

**PENNSYLVANIA HOUSE OF REPRESENTATIVES  
HOUSE CONSUMER AFFAIRS COMMITTEE**

**HEARING - HOUSE BILL 2075**

**TUESDAY, MAY 23, 2018 (9:45 AM)  
HARRISBURG, PA**

**TESTIMONY OF  
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Good morning, Chairman Godshall, Chairman Caltagirone, and distinguished members of the House Consumer Affairs Committee. And, good morning as well, to my esteemed colleagues from the Office of Consumer Advocate (“OCA”), the Public Utility Commission (“PUC”), the participating utility companies, and other interested stakeholders.

My name is Elizabeth Rose Triscari, and I am the Deputy Small Business Advocate testifying today on behalf of the Small Business Advocate, John R. Evans, and the Pennsylvania Office of Small Business Advocate (“OSBA”). Thank you for inviting us to share with this Committee our thoughts regarding House Bill 2075. As you know, the OSBA is charged with representing the interests of Pennsylvania’s small business utility customers in proceedings that come before the Pennsylvania Public Utility Commission (“PUC”), any comparable federal regulatory agencies, and in the courts. The OSBA’s statutory mission is to ensure that our small businesses, so crucial to the Commonwealth’s economy, pay reasonable rates for safe and reliable utility service.

At the outset, we would like to make perfectly clear that the OSBA supports what we believe is the primary policy goal of HB 2075, the replacement of customer-owned lead service lines by the Commonwealth’s investor-owned water utilities. Lead is a public health concern and utilities should be permitted to make changes to their tariffs to permit replacement of customer-owned lead service lines. In contrast, a damaged customer-owned sewer lateral does not involve lead and does not constitute a public health concern. Consequently, the OSBA respectfully suggests that general ratepayers should not be responsible for any of the cost of replacing or rehabilitating damaged customer-owned sewer laterals.

With respect to the proposed legislation, the OSBA has significant concerns with how lead service line replacement costs are recovered and treated for ratemaking purposes. Currently, the cost of replacement of customer-owned lead service lines falls solely on the individual customer. For public policy reasons, the OSBA supports legislation permitting utilities to replace customer-owned lead service lines and recover reasonable and prudent, but not excessive, costs from all customers. Ratepayers should not be the sole party on the hook for excessively costly service line replacements. In those circumstances, either the individual customer should be responsible for excessive replacement costs in the form of a

contribution in aid of construction (“CIAC”) (e.g., for the amount that exceeds average replacement costs), or the water utility should be barred from recovering in base rates the excessive portion of the costs. Although it may be in the public interest to now require all customers to subsidize the average cost of individual service line replacements, it would be inequitable to make ratepayers responsible for “excess” service line replacement costs. A limited CIAC would mitigate this inequity.

It would also be appropriate for the legislation to make a distinction between the replacement of lead service lines encountered when a utility replaces its mains and service lines versus those that are replaced at the request of a customer. The replacement of utility-owned mains and service lines may disturb customer-owned service lines and result in elevated lead levels from the dislodging of particulate lead and galvanic corrosion. Those customer-owned service lines affected should be prioritized and a CIAC may be appropriately waived in that scenario.

The OSBA further recommends, to avoid excessive costs being passed onto general ratepayers, the legislation require that an annual budget cap, with no carryover to subsequent years, be placed on utility spending on customer-owned lead service lines, to be established by the Pennsylvania Public Utility Commission (“PUC”) upon petition by a water utility.

In addition, while it is of course only fair for utilities to recover the reasonable and prudent costs they expend on service line replacement, they should not be permitted, as this legislation proposes, to earn a profit on replacement costs. It is a long and well-established ratemaking principle that utilities may only earn a return on investment owned by the utility and used for the public benefit.<sup>1</sup> Expenditures for the exclusive benefit of one customer, such as the improvement of service lines, constitute customer specific costs that are not for the public use.<sup>2</sup> However, this legislation contradicts this fundamental ratemaking principle by permitting utilities to earn a return on service line investment despite the fact that it will

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<sup>1</sup> *Keystone Water Co. v. Pa. Pub. Util. Cmm’n*, 339 A.2d 873 (Pa. Cmwlth. 1975) *citing* *Scranton v. Scranton Steam Heat Co.*, 176 A.2d 86 (Pa. 1961).

<sup>2</sup> *Klossman v. Duquesne Light Co.*, C-00945802 (Final Order entered July 24, 1996).

continue to be owned by the customer and is only for the benefit of an individual customer, not for public use. By treating the replacement of customer-owned service lines as a capitalized cost, the utility collects from ratepayers not only a return of that cost, but also earns a return on the investment.

Rather than treating customer-owned lead service line replacement costs as a capitalized cost, it would be more appropriate to treat replacement costs as a deferred regulatory asset to be recovered over an appropriate period through rates.<sup>3</sup> Customer-owned lead service lines simply do not have the relevant characteristics of a capital asset and their replacement is instead more akin to an extraordinary, non-recurring, one-time cost.<sup>4</sup> By recovering replacement costs through a regulatory asset account, utilities would be able to recover the full replacement cost incurred, but would not earn a return on the asset. Therefore, customers would only bear the burden of replacement costs and not additional utility profit.

The PUC has agreed that customer-owned lead service line replacement costs are appropriately treated as deferred regulatory assets. The PUC recently approved a settlement with York Water Company whereby York Water could only treat replacement costs as deferred regulatory assets.<sup>5</sup> And in a case currently pending before the PUC, the Administrative Law Judge came to the same conclusion with respect to Pennsylvania-American Water Company.<sup>6</sup> This same Recommended Decision also adopted the OSBA's recommendation to not impose excessive replacement cost overruns on general ratepayers.<sup>7</sup>

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<sup>3</sup> Regulatory assets are “recovered over a period of time through rates, and therefore, represent a compromise between immediately expensing a cost (and an immediate loss to shareholders) and an immediate charge to ratepayers (and an immediate spike in rates),” which represents a fair balance of both interests. NRR 94-7: National Regulatory Research Institute: Generally Accepted Accounting Principles for Regulated Utilities: Evolution and Impacts – P. 6.

<sup>4</sup> Section 1351 of the Public Utility Code defines “Capitalized cost” as “Costs permitted to be capitalized pursuant to the Uniform System of Accounts and Generally Accepted Accounting Principles.” 66 Pa. C.S. §1351.

<sup>5</sup> *In Re: Petition of York Water Company for an Expedited Order Authorizing Limited Waivers of Certain Tariff Provisions and Granting Accounting Approval to Record Costs of Certain Customer-Owned Service Line Replacements to the Company's Service Account*, P-2016-2577404 (Opinion and Order entered March 8, 2017).

<sup>6</sup> *In Re: Petition of Pennsylvania-American Water Company For Approval of Tariff Changes and Accounting and Rate Treatment Related to Replacement of Lead Customer-Owned Service Pipes*, P-2017-260611 (Recommended Decision dated May 1, 2018) at 13-25.

<sup>7</sup> *Id.* at 25-26.

Another issue that the OSBA respectfully encourages the legislature to consider is whether utilities should be required to provide a warranty on replacement of customer-owned service line replacements. The OSBA recommends that utilities be required to provide a workmanship warranty of at least one year, if not longer.

In summary, the OSBA supports utility replacement of customer-owned lead service lines, but with limits on excessive costs being passed on to ratepayers, and without permitting utilities to earn a profit on such investment. The OSBA opposes general ratepayers being responsible for any of the cost of replacing or rehabilitating damaged customer-owned sewer laterals, because this is not a public health concern.

Thank you again for this opportunity to testify before you today. I am happy to answer any questions you may have.

Respectfully submitted,

Elizabeth Rose Triscari, Pennsylvania Deputy Small Business Advocate