Prepared Testimony of

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before the

Pennsylvania House of Representatives
Committee on Consumer Protection,
Technology & Utilities

Hearing on House Bills 1862, 1863, 1864, and 1865 amending
Sections 1327 and 1329 of the Public Utility Code,
66 Pa.C.S. §§ 1327 ("Acquisition of Water and Sewer Utilities")
& 1329 ("Valuation of Acquired Water and Wastewater Systems")

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Chairman Matzie, Chairman Marshall, and Members of the Committee:

Thank you for this opportunity to provide testimony on House Bills 1862, 1863, 1864, and 1865, all of which address flaws in Section 1329 of the Public Utility Code, 66 Pa.C.S. § 1329 (relating to valuation of acquired water and wastewater systems), attached hereto as APPENDIX A, which was added to the Code by Act 12 of 2016.[1]

- House Bill 1862 amends Code Section 1327 by requiring selling municipal corporations to issue and advertise requests for proposals from public utilities and to retain an actuary to provide estimates of rates charged by each public utility that submits an offer in response to the RFP. It also requires the Public Utility Commission (PUC) to ensure that the public utility buyer has complied with these requirements and to hold at least two public hearings on the proposed acquisition.
- House Bill 1863 deletes Code Section 1329(d)(2) which requires the PUC to issue a final order on an acquiring public utility's application to acquire a municipal system within six months of the filing date of the application.
- House Bill 1864 amends Code Section 1329(c) by spreading out the inclusion into the acquiring utility's rate base of the determined value of the acquired municipal seller's property over four rate cases rather than total inclusion in the first rate case after the PUC's approval of the acquisition.
- House Bill 1865 amends Code Section 1329(c) by limiting the determined value of the acquired municipal seller's property that may be included in the utility's rate

[1] Act of April 14, 2016, P.L. 76, No. 12.

base if the acquired municipal seller is not a distressed system under the criteria in Code Section 1327(a).

All of these bills have merit. House Bill 1362 provides for much-needed public exposure of the details and rate effects of proposed acquisitions by investor-owned public utilities of municipal systems.

House Bills 1363, 1364, and 1365 are meritorious if Section 1329 remains in effect.

Summary of Testimony

Act 12 makes a sham of public utility regulation by restoring pre-1913 monopoly pricing and eliminating the PUC's fundamental authority to ensure that utility rates are "just and reasonable."[2]

Because of its harmful flaws described below, Section 1329 is irredeemable because its key provisions cannot be amended or curtailed without destroying the section's purpose. That section has already caused extreme rate increases approaching $100 million annually, with much more to come if left unchecked. The section must be repealed as soon as possible to prevent further windfalls to municipal sellers and utility shareholders at the expense of the customers of only three investor-owned water companies.

Investor-owned water and sewer public utilities should only be given financial incentives when they acquire truly distressed or non-viable municipal systems. Code Section 1327(a), applicable only to such troubled systems, includes essential customer protections absent from Section 1329, and, if amended to include valuation of contributed municipal property, would render Section 1329 unnecessary.

[2] The first sentence of Public Utility Code Section 1301(a) (relating to rates to be just and reasonable; regulation), 66 Pa.C.S. § 1301(a) provides: "Every rate made, demanded, or received by any public utility, or by any two or more public utilities jointly, shall be just and reasonable, and in conformity with regulations or orders of the commission."

Background

For decades, the shareholders and bondholders of Pennsylvania's private (as opposed to municipally owned) public utilities earned a return ("rate of return") on the "fair value" of the utility's property used to provide customer service (the "rate base").[3]

When the utility requested an increase in rates from the PUC, an inordinate amount of time was spent by experts opining on the appropriate rate of return and the fair value of the utility's rate base because precise numbers were impossible.

In 1975, a Pennsylvania Senate committee heard extensive testimony decrying the "delay, uncertainty and waste of regulatory resources in establishing 'fair value',"[4] even from a prominent lawyer representing utilities who concluded that "there is so much to be gained by eliminating the hocus-pocus of 'fair value' that the effort should be made."[5]

In place of valuing public utility property at its nebulous "fair value," the Committee, at the urging of Jack K. Busby, president of Pennsylvania Power & Light Company, and other witnesses,[6] recommended adoption of valuation at the property's "original cost less depreciation,"[7] i.e., the known costs incurred when the rate base property first went into service, with the total amount reduced annually to reflect obsolescence ("depreciated original cost").

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[3] *See* Edward Ross Carpenter, Note, *Fair Value or Prudent Investment as a Rate Base in Pennsylvania? A Conflict Between the Public Utility Commission and the Superior Court*, 99 U. Pa. L. Rev. 371 (1952).

[4] REPORT AND RECOMMENDATIONS OF THE SENATE CONSUMER AFFAIRS COMMITTEE TO REFORM THE PENNSYLVANIA PUBLIC UTILITY COMMISSION (September 1975) 62-69 at 68 (quoting testimony of Richard D. Cudahy, Chairman of the Wisconsin Public Service Commission).

[5] *Id.* at 69 (quoting remarks made by Robert H. Griswold, Esquire, to the Public Utility Law Section of the Pennsylvania Bar Association in 1971).

[6] *Id.* at 63.

[7] *Id.* at 68.

This change, however, was not adopted until the amendment of Public Utility Code Section 1311(b) (relating to valuation of and return on the property of a public utility) by Act 153 of 1984 applicable to all public utility property.[8]

Code Section 1327 (relating to acquisition of water and sewer utilities), attached hereto as APPENDIX B, was added in 1990 and expanded in 1995 to encourage investor-owned public utilities to acquire and remediate distressed and non-viable public utilities and municipal corporations.[9] It contains alternative provisions for instances where the acquisition cost (principally the purchase price) is either greater or lower than depreciated original cost.

Section 1327(a) very liberally creates a rebuttable presumption that any excess amount in the purchase price is reasonable and includable in the acquiring utility's rate base if (a) the acquired system either has no more than 3,300 customers OR the system is "nonviable in the absence of the acquisition," AND its owner is not "furnishing and maintaining adequate, efficient, safe and reasonable service and facilities;" (b) the PUC finds that the purchase price is reasonable and that the rates for existing customers will not increase unreasonably; and (c) needed improvements will be made according to a plan submitted by the utility.

Under Section 1329 created by Act 12 of 2016, a utility buyer, simultaneously with its application for PUC approval of the overall acquisition under Code Sections 1102 and 1103,[10] can

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[8] Act of Sept. 27, 1984, P.L. 721, No. 153. A nearly identical amendment was made by the act of Dec. 21, 1984, P.L. 1265, No. 240. Section 1311(b)(1) now provides: "The value of the property of the public utility included in the rate base shall be the original cost of the property when first devoted to the public service less the applicable accrued depreciation as such depreciation is determined by the commission."

[9] Act of April 4, 1990, P.L. 107, No. 24; act of June 1, 1995, P.L. 49, No. 7.

[10] These sections require that the PUC find that the acquisition will "affirmatively promote the 'service, accommodation, convenience, or safety of the public' in some substantial way." *City of York v. Pa. Pub. Util. Comm'n*, 295 A.2d 825, 828 (Pa. 1972); *see also Cicero v. Pa. Pub. Util. Comm'n*, 300 A.3d 1106, 1120 (Pa. Cmwlth. 2023). The PUC may consider *the impact on rates* as one factor (which can be outweighed by other factors) in its determination of whether the acquisition will result in a substantial public benefit. *McCloskey v. Pa. Pub. Util. Comm'n*, 195 A.3d 1055, 1066-67 (Pa. Cmwlth. 2018), *appeal denied*, 207 A.3d 290 (Pa. 2019).

elect to proceed under a new process that allows the utility to request ratemaking treatment of a selling municipal water or sewer utility's assets using "fair market value" (FMV), rather than the otherwise applicable depreciated original cost methodology.[11]

FMV is derived from the average of two separate appraisals performed by two "utility evaluation experts," one chosen by the seller and one by the buyer.[12]

The *lesser* of the FMV or the purchase price negotiated by the seller and buyer is the dollar value (called the "ratemaking rate base" or RMRB) that the buying utility is entitled to include in its rate base when that utility next requests the PUC to approve a rate increase.[13] The mandatory words "shall be incorporated into the rate base of (i) the acquiring public utility during the acquiring public utility's next base rate case" in Section 1329(c)(1)(i) and the requirement in Section 1329(d)(3)(i) that the PUC's acquisition application approval order specify the RMRB figure as determined in Section 1329(c)(2) make clear that (a) the PUC cannot modify the RMRB figure in its application approval order and (b) the RMRB amount cannot be challenged in the subsequent rate case even though under Section 1329(d)(3)(ii) the PUC may attach conditions to its approval of the *acquisition application but not to that part of the application approval order specifying the RMRB as determined in compliance with Section 1329(c)(2)*.

Section 1329's Flaws

1. Section 1329 is not confined to distressed or non-viable municipal systems. Advanced as a way to encourage investor-owned water companies to acquire and improve distressed municipal water and sewer systems, Act 12 has instead been used to buy healthy and

[11] Section 1329(a).

[12] Section 1329(a)(1), (2), (3).

[13] Section 1329(c)(1) & (2).

well-managed municipal systems at excessive prices because nothing in Section 1329 limits its application to distressed or non-viable municipal systems.

House Bill 1326 of the Regular 2015-2016 Session (which became Act 12 and added Section 1329 to the Public Utility Code) was promoted with this message:

> Currently, there are community owned water and wastewater utilities whose system infrastructure is urgently in need of repair or replacement, however the system owners cannot afford to make these needed upgrades.[14]

There is no sound public policy reason to force an acquiring public utility's customers throughout the state to subsidize the utility's acquisition of a healthy and well-managed municipal system.

That burden should fall on the utility's investor-owners, not on customers who may have compelling community needs of their own and who do not receive a reciprocal benefit for subsidizing their utility's acquisition of a healthy municipal system at an excessive price, especially when the municipality may use the sale proceeds for purposes unrelated to improving water or sewer service to the municipality's citizens.

2. Fair market value (FMV) is completely incompatible with public utility regulation. While "fair value" was abandoned as speculative hocus-pocus, "fair market value" determined by a different set of experts is equally so and completely incompatible where public utility property is concerned. As debated and decided at the dawn of state regulation of investor-owned public utilities during the first two decades of the last century,[15] private property selling value derived in

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[14] *See* ATTACHMENT C hereto. This language was echoed in the co-sponsorship memorandum of House Bill 1326's prime sponsor (*available at* https://www.legis.state.pa.us//cfdocs/Legis/CSM/showMemoPublic.cfm?chamber=H&SPick=20150&cosponId=18409).

[15] *See, e.g.*, Martin G. Glaeser, PUBLIC UTILITIES IN AMERICAN CAPITALISM (1957) 285 ("It was recognized that a commercial valuation predicated upon earning capacity had no place in a process of price determination whose objective was the determination of the reasonable exchange value of services produced under regulated monopolistic or semi-monopolistic conditions.").

competitive commercial real estate markets differs from the value given to public utility assets for ratemaking purposes in a non-competitive regulated monopoly environment.

The FMV method is inappropriate in a non-competitive, economically regulated monopoly environment where the property owner is given an exclusive franchise service territory and the property is used to provide a service that is absolutely and irreplaceably essential to modern life. Consequently, such property is "affected with the public interest" and the service provider's business practices, rates, and terms of service may be controlled under the Police Power of the state for the common good.

Under such regulated circumstances, there is no ready market for the sale property because it is unique in character and public utilities have control of that market. There are no competitors from whom customers may get the identical service, and there are an extremely limited number of potential buyers (all of whom are either public utilities or need to become a public utility with the PUC's approval to serve customers with the acquired assets)—those who are financially strong enough to pay many millions or tens of millions of dollars to acquire municipal systems, who have large customer bases across which they can spread the costs of the acquisition (especially valuable when such costs are excessive), and who have existing water and/or sewer operations and personnel close enough to the acquired system to make operating it economical.

For these reasons, until the enactment of Act 12, FMV was never used in Pennsylvania to value property used to provide utility services for ratemaking purposes. A variety of other methods were debated and tried, including the "fair value" methodology which had multiple meanings but none which utilized "fair market value" methodology.

In short, FMV is anathema to Pennsylvania rate regulation, and Section 1329 is an inappropriate aberration that should be abolished.

3. Section 1329 eliminates the PUC's fundamental authority to ensure that utility rates are "just and reasonable" and restores pre-1913 monopoly pricing. As described above, the PUC is given no choice but to adopt the lesser of the FMV (the average of the appraisals made by appraisers chosen by the seller and buyer) or the purchase price (negotiated by the same seller and buyer), and once this "rate making rate base" amount is adopted as part of the PUC's acquisition approval order, it cannot be challenged in the subsequent rate case when that RMRB amount is added to the acquiring utility's rate base (and the resulting increased revenue requirement results in higher rates that permit the utility to recover the excessive purchase price it paid to acquire the municipal assets).

Never in the history of public utility regulation in Pennsylvania, initiated in 1913, has the PUC or its predecessor (the Public Service Commission) been barred from ensuring that EVERY public utility rate is just and reasonable. Section 1329 makes a sham of public utility regulation in Pennsylvania because the ratemaking process it creates substitutes the regulated for the regulators.

4. The FMV appraisal process creates the wrong incentive. Excessive acquisition purchase prices occur when the two FMV appraisers are chosen by the negotiating parties who both want the final figure to be as high as possible—the selling municipal seller wants more money to spend; the buying utility wants to increase its rate base by at least the amount of the purchase price.

The acquiring utility's investors do not receive a return on the FMV (the average of the two appraisals) unless it is lower than the purchase price. But if the FMV figure is inflated by routinely higher appraisals than the purchase price (*as has occurred in all 21 purchases that have been*

approved by the PUC and closed thus far),[16] the lesser purchase price can be that much more inflated, too, yet the PUC is required to allow its inclusion in the utility's rate base.

At least the appearance of impropriety or bias is created when the two parties to the transaction choose the appraisers, especially when the customers of both parties—who will foot the bill—have no input into the appraisal process.

5. Two provisions of Section 1329 ensure an inflated FMV. First, the law allows contributed property to be included in the appraised FMV, e.g., municipal system property donated by real estate developers and property acquired using state or federal grants.[17] The FMV is inflated by this "free property" that was not paid for by either the municipal seller or its customers.

As I suggest below, allowing the inclusion of contributed property in the valuation of municipal property, although normally excluded by the "no return on contributed property" rule in public utility ratemaking, may be necessary *but only when the proceeding occurs under Section 1327(a) involving distressed or non-viable municipal systems.*

Second, the appraisers' combined fee "not exceeding 5% of the fair market value"[18] may be included in the appraised FMV along with other "transaction and closing costs incurred by the acquiring public utility,"[19] including an engineering fee, attorneys' fees, and possibly financial advisor fees.

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[16] *See* APPENDIX D hereto detailing the differences in the purchase prices and the average of the two appraisals of all 21 transactions.

[17] See the second sentence of Section 1329(d)(5) ("The original source of funding for any part of the water or sewer assets of the selling [municipal] utility shall not be relevant to determine the value of said assets.").

[18] Section 1329(b)(3).

[19] Section 1329(d)(1)(iv).

These one-time sale expenses are extraneous to the value of the municipal system and should only be used in the next rate case to set a normal level of acquisition expenses for the period in which the new rates are in effect.

Their inclusion inflates the FMV and ensures that a lesser but possibly excessive purchase price is added to the utility's rate base.

When that occurs, under Code Section 1311(c), the buying utility's water customers—even if they receive sewer service from another provider—have been required to help fund the revenue deficiency caused by excessive purchase prices paid for municipal sewer systems.

6. The conflict-of-interest prohibitions in Section 1329(b)(2) are inadequate. That subsection merely provides that the appraisers may not "derive any material financial benefit from the sale … other than fees for services rendered" and, within a year of their hiring, they may not be an immediate family member or a director, officer, or employee of either the seller or buyer.

These provisions are weak at best. Competent appraisers of public utility property often work only for, or their firms regularly do other work for, public utilities. Relatively few work only for municipal entities, government agencies, or statutory government advocates. Few if any work exclusively on behalf of municipal or public utility customers.

As I discuss below, there should be more balance in those chosen to value municipal property being sold to public utilities, including the addition of someone attuned to customers' best interests.

Also, an anti-collusion prohibition should be considered to prevent the appraisers from conferring with one another or with either the buyer or seller.

Further, no appraiser or anyone in the appraiser's firm should have been employed or performed work for the municipality or utility within the previous five years and any such employment or work performed for either should be publicly disclosed.

Suggested Solution

Repeal Section 1329 and amend Section 1327 by adding a section similar to Section 1329(d)(5).

House Bill 1326 of the Regular 2015-2016 Session was also promoted with this message:

> [C]urrent statutes in Pennsylvania can restrict private regulated water utility's ability to recover an investment for acquisition of a public or private water or wastewater system to its original cost less depreciated and contributed property. **Due to this, some private and public systems are often deprived from receiving *full market value* for their assets and regulated water utilities are prevented from recouping their entire investment.**[20]

In fact, a municipal system's only value is as a provider of water or wastewater services and therefore a buyer must either be a provider of such services or become one by PUC approval. Generally, the PUC's jurisdiction does not include municipal systems, so the system's customers (or their elected or appointed representatives) can value such systems as they like when the sale is to another unregulated municipal system.

But if an investor-owned public utility is the buyer, there is a problem if much or all of the system's assets were not constructed with customer dollars but with state and federal grants and property contributed by real estate developers. Under the "no return on contributed property" rule applicable to regulated public utility ratemaking, there would be little or no "depreciated original cost rate base" upon which a return could be earned. That is, there would be little or no rate base

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[20] *See* ATTACHMENT C hereto (emphasis and bolding added). I have already discussed why fair market value is inappropriate in public utility ratemaking, and why it is poor public policy to force a utility's customers to subsidize the utility's acquisition of healthy, well-managed municipal systems.

value to be added to the acquiring utility's rate base and the utility could not recover its purchase price in higher future rates.

With the addition of Code Section 1327(a) in 1990 with liberalizing amendments in 1995, the disincentive for public utilities to acquire *distressed or non-viable* systems was eliminated. As already noted, that section creates a rebuttable presumption that the excess of acquisition costs over the depreciated original cost of the acquired system is reasonable and includable in the acquiring utility's rate base if specified criteria are satisfied.

But, again, many municipal systems have little or no depreciated original cost rate base (or they lack the records to establish one). Therefore, there is no basis to calculate an "excess" purchase price that can be rebuttably presumed to be reasonable under Section 1327(a). What to do?

Pennsylvania Consumer Advocate Patrick Cicero has provided the solution: Repeal Section 1329 and amend Section 1327(a) by adding a provision for small or distressed municipal acquisitions that is similar to Section 1329(d)(5)—"The original source of funding for any part of the water or sewer assets of the selling utility shall not be relevant to determine the value of said assets." That is, allow a municipal system's contributed property to be included in its valuation when and only when the system falls within Section 1327(a)'s distressed or non-viable criteria.

The property of the municipal system would still need to be valued, contributed property and all. That valuation should be done in the same spirit as an independent actuary is provided in House Bill 1862, Printer's No. 2340, page 2, lines 17-22, and page 4, lines 13-18—a truly independent appraiser or multiple appraisers, not solely chosen by the seller and buyer, including one or more persons with the best interests of customers in mind. Stricter conflict-of-interest provisions should apply to them.

I lack adequate knowledge of the independent municipal and public utility property valuation profession and of valuation methods used between and among municipally owned systems to be more specific on how the above should be accomplished. I am certain, however, that it should not be done as Section 1329 provides.

I would be happy to discuss the foregoing with the Members of the Committee and their staff members.

APPENDIX A

§ 1329. Valuation of acquired water and wastewater systems.

(a) Process to establish fair market value of selling utility.--Upon agreement by both the acquiring public utility or entity and the selling utility, the following procedure shall be used to determine the fair market value of the selling utility:

(1) The commission will maintain a list of utility valuation experts from which the acquiring public utility or entity and selling utility will choose.

(2) Two utility valuation experts shall perform two separate appraisals of the selling utility for the purpose of establishing its fair market value.

(3) Each utility valuation expert shall determine fair market value in compliance with the Uniform Standards of Professional Appraisal Practice, employing the cost, market and income approaches.

(4) The acquiring public utility or entity and selling utility shall engage the services of the same licensed engineer to conduct an assessment of the tangible assets of the selling utility. The assessment shall be incorporated into the appraisal under the cost approach required under paragraph (3).

(5) Each utility valuation expert shall provide the completed appraisal to the acquiring public utility or entity and selling utility within 90 days of execution of the service contract.

(b) Utility valuation experts.--

(1) The utility valuation experts required under subsection (a) shall be selected as follows:

(i) one shall be selected by the acquiring public utility or entity; and

(ii) one shall be selected by the selling utility.

(2) The utility valuation experts shall not:

(i) derive any material financial benefit from the sale of the selling utility other than fees for services rendered; or

(ii) be an immediate family member of a director, officer or employee of either the acquiring public utility, entity or selling utility within a 12-month period of the date of hire to perform an appraisal.

(3) Fees paid to utility valuation experts may be included in the transaction and closing costs associated with acquisition by the acquiring utility or entity. Fees eligible for inclusion may be of an amount not exceeding 5% of the fair market value of the selling utility or a fee approved by the commission.

(c) Ratemaking rate base.--The following apply:

(1) The ratemaking rate base of the selling utility shall be incorporated into the rate base of:

(i) the acquiring public utility during the acquiring public utility's next base rate case; or

(ii) the entity in its initial tariff filing.

(2) The ratemaking rate base of the selling utility shall be the lesser of the purchase price negotiated by the acquiring public utility or entity and selling utility or the fair market value of the selling utility.

(d) Acquisitions by public utility.--The following apply:

(1) If the acquiring public utility and selling utility agree to use the process outlined in subsection (a), the acquiring public utility shall include the following as an attachment to its application for commission approval of the acquisition filed pursuant to section 1102 (relating to enumeration of acts requiring certificate):

(i) Copies of the two appraisals performed by the utility valuation experts under subsection (a).

(ii) The purchase price of the selling utility as agreed to by the acquiring public utility and selling utility.

(iii) The ratemaking rate base determined pursuant to subsection (c)(2).

(iv) The transaction and closing costs incurred by the acquiring public utility that will be included in its rate base.

(v) A tariff containing a rate equal to the existing rates of the selling utility at the time of the acquisition and a rate stabilization plan, if applicable to the acquisition.

(2) The commission shall issue a final order on an application submitted under this section within six months of the filing date of an application meeting the requirements of subsection (d)(1).

(3) If the commission issues an order approving the application for acquisition, the order shall include:

(i) The ratemaking rate base of the selling utility, as determined under subsection (c)(2).

(ii) Additional conditions of approval as may be required by the commission.

(4) The tariff submitted pursuant to subsection (d)(1)(v) shall remain in effect until such time as new rates are approved for the acquiring public utility as the result of a base rate case proceeding before the commission. The acquiring public utility may collect a distribution system improvement charge during this time, as approved by the commission under this chapter.

(5) The selling utility's cost of service shall be incorporated into the revenue requirement of the acquiring public utility as part of the acquiring utility's next base rate case proceeding. The original source of funding for any part of the water or sewer assets of the selling utility shall not be relevant to determine the value of said assets.

(e) Acquisitions by entity.--An entity shall provide all the information required by subsection (d)(1) to the commission as an attachment to its application for a certificate of public convenience filed pursuant to section 1102.

(f) Postacquisition projects.--The following apply:

(1) An acquiring public utility's postacquisition improvements that are not included in a distribution improvement charge shall accrue allowance for funds used during construction after the date the cost was incurred until the asset has been in service for a period of four years or until the asset is included in the acquiring public utility's next base rate case, whichever is earlier.

(2) Depreciation on an acquiring public utility's postacquisition improvements that have not been included in the calculation of a distribution system improvement charge shall be deferred for book and ratemaking purposes.

(g) Definitions.--The following words and phrases when used in this section shall have the meanings given to them in this section unless the context clearly indicates otherwise:

"Acquiring public utility." A water or wastewater public utility subject to regulation under this title that is acquiring a selling utility as the result of a voluntary arm's-length transaction between the buyer and seller.

"Allowance of funds used during construction." An accounting practice that recognizes the capital costs, including debt and equity funds that are used to finance the construction costs of an improvement to a selling utility's assets by an acquiring public utility.

"Entity." A person, partnership or corporation that is acquiring a selling utility and has filed or whose affiliate has filed an application with the commission seeking public utility status pursuant to section 1102.

"Fair market value." The average of the two utility valuation expert appraisals conducted under subsection (a)(2).

"Ratemaking rate base." The dollar value of a selling utility which, for postacquisition ratemaking purposes, is incorporated into the rate base of the acquiring public utility or entity.

"Rate stabilization plan." A plan that will hold rates constant or phase rates in over a period of time after the next base rate case.

"Selling utility." A water or wastewater company located in this Commonwealth, owned by a municipal corporation or authority that is being purchased by an acquiring public utility or entity as the result of a voluntary arm's-length transaction between the buyer and seller.

"Utility valuation expert." A person hired by an acquiring public utility and selling utility for the purpose of conducting an economic valuation of the selling utility to determine its fair market value.

(Apr. 14, 2016, P.L.76, No.12, eff. 60 days)

2016 Amendment. Act 12 added section 1329.

APPENDIX B

§ 1327. Acquisition of water and sewer utilities.

(a) Acquisition cost greater than depreciated original cost.--If a public utility acquires property from another public utility, a municipal corporation or a person at a cost which is in excess of the original cost of the property when first devoted to the public service less the applicable accrued depreciation, it shall be a rebuttable presumption that the excess is reasonable and that excess shall be included in the rate base of the acquiring public utility, provided that the acquiring public utility proves that:

(1) the property is used and useful in providing water or sewer service;

(2) the public utility acquired the property from another public utility, a municipal corporation or a person which had 3,300 or fewer customer connections or which was nonviable in the absence of the acquisition;

(3) the public utility, municipal corporation or person from which the property was acquired was not, at the time of acquisition, furnishing and maintaining adequate, efficient, safe and reasonable service and facilities, evidence of which shall include, but not be limited to, any one or more of the following:

(i) violation of statutory or regulatory requirements of the Department of Environmental Resources or the commission concerning the safety, adequacy, efficiency or reasonableness of service and facilities;

(ii) a finding by the commission of inadequate financial, managerial or technical ability of the small water or sewer utility;

(iii) a finding by the commission that there is a present deficiency concerning the availability of water, the palatability of water or the provision of water at adequate volume and pressure;

(iv) a finding by the commission that the small water or sewer utility, because of necessary improvements to its plant or distribution system, cannot reasonably be expected to furnish and maintain adequate service to its customers in the future at rates equal to or less than those of the acquiring public utility; or

(v) any other facts, as the commission may determine, that evidence the inability of the small water or sewer utility to furnish or maintain adequate, efficient, safe and reasonable service and facilities;

(4) reasonable and prudent investments will be made to assure that the customers served by the property will receive adequate, efficient, safe and reasonable service;

(5) the public utility, municipal corporation or person whose property is being acquired is in agreement with the

acquisition and the negotiations which led to the acquisition were conducted at arm's length;

(6) the actual purchase price is reasonable;

(7) neither the acquiring nor the selling public utility, municipal corporation or person is an affiliated interest of the other;

(8) the rates charged by the acquiring public utility to its preacquisition customers will not increase unreasonably because of the acquisition; and

(9) the excess of the acquisition cost over the depreciated original cost will be added to the rate base to be amortized as an addition to expense over a reasonable period of time with corresponding reductions in the rate base.

(b) Procedure.--The commission, upon application by a public utility, person or corporation which has agreed to acquire property from another public utility, municipal corporation or person, may approve an inclusion in rate base in accordance with subsection (a) prior to the acquisition and prior to a proceeding under this subchapter to determine just and reasonable rates if:

(1) the applicant has provided notice of the proposed acquisition and any proposed increase in rates to the customers served by the property to be acquired, in such form and manner as the commission, by regulation, shall require;

(2) the applicant has provided notice to its customers, in such form and manner as the commission, by regulation, shall require, if the proposed acquisition would increase rates to the acquiring public utility's customers by an amount in excess of 1% of the acquiring public utility's base annual revenue;

(3) the applicant has provided notice of the application to the Director of Trial Staff and the Consumer Advocate; and

(4) in addition to any other information required by the commission, the application includes a full description of the proposed acquisition and a plan for reasonable and prudent investments to assure that the customers served by the property to be acquired will receive adequate, efficient, safe and reasonable service.

(c) Hearings.--The commission may hold such hearings on the application as it deems necessary.

(d) Forfeiture.--Notwithstanding section 1309 (relating to rates fixed on complaint; investigation of costs of production), the commission, by regulation, shall provide for the removal of the excess costs of acquisition from its rates, or any portion thereof, found by the commission to be unreasonable and to refund any excess revenues collected as a result of this section, plus interest, which shall be the average rate of interest specified for residential mortgage lending by the Secretary of Banking in accordance with the act of January 30,

1974 (P.L.13, No.6), referred to as the Loan Interest and Protection Law, during the period or periods for which the commission orders refunds, if the commission, after notice and hearings, determines that the reasonable and prudent investments to be made in accordance with this section have not been completed within a reasonable time.

(e) Acquisition cost lower than depreciated original cost.--If a public utility acquires property from another public utility, a municipal corporation or a person at a cost which is lower than the original cost of the property when first devoted to the public service less the applicable accrued depreciation and the property is used and useful in providing water or sewer service, that difference shall, absent matters of a substantial public interest, be amortized as an addition to income over a reasonable period of time or be passed through to the ratepayers by such other methodology as the commission may direct. Notice of the proposed treatment of an acquisition cost lower than depreciated original cost shall be given to the Director of Trial Staff and the Consumer Advocate.

(f) Reports.--The commission shall annually transmit to the Governor and to the General Assembly and shall make available to the public a report on the acquisition activity under this title. Such report shall include, but not be limited to, the number of small water or sewer public utilities, municipal corporations or persons acquired by public utilities, and the amounts of any rate increases or decreases sought and granted due to the acquisition.

(Apr. 4, 1990, P.L.107, No.24, eff. 60 days; June 1, 1995, P.L.49, No.7, eff. 60 days; Feb. 14, 2012, P.L.72, No.11, eff. 60 days)

2012 Amendment. Act 11 amended subsec. (b) intro. par.

References in Text. The Department of Environmental Resources, referred to in subsec. (a), was abolished by Act 18 of 1995. Its functions were transferred to the Department of Conservation and Natural Resources and the Department of Environmental Protection.

APPENDIX C

HB 1326 Water & Sewer Utilities Valuation

Currently, there are community owned water and wastewater utilities whose system infrastructure is urgently in need of repair or replacement, however the system owners cannot afford to make these needed upgrades. For some of these systems, sale to a larger water or wastewater company is a welcome opportunity as it enables system improvements and ensures the continued provision of safe, reliable service.

However, current statutes in Pennsylvania can restrict private regulated water utility's ability to recover an investment for acquisition of a public or private water or wastewater system to its original cost less depreciated and contributed property. Due to this, some private and public systems are often deprived from receiving full market value for their assets and regulated water utilities are prevented from recouping their entire investment. This legislation removes these barriers by creating an ***optional*** and **voluntary** valuation appraisal process to determine the asset value while providing clarity to the valuation and rate making process when a private regulated utility acquires the water or wastewater assets of a public or private system.

This legislation provides needed alternatives as an option to communities with infrastructure needs. It removes roadblocks deterring investment from the private sector, with proven expertise, from acquiring and improving water or wastewater utilities. This appraisal option should bring a potential higher purchase price.

Bullet Points:

- The proposed legislation would help address the following:
  - *$ 31.6 Billion* – the investment needs for water and wastewater in Pennsylvania over the next 20 years.
  - *$ 190 Billion* – current private capital available for water and wastewater infrastructure.
  - *28,500* – jobs supported by a $1 Billion water or wastewater investment.
  - *$ 3.46 Billion* – economic output created for every $1 Billion invested in water or wastewater infrastructure.

- Pennsylvania's water and wastewater industry is currently fragmented and in need of infrastructure infusion. This fragmentation and lack of funding often leads to systems that may lack operations and financial expertise and access to capital necessary to fund investments that will keep their systems safe, reliable and in compliance with environmental standards.
  - Pennsylvania is home to an estimated 2,200 municipal, authority and investor-owned community drinking water systems and 1,059 wastewater systems.
  - The PUC has no jurisdiction over Pennsylvania's approximately 2,005 municipally and authority owned community drinking water systems or 992 municipal and authority owned wastewater systems.

- This proposed legislation clarifies and makes transparent the entire acquisition process.

- Can be used as a tool for municipalities to address pension and other costs. .

- Modernizes the acquisition process: Rate Base = lesser of purchase price or appraised value.

APPENDIX D

Buyer	Seller	Docket No.	As Filed Purchase Price	Purchase Price: Adjusted by Settlement or Litigation	Buyer's Appraisal	Seller's Appraisal	Average Of Appraisals	Difference of Purchase Price and Avg. of Appraisals	Percent Change of Purchase Price and Avg. of Appraisals
PAWC	McKeesport	A-2017-2606103	162,000,000	159,000,000	161,343,000	207,010,000	184,176,500	(25,176,500)	-14%
PAWC	Sadsbury	A-2018-3002437	9,250,000	8,600,000	8,910,000	9,590,000	9,250,000	(650,000)	-7%
PAWC	Exeter	A-2018-3004933	96,000,000	93,500,000	101,817,204	104,120,000	102,968,602	(9,468,602)	-9%
PAWC	Steelton	A-2019-3006880	22,500,000	21,750,000	23,221,800	21,459,591	22,340,695	(590,695)	-3%
PAWC	Kane	A-2019-3014248	17,560,000	17,560,000	24,491,405	22,885,000	23,688,203	(6,128,203)	-26%
PAWC	Royersford	A-2020-3019634	13,000,000	13,000,000	13,769,801	13,219,000	13,494,401	(494,401)	-4%
PAWC	Upper Pottsgrove	A-2020-3021460	13,750,000	13,750,000	17,023,691	17,617,000	17,320,346	(3,570,346)	-21%
PAWC	Valley	A-2020-3019859	7,325,000	7,325,000	11,570,369	10,532,405	11,051,387	(3,726,387)	-34%
PAWC	Valley	A-2020-3020178	13,950,000	13,950,000	19,081,000	19,846,000	19,463,500	(5,513,500)	-28%
PAWC	City of York	A-2021-3024681	235,000,000	235,000,000	240,336,741	269,376,640	254,856,691	(19,856,691)	-8%
PAWC	Butler Area Sewer	A-2022-3037047	231,500,000	228,000,000	246,178,265	232,429,000	239,303,633	(11,303,633)	-5%
Aqua	New Garden	A-2016-2580061	29,500,000	29,500,000	33,666,000	30,615,410	32,140,705	(2,640,705)	-8%
Aqua	Limerick	A-2017-2605434	75,100,000	75,100,000	80,098,000	76,890,000	78,494,000	(3,394,000)	-4%
Aqua	East Bradford	A-2018-3001582	5,000,000	5,000,000	8,050,000	9,236,581	8,643,291	(3,643,291)	-42%
Aqua	Cheltenham	A-2019-3008491	50,250,000	50,250,000	51,730,000	50,301,760	51,015,880	(765,880)	-2%
Aqua	East Norriton	A-2019-3009052	21,000,000	20,750,000	24,284,458	25,064,594	24,674,526	(3,924,526)	-16%
Aqua	Lower Makefield	A-2021-3024267	53,000,000	53,000,000	55,505,000	54,430,591	54,967,796	(1,967,796)	-4%
Aqua	East Whiteland	A-2021-3026132	54,930,000	17,500,000	55,668,000	57,781,458	56,724,729	(39,224,729)	-69%
Aqua	Shenandoah	A-2022-3034143	12,000,000	12,000,000	19,380,636	18,100,307	18,740,472	(6,740,472)	-36%
SUEZ	Mahoning	A-2018-3003519	4,734,800	4,734,800	5,688,000	5,384,879	5,536,440	(801,640)	-14%
SUEZ	Mahoning	A-2018-3003517	4,765,200	4,765,200	5,414,261	5,731,341	5,572,801	(807,601)	-14%