

VIRGINIA ACTS OF ASSEMBLY -- 2020 SESSION

CHAPTER 518

An Act to direct the State Corporation Commission to establish rules governing fair market valuations of water utility or sewer utility asset acquisitions.

[H 835]

Approved March 31, 2020

Be it enacted by the General Assembly of Virginia:

1. *§ 1. The State Corporation Commission (the Commission) shall establish rules governing petitions by an acquiring public utility that has elected to seek use of the fair market value of a municipal or other governmental selling utility's water or sewer assets to determine the initial rate base for the purpose of post-acquisition rate recovery. Such rules shall identify information to be filed in addition to all other filing requirements in the Utility Transfers Act (§ 56-88 et seq. of the Code of Virginia). Such rules shall:*

1. Establish the process for determining the acquired water or sewer utility rate base, taking into consideration the use of the lesser of (i) the agreed-upon purchase price established during a voluntary arm's-length transaction by the selling and acquiring utilities and (ii) the fair market value established using the average of the valuations provided by three qualified and impartial utility valuation experts.

2. Provide for the acquiring utility to submit complete and unredacted copies of two qualified, independent, and impartial utility valuation expert's appraisals of the system assets to be acquired in compliance with the uniform standards of professional appraisal practices. The appraisals shall be treated confidentially. Such appraisals shall be completed and submitted in accordance with the following:

a. One appraisal shall be sponsored by the public utility acquiring the utility system assets, and one appraisal shall be sponsored by the government entity selling the utility system assets.

b. The qualifications of such utility valuation experts, 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, or other methodology.

d. The appraisals shall quantify only the fair market value associated with assets that are to be currently used and useful in utility service. To the extent assets are acquired beyond those to be currently used and useful in utility service, a narrative shall be provided of the acquiring utility's intended purpose of such assets.

e. Commission staff and other intervenors may seek discovery to confirm the reasonableness of such appraisals and may provide testimony and recommendations regarding such.

f. When combined with a third appraisal sponsored by the Commission staff, the average of the three appraisals shall be deemed the fair market value for the purposes of this proceeding. The applicant may seek discovery to confirm the reasonableness of such appraisal and may provide testimony and recommendations regarding such.

3. Provide for the submission of a complete and unredacted copy of an assessment performed by a professional engineer licensed in Virginia, jointly retained by the acquiring and selling utilities, regarding tangible assets of the utility system to be acquired. Such assessment shall be used by the utility valuation experts as a basis for their valuations in determining fair market value and shall be treated confidentially. 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 and/or wastewater utility systems, shall be clearly identified in the application.

b. Commission staff and other intervenors may seek discovery to confirm the reasonableness of the assessment and may provide testimony and recommendations regarding such.

c. To the extent assets are to be acquired beyond those to be currently used and useful in utility service, such assessment shall separately quantify only the assets that are to be currently used and useful in utility service.

4. Provide that to the extent the proposed purchase price is different from that provided in the appraisals, the application shall identify such proposed purchase price.

5. Provide for the acquiring utility to submit the proposed journal entries resulting from the proposed acquisition, including tax entries, including account numbers recognized by the National Association of Regulatory Utility Commissioners.

6. Provide for the acquiring utility to submit 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 desired system and (ii) the legacy customers of the

acquiring utility. Such analysis should clearly identify all assumptions relied upon.

7. Provide that if depreciation rates for the acquired system are not based on a depreciation study:

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

b. A depreciation study on the acquired system shall be performed within five years of acquisition and provided for review by 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.

c. However, if the acquired system is of a size that would qualify under the Small Water or Sewer Public Utility Act (§ 56-265.13:1 et seq. of the Code of Virginia), such assets may be exempted from the requirement of performing a depreciation study.

8. Establish the ability to evaluate and include reasonable transaction costs and fees of the utility valuation experts in the fair market value determination in addition to reasonable transaction and closing costs when establishing the rate base.

9. Provide that the rate base value of the acquired system assets shall be the fees and costs of the utility valuation experts authorized by the acquiring and selling utilities in addition to reasonable transaction and closing costs, plus the lesser of (i) the purchase price negotiated between the acquiring utility and selling utility as the result of a voluntary arm's-length transaction and (ii) the fair market value for subsequent rate-making purposes in the acquiring utility's next base rate case.

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

Such rules shall be developed in coordination and consultation with industry experts and stakeholders and established by January 1, 2021.