



ALTERNATIVE RATEMAKING TESTIMONY

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Thank you Chairmen Godshall and Caltagirone, Representative Delozier, committee members and staff for allowing us to provide testimony today. My name is Rod Nevirauskas and I am the Senior Director of Rates and Regulatory Affairs for Pennsylvania American Water. I am here to add our support to HB 1782 and to share with you why Pennsylvania American Water would like to expand the bill's language to include water and wastewater utilities.

Pennsylvania American Water believes that HB 1782, if amended to include water and wastewater utilities, will help address present and future challenges with the existing ratemaking process. For water and wastewater utilities, the current rate design structure relies on the randomness of weather and customer consumption or use. Like other water utilities, our costs are fixed but our revenues are variable. Imagine operating a business responsible for investing nearly \$300 million annually in infrastructure wondering if Mother Nature is going to cooperate so that you will have the needed revenue to continue investing in improvements and pay your bills.

Rate design that relies heavily on the uncertainty of the weather, coupled with a trend of declining water usage has a direct and unfavorable impact on revenue stability. Pennsylvania American Water is not alone in declining water sales volume despite our increased customer base. Following the energy conservation and policy acts mandating water-efficient toilets, showerheads and faucet fixtures and the later policies establishing more stringent efficiency standards for dishwashers and washing machines, customer consumption continues to decline on average of about 2 percent per year.

Without a doubt, improving water efficiency, energy efficiency and conservation is good public policy. As stewards of the environment, we embrace and promote conservation efforts, even though the current rate design based on sales volume creates a disincentive or penalty for promoting more efficient use of resources. And that is why we are here today to support HB 1782, legislation offering the use of alternative ratemaking structures.

For Pennsylvania American Water, alternate ratemaking offers a water efficiency mechanism that separates a water utility's cost recovery from the amount of water it sells. Or in other words, it 'decouples' profits from sales. Rather than implicitly encouraging water use and penalizing a water utility for encouraging conservation, a water efficiency decoupling mechanism adjusts rates periodically to ensure that a utility's revenue will be sufficient to cover its fixed costs regardless of sales volume –and Mother Nature - while still ensuring a fair rate of return on its investments. There is no change in the revenues the utility is authorized to collect.

Like any ratemaking mechanism, there is risk that comes with any benefit derived. With decoupling, the utility surrenders some of its upside revenue potential associated with favorable weather conditions in exchange for some downside protection against unfavorable weather conditions. Despite the risk, Pennsylvania American Water believes a water efficiency mechanism offers significant opportunities that include the following:

- Removes barriers to capital investment, increasing the rate of replacing and improving the infrastructure;
- Supports local economies with job creation (every million dollars of investment in water utility infrastructure generates between 16 and 27 jobs);
- Removes disincentives to promote water efficiency and will support revenue for continued water efficiency investments;
- Promotes sustainability of natural resources;
- Makes water utilities indifferent to selling less water and mitigates the adverse effect of weather variability;
- Recognizes that normal weather is a condition that will likely never be achieved;
- Reduces expenses associated with the pass-through costs of rate cases;
- Supports a strong water-efficiency and conservation program leading to long-term sustainable water infrastructure that protects the future water supply; and,
- Reduces treatment, disposal and energy costs resulting from lower usage that will be passed through to the customer.

Again, I thank the committee for allowing us to present testimony today on this very important initiative and applaud your efforts and foresight to examine alternative ratemaking. I am happy to answer any questions.