# Overview of Pennsylvania Acquisition Adjustments for Small Water and Wastewater Systems Under 66 Pa. C.S. § 1327

## Introduction

Section 1327 is one of the Pennsylvania statutes that create financial incentives for investor-owned utilities to absorb troubled water and sewer systems. Like its companion Section 1329 dealing with municipal systems (discussed separately), it provides a distinct mechanism for adjustments to depreciated original cost. Together, they reflect Pennsylvania's policy judgment that consolidation of troubled systems into larger regulated utilities is preferable to allowing those systems to continue in a degraded state.

Section 1327 creates a specialized rate base treatment for acquisitions of small or troubled water and wastewater systems. It encourages investor-owned utilities to acquire and rehabilitate non-viable systems that struggle to deliver safe and adequate long-term service. When a qualifying acquisition is approved, the acquiring utility may include in its rate base the full purchase price. That includes amounts by which the purchase price exceeds the depreciated original cost (DOC) or where DOC exceeds the purchase price of the acquired assets.

The statute departs from general ratemaking principles by overriding the requirement that rate base be capped at DOC. Upon satisfaction of the conditions in § 1327(a), the statute treats the premium as a rebuttable presumption, shifting the burden to parties challenging the acquisition adjustment to demonstrate unreasonableness.

## Conditions for Rate Base Inclusion

The acquiring utility claiming the acquisition adjustment bears the burden of establishing:

- Property is used and useful in providing service. § 1327(a)(1).
- Seller had 3,300 or fewer customers; nonviable absent acquisition. § 1327(a)(2).
- Seller not furnishing and maintaining adequate, efficient, safe, and reasonable service. § 1327(a)(3). Statutory evidence of troubled status includes:
  - Violation of Pennsylvania Department of Environmental Protection (DEP) or Commission regs regarding safety, adequacy, efficiency, or reasonableness; § 1327(a)(3)(i).
  - Finding of inadequate financial, managerial, or technical capacity; § 1327(a)(3)(ii).
  - Finding of deficiencies in water availability, palatability, or pressure; § 1327(a)(3)(iii).
  - Finding that needed improvements make it unlikely the seller could maintain adequate service at comparable rates; § 1327(a)(3)(iv).
  - Any other facts the Commission determines evidence the seller's inability to provide adequate service. § 1327(a)(3)(v).
- Acquiring utility will make reasonable and prudent investments to assure adequate service to the acquired customers. § 1327(a)(4).
- Seller agreed to the acquisition and negotiations conducted at arm's length. § 1327(a)(5).
- Purchase price is reasonable. § 1327(a)(6).
- Acquiring and selling entities are not affiliated interests. § 1327(a)(7).
- Preacquisition customers of the acquiring utility will not face unreasonable rate increases. § 1327(a)(8).


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**When Must "Troubled" Status Be Demonstrated?**

Acquisitions under Section 1327 are frequently bifurcated for practical purposes. While the acquisition and the rate case addition could be considered jointly, most Section 1327 applicants reserve consideration of rate base additions for a subsequent rate case. This avoids mounting a mini rate case in each acquisition. Thus, an acquisition may be approved some months or years before rate case matters are addressed in the acquirer's next rate case. This is generally accomplished through the acquisition approval order deferring rate base claims to a later rate case. The acquiring utility then must demonstrate the troubled status at the time it seeks to claim the adjustment as a rate base addition. The practical consequence is that evidence of troubled status must be preserved at the time of acquisition even if rate base treatment will not be litigated for years.

**Procedures**

***Pre-Acquisition Approval***

A utility may seek Commission approval of the rate base inclusion before the acquisition closes — and before a formal rate proceeding. § 1327(b). This pre-acquisition approval requires:

- Notice of the proposed acquisition and any proposed rate increase to affected customers, in the form and manner required by Commission regulation; § 1327(b)(1).
- Separate notice to the acquiring utility's existing customers if the acquisition would increase their rates by more than 1% of base annual revenue; § 1327(b)(2).
- Notice to the Bureau of Investigation and Enforcement and the Consumer Advocate; § 1327(b)(3).
- A full description of the proposed acquisition and a plan for reasonable and prudent investments. § 1327(b)(4).

The Commission may hold hearings as it deems necessary under § 1327(c). In the case of a joint acquisition and rate base claim it likely would.

***Below-Cost Acquisitions***

Where the purchase price is below depreciated original cost, the acquiring utility may claim the DOC as in its rate base, the difference being amortized as an addition to income over a reasonable period or passed through to ratepayers by another methodology the Commission directs, absent matters of substantial public interest. § 1327(e). Notice of proposed treatment is required to the Bureau of Investigation and Enforcement and the Consumer Advocate. § 1327(e).

***Forfeiture***

If the Commission finds, after notice and hearings, that the acquiring utility has not completed the promised reasonable and prudent investments within a reasonable time, the Commission may remove the excess acquisition costs from rates and order refunds of any excess revenues collected with interest. § 1327(d).



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