



Backgrounder: *Fair Market Value Legislation*

FAIR MARKET VALUE LEGISLATION

About Fair Market Value Legislation

Small and midsize municipal utilities are facing significant infrastructure needs and increasing compliance regulations at the same time their budgets are shrinking and other local priorities are competing for resources.

The U.S. Environmental Protection Agency estimates that more than \$600 billion is needed over the next 20 years to fund the improvements necessary to provide safe drinking water and reliable wastewater services to our nation's homes and businesses.ⁱ

Given the extremely small amount of government funding available for water infrastructure and the limited bonding capacity of small and midsize municipalities, utilities across the country are being left without access to the funding and expertise necessary to operate and adequately maintain their drinking water and wastewater utilities.

The **voluntary** sale of water and wastewater systems to an experienced water operator is a proven method for municipalities to gain access to the resources necessary to enable urgent infrastructure investments and provide greater expertise to their water systems.ⁱⁱ Even those municipalities that do not face urgent infrastructure challenges have found voluntarily selling water and wastewater systems to professional water operators to be an effective way to offload risk, monetize assets, and focus resources on other local needs and priorities.

However, the sale of a water or wastewater system is a complex process, and all parties need assurances that they are getting a good deal. Fair Market Value (FMV) legislation establishes a clear process to calculate a reasonable and fair value for a municipality's assets via independent valuation experts.

Here are answers to four common questions on Fair Market Value legislation.

1. What does Fair Market Value legislation do?

Traditionally, the acquisition prices for water and wastewater systems are calculated at book value, which is the original cost of system assets minus depreciation. This valuation approach considerably undervalues the assets of troubled water and wastewater systems, because it does not account for capital investments made over several decades.

The current valuation process therefore discourages municipalities from selling their water systems. By discouraging sales and acquisitions, book value calculations limit the options available to municipalities facing urgent water and wastewater infrastructure challenges.ⁱⁱⁱ Fair Market Value (FMV) legislation establishes a transparent process for independent valuation experts to use to calculate a reasonable and fair value for a municipality's water system assets subject to approval by the state's Public Utility Commission.^{iv} Fair Market Value legislation clarifies the acquisition process and benefits for the community, water and wastewater systems and customers.

2. Who benefits from Fair Market Value legislation?

Experts agree that Fair Market Value is a win-win-win for customers, water and wastewater systems, and municipalities.^v

- **Customers** receive high quality, reliable water service provided by expert water providers.
- **Water and wastewater systems** receive needed operational expertise and infrastructure investment, which means more reliable and higher quality water and wastewater services.
- **Municipalities** get a better deal for their assets and gain the ability to put their resources and capital toward other local priorities. This may include paying down debt, making other infrastructure improvements, investing in other economic development initiatives, or providing other government services.

3. Which states have passed Fair Market Value legislation?

Fair Market Value legislation has passed in California, Illinois, Indiana, Iowa, Maryland, Missouri, New Jersey, North Carolina, Ohio and Pennsylvania.^{vi}

4. What are some case study examples that show the benefits of Fair Market Value legislation in action?

McKeesport, Pennsylvania: *Pennsylvania American Water*

The city of McKeesport, Pennsylvania, sold its wastewater system assets to Pennsylvania American Water Company for \$159 million in December 2017. The sale was the first to occur under Pennsylvania's Fair Market Value legislation. McKeesport officials say selling the wastewater system at fair market value allowed the city to stabilize its finances and avoid municipal bankruptcy. Furthermore, selling the utility allows the private sector to provide greater expertise and investment in the system. Without fair market value legislation, the sale would have likely never occurred.^{vii} According to the Municipal Authority of McKeesport, "the acquisition will provide the residents of McKeesport, Duquesne, Dravosburg and Port Vue with quality wastewater service at a fair and reasonable rate for many years to come."^{viii}



Illinois: *Aqua Illinois*

Aqua Illinois has acquired four water systems under Fair Market Value legislation since 2015 -- North Maine Utility, Crystal Clear Water Company, Eastwood Manor Water Company, and Nunda Utility. Each of these systems required urgent infrastructure updates and repairs before being acquired. In fact, Crystal Clear Water Company, Eastwood Manor Water Company, and Nunda Utility had each recently faced EPA consent orders for repeated water treatment, supply, monitoring and management violations.^{ix} Given these failures, the Illinois Commerce Commission (the PUC) found that the “sale of the water and wastewater systems to a large, financially sound utility, [was] in the best interests” of residents.^x Customers of these systems have enjoyed the benefits of more than \$4 million in much-needed infrastructure improvements, including the replacement of aging water mains, service lines, hydrants, meters, and storage facilities. These investments, along with the added operational expertise provided by professionals with Aqua Illinois, have improved service, increased efficiencies, and conserved water by replacing aged, and often leaking, infrastructure.^{xi}

ⁱ EPA Water Infrastructure and Resiliency Finance Center, Accessed 6/30/16.

ⁱⁱ Moody's Investors Service, “Municipalities and investor-owned utilities benefit from privatization legislation” 14 August 2017; Global Water Intelligence, “Investor-owned utilities benefit as fair value legislation incentivizes system sales” December 2016; Women's Council on Energy and the Environment, “Water Utility Acquisition – An Illinois Model for Incentivizing Acquisitions” January 2016; California State Legislature, “SENATE COMMITTEE ON ENERGY, UTILITIES AND COMMUNICATIONS BILL ANALYSIS – SB 1268” 8 April 1997; Blank Rome LLP, “NEW PA LAW GIVES BOOST TO INVESTOR-OWNED ACQUISITIONS OF MUNICIPAL WATER AND WASTEWATER SYSTEMS” May 2016. See also: www.truthfromthetap.com.

ⁱⁱⁱ Moody's Investors Service, “Municipalities and investor-owned utilities benefit from privatization legislation” 14 August 2017; Global Water Intelligence, “Investor-owned utilities benefit as fair value legislation incentivizes system sales” December 2016; Women's Council on Energy and the Environment, “Water Utility Acquisition – An Illinois Model for Incentivizing Acquisitions” January 2016; California State Legislature, “SENATE COMMITTEE ON ENERGY, UTILITIES AND COMMUNICATIONS BILL ANALYSIS – SB 1268” 8 April 1997; Blank Rome LLP, “NEW PA LAW GIVES BOOST TO INVESTOR-OWNED ACQUISITIONS OF MUNICIPAL WATER AND WASTEWATER SYSTEMS” May 2016.

^{iv} Moody's Investors Service, “Municipalities and investor-owned utilities benefit from privatization legislation” 14 August 2017; Global Water Intelligence, “Investor-owned utilities benefit as fair value legislation incentivizes system sales” December 2016; Women's Council on Energy and the Environment, “Water Utility Acquisition – An Illinois Model for Incentivizing Acquisitions” January 2016; California State Legislature, “SENATE COMMITTEE ON ENERGY, UTILITIES AND COMMUNICATIONS BILL ANALYSIS – SB 1268” 8 April 1997; Blank Rome LLP, “NEW PA LAW GIVES BOOST TO INVESTOR-OWNED ACQUISITIONS OF MUNICIPAL WATER AND WASTEWATER SYSTEMS” May 2016.

^v Moody's Investors Service, “Municipalities and investor-owned utilities benefit from privatization legislation” 14 August 2017; Global Water Intelligence, “Investor-owned utilities benefit as fair value legislation incentivizes system sales” December 2016; Women's Council on Energy and the Environment, “Water Utility Acquisition – An Illinois Model for Incentivizing Acquisitions” January 2016; California State Legislature, “SENATE COMMITTEE ON ENERGY, UTILITIES AND COMMUNICATIONS BILL ANALYSIS – SB 1268” 8 April 1997; Blank Rome LLP, “NEW PA LAW GIVES BOOST TO INVESTOR-OWNED ACQUISITIONS OF MUNICIPAL WATER AND WASTEWATER SYSTEMS” May 2016.

^{vi} Moody's Investors Service, “Municipalities and investor-owned utilities benefit from privatization legislation” 14 August 2017; Global Water Intelligence, “Investor-owned utilities benefit as fair value legislation incentivizes system sales” December 2016; Women's Council on Energy and the Environment, “Water Utility Acquisition – An Illinois Model for Incentivizing Acquisitions” January 2016.

^{vii} Business Wire, “Pennsylvania American Water Closes Acquisition of McKeesport Wastewater System” 18 December 2017; Letter from Illinois Environmental Protection Agency to Clear Creek Water Company regarding Public Water Supply Inspection, 21 October 2011.

^{viii} The Municipal Authority of the City of McKeesport website (<http://www.mck-macm.org/>) accessed 7 February 2018.

^{ix} Circuit Court of the Twenty-Second Judicial Circuit in McHenry County IL, “Consent Order with Crystal Clear Water Company, Inc.” filed 5 September 2012; Illinois EPA “Annual Groundwater and Drinking Water Program Review, Calendar Year 2015” June 2016; Circuit Court of the Twenty-Second Judicial Circuit in McHenry County IL, “Consent Order with Eastwood Manor Water Company and Nunda Utility” filed 11 August 2011.

^x ICC Final Order, Docket # 14-0396.

^{xi} Aqua America Annual Report 2016.

