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To the Massanutten community:

Massanutten Resort is aware of the proposed water and sewer rate increase requested by Massanutten Public Service Corporation (MPSC). While we know there are other issues in motion with regard to the relationship between MPOA and Massanutten Resort, we felt that this issue was important enough to communicate directly with you as a resident, independent of any other points that might be on our minds.

Like you, we believe MPSC's request is excessive. Massanutten Resort has suffered at the hands of MPSC every bit as much as MPOA's residents, and because the proposed new rates will result in a massive increase in water and sewer expense to the Resort, we are prepared to contest the portions of the rate increase that are most likely to be scrutinized by the Virginia State Corporation Commission (SCC), which regulates the utility. The SCC has placed a hold on this decision due to the COVID-19 situation; no hikes are likely until autumn.

Under Virginia law, utility companies are allowed to set rates based upon a certain Return on Equity (ROE) ratio. Rate increases must be applied for, and then approved by the SCC. Local governments, whether at county or city/township levels, have very little say in the matter.

We think it's important to provide MPOA's members with some background of Massanutten Resort's history with MPSC. As you may know, MPSC and Massanutten Resort do not share any common ownership or control. MPSC is owned by a privately-held corporation called Utilities Inc. (UI), which is based near Chicago. UI has 20 subsidiaries – MPSC is one of them – that operate domestic and/or waste water systems in 16 states. One of the revenue requirement adjustments that accounts for 34% of MPSC's rate increase request are service charges of $250,000 from UI to MPSC.

Many of the recent cost challenges we've all experienced trace back to clean water requirements as they developed over the past 25 years. Whether government- or privately-owned, small water and sewer utilities are held to the same federally-mandated standards as larger systems operated by, for example, Rockingham County. But they do not enjoy the same economies of scale.

Some folks in our community believe that MPSC's waste water treatment plant (WWTP), completed in 2002, was necessary to increase MPSC's capacity in order to satisfy Massanutten Resort's growth needs. This is not accurate. The real problem was that in the early 2000's, MPSC was required by Virginia's Department of Environmental Quality to come into compliance with effluent water discharge requirements applicable at the time.

This forced MPSC to design and construct the existing WWTP. The costs of that could have been simply passed on to all of MPSC's customers – including both MPOA property owners and Massanutten Resort.

In order for Massanutten Resort to continue its operations and help MPSC achieve cleaner treated water, we agreed to pay 100% of the projected costs, or approximately $4 million, for the upgrades MPSC needed to bring its WWTP into regulatory compliance. In exchange, we received the industry standard compensation: tap fee credits which we could use in the future. If you've built a structure in the area, you probably know what tap fees are: one-time charges to connect your property to the water and sewer systems.

During construction, new regulatory orders and changing standards drove project costs sharply upwards – first to $6.5 million, then to $8 million. Massanutten Resort absorbed these increases and also paid for cost overruns – ultimately reimbursing

MPSC $9.3 million for its WWTP improvements, with no additional tap fee credits. To date, Massanutten Resort has recovered only $2.2 million of that investment in the form of used tap fee credits, and is unlikely to ever use all of the remaining credits – which, again, were based on the original estimate of $4 million, not the $9.3 million ultimately spent.

When completed in 2002, the end product of the new WWTP was tertiary-treated water so clean that it could be released directly into Quail Run. Economically, the net effect of the project was that the $9.3 million asset, paid for by Massanutten Resort that was never included in the rate base that MPSC is entitled to recover through its sewer billings. The result was an enormous but invisible subsidy from Massanutten Resort to all other MPSC sewer rate payers, including MPOA members.

During MPSC's 2014 rate case, MPSC's customers were divided into four customer classes: Residential (which includes MPOA homeowners), Hospitality, Commercial and Waterpark. Since the creation of these classes, MPSC has used the latter three classes to provide an additional subsidy the Residential class through usage charges in a manner that the SCC Hearing Examiner characterized as "grossly unfair". Residential rates generated a much lower ROE for MPSC than the other three classes for both water and sewer usage.

Regulations stiffened again in 2016, when MPSC's new National Pollution Discharge Elimination System (NPDES) permit imposed even tighter discharge water quality requirements to further improve water in the Chesapeake Bay and its tributaries – which includes the Shenandoah River, Quail Run and Stony Run. This required a $3 million biological nutrient removal project upgrade to the plant.

Those improvements were paid for directly by MPSC, resulting in a higher rate base against which to bill all of its customers – including both MPOA members and Massanutten Resort. MPSC's rate case in 2017 was driven by both that and by an actual decline in water consumption in MPSC's service area.

At the conclusion of the 2017 rate case, the State Corporation Commission implemented a rate design and revenue allocation among the customer classes that brought the latter three classes half of the way to parity, reducing the subsidies to the residential class. The Hearing Examiner in that case explained that full parity would not result in rate shock to residential customers. The Commission, however, decided to move rates only half way to parity in the last rate case.

MPSC now proposes in the present case a rate design that brings its customer classes to full parity. Even if the customer class disparity ends, Massanutten Resort's unreimbursed expenditures on the WWTP will continue to benefit the entire franchise area at no cost to other rate payers.

So: with all of that as background, Massanutten Resort agrees with residential customers that MPSC's present rate request of $739,000 (a 10.7% increase) is excessive. It impacts the Resort, too. We have requested MPOA join us, and we proposed to engage an expert to challenge not only the service charges from UI, but also MPSC's effort to add $435,000 to its rate base for deferred water tank painting after having agreed not to treat tank painting costs as a regulatory asset in 2014.

We intend to fight to reduce the overall increase to something more tolerable, and we encourage you to contact the State of Virginia and register your concerns about the increase. You may file comments on the SCC's website at https://www.scc.virginia.gov/casecomments/comment/PUR-2020-00039. Although Massanutten Resort expects that some form of rate increase is inevitable, we hope that our combined efforts will help limit the increase to a more reasonable level.

Sincerely,

Garrett M. Smith
Corporate Secretary/General Counsel
Massanutten Resort