

September 20, 2017

**VIA E-FILING**

**David P. Zambito**

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Rosemary Chiavetta, Secretary  
Pennsylvania Public Utility Commission  
Commonwealth Keystone Building  
400 North Street, 2nd Floor North  
Harrisburg, PA 17120

**Re: Application of Pennsylvania-American Water Company-Wastewater under Section 1329 of the Pennsylvania Public Utility Code, 66 Pa. C.S. § 1329, for approval of the use for ratemaking purposes of the lesser of the fair market value or the negotiated purchase price of The Municipal Authority of the City of McKeesport's assets related to its wastewater collection and treatment system and other related transactions; Docket No. A-2017-2606103**

**JOINT PETITION FOR SETTLEMENT OF ALL ISSUES (INCLUDING STATEMENTS IN SUPPORT)**

Dear Secretary Chiavetta:

Enclosed for filing with the Commission is the Joint Petition for Settlement of All Issues ("Settlement") of Pennsylvania-American Water Company, the Office of Consumer Advocate, the Bureau of Investigation & Enforcement, the City of McKeesport and the Municipal Authority of the City of McKeesport (including Statements in Support) in the above-referenced proceeding.

If you have any questions regarding this filing, please do not hesitate to contact me. Copies of the Settlement are being served on the Presiding Officers, Deputy Chief Administrative Law Judge Mark A. Hoyer and Administrative Law Judge Mary D. Long, and on all parties as indicated on the enclosed Certificate of Service. Thank you for your attention to this matter.

Sincerely,

COZEN O'CONNOR



By David P. Zambito  
Counsel for Pennsylvania-American Water Company

DPZ/kmg  
Enclosures

Rosemary Chiavetta, Secretary  
September 20, 2017  
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cc: Honorable Gladys M. Brown, Chairman  
Honorable Andrew G. Place, Vice Chairman  
Honorable John F. Coleman, Commissioner  
Honorable David W. Sweet, Commissioner  
Honorable Mark A. Hoyer (*via e-mail, including Word version and First Class Mail*)  
Honorable Mary D. Long (*via e-mail, including Word version and First Class Mail*)  
Per Certificate of Service.  
Susan Simms Marsh, Esq.

**CERTIFICATE OF SERVICE**

Application of Pennsylvania-American Water Company- :  
Wastewater under Section 1329 of the Pennsylvania :  
Public Utility Code, 66 Pa. C.S. § 1329, for approval of :  
the use for ratemaking purposes of the lesser of the fair :  
market value or the negotiated purchase price of The :  
Municipal Authority of the City of McKeesport's assets :  
related to its wastewater collection and treatment :  
system and other related transactions :

Docket No. A-2017-2606103

I hereby certify that I have this day served a true copy of the foregoing Joint Petition for Approval of Settlement of All Issues and Accompanying Statements, upon the parties, listed below, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a party).

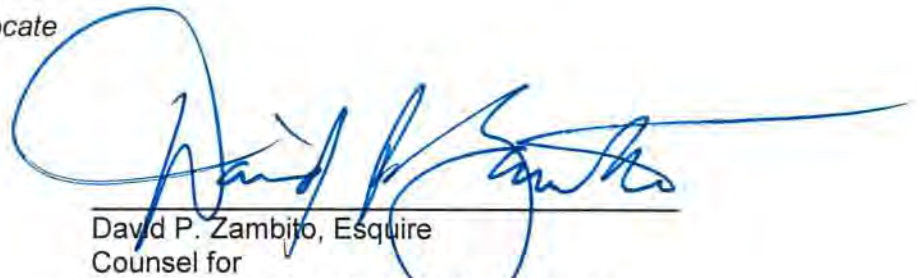
**VIA E-MAIL AND FIRST CLASS MAIL:**

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Harrisburg, PA 17101-1923  
Counsel for *Office of Consumer Advocate*

DATED: September 20, 2017



David P. Zambito, Esquire  
Counsel for  
*Pennsylvania-American Water Company*

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

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**Deputy Chief Administrative Law Judge  
Mark A. Hoyer  
and  
Administrative Law Judge Mary D. Long**

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Application of Pennsylvania-American Water Company- :  
Wastewater under Section 1329 of the Pennsylvania Public Utility :  
Code, 66 Pa. C.S. § 1329, for approval of the use for ratemaking :  
purposes of the lesser of the fair market value or the negotiated : Docket No. A-2017-2606103  
purchase price of The Municipal Authority of the City of :  
McKeesport’s assets related to its wastewater collection and :  
treatment system and other related transactions :

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**JOINT PETITION FOR APPROVAL OF  
SETTLEMENT OF ALL ISSUES**

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**I. INTRODUCTION**

Pennsylvania-American Water Company (“PAWC”), the Office of Consumer Advocate (“OCA”), the Bureau of Investigation & Enforcement of the Pennsylvania Public Utility Commission (“I&E”), the City of McKeesport (“City”) and the Municipal Authority of the City of McKeesport (“MACM”), all of the parties to the above-captioned proceeding (singularly, a “Joint Petitioner” and, collectively, the “Joint Petitioners”) hereby join in this “Joint Petition for Approval of Settlement of All Issues” (“Settlement”) and respectfully request that the Honorable Deputy Chief Administrative Law Judge Mark A. Hoyer and the Honorable Administrative Law Judge

Mary D. Long (“ALJs”) recommend approval of, and the Pennsylvania Public Utility Commission (“Commission”) approve, this Settlement without modification.

In support of the Settlement, the Joint Petitioners state the following:

## **II. BACKGROUND**

1. The Settlement pertains to the application (“Application”) filed by PAWC on May 24, 2017, pursuant to Section 1102(a) of the Pennsylvania Public Utility Code (“Code”), 66 Pa. C.S. § 1102(a), and Section 1329 of the Code, 66 Pa. C.S. § 1329, requesting (among other things) that the Commission issue Certificates of Public Convenience to PAWC for the transfer to PAWC, by sale, of substantially all of the assets, properties and rights of MACM (the “Transaction”), related to MACM’s wastewater collection and treatment system (the “System”), and to set the fair market value of the acquisition for rate-base ratemaking purposes.

2. On June 3, 2017, the Commission’s Bureau of Technical Utility Services (“TUS”) notified PAWC that it believed the Application did not contain certain required information. PAWC responded to TUS’s “Deficiency Letter” on June 8, 2017, and the Commission acknowledged receipt of the complete Application on June 14, 2017.

3. Notice of the Application was published in the *Pennsylvania Bulletin* on June 24, 2017. 47 Pa. Bull. 3568. That Notice established the deadline for filing protests and petitions to intervene as July 10, 2017.

4. I&E entered its appearance on June 21, 2017. OCA filed a Protest on June 21, 2017. On June 28, 2017, the City and MACM each filed a Petition to Intervene.

5. On June 26, 2017, PAWC filed a Petition for Protective Order to protect confidential and proprietary information. The other Joint Petitioners had no objection to the Protective Order. The ALJs issued the Protective Order on July 13, 2017.

6. On June 27, 2017, PAWC, I&E and OCA filed a Stipulation Regarding Objections and Preservation of Issues, which acknowledged that the parties to that document had differing views regarding the proper scope of Section 1329 proceedings. In an effort to streamline the instant proceedings, the parties to that document stipulated to treat the issues, objections and arguments raised in their respective briefings in *Application of Aqua Pennsylvania Wastewater, Inc. Pursuant to Sections 1102 and 1329 of the Public Utility Code for Approval of its Acquisition of the Wastewater System Assets of New Garden Township*, Docket No. A-2016-2580061, as though the parties had raised and preserved any and all such issues, objections and arguments in this proceeding.

7. Deputy Chief Administrative Law Judge Hoyer issued a Prehearing Conference Order dated June 23, 2017, which modified the Commission's procedures for formal discovery. In view of the compressed time frame to litigate this case, and as a show of good faith, the Parties voluntarily agreed to further modifications in discovery procedures to expedite this case. The ALJs' Prehearing Order adopted these procedures.

8. A prehearing conference was held on July 13, 2017. The ALJs subsequently issued a Prehearing Order on July 13, 2017. Among other things, the Prehearing Order granted the Petitions to Intervene filed by the City and MACM. That Order also established an expedited litigation schedule, in recognition of the December 14, 2017 statutory deadline for Commission action. 66 Pa. C.S. § 1329(d)(2).

9. The Joint Petitioners timely filed direct, rebuttal and surrebuttal testimony. An evidentiary hearing was held on August 3, 2017.

10. The Joint Petitioners filed Main Briefs on August 22, 2017 and Reply Briefs on September 5, 2017.

11. The Joint Petitioners had numerous meetings, telephone calls, and e-mail exchanges in an effort to settle this litigation. Their diligence and continued effort to find common ground resulted in an agreement. On September 5, 2017, after the submission of Reply Briefs, the Joint Petitioners notified the ALJs that they had reached a settlement in principle. The ALJs directed the Joint Petitioners to file a Petition for Settlement and Statements in Support on or before September 20, 2017.

### **III. SETTLEMENT TERMS**

The Joint Petitioners agree as follows:

#### **A. Approval of Application**

12. The Application shall, subject to the other terms and conditions contained in the Settlement, be approved as being in the public interest and the Commission shall issue such Certificates of Public Convenience as may be necessary to evidence its approval pursuant to 66 Pa. C.S. §§ 1102(a) of (i) the transfer, by sale, of substantially all of MACM's assets, properties and rights related to its wastewater collection and treatment system to PAWC, and (ii) PAWC's right to begin to offer, render, furnish and supply wastewater service in the areas served by MACM in the City of McKeesport, the City of Duquesne, Port Vue Borough, the Borough of Dravosburg, and a portion of West Mifflin Borough, Allegheny County, Pennsylvania and to three bulk service

interconnection points located in Liberty Borough, White Oak Borough, and North Versailles Borough, Allegheny County, Pennsylvania.

**B. Tariff**

13. The *pro forma* tariff supplement attached hereto as **Appendix A**, including all rates, rules and regulations regarding conditions of PAWC's wastewater service, shall be permitted to become effective immediately upon closing of the transaction.

**C. Fair Market Value for Ratemaking Rate Base Purposes**

14. PAWC shall be permitted to use \$158,000,000 for ratemaking rate base purposes for the acquired assets. Commission approval of the Transaction shall be conditioned upon PAWC's filing of a further amendment to the Asset Purchase Agreement, along with copies of required authorizations from PAWC's Board of Directors, the City's Council, and MACM's Board of Directors, that (a) adjusts the purchase price to \$159,000,000 and (b) modifies Paragraph F of the First Amendment to the Asset Purchase Agreement (regarding PAWC's obligation in the first base rate case following closing of the Transaction to propose rates that, if adopted by the Commission, would ensure that McKeesport-system customers benefit from 66 Pa. C.S. § 1311(c) in the same manner as PAWC's other customers) such that PAWC will seek to utilize 66 Pa. C.S. § 1311(c) for the benefit of McKeesport system customers so long as such use is not inconsistent with PAWC's obligations under the Settlement.

15. Although the Joint Petitioners reserve the right to present adjustments and oppose adjustments to appraisals in future cases, for purposes of this proceeding, the Joint Petitioners request that the Commission accept the following adjustments:



(a) Market Approach: The purchase price for each acquisition shall be based on the actual amount paid for the assets at the time of purchase and future capital improvements shall not be included;

(b) Income Approach: The rate base / rate of return methodology is not an appropriate analysis for the appraisal;

(c) The “Going Value” and “Provision for Erosion on Return” add-ons will not be adopted or included in the appraisals; and,

(d) The overhead cost add-on will not be adopted or included in the appraisals.

#### **D. Rates**

16. Except as explicitly stated herein, nothing contained in the Settlement, or in the Commission’s approval of the Application, shall preclude any Joint Petitioner from asserting any position or raising any issue in a future PAWC base rate proceeding or in any future PAWC acquisition proceeding.

17. At the time of filing its next base rate case, PAWC shall submit a cost of service study that fully separates the costs of providing the stormwater component of wastewater services in the McKeesport service area.

18. At the time of filing its next base rate case, PAWC shall submit a cost of service study that removes all costs and revenues associated with the operations (both the sanitary component and stormwater component of the wastewater service) of the MACM system and, using the same rate design methodology it proposes to be adopted in that case, develop rates in its next base rate case that exclude the impact of the System acquisition.

19. The plant-in-service costs of the Port Vue Borough component of the System shall be identified separately in the required cost of service studies. PAWC shall separately identify the plant-in-service costs at the time that the Port Vue system was purchased, the cost of any Port Vue plant retirements, and the cost of any Port Vue plant investment.

20. In its first base rate case following the closing of the acquisition, PAWC will propose to establish a rate zone for McKeesport and increase the rates of the System to an amount equal to the Zone 1 wastewater rates of PAWC's wastewater division, unless such increase would be more than two times the system-average increase for the wastewater division (calculated on a percentage increase basis). If the increase for the System would be more than two times the system-average increase of the wastewater division, PAWC will propose that the increase for the System be capped at two times the system-average wastewater division increase in this first base rate case. PAWC, the City and the OCA agree that they will not challenge or oppose this proposal in the first base rate case; provided, however, that the Joint Petitioners expressly recognize the Commission's ultimate ratemaking authority to set just and reasonable rates and, notwithstanding anything to the contrary contained in this paragraph, may enter into a settlement of the base rate case, whether full or partial and whether unanimous or non-unanimous, on reasonable terms and conditions.

21. Notwithstanding anything to the contrary contained in this paragraph, the inclusion or exclusion of separate rates for the stormwater component of wastewater service shall, for purposes of determining whether the rate cap of Paragraph 20 of this Settlement has been reached, be dictated by the Commission's final resolution and any appeals of the issue of setting separate rates for the stormwater component of wastewater service in PAWC's currently-pending base rate proceeding at Docket No. R-2017-2595853 -- whether through approval of a settlement or through

adjudication of the issue on a contested basis. PAWC may propose the use of 66 Pa. C.S. § 1311(c) with respect to any costs that would result in System rates in excess of the cap of two times the system average increase for the wastewater division. The OCA and I&E reserve the right to challenge such proposal, including any proposal to use Section 1311(c) to shift stormwater costs.

22. In its second base rate case following the closing of the acquisition, PAWC will propose to increase the rates of the System to an amount at least equal to the Zone 1 wastewater rates of PAWC's wastewater division. If such rates are less than the cost of service for the System (as determined pursuant to the cost of study performed in conjunction with such base rate filing), PAWC agrees to propose to further move the McKeesport rates towards the system's cost of service in this second base rate case. The OCA, I&E and the City reserve their rights to fully address this proposal in the base rate case and to make other rate proposals in the base rate case. The Joint Petitioners expressly recognize the Commission's ultimate ratemaking authority to set just and reasonable rates and, notwithstanding anything to the contrary contained in this paragraph, may enter into a settlement of the base rate case, whether full or partial and whether unanimous or non-unanimous, on reasonable terms and conditions.

**E. Low Income Program Outreach**

23. Within the first 90 days of PAWC's ownership of the System, PAWC shall include a bill insert to McKeesport-area customers regarding its low income programs or alternatively shall include such information in a welcome letter to McKeesport-area customers. The bill insert or welcome letter shall include, at a minimum, a description of the available low income programs, the eligibility requirements for participation in the programs, and PAWC's contact information. PAWC also agrees to ongoing, targeted outreach to its McKeesport-area customers regarding its

low income program. The Joint Petitioners shall confer in good faith and agree upon such additional outreach prior to closing of the Transaction.

**F. Distribution System Improvement Charge**

24. Pursuant to 66 Pa. C.S. § 1329, PAWC shall be permitted to collect a distribution system improvement charge (“DSIC”) prior to the first base rate case in which the McKeesport service area plant-in-service is incorporated into rate base; provided, however, that such permission shall be conditioned upon (i) PAWC’s filing of an amended wastewater long term infrastructure improvement plan (“Amended LTIIIP”) which does not re-prioritize other existing commitments in other service areas, (ii) the Commission’s approval of the Amended LTIIIP, as may be modified in the discretion of the Commission, and (iii) PAWC’s filing of a compliance tariff supplement which incorporates the McKeesport area rate zone into its existing DSIC tariff, including all customer safeguards applicable thereto, after Commission approval of the Amended LTIIIP.

**G. Accrual of Allowance for Funds Used During Construction**

25. The Joint Petitioners acknowledge that the Application includes a request that PAWC be permitted to accrue allowance for funds used during construction (“AFUDC”) for post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. The Joint Petitioners agree that they will not contest this request in this proceeding, but they reserve their rights to litigate their positions fully in future rate cases when this issue is ripe for review. The Joint Petitioners’ assent to this term should not be construed to operate as their preapproval of PAWC’s request.

**H. Deferral of Depreciation for Post-Acquisition Improvements**

26. The Joint Petitioners acknowledge that the Application includes a request that PAWC be permitted to defer depreciation related to post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. The Joint Petitioners agree that they will not contest this request in this proceeding, but they reserve their rights to litigate their positions fully in future rate cases when this issue is ripe for review. The Joint Petitioners' assent to this term should not be construed to operate as their preapproval of PAWC's request.

**I. Transaction and Closing Costs**

27. The Joint Petitioners acknowledge that the Application includes a request that PAWC be permitted to claim transaction and closing costs associated with the Transaction. The Joint Petitioners agree that they will not contest this request in this proceeding, but they reserve their rights to litigate their positions fully in future rate cases when this issue is ripe for review. The Joint Petitioners' assent to this term should not be construed to operate as their preapproval of PAWC's request.

**J. Approval of Section 507 Agreements**

28. Pursuant to 66 Pa. C.S. § 507, the Commission shall issue Certificates of Filing or approvals for the following agreements between PAWC and a municipal corporation:<sup>1</sup>

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<sup>1</sup> OCA does not join in this paragraph but does not oppose PAWC's request.

a. Asset Purchase Agreement By and Among the City of McKeesport, The Municipal Authority of the City of McKeesport, as Seller, and Pennsylvania-American Water Company, as Buyer, Dated as of September 9, 2016, as amended by First Amendment to the Asset Purchase Agreement, Dated as of May 15, 2017, along with related City of McKeesport General Obligation Note, Series of 2016, No. R-1, related Intercept Agreement, Dated November 30, 2016, and related Second Deposit Agreement, which is yet to be executed, and as further amended by the amendment specified in Paragraph 14 of the Settlement;

b. Service Agreement By and Among The Municipal Authority of the City of McKeesport and Liberty Borough, Dated as of July 28, 2010;

c. Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Liberty Borough, Dated as of July 28, 2008;

d. Service Agreement By and Among The Municipal Authority of the City of McKeesport and Lincoln Borough, Dated as of September 15, 2009;

e. Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Lincoln Borough, Dated as of September 15, 2009;

f. Service Agreement By and Among The Municipal Authority of the City of McKeesport and Elizabeth Township, Dated as of October 14, 2008;

g. Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Elizabeth Township, Dated as of October 14, 2008;

h. Service Agreement By and Among The Municipal Authority of the City of McKeesport and The Municipal Authority of Westmoreland County for White Oak Borough, Dated as of August 2009;

i. Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and The Municipal Authority of Westmoreland County for White Oak Borough, Dated as of August 2009;

j. Service Agreement By and Among The Municipal Authority of the City of McKeesport, North Versailles Township, and The North Versailles Township Sanitary Authority, Dated as of October 1, 2008;

k. Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport, North Versailles Township, and The North Versailles Township Sanitary Authority, Dated as of August 21, 2008;

l. Service Agreement By and Among The Municipal Authority of the City of McKeesport and East McKeesport Borough, Dated as of September 11, 2008;

m. Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and East McKeesport Borough, Dated as of August 2008;

n. Service Agreement By and Among The Municipal Authority of the City of McKeesport and Versailles Borough, Dated as of October 22, 2008;

o. Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Versailles Borough, Dated as of October 22, 2008;

p. Service Agreement By and Among The Municipal Authority of the City of McKeesport and Glassport Borough, Dated as of August 19, 2008; and,

q. Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Glassport Borough, Dated as of August 19, 2008.

**K. Other Necessary Approvals**

29. The Commission shall issue any other approvals or certificates appropriate, customary, or necessary under the Code to carry out the Transaction contemplated in the Application in a lawful manner.

**L. Standard Settlement Conditions**

30. The Settlement is conditioned upon the Commission's approval of the terms and conditions contained in the Settlement without modification. If the Commission modifies the Settlement, any Joint Petitioner may elect to withdraw from the Settlement and may proceed with litigation and, in such event, the Settlement shall be void and of no effect. Such election to withdraw must be made in writing, filed with the Secretary of the Commission and served upon all parties within five (5) business days after the entry of an Order modifying the Settlement. The Joint Petitioners acknowledge and agree that the Settlement, if approved, shall have the same force and effect as if they had fully litigated this proceeding.

31. This Settlement is proposed by the Joint Petitioners to settle all issues in the instant proceeding. If the Commission does not approve the Settlement and the proceedings continue, the Joint Petitioners reserve their respective procedural rights, including the right to present additional testimony and to conduct full cross-examination, briefing and argument. The Settlement is made without any admission against, or prejudice to, any position which any Joint Petitioner may adopt in the event of any subsequent litigation of these proceedings, or in any other proceeding.

32. The Joint Petitioners acknowledge that the Settlement reflects a compromise of competing positions and does not necessarily reflect any Petitioner's position with respect to any



issues raised in this proceeding. This Settlement may not be cited as precedent in any future proceeding, except to the extent required to implement this Settlement.

33. The Joint Petitioners have jointly prepared Proposed Findings of Fact (attached as **Appendix B**), Proposed Conclusions of Law (attached as **Appendix C**), and Proposed Ordering Paragraphs (attached as **Appendix D**). These Appendices represent items that the Parties agreed to and believe are sufficient to support the approval of the Settlement.

34. Each Petitioner has prepared a Statement in Support of Settlement (attached as **Appendices E - H**) setting forth the bases upon which the Petitioner believes the Settlement to be in the public interest.

35. If the ALJs recommend approval of the Settlement without modification, the Joint Petitioners waive their rights to file Exceptions.

#### **IV. REQUEST FOR RELIEF**

WHEREFORE, Pennsylvania-American Water Company, the Office of Consumer Advocate, the Bureau of Investigation and Enforcement of the Pennsylvania Public Utility Commission, the City of McKeesport, and the Municipal Authority of the City of McKeesport, by their respective counsel, respectfully request that:

(a) The Honorable Deputy Chief Administrative Law Judge Mark A. Hoyer and the Honorable Administrative Law Judge Mary D. Long recommend approval of, and the Commission approve, this Settlement as submitted, including all terms and conditions thereof, without modification.

(b) The Commission's proceeding at Docket No. A-2017-2606103 be terminated and marked closed.

(c) The Application filed by PAWC on May 24, 2017 be granted, subject to the following conditions:

(1) That PAWC file a further amendment to the Asset Purchase Agreement, along with copies of required authorizations from PAWC's Board of Directors, the City's Council, and MACM's Board of Directors, that (a) adjusts the purchase price to \$159,000,000 and (b) modifies Paragraph F of the First Amendment to the Asset Purchase Agreement (regarding PAWC's obligation in the first base rate case following closing of the transaction to propose rates that, if adopted by the Commission, would ensure that McKeesport-system customers benefit from 66 Pa. C.S. § 1311(c) in the same manner as PAWC's other customers) such that PAWC will seek to utilize 66 Pa. C.S. § 1311(c) for the benefit of McKeesport system customers so long as such use is not inconsistent with PAWC's obligations under the Commission's Order.

(2) That, at the time of filing its next base rate case, PAWC shall submit a cost of service study that fully separates the costs of providing the stormwater component of wastewater services in the McKeesport service area.

(3) That, at the time of filing its next base rate case, PAWC shall submit a cost of service study that removes all costs and revenues associated with the operations (both the sanitary component and stormwater component) of the wastewater service of the System and, using the same rate design methodology it proposes to be adopted in that case, develop rates in its next base rate case that exclude the impact of the System acquisition.

(4) That the plant-in-service costs of the Port Vue Borough component of the System shall be identified separately in the required cost of service studies. PAWC shall

separately identify the plant-in-service costs at the time that the Port Vue system was purchased, the cost of any Port Vue plant retirements, and the cost of any Port Vue plant investment.

(d) The Commission issue Certificates of Public Convenience under 66 Pa. C.S. §§ 1102(a) and 1103(a) evidencing Commission approval of: (a) the transfer, by sale, of substantially all of MACM's assets, properties and rights related to its wastewater collection and treatment system to PAWC; and (b) PAWC's right to begin to offer, render, furnish and supply wastewater service in the areas served by MACM in the City of McKeesport, the City of Duquesne, Port Vue Borough, and the Borough of Dravosburg, and a portion of West Mifflin Borough, Allegheny County, Pennsylvania and to three bulk service interconnection points located in Liberty Borough, White Oak Borough, and North Versailles Borough, Allegheny County, Pennsylvania.

(e) The Commission permit PAWC, upon closing of the Transaction, to issue a compliance tariff supplement, consistent with the *pro forma* tariff supplement attached hereto as **Appendix A**, to be effective on the date of issuance.

(f) The Commission approve, under 66 Pa. C.S. § 1329(c), a rate base addition of \$158,000,000 associated with the acquisition of the System.

(g) Although the Joint Petitioners reserve the right to present adjustments and oppose adjustments to appraisals in future cases, for purposes of this proceeding, the Joint Petitioners request that the Commission accept the following adjustments:

(1) Market Approach: The purchase price for each acquisition shall be based on the actual amount paid for the assets at the time of purchase and future capital improvements shall not be included;

(2) Income Approach: The rate base / rate of return methodology is not an appropriate analysis for the appraisal;

(3) The “Going Value” and “Provision for Erosion on Return” add-ons will not be adopted or included in the appraisals; and,

(4) The overhead cost add-on will not be adopted or included in the appraisals.

(h) Within the first 90 days of PAWC’s ownership of the System, PAWC shall include a bill insert to McKeesport-area customers regarding its low income programs or alternatively shall include such information in a welcome letter to McKeesport-area customers. The bill insert or welcome letter shall include, at a minimum, a description of the available low income programs, the eligibility requirements for participation in the programs, and PAWC’s contact information. PAWC also agrees to ongoing, targeted outreach to its McKeesport-area customers regarding its low income program. The Joint Petitioners shall confer in good faith and agree upon such additional outreach prior to closing of the Transaction.

(i) The Commission approve, under 66 Pa. C.S. § 1329(d), the collection of a distribution system improvement charge related to the System prior to the first base rate case in which the System plant-in-service is incorporated into rate base, subject to the following conditions:

(1) that PAWC files an amended wastewater long term infrastructure investment plan incorporating the McKeesport area, which does not re-prioritize other existing commitments in other service areas;

(2) that the Commission approves the amended wastewater long term infrastructure investment plan incorporating the McKeesport area, as may be modified in the discretion of the Commission; and,

(3) that PAWC files a compliance tariff supplement filing incorporating the McKeesport service territory into PAWC's existing wastewater DSIC tariff provisions.

(j) The Commission, pursuant to 66 Pa. C.S. § 1329(f), permit PAWC to accrue an allowance for funds used during construction for post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. The Commission recognizes that Joint Petitioners reserve their rights to litigate their positions fully in future rate cases when this issue is ripe for review and does not construe the Joint Petitioners' assent to this term to operate as their preapproval of PAWC's request.

(k) The Commission, pursuant to 66 Pa. C.S. § 1329(f), permit PAWC to defer depreciation related to post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. The Commission recognizes that Joint Petitioners reserve their rights to litigate their positions fully in future rate cases when this issue is ripe for review and does not construe the Joint Petitioners' assent to this term to operate as their preapproval of PAWC's request.

(l) The Commission, pursuant to 66 Pa. C.S. § 1329(d)(iv), permit PAWC to include, in its next base rate case, a claim for transaction and closing costs related to the acquisition of the MACM system. The Commission recognizes that Joint Petitioners reserve their rights to litigate their positions fully in future rate cases when this issue is ripe for review and does not construe the Joint Petitioners' assent to this term to operate as their preapproval of PAWC's request.

(m) The Commission issue Certificates of Filing or approvals for the following agreements between PAWC and a municipal corporation:

(1) Asset Purchase Agreement By and Among the City of McKeesport, The Municipal Authority of the City of McKeesport, as Seller, and Pennsylvania-American Water Company, as Buyer, Dated as of September 9, 2016, as amended by First Amendment to the Asset Purchase Agreement, Dated as of May 15, 2017, along with related City of McKeesport General Obligation Note, Series of 2016, No. R-1, related Intercept Agreement, Dated November 30, 2016, and related Second Deposit Note, which is yet to be executed, and as further amended by the amendment specified in Paragraph 14 of the Settlement;

(2) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Liberty Borough, Dated as of July 28, 2010;

(3) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Liberty Borough, Dated as of July 28, 2008;

(4) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Lincoln Borough, Dated as of September 15, 2009;

(5) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Lincoln Borough, Dated as of September 15, 2009;

(6) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Elizabeth Township, Dated as of October 14, 2008;

(7) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Elizabeth Township, Dated as of October 14, 2008;

(8) Service Agreement By and Among The Municipal Authority of the City of McKeesport and The Municipal Authority of Westmoreland County for White Oak Borough, Dated as of August 2009;

(9) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and The Municipal Authority of Westmoreland County for White Oak Borough, Dated as of August 2009;

(10) Service Agreement By and Among The Municipal Authority of the City of McKeesport, North Versailles Township, and The North Versailles Township Sanitary Authority, Dated as of October 1, 2008;

(11) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport, North Versailles Township, and The North Versailles Township Sanitary Authority, Dated as of August 21, 2008;

(12) Service Agreement By and Among The Municipal Authority of the City of McKeesport and East McKeesport Borough, Dated as of September 11, 2008;

(13) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and East McKeesport Borough, Dated as of August 2008;

(14) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Versailles Borough, Dated as of October 22, 2008;

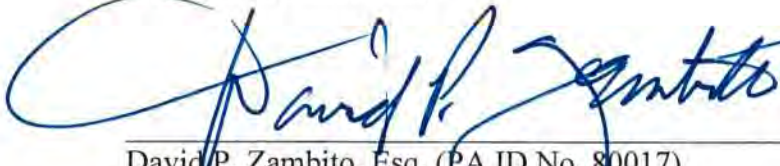
(15) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Versailles Borough, Dated as of October 22, 2008;

(16) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Glassport Borough, Dated as of August 19, 2008; and,

(17) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Glassport Borough, Dated as of August 19, 2008.

(n) The Commission issue any other approvals or certificates appropriate, customary or necessary under the Code to carry out the Transaction contemplated in the Application in a lawful manner.

Respectfully submitted,



Date: 9/20/17

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Date: \_\_\_\_\_

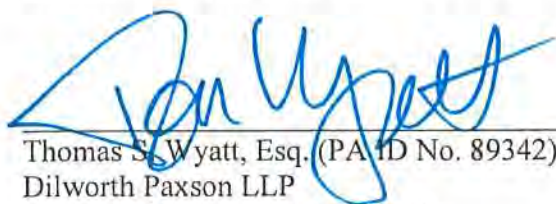
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Date: 9/20/17

Counsel for *the City of McKeesport and the  
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Appendices:

- A. *Pro Forma* Tariff Supplement
- B. Proposed Findings of Fact
- C. Proposed Conclusions of Law
- D. Proposed Ordering Paragraphs
- E. Statement in Support of Pennsylvania-American Water Company
- F. Joint Statement in Support of the City of McKeesport and the Municipal Authority of the City of McKeesport
- G. Statement in Support of the Pennsylvania Public Utility Commission's Bureau of Investigation and Enforcement
- H. Statement in Support of the Office of Consumer Advocate

**APPENDIX A. *PRO FORMA* TARIFF SUPPLEMENT**

Pennsylvania-American Water Company  
Wastewater Division  
(Hereinafter referred to as the "Company")

D/B/A

Pennsylvania American Water

RATES, RULES AND REGULATIONS  
GOVERNING THE FURNISHINGS OF  
WASTEWATER COLLECTION AND DISPOSAL SERVICE  
IN CERTAIN MUNICIPALITIES AND TERRITORIES LOCATED  
IN ADAMS COUNTY, ALLEGHENY COUNTY, BEAVER COUNTY, CHESTER COUNTY, CLARION  
COUNTY,  
CUMBERLAND COUNTY, LACKAWANNA COUNTY, MONROE COUNTY, NORTHUMBERLAND  
COUNTY, PIKE COUNTY, WASHINGTON COUNTY AND YORK COUNTY  
ALL IN THE COMMONWEALTH OF PENNSYLVANIA

By: Jeffrey L. McIntyre, President  
Pennsylvania-American Water Company  
800 West Hersheypark Drive  
Hershey, PA 17033

Issued: ~~xxxxx~~ xx, ~~xxxx~~

Effective: ~~xxxxx~~ xx, ~~xxxx~~

#### NOTICE

This tariff authorizes Pennsylvania American Water Company to furnish wastewater services to the public in the City of McKeesport, the City of Duquesne, Port Vue Borough, and the Borough of Dravosburg, Allegheny County, Pennsylvania (and related points of bulk service interconnection).  
(refer to pages 3B, 4.1x, 4.1x, 4E, xx, xx, xx)

Pennsylvania-American Water Company

LIST OF CHANGES

Changes

This tariff supplement authorizes Pennsylvania American Water Company - Wastewater Division, to begin to offer or furnish wastewater service to the public in the City of McKeesport, the City of Duquesne, Port Vue Borough, and the Borough of Dravosburg, Allegheny County, Pennsylvania (and related points of bulk service interconnection) as ordered by the Pennsylvania Public Utility Commission at Docket No. A-2017-xxxxxx entered xxxxx xx, 20xx.

I) Indicates Increase, (D) Indicates Decrease, (C) Indicates Change

Issued: xxxxx xx, xxxxx

Effective: xxxxx xx, xxxxx

Pennsylvania-American Water Company

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Pennsylvania-American Water Company

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(C)

Pennsylvania-American Water Company

**TERRITORIES SERVED**

**Coatesville**

Chester County. The City of Coatesville, the Borough of Parkesburg and portions of the Borough of South Coatesville and portions of the Townships of Caln, East Fallowfield, Highland, Sadsbury, Valley, West Caln and West Sadsbury.

**Clarion**

Clarion County. Clarion Borough and Shippenville Borough and portions of the Townships of Elk, Clarion, Monroe and Paint.

**Claysville**

Washington County. Claysville Borough and portions of the Townships of Donegal.

**Pocono**

Monroe County. A portion of Coolbaugh Township.

**Northeast - Lehman Pike and Blue Mountain Lakes**

Monroe County. Portions of the Townships of Middle Smithfield, Smithfield and Stroud.

Pike County. Portions of Lehman Township.

**Clean Treatment**

Pike County. Portions of Delaware Township.

**Koppel Borough**

Beaver County. Koppel Borough.

**Franklin Township**

Adams County. Portions of Franklin Township.

**Hamiltonban Township**

Adams County. Portions of Hamiltonban and Highland Townships.

**McEwensville Borough**

Northumberland County. McEwensville Borough.

**Fairview Township**

York County. Portions of Fairview Township.

**Borough of New Cumberland**

Cumberland County. The Borough of New Cumberland.

**Scranton Sewer**

Lackawanna County. The City of Scranton and the Borough of Dunmore.

**McKeesport Wastewater**

Allegheny County. The City of McKeesport, the City of Duquesne, Port Vue Borough, the Borough of Dravosburg, and a portion of West Mifflin Borough (and related points of bulk service interconnection).

(C)

Pennsylvania-American Water Company

RATES FOR RATE ZONE 13

Applicability: The rates as set forth below will be in effect for all former customers of the Municipal Authority of the City of McKeesport.

McKeesport - All Customers

5/8" Meter	0 - 2,000 gallons per month	\$30.70
	All over 2,000 gallons per month	\$1.275 per 100 gallons
3/4" Meter	0 - 2,000 gallons per month	\$30.70
	All over 2,000 gallons per month	\$1.275 per 100 gallons
1" Meter	0 - 5,000 gallons per month	\$76.75
	All over 5,000 gallons per month	\$1.275 per 100 gallons
2" Meter	0 - 18,000 gallons per month	\$276.30
	All over 18,000 gallons per month	\$1.275 per 100 gallons
3" Meter	0 - 35,000 gallons per month	\$537.25
	All over 35,000 gallons per month	\$1.275 per 100 gallons
4" Meter	0 - 47,000 gallons per month	\$721.45
	All over 47,000 gallons per month	\$1.275 per 100 gallons
6" Meter	0 - 95,000 gallons per month	\$1,458.25
	All over 95,000 gallons per month	\$1.275 per 100 gallons

Duquesne, Dravosburg and West Mifflin - All Customers

	0 - 2,000 gallons per month	\$30.70
	All over 2,000 gallons per month	\$1.275 per 100 gallons

Port Vue - All Customers

Monthly

	0 - 1,400 gallons per month	\$19.35
	All over 1,400 gallons per month	\$0.995 per 100 gallons

Quarterly

	0 - 4,000 gallons per month	\$58.05
	All over 4,000 gallons per month	\$0.995 per 100 gallons

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Issued:    xxxx xx,    xxxx                   Effective:   xxxx xx,    xxxx

RATES FOR RATE ZONE 13 - (Cont'd)

Bulk Customers - Versailles, Elizabeth, Liberty, Glassport,  
Lincoln, North Versailles, White Oak and East McKeesport.

All usage \$.840 Per 100 gallons

Flat Rate Account:

\$50.40 per month (Based on 6,000 gallons per month)

\$151.20 per quarter (Based on 18,000 gallons per quarter)

Provided sewage flow meters are installed, on or after January 1, 2018, during any billing period in which the gross volume of sewage from the municipality exceeds 350% of the aggregate quantity of water used by the municipality's water users, the municipality shall pay PAWC's prevailing rates for handling the excess, in addition to the sewage charges set forth above.

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Issued:    x0000 xx,    x000

Effective:   x0000 xx,    x000

Schedule of Miscellaneous Fees and Charges

E. Wastewater Plant, Residential Septage and Commercial Waste Disposal Fee.

The Fee to be paid by private contractors to the Company to dispose of private residential septage and commercial Wastes at the Company's wastewater treatment plant.

The following rates shall be charged to haulers of residential septic waste who deliver waste:

Rate Zones 1 Through 12

(C)

<u>% Solids</u>	<u>% Solids</u>	<u>Cost Per Gallon</u>
	< = 0.5%	\$.0200
	< = 1%	.0250
> 1%	< = 2%	.0300
> 2%	< = 3%	.0345
> 3%	< = 4%	.0395
> 4%	< = 5%	.0445
> 5%	< = 6%	.0495
> 6%	< = 7%	.0545
> 7%	< = 8%	.0590

Rate Zone 13 (McKeesport Area)

(C)

<u>% Solids</u>	<u>Cost Per Gallon</u>
< = 4%	\$.040
> 4%	\$.010 per % Solids

1. The Company reserves the right to limit the total amount of residential septage received in a day and /or the total numbers of loads received from a single hauler on a per day basis based on maintaining proper operation of the Company's wastewater treatment plant.
  
2. At the discretion of the Company, the Company reserves the right to accept or reject commercially generated waste based on the amount and constituents in the waste. The cost, as determined by the Company, for testing and disposal will be a multiple of the residential septage fee based on the type and strength of the waste.

tion T. Industrial Pretreatment Program (McKeesport-Area) Compliance (C)

This Section applies to Industrial and Commercial customers served under Rate Zone 13 of this tariff. All such customers shall comply with the "Industrial Pretreatment Program (McKeesport-Area)" ("IPP-M") as required by and submitted to the Pennsylvania Department of Environmental Protection and as may be amended from time to time. The currently effective IPP-M will be made available on the Company's website.

Such customers shall be responsible for the charges and fees scheduled below related to the implementation, administration, and enforcement of the IPP-M, and for the additional costs for treatment of wastewaters from such customers who have loadings and characteristics that are in excess of Domestic Sewage as defined by the IPP-M. Pursuant to the IPP-M, IPP-M fees are set by this tariff. IPP-M fees are separate from and in addition to all other rates chargeable by the Company under this tariff.

The fees as set forth in Schedule IPP-M-1 below will be in effect for customers subject to the IPP-M Terms as defined by IPP-M.

SCHEDULE IPP-M-1

1.1. General Fees

- 1.1.1. IWDP Application Fee: \$1,000.00
- 1.1.2. IWDP Transfer/Modification/Renewal Fee: \$250.00
- 1.1.3. Facility Inspection Fee: \$250.00 per inspection
- 1.1.4. Monitoring Report Review Fee: \$250.00 per monitoring report
- 1.1.5. Sampling and Analysis Fee: Actual cost of sampling and laboratory analysis plus 25% to cover administrative costs.
- 1.1.6. Accidental Discharge, Slug Control, and/or Monitoring Fee: Actual cost of response to accidental discharges or discharges of slugs loads, including but not limited to the costs incurred for any additional treatment or other actions required to manage such discharges, monitoring and response to such discharges, correction of any resulting contamination or other impacts to the Treatment Works, including the Collection System and Treatment Plant.

- 1.1.7. Compliance and Enforcement Fee - Administrative and Legal: Actual cost incurred by the Company for investigation and actions to address a User's non-compliance with the terms of this IPP or any IWDP.
- 1.1.8. Damage Repair: Actual cost for cleaning, repair, replacement and/or correction of any damage to the Treatment Works, including the Collection System and the Treatment Plant, caused or contributed to by a User's discharge.

1.2. Specific Fees

- 1.2.1. Industrial Loading Fee - applicable on a quarterly basis to discharges with loadings above typical Domestic Sewage loadings up to but not exceeding any applicable Local Limit or IWDP limit, based on sampling and analysis by the Company and sampling required to be reported by the User under an IWDP:

$$\text{Quarterly Fee (\$)} = Q \times \{ ((\text{BOD5 Actual} - \text{BOD5 Domestic}) \times \text{BOD5 Cost Factor}) + ((\text{NH3-N Actual} - \text{NH3-N Domestic}) \times \text{NH3-N Cost Factor}) + ((\text{TSS Actual} - \text{TSS Domestic}) \times \text{TSS Cost Factor}) \}$$

Where:

BOD5 Actual = actual concentration of BOD5 in mg/l as measured by the Company or the Industrial User

BOD5 Cost Factor = Treatment cost for BOD5 for the system = 0.0045

BOD5 Domestic = 330 mg/l, the typical concentration in Domestic Sewage

NH3-N Actual = actual concentration of NH3-N in mg/l as measured by the Company or the Industrial User

NH3-N Cost Factor = Treatment cost for NH3-N for the system = 0.0063

NH3-N Domestic = 23 mg/l, the typical concentration in Domestic Sewage

Q = Total flow for the quarter measured in thousand gallons

TSS Actual = actual concentration of TSS in mg/l as measured by the Company or the Industrial User

TSS Cost Factor = treatment cost for TSS for the system = 0.0028

TSS Domestic = 350 mg/l, the typical concentration in Domestic Sewage

1.2.2. Excess Loading Fee - applicable to discharges with loadings that exceed a Local Limit or IWDP limit:

If in any monthly period, the loading of BOD5, NH3-N, or TSS exceeds a Local Limit or IWDP limit, then for the applicable parameter, in calculating the Industrial Loading Fee under §1.2.1, the BOD5 Cost Factor, , NH3-N Cost Factor and/or TSS Cost Factor, applicable to the total loading of that parameter will be 125% of the value set forth in §1.2.1 to compensate for the additional administrative, oversight and management costs associated with managing such excessive loadings.

1.2.3. Special Discharge Fee - applicable to discharges with loadings or concentrations that exceed a Local Limit or IWDP limit and that impact sludge handling or disposal methods and costs, necessitate acquisition of nutrient credits, result in damages to the facility, or require extraordinary measures:

Fee = Actual cost incurred by the Company, including but not limited to: (1) additional costs of managing impacted sludge (including costs related to use of alternative disposal facilities, additional monitoring, etc.), (2) costs of acquiring nutrient credits to meet NPDES Permit cap limits; (3) costs of repairs to and restoration of the Treatment Works, including the Collection System and Treatment Plant; or (4) costs of implementing any other measures required to control, manage and address such excessive loadings or concentrations.



## APPENDIX B. PROPOSED FINDINGS OF FACT

### 1. Parties

- a. PAWC, a subsidiary of American Water Works Company, Inc., is the largest investor-owned public utility in Pennsylvania. It provides water and wastewater service to the public in a service territory encompassing more than 400 communities in 36 counties. It serves a combined population of over 2,300,000. PAWC St. No. 1 p. 13-14.
- b. As of December 31, 2016, PAWC furnished wastewater services to 54,691 customers in Pennsylvania and water services to 654,770 customers. PAWC St. No. 1 p. 15.
- c. The City is a city of the third class under the Constitution and laws of the Commonwealth of Pennsylvania and the City's Home Rule Charter. APA p. 1.
- d. The City is located in Allegheny County. PAWC St. No. 6 p. 4. It had 19,731 residents in 2010. PAWC St. No. 6 p. 4.
- e. MACM is a body corporate and politic, duly organized under the Pennsylvania Municipal Authorities Act. APA p. 1.
- f. MACM is run by a board, independent of the City. Tr. 80.
- g. I&E serves as the Commission's prosecutory bureau for the purposes of representing the public interest in ratemaking and service matters, and enforcing compliance with the Pennsylvania Public Utility Code, 66 Pa. C.S. §§ 101 *et seq.*,

and Commission regulations, 52 Pa. Code §§ 1.1 *et seq.* See *Implementation of Act 129 of 2008; Organization of Bureaus and Offices*, Docket No. M-2008-2071852 (Order entered August 11, 2011).

- h. The I&E analysis in the proceeding is based on its responsibility to represent the public interest. This responsibility requires balancing the interest of ratepayers, the utility company, and the regulated community as a whole. I&E St. No. 1 p. 1; I&E St. No. 2 p. 1.
- i. The OCA is a Commonwealth agency created by Act 161 of 1976 to represent the interests of consumers before the Pennsylvania Public Utility Commission. 71 P.S. § 309-2.

## 2. The System

- a. MACM owns and operates a combined wastewater collection system and three wastewater treatment plants which collect and treat wastewater from the City, the City of Duquesne, the Borough of Dravosburg, the Borough of Port Vue and a portion of the Borough of West Mifflin, Allegheny County, Pennsylvania. PAWC St. No. 3 p. 3.
- b. The System also provides wastewater service through bulk service connections to White Oak Borough, Lincoln Borough, Liberty Borough, East McKeesport Borough, Glassport Borough, Versailles Borough, Elizabeth Township and the Municipal Authority of Westmoreland County. Application, Appendices B-2 through B-16.

- c. The eight municipalities that have inter-municipal service agreements with MACM own and operate their own collection systems, which connect to the McKeesport interceptor system. PAWC St. No. 3 p. 3.
- d. The collection systems in Duquesne and Dravosburg transport sewage from their respective communities to their own wastewater treatment plants, and are not interconnected to the other systems. PAWC St. No. 3 p. 3.
- e. As of December 31, 2016, MACM furnished wastewater services directly to 12,780 customers. PAWC St. No. 1 p. 15. It provided service directly or indirectly to approximately 22,000 customers, because of the bulk service agreements with surrounding municipalities. PAWC St. No. 1-R p. 13.
- f. The System is a combined system, which conveys domestic sewage and other wastewaters and stormwater in the same system of pipes. PAWC St. No. 2 p. 10.
- g. There is no reasonable way to physically segregate the wastewater operations from the stormwater operations. PAWC St. No. 2 p. 12.
- h. MACM accepts and treats bulk sewage from eight communities via direct or adjoining municipal sewer systems. Three of these interconnections are located slightly outside of the applied-for service territory, and PAWC has requested Commission approval to continue providing bulk service at these points of interconnection. PAWC St. No. 1 p. 19.

3. The Asset Purchase Agreement and the First Amendment to the Asset Purchase Agreement
  - a. The City and MACM have considered selling or leasing the System for years. PAWC St. No. 6 p. 6.
  - b. MACM purchased the Dravosburg and Duquesne systems in 2011. OCA St. 1 at 14-15.
  - c. On February 26, 2016, MACM issued a Request for Bids for either an Asset Purchase Agreement of the MACM Wastewater Treatment Facilities or Concession Lease Agreement. PAWC St. No. 1 p. 8.
  - d. In April 2016, MACM purchased the Borough of Port Vue's wastewater system. I&E St. No. 1 p. 4.
  - e. PAWC has indicated that the Port Vue portion of the System was considered in both the negotiations for the APA and the appraisals completed by the utility valuation experts ("UVEs"). PAWC St. No. 1-R p. 9-11.
  - f. On July 29, 2016, PAWC submitted an Asset Purchase bid to acquire MACM's assets. PAWC St. No. 1 p. 8.
  - g. On September 9, 2016, MACM and PAWC entered into the Asset Purchase Agreement ("APA") for the sale of substantially all of the assets, properties and rights of the System to PAWC for the greater of: \$156,000,000 or the average of the two UVE's appraisals. PAWC St. No. 1 p. 11.

- h. In September 2016, PAWC's UVE appraised the System as having a fair market value of \$157,600,000. Application, Attachment A-5 (correspondence dated May 17, 2007, p. 2).
- i. HRG originally determined that the fair market value of the MACM system assets is \$207,010,000. HRG Appraisal p. 13.
- j. When PAWC was advised that MACM's UVE had appraised the System as having a fair market value of \$207,010,000, PAWC, the City and MACM negotiated the First Amendment to the APA. PAWC St. No. 1 p. 11-12; PAWC St. No. 1-R p. 9.
- k. On May 15, 2017, the City, MACM and PAWC entered into the First Amendment to the APA, which revised the purchase price of the System to be \$162,000,000. PAWC St. No. 1 p. 8.
- l. Following the execution of the First Amendment to the APA, the UVEs were advised of the new purchase price, and were given an opportunity to adjust their appraisals, as appropriate, in their independent discretion. PAWC St. No. 1 p. 12.
- m. In May, 2017, PAWC's UVE subsequently re-appraised the System. At that time, he found that the System had a fair market value of \$161,343,000. Application, Attachment A-5 (correspondence dated May 17, 2017 p. 1).
- n. MACM's UVE did not re-appraise the System following the negotiation of the First Amendment to the APA. During discovery, however, it was determined that MACM's UVE had understated the age of the collection system. Upon further

review, MACM's UVE appraised the System as having a fair market value of \$190,840,000. MACM St. No. 1 p. 67.

- o. MACM will receive a portion of the purchase price sufficient to pay off its debts, bonds and obligations that are not assigned to the City or PAWC. MACM will then be dissolved and terminated. PAWC. St. No. 6 Exh. MEC-3.
- p. The City will receive the balance of the purchase price under the APA. APA Section 3.02. The City indicates that it intends to use these funds to balance the budget, invest in infrastructure improvements, market the City and improve services to existing businesses and residents. PAWC St. No. 6 p. 9.

#### 4. The Application and the UVEs' Appraisals

- a. The Application was filed May 24, 2017. Application (Correspondence dated May 24, 2017).
- b. On June 3, 2017, the Commission's Bureau of Technical Utility Services notified PAWC that it believed the Application did not contain certain information. PAWC Response to Bureau of Technical Utility Service's Deficiency Letter (Correspondence dated June 8, 2017 p. 2).
- c. PAWC responded to TUS's "Deficiency Letter" on June 8, 2017. PAWC Response to Bureau of Technical Utility Service's Deficiency Letter (Correspondence dated June 8, 2017 p. 2).

- d. The Commission acknowledged receipt of the complete Application on June 14, 2017. Secretarial Letter dated June 14, 2017.
- e. Notice of the Application was published in the *Pennsylvania Bulletin* on June 24, 2017. *47 Pa. Bull.* 3568.
- f. PAWC's Application is seeking to utilize the process set forth in Section 1329 of the Public Utility Code, 66 Pa. C.S. § 1329, to determine the fair market value of the MACM system assets and the ratemaking rate base of those assets. PAWC St. No. 1 p. 4.
- g. As required by Section 1329, the parties to the APA engaged an engineer (KLH Engineers) to conduct an assessment of the tangible assets of the System. PAWC St. No. 7 pp. 13, 16.
- h. As required by Section 1329, the Application included the appraisals of PAWC's UVE and MACM's UVE. Application, Attachment A-5.
- i. PAWC selected Associated Utility Services, Inc. ("AUS") to perform an appraisal of the MACM system. PAWC St. No. 1 p. 7.
- j. AUS was approved by the Commission for placement on the Commission's Utility Valuation Expert ("UVE") Registry. PAWC St. No. 7 p. 7.
- k. MACM selected Herbert, Rowland & Grubic, Inc. ("HRG") as its utility valuation expert, to perform an appraisal of the MACM system. MACM St. No. 1 p. 2.

- l. HRG was approved by the Commission for placement on the Commission's Utility UVE Registry. MACM St. No. 1 p. 2.
- m. HRG included a "going value" of \$17.3 million in the cost approach and income approach in its Fair Market Valuation of MACM. Tr. 118; HRG Appraisal pp. 12-13.
- n. AUS did not include a "going value" in its fair market valuation of the MACM System.

#### 5. PAWC's Financial Fitness

- a. No party to this proceeding challenged PAWC's financial fitness to own and operate the System.
- b. PAWC had total assets of approximately \$4.35 billion as of December 31, 2016. PAWC had net income of approximately \$153 million for the 12 months ending December 31, 2016. PAWC St. No. 1 p. 18.
- c. In 2015, PAWC had operating income of approximately \$307 million, net income of approximately \$143 million, and cash flows from operations of approximately \$308 million. PAWC St. No. 5 p. 4.
- d. In addition to positive cash flows, PAWC may obtain financing from a line of credit, long term debt financing, and equity investments. PAWC St. No. 5 p. 4.



- e. PAWC is a large, financially sound company that has the capability to finance necessary capital additions. Given its size, access to capital and recognized strengths in system planning, capital budgeting and construction management, PAWC is well-positioned financially to provide wastewater service meeting all federal and state requirements. PAWC St. No. 5 p. 3.
- f. PAWC indicates that it will initially fund the Transaction with short-term debt and will later replace it with a combination of long-term debt and equity capital. PAWC St. No. 5 p. 5.
- g. PAWC carries a corporate credit rating of “A3” from Moody’s Investors Services and an “A” rating from Standard and Poor’s Rating Services. PAWC St. No. 5, p. 4.

#### 6. PAWC’s Technical Fitness

- a. No party to this proceeding challenged PAWC’s technical fitness to own and operate the System.
- b. PAWC currently operates 16 wastewater treatment plants in Pennsylvania. PAWC St. No. 2 p. 4; PAWC St. No. 3 p. 27.
- c. PAWC employs approximately 1,000 professionals with expertise in all areas of water and wastewater utility operations. PAWC St. No. 1 p. 14.
- d. PAWC indicates that, as a subsidiary of American Water, it has available to it the resources of American Water Works Service Company, Inc., which provides access

to highly-trained professionals with expertise in specialized areas. When operational issues arise at facilities owned by PAWC, the company states that it mobilizes engineering talent from its central engineering team, drawing on resources from the Service Company, to identify potential problems, recommend options, and develop action plans. PAWC St. No. 2 p. 5.

- e. PAWC has an ongoing program of capital investment focused on systematically replacing and adding new pipes and other infrastructure. PAWC St. No. 3 p. 18. PAWC has funded more than \$1 billion in infrastructure investment in the past five years. PAWC St. No. 3-R p. 7.
- f. PAWC states that it has experience working through transitions, and has already implemented a plan to integrate MACM employees, customers, and the MACM system into PAWC's operations. PAWC St. No. 2 p. 10.
- g. PAWC has extensive experience in the operation of wastewater collection and treatment systems. PAWC St. No. 1 p. 15-16.
- h. PAWC has the expertise to provide safe and reliable sewer services to the residents of MACM and surrounding areas. PAWC St. No. 1 p. 14.

## 7. PAWC's Legal Fitness

- a. No party to this proceeding challenged PAWC's legal fitness to own and operate the System.

- b. PAWC is a Commission-regulated public utility with a good compliance history. PAWC St. No. 1 p. 17.
- c. There are currently no pending legal proceedings challenging PAWC's ability to provide service to customers of the System. PAWC St. No. 1 p. 17.
- d. PAWC has the expertise, the record of environmental compliance, the commitment to invest in necessary capital improvements and resources, and experienced managerial and operating personnel necessary to provide safe and reliable sewer services to the residents of MACM and the surrounding area. PAWC St. No. 1 p. 14, 15.

#### 8. Benefits of the Transaction

- a. After Closing, the System will be operated as a standalone system, supported by PAWC's surrounding water and wastewater system operations, as well as PAWC's statewide operations and American Water's nationwide resources. PAWC St. No. 2 pp. 7-8.
- b. PAWC owns and operates water and wastewater facilities near McKeesport in the Pittsburgh Area and Southwestern Pennsylvania. PAWC St. No. 2 p. 6-7. The System is located adjacent to PAWC's MonValley/Elizabeth and Pittsburgh operations. PAWC provides water service to MACM's Dravosburg Borough customers. PAWC St. No. 2 p. 7. MACM's McKeesport and Port Vue customers are provided water service by the Municipal Authority of Westmoreland County

and Duquesne is provided water service by the City of Duquesne Water Department. PAWC App. A-21.

- c. PAWC has experience with the types of treatment technologies employed in the System, which involve activated sludge and SBR units similar to existing PAWC plants. PAWC St. No. 2 p. 4-5.
- d. PAWC has experience operating a CSO system – the Scranton wastewater system. PAWC also has experience operating a system that has substantial wet weather challenges due to high rates of infiltration and inflow. PAWC St. No. 2 pp. 11, 26.
- e. PAWC’s range of engineering and operational experience, and its financial resources make it equipped to address the needs of the MACM system. PAWC St. No. 3 p. 16.
- f. PAWC has a credit rating of “A3” from Moody’s Investors Services and an “A” rating from Standard and Poor’s Rating Services and has access to long term debt financing through its parent company at favorable interest rates and payment terms. When applicable, PAWC also uses low-cost financing through the Pennsylvania Infrastructure Investment Authority (“PENNVEST”) and the Pennsylvania Economic Development Financing Authority (“PEDFA”). PAWC St. No. 5 p. 4.
- g. The Transaction involves no duplication of services, so there is no adverse impact on PAWC’s existing efficiency. PAWC St. No. 2 p. 8.

- h. PAWC does not anticipate that the acquisition of the MACM System will have a negative impact on PAWC's cash flows, credit ratings or access to capital and, therefore, will not harm PAWC's financial status. PAWC St. No. 5 p. 3.
- i. PAWC has committed to offer employment to the forty-six existing MACM employees, if eligible, following closing. PAWC St. No. 1 p. 13; PAWC St. No. 2 p. 15.
- j. MACM's rates increased January 1, 2017. Tr. 44.
- k. Current customers of MACM are not protected by the Pennsylvania Public Utility Code, the Public Utility Commission, the Bureau of Investigation and Enforcement, the Office of Small Business Advocate and the Office of Consumer Advocate. MACM operates under a different regulatory framework. As a result of the Transaction, MACM's customers will receive those protections. PAWC St. No. 2 p. 23.
- l. Rates for PAWC's existing customers will not increase in the short term due to the Transaction because the MACM system has not been included in PAWC's current base rate proceeding. PAWC St. No. 4 p. 8-9; PAWC St. No. 1-R p. 6.
- m. Based on the estimated total cost of the MACM System under PAWC ownership, the initial rates for existing MACM customers will need to be increased in base rate case(s) following the end of the rate freeze for those customers to pay rates that cover more of their system's cost of service. OCA St. 1 p. 11, 13-14; OCA St. 1-S p. 2.

- n. The Transaction would add 12,780 direct customers to PAWC's existing wastewater customer base of 54,691. PAWC St. No. 1-R p. 13; PAWC St. No. 1 p. 15; and PAWC St. No. 2 p. 6-7.
- o. The goal of a cost of service study is to determine a utility's revenue requirement to provide service to its different customer classes. I&E St. No. 2 p. 21.
- p. A cost of service study can establish the existence and extent of subsidization and assist in determining the appropriate amount of revenue requirement to be shifted from the wastewater customers to water customers. I&E St. No. 2 p. 21.
- q. The need for a cost of service study should be assessed on a case-by-case basis. I&E St. No. 2-SR p. 16.
- r. In *Joint Application of Pennsylvania-American Water Company and the Sewer Authority of the City of Scranton*, Docket No. A-2016-2537209 (Order entered October 19, 2016) p. 86, the Commission stated "As with all rate design issues, the basis of rate setting is a cost of service study. The absence of a study designed with specific direction to address recovery of stormwater costs as a separate class would be an impediment to the full development of this issue in PAWC's next base rate proceeding."

## 9. Ratemaking Rate Base

- a. The Parties have agreed to a ratemaking rate base of \$158,000,000. PAWC, the City and MACM will amend the APA to include a purchase price of \$159,000,000. PAWC St. No. 4 p. 3.
- b. AUS's appraisal was prepared in compliance with USPAP. PAWC St. No. 7 p. 13.
- c. In compliance with Section 1329, AUS's appraisal used three approaches to value the System: cost, market and income approaches. PAWC St. No. 7 p. 14.
- d. HRG's appraisal was prepared in compliance with USPAP. MACM St. No. 1 p. 9.
- e. In compliance with Section 1329, HRG's appraisal used three approaches to value the System: cost, market and income approaches. MACM St. No. 1 p. 6.
- f. The OCA and I&E challenged and proposed adjustments to the appraisals of AUS and HRG in this proceeding.

## 10. Rate Stabilization Plan

- a. Upon closing, PAWC will charge MACM's current rates as its base rates within the service territory, and such base rates will not be increased until after the first anniversary of the closing date of the Transaction. APA Section 7.05(b).
- b. In light of PAWC's rate case filing history (approximately every three to four years), and under the provisions of the proposed Settlement, it is highly unlikely that rates for McKeesport area customers will be held constant pursuant to the APA

for any period after the first base rate case in which MACM assets are included. The first base rate case in which the System could be included is likely to occur in 2020 or later. PAWC St. No. 4 p. 7.

- c. Under the APA, PAWC has committed to maintaining MACM's current base rates until after the one year anniversary of the closing date of the Transaction. 66 Pa. C.S. § 1329(g); PAWC St. No. 4 pp. 6-7.

#### 11. DSIC, AFUDC, Deferred Depreciation, and Transaction and Closing Costs

- a. Pursuant to Section 1329, PAWC seeks permission to collect a DSIC for the McKeesport service area. PAWC St. No. 1 p. 4.
- b. An amended wastewater LTIIP must be filed and approved by the Commission before a DSIC can be implemented for the McKeesport service territory. PAWC St. No. 4-R p. 14.
- c. PAWC's DSIC for McKeesport (as amended to include McKeesport) would be governed by its existing DSIC tariff and all of the stated customer safeguards would be applicable. PAWC St. No. 4-R p. 15.
- d. PAWC's existing DSIC tariff was approved in Docket Nos. P-2014-2431005, *et al.* It is part of PAWC's Commission-approved tariff and therefore has the force and effect of law. PAWC St. No. 4-R p. 16.
- e. In conjunction with the LTIIP filing, PAWC will request permission to amend its existing DSIC tariff to include Rate Zone 13. Upon Commission approval of the



LTIP amendment, PAWC will make a tariff supplement compliance filing to include Rate Zone 13 (McKeesport Area) as part of the existing DSIC tariff. PAWC St. No. 4-R p. 15.

- f. PAWC will make improvements to the System after closing. PAWC St. No. 3 pp. 11-14. Some of these improvements will not be eligible for inclusion in PAWC's DSIC. PAWC St. No. 4 p. 10.
- g. PAWC seeks permission for the accrual of AFUDC for post-acquisition improvements not recovered through its DSIC for book and ratemaking purposes. PAWC St. No. 4 p. 9-10. The OCA and I&E reserve their rights to challenge the request in future rate cases.
- h. PAWC is requesting to defer depreciation related to post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. PAWC St. No. 4 p. 10. The OCA and I&E reserve their rights to challenge the request in future rate cases.
- i. PAWC has incurred transaction and closing costs associated with the acquisition of the System. PAWC St. No. 4-R pp. 12-13. The OCA and I&E reserve their rights to challenge the request in future rate cases.

## 12. Rates

- a. As required by Section 1329, PAWC included a *pro forma* tariff supplement in its Application. Application, Appendix A-13.

- b. During discovery, PAWC revised the *pro forma* tariff supplement to reflect a rate that is established in MACM's existing bulk service agreements with municipalities. PAWC St. No. 4-R, Exhibit RPN-1.
- c. Under the *pro forma* tariff (as revised), MACM's customers will be governed by rates for new PAWC Rate Zone 13. After PAWC closes on the Transaction, System customers will be subject to PAWC's prevailing wastewater tariff with respect to all rates other than the customer charge and consumption charge, including capacity reservation fees, reconnection fees and the like, as well as non-rate related terms and conditions of service. PAWC St. No. 4 p. 4.
- d. System customers will continue to be billed monthly after closing, except that Port Vue Borough customers will continue to be billed quarterly. PAWC St. No. 4 p. 4.
- e. Industrial Pretreatment Program (McKeesport) provisions in the *pro forma* tariff supplement would require industrial users discharging to the MACM system to comply with the industrial pretreatment program and establish fees. PAWC St. No. 3 p. 20.

### 13. Municipal Agreements

- a. MACM currently has two agreements each, with eight municipalities, which PAWC would assume as part of the Transaction, in order to provide bulk service to surrounding communities following closing. PAWC St. No. 1 p. 20.

- b. Approval of these contracts is reasonable and serves an important public purpose because the bulk services provided under the contracts are essential to the provision of wastewater service in neighboring communities. PAWC St. No. 1 p. 20.

## APPENDIX C. PROPOSED CONCLUSIONS OF LAW

1. The Commission has jurisdiction over the subject matter of, and the parties to, this application proceeding. 66 Pa. C.S. §§ 1102, 1103, 1329.
2. Commission policy promotes settlement. *See* 52 Pa. Code § 5.231.
3. A settlement lessens the time and expense that the parties must expend litigating a case and, at the same time, conserves precious administrative resources. The Commission has indicated that settlement results are often preferable to those achieved at the conclusion of a fully-litigated proceeding. *See* 52 Pa. Code § 69.401.
4. In order to accept a settlement, the Commission must determine that the proposed terms and conditions are in the public interest. *Pa. Pub. Util. Comm'n v. York Water Co.*, Docket No. R-00049165 (Order entered Oct. 4, 2004); *Pa. Pub. Util. Comm'n v. C.S. Water and Sewer Assocs.*, 74 Pa. P.U.C. 767 (1991).
5. The Settlement and its proposed terms and conditions are in the public interest and, therefore, should be approved without modification.
6. The Commission may issue a certificate of public convenience upon a finding that “the granting of such certificate is necessary or proper for the service, accommodation, convenience, or safety of the public.” 66 Pa. C.S. § 1103(a) (“Procedure to obtain certificates of public convenience”).
7. A certificate of public convenience is required for “any public utility to begin to offer, render, furnish or supply within this Commonwealth service of a different nature or to a different territory than that authorized . . . .” 66 Pa. C.S. § 1102(a)(1).

8. A certificate of public convenience is required for “any public utility . . . to acquire from . . . any person or corporation, including a municipal corporation, by any method or device whatsoever . . . the title to, or possession or use of, any tangible or intangible property used or useful in the public service.” 66 Pa. C.S. § 1102(a)(3).

9. An applicant for a certificate of public convenience must demonstrate that it is technically, financially, and legally fit to own and operate the acquired public utility assets. *Seaboard Tank Lines v. Pa. Pub. Util. Comm’n*, 502 A.2d 762, 764 (Pa. Cmwlth. 1985); *Warminster Township Mun. Auth. v. Pa. Pub. Util. Comm’n*, 138 A.2d 240, 243 (Pa. Super. 1958).

10. The fitness of a currently certificated public utility is presumed. *See e.g., South Hills Movers, Inc. v. Pa. Pub. Util. Comm’n*, 601 A.2d 1308, 1310 (Pa. Cmwlth. 1992).

11. Financial fitness means that the applicant should possess the financial resources to provide the proposed service. *Re Perry Hassman*, 55 Pa. P.U.C. 661 (1982).

12. Technical fitness means that the applicant should have sufficient staff, facilities and operating skills to provide the proposed service. *Re Perry Hassman*, 55 Pa. P.U.C. 661 (1982); *Merz White Ways Tours v. Pa. Pub. Util. Comm’n*, 201 A.2d 446 (Pa. Super. 1964).

13. Legal fitness means that the applicant has a propensity to obey the Code and the Commission’s regulations. *Re Perry Hassman*, 55 Pa. P.U.C. 661 (1982).

14. An applicant for a certificate of public convenience must demonstrate that the transaction 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*, 449 Pa. 136, 151, 295 A.2d 825, 828 (1972).

15. In granting a certificate of public convenience, the Commission may impose such conditions as it may deem to be just and reasonable. 66 Pa. C.S. § 1103(a).

16. For an acquisition in which a municipal authority and the acquiring public utility agree to use the valuation procedure delineated in 66 Pa. C.S. § 1329, the ratemaking rate base of the selling utility shall be the lesser of the purchase price negotiated by the parties or the fair market value of the selling utility. 66 Pa. C.S. 1329(c)(2).

17. “Fair market value” is defined as “the average of the two utility valuation expert appraisals conducted under subsection (a)(2).” 66 Pa. C.S. 1329(g).

18. For an acquisition in which a municipal authority and the acquiring public utility agree to use the valuation procedure delineated in 66 Pa. C.S. § 1329, the application is to contain a tariff 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. 66 Pa. C.S. § 1329(d)(1)(v).

19. A rate stabilization plan is defined as “A plan that will hold rates constant or phase rates in over a period of time after the next base rate case.” 66 Pa. C.S. § 1329(g).

20. During the period that the pro forma tariff supplement is in effect, an acquiring public utility may collect a distribution system improvement charge, as approved by the Commission. 66 Pa. C.S. § 1329(d)(4).

21. A wastewater utility must submit a long term infrastructure improvement plan to, and receive approval from, the Commission prior to collecting a distribution system improvement charge. *Implementation of Act 11 of 2012*, Docket No. M-2012-2293611 (Final Implementation Order entered August 2, 2012).

22. PAWC must submit an amended long term infrastructure improvement plan, and receive Commission approval, before including the McKeesport service territory in its DSIC. 66 Pa. C.S. §§ 1352-1353, 52 Pa. Code §§ 121.3-121.4.

23. PAWC's distribution system improvement charge tariff has been approved by the Commission. *Petition of Pennsylvania-American Water Company Wastewater Operations for Approval of Long Term Infrastructure Improvement Plan and Approval to Establish and Implement a Distribution System Improvement Charge*, Docket Nos. P-2014-2431005, *et al.* (Order entered May 7, 2015).

24. Section 1329 permits an acquiring public utility's post-acquisition improvements, which are not included in a DSIC, to 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. 66 Pa. C.S. § 1329(f)(1).

25. Section 1329 permits an acquiring public utility to defer depreciation on post-acquisition improvements, which are not included in a DSIC. 66 Pa. C.S. § 1329(f)(2).

26. Section 1329 permits an acquiring public utility to include transaction and closing costs in its rate base, during its next base rate proceeding. 66 Pa. C.S. § 1329(d)(2). The Commission will not approve these costs during the 1329 proceeding. *Implementation of Section 1329 of the Public Utility Code*, Docket No. M-2016-2543193 (Final Implementation Order entered October 27, 2016).

27. A contract between a municipality and a public utility (other than a contract to furnish service at regular tariff rates) must be filed with the Commission at least 30 days before the effective date of the contract. The Commission may approve it by issuing a certificate of filing or institute proceedings to determine whether there are any issues with the reasonableness, legality, or any other matter affecting the validity of the contract. 66 Pa. C.S. § 507.

## APPENDIX D. PROPOSED ORDERING PARAGRAPHS

IT IS ORDERED THAT:

1. The Joint Petition for Approval of Settlement of All Issues, filed by Pennsylvania-American Water Company, the City of McKeesport, the Municipal Authority of the City of McKeesport, the Office of Consumer Advocate, and the Pennsylvania Public Utility Commission's Bureau of Investigation and Enforcement on September 20, 2017 at Docket No. A-2017-2606103, including all terms and conditions thereof, is approved without modification.

2. The proceeding at Docket No. A-2017-2606103 is terminated and marked closed.

3. The Application filed by PAWC on May 24, 2017 is granted, subject to the following conditions:

(a) That PAWC file a further amendment to the Asset Purchase Agreement, along with copies of required authorizations from PAWC's Board of Directors, the City's Council, and MACM's Board of Directors, that (a) adjusts the purchase price to \$159,000,000 and (b) modifies Paragraph F of the First Amendment to the Asset Purchase Agreement (regarding PAWC's obligation in the first base rate case following closing of the transaction to propose rates that, if adopted by the Commission, would ensure that McKeesport-system customers benefit from 66 Pa. C.S. § 1311(c) in the same manner as PAWC's other customers) such that PAWC will seek to utilize 66 Pa. C.S. § 1311(c) for the benefit of McKeesport system customers so long as such use is not inconsistent with PAWC's obligations under the Commission's Order.



(b) That, at the time of filing its next base rate case, PAWC shall submit a cost of service study that fully separates the costs of providing the stormwater component of wastewater services in the McKeesport service area.

(c) That, at the time of filing its next base rate case, PAWC shall submit a cost of service study that removes all costs and revenues associated with the operations (both the sanitary component and stormwater component of the wastewater service of the MACM system and using the same rate design methodology it proposes to be adopted in that case, develop rates in its next base rate case that exclude the impact of the MACM system acquisition.

(d) That the plant-in-service costs of the Port Vue Borough component of the system shall be identified separately in the required cost of service studies. PAWC shall separately identify the plant-in-service costs at the time that the Port Vue system was purchased, the cost of any Port Vue plant retirements, and the cost of any Port Vue plant investment.

4. The Commission's Secretary's Bureau shall issue Certificates of Public Convenience under 66 Pa. C.S. §§ 1102(a) and 1103(a) evidencing Commission approval of: (a) the transfer, by sale, of substantially all of MACM's assets, properties and rights related to its wastewater collection and treatment system to PAWC; and (b) PAWC's right to begin to offer, render, furnish and supply wastewater service in the areas served by MACM in the City of McKeesport, the City of Duquesne, Port Vue Borough, and the Borough of Dravosburg, and a portion of West Mifflin Borough, Allegheny County, Pennsylvania and to three bulk service interconnection points located in Liberty Borough, White Oak Borough, and North Versailles Borough, Allegheny County, Pennsylvania.

5. Upon closing of the Transaction, PAWC shall issue a compliance tariff supplement, consistent with the *pro forma* tariff supplement attached to the Joint Petition for Approval of Settlement of All Issues, to be effective on the date of issuance.

6. Pursuant to 66 Pa. C.S. § 1329(c), the Commission approves a rate base addition of \$158,000,000 associated with PAWC's acquisition of the MACM system.

7. Although the Commission acknowledges that the Joint Petitioners reserve the right to present adjustments and oppose adjustments to appraisals in future cases, for purposes of this proceeding, the Commission accepts the following adjustments:

(a) Market Approach: The purchase price for each acquisition shall be based on the actual amount paid for the assets at the time of purchase and future capital improvements shall not be included;

(b) Income Approach: The rate base / rate of return methodology is not an appropriate analysis for the appraisal;

(c) The "Going Value" and "Provision for Erosion on Return" add-ons will not be adopted or included in the appraisals; and,

(d) The overhead cost add-on will not be adopted or included in the appraisals.

8. Within the first 90 days of PAWC's ownership of the System, PAWC shall include a bill insert to McKeesport-area customers regarding its low income programs or alternatively shall include such information in a welcome letter to McKeesport-area customers. The bill insert or welcome letter shall include, at a minimum, a description of the available low income programs, the eligibility requirements for participation in the programs, and PAWC's contact information. PAWC also agrees to ongoing, targeted outreach to its McKeesport-area customers regarding its

low income program. The Joint Petitioners shall confer in good faith and agree upon such additional outreach prior to closing of the Transaction.

9. Pursuant to 66 Pa. C.S. § 1329(d), PAWC may collect a distribution system improvement charge related to the MACM system prior to the first base rate case in which the System plant-in-service is incorporated into PAWC's rate base, subject to the following conditions:

(a) PAWC files an amended wastewater long term infrastructure investment plan incorporating the McKeesport area, which does not re-prioritize other existing commitments in other service areas;

(b) the Commission approves the amended wastewater long term infrastructure investment plan incorporating the McKeesport area, as may be modified in the discretion of the Commission; and

(c) PAWC files a compliance tariff supplement filing incorporating the McKeesport service territory into PAWC's existing wastewater DSIC tariff provisions.

10. Pursuant to 66 Pa. C.S. § 1329(f), PAWC may accrue an allowance for funds used during construction for post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. The Commission recognizes that Joint Petitioners reserve their rights to litigate their positions fully in future rate cases when this issue is ripe for review and does not construe the Joint Petitioners' assent to this term to operate as their preapproval of PAWC's request.

11. Pursuant to 66 Pa. C.S. § 1329(f), PAWC may defer depreciation related to post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. The Commission recognizes that Joint Petitioners reserve their rights to litigate their positions fully in

future rate cases when this issue is ripe for review and does not construe the Joint Petitioners' assent to this term to operate as their preapproval of PAWC's request.

12. Pursuant to 66 Pa. C.S. § 1329(d)(iv), PAWC may include, in its next base rate case, a claim for transaction and closing costs related to the acquisition of the MACM system. The Commission recognizes that Joint Petitioners reserve their rights to litigate their positions fully in future rate cases when this issue is ripe for review and does not construe the Joint Petitioners' assent to this term to operate as their preapproval of PAWC's request.

13. The Commission's Secretary's Bureau shall issue Certificates of Filing pursuant to Section 507 for the following agreements between PAWC and a municipal corporation:

(a) Asset Purchase Agreement By and Among the City of McKeesport, The Municipal Authority of the City of McKeesport, as Seller, and Pennsylvania-American Water Company, as Buyer, Dated as of September 9, 2016, as amended by First Amendment to the Asset Purchase Agreement, Dated as of May 15, 2017, along with related City of McKeesport General Obligation Note, Series of 2016, No. R-1, related Intercept Agreement, Dated November 30, 2016, and related Second Deposit Note, which is yet to be executed, and as further amended by the amendment specified in Paragraph 14 of the Settlement;

(b) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Liberty Borough, Dated as of July 28, 2010;

(c) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Liberty Borough, Dated as of July 28, 2008;

(d) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Lincoln Borough, Dated as of September 15, 2009;

(e) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Lincoln Borough, Dated as of September 15, 2009;

(f) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Elizabeth Township, Dated as of October 14, 2008;

(g) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Elizabeth Township, Dated as of October 14, 2008;

(h) Service Agreement By and Among The Municipal Authority of the City of McKeesport and The Municipal Authority of Westmoreland County for White Oak Borough, Dated as of August 2009;

(i) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and The Municipal Authority of Westmoreland County for White Oak Borough, Dated as of August 2009;

(j) Service Agreement By and Among The Municipal Authority of the City of McKeesport, North Versailles Township, and The North Versailles Township Sanitary Authority, Dated as of October 1, 2008;

(k) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport, North Versailles Township, and The North Versailles Township Sanitary Authority, Dated as of August 21, 2008;

(l) Service Agreement By and Among The Municipal Authority of the City of McKeesport and East McKeesport Borough, Dated as of September 11, 2008;

(m) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and East McKeesport Borough, Dated as of August 2008;

(n) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Versailles Borough, Dated as of October 22, 2008;

(o) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Versailles Borough, Dated as of October 22, 2008;

(p) Service Agreement By and Among The Municipal Authority of the City of McKeesport and Glassport Borough, Dated as of August 19, 2008; and,

(q) Corrective Action Agreement By and Among The Municipal Authority of the City of McKeesport and Glassport Borough, Dated as of August 19, 2008.

14. All other approvals or certificates appropriate, customary or necessary under the Pennsylvania Public Utility Code to carry out the transaction contemplated in the Application in a lawful manner, are granted.

**APPENDIX E. STATEMENT IN SUPPORT OF  
PENNSYLVANIA-AMERICAN WATER COMPANY**

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

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**Deputy Chief Administrative Law Judge  
Mark A. Hoyer  
and  
Administrative Law Judge Mary D. Long**

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Application of Pennsylvania-American Water Company- :  
Wastewater under Section 1329 of the Pennsylvania Public Utility :  
Code, 66 Pa. C.S. § 1329, for approval of the use for ratemaking :  
purposes of the lesser of the fair market value or the negotiated : Docket No. A-2017-2606103  
purchase price of The Municipal Authority of the City of :  
McKeesport’s assets related to its wastewater collection and :  
treatment system and other related transactions :

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**STATEMENT OF PENNSYLVANIA-AMERICAN WATER  
COMPANY IN SUPPORT OF JOINT PETITION FOR  
APPROVAL OF SETTLEMENT OF ALL ISSUES**

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Pennsylvania-American Water Company (“PAWC”) files this Statement in Support of the Joint Petition for Approval of Settlement of All Issues (“Settlement”), entered into by PAWC, the City of McKeesport (the “City”), the Municipal Authority of the City of McKeesport (“MACM”), the Pennsylvania Public Utility Commission’s Bureau of Investigation and Enforcement (“I&E”), and the Office of Consumer Advocate (“OCA”) (hereinafter, collectively, the “Joint Petitioners”) in the above-captioned proceeding. PAWC respectfully requests that the Honorable Deputy Chief Administrative Law Judge Mark A. Hoyer and the Honorable Administrative Law Judge Mary D. Long (“ALJs”) recommend approval of, and that the Pennsylvania Public Utility Commission



("Commission") approve, the Settlement, including all terms and conditions thereof, without modification.

## **I. INTRODUCTION**

The Settlement pertains to the application ("Application") filed by PAWC pursuant to Section 1102(a) of the Pennsylvania Public Utility Code ("Code"), 66 Pa. C.S. § 1102(a), and Section 1329 of the Code, 66 Pa. C.S. § 1329, requesting (among other things) that the Commission issue Certificates of Public Convenience to PAWC for the transfer to PAWC, by sale, of substantially all of the assets, properties and rights of MACM (the "Transaction"), related to MACM's wastewater collection and treatment system (the "System"), and to set the fair market value of the acquisition for rate-base ratemaking purposes.

The Settlement, if approved, will resolve all of the issues raised in this proceeding. The Settlement is in the best interest of the City, MACM and its existing customers, PAWC and its existing customers, and the public-at-large. It is in the public interest and, accordingly, should be approved.

Commission policy promotes settlements. *See* 52 Pa. Code § 5.231. Settlements lessen the time and expense that the parties must expend litigating a case and, at the same time, conserve precious administrative resources. The Commission has indicated that settlement results are often preferable to those achieved at the conclusion of a fully-litigated proceeding. *See* 52 Pa. Code § 69.401. In order to accept a settlement, the Commission must determine that the proposed terms and conditions are in the public interest. *Pa. Pub. Util. Comm'n v. York Water Co.*, Docket No. R-00049165 (Order entered October 4, 2004); *Pa. Pub. Util. Comm'n v. C.S. Water and Sewer Assocs.*, 74 Pa. P.U.C. 767 (1991).

As an initial matter, the fact that the Settlement resolves all issues is, in and of itself, strong evidence that the Settlement is reasonable and in the public interest – particularly given the diverse interests of the Joint Petitioners and the active role that they have taken in this proceeding. The Settlement was achieved through the hard work and perseverance of the Joint Petitioners. They have repeatedly demonstrated their good faith and willingness to cooperate to resolve this complex case within the six-month deadline mandated by the General Assembly in Section 1329 of the Public Utility Code (“Code”), 66 Pa. C.S. § 1329. For example, the Joint Petitioners agreed to modify the Commission’s discovery procedures; they worked together to resolve discovery disputes; they engaged in several informal discovery sessions; they voluntarily exchanged information; they entered into a Stipulation of the Parties Regarding Objections and Preservation of Issues; and no party objected to PAWC’s Petition for Protective Order. Through these collaborative efforts of the Joint Petitioners and effective case management by the ALJs, the Application is in a position to be decided by the Commission in less than six months -- demonstrating that the timeline set forth by the General Assembly in Section 1329 can indeed work effectively.

It should be noted that the Joint Petitioners, and their counsel and experts, have considerable experience in acquisition proceedings. Their knowledge, experience and ability to evaluate the strengths and weaknesses of their litigation positions provided a strong base upon which to build a consensus on all the issues. The Joint Petitioners, their counsel and experts fully explored all the issues in this case, as demonstrated by the fact that they did not reach an agreement until after the submission of Reply Briefs.

Nevertheless, as of this date, the Commission has only entered one final order in a Section 1329 proceeding – and even that order is presently pending before the Commission on a Petition

for Reconsideration. *See Application of Aqua Pennsylvania Wastewater, Inc. Pursuant to Sections 1102 and 1329 of the Public Utility Code for Approval of its Acquisition of the Wastewater System Assets of New Garden Township and the New Garden Township Sewer Authority*, Docket No. A-2016-2580061 (Order entered Jul. 20, 2017) (granting I&E's Petition for Reconsideration pending disposition on merits). Consequently, there are many as-yet-unanswered questions of law and procedure surrounding Section 1329. The Joint Petitioners negotiated the Settlement in consideration of this uncertain legal landscape. They recognized that, absent settlement, this case could have become mired in appellate litigation; and the public benefits of the acquisition potentially would not have been realized for years -- if at all.

The Settlement reflects a carefully balanced compromise of the interests of the Joint Petitioners and satisfies the various requirements of the Code. For these reasons, and the reasons set forth below, the Settlement is in the public interest and should be approved without modification.

## **II. THE SETTLEMENT IS IN THE PUBLIC INTEREST**

The Joint Petitioners have agreed to a settlement of all issues in this proceeding. This includes issues arising under Sections 1103(a), 1329 and 507 of the Code. 66 Pa. C.S. §§ 1103(a), 1329, and 507.

### **A. Section 1103 Approvals**

#### **1. Fitness**

PAWC must demonstrate that it is technically, financially, and legally fit to own and operate the System. *Seaboard Tank Lines, Inc. v. Pa. Pub. Util. Comm'n*, 502 A.2d 762, 764 (Pa.

Cmwlth. 1985); *Warminster Township Mun. Auth. v. Pa. Pub. Util. Comm'n*, 138 A.2d 240, 243 (Pa. Super. 1958). As a certificated public utility, PAWC enjoys a rebuttable presumption that it possesses the requisite fitness.<sup>1</sup> *South Hills Movers, Inc. v. Pa. Pub. Util. Comm'n*, 601 A2d 1308, 1310 (Pa. Cmwlth. 1992). Although no party challenged PAWC's fitness, PAWC introduced extensive evidence demonstrating its technical, financial, and legal fitness.

With respect to technical fitness, PAWC is the Commonwealth's largest water and wastewater provider. It furnishes service to more than 400 communities in 36 counties, serving a combined population in excess of 2,300,000. PAWC St. No. 1 pp. 13-14. PAWC employs approximately 1,000 professionals with expertise in all areas of water and wastewater utility operations. PAWC St. No. 1 p. 14. In addition, as a subsidiary of American Water Works Company, Inc. ("American Water"), PAWC has available to it the resources of American Water Works Service Company, Inc. ("Service Company"), which provides access to highly-trained professionals with expertise in specialized areas. When operational issues arise at facilities owned by PAWC, the company mobilizes engineering talent from its central engineering team, drawing on resources from the Service Company, to identify problems, recommend options, and develop action plans. PAWC St. No. 2 p. 5. PAWC has an ongoing program of capital investment focused on systematically replacing and adding new pipes and infrastructure. PAWC St. No. 3 p. 18. PAWC has funded more than \$1 billion in infrastructure investment in the past five years. PAWC St. No. 3-R p. 7.

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<sup>1</sup> Similarly, PAWC enjoys a presumption of a continuing public need for service because public utility service is already being provided in the service territory. *Re Glenn Yeager et al.*, 49 Pa. P.U.C. 138 (1975). No party has contested the need for wastewater service in the McKeesport area.

With respect to legal fitness, PAWC has a record of environmental compliance, a commitment to invest in necessary capital improvements and resources, and the experienced managerial and operating personnel necessary to provide safe and reliable sewer service to the residents of the McKeesport area. PAWC has a good compliance history with the Commission and there are currently no legal proceedings that would suggest that PAWC is not legally fit to provide service in the McKeesport area. PAWC St. No. 1 pp. 14, 15, 17.

With respect to financial fitness, PAWC had total assets of approximately \$4.35 billion as of December 31, 2016. It had a net income of approximately \$153 million for the 12 months ending December 31, 2016. PAWC St. No. 1 p. 18. In addition to positive operating cash flows, PAWC has a \$400 million line of credit, long term debt financing, and equity investments. PAWC St. No. 5 p. 4.

## **2. Public Benefit**

PAWC must demonstrate that the Transaction and PAWC's ownership/operation of the System 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*, 449 Pa. 136, 151, 295 A.2d 825, 828 (1972). An acquisition provides an affirmative benefit if the benefits of the transaction outweigh the adverse impacts of the transaction. *Application of CMV Sewage Co., Inc.*, 2008 Pa. PUC LEXIS 950. When looking at the benefits and detriments of a transaction, the focus of the analysis must be on all affected parties, not merely a particular group or a particular geographic area. *Middletown Township v. Pa. Pub. Util. Comm'n*, 85 Pa. Cmwlth. 191, 482 A.2d 674 (1984).

The Transaction, with the conditions described in the Settlement, benefits all of the stakeholder groups impacted by the Transaction. The Transaction benefits members of the public-at-large in the following respects:

- The Transaction promotes the Commission’s policy favoring regionalization and consolidation of water and wastewater systems.
- The Transaction is beneficial from an environmental perspective because PAWC is in a better position to address environmental deficiencies and operate the System in an environmentally-friendly manner due to its greater expertise and financial resources.<sup>2</sup>
- The Transaction is beneficial from an economic perspective. Spreading fixed costs across a larger asset platform and customer base is positive toward the company’s credit and credit ratings, which facilitates borrowing at lower interest rates. Because of its size, expertise and economies of scale, PAWC will be able to improve efficiencies and lower costs that would otherwise be incurred to operate the System and fund necessary improvements.

The Transaction benefits MACM in the same way that it benefits all other members of the public-at-large. In addition, the Transaction has specific benefits for MACM:

- MACM will receive a portion of the purchase price, re-pay a PENNVEST grant, pay off its debt (including a PENNVEST loan), and then be dissolved and terminated.
- MACM voluntarily entered into the Asset Purchase Agreement (“APA”) because it wants to get out of the utility business.

The Transaction benefits the City in the same way that it benefits all other members of the public-at-large. In addition, the Transaction has specific benefits for the City:

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<sup>2</sup> The environmental benefits of the Transaction are significant because the Commission, as a trustee of the Commonwealth’s environmental resources, has an affirmative duty under the Environmental Rights Amendment of the Pennsylvania Constitution to take the superior ability of PAWC to address environmental deficiencies into consideration in weighing public benefits and deciding the Application. PA. CONST. Art. I, § 27; *see generally Pa. Environmental Defense Foundation v. Cmwlth. of Pa.*, No. 10 MAP 2015 (Pa., Slip Op. issued Jun. 20, 2017), p. 32 (*citing Robinson Twp. v. Cmwlth. of Pa.*, 83 A.3d 901, 957 (Pa. 2013)).

- The City will receive a portion of the purchase price, which it will use to promote other public purposes (such as balancing the City's budget, investing in infrastructure improvements, and improving services to City residents). These uses of the proceeds will have a ripple effect on the local economy, enhancing the economic benefits of the Transaction.
- The System will become taxable property.
- City residents who are employees of the System will keep their jobs.
- The City will avoid going into Act 47 (the Municipalities Financial Recovery Act, 53 P.S. §§ 11701.101 *et seq.*).

The Transaction benefits municipalities other than the City in the same way that it benefits all other members of the public-at-large. In addition, the Transaction will benefit municipalities other than the City in the sense that residents of these municipalities will remain customers of the System and will enjoy the same benefits of the Transaction as will all other existing customers of MACM.

The Transaction benefits MACM's existing customers in the same way that it benefits all other members of the public-at-large. In addition, the Transaction has specific benefits for MACM's existing customers:

- The Transaction will promote rate stability, in part, because PAWC will adopt MACM's base rates existing at the time of closing on the Transaction, will not increase rates until after the first anniversary of the closing date,<sup>3</sup> and is unlikely to include MACM customers in its rates until at least 2020.
- Rates will be lower under PAWC than they would be if the System remained separate and had to deal with its infrastructure and environmental issues on its own.
- The System will become a Commission-regulated utility, and its customers would gain the protection of the Code, the Commission, I&E, OCA, and the Office of Small Business Advocate.

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<sup>3</sup> PAWC, MACM and the City acknowledged in the APA that the Commission has ratemaking authority.

- Customers will have access to PAWC's proven and enhanced customer service, including its customer assistance program (H2O Help to Others) and customer dispute resolution process.

The Settlement contains an additional public benefit for MACM's existing customers, in that it requires PAWC to provide information to McKeesport-area customers regarding its low-income programs through ongoing and targeted outreach.

The Transaction benefits PAWC's existing wastewater customers in the same way that it benefits all other members of the public-at-large. In addition, the Transaction has specific benefits for PAWC's existing wastewater customers:

- In the short term, the Transaction will have no impact on the rates paid by PAWC's existing customers.
- In the long term, the Transaction will benefit PAWC's existing wastewater customers because it will add a substantial number of new customers to PAWC's wastewater customer base, who can share the cost of operating the entire PAWC wastewater system.
- The Transaction will promote the public policy goals embodied in Section 1329.
- The Transaction will promote the public policy goal of improving and maintaining public infrastructure.

The Settlement contains additional benefits for PAWC's existing customers. In order to ensure that their rates do not increase significantly due to the Transaction, the Settlement includes commitments by PAWC regarding its rate proposals in its next two base rate cases. These proposals are intended to ensure that McKeesport area customers at least pay the same rates as PAWC's Zone 1 ratepayers (or higher rates, if the Zone 1 rates are less than the costs of service for the McKeesport service territory). These commitments provide reasonable protection for PAWC's existing wastewater customers, which probably would not have resulted from a fully litigated proceeding.



It is important to note that the rate commitments of the Settlement relate only to what PAWC is obligated to propose during its next two base rate cases. The Settlement explicitly recognizes the ability of PAWC and other parties to the rate cases to settle those cases on reasonable terms and conditions. Moreover, the Settlement explicitly recognizes that the Commission retains ultimate ratemaking authority to set just and reasonable rates as a result of those future base rate cases. The Settlement's rate commitments reflect a recognition by the Joint Petitioners that the McKeesport rates must move in a reasonable and timely manner toward the true cost of service for McKeesport-area customers, including payment by those customers for the stormwater-related costs of the combined wastewater service.

Finally, the Transaction benefits PAWC's existing water customers in the same way that it benefits all other members of the public-at-large. It will not result in an increase in rates for these customers pursuant to 66 Pa. C.S. § 1311(c) unless, in a future rate case, the Commission determines that an allocation of PAWC's wastewater requirement to water customers is "in the public interest."

In short, as modified by the terms and conditions in the Settlement, the Transaction has affirmative public benefits of a substantial nature for every impacted group. These benefits clearly outweigh any alleged detriments. Accordingly, the ALJs and the Commission should find that the Settlement is in the public interest.

### **3. Cost of Service Studies**

In the interest of resolving this case and based on the unique circumstances of this case, PAWC will not object to performing the cost of service studies proposed in I&E's Main Brief. PAWC acknowledges that the acquisition will generate novel ratemaking issues that have yet to

be resolved by the Commission in the context of a base rate proceeding (including revenue allocation associated with a Section 1329 acquisition and treatment of the stormwater-related costs of combined wastewater service). Under the Settlement, PAWC's obligation to prepare cost of service studies extends only to its next base rate case. In this way, unnecessary cost of service studies can be avoided in subsequent rate cases if the novel ratemaking issues are resolved by the Commission in such a way that separate cost of service studies are not required. Accordingly, the ALJs and the Commission should find that the Settlement is in the public interest.

## **B. Section 1329 Approvals**

As noted in the Main and Reply Briefs filed in this case, the Joint Petitioners disagree on certain threshold legal issues. Due to the Settlement, there is no need for the ALJs or the Commission to address those issues in the Recommended Decision, or for the Commission to address these issues in its Order.

### **1. Ratemaking Rate Base**

PAWC, MACM, and the City agreed to use the procedure set forth in Section 1329 for the Transaction. Section 1329 created a voluntary procedure for valuing a water or wastewater system being sold by a municipality or municipal authority to a public utility or other entity. In that procedure, the buyer and the seller each obtain an appraisal of the system by a Commission-approved utility valuation expert ("UVE"). The ratemaking rate base of the selling utility is the lesser of: (1) the purchase price agreed-to by the parties, or (2) the fair market value of the selling utility (defined as the average of the two UVEs' appraisals). The ratemaking rate base of the

selling utility is then incorporated into the rate base of the acquiring public utility during the acquiring public utility's next base rate case.

The ratemaking rate base of the System was hotly contested in this proceeding. In the Settlement, the Joint Petitioners compromised on certain adjustments in the appraisals. The Joint Petitioners also agreed that PAWC, MACM and the City would amend the purchase price for the System to be \$159,000,000, but only \$158,000,000 will go into PAWC's rate base in its next rate case. The proposed Settlement should be adopted because it produces a result that is preferable, in the eyes of each of the Joint Petitioners, to what could have resulted from litigation. Moreover, the agreed-upon ratemaking rate base of \$158,000,000 is well within the range of litigation positions of the Joint Petitioners and, accordingly, supported by substantial record evidence.<sup>4</sup>

Furthermore, this result is in the public interest because it furthers the legislative intent behind Section 1329. First, the Settlement allows a municipality *who wishes to do so*<sup>5</sup> to monetize an asset for maximum value. Second, by establishing a rate base for the System that is greater than what would have been allowed using traditional ratemaking principles, PAWC is willing to enter into the Transaction. Section 1329 would be ineffective if a willing seller would be unable to find a willing buyer. Finally, the Settlement allows the parties to the Transaction to obtain the necessary Commission approval in a timely manner -- while protecting the existing customers of

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<sup>4</sup> PAWC and the City/MACM introduced evidence supporting a ratemaking rate base of \$162,000,000, *i.e.*, the lower of the purchase price (\$162,000,000) and the average of the UVE appraisals (\$176,091,500). PAWC Main Brief p. 36. OCA introduced evidence supporting a ratemaking rate base of \$151,949,698, *i.e.*, the lower of the purchase price of \$162,000,000 and the average of the UVE appraisals as adjusted by the OCA witnesses (\$151,949,698). OCA Reply Brief p. 23.

<sup>5</sup> The public purpose of this voluntary transaction is significant. As the City/MACM state in their Main Brief p. 10: "These are assets owned by the public, and the City and the Authority are compelled to achieve the true value for its citizens and surrounding communities."

the acquiring public utility. The Joint Petitioners' negotiated result is in the public interest and should be approved by the ALJs and the Commission.

## **2. Rates**

Section 1329(d)(1)(iv) of the Code requires an application to contain a tariff containing a rate equal to the existing rates of the selling utility at the time of the acquisition, together with a rate stabilization plan, if applicable to the acquisition. As demonstrated by the Joint Petitioners' briefs, there is no dispute that this case does not involve a rate stabilization plan. Consequently, the Settlement does not address this requirement.

In terms of rates, the Settlement is in the public interest because it would not only ensure that PAWC will charge rates after closing that are equal to MACM's existing rates, it includes certain commitments by PAWC about the rates it will propose in its next *two* base rate cases. As discussed above, these commitments are an important protection for PAWC's existing wastewater customers. These commitments would not have been achieved if the case had been litigated to conclusion. For all of these reasons, the Settlement should be approved.

## **3. Distribution System Improvement Charge**

Section 1329(d) of the Code permits an acquiring public utility to collect a distribution system improvement charge ("DSIC") from the date of closing on the Transaction until new rates are approved in the utility's next base rate case. In order to qualify for DSIC recovery, a utility must submit a long term infrastructure investment plan ("LTIIP") to, and receive approval from, the Commission.

PAWC has previously received Commission approval of a wastewater LTIP plan, and received Commission approval of a DSIC tariff, for other portions of its wastewater system. In its Application, PAWC requested conditional approval to implement a DSIC for the McKeesport service territory. PAWC proposed to file an amended LTIP for the McKeesport service territory. Following Commission approval of that amended LTIP, PAWC would make a tariff supplement compliance filing, which would include the McKeesport service territory in PAWC's existing DSIC tariff.

The Settlement includes conditions to ensure that PAWC's amended LTIP will not re-prioritize existing commitments in other service areas. In addition, the Settlement recognizes the Commission's authority to modify PAWC's LTIP submission. Finally, the Settlement is consistent with the Code and *Implementation of Act 11 of 2012*, Docket No. M-2012-2293611 (Final Implementation Order entered August 2, 2012). For these reasons, the Settlement is in the public interest and should be approved.

### **3. Allowance for Funds Used During Construction**

Section 1329(f)(1) of the Code permits an acquiring public utility to accrue an allowance for funds used during construction ("AFUDC") on post-acquisition improvements that are not included in a DSIC, from the date the cost was incurred until the earlier of the following events: the asset has been in service for a period of four years, or the asset is included in the acquiring utility's next base rate case. In the Application, PAWC simply requested permission to accrue AFUDC on post-acquisition improvements that are not included in a DSIC. The Settlement is in the public interest because it makes clear that the other Joint Petitioners do not oppose this request and they reserve their rights to litigate their positions fully in future rate cases.

#### **4. Deferred Depreciation**

Similarly, Section 1329(f)(2) of the Code permits an acquiring public utility to defer depreciation on its post-acquisition improvements that are not included in a DSIC. In the Application, PAWC simply requested permission to defer depreciation on post-acquisition improvements that are not included in a DSIC. The Settlement is in the public interest because it makes clear that the other Joint Petitioners do not oppose this request and they reserve their rights to litigate their positions fully in future rate cases.

#### **5. Transaction and Closing Costs**

Section 1329(d)(1)(iv) permits an acquiring public utility to include, in its next base rate case, a claim for the transaction and closing costs incurred for the acquisition. In *Implementation of Section 1329 of the Public Utility Code*, Docket No. M-2016-2543193 (Order entered October 27, 2016) p. 14, the Commission stated that there will be no Commission preapproval of the reasonableness of recovery of these costs in a Section 1329 proceeding. Out of an abundance of caution, the Application requested permission to include, in PAWC's next base rate case filed after its currently-pending base rate proceeding, the transaction and closing costs incurred in this proceeding. The Commission will adjudicate the ratemaking treatment of PAWC's claimed transaction and closing costs at that time. The Settlement is in the public interest because it makes clear that the other Joint Petitioners do not oppose this request and they reserve their rights to litigate their positions fully in future rate cases.

### **C. Section 507 Approvals**

Section 507 of the Code requires that contracts between a public utility and a municipal corporation (except for contracts to furnish service at regular tariff rates) be filed with the Commission at least 30 days before the effective date of the contract. The Commission approves the contract by issuing a certificate of filing, unless it decides to institute proceedings to determine whether there are any issues with the reasonableness, legality, or any other matter affecting the validity of the contract.

In the Application, PAWC sought Commission approval of the APA, as amended, as well as sixteen agreements between MACM and area municipalities, which PAWC will assume at closing. Approval of these seventeen agreements is necessary for PAWC to continue to provide service, directly or indirectly, to all customers presently served by the System.

The Settlement is in the public interest because it establishes that none of the other Joint Petitioners objects to the Commission's approval of these agreements pursuant to Section 507. The Commission should accordingly issue Certificates of Filing for, or otherwise approve, the identified agreements with municipal corporations.

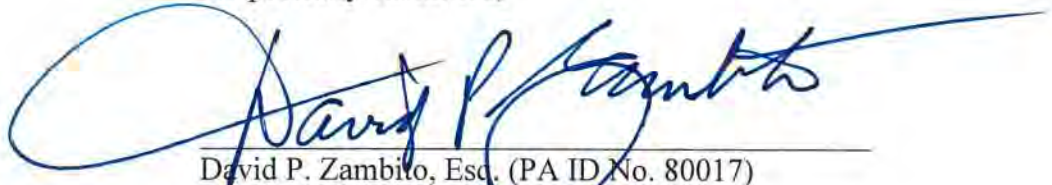
### **III. CONCLUSION**

Through cooperative efforts and the open exchange of information, the Joint Petitioners have arrived at a settlement that resolves all issues in the proceeding in a fair and equitable manner. The Settlement is the result of detailed examination of the Transaction, formal and informal discovery responses, evidence that was entered into the record, briefs and reply briefs, and extensive settlement negotiations. It is also the result of long, hard bargaining by the Joint Petitioners. A fair and reasonable compromise has been achieved in this case, as is evidenced by

the fact that all active parties to the proceeding have agreed to the resolution of the issues. PAWC fully supports the Settlement and urges the ALJs and the Commission to approve it without modification.

WHEREFORE, Pennsylvania-American Water Company respectfully requests that the Honorable Deputy Chief Administrative Law Judge Mark A. Hoyer and the Honorable Administrative Law Judge Mary D. Long recommend approval of, and that the Commission approve, the Settlement, including all terms and conditions thereof, without modification, and enter an order consistent with the Settlement.

Respectfully submitted,



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Dated: September 20, 2017



**APPENDIX F. JOINT STATEMENT IN SUPPORT OF THE CITY OF  
MCKEESPORT AND THE MUNICIPAL AUTHORITY OF THE CITY OF  
MCKEESPORT**

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

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**Deputy Chief Administrative Law Judge  
Mark A. Hoyer  
and  
Administrative Law Judge Mary D. Long**

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Application of Pennsylvania-American Water :  
Company-Wastewater under Section 1329 of the :  
Pennsylvania Public Utility Code, 66 Pa. C.S. :  
§ 1329, for approval of the use for ratemaking :  
purposes of the lesser of the fair market value or the : Docket No. A-2017-2606103  
negotiated purchase price of The Municipal :  
Authority of the City of McKeesport's assets related :  
to its wastewater collection and treatment system :  
and other related transactions. :

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**JOINT STATEMENT OF  
THE MUNICIPAL AUTHORITY OF THE CITY OF MCKEESPORT  
AND THE CITY OF MCKEESPORT IN SUPPORT OF JOINT PETITION FOR  
APPROVAL OF SETTLEMENT OF ALL ISSUES**

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**I. INTRODUCTION**

The Municipal Authority of the City of McKeesport (“MACM”) and the City of McKeesport (the “City”) hereby file this Joint Statement in Support of the Joint Petition for Approval of Settlement of All Issues (“Settlement”) entered into by MACM, the City, Pennsylvania-American Water Company (“PAWC”), the Office of Consumer Advocate (“OCA”), and the Bureau of Investigation & Enforcement of the Pennsylvania Public Utility Commission (“I&E”) (hereinafter, collectively the “Joint Petitioners”) in the above-captioned

proceeding. MACM and the City respectfully request that the Honorable Deputy Chief Administrative Law Judge Mark A. Hoyer and the Honorable Administrative Law Judge Mary D. Long recommend approval of, and that the Pennsylvania Public Utility Commission (“Commission”) approve, the Settlement, including all terms and conditions thereof, without modification.

The Settlement, if approved, will resolve all of the issues raised in this proceeding. The Settlement is in the best interest of the City, MACM and its existing customers and is otherwise in the public interest. It should, accordingly, be approved.

Commission policy promotes settlements. *See* 52 Pa. Code § 5.231. Settlements lessen the time and expense that the parties must expend litigating a case and, at the same time, conserve precious administrative resources. The Commission has indicated that settlement results are often preferable to those achieved at the conclusion of a fully-litigated proceeding. *See* 52 Pa. Code § 69.401. In order to accept a settlement, the Commission must first determine that the proposed terms and conditions are in the public interest. *Pa. Pub. Util. Comm'n v. York Water Co.*, Docket No. R-00049165 (Order entered Oct. 4, 2004); *Pa. Pub. Util. Comm'n v. C.S. Water and Sewer Assocs.*, 74 Pa. P.U.C. 767 (1991).

As an initial matter, the fact that the Settlement is supported by all active parties in this acquisition proceeding is, in and of itself, strong evidence that the Settlement is reasonable and in the public interest -- particularly given the diverse interests of the Joint Petitioners and the active role that they have taken in this proceeding. Moreover, the Settlement was achieved only after the Joint Petitioners (i) timely filed direct, rebuttal and surrebuttal testimony, (ii) actively participated in an evidentiary hearing, and (iii) filed Main Briefs and Reply Briefs. In addition,

the Joint Petitioners participated in numerous settlement discussions and formal negotiations, which ultimately led to the Settlement.

The duly-appointed Board of the Authority and the democratically-elected officials of the City believe that the sale of the Authority's wastewater system is in the best interest of the residents of the McKeesport area. They therefore agreed to the sale to Pennsylvania-American pursuant to a heavily negotiated APA and agree to and support the Settlement. These are assets owned by the public, and the City and the Authority are compelled to promote the best interests of their constituents. The officials of the City and the Authority believe the Settlement is in the public interest.

Finally, it should be noted that the Joint Petitioners, and their counsel and experts, have considerable experience in acquisition proceedings. Their knowledge, experience, and ability to evaluate the strengths and weaknesses of their litigation positions provided a strong base upon which to build a consensus on the settled issues.

The Settlement reflects a carefully balanced compromise of the interests of the Joint Petitioners. For these reasons and the reasons set forth below, the Settlement is in the public interest and should be approved without modification.

## **II. THE SETTLEMENT IS IN THE PUBLIC INTEREST**

The Joint Petitioners have agreed to a settlement of all issues in the above-captioned proceeding. Subject to certain terms and conditions, the Settlement requests approval of: (a) the transfer, by sale, of substantially all of the assets, properties and rights of MACM related to its wastewater collection and treatment system (the "System") to PAWC; (b) PAWC's right to begin to offer, render, furnish and supply wastewater service in the areas served by MACM in the City, the City of Duquesne, Port Vue Borough, the Borough of Dravosburg, and a portion of

West Mifflin Borough, Allegheny County, Pennsylvania and to three bulk service interconnection points located in Liberty Borough, White Oak Borough, and North Versailles Borough, Allegheny County, Pennsylvania; (c) PAWC's filing of a tariff supplement, consistent with the *pro forma* tariff supplement attached to the Settlement as Appendix A, to be issued and effective on the date of closing of the sale of MACM's assets, properties, and rights to PAWC (the "Transaction"); (d) the issuance of Certificates of Filings for the agreements enumerated in the Settlement between PAWC and municipal corporations as required under Section 507 of the Pennsylvania Public Utility Code ("Code"), 66 Pa. C.S. § 507; (e) PAWC's right to use \$158,000,000 for ratemaking rate base purposes for the acquired assets; and, (f) issuance of any other approval or certificate appropriate, customary, or necessary under the Code to carry out the Transaction in a lawful manner.

An applicant for a certificate of public convenience must demonstrate that the transaction 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*, 449 Pa. 136, 151, 295 A.2d 825, 828 (1972). The applicant must demonstrate that it is technically, financially, and legally fit to own and operate the acquired public utility assets. *Seaboard Tank Lines v. Pa. Pub. Util. Comm'n*, 502 A.2d 762, 764 (Pa. Cmwlth. 1985); *Warminster Township Mun. Auth. v. Pa. Pub. Util. Comm'n*, 138 A.2d. 240, 243 (Pa. Super. 1958). The fitness of a currently certificated public utility is presumed. *See e.g., South Hills Movers, Inc. v. Pa. Pub. Util. Comm'n*, 601 A.2d 1308, 1310 (Pa. Cmwlth. 1992). PAWC's Application utilized the process set forth in Section 1329 of the Public Utility Code, 66 Pa. C.S. § 1329, to determine the fair market value of the MACM system assets and the ratemaking rate base of those assets. PAWC St. No. 1 p. 4.

As demonstrated by the evidence stipulated by the Joint Petitioners into the record, PAWC ownership and operation of the System, consistent with the terms and conditions of the Settlement, will affirmatively promote the service, accommodation, convenience, or safety of the public in a substantial way. PAWC is technically, financially, and legally fit and the Transaction will produce affirmative public benefits of a substantial nature.

**A. PAWC is Technically, Financially, and Legally Fit**

PAWC, a subsidiary of American Water Works Company, Inc. (“American Water”), is the largest regulated public utility corporation in Pennsylvania. PAWC St. No. 1 p. 13. As of December 31, 2016, PAWC furnished wastewater services to 54,691 customers in Pennsylvania and water services to 654,770 customers. PAWC St. No. 2 pp. 6-7. PAWC currently owns and operates 16 wastewater treatment plants. PAWC St. No. 2 p. 4; PAWC St. No. 3 p. 27. PAWC owns and operates water and wastewater facilities near McKeesport in Southwestern Pennsylvania. In fact, the System is located adjacent to PAWC’s MonValley/Elizabeth and Pittsburgh operations, and PAWC provides water service to MACM’s Dravosburg Borough customers. PAWC St. No. 2 p. 7.

As a certificated public utility, PAWC enjoys a rebuttable presumption that it possesses the requisite fitness.<sup>1</sup> *South Hills Movers, Inc., supra*. In this proceeding, no party has challenged PAWC’s fitness. Nevertheless, PAWC introduced extensive evidence demonstrating its technical, financial, and legal fitness.

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<sup>1</sup> Similarly, PAWC enjoys a presumption of a continuing public need for service because public utility service is already being provided in the service territory. *Re Glenn Yeager et al.*, 49 Pa. P.U.C. 138 (1975). No party has contested the need for service in the McKeesport area.

With respect to technical fitness, PAWC must demonstrate that it has sufficient staff, facilities and operating skills to provide the proposed service. *Re Perry Hassman*, 55 Pa. PUC 661 (1982); *Merz White Ways Tours v. Pa. Pub. Util. Comm'n*, 201 A.2d 446 (Pa. Super. 1964). PAWC is the Commonwealth's largest water and wastewater provider. It furnishes service to more than 400 communities in 36 counties, serving a combined population in excess of 2,300,000. PAWC St. No. 1 pp. 13-14. PAWC employs approximately 1,000 professionals with expertise in all areas of water and wastewater utility operations. PAWC St. No. 1 p. 14. In addition, as a subsidiary of American Water, PAWC has available to it the resources of American Water Works Service Company, Inc. ("Service Company"), which provides access to highly-trained professionals with expertise in specialized areas. When operational issues arise at facilities owned by PAWC, the company mobilizes engineering talent from its central engineering team, drawing on resources from the Service Company team, to identify problems, recommend options, and develop action plans. PAWC St. No. 2 p. 5.

Significantly, in the context of the System, which has infrastructure problems in areas including, but not limited to, the Port Vue, Dravosburg and Duquesne portions of the system, PAWC St. No. 3 p. 12-14, PAWC has an ongoing program of capital investment focused on systematically replacing and adding new pipes and infrastructure. PAWC St. No. 3 p. 18. PAWC has funded more than \$1 billion in infrastructure investment in the past five years. PAWC St. No. 3-R p. 7.

PAWC maintains cyber security, physical security, business continuity and emergency plans. PAWC St. No. 2 p. 16. It participates in the Pennsylvania One Call system. PAWC St. No. 2 p. 18. It also has strong relationships with Commission Emergency Response Staff, the

Pennsylvania Emergency Management Agency, and local first responders. PAWC St. No. 2 p. 17.

With respect to legal fitness, PAWC must demonstrate that it obeys the Code and the Commission's regulations. *Re Perry Hassman, supra*. PAWC is a Commission-regulated public utility with a good compliance history. PAWC St. No. 1 p. 17. PAWC has a record of environmental compliance, a commitment to invest in necessary capital improvements and resources, and the experienced managerial and operating personnel necessary to provide safe and reliable sewer service to the residents of the McKeesport area. PAWC St. No. 1 pp. 14, 15.

With respect to financial fitness, PAWC must demonstrate that it has sufficient financial resources to provide the proposed service. *Re Perry Hassman, supra*. PAWC had total assets of approximately \$4.35 billion as of December 31, 2016. It had a net income of approximately \$153 million for the 12 months ending December 31, 2016. PAWC St. No. 1 p. 18. In addition to positive operating cash flows, PAWC has a \$400 million line of credit, long term debt financing, and equity investments. PAWC St. No. 5 p. 4.

For the foregoing reasons, there is substantial record evidence to support the Settlement and approval of the Transaction. It is clear that PAWC is technically, financially, and legally fit to own and operate the System in the public interest.

## **B. The Transaction Will Produce Substantial Public Benefits**

The Transaction will produce affirmative public benefits of a substantial nature. These benefits include, but are not limited to: further regionalization of wastewater operations in Pennsylvania; greater access to technical resources for operation of the System; greater access to



capital for necessary investments to the System; improved customer service for System customers; and, certain measures aimed at helping MACM customers who are facing economic hardship and maintaining the existing local MACM workforce and operational expertise.

As previously noted, PAWC is the largest investor-owned public utility in Pennsylvania. It provides water and wastewater service to the public in a service territory encompassing more than 400 communities in 36 counties. It serves a combined population of over 2,300,000. PAWC St. No. 1 p. 13-14. As of December 31, 2016, PAWC furnished wastewater services to 54,691 customers in Pennsylvania and water services to 654,770 customers. PAWC St. No. 1 p. 15.

As also noted previously, PAWC has adjacent and non-redundant operations. PAWC owns and operates water and wastewater facilities near McKeesport in the Pittsburgh Area and Southwestern Pennsylvania. PAWC St. No. 2 p. 6-7. The System is located adjacent to PAWC's MonValley/Elizabeth and Pittsburgh operations. PAWC provides water service to MACM's Dravosburg Borough customers. PAWC St. No. 2 p. 7.

The Transaction would add 22,000 direct or indirect customers to PAWC's existing wastewater customer base of 54,691. PAWC St. No. 1-R p. 13 and PAWC St. No. 2 p. 6-7. The Transaction fosters the Commission goal of regionalizing wastewater systems to provide greater environmental and economic benefits to customers. PAWC St. No. 1 p. 16. Approval of the Transaction would enable PAWC to continue to regionalize its operations. Regionalization permits PAWC to pursue economies of scale and spread costs over a larger customer base for the benefit of all of its ratepayers.

The Transaction is vitally important to the City. Mayor Cherepko of the City, indicates that the proceeds of the Transaction are crucial to the financial stability of the City. Tr. 72. The Transaction would positively impact the City's short-term and long-term financial health, improve MACM's operations and customer service, and provide additional revenue to the City in the form of sale proceeds and tax revenue. PAWC St. No. 6 p. 8. Mayor Cherepko indicated that if the Commission would disapprove the Transaction, the City's already difficult financial situation will get worse. Tr. 81. In contrast, PAWC has a better credit rating than MACM and has access to equity markets that are unavailable to MACM. PAWC St. No. 3-R p. 7-8

Under PAWC ownership, MACM customers will benefit from PAWC's additional bill payment options, extended customer service and call center hours, enhanced customer information and education programs, and access to customer assistance programs. PAWC St. No. 1 p. 16. These benefits are possible because of PAWC's larger customer base, expertise, and financial capabilities.

The employees at MACM will be protected. PAWC has committed to offer employment to eligible MACM employees following closing. PAWC St. No. 1 p. 13; PAWC St. No. 2 p. 15. In addition, pursuant to Paragraph 23. of the Settlement, within the first 90 days of PAWC's ownership of the System, PAWC shall include a bill insert to MACM customers regarding its low income programs or alternatively shall include such information in a welcome letter to MACM customers. The bill insert or welcome letter shall include, at a minimum, a description of the available low income programs, the eligibility requirements for participation in the programs, and PAWC's contact information. PAWC also agrees to ongoing, targeted outreach to its McKeesport-area customers regarding its low income program.

For the foregoing reasons, there is substantial record evidence to support the Settlement and approval of the Transaction. It is clear that the Transaction will produce a public benefit of a substantial nature.

### **C. Ratemaking Rate Base**

PAWC's Application sought to utilize the process set forth in Section 1329 of the Public Utility Code, 66 Pa. C.S. § 1329, to determine the fair market value of the MACM system assets and the ratemaking rate base of those assets. PAWC St. No. 1 p. 4. As required by Section 1329, the parties to the APA engaged an engineer (KLH Engineers) to conduct an assessment of the tangible assets of the System. PAWC St. No. 7 pp. 13, 16. Application, Attachment A-5. PAWC selected Associated Utility Services, Inc. ("AUS") to perform an appraisal of the MACM system. PAWC St. No. 1 p. 7. AUS was approved by the Commission for placement on the Commission's Utility Valuation Expert ("UVE") Registry. PAWC St. No. 7 p. 7. MACM selected Herbert, Rowland & Grubic, Inc. ("HRG") as its utility valuation expert, to perform an appraisal of the MACM system. MACM St. No. 1 p. 2. HRG was approved by the Commission for placement on the Commission's Utility UVE Registry. MACM St. No. 1 p. 2. As required by Section 1329, the Application included the appraisals of PAWC's UVE and MACM's UVE. The Settlement provides that PAWC shall be permitted to use \$158 million for ratemaking rate base purposes for the acquired assets. Using \$158 million for ratemaking rate base purposes is within a reasonable range of the fair market value as determined pursuant to Section 1329. In addition, permitting that negotiated amount to be utilized in the Settlement allows the Transaction to close in a timely manner without the threat of a protracted and costly appeal process and is therefore in the public interest because public benefits can be achieved sooner.

**D. The Settlement Promotes a Gradual Phase In of Rates**

Rates for PAWC's existing customers will not increase in the short term due to the Transaction. PAWC St. No. 4 p. 8-9. The MACM System has not been included in PAWC's current base rate proceeding. PAWC St. No. 1-R p 6.

The Settlement also provides that PAWC will propose gradual rate increases for System customers (while acknowledging that the Commission has ultimate authority to set rates). As explained in Paragraphs 20. and 22. of the Settlement, PAWC has committed to propose to increase rates for System customers in a gradual manner over the course of PAWC's next one to two base rate cases in order to bring such rates in line with PAWC's system average rates (Rate Zone 1) over that time period. These Settlement provisions are consistent with the Commission's policies of rate gradualism and single tariff pricing.

**E. The Settlement Preserves the Rights of Parties in Future Rate Proceedings**

The Settlement makes clear that approval of the Transaction would not infringe upon the rights of OCA, I&E, and other interested parties to participate in, and advocate their positions in, future PAWC rate proceedings. *See, e.g.*, Settlement, 16 ("Except as explicitly stated herein, nothing contained in the Settlement, or in the Commission's approval of the Application, shall preclude any Joint Petitioner from asserting any position or raising any issue in a future PAWC base rate proceeding.").

**F. Distribution System Improvement Charge**

Pursuant to 66 Pa. C.S. § 1329, PAWC seeks permission to collect a distribution system improvement charge ("DSIC"). PAWC St. No. 1 p. 4. The use of DSIC encourages accelerated

infrastructure repair and replacement. This accelerated infrastructure repair and replacement is in the public interest because it will provide a mechanism for more quickly addressing the environmental and infrastructure issues confronting the System and the communities it serves. In order to ensure appropriate oversight for PAWC investments, as a part of the Settlement, PAWC's filing of an amended wastewater long term infrastructure improvement plan, which will require PAWC to specify its plans before and DSIC may be implemented in the McKeesport area.

#### **G. Certificates of Filing Should be Issued for Municipal Agreements**

As part of the Settlement, the Joint Petitioners have agreed that that Commission should issue Certificates of Filing under Section 507 of the Code, 66 Pa. C.S. § 507, for certain agreements between PAWC and municipal corporations. Such agreements are enumerated in the Settlement and include the Asset Purchase Agreement for the Transaction, as amended by the First Amendment to the Asset Purchase Agreement, Dated as of May 15, 2017, along with related City of McKeesport General Obligation Note, Series of 2016, No. R-1, related Intercept Agreement, Dated November 30, 2016, and related Second Deposit Agreement, which is yet to be executed, and as further amended by the amendment specified in Paragraph 14 of the Settlement. The agreements, or forms of the agreements, have been provided to the Commission and the parties in conjunction with this proceeding. They are reasonable and necessary for the continued operation of the System, and, therefore, Certificates of Filing should be issued.

### **III. CONCLUSION**

Through cooperative efforts focused on finding common ground, the Joint Petitioners have arrived at a settlement that resolves all issues in the proceeding in a fair and equitable manner. The Settlement is the result of detailed examination of the Transaction, thorough

discovery and briefing and extensive settlement negotiations. A fair and reasonable compromise has been achieved in this case, as is evident by the fact that all active parties to this proceeding have agreed to the resolution of the issues. MACM and the City fully support this Settlement and respectfully request that the Honorable Deputy Chief Administrative Law Judge Mark A. Hoyer and the Honorable Administrative Law Judge Mary D. Long recommend approval of, and the Commission approve, the Settlement in its entirety, without modification.

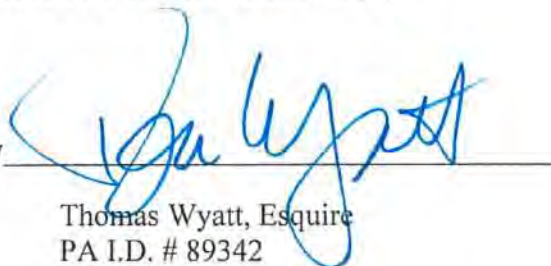
WHEREFORE, MACM and the City respectfully request that the Honorable Deputy Chief Administrative Law Judge Mark A. Hoyer and the Honorable Administrative Law Judge Mary D. Long recommend approval of, and that the Commission approve, the Settlement, including all terms and conditions thereof, and that the Commission enter an order consistent with the Settlement.

Respectfully submitted,

**THE MUNICIPAL AUTHORITY OF THE CITY OF  
MCKEESPORT**

**THE CITY OF MCKEESPORT**

By



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Dated: September 20, 2017

**APPENDIX G. STATEMENT IN SUPPORT OF THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION'S  
BUREAU OF INVESTIGATION AND ENFORCEMENT**



**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

In re: Application and related filings of	:	
Pennsylvania-American Water Company	:	
under Sections 507, 1102(a), and 1329 of	:	
the Pennsylvania Public Utility Code, 66 Pa.	:	
C.S. §§ 507, 1102(a), 1329, for approval of	:	Docket No. A-2017-2606103
its acquisition of wastewater system assets	:	
of The Municipal Authority of the City of	:	
McKeesport, related wastewater service	:	
rights, fair market valuation ratemaking	:	
treatment, deferral of the post-acquisition	:	
improvement costs, and certain contracts	:	
with municipal corporations	:	

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**BUREAU OF INVESTIGATION AND ENFORCEMENT  
STATEMENT IN SUPPORT OF  
JOINT PETITION FOR APPROVAL  
OF SETTLEMENT**

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**TO DEPUTY CHIEF ADMINISTRATIVE LAW JUDGE MARK A. HOYER AND  
ADMINISTRATIVE LAW JUDGE MARY D. LONG:**

The Bureau of Investigation and Enforcement (“I&E”) of the Pennsylvania Public Utility Commission (“Commission”), by and through its Prosecutors Gina L. Miller and Erika L. McLain, hereby respectfully submits that the terms and conditions of the foregoing Joint Petition for Approval of Settlement (“Joint Petition” or “Settlement”) are in the public interest and represent a fair and just balance of the interests of Pennsylvania-American Water Company (“PAWC”), the Office of Consumer Advocate (“OCA”), the Bureau of Investigation & Enforcement of the Pennsylvania Public Utility Commission (“I&E”), the City of McKeesport (“City”) and the Municipal Authority of

the City of McKeesport (“MACM”), parties to the above-captioned proceeding (collectively, the “Joint Petitioners”).

## **I. BACKGROUND**

1. On May 24, 2017, PAWC filed its Application, inter alia, requesting approval to (a) acquire substantially all of the MACM assets, properties and rights related to MACM's wastewater collection and treatment system assets pursuant to 66 Pa. C.S. § 1102 (“Section 1102”); (b) obtain the Certificates of Public Convenience necessary for it to begin to offer, render, furnish and supply offer, wastewater service to the public in the areas served by MACM in the City, the City of Duquesne, Port Vue Borough, the Borough of Dravosburg, a portion of West Mifflin Borough, Allegheny County, Pennsylvania and to three bulk service interconnection points located in Liberty Borough, White Oak Borough, and North Versailles Borough, Allegheny County, Pennsylvania (“Service Area”); and (c) to use, for ratemaking purposes, the lesser of the fair market value or the negotiated purchase price of MACM’s assets to establish MACM’s ratemaking rate base in this proceeding pursuant to 66 Pa. C.S. § 1329 (“Section 1329”).

2. By Secretarial Letter dated June 14, 2017, the Pennsylvania Public Utility Commission (“Commission”) acknowledged receipt of PAWC’s Application.

3. On June 21, 2017, I&E filed a Notice of Appearance in this proceeding. I&E serves as the Commission’s prosecutory bureau for the purposes of representing the public interest in ratemaking and service matters, and enforcing compliance with the

Pennsylvania Public Utility Code (“Code”).<sup>1</sup> I&E’s participation in this proceeding is warranted because its outcome will produce a direct and immediate ratemaking determination and because key components of the Code support an investigation into matters of property valuation, which are at issue in this case.

4. On the same date that I&E entered its appearance, the Office of Consumer Advocate (“OCA”) filed a Protest in this proceeding. On June 28, 2017, counsel for MACM and the City filed a Petition to Intervene in the instant proceeding.

5. A Prehearing Conference was held on July 13, 2017, with Deputy Chief Administrative Law Judge Mark A. Hoyer (“ALJ Hoyer”) and Administrative Law Judge Mary D. Long (“ALJ Long”) presiding. A litigation schedule was developed that provided for the filing of testimony, hearings and briefs as follows:

Other Parties’ Direct Testimony	July 17, 2017
Rebuttal Testimony	July 26, 2017 by 2:00 p.m.
Surrebuttal	August 2, 2017 by noon
Evidentiary Hearing	August 3-4, 2017
Main Briefs	August 22, 2017
Reply Briefs	September 1, 2017

6. Pursuant to the litigation schedule, ALJ Hoyer and ALJ Long conducted an evidentiary hearing on August 3, 2017. At the hearing, testimony and exhibits were entered into the record and cross examination was conducted. I&E entered the following statements and exhibits into the evidentiary record: I&E Statement No. 1, I&E Exhibit

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<sup>1</sup> 66 Pa. C.S. §§ 101 *et seq.*, and Commission regulations, 52 Pa. Code §§ 1.1 *et seq.* See *Implementation of Act 129 of 2008; Organization of Bureaus and Offices*, Docket No. M-2008-2071852 (Order entered August 11, 2011).

No. 1, I&E Statement No. 1-SR, I&E Statement 2, I&E Exhibit No. 2, and I&E Statement 2-SR.

7. Pursuant to the litigation schedule, on August 22, 2017 and on September 5 2017,<sup>2</sup> the Joint Petitioners filed Main Briefs and Reply Briefs, respectively.

8. The Joint Petitioners engaged in extensive settlement discussions during the entire course of this proceeding. These discussions continued beyond the evidentiary hearings, and they extended into the briefing stages of this case.

9. On September 5, 2017, the Joint Petitioners reached a unanimous settlement-in-principle of all issues, and they informed the ALJs of the settlement.

## **II. LEGAL STANDARDS**

### **a. Section 1102 Approval**

10. The Pennsylvania Public Utility Code (“Code”) requires that the Commission issue a Certificate of Public Convenience as a prerequisite to offering service, abandoning service and certain property transfers by public utilities or their affiliated interests.<sup>3</sup> The standards for the issuance of a Certificate of Public Convenience are set forth in Sections 1102 and 1103<sup>4</sup> of the Code. A Certificate of Public Convenience shall be granted “only if the commission shall find or determine that the granting of such certificate is necessary or proper for the service, accommodation, convenience or safety of the public.”<sup>5</sup> These provisions have been interpreted by the Pennsylvania Supreme

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<sup>2</sup> Although the litigation schedule contemplated a Reply Brief deadline of September 1, the ALJs extended this deadline until noon on September 5, 2017.

<sup>3</sup> 66 Pa. C.S. § 1102(a).

<sup>4</sup> 66 Pa. C.S. § 1103.

<sup>5</sup> 66 Pa. C.S. § 1103(a).

Court in the *City of York v. Pennsylvania Public Utility Commission* for the proposition that to establish that a proposed transaction benefits the public, it must be shown to affirmatively promote the service, accommodation, convenience or safety of the public in some substantial way.<sup>6</sup> Additionally, pursuant to Section 1103, PAWC must show that it is technically, legally, and financially fit to own and operate the assets it will acquire from MACM.<sup>7</sup> In addition to assessing fitness, the Commission should consider the benefits and detriments of the transaction “with respect to the impact on all affected parties”<sup>8</sup> including existing customers. To ensure that a transaction is in the public interest, the Commission may impose conditions on granting a certificate of public convenience as it may deem to be just and reasonable.<sup>9</sup>

#### **b. Legal Standard for Section 1329 Approval**

11. Section 1329 of the Public Utility Code is a newly enacted statute which prescribes the process used to determine the fair market value of a municipal utility that is the subject of an acquisition. Section 1329 provides a framework for valuing, for ratemaking purposes, water and wastewater systems that are owned by a municipal corporation or authority that are to be acquired by an investor-owned water or wastewater utility under the Commission’s jurisdiction. It allows the rate base of the municipal system being purchased to be incorporated into the rate base of the purchasing investor-

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<sup>6</sup> *City of York v. Pa. PUC*, 449 Pa. 136, 295 A.2d 825, 828 (1972).

<sup>7</sup> *Seaboard Tank Lines v. Pa. PUC*, 502 A. 2d 762, 764 (Pa. Cmmw. 1985); *Warminster Twp. Mun. Auth. v. Pa. PUC*, 138 A.2d 240, 243 (Pa. Super. 1958).

<sup>8</sup> *Middletown Twp. v. Pa. P.U.C.*, 482 A.2d 674, 682 (Pa. Commw. 1984).

<sup>9</sup> 66 Pa. C.S. § 1103(a).

owned utility at the lesser of either the purchase price or the fair market value as established by the two independent appraisals conducted by two utility valuation experts. Notably, a Commission Order approving a transaction under Section 1329 is permitted to include “[a]dditional conditions of approval.”<sup>10</sup>

**c. Legal Standard for Section 507 Approval**

12. PAWC’s request to assume enumerated municipal contracts currently held by MACM is subject to review under Section 507 of the Code. Under Section 507, other than contracts to furnish service at tariffed rates, any contract between a public utility and a municipal corporation must be filed with the Commission at least 30 days prior to its effective date to be valid. Upon receipt of the filing, and prior to the effective date of the contracts, the Commission may institute proceedings to determine whether there are any issues with the reasonableness, legality, or any other matter affecting the validity of the contract. If this Commission decides to institute such proceedings, the contracts at issue will not become effective until the Commission grants its approval.

**III. TERMS AND CONDITIONS OF SETTLEMENT**

13. It is the policy of the Commission to encourage settlements.<sup>11</sup>

14. For the reasons discussed herein, I&E maintains that the Settlement meets all the standards necessary to warrant the requisite approvals under Sections 507, 1102, 1103, and 1329 of the Code. Commission approval of the Settlement will provide substantial public

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<sup>10</sup> 66 Pa. C.S. § 1329 (d)(3)(ii); Aqua/New Garden Section 1329 Case, Docket No. A-2016-2580061, p. 69 (Order entered June 29, 2017).

<sup>11</sup> 52 Pa. Code § 5.231.

benefits for PAWC, MACM, their respective customers, and the regulated community as a whole.

15. As evidenced by the fully developed record in this proceeding and the late timing of this Settlement, the signatories to the Joint Petition actively participated in and vigorously represented their respective positions during the settlement process. As such, the issues raised by the Joint Applicants have been satisfactorily resolved through discovery and discussions with the parties and are incorporated in the Joint Petition. I&E represents that the Settlement satisfies all applicable legal standards and results in terms that are preferable to those that may have been achieved at the end of a fully litigated proceeding. Accordingly, for the reasons articulated below, I&E maintains that the proposed Settlement is in the public interest and requests that the following terms be approved by the ALJs and the Commission without modification:

**A. APPROVAL OF THE APPLICATION UNDER SECTION 1102**  
(Joint Petition ¶12)

Subject to all of terms of the Settlement, I&E opines that the Application should be approved and recommends that the Commission should issue PAWC a Certificate of Public Convenience pursuant to 66 Pa. C.S. §1102(a). PAWC's Application requests permission for it to acquire substantially all MACM's assets, properties and rights related to MACM's wastewater collection and treatment system and to obtain the Certificates of Public Convenience necessary for it to begin to offer wastewater service to the public in the Service Area. The MACM assets consist of, inter alia, a combined wastewater collection system and three wastewater treatment plants which collect and treat

wastewater from the City, the City of Duquesne, the Borough of Dravosburg, and the Borough of Port Vue.<sup>12</sup> MACM's system also provides wastewater service through bulk service connections to White Oak Borough, Liberty Borough, East McKeesport Borough, Glassport Borough, Versailles Borough, Elizabeth Township, which PAWC seeks to continue.<sup>13</sup> In total, through this acquisition, PAWC is seeking to provide service to MACM's approximately 22,000 wastewater customers.<sup>14</sup> As I&E will explain below, the record supports the findings that PAWC is technically, legally, and financially fit to acquire MACM.

Additionally, pursuant to the terms of this Settlement, PAWC's Application will provide affirmative public benefits of a substantial nature. As PAWC has correctly noted, "[a]n acquisition provides an affirmative benefit if the benefits of the transaction outweigh the adverse impacts of the transaction."<sup>15</sup> At the outset of this case, I&E's position was that PAWC's Application should be rejected because of the potentially adverse and unquantified rate impact of this transaction upon PAWC's existing customers. With this in mind, I&E recommended that PAWC's Application be approved only upon the condition that it be required to undertake a cost of service study that (1) separates capital expenses and operating costs for MACM's sanitary and storm water functions and (2) separately identifies the plant in service costs at the time that the Port Vue system was purchased, the cost of any Port-Vue plant retirements, and the cost of

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<sup>12</sup> PAWC Application, Appendix A-14, St. No. 3, p. 3.

<sup>13</sup> PAWC Application, Appendix A-14, St. No. 2, p. 7; PAWC Application, pp. 2-5.

<sup>14</sup> PAWC Application, Appendix A-14, St. No. 2, p. 7.

<sup>15</sup> PAWC Main Brief, p. 16, quoting *Application of CMV Sewage Co., Inc.*, 2008 Pa. PUC LEXIS 950 ("CMV Sewage").



any Port Vue plant investment. The need for the recommended cost of service study to protect the public interest is discussed in the “Rates” section below; however, pursuant to the Settlement, PAWC has adopted I&E’s recommendation. Accordingly, I&E’s concerns have been addressed and I&E opines that PAWC’s Application, as modified by the Joint Petition, meets the requisite standards for approval.

### 1. Legal, Technical, and Financial Fitness

As previously mentioned, as a condition of obtaining its requested Certificates of Public Convenience, under Section 1103, PAWC must show that it is technically, legally, and financially fit to own and operate the assets it will acquire from MACM.<sup>16</sup> Because PAWC is a certificated public utility, there is a rebuttable presumption that it possesses the requisite fitness.<sup>17</sup> In this case, neither I&E, nor any party to this proceeding, has presented evidence to challenge PAWC’s fitness on these bases. On the contrary, the record has established that PAWC possesses the requisite fitness.

First, the record supports a finding that PAWC is technically fit to operate the MACM assets. PAWC is the largest water and wastewater provider in Pennsylvania.<sup>18</sup> Additionally, PAWC employs approximately 1,000 professionals with expertise in all areas of water and wastewater utility operations.<sup>19</sup> Importantly, PAWC has experience working through transitions, and has already implemented a plan to integrate MACM

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<sup>16</sup> *Seaboard Tank Lines v. Pa. PUC*, 502 A.2d 762, 764 (Pa. Cmwlth. 1985); *Warminster Twp. Mun. Auth. v. Pa. PUC*, 138 A.2d 240, 243 (Pa. Super. 1958).

<sup>17</sup> *South Hills Movers, Inc. v. Pa. PUC*, 601 A.2d 1308, 1310 (Pa. Cmwlth. 1992).

<sup>18</sup> PAWC St. No. 1 p. 17.

<sup>19</sup> PAWC St. No. 1 p. 14.

employees, customers, and the MACM system into its operations.<sup>20</sup> Moreover, as MACM is a combined sewer overflow (“CSO”) system, PAWC already has experience in operating a CSO system, so it is familiar with the unique characteristics and requirements of a CSO system.<sup>21</sup> Finally, as a subsidiary of American Water, PAWC has access to the resources of American Water Works Service Company, Inc., which provides access to highly-trained professionals with expertise in specialized areas. Accordingly, PAWC can mobilize engineering talent from its central engineering team, drawing on resources from the Service Company, to identify potential problems, recommend options, and develop action plans for MACM system.<sup>22</sup>

Additionally, the record supports a finding that PAWC is legally fit to own and operate MACM’s assets, as PAWC is a certificated public utility and there are no pending legal proceedings challenging its ability to provide service to customers of the System.<sup>23</sup> Finally, PAWC’s financial fitness to own and operate the MACM assets is borne out in the record. More specifically, PAWC had total assets of approximately \$4.35 billion as of December 31, 2016 and it had net income of approximately \$153 million for the 12 months ending December 31, 2016.<sup>24</sup> Aside from its assets and income, PAWC also has access to financing from a line of credit, long term debt financing, and equity investments.<sup>25</sup> Finally, PAWC’s financial fitness is supported by

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<sup>20</sup> PAWC St. No. 2 p. 10.

<sup>21</sup> PAWC St. No. 2 pp. 11, 26.

<sup>22</sup> PAWC St. No. 2 p. 5.

<sup>23</sup> PAWC St. No. 1 p. 17.

<sup>24</sup> PAWC St. No. 1 p. 18.

<sup>25</sup> PAWC St. No. 5 p. 4.

the fact that it enjoys a corporate credit rating of “A3” from Moody’s Investors Services and an “A” rating from Standard and Poor’s Rating Services.<sup>26</sup> Accordingly, I&E concedes that PAWC has established that it possesses the requisite fitness to acquire and operate the MACM assets.

## 2. Affirmative Public Benefits of a Substantial Nature

### a. Benefits to the City and MACM Customers

The record in this case cites numerous benefits that the MACM service area and its customers would enjoy as a result of the acquisition. More specifically, PAWC witness Cherepko, the Mayor of the City, indicates that the proceeds of the transaction are crucial to the financial stability of the MACM service area.<sup>27</sup> Mayor Cherepko also indicated that the acquisition would positively impact the City’s short-term and long-term financial health, improve MACM’s operations and customer service, grant MACM access to better and more varied sources of capital, and provide additional revenue to the City in the form of sale proceeds and tax revenue.<sup>28</sup> PAWC witness Grundusky indicates that under the acquisition, MACM customers will benefit from PAWC’s additional bill payment options, extended customer service and call center hours, enhanced customer information and education programs, and access to customer assistance program.<sup>29</sup> Accordingly, it is clear that the City and existing MACM customers will substantially benefit from this acquisition.

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<sup>26</sup> PAWC St. No. 5, p. 4.

<sup>27</sup> Tr. at 72.

<sup>28</sup> PAWC Application, Appendix A-14, St. No. 6, p. 8.

<sup>29</sup> PAWC Application, Appendix A-14, St. No. 1, p. 16.

b. Benefits to the General Public

In I&E's view, the most important benefit is PAWC's commitment to address the MACM system's environmental compliance issues, which is a benefit that extends beyond the MACM service area. I&E agrees with PAWC and MACM that PAWC's plan to bring the MACM system into environmental compliance operates not just as a benefit to MACM, but also to the general public.<sup>30</sup> This benefits the public because environmental contamination and pollution caused by the MACM is not confined to the strict boundaries of the service area.<sup>31</sup> As recognized in Pennsylvania's Constitution, environmental protection measures benefit to all Pennsylvanians, and that Pennsylvanians should have access to pure water.<sup>32</sup>

The record in this case demonstrates that MACM's system had the following compliance issues pending with the Pennsylvania Department of Environmental Protection ("Pa. DEP") and/or the Allegheny County Health Department: (1) McKeesport Construction-Related Dry-Weather Overflows; (2) Duquesne Long Term control Plan ("LTCP"); (3) Dravosburg LTCP; (4) Dravosburg Mine Discharges; (5) Dravosburg Nine Minimum Controls Plan ("NMCP"); (6) Port Vue LTCP; (7) Port Vue Grade 4 and 5 Defects; and (8) Port Vue NMCP.<sup>33</sup> As an example of the reality of these compliance issues, 53 residential customers in the Dravosburg Borough portion of the MACM service area are not connected to MACM's system and sanitary-only flows from

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<sup>30</sup> PAWC Main Brief, p. 5; MACM Main Brief, pp. 13-14.

<sup>31</sup> Id.

<sup>32</sup> MACM Main Brief, pp. 13-14; Pa. Const. Art. 1, § 27.

<sup>33</sup> I&E Ex. No. 2, Sch. 2, p. 1 of 19.

these homes are currently discharged untreated into mine holes.<sup>34</sup> The record also indicates that PAWC has committed to undertaking numerous projects necessary to facilitate environmental compliance measures in the MACM system, and the estimated costs of those projects is \$37,066,723.<sup>35</sup> Accordingly, I&E agrees that PAWC's commitment to bring the MACM system into environmental compliance is an important public benefit which will extend to MACM customers, existing PAWC customers, and to the regulated community as a whole.<sup>36</sup>

c. Benefits for PAWC's Existing Customers

Despite the numerous MACM benefits, and the important public benefits that the acquisition may produce, the Commission still must consider the benefits of the transaction as they pertain to PAWC's existing customers. Ultimately, the transaction will further regionalization of wastewater systems to provide greater environmental and economic benefits to PAWC's customers.<sup>37</sup> Additionally, the acquisition will eventually mitigate of the level of net plant investment per customer by adding more customers to share future infrastructure investment costs.<sup>38</sup> PAWC also expects that the acquisition will eventually help PAWC maintain reasonable rates for all of its customers in the future because of the expansion of its customers base.<sup>39</sup> I&E notes that these benefits are substantially similar, if not more numerous, than the public benefits that the Commission

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<sup>34</sup> I&E Ex. No. 2, Sch. 2, p. 7 of 19.

<sup>35</sup> I&E St. No. 2, p. 12.

<sup>36</sup> MACM Main Brief, p. 5,8.

<sup>37</sup> PAWC Application, Appendix A-14, St. No. 1, p. 16.

<sup>38</sup> Id. at pp. 17-18.

<sup>39</sup> PAWC Application, Appendix A-14, PAWC St. No. 1, pp. 17-18; PAWC St. No. 4, pp. 8-9.

sanctioned in the first Section 1329 proceeding.<sup>40</sup> Combining these benefits with the benefit of PAWC commitment to environmental remediation, which will surely enure to existing ratepayers, and with PAWC's commitment to perform I&E's recommended cost of service study, I&E opines that a benefit to existing ratepayers will be realized.

**B. TARIFF (Joint Petition ¶ 13)**

Pursuant to the Settlement, the Joint Petitioners have agreed that the *pro forma* tariff supplement, which is attached to the Joint Petition as **Appendix A**, shall be permitted to become effective immediately upon closing of the transaction. The Joint Petitioners support the pro forma tariff supplement, under which MACM's current rates would be initially adopted. The pro forma tariff supplement reflects the fees associated with the industrial pretreatment plan that PAWC plans to implement for the MACM service area, including fees for permits, fees for industrial loadings, and fees imposed for non-compliance.<sup>41</sup> The pro forma tariff supplement also includes both quarterly and monthly rates for Port Vue-area customers to extend additional billing options to those customers, and reflects MACM's existing rates for acceptance of hauled sludge.<sup>42</sup> Finally, PAWC has indicated that it will also add a pro forma tariff provision stating that, if a municipality's wastewater volumes exceeds 350% of the aggregate quantity of water used by the municipality's water users during any billing period, the municipality must pay MACM's prevailing rates and charges for handling such excess in addition to the

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<sup>40</sup> Aqua/New Garden Section 1329 Case, pp. 66-67 (Order entered June 29, 2017).

<sup>41</sup> PAWC Application, Appendix A-14, St. No. 4, pp. 4-5.

<sup>42</sup> PAWC Application, Appendix A-14, St. No. 4, pp. 19-20.

typical sewage charges.<sup>43</sup> Accordingly, the *pro forma* tariff will accurately include all rates, rules, and regulations regarding the conditions of PAWC's wastewater service, and this full and accurate disclosure of rates is in the public interest.

**C. FAIR MARKET VALUE FOR RATEMAKING RATE BASE PURPOSES (Joint Petition ¶¶ 14-15)**

**1. Rate Base Value**

Pursuant to the Settlement, PAWC will be permitted to use \$158 million for ratemaking rate base purposes for the acquired assets. The \$158 million figure represents the lower of PAWC and MACM's negotiated purchase price, and the average of two fair market value appraisals completed by each of these parties' UVEs. Although I&E did not oppose PAWC's as-filed proposed ratemaking rate base of \$162 million, it was simply because fair market value here was predicated upon PAWC's purchase price for the MACM system and not upon the average of the UVEs' appraisals.

However, I&E was concerned that that MACM's fair market value appraisal performed by HRG was fundamentally flawed in several ways.<sup>44</sup> Despite the fact that PAWC's proposed ratemaking rate base of \$162 million was premised on a negotiated purchase price, I&E noted that those negotiations were premised upon incorrect information.<sup>45</sup> More specifically, as this proceeding developed, HRG witness Vicari acknowledged an error in the calculation of the service life of many of MACM's mains, resulting in an need to increase the service life from 50 to 85 years.<sup>46</sup> The impact of her

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<sup>43</sup> PAWC Exhibit RPN-1; PAWC. St. No. 4-R, p. 7.

<sup>44</sup> I&E Main Brief, pp. 32-40; I&E Reply Brief, pp. 22-28.

<sup>45</sup> I&E Main Brief, p. 35; MACM St. No. 1-SR, p. 2.

<sup>46</sup> MACM St. No. 1, pp. 7-8.

adjustment was substantial, as this correction led HRG to reduce its net depreciated original cost, which in turn lowered its appraised value of the MACM assets from \$207,010,000 to \$190,000,000.<sup>47</sup> This correction and corresponding reduction in fair market value was not known to PAWC, MACM, or the City when these parties negotiated a purchase price for the MACM assets.

Accordingly, it is impossible to know whether the discovery of the error in HRG's fair market valuation would have led to a material change in the parties' negotiations, and, ultimately, the impact upon PAWC's ratepayers if a lower purchase price had been negotiated. For this reason, I&E avers that the Settlement is in the public interest because the ratemaking rate base value has decreased from \$162 million to \$158 million, mitigating any potential impact that the error in HRG's fair market value may have had on the parties' negotiations. Attempting to mitigate the potential impact that any errors in the fair market valuation may have had upon the purchase price in this case is in the public interest because once established in this case, the ratemaking rate base determination will have real and measurable consequences for ratepayers.

## 2. Adjustments

While the Settlement provides that the Joint Petitioners reserve their right to present adjustments and oppose adjustments to appraisals in future cases, the Settlement also reflects the Joint Petitioners' recommendation that the Commission accept certain adjustments relative the appraisals in this proceeding. I&E supports these

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<sup>47</sup> MACM St. No. 1, pp. 6-7.



recommendations as they protect the public interest by ensuring that fair market value appraisal results are not artificially increased. Among these terms, and relevant to I&E's position in this case is the following term: the "Going Value" and "Provision for Erosion on Return" add-ons will not be adopted or included in the appraisals.<sup>48</sup>

In this case, HRG indicated that it added a "going value"<sup>49</sup> of \$17.3 million to the results of both its both cost and income approaches of fair market valuation.<sup>50</sup> I&E contested the going value adjustment because as MACM will be receiving purchase proceeds that are exponentially higher than the depreciated original cost of its assets, it is clear that MACM is being adequately compensated for its initial investment. Notably, HRG's appraiser, Ms. Vicari, conceded that she was not sure whether PAWC was already paying MACM for its going value as part of the purchase price of the transaction.<sup>51</sup>

Additionally, I&E rejected the notion that, outside of the four corners of the cost and income approaches,<sup>52</sup> MACM should receive separate and additional compensation for its customer base, employees, accounting and record keeping process and operating and management policies and procedures. Finally, the record in this case bears out the fact that Ms. Vicari has only broken out a separate quotient for going value in 3 out of the 5 or 6 Pennsylvania utility appraisals that she has performed in her professional career.<sup>53</sup> During the evidentiary hearing, Ms. Vicari reluctantly admitted that of the Pennsylvania

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<sup>48</sup> Joint Petition, ¶ 15(c).

<sup>49</sup> HRG uses the terms "going value" and "going concern" interchangeably.

<sup>50</sup> Tr. at 118, PAWC Application, Appendix A-5, HRG Appraisal, pp. 12-13; Schedule O.

<sup>51</sup> Tr. at 120.

<sup>52</sup> Although AUS indicates that it considered a "going concern" value as an element of its income and market approaches, AUS did not assign a specific, separate value for going value to be added to the results of its cost and income evaluations (PAWC St. No. 7-R, pp. 10-11).

<sup>53</sup> Tr. at 121.

utility appraisals that she completed, she has only ever employed the going value addition for Section 1329 cases.<sup>54</sup> I&E notes that there is nothing in Section 1329 that contemplates a going value adjustment or premium. Accordingly, eliminating this adjustment is in the public interest because it protects ratepayers from bearing the costs of an artificially inflated rate base, thereby preserving the Commission's ability to ensure that rates are just and reasonable for PAWC's customers.

#### **D. RATES (Joint Petition ¶¶ 16-22)**

##### **1. Cost of Service Studies**

Pursuant to the Settlement, PAWC has agreed to provide a separate cost of service study for the MACM system that separates capital expenses and operating costs for sanitary and storm water functions.<sup>55</sup> Additionally, Port Vue-specific plant in service costs of the MACM system will be identified separately within the overall MACM cost of service study.<sup>56</sup> The evidence in this proceeding supported the need for this term for several reasons, and the public interest is protected by addressing these issues, as explained below.

##### **a. The Uncertain Rate Impact of the Acquisition**

As I&E witness Cline testified, the ratemaking impact of the acquisition is relevant to this proceeding. More specifically, in the Order approving Aqua's acquisition of the wastewater system assets of New Garden Township, the Commission indicated that "it was appropriate for the ALJ to examine the ratemaking issues in the evaluation of

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<sup>54</sup> Tr. at 123.

<sup>55</sup> I&E St. No. 2, p. 20.

<sup>56</sup> Id. at 2.

the public benefit factors.”<sup>57</sup> It is therefore appropriate to analyze PAWC’s proposed post-acquisition rate structure in this case. Pursuant to the Settlement, PAWC is requesting a fair market value rate base level of \$158 million. If PAWC’s Application is approved, PAWC’s existing customers will bear the rate impact. However, without a cost of service study, the Commission’s ability to evaluate the rate impact of the acquisition upon existing PAWC customers and its options of addressing that impact to provide any appropriate relief to existing customers, could be compromised.<sup>58</sup> In this case, a cost of service study for the MACM system that separates capital expenses and operating costs for sanitary and storm water functions would help the Commission determine MACM’s revenue requirement to provide service to its different customer classes, and extend rate making options that may not exist without such a study.<sup>59</sup>

As witness Cline explained, requiring PAWC to provide this cost of service study would ensure that in a future rate case, the Commission is provided with a tool to determine the cost to operate the MACM system separately and to calculate the costs of the MACM’s different services. Additionally, the cost of service study will preserve future ratemaking options by separating the costs between PAWC’s different customer classes and jurisdictions, attributing costs to PAWC’s different customer classes and jurisdictions; and, importantly, enabling the determination of how costs will be recovered from the utility’s different customer classes and jurisdictions.<sup>60</sup>

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<sup>57</sup> Aqua/New Garden Section 1329 Case, Docket No. A-2016-2580061, p. 60 (Order entered June 29, 2017).

<sup>58</sup> I&E St. No. 2-SR, p. 4.

<sup>59</sup> I&E St. No. 2, p. 21.

<sup>60</sup> Id.

Finally, as witness Cline pointed out, the cost of service study becomes essential when rate subsidization is at issue:

a COSS [cost of service study] can establish the existence and extent of subsidization (inter and intra-class) and assist in determining the appropriate amount of revenue requirement to be shifted from the wastewater customers to the water customers, which PAWC has utilized in past base rate cases. Therefore, without the cost of service study that includes segregated storm water costs, the appropriate ratemaking recommendations for those costs cannot be proposed or implemented.<sup>61</sup>

Here, subsidization is likely to be an issue in PAWC's next rate case, as PAWC witness Nevirauskas indicated that PAWC has access to Act 11 under which it "may allocate a portion of the wastewater requirement to the combined water and wastewater customer base if in the public interest."<sup>62</sup> PAWC witness Nevirauskas further concluded that in PAWC's next base rate case, PAWC may spread a portion of the costs associated with the MACM system to its water customers.<sup>63</sup> Absent the cost of service study, the Commission's ability to evaluate any cost spreading from the perspective of cost causation would be compromised, but pursuant to the settlement, the study will be available to preserve future ratemaking options.

b. The Unique Nature and Costs of CSOs

MACM's status as a CSO highlights the importance of the cost of service term. By way of further explanation, a system's classification as a CSO means that its

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<sup>61</sup> Id. at 21-22.

<sup>62</sup> PAWC St. No. 4-R, p. 4.

<sup>63</sup> Id.

ratepayers have additional costs built into their rates that traditional sanitary sewer customers do not. Examples of these additional costs include capital plant costs for storm water catch basins, storm sewer mains prior to the combination with sanitary sewers, and overflows for when the volumes exceed the capacity of the treatment facility. Further related costs include maintenance expenses for cleaning the catch basins, repairing mains, and additional chemical expenses for the higher volumes that are treated during storm events.<sup>64</sup> Without having a cost of service study that identifies and separates these costs, there will be no way for the Commission to properly review and, as appropriate, assign these costs in PAWC's next base rate case. Additionally, as PAWC has indicated that it anticipates using Act 11 to spread costs, it is imperative that PAWC develop a separate cost of service study to isolate MACM's storm water costs so that the Commission can determine whether and how it is in the public interest to spread these costs. Because PAWC may eventually seek to spread MACM storm water-specific costs to its other wastewater and water customers,<sup>65</sup> the cost of service study will be a valuable tool in PAWC's next base rate filing. Therefore, the cost of service study term protects the public interest because it will provide available in the form necessary to enable the Commission to properly allocate costs and determine just and reasonable rates.

### c. The Port Vue System

I&E's recommendation that the plant in service costs of the Port Vue system be identified separately within the overall MACM cost of service study exists because I&E

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<sup>64</sup> I&E St. No. 2, p. 18.

<sup>65</sup> Tr. at 63-64.

has substantial concerns regarding the timing and manner in which MACM acquired the Port Vue Borough system that will be conveyed to PAWC through this proceeding. As I&E witness Spadaccio explained, MACM acquired Port Vue on April 29, 2016,<sup>66</sup> which was within fifteen days of Section 1329 being enacted.<sup>67</sup> At that time, the City had been pursuing the long-term lease or sale of the MACM assets since July 2015.<sup>68</sup> Notably, when PAWC submitted an asset purchase bid on July 29, 2016, MACM had only owned the Port Vue system for three months.<sup>69</sup> The facts surrounding MACM's purchase of the Port Vue system suggested that MACM may have strategically purchased the Port Vue System in order to increase the plant value for its pending acquisition.<sup>70</sup> To be sure, MACM purchased the Port Vue system for \$1,400,000,<sup>71</sup> but within one year's time, AUS calculated the Port Vue replacement cost new less depreciation of \$4,942,794.<sup>72</sup> Although HRG did not break out a replacement cost new less depreciation, it provided a reproduction cost analysis valuing the Port Vue System at \$18,929,210.<sup>73</sup>

Furthermore, I&E's concerns were underscored by the fact that PAWC will incur significant costs to repair the Port Vue System and to bring it into compliance with the Pennsylvania Department of Environmental Protection's ("PA DEP") regulations. More specifically, the Port Vue system requires a Long Term Control Plan ("LTCP"), has "numerous significant deficiencies" that have been identified in the collection system and

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<sup>66</sup> I&E Exhibit No. 1, Schedule 1, p. 1 of 2.

<sup>67</sup> Section 1329 was enacted on April 14, 2016 and effective on June 13, 2016.

<sup>68</sup> PAWC Application, Appendix A-14, St. No. 6, p. 9.

<sup>69</sup> PAWC Application, Appendix A-14, St. No. 1, p. 8.

<sup>70</sup> I&E St. No. 1, pp. 5-6.

<sup>71</sup> I&E Exhibit No. 1, Schedule 1, p. 1 of 2.

<sup>72</sup> PAWC Application, A-5, AUS, Fair Market Value Appraisal, p. 6.

<sup>73</sup> PAWC Application, A-5, HRG, Fair Market Valuation of the MACM Sanitary Sewer System, p. 27.

pump station, as well as a Nine Minimum Controls Plan (“NMCP”).<sup>74</sup> PAWC indicates that the cost to remedy these concerns is estimated to include \$100,000 to prepare the Port Vue LTCP and \$14,976,275 for the collection system and pump station.<sup>75</sup> PAWC has also indicated there are anticipated costs associated with the NMCP.<sup>76</sup>

Considering both the known and unknown costs of addressing Port Vue’s environmental compliance issues, I&E opines that identifying the plant in service costs of the Port Vue system separately within the overall MACM cost of service study that I&E is recommending in his proceeding. As I&E witness Cline indicated, separating the Port Vue plant in service costs is paramount because PAWC’s estimated costs for remediation of the Port Vue system are already very high and PAWC has indicated that it is still in the process of identifying the improvements necessary to address the existing deficiencies.<sup>77</sup> Isolating these costs is necessary to ensure that the Commission has an avenue to address them in PAWC’s next base rate case, where the true extent of the costs and the reality of their rate impact will be known. Therefore, PAWC’s agreement to separately identify the plant in service costs at the time Port Vue was purchased, the cost of any plant retirements, and the cost of any Port Vue plant investment will protect the public interest by ensuring that the Commission has some recourse for addressing these costs when they are fully realized.

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<sup>74</sup> I&E Ex. No. 2, Sch. 2.

<sup>75</sup> I&E St. No. 2, p. 12; I&E Ex. No. 2, Sch. 2.

<sup>76</sup> I&E Ex. No. 2, Sch. 2.

<sup>77</sup> I&E St. No. 2-SR, p. 11.

## 2. Future Base Rate Cases

Paragraph 20 of the Settlement memorializes an agreement by all Joint Petitioners, other than I&E, to propose certain terms in PAWC's next base rate case. I&E has not joined this term, as it has elected to fully reserve its rights to make any proposals deemed appropriate once all the facts are available for review in PAWC's next base rate case. However, while I&E does not join Paragraph 20, it also does not oppose this term, as it was necessary to facilitate a global resolution of this matter. The remaining rate terms in Paragraphs 21 and 22 simply memorialize PAWC's intention to make certain proposals in future base rate cases, and as these terms do not limit I&E's position in future base rate cases, I&E also does not oppose them.

### **E. LOW INCOME PROGRAM OUTREACH (Joint Petition ¶ 23)**

Pursuant to the Settlement, PAWC has agreed that within the first 90 days of its ownership of the System, it will either include a bill insert to McKeesport-area customers regarding its low-income programs or include this information in a welcome letter to McKeesport-area customers. In either case, these materials will include a description of the available low income programs, the eligibility requirements for participation in the programs, and PAWC's contact information. PAWC also committed to performing ongoing, targeted outreach to its McKeesport-area customers regarding its low-income program. Finally, the Joint Petitioners have agreed confer in good faith and agree upon such additional outreach prior to closing of the Transaction.

Although I&E did not take a position on this issue during the evidentiary portion of this proceeding, I&E nonetheless supports this term. Ensuring that low-income customers



are aware of available opportunities for financial assistance is in the public interest because will better facilitate these customers' access to wastewater service. Increasing access to wastewater service is consistent with the Code's policy of ensure that service remains available to all customers on reasonable terms and conditions.<sup>78</sup>

**F. DISTRIBUTION SYSTEM IMPROVEMENT CHARGE (Joint Petition ¶ 24)**

The Joint Petitioners have agreed that consistent with Section 1329, PAWC shall be permitted to collect a distribution system improvement charge ("DSIC") prior to the first base rate case in which the McKeesport service area plant-in-service is incorporated into rate base, subject to certain conditions. These conditions are as follows: (1) PAWC's filing of an amended wastewater long term infrastructure improvement plan ("Amended LTIIP") may not re-prioritize other existing commitments in other services areas, (ii) the Commission must approve the Amended LTIIP, which may be modified at its discretion, and (3) after Commission's approval of the Amended LTIIP, PAWC must file a compliance tariff supplement which incorporates the McKeesport area rate zone into its existing DSIC tariff, including all customer safeguards applicable thereto.

I&E took no position regarding PAWC's request for approval to collect a DSIC as permitted under Section 1329, as this request appeared to simply memorialize PAWC's intention to employ certain provisions of Section 1329. However, I&E has reserved the right to address these issues in future proceedings, including base rate and distribution system improvement charge proceedings, when additional information and facts are

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<sup>78</sup> 66 Pa. C.S. § 1402(3).

available and when these issues are ripe for review.<sup>79</sup> While I&E still reserves its rights, I&E nevertheless opines that this term serves the public interest because PAWC has agreed that existing commitments will not be re-prioritized as a result of this term. With this in mind, the System customers will benefit from improved wastewater infrastructure, promoting safer and more reliable service. At the same time, the improvements already identified and planned for existing PAWC ratepayers will not be jeopardized by PAWC's commitment to MACM. Therefore, I&E opines that this term is in the public interest.

**G. ACCRUAL OF ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION (Joint Petition ¶ 25)**

Through the Settlement, the Joint Petitioners acknowledge that PAWC's Application includes a request to accrue allowance for funds used during construction ("AFUDC") for post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. Although the Joint Petitioners agree that they will not contest this request in this proceeding, they reserve their rights to litigate their positions fully in future rate cases. I&E endorses this term because while it enables PAWC to memorialize its intent to employ certain provisions of Section 1329, it also empowers parties to review PAWC's proposal in a future base rate case. Preserving the ability to litigate the proposed AFUDC treatment protects the public interest by ensuring that interested parties are not hindered in developing a full and complete record for the Commission on this issue when additional information is available and ratemaking issues are ripe for determination

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<sup>79</sup> I&E Main Brief, p. 41.

## **H. DEFERRAL OF DEPRECIATION FOR POST-ACQUISITION IMPROVEMENTS (Joint Petition ¶ 26)**

Like the above term, the Joint Petitioners acknowledge that PAWC's Application requests permission to defer depreciation related to post-acquisition improvements not recovered through the DSIC for book and ratemaking purposes. Although the Joint Petitioners agree that they will not contest this request in this proceeding, they reserve their rights to litigate their positions fully in future rate cases. I&E endorses this term because while it enables PAWC to memorialize its intent to employ certain provisions of Section 1329, it also empowers parties to review PAWC's proposal in a future base rate case. Preserving the ability to litigate the proposal to defer depreciation for post-acquisition improvements protects the public interest by ensuring that interested parties are not hindered in developing a full and complete record for the Commission on this issue when additional information is available and ratemaking issues are ripe for determination

## **I. TRANSACTION AND CLOSING COSTS (Joint Petition ¶ 27)**

The Joint Petitioners acknowledge that PAWC's Application includes a request that PAWC be permitted to claim transaction and closing costs associated with the acquisition. Importantly, while making this acknowledgment, the Joint Petitioners nevertheless reserve their rights to litigate the transaction and closing costs when they are ripe for determination in PAWC's next base rate case. As PAWC has already correctly acknowledged, the Commission's Final Implementation Order at Docket No. M-2016-2543193 makes it clear that the reasonableness and recovery of transaction and closing

costs are not properly reviewed and cannot be approved in Section 1329 proceedings.<sup>80</sup> Instead, these costs are properly reviewed in the Applicant's next base rate case that follows the acquisition, and they will be subject to the preponderance of evidence standard in that review. From I&E's perspective, this Settlement term is in the public interest because it respects the Commission's directive that determinations regarding transactions and closing costs should be made only in the appropriate forum, a base rate case. Consistent with that directive, I&E's agreement to this term in no way operates as a concession that the identified transactions costs are reasonable or that they should be recovered from ratepayers.

**J. APPROVAL OF SECTION 507 AGREEMENTS (Joint Petition ¶ 28)**

Pursuant to the Settlement, the Joint Petitioners agree that the Commission should issue Certificates of filing or approvals, for the underlying Asset Purchase Agreement and for the enumerated municipal agreements appearing in Paragraph 28 of the Settlement. During this proceeding, I&E did not oppose approvals of these contracts under Section 507 except for the APA. Specifically, I&E opposed PAWC's Application, as filed, including the underlying APA, on the grounds that it contravened Section 1102 of the Code. However, and for the reasons indicated above, the Settlement has resolved all I&E's issues in this case, including all concerns that previously arose under Section 1102 of the Code. Therefore, I&E no longer opposes approval of the APA, and instead

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<sup>80</sup> PAWC Statement No. 1, p. 3.

recommends that the Commission approval all the enumerated contracts under Section 507 of the Code.

#### **IV. CONCLUSION**

16. Based upon I&E's analysis of the filing, acceptance of this proposed Settlement is in the public interest. Resolution of this case by settlement rather than litigation will avoid the substantial time and effort involved in continuing to formally pursue all issues in this proceeding at the risk of accumulating excessive expense.

17. I&E's agreement to settle this case is made without any admission or prejudice to any position that I&E might adopt during subsequent litigation if the Settlement is rejected by the Commission or otherwise properly withdrawn by any other parties to the instant proceeding.

18. If the ALJS recommend that the Commission adopt the Settlement as proposed, I&E agrees to waive the filing of Exceptions. However, I&E has not waived its right to file Exceptions with respect to any modifications to the terms and conditions of the Settlement, or any additional matters, that may be proposed by the ALJs in their Recommended Decision. I&E also reserves the right to file Reply Exceptions to any Exceptions that may be filed.

**WHEREFORE**, the Commission's Bureau of Investigation and Enforcement represents that it supports the Settlement as being in the public interest and respectfully requests that Administrative Law Judges Mark A. Hoyer and Mary D. Long and that the Commission approve the terms and conditions contained in the foregoing Joint Petition for Approval of Settlement of All Issues without modification.

Respectfully submitted,



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Dated: September 20, 2017

**APPENDIX H. STATEMENT IN SUPPORT OF THE  
OFFICE OF CONSUMER ADVOCATE**

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

In re: Application and related filings of	:	
Pennsylvania-American Water Co. for	:	
approval of its acquisition of wastewater	:	Docket No. A-2017-2606103
system assets of The Municipal Authority of	:	
the City of McKeesport	:	

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OCA STATEMENT IN SUPPORT OF  
JOINT PETITION FOR SETTLEMENT OF ALL ISSUES

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The Office of Consumer Advocate (OCA), one of the signatory parties to the Joint Petition for Settlement of All Issues (Settlement) respectfully requests that the terms and conditions of the Settlement be approved by the Pennsylvania Public Utility Commission (Commission).

I. INTRODUCTION

The procedural history of this proceeding and an overview of the proposed transaction is set forth in the Main Brief submitted by the OCA on August 22, 2017, pages 1 through 3.

II. TERMS AND CONDITIONS OF JOINT PETITION FOR SETTLEMENT

The terms of the proposed Settlement address two matters raised by the OCA in its testimony and briefs: the ratemaking rate base to be incorporated into the acquiring utility's revenue requirement and the rate impact for existing Pennsylvania-American Water Company (PAWC) wastewater customers, existing PAWC water customers and the acquired customers, as follows:



1. Fairmarket Value, ¶14. As part of this proceeding, PAWC sought to establish the ratemaking rate base for this acquisition pursuant to Section 1329 of the Public Utility Code, 66 Pa. C.S. § 1329. Based on appraisals presented by PAWC and the Municipal Authority of the City of McKeesport, PAWC sought a ratemaking rate base of \$162 million, which was the price PAWC agreed to pay for the McKeesport system. The originally agreed-upon purchase price of \$156 million was increased to reflect the average of the appraisals. PAWC St. 1 at 11. The OCA witnesses challenged the appraisals, identifying numerous errors and the use of assumptions and adjustments that were inconsistent with financial and utility ratemaking practices. OCA St. 1 at 18-26; OCA St. 1R at 1-11; OCA St. 1S at 16-20; OCA St. 2 at 4-28; OCA St. 2S at 1-6. The OCA's recommended adjustments served to reduce the ratemaking rate base amount below the \$162 million purchase price.

In settlement, the parties agreed that for ratemaking purposes, the ratemaking rate base pursuant to Section 1329 will be \$158 million. The proposed ratemaking rate base pursuant to Section 1329 is lower than requested in the Company's filing and represents an amount which, in the OCA's view, would be within the range of likely outcomes in the event of full litigation of the case. This provides some mitigation of the rate impact of the transaction for existing PAWC customers and the acquired McKeesport customers by reducing overall costs.

2. Fairmarket Value, ¶15. As noted above, the OCA's witnesses identified a number of errors in the Utility Valuation Engineer appraisals as well as the use of assumptions and adjustments that were unreasonable or inconsistent with financial and utility ratemaking practices and the OCA's witnesses recommended corrective adjustments. The proposed

Settlement reflects the Parties' explicit acceptance of four of the OCA's adjustments.

These four are:

- (a) Market Approach: The purchase price for each acquisition shall be based on the actual amount paid for the assets at the time of purchase and future capital improvements shall not be included;
- (b) Income Approach: The rate base / rate of return methodology is not an appropriate analysis for the appraisal;
- (c) The "Going Value" and "Provision for Erosion on Return" add-ons will not be adopted or included in the appraisals; and,
- (d) The overhead cost add-on will not be adopted or included in the appraisals.

These adjustments reflect accepted financial and ratemaking principles and help to improve the reliability of data used in appraisals and the integrity of the result.

3. Rates, ¶17-22. In this proceeding, the OCA identified specific harm to PAWC's existing customers and to the acquired McKeesport customers that would result from the acquisition. In particular, the OCA pointed out that the acquisition could increase rates for PAWC's existing wastewater customers and water customers if the costs of the MACM system are added to rate base and shifted to those customers. OCA St. 1 at 8, 11, 13, 15-18; OCA St. 1S at 10-11. The OCA also noted that if MACM customers' rates were raised to cover the cost of service under the agreed upon purchase price and PAWC ownership, those customers would see an increase of approximately 137% from current rates, in the first rate case that takes effect after the one-year rate freeze contained in the Asset Purchase Agreement. OCA St. 1 at 13.

The settlement seeks to address these issues in several ways. First, Paragraphs 17 and 18 require PAWC to provide a cost of service study that fully separates the costs of providing the stormwater component of wastewater services in the McKeesport service

area and a study that identifies all costs and revenues associated with the operations (sanitary and stormwater) of the McKeesport system. This provision helps to analyze the exact cost of the acquired system including its separate stormwater component.

Second, Paragraph 11 provides that, in its first base rate case following closing, PAWC will propose to establish a separate rate zone for McKeesport, which will provide a means for the parties to use the cost of service data to set rates for those customers that differ, as appropriate, from rates established for other wastewater customers. Third, Paragraph 11 also provides that, in the first base rate case after the acquisition closes, PAWC will propose to increase the rates for the McKeesport system to an amount equal to the Zone 1 wastewater rates of PAWC's wastewater division, unless such increase would be more than 2.0x the system-average wastewater division increase. This settlement term helps to address the potential level of subsidy by PAWC's other wastewater customers (and potentially its water customers) and applies the ratemaking principle of gradualism to rates set for customers in the McKeesport service area.

Fourth, Paragraphs 11 and 12 move the acquired customers toward their cost of service. While Paragraph 11 moves the acquired customers to or toward Zone 1 wastewater rates, Paragraph 12 moves them further toward a rate level that reflects their full cost of service. Specifically, it provides that, in PAWC's second base rate case following closing, PAWC will propose to increase the rates of the McKeesport system to an amount at least equal to Zone 1 and further toward the system's cost of service. These provisions help to mitigate any cross-subsidization.

4. Low Income Program Outreach, ¶23. The Mayor of the City of McKeesport testified that in 2015, 38% of McKeesport residents maintained incomes below the poverty level.

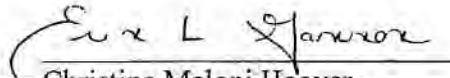
PAWC St. 6 at 5. Paragraph 23 of the proposed Settlement states that, within the first 90 days of its ownership, PAWC will provide information regarding its low-income programs to customers in the McKeesport service area via bill insert or letter, including a description of the available programs, eligibility requirements and PAWC's contact information. In addition, PAWC agrees to conduct ongoing, targeted outreach, in which the OCA will have input. These provisions will help to ensure that customers in the McKeesport service area have ongoing information about low-income programs offered by PAWC. This is an important component of the proposed Settlement, particularly, in the context of the Company's commitment to propose increases to the McKeesport rates that move the system toward its cost of service.

5. Distribution System Improvement Charge (DSIC), ¶24. The parties to the proposed Settlement agreed that PAWC may apply the DSIC to customers in the McKeesport service area prior to the first base rate case in which the system's plant in service is incorporated into rate base if certain conditions are met. In particular, Paragraph 24 states that PAWC's planned capital projects for the McKeesport system will not change the prioritization of existing commitments in other service areas. This settlement term allows for McKeesport customers to begin contributing, up to 5% of their total wastewater bill, toward DSIC-eligible capital projects and helps to ensure that DSIC investment is not shifted away from PAWC's other wastewater service areas during the amended LTIP period.

III. CONCLUSION

For the foregoing reasons, the Office of Consumer Advocate submits that the terms and conditions of the Settlement should be approved.

Respectfully Submitted,



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Dated: September 20, 2017

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