

# RULES AND REGULATIONS

## Title 52—PUBLIC UTILITIES

### PENNSYLVANIA PUBLIC UTILITY COMMISSION [52 PA. CODE CHS. 65 AND 69]

[L-930089]

#### Line Extensions

The Pennsylvania Public Utility Commission (Commission) on October 3, 1996, adopted a revised order promulgating final-form regulations regarding line extensions. The final-form regulations will require water utilities to provide line extensions without a customer contribution where the annual expected revenues equal or exceed the annual estimated operating and maintenance expenses, plus annual book depreciation and debt expenses associated with the extension. Each company will figure variables appropriate for its own use and will apply these variables into the formula created by the regulation. The contact person is Susan D. Colwell, Assistant Counsel, Law Bureau (717) 783-3459 or 783-3190.

#### Executive Summary

The Commission instituted a rulemaking proceeding at this docket at the November 19, 1993, public meeting to provide a public forum for discussion and resolution of the problem areas and uncertainty associated with the present main line extension policy in § 69.171. The advance notice of proposed rulemaking was published in the *Pennsylvania Bulletin* on December 18, 1993, with comments due on or before February 19, 1994.

The proposed regulations were adopted by order entered July 1, 1994, which proposed to require water utilities whose depreciated plant in service amounts to more than \$10 million to fund ordinary line extensions without customer contribution where the expected annual revenues equal or exceed annual depreciation expense of the extension computed consistent with the utility's Commission-approved book depreciation rate. These were published in the *Pennsylvania Bulletin* on October 8, 1994, with a 45-day comment period. Due to an early sine die by the Legislature, the comment period was extended to January 22, 1995.

The Commission entered a final order adopting regulations on December 28, 1995, which will require water utilities to provide line extensions without a customer contribution where the annual expected revenues equal or exceed the annual estimated operating and maintenance expenses, plus annual book depreciation and debt expenses associated with the extension. Each utility will figure variables appropriate for its own use and will apply these variables into the formula created by the regulation.

On April 12, 1996, the Commission elected to temporarily withdraw the regulation from formal Independent Regulatory Review Commission (IRRC) review, to consider some additional issues raised by IRRC staff, and notice was published in the *Pennsylvania Bulletin*. This final order, adopted October 3, 1996, and entered October 7, 1996, reflects our consideration of the IRRC staff comments, a recent change to Federal income tax law applicable to customer advances, and some language changes to the regulation itself for clarification.

#### Regulatory Review

Under section 5(a) of the Regulatory Review Act (71 P. S. § 745.5(a)), the Commission submitted a copy of the final rulemaking, which was published as proposed at October 8, 1994, 24 Pa.B. 5103, and served on September 23, 1994, to IRRC and the Chairpersons of House Committee on Consumer Affairs and the Senate Committee on Consumer Protection and Professional Licensure for review and comment. In compliance with section 5(b.1) of the Regulatory Review Act, the Commission also provided IRRC and the Committees with copies of the comments received, as well as other documentation.

In preparing these final-form regulations, the Commission has considered the comments received from IRRC, the Committees and the public.

No action was taken on these final-form regulations by the House Committee on Consumer Affairs prior to sine die. The final-form regulations were approved November 13, 1996, by the Senate Committee on Consumer Protection and Professional Licensure, and were approved by IRRC on November 21, 1996, in accordance with section 5(c) of the Regulatory Review Act.

Public Meeting held  
October 3, 1996

*Commissioners present:* John M. Quain, Chairperson; Lisa Crutchfield, Vice Chairperson; John Hanger, Concurring and Dissenting in part—Statement follows; David W. Rolka, Dissenting; and Robert K. Bloom

#### Revised Order

#### By the Commission:

#### I. HISTORY OF THE PROCEEDING

This rulemaking was initiated at public meeting held November 10, 1993, to provide a public forum for discussion and resolution of the problem areas and uncertainty associated with the present utility service extension policy as it appears in § 69.171. The advance notice of proposed rulemaking was published in the *Pennsylvania Bulletin* on December 18, 1993. By notice published February 4, 1994, the comment period was extended from 45 to 60 days.

The advance notice was served on the utility associations and concerned governmental offices seeking detailed answers to a series of specific questions which would be used to evaluate the present policy statement and to draft proposed line extension regulations. Respondents were also encouraged to submit draft regulations and to offer recommendations which they believed would solve controversies.

Following review of the comments and the applicable Pennsylvania case law, the Commission adopted a proposed rulemaking at the June 16, 1994, public meeting, entered July 1, 1994. The proposal was published in the *Pennsylvania Bulletin* on October 8, 1994, commencing a 45-day comment period. Again, numerous comments were received, many of which provided specific answers to the questions we had set forth in the proposal.<sup>1</sup> Although the

<sup>1</sup>Comments to the proposed regulations were filed by the following: Pennsylvania Electric Association (PEA), UGI Utilities, Inc., Duquesne Light, Pennsylvania Electric Company, PECO Energy, Penn Power, Pennsylvania Power & Light Co., West Penn Power Co., Pennsylvania Gas Association (PGA), Columbia Gas of Pennsylvania, Equitable Gas, National Fuel Gas Distribution Corporation, Peoples Natural Gas Company, Pennsylvania Gas and Water Co., T.W. Phillips Gas and Oil Co., Pennsylvania Telephone Association (PTA), National Association of Water Companies—

public comments are too numerous to discuss individually here, each was carefully reviewed and considered, and we thank each commentator for the cooperation and information forwarded to us. In addition, by letter dated February 22, 1995, we received comments from IRRC regarding the proposed-form regulation.

Based upon our consideration of these comments to the proposed-form rulemaking, the Commission adopted a final-form rulemaking at the December 7, 1995, public meeting, entered December 28, 1995. However, given the nature of some additional issues raised by the IRRC staff on April 8, 1996, regarding §§ 65.1, 65.21(b), 65.22 and 65.21(c), the Commission elected, on April 12, 1996, to temporarily withdraw the regulation from formal IRRC review in order to give further consideration to those issues. Notice of the temporary withdrawal and of the issues raised by IRRC's staff was provided to all parties; a notice was also published in the *Pennsylvania Bulletin* on April 27, 1996, at 26 Pa.B. 2061. Further comments were due on or before May 3, 1996.

The only further comment filed in response to the Commission's notice was from the PGA which reaffirmed its position that natural gas utilities should be excluded from the scope of this line extension rulemaking. Accordingly, the further changes in this revised order will reflect our consideration of the April 8, 1996, IRRC staff comments, a recent change to Federal income tax law applicable to customer advances, and some language changes to the regulation for clarification purposes.

## II. Discussion

Under section 1501 of the Public Utility Code, public utilities are obligated to provide "reasonable service" to the public, including the obligation to make line extensions "to such service and facilities as may be necessary or proper for the accommodation, convenience, and safety of its patrons, employees, and the public." 66 Pa. C.S. § 1501. At the same time, Pennsylvania case law has recognized that a public utility's duty to provide line extensions is not unlimited and, therefore, will not obligate the public utility to make line extensions for which there is no "public need" *Colonial Products Co. v. Pa. P.U.C.*, 188 Pa. Superior Ct. 163, 146 A.2d 657 (1958), *Airlines Transportation Co. v. Pa. P.U.C.*, 63 Pa. Commonwealth Ct. 298, 437 A.2d 1283 (1981), or to make line extensions which are uneconomic or unreasonable. *Sherman v. Public Service Commission*, 90 Pa. Superior Ct. 523 (1927); *Ridley Township v. Pa. P.U.C.*, 172 Pa. Superior Ct. 472, 94 A.2d 168 (1953).

In *Colonial Products*, for example, the court explained this limitation on the general obligation to make line extensions as follows:

A utility rendering reasonably adequate service should not be subjected to unreasonable expenditures, or the consuming public unduly burdened because of the unusual or extraordinary demands of one customer.

*Id.* at 173, 146 A.2d at 663. More recently, in *Lynch v. Pa. P.U.C.*, 594 A.2d 816 (Pa. Cmwlth. 1991), the court explained that in order to obtain a line extension, the applicant must show (1) that there is a "public necessity

for the service requested" and (2) that the extension will result in "a return of investment for the utility." *Id.* at 604. In other words, the claim of an individual seeking the line extension must be balanced against the right of the public utility to remain financially viable and the right of existing customers to avoid subsidizing uneconomic line extensions for new customers.

Determining exactly how this balance should be struck has been the subject of considerable uncertainty and litigation over the years before the Commission.<sup>2</sup> Thus, the purpose of this rulemaking is to create a fair, reasonable and predictable economic standard to address this regulatory problem that will eliminate uncertainty and greatly reduce the litigation in this area.

At the same time, the Commission recognizes that the electric and telephone industries are not subject to the same level of uncertainty and litigation regarding line extension issues as are the water and gas industries. See PEA Comments, pp.1-3 (recommending that the electric utility industry be excluded given the existing regulations for electric utility line extensions in § 57.19 and the lack of controversy in that industry); PTA Comments, pp. 3-4 (recommending line extension requirements of 500 feet on private property and 2,640 on public rights-of-way).

In addition, for the natural gas industry it has become increasingly clear that, in the residential energy market, the ready availability of alternative fuels and electric utility service make natural gas largely a matter of customer choice. See PGA Comments, pp. 1-3; Columbia Gas comments, p. 3. As such, it appears that in most circumstances, a request for a natural gas line extension would be deemed to be a request for "special utility service" — that is, a service request which exceeds that required for ordinary residential service or a service request that does not involve a "public necessity for the service requested" given the existence of a safe, adequate and competitively priced alternative. See *Bonneau v. North Penn*, Docket No. C-946274 (Order entered June 23, 1995); *Babyak v. Peoples*, Docket No. F-218963 (Order entered November 29, 1994); *Lynch v. Pa. P.U.C.*, 594 A.2d 816 (Pa. Cmwlth. 1991).

Under these circumstances, it is better to target the real problem area, and we are no longer proposing that the line extension regulation apply across the board. Rather, the new proposal is limited to water utilities and has been placed in the appropriate chapter in Title 52 of the *Pennsylvania Code*. We will not hesitate to institute a similar rulemaking in the future, however, if the kinds of problems that we see in the water industry begin to occur regularly in electric, telephone and gas line extension cases.

Moreover, even in the absence of mandatory regulations for the electric, telephone and natural gas industries, we suggest that the proposed water regulations serve as the appropriate economic concept and provide guidance for line extensions in the other utility industries. These regulations reflect the Commission's view regarding line extensions and may prove instructive in adjudicating complaint cases involving line extensions in any industry.

In preparing our present proposal, staff consulted informally with industry representatives, as well as with the Offices of Consumer Advocate and Small Business Advocate. Although not all concerns and viewpoints can be satisfied, we believe that we have developed a predictable

Pennsylvania Chapter (NAWC-PA), Pennsylvania-American Water Company, Philadelphia Suburban Water Co., York Water Co., George S. Emmons, Representative Teresa E. Brown, Office of Consumer Advocate, Green Valleys Association, Pennsylvania State Association of Township Supervisors, South Coventry Township Board of Supervisors, French & Pickering Creeks Conservation Trust Inc., and 22 individuals who filed form letters expressing their concern that the regulation would result in the imposition of public water and sewer in historic watershed areas near the French and Pickering Creeks. Since the regulation does not address the way in which a public utility defines its own service area nor does it require an extension of a service area, then these fears are unfounded.

<sup>2</sup>According to Law Bureau Prosecutory Staff, as of February 1994, there were between 50 and 75 formal line extension cases currently pending before the Commission, and "many more on an informal basis." Law Bureau Prosecutory Staff Comments, p. 11.

economic standard which treats all parties fairly and satisfies the requirements of Section 1501 and Pennsylvania case law.

### III. Summary of Proposed Regulation

As in the proposed-form regulation published October 8, 1994, these regulations establish the duty of each public utility to provide line extensions without a customer contribution where the annual expected revenues equal or exceed the annual expenses and capital costs associated with the new line. Based on the comments to the proposed-form regulations, we have made a number of refinements to the revenue, expense and capital elements that may be included in this economic test, most notably the inclusion of debt costs as recommended by several commentators. See PEA Comments, pp. 5-6; PGA Comments, p. 5; NAWC-PA Comments, p.3.

The overall concept behind this regulation, however, remains the same: a public utility's obligation to make line extensions is not unlimited and, accordingly, it will not be obligated to make a line extension that is uneconomic or unreasonable absent an appropriate customer contribution. Pursuant to this regulation, if the economic analysis indicates that annual revenue will equal or exceed the company's operating and maintenance expenses, depreciation and debt costs for the new line, no customer contribution will be required.<sup>3</sup> Alternatively, if the annual revenue will cover only a portion of the line's annual costs, a contribution may be required in proportion to the annual costs of the line not covered by the annual revenue.<sup>4</sup>

The basis of this customer contribution is that, absent a reasonable contribution to the line extension's construction costs, the utility would experience a negative (less than zero) equity return on the line extension. Indeed, it appears to us that a line extension that yields a negative equity return, representing an economic loss on the transaction, is one that begins to "materially handicap the utility in securing a fair return on all of its operations," *Ridley*, 172 Pa Superior Ct. at 497, 94 A.2d at 171, as well as one that unfairly asks existing customers to subsidize the costs of serving a new customer. Accordingly, the application of this regulation should ensure, as recommended by IRRRC, that utilities will "fund all line extensions that are appropriate for the level of service to be purchased by the new customer without requiring the utilities and their existing customers to incur the costs of unreasonable line extensions. IRRRC Comments, p.2.

The following discussion will summarize the further changes and refinements made to the proposed-form regulations published October 8, 1994.

**Section 65.1—Definitions.** In addition to the definitions for "bona fide service applicant" and "special utility service" set forth in the proposed regulation which appeared at 24 Pa. B. 5103, we have added definitions for six other terms which now appear in the body of the regulation and need to be defined. All of these definitions are specific to the subject of line extensions and, accordingly, are not to be viewed as controlling for ratemaking purposes or in other regulatory contexts.

**Annual line extension costs.** This specifies the cost elements which may be included in comparing line exten-

sion costs to the annual revenues of a particular line extension. The cost elements include the additional annual operating and maintenance costs, debt costs and depreciation charges associated with the line extension. Equity return has been specifically excluded as a cost element.

**Annual revenue.** The definition specifies the method of calculating the revenue which a utility may count as expected for a line extension. We note here that if for the purpose of determining "annual revenue" there are no existing customers "similar in nature and size to the bona fide service applicant," the utility may use the service applicant's projected average annual usage based on customer-specific factors such as dwelling size, location and appliances.

**Bona fide service applicant.** This term provides the answer to the threshold question of which persons or entities within a public utility's service are entitled to line extensions. It includes the individual seeking service for his own primary residence or place of business, provided that the level of service to that primary business does not exceed that of a residence.

**Debt costs.** The definition is needed because the term is now included in the definition of "annual line extension costs." Debt costs are the utility's additional annual cost of debt associated with financing the line extension investment; the annual amount is determined by multiplying the proportion of line extension investment financed by debt times the utility's debt cost rate. Due to the infrequency of base rate cases for some companies, we have decided to use a company's current debt cost data. The cost of preferred stock, however, has been specifically excluded since it is a relatively minor component of any utility's cost of service and would needlessly complicate the economic standard for a line extension.

**Depreciation charges.** This defines another expense element which is allowed under the definition of "annual line extension costs." The annual depreciation charge allowance will be line extension-specific to recognize the differing capital costs of the various sized main line extensions necessary to provide service.

**Operating and maintenance costs.** These are costs associated with serving an additional customer, including customer accounting, billing, collections and costs specific to the water industry.

**Line extension.** Defined as "an addition to the utility's main line which is necessary to serve the premises of a customer," the term is meant to differentiate between a line extension within the meaning of this rulemaking and the addition of a service line.

**Special utility service.** The economic test provided in this rulemaking for whether a customer contribution may be required, will not apply to the request for any residential or business service which exceeds that required for "ordinary residential purposes" or service for which there is a "safe, adequate and competitively priced alternative" to meet the applicant's utility needs since these circumstances would not involve a public necessity for the service requested. The special service needs of one or a few customers should not be borne by the public at large within the utility's service territory.<sup>5</sup> For special utility service, the rates, terms and conditions set forth in a utility's currently effective tariff will control. Thus, for a water service applicant seeking special utility service, the

<sup>3</sup>Implementation of this economic test may require the use of reasonably-developed company averages and/or expense allocation; in other words, we will not require companies to determine customer-specific operating and maintenance expenses.

<sup>4</sup>An illustration of how the economic test would be applied for a hypothetical company for a variety of line extension construction costs is set forth in Table III, attached hereto. Moreover, we anticipate that all utilities will voluntarily share with prospective service applicants the calculations and assumptions used to determine whether a customer contribution would be required and its amount.

<sup>5</sup>Because this regulation will apply only to the water industry, the "safe, adequate and competitively priced alternative" language contained in the order adopted December 7, 1995, has been deleted as unnecessary.

water utility's tariffed terms and conditions will control treatment of the incremental costs incurred by the water utility to provide the special service needs.

*Section 65.21—Duty of public utility to make line extensions.* A utility is required to include in its tariff a rule spelling out the conditions under which the utility will extend its facilities to an applicant. The remainder of the regulation sets out the circumstances under which extensions to bona fide service applicants shall be constructed.

*Section (a).* Where the projected annual revenue from the line extension will equal or exceed the utility's annual line extension costs, as defined above, the extension shall be made without requiring contributions from the applicant.

*Sections (b) and (c).* These sections set forth the circumstances under which a utility may require (a utility is not obligated to require) a customer contribution in order to extend a main for service and a formula for calculation of the customer contribution amount. The formula is designed to take into account the utility's cost of construction, as well as the annual expenses and expected revenues from the line extension.

Thus, to avoid the subsidization of uneconomic line extensions, the regulation will permit utilities to require a contribution where the annual revenue from the line extension will not equal or exceed the utility's annual line extension costs. The amount of the customer contribution will be determined by subtracting the utility's minimum required investment for the line extension from the total construction costs. The utility's minimum level of investment for the line extension is that portion of the total investment which causes the utility to incur annual line extension costs equal to the expected annual revenue from the line extension. We believe that this formula will result in the applicant bearing only those costs of his or her line extension which will not pay for itself through annual revenues.

We note here that the April 8, 1996, comments of the IRRRC staff recommend replacing the word "may" with "shall," which would result in the creation of a rule requiring a utility to charge a customer contribution in all circumstances if the formula reveals that the projected annual revenue from the line extension will not exceed the utility's annual line extension costs. In developing this regulation, we intended to create a rule which sets the *minimum* dollar amount which utilities must pay toward the cost of a line extension. However, it was not our intention to limit the utility's ability to fund more of the line extension costs if, for legitimate business reasons, the utility desires to do so.

Although we perceive a real need to protect bona fide service applicants from overly zealous utilities which would prefer to charge the entire cost of a main extension to the applicant in each instance, we have not perceived a need to protect utilities from themselves. Utilities do not, as a rule, make uneconomic or irrational business decisions by offering to fund their own line extensions when they are permitted to ask for a reasonable customer contribution.

Further, a mandatory customer contribution amount would serve no useful purpose since it would create a situation where a utility which desires to fund more of a given line extension than is contemplated by the formula must come before the Commission and ask for a waiver of the rule. It would be the creation of a burdensome regulation which places undue restrictions on the regu-

lated community and would be contrary to Governor Ridge's Executive Order 1996-1, which states that a regulation should be promulgated only after a determination that it is necessary to address "a compelling public interest." The minimum line extension funding requirement on utilities does address a compelling public interest, that is, ensuring that the bona fide service applicant pays only for that portion of the line extension which exceeds the utility's annual line extension costs. However, changing the minimum requirement to a hard and fast rule would mean that companies wishing to be more generous would have to seek a waiver of the rule and, in our judgment, make this regulation unnecessarily burdensome and inflexible, contrary to the principles outlined in EO 1996-1. Realistically, these companies would probably not bother, and it is the bona fide service applicant which would end up paying more as a result.

Lastly, given President Clinton's signing on August 20, 1996, of H.R. 3448, contributions in aid of construction and customer advances are no longer taxable to the utility; thus, the gross-up factor to account for this tax referred to in our earlier orders is no longer necessary. This change in Federal income tax law will substantially reduce the cost of line extensions to bona fide service applicants.

*Section 65.22. Customer advance financing, refunds and facilities on private property.*

*Section (a).* This section provides that utilities which have \$10 million or more in gross annual revenues shall give the applicant the option of paying the customer contribution over a period of not less than 3 years following the service connection, given the potentially large cost of some line extensions.<sup>6</sup> Our original proposal required all utilities to offer that option, but after consideration of the many comments we received in protest and after realizing that many of the smaller companies are unable to raise the necessary capital to allow them to exercise this provision, we are limiting the requirement to those utilities which have over \$10 million in gross annual revenues. Furthermore, in order to mitigate the risk to the utility, we are adding two provisions: (1) the utilities may require a deposit in advance in an amount up to one-third of the total contribution, and (2) the utilities may recover financing costs equal to the cost of debt associated with initially funding the construction.

With these additions, we do not believe it to be necessary to provide that a failure to honor the payment plan will be an independent reason to terminate service. Such a provision would conflict with the existing termination regulation in § 56.83(3). We also believe that these provisions reflect a fair compromise between the positions advocated on behalf of service applicants and the utilities. Indeed, the addition of financing costs should make utilities whole for the capital expended in advance for a line extension.

*Section (b).* This section requires a utility to provide for refunding a portion of the customer contribution if an additional customer or customers attach service lines to the main extension within 10 years. Specifics are to be spelled out in each utility's tariff.

*Section (c).* This section provides that the utilities must require customers and developers to pay a reasonable charge in advance for service lines and equipment installed on private property for the exclusive use of the

<sup>6</sup>At Pennsylvania American Water Company for example, the average cost of a line extension for a bona fide service applicant between 1989 and 1993 was approximately \$25,000.

customer. A reasonable charge for this service should be based on the utility's actual cost of the installation.

*Section 65.23—Special utility service.* Special utility service is specifically exempted from the strict provisions of these line extension regulations with the exception of § 65.22(b), which provides for reimbursement of contributions if another customer attaches to the main extension within 10 years. That the extension was made to benefit a single customer, to a development or to an industrial site is not a legitimate reason to exempt the utility from reimbursing some portion of the contribution if additional customers attach to the main line extension.

**IV. Application of the Regulation**

In addition to the above refinements to the economic test for line extensions, we also requested data to assist us in evaluating the results of applying the economic test to the four largest investor-owned water utilities in Pennsylvania: Philadelphia Suburban Water Company (PSW), Pennsylvania-American Water Company (PA-American), the former Pennsylvania Gas & Water Company (PG&W), and York Water Company (York). This analysis was prompted by the IRRC suggestion that we evaluate whether the new regulations will achieve "an appropriate balance between the benefits afforded to new customers and the costs that all existing ratepayers will incur as a result of the utilities' contribution." IRRC Comments, p. 3. To this end, the water industry was able to provide company-specific estimates of the customer contribution threshold for new service applicants based on current cost data. However, an analysis of future revenue requirement changes, based necessarily on a projected number of new line extensions under the new regulations, was deemed to be too speculative to generate any reliable data and, therefore, was not provided.

Nevertheless, the data available from the four largest water companies does provide a good estimate of the effect of this regulation on new service applicants as to the customer advance threshold and the maximum footage allowance related to that threshold. Based on their current revenues, operating and maintenance expenses, and capital costs, these companies have estimated that the point at which a customer would be required to begin to make a contribution to the total cost of a line extension would be in excess of \$3,400 and as high as \$5,300.

**Table I**

Average Per Line Revenues, Costs & Customer Advance Threshold	PA-			
	PSW	American	PG&W	York
Annual Revenue	\$269	\$333	\$300	\$257
O & M Costs	33	21	15	30
Depreciation	54	116	57	38
Debt Costs	182	196	228	189
Cust. Adv. Threshold	\$4,000	\$4,000	\$5,300	\$3,400

Moreover, although the cost per foot of a given line extension can vary considerably depending upon the size of the pipe and the location of the line, it appears that the economic test set forth in this regulation will result in a substantially greater amount of footage at no cost to the new customer than the so-called 35-foot rule included in

many water company's existing tariffs.<sup>7</sup> Using the industry association's figure of \$25 as the average cost per foot of a line extension, a new customer would obtain between 136 and 212 feet of line extension with no customer contribution required, depending on the company. Using a more conservative figure of \$40 based on the historic data contained in the water company's comments, the length of a line extension before a customer contribution would be required is still considerable, ranging between 85 feet and 133 feet.

**Table II**

**Maximum Footage Allowance Without Customer Contribution**

	Industry Estimate \$25 per foot	Conservative Est. \$40 per foot
Philadelphia Suburban	160	100
Pennsylvania American	160	100
PG&W	212	133
York	136	85

Whatever cost per foot estimate is used, it appears that the economic test in these regulations for determining when an individual must begin to provide a contribution to the cost of a line extension will provide a generous footage allowance to new service applicants without damaging the economic soundness of the public utility or causing existing customers to unreasonably subsidize new customers. We believe that the balance among those interests struck by this regulation is fair, reasonable and consistent with Pennsylvania law.

Lastly, since these regulations for the water industry also reflect with greater specificity the Commission's views with respect to line extensions and, in particular, the parameters of a lawful economic test for customer contributions and the definition of special utility service, the existing policy statement in § 69.171, which is general in nature, shall be rescinded, effective on the publication date of these final-form line extension regulations.

**Table III**

**Illustration of Required Level of Customer Contribution**

*Assumptions:*

- Annual Revenues (AR) at \$300 per year
- Operating and Maintenance Expenses (OM) of \$15 per year per customer
- Depreciation Rate (D) for Account 322 of 333%
- Interest Expense Rate (I) of 2.75%, based on long-term debt ratio of 55.0% and long-term debt cost rate of 5.00%

*Thus:*

Utility Investment  
 Break-even Point = [AR-OM] divided by [I+D]  
 = [\$300-15]/[0.0275+0.0333] = \$4,688

Construction Cost	Utility Investment	Customer Contribution
\$1,000	\$1,000	0
\$2,000	\$2,000	0
\$3,000	\$3,000	0
\$4,000	\$4,000	0
\$5,000	\$4,688	\$312

<sup>7</sup>According to Law Bureau Prosecutory Staff, many water companies now employ a so-called "35-foot rule" which places a tremendous economic burden on new service applicants even though the utility's facilities may be "well within the sight of the service applicant's residence." Law Bureau Prosecutory Staff Comments, pp. 9-10.

<i>Construction Cost</i>	<i>Utility Investment</i>	<i>Customer Contribution</i>
\$6,000	\$4,688	\$1,312
\$7,000	\$4,688	\$2,312
\$8,000	\$4,688	\$3,312
\$9,000	\$4,688	\$4,312
\$10,000	\$4,688	\$5,312

Accordingly, pursuant to sections 501, 504, 505, 506, 1301 and 1501 of the Public Utility Code, 66 Pa.C.S. §§ 501, 504, 505, 506, 1301 and 1501, and the Commonwealth Documents Law (45 P.S. § 1201 et seq.), and the regulations promulgated thereunder at 1 Pa. Code §§ 7.1—7.4, the Commission adopts as final the regulations for Line Extensions, §§ 65.1, 65.21, 65.22 and 65.23, as described above and set forth in Annex A. *Therefore,*

*It is Ordered That:*

1. This revised order shall supersede the order adopted December 7, 1995, at this docket.

2. The Commission's regulations, 52 Pa. Code Chapters 65 and 69, are amended by amending § 65.1, by adding §§ 65.21—65.23 and by deleting § 69.171 to read as set forth in Annex A.

3. The Commission's regulations are hereby amended by the rescission of the policy statement in § 69.171 effective upon publication in the *Pennsylvania Bulletin*.

4. The Secretary shall submit this order and Annex A to the Office of Attorney General for approval as to legality.

5. The Secretary shall submit this order and Annex A to the Governor's Budget Office for review of fiscal impact.

6. The Secretary shall submit this order and Annex A for formal review by the designated standing committees of both houses of the General Assembly, and for formal review and approval by IRRC.

7. The Secretary shall deposit this order and Annex A with the Legislative Reference Bureau for publication in the *Pennsylvania Bulletin*.

8. These amendments shall become effective upon publication in the *Pennsylvania Bulletin*.

9. The public utilities affected by these line extension regulations shall file appropriate compliance tariffs by April 16, 1997.

10. A copy of this order shall be served upon all persons who submitted comments in this rulemaking proceeding.

*By the Commission*

JOHN G. ALFORD,  
*Secretary*

*(Editor's Note: The proposal to add §§ 66.1—66.3 as proposed at 24 Pa.B. 5103 (October 8, 1994) has been withdrawn by the Commission. The amendment of § 65.1 and the addition of §§ 65.21—65.23 and the deletion of § 69.171 was not included in the proposal at 24 Pa.B. 5103.*

A proposal to amend § 65.1, amended in this document, remains outstanding at 26 Pa.B. 2325 (May 18, 1996.)

*(Editor's Note: For the text of the order of the Independent Regulatory Review Commission relating to this document, see 26 Pa.B. 5915 (December 7, 1996.)*

### Statement of Commissioner John Hanger

This rulemaking has involved consideration of complex issues for which there is no simple answer. This Commission has been asked to resolve many line extension disputes in recent years, leading not only to a large volume of time consuming cases, but also to murky, at times undecipherable, Court and Commission policies and precedent. Cases sometimes are decided through pro forma applications of "rules" which are not reflected in any written standards. Sometimes the results bear little or no relationship to the underlying policies or rationales for the "rule." While the Regulations adopted today do adopt clear standards, those standards incorporate some misplaced considerations and sometimes do not adequately meet the guidance of either case law or important policy considerations.

Because it is essential that this Commission establishes clear standards for line extensions, I concur and dissent with the Regulations proposed by the Law Bureau. While certain aspects of the Regulations applied to water utilities raise important concerns, as indicated below, I hope that passage will permit most water line extension cases to proceed expeditiously and fairly. I must dissent to the extent that the Regulations fail to include gas utilities.

The basic legal standard governing line extensions must reflect the primary "duty to serve" embodied in Section 1501 of the Public Utility Code, and the Regulations recommended by the Law Bureau do not do so. Section 1501 clearly states that:

"Every public utility ... shall make all such ... extensions and improvements in or to such service and facilities as shall be necessary or proper for the accommodation, convenience, and safety of its patrons, employees, and the public."

Thus, every case starts with a presumption that a utility which has been granted a service territory has the obligation to provide line extensions at system cost. The Courts have given the Commission some latitude to permit customer contributions when extensions are not presently required to serve actual customers or will benefit only an individual need at uneconomic public expense. This Commission does not have the authority under Section 1501 of the code, however, to declare that the duty to serve does not apply wholesale to large categories of customers.

There are extraordinary ramifications to the Law Bureau recommendation that utilities need not provide line extensions for customers who have "a safe, adequate and competitively priced alternative." Section 1501 imposes the duty to serve to include the "accommodation" and "convenience" of the public, without limiting the duty to situations in which the extension is a practical or economic necessity.

The staff recommendation suggests that gas service is always "special utility service" and that gas utilities do not have any duty to make a line extension because all uses of gas can instead be served by electricity, oil, propane or other fuels. While it is true that there are alternatives to gas, there is no legal or policy basis for suggesting that gas utilities are exempt from the duty to serve embodied in Section 1501 and a large body of appellate case law.

For these reasons, I concur and dissent.

**Fiscal Note:** Fiscal Note 57-152 remains valid for the final adoption of the subject regulations.

Annex A

TITLE 52. PUBLIC UTILITIES

PART I. PUBLIC UTILITY COMMISSION

Subpart C. FIXED UTILITY SERVICES

CHAPTER 65. WATER SERVICE

§ 65.1. Definitions.

The following words and terms, when used in this chapter, have the following meanings, unless the context clearly indicates otherwise:

*Annual line extension costs*—The sum of a utility's additional annual operating and maintenance costs, debt costs and depreciation charges associated with the construction, operation and maintenance of the line extension.

*Annual revenue*—The utility's expected additional annual revenue from the line extension based on the utility's currently effective tariff rates and on the average annual usage of customers similar in nature and size to the bona fide service applicant.

*Bona fide service applicant*—A person or entity applying for water service to an existing or proposed structure within the utility's certificated service territory for which a valid occupancy or building permit has been issued if the structure is either a primary residence of the applicant or a place of business. An applicant will not be deemed a bona fide service applicant if one of the following applies:

- (i) The applicant is requesting water service to a building lot, subdivision or a secondary residence.
- (ii) The request for service is part of a plan for the development of a residential dwelling or subdivision.
- (iii) The applicant is requesting special utility service.

*Company's service line*—The connection between the distribution facilities or pipeline extensions of the utility which connects any main with the inlet connection of a service line of a customer at the curb or property line.

*Customer*—A party contracting with a public utility for service.

*Customer's service line*—The service line extending from the curb, property line or utility connection to a point of consumption.

*Debt costs*—The utility's additional annual cost of debt associated with financing the line extension investment based on the current debt ratio and weighted long-term debt cost rate for that utility or that of a comparable jurisdictional water utility.

*Depreciation charges*—The utility's additional annual depreciation charges associated with the specific line extension investment to be made based on the current depreciation accrual rates for that utility or that of a comparable jurisdictional water utility.

*Line extension*—An addition to the utility's main line which is necessary to serve the premises of a customer.

*Main*—The pipe of a public utility system, excluding service connections, located in a public highway, street, alley or private right-of-way which pipe is used in transporting water.

*Nonessential uses of water*—Nonessential uses of water include:

(i) The use of hoses, sprinklers or other means for sprinkling or watering of shrubbery, trees, lawns, grass, plants, vines, gardens, vegetables, flowers or other vegetation.

(ii) The use of water for washing automobiles, trucks, trailers, trailer houses or another type of mobile equipment.

(iii) The washing of streets, driveways, parking lots, service station aprons, office buildings, exteriors of homes, sidewalks, apartments or other outdoor surfaces.

(iv) The operation of an ornamental fountain or other structures making a similar use of water.

(v) The use of water for filling swimming or wading pools.

(vi) The operation of any water-cooled comfort air conditioning which does not have water-conserving equipment.

(vii) The use of water from fire hydrants for construction purposes or fire drills.

(viii) The use of water to flush a sewer line or sewer manhole.

(ix) The use of water for commercial farms and nurseries other than a bare minimum to preserve plants, crops and livestock.

*Operating and maintenance costs*—The utility's average annual operating and maintenance costs associated with serving an additional customer, including customer accounting, billing, collections, water purchased, power purchased, chemicals and other variable costs based on the current total company level of the costs, as well as costs particular to the specific needs of that customer, such as line flushing.

*Public utility*—Persons or corporations owning or operating equipment or facilities in this Commonwealth for diverting, developing, pumping, impounding, distributing or furnishing water to or for the public for compensation. The term does not include a person or corporation not otherwise a public utility who or which furnishes service only to himself or itself, or a bona fide cooperative association which furnishes service only to its stockholders or members on a nonprofit basis.

*Short-term supply shortage*—An emergency which causes the total water supply of a public utility to be inadequate to meet maximum system demand.

*Special utility service*—Residential or business service which exceeds that required for ordinary residential purposes. The term may include installation of facilities such as oversized mains, booster pumps and storage tanks as necessary to provide adequate flows or to meet required pressure criteria and service to large water consuming commercial and industrial facilities.

§ 65.21. Duty of public utility to make line extensions.

Each public utility shall file with the Commission, as part of its tariff, a rule setting forth the conditions under which facilities will be extended to supply service to an applicant within its service area. Upon request by a bona fide service applicant, a utility shall construct line extensions within its franchised territory consistent with the following directives:

- (1) Line extensions to bona fide service applicants shall be funded without customer advance if the annual revenue from the line extension will equal or exceed the utility's annual line extension costs.

(2) If the annual revenue from the line extension will not equal or exceed the utility's annual line extension costs, a bona fide service applicant may be required to provide a customer advance to the utility's cost of construction for the line extension. The utility's investment for the line extension shall be the portion of the total construction costs which generate annual line extension costs equal to annual revenue from the line extension. The customer advance amount shall be determined by subtracting the utility's investment for the line extension from the total construction costs.

(3) The utility's investment for the line extension shall be based on the following formula, where X equals the utility's investment attributed to each bona fide applicant:

X = [AR - OM] divided by [I + D] ; and,  
 AR = the utility's annual revenue  
 OM = the utility's operating and maintenance costs  
 I = the utility's current debt ratio multiplied by the utility's weighted long-term debt cost rate  
 D = the utility's current depreciation accrual rate

**§ 65.22. Customer advance financing, refunds and facilities on private property.**

(a) If a customer advance is required from a bona fide service applicant for service from a company with gross annual receipts of \$10 million or more and the bona fide applicant is unable to advance the entire amount due, the utility shall do one of the following:

(1) Allow the applicant to pay the advance over a period of not less than 3 years, with the utility recovering financing costs equal to the utility's weighted cost of long

term debt. The utility may require the applicant to deposit up to one-third of the total customer advance prior to extending service.

(2) Provide information to the customer on financial institutions that may offer financing to the customer for the line extension.

(b) When a customer advance is required of a service applicant and an additional customer or customers attach service lines to the main extension within 10 years, the utility shall refund a portion of the advance to the customer in accordance with the utility's currently effective tariff. Deposits made for additional facilities other than the main extension, such as booster pumps, storage tanks and the like, are contributions in aid of construction and need not be refunded.

(c) A utility shall require a customer to pay, in advance, a reasonable charge for service lines and equipment installed on private property for the exclusive use of the customer.

**§ 65.23. Special utility service.**

Sections 65.21 and 65.22 (a) and (c) (relating to duty of public utility to make line extensions; and customer advance financing, refunds and facilities on private property) do not apply to special utility service.

**CHAPTER 69. GENERAL ORDERS, POLICY STATEMENTS AND GUIDELINES ON FIXED UTILITIES**

**§ 69.171. (Reserved).**

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