

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE JOINT APPLICATION OF)	
AQUA AMERICA, INC.,)	
STEELRIVER INFRASTRUCTURE)	CASE NO. 2018-00369
FUND NORTH AMERICA LP,)	
STEELRIVER LDC INVESTMENTS)	
LP, LDC PARENT LLC, LDC)	
FUNDING LLC, LDC HOLDINGS)	
LLC, PNG COMPANIES LLC,)	
PEOPLES GAS KY LLC, AND)	
DELTA NATURAL GAS COMPANY,)	
INC. FOR APPROVAL OF AN)	
ACQUISITION OF OWNERSHIP)	
AND CONTROL OF PNG)	
COMPANIES LLC AND DELTA)	
NATURAL GAS COMPANY, INC.)	

POST-HEARING BRIEF

Aqua America, Inc. (“Aqua America”) respectfully submits the following Post-Hearing Brief, which follows the Public Hearing of this matter on February 14, 2019.

This matter involves the acquisition of ownership and control of PNG Companies LLC (“PNG”) and Delta Natural Gas Company, Inc. (“Delta”) by Aqua America. As set forth more fully herein, Aqua America satisfies the statutory requirements of KRS 278.020(6) and (7) in that it possesses the financial, technical, and managerial abilities to provide reasonable service to Delta’s customers, and the Proposed Transaction will be made in accordance with the law, for a proper purpose, and will be consistent with the public interest.

I. Procedural History.

On November 20, 2018, Aqua America and SteelRiver Infrastructure Fund North America LP (“SRIFNA”), SteelRiver LDC Investments LP (“SRLDCI”), LDC Parent LLC (“Parent”), LDC Funding LLC (“Funding”), LDC Holdings LLC, PNG, Peoples Gas KY LLC (“Peoples KY”), and Delta (collectively, the “Applicants”) filed a Joint Application requesting approval of the proposed transaction. The Applicants attached thereto several exhibits, including the written testimony of Christopher H. Franklin (Chairman, President, and Chief Executive Officer of Aqua America), Daniel J. Schuller (Executive Vice President and Chief Financial Officer of Aqua America), Morgan K. O’Brien (President and Chief Executive Officer of PNG), and John B. Brown (President, Secretary, and Treasurer of Delta). The Commission accepted the Joint Application for filing on November 26, 2018.¹

The Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention, filed a Motion to Intervene in this matter, which the Commission granted on November 28, 2018.

During this proceeding, the Attorney General’s Office and the Commission’s Staff have submitted numerous data requests to the Joint Applicants, to which timely responses have been given.

The Public Hearing of this matter was held before the Commission on February 14, 2019. The Commission noted that notice of the hearing had been properly given and filed in the record of the case. After providing the opportunity for public comment, of which there was none, the Commission heard testimony from Christopher H. Franklin (Aqua America), Daniel J. Schuller (Aqua America), Morgan K. O’Brien (PNG), and

¹ November 26, 2018 Letter from Gwen R. Pinson.

John B. Brown (Delta), in which the witnesses adopted their previously filed written testimony and responses to data requests as their direct testimony in this matter. The Attorney General's Office and Commission Staff were present and cross-examined these witnesses as they deemed appropriate. These witnesses also responded to questions posed directly by the Vice Chairman of the Commission.

At the conclusion of the Public Hearing, the Commission offered the Applicants the opportunity to file post-hearing briefs, with the filing deadline being March 5, 2019.

II. The Proposed Transaction.

As set forth in the Joint Application and the testimony of various witnesses, the proposed acquisition of PNG and Delta will occur under the terms of a Purchase Agreement (the "Agreement") by and between Parent² and Aqua America, which was attached to the Joint Application as Exhibit A.³ Parent owns all of the issued and outstanding limited liability company membership interests of Funding, which in turn owns all of the issued and outstanding limited liability company interests of Holdings.⁴ Holdings owns all of the issued and outstanding limited liability company membership interests of PNG.⁵ Delta is wholly owned by PNG.⁶ Accordingly, as a result of Aqua America's acquisition of Funding, Aqua America will acquire indirect control of Delta.⁷

² SteelRiver LDC Ventures LLC ("Ventures") owns and controls 100% of Parent. SRIFNA, which is an investment fund focused on infrastructure assets, and SRLDCI, which is an investment fund focused on local gas distribution assets, own 100% of Ventures. See Joint Application, pp. 7-8.

³ *Id.* p. 2. The Disclosure Schedules associated with the Agreement were filed with the Commission as Exhibit B and Exhibit C-CONF to the Joint Application. *Id.*

⁴ *Id.* pp. 7-8.

⁵ *Id.*

⁶ *Id.* p. 10.

⁷ Aqua will also acquire indirect control of Peoples Gas KY LLC. Peoples Gas KY LLC is a farm tap company operating under KRS 278.485 and is not a "utility" as defined in KRS 278.010(3). See Commission's Order of September 3, 2013 in *In the Matter of: Joint Application of PNG Companies LLC, Peoples Natural Gas Company LLC, EQT Corporation, Distribution Holdco, LLC and Equitable Gas Company, LLC For Approval of Acquisition of Ownership and Control of Equitable Gas Company, LLC*, Case No. 2013-00163 (Ky. PSC 2013).

Aqua America has committed that it will maintain Delta's headquarters in Winchester, Kentucky after the closing, and intends to maintain Delta's prior levels of community involvement, charitable contributions, funding for payment assistance for low-income customers, and economic development in Delta's current operating areas.⁸ Aqua America has also committed to honoring the employment agreement of John B. Brown, Delta's current President, Secretary, and Treasurer,⁹ and intends to retain the current employees at both PNG and Delta.¹⁰

III. The Proposed Transaction Satisfies the Requirements of KRS 278.020(6).

KRS 278.020(6) provides that no acquisition or transfer of ownership or control of any utility is permitted without the Commission's approval and that "[t]he commission shall grant its approval if the person acquiring the utility has the financial, technical, and managerial abilities to provide reasonable service." The evidence of record demonstrates that Aqua America has the necessary financial, technical, and managerial abilities to provide reasonable service through PNG and Delta after the proposed transaction is completed.

A. Aqua America Has The Financial Ability to Provide Reasonable Service Through PNG And Delta.

Aqua America is a publicly traded company with strong finances and a long and successful history of acquiring and integrating other utilities. As of December 31, 2018, Aqua America had total assets of \$5.9 billion and \$838 million in annual revenues.¹¹ Aqua America has substantial experience in raising both debt and equity capital in the

⁸ Joint Applicants' Response to Item No. 25 of the Attorney General's Supplemental Data Requests.

⁹ Joint Applicants' Response to Item No. 1 of the Commission Staff's Post-Hearing Data Requests.

¹⁰ Joint Application, p. 17.

¹¹ Joint Applicants' Response to Item No. 1 of the Attorney General's Post-Hearing Data Requests, attachment KYOAG-1-SUPP, pp. 57-58.

public and private markets, and has a successful track record of major acquisitions of public utility companies and assets.¹² Aqua America also has substantial experience with post-acquisition integration planning and execution.¹³ In 2018, Aqua America added approximately \$100 million in rate base from three municipal acquisitions, and expects to add another \$100 million in 2019 from other binding commitments.¹⁴

Aqua America's strong financial profile is further evidenced by its ability to complete the proposed acquisition of PNG and Delta. The sole cash component of the consideration of the proposed transaction is a base price of \$4.275 billion, including the assumption of approximately \$1.3 billion in debt, as adjusted pursuant to the terms of the Agreement.¹⁵ Aqua America will finance the consideration through a combination of equity capital and third party debt financing.¹⁶ Aqua America secured a fully committed bridge facility to fund the transaction; however, Aqua America's intent is to raise permanent debt and equity capital for the long-term, utilizing multiple options.¹⁷ The financing will be structured to maintain strong investment grade credit ratings.¹⁸ Aqua America anticipates issuing approximately \$2.2 to \$2.9 billion of common equity and equity linked securities.¹⁹ In addition, Aqua America anticipates approximately \$0.4 to \$0.9 billion of incremental Aqua America debt issued to fund the remainder of the transaction.²⁰

¹² Direct Testimony of Daniel J. Schuller, pp. 7-8.

¹³ *Id.* p. 8.

¹⁴ *Id.*

¹⁵ *Id.* p. 4.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Id.*

Aqua America's strong finances and its history of successful acquisitions demonstrate Aqua America's financial ability to provide reasonable service through PNG and Delta if the proposed transaction is approved.

B. Aqua America Has The Technical Ability to Provide Reasonable Service Through PNG and Delta.

As a long-time operator of regulated pipe-based utilities, Aqua America has the technical ability to provide reasonable service through PNG and Delta if the proposed transaction is approved. Aqua America has operated pipe-based utilities for more than 130 years²¹ and is currently the second-largest investor-owned water utility in the country.²² Aqua America, through its subsidiaries, currently provides service to approximately three million customers in eight states (Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, and Virginia).²³ It owns and operates 1,486 water systems and produced more than 82 billion gallons of drinking water in 2017.²⁴ As of December 31, 2017, Aqua America owned, operated, and maintained more than 12,500 miles of transmission and distribution mains, 21 surface water treatment plants, more than 3,000 well locations, and 187 wastewater treatment plants.²⁵

Although water and natural gas are two different products, as Aqua America's Chairman, President, and Chief Executive Officer, Christopher H. Franklin, testified before the Commission, "There is an unbelievable match in the work done at local gas distribution companies and at water utilities, particularly in infrastructure replacement . .

²¹ Direct Testimony of Christopher H. Franklin, p. 8.

²² Schuller Direct Testimony, p. 9.

²³ Franklin Direct Testimony, p. 1.

²⁴ *Id.* p. 6.

²⁵ *Id.* p. 1.

. . [T]his is work that we're very familiar with, and we knew we could add value."²⁶ Indeed, Aqua America has a significant history of successful infrastructure replacement programs, with a focus on prudently replacing aging infrastructure. For example, when Aqua America's Pennsylvania subsidiary, Aqua Pennsylvania, Inc. ("Aqua PA") began an infrastructure replacement program for distribution pipe in 1996, Aqua PA's pipes were on a 900-year replacement cycle.²⁷ Today, those pipes are on a 90-year replacement cycle.²⁸ Aqua PA has replaced more than 1,300 miles of pipe and has invested more than \$1.1 billion in pipe replacement over the last ten years.²⁹ Across its eight-state footprint as a whole, Aqua America has invested approximately \$3.5 billion in installing and replacing water and wastewater infrastructure over the last ten years.³⁰

Aqua America's commitment to prudent infrastructure replacement will continue with its acquisition of PNG and Delta. Aqua America understands the importance of Delta's Pipeline Replacement Program,³¹ and, additionally, will evaluate service expansion opportunities as appropriate.³²

Aqua America's experience in providing safe, reliable service to its water and wastewater customers and prudently replacing infrastructure will be supported by the natural-gas specific expertise of the current employees at PNG and Delta. As noted above, Aqua America has committed to honoring the employment contract of John B. Brown, Delta's current President, Secretary, and Treasurer, and intends to retain current employees at both PNG and Delta. Thus, Aqua America's knowledge and

²⁶ 2/14/19 Hearing, VR 9:53:05.

²⁷ Franklin Direct Testimony, p. 7.

²⁸ *Id.*

²⁹ Joint Application, p. 15.

³⁰ Schuller Direct Testimony, p. 10.

³¹ See Joint Applicants Response to Item No. 25 of the Attorney General's Supplemental Data Requests.

³² Joint Applicants' Response to Item No. 5 of the Attorney General's Post-Hearing Data Requests.

experience in water and wastewater operations will be combined with the knowledge and experience of the current teams at PNG and Delta, who have extensive backgrounds in gas distribution. Delta's customers will continue to receive quality service supported by a team of natural gas experts at Delta and PNG, who in turn will be supported by a parent company with a strong background in and commitment to infrastructure replacement and safe, reliable utility operations. The evidence of record establishes that Aqua America has the technical ability to provide reasonable service after the proposed transaction concludes.

C. Aqua America Has The Managerial Ability to Provide Reasonable Service Through PNG And Delta.

Although Aqua America does not currently serve gas customers, its substantial experience in operating pipe-based regulated utilities, coupled with the gas-specific expertise of the current employees at PNG and Delta, demonstrate its managerial ability to provide reasonable service after the proposed transaction. Further, while Aqua America's current operations are solely in water and wastewater, a number of its Board of Directors have experience in operating natural gas utilities. Specifically, Aqua America's Chairman, Chief Executive Officer, and President, Christopher Franklin, previously worked at PECO Energy Company, a gas and electric utility, where he was regional, civic and economic development officer.³³ Aqua America's Chairman Emeritus, Mr. Nicholas DeBenedictis, was also previously employed at PECO Energy Company, and presently serves on Exelon's Board of Directors.³⁴ Board Member Ellen Ruff previously served in multiple executive positions for Duke Energy Corporation.³⁵

³³ 2/14/19 Hearing, VR 9:39:10.

³⁴ 2/14/19 Hearing, VR 9:40:10.

³⁵ 2/14/19 Hearing, VR 9:42:02.

Delta will also continue to benefit from the experience and expertise of Delta's and PNG's current employees. In addition, Aqua America has committed to the appointment of an independent director to Delta's Board of Directors post-closing.³⁶ Therefore, it is evident that Aqua America possesses the managerial ability to provide reasonable service following the proposed transaction.

III. The Proposed Transfer of Ownership and Control Is Being Made in Accordance with Law, Is for a Proper Purpose, and Is Consistent with the Public Interest.

KRS 278.020(7) states that the Commission shall approve the change of ownership and control if it finds that the transaction "is to be made in accordance with the law, for a proper purpose and is consistent with the public interest." The proposed transaction satisfies all of these conditions.

A. The Proposed Transfer of Ownership and Control Is Being Made in Accordance with Law.

The proposed transaction has been approved by Aqua America's Board of Directors and SRIFNA's investors.³⁷ In addition to approval by this Commission, the proposed transaction is subject to approval by the Pennsylvania Public Utility Commission and the West Virginia Public Service Commission.³⁸ Applications were timely filed with both of those bodies, and approval proceedings are currently underway. The only required federal review – review pursuant to the Hart-Scott-Rodino Antitrust Improvements Act – has been completed.³⁹ Thus, the proposed transaction is being made in accordance with the law.

³⁶ Joint Applicants' Response to Item No. 1 of the Commission Staff's Post-Hearing Data Requests.

³⁷ Joint Application, p. 8.

³⁸ *Id.*

³⁹ 2/14/19 Hearing, VR 10:09:45.

B. The Proposed Transaction Is for a Proper Purpose.

The Proposed Transaction will cause PNG and Delta to become part of a larger system of infrastructure assets within Aqua America, which possesses the size, resources, experience, and expertise to provide support and enable it to succeed and continue to provide reasonable service to their customers. Thus, the Proposed Transaction will permit PNG and Delta to continue to meet their commitments to their customers. These are proper purposes for the acquisition of control of a utility. Significantly, Aqua America, PNG, and Delta have agreed to honor, with some minor modifications, the 39 commitments adhered to by the parties to Case No. 2017-00125, the proceeding in which PNG obtained approval to acquire Delta,⁴⁰ and have also agreed to honor, with some minor modifications and clarifications, all commitments set forth in the Commission Staff's Post-Hearing Data Request.⁴¹

C. The Proposed Transaction Is Consistent with the Public Interest.

The "public interest" standard in KRS 278.020(7) requires a showing either that "the proposed transfer will not adversely affect the existing level of utility service or rates or that any potentially adverse effects can be avoided through the Commission's imposition of reasonable conditions on the acquiring party."⁴² The Commission has

⁴⁰ Joint Applicants' Response to Item No. 25 of the Attorney General's Supplemental Data Requests.

⁴¹ Joint Applicants' Response to Item No. 1 of the Commission Staff's Post-Hearing Data Request.

⁴² *In the Matter of: Application for Approval of the Transfer of Control of Kentucky-American Water Co. to RWE Atkiengesellschaft and Thames Water Aqua Holdings GmbH* (Case No. 2002-00018) Order on Rehearing (Ky. PSC, July 10, 2002), at 9, quoting Final Order dated May 30, 2002). See also *In the Matter of: Application of DLR Enterprises, Inc. and Cow Creek Gas, Inc. for Approval of the Transfer of Certain Assets Formerly Owned and Controlled by Sigma Gas Corporation* (Case No. 2007-00419) (Ky. PSC, November 21, 2007), at 6 (stating simply that "The Commission has previously held that a transfer is in the 'public interest' if it does not adversely affect the existing level of utility service or rates or that any potentially adverse effects can be avoided through the Commission's imposition of reasonable conditions on the acquiring party."); *In the Matter of Application of Worldcom, Inc. and MFS Communications Company, Inc., for Approval of Agreement and Plan of Merger and Related Transaction* (Case No. 96-432) (Ky. PSC, Nov. 25, 1996) (approving a change of control and noting only that the manner in which

further explained that, although “readily quantifiable benefits” may be “achievable in limited instances,” “most transfers of control that are presented to this Commission would be unable to meet this standard.”⁴³

The evidence of record establishes that the proposed transaction meets the “public interest” standard under KRS 278.020(7). Aqua America has committed that Delta will maintain the rates in effect at the closing of the proposed transaction, and any modifications to those rates will be done only in accordance with Kentucky law and the Commission’s regulations.⁴⁴ Aqua America has also committed that Delta will not seek to recover in its rates, directly or indirectly, any transaction or acquisition costs arising from or associated with the proposed transaction, nor will it seek to recover any goodwill or acquisition premium that may be deemed to arise or be associated with the proposed transaction.⁴⁵

Under Aqua America’s ownership and control, Delta will, as applicable, continue to file tariffs, bill customers, and maintain separate accounting records for operations in compliance with all applicable statutory and regulatory requirements.⁴⁶ Delta will, as applicable, bill its customers at the approved Commission tariff rates and billing records and financials will be timely and accurately produced and maintained.⁴⁷ Delta will also continue to keep detailed timekeeping and capital records for its operations.⁴⁸

services are provided “will not . . . change” and that the change of control “will not disrupt service or cause inconvenience or confusion to the customers”).

⁴³ *In the Matter of: Application for Approval of the Transfer of Control of Kentucky-American Water Co. to RWE Atkiengesellschaft and Thames Water Aqua Holdings GmbH* (Case No. 2002-00018) Order on Rehearing (Ky. PSC, July 10, 2002), at 9-10.

⁴⁴ Joint Application, p. 10.

⁴⁵ *Id.* pp. 18-19.

⁴⁶ *Id.* p. 21.

⁴⁷ *Id.*

⁴⁸ *Id.*

While not required under the “public interest” standard, Aqua America has also committed to maintaining Delta’s headquarters in Winchester, Kentucky, and intends to maintain Delta’s previous levels of community involvement, charitable contributions, low-income funding, and economic development in Delta’s current operating areas.⁴⁹

Moreover, while the “public interest” under KRS 278.020(7) does not require “readily quantifiable benefits,” Aqua America anticipates that PNG and Delta’s Kentucky customers will benefit from the proposed transaction. As a publicly traded company, Aqua America has access to a broad range of capital; accordingly, PNG and Delta will benefit from an increased access to capital to fund their operations and any necessary and appropriate future improvements.⁵⁰ Moreover, Aqua America’s publicly traded status will bring increased transparency to PNG and Delta’s corporate governance. Aqua America is subject to numerous reporting requirements that require it to provide information to its shareholders, government agencies, and the public.⁵¹ Aqua America’s subsidiary ownership and organization will be completely transparent, including the ownership of subsidiaries that are not in the chain of ownership of PNG or Delta,⁵² and as a publicly held corporation, Aqua America’s creditworthiness is and will be a matter of public knowledge.⁵³

The combined infrastructure experience of Aqua America, PNG, the Peoples Utilities, and Delta will also benefit PNG and Delta’s customers. As noted above, over the past ten years, Aqua America has invested approximately \$3.5 billion in installing and replacing water and wastewater infrastructure across its eight-state footprint. As subsidiaries of

⁴⁹ Joint Applicants’ Response to Item No. 25 of the Attorney General’s Supplemental Data Requests.

⁵⁰ Schuller Direct Testimony, p. 8.

⁵¹ *Id.* pp. 13-14.

⁵² *Id.* p. 13.

⁵³ Joint Application, p. 23.

Aqua America, PNG and Delta will be able to leverage Aqua America's experience in infrastructure replacement to further improve efficiency in gas pipeline replacement operations.

For all of the reasons set forth above, the Proposed Transaction is consistent with the public interest.

CONCLUSION

The evidence of record demonstrates that Aqua America's proposed transaction of PNG and Delta satisfies the requirements of KRS 278.020(6) and (7). Aqua America possesses the financial, technical, and managerial abilities to own and operate Delta, and the proposed transaction is legal, for a proper purpose, and is in the public interest.

For the foregoing reasons, Aqua America respectfully requests the Commission approve the proposed acquisition by Aqua America of indirect ownership and control of PNG and Delta. Aqua America further respectfully requests that the Commission relieve the parties in Case No. 2017-00125 of the commitments agreed to therein, so that the Applicants to this proceeding do not have inconsistent commitments, and SteelRiver Infrastructure Fund North America LP and SteelRiver LDC Investments LP have no ongoing commitments with regard to Delta.

Dated: March 5, 2019.

Respectfully submitted

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CERTIFICATE OF COMPLIANCE

In accordance with 807 KAR 5:001, Section 8(7), this is to certify that Aqua America's March 5, 2019 electronic filing is a true and accurate copy of the documents being filed in paper medium; that the electronic filing has been transmitted to the Commission on March 5, 2019; that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding; and that an original and one copy of the filing are being hand delivered to the Commission within two business days.

/s/Allison L. Brown

One of Counsel for Aqua America, Inc.