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Executive Salaries/
Governance Deficiencies

Schaben/Direct

Public Counsel

WR-2023-0006

DIRECT TESTIMONY

OF

ANGELA SCHABEN

Submitted on Behalf of the Office of the Public Counsel

**CONFLUENCE RIVERS UTILITY
OPERATING COMPANY, INC.**

CASE NO. WR-2023-0006

**

Denotes Confidential Information that has been redacted

**

May 26, 2023

PUBLIC

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DIRECT TESTIMONY
OF
ANGELA SCHABEN
CONFLUENCE RIVERS UTILITY OPERATING COMPANY, INC.
CASE NO. WR-2023-0006

1 **INTRODUCTION**

2 **Q. Please state your name, title, and business address.**

3 A. Angela Schaben, Utility Regulatory Auditor, Office of the Public Counsel (“OPC” or “Public
4 Counsel”), P.O. Box 2230, Jefferson City, Missouri 65102.

5 **Q. What are your qualifications and experience?**

6 A. Please refer to the Schedule ADS-D-1 attached hereto.

7 **Q. Have you testified previously before the Missouri Public Service Commission?**

8 A. I have prepared and submitted pre-filed testimony before the Public Service Commission of
9 the State of Missouri (the “Commission”). Please refer to the Schedule ADS-D-2 attached
10 hereto for a list of the cases in which I filed pre-filed testimony.

11 **Q. What is the purpose of your testimony?**

12 A. The purpose of my testimony is two-fold. First, I will address the seriously disproportionate
13 salaries of Central States Water Resources (“CSWR”) employees in comparison to salaries of
14 their peers from other Missouri utilities who also operate under parent companies. Second, I
15 will draw attention to CSWR’s lack of documented corporate governance policies and the
16 potentially serious consequences arising from this fact.

17 **Q. Please summarize your recommendations as presented in the subsequent testimony.**

18 A. I recommend the following:

- 19 • The Commission disallow CSWR executive salaries allocated to Confluence Rivers
20 based on the Company’s failure to justify these salaries

- 1 • The Commission disallow 10% of Confluence’s requested amount for contracted
2 operations based upon the lack of formal corporate governance and procurement
3 practices
- 4 • The Commission order CSWR to establish and file with the Commission copies of its
5 formal policies and procedures
- 6 • The Commission disallow any portion of the CSWR ESG report allocated to
7 Confluence Rivers

8 **Corporate Salaries**

9 **Q. Did you review documentation supplied by the Company relating to salaries?**

10 A. Yes.

11 **Q. What did you find?**

12 A. CSWR employs approximately 67 in-house employees as of November 2022.¹ The salaries
13 for these 67 in-house employees generally exceed reasonable salary expectation data provided
14 by the Missouri Economic Research and Information Center.² Executive level salaries, in
15 particular, greatly exceed the salaries of other Missouri regulated utilities. Additionally, the
16 CSWR organization structure is particularly top heavy. Of the approximately 67 employees,
17 nearly half are management or executive level positions that command impressive salaries
18 greatly surpassing those employed within similar positions by Confluence River’s regulated
19 peers within Missouri.

20 **Q. Could you please provide some examples?**

21 A. Yes. Table 1 below shows yearly salaries of CSWR’s higher up positions as of December 1,
22 2022: **

¹ Company response to Staff DR 0037.

² Missouri Economic Resaerch and Information Center, *Ocupational Employemnt and Wages Estiamtes*,
<https://meric.mo.gov/data/occupation/occupational-employment-wages>

1

2

**

3

Q. How does the information in Table 1 compare to top-level executive salaries of other regulated utilities within Missouri?

4

5

A. Table 1 above shows six of CSWR’s executive and high-level salaried employees. In order to draw a comparison, I sampled the six highest executive and high-level base salaries that I could find for the four largest Missouri investor owned utilities. From there, I divided these salaries by the number of customers that each utility claims to serve on their respective websites to determine an average cost per customer. The results are shown in Table 2 below:

6

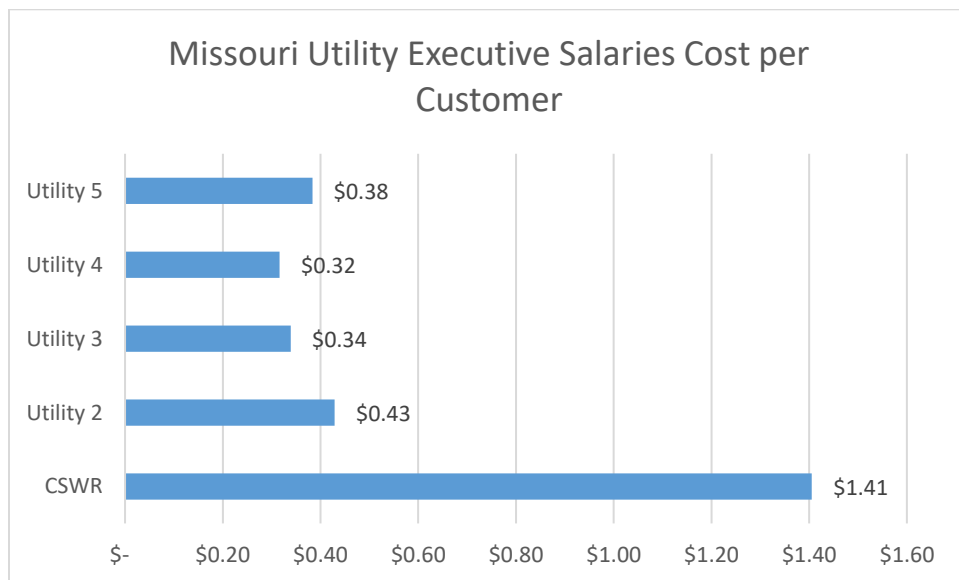
7

8

9

10

Table 2



11

1 **Q. What does Table 2 demonstrate?**

2 A. Table 2 demonstrates that the executive level base salaries of the four largest investor owned
3 utilities within Missouri averages out to \$0.32 to \$0.43 per customer. This is true despite
4 significant differences in the number of customers served by each utility. In comparison, the
5 average cost of CSWR executive and high-level employee annual base salaries exceed that of
6 other Missouri utilities by approximately \$1.00 per customer.

7 **Q. How does the President of CSWR's salary considered alone compare to the Presidential**
8 **salaries of other Missouri utilities?**

9 A. The comparison of President base salary cost per customer is shown in Table 3 below.
10 President annual base salaries for the four largest Missouri investor owned utilities range
11 between \$0.48 to \$0.63 on a per-customer basis. ** _____

12
13

14
15 **

1 **Q. Is there any other comparison that demonstrates how excessive CSWR’s presidential**
2 **annual salary is?**

3 A. The United States President’s salary is \$400,000 per year.³ ** _____
4 _____ **

5 **Q. How does the issue of exorbitant salaries paid to CSWR employees, specifically the**
6 **highest-level employees, affect Confluence Rivers and Confluence Rivers ratepayers?**

7 A. As CSWR has added in-house employees, indirectly allocated costs from CSWR to
8 Confluence Rivers has also increased while direct allocation has decreased. From 2021 to
9 2022, CSWR administrative and general salaries have increased by over ** _____ **
10 Indirect allocation charges to Confluence Rivers from CSWR have also increased over this
11 time frame.

12 **Q. What day-to-day operations related to the water and wastewater facilities owned by**
13 **CSWR are performed by employees that are actively overseen by CSWR’s management**
14 **team and executive class?**

15 A. It appears that almost all day-to-day operations of the water and wastewater facilities, including
16 ** _____
17 _____ ** are
18 handled by third party vendors.

19 **Q. Do you recommend a disallowance based on this information?**

20 A. Yes. The Company has not provided a valid basis for such exorbitant payroll expenses,
21 exceeding even executive base salaries of fortune 500 companies with millions of customers,
22 given what little the executive class contributes in the day-to-day operation of its water and
23 wastewater systems. Captive ratepayers should therefore not be extorted to pay for these
24 unreasonable and inflated payroll expenses.

³ 3 U.S.C. § 102.

1 **Q. What do you recommend?**

2 A. I recommend the Commission disallow \$322,465, the amount of CSWR executive salaries
3 allocated to Confluence Rivers for this rate case. In addition to this disallowance I would
4 recommend that all Company expenses related to business development also be removed since
5 these activities do not contribute to providing safe, clean drinking water to Confluence Rivers
6 ratepayers.

7 **Corporate Governance Deficiencies**

8 **Q. What is Corporate Governance?**

9 A. Corporate Governance is the system of rules, practices, and processes by which a firm is
10 directed and controlled.⁴ The corporate governance framework essentially lays the
11 groundwork for an organization in achieving its goals by developing objectives related to
12 internal controls, corporate disclosure, and performance measurement, to name a few.

13 **Q. Why is Corporate Governance so important?**

14 A. Attitude regarding corporate governance within a business sets expectations for organizational
15 behavior and dynamics.

16 **Q. Does effective corporate governance assist in fraud prevention?**

17 A. Absolutely. Several studies demonstrate the importance of governance, its role in promoting
18 transparent leadership, and acceptable corporate behavior relating to risk-taking and
19 management controls.⁵

⁴ James Chen, *Corporate Governance Definition: How It Works, Principles, and Examples*, INVESTOPEDIA (March 22, 2023), <https://www.investopedia.com/terms/c/corporategovernance.asp>

⁵ Free, C., Macintosh, N., & Stein, M. (2007). MANAGEMENT CONTROLS: THE ORGANIZATIONAL FRAUD TRIANGLE OF LEADERSHIP, CULTURE AND CONTROL IN ENRON. *Ivey Business Journal*, <https://iveybusinessjournal.com/publication/management-controls-the-organizational-fraud-triangle-of-leadership-culture-and-control-in-enron/>. Kassem, A. (2022). Elucidating Corporate Governance's Role and Impact in Countering Fraud. *Corporate Governance International Journal of Business in Society*. Miles, R. E., Snow, C. C., Meyer, A. D., & Coleman, Jr., H. J. (Jul., 1978, Vol. 3, No. 3 (Jul., 1978)). Organizational Strategy, Structure, and Process. *Academy of Management Review*, 546-562. IFC/World Bank (2005). *The Irresistible Case for Corporate Governance*. (collected in Schedule ADS-D3)

1 **Q. Does effective corporate governance assist in risk management?**

2 A. Yes. Effective governance is valuable in promoting the rapid identification of prospective
3 vulnerabilities.⁶ In fact, risk governance is one crucial aspect within an effective risk
4 management framework.⁷

5 **Q. Has CSWR or Confluence developed a documented plan specifically utilized for the
6 management of risk or long-term strategy?**

7 A. No. According to the Company, no such document exists.⁸

8 **Q. Does effective corporate governance assist in managing third party risk?**

9 A. Yes. Third party risk management within the business world has grown over the past decade.
10 Most of the actual operational work required to keep the Confluence Rivers systems running
11 is completed by third party contractors. Despite this fact, contracts and procurement practices
12 used to procure these services are deficient in areas of addressing risk. For instance, the
13 Company does not appear to consider financial viability of potential contractors and internal
14 assessment and audits of contractors do not appear to include financial viability consideration,
15 which increases risk.

16 **Q. Does CSWR and Confluence Rivers follow standard, written accounting policies and
17 procedures that guide the completion of necessary accounting tasks?**

18 A. According to the Company's response to Staff DR 0033, the cost allocation manual (CAM) is
19 the only formal document related to accounting policies and procedures.⁹ The Company's
20 other accounting policies and procedures have not been formally documented.¹⁰

⁶ Dogas, C. (2015, 3). *Preventing Corporate Fraud During Organizational Transformation*. Retrieved from Fraud Magazine: <https://www.fraud-magazine.com/article.aspx?id=4294987749>.

⁷ Investopedia Team, *Risk Management Framework*, INVESTOPEDIA (December 30, 2022), <https://www.investopedia.com/articles/professionals/021915/risk-management-framework-rmf-overview.asp> (Schedule ADS-D4).

⁸ ADS-D5

⁹ Schedule ADS-D6

¹⁰ *Id.*

1 Additionally, the Company does not utilize a structured procurement process for evaluating
2 and awarding contracts that utilizes formal scoring.

3 **Q. What are some benefits of efficient third party spending management?**

4 A. Evidence suggests that “effective management of third party spend can on average release
5 savings of between 7-12%.”¹¹

6 **Q. Does CSWR appear to manage third party spending in an effective and indiscriminate
7 manner?**

8 A. No. A formal scoring process of competitive bidding is not completed. ** _____
9 _____ **12

10 **Q. How do formal and documented policies and procedures benefit companies in general?**

11 A. Whether organizations truly self-govern or operate within a top-heavy managerial hierarchy,
12 formally documented policies and procedures encourages employee engagement and promotes
13 professional growth. Formal documentation closes employee knowledge gaps and provides a
14 means for developing task delegation processes. Deficient documentation practices
15 jeopardizes professional growth and creates procedural risks when an employee with all the
16 knowledge leaves the Company and the remaining employees struggle to fill in the knowledge
17 gap. This knowledge gap created by the lack of formally documented policies and procedures
18 also creates opportunities for employees storing important information in their heads to
19 demand higher salaries, or demanding other rewards, in order to remain with the Company. If
20 higher salary demands are not met, industrious employees may leave with critical company
21 information, creating a void with additional knowledge gaps.

¹¹ PricewaterhouseCoopers, *Strategic Cost Reduction Through Procurement*, pg. 4 <https://www.pwc.co.uk/retail-consumer/assets/documents/strategic-cost-reduction-through-procurement.pdf> (Schedule ADS-D7).

¹² Company response to Staff DR 212-228.

1 **Q. Is it possible CSWR has already experienced this type of phenomenon?**

2 A. Yes, it is definitely possible. As shown in the tables above, CSWR management salaries
3 already greatly exceed the management salaries of similar positions held within other Missouri
4 utilities. **

5 _____
6 _____ **

7 **Q. Is there any other potential source of value associated with good corporate governance**
8 **that Confluence may be lacking due to its failure to document certain internal**
9 **governance policies?**

10 A. Yes. Various studies exist that corroborate the correlation between accomplishing good
11 governance practices and firm value. According to one such study:

12 Governance has a substantial impact on value through its impact on cash: \$1.00 of
13 cash in a poorly governed firm is valued at only \$0.42 to \$0.88. Good governance
14 approximately doubles this value. Furthermore, [this study] show[s] that firms with
15 poor corporate governance dissipate cash quickly in ways that significantly reduce
16 operating performance. This negative impact of large cash holdings on future
17 operating performance is cancelled out if the firm is well governed.¹⁵

18 This study is just one example detailing the impacts of poor governance on firm value and
19 the message it conveys is clear. Weak governance increases risk in a variety of areas and
20 does not promote confidence in operations management, which in turn affects ratepayers.

21 **Q. What do you recommend?**

22 A. Poor governance increases risk, invites increased opportunities for fraud, increases the
23 probability of wasted resources, and amplifies the likelihood of compromised, or reduced, firm

¹³ Company response to Staff DR 79 through 79.3

¹⁴ Company response to Staff DR 262, page 6.

¹⁵ Dittmar, A., & Mahrt-Smith, J. (2007). Corporate Governance and the Value of Cash Holdings. *Journal of Financial Economics, Volume 83, Issue 3*, 599-634.

1 value. I recommend the Commission consider the damaging consequences of the non-formal,
2 improvisational governance practices when determining a fair and reasonable rate of return.
3 Ratepayers should not be subjected to overpaying for subpar managerial and governance
4 practices. Additionally, I recommend the Commission order the Company to develop formally
5 documented policies and procedures, especially relating to the accounting and procurement
6 functions and file them before the Commission.

7 **Q. Do you have additional recommendations relating to indiscriminate procurement**
8 **practices?**

9 A. Yes. CSWR does not utilize formal procurement bid scoring metrics and do not appear to
10 follow formally documented practices related to procurement ** _____

11 _____ ** For this reason, I recommend the
12 Commission disallow 10% of the Company's requested amount for contracted operations to
13 account for inefficiencies. The total disallowance amounts to \$69,786 for water operations,
14 \$92,921 for sewer operations, and \$46,274 of allocated contract services equaling \$208,981
15 overall. This 10% is based on the previously discussed report that suggests "effective
16 management of third party spend can on average release savings of between 7-12%."¹⁶

17 **CSWR ESG Report**

18 **Q. What is an ESG report?**

19 A. ESG stands for "Environmental, Social, and Governance." In general, companies commission
20 ESG reports in order to provide investor transparency.

21 **Q. Did CSWR pay for an ESG report?**

22 A. Yes. CSWR contracted with a company to compile an ESG report with 2021 information.

¹⁶ PricewaterhouseCoopers, *Strategic Cost Reduction Through Procurement*, pg. 4 <https://www.pwc.co.uk/retail-consumer/assets/documents/strategic-cost-reduction-through-procurement.pdf> (Schedule ADS-D7)

1 **Q. Should Confluence Rivers be allocated any portion of the ESG report costs?**

2 A. No. ESG reports are usually prepared by larger, publicly owned companies for public investor
3 information purposes. CSWR is not a publicly traded company, however, so there is no
4 purpose for such a report to be generated. CSWR has provided no other explanation for why
5 an ESG report was necessary and Confluence Rivers ratepayers should therefore not be
6 required to pay for a process that does not provide value for them.

7 **Q. Does this conclude your testimony?**

8 A. Yes.

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of Confluence Rivers Utility)
Operating Company, Inc.'s Request for)
Authority to Implement a General Rate Increase) Case No. WR-2023-0006
for Water Service and Sewer Service Provided in)
Missouri Service Areas)

AFFIDAVIT OF ANGELA SCHABEN

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

Angela Schaben, of lawful age and being first duly sworn, deposes and states:

1. My name is Angela Schaben. I am a Utility Regulatory Auditor for the Office of the Public Counsel.
2. Attached hereto and made a part hereof for all purposes is my direct testimony.
3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.



Angela Schaben
Utility Regulatory Auditor

Subscribed and sworn to me this 25th day of May 2023.



TIFFANY HILDEBRAND
My Commission Expires
August 8, 2023
Cole County
Commission #15637121



Tiffany Hildebrand
Notary Public

My Commission expires August 8, 2023.