

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

In the Matter of the Water Rate)
Increase Request of)
Hillcrest Utility Operating) Case No. WR-2016-0064
Company, Inc.)

HILLCREST’S INITIAL BRIEF

COMES NOW Hillcrest Utility Operating Company, Inc. (Hillcrest or Company), and as its Initial Brief in this matter, states as follows to the Missouri Public Service Commission (Commission):

The following sections will address those issues described in the *List of Issues, List and Order of Witnesses, Order of Opening Statements, and Order of Cross-Examination*, filed on May 13, 2016.

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1. Introduction

Hillcrest acquired the subject water and sewer systems from Brandco Investments, LLC, which was a company regulated by the Commission. (Hillcrest Exh. 1, Cox Dir., p. 7) The Commission provided approval of this transaction in its File No. WO-2014-0340. (*Id.*) Hillcrest became the owner of the systems on March 13, 2015. (*Id.* at p. 8)

This case is the first rate case in decades for the water and sewer systems previously owned by Brandco Investments, LLC, and now owned by Hillcrest. (*Id.* at p. 13) The original systems' tariffs were established in 1989, and readopted in whole in 2007, by the previous owner, Brandco Investments, LLC, without a change in the rate. (*Id.*) The actual rates have been unchanged since 1989. (*Id.*)

The Brandco systems had a history of serious compliance issues and were in disrepair. This was especially true on the wastewater side where the wastewater treatment plant had been under multiple Missouri Department of Natural Resources (MDNR) and Missouri Attorney General compliance and enforcement actions. (Hillcrest Exh. 1, Cox Dir., p. 8-9) The drinking water system also had significant problems. In fact, the system was so bad and had such few assets that during the acquisition case, and before it owned the systems, Hillcrest intervened and paid for emergency repairs, a temporary water disinfection system, and operations in order to get a long-going boil order lifted while the case was progressing. (*Id.* at p. 9-12) As a part of the acquisition process, Hillcrest entered into an Agreement on Consent with the Missouri Attorney

General and the Missouri Department of Natural Resources requiring Hillcrest to make immediate improvements to the Hillcrest wastewater and drinking water systems. (*Id.* at p. 9-12)

When Hillcrest came before this Commission seeking approval of its proposed acquisition and proposed financing, Hillcrest described the system issues, the costs of necessary improvements, and the cost of money it had available to address these issues. (Hillcrest Exh. 1, Cox Dir., p. 12) This included the Company's estimate that the required improvements would result in an increase of \$49/month to the Hillcrest water rates and an increase of \$71/ month for the sewer rates. (Hillcrest Exh. 2, Cox Reb., p. 5)

In the acquisition case, Staff described the Brandco situation as follows in its initial recommendation:

Staff is quite familiar with Brandco, having spent a considerable amount of time assisting the utility with its operations issues and shortcomings, customer billing, and financial reporting. Although the owner of Brandco has been running the utility for a number of years, he no longer has adequate ability to accomplish operations tasks, and also has limited financial resources. Staff takes the position that, without question, the owner of Brandco needs to be able to exit the responsibilities associated with owning and operating a utility company.

In the Matter of the Joint Application of Brandco Investments, LLC and Hillcrest Utility Operating Company, Inc., Staff Recommendation/Memorandum, p. 3 of 13, File No. WO-2014-0340 (filed August 26, 2014).

Hillcrest began construction on drinking water and wastewater improvements approximately 30 days after acquiring the systems. (Hillcrest Exh. 1, Cox Dir., p. 12) Since that time, Hillcrest invested approximately \$1,205,000, in water and sewer

facilities in order to bring these facilities into compliance. (*Id.* at p. 13) This is very comparable to the original estimate of approximately \$1,230,000 Hillcrest provided in its Application in File No. WO-2014-0340 (the acquisition and finance case). (*Id.*) The construction was completed in the fall of 2015. (*Id.*) This completed construction satisfied the Agreement on Consent Hillcrest had with the Attorney General and the Department of Natural Resources. (Hillcrest Exh. 2, Cox Reb., p. 5)

Unfortunately, no matter what the Commission decides, there will be a significant increase in rates for the Hillcrest customers. This is due to the lack of past rate increases as well as the need for a substantial rebuild of both the water and wastewater systems: (1) to be operational for the provision of service to the customers; and (2) to comply with federal and state regulations related to those services. (Hillcrest Exh. 1, Cox Dir., p. 14) There are no shortcuts when systems are in this condition. (*Id.*) Choices are very limited and those choices are expensive -- especially when compared to the number of customers served by the systems. (*Id.*)

2. Corporate Allocation

What is the appropriate corporate allocation percentage to apply to corporate costs?

Hillcrest has proposed to allocate fourteen percent (14%) of its corporate costs to Hillcrest for ratemaking purposes. Staff has used the same allocation. The 14% represents the percentage of work time the Company believes will be required of its employees, at some point in the future, provided the organization is able to complete additional acquisitions. (Hillcrest Exh. 2, Cox Reb., p. 13).

Basing the allocation on either current customers or time sheets would result in a higher allocation to Hillcrest.

Customers –

In addition to Hillcrest, First Round CSWR, LLC owns and operates Raccoon Creek Utility Operating Company, Inc. and Indian Hills Utility Operating Company, Inc. (OPC Exh. 1, Roth Dir., p. 2) Raccoon Creek has approximately 500 sewer customers. (*Id.* at p. 2) Indian Hills has approximately 700 water customers. (*Id.* at p. 3) Hillcrest has approximately 242 water customers and 240 sewer customers. (*Id.* at p. 2)

This means there are 1,682 total water and sewer customers and 482 Hillcrest customers. Dividing the 482 Hillcrest customers by the 1,682 total customers reveals that the Hillcrest customers currently represent 28.6% of the total customer base. (Tr. 198) Thus, if customer numbers are used as an allocation factor, Hillcrest would bear 28.6% of the corporate costs – more than twice as much as proposed by Hillcrest and the Staff.

Time -

OPC witness Roth proposed an allocation percentage of 10.4% based on her review of Mr. Cox's time sheets from March 13, 2015 (the date of acquisition) through October 31, 2015. (OPC Exh. 3, Roth Reb., Sch. KNR-1; Tr. 199) The referenced time sheets are those found in Hillcrest Exh. 3 HC. (Tr. 134-136, 199)

OPC witness Roth alleges that "OPC can only rely on Mr. Cox's timesheets to calculate an allocation of their time for Hillcrest" because Mr. Chalfant and Ms. Eaves (the other two First Round CSWR, LLC employees who were hired in 2015) did not begin recording their time until after October 2015. (OPC Ex. 3, p. 2; Tr. 131) However,

she is also aware that these employees do have time sheets from November 1, 2015, through the current day, and she has seen those time sheets. (Tr. 199) It appears OPC has merely “chosen” not to look at those time sheets.

Hillcrest has chosen to look at those time sheets and believes that the allocation percentages would be closer to 21%, if only operational time were considered, and a much higher percentage if time spent on the Hillcrest rate case was also considered. (Hillcrest Exh. 2, Cox Reb., p. 14)

Ms. Roth computes total period hours of 1,697, and then identifies 178 hours she says are related to Hillcrest. (OPC Exh. 3, Roth Reb., Sch. KNR-1) Dividing the 178 by the 1,697 produces the 10.49% figure. A review of Ms. Roth’s calculation in relation to Hillcrest Exh. 3 reveals that Ms. Roth used only those hours found in the HC (or Hillcrest) column to determine work associated with Hillcrest. (Tr. 205) She identified all other hours as “non-regulated”. (OPC Exh. 3, Roth Reb., Sch. KNR-1)

Mr. Cox explained that work related to the Hillcrest systems is also found in the columns identified as “Admin”, “Eng”, “Contractor Procurement”, “PSC”, and “DNR”. (Tr. 134-136) “Admin” is the ongoing operations of the utilities. (*Id.*) “Engineering” is the time spent working on the engineering of the existing systems or future system. (*Id.*) “Contract procurement” is finding, bidding and negotiating with the operations and maintenance contractors and other entities that will work on the systems. (*Id.*) “PSC” is the time meeting with Commission staff about cases involving the utilities. (*Id.*) “DNR” is working with the Department of Natural Resources on the systems. (*Id.*)

Ms. Roth did not use any of these hours in her calculation because she found it “difficult” to “pull out” hours from those other categories. (Tr. 205) Consequently, she just viewed all of those hours as non-regulated. (Tr. 206)

Basic math indicates that in the period examined by Ms. Roth, 238 hours of Mr. Cox’s time would exceed 14% of his time (1,697 total hours * 14% = 237.58). Ms. Roth identified 178 hours in the Hillcrest (HC) column alone. Thus, if at least 60 hours of the remaining time is associated with Hillcrest, the OPC allocation percentage would be 14% or greater.

A review of Hillcrest Exh. 3 reveals the following hours during the relevant time period (a time when First Round CSWR’s only regulated utilities were Hillcrest and Raccoon Creek) in the other identified categories:

Category	Hours
Admin	398.0
ENG	226.5
Contract Procurement	29.5
PSC	91.5
DNR	20.0
TOTAL	765.5

Thus, if only 8% of those hours were thought to be attributable to Hillcrest, then OPC’s approach would support the 14% allocation. If 50% of those hours were assigned to Hillcrest, then OPC’s approach would support a 33% allocation of costs to Hillcrest.

The 14% allocation factor supported by Hillcrest and Staff already is a benefit to the Hillcrest customers. There is no evidentiary basis to use a lower percentage as suggested by OPC.

3. Payroll

Hillcrest has no employees. Several functions related to its operation are provided by three employees of Central States – Mr. Cox, a financial manager, and an administrative employee. (Hillcrest Exh. 1, Cox Dir., p. 14) A portion of the costs associated with those employees is then allocated to Hillcrest.

Both Staff and the Company have sought to establish reasonable salaries by reference to the Missouri Economic Research and Information Center (MERIC) wage estimates based on the St. Louis region and a 2014 study. (Hillcrest Exh. 1, Cox Dir., p. 15)

A. What level of experience should be used to set the labor expense associated with each employee?

In utilizing the MERIC data, Staff assumed that the three employees (Mr. Chalfant, Mr. Cox, and Ms. Eaves) possessed mean (or average) experience levels, rather than “experience” levels. (Hillcrest Exh. 1, Cox Dir., p. 15)

Mr. Chalfant, the chief financial officer (or “financial manager” under MERIC) has over 41 years of financial experience. (Hillcrest Exh. 1, Cox Dir., p. 16) He is a registered CPA, holds a B.S. in Accounting, and an MBA from Kansas State University. (*Id.*) His previous experience includes being a Director of Finance at Colgate-Palmolive, a Fortune 100 company, overseeing over \$100MM of budget. (*Id.*)

Recently, Mr. Chalfant was the CFO of a privately held surfaces company with over \$90MM in balance sheet and budget. (*Id.*)

Mr. Cox, the president (or “chief executive” under MERIC) has a B.S. in Environmental Science from the University of Kansas and a MBA from Washington University in St. Louis. (*Id.*) His previous tenures have included a director role inside an engineering firm. (*Id.*) Mr. Cox has been in the capital markets raising, and attempting to raise, debt and equity for small water and sewer systems since 2010, visiting with to date over 80 investment banks, private equity firms, institutional investment groups, and financing companies. (*Id.* at p. 16-17) He is responsible for utility acquisition work including evaluation of the existing utility assets for acquisition, determination of existing net book value of acquisition targets, engineering design/technology selection for new improvements, construction contractor selection, construction management (since 2015 Central States has completed approximately \$4.3MM in new plant investment with \$2MM currently in progress), ongoing O&M management including monitoring all plant remote operations and emergency responses, new utility rate design/pro-forma financial models, and overall companywide management. (*Id.* at p. 17) This myriad current job responsibility is more than almost any executive inside the water and wastewater utility industry. (*Id.*)

Ms. Eaves, the office manager (or “executive administrative” under MERIC), holds a BA from Washington University in St. Louis. (*Id.*) She has over 30 years of director experience managing large financial institution offices, and she most recently managed the office of the third largest drinking water well services company in Missouri before coming to Central States. (*Id.*)

The employees at issue have substantial years of work experience in various business environments and significant educational backgrounds. They should be considered at the “experience” level, and not the “mean” (or average) level.

B. Should the Employment Cost Index inflation rates be applied in setting such amounts?

All the salaries should be adjusted using the Employment Cost Index inflation rates in order to accurately reflect current market conditions, rather than utilizing data that is two years old. (Hillcrest Exh. 1, Cox Dir., p. 17)

C. What is the appropriate number of annual work hours to include in calculating salaries for each employee?

It is appropriate to use a full year of work (2,080 hours), as Hillcrest proposes that only fourteen percent (14%) of the total salary be allocated to Hillcrest. The allocation percentage is further discussed above.

D. What is the appropriate hourly rate for each employee?

The use of the MERIC data, adjusted for inflation, and applied to the job titles and experience identified below lead to the following hourly rates as ** _____

_____** for Ms. Eaves. However, if Hillcrest’s position as to corporate allocations is accepted by the Commission, only 14% of MERIC salary amount is being allocated to Hillcrest. (Hillcrest Exh. 2, Cox Reb., p. 14)

E. What are the appropriate job titles to use in MERIC to compare and determine labor expense associated with Mr. Josiah Cox and Mr. Jack Chalfant?

Mr. Cox should be identified under category “11-1011 Experience Chief Executive,” and Mr. Chalfant should be identified under category “11-3031 Experience Financial Manager.” (Hillcrest Exh. 1, Cox Dir., p. 17-18)

4. Property Taxes

A. What is the appropriate amount of property taxes to include in the Hillcrest revenue requirements? B. Should estimated property tax amounts be included in rates?

This issue arises from the fact that since the last tax bill was paid for Cape Girardeau County, Hillcrest has made over \$1.2 million in improvements to the water and wastewater systems. (Hillcrest Exh. 1, Cox Dir., p. 18) Those improvements are in service during the true-up period in this case. It is known that they will be taken into account in the property tax Hillcrest will pay this year, as well as in future years. (*Id.*, p. 18-19)

Hillcrest has worked with the Cape Girardeau County Assessor's office in an effort to make the taxes as affordable as the County Assessor will allow. (Hillcrest Exh. 2, Cox Reb., p. 20) As result of these discussions, it is now estimated that the new personal property tax amount will be, at least, \$2,972. (*Id.* at p. 21)

Ignoring this obvious new cost will directly impact Hillcrest's opportunity to earn its authorized rate of return, no matter what that may be. Staff argues that the property tax should not be included in Hillcrest's revenue requirement because it is not "known and measurable." (Staff Exh. 11, Sarver Dir., p. 4) Staff witness Sarver defines "known and measurable" to mean "the utility costs under review are associated with an event that has already occurred and the change in costs associated with the event can be measured with a high degree of accuracy." (*Id.*) Certainly it is known that an increase in personal property tax will result from the construction that was completed within the true-up period. The remaining question seems to be whether the new cost can be measured with a "high degree of accuracy."

Hillcrest believes that it can, in that the amount will be least \$2,972. Any lack of accuracy will be to the detriment of the Company, not the customers. However, this lack of accuracy in the face of significant new construction can be addressed by the Commission. In the case *In the Matter of Missouri-American Water Company's Tariff Sheets Designed to Implement General Rate Increase, et al*, Report and Order, Case No. WR-2000-281 (issued August 31, 2000), the Commission authorized a refundable surcharge for property taxes in the face of the significant investment in the then new St. Joseph treatment plant.

Short of a surcharge, the Commission could include the \$2,972 in Hillcrest's revenue requirement and, in conjunction therewith, authorize a tracker through which the Company would recognize amounts paid above, or below, the \$2,972 on an annual basis (a regulatory asset or liability). Doing so would protect both the customers and the Company from any variation from the estimate.

5. Auditing and Income Tax Preparation Fees

A. What is the appropriate amount of Hillcrest's auditing and tax preparation (accounting) costs to include in Hillcrest's cost of service? B. What is the appropriate allocated level of auditing and tax preparation (accounting) costs for Central States Water Resources to include in Hillcrest's cost of service? C. Should accounting costs incurred and paid in 2016 by Hillcrest be included in Hillcrest's cost of service?

One of the major problems facing failing water and sewer companies is a lack of professional management and attention to regulatory and statutory compliance.

(Hillcrest Exh. 1, Cox Dir., p. 21) The former owner of these systems did not correctly file taxes forms, nor did they develop and maintain accurate financial records. (*Id.*) Tax preparation and audit fees are a normal course of business for a professionally

managed utility. (*Id.*) This is particularly important for a utility, or group of utilities, that is actively engaged in attempting to raise capital. (*Id.*)

The Company issued requests for proposals (RFP) and circulated those RFP's to a variety of accountants and accounting firms in order to determine the least expensive qualified firm for rate making purposes. (*Id.* at p. 20) For tax preparation services at Hillcrest, the lowest qualified cost is \$6,000 per year. (*Id.*) For audit services at Hillcrest, the lowest qualified cost is \$11,000 per year. (*Id.*) For tax preparation services at Central States, the lowest qualified cost is \$4,850 per year. For audit services at Central States, the lowest qualified cost is \$10,000. (*Id.*) Central States/Hillcrest has hired this firm. (*Id.*)

The Commission should order that the following amounts be included in Hillcrest's revenue requirement: \$6,000 for Hillcrest's tax preparation; \$11,000 for Hillcrest's audit fees and, \$2,429, to correspond with a 14% allocation of Central States tax preparation fees and a 14% allocation of Central States audit fees.

6. **Rate of Return**

A. What is the appropriate capital structure for the purpose of setting Hillcrest's allowed rate of return?

Hillcrest's actual capital structure (19% equity, 81% debt) should be used to calculate the Company's overall rate of return. (Hillcrest Exh. 2, Cox Reb., p. 21, as corrected at Tr. 44)

B. What is the appropriate allowed ROE to apply to the equity in the ratemaking capital structure?

Hillcrest finds the Staff's range of equity recommendations – 12.88% to 14.13% - to be reasonable. (Hillcrest Exh. 2, Cox Reb., p. 22)

C. What is the appropriate allowed debt rate to apply to the debt in the ratemaking capital structure?

Hillcrest's actual debt cost (14%) should be used. To do otherwise, is to assume financing that just is not available to Hillcrest for the purpose of completing the necessary improvements. (Hillcrest Exh. 2, Cox Reb., p. 22)

The Commission is familiar with the following quote from *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944):

'[R]egulation does not insure that the business shall produce net revenues.' But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.

Normally, this standard is applied to the equity side of the equation, as the Staff would normally take a corporation's actual debt cost into consideration in developing the rate of return. (Tr. 178) Here, the Staff is attempting to develop a hypothetical debt cost in addition to the appropriate equity return.

Staff has not alleged that the debt is imprudent. (Tr. 178) This would, in fact, be a difficult argument to make given that the Commission provided Hillcrest authority to enter into this evidence of indebtedness, and to encumber its assets, in Commission File No. WO-2014-0340. *In the Matter of the Joint Application of Brandco Investments, LLC and Hillcrest Utility Operating Company, Inc.*, Order Approving Stipulation and Agreement and Granting a Certificate of Convenience and Necessity (Issued October 22, 2014) (Hillcrest was authorized "to enter into, execute, and deliver loan

agreements”; “to create and make effective a first lien on all the franchises, certificates of convenience and necessity, plant and systems of Hillcrest, to secure its obligations”; and, “to enter into, execute, deliver, and perform the necessary promissory notes, loan agreements, and other documents necessary to effectuate the financing transactions).

However, if the Commission should consider the abandonment of the actual debt cost, it should only do so while keeping in mind the purpose of this process as set forth in the *Hope* case. That is, the goal to provide a sufficient return such that the utility can attract capital.

As was suggested in the Company’s opening statement, the Staff, OPC, and Company are, to a certain extent, ships passing in the night.

Mr. Cox has attempted to raise money for the purpose of construction in small water and sewer companies for many years. Prior to filing its first asset acquisition and financing case, Central States/Hillcrest met with over fifty specialized infrastructure institutional investors, private equity investors, and investment bankers in an attempt to create a program to build water and wastewater improvements to support distressed small water and wastewater utilities in Missouri. (Hillcrest Exh. 1, Cox Dir., p. 24) In addition, he met with numerous traditional banks seeking commercial bank financing. (*Id.*) The capital structure Hillcrest is utilizing is the only structure that could be found. (*Id.*) Moreover, this is the same structure Hillcrest presented to Commission in its acquisition and financing application. (*Id.*)

Staff has taken an academic approach to identifying a debt cost. However, that academic approach is based on on all sorts of theoretical niceties that are not applicable here.

OPC has taken the approach of attempting to attack the character of Mr. Cox in ways that have no impact on the underlying facts.

The bottom line is that no party, other than Hillcrest, can identify a source of capital and debt that can provide the money to make \$1.2 M in improvements necessary for these failing water and sewer systems.

For perspective, Staff determined that Brandco (the prior owner of the Hillcrest systems) had a net book value of \$82,282 (water and wastewater combined) at the time of Hillcrest's acquisition case. (Hillcrest Exh. 1, Cox Dir., p. 23) Hillcrest estimated the MDNR mandated capital expenditure would be \$1,230,000. (*Id.*) Hillcrest's net book value versus required MDNR investment dollars represented a 7% equity basis. (*Id.*) The utility had a significant commercial liability with existing Missouri Attorney General enforcement actions, on-going and past pollution, and an actual public health risk with the on-going boil order. (*Id.*) In order to keep the system running and provide basic services during the acquisition, Hillcrest had to enter into an agreement with MDNR to pay for repairs, disinfection of the drinking water, and on-going inspections for a system it did not yet own. (*Id.*) Hillcrest also had to enter into an agreement with MDNR and the Missouri Attorney General to build all of the necessary improvements during a set time frame, in order to not be held liable for previous violations at the site. (*Id.*) This meant Hillcrest had to agree to invest over \$1.2 million, in a very short time frame, without any new revenues until some unknown time after the construction had been completed -- something that would be required of any entity that attempted to bring these systems into compliance. (*Id.*)

Capital has not been attracted to small systems that require this type of substantial construction at any rate other than Hillcrest's actual debt rate. It is certainly Mr. Cox's hope that this organization can grow, establish a track record, and establish sufficient revenues to make less expensive financing available for systems in the future. However, that day is not here yet.

Because of the need to attract capital, this rate of return issue may be the most important issue before the Commission in this case. This organization has also made approximately \$1.4 million in investments in the three systems that are a part of the Raccoon Creek Utility Operating Company, Inc.; has begun making improvements to the Indian Hills Utility Operating Company, Inc. system that are estimated to cost about \$1.8 million; and is working with the Commission Staff as to various other failing systems, to include contracts concerning two other systems that are currently in receivership.

The Commission's treatment of the funds that are available to address those situations will be important information for those involved, or to those that might agree to become involved as this effort moves forward. Any potential investor has to have confidence that the actual capital structure required to fix failing water and sewer utilities will be recognized for rate making purposes. (Hillcrest Exh. 1, Cox Dir., p. 24) This is especially true for systems that are out of regulatory compliance and carrying higher commercial liability risks with lower equity bases. (*Id.*)

7. **Rate Design**

A. How many classes should Hillcrest's customers be divided into for the purpose of designing rates for both water and sewer?

Hillcrest does not object to the classes proposed by either the Staff or the OPC.
(Hillcrest Exh. 2, Cox Reb., p. 2)

B. What are the proper allocation percentages to be used to allocate expenses between the customer charge and volumetric rate?

In setting the customer charge and volumetric charge for the water rates, the Commission should be mindful of the fact that water costs are primarily fixed, the average volumes used by Staff may be overstated (Hillcrest Exh. 2, Cox Reb., p. 2), and recovery of most costs through the customer charge may be the only way to provide Hillcrest with a reasonable opportunity to recover whatever revenue requirement may be set in this case.

Hillcrest supports the assignment of costs to the customer charge and volumetric charge as reflected in the Direct Testimony of OPC witness Russo. (OPC Exh. 5)

C. Should a rate increase be implemented all at once or phased-in over time?

There should not be a “phase-in.” Between the agreed upon partial stipulation operational costs and Hillcrest’s actual debt service payments, a phase-in year would not provide Hillcrest with enough money to make its debt payment. (Hillcrest Exh. 2, Cox Reb., p. 9) The “phase in year” does not include any money for corporate management of Hillcrest, taxes, earnings on improvements that are in service and used and useful, or depreciation expense on improvements that are in service and used and useful. (*Id.*)

Small utilities are cash businesses that have real expenses like debt payments, tax preparation fees, property taxes, and actual management costs that are required to operate. (*Id.* at p. 10) Hillcrest believes a lack of professional management and a lack

of access to capital are major contributors to difficulties being experienced in many of Missouri's small water and sewer systems. (*Id.*)

Further, the carrying costs associated with the booking of the deferred revenues resulting from a phase-in means that, in the end, the customers will pay more out of their pockets than they would in the absence of a phase-in, all else being equal. (*Id.* at p. 10)

OPC witness Russo indicated that he was not aware of the Commission ordering a phase-in of rates. (Tr. 233) This is not a surprise. The only statute that purports to provide the Commission with authority to authorize a rate increase that is less than the full amount of a utility's revenue deficiency is found in Section 393.155, RSMo, which states in pertinent part as follows:

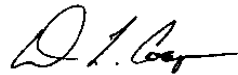
If, after hearing, the commission determines that any electrical corporation should be allowed a total increase in revenue that is primarily due to an unusually large increase in the corporation's rate base, the commission, in its discretion, need not allow the full amount of such increase to take effect at one time, but may instead phase-in such increase over a reasonable number of years. Any such phase-in shall allow the electrical corporation to recover the revenue which would have been allowed in the absence of a phase-in and shall make a just and reasonable adjustment thereto to reflect the fact that recovery of a part of such revenue is deferred to future years. In order to implement the phase-in, the commission may, in its discretion, approve tariff schedules which will take effect from time to time after the phase-in is initially approved.

Courts have stated that when a statute mentions something specifically, it in turn implies the exclusion of something else. *Harrison v. MFA Mutual Insurance Corporation*, 607 S.W.2d 137, 146 (Mo. banc 1980); *see also Bridges v. Van Enterprises*, 992 S.W.2d 322, 325 (Mo. App. SD. 1999) (Citing *Brown v. Morris*, 290 S.W.2d 160 (Mo Banc 1956)). Section 393.155.1, RSMo does not mention water, gas, or sewer utilities.

Therefore, it appears that the Commission does not have authority to require a phase-in of rates due to an unusually large increase in a water company's rate base.

WHEREFORE, Hillcrest respectfully requests that the Commission consider this Initial Brief and, thereafter, issue such order as it shall find to be reasonable and just.

Respectfully submitted,



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CERTIFICATE OF SERVICE

The undersigned certifies that a true and correct copy of the foregoing document was sent by electronic mail on June 3, 2016, to counsel for the parties to Case No. WR-2016-0064.

