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May 31, 2012

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

**RE: Comments of Aqua Pennsylvania, Inc.
Implementation of Act 11 of 2012 – Docket No.: M-2012-2293611**

Dear Secretary Chiavetta:

Enclosed for filing are three copies of Comments of Aqua Pennsylvania, Inc. to The Commission's May 10, 2012 Tentative Implementation Order.

If you have any questions regarding this filing, please contact me at (610) 645-1077.

Sincerely,

Kimberly A. Joyce
Regulatory Counsel and Manager of
Legislative Affairs

/lf
Attachments

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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Implementation of Act 11 of 2012

Docket No. M-2012-2293611

**COMMENTS OF AQUA PENNSYLVANIA, INC.
TO THE COMMISSION'S
MAY 10, 2012 TENTATIVE IMPLEMENTATION ORDER**

SECRETARY'S BUREAU
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I. INTRODUCTION

Aqua Pennsylvania, Inc. ("Aqua PA") appreciates the opportunity to comment on the Pennsylvania Public Utility Commission's ("PUC" or "Commission") Tentative Implementation Order ("Tentative Order") entered May 11, 2012 regarding the implementation of Act 11. Aqua PA provides drinking water to customers throughout Pennsylvania and its water system includes approximately 5,100 miles of water mains. Aqua's water systems serve both urban and rural areas. Since 2001, Aqua has been acquiring various small water systems throughout the Commonwealth.

In response to the problems presented by the Commonwealth's aging water infrastructure, the Commission, on August 26, 1996, issued an order authorizing Aqua PA (then "Philadelphia Suburban Water Company") to establish a Distribution System Improvement Charge ("DSIC"). *Petition of Philadelphia Suburban Water Company*, Docket No. P-00961036 (August 26, 1996). Thereafter, on December 18, 1996, the General Assembly enacted Section

1307(g) of the Public Utility Code, 66 Pa.C.S. § 1307(g), to eliminate any uncertainty as to the Commission's authority in this area. Aqua PA subsequently filed and had approved a DSIC surcharge which outlined requirements, processes, and procedures for calculating and processing the DSIC. Aqua PA's DSIC recovery was capped at 5%.

On December 23, 2008, Aqua PA filed Supplement No. 88 to Tariff Water-Pa. P.U.C. No. 1 requesting approval to increase the DSIC surcharge cap from 5% to 7.5%. In support of the tariff supplement filing, Aqua PA included a detailed analysis and a long-term pipe replacement plan. Following its investigation of Aqua PA's request, the Commission, by Order entered February 9, 2009, approved the proposed increase in the DSIC surcharge cap from 5% to 7.5%. In so doing, the Commission concluded that the tariff water DSIC model was working effectively and, indeed, that its use has made a significant impact in terms of improving Aqua PA's distribution system.

Aqua PA commends the General Assembly and the Commission for taking steps to encourage infrastructure investment by Pennsylvania's other utilities, including wastewater companies, by extending to them the use of the DSIC. The benefits of the DSIC program for the water industry have been well documented since its implementation in the mid-1990s. It is with this background that Aqua PA provides the following suggestions and clarifying comments for the Commission's consideration.

II. COMMENTS

A. The General Assembly Directed That The Current Water DSIC Practices And Procedures Remain In Effect

As noted previously, the current water DSIC model has been working extremely effectively for the past fifteen years. The General Assembly recognized this fact and created a

carve out provision in Act 11 to ensure that the current water DSIC model would remain unchanged. More specifically, the General Assembly directed that the current practices and procedures remain in place for those water companies that have an approved DSIC. Section 1358 of the Code provides:

All proceedings, orders and other actions of the commission related to a distribution system improvement charge granted to a water utility and all practices and procedures of a water utility operating under a distribution system improvement charge prior to the effective date of this paragraph shall remain in effect unless specifically amended or revoked by the commission.

Given this clear directive, Aqua PA submits that the Tentative Order's filing and reporting requirements should only apply to those utilities that have not yet applied for a DSIC surcharge. Throughout the discussions leading up to the passage of Act 11, the water DSIC was frequently cited as a regulatory mechanism that was working well and achieving its intended purpose (i.e., the acceleration of infrastructure rehabilitation). Accordingly, and not surprisingly, the General Assembly concluded, with respect to the water DSIC, that "if it aint broke, don't fix it."

Aqua PA therefore suggests that most of the discussion in the Tentative Order applies to a utility seeking a DSIC surcharge for the first time. For example, Aqua PA asserts that the requirement to file an asset optimization plan applies only to those utilities that do not presently have a DSIC in place. As noted in the Tentative Order, substantial progress has been made by Pennsylvania's water industry over the past 15 years in accelerating the rate of main replacements and other infrastructure improvements. While Aqua PA will not address every specific aspect of the Tentative Order, it believes that the DSIC which it has on file should

remain in effect and asks the Commission to confirm that there is no reason or compelling evidence requiring a change.

B. Ability to Negotiate the DSIC ROE in a Rate Case

It has been a long standing practice of Aqua PA and intervening parties to settle the DSIC Return on Equity ("ROE") in rate cases. Aqua PA believes that this is a valuable tool in maintaining a constant and steady DSIC program. For the most part, this practice has not created any controversy or concern over the fifteen sixteen years that the water DSIC has been in effect. In fact, since Aqua PA is typically on a two year base rate filing cycle, this allows the calculation to be done in a transparent and consistent manner. Consistent with its comments above, Aqua PA asserts that this practice should remain in effect per the General Assembly's direction for current water DSICs.

To this end, Aqua PA respectfully submits that the Tentative Order inappropriately interprets the language in the statute. Section 1357(b)(2) states:

The cost of equity shall be the equity return rate approved in the utility's most recent fully litigated base rate proceeding for which a final order was entered not more than two years prior to the effective date of the distribution system improvement charge.

Aqua PA disagrees with the Commission's interpretation of the phrase "fully litigated base rate proceeding," at page 15 of the Tentative Order, as one in which all revenue requirement issues are addressed and adjudicated by the Commission in a final rate order. To the contrary, as soon as a tariff proposing a rate increase is suspended and the case is transferred to the Office of Administrative Law Judge ("OALJ"), the proceeding becomes a fully litigated case.

Moreover, a base rate case filing assigned to OALJ will rarely result in all issues being "fully litigated." As a result, taking the Commission's interpretation to its full conclusion, the

parties would have little or no incentive to try to stipulate the utility's authorized rate of return. Aqua PA asserts that this is not the intent of the language and the Commission's interpretation is overreaching.

Finally, Aqua PA notes that the settlement of a DSIC ROE does not undermine the authority of the Commission to set just and reasonable rates. The Commission retains the right to review and either approve or reject any settlement provision that would affect the DSIC and in particular, the calculation of the utility's ROE.

For the reasons stated above, Aqua PA recommends that the language on page 15 regarding the disqualification of a full or partial settlement be eliminated. In addition, the Commission should clarify that a base rate case becomes "fully litigated" when it is assigned to the Office of Administrative Law Judge for hearing and a Recommended Decision.

C. Bills Rendered vs. Service Rendered

Aqua PA is currently involved in litigation before the Commission at Docket No. C-2011-2239556 that involves a dispute over whether Aqua PA is billing the DSIC surcharge in compliance with its Commission-approved tariff and prior Commission guidance. Aqua PA's comments are limited to the Implementation Order and do not address the specific issues involved in the litigation. Aqua PA nevertheless wants to make the Commission aware that its final action on the Implementation Order could unduly affect other pending proceedings, including a similar case filed against Pennsylvania American Water Company at Docket No. C-2011-2226096, and to encourage the Commission to refrain from any action with regard to the Implementation Order that may infringe upon the due process rights of any of the parties involved in the other pending proceedings.

For background purposes, the Commission's Bureau of Audits, in 2000, reviewed the issue of whether Aqua PA should bill its customers for the DSIC on a bills rendered or service rendered basis. At that time, the Bureau of Audits requested that Aqua PA bill on a bills rendered basis and Aqua complied with the request. Aqua PA has been billing consistently since that time under that direction. This method of billing is reflected in Aqua PA's Commission-approved tariff.

Since the General Assembly has directed the Commission to maintain the status quo for the current water DSIC process, water utilities' methods of billing their DSIC should continue unless they are specifically amended or revoked. If any change is made, the Commission should expressly explain and clarify that it would be prospective in nature and would only apply to utilities that have not yet filed a DSIC.

The Tentative Order has certain inconsistencies within it and could be interpreted as contrary to the Commission's and its Bureau of Audits' prior guidance with regard to Aqua PA's method of billing the DSIC. Specifically, page 13 of the Tentative Order, states that: "*The DSIC then becomes effective and applicable to rates for service rendered on and after the effective date.*" This statement should be deleted because it conflicts with existing Commission-approved tariffs and Commission guidance. The statement is also arguably inconsistent with the model tariff which is attached to the Tentative Order, which provides as follows:

3) Customer Safeguards:

- D. *Cap: The DSIC is capped at 5.0% of the amount billed to customers for distribution service (including all applicable clauses and riders) as determined on an annualized basis*

[Note: Several water utilities have Commission-approved DSICs that are

capped at 7.5% of the amount billed for service.]

The fundamental concept underlying billing customers on an “amount billed” or “bills rendered” basis is to keep the DSIC charge simple, understandable, and transparent.

Accordingly, the Commission should adhere to its previously approved tariffs and prior guidance, and direct all utilities to bill on a bills rendered basis to promote consistency and uniformity in the industry. Alternatively, the Commission should, at a minimum, expressly acknowledge that any changes to the method of billing resulting from the Implementation Order are prospective in nature and should not in any way be interpreted as an indication of the Commission’s prior position on the method of billing.

D. Accumulated Deferred Income Taxes

Aqua PA agrees with the Tentative Order’s discussion at page 16 regarding accumulated deferred income taxes. Under the current water DSIC tariff that has been in effect for over 15 years, there is no provision for accumulated deferred income taxes. Credits for accumulated deferred income taxes, like many other adjustments, are accounted for in the normal base rate case process. For a capital intensive water company like Aqua PA, a base rate case is typically filed on a two-year rate cycle. The General Assembly specifically concluded that this process should remain in effect. It is the intent of the DSIC to create an efficient way to update and file on a quarterly basis. The process should remain transparent and efficient and, as such, the manner in which the water DSIC charge is calculated should not be changed.

E. Asset Optimization Plan

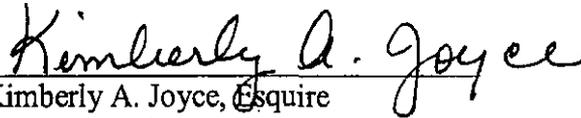
A specific example of where the carve-out language for existing water DSIC programs would apply for Aqua PA is in relation to the asset optimization plan – discussed at Section

1356. The General Assembly acknowledged the unique nature of the water industry when it enacted Section 1307(g) of the Code in 1996. Aqua PA maintains that this section of the Code requiring an asset optimization plan applies to those utilities that will be prospectively applying for a surcharge and not those that currently have an approved DSIC on file with the Commission.

Aqua PA notes that if this requirement were to apply to the current water DSIC companies, it would be unnecessarily repetitive. Aqua PA and most all other water companies that have a current DSIC file a base rate case on a two-year rate cycle. Upon filing a base rate case, the Company seeks a return on and a return of its investment in all infrastructure projects including the costs of those projects then being recovered through the DSIC. If Aqua PA were required to file annual asset optimization plans, the Company would be essentially furnishing ongoing DSIC data on an unending basis throughout the year, particularly in base rate case years and years when the DSIC is audited. Aqua PA has a recognized and well respected track record of DSIC infrastructure improvements. There have been a number of audits performed by the Commission's staff over the years in regard to DSIC planning and timing of construction projects with no issues resulting in any of these thorough audits. Supplying DSIC project information more than once a year and in multiple dockets is overly burdensome and inefficient. Consequently, similar to the long term infrastructure plan, the Commission should acknowledge the unique long standing history of the water DSIC and follow the General Assembly's guidance in allowing the same policies and procedures to continue which would eliminate the need for utilities with DSICs to file asset optimization plans.

In conclusion, Aqua PA appreciates the opportunity to comment on the Tentative Order and commends the Commission for taking the lead on these key utility industry issues. Please direct any questions with regard to these comments to the undersigned.

Respectfully submitted,



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