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H.R. _____, Drinking Water System Improvement Act and Related Issues of Funding, Management, and Compliance Assistance Under the Safe Drinking Water Act.

Presented on behalf of the National Association of Water Companies

House Energy and Commerce Committee
Subcommittee on Environment
May 19, 2017

Good morning, Chairman Shimkus, Ranking Member Tonko, and Members of the Subcommittee. Thank you for the opportunity to discuss efforts to improve the federal Safe Drinking Water Act. We appreciate the opportunity to comment on the Committee's discussion draft legislation.

I am Marty Kropelnicki, President and CEO of California Water Service Group (Cal Water), the third largest publicly traded water and wastewater utility company in the United States. I had the pleasure of appearing before this Subcommittee in March to discuss the challenges facing the water industry and the nation's drinking water infrastructure. I am pleased to be here today to continue exploring solutions to these challenges.

I am also the President of the National Association of Water Companies (NAWC) – the association that represents the regulated private water utility service industry and professional water management companies. NAWC's core belief is that by embracing the powerful combination of public service and private enterprise, we can improve our nation's water infrastructure, and by doing so, ensure that all Americans and future generations have access to safe, reliable, and high-quality water utility service.

NAWC applauds you, Mr. Chairman, and this Subcommittee for highlighting America's drinking water infrastructure needs and for putting forward a discussion draft of amendments to the Safe Drinking Water Act for utilities and regulators to review. We are all working toward the same outcome - safe, reliable, and high-quality drinking water, which is critical to every person, community, and business in this country. NAWC's members are proud to provide these services to our customers.

NAWC members are located throughout the nation and range in size from large companies that own, operate, or partner with hundreds of systems in multiple states to individual utilities serving a few hundred customers. Through various innovative business models, NAWC's members serve more than 73 million Americans, nearly a quarter of our country's population.

Cal Water, for one, provides water and wastewater service to approximately two million people in California, Hawaii, New Mexico, and Washington. Every day, Cal Water treats and delivers more than 320 million gallons of drinking water to our customers. For us, there is nothing more important than protecting our customers' health and safety, and working each and every day to ensure they have safe,

high-quality water each time they turn on the tap.

There are two key areas that I will focus on today as they relate to the discussion draft before us. First, there is a need to embrace and enact effective utility management practices and accountability for all water systems – whether these systems are public or private. Second, there is a need to address those drinking water systems that are consistently non-compliant with federal health and safety standards. Working on these two critical areas can help improve the drinking water systems across the country while also ensuring that limited federal dollars are spent efficiently and wisely.

Private Utility Role in Meeting the Nation's Drinking Water Needs

Let me start by providing some background on the private utility role in meeting today's drinking water needs. Private water systems have existed in the United States for more than 200 years. Today, the private water utility sector is highly regulated by state public utility commissions (PUCs), which set water rates; the U.S. Environmental Protection Agency, which sets federal drinking water quality standards; and various state agencies, which are also responsible for setting water quality standards and protecting public health. The private water utility sector focuses on long-term planning by making appropriate and necessary infrastructure investments in our nation's communities. As a result, private water companies have a proven track record of consistently meeting the drinking water needs of consumers in many areas of the country.

The private sector is already helping overcome water infrastructure challenges facing the country. Ensuring the high standard of quality that private water companies deliver requires extraordinary amounts of capital investment. NAWC estimates that its six largest members alone are collectively investing nearly $2.7 billion each year in their water systems – and these six companies provide service to about six percent of the U.S. population. In Cal Water's case, we are budgeting to invest about $1 billion in our water systems over the next five years.

It is significant that six of NAWC's members are collectively investing nearly $2.7 billion in their water systems when one considers that the current total federal appropriation for the Clean Water and Drinking Water State Revolving Fund (SRF) programs is approximately $2.3 billion annually.
One of the factors that enable the private water sector to undertake such significant levels of

investment is outstanding credit ratings. In fact, the corporate credit ratings of some of NAWC's members are amongst the highest in the U.S. For example, Cal Water's first mortgage bonds are currently rated AA-, and Cal Water has the highest credit rating of any utility in the U.S., as rated by Standard & Poor's.

In addition to helping to ensure our customers have safe, reliable, and high-quality water utility service, NAWC members provide significant economic benefits to the communities we serve. We pay federal and state income taxes, local property taxes, local pump taxes, and permit fees for projects, all of which provide much needed revenue to all levels of government in the country. We hire local employees, and provide them with good-paying jobs and competitive benefits. We procure local goods and services. And to help ensure our medium- and long-term financial stability, our employees' retirement benefits are fully funded as required by Generally Accepted Accounting Principles. All of these things contribute to the economic multiplier effect that benefits the regions and communities that we serve.

Perhaps most importantly, NAWC's members work diligently with our public health and economic regulators to ensure that we meet federal and state water quality and customer service standards every day. For example, a review of the EPA's enforcement database shows that there are more than 2,000 public water systems in the country that are deemed serious violators of the nation's drinking water standards. Yet, not a single one of those systems is owned and operated by one of NAWC's members. This fact confirms earlier research conducted by American Water Intelligence, which found that the "compliance record of major companies in the private water utility sector has remained nearly spotless."[1]

In summary, the private water utility sector stands able, ready, and willing to partner with local and state governments, as well as the federal government, to help meet the challenges our nation's water infrastructure will face in the coming years and decades. In addition to supplying necessary capital, private water companies can leverage decades of experience solving complex water challenges to help bring new water infrastructure projects online more quickly and efficiently.

[1] American Water Intelligence, "Data Show IOUs a Cut Above in SDWA Compliance," October 2012, p. 10.

Effective Utility Management and Accountability

Our water infrastructure systems are the backbone upon which communities are built. Water service is a critical part of the physical platform of the U.S. economy. Not a single business in any community can be established, let alone survive and thrive, without a sustainable water supply. Communities must have reliable, resilient, and sustainable water infrastructure systems to attract and retain industry, business, and qualified workers. Simply put, capital investment in water infrastructure means job creation across the country.

Unfortunately, aging and deteriorating water systems threaten economic vitality and public health, and communities nationwide are faced with massive fiscal challenges to replace critical water and wastewater infrastructure and effectively manage their systems. After all, water systems are one of the most expensive assets for a community to maintain, and many municipally-owned utilities simply cannot afford to properly maintain, let alone improve and modernize, their infrastructure. They have a limited revenue base, which must be used to meet all of the needs of the community, including everything from street maintenance to public safety, not just water and wastewater services. Oftentimes, these fiscal challenges exacerbate the fact that many municipally-owned suppliers are not subject to stringent oversight of their operations and have not implemented best management practices designed to ensure the safety and reliability of the service they provide their customers.

NAWC and its members support the Environmental Protection Agency's (EPA) ten attributes of effective utility management endorsed by all major water and wastewater associations, including the American Water Works Association (AWWA), National Association of Clean Water Agencies (NACWA), Water Environment Federation (WEF), Association of Metropolitan Water Agencies (AMWA), Association of Drinking Water Agencies (ASDWA), and the Association of Clean Water Administrators (ACWA). The attributes include priorities such as financial viability, infrastructure stability, and operational resiliency, which reflect the basics of financial, technical and operational capacity of sustainable utility management.

Failing and noncompliant water systems not only create a growing financial burden, but they pose significant risks to public health and the environment. The fact that there are thousands of water systems across the country in significant noncompliance with the nation's drinking water standards is

both unacceptable and unsustainable. If we are to change the status quo, we must offer more "carrots and sticks" in the regulatory toolbox.

As a good first step, and as a general rule, applicants for public dollars should demonstrate that they have fully accounted for the long-term costs of their projects, including any risks inherent in construction, operations, and/or maintenance, and have selected the delivery model that provides the best long-term value to the water supplier's customers. For a community to maintain and improve the condition of its infrastructure, and to ensure its long-term safety and reliability, water utilities should be expected, at a minimum, to manage their assets based on a process where adequate repair, rehabilitation, and replacement are fully reflected in management decisions and fully accounted for in water rates.

On this latter point, it is important to note one of the core differences between regulated private water utilities, like Cal Water, and some of their public counterparts. The water rates charged by regulated private water utilities are set by state public utilities commissions to ensure they reflect the actual cost of service, including the cost of capital, as well the costs of operating, maintaining, and upgrading their water systems. Regulated utilities do not rely on other sources of revenue that are not related to the water system, such as sales or property tax revenue. Nor can money customers pay to receive water service be diverted to other uses, which too often happens in some municipal systems. Not only does this approach send an efficient price signal to customers, but it also helps to ensure that the utility remains financially stable and is able to maximize the efficiency and service life of its water system infrastructure.

As well, we would be wise to assess impediments to effective utility management resulting from local procurement processes. Public procurement today tends to overvalue low initial costs and undervalue future obligations, rewarding bidders who can build cheaply, rather than those who offer the best value over a project's lifecycle. The end result is oftentimes higher operations and maintenance costs, and as repairs go unaddressed, water system infrastructure fails prematurely, resulting in expensive rebuilds and threats to public health. This is unacceptable and fiscally irresponsible.

Partnerships and Consolidation

We appreciate the Committee's inclusion in the discussion draft of language related to the need for asset management plans. This is an important step but we would ask the Committee to consider a more robust approach.

Drinking water systems must be expected to maintain their assets and operations in compliance with health-based laws. One option to help struggling systems that is currently under discussion is to encourage these systems to pursue partnerships *in lieu* of traditional enforcement.[2] Alternatively, when a return to compliance is unlikely to occur, the State should compel the transfer of water systems assets and/or operational control over the water system to a supplier with a proven track-record of effectively operating, maintaining, and upgrading its water systems. NAWC recognizes that traditional enforcement tools, such as administrative orders and civil penalties, are not always appropriate or practicable. However, if we are to address the nation's drinking water challenges, we must expect failing systems to do things differently and, in terms of compliance with water quality regulations, all water suppliers – public or private – need to be held to the same standard.

In this regard, NAWC has been working closely with other water groups to promote legislation that would encourage partnerships, ranging from peer-to-peer support and public-private partnerships (P3s) to transfer and consolidation. We simply cannot continue to expect failing systems to change unless good decision-making is incentivized, bad decision-making is discouraged by holding utilities accountable, and federal funds are targeted in a way to ensure they are being used efficiently and cost-effectively.

While NAWC and its members are mindful of the socioeconomic and financial complexities associated with our nation's growing water crisis, water suppliers must be held accountable when their water systems fail. We should expect communities to proactively seek assistance and support or they should get out of the business of water provision. Year after year there is talk of the growing water crisis, yet little is done to actually address it and the number of customers exposed to water that does not meet minimum water quality standards continues to grow.

[2] This approach has been endorsed by the Business Roundtable in a report release this week titled "Back to Business: A Blueprint for Renewing America's Infrastructure," available at: http://bit.ly/2pWRcf9.

What is truly needed to address these kinds of compliance issues is a willingness to explore innovative solutions such as partnerships and incentivized consolidation. While many communities continue to clamor for more federal funding, more funding is not going to solve this growing crisis. In many cases, water system failures – be they related to water quality, reliability, or both – are not solely due to the absence of funding, but rather are directly attributable to the failure of proper governance, poor decision-making, and lack of stringent oversight.

There are numerous opportunities for these kinds of partnerships to be employed across the country. For example, there are currently several thousand public water systems that the EPA has deemed serious violators of federal drinking water standards. Many of these communities are simply unable to address these violations on their own, and they would benefit from a partnership with either the private sector or even a neighboring municipality.

Several states have already made progress in effectively utilizing partnership and consolidations. Kentucky, for example, has been a national leader in incentivizing the consolidation of public water systems. Over the last several decades, Kentucky has been able to consolidate more than 2,100 public water systems to less than 400 systems today. Similarly, in 2015, California enacted Senate Bill 88 that authorized the State Water Board to require systems that consistently failed to meet public health standards to consolidate with other systems through physical or managerial consolidation.

We recognize there are small and rural communities where few, if any, viable partnership options exist. It is in these cases where federal funding and technical assistance can be the most beneficial. Doing more to encourage and incentivize partnerships and consolidation where they are viable would allow Congress to reprioritize federal funding and technical assistance toward those systems and communities where partnerships and consolidation are not viable.

While these types of public-private partnerships are, in many cases, an efficient and cost-effective solution, there are numerous impediments to their expanded use, including the legal and financial liabilities of distressed systems. Such liabilities for past noncompliance, which can range from hundreds of thousands to millions of dollars, can be a “poison pill” to a prospective new operator or owner. To solve this problem, Congress should consider providing a more robust legal “safe harbor” to encourage

more private sector participation, including investment. Without such liability relief, significant amounts of private capital and investment remain on the sideline.

Performance and Full Access

All water suppliers in the country – whether they are government- or privately owned – are public service providers and their customers are comprised of taxpayers who fund programs such as the State Revolving Fund (SRF) programs. Despite this, there has been a long-standing prohibition against private entities from receiving Clean Water SRF funding for treatment works and, although the EPA does not prohibit such access to the Drinking Water SRF, no fewer than 12 states have adopted such blanket prohibitions.[3] Congress should seek to correct this imbalance by making future SRF funding contingent on states giving all water suppliers equal opportunity to apply for these funds.

Additionally, in 2003, the EPA established its Four Pillars of Sustainable Infrastructure, one of which was full-cost pricing. The principle was established based on a 2002 Government Accountability Office (GAO) report that found that 29 percent of drinking water utilities were not generating enough revenues, and 43 percent of those received some form of federal or state grant or loan.[4] Further, more than one in four utilities failed to have plans to manage existing capital assets, and more than half of the utilities with plans did not cover all of their assets or omitted key elements, such as an assessment of capital conditions. Things have not changed over the last 15 years. In fact, the situation has only gotten worse and the infrastructure funding gap continues to widen.

Toward this end, we believe it is time that those utilities that receive federal assistance be expected to develop and implement a financial plan that covers not only capitalization costs, but operation and maintenance, and rehabilitation and repair costs. We must expect performance in terms of meeting federal and state standards, protecting public health, and providing cost-effective services, not more of the status quo. Failing systems should no longer be subsidized without an expectation of financial and

[3] Alabama, Arkansas, Colorado, Georgia, Kansas, Louisiana, Mississippi, Nebraska, North Carolina, Oklahoma, Tennessee, and Wyoming. *See*, May 3, 2017, Congressional Research Service, *Drinking Water State Revolving Fund: Program Overview and Issues*, available at https://fas.org/sgp/crs/misc/RS22037.pdf (last visited May 13, 2017).

[4] *See*, GAO Report, April 11, 2002, *Drinking Water Infrastructure, Information on Estimated Needs and Financial Assistance*, available at http://www.gao.gov/assets/110/109253.pdf (last visited May 13, 2017).

operational viability.

Quite simply, full-cost pricing of water utility service is the single most important element of any strategy to improve the nation's drinking water infrastructure and compliance with the country's water quality standards. Full-cost pricing helps to ensure the financial viability of water suppliers, which then enables the supplier to undertake needed maintenance of and upgrades to its facilities, both of which play a critical role in the supplier's ability to provide safe and high-quality water to its customers.

This transition to full-cost pricing should, however, be accompanied by adequate financial support to assist economically distressed communities and low-income households. In this regard, Congress may wish to consider providing relief directly to challenged and low-income customers. Currently, federal funds flow directly to water utilities, which enables them to charge lower rates to all of their customers, including those who are not facing any type of economic hardship. A more efficient approach may be to transfer funds directly to challenged and low-income customers, similar to the Low Income Home Energy Assistance Program for gas and electric customers.

Conclusion

Our current water infrastructure crisis has been in the making for several decades, and it may take several decades to change the direction and right the ship. Today's dwindling resources and increasing demand for safe, reliable, and high-quality water require a fundamentally different approach than what we have taken over the last several decades.

The discussion draft in front of the Committee today is a good first step to addressing this crisis. As outlined in my testimony, we have specific suggestions related to effective utility management, partnerships, and the future of the State Revolving Funds. We look forward to continuing to work with the Committee as this legislation as it works its way through the Congressional process.

I sincerely appreciate your invitation to appear before the Subcommittee today and, along with my many colleagues in the National Association of Water Companies, look forward to continuing our work with you to ensure that all Americans benefit from innovations in financing which improve the water

infrastructure so essential to their quality of life. Thank you, and I would be happy to respond to any questions you may have.