

Aqua Exh. 5-A, Part I, Sch. A; Aqua Exh. 5-B, Part I, Sch. WW-A; 66 Pa. C.S. § 1311(c)).

Aqua explained that Act 11 allows a utility that provides both water and wastewater services to allocate a portion of the wastewater revenue requirement to the combined water and wastewater customer base if doing so is in the public interest. Aqua M.B. at 213 (citing *Aqua 2018 Rate Case*, additional citations omitted). Aqua further explained that the public interest is served if properly incurred costs to upgrade a nonviable system can be allocated to the combined wastewater and water customer base. Aqua provided that the Commission noted that one of the benefits of Act 11 is that the costs of necessary upgrades which can be substantial can be spread among the common customer base of water and wastewater utilities. Aqua M.B. at 214-215 (citing Docket No. M-2012-2293611 (Tentative Implementation Order entered May 12, 2012, and Final Implementation Order entered August 2, 2012)).

In order to provide a direction for gradualism and avoid substantial rate shock to wastewater customers who will be subject to their first rate increases resulting from a Commission rate case, the Company allocated a portion of the wastewater revenue requirement to its water customers. Aqua M.B. at 215-216 (citing Aqua St. 1-R at 23-25). Aqua determined its Act 11 allocation from wastewater to water rates “by subtracting the proposed level of wastewater revenue after various increases from the *pro forma* cost of wastewater service for the twelve months ended March 31, 2023 from the revenue requirement for each area.” Aqua M.B. at 216 (citing Aqua St. 5 at 10; 66 Pa. C.S. § 1311). After increasing and consolidating various wastewater rates to a level that moved each division towards the cost of service while mitigating significant rate impacts, the Company proposed to allocate \$20,818,925 of the remaining shortfall

66 Pa. C.S. § 1311(c).

from wastewater revenues to water customers.⁷⁰ Aqua St. 1-R at 2-3; Aqua Exh. 1-A(a). Aqua noted that this allocation represents approximately 30% of the Company's proposed revenue requirement from wastewater to water. Aqua M.B. at 216 (citing Aqua St. 1-R at 24).

Aqua proposed that if the Commission approves a rate increase that is less than that proposed by the Company, that the scale back (or reduction) be applied proportionately based on the Company's proposed revenue allocation. Aqua further proposed that no wastewater scale back occur until the total wastewater Act 11 allocation is eliminated, and any scale back after the Act 11 allocation is eliminated be based on the Company's proposed rates. Aqua M.B. at 265 (citing Aqua St. 5-R at 19-20, 24-25).

I&E's witness, Mr. Joseph Kubas, disagreed with the Company's proposal that its water customers subsidize wastewater customers by approximately \$20.8 million because it is large and unreasonable. Mr. Kubas contended that water customers are not wastewater customers, and each utility service should recover as much of the cost to provide that service as possible. I&E M.B. at 70; I&E St. 5 at 7-8. Further, Mr. Kubas contended that the Company did not demonstrate how allocating 30% of the cost of operating wastewater systems to water customers is reasonable. I&E St. 5-SR at 6.

I&E submitted that Mr. Kubas created a rate design that applies an Act 11 subsidy from wastewater to water consistent with cost of service principles and is in the public interest. Accordingly, I&E recommended that the Company's proposed water subsidy be reduced by \$5,072,876. I&E St. 5-SR at 4-5; I&E Exh. No. 5, Sch. 1 at 1. Subsequently, in surrebuttal testimony, Mr. Kubas revised his recommended reduction to

⁷⁰ Initially, Aqua submitted that wastewater revenues of \$20,839,425 be allocated to water customers. Aqua M.B. at 216.

the subsidy necessary for wastewater systems operation by \$5,044,324. I&E St. 5-SR at 8; I&E Exh. 5-SR, Sch 1 at 1.

With regard to any scale back that may result if the Commission approves a rate increase that is less than that proposed by the Company, I&E submitted that the Company's proposed rates should be scaled back to produce the revenue requirement allowed by the Commission. I&E further proposed that, to determine the amount of the Act 11 subsidy revenue requirement to be allocated to water operations, the wastewater operations revenue requirements should be determined first, and that the water rates should then be scaled back to recover the resulting water operations' full revenue requirement. Regarding wastewater, I&E recommended that no scale back of wastewater rates should occur until the total Act 11 wastewater subsidy is eliminated. I&E R.B. at 55-56 (citing I&E M.B. at 71).

Similar to I&E, the OCA disagreed with the Company's proposal for its water customers to pay approximately \$20.8 million to subsidize its wastewater operations because the wastewater rates would not support a reasonable relationship to the utility's cost of serving the wastewater customers. According to the OCA, it is not in the public interest to use Section 1311(c) and Section 1329 in combination to require that water customers subsidize approximately 75% of the revenue requirement generated by the FMV premiums for the five wastewater systems acquired under Section 1329.⁷¹ OCA R.B. at 46-47 (citing OCA M.B. at 89-91; OCA St. 4 at 7-8).

The OCA submitted that its proposed Act 11 wastewater to water subsidy of \$11.774 million is more moderate and in the public interest than that proposed by the other Parties because it recognizes that the Company's water customers do not receive a

⁷¹ Acquired systems or customers represent Rate Zones 7 through 11, or systems/customers that were acquired by the Company since its last rate proceeding.

direct or indirect benefit from FMV premiums paid to residents of the seller municipalities and the impact of rate increases will be mitigated on the Company's legacy wastewater customers by shifting a substantial amount of their share of the wastewater increase to water customers.⁷² OCA R.B. at 47. The OCA asserted that its proposed Act 11 subsidy recognizes the benefit that customers of the acquired Section 1329 systems receive from the FMV premiums and mitigates the impact of the rate increases by shifting their share of the wastewater increase to water customers. OCA R.B. at 47 (citing OCA St. 4 at 3-4, 7-9; I&E St. 5 at 66). The OCA also proposed that, if the Commission adopts the OCA's recommendation that assigns more revenue requirement to the five wastewater systems acquired under Section 1329, then the revenue requirement calculation should be based on the Company's authorized ROE. In this manner, the OCA explained that if the Commission adopts a different capital structure and/or lower ROE than proposed by the Company, then the scale back should first reduce the revenue requirement associated with the FMV premiums, to the benefit of the acquired customers. The OCA further recommended that if the Commission reduces the revenue requirement for non-ROR reasons, then the benefit should be applied to reduce the subsidy by water operations. OCA R.B. at 53-54 (citing OCA M.B. at 96-98; OCA St. 4 at 11-12).

The OSBA criticized the Company's proposed revenue allocation for water service as being unjust, unreasonable, and in violation of *Lloyd* because it fails to move the Residential, Public, Other Water Utilities and Private Fire Protection customer classes closer to their respective cost of service. OSBA R.B. at 7-8 (citing OSBA M.B. at 9-10; *Pa. PUC v. City of Bethlehem-Water Department*, Docket No. R-2020-3020256 (Order entered April 15, 2021) (*City of Bethlehem*) at 36; *Lloyd*). The OSBA also asserted that the Company's proposal to move each customer classification toward its appropriate

⁷² Legacy systems or customers represent Rate Zones 1 through 6, or systems/customers that were under the Company at the time of its last rate case proceeding.

percentage cost of service without isolating the Act 11 allocation has no legal foundation. OSBA R.B. at 9-11 (citing OSBA St. 1-S at 4-8).

The OSBA's witness, Mr. Brian Kalcic, proposed an alternative revenue allocation for water service, exclusive of Act 11 considerations, to move customer classes toward their respective costs of service. OSBA R.B. at 8-9 (citing OSBA Exh. BK-1 W, Schs. BK-4W, BK-5W). The OSBA averred that isolating Aqua's claimed water cost of service from Act 11 subsidies is necessary because Act 11 addresses the recovery of proposed wastewater subsidies and is not related to the water cost of service. The OSBA explained that its proposed revenue allocation approach assigns a greater revenue responsibility to the Residential class than under the Company's proposal because the Company's proposed revenue allocation actually moves the Residential class away from its cost of service. The OSBA notes that in this proceeding, any revenue allocation that moves all classes toward cost of service must assign greater revenue responsibility to the Residential class. OSBA R.B. at 11-12. Regarding wastewater service, the OSBA submitted that the Company's proposed Act 11 revenue requirement be reduced by assigning an additional total increase to Aqua's Base and New Garden wastewater divisions. OSBA R.B. at 15 (citing OSBA St. 1-S at 1-3; OSBA St. 1 at 15-16).

Regarding the Company's proposed scale back of its proposed revenue allocation, the OSBA asserted that: (1) because the Company's proposed revenue allocation is cost based, using it as a starting point for any scale back is not valid; and (2) a separate scale back for reductions in the Company's allowed water service revenue requirement is necessary. OSBA R.B. at 16-17 (citing OSBA St. 1-R at 8-11). The OSBA proposed that if the Commission awards the Company a water service revenue increase that is less than Aqua's requested amount and exclusive of Act 11 considerations, then the OSBA's recommended class increases for water service should be proportionately scaled back. OSBA R.B. at 17 (citing OSBA M.B. at 19; OSBA Exh. BK-1 W, Sch. BK-4W). The OSBA also proposed that, at the conclusion of this

proceeding, the Act 11 revenues assigned to water classes should be subject to a separate scale back of Aqua's proposed allocation of Act 11 revenues to water customers. OSBA R.B. at 18 (citing OSBA M.B. at 20).

Aqua LUG submitted that the Company's proposed revenue allocation fails to sufficiently move the customer classes towards cost of service. Therefore, Aqua LUG's witness, Mr. Richard A. Baudino, proposed adjustments to the Company's proposed revenue allocation that would result in most customer classes moving closer to their costs of service, consistent with *Lloyd*. Specifically, Mr. Baudino recommended as follows: (1) move the Residential class Relative Rate of Return (RROR) from 0.96 to 0.98; (2) move the Commercial class RROR from 1.04 to 1.02; (3) move the Industrial class RROR from 0.93 to 0.99; and (4) move the Public class RROR from 1.18 to 1.15. Mr. Baudino also recommended that, in the spirit of gradualism, any excess revenue requirement above the Industrial customer cost of service should be allocated to the Residential customer class. Aqua LUG M.B. at 7, 9-10 (citing Aqua LUG St. 1 at 5-6; Aqua LUG Exh.__(RAB-2)).

Aqua LUG provided that Mr. Baudino supported the adjusted revenue allocation recommended by the OSBA witness, Mr. Kalcic, to achieve additional movement towards cost of service. Aqua LUG M.B. at 10 (citing Aqua LUG St. 1S at 3; OSBA St. 1-R at 11-12). Accordingly, Aqua LUG recommended that the Commission should modify the Company's proposed revenue allocation to reflect the OSBA's proposed adjustments or, alternatively, Aqua LUG's proposed adjustments. Aqua LUG M.B. at 7, 11 (citing OSBA St. 1, Exh. BK-1 W, Sch. BK-4W; Aqua LUG St. 1, Exh.__(RAB-2)). Aqua LUG also recommended that, if the Commission approves a revenue increase lower than the proposed revenue allocation, then the approved revenue allocation should be scaled back proportionately. Aqua LUG M.B. at 11-12 (citing Aqua LUG St. 1 at 6).

Masthope submitted that any revenue allocation pursuant to Act 11 and any rate design or rate structure will result in significant increases in wastewater rates for Masthope ratepayers. Masthope R.B. at 6 (citing Masthope M.B. at 19-24; 66 Pa. C.S. § 1311). Further, Masthope asserted that the Act 11 subsidy adjustments proposed by I&E and the OCA will result in unjust and unreasonable rates that would have an adverse effect on Masthope's wastewater customers. Moreover, Masthope recommended that, if the Commission approves revenues in amounts less than what the Company proposed, any increased revenue requirement for water and wastewater customers and the amount of revenue support to be provided by water customers should be distributed in a manner consistent with the Company's proposal. Masthope M.B. at 20-22 (citing Masthope St. 2-R at 3-5). Additionally, Masthope proposed that, in anticipation that increases in costs and the potential need for cross-subsidies will continue for several years, the Commission should hold Aqua's wastewater revenue increase at the Company's proposed level while reducing the water increase to achieve a reduction in any computed cross subsidies. Masthope M.B. at 22.

2. Recommended Decision

In her Recommended Decision, the ALJ determined that Aqua's allocation of revenues between all water and wastewater customer classifications is reasonable and should be approved. Regarding the Act 11 subsidy allocated to water customers, the ALJ recommended that the Commission adopt I&E's proposed methodology for allocating revenue and designing wastewater rates. R.D. at 91, 93.

The ALJ recommended an additional adjustment for shifting the wastewater revenue requirement to water customers. Specifically, the ALJ provided that the wastewater revenue is based upon the expenses associated with wastewater service, such as bad debt expense, which is determined using an uncollectible accounts factor. The ALJ concluded that because the Company would incur bad debt expenses from water

customers at the water uncollectible accounts factor rather than at the wastewater uncollectible accounts factor, it is not reasonable to charge water customers for bad debt expenses at the wastewater uncollectible accounts factor because water customers will ultimately pay the revenue requirement that was shifted to them. Therefore, the ALJ reasoned that, when wastewater revenue requirement is shifted to water customers, the gross wastewater revenue requirement must be reduced to a net basis using the revenue factor for each service, as reflected in Table I(B) for each of the wastewater tables in the Appendix of the Recommended Decision, to determine the water net income that the Company will receive and the wastewater net income that the Company would have received. The ALJ found that the difference between these net values is grossed up using the water revenue factor before being deducted from the gross allocated wastewater revenue requirement, thereby resulting in an adjusted gross water revenue requirement that provides the Company the same net income from water customers that it would have received from wastewater customers. R.D. at 86-87. Table Act 11 in the Appendix of the Recommended Decision provides the detail of the ALJ's adjusted gross water revenue requirement.

The ALJ addressed Mr. Kubas' recommendation to shift some of the revenue increase from the acquired systems (Rate Zones 7 through 11) to the legacy systems (Rate Zones 1 through 6).⁷³ R.D. at 87-88. Specifically, the ALJ discussed Mr. Kubas' view that, although each type of utility service should recover the cost of providing service as much as possible to the subsidy allocated to water customers, eliminating the subsidy would result in large increases to the monthly charges and rates for residential and commercial wastewater customers. The ALJ continued that

⁷³ We note that in her Recommended Decision, the ALJ presented a table prepared by Mr. Kubas "which summarized each party's proposed allocation of revenue." R.D. at 87-88 (citing I&E Exh. 5, Sch. 1). As discussed, *infra*, we shall strike the table presented at the top of page 88 in the Recommended Decision, consistent with this Opinion and Order.

Mr. Kubas reduced the subsidy allocated to water customers by recommending that the usage rate increases to the average residential customers be limited. The ALJ also addressed the proposed alternative Act 11 subsidy analyses offered by the OCA and the OSBA. R.D. at 88-89 (citing I&E St. 5 at 7-8, 10, 35-36, 38; OCA St. 4 at 1; OSBA St. 1 at 16-17).

The ALJ explained that in public utility regulation, and particularly in infrastructure improvements, it is not uncommon to approve the socialization of costs which benefit a subset of consumers over a larger group of consumers. The ALJ noted Act 11 permits the costs associated with wastewater system improvements to be shifted to water customers to avoid steep rate hikes to wastewater customers. The ALJ addressed Aqua's statement that the proposed revenue increase for both water and wastewater is primarily driven by investment in infrastructure, noting that it is important to understand that for the Acquired Systems, both the buyer, Aqua, and the selling municipalities should know that at the time of acquisition customers were likely paying rates that were well below the cost of service, either because rates had not been increased or facility improvements had been deferred. R.D. at 90.

Therefore, the ALJ reasoned that to meet the increased costs associated with system improvements, rates will need to be increased, and the increases might be substantial. The ALJ also addressed the responsibility of the community representatives of the acquired systems who sold their systems to avoid increasing taxes or utility rates or both. Specifically, the ALJ reasoned that such communities achieved a benefit from the revenue generated by the sale of their wastewater systems, and, because these communities have already enjoyed some benefit from the sale of the system, it is not equitable to the Company's water customers to mitigate the resulting increases in expenses to care for the acquired systems. R.D. at 90. Moreover, the ALJ reasoned that it is not fair for water customers to take on the burden of filling the gap between the cost of service to serve these wastewater systems because the proceeds Aqua paid

municipalities to acquire the wastewater systems are used by those municipal governments to reduce, stabilize, or eliminate municipal costs recovered through taxes to the benefit of the wastewater customers residing within those municipalities. *Id.* (citing Aqua St. 1-R at 25). The ALJ highlighted that the Commission relied on these benefits when it determined that the acquisitions were in the public interest. R.D. at 90.

According to the ALJ, although increasing rates gradually to avoid rate shock is important to consider in setting reasonable rates, such gradualism is only one consideration among many, and some level of rate shock is inevitable. The ALJ reasoned that Aqua's approach of allocating 30% of the proposed wastewater revenue requirement to water customers is arbitrary and will not result in just and reasonable rates. Therefore, the ALJ found that, given the consideration of rate shock in the setting of rates in certain circumstances, Aqua's proposal to shift 30% of the wastewater revenue requirement to water customers is not equitable. *Id.*

Additionally, the ALJ addressed the agreement of both I&E and Aqua that no scale back of the Company's proposed wastewater rates should occur until the total wastewater allocation is eliminated. The ALJ found that any scale back of water rates will first reduce the Act 11 allocation. R.D. at 90-91 (citing Aqua St. 5-R at 25; *Lloyd*).

Ultimately, the ALJ recommended adoption of I&E's proposed methodology for allocating revenue and designing wastewater rates, reasoning that I&E's approach considers the number of water and wastewater customers in each system and balances the goal of moving rates toward alignment with the cost of service while mitigating some of the large rate increases that would result if no allocation of wastewater revenue was approved. The ALJ found that I&E's approach addresses the benefits received by the communities serviced by the acquired systems from the sale of their systems to the Company, adding that I&E's method is less complicated than the method advocated by the OCA. R.D. at 91.

Regarding water allocation, the ALJ reasoned that Aqua and the OCA's approach to revenue increases for water is more reasonable than the proposed modifications of the OSBA and Aqua LUG. *Id.* at 91. The ALJ found that, but for the Act 11 subsidy allocated to water customers, Aqua's allocation of revenues between all water customer classifications and all wastewater customer classifications is reasonable and should otherwise be approved. R.D. at 91, 93 (citing OSBA M.B. at 9-20; Aqua LUG M.B. at 8-11).

The ALJ highlighted the OCA's argument that the results of the OSBA's witness, Mr. Kalcic's, class revenue allocations (before the Act 11 subsidy) are not reasonable. R.D. at 91 (citing OCA St. 4R at 5-7). Specifically, the ALJ observed that, although the Residential and Industrial classes are currently earning close to parity, Mr. Kalcic's proposal would increase their percentage of system average revenue responsibility. *Id.* Similarly, the ALJ observed that concurrently, the Commercial class is also earning close to parity, but Mr. Kalcic recommended that this class receive 74% of the system average percentage increase. R.D. at 92. The ALJ also reasoned that Aqua's proposed allocation of revenues views cost of service as a whole and does not attempt to exclude the Act 11 allocation from its analysis. *Id.* Further, the ALJ reasoned that Aqua moves each customer classification toward its appropriate percentage cost of service, including Act 11 allocation. R.D. at 92.

In reviewing the Company's proposed revenue allocation compared to the OSBA's recommended revenue allocation, the ALJ noted that it appears that the OSBA's recommendations to isolate and remove the Act 11 allocation from its analysis is motivated by its preference to decrease the revenue allocated to non-residential customer classes while increasing the revenue allocated to residential classes. R.D. at 92 (citing Aqua St. 5-R at 5). However, the ALJ emphasized that, from the perspective of customers, the effect of the increase includes both the water increase and the wastewater

allocation. Therefore, the ALJ found that Aqua's methodology better reflects the cost of service. R.D. at 92.

The ALJ also addressed Aqua LUG's witness, Mr. Baudino's, proposed reductions to the projected increases to the Commercial and Public classes. R.D. at 93 (citing Aqua LUG St. 1 at 5; Aqua LUG Exh. __ (RAB-2)). Specifically, the ALJ agreed with Aqua witness, Ms. Constance E. Heppenstall, that Mr. Baudino's recommendation, which is based on moving a portion of the Industrial class increase to the Residential class due to a larger increase to blocks 5 and 6 of the consumption rates for the Industrial class, would result in RROR between 0.98 and 0.96 and, therefore, should be rejected. R.D. at 93 (citing Aqua St. 5-R at 25). Similarly, the ALJ agreed with the OCA that Aqua LUG does not consider other inherent complexities in this case, including: (1) gradual movement of various divisions to a state-wide rate; (2) the Public Fire revenue subsidy required by statute; and (3) subsidization of wastewater operations by water operations. R.D. at 93 (citing Aqua St. 4R at 12).

3. Exceptions and Replies

a. Aqua Exception No. 9 and Replies

In its Exception No. 9, Aqua submits that the ALJ's recommendation that the Commission accept I&E's methodology for allocating wastewater revenues and wastewater rates under Act 11 should be rejected, and the Company's proposed Act 11 revenue allocation should be adopted. Aqua Exc. at 31, 34 (citing R.D. at 91, 96). Aqua challenges the ALJ's reasoning that the Company's proposed allocation of wastewater revenues is not fair to water customers because the Company and the selling municipalities should know that rates would increase at the time of a wastewater system acquisition as wastewater customers were likely paying rates that were below the cost of service. Aqua Exc. at 31-32 (citing R.D. at 89-90). Aqua counters that the Company

demonstrated that justifications advanced by I&E and restated by the ALJ are unreasonable and unsupported by record evidence. Aqua Exc. at 32. Specifically, the Company contends that I&E's testimony: (1) implies that municipal governments believed that the cost of acquiring the subject systems would be carried by existing Aqua customers; and (2) ignores the Company's explanation that, as part of the Section 1329 process, future customer rates will be impacted by the purchase price. Moreover, Aqua notes that, contrary to I&E's arguments, the Company demonstrated that it educates and engages with municipal leaders on the ratemaking process. Aqua Exc. at 32 (citing Aqua M.B. at 218-19).

Aqua also challenges the ALJ's reasoning that: (1) community representatives who decided to sell a system due to increasing taxes and/or utility rates are unable to avoid the consequences of that decision; and (2) the revenue generated by the sale of a community's wastewater system is a benefit to the communities of the acquired systems. Aqua Exc. at 32 (citing R.D. at 90). Specifically, Aqua posits that the ALJ took the testimony of Aqua's witness, Mr. Packer, out of context because Mr. Packer was responding to the proposed Act 11 revenue allocation advanced by the OCA, and although Mr. Packer did not disagree with the benefits to the communities whose systems were acquired by Aqua, he states that, "the principles of gradualism should prevail and be utilized to mitigate these first in rate increases." Aqua Exc. at 32 (citing Aqua M.B. at 217-18; Aqua St. 1-R at 25). Further, Aqua claims that the ALJ ignored Mr. Packer's testimony that over the long-term, the Commission will have sufficient opportunities in subsequent rate cases to adjust the rate design for each of the acquired systems. Aqua Exc. at 32-33 (citing Aqua St. 1-R at 25-26). Aqua asserts that the ALJ, instead, reasoned that each system should be subjected to a large and immediate rate increase in this proceeding because an immediate benefit was obtained by the communities which sold wastewater systems to the Company. Accordingly, Aqua contends that such reasoning highlights that I&E's proposal will result in rate shock. Aqua Exc. at 33.

Aqua also challenges the ALJ's determination that the Company's approach of allocating 30% of the proposed wastewater revenue requirement to water customers is "arbitrary." Aqua Exc. at 33 (citing R.D. at 90). Aqua counters that, although the ALJ cited to *Lloyd*, which rejected the definition of gradualism as limiting a rate increase to 10% of the total bill as "the magic number that will prevent rate shock," the Company explained why its proposal is just and reasonable and does not aver that its proposed 30% allocation is the "magic number." Aqua Exc. at 33 (citing Aqua R.B. at 95-99; Aqua M.B. at 216-225). Further, Aqua notes that given the size and number of the systems acquired since the Company's last base rate case and to mitigate the impacts of the initial rate increase for these systems while still moving each towards the cost of service, it is appropriate for the initial allocation of revenues to be higher. Aqua Exc. at 33 (citing Aqua M.B. at 216; Aqua St. 1-R at 24). Moreover, Aqua notes that the other Parties' alternatives are disruptive to the Company's balanced approach and would subject the customers of the acquired systems to significant and immediate rate increases. Aqua Exc. at 33.

Finally, Aqua argues that I&E's proposed rate zone-specific rate design, and Act 11 revenue allocation proposal, are inappropriate. Aqua posits that the ALJ did not analyze the Company's detailed wastewater rate design proposal beyond determining that I&E's proposed rate design should be adopted as a part of the Act 11 revenue allocation. Aqua Exc. at 34 (citing R.D. at 91; Aqua M.B. at 237-38).

In its Replies, I&E argues that the ALJ considered all of the wastewater revenue allocations presented by the Parties and properly recommended the methodology presented by I&E for allocating revenue and designing the wastewater rates. Further, I&E notes the ALJ's finding that I&E's approach: (1) takes into consideration the number of water and wastewater customers in each system; (2) balances the goal of moving rates toward alignment with the cost of service; and (3) mitigates some of the resulting large rate increases if a wastewater revenue allocation is not approved.

Moreover, I&E avers the ALJ acknowledged that I&E's approach is: (1) more beneficial to the communities served by the systems acquired by the Company pursuant to Section 1329; and (2) less complicated and more logical than the methods advocated by the other Parties. I&E R. Exc. at 10 (citing R.D. at 91).

In its Replies, the OSBA disagrees with the Company's Exception to reverse the ALJ's recommendation that reduces the Company's proposed amount by approximately \$10 million. The OSBA avers that it does not oppose the magnitude of the Act 11 subsidy reduction recommended by the ALJ because it argued in this proceeding that the Company's request to recover \$20.839 million of the wastewater revenue requirement from water service customers was not supported by the record evidence. The OSBA further notes that, as a result of its proposal to assign additional increases to Aqua's Base and New Garden Divisions, the OSBA's overall proposed wastewater increase and its recommended Act 11 revenue requirement was less than the Company's proposal. Therefore, the OSBA concludes that it supports the ALJ's recommendation to reduce the Act 11 subsidy paid by the Company's water customers. OSBA R. Exc. at 2-3 (citing OSBA St. 1 at 15-17).

In its Replies, the OCA, likewise, submits that the ALJ properly rejected the Company's Act 11 subsidy and rate design, arguing that the subsidy is unreasonable and inconsistent with generally accepted ratemaking principles. The OCA notes that, with regard to the Act 11 subsidy amount, the recommendations of I&E and the OCA are based on the same reasoning that it is not reasonable or in the public interest for water customers, who receive no benefit from wastewater operations or Section 1329 acquisitions, to support a disproportionate share of the revenue requirement driven by those acquisitions. OCA R. Exc. at 16 (citing R.D. at 89-91; 96; OCA St. 4 at 4-5; I&E St. 5 at 66). Further, the OCA contends that establishing a subsidy close to one-third of the wastewater revenue requirement would mean that wastewater rates do not support a

reasonable relationship to the utility's cost of serving the customer. OCA R. Exc. at 16 (citing OCA M.B. at 89-91).

The OCA also disagrees with the Company's claims that the subsidy is necessary to mitigate significant rate impacts for the acquired wastewater customers and that the more moderate subsidy recommended by I&E produces wastewater rate increases that are not sufficiently gradual. OCA R. Exc. at 16 (citing Aqua Exc. at 31-33). The OCA posits that the Company neglects the role that FMV ratemaking rate base and the Company's high proposed return on common equity play in worsening the rate impact on the customers of the acquired systems. Therefore, the OCA asserts that it is reasonable to assign more of the revenue requirement generated by the acquired systems. Moreover, the OCA notes that under the ALJ's recommended reduction to the Act 11 subsidy, the acquired wastewater customers and legacy wastewater customers will not pay the full cost of service, and there would still be a \$10 million subsidy by water customers. OCA R. Exc. at 16-17 (citing OCA St. 4-SR at 2-3).

b. I&E Exception No. 2 and Replies

In its Exception No. 2, I&E submits that the ALJ erred in using I&E's wastewater increase by class recommendation table that was prepared to support the rebuttal testimony of I&E's witness, Mr. Kubas, instead of I&E's updated wastewater increase by class recommendation table that Mr. Kubas submitted in support of his surrebuttal testimony. I&E explains that Mr. Kubas prepared a table in support of his rebuttal testimony that summarized the proposed revenue allocations set forth in the Parties' direct testimony. However, I&E restates that in the surrebuttal phase of the case, Mr. Kubas revised I&E's proposed wastewater revenue increase by system to reflect revisions to Aqua's original claim, late payment revenues, and proposed revenues, as well as to address the positions of the other Parties. Accordingly, I&E argues that the Commission should rely on the wastewater increases by class which were updated in

Mr. Kubas' surrebuttal testimony. I&E Exc. at 4-5 (citing R.D at 88; I&E St. 5-SR at 4; I&E Exh. 5-SR, Sch. 1 at 1; I&E St. 5-R at 1-23; I&E Exh. 5-R, Sch 1).

In its Replies, Aqua submits that I&E's surrebuttal wastewater revenue allocation should be rejected for the same reasons it argued against adopting I&E's rebuttal proposal. Aqua R. Exc. at 9 (citing I&E Exc. at 4-5).

c. OCA Exception No. 11 and Replies

In its Exception No. 11, the OCA submits that, although it supports the reduction to the subsidy, the OCA's method for allocating the revenue requirement between water and wastewater customers is more reasonable and should be adopted. OCA Exc. at 16 (citing R.D. at 89-91). The OCA asserts that, by allocating a portion of the wastewater revenue requirement to water customers, the OCA's method moves the acquired and legacy system rates closer to their cost of service while mitigating rate increases to all wastewater customers. OCA Exc. at 18 (citing OCA St. 4SR at 1-2; OCA St. 4 at 4-9).

The OCA notes that although I&E's method focuses on the gap generated by each system's revenue requirement, the OCA's method also considers how much of the gap is generated by the FMV premium paid for each acquired system. The OCA argues that, in determining relative burdens, it is not reasonable for the subset of wastewater customers benefiting from the FMV premium to further benefit by having water customers pay the portion of the acquired system's revenue requirement generated by the FMV premium. OCA Exc. at 16-17 (citing OCA R.B. at 46-49; OCA M.B. at 88-89, 91-96; OCA St. 4 at 6-8; OCA St. 4-SR at 2-3).

The OCA also claims that contrary to the ALJ's concerns regarding the complexity of the OCA's recommendation, the additional steps for implementation of the

OCA's method are warranted and not unreasonably complicated. OCA Exc. at 17 (citing R.D. at 91). The OCA explains that the calculated amount of the revenue requirement associated with the FMV premiums is allocated to the five acquired systems such that no system exceeds its cost of service, and the remainder is allocated to the legacy systems. The OCA notes that the Company's proposed class increases for each division are prorated when applied. OCA Exc. at 17 (citing OCA St. 4 at 8-10; OCA Exh. Sch. GAW-4).

Further, the OCA argues that, when compared to the OCA's method, I&E's method recommends that the Cheltenham wastewater system be assigned a larger revenue requirement and, if I&E's method is adopted, then Cheltenham's resulting rates at the Company's revenue requirement would be higher than its cost of service. OCA Exc. at 17 (citing OCA St. 4-SR at 5-6; I&E St. 4-SR at 5, 14). Moreover, the OCA notes that, although it agrees that the wastewater subsidy should be reduced, the revenue allocations should also be guided by cost-causation. Accordingly, the OCA submits that, if the OCA's allocation method is not adopted and if the revenue allocated to the Cheltenham system would otherwise exceed its cost of service, then an adjustment should be made as part of the scale back. OCA Exc. at 17 (citing OCA R.B. at 54).

The OCA also explains that it does not except to the ALJ's recommendation regarding water allocation because, but for the Act 11 subsidy, the ALJ adopted the Company's and the OCA's recommendation. The OCA provides that it is the OCA's understanding that the ALJ accepts the OCA's recommended proportional scale back across the divisions and classes and, other than the Act 11 subsidy, this is consistent with the water revenue increase allocation adopted by the ALJ and supported for the same reasons. OCA Exc. at 18 (citing R.D. at 91-93; OCA R.B. at 55-58; OCA St. 4 at 12-13).

The OCA disagrees with the ALJ's recommendation that adopts I&E's and the Company's scale-back proposal which would not reduce wastewater rates until the Act 11 subsidy is eliminated. OCA Exc. at 18 (citing R.D. at 91; Aqua St. 5-R at 25; I&E St. 5 at 63-64). The OCA recommends a different scale-back approach that would allocate additional wastewater revenue to the acquired systems and legacy systems based on the Company's authorized ROE. Therefore, the OCA maintains that if the Commission adopts a different capital structure and/or a lower ROE than proposed by the Company, then the scale back should first be applied to reduce the revenue requirement associated with the FMV premiums, to the benefit of wastewater customers. Further, the OCA maintains that if the Commission reduces revenue requirement for non-ROR reasons, or the Commission does not adopt the OCA's method for allocating wastewater revenue requirement based on FMV premiums, then the OCA agrees that the benefit should be applied to reduce the subsidy by water operations. OCA Exc. at 18 (citing OCA M.B. at 96-97; OCA St. 4 at 11-12).

In its Replies, Aqua argues that the OCA's proposed allocation of Act 11 revenues was properly rejected because it is neither fair nor reasonable. Aqua counters that the arguments advanced by the OCA in support of its proposed Act 11 revenue allocation are without merit and should be rejected for the same reasons as its revenue allocation proposal. Aqua argues that the OCA's calculation of the revenue requirement associated with FMV premiums: (1) is improper; (2) seeks to mask a large increase to wastewater base customers; and (3) ignores that the Company's proposal already accounts for the premiums which the OCA seeks to undo. Aqua adds that the OCA's scale-back method should be rejected for the same reasons as its proposed revenue allocation. Aqua R. Exc. at 9-10 (citing OCA Exc. 17; Aqua R.B. at 95-98; Aqua M.B. at 220-21, 266).

In its Replies, I&E submits that, upon consideration of all of the proposals set forth by the Parties regarding this issue, it supports the ALJ's recommendation. I&E R. Exc. at 16.

d. OSBA Exception No. 1 and Replies

In its Exception No. 1, the OSBA argues that the ALJ erred in adopting the Company's proposed revenue allocation for its water service customers. OSBA Exc. at 2 (citing R.D. at 93). First, the OSBA disagrees with the ALJ's conclusion that Aqua's methodology better reflects the cost of service compared to those advocated by the other Parties because it is based on "a combined water and wastewater revenue, or 'total bill,' evaluation." OSBA Exc. at 2-3 (citing R.D. at 81, 92). The OSBA argues that the ALJ's conclusion violates the decision in *Lloyd* that ratemaking must be conducted using each specific service's cost of service. OSBA Exc. at 3. The OSBA notes that, when developing a revenue allocation based upon an accepted cost of service study, the ALJ and the Commission must follow the requirements set forth in *Lloyd* because if ratemaking is performed on a combined or total-bill basis, such as Aqua, proposes the true impact of the revenue increases required by the Company's separate water and wastewater cost of service study will be hidden. *Id.* (citing *Lloyd* at 1015, 1020-21).

The OSBA also argues that the Company's proposed water revenue allocation violates the principles of *Lloyd* because it moves each class "toward its appropriate percentage cost of service including the Act 11 allocation." OSBA Exc. at 4 (citing R.D. at 92-93). The OSBA asserts that the plain language of Section 1311(c) of the Code sets the legal standard that must be met in all combined water/wastewater rate cases under Act 11. The OSBA specifically notes that Section 1311(c) provides that "[t]he commission when setting base rates, after notice and an opportunity to be heard, may allocate a portion of the wastewater revenue requirement to the combined water and wastewater customer base if in the public interest." OSBA Exc. at 4 (citing 66 Pa. C.S.

§ 1311(c) (emphasis added by the OSBA)). However, the OSBA contends that Section 1311(c) does not provide the legal authority to violate the requirement of *Lloyd* that rates for individual utility services be based on separate cost of service determinations. OSBA Exc. at 4 (citing *Lloyd*). Accordingly, the OSBA contends that the ALJ's approval of Aqua's water revenue allocation on the basis that it moves each class "toward its appropriate percentage costs of service including the Act 11 allocation" must be rejected because the ALJ made her decision without any legal basis set forth in Act 11. OSBA Exc. at 4 (citing R.D. at 92-93).

The OSBA also argues that the Company's revenue allocation violates *City of Bethlehem* where the Commission agreed with the OSBA when it determined that "the proper yardstick for measuring the degree of movement toward cost of service is the change in the absolute level of class subsidies at present and proposed rates." The OSBA asserts that in this case, the ALJ ignored the Commission's standard in *City of Bethlehem* for measuring progress towards cost of service when designing a revenue allocation. OSBA Exc. at 4-5 (citing *City of Bethlehem* at 36). In fact, the OSBA contends that its subsidy analysis demonstrates that the Company's proposed revenue allocation for water service, at the Company's requested revenue requirement level, would result in the Commercial, Industrial, and Public Fire customer classes moving toward cost of service and the Residential, Public, Other Water Utilities and Private Fire customer classes moving away from cost of service. OSBA Exc. at 5-8 (citing OSBA St. 1 at 4, 6-9; OSBA Exh. BK-1 W, Schs. BK-1W, BK-3W). Thus, the OSBA maintains that the Company's proposed revenue allocation for water service, exclusive of Act 11 subsidies, is unjust and unreasonable because it violates *Lloyd* by failing to move all of the customer classes closer to their respective cost-based revenue levels. OSBA Exc. at 8.

Finally, the OSBA further disagrees with the ALJ's finding that Aqua's revenue allocation better reflects cost of service since it moves each customer classification toward its appropriate percentage of cost of service when the Act 11

allocation is included. OSBA Exc. at 8-9. The OSBA argues, however, that the preferred cost metric used by Aqua in support of its revenue allocation is conceptually invalid. In this regard, the OSBA cites the testimony and detailed analysis (see OSBA Exc. at 8-11) of its witness, Mr. Kalcic, in reiterating its position that the Company's proposed class revenue allocation for water service, including Aqua's alternative percentage of cost of service metric, and Aqua's claim that Act 11 revenues should be included in class revenue allocation evaluations, is without legal foundation. OSBA Exc. at 9-11 (citing OSBA St. 1-S at 4-8). Therefore, the OSBA avers that the Company's proposed class revenue allocation for water service must be rejected by the Commission. OSBA Exc. at 11.

In its Replies, Aqua counters that the Company's proposals are consistent with Act 11 and *Lloyd*. Further, Aqua notes that the OSBA essentially is repeating the same arguments it made in its Briefs against the Company's proposed water revenue allocation in favor of its own water revenue allocation. The Company cites to its arguments included in its Briefs against the OSBA's position. Aqua R. Exc. at 10 (citing OSBA Exc. at 11-17; Aqua R.B. at 98-100; Aqua M.B. at 224, 228-29). Additionally, Aqua avers that the OSBA's reliance upon *Lloyd* is misplaced in that the OSBA "treats the allocation of wastewater costs as though they were a separate rate charged to water customers." Aqua R. Exc. at 10.

e. OSBA Exception No. 2 and Replies

In its Exception No. 2, the OSBA submits that the ALJ erred in rejecting the OSBA's proposed water revenue allocation. The OSBA begins its Exception No. 2 by citing to the ALJ's conclusion that "it appears that OSBA's recommendation to isolate and remove the Act 11 allocation from its analysis is motivated by a desire to decrease the revenue allocated to non-residential customer classifications, while increasing the revenue allocated to residential customer classes." OSBA Exc. at 11 (citing R.D. at 92;

Aqua M.B. at 229). In response, the OSBA argues that the ALJ's conclusion with respect to its motivations is baseless. The OSBA submits that its proposed water revenue allocation should be adopted by the Commission because it correctly isolates Act 11 revenues in its proposed revenue allocation. The OSBA explains that its approach of isolating the Company's claimed water cost of service from Act 11 subsidies: (1) is the only revenue allocation sponsored by any Party that follows both the requirements of *Lloyd* and the Commission's decision in *City of Bethlehem*; and (2) is necessary to develop a cost-based water revenue allocation, given that the Company's claimed wastewater cost of service and associated Act 11 subsidies are separate from, and unrelated to, its claimed water revenue requirement. Furthermore, the OSBA maintains that, given that Aqua's proposed revenue allocation moves the Residential class in the wrong direction (*i.e.*, away from the cost of service), the OSBA's revenue allocation assigns greater revenue responsibility to the Residential class because any revenue allocation which corrects the Company's failure to move all classes toward cost of service will assign a greater revenue responsibility to the Residential class. OSBA Exc. at 11-12 (citing OSBA M.B. at 9-14).

The OSBA repeats its argument that the Commission should adopt its alternative water revenue allocation proposal sponsored by its witness, Mr. Kalcic, in this proceeding because it: (1) implements the Company's requested revenue increase; (2) is exclusive of any allocation of Act 11 subsidies; and (3) would move all classes toward their respective cost-based revenue levels without imposing an excessive increase on any class of water customers. OSBA Exc. at 12-15, 17 (citing OSBA St. 1 at 9-11; OSBA Exh. BK-1 W, Schs. BK-4W, BK-5W). Moreover, the OSBA notes that, although it agrees with the Company's method of allocating its Act 11 revenue requirement to its water service classes, the OSBA does not agree with the overall magnitude of the Company's proposed Act 11 revenue requirement. OSBA Exc. at 15-16 (citing OSBA St. 1 at 11, 15, 17; OSBA Exh. BK-1 W, Schs. BK-1W, BK-6W).

In its replies, Aqua counters that the Company's proposals are consistent with Act 11 and *Lloyd*. Further, Aqua notes that the OSBA essentially is repeating the same arguments it made in its Briefs against the Company's proposed water revenue allocation in favor of its own water revenue allocation. The Company cites to its arguments included in its Briefs against the OSBA's position. Aqua R. Exc. at 10 (citing OSBA Exc. at 11-17; Aqua R.B. at 98-100; Aqua M.B. at 224, 228-29).

In its replies, the OCA disagrees with the OSBA's arguments in its Exception No. 2 and opines that the ALJ properly found that the OSBA's recommended total class water increases are unreasonable. The OCA agrees with the ALJ that, from the perspective of the customers, both the water increase and the wastewater allocation are included in the effect of the increases. Further, the OCA states that with the Act 11 subsidy excluded, the results of the OSBA's class revenue allocations are not reasonable. OCA R. Exc. at 18-19 (citing R.D. at 92; OSBA Exc. at 11-17). Moreover, the OCA asserts that, although the Residential, Industrial and Commercial classes are currently earning close to parity, the OSBA's proposal would result in skewed, unreasonable, and inequitable increases because the Residential and Industrial classes would experience a higher percentage of revenue responsibility than that of the Commercial class. OCA R. Exc. at 19 (citing OCA R.B. at 55-58; Aqua M.B. at 228-29; OCA St. 4R at 7, 9-10).

f. OSBA Exception No. 3 and Replies

In its Exception No. 3, the OSBA disagrees with the ALJ's adoption of I&E's recommended wastewater rate design and rate increases because it does not include an analysis of how the Company's Act 11 wastewater subsidies should be allocated to Aqua's customers. OSBA Exc. at 17 (citing R.D. at 91). Thus, the OSBA supports the Company's proposed method of allocating the Act 11 subsidy because, as discussed in more detail below, it is consistent with the OSBA's position that the recovery of Act 11 wastewater subsidies from water customers on a revenue neutral basis

by customer class is the only just and reasonable resolution of this issue that is consistent with the requirements of *Lloyd*. OSBA Exc. at 17, 20.

In support of this Exception, the OSBA references its witness, Mr. Kalcic's, review and analysis of the Company's proposed method of allocating its Act 11 revenue requirement to water customers to argue that the Company's proposed wastewater increase would not recover all of the Company's claimed wastewater revenue requirement. OSBA Exc. at 18-19 (citing OSBA St. 1 at 13-14, OSBA Exh. BK-1 WW, Sch. BK-1WW). Further, the OSBA contends that, although Act 11 provides the statutory authority to temporarily recover the costs associated with Aqua's wastewater system from its water customers, Act 11 does not allow for any "cross-subsidization" of customer classes between water and wastewater customers. OSBA Exc. at 19. Moreover, the OSBA argues that Act 11 does not supersede the requirements of *Lloyd*, meaning that the Company's water rates, exclusive of Act 11, must be based primarily on the results of Aqua's water cost of service study. Accordingly, the OSBA requests that the Commission adopt the Company's proposal to recover Act 11 wastewater subsidies from water customers on a revenue neutral basis by customer class because it is just, reasonable, and consistent with the requirements of *Lloyd* and the language of Act 11. OSBA Exc. at 19-20 (citing OSBA St. 1 at 17-18).

In its Replies, the OCA argues that the OSBA's recommended total class water increases are unreasonable and should not be adopted by the Commission. With regard to the OSBA's argument that the ALJ erred in not accepting the OSBA's proposal with regard to the Act 11 allocation subsidy between Residential and non-Residential classes, the OCA retorts that, because the Company has much fewer wastewater customers (63,869) to non-fire water customers (415,059), most water customers do not rely upon the Company's wastewater operations and there is no reasonable basis for a particular class of water customers to have to subsidize the same class of wastewater customers. OCA R. Exc. at 19-20 (citing OSBA Exc. at 17-20; OCA St. 4-R at 10-11).

Further, the OCA counters that the OSBA's proposal results in the Residential class being assigned a larger relative percentage of Act 11 subsidy revenues than the system average, while the Commercial class is assigned significantly less than the system average and the Industrial class is not assigned Act 11 subsidy responsibility. The OCA elaborates that, because the Residential, Commercial, and Industrial class indexed RORs are all reasonably close to unity, when the OSBA's initial class revenue allocations (prior to the Act 11 revenue shift) are combined with the Act 11 revenue increases, the OSBA's recommendation unreasonably favors the Commercial class. OCA R. Exc. at 20 (citing OCA St. 4R at 9-10).

g. OSBA Exception No. 4 and Replies

In its Exception No. 4, the OSBA submits that Aqua's proposal to scale back the Company's proposed revenue allocation must be rejected. The OSBA contends that, although the ALJ acknowledged that the exclusion of wastewater rates from any scale back in this proceeding will reduce Aqua's Act 11 revenue requirement, the ALJ did not discuss how the Company's allocation of its proposed Act 11 revenue requirement of approximately \$20.8 million for water classes should be scaled back to the ALJ's recommended level of approximately \$10.2 million. OSBA Exc. at 20-21 (citing R.D. at 91, Table Act 11; Aqua M.B. at 265; OSBA Exh. BK-1 W, Sch. BK-6W). In order to ensure that the Company's Commission-approved revenue requirement is recovered from water customers on a revenue neutral basis, the OSBA recommends that the Commission: (1) scale back the wastewater class revenue requirements proportionately to reflect the Company's total approved wastewater revenue requirement level; and (2) subtract the Company's approved level of wastewater revenues, by class, from the adjusted wastewater class revenue requirement levels. OSBA Exc. at 25 (citing OSBA St. 1 at 18-19). The OSBA submits that its recommended water service and Act 11 scale-back proposals are consistent with *Lloyd* and Act 11 and would ensure that

the Aqua's approved Act 11 revenue requirement would be recovered from water customers on a revenue neutral basis, by customer class. OSBA Exc. at 25.

The OSBA repeats its argument that the Company's proposed scale back of its proposed revenue allocation must be rejected because: (1) the Company's proposed revenue allocation is not cost based and, therefore, using it as a starting point for any scale back is not valid; and (2) a separate scale back is necessary for reductions in the Company's allowed water service revenue requirement and changes in the Company's Act 11 revenue requirement. OSBA Exc. at 21-22 (citing OSBA St. 1-R at 8-11). The OSBA maintains that if the Commission awards the Company a water service revenue increase that is less than Aqua's requested amount and exclusive of Act 11 considerations, then the OSBA's recommended class increases for water service should be proportionately scaled back. OSBA Exc. at 22-23 (citing OSBA M.B. at 19-20; OSBA Exh. BK-1 W, Sch. BK-4W). Thus, the OSBA maintains its position that whatever the Act 11 revenues that the Commission decides to assign to water classes should be subject to a separate scale back, as determined by the level of Aqua's awarded wastewater revenue requirement and the overall level of final wastewater rates. OSBA Exc. at 23-24 (citing OSBA St. 1 at 12, 19; OSBA Exh. 5-B, part 1; OSBA Sch. BK-6WW).

In reply to the OSBA's position that the Commission reject the Company's proposed scale back for water rates for the same reasons that it opposed the Company's water revenue allocation, Aqua contends that the Company has demonstrated that its proposed scale back was reasonable, and therefore, the OSBA's exception regarding this matter should be rejected. Aqua R. Exc. at 10 (citing OSBA Exc. at 20; Aqua R.B. at 107-108; Aqua M.B. at 265-66).

In its Replies, I&E submits that it agrees with the ALJ's recommendation to adopt the I&E methodology for allocating revenue and designing wastewater rates,

including I&E's recommended Act 11 subsidy. I&E also agrees that no scale back of Aqua's proposed wastewater rates should be permitted until the entire wastewater Act 11 subsidy allocation is eliminated. I&E R. Exc. at 22 (citing OSBA Exc. at 20-21; R.D. at 88, 91).

h. Aqua LUG Exception No. 1 and Replies

In its Exception No. 1, Aqua LUG disagrees with the ALJ's reliance on the testimony provided by Aqua and the OCA that alleged that Aqua LUG's proposed revenue allocation would result in an unacceptable RROR. According to Aqua LUG, the ALJ never addressed the unfavorable RROR effects that her recommended revenue allocation would have on Commercial customers and the very limited progress that would be made towards cost of service rates for the other classes. Aqua LUG Exc. at 2 (citing R.D. at 93). In this regard, Aqua LUG requests that the Commission adopt its revenue allocation proposal that it developed consistent with *Lloyd*, to determine the reasonableness of the movement towards cost of service. Aqua LUG Exc. at 2-3 (citing *Lloyd*; *Pa. PUC v. Philadelphia Gas Works*, Docket No. R-2008-2073938 (Order entered March 26, 2009)).

More specifically, Aqua LUG asserts that the Company's proposed movement of the Commercial rate class closer to the Company's cost to serve, from a current RROR of 1.07 to 1.05 RROR, would not achieve sufficient movement for the Residential customer class because the resulting RROR under current residential rates would be 0.96 and would not move towards the system average increase in the Company's proposed revenue allocation. Aqua LUG Exc. at 2-3 (citing Aqua M.B. at 9; Aqua LUG St. 1 at 4). Aqua LUG maintains that its recommendation would require the Company to modify its revenue allocation so that: (1) the Residential class RROR would move from 0.96 to 0.98; (2) the Commercial class RROR would move from 1.04 to 1.02; (3) the Industrial class RROR would move from 0.93 to 0.99; and (4) the Public class

RROR would move from 1.18 to 1.15.⁷⁴ Aqua LUG Exc. at 3-4 (citing Aqua LUG M.B. at 9-10). Aqua LUG further contends that the basis for its recommendation is the unreasonableness of setting rates that preserve substantial interclass subsidies for the Commercial class (*i.e.*, the Commercial class RROR decreasing from present to proposed rates by 0.02) while not progressing towards cost of service for the Residential class (*i.e.*, the Residential RROR at present and proposed rates remaining at 0.96). Aqua LUG Exc. at 4-5. Moreover, Aqua LUG argues that, given that the Residential class has a RROR of 0.96 under present rates, it is not clear how a reasonable movement towards cost of service justifies a rejection of Aqua LUG's proposed revenue allocation. Aqua LUG adds that, by not immediately moving the Residential customer class to cost of service, Aqua LUG's recommended movement for the Residential class incorporates principles of gradualism. Aqua LUG Exc. at 5 (citing Aqua LUG M.B. at 9-10).

Accordingly, Aqua LUG requests that the Commission reject the ALJ's recommendation and direct the Company to implement the revenue allocation modifications submitted by Aqua LUG because its proposed allocations would move all customer classes closer to their cost to serve. In the alternative, Aqua LUG requests that the Commission adopt the OSBA's recommendation. Aqua LUG Exc. at 2, 6.

Next, Aqua LUG excepts to the ALJ's decision to adopt Aqua's class allocation methodology based on her determination that the Company's proposal does not attempt to exclude the Act 11 allocation from its analysis. More specifically, Aqua LUG takes issue with the discussion in the Recommended Decision where the ALJ accepted the OCA's observation that Aqua LUG's recommendation does not incorporate the subsidization of wastewater operations by water operations. Aqua LUG Exc. at 5 (citing

⁷⁴ Aqua LUG notes that it remains unopposed to the OSBA's proposed alternative revenue allocation that is also intended to adjust the Company's proposed revenue allocation by advancing various customer classes towards their cost of service. Aqua LUG Exc. at 4 (citing Aqua LUG St. 1-S at 2).

R.D. at 92). Aqua LUG submits that the ALJ's discussion lacks the appropriate context, explaining that the ALJ adopted I&E's scale-back recommendation to eliminate the subsidy to wastewater customers prior to proportionately scaling back the additional rates. Aqua LUG Exc. at 5-6 (citing R.D. at 91). Aqua LUG contends that, to the extent I&E's recommendation is adopted by the Commission, any further accounting consideration of the Act 11 subsidy would be a double count. Aqua LUG Exc. at 6. Therefore, Aqua LUG submits that, if the Commission accepts I&E's scale-back proposal to eliminate the subsidy to water customers first, then the Commission should scale back the additional water rates, consistent with Aqua LUG's proposed revenue allocation. *Id.* at 6.

Finally, Aqua LUG argues that without the I&E scale-back recommendation, the legislative authority to allocate a portion of the wastewater cost of service to water customers should not supersede the Commission's evaluation of the water revenue allocation. Aqua LUG notes the OSBA's observation that Act 11 revenue requirements are assigned on a revenue-neutral basis and do not reflect class cost of service. Aqua LUG Exc. at 6 (citing OSBA St. 1-S at 6-7). Therefore, Aqua LUG contends that pursuant to *Lloyd*, the appropriate Act 11 subsidy should be determined after establishing the appropriate water system revenue allocation on a cost of service basis. Aqua LUG Exc. at 6.

In its Replies, Aqua argues that Aqua LUG's exception should be denied because the ALJ correctly rejected Aqua LUG's proposal to move a portion of the industrial class increase to the Residential class, due to a larger increase to blocks 5 and 6 of the consumption rates for the industrial class. Aqua R. Exc. at 10-11 (citing Aqua LUG Exc. at 2-6; Aqua M.B. at 229-30).

In its Replies, the OCA argues that the Commission should reject Aqua LUG's adjustments because Aqua LUG's proposals would move classes by small

percentage increments and do not reflect the lack of accuracy of the underlying cost allocations, among other complexities in this case. Therefore, the OCA contends that the ALJ properly concluded that the Company's proposed allocation of class revenues is more appropriate. OCA R. Exc. at 19 (citing Aqua LUG Exc. at 2-6; R.D. at 93; OCA St. 4-R at 12).

i. Masthope Exception No. 2 and Replies

In its Exception No. 2, Masthope argues that the ALJ's adoption of the Act 11 subsidy adjustments results in unjust and unreasonable rates that disproportionately and negatively affect Masthope wastewater customers, particularly commercial customers. Masthope Exc. at 10-11 (citing R.D. at 84-91). Masthope explains that it expressed its concern throughout this proceeding about allocating water revenues to the Company's wastewater revenue requirement which may result in large rate increases to wastewater rates for Masthope customers and, therefore, urged the ALJ to adopt Aqua's original distribution of the proposed rate increases between and within water and wastewater rate schedules. Masthope Exc. at 10 (citing Masthope M.B. at 19-24). Notwithstanding its concerns, Masthope avers that the ALJ ultimately adopted I&E's proposed Act 11 revenue allocation methodology that would result in large increases in Masthope's wastewater usage rates (147% increase) and monthly service charge (35% increase). Masthope Exc. at 10 (citing R.D. at 84-91; Masthope R.B. at 6-7; Masthope M.B. at 19-24). Thus, Masthope requests that the Commission reverse the ALJ's recommendation to the extent it results in dramatic rate increases for Masthope water customers. Masthope Exc. at 10-11.

Masthope also argues that although Act 11 provides the Commission has broad discretion to allocate wastewater revenue requirements across a utility's combined customer base, the Commission should: (1) assure just and reasonable rates for all classes of customers, pursuant to Section 1301 of the Code, 66 Pa. C.S. § 1301; (2) avoid

rate shock; and (3) embrace the principles of gradualism. Masthope Exc. at 11 (citing 66 Pa. C.S. § 1311(c); *Implementation of Act 11 of 2012*, Docket No. M-2012-2293611 (Order entered August 2, 2012)). Further, Masthope maintains that the impact on its community would be especially detrimental to the unique mix of part-time/seasonal residents and residential and commercial customers. Moreover, Masthope asserts that, if the Commission approves revenues in amounts less than the Company originally proposed, then the Commission should distribute any increased revenue requirement for water and wastewater customers and the amount of revenue support to be provided by water customers in a manner consistent with the Company's proposal. Furthermore, Masthope avers that the Commission should distribute any increase in rates, both between and within rate schedules, in a manner consistent with the Company's original proposal. Masthope explains that Aqua selectively proposed increases between and within rate schedules to encourage its long-term plan of rate schedule consolidation into a uniform tariff. Masthope details that by contrast, the adjustments adopted by the ALJ are excessive for certain customers in specific schedules, including commercial customers in wastewater Zone 6 who would experience as much as a 147% rate increase. Masthope Exc. at 11-12 (citing Masthope M.B. at 19-23).

In its Replies, Aqua notes that it does not oppose Masthope's Exception, explaining that Masthope supports Aqua's proposed Act 11 revenue allocation and Masthope's Exceptions lend further support to Aqua's proposed allocation of revenues. Aqua R. Exc. at 11 (citing Masthope Exc. at 10-11; Aqua R.B. at 99).

In its Replies, I&E argues that although it understands Masthope's argument, any Act 11 subsidy imposed on Aqua's water customers is for the benefit of Aqua's wastewater customers, including Masthope. I&E explains that absent the Act 11 subsidy from wastewater to water customers, the Masthope wastewater rates would have to be further increased. Further, I&E notes that in similar Commission cases, the ALJ and the Commission must balance the justness and reasonableness of all revenue

allocation and rate design components, within the complexities of a cost of service methodology, among all customer classes. Moreover, I&E asserts that as a result of making the required choices, ultimately all customer classes will be adversely affected. Therefore, I&E submits that it supports the ALJ's recommendation that the Commission adopt I&E's methodology for allocating revenue and designing wastewater rates, including I&E's recommended Act 11 subsidy. I&E R. Exc. at 24-25 (citing Masthope Exc. at 10-11; R.D. at 82-91).

In its Replies, the OCA refers to its argument that Aqua's Exception No. 9 regarding the Act 11 subsidy should be rejected, to contend that Masthope's objection to decreasing the subsidy for Masthope (one of the legacy systems) should be rejected for the same reasons. OCA R. Exc. at 17 (citing Masthope Exc. at 10-12; R.D. at 88; OCA R.B. at 51-53).

4. Disposition

At the outset, we will address I&E's Exception No. 2. Based on our review, we agree with I&E that the Commission should rely on the wastewater increases by class which were updated in Mr. Kubas' surrebuttal testimony. *See* I&E Exh. 5-SR, Sch 1 at 1. Therefore, we shall grant I&E's Exception No. 2 and strike the table presented in the Recommended Decision at the top of page 88 and replace it with the table set forth in I&E Exhibit 5-SR, Schedule 1, Page 1 of 3, as reproduced below:

Aqua Pennsylvania, Inc.
R-2021-3027386 Schedule "WW-A" PSW Cost of Service Study
Zones 1 through 6 and Zones 7 through 11 and Grand Total for Aqua Wastewater

Zone	Cost of Service	Percent	Act 11 *	Percent	Adjusted Cost of Service	Revenue Present Rates	Revenue Proposed Rates	I&E Increase	Percent Increase	I&E Adjustment	Company Increase **	I&E Subsidy
(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)	(J)	(K)	(L)*	(M)
Zones 1-6												
1 Residential	\$27,146,216	79.3%	(\$11,078,966)	82.4%	\$16,069,250	\$12,419,396	\$17,942,695	\$4,523,299	33.7%	\$1,887,342	\$2,635,957	-\$9,189,624
2 Non Residential	\$7,066,927	20.7%	(\$2,361,992)	17.6%	\$4,704,935	\$3,976,095	\$5,365,264	\$1,389,169	34.9%	\$656,907	\$732,262	-\$1,703,085
3 Third Party	\$1,388,690		\$0		\$1,388,690	\$1,280,031	\$1,437,920	\$157,889	12.3%	\$381	\$157,508	\$381
4 Total Sales	\$35,601,833	100.0%	(\$13,438,958)	100.0%	\$22,162,875	\$18,675,522	\$24,745,879	\$6,070,357	32.5%	\$2,544,630	\$3,525,727	-\$10,894,328
5 Contract	\$312,754		\$0		\$312,754	\$312,754	\$331,801	\$19,047	6.1%	\$0	\$19,046	\$0
6 Late Payment	\$23,436		\$0		\$23,436	\$23,436	\$31,054	\$7,618	32.5%	\$7,618	\$0	\$7,618
7 TOTALS - Zone 1-6	\$35,938,023		(\$13,438,958)		\$22,499,065	\$19,011,712	\$25,108,734	\$6,097,022	32.1%	\$2,552,248	\$3,544,773	-\$10,886,710
Zone 7												
8 Zone 7	\$9,925,668		(\$2,974,708)	-30.0%	\$6,950,960	\$3,969,765	\$6,945,307	\$2,975,542	75.0%	\$6,665	\$2,968,827	-\$2,968,043
9 Late Payment						\$8,808	\$15,410	\$6,602	75.0%	\$6,602	\$0	\$6,602
Zone 8												
10 Zone 8	\$1,831,445		(\$457,466)	-25.0%	\$1,373,979	\$998,190	\$1,599,095	\$600,905	60.2%	\$242,526	\$158,579	-\$214,940
11 Late Payment						\$16,378	\$26,237	\$9,859	60.2%	\$9,859	\$0	\$9,859
Zone 9												
12 Zone 9	\$10,316,073		(\$514,835)	-5.0%	\$9,801,238	\$7,238,362	\$11,311,729	\$4,073,366	56.3%	\$1,532,060	\$2,541,306	\$1,017,225
13 Late Payment						\$20,377	\$31,844	\$11,467	56.3%	\$11,467	\$0	\$11,467
Zone 10												
14 Zone 10	\$3,850,938		(\$1,746,595)	-30.0%	\$4,084,341	\$2,916,336	\$4,440,845	\$1,524,509	52.3%	\$366,658	\$1,157,651	-\$1,379,937
15 Late Payment						\$7,435	\$11,322	\$3,887	52.3%	\$3,887	\$0	\$3,887
Zone 11												
16 Zone 11	\$5,622,603		(\$1,686,363)	-30.0%	\$3,936,240	\$2,871,704	\$4,246,926	\$1,375,222	47.9%	\$304,027	\$1,071,195	-\$1,382,336
17 Late Payment						\$17,382	\$25,706	\$8,324	47.9%	\$8,324	\$0	\$8,324
18 TOTALS - Zone 7-11	\$33,526,725		(\$7,379,967)		\$26,146,758	\$18,064,737	\$28,654,423	\$10,589,684	58.6%	\$2,492,076	\$8,097,608	-\$4,887,891
19 WW TOTALS	\$69,464,748		(\$20,818,925)		\$48,645,823	\$37,076,449	\$53,763,157	\$16,686,705	45.0%	\$5,044,324	\$11,642,381	-\$15,774,601
20 I&E Proposed Change in Subsidy			(\$5,044,324)			\$70,380	\$110,519	\$40,139	57.0%	Late Payment Revenue Zones 7-11		

* Column D Adjusted to Match Aqua Exhibit I-A(a) Schedule Act 11

** Column L Adjusted to Match Aqua Exhibit 5B-B

As will be discussed, at length, below, after our review of the Exceptions and Replies, we agree with the ALJ that Aqua's allocations of revenue between all water customer classifications and all wastewater customer classifications are reasonable and should be approved. We also agree that I&E's methodology for allocating the Act 11 wastewater revenue subsidy should be approved. Table Act 11, which is included in the Commission Tables Calculating Allowed Revenue Increase attached to this Opinion and Order, sets forth the water and wastewater revenue requirement summary for Aqua, based on I&E's allocation methodology.

Additionally, we support the ALJ's recommended adjustment to reduce the gross wastewater revenue requirement to a net basis when shifting the wastewater revenue requirement to water customers.⁷⁵ Finally, we agree with the ALJ that any scale back of water rates will first reduce the Act 11 allocation.

To recap, the allocation of revenue among a utility's rate classes involves, *inter alia*, consideration of ratemaking policy and the principles of gradualism. Here, Aqua proposed revenues to be allocated to each customer classification that would be required to move that classification toward the cost of providing service (or revenue requirement). R.D. at 84-85 (citing Aqua St. 5 at 10, 21; Aqua Exh. 5-A, Part I, Sch. A; Aqua Exh. 5-B, Part I, Sch. WW-A). Additionally, Aqua proposed to recover a shortfall of approximately 30% of the Company's proposed revenue requirement from wastewater revenues in water rates. R.D. at 85; Aqua M.B. at 216. I&E, the OCA, the OSBA, and Aqua LUG all opposed Aqua's Act 11 subsidy proposal and proposed alternative Act 11 subsidy reduction methodologies. R.D. at 87-89; Aqua LUG M.B. at 7, 9-10. The ALJ recommended I&E's methodology and agreed with I&E and the Company that any scale back of water rates should reduce the Act 11 allocation first. The ALJ reasoned that

⁷⁵ We note that, as outlined in Table Act 11, this will result in the Company's overall allowed revenue requirement being reduced by approximately \$77,706 after the Act 11 Allocation.

I&E's approach, *inter alia*: (1) considers the number of water and wastewater customers in each system; (2) balances the goal of aligning rates with the cost of service while mitigating some of the large rate increases that would result absent an allocation of wastewater revenue; and (3) acknowledges the benefits received by the communities serviced by the acquired systems. R.D. at 91.

In its Exceptions, Aqua argues that it demonstrated that justifications and arguments advanced by I&E and discussed by the ALJ were unreasonable and unsupported by record evidence, and that the ALJ misrepresented and/or ignored the testimony and exhibits presented by the Company in support of its proposed wastewater rate design. Similarly, in its Exceptions, the OSBA argues that the ALJ adopted the I&E's recommended wastewater rate design and rate increases without providing details regarding the allocation of Act 11 wastewater subsidies to water customers. We disagree with the arguments expressed by Aqua and the OSBA on these matters. In our view, the ALJ appropriately reasoned that the Company did not present sufficient evidence to demonstrate that allocating 30% of the proposed wastewater requirement to water customers is reasonable and in the public interest. Further, the ALJ appropriately found that shifting 30% of the wastewater revenue requirement to water customers is not equitable and will not result in just and reasonable rates. Indeed, we agree with the OCA's position in its Replies to Exceptions that it is not reasonable or in the public interest for those water customers who do not receive a benefit from wastewater operations or Section 1329 acquisitions to support a disproportionate share of the revenue requirement driven by such acquisitions. With regard to Aqua's and the OSBA's arguments that the ALJ did not provide sufficient analysis in her discussion, we disagree. The ALJ was aware of the positions and arguments put forth by the Company and the OSBA, including the testimonies and exhibits submitted in support of their positions. However, the ALJ has the discretion to determine whether, and to what extent, further discussion and analysis is warranted. Here, it appears that the ALJ did not believe that further consideration of these matters was necessary to recommend that I&E's proposed

wastewater allocation methodology be approved. Accordingly, we will deny Aqua Exception No. 9 and OSBA Exception No. 3.

The OCA also filed Exceptions arguing that its method for allocating a portion of the wastewater revenue requirement to water customers is more reasonable because it considers the FMV premium paid for each acquired system. We agree that a portion of wastewater customers benefitted from the revenue generated by the 1329 acquisition; however, we also agree with the ALJ's reasoning that I&E's approach for allocating the wastewater revenue requirement and designing wastewater rates is less complex than the method offered by the OCA. Indeed, I&E's approach is more streamlined than the methods advanced by the other Parties, while also addressing the benefits received by the communities serviced by the acquired systems and moving rates toward their respective cost of service. Similarly, with regard to the scale-back approach, both the OCA and the OSBA contest the ALJ's adoption of the scale-back approach; however, we are of the opinion that the scale back agreed upon by Aqua and I&E offers a less complicated method than other alternatives. Therefore, we agree with the ALJ's conclusion that any scale back of water rates will first reduce the Act 11 allocation. Accordingly, we will deny the OCA's Exception No. 11 and the OSBA's Exception No. 4.

The OSBA also filed Exceptions challenging the ALJ's reasoning and submitting that the OSBA's proposed water revenue allocation should be adopted. The OSBA is of the opinion that the ALJ violated *Lloyd*, misapplied Section 1311, and ignored Commission precedent by reasoning that Aqua's methodology better reflects cost of service and concluding that the Company's allocation of revenues is reasonable. We disagree with the OSBA. We are of the opinion that reasons considered by the ALJ upon which she based her recommendation to approve the Company's allocations of revenues between all water and wastewater customer classifications are just, reasonable, and in the public interest, and should be approved. The OSBA's contention is that Aqua's proposed

revenue allocation, which views cost of service as a whole and does not exclude the Act 11 allocation, conflicts with the requirement in *Lloyd* that the basis for individual utility service rates is specific to each service's cost of service. We find this argument unpersuasive. As noted by Aqua in its Replies, the OSBA's reliance upon *Lloyd* appears to be misplaced as wastewater costs are not stand-alone, separate rates charged to water customers. Therefore, we do not believe that the principles of *Lloyd* have been violated. The OSBA also argues that its proposed water revenue allocation correctly isolates the Act 11 allocation. We disagree. Rather, we find the ALJ's conclusion, that the Company's methodology better reflects the cost of service because Aqua's proposed allocation views cost of service "as a whole" and moves each customer classification toward its appropriate cost of service, is more persuasive and in the best interest of the public. R.D. at 92. Accordingly, we shall deny the OSBA's Exception Nos. 1 and 2.

In its Exceptions, Aqua LUG argues that the ALJ erred in adopting the Company's revenue allocations rather than the revenue allocations proffered by the OSBA and itself. Aqua LUG opines that the ALJ's recommendation is baseless and will delay progress of the movement of all customer classes towards their cost of service and result in an unfavorable RROR for Commercial customers. As discussed above, we agree with the ALJ's reasoning and basis for recommending that the Company's allocation of revenues between all water and wastewater customer classifications be approved. Accordingly, we will deny Aqua LUG's Exception No. 1.

Finally, in its Exceptions, Masthope disagrees with the ALJ's adoption of the Act 11 subsidy adjustments because they will disproportionately affect Masthope's wastewater customers. As discussed by the ALJ, it is not fair to the Company's water customers to mitigate increases in expenses to repair acquired systems and to take on the shortfall between the cost of service to serve the wastewater systems. I&E's approach for allocating wastewater revenue and designing wastewater rates allows for each service to recover as much of the cost of providing that service as possible without removing the

subsidy, which would result in large increases for every customer. R.D. at 88, 90. Indeed, we agree with I&E's position in its Replies to Exceptions that Masthope's rates would have further increased without the Act 11 subsidy from wastewater to water customers and, as a result of balancing the justness and reasonableness of all revenue allocation and rate design components with the inherent complexities of a cost of service methodology, all customers will ultimately be affected. Therefore, although we understand Masthope's point of contention, we will deny Masthope's Exception No. 2.

D. Tariff Structure and Rate Design

A utility's rate structure implements the Commission's approved revenue increase to determine how the overall increase will be allocated among the utility's various customer classes. Once a class revenue allocation is determined, development of a rate design will address how the tariffed rates and rate elements will generate the allocated revenues. I&E noted the following unique rate structure and rate design challenges present in this proceeding: (1) water base rates; (2) an Act 11 subsidy applied to water base rates to subsidize wastewater customers; (3) wastewater base rates; (4) new rate zones for numerous Section 1329 acquisitions; and (5) third-party sales rates. I&E R.B. at 49. Under the Company's proposal, a residential water customer in the Main Division of Rate Zone 1, using 4,000 gallons of water per month,⁷⁶ would experience a monthly bill increase from \$69.35 to \$81.32, or 17.3% per month, and residential customers in other water divisions would experience increases ranging from 17.3% to 51.3%. *See* Aqua Exh. 5-A, Part II, Sch. 8.⁷⁷ Wastewater customers would see increases

⁷⁶ The Company claimed that the average usage of 4,000 gallons per month is substantiated in the Company's prior rate case as the pre-COVID pandemic average residential usage was 4,068 per month for the residential class. Aqua St. 5-R at 14.

⁷⁷ Present Rates include 7.5% DSIC.

ranging from 7.9% to 84.87%, with one division seeing a proposed decrease (Rate Zone 5 – Newlin Green). *See Aqua Exh. 5-B, Part II, Sch. WW-7.*⁷⁸

1. Positions of the Parties

a. Water Rate Design

(1) Aqua's Water Rate Design Proposal

As shown in Table 8, below, the majority of Aqua's water rate divisions are grouped into three rate zones (Rate Zones 1-3) based on the similarity of their rate structure and rate design, while the Bunker Hill, Sun Valley, Phoenixville, and Belle Aire Acres Divisions are displayed separately because they are dissimilar from those divisions grouped into Rate Zones 1-3.

The majority of Aqua's water customers are charged the rates applicable to its Main Division, designated as Rate Zone 1. The Company proposed to continue to move rate divisions closer to each other and to the Rate Zone 1 in order to facilitate further consolidation with the Main Division. Aqua St. 1 at 29. Specifically, Aqua's proposal indicated that it is working to consolidate water rates for Rate Zones 1 and 2 (with the exception of Chalfont, Concord Park and Treasure Lake in Rate Zone 2). Aqua's witness, Ms. Heppenstall, explained that the Company developed the following five guidelines for the design of water rates: (1) maintain separate rate divisions for those areas with year-round usage and those areas with seasonal usage; (2) maintain a low-use block for the residential class at 2,000 gallons per month in each division, and a sixth block for the industrial classification for usage over 10 million gallons per month; (3) continue movement of those areas with year-round usage toward the Main Division

⁷⁸ Present Rates include 5.0% DSIC.

rates; (4) increase existing Main Division private fire service line rates 17.5% and private hydrant charges by 20.6%; and (5) increase the existing Public Fire Hydrant rate up to the 25% of cost of service level. *See Aqua St. 5 at 11.*

Water Operations - Rate Zones / Divisions

<u>Rate Zone 1</u> Main Division Country Club Gardens and Sand Springs Division Beech Mountain Division Bristol Township Division Mifflin Township Division Mount Jewett Division Robin Hood Lakes Division
<u>Rate Zone 2</u> Superior Division Chalfont Division Concord Park Division Treasure Lake Division
<u>Rate Zone 3</u> Oakland Beach Division CS Water (Masthope) Division Eagle Rock Division Bunker Hill Division Sun Valley Division Phoenixville Division Belle Aire Acres Division (Receivership)*
<p>* The James Black Water Service Company – Belle Aire Acres Development is being operated by Aqua under a Receivership established via Commission Order on September 3, 2019 at Docket No. M-2019-3012563. Aqua began its Receivership on September 11, 2019 and will continue to act as Receiver for the system until a final determination is made by the Commission. Belle Aire Acres customers are flat rate unmetered customers.</p>

Table 8: Aqua's water operations showing its Division by Rate Zone

As explained by the OCA’s witness, Mr. Glenn A. Watkins, Aqua’s rate design proposal pertaining to its water operations generally consisted of: (1) the continued movement of those areas with year-round usage toward the Main Division rates; (2) the continuation of its inverted-block usage rate structure; and (3) an increase to its monthly fixed customer charges. The Company’s present and proposed water rates by class, set forth in Schedule I of Aqua Exhibit 5-A, Part I, reflect its rate structure, rate design and the distribution of the increase in revenue proposals in this proceeding.⁷⁹

Table 9, below, provides a summary of the Company’s current and proposed 5/8” meter residential customer charges:

Aqua Water Current & Proposed Residential 5/8” Customer Charges				
Rate Zone	Division	Current	Proposed	Percent Change
1	Main	\$18.00	\$22.40	24.44%
2	Main	\$18.00	\$22.40	24.44%
3	Main	\$28.00	\$32.40	15.71%
BH	Bunker Hill	\$8.00	\$11.80	47.50%
PH	Phoenixville	\$3.33	\$4.90	47.15%

Table 9: Summary of Aqua’s current and proposed customer charges by Rate Zone for residential 5/8” meter water customers. OCA St. 4 at 13.

⁷⁹ Ms. Heppenstall provided updates to her revenue allocation and rate design for water service in Aqua Exhibit 5R-A, Part I, as part of her rebuttal testimony. The Company’s revised revenue exhibits reflect corrections to: (1) the 6-inch and 8-inch private fire rates in the Superior Division, and (2) Aqua’s public fire revenue under proposed rates. *See* Aqua Exh. 5R-A, Part I, Schs. 1 and 7A.

Aqua indicated that its proposal includes increases in consumption charges so that revenues by class move toward cost of service indicators and to recover the total revenue requirement. Aqua St. 5 at 12.

The Company explained its proposed rates for the remaining non-seasonal water divisions as follows:

Zone 1 – CC Garden, Sand Springs, Mifflin Township, Mount Jewett, and Robin Hood rates will move fully to Rate Zone 1 rates. Beech Mountain and Bristol Township division rates will continue to move toward Zone 1 rates.

Zone 2 – will move fully to rates in Rate Zone 1 by raising the meter charges for $\frac{3}{4}$ -inch to 4-inch to the level of Rate Zone 1 rates. All other rates were previously equal to Zone 1 rates.

Two other areas, Bunker Hill and Phoenixville, rates were increased to move toward Zone 1 rates. The Company capped the rate increases for these two areas to 48%.

Aqua St. 5 at 12.

The Company explained its proposed rate structure for seasonal areas as follows:

The Zone 3 Division has a significant number of seasonal customers and will continue to be served under the merged seasonal rate design. The customer charge is increased to \$32.40 per month, but is offset with a lower first block consumption rate than Main Division for the first 4,000 gallons. The bills for the seasonal rate structure are equalized with Main Division at the 4,000 gallon average per month and greater consumption levels.

Aqua St. 5 at 13.

The Company further explained its use of competitive service riders⁸⁰ and summarized the development of its rate proposals regarding public and private fire and those for Industrial Standby Rates, Resale, and Electric Generation Standby Rates. *See* Aqua St. 5 at 13-15; Aqua M.B. at 232-33.

(2) I&E

As previously discussed, Aqua proposed to subsidize its wastewater revenue requirement by approximately \$20.8 million with increased water revenues by the same amount under Act 11. Aqua Exh. 1-A(a), Sch. Act 11. Although the actual recommendations differ, I&E, the OCA, and the OSBA⁸¹ each recommended a reduction to the requested subsidy from Aqua water customers, indicating a reflection of that reduced subsidy through a corresponding increase to the wastewater rates proposed by the Company.

Therefore, I&E's recommended water rate design changes are based upon its proposal to reduce the Act 11 subsidy from water customers. Specifically, I&E proposed a 20% increase for water customers as compared to the Company's proposal for water customers. Thus, I&E asserted that the Company's proposed percentage increases to the water customer classes should all be scaled back to 20% of the Company's original proposed percentage increases. I&E M.B. at 73. I&E explained that this scale back of water rates, including customer charges, should be proportional to the percentage increase originally proposed by the Company. I&E St. 4 at 18-20.

⁸⁰ The Company noted that it has not proposed any changes to its competitive service riders in this proceeding. Aqua M.B. at 232.

⁸¹ "As a result of the OSBA's proposal to assign additional increases, in aggregate, of \$2.259 million to the Company's Base and New Garden Divisions, Mr. Kalcic testified that the OSBA's overall proposed wastewater increase is \$13.8 million or 37.3%, and its recommended Act 11 revenue requirement is \$18.580 million, or \$2.259 million less than Aqua's proposal." OSBA St. 1 at 16-17.

(3) OCA

Although the OCA did not agree with I&E's methodology, the OCA did agree that the wastewater subsidy should be reduced. Therefore, the OCA's recommended water rate design changes are also based upon its proposal to reduce the Act 11 subsidy from water customers. Specifically, the OCA recommended to reduce the Company's proposed Act 11 water subsidization of approximately \$20.8 million by \$9.065 million. Accepting the Company's proposed water increases by division and class, the OCA allocated the \$9.065 million to each division and class on a prorated basis. OCA St. 4 at 11.

Additionally, the OCA contended that Aqua's proposed increase to water customer charges was unsupported and that certain overhead costs were improperly included in the Company's customer cost analysis. Specifically, according to the OCA, Aqua included indirect O&M expenses, indirect depreciation expenses and indirect rate base within its customer cost analysis. OCA M.B. at 99-101.

Based on the customer cost analyses performed by its witness, Mr. Watkins, the OCA argued that there is no reasonable basis for Aqua's proposal to increase the existing monthly residential water customer charges in the Main Division of Zone 1 (\$18.00), Zone 2 (\$18.00) and Zone 3 (\$28.00) above current rates.⁸² OCA St. 4 at 16. The details of Mr. Watkins' customer cost analyses are presented in OCA Schedule GAW-7. Table 10, below, provides a summary of the OCA's residential customer cost analyses for residential 5/8" meter water customers under the OCA's and Aqua's proposed cost of capital.

⁸² The OCA accepted Aqua's proposed increases to the customer charges for Bunker Hill and Phoenixville because the current rates and proposed rates are significantly lower than the current Main Division rates. OCA St. 4 at 16.

Aqua Water Residential Customer Costs (5/8" Meter Equivalent)		
	<u>OCA Proposed Cost of Capital</u>	<u>Aqua Proposed Cost of Capital</u>
Direct Costs	\$17.07	\$19.26
Direct + Indirect Costs	\$17.36	\$19.55

Table 10: Summary of results of the OCA’s residential customer cost analyses (OCA Schedule GAW-7) for residential 5/8” meter water customers under the OCA’s and Aqua’s proposed cost of capital. *See* OCA St. 4 at 16.

Aqua contended that the OCA’s attempt to exclude certain costs from the calculation of the residential water customer charge lacks merit and undermines the support provided by Aqua for its proposed residential water customer charges. Aqua M.B. at 234-35. Aqua specifically noted its reliance on Commission precedent in the *Aqua 2004 Order* in the development of its residential customer charge⁸³ and further averred that the Commission’s determination in the *Aqua 2004 Order* was subsequently affirmed in the *2012 PPL Order*. Aqua M.B. at 234-235.

(4) Aqua LUG

Only Aqua LUG addressed the issue of non-residential water charges. Aqua LUG’s Main Brief reiterated the arguments it raised in testimony regarding changes to the design of the customer charges and the rates for consumption blocks for commercial and industrial customers. *See* Aqua LUG M.B. at 10-12. Specifically, Aqua LUG’s witness, Mr. Baudino, testified that “Commercial and Industrial customer charges

⁸³ *Pa. PUC v. Aqua Pennsylvania, Inc.*, Docket No. R-00038805 (Order entered August 5, 2004) (*Aqua 2004 Order*).

and the rates for consumption blocks 1 through 4 are the same for both classes,” but noted “Industrial class rates also have 5th and 6th blocks that Commercial customers do not have.” Therefore, he recommended that the Company keep charges for blocks 1 through 4 of the Commercial and Industrial classes similar, while avoiding “excessive increases for blocks 5 and 6 of the Industrial class.” Aqua LUG St. 1 at 5-6. He further recommended that Aqua could shift some of the revenue allocated to the Industrial class to the Residential class to moderate any increases, if necessary. Aqua LUG St. 1 at 6.

Aqua responded to the arguments posed by Aqua LUG, contending that Aqua LUG’s proposals are unreasonable and unnecessary. Aqua M.B. at 229-230, 236-237.

b. Wastewater Rate Design

(1) Aqua’s Wastewater Rate Design Proposal

Aqua currently has eleven different wastewater rate zones, with different subsystems and eight different third-party customers. *See* Aqua Exh. 5-B, Part II, Schs. WW-2, LMK-3, EB-3, CH-3, EN-2, and NG-2. Since the Company’s last base rate proceeding, it has acquired the Limerick, East Bradford, Cheltenham, East Norriton, and New Garden systems through separate Section 1329 proceedings.⁸⁴ These five systems became Rate Zones seven through eleven, as shown in Table 11, below:

⁸⁴ *See* Aqua Pennsylvania, Inc. Tariff Sewer – PA P.U.C. No. 2, Original Page 5 through Supplement No. 6 to Tariff Sewer – PA P.U.C. No. 2, Third Revised Page 6.

Wastewater Operations - Rate Zones / Divisions

<u>Rate Zone 1 (Main)</u>	<u>Rate Zone 1A</u>	<u>Rate Zone 1B</u>
Media Division	Treasure Lake Division	Penn Township Division
Bidlewood Division	Village at Valley Forge Division	
Eagle Rock Division	Bunker Hill Division	
<u>Rate Zone 2</u>	<u>Rate Zone 3</u>	
Emlenton Borough Division	Beech Mountain Lakes Division	Story Creek Division
Rivercrest Division	Deerfield Knoll Division	Thornhurst Division
White Haven Division	Laurel Lakes Division	Willistown Woods Division
Pinecrest Division	Links at Gettysburg Division	Woodloch Springs Division
<u>Rate Zone 4</u>	<u>Rate Zone 5</u>	<u>Rate Zone 6</u>
Honeycroft Village Division	Avon Grove School Division	CS Sewer Division (Masthope)
Lake Harmony Division	East Bradford Division	
New Daleville Division	Little Washington Division	
Peddlers View Division	Plumsock Division	
Tobyhanna Township Division	The Greens at Penn Oaks Division	
Twin Hills Division	Newlin Green Division	
	Sage Hill Division	
<u>Zones Recently Acquired Under Act 129, at 66 Pa. C.S. § 1329</u>		
Rate Zone 7 - Limerick Division		
Rate Zone 8 - East Bradford Township Division		
Rate Zone 9 - Cheltenham Township Division		
Rate Zone 10 - East Norriton Township Division		
Rate Zone 11 - New Garden Township Division		

Table 11: Aqua's wastewater operations showing its Divisions by Rate Zone.

As a result of recent and prior acquisitions of wastewater systems, Aqua's wastewater rates are comprised of several varying rate structures, including fixed

customer or EDU⁸⁵ charges, plus usage charges, unmetered flat rates, and structures with minimum usage allowances. Aqua proposed a similar model to its water operations for its wastewater operations with the intent of gradually grouping and consolidating divisions towards Rate Zones, specifically proposing to begin (or continue) movement to unified customer charges for metered customers.

Aqua's witness, Ms. Heppenstall, explained that the Company developed the following four guidelines for the design of wastewater rates: (1) move toward additional consolidation of rates across rate zones; (2) for metered areas, develop a rate structure that includes a customer charge or EDU charge and a single block usage charge; (3) for unmetered areas, develop a monthly flat rate equal to 4,000 gallons priced-out at the respective zone rates; and (4) where possible, eliminate an allowance. *See* Aqua St. 5 at 21-22. The Company presented a comparison of its present and proposed wastewater rates in Schedule F-WW of Aqua Exhibit 5-B, Part I.⁸⁶

⁸⁵ The Company's proposed wastewater tariff defines an EDU as follows:

Equivalent Dwelling Unit or "EDU": The EDU is a measure based upon the estimated average daily wastewater flow for the type of business, as calculated by the Pennsylvania Department of Environmental Protection regulation at 25 Pa. Code § 73.17 divided by the typical estimated average daily wastewater flow from a current single-family unit. In the Company's sole discretion, the Company may assign more than one (1) EDU for a residential Property.

See Tariff Sewer No. 3, Original Page 25.

⁸⁶ Ms. Heppenstall provided updates to her revenue allocation and rate design for wastewater service in Aqua Exhibit 5R-B, Part I, as part of her rebuttal testimony. The Company's revised revenue exhibits reflect corrections to: (1) Aqua's proposed unmetered charges for Woodloch Springs, and (2) Aqua's proposed rate for Southdown Homes. *See* Aqua Exh. 5R-B, Part II, Sch. WW-5 at 9 and 17.

In this proceeding, Aqua has proposed the same rates for Zones 1 and 2, and therefore, has merged Zone 2 into Zone 1. The proposed merger of Zone 2 into 1 (with which I&E disagrees) would mean that each subsequent zone could be reclassified up one (*i.e.*, Zone 3 customers would become Zone 2; Zone 4 customers would become Zone 3; Zone 5 customers would become Zone 4; and Zone 6 customers would become Zone 5). *See* Tariff Sewer, Original Page 5 and 6.

Additionally, as part of its consideration of the design of wastewater rates, Aqua performed an analysis of the feasibility of implementing a summer wastewater cap, as required by the settlement of its 2018 base rate proceeding. *See* Aqua Exh. 5-C. Based on this analysis, Aqua witness, Ms. Heppenstall, explained Aqua's contention that it was not appropriate to implement a summer wastewater cap for its wastewater customers:

[Aqua] performed an analysis based on capping usage at winter water usage levels for the Wastewater Base Operations. This cap would have the affect[sic] of raising the rates for all wastewater customers significantly and benefiting high water users. Our analysis, attached as Exhibit 5-C, shows that, under the cap, billed usage would decline by 38% and the average monthly bill for a residential customer using 4,000 gallons per month would rise to \$85.73, a 10.6% increase over the projected bill under proposed filed rates of \$77.49. In addition, as the wastewater operations benefit from the shift under Act 11 from wastewater to the water operations, it is conceivable that as wastewater rates rise due to the implementation of the cap, more Act 11 shifting would be needed to mitigate this increase.

Aqua St. 5 at 21-22.

(2) I&E

Consistent with the modifications I&E recommended for the Company's water rate design changes, I&E recommended similar adjustments to Aqua's proposed wastewater rates that are intended to reduce the size of Aqua's proposed Act 11 subsidy of wastewater customers. As such, I&E generally recommended higher rates for wastewater customers than those proposed by the Company, producing a larger increase for each division.⁸⁷ I&E provided a comprehensive summary of its proposed wastewater rate structure in its Main Brief that was presented in greater detail by its witness, Mr. Kubas, in his direct and surrebuttal testimony and accompanying exhibits. *See* I&E M.B. at 74-92; I&E St. 5; I&E St. 5-SR. In revising rates in Zones 1 through 6 to reduce the Act 11 contribution related to the wastewater customers in these rate zones, Mr. Kubas proposed the following recommendations shown in Table 12, below.

⁸⁷ As previously explained, I&E recommended an increase of \$6,097,022 for Rate Zones 1 through 6, as opposed to the Company's \$3,544,773 requested increase for those Zones, and an increase of \$10,589,684 for Rate Zones 7 through 11, as opposed to the Company's \$8,097,608 requested increase for those Zones. *See* I&E Exh. 5-SR, Sch. 1 at 1, Cols. I and L, lns. 7 and 18.

Summary of I&E Recommendation for Rate Zones 1-6

RZ 1:

- Increase the customer charges, unmetered rates and the volumetric charge by 46.8%.
- Increase the Media and Bunker Hill unmetered charge to \$90.00/month.
- **39.8% bill increase for an average residential customer.***

RZ 1A and 1B:

- Set these rates equal to Zone 1 rates.
- Eliminate the allowance in Zone 1B.
- **52.2% bill increase for an average residential customer in Zone 1A.***
- **42.5% bill increase for an average residential customer in Zone 1B.***

RZ 2 - Main:

- An across-the-board increase of 46.7% to tariff rates.
- No consolidation of Rate Zone 2 with Rate Zone 1 as proposed by Aqua.
- **39.7% bill increase for an average residential customer.***

RZ 2 - Pincrest:

- Maintain Aqua's proposed rate design of no increase.

RZ 3 - Main:

- Increase the customer and volumetric charges by 36.6% per month.
- Consolidate the unmetered charges to one charge.
- **29.8% bill increase for an average residential customer.***

RZ 3 - Woodloch Springs (Flat Rate):

- Accepts Aqua's proposed rate structure based upon EDU billing, with no usage charge.
- Increase the monthly unmetered charge to \$109.00/month, as opposed to Aqua's proposal of \$101.03/month (\$109.00 per EDU is the same unmetered charge I&E proposed for Zone 3 - Main customers).
- **52.5% bill increase for an unmetered commercial customer.**

RZ 4:

- An across-the-board increase of 31.1% to tariff rates.
- **24.9% bill increase for an average residential customer.***

RZ 5:

- Accepts Aqua's proposed rates.
- **20.3% bill increase for an average residential customer in RZ 5 - Main.***
- **4.4% bill decrease for an average residential customer in RZ 5 - Newlin Green.***

RZ 6:

- Increase the customer charge by 41.8%, the usage rate by 160%, and the unmetered rate by 53.5%.
- **44.6% bill increase for an average residential customer.***

* I&E assumed an average 5/8" residential customer using 3,700 gallons per month.

Table 12: Summary of I&E's recommended rate changes for Aqua's wastewater Rate Zones 1 through 6 (See I&E Exh. 5, Sch. 2 at 1, Cols. F and L; I&E Exh. 5, Schs. 3-8 at 1, Col. F; *see also*, I&E Exh. 5, Sch. 2 at 2-4, Sch. 3 at 2; Sch. 4 at 2-4; Sch. 5 at 2; I&E Exh. 5-SR, Sch. 2; Aqua Exh. 5-B, Part II, Sch. WW-7 at 11-12; Aqua Exh. 5R-B, Part II, Sch. WW-5 at 9).

As previously indicated, Zones 7 through 11 include the Limerick, East Bradford, Cheltenham, East Norriton,⁸⁸ and New Garden systems, which were acquired after the *Aqua 2018 Rate Case*. Some of these systems have rates lower than present rates in Zones 1 through 6, and therefore, I&E argued that it is unfair to keep these rates artificially lower than the rates of existing customers. As delineated in Table 13, below, I&E recommended adjustments to rates in Zones 7 through 11 to reduce the subsidy, simplify the rate structure, and limit the increase to Zone 7 flat-rate customers and certain Zone 11 usage blocks. I&E reasoned that acquiring these systems should not harm existing Aqua customers; therefore, the larger than average increase to rates in Zones 7 through 11, shown on page 3 of I&E Exhibit 5-SR, Schedule 1, balanced out by the benefits to the municipality and/or customers of the acquired systems, will, according to I&E, limit the harm to other Aqua customers by reducing the subsidy paid by other non-Zone 7-11 Aqua customers. I&E noted that it is tempering the proposed increases in order to mitigate the large increases to the monthly customer charges, usage rates, unmetered rates, and average bills for both residential and commercial customers in Zones 7-11. I&E added that it is recommending rates so that the average residential bill increase is limited to generally less than 100%. I&E St. 5 at 35-38.

⁸⁸ Aqua acquired the Whitpain system with the East Norriton system on June 19, 2020 at Docket No. A-2019-3009052.

Summary of I&E Recommendation for Rate Zones 7-11

RZ 7 - Limerick:

- Increase the customer charge by 40.6% and the volumetric rate by 33.1%.
- Eliminate the allowance (also proposed by Aqua).
- Increase the unmetered rate to \$60.00/month.
- **89.2% bill increase for an average residential customer.***

RZ 8 - East Bradford:

- Monthly customer (EDU) charge of \$55.00, as opposed to Aqua's proposal of \$39.10.
- Volumetric charge of \$1.12/100 gallons.
- Accepts Aqua's proposed monthly commercial customer charge of \$39.10.
- **74.2% bill increase for an average Multi-Family Residential customer.***
- **84.3% bill increase for an average commercial customer.**

RZ 9 - Cheltenham:

- Increase the customer charge to \$30.00/month (43.6% increase).
- Increase the volumetric charge to \$0.68/100 gallons (73.9% increase).
- **56% bill increase for an average residential customer.***

RZ 10 - East Norriton & Whitpain:

- Increase the customer charge to \$35.00/month (66.0% increase).
- Increase the volumetric charge to \$0.76/100 gallons (16.2% increase).
- Eliminate the allowance (also proposed by Aqua).
- **72.6% bill increase for an average residential customer in RZ 10 - East Norriton.***
- **99.4% bill increase for an average residential customer in RZ 10 - Whitpain.***

RZ 11 - New Garden:

- Increase the customer charge to \$43.00/month (14.2% increase).
- Increase the residential volumetric charge to \$2.20/100 gallons for usage up to 5,000 gallons/month and \$3.1626/100 gallons for usage over 5,000 gallons per month.
- Eliminate the allowance (not proposed by Aqua).
- **81.7% bill increase for an average residential customer.***

* I&E assumed an average 5/8" residential customer using 3,700 gallons per month.

Table 13: Summary of I&E's recommended rate changes for Aqua's wastewater Rate Zones 7 through 11 (*See I&E Exh. 5, Schs. 6-7 at 1, Cols. F and G; I&E Exh. 5-R, Sch. 2 at 1, Cols. F and G; see also, I&E Exh. 5, Sch. 6 at 2, 4, 5, Sch. 7 at 2, 3, 4; I&E Exh. 5-R, Sch. 2 at 2).*

With respect to non-residential wastewater charges, only I&E addressed this issue. Specifically, as previously explained, I&E's proposed rate design changes

regarding Rate Zone 8 – East Bradford operations were based upon its proposals to reduce the Act 11 wastewater revenue allocation from this Rate Zone to water customers.

Aqua responded to I&E's rate design proposals for wastewater rates, generally opposing the rate design modifications proposed by I&E. In this regard, the Company contended that I&E's proposals would be contrary to the principles of gradualism, resulting in significant percentage increases to an average customer bill, as well as significant dollar-for-dollar increases. *See Aqua M.B. at 222-23.* Aqua particularly noted that I&E's proposed changes to the commercial wastewater customer rates for Rate Zone 8 – East Bradford would increase the average bill by over 84%. Aqua M.B. at 245 (citing I&E Exh. 5, Sch. 6 at 5).

(3) OCA

As he contended with respect to the Company's proposed increase to water customer charges, the OCA's witness, Mr. Watkins, argued that the Company provided no support for its proposed increase to wastewater residential customer charges. OCA St. 4 at 17. Therefore, Mr. Watkins opposed Aqua's proposal to increase the wastewater Rate Zone 1 5/8" monthly residential customer charge by \$8.10 per month, from \$31.00 to \$39.10. OCA St. 4-S at 17. Mr. Watkins argued that similar to Ms. Heppenstall's customer cost analysis for water, her analysis for wastewater also includes numerous overhead costs that cannot be reasonably considered "direct costs" required to connect and maintain a customer's account. OCA St. 4-SR at 7.

Aqua contended that the OCA's arguments it proffered against the approval of the Company's proposed residential wastewater customer charges lack merit and ignore the record evidence provided by Aqua. Aqua M.B. at 238-239. Aqua averred that the OCA's proposal regarding Rate Zone 1 rates should be rejected because, as the Company's witness, Ms. Heppenstall, demonstrated, the weighted average of all

wastewater customer charges under proposed rates is lower than the customer charge that the Company can support based upon a customer cost analysis which is summarized in Table 14, below:

Rate Zone	Metered Bills	Customer Charge Revenue*	Average Customer Charge
RZ 1	\$ 16,897	\$ 660,689	\$ 39.10
RZ1A	26,337	1,146,776	43.54
RZ1B	9,833	384,466	39.10
RZ2	11,663	492,629	42.24
RZ3	27,676	1,607,722	58.09
RZ4	8,065	626,580	77.50
RZ5	6,457	607,967	94.15
RZ5 - NG	588	54,957	93.45
RZ6	16,548	829,074	50.10
RZ7	82,876	3,271,931	39.48
RZ8	14,399	562,999	39.10
RZ9	202,241	5,705,208	28.21
RZ10	56,687	1,834,952	32.37
RZ11	26,382	1,361,551	53.62
Total	\$ 505,680	\$ 19,147,501	\$ 37.86

* Under proposed rates.

Table 14: Aqua’s summary of its average wastewater customer charge by Rate Zones (Aqua M.B. at 239 (citing Aqua St. 5-R at 11)).

Aqua further asserted that the OCA’s rate analysis was “incomplete,” and noted that although Mr. Watkins proposed to maintain the existing customer charge of Rate Zone 1, he did not discuss the customer charges for Rate Zones 2 through 6. Aqua St. 5-R at 11, 14.

With regard to Rate Zones 7, 8 and 10, the only area of disagreement between Aqua and the OCA is whether the residential wastewater customer charges should be \$31.00, which is the rate recommended by the OCA for residential Rate

Zone 1, rather than the Company's proposed charges of \$39.48, \$39.10 and \$32.37, respectively.⁸⁹ Aqua M.B. at 240-41; OCA M.B. at 102-03; OCA St. 4 at 18-19.

With regard to Rate Zone 11, the OCA objected to Aqua's proposal to increase the fixed monthly charge from \$37.64 to \$51.71 per month and recommended holding it at the current \$37.64 level, to avoid moving the charge further from the \$31.00 residential customer charge recommended by the OCA for most of the wastewater rate zones. OCA M.B. at 103. Also, similar to I&E, the OCA recommended eliminating the usage allowance. OCA M.B. at 103; OCA St. 4 at 18.

Aqua contended that the OCA's proposals regarding Rate Zones 7 through 11 are similarly meritless. Aqua M.B. at 240-43.

In addition to its recommended modifications to the Company's proposed wastewater rates, the OCA offered further proposals regarding Aqua's unmetered rates. OCA M.B. at 104-108. The OCA's discussion surrounding the rate design of Aqua's metered and unmetered customers centered on its concern that under present rates, the Company's average monthly metered revenue per customer, for all customers, is different than the Company's current unmetered rate. The OCA's witness, Mr. Watkins, identified nine wastewater rate zones that have both metered and unmetered residential rates. He explained that for some zones, the metered and unmetered rates are relatively close; but in others, there is a significant difference between rates for an average metered rate customer and flat rate customer. OCA St. 4 at 20; OCA Sch. GAW-8. For example, compared to metered rates, flat rates are 57% higher in Zone 5 and 30% lower in the

⁸⁹ The OCA accepted Aqua's proposed customer charge increase for Zone 9 residential customers. See OCA M.B. at 241.

Limerick Zone.⁹⁰ In this regard, the OCA requested that the Company study the reasonableness of its unmetered rates and provide the results in its next base rate proceeding. OCA St. 4 at 21.

According to Aqua, there are valid reasons for the differences between metered and unmetered rates. Aqua further explained that its unmetered rates assume an average usage of 4,000 gallons per month, which is standard industry practice. Aqua St. 5-R at 14-15. As to customers who pay a flat rate in Lake Harmony and Tobyhanna, Aqua took the position that customers pay to have wastewater service available, whether they are present at the service address for a few days or for longer periods of time; residency status is not a determinative factor. Aqua St. 9-R at 29.

Based on the concerns and testimony of several Lake Harmony wastewater customers regarding flat wastewater rates, as voiced at the public input hearings, the OCA's witness, Mr. Watkins, submitted supplemental direct testimony addressing the issue in Lake Harmony and several other developments where Aqua provides wastewater service, in which the water service is unmetered. OCA St. 4 SUPP. At those locations, wastewater customers either have their own wells or receive unmetered water from a community system. In these situations, the Company will bill wastewater service at a flat rate, where it uses average metered wastewater usage from customers with metered rates to develop a proxy of usage, which is then used to develop the rates. The OCA recommended that Aqua develop a pilot program to install meters for those customers who want them.⁹¹ Under this proposal, Aqua would install water meters on customer-owned wells on an opt-in basis. These opt-in customers would be billed at the applicable

⁹⁰ The current average monthly metered rate for the Avon Grove Division in Rate Zone 5 is \$113 (before DSIC) compared to \$177 for flat-rate customers. The current average monthly metered rate for Rate Zone 7 – Limerick is \$40 (before DSIC) compared to \$28 for flat rate. OCA St. 4 at 20, Table 8.

⁹¹ Complainant John Day wrote in support of the OCA's proposal. Letter in Lieu of Brief filed January 10, 2022.

metered rate. Mr. Watkins further proposed that the Company install water meters on other customer-owned wells based upon a random sample of 10% to 20% of the unmetered customers. These customers would be billed on a flat-rate basis, but the Company would prepare “shadow” bills based upon consumption. OCA St. 4 SUPP. at 2.

Aqua opposed this recommendation for a variety of reasons including cost and feasibility. Aqua St. 5-R at 17-18; Aqua St. 9-R at 29-30.

The OCA’s witness, Mr. Watkins, further testified in response to the result of the Company’s analysis of capping non-seasonal wastewater rates. *See* OCA St. 4 at 21-22. As previously indicated, Aqua performed an analysis of the feasibility of implementing a summer wastewater cap, as required by the settlement of its 2018 base rate proceeding. *See* Aqua Exh. 5-C. The basis for the cap is to address potential inaccuracies in the calculation of wastewater volumetric charges during the summer months when irrigation, swimming pool filling, and other outside watering activities are traditionally in use.⁹² Mr. Watkins recommended that the Company continue to study the feasibility of: (1) a capping mechanism with a winter multiplier greater than 100%;⁹³ and (2) the implementation of irrigation water meters on a customer-by-customer request basis. OCA St. 4 at 22.

⁹² Mr. Watkins testified that “In my experience, I am familiar with two mechanisms to fairly treat those customers whose Summer irrigation use is significant. The first and most prevalent are capping mechanisms similar to the one considered in the study conducted by Aqua. However, more often than not, I have seen capping mechanisms with an admittedly arbitrary multiplier such as 125% of Winter usage or 150% of Winter usage as a cap. This is different from the Company’s study wherein they used a multiplier of 100%; *i.e.*, simply capped at average Winter usage.” OCA St. 4 at 22.

⁹³ The OCA acknowledged that Aqua has already conducted an analysis of a capping mechanism with a multiplier of 100% but recommended that Aqua could study a multiplier greater than 100%. OCA St. 4 at 21-22.

Aqua opposed further study of a cap on non-seasonal wastewater rates, noting that it complied with its prior commitment from the 2018 base rate proceeding to provide a study as a part of this proceeding, and the results of the study revealed that a cap only benefits high water users. In addition, the imposition of a cap on non-seasonal wastewater rates could also result in a need to shift more wastewater revenue requirement to water rates. Aqua explained that the further studies proposed by the OCA will produce results similar to the analysis presented by Aqua in this case, and thus further studies are not necessary. Aqua St. 5-R at 15. Aqua also disagreed with the OCA's proposal to install irrigation meters on a customer opt-in basis, noting that such an implementation would increase revenue requirement for the installation and reading of meters and would not reduce revenue requirement recovery. Aqua R.B. at 104.

2. Recommended Decision

In her Recommended Decision, the ALJ recommended that the Commission adopt the overall wastewater rate design advocated by I&E, which was proposed to obtain I&E's Act 11 revenue allocation proposal:

I recommend that the Commission accept the methodology of I&E for allocating revenue and designing wastewater rates. I&E's approach takes into consideration the number of water and wastewater customers in each system and balances the goal of moving rates toward alignment with the cost of service, while also mitigating some of the large rate increases that would result if no allocation of wastewater revenue was approved. I&E's approach acknowledges the benefits received by the communities serviced by the Acquired Systems from the sale of their systems to Aqua, but is less complicated than the method advocated by OCA.

R.D. at 91.

Although the ALJ recommended adoption of I&E's proposed wastewater rate design, including its recommended customer charges, the ALJ found Aqua's water and wastewater residential customer cost analyses upon which it based its proposed increases to customer charges to be reasonable, stating:

While the Commission generally disfavors the inclusion of indirect costs into the calculation of customer charges, the Commission has nevertheless permitted the allocated portions of certain indirect costs such as employee benefits, local taxes and other general and administrative costs. I find that Aqua's witness adequately demonstrated that the indirect costs included in her study fall within the ambit of permissible general and administrative costs.

R.D. at 95.

In this regard, the ALJ implicitly rejected the OCA's residential customer charge proposals for water customers, while nonetheless, adopting I&E's recommended water rate design changes, based upon its proposal to reduce the Act 11 subsidy from water customers.⁹⁴ R.D. at 91, 95.

Regarding the reasonableness of unmetered rates, the ALJ agreed with the OCA and recommended that Aqua study whether a different method of calculating a flat rate would be more reasonable for some systems than applying a system-wide average and report the results in its next base rate case. R.D. at 98.

⁹⁴ I&E asserted that the Company's proposed percentage increases to the water customer classes should all be scaled back to 20% of the Company's original proposed percentage increases. I&E M.B. at 73. I&E explained that this scale back of water rates, including customer charges, should be proportional to the percentage increase originally proposed by the Company. I&E St. 4 at 18-20.

Although the ALJ saw the benefits of Aqua studying the reasonableness of its unmetered rates, finding that there may be areas in Aqua's service territory where unique circumstances may suggest that a different method of calculating a flat rate is more reasonable, ALJ Long however, rejected the OCA's proposal for the implementation of a metering pilot for flat-rate customers in the Lake Harmony service area, providing the following reasoning:

OCA does not include any cost estimates for its recommended pilot program but proposes that the meters be installed at Aqua's cost. No doubt, that cost would be socialized to all of Aqua's wastewater ratepayers. Some customers would "opt-in" for the installation of a meter. Other customers would not opt-in. This adds a layer of administrative complexity and costs, including costs to test and maintain meters and administer this program. While the Commission certainly favors consumption-based utility rates, it is not clear that the cost of OCA's proposed pilot will achieve overall benefits to Aqua's customers that will outweigh the costs. Therefore, I recommend the Commission reject OCA's proposal.

R.D. at 97.

Finally, the ALJ recommended that the Commission reject the OCA's recommendation regarding additional studies of a non-seasonal wastewater capping mechanism. The ALJ agreed with Aqua that further study of a non-seasonal wastewater capping mechanism is unnecessary, reasoning that the OCA did not demonstrate that further study would yield better results. R.D. at 99.

3. Exceptions and Replies

a. Aqua Exception No. 10 and Replies

In its Exception No. 10, Aqua submits that the ALJ erred in recommending that Aqua be required to provide a study in its next base rate case that would determine the reasonableness of unmetered rates. Aqua maintains its position, as argued by its witness, Ms. Heppenstall, that such a study is not needed. Aqua Exc. at 35. Aqua contends that Ms. Heppenstall fully explained the basis for the differences between metered and unmetered rates, as follows:

The large difference in Limerick and East Norriton is based on the fact that these are new acquisitions with legacy rates. The Company will rectify this disparity when it sets the rates in this case. For the other rate zones, the unmetered rate is based on an assumed average usage of 4,000 gallons per month plus a customer charge. The average usage of 4,000 gallons is substantiated in the Company's prior rate case as the pre-COVID pandemic average residential usage was 4,068 per month for the residential class. For example, in Bridlewood, the calculation of the unmetered rate under present rates equals \$31.00 plus the usage rate of .7600 per 100 gallons at 4000 gallons ($\$31.00 + .7600 \times 40$) or \$61.40. This calculation of the unmetered rate based on average usage is standard in the industry and used by other regulated water and wastewater utilities in Pennsylvania. For example, Pennsylvania American Water Company's unmetered wastewater rate for Zone 1 for 2022 is \$78.41 per month which was designed to equal the metered customer charge plus the usage rate multiplied by an average usage of 3,458 gallons.

Aqua M.B. at 244 (citing Aqua St. 5-R at 14-15) (emphasis added by Aqua).

Aqua further argues that the ALJ did not find the Company's use of unmetered rates or use of an average monthly usage of 4,000 gallons to be unreasonable,

but rather only found “that the use of a 4,000-gallon average monthly usage rate may not result in fair rates, and that there may be areas where a different method of calculating a flat rate is more reasonable.” Aqua Exc. at 35 (citing R.D. at 98 (emphasis added by Aqua)). Aqua notes that its witness, Mr. Todd M. Duerr, credibly testified that the average usage of 4,000 gallons was substantiated by the pre-COVID pandemic average residential usage shown in Aqua’s last base rate proceeding, and that its average usage amount was consistent with the average usage of other water utilities such as Pennsylvania-American Water Company. Aqua Exc. at 35 (citing Aqua St. 9-R at 14-15).

Additionally, Aqua posits that any results of such a study would be “speculative,” since many of the areas without metered water service have individual customer wells, which prevents access to the usage data needed to assess average usage for an area. Aqua Exc. at 35.

In its Replies, the OCA asserts that Aqua misunderstood the ALJ’s reasoning based on her concern that the usage amount assumption (derived from the system-wide average) for flat rates may not be reasonable for all areas of Aqua’s service territory, particularly in areas where there is a significant mix of types of housing or other unique circumstances. OCA R. Exc. at 15 (citing R.D. at 98; Aqua Exc. at 35). Therefore, the OCA maintains that, where the Company’s use of a system-wide average in the derivation of its unmetered rates is causing an unreasonable disparity in the rates charged to metered and unmetered customers, it is reasonable for Aqua to study and propose adjustments to its unmetered rates, which may include an adjustment to the usage assumption applied in a particular territory. OCA R. Exc. at 15.

Moreover, in reply to Aqua’s argument that due to customers being served by unmetered individual wells in some areas of its service territory, it lacks access to the usage data needed to perform such an analysis, the OCA notes that Aqua is ignoring the

nine individual territories where it charges some customers metered rates. OCA R. Exc. at 15. The OCA continues that Aqua has usage data at the individual system level, which informs its operations and compliance with regulatory requirements for wastewater collection, conveyance, treatment, and discharge. OCA R. Exc. at 15 (citing 25 Pa. Code. Chapters 91, 92a). Other information regarding housing size, occupancy and seasonal usage may be available from property owners' associations, local municipalities, and observation. OCA R. Exc. at 15.

b. OCA Exception No. 12 and Replies

In its Exception No. 12, the OCA disagrees with the ALJ's adoption of what it believes are overly inclusive residential customer cost analyses performed by Aqua, upon which the Company has based its residential customer charges for water and wastewater customers. OCA Exc. at 19-22.

The OCA maintains that a review of the specific indirect costs included in Aqua's studies show they do not fall within the ambit of costs that the Commission has historically permitted but are merely costs related to Aqua's general operation as a utility. The OCA noted its reliance on Commission precedent, which has generally permitted only expenses directly related to meter reading, customer service, accounting and customer records and collection, but has allowed costs associated with direct labor costs, including employee benefits, workers compensation insurance and payroll taxes, where portions of indirect costs have been permitted on a case-by-case basis. OCA Exc. at 20 (citing *Pa. PUC v. Metropolitan Edison Company*, 60 Pa. P.U.C. 349 (1985); *Pa. PUC v. West Penn Power Company*, 59 Pa. P.U.C. 552 (1985); *Pa. PUC v. West Penn Power Company*, 1994 Pa. PUC LEXIS 144, *154; *Pa. PUC v. National Fuel Gas Distribution Corporation*, 83 Pa. P.U.C. 262, 371 (1994); *see also*, 2004 PPI Order and Aqua 2004 Order). The OCA notes that more recently, the Commission has rejected a utility's proposed customer charge increase based on a cost analysis that included indirect costs.

OCA Exc. at 20 (citing *Pa. PUC v. PPL Gas Utilities Corporation*, Docket No. R-00061398 (Order entered February 8, 2007) at 137) (*2007 PPL Gas Order*).

The OCA submits that even when the additional types of costs that the Commission allowed in the *PSWC 2004 Order*⁹⁵ are included, the indicated customer costs are below the current Main Division 5/8” residential water customer charge of \$18.00 and, thus, there is no reasonable basis to increase the customer charges. OCA Exc. at 21. The OCA also maintains that Aqua’s proposal to increase the wastewater Zone 1 5/8” residential customer charge to \$39.10 should be rejected because the study that Aqua relies on improperly includes indirect overhead costs that are not reasonably related to connecting and maintaining a customer’s account, such as uncollectibles expense and rate case amortization. OCA Exc. at 21.

In addition to not supporting that level of customer charge increases with a direct cost study, the OCA contends that the magnitude of the increases is not supported by the public policy of gradualism and incentivizing conservation. OCA Exc. at 21 (citing *2007 PPL Gas Order*; *Pa. PUC v. Community Utilities of Pennsylvania, Inc.*, R-2021-3025206, *et al.* (Order entered January 13, 2022) at 62-63). The more revenue recovered through customer charges, the lower the volumetric rate, which impacts customers’ incentive to conserve. OCA Exc. at 21.

Contrary to the OCA’s claims in its Exceptions, Aqua maintains that the items the OCA asserts are “overhead costs” or “indirect expenses” are actually necessary for the support of customer facilities and customer accounting and should be considered direct costs. Aqua R. Exc. at 11 (citing Aqua M.B. at 234-35).

⁹⁵ *Pa. PUC v. Philadelphia Suburban Water Company*, Docket No. R-00038805 (Order entered August 3, 2004) at 72 (*PSWC 2004 Order*).

Moreover, Aqua counters that its customer cost analysis is consistent with Commission precedent; the ALJ evaluated these costs “on a case-by-case basis” consistent with this precedent. Aqua R. Exc. at 11 (citing Aqua M.B. at 235; R.D. at 95). Aqua further asserts that the OCA’s argument that Aqua’s proposed customer charges violate gradualism and do not incentivize conservation should be rejected. Aqua R. Exc. at 11 (citing OCA Exc. at 21). Aqua argues that its rates were designed to balance these considerations with the cost of serving its customers and demonstrated that its rate design guidelines were reasonable and appropriate. Aqua R. Exc. at 11-12 (citing Aqua M.B. at 230-33, 237-38).

c. OCA Exception No. 13 and Replies

In its Exception No. 13, the OCA disagrees with the ALJ’s adoption of I&E’s wastewater rate design methodology. OCA Exc. at 22 (citing R.D. at 88-89, 91, 96; OCA M.B. at 101-04; OCA R.B. at 60-61). Rather, the OCA maintains that its proposed wastewater rate design for the legacy systems and acquired systems is more reasonable and should be adopted. OCA Exc. at 22.

The OCA noted that I&E witness, Mr. Kubas, acknowledged that he normally would not support increasing the customer charges above cost, but he did so in this case because it provided more revenue. OCA Exc. at 22 (citing I&E St. 5 at 10, 38; I&E St. 5-R at 5). The OCA argues the additional revenue is derived from I&E’s proposed 46.8% increase to Zone 1 customer charges, from \$31.00 to \$45.50 per month, which is nearly two times the increase proposed by the Company as well as I&E’s proposed increases to all of the 5/8 customer charges that range between 26% and 66% and exceed their costs. OCA Exc. at 22 (citing I&E Exh. 5, Schs. 2-8).

On the other hand, the OCA submits that under its proposal, customer charges are supported by cost analyses and move customer charges toward consolidation

with the main wastewater zone customer charges. The OCA posits that under its proposal, customers will: (1) be charged cost-based fixed rates; (2) receive proper price signals; and (3) have more control of their bills. OCA Exc. at 22-23 (citing OCA R.B. at 58-61; OCA M.B. at 102-04; OCA St. 4 at 17-20). Further, the OCA contends that unlike I&E's proposal, the OCA's recommendations flow from its proposed customer charges for Zone 1 and reasonably move other divisions toward consolidation with those charges. OCA Exc. at 22 (citing OCA St. 4 at 17-20).

In its Replies, Aqua submits that the OCA's argument regarding the adoption of I&E's proposed wastewater rate design should be denied for the same reasons that the Company opposes the ALJ's adoption of I&E's proposed wastewater rate design and revenue allocation. Aqua R. Exc. at 12 (citing OCA Exc. at 22-23; Aqua Exc. at 31-34; Aqua R.B. at 102-04; Aqua M.B. at 237-43).

In its Replies, I&E notes that it made revisions in its final schedule that addressed the positions proffered by other Parties, including the OCA. Therefore, I&E asserts that the Commission adopt I&E's final wastewater revenue allocation and rate design, as discussed in I&E Exception No. 2. I&E R. Exc. at 17 (citing I&E Exc. at 4-5; I&E St. 5-SR at 4; I&E Exh. 5-SR, Sch. 1 at 1).

d. OCA Exception No. 14, Mr. Osinski's Exceptions, and Replies

In its Exception No. 14, the OCA submits that the ALJ erred by rejecting its proposal for the implementation of a metering pilot for flat-rate customers in the Lake Harmony service area. OCA Exc. at 23-25.

Referencing Aqua's continuation of deduct metering⁹⁶ programs for some of its acquired systems, specifically its Cheltenham service territory, the OCA contends that the cost and operational data from that existing deduct metering program can help to inform how the pilot is structured. Moreover, the OCA argues that the benefits of a pilot program, which assists in moving flat-rate customers to metered rates in an area where a significant number of customers may use less than (or more than) the average usage of 4,000 gallons, outweigh the costs, which, according to the OCA, should be reasonable since the pilot would involve only a few hundred customers. OCA Exc. at 23-24.

As such, the OCA excepts to the ALJ's suggestion to delay a remedy until the next base rate case because it will delay relief to customers who, under the OCA's proposal, could begin participating in a pilot program within a few months of a final order in the current case. The OCA maintains that Aqua should be directed to adopt a program, on a pilot basis, as a reasonable and measured response to the concerns raised by its customers regarding flat rates. OCA Exc. at 24-25.

In its Replies, Aqua maintains its opposition to any requirement to install Company water meters on customer owned (wells) or community owned water supplies, in order to implement metered wastewater rates, reemphasizing the arguments presented in its briefs. Aqua R. Exc. at 12-13 (citing Aqua M.B. at 243-44; Aqua R.B. at 103). Aqua adds that it has no right to enter customers' premises to demand the installation of water meters where Aqua does not provide the water supply and posits that an "opt-in" pilot will only lead to meter installations where customers have decided that their usage is below average, thereby negating the validity of the "pilot." Aqua R. Exc. at 12.

⁹⁶ Deduct metering is a mechanism which allows individual customers, using a significant amount of outside water, such as for an irrigation system, to have a separate irrigation water meter installed. This second meter, known as a deduct meter, measures the flow of water that does not enter the wastewater system and is used to calculate a reduction in wastewater charges. *See generally*, OCA St. 4 at 21-22, and 25; OCA Exc. at 25; Aqua R. Exc. at 13; and OCA M.B. at 109.

Mr. Osinski also filed exceptions to the Recommended Decision, specifically taking issue with the flat-rate service provided to the Camp Stead Property Owners Association, which is part of Aqua's Tobyhanna Township Division. Mr. Osinski argues that the private development (Camp Stead Property Owners Association) in which he resides is served by a metered community well; however, Aqua does not meter his wastewater. Mr. Osinski contends that Aqua's practice of basing his flat rate on 4,000 gallons of consumption per month is unjustified, and as a result, he is being charged far more than he uses. Osinski Exc. at 1-4.

In its Replies to the Exceptions of Mr. Osinski, Aqua points to its response to OCA Exception No. 14, in which it addresses concerns related to the flat-rate service provided to certain customers. Additionally, Aqua notes that it responded to concerns raised by customers at residences on Camp Stead Circle in its Main Brief. Aqua R. Exc. at 13 (citing Aqua M.B. at 179-180).

Furthermore, Aqua notes that Exhibits A-G, L and Q, attached to Mr. Osinski's Exceptions, appear to be extra record evidence, not permitted to be introduced in his Exceptions, and thus, should be disregarded. Aqua R. Exc. at 13 (citing *Application of Apollo Gas Company*, 1994 Pa. PUC LEXIS 45 (Order entered February 10, 1994) at *8-9 (denying party's attempt to introduce extra-record evidence in its exceptions)).

e. OCA Exception No. 15 and Replies

In its Exception No. 15, the OCA submits that the ALJ erred by not requiring the Company to study the feasibility of affording additional customers the option of deduct metering. OCA Exc. at 25-26 (citing R.D. at 99).

The OCA explains that the ALJ did not distinguish between the studies recommended by its witness, Mr. Watkins, and, as such, did not address the OCA's recommendation for an alternative study, which Mr. Watkins opined may be the fairest for Aqua – installing irrigation water meters on a customer-by-customer request basis. OCA Exc. at 25 (citing OCA M.B. at 109-10; OCA R.B. at 65-66; OCA St. 4 at 22). The OCA notes that, to its knowledge, Aqua has not already conducted any studies on irrigation metering, also referred to as deduct metering. *Id.*

Further, the OCA argues that Aqua's objection to studying the feasibility of opening its deduct metering program to Aqua's non-Cheltenham customers is not reasonable, since the Company already has a deduct metering program in its Cheltenham service territory and two years of cost and operational data from that program. Therefore, the OCA submits that the results of that study, including either a proposal to make deduct metering available to more or all customers or a detailed explanation for why Aqua believes expansion is infeasible in other service territories, should be filed no later than Aqua's next base rate case. OCA Exc. at 25-26.

Contrary to the OCA's arguments, Aqua replies that no such study should be ordered. Aqua maintains its argument that the installation of a second meter to measure usage deductions will only increase the revenue requirement for installing and reading meters and will not reduce the revenue requirement that needs to be recovered. Aqua R. Exc. at 13 (citing Aqua R.B. at 104; Aqua M.B. at 244-45).

4. Disposition

a. Water and Wastewater Rate Design

As previously explained, the allocation of the rate increase among the customer classes of both Aqua's water and wastewater divisions, and ultimately the rate

design under each division, was a significant issue in this proceeding.⁹⁷ In cases such as the instant one before us, the ALJ and the Commission are faced with the difficult task of balancing the justness and reasonableness of all components of revenue allocation and rate design. The reality is, as a result of the difficult choices that must be made, all customer classes will inevitably experience some degree of an undesired impact. Consistent with our discussion, *supra*, regarding the issue of revenue allocation, and based on our review of the supporting information contained in the record, we find that the ALJ's determinations regarding rate design are sufficiently supported by the evidentiary record. Accordingly, based on our discussion below, we find that the OCA's arguments against the ALJ's recommendation concerning this matter are without merit.

In reaching this determination, we have reviewed the rate designs adopted by the ALJ and found them to be reasonable, affording appropriate primary consideration to cost causation principles per *Lloyd* in tandem with secondary consideration for the value of service, gradualism, and affordability.

There is not a prescribed "ratemaking formula" that the Commission must adhere to when determining just and reasonable rates. Rather, the Commission "has broad discretion in determining whether rates are reasonable" and "is vested with discretion to decide what factors it will consider in setting or evaluating a utility's rates." *Popowsky II*. Included in the Commission's broad ratemaking authority is the authority to approve alternative rates and rate mechanisms, including formula rates as well as decoupling mechanisms, performance-based rates, and multiyear rate plans. 66 Pa. C.S. § 1330(b)(1)(i)-(v).

⁹⁷ In this proceeding, the Company invoked the Commission's authority under Section 1311(c) of the Code to mitigate the impact of revenue increases on wastewater customers by recovering a portion of the Company's wastewater revenue requirement from its total water and wastewater customer base. *See* 66 C.S. § 1311(c).

With that said, we acknowledge that a set of ratemaking norms have been developed over time and have been consistently utilized by parties in rate cases before the Commission to determine the appropriate level of a utility's requested revenue increase in accordance with all applicable legal and constitutional standards. These norms, or traditional ratemaking methodologies,⁹⁸ are used to determine a utility's cost of providing service, or its revenue requirement, and to determine appropriate rate structure, which includes, among other things, the appropriate allocation of the revenue requirement to various customer classes. However, while these ratemaking norms provide a rational and methodical way to analyze and determine the utility's cost of service, they also permit the consideration and weighing of important factors or principles in setting just and reasonable rates, such as quality of service,⁹⁹ gradualism,¹⁰⁰ and rate affordability.¹⁰¹

We acknowledge that there are several factors that must be considered when designing a rate recovery proposal, including the concepts of gradualism and affordability. We emphasize, however, that while affordability is permitted to be considered, it is but one of many factors to be considered and weighed by the Commission in determining the utility's rates. The rate increase reflects the business challenges the Company currently faces, including required investments in the repair/replacement or improvement of its distribution systems, including newly acquired

⁹⁸ See, e.g., *Pa. PUC, et al. v. PPL Electric Utilities Corporation*, Docket Nos. R-2015-2469275 *et al.* (Recommended Decision issued October 5, 2015) at 32-33.

⁹⁹ See 66 Pa. C.S. §§ 523, 526(a).

¹⁰⁰ See *Lloyd*, 904 A.2d at 1020 (explaining that gradualism is the principle under which utility rates are gradually increased in order to avoid rate shock, as part of what is overall considered a reasonable rate under the circumstances and is permitted in implementing large rate increases).

¹⁰¹ See *Pa. PUC et. al v. Twin Lakes Utilities, Inc.*, Docket No. R-2019-3010958 (Order entered March 26, 2020) at 48, 80 (the ALJ did not err in considering evidence relating to the various quality of service and rate affordability issues in the proceeding and factoring in such evidence as part of her overall determination on which expert witnesses' cost of equity to adopt for setting just and reasonable rates).

water and wastewater distribution systems; and the high costs associated with maintaining a distribution system necessary to provide safe and reliable water and wastewater service within the Commonwealth.

As discussed, *supra*, Aqua's proposal, establishing an Act 11 subsidy close to one-third of the wastewater revenue requirement would result in wastewater rates that do not bear a reasonable relationship to the Company's cost of serving those customers. In consideration of Aqua's recent Section 1329 acquisitions and the consequences of the Company's request to have water customers subsidize rate increases for customers in wastewater Rate Zones 1 through 6, as well as to absorb a significant portion of the revenue shortfalls of the newly acquired wastewater systems, Rate Zones 7 through 11, we find I&E's approach in limiting the Act 11 subsidies¹⁰² and its subsequent rate design proposals, adopted by the ALJ, to be a reasonable compromise between the conflicting objectives of moving towards consolidated rates and maintaining gradualism in customer bill impacts.

Table 15, below, provides a comparison of residential wastewater bills for a typical residential customer under the Company's proposed rates and under I&E's proposal. Under Aqua's proposed rates, residential wastewater customers would see increases ranging from 7.9% to 84.9%, with Rate Zone 5 – Newlin Green experiencing a proposed decrease. Under I&E's proposed rates, residential wastewater customers would see increases ranging from 20.3% to 86.0%, excluding the increase to Rate Zone 10 – Whitpain, where the average residential customer will experience an increase of approximately 106.6%. As I&E noted, this larger than average increase is

¹⁰² I&E's approach for allocating wastewater revenue and designing wastewater rates allows for each type of utility service to recover as much of the cost of providing services as possible without removing the Act 11 subsidy, which would result in unreasonably large increases to the monthly customer charges, usage rates, unmetered rates, and average bills for both residential and commercial wastewater customers.

justified for three reasons: (1) the average bill under current rates of \$31.66 per month is the lowest average bill for all zones; therefore, to move the average bill closer to other average bills, a larger percentage increase is necessary; (2) the Company's desire to consolidate all Zone 10 rates justifies the higher rates for Zone 10 – Whitpain to match Zone 10 – East Norriton rates; and (3) even with higher rates causing a higher than average increase for Zone 10 – Whitpain, total Rate Zone 10 operations will continue to need \$1,378,735 of subsidy from water customers. *See* I&E St. 5 at 52-53.

Wastewater Division
Bill Comparison of 5/8" Metered Residential Customers with Average Usage*

	Average Current Monthly Bill	Aqua Proposal		I&E Proposal	
		Monthly Bill	% Increase	Monthly Bill	% Increase
RZ 1 - Main	\$64.47	\$77.49	20.2%	\$90.12	39.8%
RZ 1A	\$59.01	\$77.49	31.3%	\$90.12	52.7%
RZ 1B	\$64.05	\$77.49	21.0%	\$90.12	40.7%
RZ 2 - Main	\$71.82	\$77.49	7.9%	\$100.32	39.7%
RZ 3 - Main	\$84.00	\$101.03	20.3%	\$109.04	29.8%
RZ 4 - Main	\$105.00	\$125.00	19.0%	\$131.13	24.9%
RZ 5 - Main	\$118.02	\$141.94	20.3%	\$141.94	20.3%
RZ 5 - Newlin Green	\$147.00	\$141.94	-3.4%	\$141.94	-3.4%
RZ 6 - Masthope	\$45.82	\$55.15	20.4%	\$66.60	45.4%
<u>Zones Recently Acquired</u>					
RZ 7 - Limerick	\$39.73	\$72.94	83.6%	\$73.90	86.0%
RZ 8 - East Bradford (Multifamily Residential)	\$55.36	\$83.42	50.7%	\$99.80	80.3%
RZ 9 - Cheltenham	\$36.53	\$49.34	35.1%	\$57.20	56.6%
RZ 10 - East Norriton	\$38.52	\$58.53	51.9%	\$65.40	69.8%
RZ 10 - Whitpain	\$31.66	\$58.53	84.9%	\$65.40	106.6%
RZ 11 - New Garden	\$73.03	\$100.34	37.4%	\$130.99	79.4%

* Average 5/8" residential customer using 4,000 gallons per month.

Table 15: Comparison of residential wastewater bills for a typical residential customer under the Company's proposed rates and under I&E's proposal. *See Aqua Exh. 5-B, Part II, Sch. WW-7; see also, I&E Exh. 5, Sch. 2 at 2-4, Sch. 3 at 2, Sch. 4 at 2 and 4, Sch. 5 at 2, Sch. 6 at 2 and 4, Sch. 7 at 2-3; I&E Exh. 5-R, Sch. 2 at 2.*

Furthermore, since the average bill under current rates is lower in Rate Zones 1 and 6 than it is for Rate Zones 2 through 5, it is reasonable that Rate Zones 1 and 6 would experience larger percentage increases compared to Rate Zones 2 through 5. Since the Company presented one cost of service study for Rate Zones 1 through 6, there is no justification for such a wide variety in rates and corresponding average bills.

The overall bill impact to a typical residential water customer bill would be overall less than the Company's proposal,¹⁰³ since I&E's recommended water rate design changes are based upon its proposal to reduce the Act 11 subsidy from water customers. In this regard, a bill for a typical residential water customer would reflect I&E's recommendation that the Company's water rates be scaled back to 20% of the Company's original proposed percentage increases, and that the recommended scale back, including customer charges, be proportional to the percentage increase originally proposed by the Company. *See* I&E M.B. at 73; I&E St. 4 at 18-20.

Moreover, the higher percentage increases to a typical residential customer bill recommended by I&E's rate design for Rate Zones 7 through 11 are indicative of the substantial revenue shortfall attributable to these newly acquired systems, even under the Company's proposed rates. Without the, albeit, more moderate Act 11 subsidy proposed by I&E, compared to Aqua's proposal, these wastewater rates would necessarily have to be increased even further. As such, we find I&E's rate design reasonably mitigates the impact of revenue increases onto these wastewater customers by recovering a portion of the Company's wastewater revenue requirement from its total water and wastewater customer base.

The OCA also excepts to the ALJ's recommendation, arguing that Aqua's proposed customer charges are based on its flawed cost of service study results, violate the principle of gradualism, and would result in a disincentive for customers to engage in conservation activities. Therefore, the OCA's wastewater rate design recommendations include its contention that there is no cost justification for increasing the present \$31.00

¹⁰³ Under the Company's proposal, a residential customer in the Main Division of Rate Zone 1, using 4,000 gallons of water per month, would experience a monthly bill increase from \$69.35 to \$81.32, or 17.3% per month, and residential customers in other water divisions would experience increases ranging from 17.3% to 51.3%. *See* Aqua Exh. 5-A, Part II, Sch. 8.

per month 5/8" residential customer charge in Rate Zone 1. Upon our consideration of the evidence and record herein, we conclude that the ALJ correctly recommended that, consistent with the *Aqua 2004 Order*, and subsequently affirmed in the *2012 PPL Order*, other customer-related costs are properly includable in a customer cost analysis. We find that the OCA proposed limitation of costs excludes customer costs that should be included in a customer charge and is unreasonably narrow.

As previously indicated, although the ALJ accepted Aqua's water and wastewater residential customer cost analyses upon which it based its proposed increases to customer charges, the ALJ adopted I&E's proposed rate design which includes the wastewater customer charges summarized in Table 16, below.

Further, we are persuaded by I&E's reasoning for its increase to the 5/8" residential customer charge for Rate Zone 1:

While I normally would support not increasing the monthly 5/8th inch residential customer charge based upon cost, there are other factors to consider in this case. First, the present \$31.00 per month customer charge is below the monthly customer charges in Zones 3 through 5. Therefore, in order to move towards consolidation of the customer charges in these zones, the present Zone 1 customer charge of \$31.00 per month should be increased. Customer charges should be consolidated in Zones 1 through 6 for fairness and simplicity. Second, the remaining revenue increase will have to come from increasing the usage charge. Therefore, given this low customer charge, I recommend that the OCA proposal be rejected.

I&E St. 5-R at 5-6. Additionally, as I&E indicated, the OCA did not address the remaining meter sizes in Rate Zone 1, the other classes in Rate Zone 1, or the other customer charges in Rate Zones 2 through 6.

Wastewater Division
Comparison of 5/8" Metered Residential Customer Charges

	Current	Aqua Proposal		I&E Proposal	
	Customer Charge	Customer Charge	% Increase	Customer Charge	% Increase
RZ1 - Main	\$31.00	\$39.10	26.1%	\$45.50	46.8%
RZ1A	\$31.00	\$39.10	26.1%	\$45.50	46.8%
RZ1B	\$31.00	\$39.10	26.1%	\$45.50	46.8%
RZ2 - Main	\$36.00	\$39.10	8.6%	\$52.80	46.7%
RZ3 - Main	\$46.00	\$58.09	26.3%	\$62.70	36.3%
RZ4 - Main	\$62.00	\$77.50	25.0%	\$81.30	31.1%
RZ5 - Main	\$74.00	\$93.45	26.3%	\$93.45	26.3%
RZ5 - Newlin Green	\$110.00	\$93.45	-15.0%	\$93.45	-15.0%
RZ6 - Masthope	\$39.64	\$50.10	20.4%	\$56.20	41.8%
<u>Zones Recently Acquired</u>					
RZ7 - Limerick	\$28.10	\$39.48	40.5%	\$39.50	40.6%
RZ8 - East Bradford (Multi-Family Residential)	Current Flat Rate	\$39.10		\$55.00	
RZ9 - Cheltenham	\$20.89	\$28.21	35.0%	\$30.00	43.6%
RZ10 - East Norriton	\$21.08	\$32.37	53.6%	\$35.00	66.0%
RZ10 - Whitpain	\$31.66	\$32.37	2.2%	\$35.00	10.5%
RZ11 - New Garden	\$37.64	\$51.71	37.4%	\$43.00	14.2%

Table 16: Comparison of 5/8" metered residential wastewater customer charges. *See* I&E Exh. 5, Schs. 2-7 at 1; I&E Exh. 5-R, Sch. 2 at 1.

With regard to the concerns expressed by the OCA that the Company's proposed customer charges will discourage conservation, we note that the customer charges, shown above, in the context of the total monthly bill for a typical 5/8" meter residential wastewater customer, would comprise approximately 47% to 91% of the charges on the bill under the Company's proposal and only approximately 33% $[(\$43.00 \div \$130.99) \times 100 = 33\%]$ to 84% $[(\$56.20 \div \$66.60) \times 100 = 84\%]$ under I&E's wastewater rate design proposal. This is less than the portion of a typical bill for a 5/8" meter wastewater residential customer under current rates, of which approximately 48% to 87% is attributable to the customer charge, as shown in Table 17 below:

Wastewater Division**Comparison of the Portion of a Customer's Bill Attributable to the Customer Charge**

	<u>Current Rates</u>	<u>Aqua Proposed Rates</u>	<u>I&E Proposed Rates</u>
RZ 1 - Main	48%	50%	50%
RZ 1A	53%	50%	50%
RZ 1B	48%	50%	50%
RZ 2 - Main	50%	50%	53%
RZ 3 - Main	55%	57%	58%
RZ 4 - Main	59%	62%	62%
RZ 5 - Main	63%	66%	66%
RZ 5 - Newlin Green	75%	66%	66%
RZ 6 - Masthope	87%	91%	84%
<u>Zones Recently Acquired</u>			
RZ 7 - Limerick	71%	54%	53%
RZ 8 - East Bradford (Multifamily Residential)	100%*	47%	55%
RZ 9 - Cheltenham	57%	57%	52%
RZ 10 - East Norriton	55%	55%	54%
RZ 10 - Whitpain	100%*	55%	54%
RZ 11 - New Garden	52%	52%	33%

*Average use customers, using 4,000 gallons per month, are currently billed a flat rate.

Table 17: Comparison of the portion of a customer's wastewater bill attributable to the customer charge.

Regarding the Company's water rate design proposal, the portion of charges attributable to the customer charge on a typical 5/8" meter water residential customer would range from approximately 21.6% [$(\$4.90 \div \$22.66) \times 100 = 21.6\%$] for customers in the Phoenixville Division to 39.8% [$(\$32.40 \div \$81.32) \times 100 = 39.8\%$] for customers in Rate Zone 3 – Main. Reflective of I&E's effort to reduce the Act 11 subsidy, with which we agree, I&E's proposal simply scales back the Company's proposed percentage increases for water customers to 20% of the Company's original

proposal. Therefore, we find that I&E's proposal reasonably balances the principles of gradualism with the challenges of rate consolidation, especially those that come with newly acquired systems, while preserving adequate opportunity for customer savings due to conservation efforts. As such, we find no basis to reverse the ALJ's recommendation. Accordingly, OCA Exception Nos. 12 and 13 are denied.

b. Unmetered Residential Wastewater Rates

Aqua explained that similar to many wastewater systems throughout the Commonwealth, Aqua does serve a limited number of areas where wastewater customers are billed on a flat rate, meaning that unmetered customers receiving wastewater service from Aqua pay the same amount each month, *i.e.*, their water consumption does not have an effect on their monthly wastewater bills. Unmetered, flat-rate wastewater customers make up the communities of Tobyhanna, Pennsylvania (730 customers) and Lake Harmony, Pennsylvania (995 customers).¹⁰⁴ These communities were billed on a flat rate prior to Aqua's acquisition of these wastewater systems, and the Company has continued to bill the customers on a flat-rate basis. Aqua St. 9-R at 28.

There is no question that volumetric billing is preferable to flat-rate billing, as it provides better price signals and promotes conservation, as well as resulting in a more equitable distribution of the variable costs of wastewater service among ratepayers. However, in situations, such as this, where metered water information is unavailable, we acknowledge the standard industry practice of basing the flat rate on a system-wide average usage per month plus a customer charge. As indicated previously, Aqua assumes an average 5/8" meter residential customer uses 4,000 gallons per month.

¹⁰⁴ Customers in Tobyhanna and Lake Harmony obtain their water supplies from individual wells not owned or operated by a utility or a municipality/municipal authority. Aqua St. 9-R at 28.

The flat charge should be reasonable and appropriate, and sufficient to cover the intended costs. The challenge is the development of a reasonable flat-rate charge. In this regard, we cannot ignore the disparity in the rates charged to metered and unmetered customers in certain divisions where Aqua serves both types of customers, as illustrated by the OCA. For these reasons, we agree with the ALJ's recommendation that directs Aqua to study and report the results in the next base rate proceeding, in order to determine whether different methods of calculating a flat rate would be more reasonable for some systems rather than applying a system-wide average to each system. Accordingly, Aqua Exception No. 10 is denied.

The primary concern at the public input hearings voiced by customers receiving wastewater service in the Tobyhanna and Lake Harmony service areas, including Mr. Osinski, was that flat-rate billing is unfair to customers with below average usage, including customers who may be part-time residents that may use less than full-time residents. *See* Tr. at 70-71, 166-68, 175-81, and 323-25. Recognizing that customers in Lake Harmony have private water wells on their property that are not individually metered, the OCA proposed a pilot program in Lake Harmony to install meters: (1) on an opt-in basis for those customers that request metered wastewater service, (2) on other customer-owned wells based upon a random sample of 10% to 20% of the unmetered customers. *See* OCA St. 4 SUPP. at 2.

Although we find merit in the OCA's proposal that Aqua study whether a different method of calculating a flat rate would be more reasonable for some systems than applying a system-wide average, we cannot say the same for its Lake Harmony pilot program proposal. Instead, we find persuasive the testimony of Aqua's witness, Ms. Heppenstall, explaining the impracticability of the OCA's proposal:

I disagree for two reasons. One, the Company does not have the authority to meter a representative sampling of customer owned private wells. Allowing customers to opt in would

only incentivize those customers with low water consumption, not the perceived larger users. Second, there are concerns about the ability to access customers' property to properly install a meter on a well. I understand that Company Witness Todd Duerr will explain the operational issues with this pilot program in his rebuttal testimony ([Aqua St. 9-R]). There may be substantial cost involved, and Mr. Watkins' proposal is that the Company bear the cost of such installations. Finally, the lack of authority to meter all privately owned wells means that the "pilot" can never be adopted as a permanent solution. Customers would continually opt for the lesser cost alternative. Mr. Watkins' proposal is unworkable.

Aqua St. 5-R at 17-18. We also find it difficult to ignore the operational issues with the OCA's proposal, highlighted by Aqua's witness, Mr. Duerr:

First, we reinforce that industrywide flat sewer rates have been utilized to bill for public or private wastewater service in instances where customers have private wells throughout the Commonwealth. While we understand the customer's desire to limit any rate increase, resorting to changing the current methodology on which these customers are billed will not impact that reality, and in fact, some customers could be billed more. For wastewater only customers that receive water from private wells, the Company would be required to enter, traverse, and locate a customer's water well, to a property the Company does not have a right to enter, install a Company owned meter somewhere on a customer's property where a water well is located, and maintain that property going forward. That in and of itself is problematic.

Aqua St. 9-R at 29-30.

Regarding Mr. Osinski's assertion that the well servicing his community is metered, Mr. Duerr explained that "the well, the water meter, and the water distribution system are owned by the community. There are not individual meters measuring usage to

each customer's residence. As such, the Company cannot bill these individual customers based on usage from one community water meter." Aqua St. 9-R at 30-31.

Based upon our review of the record evidence, we agree with the recommendation of the ALJ that the OCA's proposal be rejected, as it is not clear that the cost of the OCA's proposed pilot will achieve overall benefits to Aqua's customers that will outweigh the costs. The OCA does not explain: (1) Aqua's authority to place a meter on a person's water line; (2) how higher-usage customers could be "incentivized" to opt-in in the future; nor (3) why wastewater cost of service should be increased to cover the cost of installing, maintaining, and reading water meters for wastewater service. As such, we find no basis to reverse the ALJ's recommendation. Accordingly, OCA Exception No. 14 and Mr. Osinski's Exceptions are denied.

With regard to the OCA's argument that the Company be required to study the feasibility of opening an irrigation or deduct metering program to Aqua's non-Cheltenham customers and file the results of the study no later than the Company's next base rate case, we agree with the ALJ that the OCA has not demonstrated that further study would yield better results. Aqua noted that further studies are not necessary because the results will be similar to the analysis presented by the Company in the instant base rate case. Further, Aqua noted that the installation of a meter to measure usage deductions will increase the revenue requirement and not reduce the revenue requirement subject to recovery. Aqua M.B. at 244-45. Moreover, beyond arguing that it is unaware if the Company has conducted any studies on irrigation metering, the OCA has not sufficiently demonstrated why the Company should be required to conduct an irrigation metering study at this time. Accordingly, we find the OCA's argument that the Commission require the Company to conduct an irrigation metering program study to be unpersuasive.

To the extent that the OCA contends that the ALJ did not sufficiently acknowledge the OCA's irrigation water meter study, we note that the ALJ was aware of the positions and arguments put forth by the OCA, including the studies recommended by the OCA; however, it is up to the ALJ to determine whether, and to what extent, further discussion and analysis is warranted. See 52 Pa. Code §§ 5.403, 5.404. Here, it appears that the ALJ did not believe that further consideration of these matters was necessary to agree with Aqua that no further study is necessary. Accordingly, we will deny OCA Exception No. 15.

E. Tariff Structure - Proposed Reconcilable Rider Mechanisms

1. Energy Cost Adjustment Mechanism (ECAM) and Purchased Water Adjustment Clause (PWAC)

In this proceeding, Aqua proposed two new reconcilable rider mechanisms in its Tariff Water No. 3 to recover the costs associated with its energy and purchased water costs. These riders are the Energy Cost Adjustment Mechanism (ECAM) and the Purchased Water Adjustment Clause (PWAC) which are described in more detail, below. Inasmuch as the Exceptions address the ECAM and PWAC in combination, we shall address the merits of the Exceptions on these two items in a single consolidated disposition at the end of this section.

a. ECAM

(1) Positions of the Parties

Aqua proposed to implement the ECAM in its Tariff Water No. 3 (Tariff Water No. 3, Original Pages 35-36) to ensure that it will recover all of the energy costs it purchases from natural gas and electric providers. Aqua St. 4 at 5; R.D. at 99. According

to the Company, the ECAM addresses both increases and decreases in the energy rates charged by energy suppliers from whom the Company purchases natural gas and electricity. *Id.* The Company provided the following explanation on how it proposes to implement the ECAM:

The mechanism would collect or refund any difference between the energy costs included in base rates from the Company's last rate filing and the actual energy costs incurred in the period of calculation. Within 60 days after the end of each calendar year, the Company would file a reconciliation of its actual costs to the amount recovered in base rates per actual thousand gallons sold as established in the last rate case. Any increase or decrease in these costs would be divided by the projected normalized volumes increased for growth to develop a volumetric surcharge/surcredit applied to metered customers in the following 12-month period. In this way, the Company is protected from uncontrollable increases in costs and customers will receive the benefit of decreases if those costs are less than those included in rates. The ECAM is included as a rider in the proposed tariff submitted with this filing and describes the mechanics of the clause. At the end of a 12-month period, the amount refunded/collected via the mechanism would be compared to the actual costs to be refunded/collected and the difference would be added or subtracted to the difference to be recovered/refunded in the following period.

Aqua St. 4 at 6; Aqua M.B. at 255-256.

The Company is of the opinion that the ECAM and PWAC are authorized under Section 1307 of the Code and, thus, qualify as an exception to the general prohibition of single-issue ratemaking.¹⁰⁵ The Company argued that the ECAM is similar

¹⁰⁵ In this case, as discussed below, the statutory advocates argued that the ECAM would constitute "single-issue ratemaking" because, if the ECAM were approved, the Company would be permitted "to automatically change customers' prices (rates) due to changes in single cost components." OCA St. 4 at 24.

to where other utilities are permitted to pass certain costs through a rider or surcharge as authorized by Section 1307 of the Code. Aqua St. 4-R at 2. The Company proposed that the same safeguards it proposed for its PWAC also apply to its ECAM, with the exception of the 3% billing cap. Aqua M.B. at 256, n.93. According to the Company, the Commission has approved similar clauses (*i.e.*, such as the State Tax Adjustment Surcharge (STAS) and the implementation of the reduced tax associated with the federal Tax Cuts and Jobs Act of 2017 (TCJA)) in circumstances where the costs are volatile, unpredictable, or significant. Aqua submitted that, if the PWAC is approved, its incentive to reduce operating costs will remain an important tenant of its regulatory compact with customers and regulators in the delivery of safe, adequate, and reliable utility service. Aqua St. 4 at 6; Aqua St. 4-R at 3. Similarly, the Company submitted that if the PWAC is approved, it would have ample incentive to take advantage of every reasonable opportunity to prevent increases and pursue decreases in its purchased water cost to the benefit of its customers. Aqua St. 4 at 5; Aqua St. 4-R at 3. In response to opponents who believe the ECAM and PWAC would discriminate in favor of competitive rate rider (CRR) customers and against all other customers because the proposed riders would not apply to CRR customers even though these customers are served, at least in part, with purchased water, the Company averred that the exclusion of contract customers from the operation of surcharges is not unduly discriminatory because the Commission has approved various surcharge provisions that exempt negotiated contract rate customers. Aqua St. 4-R at 4. The Company explained that CRR customers' contract prices would not change based on increases/decreases in the cost of purchased water or energy regardless of whether those changes are implemented through the PWAC or the ECAM or through changes in base rates. *Id.*

I&E, the OCA, and the OSBA each opposed the use of the proposed mechanisms for the recovery of energy expenses. R.D. at 100. According to I&E: (1) it is not appropriate to use a reconcilable rider such as the ECAM to recover O&M expenses because the energy expenses to be recovered via the ECAM are a minimal

portion of routine O&M expenses for which the Commission must undertake a substantive audit and implementation task if it is approved;¹⁰⁶ (2) contrary to the Company's opinion, the ECAM would reduce the incentive for the Company to minimize its energy usage and minimize costs via shopping/negotiating for lower rates;¹⁰⁷ (3) Aqua failed to clearly explain how its claim for recovery of a routine operating expense through the ECAM mechanism would be appropriate;¹⁰⁸ (4) Aqua ignores the fact that the other utilities, to which it referred in direct testimony, are energy companies and those energy costs are pass-through gas and electric commodity costs, not expenses for energy consumed by those utilities during routine operations;¹⁰⁹ (5) the proposed ECAM is discriminatory because it would only apply to tariff rate customers and not rider rate customers;¹¹⁰ (6) the Company has not shown that implementing the ECAM will result in the filing of fewer rate cases as it claimed, because the energy cost expense is not significantly volatile; nor is it a large enough expense to represent an extraordinary impact to the Company's operational output;¹¹¹ (7) the ECAM will only apply to the Water Tariff, which is problematic because the Company either will inappropriately use the Water Tariff to reconcile wastewater expenses, or the Company will simply treat water and wastewater customers unequally (I&E St. 1 at 53); and (8) the Company's arguments that it reports earnings on a quarterly basis does not negate the single-issue ratemaking nature of the ECAM because the proposed surcharge would benefit Aqua by increasing revenue in lockstep with expense increases for specific individual expenses while circumventing the normal rate case process in which the full examination of all expenses and revenues would be evaluated simultaneously. I&E St. 3-SR at 10-11.

¹⁰⁶ I&E St. 1 at 52-53; I&E St. 1-SR at 3; I&E St. 1-SR at 67.

¹⁰⁷ I&E St. 1 at 51; I&E St. 1-SR at 61.

¹⁰⁸ See I&E St. 3-SR at 9-13.

¹⁰⁹ I&E St. 1 at 51-52; I&E St. 1-SR at 65.

¹¹⁰ I&E St. 3 at 23-24; I&E St. 3-SR at 11-13.

¹¹¹ I&E St. 3 at 22-23; I&E St. 3-SR at 9-13.

The OCA echoed I&E's arguments and emphasized that Aqua's ECAM proposal amounts to single-issue ratemaking. OCA St. 4 at 24-25. The OCA submitted that the costs to be recovered through the ECAM do not warrant special recovery separate and apart from other costs recovered through base rates. OCA St. 4 at 25. The OCA notes that Aqua has exercised some control of purchased energy costs through its selection of suppliers (*See* Aqua Exh. 1-A, Schs. C-6.1.i., C-6.1.ii.) and has already captured the potential for future changes in purchased water and energy costs as part of its adjustments to its FPFTY claims. OCA St. 4 at 25; *see* Aqua Exh. 1-A, Schs. 6.1, 7.1.

The OSBA also agreed with I&E and the OCA that since the ECAM would make the Company whole for all energy cost increases between base rate proceedings, the ECAM would constitute single-issue ratemaking. OSBA M.B. at 6. The OSBA submitted that recovery of energy costs through the ECAM is unreasonable because the Company would have no incentive to control its energy usage or costs because they would automatically be passed onto customers. OSBA St. 1 at 22. The OSBA further noted that the ECAM would insulate the Company from fluctuating energy costs, thereby lowering Aqua's business risk, which should result in a lower ROE for Aqua. *Id.* However, the OSBA indicated that the Company made no such proposal, and that by lowering Aqua's business risk, while not lowering the Company's ROE, the Company's shareholders are the entities that would most benefit from the ECAM proposal. OSBA St. 1 at 22. According to the OSBA, the only way ratepayers would benefit from ECAM is if energy costs decrease between base rate proceedings; but given the economic challenges due to rising energy costs as well as the ongoing impact of the COVID-19 pandemic, the OSBA urged the Commission to incentivize Aqua to aggressively control its energy costs by rejecting the ECAM proposal. OSBA M.B. at 6.

Aqua LUG agreed with the statutory advocates' arguments that the ECAM is nothing more than an unjust and unreasonable attempt at single-issue ratemaking that should be rejected by the Commission. In addition, the Aqua LUG argued that Aqua's

circumstances with relation to its purchased water and energy expenses simply do not warrant the implementation of an automatic recovery mechanism, as the costs to Aqua for its purchases of water supplies do not constitute significant expenses that require adjustments between base rate cases. Aqua LUG M.B. at 5-6.

(2) Recommended Decision

The ALJ agreed with the statutory advocates and recommended that the ECAM for the recovery of energy costs be rejected. The ALJ found that Aqua is a large company with considerable buying power and there is no reason to believe that it cannot adequately control its energy costs through normal cost control mechanisms. R.D. at 101-02. The ALJ further found that incentivizing cost containment by including energy costs in base rates is more effective than relying on the notion of a “regulatory compact with customers and ratepayers in the delivery of safe, adequate, and reliable utility service.” *Id.* (citing Aqua St. 4 at 6). The ALJ noted that in the current economic climate, energy costs are not likely to decline, and this would be the only scenario where ratepayers would benefit from permitting the recovery of costs through a rider rather than through base rates. R.D. at 102.

The ALJ also agreed with the advocates that the ECAM equates to single-issue ratemaking. R.D. at 102. In support of this determination, the ALJ cited to a prior case involving a Collection System Improvement Charge (CSIC) rider in which the Pennsylvania Commonwealth Court declared that “single-issue rate making is prohibited if it impacts on a matter considered in a base rate case.”¹¹² R.D. at 102 (citing *CSIC Order*). In *CSIC Order*, the Court ruled that “[t]he ‘cursory’ review undertaken for a

¹¹² *Popowsky v. Pa. PUC*, 869 A.2d 1144, 1152 (Pa. Cmwlth. 2005) (*CSIC Order*), appeal denied, 895 A.2d 552 (Pa. 2006) (citing *Phila. Elec. Co. v. Pa. PUC*, 502 A.2d 722, 727-28 (Pa. Cmwlth. 1985) (*PECO 1985*) and overturning Commission’s grant of a wastewater utility’s request to implement a CSIC).

surcharge is not a substitute for the review undertaken in a base rate case to determine whether a rate is just and reasonable.” R.D. at 102 (quoting *CSIC Order*, 869 A.2d at 1157). Thus, the ALJ ruled that “[i]t is inappropriate to single out this cost for rate recovery without recognizing other possibly offsetting changes in costs and revenues that could ordinarily be thoroughly examined in a base rate proceeding, as Aqua’s claims of expenses and offsetting savings and revenues are being examined in the instant case.” R.D. at 102. The ALJ explained that to do so would violate the ratemaking principle of matching revenues, expenses, return and rate base. R.D. at 102 (citing OCA St. 3 at 15-16).

The ALJ concluded her recommendation with regard to the ECAM by noting that the financial risk of greater energy bills serves as an incentive to Aqua to seek methods to reduce its energy costs, whether through shopping for competitive suppliers or implementing other cost-saving conservation measures. R.D. at 102.

b. PWAC

(1) Positions of the Parties

Aqua proposed to implement the PWAC in its Tariff Water No. 3 (Tariff Water No. 3, Original Pages 37-38) that would enable the Company to recover the costs of water it purchases for resale from non-affiliated suppliers. Aqua St. 4 at 2. According to the Company, the rider addresses both increases and decreases in the price it pays for purchased water. *Id.* at 2-3. If rates are increased, the Company cannot recover those costs until the next rate case is filed; if rates are decreased, the customer must wait until the next rate case to benefit from that reduced cost. *Id.* at 3. Additionally, the Company proposed to include a 3% cap to its proposed PWAC as well as an audit and reconciliation process to protect its customers from unjust and unreasonable rates. *Id.*

The Company provided the following explanation on how it proposes to implement the PWAC:

The PWA[C] would adjust customers' bills by adding a charge or credit to reflect increases or decreases, respectively, in the Company's "Baseline Cost." The Baseline Cost is the annual purchased water costs approved as an operating expense in the Company's last base rate case. When one or more of the Company's suppliers change the rates for water purchased by the Company, the Company will re-compute its annual purchased water costs based on the level of consumption and other billing determinants that formed the basis for the Company's calculation of its Baseline Cost. If there is a change in purchased water costs above or below the Baseline Cost, a charge or credit, as applicable, would be added to customers' bills. More precisely, the PWA[C] provides the Company the ability to implement a charge to recover an increase in purchased water costs above the Baseline Cost or a credit to pass back savings from a decrease in purchased water costs below the Baseline Cost.

Aqua St. 4 at 3-4; Aqua M.B. at 248-49.

As noted, Aqua proposed the PWAC to address both increases and decreases in the rates charged by non-affiliated suppliers from whom the Company purchases water. R.D. at 102 (citing Aqua St. 4 at 2); Aqua Tariff Water-PA P.U.C. No. 3 at 37-38. Aqua's PWAC proposal relies, in part, on the Commission's prior approval of a similar recovery mechanism for Newtown Artesian Water Company in 2010.¹¹³ The Company noted that the PWAC for Newtown Artesian Water Company contained safeguards, and that it has proposed those same safeguards for the PWAC in this proceeding. *See* Aqua M.B. at 249, n. 88, which delineates the four safeguards.

¹¹³ *Pa. PUC v. Newtown Artesian Water Co.*, Docket No. R-2009-2117550 (Order entered April 15, 2010) (*Newtown Artesian Water*) at 6-17 affirmed by *Popowsky v. Pa. PUC*, 13 A.3d 583 (Pa. Cmwlth. 2011) (*Popowsky 2011*).

The statutory advocates have raised most of the same arguments against the PWAC that they made against the ECAM. R.D. at 103. As with the ECAM, I&E argued that the PWAC is discriminatory and that Aqua has not provided a convincing reason for treating purchased water expenses as anything other than an O&M expense which should be recovered in base rates. *Id.* (citing I&E St. 3 at 14). I&E asserted that the Company's request to use the PWAC to recover future increases in purchased water through a reconcilable surcharge is an unreasonable exception to the normal rate making treatment for purchased water expense and would violate the principle of "single issue ratemaking." *Id.* Aqua M.B. at 250. I&E submitted that in the past, the Commission only granted surcharge treatment when a utility has demonstrated that the expense in question was volatile or unpredictable and the level of the expense is significant when compared to total O&M expenses including depreciation expense. *Id.* However, in this case, I&E asserted that Aqua failed to present sufficient evidence that its purchased water expense is volatile, unpredictable, or significant.¹¹⁴

The OCA added that purchased water costs are known and are subject to agreements with the provider. OCA St. 4 at 25. Since Aqua has voluntarily entered into its contracts to purchase water with various entities, the OCA contended that those costs are not entirely beyond its control.¹¹⁵

The OSBA observed that like the ECAM, allowing Aqua to use the adjustment clause would not incentivize the Company to control its purchased water costs and the only way that ratepayers would benefit would be if purchased water costs declined between rate cases. OSBA St. 1 at 25. In addition, the OSBA's witness, Mr. Kalcic, argued that the PWAC was biased in favor of shareholders and would

¹¹⁴ See I&E St. 3 at 11-19 and I&E St. 3-SR at 7-8 for a full discussion of the PWAC issue.

¹¹⁵ See, e.g., Aqua Exh. 1-A, Sch. C-7.1.i. Also, see OCA St. 4 at 24-25 for a full discussion of the OCA's position on the ECAM and PWAC.

insulate Aqua's earnings. OSBA St. 1 at 22-25. Finally, the OSBA asserted that PWAC is unnecessary because the Company's purchased water costs are \$4.5 million, whereas Aqua's claimed water cost of service is \$575.03 million. Purchased water costs are only 0.7% of the Company's total costs. Any changes in water costs will have a minimal impact on Aqua's earnings. OSBA St. 1 at 24.

(2) Recommended Decision

The ALJ recommended that Aqua's proposed PWAC be rejected because Aqua failed to demonstrate that the PWAC is necessary, just, or reasonable. R.D. at 102-04. In reaching her decision, the ALJ relied on the arguments proffered by the statutory advocates which included many of the same arguments made in opposition to the ECAM.

The ALJ initially found that Aqua did not provide any convincing reasons why purchased water expenses should be treated as anything other than an O&M expense that are recoverable in base rates. R.D. at 103. The ALJ agreed with I&E that the Company's request for an exception to the normal ratemaking treatment for purchased water expense through a reconcilable surcharge is unreasonable based on past policy where the Commission only granted surcharge treatment when it had been demonstrated that the expense in question was volatile or unpredictable, and the level of the expense was significant when compared to total O&M expenses, including depreciation expense. R.D. at 103 (citing I&E St. 3 at 14). The ALJ found that Aqua did not present any such evidence related to its purchased water expense. R.D. at 103 (citing I&E St. 3 at 11-19; I&E St. 3-SR at 7-8).

Next, the ALJ concluded that Aqua's purchased water costs are not entirely beyond its control in that Aqua's purchased water costs are known costs because they are subject to agreements with the provider. R.D. at 103 (citing Aqua Exh. 1-A,

Sch. C-7.1.i). The ALJ also concluded that permitting Aqua to use the PWAC would not incentivize the Company to control its purchased water costs and the only way that ratepayers would benefit would be if purchased water costs declined between rate cases. R.D. at 103. The ALJ further found that the PWAC is not necessary because any changes in water costs will have minimal impact on Aqua's earnings since the Company's purchased water cost of \$4.5 million is only 0.7% of its total claimed water cost of service of \$570.03 million. R.D. at 104 (citing OSBA St. 1 at 24).

Finally, the ALJ ruled that Aqua's reliance on *Newtown Artesian Water* is misplaced. R.D. at 104. In support of her judgment, the ALJ explained:

At the time of its request, Newtown purchased nearly 60% of its water from other sources. [*Newtown Artesian Water* at 3] Its purchased water expense represented about 25% of its annual revenues and 34% of its O&M expenses for the same period. [*Newtown Artesian Water* at 3; *see also* I&E St. 3 at 18-19; I&E Exh. 3, Sch. 3 at 1-2] In stark contrast, Aqua's projected purchased water costs will amount to only about 0.7% of its total water cost of service. [OCA St. 4 at 25] Aqua is not a small utility where purchased water or energy costs constitute a significant portion of its cost of service. Aqua's costs are not so significant such that they would cause its overall cost of service to vary widely from authorized revenues as a result of suppliers' price changes. Similar to ECAM, the financial risk of greater purchased water bills serves as an incentive to Aqua to seek methods to reduce its purchased water costs, whether through shopping for competitive suppliers, supplying more of its own water, reducing water losses, or implementing other cost-saving conservation measures. Aqua has failed to demonstrate that the PWAC is necessary, just or reasonable.

R.D. at 104 (footnote numbers omitted).

c. Aqua Exception No. 11 and Replies

In its Exception No. 11, Aqua disagrees with the conclusions the ALJ reached in support of her recommendations that the proposed ECAM and PWAC be rejected. Aqua Exc. at 35-36; R.D. at 99-104. Those conclusions include: (1) the ECAM and PWAC constitute impermissible single-issue ratemaking (R.D. at 102); (2) the Company failed to demonstrate that it cannot adequately control its energy and purchased water costs through normal mechanisms (R.D. at 101-102; 104); (3) the Company's energy and purchased water costs each do not constitute a significant amount of Aqua's cost of service (*Id.*); and (4) customers are not likely to benefit from the ECAM because energy costs are not, likely to decline in this climate (R.D. at 102). For the reasons discussed below, the Company requests that the above findings be rejected and each of the reconcilable riders be approved.

First, Aqua maintains its position that the two new reconcilable riders should be approved because it has demonstrated that they satisfy the requirements for approval of reconcilable riders under Pennsylvania law and Section 1307(a) of the Code. Aqua Exc. at 36 (citing Aqua M.B. at 245-249; Aqua R.B. at 105-106). Additionally, Aqua submits that because each rider seeks to recover an expense that is easily identifiable and beyond the Company's control, it has adequately demonstrated that the ECAM satisfies the exception to the prohibition against single-issue ratemaking. Aqua Exc. at 36.

The Company also disagrees with the ALJ's finding that energy costs are not likely to decline. The Company contends that the ALJ's statement is an unsupported assertion used to undermine Aqua's otherwise unrebutted testimony that any energy cost savings would be passed through to customers in a timely manner. *Id.*

In view of the above arguments, the Company requests that, for the reasons more fully explained in its Briefs, the Commission reject the ALJ's findings and approve the proposed ECAM. Aqua Exc. at 36 (citing Aqua M.B. at 235-58; Aqua R.B. at 105-07). We refer to the "Positions of the Parties" sections, above, which address the Company's positions with regard to the issues it raised in its Exceptions here concerning these ECAM and PWAC riders.

In its reply, I&E disagrees with the Company that its ECAM and PWAC riders satisfy the requirements under Pennsylvania law and Section 1307(a) of the Code. I&E also submits that Aqua continues to aver, incorrectly, that the proposed reconcilable riders satisfy the well-recognized exception to the prohibition against single-issue ratemaking, and that each rider seeks to recover an expense that is easily identifiable and beyond the Company's control. I&E R. Exc. at 11.

In regard to the ECAM, I&E avers that the ALJ appropriately considered the counter arguments made by the statutory advocates and correctly recommended that the ECAM for the recovery of energy costs should be rejected. I&E R. Exc. at 11 (citing R.D. at 101). I&E agrees with the ALJ's reasoning that because Aqua is a large company with considerable buying power, there is no reason to believe that it cannot adequately control its energy costs through normal cost control mechanisms. In consideration of the above, and the fact that the ALJ concluded that the ECAM would equate to single-issue ratemaking, I&E believes Aqua's Exception should be denied. I&E R. Exc. at 11.

With regard to the PWAC, I&E opines that the ALJ correctly agreed with the statutory advocates by rejecting the PWAC and recommending that Aqua continue to recover its purchased water costs in base rates rather than through the PWAC. I&E R. Exc. at 11 (citing R.D. at 103). I&E agreed with the ALJ that Aqua's purchased water cost, which amounts to only 0.7% of its total water cost of service, is not a significant portion of its total water cost of service. I&E R. Exc. at 11 (citing R.D. at 104). As such,

I&E maintains that Aqua's costs are not so significant that they would cause its overall cost of service to vary widely from authorized revenues due to its suppliers' price changes. *Id.* I&E, therefore, asserts that since Aqua has failed to demonstrate that the PWAC is necessary, just or reasonable, the Commission should reject Aqua's Exception on this matter. I&E R. Exc. at 11-12.

In its reply to Aqua's Exception No. 11, the OCA renders similar arguments to those raised by I&E. OCA R. Exc. at 20-21. The OCA agrees with the ALJ to reject the ECAM because it constitutes single-issue ratemaking, and it is not appropriate to adopt this type of reconcilable rider mechanism because Aqua is adequately able to control its energy costs. OCA R. Exc. at 20 (citing R.D. at 101-02).

The OCA also submits that it supports the ALJ's recommendation to reject the PWAC because the ALJ correctly found that Aqua's reliance on *Newtown Artesian Water* was misplaced. OCA R. Exc. at 20 (citing R.D. at 103 and *Newtown Artesian Water* at 6-17). The OCA references the ALJ's Recommended Decision comparing Newtown with Aqua in which the ALJ stated that Newtown purchased nearly 60% of its water and that Newtown's expense was about 25% of its annual revenues and 34% of its operation and maintenance expenses. In contrast, Aqua's projected purchased water costs are only about 0.7% of its total water cost of service.¹¹⁶ OCA R. Exc. at 20 (citing R.D. at 104; OCA M.B. at 114).

The OCA also requests that the Commission reject Aqua's continued stance in its Exceptions that Section 1307(a) justifies implementing the ECAM and PWAC because Aqua's energy costs and purchased water costs are outside of its control. In this regard, the OCA submits that Aqua's position is unsupported because, as the ALJ found,

¹¹⁶ It is noted that the OCA appears to inadvertently state in its reply that Aqua's projected purchased water costs are about "1.4% of its total water cost of service."

due to the large size of Aqua, which has considerable buying power, there is “no reason to believe that it cannot adequately control its energy costs through normal cost control mechanisms.” OCA R. Exc. at 21 (citing R.D. at 101). Since Aqua has voluntarily entered into contracts to purchase water with various entities, the OCA contends that those are known costs for which Aqua can exercise some control. *Id.* The OCA also notes that Aqua has exercised some control through its selection of electricity suppliers. OCA R. Exc. at 21 (citing OCA R.B. at 69).

The OCA concludes its reply by asserting that the costs at issue in the ECAM and PWAC do not meet the criteria that the Commission and Courts have applied in approving a Section 1307(a) surcharge. OCA R. Exc. at 21 (citing OCA R.B. at 70-71). In this regard, the OCA argues that the associated costs are not extraordinary, substantial, unexpected, or non-recurring. Instead, the OCA opines that such costs represent the normal, ongoing costs of providing water service that are such a small percentage of Aqua’s overall cost of service that any fluctuations will have minimal impact. OCA R. Exc. at 21.

In its reply to Aqua’s Exception No. 11, the OSBA makes similar arguments as I&E and the OCA that Aqua’s ECAM and PWAC do not satisfy the requirements of Section 1307(a) of the Code. OSBA R. Exc. at 4, 5. The OSBA also disagrees with the Company’s argument that the proposed riders qualify as a “well recognized exception to the prohibition against single-issue ratemaking” because each of them would move consideration of a *single* ratemaking expense outside the context of a traditional base rate proceeding. OSBA R. Exc. at 3, 4, 6 (citing Aqua Exc. at 36). The OSBA submits that the ECAM and PWAC are classic examples of single-issue ratemaking and would provide no incentive to control its energy and purchased water costs because the ECAM, in particular, would insulate the Company from fluctuating energy costs, and any energy and purchased water cost increases under the ECAM and PWAC, respectively, would be passed along to customers. OSBA R. Exc. at 4, 5.

The OSBA also reinforces its previous argument that the ECAM would lower Aqua's business risk, which should lower its ROE. The OSBA notes that the Company did not make such a proposal in this rate proceeding. Accordingly, the OSBA remains of the opinion that if the Company's ROE is not lowered in conjunction with the resulting lower business risk, the approval of the ECAM rider would only serve to benefit the Company's shareholders. OSBA R. Exc. at 4 (citing OSBA St. No. 1 at 21-22).

d. Disposition

After thoroughly reviewing the record with respect to the ECAM and the PWAC, we shall deny Aqua's Exception No. 11 and adopt the ALJ's recommendations that reject the two reconcilable rider mechanisms in accordance with the arguments set forth by I&E, the OCA, the OSBA and Aqua LUG in this proceeding.

The primary disagreement between the Company and the opposing Parties centers on whether the tariffed ECAM and PWAC riders satisfy the requirements for approval of reconcilable riders under Pennsylvania law and Section 1307(a) of the Code. I&E, the OCA, the OSBA and Aqua LUG (opposing Parties) were opposed to these riders and argued that approving them would constitute impermissible single-issue ratemaking. I&E M.B. at 91-95; OCA M.B. at 112-15; OSBA M.B. at 5-7; Aqua LUG M.B. at 4-6. Aqua, however, took the position that Section 1307(a) specifically provides an exception to the prohibition against single-issue ratemaking, and that Aqua's proposal to add the riders is almost identical to the rider proposed and approved in *Newtown Artesian Water*. Aqua R.B. at 105. Aqua also submitted that I&E's, the OCA's, and the OSBA's attempts to distinguish this case on the basis that Aqua's cost are not as significant as in *Newtown Artesian Water* also fail.¹¹⁷ The Company argued that while

¹¹⁷ See Aqua R.B. at 105, n.41 OCA M.B. at 114; I&E M.B. at 92, 94; OSBA M.B. at 6-7.