

Prepared Testimony of

Stephen M. DeFrank

Chairman, Pennsylvania Public Utility Commission

before a public hearing of the

Pennsylvania House Consumer Protection,
Technology & Utilities Committee

December 12, 2023



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Introduction

Greetings Chairman Matzie, Chairman Marshall, and members of the House Consumer Protection, Technology & Utilities Committee. I am Stephen M. DeFrank, Chairman of the Public Utility Commission (Commission or PUC). On behalf of the Commission, I would like to thank the Committee for hosting this hearing and bringing stakeholders to the table to discuss water and wastewater utility acquisitions under Section 1329 of the Public Utility Code. Water and wastewater services are essential to the health and wellbeing of the Commonwealth, and the consideration of our experience to date under Act 12 of 2016 along with any possible revisions to improve the Act are worthy endeavors.

Act 12 of 2016 and Title 66

On April 14, 2016, former Governor Tom Wolf signed Act 12 of 2016 (Act 12) into law. Act 12 amended Chapter 13 of the Public Utility Code by adding Section 1329, 66 Pa.C.S. § 1329, which provides additional options for the valuation of assets of municipally-owned and authority-owned water and wastewater systems, or a “selling utility,” acquired by investor-owned water and wastewater public utilities, or an “acquiring public utility,” as those terms are defined in Section 1329(g).

Prior law, specifically Section 1311(b), 66 Pa.C.S. § 1311(b), discouraged such sales because the value of the acquired property was defined as the original cost of construction less accumulated depreciation, rather than the acquisition cost. Act 12 created a process to determine the fair market value (FMV) of a selling utility that is to be acquired by an acquiring utility. Under Section 1329, for ratemaking purposes, the valuation is the lesser of the FMV or the negotiated purchase price. Thus, Section 1329 mitigates the risk that an acquiring utility will not be able to fully recover its investment when water or wastewater assets are acquired from a selling utility. The FMV is not tied to the original cost of construction minus the accumulated depreciation (also known as the “depreciated original cost”); rather, the FMV allows consideration of cost, market, and income approaches in valuing the system and in establishing future rates reflecting the system acquisition. Section 1329 also allows the acquiring public utility’s post-acquisition-improvement costs not recovered through a distribution system improvement charge to be deferred for book and ratemaking purposes. Overall, Act 12 provides for deferral of post-acquisition improvement costs and also enhanced rate base treatment based on the lesser of the FMV of the acquired assets or the negotiated purchase price.¹

¹ *Implementation of Section 1329 of the Public Utility Code*, Docket No. M-2016-2543193, at 2-3 (Final Implementation Order entered October 27, 2016) (FIO).

Act 12 became effective on June 13, 2016, and was implemented by a series of Commission orders. The Commission's implementation orders (IOs) set forth a comprehensive process for applications filed with the Commission under Section 1329 and provide acquiring utilities under Section 1329 with an application filing checklist, standard data requests, a direct testimony template, and guidelines for utility valuation experts (UVEs).²

Section 1329 applications are filed in conjunction with applications under Section 1102, 66 Pa.C.S. § 1102, which require a determination of substantial affirmative benefits for Commission approval. *City of York v. Pa. Pub. Util. Comm'n*, 295 A.2d 825, 828 (Pa. 1972) (*City of York*). Aqua Pennsylvania Wastewater, Inc.'s (APW's) 2016 application to acquire the wastewater system assets of New Garden Township was the first Section 1329 proceeding to be reviewed by the Commonwealth Court and, in that case, the Court addressed ratepayer impact relative to Section 1329. The Commonwealth Court stated that the Commission is charged with deciding whether the impact of a transaction on rates is outweighed by other positive factors that provide a substantial affirmative benefit and warrant approval.³ The Court also held that notice to all ratepayers of the proposed sale as well as an opportunity for them to participate in the Section 1329 proceeding is required.⁴

Section 1329 Acquisitions as of November 2023

The Commission has received 27 applications under Section 1329 since Act 12 was enacted and 22 of those applications have been approved. Note that the Commission's approval of one of the applications, APW's acquisition of East Whiteland Township's wastewater system (East Whiteland), was overturned by a Commonwealth Court decision. *Cicero v. Pa. Pub. Util. Comm'n*, 300 A.3d 1106 (Pa. Cmwlth. 2023)(*East Whiteland*). The Commission, Aqua, and East Whiteland have filed Petitions for Allowance of Appeal of this Commonwealth Court decision to the Pennsylvania Supreme Court and are awaiting the Court's decision on whether it will accept the appeal.

The Commission currently has five Section 1329 applications filed with one, APW's acquisition of the Delaware County Regional Water Control Authority (DELCORA), that has been officially accepted. As noted above, applications under Section 1329 must meet the Commission's application filing checklist before they are officially accepted after which the statutory six-month timeframe for Commission

² *Implementation of Section 1329 of the Public Utility Code*, Docket No. M-2016-2543193 (Final Supplemental Implementation Order entered February 28, 2019).

³ *McCloskey v. Pa. Pub. Util. Comm'n*, 195 A.3d 1055, 1067 (Pa. Cmwlth. 2018) (*New Garden*).

⁴ *Id.* at 1069.

review and action begins. The other four Section 1329 applications are in varying stages of checklist review.

Once a Section 1329 application is approved, the legislation requires the acquiring utility to incorporate the ratemaking rate base, as defined by the statute, into its rate base in its next base rate case or initial tariff. The approved rate base amount is the lesser of the purchase price negotiated by the acquiring utility and the selling utility, or the FMV of the selling utility. In plain language, the acquiring utility may add the rate base dollar amount to its total rate base, which is used to calculate overall rates to customers. In theory, the larger the rate base, the larger the revenue requirement of the acquiring utility used to set the rates that it charges customers. Now, some of that increased revenue requirement is offset by the additional customers from the selling utility. On balance, whether overall rates for all of the acquiring utilities' customers will increase over time due to 1329 acquisitions depends on that balance of approved rate base amounts and the acquiring utility's other costs to serve acquired customers. As can be seen in Table 1 of the Appendix to this testimony, the approximate rate base per customer (RBPC) varies from a low of \$2,942 (Mahoning Township Wastewater) to a high of \$16,840 (York City Sewer Authority). For comparison, the current RBPC for water customers of Aqua Pennsylvania, Inc. and Pennsylvania-American Water Company (PAWC) are approximately \$8,745 and \$5,559, respectively. The RBPC for wastewater customers of APW and PAWC Wastewater Division are approximately \$9,011 and \$10,268, respectively.

Rates for customers that are acquired under Section 1329 are likely to increase. This is due to a number of factors, such as that the selling utility may have deferred maintenance and capital projects and charged rates that were less than required by the cost of service. Also, the selling utility's customers are often not charged rates which include a return on investment as the selling utility is not investor-owned. In prior cases, the Commission has considered the evidence of the following benefits introduced by the acquiring public utility: commitments to improve service, to undertake necessary maintenance projects, and make capital improvements that benefit acquired customers, local communities and the environment. Additionally, the Commission has considered evidence entered related to the benefit of regionalization brought by these transactions. Finally, we note that the Commission has determined that the acquiring utilities' access to more robust income challenged assistance programs is a benefit. As stated above, the Commission is charged with deciding whether the impact of a transaction on rates is outweighed by other positive factors that provide a substantial affirmative benefit and warrant approval.

Table 2 of the Appendix to this testimony details the approximate rate impacts for the residential customers in those acquired systems under Section 1329. The

Commission-approved rate increases range from a low of 44.9% (East Bradford Township) to a high of 166.6% (Exeter Township). Note this table assumes the selling utility would have kept its rates static. Further, note that some rates have not changed yet due to the acquiring utility not including those systems in base rate cases as of this time. The rates in Table 2 are only for residential customers using 3,500 gallons of water per month, which is a general rule of thumb for average residential usage. The rates are also purely base rates and do not include any surcharges or riders such as a distribution system improvement charge or state tax adjustment surcharge. Adding the riders would complicate the calculation and add little in terms of comparison. We did not include commercial or industrial customers as those are much more difficult customer classes to come up with an “average” user due to varying usage patterns.

Proposed Legislative Updates to Title 66

Now we will highlight the legislative proposals to 66 Pa.C.S. and the potential benefits of those updates. We will discuss each of the four updates in order of where they would appear in Title 66.

House Bill 1862 would add language to 66 Pa.C.S. § 1327, which pertains to the acquisition of water and wastewater utilities, municipal corporations, or persons. The proposed language added to § 1327(a) (pertaining to acquisition cost greater than depreciated original cost) would add requirements specific to selling municipal corporations. Under proposed Section 1327(a.1), the selling municipal corporation would have additional requirements in terms of issuing requests for proposals (RFPs), specifically that the selling municipal corporation must issue an RFP before any purchase agreements can be signed. Additionally, the selling municipal corporation would be required to provide certain noticing, including potential rate impacts, and updating on the status of the RFPs. There are also proposed additional notification requirements under § 1327(b), and a substantial change and addition to § 1327(c), which relates to hearings. Finally, a subsection (g) is added to the section to provide a definition for “approved actuary.”

The additional language to § 1327(a) and (b) primarily impacts a selling municipal corporation and does not substantially impact the Commission other than the Commission would need to verify the necessary actions were completed and detailed in any applications for acquisitions where § 1327(a) and (b) apply. However, we do note that if the intent is to add the RFP and notification requirements to utilities that would be a selling utility under Section 1329, the requirements of Section 1327 would not apply. In other words, applicants filing for an acquisition under Section 1329 have rate base for the selling utility determined under Section 1329 rather than Section 1327. If the intent of HB 1862 is to have this process apply

to applications filed under Section 1329, we would recommend that the proposed language be amended to Section 1329 and not Section 1327.

House Bill 1865 seeks to add language to 66 Pa.C.S. § 1329(c), relating to the ratemaking rate base that would be incorporated into the acquiring utility's rate base upon approval of the application. The proposed change would cap the ratemaking rate base at the lesser of the negotiated purchase price, the FMV, or 125% of the depreciated original cost as calculated under § 1329(d)(5) if the acquisition does not meet the criteria specified under § 1327(a)(2) (the selling utility, municipal corporation, or person has 3,300 or less customers or which is non-viable in the absence of the acquisition) or (3) (the selling utility, municipal corporation, or person from which property was acquired was not, at the time of acquisition, furnishing and maintaining adequate, efficient, safe and reasonable service and facilities).

We do see an issue with proposing a cap on the ratemaking rate base calculated under § 1329(d)(5). We note that § 1329(d)(5) does not contain a calculation of depreciated original cost, but rather a provision for ensuring that the selling utility's cost of service is factored into ratemaking for the acquiring utility with no consideration for the original sources of funding for the acquired assets. If the intention of the bill is to limit the ratemaking rate base to a certain percentage of depreciated original cost, then we respectfully recommend stating as such in the bill and avoid the reference to § 1329(d)(5).

House Bill 1864 builds upon the previous addition to statute by HB 1865 and adds § 1329(c)(3)-(4). The intent of these additions appears to be to spread out the ratemaking rate base impact over the next three base rate cases for those acquisitions that have a ratemaking rate base that exceeds depreciated original cost. However, the proposed language again references the depreciated original cost as calculated under § 1329(d)(5). As previously mentioned, § 1329(d)(5) does not contain a calculation of depreciated original cost and we suggest that the language be consistent with what was suggested above to House Bill 1865.

Lastly, House Bill 1863 seeks to eliminate 66 Pa.C.S. § 1329(d)(2), relating to the six-month limitation on Commission consideration of an application that has been accepted by the Commission. We would support this change as it would lessen the burden of Section 1329 applications on the Commission's staff and allow for the statutory advocates and other protestants to perform a more thorough review of the merits of the application and provide ample opportunity for ratepayers and impacted customers to weigh in.

Conclusion

In conclusion, the Commission appreciates the opportunity to discuss the proposed revisions regarding Act 12. Given the years of experience realized by the

Commission, and all stakeholders involved, we find it reasonable, prudent and appropriate to consider possible revisions to the statute. Similarly, the Commission has begun to consider what options may be available within our purview to improve our administration of the Act.

We thank the Committee Chairs and Members of the Committee for the opportunity to testify and look forward to your questions and further discussion.

Appendix

Table 1: Filed Section 1329 Application Information

#	Docket No.	Buyer	Seller	County	Industry	Date Submitted for Filing	Date Accepted for Filing2	PUC Decision	Order Entry	Purchase Price (\$)	Approved Rate Base (\$)	Customer Count	Rate Base per Customer (\$)
1	A-2016-2580061	APW	New Garden Township Municipal Authority	Chester	Wastewater	12/19/16	12/30/16	Approved	12/03/20	29,500,000	29,500,000	2,106	14,007.60
2	A-2017-2605434	APW	Limerick Township	Montgomery	Wastewater	05/22/17	05/31/17	Approved	11/29/17	75,100,000	64,373,378	5,434	11,846.41
3	A-2017-2606103	PAWC-WD	Municipal Authority of the City of McKeesport	Allegheny	Wastewater	05/25/17	06/14/17	Approved	10/26/17	159,000,000	158,000,000	12,780	12,363.07
4	A-2018-3001582	APW	East Bradford Township	Chester	Wastewater	05/02/18	05/15/18	Approved	09/20/18	5,000,000	5,000,000	1,248	4,006.41
5	A-2018-3002437	PAWC-WD	Sadsbury Township	Chester	Wastewater	06/07/18	06/19/18	Approved	10/25/18	8,600,000	8,300,000	998	8,316.63
6	A-2018-3003517	Veolia-WD	Mahoning Township	Montour	Wastewater	07/24/18	08/08/18	Approved	12/20/18	4,765,200	4,765,200	1,620	2,941.48
7	A-2018-3003519	Veolia	Mahoning Township	Montour	Water	07/24/18	08/08/18	Approved	12/20/18	4,734,800	4,734,800	1,186	3,992.24
8	A-2018-3004933	PAWC-WD	Exeter Township	Berks	Wastewater	09/26/18	04/16/19	Approved	10/03/19	93,500,000	92,000,000	9,015	10,205.21
9	A-2019-3006880	PAWC	Steelton Borough Authority	Dauphin	Water	01/02/19	04/16/19	Approved	10/03/19	21,750,000	20,500,000	2,472	8,292.88
10	A-2019-3008491	APW	Cheltenham Township	Montgomery	Wastewater	03/13/19	05/06/19	Approved	11/05/19	50,250,000	44,558,258	10,219	4,360.33
11	A-2019-3009052	APW	East Norriton Township	Montgomery	Wastewater	07/30/19	11/26/19	Approved	05/21/20	21,000,000	20,750,000	4,966	4,178.41
12	A-2019-3014248	PAWC-WD	Kane Borough Municipal Authority	McKean	Wastewater	12/02/19	02/06/20	Approved	06/18/20	17,560,000	17,560,000	2,019	8,697.37
13	A-2019-3015173	APW	Delaware County Reg. (DELCORA)	Delaware & Chester	Wastewater	03/03/20	07/27/20	Pending		276,500,000		16,328	-
14	A-2020-3019634	PAWC-WD	Roversford Borough	Montgomery	Wastewater	07/14/20	11/09/20	Approved	05/07/21	13,000,000	13,000,000	1,620	8,024.69
15	A-2020-3019859	PAWC	Valley Township	Chester	Water	10/09/20	05/18/21	Approved	10/28/21	7,325,000	7,325,000	1,670	4,386.23
16	A-2020-3020178	PAWC-WD	Valley Township	Chester	Wastewater	10/09/20	05/18/21	Approved	10/28/21	13,950,000	13,950,000	3,125	4,464.00
17	A-2020-3021460	PAWC-WD	Upper Pottsgrove Township	Montgomery	Wastewater	11/24/20	04/14/21	Approved	09/15/21	13,750,000	13,750,000	1,600	8,593.75
18	A-2021-3024267	APW	Lower Makefield Township Sewer Authority	Bucks	Wastewater	05/14/21	08/05/21	Approved	01/13/22	53,000,000	53,000,000	11,800	4,491.53
19	A-2021-3024681	PAWC-WD	York City Sewer Authority	York	Wastewater	07/01/21	10/29/21	Approved	04/14/22	235,000,000	231,500,000	13,747	16,840.04
20	A-2021-3026132	APW	East Whitehall Township	Chester	Wastewater	07/26/21	02/04/22	Approved	07/29/22	54,930,000	54,413,635	3,895	13,970.12
21	A-2021-3027268	APW	Willistown Township	Chester	Wastewater	08/04/21	01/14/22	Approved	07/08/22	17,500,000	17,500,000	2,294	7,628.60
22	A-2022-3034143	Aqua	Shenandoah Borough Municipal Authority	Schuylkill	Water	10/06/22	02/03/23	Approved	07/13/23	12,000,000	12,000,000	2,899	4,139.36
23	A-2022-3037047	PAWC-WD	Butler Area Sewer Authority	Butler	Wastewater	02/14/23	05/23/23	Approved	11/09/23	231,500,000	228,000,000	14,792	15,413.74
24	A-2022-3033138	APW	City of Beaver Falls	Beaver	Wastewater	02/17/23	Pending	Pending		41,250,000		3,197	
25	A-2021-3024058	PAWC-WD	Brentwood Borough	Allegheny	Wastewater	03/31/23	Pending	Pending		19,200,000		3,974	
26	A-2023-3039900	PAWC-WD	Towamencin Township	Montgomery	Wastewater	05/15/23	Pending	Pending		104,000,000		5,886	
27	A-2023-3041695	APW	Greenville Sewer Authority	Mercer	Wastewater	11/17/23	Pending	Pending		18,000,000		4,000	

Acronyms:

Aqua = Aqua Pennsylvania, Inc.

APW = Aqua Pennsylvania Wastewater, Inc.

PAWC = Pennsylvania-American Water Company

PAWC-WD = Pennsylvania-American Water Company - Wastewater Division

Veolia = Veolia Water Pennsylvania, Inc., formerly SUEZ Water Pennsylvania Inc.

Veolia-WD = Veolia Water Pennsylvania, Inc. - Wastewater Division, formerly SUEZ Water Pennsylvania Inc. - Wastewater Division

Table 2: Section 1329 Application Bill Analysis

Section 1329 Application Residential Bill Analysis - Base Rates Only - Assuming 3,500 Gallons of Monthly Usage/Residential Customer 12/5/2023									
#	Docket No.	Buyer	System Acquisition/Rate Zone	Sale Complete?	Total Bill (Customer Charge + Usage Charge)			Notes	
					Initial Bill	Current Bill	Difference Bill \$	Difference Bill %	
1	A-2016-2580061	APW	New Garden Township Municipal Authority	Yes	65.45	126.87	61.42	93.8%	
2	A-2017-2605434	APW	Limerick Township	Yes	34.61	73.98	39.37	113.8%	
3	A-2017-2606103	PAWC-WD	Municipal Authority of the City of McKeesport	Yes	49.83	114.93	65.10	130.6%	
4	A-2018-3001582	APW	East Bradford Township	Yes	68.09	98.69	30.60	44.9%	(3)
5	A-2018-3002437	PAWC-WD	Sadsbury Township	Yes	74.63	114.93	40.30	54.0%	
6	A-2018-3003517	Veolia-WD	Mahoning Township Wastewater	Yes	56.20	56.20	-	0.0%	(4)
7	A-2018-3003519	Veolia	Mahoning Township Water	Yes	28.12	28.12	-	0.0%	(4)
8	A-2018-3004933	PAWC-WD	Exeter Township	Yes	43.11	114.93	71.82	166.6%	
9	A-2019-3006880	PAWC	Steelton Borough Authority	Yes	29.65	73.88	44.23	149.2%	
10	A-2019-3008491	APW	Cheltenham Township	Yes	34.58	58.15	23.57	68.2%	
11	A-2019-3009052	APW	East Norriton Township	Yes	35.25	62.61	27.36	77.6%	
12	A-2019-3014248	PAWC-WD	Kane Borough Municipal Authority	Yes	51.01	113.50	62.49	122.5%	
13	A-2019-3015173	APW	Delaware County Regional Water Control Authority	No					(5)
14	A-2020-3019634	PAWC-WD	Royersford Borough	Yes	30.00	52.70	22.70	75.7%	
15	A-2020-3019859	PAWC	Valley Township	Yes	28.96	56.00	27.04	93.4%	
16	A-2020-3020178	PAWC-WD	Valley Township	Yes	60.79	114.93	54.14	89.1%	
17	A-2020-3021460	PAWC-WD	Upper Pottsgrove Township	Yes	65.00	106.00	41.00	63.1%	
18	A-2021-3024267	APW	Lower Makefield Township Sewer Authority	Yes	68.83	68.83	-	0.0%	(4)
19	A-2021-3024681	PAWC-WD	York City Sewer Authority	Yes	32.06	59.06	27.00	84.2%	
20	A-2021-3026132	APW	East Whiteland Township	Yes	33.33	33.33	-	0.0%	(4) (6)
21	A-2021-3027268	APW	Willistown Township	No					(5)
22	A-2022-3034143	Aqua	Shenandoah Borough Municipal Authority	Yes	54.36	54.36	-	0.0%	(4)
23	A-2022-3037047	PAWC-WD	Butler Area Sewer Authority	No					(5)
24	A-2022-3033138	APW	City of Beaver Falls	No					(5)
25	A-2021-3024058	PAWC-WD	Brentwood Borough	No					(5)
26	A-2023-3039900	PAWC-WD	Towamencin Township	No					(5)
27	A-2023-3041695	APW	Greenville Sewer Authority	No					(5)

Notes and Sources:

(1) Initial bills were calculated using the compliance tariffs filed at the end of each docketed proceeding. Current bills were calculated using tariffs on each Company's website on 11/29/2023. Bills calculations include customer and usage charges only, excluding surcharges (i.e., DSIC, STAS, TCJA, etc.).

(2) Certain rate zones use, or used, minimum or flat rates, where customer charges include a usage allowance of either a designated usage amount or unlimited usage, and which may result in \$0 in billed usage charges. Usage allowance reductions typically result in customer charge decreases that are offset by usage charge increases.

(3) This is the rate for residential single-family homes only, excluding residential townhomes.

(4) This rate zone hasn't been included in a base rate case proceeding filed with the Commission.

(5) Bill analyses aren't available for these rate zones since these transactions haven't closed.

(6) This is the rate for APW's East Whiteland Township Rate Districts A & B only, excluding APW's East Whiteland Township Rate Districts C, D, and E.

Aqua = Aqua Pennsylvania, Inc.
APW = Aqua Pennsylvania Wastewater, Inc.
PAWC = Pennsylvania-American Water Company
PAWC-WD = Pennsylvania-American Water Company - Wastewater Division
Veolia = Veolia Water Pennsylvania, Inc., formerly SUEZ Water Pennsylvania Inc.
Veolia-WD = Veolia Water Pennsylvania, Inc. - Wastewater Division, formerly SUEZ Water Pennsylvania Inc. - Wastewater Division

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December 6, 2023

The Honorable Robert Matzie, Chairman

House Democratic Consumer Protection, Technology & Utilities Committee

202 Irvis Office Building,

Harrisburg, PA 17120

Dear Chairman Matzie:

I write to submit this testimony in support of HB1862, HB1863, HB1864 and HB1865. Thank you for your leadership in calling a hearing on these important bills, which I am proud to co-sponsor.

In my district, in Delaware County, we have been fighting Aqua America's attempt to take over the Chester Water Authority. Over 200,000 residents and businesses in Delaware and Chester County receive their water from this award-winning public water authority and the board and customers oppose this sale.

This takeover attempt has made possible by changes to the law made in Act 12 of 2016. Over the past seven years, it has become clear to me that we need to reform Act 12 and this package of bills would make much-needed changes. The legislative intent of the bill that became Act 12 was to help distressed water systems and their communities, allowing companies to pay more for a system than it was actually worth in order to have the resources to fix the failing infrastructure of the distressed system. However, big publicly traded water companies have used Act 12 to take over small municipal authorities across Pennsylvania, whether they were distressed or not.

The Chester Water Authority is not a distressed system, yet it is under threat of a takeover because of Act 12. If a sale were to go through, not only would we lose local control, but customers could pay more for their water. According to the Consumer Advocate's testimony during a hearing of this Committee in May 2021, customer rates increased from 35% to 105% because acquisitions are being made at high premiums. When the goal is to maximize profits for corporate shareholders, customers often shoulder the burden through higher water and sewer bills.

I support this package of bills because it will place much needed guiderails on Act 12. These bills will still permit truly struggling systems to be acquired if that's in the best interest of and supported by local communities. But they will also greatly limit the amount of acquisitions of healthy systems, ease the immediate burden on ratepayers by spreading out any costs incurred, and place strict notification

requirements on both buyers and sellers from the formal inception of a sale so that ratepayers are truly part of the process.

Thank you for holding this hearing and I hope that you schedule the bills for a Committee vote as soon as possible.

Sincerely,

A handwritten signature in black ink, appearing to read "L. Krueger".

The Honorable Leanne Krueger
State Representative
161st Legislative District

Pennsylvania House of Representatives
Consumer Protection, Technology & Utilities Committee
Room G-50, Irvis Office Building, December 12, 2023

Public Hearing on Act 12 Reform

Testimony of Justin Ladner, President, Pennsylvania American Water

Good morning, and thank you to Chairman Matzie, Chairman Marshall and distinguished members of the House Consumer Protection, Technology and Utilities Committee for holding this important hearing today. My name is Justin Ladner, and I am the President of Pennsylvania American Water. For more than 135 years, we have provided water services across Pennsylvania and currently serve 2.3 million Pennsylvanians in more than 400 communities in 37 counties. We are proud to serve as the Commonwealth's largest water and wastewater utility, and we value our relationship with the General Assembly and are thankful we have been invited to provide our perspective on the package of bills before us.

Let me start by saying we are openminded to modifications to Act 12 of 2016 that will truly improve the fair valuation of systems, promote public input and transparency, and allow for sufficient and timely regulatory review, while continuing to promote the Commonwealth's policy of water and wastewater regionalization and consolidation. We are committed to participating in this discourse and continuing to be part of solutions that bring necessary investment to water and wastewater systems in Pennsylvania.

Before I get into the substance of the legislation, I think it's important that I express our fundamental disagreement with the premise that the "vast majority of Act 12 acquisitions have been of well-run and well-maintained systems, not failing or stressed" systems, and these were "healthy systems" that sold at prices "much greater than their current value." In fact, I'd say the opposite is true. The vast majority of the systems we have acquired suffered from chronic underinvestment, deferred maintenance, and regulatory non-compliance, placing customers and the environment at risk. I say this because it's important to agree what the problem is in order to work together to solve it.

Opponents of Act 12 claim the acquisition prices are responsible for higher rates. We need to make this abundantly clear, and as we have outlined to the Commission in our recent general rate case filing, our significant capital investments to upgrade and replace aging infrastructure, bring systems into compliance, and meet increasingly stringent regulations are the primary drivers of upward pressure on rates – not acquisition purchase prices. Acquisition purchases only account for approximately one-eighth of our current rate filing, so while they are a component, they are not the main driver historically nor going forward.

Furthermore, with regard to acquisition purchase prices, our company is not interested in overpaying for systems, and under the current law all purchase prices are grounded in (1) a detailed review of assets comprising a system and (2) professional valuations conducted by PUC-approved appraisers using standards established by Uniform Standards of Professional Appraisal Practice (USPAP)¹. These valuation standards are used across a number of sectors including, for example, the real estate sector, should a municipal owner choose to sell underutilized buildings. Accordingly, we could support reforms that potentially reduce purchase prices as long as they continue applying a market-based approach and allow for a timely recovery of investments.

As part of these policy discussions, we also cannot solely look at post-acquisition rate impacts in a vacuum. Rather, we must consider the full picture. Estimates provided on post-acquisition rate impacts often ignore the fact that rates would be rising for these customers due to investment needs and more stringent regulations, regardless of ownership, and would have continued to rise absent a sale, perhaps at an even greater rate. The issue of rising water and sewer rates is also not just a private sector issue; rather, municipalities across the Commonwealth are raising customer rates to address infrastructure replacement, system resiliency, and regulatory compliance needs along with higher operating costs due to inflation and the rising price of labor, supplies and commodities.

The current price control proposal in HB 1865 to cap purchase prices at 125 percent of Depreciated Original Cost (DOC) is not an appropriate valuation method, would drastically disincentivize municipal acquisitions and hamstring critically needed investment in water and wastewater systems. Determining

¹ The *Uniform Standards of Professional Appraisal Practice* (USPAP) is the generally recognized ethical and performance standards for the appraisal profession in the United States. USPAP was adopted by Congress in 1989, and contains standards for all types of appraisal services, including real estate, personal property, business and mass appraisal. Compliance is required for state-licensed and state-certified appraisers involved in federally related real estate transactions.

an asset's original cost is important if you were calculating the asset's income tax basis but is not and was never meant to be a basis for valuing assets for a present-day sale. DOC, also referred to as Net Book Value, is based on the accounting value of the system when it went into operation in many cases 75 years ago, less decades of depreciation. It is not an actual reflection of a system's value.

On many occasions, we have encountered municipalities that have depreciated assets of their water or wastewater system to zero, even though the asset is still in use. These assets, while depreciated for accounting purposes, still have real value and the seller should be compensated for that asset. That value is best determined by conducting professional appraisals by valuation experts using USPAP standards. Act 12 requires two appraisals, one commissioned by the seller and one by the buyer. The lesser of the purchase price or the average of these two appraisals is used to determine what value the utility is able to recover.

When you sell a major asset like your home, naturally, you would want the current market to determine its value and selling price. Imagine if state law limited the price you could receive for your home because an archaic accounting rule only allowed it to be sold for the original building cost, plus some improvements, minus depreciation. And when you subtract depreciation, the accounting value of your house using this model may be zero. Even though your property could receive a fair market price through bids from buyers, you may only receive a price that is far below its real market value – or even nothing at all. Using perhaps a starker example further highlighting the time value of money, the original cost to construct the Brooklyn Bridge was \$15 million in 1883; however, it is unreasonable to believe that today it is worth \$15 million less depreciation.

Prior to the passage of Act 12 when a municipal system could only be valued at DOC less contributed property for purposes of a sale, the monetary value of systems was artificially low, disadvantaging local municipalities, stifling regionalization, and delaying much-needed investments in many Pennsylvania communities. With the passage of Act 12, municipalities now receive a purchase price reflective of all assets in service within a system and their system's actual value – not an unfair windfall, as some would have you believe. Pennsylvania American Water is open to discussing market-based valuation reforms that could improve the fair valuation of systems.

Similarly, the current proposal in HB 1865 to limit Section 1329 to troubled and distressed systems would result in even more egregious and chronic under-investment in water and wastewater infrastructure than the Commonwealth is seeing today. This drastic policy change would incentivize

municipalities to drive their systems to failure before they could receive a reasonable price for selling the system to a professional company. The General Assembly should reject any proposals that incentivize such behavior, as it will even further exacerbate the epidemic of under-investment, as we've recently seen in Greene County where chronic underinvestment led to a treatment plant failure at the East Dunkard Water Authority, leaving a community without clean, reliable water. Waiting until these systems meet the legal definition of "troubled" is the most expensive way to solve a community's, and this Commonwealth's, water and wastewater challenges.

Even when systems have not met the onerous criteria of a distressed utility (See 66 PA.C.S. § 1327), I assure you that Pennsylvania American Water has acquired a number of systems where chronic municipal under-investment had resulted in sewer overflows, unreliable service and crumbling infrastructure. In McKeesport, the city and its taxpayers were facing Act 47 municipal bankruptcy, the sewer system faced significant investment needs to support regulatory compliance, and the system was illegally discharging raw sewage from dozens of homes directly into abandoned mines. In Exeter Township, the municipal wastewater plant spilled four million gallons of untreated sewage into the Schuylkill River. Whether or not to technically label these municipalities as "troubled" or "distressed" is secondary; significant private investment following decades of government under-investment is paramount. Since acquiring these systems, Pennsylvania American Water has invested \$57 million and \$19 million respectively in these two systems to upgrade aging sewer infrastructure and achieve environmental compliance.

With regard to HB 1862, we support public notification and transparency around potential acquisitions and welcome opportunities to enhance transparency throughout the acquisition process. Upon reviewing the legislation, there are some opportunities to improve the legislation to ensure the most effective outcome and to eliminate redundancy.

With regard to HB 1863, we are not in favor of eliminating the requirement that the PUC issue an order on an acquisition application within six months. Providing no required timeframe leaves both the buyer and seller with no certainty about the timing of PUC action and runs counter to PUC norms. Acquisition applications are certainly no more complex than a general utility rate case, and PUC orders are required in nine months for those cases.

With regard to HB 1864, we understand the intent of this legislation is to phase in rate increases to acquired systems over multiple rate cases. We do not disagree with this goal, and in fact, our company

frequently requests that the PUC permit rates of acquired systems to be moved toward our statewide rates over several rate cases. However, the bill would prevent acquiring utilities from recovering the full PUC-approved rate base for potentially years. We believe that this prohibition is a violation of the regulatory compact.

In closing, the Pennsylvania General Assembly passed Act 12 of 2016 in response to statewide infrastructure challenges and restrictive valuation rules to update unfair and obsolete laws that prevented municipal governments from getting a fair price for their water and wastewater assets. Without these commonsense utility valuation reforms, communities would continue to have limited options to repair and rebuild water and wastewater systems that are, in most cases, aging and in need of infrastructure improvements.

Through local democracy, many elected municipal leaders in your communities are determining that it is in the best interest of their constituents to redeploy municipal assets to more pressing needs and allow professional water companies with scale and experience to address the challenges of rebuilding and managing aging infrastructure under significant regulatory oversight. Act 12 encourages such investment by providing a tool for municipalities and their taxpayers to receive the fair market value of their assets — and in turn unlock funding to reinvest in infrastructure, retire debt, fund pensions, and address other critical local priorities.

Following a sale, these communities received professional, reliable water and/or wastewater service from a PUC-regulated utility with robust low-income customer assistance programs and a record of excellence in environmental stewardship. And, rather than diminishing oversight, the sale of municipal water and wastewater systems actually increases the regulatory scrutiny of investments in physical infrastructure, rates charged to customers, and the financial health of the utility. We look forward to continuing the conversation surrounding Act 12 reform and I certainly welcome the opportunity to answer any questions you may have.



House Consumer Protection, Technology and Utilities Committee
Public Hearing on HB 1862 P.N. 2340, HB 1863 P.N. 2341, HB 1864 P.N. 2342, and HB 1865 P.N. 2343

December 12, 2023

Testimony of:

Anthony Bellitto, Executive Director, North Penn Water Authority
Liesel Gross, Chief Executive Officer, Lehigh County Authority

Good morning, Chairman Matzie, Chairman Marshall and members of the House Consumer Protection, Technology and Utilities Committee. Thank you for your invitation to provide testimony on HB 1862 P.N. 2340, HB 1863 P.N. 2341, HB 1864 P.N. 2342, and HB 1865 P.N. 2343.

We are testifying on behalf of the Pennsylvania Municipal Authorities Association (PMAA) which represents over 700 municipal authorities across the Commonwealth, the vast majority of which provide drinking water and wastewater treatment services to more than six million citizens. If you live in Pennsylvania, you are likely within the service area of at least one authority. In addition, PMAA has over 500 associate members, such as certified public accountants, engineers, and solicitors, who provide services to authorities.

To provide some background, an authority, by virtue of the Municipality Authorities Act (MAA), is an alternate vehicle for accomplishing public purposes rather than through direct action of local governments, such as boroughs, cities, and townships. Municipal authorities may provide services to the community and finance its services by means of user fees. Authorities also commonly serve more than one municipality and in so doing provide operational efficiencies and economies of scale by serving beyond political boundaries. Irrespective of how many communities they serve, the mission of municipal authorities is to provide excellent quality, reliable, and safe services at an affordable cost to the customers of their local community, whether that be large or small. Furthermore, the operation of authority projects and services does not compete with other traditional components and associated costs of local government. To reiterate, for these reasons, the authority model is perfectly suited for providing services on a regional level.

To bolster this viewpoint, it is important to understand the governing structure of a municipal authority. Authorities can be created by any county, borough, city, or township, functioning singly or jointly with one or more other local governments. Once created, the authority manages all aspects of the authority's operation, freeing the municipality of these critical and complex responsibilities. Authorities are governed by a municipally appointed board of directors, and authority meetings are conducted in public, complying with the open meeting requirements of the Sunshine Act. It is also important to note that in the MAA, an authority cannot "duplicate or compete with existing enterprises serving substantially the same purposes." These features ensure that authorities act in a transparent manner, separated from local political influences, but governed

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locally with full public access, and operate only in the best interests of the communities they serve.

Aside from the MAA, municipal authorities are governed and regulated under numerous other state and federal laws including, but not limited to:

- Safe Drinking Water Act
- Clean Water Act
- Clean Streams Law
- Sewage Facilities Act
- Plumbing System Lead Ban and Notification Act
- Terrorism Infrastructure Disclosure Protection Act
- Public Health Security and Bioterrorism Preparedness and Response Act
- Water Resources Planning Act
- Underground Utility Line Protection Law (PA One Call)
- Water and Wastewater Systems Operators' Certification Act
- Storage Tank and Spill Prevention Act
- Construction Code Act
- Municipalities Planning Code
- Procurement Code
- Prevailing Wage Act
- Separations Act
- Public Official and Employee Ethics Law
- Public Employee Relations Act
- Right-to-Know Law
- Sunshine Act
- Municipal Records Act
- Intergovernmental Cooperation Act

In addition to state and federal laws, authorities must meet all current regulatory requirements as well as plan, prepare, and budget for future requirements once identified by state and federal agencies.

In 2016, the Pennsylvania General Assembly passed Act 12 which added Section 1329 to Title 66 (Public Utilities). Section 1329 established a system called “fair market value” for the acquisition of municipal water and wastewater systems by investor-owned utilities. Act 12 contained no provisions that provided for any limitations on municipal acquisitions. As a result, “fair market value” allows for both negotiating parties to increase the purchase price as high as possible. To date, almost all approved acquisitions far exceeded the net original cost of the system. As these acquisitions continue under Section 1329, the most prevalent impact to Pennsylvania ratepayers is increased rates. Because of this, any tightening or further restrictions to Act 12 is a step in the right direction and so PMAA generally supports Chairman Matzie’s legislative package.

HB 1862 amends Title 66 (Public Utilities), in rates and distribution systems, further providing for acquisition of water and sewer utilities by imposing new enhanced and increased public notification and participation requirements on all parties.

We particularly like this attempt to engage the community by requiring public advertisement of the proposed sale, and public participation in the process, publishing proposed rate adjustments prior to a sale, holding public hearings, establishing a public comment period on the request for proposals and imposing associated timeframes.

HB 1863 amends Title 66 (Public Utilities), in rates and distribution systems, further providing for valuation of acquired water and wastewater systems by eliminating the Public Utility Commission (PUC) six-month evaluation deadline.

We support this language as it provides the PUC with more time to consider the substantial implications of an acquisition.

HB 1864 amends Title 66 (Public Utilities), in rates and distribution systems, further providing for valuation of acquired water and wastewater systems by requiring any rate increase after an acquisition be incorporated into the rate base over three separate base rate cases.

Section 1329 (c)(4) in the proposed legislation requires the acquiring entity to incorporate its proposed rate increases between the depreciated original cost and the rate base of the selling utility over three rate base cases. Although this may slow down the proposed rate shock to the customers, it would only minimally impact the investor-owned utilities because once the sale is finalized, the revenue is going to be perpetual and eventually they will recoup their investment. Although delayed, ultimately, they recognize their initial investment, and the customer shock of the new rate is deferred for a short time until rates can be increased, which will continue indefinitely.

HB 1865 amends Title 66 (Public Utilities), in rates and distribution systems, further providing for valuation of acquired water and wastewater systems by capping any purchase price for a system at 125% of the depreciated original cost.

While we appreciate the intent, the 125% valuation cap gives us some pause. First, it appears to be somewhat of a compromise between the old depreciated original cost concept and the Act 12 “fair market value” analysis. More importantly, however, is the reliance on Section 1327(a)(3) of the Public Utility Code in determining whether a system is indeed distressed. This particular section provides for too much unfettered discretion in determining whether a system is distressed.

In conclusion, it is important to note that Section 1327, the previously and still used acquisition law, includes a provision for acquisitions above depreciated cost. Key features in Section 1327 are protections from rate increases to existing customers, burden of proof of distress on the investor-owned utility, and statutory amortization of purchase price in excess of depreciated cost. Under Section 1329, for-profit utilities can presumably keep these high purchase prices in their rate base forever. As a result, there has been a shift from acquisitions of distressed systems to those systems that are well funded and have excellent system integrity.

Again, thank you for the opportunity to testify before you today. We are happy to answer any questions.

**BEFORE THE
PENNSYLVANIA HOUSE OF REPRESENTATIVES
COMMITTEE ON CONSUMER PROTECTION,
TECHNOLOGY AND UTILITIES**

Testimony Of

**PATRICK M. CICERO
CONSUMER ADVOCATE**

Regarding

**House Bills 1862, 1863, 1864, and 1865 amending
Sections 1327 and 1329 of the Public Utility Code**

**Harrisburg, Pennsylvania
December 12, 2023**

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**Members of the Pennsylvania House of Representatives
Committee on Consumer Protection, Technology and Utilities**

My name is Patrick Cicero and I have the privilege of serving as Pennsylvania's Consumer Advocate. Thank you for the opportunity to provide feedback and comments this morning about House Bills 1862, 1863, 1864, and 1865 and the necessary changes to Section 1329 of the Public Utility Code. My office, the Pennsylvania Office of Consumer Advocate (OCA), was created in 1976 to serve as an advocate for Pennsylvania consumers before the Public Utility Commission (PUC). At the outset, I want to add that I support each of the bills that will be discussed at today's meeting. In total, they would help to mitigate the harms that have occurred because of Act 12 of 2016 which added Section 1329 to the Public Utility Code. I will discuss the particulars of each bill in this written testimony, but before I do so, I will provide an overview of the harm that has occurred to consumers and ratepayers since Act 12's enactment. I will also urge the Committee and the General Assembly to consider a full repeal of Act 12. As I will outline, it has wrought significant harm, little to no benefit to consumers or the public, and should be repealed.

Background

Section 1329 of the Public Utility Code (66 Pa. C.S. § 1329) was added through Act 12 of 2016 and changed the method and timing for calculating what is included in utility rates for specific acquisitions of municipal water and wastewater acquisitions by regulated public utilities. The result has been a significant increase in rates for customers of both the acquired and acquiring systems. In fact, water and wastewater rates have increased at the fastest pace of all utility rates over the past several years and these increases have been driven, in no small part, by acquisitions filed seeking a valuation under Section 1329. Water rates for the two largest companies in Pennsylvania are between \$880 -\$1,100 dollars per year for households using between 3,600 – 5,000 gallons each month and if the customer is also a wastewater customer of the utility, they

would be paying an additional \$1,070 - \$1,590 per year. This means that combined water and wastewater customers of each of the largest two utilities are paying \$1,950 - \$2,690 per year for water and wastewater at relatively modest usage levels of 3,600-5,000 gallons per month. Many households use considerably more and, thus, their bills would be substantially higher. Customers of regulated water and wastewater utilities often pay as much or more each year for those utilities than they pay for electricity and natural gas.

Since Section 1329 was added to the Public Utility Code there have been twenty (21) approved acquisitions that have proceeded to closing. In our view, none of these approved acquisitions have been troubled or non-viable systems. As shown below, the twenty-one acquisitions have a combined ratemaking rate base of more than \$1 billion, which is approximately 2x the depreciated original cost of the acquired systems' assets of approximately \$538 million.

Table 1: Summary of Section 1329 (Ratemaking Rate Base vs. Depreciated Original Cost)

Seller	Buyer	Type of System	Ratemaking Rate Base	Depreciated Original Cost
New Garden	Aqua PA	Wastewater	\$ 29,500,000	\$ 18,567,728
Limerick	Aqua PA	Wastewater	\$ 64,373,378	\$ 46,153,867
McKeesport	PAWC	Wastewater	\$ 158,000,000	\$ 80,085,602
East Bradford	Aqua PA	Wastewater	\$ 5,000,000	\$ 5,473,948
Sadsbury	PAWC	Wastewater	\$ 8,300,000	\$ 7,480,573
Mahoning	SUEZ	Water	\$ 4,734,800	\$ 3,507,138
Mahoning	SUEZ	Wastewater	\$ 4,765,200	\$ 3,234,859
Exeter	PAWC	Wastewater	\$ 92,000,000	\$ 40,057,634
Steelton	PAWC	Water	\$ 20,500,000	\$ 14,433,435
Cheltenham	Aqua PA	Wastewater	\$ 44,558,259	\$ 15,408,458
East Norriton	Aqua PA	Wastewater	\$ 20,750,000	\$ 8,407,007
Kane	PAWC	Wastewater	\$ 17,560,000	\$ 12,070,455
Royersford	PAWC	Wastewater	\$ 13,000,000	\$ 5,173,559
Valley	PAWC	Water	\$ 7,325,000	\$ 5,370,438
Valley	PAWC	Wastewater	\$ 13,950,000	\$ 9,214,738
Upper Pottsgrove	PAWC	Wastewater	\$ 13,750,000	\$ 8,970,325
Lower Makefield	Aqua PA	Wastewater	\$ 53,000,000	\$ 19,808,274
East Whiteland	Aqua PA	Wastewater	\$ 54,413,635	\$ 33,403,972
City of York	PAWC	Wastewater	\$ 231,500,000	\$ 97,106,105
Shenandoah	Aqua PA	Water	\$ 12,000,000	\$ 10,784,743
Butler Area Sewer	PAWC	Wastewater	\$ 228,000,000	\$ 93,409,083
TOTAL			\$ 1,096,980,272	\$ 538,121,941

¹Depreciated original cost is shown without considering the "original source of funding" pursuant to Section 1329; i.e. contributions have not been deducted.

By our office's conservative estimate, because of these acquisitions and directly due to the fair market value embedded into Section 1329, consumers are or will be required to pay in excess of **\$85 million more each year for water and wastewater service than they would have without Section 1329**. This amount will only increase because as of the filing of this testimony, there are five more acquisitions that have started the process of Public Utility Commission (PUC) review which if approved as filed would add an additional \$19.4 million in added annual costs.

Table 2. Annual Revenue Requirement Deficiency of Approved and Pending Acquisitions

ANNUAL REVENUE REQUIREMENT DEFICIENCY					
Aqua	New Garden	\$ 1,662,142	PAWC	McKeesport	\$ 16,737,759
Aqua	Limerick	\$ 7,778,000	PAWC	Sadsbury	\$ 94,062
Aqua	East Bradford	\$ 0	PAWC	Exeter	\$ 5,378,000
Aqua	Cheltenham	\$ 2,772,000	PAWC	Steelton	\$ 1,117,000
Aqua	East Norriton	\$ 1,155,000	PAWC	Kane	\$ 1,265,000
Aqua	Lower Makefield	\$ 2,828,000	PAWC	Royersford	\$ 1,210,343
Aqua	East Whiteland	\$ 5,011,000	PAWC	Upper Pottsgrove	\$ 1,002,000
Aqua	Shenandoah W	\$ 865,031	PAWC	Valley W	\$ 1,697,000
Veolia	Mahoning W	\$ 492,666	PAWC	Valley WW	\$ (1,413,000)
Veolia	Mahoning WW	\$ 114,651	PAWC	City of York	\$ 17,557,000
				PAWC	BASA
					\$ 17,895,000
TOTAL ANNUAL REVENUE DEFICIENCY					\$ 85,218,654
PENDING CASES					
Aqua	DELCORA	\$ 4,553,000	PAWC	Brentwood	\$ 664,000
Aqua	Beaver Falls	\$ 4,288,000	PAWC	Towamencin	\$ 7,731,000
Aqua	Greenville Sewer	\$ 2,230,000	PAWC		
TOTAL PENDING ANNUAL REVENUE DEFICIENCY					\$ 19,466,000

When the General Assembly passed Act 12 many of the municipal owners of water and wastewater systems faced the same state and federal regulatory requirements and aging infrastructure that the investor-owned utilities faced. They all face these challenges today. Even though municipal entities and municipal authorities can finance infrastructure at a lower cost to ratepayers than investor-owned utilities,¹ there was a concern expressed about municipalities facing large costs to maintain and upgrade their water and wastewater systems. H. Journal, 199th Leg. – No. 71 at 1773 (Oct. 19, 2015). However, there was no provision contained within Act 12 that provided for any limitation on municipal acquisitions either in terms of the costs that could be assessed to ratepayers or any limitation that only troubled systems could be acquired.

My office did not support Act 12 when it passed, and I do not support Section 1329 today. Let me be clear, neither I nor my office is and has ever been against the consolidation of water and wastewater utilities or the acquisition of municipal systems by investor-owned utilities in the abstract or in principle. We are not anti-privatization, and we are not against well thought out consolidation or regionalization. What we oppose is privatization for its own sake and privatization and consolidation regardless of the cost to consumers. Systems bought at reasonable prices that are reflective of depreciated original cost and that are designed with economic efficiency and regulatory compliance in mind can provide a benefit to existing and acquired ratepayers, as well as provide important environmental benefits that ensure clean and potable water for all. Also, the acquisition of troubled, small systems that has occurred in Pennsylvania since 1990 pursuant to Section 1327 of the Public Utility Code has successfully brought many small systems under the

¹ Municipalities or municipal authorities, as government-owned utilities, do not pay income taxes and can usually issue bonds at a lower interest rate than for profit companies. As a result, most municipalities and municipal authorities have lower rates than investor-owned utilities.

professional management of our large investor-owned utilities and improved the safety and reliability of water service to thousands of Pennsylvania residents.

Another measure of the impact of these acquisitions on customers is to assess the average plant cost per customer for the acquired system as compared to the utilities' average plant cost per customer before the acquisitions began. For example, the average rate base per customer for both Aqua Pennsylvania (Aqua) and for Pennsylvania American Water Company (PAWC) have grown significantly since 2016 as reflected in the table below.

Table 3: Aqua's Average Rate Base Per Customer

Average Rate Base per Customer 2016		Average Rate Base per Customer 2022		Percentage Increase 2016 to 2022
Aqua Pa Wastewater:	\$3,795	Aqua Pa Wastewater	\$9,449	249%
Aqua Pa Water:	\$7,177	Aqua Pa Water:	\$9,812	137%

Table 4: PAWC's Average Rate Base Per Customer

Average Rate Base per Customer 2016		Average Rate Base per Customer 2022		Percentage Increase 2016 to 2022
PAWC Wastewater:	\$7,162	PAWC Wastewater:	\$12,458	174%
PAWC Water:	\$5,565	PAWC Water:	\$7,423	133%

The average rate base per customer for Section 1329 acquisitions approved to date is shown in

Table 5, below.

Average Rate Base per Customer				
	Acquired Utility	1329 Allowed Rate Base	Number of Customers	Average Rate Base per Customer
Aqua Purchases	New Garden A-2016-2580061	\$29,500,000	2,106	\$14,008
	Limerick A-2017-2605434	\$64,373,378	5,434	\$11,846
	East Bradford A-2018-3001582	\$5,000,000	1,248	\$4,006
	Cheltenham A-2019-3008491	\$44,558,259	10,219	\$4,360
	East Norriton A-2019-3009052	\$20,750,000	4,966	\$4,178
	Lower Makefield A-2021-3024267	\$53,000,000	11,151	\$4,753
	East Whiteland A-2021-3026131	\$54,413,635	3,895	\$13,970
	Shenandoah A-2022-3034143	\$12,000,000	2,899	\$4,139
Total		\$283,595,272	41,918	\$7,658
PAWC Purchases	McKeesport A-2017-2606103	\$158,000,000	12,780	\$12,363
	Sadsbury A-2018-3002437	\$8,300,000	998	\$8,317
	Exeter A-2017-3004933	\$92,000,000	9,015	\$10,205
	Steelton (Water) A-2019-3006880	\$20,500,000	2,415	\$8,489
	Kane A-2019-3014248	\$17,560,000	2,019	\$8,697
	Royersford A-2020-3019634	\$13,000,000	1,620	\$8,025
	Upper Pottsgrove A-2020-3021460	\$13,750,000	1,447	\$9,502
	Valley (Water) A-2020-3019859	\$7,325,000	1,670	\$4,386
	Valley (Wastewater) A-2020-3020178	\$13,950,000	3,125	\$4,464
	City of York A-2021-3024681	\$231,500,000	13,747	\$16,840
	Butler Area Sewer A-2022-3037047	\$228,000,000	14,792	\$15,414
	Total	\$575,885,000	63,628	\$9,129

The higher the average rate base cost per customer, the higher rates will need to go to support these acquisitions.

All of the data that I presented above paints an increasingly grim and accurate picture that Section 1329 created an incentive for investor-owned water and wastewater utilities to purchase municipal utilities at significantly inflated prices to the detriment of consumers. In short, Act 12 has been a financial disaster for customers and has not materially or substantially improved service. In my view, the best path forward would be to put a halt to municipal acquisitions at fair market value and arrive at a more targeted approach to these acquisitions that is fair to ratepayers and the communities seeking to sell the assets.

OCA Primary Recommendation: Repeal Section 1329

Given the other mechanisms available for utilities to increase their rate base and profits by acquiring systems and replacing and repairing infrastructure and due to the inherent problems with Section 1329, the OCA recommends Section 1329 be repealed. I recognize that there is currently no repeal bill before this Committee, but I would urge the Committee to consider such a bill. In my view, section 1329 is not necessary because other provisions of the Public Utility Code exist to incentivize and reward utilities for acquisitions of small or non-viable systems that are not maintaining adequate, safe, reliable or efficient service.

For example, Section 1327(a) of the Public Utility Code allows a utility that acquires a small or troubled water or wastewater system to request a return on and a return of the excess of acquisition costs over the depreciated original cost of the acquired system if specified criteria are satisfied. Section 523 authorizes the PUC to increase the allowed return on equity by additional basis points as a reward or incentive for utility acquisitions. This premium is available for an acquisition that does not meet the criteria of Section 1327(a). In addition, existing provisions of the Public Utility Code incentivize and reward utilities for replacing and repairing infrastructure.

Section 315(e) was revised in 2012 to create an exception to test year requirements to allow utilities to set base rates to recover in advance investment that will not be made for up to one year after rates take effect. The Distribution System Improvement Charge (DSIC) has been available to water utilities since 1999 and expanded to wastewater utilities in 2012. The DSIC allows water and wastewater utilities to recover a return of and on their investment in distribution system improvement projects through a surcharge on utility bills (5% or 7.5% of the total bill). *See* 66 Pa. C.S. §§ 1350-1360. Section 1311(b) was added in 2018 and allows utilities to add to rate base and earn a profit on investment in replacing certain customer-owned lead water service lines or damaged wastewater laterals.

The framework of Section 1329 is simply not necessary for either the protection of the public or for well-coordinated or regionalized systems.

Secondary OCA Recommendation: Sunset and Review

If the General Assembly does not believe that it has sufficient information to completely repeal Act 12 at this stage, it should consider adding a sunset provision to Section 1329 and a legislative review by the Legislative Budget and Finance Committee (LBFC) about the impact that Act 12 of 2016 has had on consumer rates as well as whether it has produced a substantial affirmative benefit to the public. Act 12 has been in place since 2016 and has not been thoroughly reexamined considering the full impact of the acquisitions since that time. If the General Assembly needs more information about whether it should be repealed or amended, it should add a sunset provision and a required review by the LBFC. The OCA suggests a bill with following language could be added:

1329.1 – Legislative Review and Expiration.

Section 1329 shall expire on December 31, 2026. By no later than June 30, 2025, the Legislative Budget and Finance Committee shall prepare a comprehensive report concerning the impact that Section 1329 has had on the utility rates paid by water and wastewater customers across the Commonwealth.

Discussion of Bills before the Committee

While the OCA's primary and secondary recommendations above address issues that are not currently before the Committee, the OCA supports the bills that are currently before the Committee as they would seek to restrain the excesses of the current paradigm. I will discuss each bill in turn except that I will discuss HB 1862 last as it deals with a separate set of issues than the other three bills.

House Bill 1863

House Bill 1863 would remove the 6-month statutory requirement that the Commission issue a final order from the date an application is submitted that meets the requirements of Section 1329. The OCA fully supports this bill as drafted. The current process whereby the Commission must issue an order within 6 months of acceptance of an application has produced ridiculously short litigation time frames for the parties. This is because of the 6-month time frame, the Commission itself (between the Office of Administrative Law Judge, the other advisory bureaus of the Commission and the Commissioners' offices) take 2 ½ - 3 months from the date the Reply Briefs are due by the parties, leaving the parties very little time to develop a record. It is the typical pattern in cases where valuation is established under Section 1329, for the direct testimony of parties to be due a mere few days after the pre-hearing conference and parties often litigate the

case and close the record within 45 days of a prehearing conference. This is simply not enough time to allow for proper litigation. Furthermore, the 6-month clock has required the Commission to hold final acceptance of applications until its Bureau of Technical Utility Services completes its initial review. During this liminal time, after the utility files and before the Commission finally accepts, other parties, including my office, cannot conduct formal discovery and we cannot compel the utilities to cooperate in sending our office any information. While the utilities have in the past voluntarily provided informal discovery, their cooperativeness in doing so is at their whim and pleasure rather than a requirement afforded to parties to a case. Furthermore, to the extent that disputes arise during this time the Commission has not adjudicated those disputes based on the assertion that the docket is not active until they finally accept. Each of these machinations is the result of a 6-month clock that does not leave appropriate time for a full and proper review.

It is important to note that when electing to proceed under Section 1329, a utility is required to file an application for approval of an acquisition pursuant to Sections 1102 and 1103 of the Public Utility Code. Those sections require that the Commission can only approve the acquisition if it will “affirmatively promote the ‘service, accommodation, convenience, or safety of the public’ in some substantial way.” *City of York v. Pa. P.U.C.*, 295 A.2d 825, 828 (Pa. 1972). This is the same test and standard that is used for all applications for service in a new service territory, to expand a service territory, for applications for one utility to acquire another, and for applications that would result in mergers or internal reorganizations. None of those other proceedings where Section 1329 valuation is not in play has any statutory deadline and the Commission evaluates the case on its merits.

The OCA submits that there is no reason for there to be any statutory deadline on any application brought under Section 1329, and, in fact, Section 1329 applications are particularly

problematic cases to impose a short adjudicatory time period. Under normal circumstances, when one utility is buying another utility, the parties to that proceeding have the right in a future rate case to challenge the amount of rate making rate base that is put into the acquiring utilities final rate base. This is not the case under Section 1329 because the statute defines that the rate making rate base for purposes of ratemaking is the lesser of the purchase price or the average of the two fair market value appraisals. 66 Pa. C.S. § 1329(c)(2). In my view, the Commission's balancing act is more challenging in these cases not less and, thus, it makes little sense to constrain the time frame in which the Commission and the parties must litigate the case. The OCA fully supports HB 1863. It would improve the administrative processes at the Commission, it would provide a more realistic framework for the adjudication of these critical issues, and it would not harm either the buying or selling utilities. There is simply no urgency to these cases other than the false sense of urgency that may be created by utilities.

House Bill 1864

House Bill 1864 would, working in conjunction or in isolation with the changes proposed by House Bill 1865, constrain the excesses of these purchases that would have to be paid by ratepayers. If enacted, HB 1864 would spread out the total dollar amount that could be put into rate base during the first rate case post-closing. It would in essence allow a utility to put into rate base the depreciated original cost of the acquisition immediately in the first case. It is important to remember that in this context, as used in Section 1329, the term "depreciated original cost" does not take into consideration the original source of funding for the utility plant which means that grants or other contributions are treated the same as if it was paid for even where the contribution did not cost the selling utility anything. Contributed plant is not deducted. This has the effect of increasing depreciated original cost from what it has been traditionally. This in and of itself is a

benefit to both the selling and buying utility because the seller can sell it at a higher dollar amount and the buyer can put a higher amount into rates and earn a return on and of plant that was built/constructed by the seller at no cost. This is a statutory ratemaking fiction that increases costs to consumers, but it is a part of Section 1329.

House Bill 1864 would retain this fiction and allow the full amount of the depreciated original cost to be put into rates in the first case. Anything above that amount – the difference between the approved 1329 ratemaking rate base amount and 1329 depreciated original cost – would have to be spread out over the next three rate cases of the utility. An example may prove illustrative. In the recently approved acquisition by PAWC of the Butler Area Sewer Authority, the Commission approved a ratemaking rate base of \$228,000,000. The depreciated original cost under 1329 of that system was \$93,409,083. The difference between these two is \$116,761,353. If House Bill 1864 were enacted prior to the Butler acquisition, PAWC would have been able to put into rate base and earn a return on and of the \$93,409,083 in its first-rate case post-closing but it would be required to add the remaining \$116,761,353 into rate base equally over the next three rate cases. This would require PAWC and its shareholders to carry the cost of this additional amount above the depreciated original cost for longer than they do currently and would help ratepayers by spreading out premium purchase price above depreciated original cost over a longer period. It would constrain rate shock from these acquisitions. In the OCA's view, over the long run this will likely shrink the delta between purchase prices and depreciated original costs because the utilities are not going to want to carry significant amounts of excessive purchase prices for longer periods of time. This would be a net benefit to ratepayers but would still provide significant value to the utilities because they could put into rate base a higher amount than they could pre-1329 and would be assured, over the long term, a return of and on their investment.

I think it is important to clarify that the OCA takes no position on the price a buyer can or should pay or a seller can or should sell its utility plant. The issue is what amount can be put into rate base and paid for by customers versus what amount should be paid for by the acquiring utility. Utilities have often paid more than book value to acquire systems. For example, when Essential Utilities, the parent company of Aqua Pennsylvania purchased Peoples Gas in March 2020 (PUC Order entered January 24, 2020), it paid \$2 billion over book value, or 87% over the net book value of the company at the time, but it was only allowed to put into ratemaking rate base the net book value of the Company. It did not get to recover from ratepayers that amount above net book value. The changes proposed by HB 1864 would still allow the utility to recover more than its depreciated original cost amount, it would just spread it out over a longer period. The OCA supports that approach especially if twinned with the changes proposed in House Bill 1865.

House Bill 1865

House Bill 1865 would amend § 1329(c) and would add an additional protection for ratepayers that would constrain the amount ratepayers would have to pay above depreciated original cost for non-troubled systems. Like HB 1864, this bill would maintain the higher calculation for determining depreciated original cost that is currently in § 1329(d)(5), but it would cap the amount that a utility could put into ratemaking rate base as the lesser of: (1) the purchase price negotiated by the acquiring public utility and selling utility; (2) the fair market value of the selling utility; or (3) 125% of the depreciated original cost as calculated under subsection (d)(5) if the acquisition does not meet the requirements of Section 1327(a)(2) or (3). In effect, this would continue to encourage the acquisition of troubled systems that meet the defined statutory criteria outlined in Section 1327(a)(2) and (3) by not imposing the 125% cap on those systems. Systems that are not troubled would still be able to be bought at a premium, but the amount that could be

put into rate base would be capped. This change would make a significant difference to consumers but would not otherwise disincentivize the acquisition of troubled systems. Below is a table that shows (1) what was added to ratemaking rate base (Column A) because of the approval of the application (2) the amount of the 125% of depreciated original cost (Column C), and (3) the amount that would be added to ratemaking rate base had HB 1865 been in place (Column D).

Table 6 - Ratemaking Rate Base vs. Dep. Orig. Cost vs. 125% of Dep. Orig. Cost

Seller	Buyer	Type of System	A	B	C	D
			Ratemaking Rate Base	Depreciated Original Cost	125% Depreciated Original Cost	Lesser of Column A or C
New Garden	Aqua PA	Wastewater	\$ 29,500,000	\$ 18,567,728	\$ 23,209,660	\$ 23,209,660
Limerick	Aqua PA	Wastewater	\$ 64,373,378	\$ 46,153,867	\$ 57,692,334	\$ 57,692,334
McKeesport	PAWC	Wastewater	\$ 158,000,000	\$ 80,085,602	\$ 100,107,003	\$ 100,107,003
East Bradford	Aqua PA	Wastewater	\$ 5,000,000	\$ 5,473,948	\$ 6,842,435	\$ 5,000,000
Sadsbury	PAWC	Wastewater	\$ 8,300,000	\$ 7,480,573	\$ 9,350,716	\$ 8,300,000
Mahoning	SUEZ	Water	\$ 4,734,800	\$ 3,507,138	\$ 4,383,923	\$ 4,383,923
Mahoning	SUEZ	Wastewater	\$ 4,765,200	\$ 3,234,859	\$ 4,043,574	\$ 4,043,574
Exeter	PAWC	Wastewater	\$ 92,000,000	\$ 40,057,634	\$ 50,072,043	\$ 50,072,043
Steelton	PAWC	Water	\$ 20,500,000	\$ 14,433,435	\$ 18,041,794	\$ 18,041,794
Cheltenham	Aqua PA	Wastewater	\$ 44,558,259	\$ 15,408,458	\$ 19,260,573	\$ 19,260,573
East Norriton	Aqua PA	Wastewater	\$ 20,750,000	\$ 8,407,007	\$ 10,508,759	\$ 10,508,759
Kane	PAWC	Wastewater	\$ 17,560,000	\$ 12,070,455	\$ 15,088,069	\$ 15,088,069
Royersford	PAWC	Wastewater	\$ 13,000,000	\$ 5,173,559	\$ 6,466,949	\$ 6,466,949
Valley	PAWC	Water	\$ 7,325,000	\$ 5,370,438	\$ 6,713,048	\$ 6,713,048
Valley	PAWC	Wastewater	\$ 13,950,000	\$ 9,214,738	\$ 11,518,423	\$ 11,518,423
Upper Pottsgrove	PAWC	Wastewater	\$ 13,750,000	\$ 8,970,325	\$ 11,212,906	\$ 11,212,906
Lower Makefield	Aqua PA	Wastewater	\$ 53,000,000	\$ 19,808,274	\$ 24,760,343	\$ 24,760,343
East Whiteland	Aqua PA	Wastewater	\$ 54,413,635	\$ 33,403,972	\$ 41,754,965	\$ 41,754,965
City of York	PAWC	Wastewater	\$ 231,500,000	\$ 97,106,105	\$ 121,382,631	\$ 121,382,631
Shenandoah	Aqua PA	Water	\$ 12,000,000	\$ 10,784,743	\$ 13,480,929	\$ 12,000,000
Butler Area Sewer	PAWC	Wastewater	\$ 228,000,000	\$ 93,409,083	\$ 116,761,354	\$ 116,761,354
TOTAL			\$ 1,096,980,272	\$ 538,121,941	\$ 672,652,426	\$ 668,278,346

None of the acquisitions approved so far would have likely met the § 1327(a)(2) or (3) criteria because none were troubled systems, thus all of them – except a few where the purchase price was less than 125% of the depreciated original cost – would have been subject to the cap. As you can see from **Table 6**, under the current paradigm \$1,096,980,272 was or will be added to the acquiring utility's ratemaking rate base as compared to \$668,278,346 had HB 1865 been in place. This is a difference of \$428,701,926 or 39%. While my office has not calculated the revenue requirement difference between these two different rate bases, it is fair to predict that this change alone would have saved ratepayers tens of millions of dollars each year. Of course, even the \$668.2

million of ratemaking rate base would be more than the utilities would have received in the absence of 1329. The OCA supports HB 1865 – especially if enacted in conjunction with HB 1864 – as a means of capping the excessive purchase prices that ratepayers are asked to pay for the acquisitions of non-troubled systems. As is the case with HB 1864, nothing would prevent a utility for paying anything it wants for another utility, but in so doing it would have to make more informed and strategic choices because its shareholders would bear the costs associated with the acquisition above a certain threshold.

House Bill 1862

House Bill 1862, unlike the other bills, would amend Section 1327 rather than Section 1329 and would do so by adding a new section that would impose certain duties on a selling municipal corporation to issue certain notices, and the Commission to hold public hearings, where an acquiring utility elects to put into rate base immediately – as opposed to in a subsequent rate case – the amount of its purchase price as well as the positive acquisition adjustment. Section 1327 is not like Section 1329 as it does not add a fair market value premium to rates, but rather allows an acquiring utility to seek an upwards adjustment if it purchases a utility for more than its book value depending on the condition of the system. This acquisition adjustment has been a “carrot” that is meant to entice a utility to buy a non-viable system that was not providing safe, adequate or reliable service. The changes proposed in HB 1862 would require certain notice and valuation provisions to be provided if a utility seeks to have the amount added to rate base immediately rather than in the next rate case. The OCA supports the additions contained in HB 1862, though it notes that it does not correct or otherwise adjust what occurs pursuant to Section 1329. Nevertheless, the changes proposed would provide additional clarity, protection, and a voice to consumers who are being served by small or non-viable systems that are not currently providing safe, adequate, or

reliable service. There are several, small technical changes to the bill that the OCA believes would improve clarity that the Committee may want to consider prior to passage, those are noted below:

- In Section (a.1)(2), the OCA recommends adding “social media” to the list of required notice for the request for proposals;
- In Section (a.1)(4), the phrase “estimates of the rates” is likely too vague. The OCA recommends specifications for "rates" or the median system usage (not typical usage) in 3 years, 6 years and 9 years or over the first 10 years of ownership (rather than one point in time), and for the public utility's residential, commercial, and industrial classes. The OCA also recommends that there be a requirement to include a link to a rate calculator hosted on the buying systems' website that allows a household to enter the specifics of their household usage to see what their estimate of rates will be.
- In Section (b)(2), it is not clear what is required by what has been added. The newly added language could be read that the estimate to be provided in this provision is tied to the notice that is required if that proposed acquisition would increase rates to the acquiring public utility's customer by more than 1% of the base annual revenue or that the public utility has a separate obligation to calculate rates for its customers from an actuary. More clarification is required.
- In Section (g), the OCA recommends that the clarity be provided about the approved actuary and, specifically, should not have been employed or performed work for the utility or municipality within the last 5 years and should be required to publicly disclose whether they have ever done work for the municipality or utility.

As noted above, the OCA supports the changes proposed by HB 1862 which would amend Section 1327. This would be a good and helpful companion to the changes proposed by HB 1863, 1864, and 1865 which would provide needed revisions to Section 1329.

Conclusion

Thank you for the opportunity to testify today about these important issues. As indicated throughout, it is my view that the Committee should consider a bill that would repeal Section 1329 in its entirety. Section 1329 is neither necessary nor in my judgment good public policy for the Commonwealth or its ratepayers. In the absence of full repeal, the General Assembly could insert a sunset into its provisions with an opportunity to study the impact of 1329. If, after this study, the General Assembly believed that the legislation continued to have merit then it could remove and/or amend Section 1329. If it does not have merit, it could allow Act 12 to fade into the sunset.

In the absence of a full repeal or sunset, the OCA supports the changes proposed in HB 1863, HB 1864, and HB 1865. Each would add needed protections and constrain the excesses that have materialized as a result of Act 12. In addition, the OCA supports the purpose and intent to HB 1862 and would be pleased to work with the Committee to make some necessary technical changes and clarifications.

I am happy to answer any questions that the Committee may have about my testimony or the information presented today.



An  Essential Utilities Company

House Committee on Consumer Protection, Technology, and Utilities

Public Hearing - Act 12 Legislation

December 12, 2023

Testimony of

Marc Lucca

President, Aqua Pennsylvania

Good morning, Chairman Matzie, Chairman Marshall, and members of the House Committee on Consumer Protection, Technology and Utilities. My name is Marc Lucca, President of Aqua Pennsylvania (“Aqua”) and I’m honored to share with you the benefits of Act 12 of 2016 (“Act 12”), also known as fair market value. Based on our experience, we have thoughts on how the process could be improved to better serve all the impacted constituencies. Specifically, I’m speaking of sellers (government-owned water and wastewater utilities) and their customers, as well as buyers, like Aqua, and our customers. I want to be clear Mr. Chairman, we hear you and other concerned parties – while this law does a lot of good, it needs some improvement.

Aqua was founded more than 135-years ago in Delaware County and today remains one of the largest PUC-regulated water and wastewater utilities in Pennsylvania. We proudly serve drinking water and provide wastewater services to more than half million customers (1.5 million residents) in 32 counties. Our mission, protecting and providing Earth’s most essential resource, is more than a slogan; it is a way of life. It is a commitment made every day, by nearly 600 Aqua employees working throughout the Commonwealth.

We are here today to talk about one of the tools that the Legislature provided to government-owned water and wastewater service providers who desire to exit water and wastewater service. Act 12, passed in 2016 has incentivized a number of these government-owned providers to consider a sale and some of them have moved forward with that decision, while others have decided not to. Aqua has acquired many water and wastewater systems over time, but we are not successful in every transaction and do not bid on every opportunity. In fact, since 2016 Aqua competed against and was outbid by other investor-owned utilities and even government entities. Water and wastewater systems come in all different conditions, and the reasons for the sales vary. In the end, the decision to sell relies on extensive amounts of information shared about the transaction and can only be executed by a majority vote of the governing board. This is a voluntary decision made by municipalities. In my experience working with municipalities and authorities, these decisions have been made after discussion, debate, and education, and done in a transparent and open process. In the seven years since Act 12’s passage, the industry has learned a great deal about the mechanics of using the Act. I believe that overall, Act 12 has been successfully utilized, but think lessons learned can inform how we move forward. I recognize that there are numerous bills now introduced in both the House and Senate recommending certain changes to the Act, including the four recently introduced by Chairman Matzie. Aqua stands ready to ensure Act 12 is utilized to the benefit of all stakeholders and we are committed to working to ensure it is implemented in the public interest.

Act 12 Proposed Bills

In the seven years since Act 12 was adopted, Aqua has learned much and sees benefits and opportunities for improvements. We’ve heard concerns around the impact of purchase price on customer rates, transparency of the sale process, and ensuring that terms of contracts are met. To be clear, we stand ready to work to address those issues.

We have heard in some instances that residents are not aware of the sale. I will attempt to describe the experience Aqua has in working with sellers and the amount of time, transparency and education that goes into these partnerships to address public notification and timing for approval of transactions. I believe that municipal officials understand and support the notion that the sale of a water and

wastewater system needs to be properly publicized, discussions held openly at public meetings and encourage community participation which is often covered by local media.

The process a municipality goes through to sell its water and wastewater systems are long, transparent, and complex. They are hardly completed fast. Selling municipalities often take years before even deciding to sell. Once that decision is made, there is often a request for bid process that involves the purchase price, contract terms, and public engagement. Our acquisition of the Municipal Authority of the Borough of Shenandoah ("Shenandoah") took almost 4-years from the borough's selection of Aqua to completion. Our acquisition of the Beaver Falls Sewer Authority will take about 3-years from the final vote to sell to the time when the PUC is expected to respond to our completed application. Limerick Township's sewer system sale took around 2-years to complete. The sale of the Cheltenham Township sewer system took more than 3-years from the township's decision to sell its collection system. I personally attended no less than three well-attended public meetings including a workshop we hosted in which residents and Township commissioners were available to interact with Aqua employees.

As stated, the current process from final vote to closing can easily take more than twelve months as many parties are engaged through public meetings with the selling entity's leadership, staff, and neighboring communities. Once a selling entity decides to sell, which can be years before it is sold, there is little incentive and possibly little funds for it to do anything more than basic system operations. That may mean that for several years prior to selling, there will be little work performed. It is likely that systems will deteriorate, and operating conditions allowed to diminish, creating a worse situation than may have already existed. Therefore, any additional delay of the PUC application process only exacerbates this situation. It is also very important to underscore the impact that these transactions have on the employees of the selling entity. Aqua commits to hiring the seller's employees. These water and wastewater operators have important jobs and the longer a transaction is delayed, the more stress is taken on by these employees. Consider what it is like for an individual to know his/her place of employment was being sold, but it is on hold for two or more years. During a recent and ongoing acquisition, Aqua management including a representative from human resources, met four times with the employees to discuss the process job duties and benefits, and to answer their questions.

In addition, as part of the PUC approval process, a robust process is in place to ensure customers can participate in the proceeding. The acquiring utility is required to notice its customers and requires the selling utility to notice them of the impending acquisition and the potential impact of that acquisition to its water or wastewater bill. Every Aqua customer across Pennsylvania is mailed a notice. The selling entity also mails a notice to its customers. Samples of these notices are attached. This would be in addition to public notices and meeting notices by the selling entity. Along with the potential estimated rate impact, these notices contain information about the bid, requested ratemaking rate base, rate impact, and an explanation of the process through which customers can participate in the proceeding. By way of comparison, these notice requirements exceed requirements of a municipal authority to notify its customers of a rate increase. While they are required to provide public notice of board meetings, the Municipal Authorities Act does not require specific public notice be given about its intention to increase rates. Despite these notifications, if current notice provisions of Act 12 are insufficient, we will work to ensure proper notification is achieved.

Turning next to purchase price, we acknowledge that all or some of the purchase price becomes rate making rate base and ultimately has an impact on customer rates. Sellers are told in writing prior to

rendering their final decision what they can expect to happen, following PUC approval, to their customer's rates, based on the purchase price they choose. We need to do everything we can to ensure that the tool in Act 12 meant to allow a sale to occur creates a rate that is ultimately affordable for water and wastewater customers in the Commonwealth. Based on our experience since inception of Act 12, we believe it is very important that sellers understand how a purchase price becomes ratemaking rate base and impacts customer rates.

In addition to transparency concerns, we've heard a lot about Act 12's actual impact on rates. To be clear, in some cases, purchase prices have grown to levels that are placing upward pressure on rates. Aqua believes that Chairman Matzie's proposed cap of depreciated original cost applied to some types of systems is a concept with merit and is worth exploring and further discussion. The intent, which appears to be to limit the impact on customer rates, is a good one.

Chairman Matzie's proposal to recover ratemaking rate base over three base rate cases also appears to limit the impact on customer rates. Aqua believes that while the intent of this proposal to limit rates is a good one, as drafted, it will negatively impact the ability of PUC regulated utilities to bid and purchase municipal water and wastewater systems. We believe a cap would have a similar impact by limiting the purchase price and thus rates.

Additionally, the Act 11 subsidy used for wastewater acquisitions, on water customers is another area for consideration. While a temporary subsidy at a reasonable, PUC-approved level is prudent public policy, regulators should consider providing guidance to utilities on a limit to that subsidy.

Finally, there has been legislation proposed in the Senate to ensure commitments made by acquiring utilities are kept. Residents and elected officials should be comfortable making the decision to partner with PUC-regulated utilities like Aqua PA and we stand ready to ensure that goal is met.

Condition of our Nation's Water & Wastewater Systems

Before providing some examples of municipalities and authorities that have voluntarily made the decision to sell to Aqua, I would like to provide some background on the condition of water and wastewater systems and what we are experiencing. "Water is an essential and primary need of every American, yet most Americans take water for granted. Local water suppliers are dealing with aging, obsolete infrastructure, a challenged and shrinking workforce, and compliance with regulations of increased scope.¹" The American Society of Civil Engineer's 2021 Report Card for America's Infrastructure gave Pennsylvania's Drinking Water infrastructure a grade of a "D" and its wastewater infrastructure a grade of a "D-." "Most of Pennsylvania's public drinking water systems are struggling to fund projects to meet their replacement goals as well as new regulations. Over the next 10 years, Pennsylvania's public water systems are projected to have a \$10.2 billion funding gap, a number only very slightly offset with recent federal actions to provide infrastructure funding. Aging wastewater management systems discharge sewage into Pennsylvania's surface water each year. The average age of most sewer systems is approaching 75 years with many pipes over 100 years old. 26% of the state is served by on-lot systems with nearly one-quarter failure rate. Two-thirds of the state's Sewage Facility Plans are over 20 years old. The Commonwealth has a funding gap of \$8.4 billion over the next 10 years to repair existing systems,

¹ The President's National Infrastructure Advisory Council, Preparing United States Critical Infrastructure for Today's Evolving Water Crises, August 2023, pp 22 – 23.

upgrade existing systems to meet regulatory requirements, control Combined Sewer Overflows (CSOs), address illicit Sanitary Sewer Overflows, and construct new or expand existing systems to meet increasing demand. Available funding over that time is estimated to be \$900 million, only about one-tenth of the required annual investment.²

The above information reflects findings of two independent organizations. These conditions exist due to lack of investment that spanned decades by the owners of these systems. These conditions persisted because owners saw no escape from the untenable situation due to their own inaction or those of prior boards of directors. My point is these conditions lasted long before Act 12 became law. Act 12 helped change the landscape for such systems and many communities by providing an option to exit from either the water or wastewater business; however, I will limit my comments to systems acquired by Aqua and the experience we have had with Act 12.

In addition to required capital improvements, operating and maintaining a water and wastewater system is a full-time profession requiring skilled individuals dedicated to a single purpose. Operating a utility is not and cannot be a part time job. Issues facing water and wastewater utilities are increasing each day. In addition to new and more stringent regulations, the industry is also experiencing an increased threat from hostile actors. Consider one example which occurred on November 25, 2023, when the Municipal Water Authority of Aliquippa, located in western Pennsylvania, reported that an Iranian-backed hacktivist group successfully compromised one of its booster stations. The authority reported no damage to its drinking water; however, it is likely that this and other threat actors with similar motivations related to the Israel-Hamas conflict will continue to opportunistically target select operating systems. Professionally operated systems like Aqua PA have the cyber infrastructure in place to better position our operations to withstand such cyberattacks.

There remain substantial amounts of lead service lines posing significant risk to public health, particularly for underserved communities. Emerging contaminants such as perfluoroalkyl and polyfluoroalkyl substances (PFAS) pose growing public health threat. Water and wastewater utilities must remain focused on investing in equipment and assets, and hiring and retaining skilled workers who are focused on water and wastewater service. The ability to provide safe and reliable drinking water requires licensed professionals, skilled in chemistry, biology, computer systems, safety and security, and the changing and tightening of regulations makes it nearly impossible for public works crews to maintain streets in the morning and operate water and wastewater assets in the afternoon.

Increasing Regulations Effecting the Water & Wastewater Industry

Selling a water and wastewater system is one way to maintain or, in some cases, regain and sustain compliance with the myriad of regulations from PA Department of Environmental Protection (“PADEP”), US Environmental Protection Agency (“USEPA”), Occupational Safety & Health Administration (“OSHA”) and others. Consider three regulations that have markedly changed our industry. The 1996 Safe Drinking Water Act revisions were the result of significant health issue resulting from cryptosporidium entering streams that were source to drinking water plants and required additional filter operations. The 2009 Groundwater Rule established more demanding disinfection conditions before delivering water to

² Pennsylvania State Council of the American Society of Civil Engineer, 2022 Report Card for America’s Infrastructure, 2022.

customers. The 2017 Disinfection Residuals Rule mandated increased chlorine residual in drinking water to prevent water borne disease such as legionella.

More recently, the industry has seen regulations on: (1) customer owned lead service lines, (2) lead & copper rule (3) PFAS in drinking water which we at Aqua have been focused on since 2016, (4) manganese, which is naturally occurring, in drinking water sources which for decades had been a secondary standard requiring no action , but now requires an immediate customer notice of "Do Not Consume" until treatment can be installed, (5) health impacts from toxic algae blooms, (6) focus on nutrient limits in treated wastewater disposal and others. One example of possible future regulatory changes is the possible hazardous waste designation for PFAS in drinking water treatment sludge. My point is that regulations are changing at a faster pace and outpacing some utility owners' ability to understand, fund and comply.

It is also important to consider the safety of our water and wastewater employees throughout the Commonwealth. In Pennsylvania OSHA oversees Aqua and other regulated utilities but does not cover local and government workers; that oversight is provided by Department of Labor & Industry (L&I). While basic regulatory safety oversight exists in Pennsylvania for government workers through L&I, federal OSHA's oversight requires broader compliance to more specific safety standards and addresses the hazards that are not specifically listed in the OSHA Standards. For example, OSHA requires compliance with 14 Elements of a Process Safety Management Program in places where 1,500 pounds or more of chlorine gas is stored. Program elements include employee participation, process safety management training, contractor training, mechanical integrity, and others. OSHA's comprehensive safety program seeks to prevent exposure to employees, nearby residents, and the environment from an uncontrolled chlorine gas leak.

In addition to the technical challenges of managing water and wastewater systems and complications by increasing regulations, it is my experience that some municipalities are having difficulty hiring and retaining qualified employees and board members. In one case, a retired employee had to be recalled to cover for the general manager who was out of work for an extended period. In another case, the Greenville Water Authority board members reported one reason to sell is it cannot find volunteers interested in serving on the board. In October 2009 the board adopted Resolution No. 5-09 which reduced its complement by from seven members to five³.

I believe Act 12 provides options for struggling municipalities and I see many benefits that Aqua has brought to these systems once our team started running and operating them.

Act 12 Acquisitions

Next, I'd like to talk about the transactions that municipalities have chosen Aqua to partner under Act 12. Aqua has successfully acquired systems utilizing Act 12. However, there are examples in which we bid and the seller ultimately chose not to sell their assets or Aqua was outbid by municipal utilities and other investor-owned utilities.

I'll begin in 2019 with Aqua's partnership with Cheltenham Township's wastewater system. Cheltenham Township had multiple public hearings that I personally attended and responded to their questions. The

³ Greenville Water Authority Regular Meeting of the Board of Directors Minutes (2009) Greenville Water Authority. Available at: www.gmwa.info

collection system was in a state of disrepair and causing significant problems for Philadelphia Water Department (“PWD”) as wastewater from Abington and Jenkintown flows through Cheltenham to the PWD wastewater treatment plant. The collection system experienced significant sanitary sewer (raw sewage) overflows (SSOs) that contaminated Tookany Creek where residents visit, and children play. The township failed over many years to correct the problem resulting in the relationship between the township and PADEP to deteriorate. Since utilizing Act 12, Aqua went into action – working with PADEP, PWD, the township, investing more than \$3.3 million to improve system reliability through a fix and repair program, main (pipe) flushing which prevents SSOs, plus “recreating” a hydraulic computer model that has identified long-term alternatives. Aqua and PWD have made significant progress toward a regional solution which, in my opinion, exemplifies a public/private partnership. There is still much work to do, but I am hopeful the regional solution will work.

In July 2023, we completed our acquisition of Shenandoah. For background, this sale process took multiple years to complete. The system had significant unaccounted for water. That is, 60 % of the water was leaking from the system meaning that for every 10 gallons taken from the lakes in this area, only 4 gallons is known to reach the customer. And there were very real concerns about system fire hydrant operability in the event of a fire. Within a few weeks of our acquisition, we identified that 23% of the 195 hydrants were inoperable which we promptly bagged as shown in photo number 1 below. Imagine what would have happened if a fire company attempted to use one of these hydrants during a fire emergency.

Featured WWD Proposed Sale
Aqua: Quarter of area fire hydrants inoperable after evaluation, will be repaired or replaced

© August 10, 2023 Kaylee Lindermuth



KAYLEE LINDERMUTH / SHENANDOAH SENTINEL - A bag covers a fire hydrant at West Centre and South Catherine Streets in Shenandoah on August 10, 2023.

Photo 1. Inoperable fire hydrant bagged by Aqua until replaced. Shensentinel newspaper, August 10, 2023.

In addition, some hydrants have been observed to freeze in wintertime. Photo number 2⁴ below shows a firefighter struggling during a fire to open a frozen hydrant. Another problem identified is that some hydrants are installed on a 4" diameter pipe which would almost certainly render insufficient flows for

⁴ "Turkey Run – House Fire - 3/7/23," YouTube video, 3:17 minutes, June 22, 2023.

firefighting; 6" or greater would be more typical. Aqua is proactively working to correct these problems. These are all long-time, systemic problems that we are now engaged in addressing.



Photo 2 Firefighter stands on wrench to attempt to force open a fire hydrant for use during a fire.

As I alluded to earlier, Aqua has purchased systems in various conditions, sizes, and age. Each system has some differences and challenges. Consider for example an East Whiteland (Chester County) sewer pipe shown in Photo number 3.



Photo 3. Camera view inside an active sewer pipe in East Whiteland, Chester County shows pipeline break which allows raw sewage to enter the environment.

Aqua's team discovered this pipe after acquiring the system. The pipe separation shown sometimes occurs due to aging. This pipe conveys raw sewage from homes and businesses. Here, the separation discovered by Aqua operators is causing raw sewage to escape the pipe and enter the environment. Under certain circumstances, the opposite may occur which would allow groundwater and rainwater to enter the pipe and the wastewater treatment plant where it can cause exceedances and raw sewage to enter receiving streams, creeks and lakes.

In 2020, Aqua purchased the wastewater assets of New Garden Township. This transaction benefited customers in this community and the surrounding environment. It is true that customer rates were

lower prior to the sale, but that rate reflected the lack of investment that led to the poor condition of the assets. First, I want to specifically address rates for this particular community. Due to the length of time before closing, New Garden Township which billed on a quarterly basis did implement a rate increase, that based on timing, appeared for the first time in Aqua's monthly bill after closing. Aqua did not raise rates during the acquisition process nor did it do so prior to its PUC-approved rate case. In addition, prior to selling, the customer's base wastewater charge included a quarterly allowance of 5,000 gallons of wastewater which basically acted as cap for some customers. The PUC did not adopt a similar quarterly allowance resulting in higher rates than anticipated in Aqua's last rate request.

This system faced significant challenges. For example, the wastewater lagoons were nearing overflow, that if occurred could release partially treated sewage into neighboring fields and streets. Since owning the system Aqua invested almost \$4 million in improvements that addressed compliance, safety and equipment that was in an imminent threat of failure including such basic additions as portable generators at pump stations. Without backup power raw sewage may spill into surrounding neighborhoods, streets and even homes during a power failure. Prior to Aqua's involvement, the township had a "truck and haul" operation in which "treated" wastewater was hauled from one of its wastewater treatment plants to another because of disposal capacity issues. In addition, the capacity issues included underperforming spray irrigation fields that were operating at only about 62% capacity. As a result, there is a need to haul wastewater at an additional expense. Aqua's experienced team spent the first 10-months following the acquisition placing into operation an existing plastic pipeline that would end the truck hauling. This pipeline was installed years earlier by the authority for this purpose but had never been used. Our expertise was on display as we located and repaired the pipeline and prepared it for service. The current operation reduces costs and savings will be identified in our next rate case.

In closing, I would like to thank this committee for receiving my testimony today which shares our experience from the perspective of a water and wastewater utility provider with Act 12. In summary, our nation's infrastructure is failing because of lack of investment. We are leaving the next generation a significant problem they need to address simply because we did not. The condition of these systems occurred long before Act 12 so I simply do not agree with the sentiment that removing it will correct these problems. However, after seven years of experience with Act 12 we have learned much, and I believe there is opportunity from those lessons to improve the process. Aqua stands committed to making sure Act 12 is utilized to the benefit of all stakeholders and ready to ensure Act 12 is implemented in the public interest and results in affordable rates.

-END OF COMMENTS-

ATTACHMENTS

Limerick Supervisors clarify issues on sale of sewer system

We are writing to clarify the issues noted within the Sept. 9 article concerning the sale of the Limerick Township sewer system to Aqua Pennsylvania. In particular, the article fails to fully detail long-term benefits of the sale which will enable the township to maintain low real estate tax rates for many years, while still addressing the rising cost of core services which include police, fire, emergency medical, roads and public works. These core municipal services come at a cost to the community, but are essential in maintaining the health, safety and welfare of a growing community such as Limerick.

The sale of the sewer system did not happen overnight and was the result of a study to deter

mine long-term services required of every township department. Most significant was the future cost of the police and volunteer fire departments, which are at the forefront of public safety services provided to the community. Included were projections which set forth a potential \$20 million capital improvement plan required for the sewer system over the next 15-plus years to address an aging collection and treatment system. In addition, increasing state environmental regulations under Pennsylvania Department of Environmental Protection (DEP) were projected to further burden operational costs associated with the sewer system.

The study was not limited to these departments and with Limerick be

ing a diverse and growing community, requests for additional recreational fields, parks, trails and open space have also been asked of the township for many years, as well. The board is cognizant of the burden that is placed on the taxpayers and has worked diligently for well over a decade to maintain below average real estate tax rates while answering the increasing demand for services. The passage of PA Act 12 by the State Legislature in 2016 provided an opportunity to enhance this strategy and step away from the growing burden of operating the sewer utility system, and focus on core township services.

The basic intent of Act 12 is to encourage the sale of standalone municipal utility systems to larger

operators such as Aqua, who can provide a higher level of expertise at a greater economy of scale. Utility operators, such as Aqua, also come under the control of the state Public Utility Commission (PUC) who has oversight of rates. With growing environmental issues of municipal sewer systems, Pennsylvania DEP also benefits with consolidation of the thousands of fragmented municipal sewer systems under larger operators who can ensure higher level of environmental control.

After careful consideration of all issues, the Limerick board approved the sale by way of a public bid. Aqua was the highest bidder and the board agreed to complete the transaction and utilize the sale proceeds to cover

the long-term needs of the township and protect real estate tax rates. It is important to note, if the sewer sale did not take place, the combined Limerick real estate taxes and sewer rates were expected to be higher in years 2020 and beyond what Aqua is projecting for just sewer rates when the current three-year rate freeze expires. The public must be reminded that any future rate increases desired by Aqua must be approved by the PUC and that rate payers have a voice in that process.

The success of the sewer sale is ultimately dependent on how the funds are utilized and protected for future generations of Limerick residents. Toward this endeavor, the board stands committed to proper use

and investment of the sale proceeds in which interest returns are maximized and used to offset ongoing costs of services and thereby, reducing the burden on township real estate tax rates. With the increasing real estate tax burden imposed by the school district and county, the Limerick Board of Supervisors is confident that this investment strategy will provide stability of township real estate taxes, and enable an offset to any sewer increase that is projected under the new ownership of Aqua.

*Limerick Township
Board of Supervisors
D. Elaine DeWan,
Patrick M. Morrane,
Thomas J. Neafly Jr.,
Kara Shuler
Kenneth Sparrin Jr.*

Attachment no. 2: Limerick Township Board members letter posted in the local newspaper about the sewer sale to Aqua Pennsylvania. September 17, 2018.



NOTICE OF PROPOSED ACQUISITION AND RATE BASE ADDITION

Docket No. A-2022-3034143

Dear Customer:

On December 9, 2022, the Pennsylvania Public Utility Commission (PUC) conditionally accepted for filing the application of Aqua Pennsylvania, Inc. (Aqua) for approval to acquire the Borough of Shenandoah / Municipal Authority of the Borough of Shenandoah (Shenandoah) water system assets. Shenandoah serves approximately 2,900 customers in Schuylkill County, Pennsylvania. Aqua's application also requests that the PUC authorize a purchase price and addition of \$12 million to Aqua's rate base pursuant to 66 Pa. C.S. § 1329. A utility's rate base is the value of property it uses to provide service to its customers and is one of several components used by the PUC to establish a utility's customer rates.

Aqua periodically makes applications to the PUC for newly acquired systems which requires Aqua to send these types of notices. This notice is specific to the Shenandoah acquisition.

This acquisition will not immediately, but may in the future, affect water bills of Aqua customers, including the new Shenandoah water customers. Aqua is not requesting a rate increase as part of the acquisition. Your rates will not change at the time we close this transaction and can only change with when approved by the PUC following an Aqua rate case that includes the Shenandoah system. Aqua estimates that the rates of the average customer could increase at that time, based on our preliminary analysis. The amount of the increase will be determined by the PUC in Aqua's next base rate case and will be dependent on how the PUC chooses to apportion the increase among Aqua's acquired and existing customers. The tables below present non-binding, estimated incremental rate effects of the proposed rate base addition on Aqua's existing water customers:

Aqua Water Customers

Rate Class	Average Usage	Estimated Monthly Increase	Estimated Percentage Increase
Residential	4,000 gal/month	\$0.08	0.10%
Commercial	33,380 gal/month	\$0.44	0.10%
Industrial	200,150 gal/month	\$2.14	0.10%
Public	33,380 gal/month	\$0.44	0.10%

The amounts stated above could change and will depend on how the PUC chooses to apportion any increase among the types of service, rate zones, and classes of customers as well as the actual amount of water used.

PUC ROLE

The state agency which approves acquisitions and rates for regulated public utilities is the PUC. The PUC will review and investigate the proposed acquisition and requested \$12 million in additional rate base. After examining the evidence, the PUC may approve, modify or deny the acquisition and may approve or modify the \$12 million addition to rate base. The PUC will issue a decision on the application on or around July 13, 2023.

ACTIONS YOU CAN TAKE

You can support or challenge Aqua's request by:

- 1) Sending a letter to the PUC. You can tell the PUC why you support or object to Aqua's acquisition of Shenandoah's water system in your letter. This information can be helpful when the PUC investigates the application. Send your letter to the Pennsylvania Public Utility Commission, Post Office Box 3265, Harrisburg, PA 17105-3265.
- 2) Attending or presenting testimony at a PUC Public Input Hearing. You can attend or be a witness at a PUC public input hearing. The PUC holds public input hearings if it opens an investigation into Aqua's transaction and there is enough interest in the case. At these hearings, you can present your views in person to the PUC judge and to company representatives. Testimony under oath becomes part of the application case record. The PUC holds these hearings in the service area of the company. For more information, call the PUC at 1.800.692.7380.
- 3) Filing a protest or a petition to intervene. If you want to be a party to the case, you must file a protest or a petition to intervene. You then have an opportunity to take part in all the hearings about the proposed acquisition. You can receive copies of all materials distributed by the other parties. Protests and petitions to intervene must be filed in accordance with 52 Pa. Code (relating to public utilities) on or before February 27, 2023. Filings must be made with the Secretary of the Pennsylvania Public Utility Commission at P.O. Box 3265, Harrisburg, PA 17105-3265, with a copy served on Aqua's counsel at Saul Ewing Arnstein & Lehr, LLP, Attn: Courtney L. Schultz, 1500 Market Street, Center Square West, 38th Floor, Philadelphia, PA 19102.

The documents filed as part of this application are available for inspection and copying at the Office of the Secretary of the PUC between 8 a.m. and 4:30 p.m., Monday through Friday, on the PUC's website at www.puc.pa.gov and at Aqua's offices at 762 West Lancaster Avenue, Bryn Mawr, PA 19010. The PUC docket number is A-2022-3034143.

BOROUGH OF SHENANDOAH

15 West Washington Street Shenandoah, PA 17976

Phone (570)462-1918 Fax (570)462-2772

Email - shenboro@ptd.net

shenandoahpa.org

"Shenandoah Borough is an Equal Opportunity Employer and Provider"

Dear Customer of Municipal Authority of the Borough of Shenandoah ("MABS"):

At its public meeting on November 25, 2020, the Borough Council of the Borough of Shenandoah (the "Borough") voted to sell the Borough's water treatment and distribution system (the "System") to Aqua Pennsylvania, Inc. ("Aqua") for a purchase price of \$12,000,000. The primary goals of the sale were to ensure that (i) much needed improvements to the water system are undertaken by Aqua, to the largest extent possible, (ii) your rates are kept as low as possible, and (iii) all current MABS employees are offered employment with Aqua. All information relating to the sale was discussed at public meetings convened by the Borough on October 19, 2020 and October 26, 2020.

The Borough began this process in 2017 after Council was advised by the Pennsylvania Economy League ("PEL") that (1) the Borough faced a looming financial crisis because its water authority did not possess adequate funds to operate and undertake necessary future upgrades required to provide its customers with vital and necessary water services in compliance with applicable laws and regulations, and (2) this situation has jeopardized the Borough's water infrastructure and created financial risks to the System's customers and the Borough's taxpayers. MABS had been unable to pay its financial obligations and was forced to modify its loan terms on multiple occasions to avoid a payment default.

In order to fund necessary capital improvements, which the Borough has estimated at more than \$25 million, the Borough received an analysis that MABS would have to increase its rates by 10% per year for each of the next several years and then 5% per year for each year thereafter over the next two decades to fund necessary System improvements. The Borough decided that the risk associated with operating the System without sufficient revenues to pay for necessary upgrades is too great for the System's customers or its taxpayers to absorb. Aqua's financial resources and professional expertise, however, enable it to provide needed long-term investment in the System, restore the System to a state of good repair and reliability, and remain in compliance with environmental and regulatory requirements. If the sale is completed, the cost of some of those necessary capital improvements are expected to be spread over Aqua's more than 450,000 water customers.

Proceeds of the sale of the System will be used to pay off all of MABS' existing debt, fund accrued pension liabilities owed to the MABS' employees, and fund other accrued post-employment benefits of the MABS' employees. Additionally, the residents of the Borough will enjoy the benefits of capital investment by the Borough using excess proceeds of the sale.

Currently, an average bill for a metered single-family dwelling of the Borough's water system is \$49.64 per month or, \$148.91 per quarter (assuming a monthly water consumption of 2,790 gallons). An

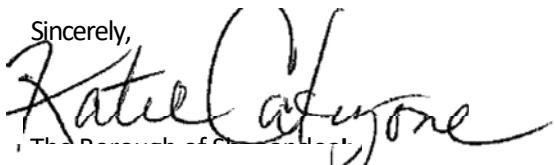


average bill using 4,000 gallons per month under the Borough's current rates would be \$58.82. If MABS were to retain and properly invest in the System, those rates are expected to increase to an amount higher than those charged by Aqua. Increases in Aqua's future rates will be based on its cost to provide service to its customers. Aqua is regulated by the Pennsylvania Public Utility Commission ("PUC"), which examines any proposed rate change to ensure Aqua's rates are just and reasonable.

Enclosed is the notice that the PUC requires to be sent to Borough customers containing an estimate of potential future rate increases. Aqua is required to provide you with a non-binding estimate of potential future rate increases assuming that it seeks to include 100% of its acquisition price of the System in its next rate case and does not have any of the costs allocated to its other customers outside of Shenandoah. Aqua has also provided an estimate of potential future rate increase which assumes some costs are shared among all of Aqua's customers. Actual rates will be set by the PUC and must, under state law, be "just and reasonable," taking gradualism into consideration. As such, future increases may be different than those set forth in the notice. As part of the agreement of sale, however, Aqua will adopt the Borough's water treatment and distribution rates in effect on the date the System is acquired, and Aqua has agreed to hold those rates until the PUC approves Aqua next rate increase, which is expected to be in 2025.

The two paragraphs above the tables in the enclosed notice describe how Aqua applies for rate changes with the PUC; the area below the tables in the enclosed notice describes how customers can participate in the acquisition application process.

Sincerely,

A handwritten signature in black ink, appearing to read "Katie Layrone".

NOTICE OF PROPOSED ACQUISITION AND RATE BASE
ADDITION Docket No. A-2022-3034143

Dear Customer:

On December 9, 2022, the Pennsylvania Public Utility Commission (PUC) conditionally accepted for filing the application of Aqua Pennsylvania, Inc. (Aqua) for approval to acquire the Borough of Shenandoah / Municipal Authority of the Borough of Shenandoah (Shenandoah) water system assets. Shenandoah serves approximately 2,900 customers in Schuylkill County, Pennsylvania. Aqua's application also requests that the PUC authorize an addition of up to \$12 million to Aqua's rate base pursuant to 66 Pa. C.S. § 1329. A utility's rate base is the value of property used by the utility to provide service to its customers and is one of several components used to establish a utility's customer rates.

This acquisition will not immediately, but may in the future, affect water bills of Aqua customers, including the new Shenandoah water customers. **Aqua is not requesting a rate increase as part of the PUC acquisition approval process.** Your rates will not change as a result of this transaction until the conclusion of an Aqua rate case where Aqua includes the Shenandoah system and requests and receives PUC approval to increase its rates. **At this time, Aqua projects its next base rate case will be effective in 2025.** At that time, based on a preliminary analysis of the potential rate impacts, Aqua estimates that the rates of the average customer could increase. The amount of the increase will be determined in Aqua's next base rate case and will be dependent on how the PUC chooses to apportion the increase among Aqua's acquired and existing customers. The tables below present a non-binding, estimated incremental rate effect of the proposed rate base addition on Shenandoah's water customers, which include estimates with and without cost sharing. Aqua has sought cost sharing in later rate filings for acquired systems and therefore we are providing both scenarios in this notice:

Shenandoah Customers rates assuming costs are shared among other Aqua customers

Rate Class	Average Usage	Estimated Monthly Increase	Estimated Percentage Increase
Residential	2,790 gal/month	\$6.91	15.90%
Commercial	6,180 gal/month	\$12.49	15.90%
Industrial	318,750 gal/month	\$167.05	15.90%
Public	55,700 gal/month	\$35.16	15.90%

Shenandoah Customers rates assuming no costs are shared with other Aqua customers

Rate Class	Average Usage	Estimated Monthly Increase	Estimated Percentage Increase
Residential	2,790 gal/month	\$19.50	44.87%
Commercial	6,180 gal/month	\$35.25	44.87%
Industrial	318,750 gal/month	\$471.52	44.87%
Public	55,700 gal/month	\$99.24	44.87%



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PUC ROLE

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ACTIONS YOU CAN TAKE

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- 2) Attending or presenting testimony at a PUC Public Input Hearing. You can attend or be a witness at a PUC public input hearing. The PUC holds public input hearings if it opens an investigation into Aqua's transaction and there is enough interest in the case. At these hearings, you can present your views in person to the PUC judge and to company representatives. Testimony under oath becomes part of the application case record. The PUC holds these hearings in the service area of the company. For more information, call the PUC at 1.800.692.7380.
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