

## Receivers of Public Utilities in Pennsylvania: The Need for Legislation or Regulations

In several recent cases,<sup>1</sup> the Pennsylvania Public Utility Commission (PUC or Commission) simultaneously ordered: (1) the commencement of an investigation into whether the Commission should order a troubled small water or wastewater utility to be sold to a proximate capable public utility, and (2) a public utility to become the receiver of the troubled small utility during the pendency of that investigation. While the PUC has previously ordered public utilities to serve as receivers for troubled public utilities, the Commission appears to be using this tool more frequently. If the PUC is going to use this regulatory tool frequently, unresolved issues should be addressed to make that tool more effective and efficient in the future. These issues should be addressed through legislation or regulations, rather than case-by-case litigation.

### Background

To order a troubled small water/wastewater utility to be sold to a capable public utility, the PUC conducts a trial-type proceeding pursuant to Section 529 of the Pennsylvania Public Utility Code<sup>2</sup> (a 529 Investigation). The vast majority of 529 Investigations result in a settlement in which the troubled small utility agrees to be sold to a willing buyer. This does not necessarily mean that receiverships are for short durations, however. These investigations are frequently prolonged proceedings, generally lasting several years from the date the proceeding is opened to the date the Commission directs the sale.<sup>3</sup>

The Commission has not always appointed a receiver to operate the troubled small system during the pendency of the 529 Investigation, but in some cases, the Commission has determined that the public health and safety required the appointment of a receiver.

### Need for Legislation or Rule-Making

The statutory provisions regarding receivers of public utilities are rather sparse. Section 529(g) merely states: "The commission may, in its discretion, appoint a receiver to protect the interests of the customers of the small water or sewer utility. Any such appointment shall be by order of the commission, which order shall specify the duties and responsibilities of the receiver."

The PUC's appointment of a receiver raises many difficult questions, such as: Who can become a receiver? What process does the Commission use to select a receiver? And does the PUC's selection of a receiver pre-judge the 529 Investigation?

Many of the thorniest questions center around the costs incurred by the receiver. The PUC's orders appointing a receiver state the powers and duties of the receiver, seemingly contemplating that the receiver will rectify any deficiencies in service during the receivership (e.g., by making the capital improvements necessary to improve service). Although the PUC's orders allow the receiver to collect tariffed rates for the troubled system during the receivership and to invoice the owner of the troubled system for the receiver's services, amounts received on behalf of the troubled small utility may be insufficient to cover the costs incurred by the receiver. Who pays the shortfall?

Some of these issues may require a statutory resolution, but the Commission can address at least some of them through a rule-making proceeding. The remainder of this article discusses some of the issues that should receive further consideration by the legislature and/or the Commission.



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## Issues to Consider

### Qualifications for Becoming a Receiver

In the four cases cited above, the Commission chose one of the largest investor-owned water/wastewater utilities in the commonwealth to serve as receiver.<sup>4</sup> This approach raises several fairness issues. First, other companies may be interested in serving as a receiver and should be given the opportunity to be considered for that position. Second, the compensation of the receiver raises fairness issues. For example, if Company X is repeatedly selected as a receiver and the receiver's ratepayers ultimately pay the difference between the costs incurred by the receiver and the amount paid on behalf of the troubled small utility, the ratepayers of Company X seem to pay more than their fair share to address the state-wide problem of troubled water/wastewater systems.<sup>5</sup>

The insurance industry offers an alternative model. Pennsylvania domiciled insurance companies that are experiencing substantial financial difficulties may be required to develop and submit to the Insurance Commissioner (Commissioner), for review and approval, a corrective action plan to address the company's difficulties.<sup>6</sup> In more severe circumstances, a troubled company may be placed under the supervision or control of the Commissioner. Such supervision may be pursuant to an administrative order that may include the Commissioner's appointment of a supervisor for the company.<sup>7</sup> Alternatively, the Commissioner may seek a court order of rehabilitation or liquidation.<sup>8</sup> In a court ordered rehabilitation or liquidation, the Commissioner is appointed as the receiver for the insurance company and acts under the supervision of the court. In a rehabilitation proceeding, the Commissioner may appoint special deputies to carry out her powers and duties as receiver.<sup>9</sup> Generally, the administrative costs of rehabilitation or liquidation are paid for by the troubled insurance company.

In other words, one alternative to the PUC's present approach would be to place the troubled system under the supervision or control of a state agency rather than a public utility. This approach would address the fairness issues discussed above, but, of course, would present new issues (such as which state agency should be the day-to-day operator of the troubled small utility).

### Process for Becoming a Receiver

The process that the Commission uses to select a receiver is unclear. For example, does a company receive notice and an opportunity to be heard before the PUC orders it to serve as a receiver?<sup>10</sup> Due process would seem to require that. Additionally, the appointment of a receiver in the same order commencing a 529 Investigation arguably creates the appearance that the Commission has pre-judged the 529 Investigation, both in terms of whether the troubled small utility should be sold and to whom that utility should be sold. As an adjudicator, the Commission should not decide a future case when rendering a decision in a current proceeding.

In a traditional receivership, the court appoints a corporate entity or an individual qualified to operate as a receiver under the laws of the applicable jurisdiction. As a general rule, the receiver must not be a party to the action, an attorney involved in the action, or any other person with an interest in the outcome of the action. In most jurisdictions, the receiver must execute an oath to perform the duties of the receiver faithfully and must also provide a good and sufficient bond to secure the receiver's faithful performance in the care and administration of the property in the receivership estate and in the proper disposition and distribution of the property in accordance with orders of the appointing court.

One option for the PUC would be to establish a process by which public utilities or management companies become qualified to serve as a receiver. When the PUC needs a receiver in a particular case, it could notify the entities on that list to determine which ones would be interested in serving as the receiver for that utility. The Commission could then select a receiver from among those entities expressing an interest, but a party to the 529 Investigation would not be appointed as receiver.

### Recovery of the Costs of Serving as Receiver

As discussed previously, the PUC's orders appointing a receiver generally contemplate that the receiver will not just maintain the *status quo* during the pendency of the 529 Investigation, but will incur costs to rectify any deficiencies in service. If the receiver's costs exceed the amount it receives on behalf of the troubled small system, the PUC generally allows the receiver to include a claim for this amount in its next base rate case.

Ratepayers of the receiver may not find this approach satisfactory because they are paying part of the cost to rectify a situation that was not caused by them or their water/sewer provider. Additionally, the receiver may not find this approach satisfactory. First, the receiver faces the risk that the PUC will disallow some of its claim for receivership costs (thereby imposing those costs on shareholders of the receiver). Second, even if the receiver recovers all of its claimed expenses, there may be a significant lag between the date the receiver incurs a cost and the date the receiver is reimbursed for that expense.

In traditional receiverships, it is generally accepted that receivers have a right to compensation for their services and expenses. The receiver's compensation is a charge on the property or funds in receivership. The receiver must look to the current receipts of the property or funds for payment of its compensation. The general rule is that costs and expenses of the receivership, including compensation for the receiver, counsel fees, and obligations incurred by the receiver in the discharge of its duties constitute a first-priority charge against the property or funds in receivership. This general rule also governs the payment of the operating expenses of the receivership. Generally, in addition to a statutory commission, a receiver is entitled to be reimbursed for expenditures that are necessary to preserve the receivership estate and are authorized by order of the court. The customary practice is for the order appointing the receiver to specifically set forth the receiver's compensation and the procedures for obtaining expense reimbursement.

In the insurance industry, the costs of the receivership are generally borne by the troubled company or its estate. This includes the fees and expenses of any special deputies or specialists retained by the receiver to assist with the turn-around or liquidation of the company. In a liquidation, those administrative expenses are first in line for payment ahead of all other claimants.<sup>11</sup>

Legislation may be the best avenue for addressing compensation issues, particularly if the insurance model is to be followed. Whether legislation or regulations are used, policymakers need to address several fact patterns, including the scenario in which a capable public utility is ordered to acquire the troubled small utility, the scenario in which the troubled small utility continues to provide service independently, and the scenario in which the troubled small utility abandons service.

## Conclusion

The PUC continues to wrestle with the problem of troubled small water and wastewater utilities. The PUC appears to be increasingly using receiverships as a tool for dealing with this problem. While receiverships are a helpful regulatory device, they raise issues that may not be suitable for resolution on a case-by-case basis. Instead, the General Assembly should consider enacting legislation and/or the Commission should consider initiating a formal rule-making proceeding to address these issues.

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<sup>1</sup> *In re James Black Water Service Company* (ex parte emergency order entered September 3, 2019); *In re: The Indian Springs Water Company*, Docket No. M-2019-30011972 (order entered August 8, 2019); *Pennsylvania Public Utility Commission, Bureau of Investigation and Enforcement v. Winola Water Company*, Docket Nos. P-2018-3006216 and C-2018-2644592 (ex parte emergency order entered November 29, 2018; ratification order entered December 6, 2018); and *Pennsylvania Public Utility Commission v. North Heidelberg Sewer Company*, Docket No. M-2018-2645983 (order entered February 8, 2018).

<sup>2</sup> 66 Pa. C.S. § 529.

<sup>3</sup> There may also be a substantial time period between the date the Commission issues an order directing the sale and the date of closing on the acquisition. Presumably, the utility ordered to serve as receiver during the pendency of the 529 Investigation will continue to serve as receiver until closing on the acquisition.

<sup>4</sup> Aqua Pennsylvania Wastewater Company, Inc. was named the receiver in one case, Aqua Pennsylvania, Inc. was named the receiver in one case, and Pennsylvania-American Water Company was named the receiver in two cases.

<sup>5</sup> Some of the troubled small systems have caused environmental damage. Addressing these issues is in the public interest, but again, if the ratepayers of Company X are repeatedly required to pay the difference between the costs incurred by the receiver and the amount paid on behalf of the troubled small utility, the ratepayers of Company X seem to be paying more than their fair share to address this issue.

<sup>6</sup> 40 P.S. § 221.6-A and 221.5-B.

<sup>7</sup> 40 P.S. § 221.10-221.11.

<sup>8</sup> 40 P.S. § 221.15 and 221.20.

<sup>9</sup> 40 P.S. § 221.16(a).

<sup>10</sup> In two of the cases cited above, the receiver was named in an *ex parte* emergency order, which is issued without a hearing, but the person against whom the order is issued may request an expedited hearing after the order is issued. 52 Pa. Code § 3.4.

<sup>11</sup> 40 P.S. § 221.44