



COMMUNITY LEGAL SERVICES
OF PHILADELPHIA

April 6, 2018

VIA ELECTRONIC MAIL

Ms. Rasheia Johnson
City Treasurer
1401 JFK Boulevard
Municipal Services Building, Room 640
Philadelphia, PA 19102

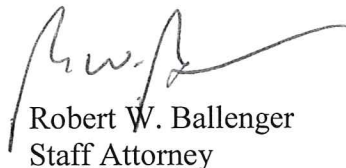
Dear Ms. Johnson,

Enclosed please find the Public Advocate's Motion and Memorandum of Law requesting that you recuse yourself from participation in the determination of the Philadelphia Water, Sewer and Stormwater Rate Board ("Board") in the matter of the Philadelphia Water Department Proposed FY2019-2021 Rate Increase.

As you may be aware, we attempted to avoid the necessity of submitting this motion, without success, prior to the commencement of this FY2019-2021 Rate Increase proceeding. We believe that your appointment to the Board creates an appearance of bias and potential for actual bias, which violates the due process standards applicable to the FY2019-2021 Rate Increase proceeding. We express no reservation about your qualification, skills, and suitability to serve as City Treasurer. However, due to your duties, functions and services as City Treasurer with respect to PWD financial matters, we respectfully submit that your participation in rendering a decision on PWD rates and charges would be impermissible.

On behalf of the approximately half-million small user customers whose interests the Public Advocate represents, we respectfully urge you to recuse yourself, in order to demonstrate to all PWD customers that the Board is truly independent, without even the appearance of bias or impartiality, as required by Pennsylvania law.

Sincerely,



Robert W. Ballenger
Staff Attorney

cc. Rate Board Members and Counsel
Rate Proceeding Service List

RBallenger@CLSPHila.org ▪ Direct Dial: 215.981.3788 ▪ Fax: 267.765.6481

WWW.CLSPHILA.ORG

**Before the
Philadelphia Water, Sewer and Storm Water Rate Board**

In Re: Philadelphia Water Department :
Proposed FY2019-2021 : **Advance Notice Filed February 12, 2018**
Rate Increase :

Motion for Recusal of Ms. Rasheia Johnson

The Public Advocate hereby moves for the recusal of Ms. Rasheia Johnson from participation as a member of the Philadelphia Water, Sewer and Storm Water Rate Board (Board) in PWD's FY 2019-2021 rate increase proceeding. Because discovery in this rate proceeding is ongoing, the Public Advocate reserves the right to supplement, modify and/or resubmit this Motion on the basis of any new information that may be acquired. Documents referenced in this Motion¹ are (1) included and/or referenced on the Board's website for this FY 2019-2021 rate increase proceeding, and/or (2) publicly available records. Fuller description and discussion of the contents of these documents is provided in the attached Memorandum of Law. As set forth more fully in the attached Memorandum of Law, the Public Advocate submits as follows:

1. Ms. Rasheia Johnson was appointed to serve as Philadelphia's City Treasurer on January 19, 2016.
2. Ms. Johnson was appointed to serve as a member of the Board on September 21, 2017.
3. The Philadelphia Water Department filed its Formal Notice of Proposed Changes in Water, Sewer and Stormwater rates on March 14, 2018, requesting Board approval of a \$116 Million rate increase over FY 2019 – 2021.

¹ Such documents are incorporated herein by reference.

4. The Board has the exclusive jurisdiction to evaluate PWD's request for higher rates and charges and to reach a determination regarding the positions of other parties in the rate proceeding.
5. The Board's determination, issued in the form of a Rate Report, is appealable to the Court of Common Pleas in Philadelphia by any party to the proceeding. Phila. Code § 13-101(10).
6. The Board's determination constitutes an appealable adjudication under Pennsylvania's Local Agency Law. 2 Pa. C.S. §§ 105, 551-588; 751-754.
7. The Board must, pursuant to Local Agency Law, avoid even the appearance of bias or lack of impartiality.
8. Ms. Johnson serves as a member of the Executive and Administrative Branch of the City of Philadelphia having specific financial duties and oversight responsibilities with respect to funds and securities of the City, including water and wastewater revenues, revenue bonds, and other indebtedness of PWD. Phila. Home Rule Charter §§ 6-300, 8-105; PA-I-1-PA-I-8; HO-I-1.
9. Ms. Johnson's service on the Board creates the appearance of bias and lack of impartiality for the reasons set forth herein.

I. Ms. Johnson Must Recuse Herself Due To Her Financial And Fiduciary Relationship With PWD And The Actual Conflict Of Interest Presented Due To The Impact Of The Board's Rate Determination Upon Her Functions As City Treasurer.

A. Ms. Johnson's Financial and Fiduciary Relationship with PWD is Grounds for her Recusal.

10. Paragraphs 1-9 are incorporated as if fully set forth herein.

11. As City Treasurer, Ms. Johnson oversees the cash management and debt management services provided to PWD. PWD Objections to Public Advocate Discovery, Set I (PA-I-1 to PA-I-8); PA-I-1-PA-I-8; PWD Ex. 5; PA-I-13; PA-I-14.
12. As City Treasurer, Ms. Johnson oversees Financial Advisors, Bond Counsel and/or Disclosure Counsel, in the process of marketing and selling water and wastewater revenue bonds secured and supported by customer rates and charges. PA-V-84; PA-V-85; PA-V-86.
13. As City Treasurer, Ms. Johnson's duties are to manage debt issuances, with the goals of maximizing value to the City, managing and refinancing existing portfolios to decrease ongoing debt service costs, attracting and retaining investors, and improving and maintaining the credit ratings of City indebtedness, including water and wastewater revenue bonds. PA-I-1; HO-I-1; City Treasurer FY 2018 Budget Testimony.
14. Ms. Johnson has an ongoing financial and fiduciary relationship with PWD (a party in this rate proceeding) that requires her to exercise a high standard of care in managing cash and indebtedness, and to which she owes duties of good faith, trust, confidence and candor. PA-I-1; PWD Ex. 5; Phila. Home Rule Charter §§6-300; 8-105.
15. Ms. Johnson should recuse herself on the basis of her fiduciary and financial relationship with PWD. See Christman v. Zoning Hearing Bd. of Twp. Of Windsor, 854 A.2d 629 at 633 (Pa. Commw. Ct. 2004) (recusal is warranted where a member of a tribunal has a fiduciary relationship with a party in interest).

B. Ms. Johnson's Service Presents a Conflict of Interest Because Her Official Duties as City Treasurer Will Be Directly Impacted by the Board's Decision.

16. Paragraphs 1-15 are incorporated as if fully set forth herein.

17. PWD's Financial Stability Plan is a required filing in PWD's rate proceeding, which the Board must review and fully consider. Phila. Code §13-101(4)(b)(1).
18. The objectives of PWD's Financial Stability Plan include specific targets for debt service coverage, pay-go capital, and cash/liquidity with the intention of maintaining an "A" credit rating. PWD St. 2, Sch. ML-2.
19. The stated goals of the City Treasurer (maximizing value, decreasing debt service costs, and maintaining credit ratings) depend on the availability of customer revenues to satisfy financial performance metrics. PA-I-1-PA-I-8; PWD St. 2, Sch. ML-4.
20. The Board's determination whether or not to increase PWD rates and charges will directly impact upon Ms. Johnson's actions in the performance of her duties as City Treasurer.
21. Under the ordinance establishing the Board, a conflict of interest constitutes cause for removal. Phila. Code § 13-101(3)(b).
22. Ms. Johnson should recuse herself because her participation in rendering a determination on PWD rates and charges presents a direct conflict of interest with her duties and obligations as City Treasurer.

C. Ongoing Responses to Discovery Requests, as Well as Publicly Available Information.

Substantiate the City Treasurer's Involvement in Formulating Financial Assumptions in this Rate Proceeding.

23. Paragraphs 1-22 are incorporated as if fully set forth herein.
24. Ms. Johnson, as City Treasurer, is involved in frequent consultations with PWD relevant to financial assumptions underpinning PWD's rate increase request. March 23 Ruling on PA Set I Discovery; HO-I-1.

25. PWD asserts that there are a minimum of 4,000 emails between PWD's Deputy Director of Finance (or the Utility Financial Services Manager) and the City Treasurer's Office that may be relevant to financial assumptions at issue in this rate proceeding. March 23 Ruling on PA Set I Discovery.
26. PWD acknowledges that the City Treasurer is involved in collective efforts with PWD regarding financial matters, and that such process involves a "give and take" where everyone's input, including the City Treasurer's, is important. HO-I-1; cf. April 15, 2016 Rate Board Hearing Tr.; CTO FY 2018 Budget Testimony.
27. Through her oversight of PFM and Acacia Financial, Ms. Johnson, as City Treasurer, is involved in the process of establishing interest rate assumptions used in this rate proceeding. PA-I-9; PA-I-84; PA-I-85.
28. Through her oversight of PFM and Acacia Financial and through the sinking fund, Ms. Johnson, as City Treasurer, is involved in the process of establishing PWD's debt service projections used in this rate proceeding. PA-I-10(a)-(c); March 23 Ruling on PA Set I Discovery; PA-I-84; PA-I-85; March 1, 2018 FY2019-2023 Five Year Plan; Sinking Fund Commission FY 2017 and FY 2018 Budget Testimony; cf. 2016 Rate Proceeding PWD St. No. 2.
29. Ms. Johnson should recuse herself due to her involvement in formulating financial assumptions utilized in this rate proceeding, which present apparent bias and lack of impartiality.

II. Ms. Johnson Should Recuse Herself Due To Her Authority Over Witnesses In This Proceeding.

30. Paragraphs 1-29 are incorporated as if fully set forth herein.

31. PWD identifies PFM and Acacia Financial as its “Financial Advisors” in this proceeding. PWD St. 2.
32. The Financial Advisors will be proffered for examination in technical hearings in this proceeding.
33. Under their contracts, the Financial Advisors are specifically required to, and have agreed to, provide ongoing support for rate case peer analysis and testimony. October 1, 2015 RFP No. 2115092913050; PA-V-84, Attachment; PA-V-85, Attachment.
34. Financial Advisors serve in this proceeding pursuant to written contracts with the City Treasurer’s Office which were most recently renewed by Ms. Johnson. PA-V-84, Attachment; PA-V-85, Attachment; April 26, 2017 Committee of the Whole Hearing Transcript.
35. PWD identifies Ballard Spahr as its “Bond Counsel” in this proceeding. PWD St. 2.
36. Bond Counsel will be proffered for examination in technical hearings in this proceeding.
37. In its response to the City’s request for proposals (incorporated into the contract), Bond Counsel asserts that the Board needs to be educated in a nonadversarial setting regarding PWD’s financial needs and that the Board needs to buy into and support PWD’s capital funding needs through rate setting. PA-V-86, Attachment; August 16, 2016 RFP No. 21160811105157.
38. Bond Counsel serves in this proceeding pursuant to its written contract with the City Treasurer’s Office which was signed by Ms. Johnson. PA-V-86, Attachment.
39. Ms. Johnson’s service on the Board in this proceeding presents an impermissible conflict of interest wherein acting as a Board Member, Ms. Johnson would weigh the testimony of consultants and counsel hired by her as City Treasurer.

40. Ms. Johnson must recuse herself to eliminate the appearance of bias and the actual potential bias presented by hearing evidence of witnesses hired by her office for the purpose of supporting PWD in efforts to increase rates and charges.

V. Ms. Johnson Should Recuse Herself Due To Her Support, As City Treasurer, Of An Approximate \$12 Million Increase In The Capital Account Deposit, Paid For By Rates.

41. Paragraphs 1-40 are incorporated as if fully set forth herein.

42. Ms. Johnson, as City Treasurer, appears before City Council in support of ordinances that authorize the issuance of water and wastewater revenue bonds and that amend the provisions that apply to water and wastewater revenue bonds. PA-I-16; March 19, 2018 Testimony of R. Johnson Re: Bill Nos. 171110 and 171111; March 19, 2018 Committee of the Whole Hearing Transcript.

43. Ms. Johnson supported Bill No. 171110, which, as introduced on December 14, 2017 would have imposed a mandatory 0.5% increase in the Capital Account Deposit paid for through customer rates. PA-I-21; Bill No. 171110.

44. A 0.5% increase in the Capital Account Deposit would cost customers approximately \$12 Million more in FY 2019 and \$37 Million more over the three years FY 2019 through FY 2021. PWD St. 9A; PWD Ex. 6.

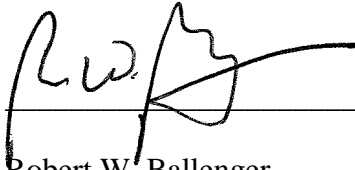
45. Although Bill No. 171110 was amended on March 19, 2018 to eliminate the 0.5% increase in the Capital Account Deposit, Bill No. 171110 has not been passed and could be further amended.

46. PWD has included a 0.5% increase to the Capital Account Deposit in its rate filing, which forms part of its request for higher rates and affects one coverage requirement under the Bond Ordinance. PWD St. 9A; PWD Ex. 6; PA-I-21.

47. The determination of “the extent to which current revenues should fund capital expenditures” is specifically vested in the Board and seeking an increase via a City Council ordinance exhibits a conflict of interest between Ms. Johnson’s action as City Treasurer and her obligations as a Board Member. Phila. Code §13-101(4)(b)(i).
48. If the Board denies PWD’s request for a 0.5% increase in the Capital Account Deposit, and all other factors are held constant, PWD may not need a rate increase in FY 2019 because the \$12 Million increase to the Capital Account Deposit exceeds PWD’s proposed net revenue increase for FY 2019. PWD St. 9A.
49. Ms. Johnson’s support of a 0.5% increase in the Capital Account Deposit demonstrates actual bias in favor of increasing customer rates.
50. Ms. Johnson should recuse herself due to her support of a \$12 Million increase in the Capital Account Deposit in FY 2019, without which PWD may have no need for higher FY 2019 rates.

WHEREFORE, on the basis of the foregoing, the Public Advocate submits that Ms. Johnson should recuse herself from participating in this FY 2019-2021 Rate Increase Proceeding.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'R.W. Ballenger', is written over a horizontal line.

Robert W. Ballenger
Josie B.H. Pickens
Joline R. Price
Philip A. Bertocci

For the Public Advocate

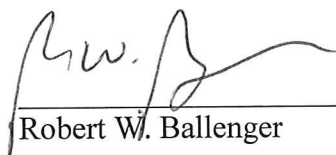
Community Legal Services, Inc.
1424 Chestnut Street
Philadelphia, PA 19102
(215) 981-3788
rballenger@clsphila.org

April 6, 2018

VERIFICATION

I, Robert W. Ballenger, hereby state that the facts above set forth are true and correct (or are true and correct to the best of my knowledge, information and belief) and that I expect to be able to prove the same at a hearing held in this matter. I understand that statements herein are made subject to the penalties of 18 Pa. C.S. § 4904 (relating to unsworn falsification to authorities)

April 6, 2018



Robert W. Ballenger

**Before the
Philadelphia Water, Sewer and Storm Water Rate Board**

In Re: Philadelphia Water Department :
Proposed FY2019-2021 : **Advance Notice Filed February 12, 2018**
Rate Increase :

**Public Advocate's Memorandum of Law in Support of
Motion for Recusal of Ms. Rasheia Johnson**

The Public Advocate hereby submits this memorandum of law in support of its Motion for Recusal of Ms. Rasheia Johnson from participation as a member of the Philadelphia Water, Sewer and Storm Water Rate Board (Board) in PWD's FY 2019-2021 rate increase proceeding.

I. INTRODUCTION

Ms. Rasheia Johnson was appointed to serve as Philadelphia's City Treasurer on January 19, 2016 and appointed to serve as a member of the Board on September 21, 2017. The Philadelphia Water Department (PWD) filed its Formal Notice of Proposed Changes in Water, Sewer and Stormwater Rates and Related Charges (FY2019-2021) on March 14, 2018. PWD requests the Board approve an increase of \$116 Million in net revenues, which would result in an approximately 11% increase in an average residential customer's monthly bills. PWD's request is predicated upon multiple financial assumptions, including forecast revenues, forecast operating expenses, debt service coverage, financing of capital improvements, and maintenance of reserves.

In support of its motion for recusal, the Public Advocate raises three significant due process concerns regarding Ms. Johnson's service on the Board:

(1) Ms. Johnson's service on the Board creates an appearance of bias due to her financial and fiduciary relationship with PWD and an actual conflict of interest due to the impact of the Board's rate determination upon her functions as City Treasurer. See Section III, infra.

(2) Ms. Johnson’s service presents an actual, impermissible conflict of interest due to her contractual authority, as City Treasurer, over PWD witnesses regarding the subject matter of PWD rates. See Section IV, infra.

(3) Ms. Johnson’s support, as City Treasurer, of pending legislation that would have mandated an increase in customer water rates demonstrates actual bias in favor of rate increases. See Section V, infra.

Each of these bases for Ms. Johnson’s recusal is discussed more fully in the sections that follow.

II. BACKGROUND

A. The Board’s Determination on PWD Rates and Charges Constitutes an Appealable Adjudication Implicating Due Process Requirements.

The Board’s final, appealable determination regarding PWD rates and charges constitutes an administrative adjudication under Pennsylvania law. In 2012, City Council passed a resolution and ordinance, providing for the submission of a voter referendum to establish an “independent” rate-making body to fix and regulate water and sewer rates and charges. Resolution 120188; Bill No. 120177. Following voter approval, City Council passed an ordinance establishing the Board to fulfill the will of the electorate. Bill No. 130251 (codified at Phila. Code §13-101) (hereinafter, “Rate Board Ordinance”). City Council established the Board as an “independent” unit of Philadelphia government, with the authority and obligation to preside over PWD rate proceedings, and to determine the rights of PWD and customers regarding the amount that may be lawfully charged for water, sewer and stormwater service. That the Board is statutorily required to be “independent” reflects City Council’s explicit acknowledgment of the due process implications of the Board’s determination, underscored by the prohibition on

conflicts of interest and the inclusion of a statutory right to appeal Board determinations. Rate Board Ordinance §§ 13-101(3)(b), 13-101(10).

The Board is a “Local Agency” under Pennsylvania Law,¹ and its actions are governed by Pennsylvania’s Local Agency Law. 2 Pa. C.S. §§ 105, 551-588; 751-754. The Board’s determination on rates and charges constitutes an “adjudication” defined as:

Any final order, decree, decision, determination or ruling by an agency affecting personal or property rights, privileges, immunities, duties, liabilities or obligations of any or all of the parties to the proceeding in which the adjudication is made. 2 Pa. C.S. § 101.

The adjudicatory nature of the Board’s determination is easily contrasted with the pre-Rate Board Ordinance framework of PWD ratemaking. Indeed the pre-Rate Board Ordinance framework, under which rates were set by the Water Department, by regulation, and without any statute or ordinance establishing an appeal right has been entirely abandoned through the establishment of an independent Board to which PWD must now apply for any change in rates and charges, with the decision *specifically subject to a 30-day right of appeal*.² Rate Board Ordinance §13-101(9).

Prior to the Rate Board Ordinance, two cases considered whether PWD rate making constituted an “adjudication” subject to due process standards. Both of those cases analyzed and relied upon the pre-Rate Board Ordinance framework for the establishment of PWD rates and charges, in which the PWD Commissioner both proposed and approved water rates under the then-existing statutory scheme of the Home Rule Charter and Philadelphia Code. See, e.g.,

¹ A “Local Agency” is defined to mean “a government agency other than a Commonwealth agency.” A “Government Agency” means “any Commonwealth agency or any political subdivision or municipal or other local authority, or any officer or agency of any such political subdivision or local authority.” See 2 Pa. C.S. § 101.

² The Board’s regulations incorporate further procedural safeguards reflecting the adjudicatory nature of its determinations, including standards for the conduct of public and technical hearings, discovery, submission of testimony, briefs, recommended decisions, exceptions, and the Board’s ultimate, appealable determination.

Consumer Educ. & Protective Ass'n Int'l, Inc. v. Philadelphia Water Dep't Com'r, 575 A.2d 160, 163 (1990), aff'd sub nom. Consumer Educ. & Protective Ass'n Int'l, Inc. v. Philadelphia Water Dep't, 600 A.2d 189 (1992) (hereinafter CEPA) (contrasting (1) the PUC statutory scheme of an administrative adjudication which provided appeal rights, with (2) the statutory scheme then set forth in the Philadelphia Code and the Charter, requiring the Water Department to establish rates by regulation, which did not provide appeal rights). In the most recent case addressing that historical, pre-Rate Board Ordinance framework for establishing rates, the Commonwealth Court held that the rate determination was not an appealable adjudication. Instead, the Commissioner's rate regulation could only be challenged by an original jurisdiction action in equity in Common Pleas Court. See Public Advocate v. Brunwasser, 22 A.3d 261 (Pa. Cmwlth. 2011). The Rate Board Ordinance completely changed the statutory framework for PWD ratemaking.

Unlike in Brunwasser and CEPA, as a result of the Rate Board Ordinance PWD must now seek permission from the Board to charge additional or different rates. PWD has no right to charge increased rates and charges unless the separate, "independent" Rate Board determines that PWD has presented a convincing need for increased rates and charges. The Board possesses the exclusive jurisdiction to evaluate PWD's request for such rates and charges. Similarly, the other parties have substantially different rights before an independent Board than they had when the PWD commissioner set rates. Indeed, the independent Board must reach a determination regarding other parties' proposed adjustments and/or opposition to PWD's request, and address other issues with a sufficient nexus to rates and charges, and those decisions must be based on substantial evidence on the record produced before the Board.

In enacting the Rate Board Ordinance, City Council's clear legislative intent was that the establishment of rates and charges be the subject of an administrative adjudication. City Council

mandated that the Board must apply the legal standard that rates be “just, reasonable and nondiscriminatory as to the same class of customers” in its determinations.³ In requiring the Board to be “independent”, and establishing that a conflict of interest constitutes cause for removal, City Council signaled the importance of impartiality and freedom from potential bias. Rate Board Ordinance §13-101(3). Finally, City Council specifically incorporated into the ordinance both the timing and venue for an appeal: “Any party to the proceedings of the Board affected by the Rate Report may appeal to the Court of Common Pleas in Philadelphia. Appeals shall be made within thirty (30) days of the filing of the Board’s Rate Report with the Department of Records.” Rate Board Ordinance §13-101(10). These requirements directly correspond to the appeal provisions for Local Agency adjudications pursuant to Pennsylvania’s Local Agency Law and the Judicial Code. See 2 Pa. C.S. § 752; 42 Pa. C.S. § 933(a)(2); 42 Pa. C.S. § 5571(b).

Under the pre-Rate Board Ordinance framework, the Commonwealth Court in the Brunwasser case decided that the establishment of PWD rates and charges was not an adjudication, based on three factors. First, rates and charges were set by regulation, pursuant to Section 8-407 of the Philadelphia Home Rule Charter. Although the Water Department provided a procedure which included a Hearing Officer, Public Advocate, and a recommended decision, the Water Commissioner retained substantial discretion to make a final determination. This process was deemed “investigatory” and culminated in the promulgation of a final rate regulation.⁴ Second, the ultimate decision regarding rates and charges was made by Water

³ See Action Alliance v. Phila. Gas Comm’n, 6 D&C 3d 144 (Phila. CCP 1977) (holding that the right to a “just and reasonable” rate structure required local agency due process protections to be observed).

⁴ Of course, the Board’s final determination regarding rates and charges is not a regulation. Indeed, under the framework of the Home Rule Charter, the Board cannot promulgate regulations governing the exercise of powers or performance of duties by another department such as PWD. In contrast, pursuant to

Commissioner. By definition, an adjudication determines the rights and obligations of the particular parties appearing before the agency. The Water Commissioner commenced the rate increase by filing proposed regulations, and determined its ultimate outcome by final regulation; the Water Commissioner was not a party appearing before an agency making a determination. Finally, the Commonwealth Court specifically recognized that, under the pre-Rate Board Ordinance framework, no statute or ordinance authorized appeals to the trial court.

Each of the three factors relied upon by the Commonwealth Court in Brunwasser have been eliminated by the Rate Board Ordinance. The Board's process of reaching a determination regarding PWD rates and charges now resembles the process of ratemaking for the Philadelphia Gas Works (PGW) that existed for many years prior to the Public Utility Commission acquiring ratemaking jurisdiction over PGW. The Philadelphia Court of Common Pleas, reviewing a rate determination made by the Philadelphia Gas Commission, determined that the Local Agency Law applied and that the Gas Commission's rate decision constituted an appealable adjudication. As a result, the Common Pleas Court held that federal and state due process protections applied in PGW rate making. Action Alliance v. Phila. Gas Comm'n, 6 D&C 3d 144 (Phila. Ct. Com. Pl. 1977); see also Public Advocate v. Phila. Gas Comm'n, 637 A.2d 676 (Pa. Commw. Ct. 1994), *reversed on other grounds*, 674 A.2d 1056 (Pa. 1996) (case commenced by cross appeals to the Philadelphia Court of Common Pleas of the Philadelphia Gas Commission's decision granting PGW rate increase). Ultimately, upon review of a determination by the Board, Pennsylvania Courts will reach the same conclusion: that the Board's determination constitutes an adjudication to which the due process protections of Local Agency Law apply.

its establishing ordinance, the Board can issue a final, appealable decision regarding PWD rates and charges.

B. Pennsylvania Law Requires that the Board Must Avoid Even the Appearance of Bias or Lack of Impartiality.

Because the Rate Board's determination of PWD rates and charges constitutes an appealable adjudication, the substantial body of due process case law in Pennsylvania requires that the Board must not only be impartial, but must avoid even the appearance of bias or impropriety. Pennsylvania Courts have incorporated the standard articulated by the U.S. Supreme Court in Commonwealth Coatings Corp. v. Continental Casualty, 393 U.S. 145 (1968) that "any tribunal permitted by law to try cases and controversies must not only be unbiased but must avoid even the appearance of bias." See Gardner v. Repasky, 252 A.2d 704 (Pa. 1969). This standard has been explicitly applied to Local Agencies, such as the Board. See Horn v. Hilltown Twp., 337 A.2d 858, 860 (Pa. 1975) ("[W]hile we are not faced with a tribunal that has allegedly denied due process to a litigant, we are presented with a governmental body [local zoning board] charged with certain decision-making functions that must avoid the appearance of possible prejudice, be it from its members or from those who advise it or represent parties before it.")

Under Pennsylvania case law, a susceptibility to prejudice or an appearance of bias must be prohibited in a Local Agency adjudication. A party is not required to show actual prejudice or bias on the part of a member of a Local Agency in order to show that individual should not be involved in rendering an adjudication.⁵ See, e.g., Horn, 337 A.2d at 860 ("[I]t is our opinion that such a procedure is susceptible to prejudice and, therefore, must be prohibited."); Bell v. City of Phila., Bd. of Pensions & Ret., 478 A.2d 537, at 538-39 (Pa. Commw. Ct. 1984) ("The principle that judicial proceedings must not only be unbiased, but must also avoid the appearance

⁵ Significant complementary case law applies this principle in Commonwealth Agency adjudications. See, e.g., Riverwalk Casino, LP v. Pennsylvania Gaming Control Bd., 926 A.2d 926, 939-940 (Pa. 2007) (citing Kuszyk, supra); Lyness v. State Board of Medicine, 605 A.2d 1204, 1210 (Pa. 1992)

of bias, is firmly entrenched in our law by a plethora of cases.”); Kuszyk v. Zoning Hearing Bd., 834 A.2d at 665 (Pa. Commw. Ct. 2003) (“The Court recognizes that due process requires a local governing body in the performance of its quasi-judicial functions to avoid even the appearance of bias or impropriety....A showing of actual bias is unnecessary to assert a cognizable due process claim; the mere potential for bias or the appearance of non-objectivity may be sufficient to constitute a violation of that right.”); FR & S, Inc. v. Comm. Dept of Env. Res., 537 A.2d 957, 965-66 (Pa. Commw. Ct. 1988) (“[R]egardless of best intentions, which we can presume the chairman has possessed, an appearance of bias has so tarnished these proceedings that the adjudication cannot be upheld.”); Purcell v. Reading Sch. Dist., 167 A.3d 216, 226 (Pa. Commw. Ct. 2017) (“Purcell does not need to prove a stacked deck to prevail; rather, all she needs to establish is that the District’s process was infected with ‘the appearance of non-objectivity.’”).

C. Recusal is Warranted and Proper Where a Board Member’s Service Creates an Appearance of Bias or Lack of Impartiality.

Upon identification of the appearance of potential bias or lack of impartiality, it is proper for a party to an administrative adjudication to request that the member of the agency recuse herself. Recusal motions are directed in the first instance to the official whose recusal is sought, for that official’s self-assessment. Reilly by Reilly v. Southeastern Pennsylvania Transportation Authority, 507 Pa. 204, 489 A.2d 1291 (1985); see also Appeal of Blystone, 600 A.2d 672, 674 (Pa. Commw. Ct. 1991) (“A trial court judge may decide his own recusal motion in the first instance.... We see no basis for a different rule for a Commissioner acting in his judicial capacity.”). Substantively, whether a Board member should recuse him- or herself turns upon that member’s relationship with the parties before the Board, that member’s apparent

predetermination regarding the subject matter before the Board, and/or that member's involvement in conflicting roles regarding the subject matter before the Board. Pennsylvania courts have held that: "Generally, recusal is warranted where a member of the tribunal participates as an advocate or witness, publicly expresses predisposition or has a financial interest or fiduciary relationship with a party in interest." Christman v. Zoning Hearing Bd. of Twp. of Windsor, 854 A.2d 629 at 633 (Pa. Commw. Ct. 2004) (internal quotations omitted). Similarly, participation in providing advice or opinion, as an attorney or otherwise, in the development of the basis for an application or petition to a local agency, is grounds for recusal, because such participation indicates the Board member may lack objectivity. See, e.g., Gardner v. Repasky, 252 A.2d 704 (Pa. 1969) (reversing suspension of employment where member of local agency participated in lodging complaint against employee and also presided over agency determination to suspend employment); Borough of Youngsville v. Zoning Hearing Bd. of Borough of Youngsville, 69 Pa. Cmwlth. 282, 289–91, 450 A.2d 1086, 1090–91 (1982) ("the fact that one of the Board members was employed to survey the property here concerned, coupled with his participation in an earlier proceeding as a witness in support of the appellee's proposed use, does raise a significant question as to his objectivity in this matter.").

As discussed more fully in each of the sections below, Ms. Johnson, who serves as the City Treasurer for the City of Philadelphia must recuse herself from participation in this Rate Proceeding. Ms. Johnson's service creates the appearance of bias and lack of impartiality, and her official roles with respect to PWD finances, supervisory authority over PWD witnesses, and demonstrated support of ordinances that impact upon customer rates and charges are sufficient to require her recusal.

III. MS. JOHNSON MUST RECUSE HERSELF DUE TO HER FINANCIAL AND FIDUCIARY RELATIONSHIP WITH PWD AND THE ACTUAL CONFLICT OF INTEREST PRESENTED DUE TO THE IMPACT OF THE BOARD’S RATE DETERMINATION UPON HER FUNCTIONS AS CITY TREASURER.

The Public Advocate submits that Ms. Johnson’s service as a member of the Board creates the appearance of bias, and potential actual bias, due to her clear conflict of interest between her official duties as the City Treasurer, with fiduciary responsibility concerning PWD financial affairs, and her role as a member of the Board charged with evaluating and making a final, appealable decision regarding PWD’s request for additional rates and charges. As the head of the City Treasurer’s Office, Ms. Johnson is charged with specific functions, of a fiduciary nature, regarding PWD and its finances. The decisions, judgments and prioritizing determinations she must make in the performance of those duties will be impacted by the outcome of this proceeding. Finally, PWD’s request for additional rates and charges seeks to obtain Board approval for rates based on projections of future financial needs which the City Treasurer and/or her agents have directly participated in crafting.

A. Ms. Johnson’s Financial and Fiduciary Relationship with PWD is Grounds for her Recusal.

A fiduciary is defined as: 1. One who owes to another the duties of good faith, trust, confidence, and candor. 2. One who must exercise a high standard of care in managing another’s money or property. Black’s Law Dictionary, 17th Ed. Ms. Johnson, the Philadelphia City Treasurer, has a fiduciary relationship with respect to PWD revenues. Indeed, Pennsylvania law establishes this fiduciary duty based on the City Treasurer’s status as the custodian of City funds:

It is *not* the law in Pennsylvania that a public official who is the custodian of public funds may properly use them for his own benefit, with his resulting liability being limited to his

official bond. On the contrary, all of our later cases hold that such funds do not belong to the official as his individual property but are public moneys held by him in a fiduciary capacity and for which he must account. Columbia Gas. Co. v. Westmoreland Cty., 74 A.2d 86, 88 (Pa. 1950) (emphasis supplied).

Mirroring the fiduciary standard pronounced in Columbia Gas, the City's Home Rule Charter clearly designates the City Treasurer as the custodian of City funds received from the Revenue Department (including water bill payments), and requires specific accounting and verification. See Phila. Home Rule Charter § 6-300. The City Treasurer also shares sole access with the City Controller to securities and uncanceled obligations of the City. Phila. Home Rule Charter § 8-105. Finally, the City Treasurer's fiduciary status is further substantiated by her oversight role with respect to the marketing and sale of PWD revenue bonds, upon which PWD relies for significant capital expenditures, and which are secured and supported by customer revenues. PA-I-1-PA-I-8; HO-I-1.

As PWD has acknowledged, sections of PWD's July 26, 2017 Official Statement, Series 2017B⁶ "generally describe the cash management and debt management services provided by the City Treasurer's Office." See PWD Objections, Response to PA-I-1 through PA-I-8. This Official Statement elaborates on these services, to an extent, clarifying that the City Treasurer's Office manages the City's debt program and serves as the disbursing agent for distribution of checks and electronic payments from the City Treasury and the management of cash resources. PWD Ex. 5 at IV-3. Regarding the management of cash resources, PWD provided quarterly reports from Standish and PFM Asset Management LLC, who both serve as investment advisors-managers regarding PWD investments in various funds and accounts. PA-I-13, PA-I-14. Those

⁶ PWD's Official Statement is included as Exhibit 5 to PWD's Formal Notice, available here: <https://beta.phila.gov/media/20180212151536/PWDEXhibit5OfficialStatementCityofPhiladelphiaWaterandWastewaterRevenueRefundingBondsSeries2017B.pdf>

investment managers are retained by the City Treasurer.⁷ Those funds and investments are “guided by the administrative direction of the City Treasurer per the Investment Committee and the Investment Policy.” PWD Ex. 5 at IV-75. The investment gains on those sums, consisting of non-operating revenues, are also included in the assumptions in this rate proceeding. See PWD St. 9 at 27-28. Furthermore, a representative of PWD (the Water Department’s Deputy Director of Finance or her designee) sits on the Investment Committee with the City Treasurer or her designee, in further demonstration of the City Treasurer’s close and ongoing relationship with PWD witnesses in this proceeding.⁸ PA-I-11; PA-1-12. That ongoing relationship, in which the City Treasurer establishes and provides administrative direction to ensure compliance with investment policy, is a fiduciary relationship. By law, the City Treasurer owes clear duties and must exercise the highest standard of care in managing PWD funds.

Regarding PWD’s bonds, the City Treasurer contracts with and oversees Financial Advisors, Bond Counsel and/or Disclosure Counsel, in the process of marketing and selling water and wastewater revenue bonds. The City Treasurer’s Office is specifically charged with the function of managing those debt issuances, with the goals of maximizing value to the City, managing and refinancing existing portfolios to decrease ongoing debt service costs, attracting and retaining investors, and improving and maintaining the City’s credit ratings. See PA-I-1, referring to <http://www.phila.gov/Treasurer/Pages/Functions.aspx>. As such, the City Treasurer is also required to exercise the highest level of care in managing the issuance of water and

⁷ According to the City’s eContract web portal, the City Treasurer’s Office posted a Notice of Intent to Contract with Standish on October 1, 2015 (Contract Opportunity Number: 21140115092058g) and a Notice of Intent to Contract with PFM Asset Management, LLC on December 16, 2014 (Contract Opportunity Number: 21140227155414).

⁸ As discussed more fully below, PWD estimates that the Water Department’s Deputy Commissioner of Finance and her assistant have exchanged a minimum of 4,000 emails with the City Treasurer and her office in recent months which may pertain to various financial assumptions or proposals relevant to this Rate Proceeding.

wastewater revenue bonds, and other debt issuances, again demonstrating that she functions as a fiduciary with respect to PWD obligations, which are secured and supported entirely by customer revenues.

Ms. Johnson should recuse herself because, as the City Treasurer, she has a financial interest and fiduciary relationship with a party in this proceeding. Ms. Johnson's participation on the Board creates the appearance of bias because her fiduciary obligations are likely to require her to uphold the interest of the party with whom she has that relationship. Indeed, that party, PWD, has a significant, at least \$116 Million interest in this proceeding. Ms. Johnson should recuse herself under the standard articulated in Christman, *supra* (recusal is warranted where a member of a tribunal has a fiduciary relationship with a party in interest).⁹

B. Ms. Johnson's Service Presents a Conflict of Interest Because Her Official Duties as City Treasurer Will Be Directly Impacted by the Board's Decision.

PWD's request for increased rates and charges relies significantly on assumptions surrounding and affecting current and future debt issuances and funding goals associated with capital projects, overall indebtedness, and credit ratings. PWD St. 2, Ex. ML-2. Ms. Johnson's actions in the performance of her official duties as City Treasurer will be directly impacted by the decision of the Board regarding those assumptions.

The Board is constitutionally required to balance the interests of PWD and its customers in making a rate determination. See Public Advocate v. Philadelphia Gas Comm'n, 674 A.2d 1056, 1061 (1996) ("[T]his Court is mindful that no applicable constitutional requirement is more exacting than the requirement of 'just and reasonable' rates....The Constitution leaves the states free to decide what ratemaking methodology best balances the interest of the utility and the

⁹ *A fortiori*, a financial or fiduciary relationship with a named party in an action is an even more significant basis for recusal than the existence of such a relationship with an interested party that is not named in the action.

public.”). The Rate Board Ordinance directs the Board to approve, modify or reject PWD’s proposed rates and charges, requiring the Board to conduct a balancing in determining just and reasonable rates. Rate Board Ordinance §§13-101(4)(b)(iii); 13-101(4)(b)(iv); 13-101(4)(d); 13-101(8). But Ms. Johnson’s duties as City Treasurer require that she give paramount importance to the interests of PWD, thus prohibiting her from legitimately performing all of the duties required of a Board member. Her service on the Board presents a clear conflict of interest. Furthermore, if Ms. Johnson participates as a member of the Board in rendering a determination on rates and charges, she will be presented with rate assumptions which the City Treasurer’s Office, which she heads, has participated directly or indirectly in formulating. Ms. Johnson cannot be expected to be unbiased or impartial when presented with information developed by, or in collaboration with, her office.¹⁰

The City Treasurer is specifically charged with the direct oversight of debt issuances for the Water Department, with the goal of maximizing value, decreasing ongoing debt service costs, attracting and retaining investors, and improving and maintaining credit ratings. See PA-I-1, referring to <http://www.phila.gov/Treasurer/Pages/Functions.aspx>. The ability to accomplish these goals depends on the availability of customer revenues to fund reserves and/or increase debt service coverage. Indeed, Fitch, Moody’s and S&P note their reported “stable outlooks” are based upon consistent rate increases and acknowledge that lack of consistent rate increases could cause negative ratings actions, whether due to a decline in coverage or a deterioration in cash or liquidity. See PWD St. 2, Schedule ML-4. Of course, debt service costs depend significantly on the credit rating of PWD’s revenue bonds. The ability to maintain or improve PWD’s credit rating depends in significant part upon the actions the Board may take in determining whether,

¹⁰ The extent of the City Treasurer’s Office’s participation with PWD and others in formulating rate assumptions in this proceeding is the subject of ongoing discovery, and discussed more fully below.

and if so how much, to increase PWD rates and charges. PWD's credit ratings are a required component of its Financial Stability Plan, which must be fully considered by the Board in fixing rates and charges. Rate Board Ordinance §13-101(4)(b)(i).

The Board's determination will, by necessity, impact upon the Ms. Johnson's obligations as City Treasurer. Ms. Johnson's service on the Board presents a conflict of interest, where her contribution to the Board's determination impacts upon her ability to achieve the specific functions of her office. Ms. Johnson is conflicted because her objectives as City Treasurer are likely to be furthered by an increase in rates even if the record in this proceeding supports denying some or all of the rate request.

C. Ongoing Responses to Discovery Requests, as Well as Publicly Available Information, Substantiate the City Treasurer's Involvement in Formulating Financial Assumptions in this Rate Proceeding.

As discussed above, the City Treasurer's Office is directly responsible for cash management and debt management services for PWD, with oversight responsibility regarding the investment of PWD funds, the sale of water and wastewater revenue bonds, and the management of advisors, consultants, and counsel in such transactions. In this capacity, the City Treasurer's Office, through its close working relationship with PWD and its oversight of cash and indebtedness, is directly involved in the formulation of financial assumptions presented by PWD in this proceeding. In multiple discussions regarding PWD discovery objections and insufficient responses, PWD counsel has distinguished the manner in which Ms. Johnson is involved, as compared to her predecessor, but has not clearly or convincingly denied her involvement. PWD's response to a Hearing Officer discovery request acknowledges the City Treasurer's involvement. HO-I-1.

Through discovery in this proceeding, the Public Advocate has sought to understand the City Treasurer's involvement more fully. However, as a result of PWD's repeated attempts to obstruct discovery concerning the direct and indirect role the City Treasurer plays in the formulation of financial assumptions utilized in this rate proceeding, the public is being denied access to an open and transparent rate process, contrary to the express requirements of the ordinance establishing the Board. Rate Board Ordinance §13-101(3)(e). Although discovery is ongoing, the ability of the public to express their input and comment regarding concerns of bias and lack of impartiality is being impeded by vague, insufficient, and unclear PWD responses to Public Advocate discovery requests. PWD's refusal to clearly and completely respond to discovery questions is astonishing and indicative of the extent to which PWD seeks to obscure Ms. Johnson's direct and indirect involvement in PWD financial matters.

PWD has consistently objected to answering questions regarding the City Treasurer's involvement with and participation in the development of financial assumptions utilized in this rate proceeding. The Public Advocate issued three discovery requests, narrowly focused on the relations between the City Treasurer's Office and PWD, seeking to obtain copies of recent correspondence between (1) PWD and the City Treasurer regarding PWD financial status and performance, (2) PWD and the City Treasurer's Office regarding proposed City Council legislation that would directly mandate an increase in customer rates (discussed more fully below), and (3) PWD and the City Treasurer's Office regarding PWD's proposed rate increase.¹¹

¹¹ These three requests were as follows:

PA-I-17. Please provide copies of all correspondence (written, electronic or otherwise) between the Philadelphia Water Department and the City Treasurer from September 14, 2017 through present, regarding:

- a. PWD revenue bonds.

In support of its objections to these requests, PWD submitted that, solely on the basis of discussions with its Deputy Commissioner of Finance (Ms. LaBuda) and her assistant (Ms. Rogers), *there are a minimum of 4,000 emails that may be relevant to these three responses.* See March 23 Ruling on PA Set I Discovery. The sheer extent of recent communication between PWD and the City Treasurer's Office regarding matters relevant to this proceeding is startling and indicates the significant, ongoing relationship between the City Treasurer and PWD regarding the subject matter of this rate proceeding.

Rather than requiring PWD to cull through the more than 4,000 emails, on March 23, 2018, Hearing Officer Brockway entered an order requiring PWD to provide written responses to two questions concerning advice, suggestions, recommendations or requests from the Office of City Treasurer regarding a range of PWD financial issues.¹² Remarkably, while the Hearing

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- b. PWD indebtedness other than revenue bonds.
 - c. PWD revenues.
 - d. PWD financial performance.

PA-I-18. Please provide a copy of all correspondence (written, electronic or otherwise) between the Water Department and the City Treasurer's Office regarding 2017 proposed legislation amending PWD's general bond ordinance, currently designated City Council Bill No. 171110.

PA-I-20. Please provide a copy of all correspondence (written, electronic or otherwise) between the Water Department and the City Treasurer's Office regarding PWD's proposed rate increase for FY 2019-2021.

¹² See March 23 Hearing Officer Ruling on Objections to PA Set I Discovery, at 6-7:

For the above reasons, I deny the motion to compel, subject to the Department's providing within one week (by Friday, March 30, 2018) its answers to the following questions:

1. Please state what the Deputy Director for Finance remembers about advice, suggestion, recommendation or requests, if any, from the Office of the City Treasurer to the Department regarding PWD revenue bonds, PWD indebtedness other than revenue bonds, PWD revenues, PWD financial performance, PWD financial goals, and assumptions on these topics to be included in the Financial Stability Plan and the rate case.

Officer's questions clearly asked PWD's Deputy Commissioner of Finance and her assistant to respond personally based on their recollections, PWD instead utilized its Financial Advisors to provide a sanitized description of the bond offering process, PWD non-current liabilities (indebtedness), and financial plan assumptions, performance and statements. HO-I-1. PWD fails to respond at all to the Hearing Officer's request that PWD explain the City Treasurer's Office's involvement regarding PWD revenues. HO-I-1. What response PWD does provide to HO-I-1 raises further questions due to its inconsistency with other statements, including public statements by the City Treasurer and statements made by PWD witnesses in the 2016 rate proceeding.¹³ For example, PWD states that Melissa LaBuda and Jaclyn Rogers lead the Department's efforts with respect to rating agency matters, and that the City Treasurer's Office provides assistance only if "questions arise regarding other City related issues and concerns." HO-I-1 at 5. In contrast, Ms. Johnson's Fiscal Year 2018 Budget Testimony flatly states: "the CTO manages the City's credit relationship with the three major rating agencies."¹⁴

In two written requests, the Public Advocate sought to confirm the City Treasurer's specific role in establishing PWD interest rate assumptions and debt service projections. PWD consistently provided insufficient, unclear and/or unconvincing responses. However, as discussed below, the information PWD provided, as well as publicly available information,

2. To the extent different from or additive to the statement of the Deputy Director for Finance, please state what the Assistant to the Deputy Director for Finance remembers about advice, suggestion, recommendation or requests, if any, from the Office of the City Treasurer to the Department regarding PWD revenue bonds, PWD indebtedness other than revenue bonds, PWD revenues, PWD financial performance, PWD financial goals, and assumptions on these topics to be included in the Financial Stability Plan rate case.

¹³ See *infra* notes 15, 16, 18; April 5, 2016 Rate Board Hearing Transcript at 107, available at: <https://www.phila.gov/water/rateboard/Transcripts/4.5.16.Transcript.pdf>.

¹⁴ This testimony is available at http://phlcouncil.com/wp-content/uploads/2017/04/FY18-CTO-Budget-Testimony_4.3.17.pdf.

clearly establish the City Treasurer is involved in the formulation of these specific financial assumptions.

The Public Advocate requested that PWD confirm or deny the City Treasurer's role in establishing PWD interest rate assumptions, as was discussed in the 2016 rate proceeding.¹⁵ In response, PWD claimed that the City Treasurer's Office "does not utilize the same approach" to formulating these assumptions that was described by PWD witnesses in the 2016 Rate Proceeding.¹⁶ PA-I-9.¹⁷ In distinguishing the current approach to formulating interest rate assumptions, PWD appears to acknowledge that the City Treasurer's Office remains involved in this process, albeit in some different way. Indeed, PWD cannot deny the City Treasurer's

¹⁵ This interrogatory stated:

PA-I-9. Reference the April 5, 2016 transcript in the 2016 rate proceeding, at Page 107 (explaining the City Treasurer's Office's practice for formulating interest rate assumptions in the Water Department's debt service budget):

- a. Does the City Treasurer's Office utilize the same practice to formulate interest rate assumptions for the Water Department's debt service that was described in the April 5, 2016 transcript in the 2016 rate proceeding, at Page 107?
- b. If the answer to PA-I-9(a) is anything other than an unequivocal "yes," please provide a description of the practice used to formulate the interest rate assumptions for the Water Department's debt service.
- c. Please identify all individuals, by name and title, who participated in formulating the interest rate assumptions for the Water Department's debt service shown in the filing (reference Schedule BV-E1, Table C-9).

¹⁶ See April 5, 2016 transcript in the 2016 rate proceeding, at Page 107 (explaining the City Treasurer's Office's practice for formulating interest rate assumptions in the Water Department's debt service budget), available at: <https://www.phila.gov/water/rateboard/Transcripts/4.5.16-Transcript-mini.pdf>

¹⁷ PWD failed to identify all individuals, by name and title, who participated in formulating the interest rate assumptions shown in PWD's filing, as requested by the Public Advocate. PA-I-9(c). The March 23 Hearing Officer Ruling on Objections to PA Set I Discovery did not reach this aspect of the dispute concerning PWD's insufficient responses to PA-I-9. The Public Advocate submitted, in its Answer to PWD Objections And Motion to Compel Responses to Discovery Requests, at 14, submitted on February 26, 2018:

A complete list of all persons who participated in in [sic] formulating the interest rate assumptions for PWD debt service, including personnel at PWD and the City Treasurer's Office, as well as outside consultants, should be provided in response to PA-I-9(c).

Office's involvement since PWD acknowledges that the interest rate assumptions were made "in consultation with" financial advisors, PFM and Acacia Financial. PA-I-9. Those financial advisors serve pursuant to contracts with the City Treasurer's Office, as discussed more fully below, and it should be presumed that part of the "consultation" PWD describes involved the City Treasurer's Office. Accordingly, whether by direct involvement or through its agents, the City Treasurer's Office, led by Ms. Johnson, continues to be involved in formulating interest rate assumptions which underpin PWD's rate request.

The Public Advocate also requested that PWD confirm or deny the City Treasurer's Office's involvement in establishing PWD's debt service budget. See PA-I-10(a).¹⁸ PWD repeatedly avoided providing a clear answer. In its third attempt to respond to PA-I-10(a), PWD stated: "The response to this question is not an unequivocal yes or no. The Water Department works with multiple stakeholders to formulate its debt service budget."¹⁹ PWD did not deny that the City Treasurer's Office is involved in this process, and, indeed, specifically acknowledged

¹⁸ This interrogatory stated:

PA-I-10. Reference PWD Statement No. 2 in the 2016 rate proceeding (Direct Testimony of Melissa LaBuda), at Page 18 ("As part of the City's budgeting process, the Department works with the City of Philadelphia Treasurer's Office to establish the Department's debt service budget for the following five fiscal years"):

- a. Does the Water Department work with the City Treasurer's Office to establish its debt service budget as part of the City's budgeting process, including projected debt service for five fiscal years, as described in the 2016 rate proceeding?
- b. If the answer to PA-I-10(a) is anything other than an unequivocal "yes," please provide a description of the practice used to establish the Water Department's debt service budget as part of the City's budgeting process.
- c. Please identify all individuals, by name and title, who participate in establishing the Water Department's debt service budget as part of the City's budgeting process.

¹⁹ This is a legally insufficient answer, for which the Public Advocate requested sanctions. The City Treasurer is most certainly one of the "multiple stakeholders," and PWD's answer is deliberately obtuse and misleading.

that the answer is not “no.” Pursuant to the direction of the Hearing Officer, PWD was required to provide a yes or no answer, and in its fourth attempt to respond to PA-I-10(a), PWD submitted as follows:

No, the Department does not work with the City Treasurer’s Office to establish its debt service budget. This response should be reviewed with the considerations below. The Water Department works with multiple stakeholders to formulate its debt service budget. See explanation below.²⁰

This response continues to be equivocal, indicating that PWD’s “no” is not absolute, but must be reviewed in light of other considerations.²¹ Indeed, PWD simply cannot convincingly deny that it works with the City Treasurer’s Office to formulate its debt service budget because the City Treasurer’s Office is directly or indirectly involved in that process and is, at a minimum, a stakeholder with whom such information is shared outside the confines of PWD’s rate proceeding.

In response to PA-I-10(b), PWD states: “The Department’s Five-Year Plan debt service budget is formulated in consultation with the Department’s financial advisors, PFM and Acacia Financial, in addition to using the Black & Veatch projected total capital program expenditures and construction fund cashflow.” Again, PFM and Acacia Financial serve as financial advisors pursuant to contracts with, and subject to direction by, the City Treasurer’s Office, as discussed more fully below. The Public Advocate submits that the “consultation” described by PWD necessarily includes the City Treasurer’s Office.

Finally, in response to PA-I-10(c), requesting that PWD identify all individuals involved in establishing the Water Department’s debt service budget, PWD states: “The projected debt issuance as well as current debt payments due and payable are summarized and sent to the

²⁰ The term “see explanation below” apparently refers to PWD’s responses to PA-I-10(b) and PA-I-10(c), neither of which provides adequate explanation, as discussed herein.

²¹ As set forth in the March 23 Hearing Officer Ruling on Objections to PA Set I Discovery, at 7, PWD argued that its response was “necessarily nuanced” and that “a team of people” are involved.

Executive Director of the Sinking Fund Commission, Matthew Bowman, for inclusion in the Sinking Fund Commission budget.” Noticeably, PWD’s response indicates who receives the information regarding estimated projected debt service payments, rather than identifying who formulates those projections. Although PWD acknowledges in argument that a team of people are involved in these calculations, it flatly refuses to identify them in response to the Public Advocate’s clear request.²² Still, PWD’s response (regarding the Sinking Fund Commission) continues to demonstrate the City Treasurer’s Office’s involvement in establishing the debt service assumptions for water and wastewater revenue bonds which is transmitted to the Sinking Fund Commission. The City’s FY 2019-2023 Five Year Plan, submitted to City Council on March 1, 2018, recognizes that the City Treasurer operates various programs to accomplish its functions, including debt management, banking and investment management, and the *sinking fund*.²³ Indeed, the mission of the Sinking Fund Commission is “[t]o efficiently pay appropriate debt service and bills for the City of Philadelphia Treasurer’s Department.”²⁴ The budget for the single employee of the Sinking Fund Commission is included in the City Treasurer’s budget.²⁵ The Public Advocate submits that the City Treasurer is involved, directly and indirectly, in the formulation of projected water and wastewater bond debt service assumptions.

²² The March 23 Hearing Officer Ruling on Objections to PA Set I Discovery did not reach this aspect of the dispute concerning PWD’s insufficient responses to PA-I-10. The Public Advocate requested the Hearing Officer order complete response to PA-I-10(c) in its Answer to PWD Objections And Motion to Compel Responses to Discovery Requests, at 15, submitted on February 26, 2018:

The Public Advocate respectfully requests the Hearing Officer order PWD to provide a complete response to PA-I-10(c), which requests identification of “all individuals, by name and title, who participate in establishing the Water Department’s debt service budget as part of the City’s budgeting process.”

²³ Five Year Financial and Strategic Plan for Fiscal Years 2019-2023, at 91, available at <http://phlcouncil.com/wp-content/uploads/2018/03/FY19-23-Five-Year-Plan.pdf>.

²⁴ Sinking Fund Commission FY 2017 Budget Testimony, available at: <http://phlcouncil.com/wp-content/uploads/2016/04/Sinking-Fund-Commission-Testimony-April-05-2016.pdf> (emphasis added).

²⁵ Sinking Fund Commission FY 2018 Budget Testimony, available at: <http://phlcouncil.com/wp-content/uploads/2017/04/FY18-Sinking-Fund-Testimony-submitted-4.3.17.pdf>.

Ms. Johnson's uncontestable statutory obligations, as City Treasurer, require her to participate in the major financing decisions affecting PWD. PWD's insufficient and unclear responses to discovery requests nevertheless establish that she exercises those duties. On that basis, Ms. Johnson's service on the Board creates an appearance of bias and potential actual bias that requires her recusal.

IV. MS. JOHNSON SHOULD RECUSE HERSELF DUE TO HER AUTHORITY OVER WITNESSES IN THIS PROCEEDING.

The Public Advocate submits that Ms. Johnson's service as a member of the Board is impermissible due to the City Treasurer's contractual authority over PWD witnesses. Ms. Johnson's participation on the Board creates a clear appearance of bias and lack of impartiality due to her contract authority over PWD's Financial Advisors and Bond Counsel, whose statements have been offered on the record and will testify at Technical Hearings in this proceeding. Bond Counsel and Financial Advisors seek to support PWD's request for an increase in rates and charges pursuant to their contracts with the City Treasurer's Office, under which they provide related services to the City Treasurer's Office. Ms. Johnson must not be allowed to participate in decisions of the Board, which require weighing evidence submitted by witnesses performing services pursuant to contracts Ms. Johnson signed as City Treasurer.

PWD's filing includes a Memorandum from Bond Counsel and a Memorandum from Financial Advisor. PWD St. 2, Ex. ML-3 and Ex. ML-4. Bond Counsel (Valerie Allen, Ballard Spahr) and Financial Advisors (PFM and Acacia Financial) have historically served as witnesses in PWD rate proceedings. Indeed, Bond Counsel and PFM have provided responses to data requests and will thus be proffered for examination in technical hearings in this proceeding.

In response to discovery requests, PWD provided copies of the contracts for Financial Advisors, PFM and Acacia Financial. PA-V-84; PA-V-85. These contracts confirm that these parties, hired by the City Treasurer's Office, are providing services as witnesses under the direction and control of the City Treasurer.²⁶ Furthermore, the Request for Proposals, Opportunity No. 21150929134050, issued by the City Treasurer's Office on October 1, 2015, seeking Financial Advisors for the Philadelphia Water Department specifically includes within the expected scope of services "providing ongoing support for rate case peer analysis and testimony" and reviewing and commenting on "Cost of Service Financial Plans."²⁷ Both PFM and Acacia Financial were selected to provide services under this contract, via Notices of Intent published on January 7, 2016.²⁸ The RFP makes clear that, in addition to services directly related to the financing, structuring and issuing of revenue bonds, providing "ongoing support" for rate case analysis, testimony and review of Cost of Service Financial Plans is a *required service* under the Financial Advisors' contracts with the City Treasurer.

PFM's scope of work, incorporated into its contract to serve as Financial Advisor, does not provide any further detail regarding its proposed work product to provide the required service in support of PWD's rate increase request. However, PFM does indicate it is "fully prepared" to provide those services, and acknowledges its past testimony at PWD rate hearings. Indeed, PFM highlights that, at the time of its proposal, it was "currently working with PWD in preparing its Financial Stability Plan as required by the Rate Ordinance" for purposes of supporting a request

²⁶ See also April 26, 2017 Committee of the Whole Hearing Transcript, at 88-89, available at <http://legislation.phila.gov/transcripts/Public%20Hearings/whole/2017/wh042617.pdf> (discussing the hiring of PFM and Acacia Financial by the City Treasurer's Office).

²⁷ This document may be obtained from the City's eContract website, at the following address: <https://secure.phila.gov/ECONTRACT/documents/frmPDFWindow.aspx?docid=211509291340500211509301022251N&ext=pdf>

²⁸ The most recent renewals of these contracts were executed by Ms. Johnson. PA-V-84, Attachment; PA-V-85, Attachment.

for higher rates and charges. PA-V-84, Attachment, PFM Proposal at 3. Acacia Financial, on the other hand, indicates that it has previously provided rate case peer analysis and testimony support services to other clients and “is prepared to assist PWD” with those services. PA-V-85, Attachment, Acacia Financial Proposal at Ex. A, 2.

Similarly, in response to a discovery request, PWD provided a copy of the contract for Bond Counsel, Ballard Spahr. PA-V-86. This contract confirms that Bond Counsel, hired by the City Treasurer’s Office, is providing services as a witness and advisor under the direction and control of the City Treasurer.²⁹ The Request for Proposals, Opportunity No. 21160811105157, issued by the City Treasurer’s Office on August 16, 2016, seeking Bond Counsel and Disclosure Counsel for PWD and PGW, requires respondents to address specific questions about PWD rates, address any special challenges or complications posed by a substantial increase in capital funding needs, and describe any challenges or concerns regarding the Board’s findings in the 2016 rate proceeding.³⁰

In response to these specific requests, Ballard Spahr states it supported PWD in the 2016 rate proceeding, including reviewing presentations and testimony to be submitted to the Board, and participated in hearings as a witness. PA-V-86, Attachment, Ballard Proposal at 7.

Regarding capital funding challenges, Ballard Spahr responded as follows:

PWD derives capital funding from two sources: debt and pay-go. To the extent PWD has to increase its indebtedness, the concern is that it will over leverage and not be able to meet its rate covenant over the long term. The solutions are to raise rates and thereby increase coverage, increase the rate stabilization fund so that there is a reserve available

²⁹ This contract was executed by Ms. Johnson. PA-V-86, Attachment.

³⁰ This document may be obtained from the City’s eContract website, at the following address: <https://secure.phila.gov/ECONTRACT/documents/frmPDFWindow.aspx?docid=211608111051570211608151630131N&ext=pdf>. It should be noted that Andre C. Dasent, P.C., was also selected to provide services as Bond Counsel to the City Treasurer’s Office pursuant to the same RFP by Notice of Intent published February 28, 2017. Mr. Dasent serves as PWD’s counsel in this proceeding pursuant to a separate contract. This is yet another example of potential conflicts posed by having the head of the City Treasurer’s Office serve on the Board.

to manage coverage, or raise pay-go relative to debt. The challenge is that all three of these solutions require raising or structuring rates and charges for such purposes, which means the independent rate board, in the face of opposition from the public advocate, must buy into and support the effort through rate setting. PA-V-86, Attachment, Ballard Proposal at 8.

Regarding the Rate Board's finding in the 2016 proceeding, Ballard Spahr states that the 2016 rate proceeding was "the first time that the PWD sought to submit a lean and exacting proposal without any cushion for risk, or negotiation." PA-V-86, Attachment, Ballard Proposal at 10. Ballard Spahr indicates the Board's findings "were conservative in terms of granting PWD the rate increases and structural changes proposed." *Id.* Finally, it identifies "the challenge going forward" as having to "educate the Board – and the rate payers – in a nonadversarial setting concerning the pressure points for the PWD financial operations and sustainability." *Id.*³¹

Financial Advisors and Bond Counsel providing testimony and support to PWD in this rate proceeding serve the City Treasurer's Office. For the City Treasurer to stand in judgment of the weight to be given to witnesses that she hired and documentation prepared by such persons would clearly demonstrate likely bias and predetermination that is impermissible in a Local Agency Adjudication. The Public Advocate submits that it is inappropriate for Ms. Johnson, as head of the City Treasurer's Office, to serve on the Board and evaluate the testimony of those consultants and counsel hired by her. Ms. Johnson must recuse herself in order to alleviate the appearance of bias presented by the service of witnesses for PWD who are under the contract authority of Ms. Johnson's office and who were retained on the explicit assumption that their service in support of higher rates would be indispensable to the City Treasurer's Office.

³¹ The Public Advocate finds Bond Counsel's assertion that Board members should be educated about PWD financial matters in a nonadversarial setting troublesome. Any such efforts, undertaken outside of the rate proceeding (which is an adversarial setting) would appear to violate the City's ethics rules concerning ex parte communication. See Phila. Code § 20-605.

V. MS. JOHNSON SHOULD RECUSE HERSELF DUE TO HER SUPPORT, AS CITY TREASURER, OF AN APPROXIMATE \$12 MILLION INCREASE IN THE CAPITAL ACCOUNT DEPOSIT, PAID FOR BY RATES.

Ms. Johnson, as head of the City Treasurer's Office, appears before City Council in support of ordinances overseen by her office that authorize the issuance of water and wastewater revenue bonds and amend the provisions that apply to water and wastewater revenue bonds. See PA-I-16; March 19, 2018 Testimony of R. Johnson Re: Bill Nos. 171110 and 171111. In so doing, Ms. Johnson, as the head of the City Treasurer's Office, participates directly in key drivers of financial assumptions regarding current and future customer rates, which are the subject of the rate proceeding currently before the Board.³² Two ordinances are currently pending before City Council that would authorize new bond issuances and refunding transactions, and amend the long-standing General Bond Ordinance governing water and wastewater revenue bonds. Ms. Johnson and PWD's Deputy Water Commissioner, Ms. LaBuda, testified together in support of these ordinances on March 19, 2018.

As introduced, Bill No. 171110 would have imposed a mandatory 0.5% increase in the Capital Account Deposit paid for through customer rates. This change would directly contribute to an increase in customer funding of capital expenditures through current revenues. Pursuant to the Rate Board Ordinance, the Board is specifically vested with the power and authority to determine "the extent to which current revenues should fund capital expenditures" in establishing rates and charges, and must set forth that determination in its appealable Rate Report. Rate Board Ordinance §13-101(4)(b)(i). In response to discovery requests, PWD acknowledged that the City Treasurer's Office "coordinates all City related debt ordinances" including Bill No.

³² As shown in PWD St. 9A, Sch. BV-E1, Table C-1, during the rate period, senior debt service is projected at approximately \$200 Million per year.

171110. PA-I-16. Ms. Johnson's support, as City Treasurer, of an ordinance to increase the funding of PWD capital expenditures from current revenues, outside of the context of a rate proceeding, directly contravenes and conflicts with her obligations as a Board member pursuant to the Rate Board Ordinance.

Under PWD's General Bond Ordinance, the Capital Account Deposit is calculated as 1% of the depreciated value of property, plant and equipment of the water and wastewater system. See PA-I-21, Attachment (Restated General Bond Ordinance). As shown in Assumptions-21 of PWD Exhibit 6, PWD has provided the underlying assumptions upon which its Capital Account Deposit is forecast. During the rate period, PWD estimates the value of its property, plant and equipment will increase by 3.4% each year. Putting aside whether this estimate is reasonable, the amount by which rates would have to increase over the three years in PWD's rate case,³³ solely as a result of a 0.5% change in the Capital Account Deposit, can be calculated as follows:

<u>Year</u>	<u>Net PPE</u>	<u>Deposit @ 1.00%</u>	<u>Deposit @ 1.50%</u>	<u>Difference</u>
2019	\$2,384,466,666.67	\$23,844,666.67	\$35,767,000.00	\$11,922,333.33
2020	\$2,465,533,333.33	\$24,655,333.33	\$36,983,000.00	\$12,327,666.67
2021	\$2,549,400,000.00	\$25,494,000.00	\$38,241,000.00	\$12,747,000.00
			<u>TOTAL</u>	<u>\$36,997,000.00</u>

In addition, an increase in the Capital Account Deposit directly affects coverage requirements under the Bond Ordinance. As explained by Black & Veatch, the rate covenant requires that:

[I]n each fiscal year, water and wastewater rents, rates, fees, and charges shall yield net revenues which shall be at least equal to 1.00 times the sum of the following:

- the debt service requirements for such fiscal year (including debt service requirements in respect of Subordinated Bonds);
- amounts required to be deposited into the Debt Reserve Fund during such fiscal year;

³³ If this amendment to the Bond Ordinance were approved, the additional rate demand placed on customers would continue to increase in years beyond the three year rate period and the Board would have no power or authority to reduce the 1.5% Capital Account Deposit.

- the principal or redemption price of and interest on General Obligation Bonds issued to fund capital expenditures of the water and wastewater systems payable during such fiscal year;
- debt service requirements on interim debt payable during such fiscal year; and
- *the Capital Account Deposit for such fiscal year (less any amounts transferred from the Residual Fund to the Capital Account during such fiscal year).*

See PWD St. 9A at 44-45 (emphasis added).

Accordingly, increasing the Capital Account Deposit reduces coverage, putting pressure on PWD to further increase rates and charges. Indeed, based on Black & Veatch's calculations, shown in Schedule BV-E1, Table C-1, PWD's total coverage declines from 1.23x³⁴ to 1.08x in FY 2019. PWD St. 9A, Sch. BV-E1. If the Capital Account Deposit used in these calculations is reduced by \$11,922,333.33 for FY 2019 (the amount by which PWD's Capital Account Deposit increases due to the additional 0.5% proposed, shown above), PWD's total coverage would increase to 1.14x, demonstrating that the proposed 0.5% increase to the Capital Account Deposit has at least a 0.06x impact on coverage in a single year.

On March 19, 2018, Bill No. 171110 was amended to eliminate the change in the Capital Account Deposit that would have required an additional \$12 million in customer rates and charges to be deposited in the Capital Account and increased pressure on PWD's coverage requirements.³⁵ Rather than remedying the clear conflict posed by Ms. Johnson's support of this legislation as introduced, the amendment now leaves only one potential venue for PWD and the City Treasurer's Office to pursue their shared objective to increase the Capital Account Deposit – the rate proceeding pending before the Board. Indeed, all other factors remaining the same, PWD may not require a rate increase in FY 2019 if the Board rejects the requested increase in

³⁴ It should be noted that this high coverage level is partially attributable to significant "Other Operating Revenue," primarily as a result of a \$19 million release from the Debt Service Reserve. See PWD St. 9A, Sch. BV-E1, Table C-3.

³⁵ See March 19 Committee of the Whole Hearing Transcript, available at <http://legislation.phila.gov/transcripts/Public%20Hearings/finance/2018/fi031918.pdf>.

the Capital Account Deposit, since PWD's requested FY 2019 rate increase is \$9.2 million, more than \$2.5 LESS than the amount by which it seeks to increase its Capital Account Deposit.

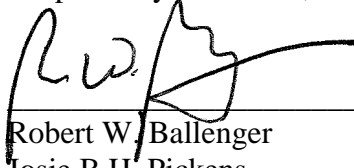
PWD St. 9A at 22, 41.

Based on Ms. Johnson's public support of Bill No. 171110, in her capacity as City Treasurer, the Public Advocate submits that Ms. Johnson's service on the Board would violate due process. Although all that is required to support her recusal is the appearance of impartiality and bias, it is apparent that, in supporting an ordinance that would mandate an immediate increase in customer rates, Ms. Johnson is actually partial and biased in favor of increasing the Capital Account Deposit, a crucial assumption in PWD's proposed rate increase.

VI. CONCLUSION

The Public Advocate represents the interests of the approximately half-million small user customers who rely upon the Board to balance their need for affordable water and wastewater service against PWD's interests in higher rates. In addition to requirements on the Board in reaching its substantive determination on rates and charges, within the bounds of the constitutionally-based requirement that rates be just and reasonable, the interests of these customers in a fundamentally fair rate proceeding, before an impartial Board, must be preserved. Due to the clear appearance of bias and lack of impartiality presented by Ms. Johnson's service, as well as her actual bias in favor of measures which would increase rates and charges, the Public Advocate respectfully submits that Ms. Johnson may not permissibly participate in the Board's Rate Determination and must recuse herself.

Respectfully submitted,



Robert W. Ballenger
Josie B.H. Pickens
Joline R. Price
Philip A. Bertocci

For the Public Advocate

Community Legal Services, Inc.
1424 Chestnut Street
Philadelphia, PA 19102
215-981-3788

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