

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

City of O’Fallon, Missouri,)	
)	
Complainant,)	
)	
v.)	
)	
Missouri-American Water Company)	File No. WC-2010-0010
)	
and)	
)	
Public Water Supply District No. 2 of)	
Saint Charles County, Missouri,)	
)	
Respondents.)	

STAFF INVESTIGATION AND RECOMMENDATION

COMES NOW the Staff of the Missouri Public Service Commission, through the undersigned counsel, and files this *Investigation And Recommendation* with the Missouri Public Service Commission, respectfully stating the following:

Procedural History

1. On July 8, 2009, the City of O’Fallon, Missouri (O’Fallon) filed a *Complaint* in the above-stated cause, which stated O’Fallon seeks a new source of supply of water and desires to take wholesale service from Missouri-American Water Company (MAWC). *Complaint* p. 3. O’Fallon requests the Commission find either that the Territorial Agreement entered into by the Public Water Supply District No. 2 of Saint Charles County, Missouri (District) and MAWC is no longer in the public interest and should be revoked or that the Territorial Agreement is unlawful and with no force or effect as to O’Fallon.

2. On July 15, 2009, the Commission issued a *Notice Of Complaint And Order Directing Staff Investigation*, which directed the District and MAWC to file answers to the

Complaint by August 14, 2009, and the Staff to file a report and recommendation on its investigation no later than thirty (30) days after the Respondents filed their answers.

3. On August 14, 2009, the District filed their *Answer To Complaint*, which asserted four (4) affirmative defenses.

4. Also, on August 14, 2009, MAWC filed their *Answer And Motion To Dismiss*.

5. On September 14, 2009, Staff filed a *Motion For Extension To File Recommendation*, which requested the Commission allow until September 24, 2009 for the Staff to file a report of investigation and recommendation.

6. Also, on September 14, 2009, the Commission issued its *Ordering Granting Motion For Extension Of Time*, which allowed Staff until September 24, 2009 to file a report.

Investigation - Background

7. On January 17, 1985, O'Fallon and the District entered into a *Water Supply Agreement*. During this investigation, the Staff reviewed the agreement and determined that the agreement is essentially a territorial agreement couched as a water supply agreement, as the District was supplying no water to O'Fallon for resale distribution. Rather, the District supplies retail water to citizens within O'Fallon's city limits. Relevant provisions of the *Water Supply Agreement* for determining service areas are:

....[O'Fallon] intends to expand its corporate boundaries in certain areas south of Interstate Highway 70 and desires to have a water supply available in such areas; and....[O'Fallon's] present water supply is limited and expansion of its system into the areas described herein would require a substantial expenditure of funds; and....the parties agree that the District is in a more advantageous position than the City to economically expand and extend its water system and to furnish a water supply at a reasonable cost....and....[t]he District will be the exclusive supplier of water in the area south of Interstate Highway 70 within the present or future city limits of the City, except for the "excepted area"; and [O'Fallon] will not construct or extend facilities for the purpose of supplying water to said outlined area....

The term of the water supply agreement was twenty years from execution, or January 17, 2005.

8. On October 4, 2000, the District and MAWC entered into a *Territorial Agreement* pursuant to Section 247.172 RSMo (Supp. 2008), which designated the boundaries of the water service areas and powers granted to each of the signatories. Staff has reviewed maps provided by all parties of the service areas in question.

9. The term of the *Territorial Agreement* is thirty years. The relevant provision to the District's *Answer To Complaint* is paragraph four (4) of the agreement, which states "[n]either party may furnish, make available, render or extend service to a structure or customer or for use within the territory of the other party either directly, *indirectly* or through another entity controlled by the party or controlling the party, in whole or in part, excepting sales to each other." (Emphasis added).

10. On February 13, 2001, MAWC and the District filed a *Joint Application* that requested the Commission find the proposed *Territorial Agreement* not detrimental to the public interest and approve the agreement. On February 23, 2001, the Commission issued its *Order And Notice*, directing the Commission's Data Center to send "...a copy of the *Order And Notice* to the St. Charles County Commission", "notice to the members of the General Assembly representing the [signatories'] service areas, and to the newspapers which serve [the signatories'] service areas as listed in the newspaper directory of the current *Official Manual of the State of Missouri*." Additionally, interested parties were allowed twenty days to file for intervention. No applications to intervene were filed.

11. On April 16, 2001, the Staff, District, MAWC, and the Office of Public Counsel (OPC) filed a *Unanimous Stipulation And Agreement*, in which the parties stipulated that the *Territorial Agreement* meets the requirements of Section 247.172, and that the agreement is not detrimental to the public interest. On May 1, 2001, the Commission held an evidentiary hearing.

On May 15, 2001, the Commission issued its *Report And Order*, in which it concluded the proposed *Territorial Agreement* is not detrimental to the public interest, approved the *Territorial Agreement*, and the *Unanimous Stipulation And Agreement*.

12. On June 10, 2004, the District and O’Fallon entered into the *First Amendment To Water Supply Agreement*, which extended the *Water Supply Agreement* for another twenty (20) years.

Justiciability of Complaint—District Affirmative Defenses

13. To begin the analysis, Staff determined whether O’Fallon’s *Complaint* is a justiciable dispute before the Commission. The District alleged four (4) affirmative defenses: (1) “O’Fallon’s complaint fails to state a claim upon which relief can be granted by the Commission”, (2) “The complaint is an impermissible collateral attack on an order of the Commission barred by Section 386.550, RSMo 2000”, (3) “O’Fallon lacks standing”, and (4) “The Territorial Agreement was, at the time of its approval, and is, and continues to be, in the public interest.”

14. As to the District’s first affirmative defense, Section 247.172.7 provides:

[t]he commission shall have jurisdiction to entertain and hear complaints involving any commission-approved territorial agreement. Such complaints shall be brought and prosecuted in the same manner as other complaints before the commission.If the commission determines that a territorial agreement that is subject to a complaint is no longer in the public interest, it shall have the authority to *suspend or revoke* the territorial agreement. If the commission determines that the territorial agreement is still in the public interest, such territorial agreement shall remain in full force and effect.

(Emphasis added). Commission rule 4 CSR 240-2.070 (3) provides a....[f]ormal complaint may be made by petition or complaint in writing, setting forth any act or thing done or omitted to be done by any person, corporation or public utility,....in violation or

claimed to be in violation of any provision of law or of any rule or order or decision of the commission.

Further, Section (4) of the rule provides “[t]he commission shall not be required to dismiss any complaint because of the absence of direct damage to the complainant.”

15. In paragraph eight (8) of the *Complaint*, O’Fallon alleges it “is seeking a new source of supply of water and desires to take wholesale service from MAWC.” MAWC admits that O’Fallon has informed MAWC “that it desires to take service from MAWC pursuant to MAWC’s rates for ‘Sale to Resale’ water service now in effect....subject to the rules and regulations on file with, and approved by, the Commission.” *Answer And Motion To Dismiss*, Paragraph 10. The District answered that it “is without sufficient information sufficient to either admit or deny paragraph 8 and therefore denies the same.” *Answer To Complaint*, Paragraph 8. Further, in paragraph nine (9) of the *Complaint*, O’Fallon alleges “MAWC has, thus far, not agreed to provide service because of uncertainty surrounding the *Territorial Agreement*.” MAWC admits this allegation. *Answer And Motion To Dismiss*, paragraph 11. The District answered that it “is without sufficient information sufficient to either admit or deny the remaining allegations of paragraph [9] and therefore denies the same.” *Answer To Complaint*, paragraph 9.

16. Staff takes the position that O’Fallon has brought a *Complaint* that complies with 4 CSR 240-2.070 (3). Additionally, pursuant to Section 247.172 O’Fallon alleges a dispute of a *Territorial Agreement* approved by the Commission on May 15, 2001. The statute gives the Commission authority to grant relief, specifically, the authority to suspend or revoke territorial agreements that are no longer in the public interest.

17. As to the District's second and fourth affirmative defenses, Section 386.550 RSMo (2000) provides that "[i]n all collateral actions or proceedings the orders and decisions of the commission which have become final shall be conclusive." Section 247.172.5 (Supp. 2008) provides "[r]eview of commission decision under this section shall be governed by the provisions of sections 386.500 to 386.550, RSMo." Most applicable to this case is Section 386.550. The case of *Ozark Border Electric Cooperative v. Public Service Com'n*, 924 S.W.2d 597 (Mo. App. W.D. 1996) provides an applicable discussion on collateral attacks of final orders. Section 386.550 "makes a decision of the Commission immune to collateral attack." *Ozark* at 601. "If a complaint does not *allege* a change in circumstances it would be in conflict with this section providing for finality." *Id.* (Emphasis added). However,

[i]f a change in circumstance has occurred since the last order, the complaint would not be attacking the previous order and would not be in conflict with section 396.550. It would be an independent proceeding to determine whether the change in circumstances causes the territorial agreement to no longer be in the public interest.

Id. The *Complaint* alleges "there has been a substantial change in the character of the areas that were the subject of the *Territorial Agreement*." "In this substantially changed circumstance, the *Territorial Agreement* no longer serves the public interest to the extent it could be used to block the purchase of water by another water provider. This is especially the case here as whichever party supplies O'Fallon will have to construct facilities to do so." *Complaint*, paragraphs 15-16.

18. Described further below, Staff takes the position that O'Fallon is not collaterally attacking the Commission's *Report And Order* approving the *Territorial Agreement* as O'Fallon's *Complaint* alleged a change in circumstances. Additionally, from the pleadings, Staff asserts that the *Territorial Agreement* is no longer in the public interest.

19. As to the District's third affirmative defense, Staff takes the position that O'Fallon has standing to bring its *Complaint* before the Commission. To have legal standing to

prosecute a legal action a party seeking relief must have a legally cognizable interest in the subject matter and he or she must be facing a threatened injury or have suffered actual injury. *Eastern Missouri Laborers Dist. Council v. St. Louis County*, 781 S.W.2d 43, 46 (Mo. Banc 1989). “A legally protectible interest contemplates a pecuniary or personal interest directly in issue or jeopardy which is subject to some consequential relief, immediate or prospective.” *Absher v. Cooper*, 495 S.W.2d 696, 698 (Mo. App. 1973).

20. Section 247.172.6 RSMo (Supp. 2008) prescribes that “Commission approval of any territorial agreement entered into under the provisions of this section shall in no way affect or diminish the rights and duties of any water supplier not a party to the agreement to provide service within the boundaries designated in such territorial agreement.” Paragraph 18 of the *Complaint* states

[a]n interpretation of the *Territorial Agreement* that would require O’Fallon to purchase wholesale water exclusively from the District at a price that is substantially greater than that for which it can purchase that water from MAWC would certainly affect or diminish the rights and duties of O’Fallon – a water supplier that was not a party to the agreement....

O’Fallon’s pecuniary and personal interest at issue is its ability to purchase wholesale water from a provider of its choice. Although not calculated, O’Fallon alleged a threatened pecuniary injury, as well as a personal interest in its rights and duties as a water supplier.

Justiciability of Complaint—MAWC’s Motion To Dismiss

21. MAWC urges the Commission to dismiss O’Fallon’s *Complaint* because the *Territorial Agreement* only addresses the provision of retail water service to customers within the described boundaries. For Staff, while the *Territorial Agreement* is vague, when read as a whole it appears the agreement only supports the inclusion of retail service. Several paragraphs of the *Territorial Agreement* mention “customer” and “structures”, indicative of retail service.

Further, the exclusion of wholesale service does not mar the outlined intent of the *Territorial Agreement*; “to avoid wasteful duplication of facilities, stranded investment and underutilized system capacity and to allow orderly development, efficient planning for water system expansion and improvement, effective utilization of existing and future system capacity, efficient service and to minimize disputes which may result in higher costs in serving each party’s respective inhabitants.”

22. Neither the Commission’s statutes nor the *Territorial Agreement* specifically mention “wholesale service”. Wholesale service, unlike retail service under Section 393.130, is not an obligatory class of utility service. Further, as wholesale service involves two or more utilities, usually within different geographical and service areas, the provision of this service is not inherently exclusive to any one provider like retail service. Each agreement must be read to determine whether the parties contemplated retail and/or wholesale service within an agreement.

23. Although Staff takes this position on wholesale service, MAWC’s motion to dismiss should be denied. A “motion to dismiss.... admits the allegations of the petition for the purposes of that motion, it does not admit the truth of those allegations for all purposes. It is a limited admission only, and is no more or less than a claim by the defendant [MAWC] that even if those allegations were true, nevertheless they would be insufficient to constitute a cause of action against the defendant [MAWC]. *Leone v. Bilyeu*, 231 S.W.2d 265, 266 (Mo.App.1950). Considered true, the assertions within O’Fallon’s *Complaint* support a finding that the *Territorial Agreement* is no longer in the public interest.

Findings of Investigation

24. As discussed above, Staff's position is that the *Territorial Agreement* excludes wholesale service from its provisions.

25. However, independent of whether the parties contemplated wholesale within the *Territorial Agreement*, O'Fallon's *Complaint* and Staff's investigation support the Commission finding a substantial change in circumstances in this matter. A substantial change in the facts surrounding the approval of the *Territorial Agreement* successfully invokes the jurisdiction of the Commission:

O'Fallon provides water service to approximately 12,200 customers; approximately 9,900 of those customers are located outside the area covered by the *Territorial Agreement*; neither MAWC nor the District will incur stranded investment or wasteful duplication of current systems, as provision of the wholesale service requires additional placement of infrastructure regardless of the providing party; O'Fallon states "it has no intention to and will not provide water service to any customer within the area that is subject to its *Supply Agreement* with the District; the District will not lose any current customers; MAWC's wholesale commodity rate is \$1.5128 per 1,000 gallons, compared to the District's wholesale rate of \$3.00 per \$1,000 gallons; O'Fallon was not a party to the *Territorial Agreement*, and pursuant to 247.172.6 can not be limited in its provision of service.

26. The General Assembly of the State of Missouri many years ago, by enactment of the Public Service Commission Law (now Chapter 386), wisely concluded that the public interest would best be served by regulating public utilities. *Missouri Public Service Co. v. City of Trenton*, 509 S.W.2d 770, 775 (Mo. App. 1974). The legislature delegated the task of determining the public interest in relation to the regulation of public utilities to the Commission when it enacted Chapter 386, and all other chapters and sections related to the exercise of the Commission's authority.

27. The public interest is a matter of policy to be determined by the Commission. *State ex rel. Public Water Supply District v. Public Service Commission*, 600 S.W.2d 147, 154 (Mo. App. 1980). The dominant purpose in creation of the Commission is public welfare. *State*

ex rel. Mo. Pac. Freight Transport Co. v. Public Service Commission, 288 S.W.2d 679, 682 (Mo. App. 1956).

28. It is within the discretion of the Public Service Commission to determine when the evidence indicates the public interest would be served. *State ex rel. Intercon Gas, Inc. v. Public Service Com'n of Missouri*, 848 S.W.2d 593, 597 -598 (Mo. App. 1993). Determining what is in the interest of the public is a balancing process. *In the Matter of Sho-Me Power Electric Cooperative's Conversion from a Chapter 351 Corporation to a Chapter 394 Rural Electric Cooperative*, Case No. EO-93-0259, Report and Order issued September 17, 1993 , 1993 WL 719871 (Mo. P.S.C.). In making such a determination, the total interests of the public served must be assessed. *Id.* This means that some of the public may suffer adverse consequences for the total public interest. *Id.* Individual rights are subservient to the rights of the public. *State ex rel. Mo. Pac. Freight Transport Co. v. Public Service Commission*, 288 S.W.2d 679, 682 (Mo. App. 1956). The “public interest” necessarily must include the interests of both the rate-paying public and the investing public; however, as noted, the rights of individual groups are subservient to the rights of the public in general.

Recommendation

29. The *Territorial Agreement* should not restrict O'Fallon's water utility operations. The Staff believes the *Territorial Agreement* does not apply to the proposed wholesale arrangement, and recommends that the Commission find the *Territorial Agreement* does not apply to wholesale service with respect to O'Fallon. However, due to the vagueness of exclusions within the document, this point is arguable. Therefore, Staff makes an alternative recommendation that, for the reasons mentioned above, the Commission find the *Territorial Agreement* between the District and MAWC no longer in the public interest and suspend the

Territorial Agreement until such time the District and MAWC present the Commission with a *Territorial Agreement* in the public interest and approvable. Staff's Memorandum is attached hereto as Attachment A and incorporated herein.

WHEREFORE, the Staff submits this *Investigation And Recommendation* to the Commission for its information and consideration.

Respectfully submitted,

/s/ Jennifer Hernandez

Jennifer Hernandez

Legal Counsel

Missouri Bar No. 59814

Attorney for the Staff of the
Missouri Public Service Commission
P. O. Box 360

Jefferson City, MO 65102

(573) 751- 8706 (Telephone)

(573) 751-9285 (Fax)

jennifer.hernandez@psc.mo.gov

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served via electronic mail on Leland B. Curtis and Kevin M. O'Keefe of Curtis, Heinz, Garrett & O'Keefe, P.C., attorneys for the City of O'Fallon at lcurtis@lawfirmemail.com; Mark W. Comley, Newman, Comley & Ruth P.C., attorney for the District at comley@ncrpc.com; Mark C. Piontek, Lewis Rice Fingersh L.C., attorney for the District at mpiontek@lewisrice.com; Kenneth Jones, attorney for MAWC at kenneth.jones@amwater.com; Dean L. Cooper, Brydon, Swearngen & England P.C., attorney for MAWC at dcooper@brydonlaw.com; and the Office of Public Counsel at opcservice@ded.mo.gov this 24th day of September, 2009.

/s/ Jennifer Hernandez

MEMORANDUM

TO: Missouri Public Service Commission Official Case File
Case Nos. WC-2010-0010
City of O'Fallon, Missouri, Complainant, v. Missouri-American Water
Company and Public Water Supply District No. 2 of St. Charles County

FROM: Jim Merciel – Water & Sewer Department

<u>/s/ Jim Merciel</u> Project Coordinator	<u>9/24/09</u> Date
<u>/s/ Jennifer Hernandez</u> General Counsel's Office	<u>9/24/09</u> Date

SUBJECT: Staff's Recommendation Regarding Complaint

DATE: September 24, 2009

BACKGROUND

On July 8, 2009, the City of O'Fallon (O'Fallon) filed a formal complaint against Missouri-American Water Company (MAWC or Company) and Public Water Supply District 2 of St. Charles County (District). In its complaint, O'Fallon states that it desires to obtain wholesale water service from MAWC, but that there are uncertainties as to whether a *Territorial Agreement* between MAWC and the District, approved by the Commission, permits such a wholesale arrangement since many of O'Fallon's customers who would benefit from such wholesale service are located within the District's area that is included in the *Territorial Agreement*.

STAFF'S ANALYSIS OF THE ISSUE

Wholesale service is not specifically mentioned in the state statutes, or in the *Territorial Agreement*. Wholesale service, unlike retail service, is not an obligatory class of utility service. Further, because it involves two or more utilities, usually with different service areas, providing wholesale service is not inherently exclusive to any provider. However, when a territorial agreement exists between two utility parties, wholesale service prohibition between one of the parties as a seller and a third party purchaser outside of the seller's territorial area should apply in some circumstances if the wholesale purchaser and/or seller are violating the intent of a territorial agreement, meaning that providing service by wholesale results in denial of retail service to those customers to the territorial party who would otherwise be providing service. A clear example of this would be the creation a homeowners association or nonprofit utility that is formed in one party's territorial area to create the ability to obtain wholesale service from the other party.

While a specific case by case analysis is necessary, the policy of wholesale service should not be prohibited between a seller and a legitimately established utility that may have overlapping service areas with one or both of the territorial parties, and the established utility obtains the service simply for the purpose of serving its own customers. As support in this case, the third party utility and its customers are not a party to the territorial agreement, and additionally as in most circumstances, the third party utility serves customers that are outside of the areas contemplated by the territorial agreement.

The municipality of O'Fallon is in St. Charles County, and provides water service to approximately 12,200 customers. Approximately 9,900 of those customers are located north of Interstate 70 and outside of the area covered by the *Territorial Agreement*. O'Fallon's city limits extend to areas both north and south of Interstate 70, overlapping both the District's and MAWC's approved service territories. Approximately 2,300 of O'Fallon's customers are within the area of the Territorial Agreement, the vast majority of those customers within the District's area. Many O'Fallon citizens south of Interstate 70 also obtain retail water service from either the District or MAWC. While the Staff investigated the situation, O'Fallon stated that it needs to improve water distribution in its service area south of I-70, and it is attempting to do so in the most economical way. O'Fallon's alternatives include wholesale service from MAWC at a commodity rate of \$1.5128 per 1,000 gallons, wholesale service from the District at a commodity rate of \$3.00 per 1,000 gallons, or construction of a storage tank. Also necessary are the appropriate pipeline improvements to work best with the selected alternative.

O'Fallon is a municipal utility that is not a signatory to the *Territorial Agreement*, and which provides service to its own customers both within and without the territorial service areas of the District and MAWC. O'Fallon also has an agreement with the District that is similar to a territorial agreement. Though not approved by the Commission, the agreement outlines the areas that will be served retail by O'Fallon, and those and that will be served by the District. This agreement applies within the District's area of the *Territorial Agreement*. If the *Territorial Agreement* includes the provision of wholesale service, the proposed wholesale arrangement between MAWC and O'Fallon is arguably "indirectly" furnishing service to customers within the District's territory, a violation of paragraph 4 of the *Territorial Agreement*. On the other hand, MAWC is simply supplying water to O'Fallon for resale to any of its customers, and the supply has no negative impact upon the District or its customers. If a MAWC wholesale arrangement is put in place, no customers or assets would be transferred from or to any other utility. The Staff believes, given all of the aspects of this arrangement, that O'Fallon should not be affected by the territorial agreement, and therefore any wholesale arrangement that O'Fallon is able to enter into with any party should not be prohibited by the *Territorial Agreement*. Further, however, the Staff believes that if it is determined that O'Fallon was limited due to the *Territorial Agreement* in how it operates its water utility and the costs it must incur, then the *Territorial Agreement* is no longer in the public interest.

CONCLUSION AND RECOMMENDATION

The Staff believes that it is important that O'Fallon not be restricted with respect to its water utility operation because of the *Territorial Agreement*. The Staff believes the *Territorial Agreement* does not apply to the proposed wholesale arrangement, and therefore Staff recommends that the Commission determine the *Territorial Agreement* does not apply to wholesale service with respect to O'Fallon. However, due to the vagueness of exclusions within the document, this point is arguable. Therefore, Staff makes an alternative recommendation that, for the reasons mentioned above regarding O'Fallon as a third-party utility, the Commission find the *Territorial Agreement* between the District and MAWC no longer in the public interest, and suspend the *Territorial Agreement* until such time the Commission is presented with a modification to the *Territorial Agreement* that it believes in the public interest and that can be approved.

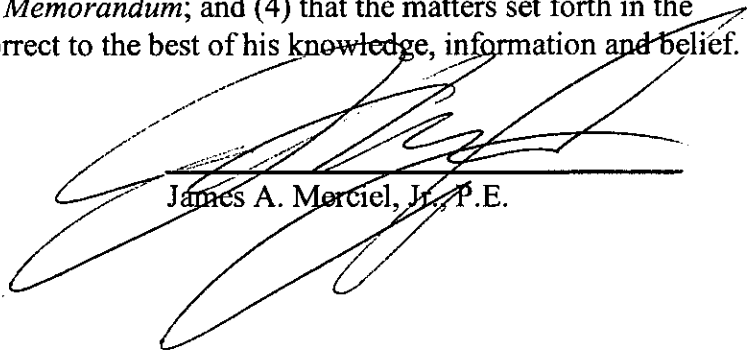
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Missouri, Respondents)	

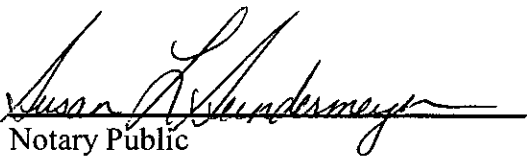
AFFIDAVIT OF JAMES A. MERCIEL, JR., P.E.

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

James A. Merciel, Jr., of lawful age, on his oath states: (1) that he is the Assistant Manager – Engineering in the Water and Sewer Department of the Missouri Public Service Commission; (2) that he participated in the preparation of the foregoing *Memorandum*; (3) that he has knowledge of the matters set forth in the foregoing *Memorandum*; and (4) that the matters set forth in the foregoing *Memorandum* are true and correct to the best of his knowledge, information and belief.


James A. Merciel, Jr., P.E.

Subscribed and sworn to before me this 24th day of September 2009.


Notary Public



SUSAN L. SUNDERMEYER
My Commission Expires
September 21, 2010
Callaway County
Commission #06942086