PENNSYLVANIA-AMERICAN WATER COMPANY

STATEMENT OF SPECIFIC REASONS
FOR PROPOSED INCREASE IN RATES

Pennsylvania-American Water Company ("PAWC" or the "Company") is filing herewith Supplement No. 45 to Tariff Water-Pa. P.U.C. No. 5 and Supplement No. 47 to Tariff Wastewater PA P.U.C. No. 16, which bear a proposed effective date of January 7, 2024, but may be suspended by operation of Section 1308(d) of the Pennsylvania Public Utility Code ("Code") until August 7, 2024. The rates proposed in those tariffs would increase the Company's total annual operating revenues by $203.9 million, or approximately 20.2%, above the level of pro forma revenues for the fully projected future test year ending June 30, 2025. The reasons for the proposed increase are summarized below.

RATE INCREASE

One of the factors accounting for the need for rate relief is the Company's substantial investment in new utility plant. The Company is planning to invest approximately $1 billion in new utility plant during the future test year ending June 30, 2024 and its fully projected future test year ending June 30, 2025.

Absent rate relief, the Company's overall rate of return on an original cost basis as of June 30, 2025 will be 5.78%. More significantly, the indicated return on common equity is anticipated to be 6.63%, which is obviously less than is required, by any standard, to permit a reasonable return on such common equity and to provide a reasonable opportunity for the Company to attract the additional capital required to finance needed plant additions.

Ms. Ann E. Bulkley, Principal of The Brattle Group and an expert on the subject of rate of return, has recommended an equity return rate of 10.95% and resulting overall return rates of 8.22% and 7.94%, for the Company's water and wastewater operations, respectively. Ms. Bulkley's rate of return recommendations are being filed with the Company's supporting data as PAWC Statement No. 13 and Exhibit No. 13-A and may be summarized as follows:

WATER OPERATIONS

TYPE OF CAPITAL	RATIO	COST RATE	WEIGHTED COST RATE
Long Term Debt	44.01%	4.76%	2.09%
Common Equity	55.99%	10.95%	6.13%
Overall Rate of Return			8.22%

WASTEWATER (WW) OPERATIONS

TYPE OF CAPITAL	RATIO	COST RATE	WEIGHTED COST RATE
Long Term Debt	42.73%	4.76%	2.03%
WW-Specific LTD	4.40%	2.62%	0.12%
Common Equity	52.87%	10.95%	5.79%
Overall Rate of Return			7.94%

The Company is filing herewith all of the supporting data required by the Pennsylvania Public Utility Commission's ("Commission") regulations. The Company is basing its claim principally on the fully projected future test year data and, therefore, the discussion that follows will primarily address such data.

Pursuant to Section 315(e), which was added to the Code by Act 11 of 2012 ("Act 11"), the Company is employing, in this case, a fully projected future test year ("FPFTY") ending June 30, 2025. The Company is also providing supporting data based on a historic test year ("HTY") ended June 30, 2023 and a future test year ("FTY") ending June 30, 2024. The revenue and expense data for the year ending June 30, 2025 have been prepared in a manner substantially consistent with the Company's most recent (2022) general water rate filing and in accordance with the accepted practices of the Commission.

To establish anticipated operating revenues under the proposed rates, operating revenues for the HTY were adjusted: (1) to annualize various rate changes and to annualize additional revenues obtained from acquisitions of water and wastewater systems; (2) to reflect the trend of declining per-customer consumption; (3) to reflect changes in customer usage; and (4) to reflect changes in the number of customers and usage by specific customers during the HTY, FTY and FPFTY.

After extensive and careful review of the Company's accounts, actual operating expenses for the HTY were adjusted to reflect currently effective and anticipated changes in expense levels, as summarized in Exhibit No. 3-A, through June 30, 2025. Such adjustments capture, among other things, increases in labor (salaries and wages), changes in production costs, insurance, and maintenance costs.

Operating revenue deductions other than expenses have also been adjusted to reflect changes in taxes other than income taxes, including the General Assessments for the Commission, the Damage Prevention Committee, the Office of Consumer Advocate and the Office of Small Business Advocate. Federal and state income taxes have been calculated on a pro forma basis to reflect the effect on the Company's taxable income at the proposed rates, the various expense adjustments made for ratemaking purposes and the use of state and federal income tax rates effective as of the end of the FPFTY.

Annual depreciation charges included for ratemaking for major plant accounts have been calculated using the straight-line remaining life method. Provision has also been made for the deferred federal income taxes resulting from the use of the Accelerated Cost Recovery System for qualifying property additions, in accordance with the provisions of the Economic Recovery Tax Act of 1981, from the use of the Modified Accelerated Cost Recovery System for qualifying property additions, in accordance with the Tax Reform Act of 1986, from the Tax Cuts and Jobs Act of 2017 ("TCJA"), and from repair costs that can be deducted for income tax purposes but are capitalized for book accounting purposes.

After making the proper allowances for all necessary adjustments to determine the appropriate levels of revenue and expense for ratemaking purposes, the Company's anticipated operating income under the proposed rates will be:

Operating Revenues (000's)	$1,215,842
Operating Revenue Deductions (000's)	$718,634
Operating Income (000's)	$497,208

The rate base elements that are submitted as part of this filing reflect the original cost of the Company's utility plant, as taken from its continuing property records, together with anticipated additions and retirements occurring through the period ending June 30, 2025. The Company's claim for accrued depreciation applicable to original cost has been determined on the basis of the ratemaking book reserve, consistent with the procedures approved by the Commission in the past. As previously noted, the resulting claim for depreciated utility plant in service encompasses the Company's planned investment of approximately $1 billion in new utility plant, as well as investment in acquired utility plant during the FTY and FPFTY.

From the depreciated utility plant in service figures, the Company has deducted contributions-in-aid-of-construction, customer advances for construction and excluded property. Also deducted is the net cash working capital amount of long-term debt interest and preferred stock dividends accrued prior to payment, unamortized investment tax credits generated prior to 1971, extension deposits in suspense, contributions-in-aid-of-construction and customer advances for construction associated with the acquisition of the water assets of the former Citizens Utilities Water Company of Pennsylvania, the regulatory liability recorded for federal income tax savings associated with the TCJA for the period January 1, 2018 through June 30, 2018, other deductions, and the accumulated balance of deferred taxes attributable to accelerated depreciation and capitalized repair deductions. In addition, allowances for materials and supplies, cash working capital, prepaid taxes net of accrued taxes, and the unamortized portion of the Company's investment in certain property obtained through acquisitions are reflected in the Company's rate base claim. As so developed, the estimated original cost measure of value at June 30, 2025 is $6,096,173,421.

As part of its rate filing, the Company is seeking approval to implement a Revenue

Decoupling Mechanism ("RDM") an Environmental Compliance Investment Charge ("ECIC"), deferred accounting treatment for pension and other post-employment benefits ("OPEB") expense and deferred accounting treatment for production costs. The RDM is an alternative rate design mechanism designed to provide the Company with the opportunity to more reliably recover its authorized revenue requirement and the fixed costs authorized in this proceeding. The ECIC is a rate adjustment mechanism designed to support full and timely rate recognition of the capital costs and expenses imposed on the Company between base rate cases to comply with evolving environmental requirements in a prudent and efficient manner as they emerge. The request for deferred accounting of pension and OPEB expenses is designed to reflect differences that occur, between base rate cases, in the annual amount of pension/OPEB accounts expense reflected in base rates and the actual annual amount of pension and OPEB accounts expense the Company incurs. The request for deferred accounting for production costs is designed to reflect differences that occur, between base rate cases, in the annual amount of production cost accounts expense reflected in base rates and the actual annual amount of product cost accounts expense the Company incurs.

Additionally, the company is proposing a change to the computation of residential wastewater bills. The Company proposes to determine usage during summer months on the basis of Winter Average Consumption in order to reduce the impact of seasonal outdoor water usage on residential wastewater bills.

It is evident from the information furnished above and from the voluminous supporting data filed by the Company with its proposed water and wastewater tariffs that the proposed rate increase is just and reasonable and represents the minimum rate increase necessary to enable the Company to earn a reasonable return on the fair value of its property used and useful in the public service and to maintain the integrity of its existing capital.

RATE STRUCTURE

As part of its supporting data, the Company has submitted, in Exhibits No. 12 A-E, Cost of Service Studies performed by the engineering firm of Gannett Fleming Valuation and Rate Consultants, Inc. The results of the Cost of Service Studies were one of the factors considered by the Company in developing its rate structure proposal. The principal elements of that proposal consist of the following:

- The consolidation of rate zones, where possible, such that the rates charged to customers are the same regardless of geographic location;
- For wastewater service, separate consolidation of sanitary sewer service, combined sewer service, and collection-only service;
- A modification to the low-income discount for water and wastewater customers to include an expansion of the tiered discount structure;
- An increase of monthly service charges to be more in line with customer costs;
- The combining of a portion of the revenue requirement for wastewater operations with the revenue requirement for water operations pursuant to Section 1311(c), which was also added to the Code by Act 11 of 2012;
- A change in annual public fire hydrant rates to reflect 25% of the cost of public fire protection service, pursuant to Section 1328 of the Code; and
- The allocation of the requested rate increase in a manner designed to realign revenues by major customer classes to be more commensurate with the indicated cost of service.

CONCLUSION

In summary, the proposed increase in revenues is the minimum increase necessary to permit the Company to preserve public health and safety and to maintain the integrity of its existing capital, attract additional necessary capital at reasonable costs and have an opportunity to actually achieve a fair rate of return, particularly on its common equity capital. For these and the other reasons set forth above, the proposed rates should be permitted to become effective as filed.