

## STATE CORPORATION COMMISSION

AT RICHMOND, JUNE 16, 2020

*Document Control Center 06/16/20@3.42 PM*COMMONWEALTH OF VIRGINIA, *ex rel.*

STATE CORPORATION COMMISSION

CASE NO. PUR-2020-00116

*Ex Parte:* In the matter of adopting new  
rules of the State Corporation Commission  
governing utility applications  
seeking fair valuation of acquisitions of municipal  
water or wastewater systems

ORDER FOR NOTICE AND COMMENT

The Virginia General Assembly enacted legislation during its 2020 Session<sup>1</sup> requiring the State Corporation Commission ("Commission") to establish rules governing utility applications seeking fair valuation of acquisitions of municipal water or wastewater systems related to applications filed pursuant to Chapter 5 of Title 56 of the Code of Virginia.<sup>2</sup> The new rules are to be effective by January 1, 2021.

NOW THE COMMISSION, upon consideration of the foregoing, is of the opinion and finds that a proceeding should be established to promulgate rules governing water or wastewater utility applications seeking fair valuation of acquisitions of municipal water or wastewater systems. To initiate this proceeding, the Commission's Staff ("Staff") has prepared proposed rules which are appended to this Order ("Proposed Rules"). We will direct that notice of the Proposed Rules be given to the public and that interested persons be provided an opportunity to file written comments on, propose modifications or supplements to, or request a hearing on the

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<sup>1</sup> Chapter 519 of the 2020 Acts of Assembly (SB 831); Chapter 518 of the 2020 Acts of Assembly (HB 835).

<sup>2</sup> Section 56-88 *et seq.*

Proposed Rules. We further find that a copy of the Proposed Rules should be sent to the Registrar of Regulations for publication in the *Virginia Register of Regulations*.

The Commission further takes judicial notice of the ongoing public health emergency related to the spread of the coronavirus, or COVID-19, and the declarations of emergency issued at both the state and federal levels.<sup>3</sup> The Commission has taken certain actions, and may take additional actions going forward, which could impact the procedures in this proceeding.<sup>4</sup> Consistent with these actions, in regard to the terms of the procedural framework established below, the Commission will, among other things, direct the electronic filing of comments.

Accordingly, IT IS ORDERED THAT:

- (1) This matter is docketed as Case No. PUR-2020-00116.
- (2) All filings in this matter should be submitted electronically to the extent authorized by Rule 5 VAC 5-20-150, *Copies and Format*, of the Commission's Rules of Practice and

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<sup>3</sup> See, e.g., Executive Order No. 51, Declaration of a State of Emergency Due to Novel Coronavirus, COVID-19, issued March 12, 2020, by Gov. Ralph S. Northam. See also Executive Order No. 53, Temporary Restrictions on Restaurants, Recreational, Entertainment, Gatherings, Non-Essential Retail Businesses, and Closure of K-12 Schools Due to Novel Coronavirus (COVID-19), issued March 23, 2020, by Governor Ralph S. Northam, and Executive Order No. 55, Temporary Stay at Home Order Due to Novel Coronavirus (COVID-19), issued March 30, 2020, by Governor Ralph S. Northam. These and subsequent Executive Orders related to COVID-19 may be found at: <https://www.governor.virginia.gov/executive-actions/>.

<sup>4</sup> See, e.g., *Commonwealth of Virginia, ex rel. State Corporation Commission, Ex Parte: Electronic Service of Commission Orders*, Case No. CLK-2020-00004, Doc. Con. Cen. No. 200330035, Order Concerning Electronic Service of Commission Orders (Mar. 19, 2020), *extended by* Doc. Con. Cen. No. 200520105, Order Regarding the State Corporation Commission's Revised Operating Procedures During COVID-19 Emergency (May 11, 2020); *Commonwealth of Virginia, ex rel., State Corporation Commission, Ex Parte: Revised Operating Procedures During COVID-19 Emergency*, Case No. CLK-2020-00005, Doc. Con. Cen. No. 200330042, Order Regarding the State Corporation Commission's Revised Operating Procedures During COVID-19 Emergency (Mar. 19, 2020) ("Revised Operating Procedures Order"), *extended by* Doc. Con. Cen. No. 200520105, Order Regarding the State Corporation Commission's Revised Operating Procedures During COVID-19 Emergency (May 11, 2020); *Commonwealth of Virginia, ex rel. State Corporation Commission, Ex Parte: Electronic service among parties during COVID-19 emergency*, Case No. CLK-2020-00007, Doc. Con. Cen. No. 200410009, Order Requiring Electronic Service (Apr. 1, 2020).

Procedure ("Rules of Practice").<sup>5</sup> For the duration of the COVID-19 emergency, any person seeking to hand deliver and physically file or submit any pleading or other document shall contact the Clerk's Office Document Control Center at (804) 371-9838 to arrange the delivery.<sup>6</sup>

(3) The Commission's Division of Information Resources shall forward a copy of this Order for Notice and Comment ("Order"), including a copy of the Proposed Rules, to the Registrar of Regulations for publication in the *Virginia Register of Regulations*.

(4) An electronic copy of the Proposed Rules may be obtained by submitting a request to Scott Armstrong in the Commission's Division of Utility Accounting and Finance at the following email address: [Scott.Armstrong@scc.virginia.gov](mailto:Scott.Armstrong@scc.virginia.gov). An electronic copy of the Proposed Rules can be found at the Division of Public Utility Regulation's website:

<https://scc.virginia.gov/pages/Rulemaking>. Interested persons may also download unofficial copies of the Order and the Proposed Rules from the Commission's website:

<https://scc.virginia.gov/pages/Case-Information>.

(5) On or before July 27, 2020, any interested person may file comments on the Proposed Rules by following the instructions found on the Commission's website: <https://scc.virginia.gov/casecomments/Submit-Public-Comments>. Such comments may also include proposed modifications and hearing requests. All comments shall refer to Case No. PUR-2020-00116. Any request for hearing shall state with specificity why the issues raised in the request for hearing cannot be adequately addressed in written comments. If a sufficient

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<sup>5</sup> 5 VAC 5-20-10 *et seq.*

<sup>6</sup> As noted in the Revised Operating Procedures Order, submissions to the Commission's Clerk's Office via U.S. mail or commercial mail equivalents may not be processed for an indefinite period of time due to the COVID-19 emergency.

request for hearing is not received, the Commission may consider the matter and enter an order based upon the papers filed herein.

(6) On or before August 17, 2020, the Staff may file with the Clerk of the Commission a report on or a response to any comments, proposals, or requests for hearing submitted to the Commission on the Proposed Rules.

(7) This matter is continued.

A COPY hereof shall be sent electronically by the Clerk of the Commission to utilities providing water or sewer service in the Commonwealth of Virginia that are subject to regulation by the Commission as identified in the attached list; and C. Meade Browder, Jr., Senior Assistant Attorney General, Division of Consumer Counsel, Office of the Attorney General, 202 North 9th Street, 8th Floor, Richmond, Virginia 23219-3424.

**STATE CORPORATION COMMISSION****Water Or Wastewater Utility Applications Seeking Fair Valuation Of Acquisitions Of  
Municipal Water Or Wastewater Systems****20VAC5-210-10. Purpose and applicability.**

This chapter sets forth minimum filing requirements for Virginia's investor-owned water and wastewater utilities related to applications pursuant to Chapter 5 (§ 56-88 et seq.) of Title 56 of the Code of Virginia when electing to seek use of fair market value (i) in the acquisition of a municipal or other governmental selling entity's water or wastewater system, and (ii) for purposes of determining initial rate base in conjunction with such acquisition. The commission may waive any or all parts of this chapter for good cause shown.

**20VAC5-210-20. General filing instructions.**

A. An applicant shall provide a notice of intent to file an application pursuant to this chapter to the commission at least 30 days prior to the application filing date. Such notice of intent shall identify the parties involved in the proposed transaction, as well as the specific section and subsection of the Code of Virginia pursuant to which the application will be filed.

B. Applications filed pursuant to this chapter shall include, in addition to all other filing requirements in Chapter 5 (§ 56-88 et seq.) of Title 56 of the Code of Virginia applications:

1. Testimony in support of the proposed acquisition and purchase price. Such testimony shall include a statement from each of the acquiring and selling entities concerning their agreement and intent to consummate the transaction according to the terms and conditions represented in the application.
2. Complete and unredacted copies, including all supporting documentation and workpapers, of two qualified, independent, and impartial utility valuation experts'

appraisals of the system assets to be acquired in compliance with the uniform standards of professional appraisal practices. The appraisals shall be submitted and treated confidentially under 5VAC5-20-170, Confidential Information, of the Commission's Rules of Practice and Procedure. Such appraisals shall be completed and submitted in accordance with the following requirements:

- a. One appraisal shall be sponsored by the water or wastewater public utility acquiring the utility system assets, and one appraisal shall be sponsored by the government entity selling its utility system assets.
  - b. The qualifications of each utility valuation expert, specifically as they relate to water or wastewater utility systems, shall be clearly identified in the application.
  - c. The appraisals shall clearly identify whether they are based on a cost, market, income, other methodology, or a combination of such methodologies, and shall state the historical period on which they are based.
  - d. To the extent any assets are proposed to be acquired apart from those to be currently used and useful in utility service, the appraisals shall (i) separately identify such assets, and (ii) describe the acquiring utility's intended use of such assets.
3. A complete and unredacted copy, including all supporting documentation and workpapers, of the assessment performed by an independent professional engineer licensed in Virginia, jointly retained by the acquiring and selling entities, regarding the tangible assets of the utility system to be acquired. For purposes of this section, "jointly retained" means retained collectively by the acquiring and selling entities, retained by the selling entity and adopted by the acquiring entity or retained by the acquiring entity and adopted by the selling entity. Such assessment shall be (i) used by the utility valuation experts as a basis for their valuations in determining fair market value and (ii) submitted

and treated confidentially under 5VAC5-20-170, Confidential Information, of the Commission's Rules of Practice of Procedure. Such assessments shall be completed and submitted in accordance with the following:

- a. The qualifications of such licensed engineer, specifically as they relate to water or wastewater utility systems, shall be clearly identified in the application.
  - b. To the extent assets are to be acquired apart from those to be currently used and useful in utility service, such assessment shall separately quantify the assets that are to be currently used and useful in utility service.
  - c. An analysis of the condition of the system shall be provided, including the in-service date, if available, and an assessment of the useful life of each asset and its operating condition.
4. The following market data regarding water or wastewater utility transfers, if available, should be provided as part of the appraisals. To the extent such data is not available from the selling entity, an explanation should be provided.
- a. Identification of the acquiring and selling entities.
  - b. A description of the assets.
  - c. The geographic footprint of the acquired system.
  - d. The number of customers.
  - e. The transaction amount, identification of the recorded cost of the assets, and identification of whether such transaction was based on original cost, fair value, or other basis.
  - f. Quantification of purchase of equity and/or debt, if applicable.
  - g. Date of the transaction.

5. The following cost data for the assets to be acquired, if available, should be included as part of the appraisals. To the extent such data is not available from the selling entity, an explanation should be provided.

a. A detail of historical cost of assets by plant account, or categories of assets if not available by account, including plant additions and retirements by vintage year.

b. A detail of the recorded reserve for depreciation by plant account or categories of assets if not available by account.

c. Existing depreciation rates by account, or categories of assets, for the system to be acquired.

6. The following income data, if available, should be included as part of the appraisals. To the extent such data is not available from the selling entity, an explanation should be provided.

a. Any impairment tests performed for the system to be acquired as performed internally by the selling entity or its external auditors for the five prior years.

b. Annual financial forecasts prepared by management of the selling entity for the three prior years.

c. An analysis of the following for the acquired system by rate class and meter or service line size for the three most recent years:

(1) Number of customers.

(2) Usage data.

(3) Billed revenues.

(4) Net charge-offs.

7. Other required information pertaining to the acquired system to include:



- a. An unredacted copy of the purchase agreement.
  - b. A map of the service area of the acquired system.
  - c. A detailed description of all assets of the acquired system, with identification of any assets which were not used and useful at the time of the appraisals.
  - d. A statement of any obsolescence considered (e.g. physical, functional, and economic) and supporting documentation and calculations for any obsolescence quantified.
  - e. The comprehensive annual financial report for the municipality or other selling governmental entity for the three prior years.
  - f. Any presentations made by investment advisors or senior management of either the acquiring or selling entity regarding the potential sale.
  - g. A detailed analysis of any rehabilitations or improvements the acquiring utility plans to make to the acquired system to address any known deficiencies of the acquired system.
8. To the extent the proposed purchase price is different than that provided in the filed appraisals, the application shall identify the proposed purchase price.
9. The acquiring utility's proposed journal entries anticipated to result from the proposed acquisition, including tax entries and account numbers recognized by the National Association of Regulatory Utility Commissioners.
10. An analysis identifying the qualitative and quantitative benefits and estimated customer rate impacts for the next five years as a result of the proposed acquisition for each of (i) the customers of the acquired system and (ii) the legacy customers of the acquiring utility. Such analysis shall clearly identify all assumptions relied upon.

11. Documentation of: (i) incurred and additional estimated costs and fees of the utility valuation experts in the fair market value determination; and (ii) incurred and additional estimated transaction and closing costs.

C. An application filed pursuant to this chapter shall not be deemed filed pursuant to Chapter 5 (§ 56-88 et seq.) of Title 56 of the Code of Virginia unless it is in full compliance with this chapter.

**20VAC5-210-30. Commission determination of rate base.**

A. An average of the three appraisals, which includes one sponsored by commission staff, shall be deemed the fair market value for purposes of the proceeding.

B. The rate base value of the acquired system for purposes of subsequent rate filings made pursuant to Chapter 10 (§ 56-232 et seq.) of Title 56 of the Code of Virginia shall be the following: the fees and costs of the utility valuation experts authorized by the acquiring and selling entities, transaction costs, and other closing costs found by the commission to be reasonable and prudently incurred, plus the lesser of (i) the purchase price negotiated between the acquiring utility and selling entity as the result of a voluntary arm's-length transaction and (ii) the fair market value. The rate base value shall incorporate the provisions for depreciation as identified in this chapter.

**20VAC5-210-40. Miscellaneous general provisions.**

A. Nothing in this chapter shall be construed to relieve the applicant from its duty to demonstrate that "...adequate service to the public at just and reasonable rates will not be impaired or jeopardized by granting the prayer of the petition..." as provided in § 56-90 of the Code of Virginia.

B. Any information deemed confidential by the applicant may be submitted and treated confidentially under 5VAC5-20-170, Confidential Information, of the Commission's Rules of Practice and Procedure.

C. This chapter does not limit the commission staff or parties from raising issues related to the proposed acquisition for commission consideration that have not been addressed in the applicant's filing before the commission.

D. Commission staff and parties may seek discovery to confirm the reasonableness of, and provide testimony and recommendations regarding, the appraisals and engineering assessment sponsored by the acquiring and selling entities. The applicant may seek discovery as permitted of commission staff pursuant to 5VAC5-20-260, Interrogatories or requests for production of documents and things, of the Commission's Rules of Practice and Procedure, to confirm the reasonableness of the appraisal sponsored by commission staff and may provide rebuttal testimony or response and recommendations regarding such.

E. If the depreciation rates for the acquired system are not based on a depreciation study:

1. The acquiring utility may apply a three percent composite depreciation rate to the fair market value of the utility system assets acquired; and

2. A depreciation study on the acquired system shall be performed within five years of acquisition and provided for review by the commission staff. Upon acceptance of the depreciation rates by commission staff for booking purposes, such rates shall be utilized for the system effective as of the date of the study. However, if the acquired system is of a size that would qualify under the Small Water or Sewer Public Utility Act (Chapter 10.2:1 (§ 56-265.13:1, et seq.) of Title 56 of the Code of Virginia), such assets may be exempted from the requirement of performing a depreciation study.

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