



COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
COMMONWEALTH KEYSTONE BUILDING
400 NORTH STREET, HARRISBURG, PA 17120

BUREAU OF
INVESTIGATION
&
ENFORCEMENT

April 5, 2024

Via Electronic Filing

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

Re: Pennsylvania Public Utility Commission v.
Pennsylvania-American Water Company
Docket Nos. R-2023-3043189 (Water)
R-2023-3043190 (Wastewater)

I&E Reply Brief

Dear Secretary Chiavetta:

Enclosed for electronic filing please find the Reply Brief of the Bureau of Investigation and Enforcement in the above-captioned proceeding.

Copies are being served on parties of record per the attached Certificate of Service. Should you have any questions, please do not hesitate to contact me.

Respectfully,

A handwritten signature in black ink that reads 'Carrie B. Wright'.

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Per Certificate of Service

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket Nos. R-2023-3043189
	:	R-2023-3043190
Pennsylvania-American Water Company	:	

**REPLY BRIEF
OF THE
BUREAU OF INVESTIGATION AND ENFORCEMENT**

Carrie B. Wright
Prosecutor
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Pennsylvania Public Utility Commission
Bureau of Investigation and Enforcement
Commonwealth Keystone Building
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Dated: April 5, 2024

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I. INTRODUCTION

A. Description of the Party Submitting the Brief

Please see the I&E Main Brief.¹

B. Procedural History

See the I&E Main Brief.² On March 26, 2024, Main Briefs were filed by various parties to this proceeding, which I&E respond to with this Reply Brief.

C. Overview of PAWC's Filing

See the information contained in the I&E Main Brief.³

D. Legal Standards and Burden of Proof

See the information contained in the I&E Main Brief.⁴

I&E reiterates that PAWC has failed to meet its burden of proof that the rates it proposes are just and reasonable and respectfully request that the Administrative Law Judges (ALJ) and the Commission adopt the adjustments as set forth in the I&E testimony and exhibits and the I&E Main Brief.

II. SUMMARY OF ARGUMENT

Reiterating the summary contained in the I&E Main Brief, I&E avers that PAWC has failed to fully carry its burden of proof with respect to its proposed revenue increase of \$203,945,911, updated in Rebuttal to \$204,291,164. To the contrary, I&E's presentation of expert witness testimony demonstrates that PAWC should receive a

¹ I&E MB, p. 1.

² I&E MB, pp. 1-3.

³ I&E MB, pp. 3-4.

⁴ I&E MB, pp. 4-6.

revenue increase of no more than \$56,050,684.⁵ Broken down further, this represents an increase of \$29,343,583 to PAWC water operations; an increase of \$19,925,077 to PAWC Wastewater Sanitary Sewer Systems (SSS) operations; and an increase of \$6,782,024 to PAWC Wastewater Combined Sewer Systems (CSS) operations.⁶

III. OVERALL POSITION ON RATE INCREASE

See I&E Main Brief.⁷

IV. RATE BASE

A. Utility Plant In Service

I&E is recommending a total fair value for PAWC's water rate base of \$4,688,960,669.⁸ In addition, I&E is recommending a total fair value for PAWC Wastewater SSS rate base of \$646,311,450.⁹ In addition, I&E is recommending a total fair value for PAWC Wastewater CSS rate base of \$480,501,661.¹⁰

As the Company notes in its Main Brief, the challenges the to the Company's plant in service generally related to the removal of Audubon Water Company (AWC), the Butler Area Sewer Authority, Farmington Township, and Sadsbury Township.¹¹

PAWC has characterized the closing of these systems as "likely" to occur before the end of the FPFTY. In its Main Brief, the Company says that there is no reason to treat these systems any differently than any plant the utility places in service during the

⁵ I&E St. No. 1-SR, p. 14.

⁶ I&E St. No. 1-SR, pp. 10-13.

⁷ I&E MB, pp. 7-9.

⁸ I&E MB, Appendix A, I&E Table I - Water Operations, column F, line 22.

⁹ I&E MB, Appendix A, I&E Table I - Wastewater SSS Operations, column F, line 22.

¹⁰ I&E MB, Appendix A, I&E Table I - Wastewater CSS Operations, column F, line 22.

¹¹ PAWC MB, p. 12.

FPFTY. I&E submits, however, that there are good reasons to treat these systems differently than plant place in service in the FPFTY. First, and foremost, there is no law that allows them to place these systems they do not own into rate base, while current law does allow for the inclusion in rate base of plant that will be placed in service in the FPFTY. Further, the Company's argument ignores a glaring difference. This plant to be placed in service in the FPFTY that is being discussed is all related to systems that it already owns.

PAWC notes that in its 2020 base rate case, the not-yet-completed acquisitions of the Borough of Kane, Winola Water, and Delaware Sewer were included in rates.¹² Additionally, PAWC explains that in its 2022 base rate case, the pending acquisitions of the York Sewer Authority, Upper Pottsgrove Township, Foster Township and Creekside Homeowners Association were included in its rates.¹³

While the above is true, PAWC has failed to include what separates those acquisitions from the ones in the instant case. Regarding PAWC's 2020 base rate case, the case was filed on or about March 31, 2020. Other parties direct testimony was due September 2, 2020. The Recommended Decision in the Borough of Kane proceeding, which approved the unopposed settlement, was issued on May 7, 2020, and the Commission's final Order was adopted on June 18, 2020.¹⁴ This was almost three months before the other parties direct was due and the appeal period, which was unlikely

¹² PAWC MB, p. 13.

¹³ PAWC MB, pp. 13-14.

¹⁴ *App. of Pa. American Water for Approval of the Transfer, by Sale, of the Wastewater Collection and Treatment System of the Borough of Kane Auth.*, Docket No. A-2019-3014248 (Order entered June 18, 2020).

to be used because the Commission approved an unopposed settlement, had expired. Winola Water was not a “normal” acquisition, but a Section 529 acquisition. Section 529 acquisitions generally occur when a utility is being operated in a manner which necessitates the appointment of a receiver to operate the utility for a time and an investigation into whether another capable utility should take them over. That proceeding was instituted by I&E with the filing of a *Petition for the Issuance of an Ex Parte Emergency Order*.¹⁵ In that proceeding, the Commission directed PAWC to act as the receiver for Winola Water.¹⁶ On August 6, 2020, the Commission entered an Order approving an unopposed settlement by which PAWC, which was already the receiver of Winola, would purchase the system.¹⁷ This was approximately one month before the other parties direct was due in the base rate case, and being an approved unopposed settlement was unlikely to be appealed. Delaware Sewer was another Section 529 acquisition. Once again, this acquisition was the product of an unopposed settlement which was approved by the Commission. The Commission’s final order in the Delaware Sewer acquisition was entered June 13, 2019.¹⁸

As can clearly be seen, the above-referenced acquisitions were clearly different than the acquisitions included in the instant filing. Further, there was reasonable degree of certainty that they would be closed within the FPFTY that we do not have here.

¹⁵ *Pa. Public Util. Comm’n, BIE v. Winola Water Company*, Docket No. P-2018-3006216 (Order entered August 6, 2024).

¹⁶ *Pa. Public Util. Comm’n, BIE v. Winola Water Company*, Docket No. P-2018-3006216, *Ex Parte Emergency Order*, p. 6 (Dated November, 29, 2018, ratified, December 6, 2020).

¹⁷ *Pa. Public Util. Comm’n, BIE v. Winola Water Company*, Docket No. P-2018-3006216, pp. 1-2, (Order entered August 6, 2020).

¹⁸ *Investigation Instituted per Section 529 Into Whether the Commission Shall Order a Capable Public Utility to Acquire Delaware Sewer Company*, Docket No. I-2016-2526085 (Order entered June 13, 2019).

PAWC's 2022 base rate case was filed on March 20, 2022.¹⁹ An Order approving the settlement in that proceeding was entered on December 8, 2022. In that proceeding, non-company direct testimony was due July 29, 2022. In that proceeding, the York acquisition²⁰ was included in rate base. The unanimous settlement of all issues approving the York Sewer Authority acquisition was approved in an Order entered April 14, 2022. As like most of the acquisitions above, it was unlikely that this Order would be appealed since all parties to the proceeding joined in the approved settlement. Regarding the Upper Pottsgrove Acquisitions, the Commission's Order approving the non-Unanimous settlement was entered on September 15, 2021.²¹ On June 30, 2022, PAWC closed on the acquisition. This was approximately a month before the parties' direct testimony was due in the 2022 base rate case.

Lastly, PAWC's acquisition of the Creekside Development involved the acquisition of a system that at the time served 49 residential customers, and when the subdivision was fully developed, would serve approximately 102 single-family homes and 17 townhomes.²² The Commission's Bureau of Technical Utility Services (TUS) reviewed the filing, and no other parties were involved. In this case, although the opportunity was available, no parties (not I&E, OCA or OSBA, among others) were involved in this proceeding seemingly suggesting that there was no large opposition or

¹⁹ *Pa. P.U.C. v. Pa. American Water*, Docket Nos. R-2022-3031672 and R-2022-3031673 (Order entered December 8, 2022).

²⁰ *App. of Pa. American Water Co. to Acquire the York City Sewer Auth.*, Docket No. A-2021-3024681 (Order entered Apr. 14, 2022).

²¹ *App. of Pa. American Water to Acquire Upper Pottsgrove Twp.*, Docket No. A-2020-3021460 (Order entered Sept. 15, 2021)

²² *App. of Pa. American Water to Acquire the Water System Assets from Creekside Homeowners Assoc.*, Docket No. A-2022-3031020, p. 2 (Order entered May 18, 2023).

major concern with this acquisition. Furthermore, of all the acquisitions discussed, this was by far the smallest and would have the least impact on PAWC’s customers and rate base.

A quick review of the acquisitions involved shows that all those that were allowed to be included in rate base were vastly different than the acquisitions included in the instant base rate case. The prior acquisitions could all reasonably be assumed to be closed at some point within the FPFTY, whereas the various acquisitions included in this base rate case have generally either barely started or are working through various different appeal processes. Therefore, while in some instances, PAWC has been allowed to include in rate base some systems that it does not outright own at the filing of the case, it is clear that in this case, it would be inappropriate to include systems that PAWC cannot say with any level of certainty it will own by the end of the FPFTY.

B. Depreciation Reserve

I&E did not provide testimony specifically related to depreciation reserve.

C. Cash Working Capital

As explained in the I&E Main Brief, I&E witness Okum presented the following CWC recommendation which is based on the I&E O&M expense adjustments:

	Updated Claim	Updated I&E Allowance	Adjustment²³
Water Operations	\$23,152,054	\$22,063,423	(\$1,088,631)
Wastewater SSS Ops.	\$2,235,324	\$2,204,399	(\$30,925)
Wastewater CSS Ops.	<u>\$1,881,933</u>	<u>\$1,881,933</u>	<u>\$0</u>
Total	<u>\$27,269,311</u>	<u>\$26,149,755</u>	<u>(\$1,119,556)</u>

²³ I&E Statement No. 1-SR, p. 36.

To reiterate, however, “[a]ll adjustments to the Company’s claims for revenues, expenses, taxes, and rate base must be continually brought together for each operating unit in the Administrative Law Judge’s Recommended Decision and again in the Commission’s Final Order. This process, known as iteration, effectively prevents the determination of a precise calculation until all adjustments have been made to the Company’s claims.”²⁴ The Company also acknowledges in its Main Brief, “[i]f any changes are made to the Company’s proposed O&M expenses, its cash working capital would need to be recalculated.”²⁵ As a result, this number would be subject to change based on any other expense adjustments the ALJs may adopt in their Recommended Decision, or those that the Commission may adopt in their final Order.

D. Acquisition Adjustment and Amortization Expense

An Acquisition adjustment occurs when a utility purchases another system for more or less than the book value. It can also include transaction costs incurred to acquire a system and is typically claimed in rate base and amortized over a reasonable period of time. Annual amortization expense is an operating expense. It represents the recovery or refund of regulatory assets and liabilities over an agreed upon period of time. Regulatory assets and liabilities may or may not be included in a company’s rate base.

PAWC is claiming \$3,749,235 of Acquisition Adjustment in the FPFTY.²⁶

²⁴ I&E Statement No. 1-SR, p. 37.

²⁵ PAWC MB, p. 20.

²⁶ PAWC Volume 3, Ex. 3-A, p. 96, line 16 and p. 106.

For the Sadsbury system, the Company is projecting that the purchase price will be \$945,612 less than the net book value of the Sadsbury plant.²⁷ Because it is a negative Acquisition Adjustment, the Company is required to amortize the adjustment as a credit back to customers over 10 years. While there is no rate base adjustment, the Company is claiming a negative \$94,561 ($\$945,612 / 10$) Acquisition Adjustment expense be credited back to customers over 10 years. As I&E has recommended the Sadsbury acquisition be removed from this proceeding in total, it will also be necessary to remove this negative acquisition adjustment.²⁸

I&E witness Kubas recommends that \$83,085 of Transaction Costs related to the Sadsbury system and \$51,761 of Transaction Costs related to the Farmington system included in the Acquisition Adjustments be removed from the total Acquisition Adjustment claimed in rate base. These systems are not yet owned by PAWC, therefore PAWC should not be able to include the corresponding Transaction Costs incurred to acquire these systems as part of the total Acquisition Adjustment in rate base from these systems in the SSS Operations.

If the Commission adopts I&E's recommendation to exclude the Sadsbury and Farmington system, there should be a corresponding \$9,147 reduction of amortization expense claimed for the Sadsbury system and \$5,699 claimed for the Farmington System.²⁹ As described above, these systems are not yet owned by PAWC and it is premature to allow PAWC to recover these corresponding transaction expense in this

²⁷ PAWC Volume 4, Ex. 3-B, p. 344.

²⁸ I&E Statement No. 3, p. 83.

²⁹ PAWC Volume 3, SSS Operations, page 130.

case. In addition, if the \$83,085 of Transaction Costs related to the Sadsbury system and \$51,761 of Transaction Costs related to the Farmington system be removed from the total Acquisition Adjustment claimed in rate base, there should be a corresponding reduction of \$8,358 of Annual Amortization related to the Sadsbury system and a reduction of \$5,224 of Annual Amortization related to the Farmington system.³⁰

E. Annual Depreciation Expense

This issue was adequately addressed in the I&E Main Brief.³¹

To reiterate, I&E witness Kubas recommends that \$24,342 of annual depreciation expense associated with the Sadsbury wastewater system and \$11,611 associated with the Farmington wastewater system be removed from the SSS Operations annual depreciation expense.³² Mr. Kubas explains that the filing did not contain a breakdown of annual depreciation expense for the Farmington System; therefore, he applied the approximately 1.26% composite depreciation rate applicable in the Sadsbury system to the Farmington system net plant to arrive at the \$11,611 ($\$923,272 \times 0.012576$) of Farmington annual depreciation expense.³³

This recommendation is consistent with the I&E recommendation that these systems be removed from this filing as there is no certain date when PAWC will actually own them. As PAWC is not currently the owner of the systems, PAWC should not be able to include the annual depreciation expense therefrom.

³⁰ I&E Statement No. 3, pp. 84-85, citing I&E Ex. No. 3, Sch. 28, lines 10 and 18.

³¹ I&E Main Brief, pp. 19-20.

³² I&E Statement No. 3, pp. 80-81. *See also* I&E Exhibit No. 3, Sch. 28, lines 6-8.

³³ *Id.* at 81.

F. Reporting – Utility Plant in Service

This issue was adequately addressed in the I&E Main Brief.³⁴

V. REVENUES

A. Present Rate Revenue

This issue was adequately addressed in the I&E Main Brief.³⁵ To reiterate, I&E recommends that \$12,814,193 of present rate revenue from BASA and \$1,824,191 of present rate revenue from Brentwood³⁶ be excluded from rate recovery. I&E also recommends that \$322,926 of present rate revenue from Farmington and \$471,228 of present rate revenue from Sadsbury be excluded from this case.³⁷ As explained above, these are systems that PAWC does not currently own, and it is unclear at what point PAWC will actually own these systems. As such it is I&E's recommendation that all inclusion of these pending acquisitions be removed from the instant proceeding.

B. Late Payment Revenue

Late Payment Revenue was adequately addressed in the I&E Main Brief.³⁸ As explained therein, I&E witness Kubas recommend that Other Operating Revenue be increased from \$673,367 to \$752,121 which is an increase of \$78,755 entirely composed of Late Payment Revenue.³⁹

³⁴ I&E MB, pp. 20-21.

³⁵ I&E MB, p. 22.

³⁶ It is I&E's understanding that it is the Company's intent to remove Brentwood from this filing, however, for purposes of clarity, I&E has noted this recommendation related to Brentwood.

³⁷ I&E Statement No.3-R, p. 17.

³⁸ I&E MB, p. 23.

³⁹ I&E Statement No. 3, p. 71.

VI. EXPENSES

The public utility requesting a rate increase and seeking to recover expenses has the burden of showing that the rate requested, including all claimed expenses, is just and reasonable.⁴⁰

A. Payroll Costs – Vacancy Rate

I&E did not make an adjustment to this expense.

B. Annualized Performance Pay

I&E withdrew this adjustment in Surrebuttal testimony.⁴¹

C. Group Insurance Expense

I&E did not make an adjustment to this expense.

D. 401K, Defined Contribution Plan and Employee Stock Purchase Plan

I&E did not make an adjustment to this expense.

E. Stock Based Compensation Expense – AWW Executives

I&E did not make an adjustment to this expense.

F. Executive Prerequisites (AWW Executives Dividend Equivalents)

I&E did not make an adjustment to this expense.

G. Payroll Tax

As noted above, I&E withdrew its performance pay adjustment in Surrebuttal testimony. As the I&E payroll tax expense adjustment was the result of the I&E

⁴⁰ 66 Pa. C.S. § 315(a).

⁴¹ I&E Statement No. 1, p 16.

performance pay adjustment, I&E withdrew its payroll tax expense adjustment in Surrebuttal testimony as well.⁴²

H. Insurance Other Than Group

I&E did not make an adjustment to this expense.

I. Uncollectible Expense

I&E did not make an adjustment to this expense.

J. Arrearage Management Plan (AMP) Credits - Uncollectible Expense

I&E did not make an adjustment to this expense.

K. Acquisition Related Expense

This issue was adequately addressed in the I&E Main Brief.⁴³ To reiterate, as part of the acquisition O&M claim, the Company has included various O&M expenses for the following potential acquisitions: Farmington Water, Audubon Water, Farmington Wastewater, Sadsbury Wastewater, BASA Wastewater, and Brentwood Wastewater.⁴⁴ The following table shows the Company's allocation of O&M expense among Water Operations and Wastewater SSS Operations:

Acquisition O&M Expense:	FPFTY⁴⁵
Water Operations	\$1,675,709
Wastewater SSS Operations	<u>\$504,709</u>
Total PAWC Expense	<u>\$2,180,418</u>

⁴² I&E Statement No. 1-SR, p. 17.

⁴³ I&E MB, pp. 26-28.

⁴⁴ PAWC Exhibit No. 3-B, pp. 303-308.

⁴⁵ I&E Statement No. 1, p. 26.

As discussed above, it is not appropriate for the Company to claim and recover expenses for utilities that it does not own. With the exception of BASA, the Commission has not yet made a ruling on any of these acquisitions. The BASA decision is currently under appeal and the outcome is, therefore, unknown. Due to the uncertainty surrounding each of these acquisitions, I&E recommends disallowance of the entire claim.

It is simply not in the public interest for PAWC to require its already burdened ratepayers to pay for assets that PAWC does not own. For the reasons stated above, I&E recommends disallowance of PAWC's claim of \$1,675,709 for Water Operations O&M expense.⁴⁶ Additionally, I&E recommends a disallowance of \$504,709 of acquisition related O&M expense for Wastewater SSS Operations.⁴⁷

L. Interest Synchronization

I&E did not make an adjustment to this expense.

M. Amortization Expense

This issue was adequately addressed in the I&E Main Brief.⁴⁸ Annual amortization expense is an operating expense.

To reiterate, I&E witness Kubas explains that if the Commission agrees with the recommendation to exclude the Sadsbury and Farmington systems, there should be a corresponding \$9,147 reduction of amortization expense claimed for the Sadsbury system and \$5,699 claimed for the Farmington system as shown on PAWC Volume 3, SSS

⁴⁶ I&E Statement No. 1, p. 27.

⁴⁷ I&E Statement No. 1, p. 27.

⁴⁸ I&E MB, pp. 29-30.

Operations, page 130.⁴⁹ As previously noted these systems are not yet owned by PAWC and, therefore, it is premature to allow PAWC to recover these corresponding transaction expense in this case.

The Company also claimed a negative plant acquisition adjustment in the total amortization expense related to the Sadsbury system. For the Sadsbury system, the Company is projecting that the purchase price will be \$945,612 less than the net book value of the Sadsbury plant. This \$945,612 is shown on PAWC Volume 4, Ex. 3-B, p. 344. Because it is a negative Acquisition Adjustment, the Company is required to amortize the adjustment as a credit back to customers over 10 years. While there is no rate base adjustment, the Company is claiming a negative \$94,561 ($\$945,612 / 10$) Acquisition Adjustment expense be credited back to customers over 10 years (PAWC Volume 3, Ex. 3-A, p. 130). If the Commission agrees with the I&E recommendation to remove the plant, revenue, expenses, taxes, and amortizations related to the Sadsbury system, the Commission should also remove the negative \$94,561 Annual Amortization expense credit related to the Sadsbury system shown on PAWC Volume 3, Ex. 3-A, p. 130. Since the system has not yet been acquired, the Company should not be required to credit this \$94,561 Annual Amortization expense back to customers.

N. Call Center Expense

I&E did not make an adjustment to this expense.

⁴⁹ I&E Statement No. 3, p. 82.

O. Depreciation Expense

I&E's only depreciation expense adjustment is discussed above in the "Annual Depreciation Expense" portion of the brief.

P. Pension and Other Post Employment Benefits (OPEB) Expense and Request for Deferred Regulatory Accounting Treatment

1. Pension and OPEB Tracker

As explained in I&E's Main Brief, a Pension and OPEB tracker is not appropriate. Typically, the Commission has permitted extraordinary, unanticipated, non-recurring, and substantial expenses to be deferred for accounting purposes. Examples of these types of costs include those costs to make repairs in order to avoid and imminent threat to public health and safety, hurricane damage, and across the board accounting changes that would have a significant financial impact on a utility.⁵⁰ The Commission has stated "the standard which a utility must meet when seeking Commission authorization for deferral accounting is whether, based on Commission precedent, the expense item appears to be within the scope of the type of items that the Commission has allowed as an exception to the general rule against retroactive recovery of past expense."⁵¹ Deferred accounting treatment may be granted if the expense is: 1) extraordinary; 2) unanticipated; 3) non-

⁵⁰ *Petition of Pennsylvania Util. Co., Inc.*, 2012 PaPUC LEXIS 1124, at 2-3; *see also* *Petition of Pike County Light and Power Co.*, 2012 PaPUC LEXIS 939 at 5-6; *Petition of Columbia Gas of Pa. Inc.*, 2012 PaPUC LEXIS 836.

⁵¹ *Petition of Columbia Gas of Pa., Inc. for Authority to Defer for Accounting and Financial Purposes Certain Start Up Expenses Assoc. with the Redesign of Upgrade of Financial Processes and Info. Systems*, Docket No. P-2012-2319920 (Order Entered December 5, 2012).

recurring; and 4) substantial.⁵² In *Popowsky v. Pa. P.U.C.*, it was noted that:

Extraordinary cannot mean merely unanticipated, because then every unexpected occurrence or failure to predict an item would be recoverable and the exception would overwhelm the rule, making test years meaningless. To be extraordinary, it must also be a substantial, one-time expense or a substantial item that will not appear as a continuing expense and could otherwise never be recovered in rates because, like the weather-related expenses, it would be normalized out of the test year as abnormal.⁵³

While these costs have sometimes been substantial in the past, the costs are not extraordinary because pension and OPEB costs are routine expenses incurred by PAWC as well as many other water and wastewater utilities. These expenses are not one-time expenses and occur year after year. Secondly, the costs are not unanticipated because they are a part of contractual agreements with past employees. Finally, the expenses cannot be categorized as non-recurring while also being forecasted on an annual basis. As the Company's pension and OPEB expenses may have only met one of four criteria to be considered for regulatory asset treatment, it is not appropriate for the Commission to grant approval for the Company to defer these costs.

As explained in the OCA Main Brief, approval of this proposal will also remove PAWC's incentive to manage or reduce these costs because it provides certainty that these costs will be recovered without a prudence or reasonableness review.⁵⁴

Pension and OPEB expenses are normal, expected, recurring costs for which the Company cannot expect a virtually guaranteed dollar-for-dollar recovery. Pensions and

⁵² *Id.*

⁵³ *Popowsky v. Pa. Publ. Util. Comm'n*, 642 A.2d 648, 652 (Pa. Cmmwlth 1994).

⁵⁴ OCA MB, p. 46.

OPEB costs do not meet the requirements for deferral treatment, and I&E recommends that the Commission deny the Company's request. The Company's Main Brief does not provide any information that would support a determination that these expenses meet the requirement for deferral treatment.

2. Pension Expense

As explained in the I&E Main Brief, a historic three-year average is appropriate for this expense.⁵⁵ This approach was recently adopted by the Commission in PGW's 2023 base rate case (*PGW 2023*). There the Commission adopted a three-year normalization of rate case expense.⁵⁶ Therefore, I&E continues to recommend using a three-year average of historic actual expenses for pension based on the evidence presented and relevant case law. In Main Brief, the Company provided no evidence that demonstrated a departure from this methodology was appropriate.

3. OPEB Expense

Additionally, I&E continues to recommend a historic three-year average for the calculation of OPEB expense.

The approach recommended by I&E witness Okum is consistent with prior Commission determinations. In the 2023 PGW Base Rate Case (*PGW 2023*) the Commission stated, "...similar to PGW's pension expense claim, a three-year normalization of the Company's claim for OPEB expense is appropriate."⁵⁷ In addition,

⁵⁵ I&E MB, pp. 33-34.

⁵⁶ *Pa. P.U.C. v. PGW*, Docket No. R-2023-3037933, p. 883 (Order entered November 9, 2023).

⁵⁷ *Pa. P.U.C. v. PGW*, Docket No. R-2023-3037933, p. 86 (Order entered November 9, 2023).

in a recent PECO Gas base rate Case (*PECO Gas 2021*) the Commission stated the following regarding a three-year average of OPEB expense:

We agree with the ALJ's recommendation that the OCA's proposed adjustment to OPEB expense, in which actual and projected OPEB expense for the years 2020-2022 are averaged, will reflect a level of OPEB expense that is more accurate and reasonable. We are persuaded by the OCA's argument that its proposed adjustment calculation, which utilizes the Company's actual and estimated OPEB costs from 2020-2022, will include the projected increase in OPEB expenses that will result from the expiration of the prior service credit amortization.⁵⁸

As previously explained in the I&E Main Brief, the evidence presented by I&E and the relevant case law demonstrate that a three-year average for OPEB expense is the appropriate measure. Therefore, I&E witness Okum's recommendation should be adopted.

Q. Production Expense and Request for Deferred Regulatory Accounting Treatment

For largely the same reasons as described above related to the Pension and OPEB tracker, I&E recommends denial of the Companies' proposed Production Expense Tracker. As succinctly stated in the OSBA Main Brief, Utility management should be expected to cope with normal business risks and the operation of economic forces, without resorting to single-issue ratemaking, such as the requested deferred accounting treatment, except in circumstances of compelling public interest.⁵⁹

The expenses in question are not extraordinary, unanticipated, or non-recurring,

⁵⁸ *Pa. P.U.C. v. PECO Energy Co. – Gas Division*, Docket No. R-2020-3018929, p. 90 (Order entered June 22, 2021).

⁵⁹ OSBA MB, p. 13.

and while in some instances they may be substantial expenses they do not meet the requirements to be deferred for accounting purposes. Nothing in the Company’s Main Brief demonstrates a compelling argument for granting deferred accounting in this instance.

R. Miscellaneous Expense Adjustment – Credit Card and E-check Fees

This issue was fully addressed in the I&E Main Brief.⁶⁰

VII. TAXES

As explained in the I&E Main Brief, I&E made no specific recommendations related to adjustments to taxes.⁶¹ Any impact on taxes, if at all, would simply be a result of the flow through of other adjustments.

VIII. RATE OF RETURN

A. Summary

I&E witness DC Patel recommends the following rate of return for PAWC:⁶²

I&E Summary of Cost of Capital Pennsylvania-American Water Company - Water Operations			
Type of Capital	Ratio	Cost Rate	Weighted Cost Rate
Long-Term Debt	44.01%	4.76%	2.09%
Preferred Stock	0.00%	0.00%	0.00%
Common Equity	<u>55.99%</u>	8.45%	<u>4.73%</u>
Total	<u>100.00%</u>		<u>6.82%</u>

⁶⁰ I&E MB, pp. 38-39.

⁶¹ I&E MB, p. 39.

⁶² I&E Statement No. 2-SR, p. 44.

In addition, I&E witness Patel recommends the following rate of return for PAWC wastewater division:⁶³

I&E Summary of Cost of Capital Pennsylvania-American Water Company - Wastewater Operations			
Type of Capital	Ratio	Cost Rate	Weighted Cost Rate
Long-Term Debt	42.73%	4.76%	2.03%
Wastewater Specific Debt	4.40%	2.67%	0.12%
Preferred Stock	0.00%	0.00%	0.00%
Common Equity	<u>52.87%</u>	8.45%	<u>4.47%</u>
Total	<u>100.00%</u>		<u>6.62%</u>

I&E witness Patel accepts PAWC’s claimed cost rates of long-term debt as these cost rates are based on projected actual costs and are representative of the industry.⁶⁴ Mr. Patel also recommends using the Company’s capital structure for both water and wastewater as they fall within his proxy group’s capital structures.⁶⁵ However, I&E witness Patel rejects the Company’s method for calculating return on common equity. Instead, I&E witness Patel calculates his recommended return on equity pursuant to the Discounted Cash Flow (DCF) methodology frequently used by the Commission while using the Capital Asset Pricing Model (CAPM) as an alternate means to verify the reasonableness of his return.

⁶³ I&E Statement No. 2-SR, p. 44.

⁶⁴ I&E St. No. 2, pp. 17-18.

⁶⁵ I&E St. No. 2, p. 16.

B. Proxy Group

I&E fully addressed the appropriateness of including a parent company in a proxy group in its Main Brief.⁶⁶ Therefore, I&E continues to recommend that PAWC's parent Company, American Waterworks be included in the proxy group used to determine the rate of return in this proceeding. Further, as fully explained in I&E's Main Brief, gas and electric utilities have differing risks from water and wastewater utilities that make them not appropriate for use in a proxy group for water and wastewater utilities.⁶⁷

In Main Brief, PAWC criticizes Mr. Patel's "small" proxy group and says that this "small" proxy group led to flawed DCF results. Mr. Patel's proxy group is made up of 5 companies, as described in testimony and the I&E Main Brief.⁶⁸

The argument that Mr. Patel's proxy group is too small is belied by PAWC's own rate of return witness Ann Bulkley who herself admits that the appropriate size for a proxy group has been established by FERC and is, in fact, 5 utilities of comparable risk.⁶⁹ This is, in fact, precisely what Mr. Patel used; a proxy group comprised of 5 companies of comparable risk.

Therefore, I&E continues to recommend the use of Mr. Patel's proxy group in this proceeding as it produces the appropriate rate of return and return on equity.

⁶⁶ I&E MB, pp. 42-47.

⁶⁷ I&E MB, pp. 42-47.

⁶⁸ I&E MB, p. 43.

⁶⁹ Tr. at 2100.

C. Capital Structure

I&E witness Patel recommends using the Company's claimed capital structures for both water and wastewater as these capital structures fall within the range of Mr. Patel's proxy group.⁷⁰

D. Cost of Long-Term Debt

I&E accepts PAWC's claimed cost rate of long-term debt of 4.76% for water and wastewater, as well as the 2.67% cost rate of long-term debt for wastewater specific issuances.⁷¹

E. Return on Common Equity

1. Introduction

As recommended by I&E witness Patel, an 8.45% return on common equity for both PAWC Water Operations and PAWC Wastewater Operations, based upon I&E witness Patel's use of a similarly-situated proxy group of companies, best balances the interests of the ratepayers and the Company.

2. I&E's Discounted Cash Flow Analysis

As explained above, the main criticism of PAWC with regard to I&E's DCF analysis is that it is based on a "flawed" proxy group. However, as I&E has explained, PAWC witness Bulkley, along with FERC, agree that a proxy group comprised of 5 companies of comparable risk is generally sufficient. This is precisely what I&E's proxy group consists of.

⁷⁰ I&E St. No. 2, p. 16.

⁷¹ I&E St. No. 2-SR, p. 43.

PAWC's takes liberties with I&E's analysis and removes Middlesex Water, which oddly enough, PAWC keeps in its own proxy group, to make Mr. Patel's proxy group smaller than its own witness believes is appropriate.⁷² Additionally, PAWC incorporates Essential Utilities, which as explained in I&E's Main Brief,⁷³ is not appropriately included in this proxy group, into Mr. Patel's proxy group and arrives at a DCF result of 9.21% and notes that using PAWC's proxy group would result in a 9.82% DCF result.⁷⁴ Ironically, even after "correcting" I&E's DCF analysis, the results that are produced are not where near Ms. Bulkley's recommended 10.95%.

3. CAPM

PAWC's criticizes I&E for not weighting its CAPM analysis and merely using it as a comparison to its DCF.

In addition, PAWC criticizes Mr. Patel for the use of a 10-year treasury rate, while simultaneously acknowledging that the Commission has approved it in the past. For the reasons set forth in testimony and the I&E Main Brief, I&E submits the 10-year treasury rate is appropriate.⁷⁵

However, as explained in the I&E Main Brief, the CAPM is a flawed methodology to determine ROE. I&E witness Patel gave no specific weight to his CAPM results because of his concerns that unlike the DCF, which measures the cost of equity directly

⁷² PAWC MB, p. 48.

⁷³ Commission has affirmed its standard of relying on percentage of revenue for determining whether a company should be included in a proxy group. The Commission once again explained that a company's revenue, rather than operating income, was the appropriate measure to gauge whether to include a utility in a proxy group. *See also*, I&E MB, pp. 45-46.

⁷⁴ *Id.*

⁷⁵ I&E MB, p. 51.

by measuring the discounted present value of future cash flows, the CAPM measures the cost of equity indirectly and can be manipulated by the time period used. However, I&E submits that for purposes of providing another point of comparison, the 10.44% CAPM analysis confirms the reasonableness of I&E witness Patel's 8.45% return under his DCF calculation.

F. Business Risks and Management Performance

As explained in the I&E Main Brief, nothing demonstrates that PAWC is any riskier than other water and wastewater utilities. Therefore, business risk is already accounted for in I&E witness Patel's proxy group and does not need to be further accounted for when setting PAWC's ROE.

The Commission has confirmed the position set forth in the I&E Main Brief. the Commission affirmed the Administrative Law Judge's denial of management performance points in *Pa. P.U.C. v. Columbia Gas*.⁷⁶ The Commission summarized the Recommended Decision and stated:

[The ALJ] agreed with I&E, the OCA, and the OSBA that Columbia failed to provide sufficient evidence to support its proposal for an additional twenty-basis points for "strong management performance." The ALJ reasoned that while effective operating and maintenance cost measures should flow through to ratepayers and/or investors, Columbia's proposal defeats the purpose of cutting expenses to benefit ratepayers, particularly during a pandemic when so many ratepayers have experienced reduced household income from job loss or reduction in hours. Therefore, the ALJ recommended that no upward management effectiveness adjustment be made to the Company's cost of equity.⁷⁷

⁷⁶ *Id.*, p. 50, citing *Columbia Gas*, p. 78.

⁷⁷ *Id.*, citing *Columbia Gas*, p. 134.

Regarding a management performance adder to rate of return, I&Es maintains the essence of true strong management performance is earning a higher return through efficient use of resources and cost cutting measures. The greater net income resulting from cost savings and true efficiency in management and operations is then available to be passed on to shareholders. Therefore, PAWC, or any utility, should not be awarded additional rate of return basis points for doing what they are required to do in order to provide adequate, efficient, safe, and reasonable service under 66 Pa. C.S.A. § 1501 and for increasing profits as they are incentivized to do by their board of directors and shareholders.⁷⁸ As explained by I&E witness Patel and OCA witness Garrett, this 25 basis point addition would amount to approximately \$11.8 million per year in rates.⁷⁹ This amount is unsupported and excessive, and must be denied.

G. Conclusion

PAWC's claimed rate of return overstates its need for a revenue increase. When adjusted by I&E to more reasonable levels that approximate expected returns in today's economy for similarly-situated water utilities, PAWC's evidentiary support for its \$203,945,911 rate increase is substantially reduced. As demonstrated by I&E witness Patel, the appropriate overall rate of return that will result in just and reasonable rates is 6.82% for PAWC water operations and 6.62% for PAWC wastewater operations with an included 8.45% cost rate of common equity.

⁷⁸ I&E Statement No. 2, p. 81.

⁷⁹ I&E Statement No. 2, p. 80 and OCA Statement No. 2, p. 50.

IX. RATE STRUCTURE

A. Cost of Service Studies

While I&E made various recommendations based on the COSSs presented by PAWC which are explained below, I&E did not challenge specific elements of the COSSs presented by PAWC.

1. Water Operations

Regarding the COSS for Water Operations, I&E witness Cline made no recommended changes. Additionally, regarding the customer cost analysis, witness Cline recommended the results of the Company's more direct customer cost be used to determine the customer charge. The customer charges are discussed in more detail below.

2. Wastewater Operations

I&E witness Kubas did not recommend changes to the Company's COSS for wastewater operations. Mr. Kubas notes that he used the Company's COSS to develop his various wastewater rates that move the relative rate of return for each class toward 0.

3. Cost of Service Studies for Future General Rate Increases

This issue was adequately discussed in the I&E Main Brief.⁸⁰ To reiterate, I&E witness Kubas recommended that in the next base rate case filed by PAWC it provides a separate COSS for BASA in the event that PAWC owns the system at that point.⁸¹

⁸⁰ I&E MB, pp. 68-69.

⁸¹ I&E Statement 3, pp. 73-74.

Further, while I&E understands it is the Company's intent to eliminate Brentwood from the current filing, witness Kubas recommended that PAWC provide a COSS for Brentwood in subsequent base rate cases, if and when PAWC owns the system in order for the parties to be able to determine what plant in the Brentwood system is used and useful in public service. Some of the flow carried by the Brentwood plant is from what the Company refers to as "non-customers." Since only plant "used and useful" to serve customers can be recovered from customers, plant in service to serve "non-customers" should be identified and excluded from rate base. Second, Brentwood customers will also pay a separate treatment fee. With no treatment costs in base rates, it could be reasonable to establish a lower rate for Brentwood customers than other SSS customers that have treatment costs recovered in their usage rates. The two primary inputs for cost allocation are the number of customers, and flow. Almost all allocations in a COSS are based on one of these inputs. The Company has no idea how much flow is coming into the system from "non-customers" and how much flow is going out of the system from a combination of "non-customers" and Brentwood customers.⁸² This lack of data indicates that the Brentwood COSS filed in this case is totally speculative and not based on any known and measurable data.

Having the specific COSSs for each of these systems, if owned by PAWC, will ensure that the rates charged to these customers are appropriate. Therefore, I&E recommends that when PAWC files its next base rate case, should it then own the BASA

⁸² I&E Ex. No. 3 Sch. 29.

and/or Brentwood systems, a separate COSS be provided for each system to ensure the rates charge thereto are just, reasonable, non-discriminatory, and in the public interest.

4. Allocation of AMP Costs and Administrative Costs for H2O Programs

I&E did not take a position on these issues.

B. Revenue Allocation and Act 11

Revenue allocation and the Act 11 allocation were adequately discussed in the I&E Main Brief. Shifting the amount of wastewater revenue to water customers that PAWC wishes to shift is simply not in the public interest. Therefore, I&E witness Kubas was able to reduce the \$69.5 million subsidy to \$357,517 (at the full requested increase) with reasonable wastewater rate increases.

I&E determined that it's not in the public interest to shift this much revenue to water customers because only 12.6% of PAWC water customers are also PAWC wastewater customers.⁸³ While the Company claims its proposal is based on the results of various COSS studies, I&E provided un rebutted testimony that while the Company stated this claim, it ignored COSS when it designed rates.⁸⁴ It appears the only justification for decreasing or limiting the increase in wastewater rates was to make them affordable and make the average bill of a wastewater customers comparable to the average bill of a water customers, even though it increases the average bill of a water customer by \$6 per month. Shifting costs to one set of customers at the expense of

⁸³ I&E St. No. 3, p. 16.

⁸⁴ I&E St. No. 3, p. 12.

others, simply to make one group's rates appear more affordable is not in the public interest. The Company failed to rebut the I&E claim that the average bill of a water and wastewater customer does not have to be comparable.⁸⁵ As described below and in direct testimony, I&E described how this \$69.5 million subsidy can be reduced to \$357,517 with reasonable wastewater rate increases.⁸⁶ With this small subsidy, I&E's proposal will reduce the average bill of a water customer by \$6, make the average water bill more "affordable".

The OCA alleges the I&E proposal to reduce the subsidy being provided by water customer goes too far because of the recent increases proposed by PAWC and the smaller customer base onto which to spread the cost of wastewater. Applying the OCA proposed rate increase to all Operations results in an increase of 5.3% for the SSS Operations, 4.7% for the CSS Operations and 5.3% for the Water Operations.⁸⁷

I&E disagrees that it's SSS and CSS Operations rate increases go too far. As described in testimony, Brief and here, the increases wastewater customers will experience are reasonable, regardless of the size of the customer base on to which to spread the revenue requirement and revenue increase.

C. Tariff Structure

1. Residential Customer Charge

For water customers, I&E recommends a residential customer charge of \$20.00. For the various wastewater rate zones, I&E witness Kubas recommends the customer

⁸⁵ I&E St. No. 3, p. 13.

⁸⁶ I&E Ex. No. 3, Sch. 1, corrected February 12, 2024.

⁸⁷ OCA MB, pp 71-75.

charge be set at \$15.00. The I&E customer charge proposals are discussed in further detail and in the I&E testimony and exhibits.

In Main Brief, PAWC refers to I&E witness Cline’s recommended water customer charge as being based on the “extreme” decision to calculate the customer charge on a cost allocation study restricted to only direct customer costs and ask the Commission to reject his recommendation to set the charge at \$19.50.⁸⁸ Notwithstanding the fact that Mr. Cline updated his position in Surrebuttal testimony to adopt the Company’s proposed \$20.00 per month customer charge,⁸⁹ I&E takes issue with the reference to Mr. Cline’s use of a cost allocation study restricted to direct customer costs as being “extreme.” I&E witness Cline’s use of a cost allocation study restricted to direct customer costs is, in fact, consistent with Commission precedent. Traditionally, the Commission has determined customer charges based upon the direct-cost customer cost analysis. Further, the Commission reaffirmed its preference for this customer cost analysis in the 2018 UGI Electric base rate case.⁹⁰ In addition, as explained in the I&E Main Brief, at less than a full increase I&E recommends the customer charge be scaled back proportional to the increase.

2. Water Rate Design

In Main Brief, the Company disagrees with I&E witness Cline’s proposed volumetric rates.⁹¹ However, as explained in the I&E Main Brief,⁹² Mr. Cline’s rate design

⁸⁸ PAWC MB, p. 63.

⁸⁹ I&E St. No. 4-SR, p. 26.

⁹⁰ *Pa. P.U.C. v. UGI Electric*, Docket No. R-2017-2640058, p. 182 (Order entered October 25, 2018).

⁹¹ PAWC MB, p. 63.

⁹² I&E MB, pp. 76-79.

proposals are based on sound Commission ratemaking policies and precedent and should be adopted in total.

3. Wastewater Rate Design

Wastewater SSS Operations

The Company recommends that the Commission reject the I&E proposals set forth by I&E because the Company alleges they do not take into account affordability for wastewater SSS Operations. Additionally, the Company recommends the I&E and OCA proposal to reduce the residential customer charges to make them the same. Also, the Company recommends that the Commission reject the I&E proposal concerning unmetered and special flat rate customers.⁹³

I&E proposed SSS Operations rates and revenue are based upon the cost of providing service to SSS Operations customers that result in reasonable bill increases for average customers.⁹⁴ Regarding “affordability” and “rate shock” concerns, I&E described in testimony how the 24.9% increase the Company proposed for an average Zone 1 water customer is comparable to the 25.3% increase that I&E proposed for a Zone 1 wastewater customer. If a 24.9% increase as proposed by the Company results in an affordable bill and does not create rate shock, by the Company’s own logic a 25.3% increase in a wastewater bill will also result in an affordable wastewater bill that does not create rate shock.

⁹³ PAWC MB, p. 64.

⁹⁴ I&E St. No. 3, pp. 15- 54 and I&E Ex. No. 3, Sch. 3-15.

The Company's concern regarding the Residential customer charge is misplaced. I&E proposed a Residential customer charge of \$15.00 per month change which is not a decrease for most wastewater customers as suggested by the Company. For Zones 1, 2, and 5, which constitute the vast majority of SSS Operations wastewater customers, the \$15.00 per month customer charge that I&E proposed is an **increase** of \$0.70 per month.⁹⁵ For Zone 7, there is a small decrease in the Residential customer charge from \$18.00 to \$15.00 per month, but this decrease will be offset by the I&E proposed 70.9% increase in the Zone 7 usage rate. Both together increase the average Zone 7 Residential bill by 69.2%.⁹⁶ For Zone 9, the Company also proposed a decrease in the monthly flat rate, which included an allowance. Overall, it's misleading to suggest that I&E's \$15.00 per month Residential customer charges in the SSS Operations is unreasonable.

I&E also disagrees with the Company's concern regarding flat rate service. I&E described how the Residential flat rate should be determined and described how the Non-Residential flat rate should eventually match the average bill of a Non-Residential customer.⁹⁷ I&E clarified and described how to properly establish the Residential flat rate.⁹⁸ The Company failed to specifically rebut the I&E testimony concerning the Non-Residential flat rates, and therefore, they should be approved.

The Company's concern regarding special rates is also misplaced. For these special rates, I&E proposed that the percentage increases to these special rates is

⁹⁵ I&E Ex. No. 3, Sch. 3.

⁹⁶ I&E Ex. No. 3, Sch. 3, p. 2, lines 1-6 and Sch. 7, p. 4, line 7.

⁹⁷ I&E St. No. 3, pp. 21-22 and 29.

⁹⁸ I&E St. No. 3-SR, p. 27.

comparable and, in some cases, less than the percentage increase I&E proposed for the classes in which these special rate customers reside.

York Bulk Rates

PAWC proposed that the York Bulk customers receive an increase of 4.9% per year over the next two years for a total increase of 9.8%.⁹⁹ I&E proposed a one-time increase of 50%.¹⁰⁰ The Company claims that these customers have a “viable competitive alternative” and that the proposed rates recover the variable cost of providing service and provide a meaningful contribution to fixed costs.

The Company’s claims concerning the “viable competitive alternative” are unsupported. As described by I&E, the Company failed to describe the alternative, and failed to provide the fixed costs or variable costs these customers would incur to utilize the alternative.¹⁰¹ The Commission is left to speculate if the alternative these customer may have is more or less than the rate they are being charged and if they are making the maximum contribution to fixed costs.¹⁰² This is important because if they are not making the maximum contribution, tariff rate customers are picking up the cost of providing service to these Bulk customers. As described by I&E, the determination should not be if the Company is recovering the incremental cost to serve these customers, the determination should be if they are making the maximum contribution to fixed costs.¹⁰³

While PAWC is critical of I&E for giving up this issue in its most recent prior base rate

⁹⁹ I&E St. No. 3, p. 47.

¹⁰⁰ I&E St. No. 3, p. 50.

¹⁰¹ I&E St. No. 3, p. 48 and St. No. 3-RS, pp. 31-32.

¹⁰² I&E St. No. 3, p. 50

¹⁰³ I&E St. No. 3, pp. 49-50.

case. However, in that base rate case, the cost to serve and the subsidy being provided to these Bulk customers was not known. It's now known that the subsidy after the I&E proposed rate increase to Bulk customers will be approximately \$8 million that will be paid by tariff rate customers.¹⁰⁴ Additionally, the Company has not provided any evidence of the cost these customers would incur to utilize the alternative since these customers chose not to study the alternative and therefore do not know the cost of the alternative.

Regarding the Company's claim that I&E agreed that these customers may have a competitive alternative, I&E submits that does not mean that the competitive alternative described by the Company is viable, or that the rates these customers are being charged maximizes revenue. As described by I&E during the hearings, most large customers have alternatives, but that does not mean they are viable and does not justify granting them a large discount.¹⁰⁵

Concerning maximizing revenue there are two issues. First, the Company's claim that it can't maximize revenue is self-serving because the Company knows any revenue shortfall will be recovered from tariff rate customers, not shareholders. Therefore, it has no incentive to maximize revenue from these customers. Second, it makes no sense not to maximize revenue because if the cost of the alternative is more than the PAWC rate, the Bulk customers have no incentive to utilize a higher cost alternative. Unfortunately,

¹⁰⁴ I&E St. No. 3-SR, pp. 32-33.

¹⁰⁵ Tr. pp. 2155-2156.

the Company failed to describe the alternative and therefore failed to provide the cost of the alternative.

The argument concerning the risk that these customers will leave if the rates are increased 50% is not supported. As described above and in I&E testimony, the claim that these customers would leave is speculation because there is no evidence to suggest the point at which these customers will leave. As described in the customer's affidavit, they are only considering "exploring wastewater treatment options" at this time without any definitive alternatives or plans to leave the system.

The Company's comments concerning regionalization are mere speculation.¹⁰⁶ Simply switching treatment plants does nothing to impact regionalization goals.

Wastewater CSS Operations

Regarding wastewater CSS Operations, the Company refers back to its disagreement with I&E on the overall Act 11 allocation for rejecting the I&E proposed CSS rates.¹⁰⁷ The Company also claims that the rates it proposes for Scranton Zone 3 are consistent with the Asset Purchase Agreement (APA) with Scranton and that any increase to those rates should be just and reasonable and consistent with the concept of gradualism so as to avoid rate shock.¹⁰⁸

Based upon the Company's CSS Operations COSS, there is no support for decreasing present rate revenue. I&E proposed CSS Operations rates and revenue are based upon the cost of providing service to CSS Operations customers that provide

¹⁰⁶ PAWC MB, p. 67.

¹⁰⁷ PAWC MB, p. 67.

¹⁰⁸ PAWC MB, p. 67, fn. 298.

reasonable increase to the bills of average customers.¹⁰⁹ These rates reduce the subsidy needed to operate the CSS Operations.

To address the Company's "rate shock" concerns, I&E described how the 24.9% increase the Company proposed for an average Zone 1 water customer is less than the 17.8% increase that I&E proposed for an average Zone 3 Residential wastewater customers. Logically, if a 24.9% increase proposed by the Company does not result in rate shock, a 17.8% increase in a wastewater bill also would likely not result in rate shock. Finally, as explain in testimony, the Commission is not bound by the APA as this rate commitment is only a proposal, and the Commission is not bound by any rate promises made in asset purchase agreements, as stated in the Order approving the acquisition of the Scranton system.¹¹⁰

In its letter in lieu of brief, the City of Scranton disagrees with Mr. Kubas' recommendation as "...his recommendations include higher rates for the City of Scranton than those originally proposed by the Company."¹¹¹ However, the rates proposed by Mr. Kubas are cost based, and based on sound, Commission approved ratemaking principles.

Additionally, the OCA disagrees with the I&E recommendation stating that the \$20.00 per month CSS Residential customer charge is not cost based and recommends utilizing the \$14.30 per month Residential customer charge in each of the CSS Wastewater rate zones. The OCA claims that the decrease in revenues from reducing the

¹⁰⁹ I&E St. No. 3, pp. 56- 72 and I&E Ex. No. 3, Sch. 17-26.

¹¹⁰ I&E St. No. 3, p. 60.

¹¹¹ City of Scranton Letter in Lieu of Brief, p. 1.

customer charge would only require an increase of 7 to 10% in volumetric usage charges.¹¹²

While I&E acknowledges the \$20.00 per month CSS Residential customer charge is above cost it is more important to maintain the customer charge because: 1) customers are used to paying it, 2) it generates needed revenue and 3), a \$20.00 per month CSS Residential customer results in a smaller decrease for Zone 4. Furthermore, if the average Zone 3 Residential customer that uses 3,200 gallons per month has its present usage rate is increased 10%, the customer will pay an additional \$8.28 ($\$2.351 \times 1.10 \times 3.2$) more per month¹¹³) which is much more than the \$5.70 ($\$20.00 - \14.30) per month increase that I propose in the Zone 3 Residential customer charge. Therefore, the OCA proposal appears to cause the bill for an average Zone 3 customer to increase by approximately \$2.58 ($\$8.28 - \5.70) per month more than I&E proposed.

4. Winter Averaging Proposal

This issue was adequately addressed in the I&E Main Brief.¹¹⁴ To reiterate, after considering the arguments presented by OCA and CAUSE-PA regarding the disproportionate adverse impact on low-income customers, combined with the Company's refusal to adopt the program as temporary, I&E witness Kubas recommends the winter averaging program be rejected in its entirety.¹¹⁵

¹¹² OCA MB, p. 79.

¹¹³ PAWC Volume 9, Ex 10-C, p. 3 and 29.

¹¹⁴ I&E MB, p. 83.

¹¹⁵ I&E Statement No. 3-SR, pp. 38-39.

D. Summary Including Scale Back of Rates

In Main Brief, the Company proposes a proportional scale back of rates if less than a full increase is granted. I&E disagrees and continues to recommend the scale backs as proposed by I&E witnesses Kubas and Cline, as described in the I&E Main Brief, be applied.

I&E's customer cost analysis, customer charge, and scale back proposals are based on sound Commission ratemaking policies and precedent and should be adopted in total.

X. ALTERNATIVE RATEMAKING REQUESTS

As explained in the I&E Main Brief, I&E opposes both Alternative Ratemaking Requests proposed by PAWC in this proceeding.¹¹⁶

A. Revenue Decoupling Mechanism (RDM)

Nothing in the Company's Main Brief demonstrates why the RDM would be appropriate, or how it would satisfy the fourteen factors the Commission must consider when determining whether an alternative ratemaking proposal is appropriate. All arguments set forth in the Company's Main Brief regarding why it believes the RDM should be approved were properly disposed of in the I&E Main Brief¹¹⁷, as well as the Main Briefs of the other parties.¹¹⁸

The RDM does nothing to support conservation as the Company implies in its Main Brief.¹¹⁹ As explained by OCA, "[a] customer would have to reduce their

¹¹⁶ I&E MB, pp. 91-101.

¹¹⁷ I&E MB, pp. 91-98.

¹¹⁸ OCA MB, pp. 85-88, OSBA MB, pp. 22-23, PAWLUG MB, pp. 28-30.

¹¹⁹ PAWC MB, pp. 71-72.

consumption by more than the reduction in usage by all other customers in order to reap the full benefit of their reduction. If an individual customer's reduction turns out to be less than the reduction in usage by all other customers, RDM will take those savings away from the customer and, in fact, the customer's bill will be higher."¹²⁰ The RDM is unlikely to serve to encourage water efficiency and conservation, and is, in fact, likely to discourage conservation as cost savings are eroded. As witness Cline explains, the RDM will appear as a random surcharge or credit on a ratepayer's bill that is completely removed from their own usage and will create confusion. Specifically, by calculating the RDM based on a total class-wide basis, a single customer, particularly low-usage customers, will be unable to affect whether they are assessed an additional surcharge or a credit on their bill in the subsequent year.

To reiterate the points made in the I&E Main Brief, the sole way for a utility customer to reduce their bill, particularly for water customers, is through conservation efforts. Unlike gas and electric utilities, there is no way for a water customer to shop for a new supplier. The RDM will force these customers who take measures to reduce their water consumption to share some, or nearly all, of their bill savings with the utility.¹²¹ Implementing a confusing surcharge that diminishes the benefits of water conservation is not in the public interest.

Should PAWC find itself in financial distress due to volatile rates, it has the means to address this (filing a base rate case, using the DSCI, use of the FPFTY, declining usage

¹²⁰ OCA MB, p. 84-85.

¹²¹ OCA Statement No. 4, p. 58.

adjustments). PAWC has not, however, shown that its level of concern rises that high. PAWC's desire for revenue stability should not come at the costs of the efforts its customers put into conserving water. Unlike PAWC, these customers do not have options if PAWC removes the benefit of conservation from their bills.

For the RDM to be approved, it should have some benefit to customers; however, in this case, it not only would not provide any benefit, but it may harm customers by causing them to overpay and negating any cost incentive to conserve water. Customers who undertake conservation efforts will see their savings eroded and their investment payback time increased as the Company is permitted to increase rates in response to usage declines. PAWC's request for the RDM importantly avoids an explanation of "why." Why is PAWC currently in need of this mechanism? PAWC notes that 81% of its revenues are collected under volumetric rates, but 95% of its costs are fixed and that its ability to recover Commission approved costs will be diminished if it sells less water than anticipated.¹²² However, PAWC has not demonstrated that this impact is currently, actually occurring, or when in the future this impact might be felt by the Company. Ratepayers, however, feel the impact of increased rates frequently and their only means to save money on their utilities is conservation.

With the frequent base rate cases and increasing rates customers are already facing, along with the potential for the RDM to erode the benefits of conservation, it would not be in the public interest for the Commission to approve this alternative rate

¹²² PAWC MB, p. 69.

mechanism. The risk to ratepayers of seeing their conservation savings eroded is not worth the benefit of proving this type of revenue stabilization to PAWC.

B. Environmental Compliance Investment Charge (ECIC)

As with the RDM, nothing in the Company's Main Brief demonstrates why the ECIC should be approved or how it satisfies the fourteen alternative ratemaking factors.¹²³ All arguments set forth in the Company's Main Brief regarding why it believes the ECIC should be approved were properly disposed of in the I&E Main Brief¹²⁴, as well as the Main Briefs of the other parties.¹²⁵

As I&E explained in Main Brief, although environmental issues will be ongoing as environmental science continues to evolve, the implementation of such a charge indefinitely seems, in I&E's view, unnecessary. Environmental compliance has always been a normal part of a utility's expenditures and will be a normal part of PAWC's expenditures whether the ECIC is approved or not. All water and wastewater utilities nationwide face these same emerging contaminant issues. In I&E's view implementing a rider recovery mechanism for just one company before any universal Commission action could occur and before any potential government funding has been established is simply premature. I&E does not dispute that a utility should generally be able to recover costs associated with environmental compliance; however, I&E does not believe that an open-ended surcharge, such as what has been proposed by PAWC, is the proper way to do so, and certainly not while there are still so many unknowns.

¹²³ PAWC MB, pp. 74-76.

¹²⁴ I&E MB, pp. 98-101.

¹²⁵ OCA MB, pp. 88-95, OSBA MB, pp. 23-24, PAWLUG MB, pp. 30-31.

As explained above, the issue of environmental rules changes to deal with PFAS is an industry-wide concern facing all water utilities in the Commonwealth. At this juncture, final regulations have not been formulated, and the Commission has not had the opportunity to react to this situation on a utility-wide basis as it has done in other areas such as COVID cost impacts. Furthermore, this is not a concern that is limited just to Pennsylvania utilities, and like other issues such as lead, there may be federal or state programs and funding that have yet to be established to address this problem on a nationwide or state basis.

Therefore, approval of the ECIC in this proceeding would be premature and would not be in the public interest.

XI. LOW-INCOME CUSTOMER ASSISTANCE

A. Summary

I&E's recommendations related to PAWC's low-income customer programs related mainly to how these programs are funded.

Further, regarding the recommendation made by OCA witness Colton and CAUSE-PA witness Geller that PAWC be required to prepare a written universal service program, I&E maintains that rather than singling out PAWC for this requirement, if the Commission believes written universal service plans are appropriate for water and wastewater utilities, that this be done on a statewide basis as it has been for electric and natural gas utilities.

B. Affordability Analysis

As explained in the I&E Main Brief, I&E witness Kubas recommends that the Commission not rely on the Company's affordability analysis to justify limiting PAWC's wastewater rates for three reasons. First, I&E does not believe that making the average bills of water and wastewater customers comparable should be the primary goal as there is a substantial difference in operating costs between water and wastewater systems. In fact, cost causation, should be the primary factor in setting rates. There is no ratemaking criteria that would imply that water customers and wastewater customers should have comparable rates. Second, the analysis ignores the fact that water customer who do not receive wastewater service from PAWC will incur their own wastewater costs that may or may not be comparable to their PAWC water rates while they subsidize PAWC wastewater customers to provide them with comparable rates. Third, the analysis ignores the benefits the Company claims that could or have accrued to customers in acquired systems. As an example, the analysis ignores the potential local tax reductions PAWC claimed a customer may receive after the wastewater system was acquired by PAWC. Therefore, the affordability analysis is flawed and should not be used to establish wastewater rates.¹²⁶

C. H2O Bill Discount Program Design

I&E made no recommendations related to PAWC's H2O Bill Discount Program.

¹²⁶ I&E Statement No. 3, pp. 13-14.

D. Hardship Fund

This issue was adequately addressed in the I&E Main Brief.¹²⁷ To reiterate, I&E recommends that if CAUSE-PA witness Harry Geller's recommendation to increase PAWC's hardship fund by \$1 million over its existing funding levels is approved, that the Commission specify that the funding source continue to be PAWC shareholders.¹²⁸ In surrebuttal testimony, CAUSE-PA witness Geller indicated his agreement with this recommendation.¹²⁹

E. Conservation Assistance

This issue was adequately addressed in the I&E Main Brief.¹³⁰ To reiterate, CAUSE-PA witness Geller recommends the Company implement a comprehensive conservation and line repair and replacement program for all customer at or below 200% of the federal poverty level (FPL).¹³¹

I&E recommends that if approved, the program should be funded by shareholders and not by ratepayers.¹³²

F. Low-Income Customer Outreach, Screening, and Intake

I&E took no position on these issues.

G. Data Collection, Reporting, and Monitoring of Low-Income Programs

I&E took no position on these issues.

¹²⁷ I&E MB, pp. 102-103.

¹²⁸ I&E Statement No. 1-R, p. 3.

¹²⁹ CAUSE-PA Statement No. 1-SR, p. 4.

¹³⁰ I&E MB, pp. 103-104

¹³¹ CAUSE-PA Statement No. 1, p. 63.

¹³² I&E Statement No. 1-R, p. 4.

H. Comprehensive Written Universal Service Plan

This issue was adequately addressed in the I&E Main Brief.¹³³ Both OCA witness Roger Colton and CAUSE-PA witness Geller recommend that PAWC should be required to develop a written comprehensive universal service plan, which OCA recommends be filed with the Bureau of Consumer Services for review by interested parties.¹³⁴

I&E recommends that rather than singling out PAWC to provide a written universal service plan, if the Commission believes that universal services plans are appropriate for water and wastewater utilities, it provide statewide guidance for all water and wastewater utilities as it has done in the gas and electric industries.

I. Administration of PAWC's Low-Income Assistance Programs

I&E took no position on these issues.

XII. SERVICE QUALITY AND CUSTOMER SERVICE ISSUES

I&E made no recommendations related to service quality and customer service issues.

XIII. MISCELLANEOUS

A. Customer Notices Related to Rate Changes

I&E did not make any recommendations related to customer notices.

B. Tariff Changes (not addressed above)

I&E did not make any further recommendations related to tariff changes, apart from those mentioned in the above sections.

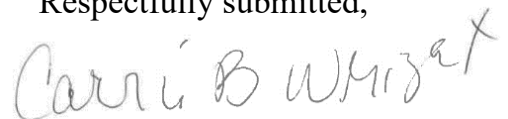
¹³³ I&E MB, pp. 104-105.

¹³⁴ CAUSE-PA Statement No. 1, p. 56 and OCA Statement No. 5, p. 67.

XIV. CONCLUSION

PAWC has failed to satisfy its burden of proof with respect to its proposed revenue increase. To the contrary, I&E's presentation of expert witness testimony demonstrates that PAWC should receive a revenue increase of no more than \$56,050,684. Broken down further, this represents an increase of \$29,343,583 to water operations; an increase of \$19,925,077 to wastewater SSS operations; and an increase of \$6,782,024 to wastewater CSS operations. The Company's ratemaking claims must be amended to reflect the necessary and appropriate adjustments proposed by the Bureau of Investigation & Enforcement's fixed utility financial analyst and engineering witnesses. Accordingly, the Bureau of Investigation & Enforcement respectfully requests the Administrative Law Judges and the Commission adopt its recommendations in this proceeding, including all adjustments and modifications as supported herein, and grant Pennsylvania-American Water Company a rate increase of no more than \$56,050,684.

Respectfully submitted,



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Dated: April 5, 2024

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Pennsylvania Public Utility Commission :
 :
 v. : Docket Nos. R-2023-3043189 (Water)
 : R-2023-3043190 (Wastewater)
 Pennsylvania-American Water Company :

CERTIFICATE OF SERVICE

I hereby certify that I am serving the foregoing **Reply Brief** dated April 5, 2024, in the manner and upon the persons listed below:

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