

FILED
May 17, 2013
Data Center
Missouri Public
Service Commission

Exhibit No. _____
Issue: Return on Equity
Local Hearing
Refund Issues
Witness: Bruce D. Menke
Type of Exhibit: Surrebuttal Testimony
Sponsoring Party: Emerald Pointe
Case No. SR-2013-0016

Missouri Public Service Commission

Surrebuttal Testimony

of

Bruce D. Menke

On Behalf of

Emerald Pointe Utility Company

Company Exhibit No. 20
Date 5.9.13 Reporter SB
File No. SR 2013.0016

BRUCE D. MENKE
SURREBUTTAL TESTIMONY

AFFIDAVIT

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29

STATE OF MISSOURI)
)
) ss
COUNTY OF _____)

I, Bruce D. Menke, state that I am the Chief Operations Officer of Shepherd of the Hills Entertainment group, which includes Emerald Pointe Utility Company, and, that the answers to the questions posed in the attached Surrebuttal Testimony are true to the best of my knowledge, information and belief.

B. Menke

Subscribed and sworn to before me this 29 day of April, 2013.

Lawrence E. Pittman
Notary Public

My Commission Expires:

MAY 10, 2013
(SEAL)

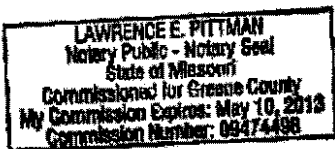


TABLE OF CONTENTS

WITNESS INTRODUCTION.....1
PURPOSE.....1
RETURN ON EQUITY.....2
LOCAL HEARING.....6
REFUND ISSUES.....7

SURREBUTTAL TESTIMONY
OF
BRUCE D. MENKE
EMERALD POINTE UTILITY COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION

WITNESS INTRODUCTION

1

2 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

3 A. My name is Bruce D. Menke. My business address is 118 State Drive, Hollister,
4 MO 65672.

5

6 Q. ARE YOU THE SAME BRUCE D. MENKE THAT PREVIOUSLY PROVIDED
7 REBUTTAL TESTIMONY IN THIS CASE?

8 A. Yes, I am.

9

10

PURPOSE

11 Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

12 A. I will respond to the Rebuttal Testimony of Office of the Public Counsel (Public
13 Counsel) witness Ted Robertson in regard to the basis for his suggestion that an
14 appropriate return on equity for Emerald Pointe is 9.35%. (Robertson Rebuttal, p.
15 21, line 14-18).

16

RETURN ON EQUITY

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23

Q. HOW DID PUBLIC COUNSEL WITNESS ROBERTSON ARRIVE AT HIS RECOMMENDED 9.35% RETURN ON EQUITY?

A. It appears that Mr. Robertson took Emerald Pointe's actual cost of debt of 5.35% and added a 4% risk premium to arrive at a recommended return on equity (ROE) of 9.35%.

Q. HOW DOES THAT COMPARE TO STAFF'S RECOMMENDED RETURN ON EQUITY?

A. It appears that Staff took an estimate of the corporate bond yield of 9.26% and added a 4% risk premium to arrive at a recommended return on equity of 13.26%.

Q. WHY DOES MR. ROBERTSON BELIEVE THAT THE ACTUAL COST OF DEBT OF 5.35% SHOULD BE USED AS A BASIS FOR HIS ROE RECOMMENDATION?

A. Mr. Robertson states in his Rebuttal Testimony, beginning on line 18 of page 20, that "Staff's extrapolation of credit ratings and bond yields for debt cost for larger water and sewer utilities that have actively traded debt makes little sense when compared to a small water and sewer company that actually has issue debt that is based on and subject to current market rates as determined by the parties (Investors) that loan the utility the funds." He then goes on to say that

1 "Company's actual debt costs are more relevant because they are a component
2 of its actual capital structure and true cost of service." (p. 21, lines 4-6)

3
4 **Q. ARE THERE ANY FLAWS IN PUBLIC COUNSEL WITNESS ROBERTSON'S**
5 **ANALYSIS?**

6 **A.** Yes, I believe there are two.

7
8 **Q. WHAT IS THE FIRST FLAW?**

9 **A.** First, as noted by Mr. Robertson, what is referred to as the "actual cost of debt"
10 includes the impact of both a bank loan in the amount of \$1,000,000, at 5.5%,
11 and a loan from White River Valley Electric Cooperative for approximately
12 \$66,000, at 3.15%. The White River loan was specifically associated with the
13 purchase from, and installation by, White River of electric generators. This is not
14 money or a credit opportunity that would be available to Emerald Pointe in any
15 other context.

16
17 **Q. WHAT IS THE SECOND FLAW?**

18 **A.** The second flaw in Mr. Robertson's analysis is that even the bank loan Emerald
19 Pointe obtained at a 5.5% interest rate is not a true cost of debt for a "stand
20 alone" small water and sewer company.

21

1 Q. WHY DO YOU SAY THAT EMERALD POINTE'S ACTUAL COST OF DEBT IS
2 NOT A TRUE COST FOR A SMALL WATER AND SEWER COMPANY'S
3 ACTUAL COST OF DEBT?

4 A. The only reason Emerald Pointe was able to obtain a loan at this rate was
5 because Mr. Gary Snadon, Emerald Pointe's owner, personally guaranteed the
6 loan and pledged his personal assets, which are unrelated to the water and
7 sewer company's operations, as additional security. Had Mr. Snadon not
8 personally guaranteed this loan, lenders were not willing to loan Emerald Pointe
9 the money necessary to complete the sewer line project. The bank loan and the
10 rate of 5.5% were only available because of Mr. Snadon's extraordinary
11 individual actions.

12
13 Q. HOW DO YOU KNOW THAT BANKS WERE NOT WILLING TO LOAN MONEY
14 TO EMERALD POINTE WITHOUT A PERSONAL GUARANTEE FROM MR.
15 SNADON?

16 A. Because I personally talked with several banks and that is what I was told. The
17 bank that ultimately made the loan to Emerald Pointe specifically required Mr.
18 Snadon to personally guarantee, as well as pledge personal assets, before it
19 would be willing to make the loan. Even then, Emerald Pointe was only able to
20 obtain a five (5) year term, as the monthly principal and interest payments are
21 based on a twenty (20) year amortization with a five (5) year balloon payment. A
22 copy of the Bank's Conditional Loan Commitment is attached to my testimony as
23 Surrebuttal Schedule BDM-1.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23

Q. IF EMERALD POINTE HAD ATTEMPTED TO SECURE A LOAN BASED SOLELY UPON ITS OWN FINANCIAL CONDITION AND ASSETS, WHAT INTEREST RATE DO YOU BELIEVE IT WOULD HAVE CHARGED?

A. First, I don't believe Emerald Pointe would have been able to obtain a loan at any interest rate based on its financial condition and its assets. However, if a bank was willing to make such a loan, it would have been at an interest rate well above that of the larger water and sewer companies that Staff analyzed as part of its rate of return recommendation.

Q. PUBLIC COUNSEL CRITICIZES STAFF'S POSITION AS "NON-SENSICAL." (P. 20, LINE 12-16) DOES PUBLIC COUNSEL'S POSITION MAKE SENSE TO YOU?

A. No. Public Counsel is proposing a return on equity for Emerald Pointe of 9.35% which is lower than the 9.8% return on equity the Commission recently authorized Ameren Missouri and the 9.7% return on equity recently authorized for Kansas City Power & Light Company (KCPL). Clearly, Emerald Pointe's financial risk (i.e., debt to ratio) is far greater than Ameren or KCPL and its business risks (i.e., size and diversity) are also far greater. However, Mr. Robertson is recommending a lower return on equity for Emerald Pointe. This clearly does not make any sense in light of the Company's much higher risk factors.

1 Q. MR. MENKE, WHAT BACKGROUND DO YOU HAVE IN BUSINESS OR
2 FINANCE TO OFFER TESTIMONY REGARDING DEBT MATTERS?

3 A. As was stated in my Rebuttal Testimony, I spent approximately twenty-nine (29)
4 years working in the banking industry, with much of that time in commercial
5 lending.

6

7

LOCAL HEARING

8

9 Q. AT THE LOCAL HEARING IN THIS MATTER, THERE WAS SOME
10 TESTIMONY CONCERNING THE PERSONNEL RESPONSIBLE FOR
11 THE OPERATION AND MAINTENANCE OF THE EMERALD POINTE
12 SYSTEM. HOW DOES EMERALD POINTE OPERATE AND MAINTAIN
13 ITS SYSTEM?

14 A. Emerald Pointe has contracted with White River Valley Environmental for
15 approximately six and a half years to perform the tasks that are required to be
16 performed by a Missouri Department of Natural Resources certified operator.
17 Emerald Pointe has been pleased with this relationship and plans to continue this
18 relationship. Prior to that, the Company contracted with Hall, Inc., environmental
19 services, for its certified operator. Emerald Pointe also has a full time employee
20 to provide daily operations and maintenance for the Company. While the person
21 filling this full time position recently changed, a new employee was put in place
22 without any significant gap in the provision of services to customers.

23

1 Q. THERE WAS ALSO TESTIMONY AT THE LOCAL HEARING
2 CONCERNING SMELLS ASSOCIATED WITH EMERALD POINTE'S
3 SEWER SYSTEM. WHAT DO YOU BELIEVE WAS THE SOURCE OF
4 THESE COMPLAINTS?

5 A. It is my belief that the old treatment plant was the source of certain
6 unpleasant smells. That plant was operating near capacity and was in
7 need of replacement. Additionally, even after the Emerald Pointe
8 completed construction of the new line, the process of demolishing the old
9 plant would have also had a smell associated with it.

10

11 Q. SHOULD THIS SITUATION BE IMPROVED GOING FORWARD?

12 A. Yes. One of the advantages of the new line to Hollister and utilizing the
13 existing treatment plant in Hollister should be the elimination of these
14 issues in and around the Emerald Pointe system and Table Rock Lake.

15

16 REFUND ISSUES

17

18 Q. PUBLIC COUNSEL WITNESS KERI ROTH'S REBUTTAL TESTIMONY
19 DISCUSSED THE PUBLIC COUNSEL'S POSITION IN REGARD TO
20 CERTAIN ALLEGED REFUNDS. WHAT IS EMERALD POINTE'S
21 POSITION IN REGARD TO THOSE ISSUES?

22 A. Emerald Pointe believes that no refund is due in regard to the sewer
23 commodity charge issue. As to the late fees and reconnection fee issues,

BRUCE D. MENKE
SURREBUTTAL TESTIMONY

1 Emerald Pointe agrees with the calculation of the basic refund amounts,
2 but disputes the addition of interest. Emerald Pointe agrees the proposed
3 deposit refund, to include the interest calculations. Emerald Pointe
4 described its position in regard to these issues in its rebuttal testimony. I
5 do not believe that Ms. Roth's testimony requires any further response at
6 this time.

7

8 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

9 **A. Yes, it does.**