SUEZ/Mahoning Water	Wtr Dist	\$4,734,800	\$ 4,734,800	\$ 8,899,336	0.5320	0.5320	0.53		
SUEZ/Mahoning Wastewater	C/D	\$4,765,200	\$ 4,765,200	\$ 7,991,234	0.5963	0.5963	0.60	0.60	0.60
Aqua/East Bradford Township	C/D	\$5,000,000	\$ 5,000,000	\$ 9,236,581	0.5413	0.5413	0.54	0.54	0.54
PAWC/Sadsbury	C/D	\$8,300,000	\$ 8,600,000	\$ 8,517,587	0.9745	1.0097	0.97	0.97	1.01
PAWC/Exeter	Int	\$92,000,000	\$ 93,500,000	\$ 99,589,819	0.9238	0.9389			
PAWC/Steelton	Wtr Dist	\$20,500,000	\$ 21,750,000	\$ 23,921,473	0.8570	0.9092	0.86		
Aqua/Cheltenham	C/D	\$44,558,259	\$ 50,250,000	\$ 49,940,486	0.8922	1.0062	0.89	0.89	1.01
PAWC/Kane	Int	\$17,560,000	\$ 17,560,000	\$ 29,015,055	0.6052	0.6052			
PAWC/Valley Water	Wtr Dist	\$7,325,000	\$ 7,325,000	\$ 11,664,026	0.6280	0.6280	0.63		
PAWC/Valley Wastewater	C/D	\$13,950,000	\$ 13,950,000	\$ 19,252,333	0.7246	0.7246	0.72	0.72	0.72
PAWC/Upper Pottsgrove	C/D	\$13,750,000	\$ 13,750,000	\$ 18,460,028	0.7449	0.7449	0.74	0.74	0.74
PAWC/Royersford	C/D	\$13,000,000	\$ 13,000,000	\$ 13,376,109	0.9719	0.9719	0.97	0.97	0.97
Aqua/Lower Makefield	C/D	\$53,000,000	\$ 53,000,000	\$ 51,414,555	1.0308	1.0308	1.03	1.03	1.03
Aqua/East Norritown	C/D	\$20,750,000	\$ 21,000,000	\$ 27,461,356	0.7556	0.7647	0.76	0.76	0.76
Total		\$571,066,637	\$581,058,378	\$655,743,635	0.8861				
Simple Average					0.7927	0.8063	0.7700	0.8022	0.8200
Standard Deviation (Simple Average)					0.1699	0.1809	0.1739	0.1725	0.1889
Median (Simple Average)					0.7556	0.7647	0.7500	0.7600	0.7600
East Whiteland Twp. Wastewater System RCNLD							\$53,125,071	\$53,125,071	\$53,125,071
East Whiteland Twp. Wastewater System Market Price							\$40,906,305	\$42,618,113	\$43,562,558

Commission Adjustments to the OCA's Market Approach Analysis and AUS Adjustments in Table on page 7 of Aqua St. 5-R.

5. Conclusion – Section 1329 Fair Market Valuation

a. Positions of the Parties

Aqua submitted that the ratemaking rate base of the EWT System, determined pursuant to Section 1329(c)(2), is \$54,930,000, the lesser of the negotiated purchase price of \$54,930,000 and the average of the UVE appraisals of \$56,724,729. Aqua averred that the OCA's criticisms of the appraisals should be rejected and given no weight. Aqua M.B. at 43.

The OCA provided that the OCA's witness, Mr. Garrett, calculated that with the appropriate adjustments, discussed above, the adjusted Gannett Fleming appraisal result would be \$45,748,213 and the adjusted AUS appraisal result would be \$47,200,091. The average of these two appraisals results is approximately \$46,500,000, which is the amount that Mr. Garrett recommends be used by the Commission for establishing ratemaking rate base under Section 1329 rather than the \$54,930,000 proposed by Aqua. OCA M.B. at 44.

b. Recommended Decision

As explained *supra*, the ALJ did not address the appropriate ratemaking rate base, should the transaction be approved, in her Recommended Decision.

c. Aqua Exception No. 3⁵⁴ and Replies

The ALJ did not make a determination regarding the appropriate ratemaking rate base. Nevertheless, as part of its Exception No. 3 Aqua maintains that the correct ratemaking rate base of the EWT System, should the transaction be approved, is \$54,930,000, being the lesser of the negotiated purchase price and the average of the UVE appraisals. Aqua Exc. at 35.

In reply, the OCA similarly maintains its contention that Aqua's criticisms of Mr. Garrett's adjustments are without merit, and asserts that, if the transaction is approved, the Commission should establish a ratemaking rate base of \$46.5 million for the System. OCA R. Exc. at 25.

⁵⁴ It is noted that EWT stated in its Exceptions that it adopts and incorporates by reference all of Aqua's Exceptions related to the appropriate ratemaking rate base. EWT Exc. at 8.

d. Disposition

As discussed *supra*, we disagree with the OCA's proposed adjustments to Gannett Fleming's Cost, Income, and Market Approach results. We also disagree with the OCA's proposed adjustments to AUS' Income Approach and its proposal to use Commission-determined rate base in the AUS Market Approach. However, we agree with the OCA that its proposed adjustment to the service lives of Account Nos. 360.21, 361.21, and 361.23 under AUS' Cost Approach are reasonable and appropriate and should be reflected through a corresponding adjustment to AUS' Market Approach result. We also agree with the OCA's use of the simple average of selected transactions in AUS' Market Approach. Lastly, regarding the OCA's recommended adjustments to AUS' Market Approach result, we agree with the OCA that for comparability purposes, integrated systems should be removed from the list of transactions used by AUS in its Market Approach. However, we also agree with Aqua, that if integrated systems are excluded, it is also proper to exclude those transactions involving water distribution systems.

As such, the weighted value of Gannett Fleming's appraisal remains unchanged at \$55,668,460 from that proposed by Gannett Fleming. The AUS appraisal is modified by reducing the Cost Approach by \$6,722,100 from \$59,847,171 to \$53,125,071 and the Market Approach by \$12,615,981 from \$56,178,539 to \$43,562,558. The recalculated AUS appraisal result is \$53,158,810. The recalculated average of the Gannett Fleming appraisal result and the adjusted AUS appraisal result is \$54,413,635, as follows:

Gannett Fleming Appraisal (Unchanged)			
Conclusion	→		\$55,668,460
Summary of Results Prepared by AUS (As Modified)			
	<u>Indicated Value</u>	<u>Weight</u>	<u>Weighted Value</u>
Cost Approach	\$53,125,071	50%	\$26,562,536
Income Approach	\$55,600,045	40%	\$22,240,018
Market Approach	\$43,562,558	10%	\$4,356,256
		100%	\$53,158,810
Conclusion	→		\$53,158,810
	Average		\$54,413,635

The FMV is the lesser of the purchase price and the average of the appraisal results, or \$54,413,635.

C. Stipulation of Active Parties

Aqua, I&E, the OCA, the OSBA, Mr. Gage, and the Township entered into a Stipulation regarding certain issues if the Commission approves Aqua’s acquisition of the Township’s wastewater collection system and grants Aqua the right to begin to offer, render, furnish or supply wastewater service in the areas served by the Township. The terms of the Stipulation are set forth below in full as they appear in the Stipulation:

Tariff:

Aqua included proposed schedule of rates tariff pages with its Application. No party presented testimony in opposition to the proposed tariff pages.

Stipulated Resolution:

The pro forma tariff submitted with the Application, including all rates, rules and regulations regarding conditions of Aqua's wastewater service, shall be permitted to become effective immediately upon closing of the transaction.

Easements and Other Property Rights

I&E recommended that the Commission require Aqua and EWT to (1) Identify all missing easements, including rights of way; (2) Take any and all actions to obtain the missing easements and rights of way so that they may be conveyed to Aqua at closing; and (3) EWT should bear all costs and expenses for obtaining the missing easements and rights of way. I&E also recommended that for situations beyond EWT's control where it is unable to transfer certain missing easements or other property rights at closing, Aqua and EWT may proceed to closing provided that an escrow account is established of an appropriate portion of the purchase price to ensure the Township obtains any remaining missing easements or other property rights post-closing and delivers them to Aqua.

Stipulated Resolution

Aqua and the Township will work to ensure the transfer of all real property rights including easements and missing easements as defined in the Asset Purchase Agreement ("APA") by Closing. However, Aqua shall be permitted in its discretion to close without the transfer of all of the Real Property Rights, provided that an escrow is established from the Purchase Price to be used to obtain any post-Closing transfers of the Real Property Rights. Aqua will provide an update to I&E, OCA, and OSBA

approximately 30 days in advance of the anticipated Closing Date and a final update before Closing regarding the status of the transfer of real property rights including easements related to the system.

Legal Fees

Aqua anticipates that transaction and closing costs will be approximately \$308,300 including the Company's UVE fees and proposed that the exact closing costs will be determined at closing.

Stipulated Resolution

In its next base rate case, Aqua shall separately identify any legal fees included in its transaction and closing costs pursuant to the APA between Aqua and EWT and specify amounts expended by Aqua on behalf of the Township. I&E, OCA and OSBA reserve the right to challenge the reasonableness, prudence, and basis for such fees.

Cost of Service Study ("COSS")

I&E and OCA recommended that, in its next base rate case, Aqua provide a separate cost of service study for the EWT system.

Stipulated Resolution

In its first base rate case filing that includes the EWT system assets, Aqua will:

- a. Include a COSS that removes all costs and revenues associated with the operation of the EWT system; and
- b. Include a separate COSS for the EWT system.

These studies are in addition to any form of COSS directed by the Commission's final order in the Company's base rate case filing at Docket Nos. R-2021-3027385 and R-2021-3027386.

EWT Rates, Rate Freeze and Rate Stabilization

I&E, OCA and OSBA challenged the three-year rate freeze in Section 7.03 of the APA. I&E and OCA also contended that the rate freeze is a Section 1329 rate stabilization plan.

Stipulated Resolution

- a. The current average EWT residential rate is \$33.33 per month based on one equivalent dwelling unit (“EDU”). As set forth in the notice sent to EWT customers in this proceeding (Application Exhibit I2), Aqua provided a non-binding, estimated incremental rate effect of the proposed rate base addition on EWT wastewater customers of 132.93%.
- b. The Stipulating Parties acknowledge that the Commission retains ultimate authority to set rates including, but not limited to, the authority to allocate revenues to the EWT customers that are in excess of the restrictions contained in Section 7.03 of the Asset Purchase Agreement.
- c. Aqua and EWT agree that, at the time of Aqua’s first base rate case that includes the EWT system, Aqua may propose an effective date for new rates for EWT wastewater customers that is different from the effective date of new rates for other customers, consistent with the terms of Section 7.03 of the Asset Purchase Agreement. All parties reserve their rights to address Aqua’s proposal.
- d. If Aqua proposes to freeze EWT rates beyond the effective date of new rates in Aqua’s first base rate case that includes the EWT system assets, (1) Aqua shall propose a separate rate for EWT customers in its tariff that reflects the continuation of EWT’s existing rates through the end of the rate freeze period, and (2) Aqua’s compliance proof of revenue will be calculated using the new rate otherwise applicable to EWT

customers at the conclusion of Aqua's base rate case, not EWT's frozen rate, such that existing ratepayers are not required to fund the revenue deficiency related to the rate freeze. Once the contractual rate freeze term expires, the customers acquired through the acquisition of the EWT system shall immediately become subject to the new rate applicable to EWT customers, as determined in Aqua's first base rate case that includes the EWT system assets.

- e. In the first base rate proceeding filed by Aqua that includes EWT's wastewater system assets, Aqua shall propose to move the EWT system to its full cost of service, based on a separate cost of service study for EWT's system; provided, however, that Aqua will not be obligated to propose EWT wastewater rates in excess of Aqua's proposed Rate Zone 1 system-average rates. The Stipulating Parties acknowledge, however, that Aqua may agree to rates other than those proposed for EWT customers in the context of a settlement of the base rate case. OCA, I&E, OSBA and EWT reserve their rights to fully address this proposal, and to make other rate proposals in the base rate case. In the next rate case, Aqua agrees to provide written notice to EWT customers of the rate filing and the level of increase, if any, resulting from this provision.
- f. Aqua will send a welcome letter to EWT Wastewater customers within 30 days following Closing which will include information regarding the conversion to monthly billing for their sewer service.

Long Term Infrastructure Improvement Plan ("LTIIIP")

Aqua and OCA agreed that Aqua must file and receive approval of an amended LTIIIP that includes the EWT system prior to charging the Distribution System

Improvement Charge (“DSIC”) to EWT customers. OCA further recommended that any EWT improvement projects reflected in the amended LTIP should be in addition to, and not reprioritize existing capital projects.

Stipulated Resolution:

- a. If Aqua proposes to modify its LTIP to include the EWT wastewater system, the projects added for EWT will be in addition to those that Aqua plans for its existing systems.
- b. In LTIPs or Annual Asset Optimization Plans that include the EWT wastewater system, Aqua will not reprioritize other existing capital improvements that the Company already committed to undertake. This section does not limit Aqua’s current practice and ability to allocate projects as needed for its capital program.
- c. Upon approval of the Commission of a modification to Aqua’s LTIP that includes the EWT wastewater system, Aqua shall be permitted to apply the DSIC to the EWT wastewater system prior to the first base rate case in which the EWT assets are incorporated into rate base.
- d. If Aqua is not already applying the DSIC to the EWT wastewater system, it will do so when rates for those customers are implemented in the first base rate proceeding that includes the EWT system assets.

Allowance for Funds Used During Construction (“AFUDC”), Deferral of Depreciation and Transaction Costs

OCA recommended that, if approved, the acquisition should be conditioned on a requirement that claims for AFUDC and deferred depreciation be made no later than Aqua’s next base rate case.

Stipulated Resolution:

- a. Any claims for AFUDC and deferred depreciation related to post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes, will be addressed in Aqua’s first base rate case which includes EWT wastewater system assets.

- b. Regarding future claims for AFUDC, deferral of depreciation, and transaction costs related to this acquisition, the Stipulating Parties reserve the right to litigate their positions fully in future rate cases when these issues are ripe for review. The parties’ assent to this agreement should not be construed to operate as its preapproval of Aqua’s requests. The pro forma tariff submitted with the Application, including all rates, rules and regulations regarding conditions of Aqua’s wastewater service, shall be permitted to become effective immediately upon closing of the transaction.

Section 507 and 2102 Approvals

Aqua asked the Commission to approve, if necessary, its acquisition agreement with EWT and the assignment of 22 contracts with municipalities under Section 507 of the Code and also to approve, under Section 2101 of the Code, the assignment of EWT’s rights and responsibilities under an Agreement between Aqua Resources, an affiliate of Aqua, and various municipalities for conveyance of wastewater through the Valley Creek Trunk Line.

Stipulated Resolution

The Stipulating Parties agree that the Commission shall issue any necessary approvals or certificates for

the transaction pursuant to 66 Pa.C.S. Section 507 and Section 2102.⁵⁵

See Stipulation at 2-7.

1. Positions of the Parties

As discussed *supra*, Aqua, I&E, the OCA, the OSBA, Mr. Gage and the Township stipulated to the terms of the Stipulation if the Commission approves Aqua's acquisition of the Township's System and grants Aqua the right to begin to offer, render, furnish or supply wastewater services in the areas served by the Township, and requested that the Commission approve the Stipulation. Stipulation at 2, 7.

2. Recommended Decision

Inasmuch as the ALJ recommended that Aqua's Application be denied because Aqua failed to establish that the Township's System under Aqua's ownership would affirmatively promote the service, accommodation, convenience, or safety of the public, and because the evidence did not establish that any benefit to be realized from the proposed transaction would outweigh the harms to current Aqua water and wastewater customers or existing Township wastewater customers, the ALJ did not address the Stipulation in the Recommended Decision. R.D. at 59, 64.

3. Exceptions

In its Exception No. 4, Aqua argues that the ALJ failed to substantially address the Stipulation, and that the Stipulation is in the public interest and should be accepted and approved. Aqua avers that the Parties negotiated a resolution of the

⁵⁵ The OCA did not join in this paragraph but does not oppose it.

conditions recommended by I&E, the OCA, and the OSBA, with the exception of the reduced ratemaking rate base recommended by the OCA, and the proposed resolution is supported by the evidence of record. Aqua contends that while the Stipulation does not resolve all contested issues in the proceeding, it does remove several issues from litigation, if accepted and approved. Aqua Exc. at 36.

In I&E's Exception, I&E contends that if the proposed transaction is approved, the Stipulation must be adopted as a condition of the acquisition. I&E avers that its recommended conditions to be implemented if the transaction is approved were contained in the Stipulation, and that the Parties carefully crafted the conditions to eliminate certain issues with the acquisition and achieve a desired result if the Commission approves the transaction. I&E Exc. at 2-4.

No Replies to Exceptions on this issue were filed by any of the Parties.

4. Disposition

The Stipulation resolves several issues raised in this proceeding with respect to various conditions that the Parties recommended be imposed upon the transaction if it is approved, which are described above and discussed in greater detail *infra* in Section V.D. Recommended Conditions. Upon review, we find that the Stipulation is supported by substantial evidence and is in the public interest and should be approved. The Stipulation, and the conditions imposed on the transaction as a result of it, will benefit and protect the public, the Township, the Township's customers, and Aqua's existing customers.

Specifically, the Parties agreed that the *pro forma* tariff that Aqua submitted with its Application shall become effective upon Closing of the transaction. The *pro forma* tariff will accurately include all rates, rules, and regulations regarding the

conditions of Aqua's wastewater service, and this full and accurate disclosure of rates in the public interest.

Regarding missing easements, under the Stipulation Aqua has agreed to work with the Township to ensure the transfer of all real property rights by Closing, and to establish an escrow from the purchase price to ensure the post-Closing transfer of real property rights. This provision helps to ensure that the purchase price for the transaction includes that all property rights necessary for Aqua to operate in the Township are transferred, and the establishment of the escrow account ensures that the Township will be financially responsible for any property rights not transferred at Closing. In addition, the establishment of the escrow account provides an additional layer of protection if Aqua and the Township would mutually decide to waive the provisions of the APA that obligate the Township to deliver good and marketable title to all real property necessary for the operation of the acquired System.⁵⁶ See I&E M.B. at 15; I&E R.B. at 7. The public interest would be harmed if Aqua paid a purchase price that assumed all rights necessary to operate in the Township would be transferred at the Township's cost and such action did not occur. These provisions are designed to protect Aqua customers, so that they are not burdened with the associated cost of obtaining and conveying missing easements and other property rights. Therefore, we find these provisions to be in the public interest.

⁵⁶ Section 15.07 of the APA, which governs amendments and waivers, provides, in relevant part, the following:

The Parties may amend this Agreement only by the Parties' written agreement that identifies itself as an amendment to this Agreement. Any waiver of, or consent to depart from, the requirements of any provision of this Agreement will be effective only if it is in writing and signed by the Party giving it, and only in the specific instance and for the specific purpose for which it has been given.

Application Exh. B, Section 15.07.

With respect to legal fees, under the Stipulation Aqua has agreed, in its next base rate case, to separately identify legal fees included in the transaction and closing costs pursuant to the APA between Aqua and the Township and specify amounts expended by Aqua on behalf of the Township. Further, I&E, the OCA and the OSBA reserve the right to challenge the reasonableness and basis for these legal fees. This provision will ensure that Aqua will only be permitted to recover prudently incurred costs from customers and will protect Aqua's customers from bearing the burden of the Township's legal fees, which is in the public interest.

Next, pursuant to the Stipulation, in its first base rate case following Closing in which the Township's assets are included in rate base, Aqua will submit a wastewater cost of service study that removes all costs and revenues associated with the Township System and a separate cost of service study for the Township System. These cost of service studies will provide a mechanism to establish the existence of any improper subsidization and determine revenue requirement and the appropriate level of rates for the Township's customers that differ from rates established for other wastewater customers. *See* I&E R.B. at 5; OCA R.B. at 30. We find that this is in the public interest.⁵⁷

⁵⁷ The Stipulation contained a sentence in the Stipulated Resolution of the cost of service study issue that stated: "These studies are in addition to any form of COSS directed by the Commission's final order in the Company's base rate case filing at Docket Nos. R-2021-3027385 and R-2021-3027386." The Commission, in the final Opinion and Order of Aqua's base rate case proceeding at those dockets, rejected the arguments of I&E and the OCA that Aqua be required to prepare ongoing cost of service studies in future base rate cases for the wastewater systems acquired under Section 1329 proceedings. Rather, the Commission found that the decision to require any cost of service study should be considered in the context of each Section 1329 proceeding. *Pa. PUC et al. v. Aqua Pennsylvania, Inc.*, R-2021-3027385, *et al.* and *Pa. PUC et al. v. Aqua Pennsylvania Wastewater, Inc.*, R-2021-3027386, *et al.* (Order entered May 16, 2022) at 185-186.

Regarding Township rates, under the Stipulation, if Aqua proposes to freeze the Township's rates beyond the effective date of new rates in Aqua's first base rate case that includes the Township's System assets, provisions are in place to ensure that existing customers are not required to fund any revenue deficiency related to the rate freeze. Following the expiration of the rate freeze, the customers acquired through the acquisition of the Township's System shall become subject to the new rate applicable to Township customers resulting from Aqua's first base rate case that includes the Township System assets. In addition, Aqua will provide written notice to Township customers of the rate filing and any level of increase. Aqua will also send a welcome letter to the Township's wastewater customers within thirty days after Closing of the transaction with information on the conversion to monthly billing for their sewer service. These provisions protect the Township's customers in the event Aqua would file for a base rate case that would take effect prior to the expiration of the rate freeze period. In addition, these provisions protect Aqua's existing and future customers by preserving the Parties' ability to address rates in the future. *See* I&E R.B. at 6; OCA R.B. at 31-32; OSBA R.B. at 14. Therefore, we find these provisions to be in the public interest.

Turning to the provisions in the Stipulation regarding LTIPs, any projects added to Aqua's LTIP that includes the Township's System will be in addition to the projects that Aqua plans for its existing systems, and Aqua will not reprioritize other capital projects that it already committed to undertake. Furthermore, Aqua may apply the DSIC to the Township System prior to the first base rate case in which the EWT assets are incorporated into rate base. These terms are in the public interest because Township customers will be able to contribute toward DSIC-eligible projects, and previously planned capital projects for existing Aqua wastewater customers will not be given less priority as a result of the transaction. *See* OCA R.B. at 32-33.

With respect to AFUDC provisions in the Stipulation, any claims for AFUDC and deferred depreciation related to post-acquisition improvements not

recovered through the DSIC will be addressed in Aqua's first base rate case which includes the Township's System assets, and the Parties' rights to litigate claims for AFUDC, deferral of depreciation, and transaction costs in future rate cases are reserved. Preserving the ability to review and litigate these items in the future protects the public interest by fostering the development of a complete record when additional information is available for ratemaking purposes. *See* OCA R.B. at 33.

Finally, under the Stipulation the necessary approvals for the transaction pursuant to 66 Pa. C.S. Sections 507 and 2102 shall be issued. There was no opposition by the Parties to the issuance of these approvals; therefore, this provision of the Stipulation is in the public interest.

As set forth above, we conclude that that the Stipulation, and the terms contained therein, are reasonable and in the public interest and, therefore, should be approved without modification. The Stipulation includes various important protections for Aqua's existing customers and the Township customers who will become Aqua customers as a result of this transaction. The Stipulation reflects a consensus on the issues regarding recommended conditions if the transaction is approved, and it reduced the time, effort and expense of fully litigating these issues in this proceeding. For these reasons, we shall approve the Stipulation. Accordingly, Aqua's Exception No. 4 and I&E's Exception will be granted.

D. Recommended Conditions

As discussed above, I&E, the OCA, and the OSBA recommended that the Commission impose certain conditions on the proposed transaction if the Application is approved.

1. Rate Freeze

I&E, the OCA, and the OSBA each recommended that the three-year rate freeze proposed by Aqua and the Township in the APA be rejected. In opposing the proposed rate freeze, I&E, the OCA and the OSBA argued that the rate freeze constitutes a rate stabilization plan which adds no value to the transaction, and that existing Aqua customers should not be put at risk to cover the revenue requirement needed to keep EWT rates lower than rates set in a base rate case. They further contended that the Commission, not Aqua, maintains rate setting authority, and that it is possible that Aqua may file a rate case prior to the end of the rate freeze period which would exacerbate the rate differential between Aqua's existing wastewater customers and the EWT customers. In addition, the OSBA alternatively proposed that the Commission should direct Aqua to impute revenues to EWT customers to make up for any revenue shortfall associated with any rate increase applicable to EWT in Aqua's first base rate case after closing of the proposed transaction, which is similar to how Aqua has addressed this concern in prior acquisitions. I&E M.B. at 11-12; OCA M.B. at 45; OSBA M.B. at 15-18.

Aqua and the Township argued that a rate freeze is not a rate stabilization plan because there is no language in Aqua's proposed tariff proposing that rates be held constant or phased in over time after the next base rate case, nor is there language that would bind the Commission from modifying rates in future cases. Also, Aqua averred that it is likely that the EWT System will not see a rate increase prior to expiration of the proposed rate freeze. Aqua contended that the OSBA's alternative approach is unnecessary because Aqua would handle any rate increase that would occur before the rate freeze expires by proposing an effective date of new rates for EWT customers synchronized with the date of the rate freeze expiration so that no existing customers will pay to fund the System. Aqua M.B. at 46-49; EWT M.B. at 14.

2. Cost of Service

I&E and the OCA recommended that Aqua be required to provide a cost of service study for the EWT System. They argued that this would protect customers because it will help determine the costs required to operate the EWT System and assist in establishing rates to reflect those costs. I&E M.B. at 10-11; OCA M.B. at 46.

Aqua agreed that, in its next base rate case that includes the EWT System, it will include a separate cost of service study for the EWT System using the same methodology it used for prior systems acquired through Section 1329 proceedings. Aqua M.B. at 45.

3. Missing Easements

I&E recommended that the closing of the transaction not be permitted to occur until the Township provides proof that it has identified all missing easements and taken all necessary actions to obtain the missing easements to convey to Aqua at closing, at the Township's sole expense. Further, I&E argued that the Commission should condition approval of the Application to address circumstances beyond the Township's control where it is unable to transfer all missing easements. To that end, I&E recommended that Aqua and the Township be allowed to close the transaction at their discretion provided that an escrow account be established from the purchase price proceeds to be used to obtain any post-closing transfers of easements. I&E M.B. at 13.

Aqua contended that the conditions recommended by I&E are not necessary because this issue is already contemplated in the APA. Aqua averred that Section 6.06 of the APA provides that if a parcel of unidentified and unscheduled real property is discovered, the Township shall convey the property rights to such parcel without additional consideration. Aqua M.B. at 44-45.

4. Long Term Infrastructure and Improvement Plan (LTIIIP) Projects

The OCA argued that the proposed projects reflected in Aqua's revised LTIIIP should be in addition to, and not reprioritize, any capital improvements that Aqua was already committed to undertake for existing customers. The OCA contended that this condition would help to ensure that projects and expenditures already planned for existing customers will not be given less priority as a result of the proposed acquisition. OCA M.B. at 46.

Aqua argued that capital plans and prioritization of projects are not set in stone. Therefore, Aqua asserted that it must maintain the ability to prioritize and allocate projects based on system needs as they evolve during an LTIIIP period. Aqua M.B. at 49-50.

5. Allowance for Funds Used During Construction (AFUDC) for Non-Distribution System Improvement Charge (DSIC) Improvements

The OCA contended that rate claims related to the accrual of AFUDC for non-DSIC post acquisition improvements should be made in the next Aqua base rate case following the plant additions. The OCA argued that this condition would ensure that AFUDC would be claimed at the same time as the improvements are included in rates. OCA M.B. at 46.

Aqua stated that it agreed with the OCA's recommendation with the clarification that, if claims are made for AFUDC and deferred depreciation, they should be made in Aqua's first base rate case that includes the EWT System, and not simply Aqua's next base rate case. Aqua M.B. at 50.

6. Rate Base

The OCA argued that the Commission should adopt the OCA's proposed adjustments to the appraisals, resulting in an overall ratemaking rate base of \$46,500,000. The OCA contended that the average of the adjusted appraisal results is less than the purchase price and should be adopted as the ratemaking rate base pursuant to 66 Pa. C.S. § 1329(c)(2). The OCA further averred that the lower ratemaking rate base will reduce the revenue deficiency created by the acquisition and the resulting rate increases for customers. OCA M.B. at 45.

Aqua contended that the ratemaking rate base of the EWT System, determined pursuant to Section 1329 (c)(2), is \$54,930,000, which is the lesser of the negotiated purchase price of \$54,930,000 and the average of the UVE appraisals of \$56,724,729. Therefore, Aqua argued that the OCA's criticisms of the appraisals should be rejected and given no weight. Aqua M.B. at 42.

7. Disposition

The Commission may impose conditions on granting a certificate of public convenience as it may deem to be just and reasonable in order to ensure that a transaction is in the public interest. 66 Pa. C.S. § 1103(a). Great latitude is provided to the Commission when determining conditions imposed on award of a certificate of public convenience. *Rheems Water Co. v. Pa. PUC*, 620 A.2d 609 (Pa. Cmwlth. 1993).

Through the Stipulation discussed *supra*, Aqua, the Township, I&E, the OCA, the OSBA, and Mr. Gage negotiated, among other things, a resolution of the conditions for approval recommended by I&E, the OCA, and the OSBA, with the exception of the reduced ratemaking rate base condition recommended by the OCA.

Moreover, the Parties recommended the imposition of the conditions described above if the Stipulation is not approved.

Specifically, the Stipulation resolved the issues regarding the conditions addressing the rate freeze, cost of service study, missing easements, LTIIP projects, and AFUDC treatment for non-DSIC related improvements. Consistent with our conclusion above that the Stipulation is in the public interest and shall be adopted, we will only impose those conditions contained in, and consistent with, the Stipulation. In addition, we note that the OCA's recommended condition to reduce the ratemaking rate base was not resolved or included in the Stipulation. However, the ratemaking rate base value was thoroughly considered in this proceeding and decided above. Accordingly, we will not adopt or further consider here the OCA's recommended condition regarding the ratemaking rate base.

Finally, as discussed *supra*, I&E filed an Exception asserting that while it did not present testimony challenging the affirmative public benefits of the proposed transaction, it did, however, recommend that certain conditions must be implemented if the transaction is approved. I&E stated that its recommended conditions are contained in the Stipulation, and therefore, it supported the approval of the Stipulation if the Commission approves the Application. I&E Exc. at 2-4. As set forth above in our disposition of the Stipulation, we will adopt the Stipulation and grant I&E's Exception on this issue.

E. Section 507 Approvals

Aqua requested the Commission's approval of the assignment of twenty-two contracts with municipalities under 66 Pa. C.S. § 507. Aqua M.B. at 50 (citing Aqua St. 1 at 6). Aqua asserted that the contracts are necessary for the operation of the wastewater System, and that no party opposed Commission approval of the contracts.

Aqua also contended that the contracts, including assignments, are reasonable, legal and valid. *Id.* The ALJ did not address Aqua's request to approve the assignment of the contracts under 66 Pa. C.S. § 507.

In its Exception No. 5, Aqua excepts to the failure of the Recommended Decision to recommend Section 507 approvals for the contracts, including assignment of contracts, between Aqua and the Township. Aqua argued that the contracts are necessary for the operation of the System and that no Party opposed the approval of them. Aqua Exc. at 37. No Replies to Exceptions were filed on this issue.

In the Stipulation discussed *supra*, the Parties agreed that the Commission shall issue the necessary approvals or certificates for the transaction pursuant to 66 Pa. C.S. § 507. Accordingly, we will direct that certificates of filing under Section 507 of the Code shall be issued. Since we are adopting the Stipulation in this Opinion and Order, which includes the approval of the contracts and assignments under 66 Pa. C.S. § 507, we find that Aqua's Exception No. 5 is moot, requiring no further discussion or consideration herein. Therefore, we will deny Aqua's Exception No. 5.

F. Section 2102 Approval

Upon approval of the Application, Aqua asserted that it will be taking assignment of the Township's rights and responsibilities under an agreement between Aqua Resources, an affiliate of Aqua, and various municipalities, for conveyance of wastewater through the Valley Creek Trunk Line. Aqua averred that the agreement and charges under it were negotiated by Aqua Resources and non-affiliates, and are reflective of a negotiated, market rate for the conveyance of wastewater. Finally, Aqua stated that no changes in the negotiated, market rates will occur as a result of the assignment of the

agreement. Aqua M.B. at 50-51. The ALJ did not address Aqua's request to approve the assignment of the agreement under 66 Pa. C.S. § 2102.

In its Exception No. 6, Aqua excepts to the failure of the Recommended Decision to recommend Section 2102 approval of the assignment of the agreement between Aqua Resources and various municipalities. Aqua argues that the charges under the agreement are reflective of a negotiated, market rate for conveyance of wastewater, and that no Party opposed the assignment. Aqua contends that the Commission should approve the assignment of the agreement. Aqua Exc. at 37-38. No Replies to Exceptions were filed on this issue.

In the Stipulation discussed *supra*, the Parties agreed that the Commission shall issue the necessary approvals or certificates for the assignment of the agreement pursuant to 66 Pa. C.S. § 2102. Accordingly, we will direct that a certificate of filing under Section 2102 of the Code shall be issued. Since we are adopting the Stipulation in this Opinion and Order, which includes the approval of the assignment of the agreement under 66 Pa. C.S. § 2102, we find that Aqua's Exception No. 6 is moot, requiring no further discussion or consideration herein. Therefore, we will deny Aqua's Exception No. 6.

G. Other Approvals, Certificates, Registrations and Relief, if any, Under the Code

Aqua also requested that the Commission acknowledge the issuance of all other approvals, certificates, registrations, and relief, if any, under the Code as may be appropriate. Aqua M.B. at 51.

None of the Parties raised objections to this general request. The ALJ did not address this issue in the Recommended Decision.

It is unclear what specific relief the Company is requesting with this general argument. To the extent that Aqua is requesting that we acknowledge our general powers under Section 501 of the Code, 66 Pa. C.S. § 501, we find such an announcement to be unnecessary. Accordingly, we will not grant Aqua's general request pertaining to unspecified approvals, certificates, registrations, and other relief.

VI. Conclusion

Based on the foregoing discussion, we shall: (1) grant, in part, and deny, in part, the Exceptions of Aqua and the Township, and grant the Exception of I&E; (2) adopt the Recommended Decision, as modified; and (3) approve the Application, as modified; all consistent with this Opinion and Order; **THEREFORE,**

IT IS ORDERED:

1. That the Exceptions of Aqua Pennsylvania Wastewater, Inc., filed on May 20, 2022, to the Recommended Decision of Administrative Law Judge Marta Guhl, issued on May 10, 2022, are granted, in part, and denied, in part, consistent with this Opinion and Order.

2. That the Exceptions of East Whiteland Township, filed on May 20, 2022, to the Recommended Decision of Administrative Law Judge Marta Guhl, issued on May 10, 2022, are granted, in part, and denied, in part, consistent with this Opinion and Order.

3. That the Exception of the Commission's Bureau of Investigation and Enforcement filed on May 20, 2022, to the Recommended Decision of Administrative Law Judge Marta Guhl, issued on May 10, 2022, is granted, consistent with this Opinion and Order.

4. That the Recommended Decision of Administrative Law Judge Marta Guhl, issued on May 10, 2022, is adopted as modified, consistent with this Opinion and Order.

5. That the Stipulation filed by Aqua Pennsylvania Wastewater, Inc., the Bureau of Investigation and Enforcement of the Pennsylvania Public Utility Commission, the Office of Consumer Advocate, the Office of Small Business Advocate, East Whiteland Township, and Mr. Richard Gage on April 14, 2022, is approved.

6. That the Application of Aqua Pennsylvania Wastewater, Inc., filed on July 26, 2021, seeking approval pursuant to Sections 1102, 1329, 507, and 2102 of the Public Utility Code, 66 Pa. C.S. §§ 507, 1102, 1329, 2102, for: (1) the acquisition, by Aqua Pennsylvania Wastewater, Inc., of the wastewater system assets of East Whiteland Township situated within Chester County, Pennsylvania; (2) the approval of the right of Aqua Pennsylvania Wastewater, Inc., to begin to offer, render, furnish, and supply wastewater service to the public in the areas served by the East Whiteland Township wastewater system; (3) an order establishing the ratemaking rate base of East Whiteland Township's wastewater system assets pursuant to 66 Pa. C.S. § 1329(c)(2); and (4) the approval of the Asset Purchase Agreement, between Aqua Pennsylvania Wastewater, Inc., and East Whiteland Township and certain contracts in connection with the proposed acquisition, including the assignments of certain contracts, pursuant to 66 Pa. C.S. §§ 507 and 2102, is approved subject to the following conditions in (a) through (o) below:

a) That, at the time of Aqua Pennsylvania Wastewater, Inc.'s first base rate case that includes the East Whiteland Township system, Aqua Pennsylvania Wastewater, Inc. may propose an effective date for new rates for East Whiteland Township wastewater customers that is different from the effective date of new rates for other customers, consistent with the terms of Section 7.03 of the Asset Purchase Agreement, and all Parties' rights are reserved to address this proposal.

b) That, if Aqua Pennsylvania Wastewater, Inc. proposes to freeze East Whiteland Township rates beyond the effective date of new rates in Aqua Pennsylvania Wastewater, Inc.'s first base rate case that includes the East Whiteland Township system assets, then: 1) Aqua Pennsylvania Wastewater, Inc. shall propose a separate rate for East Whiteland Township customers in its tariff that reflects the continuation of East Whiteland Township's existing rates through the end of the rate freeze period; and 2) Aqua Pennsylvania Wastewater, Inc.'s compliance proof of revenue will be calculated using the new rate otherwise applicable to East Whiteland Township customers at the conclusion of Aqua Pennsylvania Wastewater, Inc.'s base rate case, not East Whiteland Township's frozen rate, such that existing ratepayers are not required to fund the revenue deficiency related to the rate freeze. Upon the expiration of the contractual rate freeze term, the customers acquired through the acquisition of the East Whiteland Township system shall immediately become subject to the new rate applicable to East Whiteland Township customers, as determined in Aqua Pennsylvania Wastewater, Inc.'s first base rate case that includes the East Whiteland Township system assets.

c) That, in the first base rate proceeding filed by Aqua Pennsylvania Wastewater, Inc. that includes East Whiteland Township's wastewater system assets, Aqua Pennsylvania Wastewater, Inc. shall propose to move the East Whiteland Township system to its full cost of service, based on a separate cost of service study for East Whiteland Township's system; provided, however, that Aqua Pennsylvania Wastewater, Inc. will not be obligated to propose East Whiteland Township wastewater rates in excess of Aqua Pennsylvania Wastewater, Inc.'s proposed Rate Zone 1 system-average rates. However, Aqua Pennsylvania Wastewater, Inc. may agree to rates other than those proposed for East Whiteland Township customers in the context of a settlement of the base rate

case, and the rights of the Commission's Bureau of Investigation and Enforcement, the Office of Consumer Advocate, the Office of Small Business Advocate, and East Whiteland Township are reserved to fully address this proposal and make other rate proposals in the base rate case.

d) That, in the next rate case, Aqua Pennsylvania Wastewater, Inc. shall provide written notice to East Whiteland Township customers of the rate filing and the level of increase, if any, resulting from the provision at Paragraph 6(c) above.

e) That, Aqua Pennsylvania Wastewater, Inc. shall send a welcome letter to East Whiteland Township wastewater customers within thirty days following Closing which will include information regarding the conversion to monthly billing for their sewer service.

f) That, in the first base rate case filing that includes the East Whiteland Township assets, Aqua Pennsylvania Wastewater, Inc. shall:
(1) include a cost of service study that removes all costs and revenues associated with the operation of the East Whiteland Township system; and (2) include a separate cost of service study for the East Whiteland Township system.

g) That, Aqua Pennsylvania Wastewater, Inc. and East Whiteland Township shall work to ensure the transfer of all real property rights, including easements and missing easements as defined in the Asset Purchase Agreement by Closing.

h) That, Aqua Pennsylvania Wastewater, Inc. shall be permitted, in its discretion, to close the transaction without the transfer of all of the real property rights, provided that an escrow is established from the purchase price to be used to obtain any post-Closing transfer of the real property rights.

i) That, Aqua Pennsylvania Wastewater, Inc. shall provide an update to the Commission's Bureau of Investigation and Enforcement, the Office of Consumer Advocate, and the Office of Small Business Advocate approximately thirty days in advance of the anticipated Closing Date and a final update before Closing regarding the status of the transfer of real property rights including easements related to the system.

j) That, if Aqua Pennsylvania Wastewater, Inc. proposes to modify its Long Term Infrastructure Improvement Plan to include the East Whiteland Township wastewater system, the projects added for East Whiteland Township shall be in addition to those that Aqua plans for its existing systems.

k) That, in Long Term Infrastructure Improvement Plans or Annual Optimization Plans that include the East Whiteland Township wastewater system, Aqua Pennsylvania Wastewater, Inc. shall not reprioritize other existing capital improvements that it already committed to undertake. However, this does not limit the current practice and ability of Aqua Pennsylvania Wastewater, Inc. to allocate projects as needed for its capital program.

l) That, upon Commission approval of a modification to Aqua Pennsylvania Wastewater, Inc.'s Long Term Infrastructure Improvement Plan that includes the East Whiteland Township wastewater system, Aqua Pennsylvania Wastewater, Inc. shall be permitted to apply the Distribution System Improvement Charge to the East Whiteland Township wastewater system prior to the first base rate case in which the East Whiteland Township assets are incorporated into rate base.

m) That, if Aqua Pennsylvania Wastewater, Inc. is not already applying the Distribution System Improvement Charge to the East Whiteland Township wastewater system, it shall do so when rates for those customers are implemented

in the first base rate proceeding that includes the East Whiteland Township system assets.

n) That, any claims for Allowance for Funds Used During Construction and deferred depreciation related to post-acquisition improvements not recovered through the Distribution System Improvement Charge for book and ratemaking purposes, shall be addressed in Aqua Pennsylvania Wastewater, Inc.'s first base rate case which includes East Whiteland Township wastewater system assets, and the Parties rights to fully litigate their positions in future rate cases regarding any future claims for Allowance for Funds Used During Construction, deferral of depreciation, and transaction costs related to this acquisition are reserved.

o) That, in its next base rate case, Aqua Pennsylvania Wastewater, Inc. shall separately identify any legal fees included in its transaction and closing costs pursuant to the Asset Purchase Agreement between Aqua Pennsylvania Wastewater, Inc. and East Whiteland Township and specify amounts expended by Aqua Pennsylvania Wastewater, Inc. on behalf of East Whiteland Township. The rights of the Commission's Bureau of Investigation and Enforcement, the Office of Consumer Advocate, and the Office of Small Business Advocate to challenge the reasonableness, prudence, and basis for such fees are reserved.

7. That, pursuant to 66 Pa. C.S. § 1329(c)(2), the ratemaking rate base of the East Whiteland Township wastewater system assets is \$54,413,635.

8. That the Commission's Secretary shall issue a Certificate of Public Convenience evidencing Aqua Pennsylvania Wastewater, Inc.'s right under Sections 1102(a)(1), 1102(a)(3) and 1329(c)(2) of the Pennsylvania Public Utility Code, 66 Pa. C.S. §§ 1102(a)(1), 1102(a)(3) and 1329(c)(2), subject to the conditions set forth in this Opinion and Order, to: (a) acquire, by sale, the wastewater system assets of East

Whiteland Township; (b) the right of Aqua Pennsylvania Wastewater, Inc., to begin to offer, render, furnish and supply wastewater service to the public in portions of East Whiteland Township, Chester County, Pennsylvania; and (c) allow Aqua Pennsylvania Wastewater, Inc., to incorporate the ratemaking rate base of \$54,413,635 for the East Whiteland Township wastewater system assets in its next base rate case pursuant to 66 Pa. C.S. § 1329(c)(2).

9. That the Commission's Secretary shall issue a Certificate of Filing under Section 507 of the Public Utility Code, 66 Pa. C.S. § 507, for each of the following agreements:

a) Asset Purchase Agreement between the Township of East Whiteland (as Seller) and Aqua Pennsylvania Wastewater, Inc. (as Buyer) dated as of January 8, 2021, attached to the Application as Exhibit B.

b) Valley Forge Treatment Plant Agreement, dated November 1, 1970, by and between Valley Forge Sewer Authority; the Townships of Schuylkill, East Pikeland, Charlestown, East Whiteland, Tredyffrin, Willistown, and Easttown; the Borough of Malvern; Malvern Municipal Authority; East Whiteland Municipal Authority; Tredyffrin Township Municipal Authority; and Easttown Township Municipal Authority, attached to the Application as Exhibit F1.

c) Composite Amendment No. 1 to Valley Creek Trunk Sewer Agreement, East Whiteland Trunk Line Agreement, and Valley Forge Sewage Treatment Plant Agreement dated December 1, 1974, by and between Tredyffrin Township Municipal Authority, Township of Tredyffrin, Township of Schuylkill, Township of East Pikeland, Township of Charlestown, Township of East Whiteland, Township of Willistown, Township of Easttown, Borough of Malvern, Valley Forge Sewer Authority, Malvern Municipal Authority, East Whiteland

Municipal Authority, and Easttown Municipal Authority, attached to the Application as Exhibit F2.

d) Amendment to Valley Forge Sewer Treatment Plant Agreement, dated January 1, 1983, by and between Valley Forge Sewer Authority; the Townships of Schuylkill, East Pikeland, Charlestown, East Whiteland, Tredyffrin, Willistown, and Easttown; the Borough of Malvern; Malvern Municipal Authority; East Whiteland Municipal Authority; Easttown Municipal Authority; Tredyffrin Township Municipal Authority; and Willistown Township Municipal Authority, attached to the Application as Exhibit F3.

e) Supplement to Valley Forge Sewage Treatment Plant Agreement For the Purpose of Complying with United States Environmental Protection Agency Regulations, dated December 2, 1985, by and between Valley Forge Sewer Authority; the Townships of Schuylkill, East Pikeland, Charlestown, East Whiteland, Tredyffrin, Willistown, and Easttown; the Borough of Malvern; Malvern Municipal Authority; East Whiteland Municipal Authority; Tredyffrin Township Municipal Authority; Easttown Township Municipal Authority, and Willistown Township Municipal Authority, attached to the Application as Exhibit F4.

f) Addendum to Valley Forge Sewage Treatment Plant Agreement for the Purpose of Permitting and Administering the Sale of Reserved Capacity Among the Parties, dated May 26, 1994, by and between Valley Forge Sewer Authority, the Townships of Schuylkill, East Pikeland, Charlestown, East Whiteland, Tredyffrin, Willistown, and Easttown; the Borough of Malvern; East Whiteland Township Municipal Authority; Easttown Municipal Authority; and Tredyffrin Township Municipal Authority, attached to the Application as Exhibit F5.

g) East Whiteland Trunk Line Agreement, dated February 1, 1971, by and between East Whiteland Municipal Authority, the Township of East Whiteland, Malvern Municipal Authority, the Borough of Malvern, and Valley Forge Sewer Authority, attached to the Application as Exhibit F6.

h) Amendment to East Whiteland Trunk Line Agreement, dated December 12, 1979, by and between East Whiteland Municipal Authority, the Township of East Whiteland, the Borough of Malvern, Malvern Municipal Authority, and Valley Forge Sewer Authority, attached to the Application as Exhibit F7.

i) Amendment to East Whiteland Trunkline Agreement, dated April 18, 2014, by and between East Whiteland Township, East Whiteland Municipal Authority, and Valley Forge Sewer Authority, attached to the Application as Exhibit F8.

j) Sidley Road Trunk Line Repairs Agreement, dated December 27, 1978, by and between East Whiteland Municipal Authority and Valley Forge Sewer Authority, attached to the Application as Exhibit F9.

k) Sewage Treatment Agreement, dated November 17, 1987, by and between East Goshen Township, East Goshen Municipal Authority, East Whiteland Township, and East Whiteland Municipal Authority, attached to the Application as Exhibit F10.

l) Agreement, dated September 14, 1993, by and between Willistown Township, East Whiteland Township and East Whiteland Municipal Authority, attached to the Application as Exhibit F11.

m) Agreement, dated July 10, 1995, by and between Malvern Borough, East Whiteland Township, and East Whiteland Municipal Authority, attached to the Application as Exhibit F12.

n) Sewage Treatment Agreement, dated October 17, 2000, by and between East Goshen Township, East Goshen Municipal Authority, East Whiteland Township, and East Whiteland Municipal Authority, attached to the Application as Exhibit F13.

o) Sewage Capacity/Service Agreement, dated November 1, 2000, by and between East Whiteland Township, East Whiteland Township Municipal Authority, Tredyffrin Township, Tredyffrin Township Municipal Authority, and Trammell Crow Northeast Metro Development, Inc., attached to the Application as Exhibit F14.

p) Addendum to Sewage Capacity/Service Agreement, dated November 19, 2015, by and between East Whiteland Township and Tredyffrin Township with the jointers of RLD Atwater JV, LLC and The Haven At Atwater Village, LLC, attached to the Application as Exhibit F15.

q) Sewage Treatment Agreement, dated March 2, 2004, by and between East Whiteland Township, East Goshen Township, and Malvern Institute for Psychiatric & Alcoholic Studies, attached to the Application as Exhibit F16.

r) Wastewater Conveyance Agreement, dated November 20, 2018, by and between Aqua Resources, Inc., Tredyffrin Township, East Whiteland Township, Willistown Township, Charlestown Township, Schuylkill Township, East Pikeland Township, Easttown Township, Easttown Township Municipal Authority, The Borough of Malvern, Tredyffrin Township Municipal Authority, and Valley Forge Sewer Authority, attached to the Application as Exhibit F17.

s) Agreement with Public Utility or Municipality for Crossing Under Railroad Private Property, dated March 21, 1972, by and between Reading Company and East Whiteland Municipal Authority, attached to the Application as Exhibit F18.

t) License Agreement for Wire, Pipe and Cable Transverse Crossings and Longitudinal Occupations, dated July 11, 1975, by and between Penn Central Transportation Company and East Whiteland Municipal Authority, attached to the Application as Exhibit F19.

u) License Agreement, dated November 18, 1993, by and between National Railroad Passenger Corporation and East Whiteland Township Municipal Authority, attached to the Application as Exhibit F20.

v) Amendment to License Agreement, dated May 6, 2002, by and between National Railroad Passenger Corporation and East Whiteland Township Municipal Authority, attached to the Application as Exhibit F21.

w) License Agreement, dated September 10, 1999, by and between National Railroad Passenger Corporation and East Whiteland Township, attached to the Application as Exhibit F22.

10. That the Commission's Secretary shall issue a Certificate pursuant to Section 2102 of the Public Utility Code, 66 Pa. C.S. § 2102, approving the assignment from East Whiteland Township to Aqua Pennsylvania Wastewater, Inc., of the Wastewater Conveyance Agreement, dated November 20, 2018, by and between Aqua Resources, Inc., Tredyffrin Township, East Whiteland Township, Willistown Township, Charlestown Township, Schuylkill Township, East Pikeland Township, Easttown Township, Easttown Township Municipal Authority, The Borough of Malvern, Tredyffrin

Township Municipal Authority, and Valley Forge Sewer Authority, attached to the Application as Exhibit F17.

11. That, after closing of the acquisition, Aqua Pennsylvania Wastewater, Inc., shall file with the Commission a compliance tariff supplement to be effective immediately upon closing, consistent in form and content with the Tariff Supplement attached to the Application, filed on July 26, 2021, implementing rates for East Whiteland Township customers post-closing.

12. That the Commission's Secretary, upon the receipt of written notice from Aqua Pennsylvania Wastewater, Inc., filed with the Secretary's Bureau notifying the Commission of the closing of the acquisition and upon the completion of Ordering Paragraph No. 11 above, mark this docket closed.

BY THE COMMISSION,

A handwritten signature in black ink, appearing to read "Rosemary Chiavetta". The signature is written in a cursive, flowing style.

Rosemary Chiavetta
Secretary

(SEAL)

ORDER ADOPTED: July 29, 2022

ORDER ENTERED: July 29, 2022