

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

In the Matter of the Joint Application of)
Stoddard County Sewer Company, Inc., R.D.)
Sewer Co., L.L.C. and the Staff of the)
Missouri Public Service Commission for an)
Order Authorizing Stoddard County Sewer Co.,)
Inc. to Transfer its Assets to R.D. Sewer Co.,)
L.L.C., and for an Interim Rate Increase.)

Case No. SO-2008-0289

**POST-HEARING BRIEF OF THE
OFFICE OF THE PUBLIC COUNSEL**

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POST-HEARING BRIEF OF THE OFFICE OF THE PUBLIC COUNSEL

COMES NOW the Office of the Public Counsel (Public Counsel) and states for its Post-Hearing Brief as follows:

A. Is the proposed transfer of assets detrimental to the public?

Overall, the evidence indicates that the proposed transfer of Stoddard County Sewer Co., Inc. (Stoddard County) assets to R.D. Sewer Co., L.L.C. (R.D. Sewer) is not detrimental to the public. However, there is evidence of multiple encumbrances in the form of security interests which have been placed on the Stoddard County assets. (Exhibits 6 & 7; Tr. 152 L. 21-25; Tr. 153 L. 1-6 & 19-22; Tr. 168 L. 4-7; Tr. 181 L. 14-18) While some encumbrances may be known, there is a possibility that other encumbrances may exist which are at this time unknown. These encumbrances may not have been for the benefit of the customers and the cloud of encumbrances, known and unknown, is a detriment to the public.

A separate issue in this case is whether any and all purported transfers of any security interest in the assets described in Paragraphs 42 and 43 of the Application in this case are void. As long as the Commission makes a determination that any and all, known or unknown, purported transfers of any security interest in the assets described in Paragraphs 42 and 43 of the

Application in this case are void, the transfer of the Stoddard County assets to R.D. Sewer would not be detrimental to the public.

B. Did Stoddard County or any other entity, at any time since Stoddard County acquired the real and personal assets described in Paragraphs 42 and 43 of the Application in this case, secure from the Commission an order authorizing it to sell, assign, lease, transfer, mortgage, or otherwise dispose of or encumber any of the assets that are described in Paragraphs 42 and 43 of the Application in this case?

The testimony of Missouri Public Service Commission Staff (Staff) witness James A. Merciel, Jr. indicates there is no evidence that Stoddard County or any other entity secured from the Missouri Public Service Commission (Commission) an order authorizing it to sell, assign, lease, transfer, mortgage, or otherwise dispose of or encumber any of the assets that are described in Paragraphs 42 and 43 of the Application in this case. (Tr. 181 L. 19-24)

Therefore, the Commission should make a determination that neither Stoddard County, nor any other entity, at any time since Stoddard County acquired the real and personal assets described in Paragraphs 42 and 43 of the Application in this case, secured from the Commission an order authorizing it to sell, assign, lease, transfer, mortgage, or otherwise dispose of or encumber any of the assets that are described in Paragraphs 42 and 43 of the Application in this case.

C. Are any and all purported transfers of any security interest in the assets described in Paragraphs 42 and 43 of the Application in this case therefore void?

RSMo §393.190.1 (2000) states that the transfer of a security interest in a public utility's assets without the prior approval of the Commission is void. Given that there is no evidence that Stoddard County or any other entity secured an order from the Commission authorizing it to sell,

assign, lease, transfer, mortgage, or otherwise dispose of or encumber any of the assets described in Paragraphs 42 and 43 of the Application in this case, all of the purported transfers of any security interest in those assets are void pursuant to the provisions of § 393.190.1, RSMo 2000.

As stated above, while some encumbrances may be known, there is a possibility that encumbrances may exist which are at this time unknown. There is a concern that these encumbrances may not have been for the benefit of the customers and the cloud of encumbrances, known and unknown, is a detriment to the public.

Therefore, the Commission should make a determination that any and all, known or unknown, purported transfers of any security interest in the assets described in Paragraphs 42 and 43 of the Application in this case are void.

D. Should the Commission approve an interim rate increase for the customers who are now served by Stoddard County?

Stoddard County, R.D. Sewer and Staff requested an interim rate increase in this case. In his opening statement, the Attorney for Staff stated that R.D. Sewer is willing to make the interim rate increase subject to refund based upon an audit and a subsequent rate case. (Tr. 30 L. 3-6) The Attorney for Staff also stated that R.D. Sewer is willing to request a rate increase within thirty days after the effective date of the Order in this case and will prosecute that case to conclusion regardless of whether it results in an increase or a decrease in the rates that it would be able to charge and that the interim rate would be subject to refund based upon that rate increase case. (Tr. 30 L. 7-13)

The Commission has the authority to grant emergency interim rate increases which are requested by a regulated utility and also to order emergency interim rate increases it deems necessary after investigation or hearing. The Commission in previous cases has determined an

interim rate increase is appropriate if (1) the evidence shows the utility is operating at a deficit and (2) to disallow the interim rate relief would result in damage to the company's financial integrity and ability to render safe and adequate service.¹

Public Counsel witness Ted Robertson testified that the revenues are meeting the current operating costs of the utility, with the exception being that Mr. Owens is not receiving a reasonable salary as operator of the utility. (Tr. 232 L. 23-25; Tr. 233 L. 1-2) Therefore, Public Counsel is not opposed to an interim rate increase as long as it is subject to refund and in a reasonable amount. (Tr. 31 L. 1-3)

Given that all the parties have agreed on this issue, the Commission should approve a reasonable interim rate increase for the customers that are now served by Stoddard County. Additionally, the Commission should condition its approval on R.D. Sewer's agreements to request a rate increase within thirty days after the effective date of the Order in this case, to prosecute that case to conclusion regardless of whether it results in an increase or a decrease in the rates that it would be able to charge, and that the interim rate would be subject to refund based upon that rate increase case.

E. If the Commission determines that a rate increase for the customers who are now served by Stoddard County should be approved, how much should the rate increase be?

Public Counsel, in its opening statement, indicated that it is not opposed to an interim rate increase, as long as it is subject to refund and in a reasonable amount. (Tr. 31 L. 1-3) Any rate increase approved by the Commission in this case must be an interim rate increase in an amount

¹ *In the matter of Terre Du Lac Utilities Corporation*, 25 Mo. P.S.C (N.S.) 327 (1982)

sufficient to allow the utility to operate without a deficit so as not to damage the company's financial integrity and its ability to render safe and adequate service.²

But, any interim rate increase must also be reasonable for the customers of the utility. It may be tempting to say that any overpayment by the customers will be refunded so there is no harm in having an interim rate that turns out to be too high. But in the everyday world of a small utility, getting a customer a refund is often easier said than done. Even when rates are subject to refund, it is the customers who bear the risk that their money may not actually be returned. (Tr. 280 L. 22-25; Tr. 281 L. 1-19) When an interim rate is set too high, customers are not provided any interest from the utility for that money's use, so those customers lose the value and use of their own money during the timeframe the interim rate is in place. (Tr. 281 L. 20-25; Tr. 282 L. 1-4) Therefore, it is imperative that the interim rate increase be in a reasonable amount which reflects the current cost structure of the company as closely as possible.

Commission's Witnesses' Proposals Are Not Reasonable

The Commission itself called its own witnesses, Mr. Rodger Williams, P.E., of Smith & Co. Engineers, and Mr. Randall R. Shepard, CPA, of The Bonadio Group, to provide factual evidence in this case. These witnesses do not meet the standards set forth in RSMo §490.065 (2000), and the related case law under which expert testimony is admissible as competent opinion evidence. The evidentiary record shows that the Commission's witnesses were not qualified as experts by education, training or experience. (Tr. 34 L. 7-25; Tr. 35 L. 1-22; Tr. 93 L. 6-25; Tr. 94 L. 1-4) In fact, Mr. Shepard testified that he did not believe his company was hired by the Commission to be a regulated utility ratemaking expert. (Tr. 35 L. 16-21) The Commission's fact-witnesses know nothing about regulatory ratemaking or how utilities' cost

² *Id.*

structures are determined. (Tr. 230 L. 1-6) Therefore, the proposals of these witnesses have no evidentiary foundation and no probative value.

The Commission's witnesses, Mr. Rodger Williams, P.E., of Smith & Co. Engineers, and Mr. Randall R. Shepard, CPA, of The Bonadio Group, were hired by the Commission to provide an independent, neutral review of the cost structure of the utility. The Bonadio Group did not perform an audit; it performed only a limited review of the utility. (Tr. 52 L. 23-25; Tr. 53 L. 1-22) The Bonadio Group's recommendations were not independent or neutral because for many of the cost items, the numbers came from Staff, the utility and even from Smith & Co. Engineers through verbal statements and were just accepted at face value without any independent review. (Tr. 54 L. 2 through Tr. 79 L. 24; Tr. 101 L. 13-25; Tr. 102 L. 1-25; Tr. 103 L. 1-25; Tr. 104 L. 1-5; Tr. 279 L. 3-10) The information relied upon by the Commission's fact-witnesses was not verified for accuracy or reasonableness nor was it even compared to other utilities operating in this state. (Tr. 224 L. 25; Tr. 225 L. 1-5) Even though Public Counsel is also a party to this case, Public Counsel was not contacted regarding what it believed to be the reasonable costs to be. (Tr. 54 L. 2 through Tr. 79 L. 24; Tr. 101 L. 13-25; Tr. 102 L. 1-25; Tr. 103 L. 1-25; Tr. 104 L. 1-5; Tr. 279 L. 3-10)

It is unreasonable to consider or rely on the proposals of Smith & Co. Engineers and The Bonadio Group as factual evidence in this case because they are not based on the testimony of proper experts in Missouri public utility ratemaking. In addition, the evidence shows that these fact-witnesses could not, and did not, offer an unbiased, third-party determination of reasonable public utility rates. This is evidenced by the fact that the Commission's witnesses did not conduct any independent investigation or verification of data provided to them by Staff and the utility, and they lack expertise, experience and education in public utility ratemaking.

The testimony, exhibits and reports of the Commission's witnesses are not competent testimony because the witnesses are not qualified experts in utility operation and ratemaking. Their testimony, exhibits and reports constitute hearsay and are not subject to admission as the basis of expert testimony, in that the witnesses cannot vouch for the accuracy of the data provided in the reports and cannot address issues and topics beyond the scope of the application and the issues contested by the parties. These witnesses are not qualified to render an opinion on the purported subject matter as illustrated by their reports.

The testimony, reports and exhibits of Commission witnesses Mr. Rodger Williams, P.E., of Smith & Co. Engineers, and Mr. Randall R. Shepard, CPA, of The Bonadio Group, are also prejudicial, irrelevant and lacking in probative value in that they do not consist of competent and substantial evidence brought by a party to the case. The Commission cannot act as both party and adjudicator. It is unreasonable to rely on the Commission's own fact-witnesses for a determination of reasonable rates in this case. This mixing of roles as judge and party is inconsistent with the high standard that judicial officers must clearly preserve and protect the impartiality of the tribunal and the public's view of that impartial role. When the Commission comes off the bench to offer its own fact-witnesses like the other parties, the appearance of impartiality is diminished, if not destroyed. The Commission must not only be free of any partiality or interest in the matter to be considered by them, but must avoid even the appearance of a lack of impartiality.

Therefore the Commission should not rely on the testimony of the Commission's own outside witnesses, Mr. Rodger Williams, P.E., of Smith & Co. Engineers, and Mr. Randall R. Shepard, CPA, of The Bonadio Group to set a reasonable interim rate increase for R.D. Sewer.

Staff 2002 Audit Is Not Reasonable

Stoddard County, R.D. Sewer and Staff requested an interim rate increase of approximately \$23,000 per year based upon the preliminary findings of an audit performed in a 2002 informal rate case which was subsequently dismissed.

Exhibit 10 was used as evidence of the 2002 audit and as justification for the proposal that the 2002 audit should be applied to this case. Exhibit 10 is just a collection of rate design work papers which were never submitted for verification or filed in the 2002 rate case because the rate case was ultimately withdrawn. (Tr. 170 L. 20-25; Tr. 171 L. 1 & 14-21) The employee who apparently prepared Exhibit 10 no longer works for the Staff of the Commission. (Tr. 170 L. 23-25; Tr. 171 L. 1-10; Tr. 172 L. 6-11) The auditor on the 2002 case apparently also no longer works for the Staff of the Commission. (Tr. 185 L. 2-8) The auditor's work, at least in part, was based on costs that were even older than 2002, so the 2002 audit as compared to today, is based on numbers that are well in excess of six years old and may be as much as eight years old. (Tr. 184 L. 9-24) The 2002 audit does not reflect any costs pertaining to R.D. Sewer who took over operating Stoddard County in January 2002. (Tr. 110 L. 1-2; Tr. 185 L. 9-15) Even Staff's own witness James A. Merciel, Jr. stated that the 2002 audit is not accurate due to changes such as investment, depreciation, operations and even the operator. (Tr. 186 L. 9-19)

The use of the Staff's 2002 audit is not reasonable because it reflects only the beginning of the audit procedure in that the 2002 audit was never finalized nor validated, the corresponding rate case request case was dismissed, the Staff auditing personnel who worked on the audit are no longer with Staff and there exists only extremely limited workpapers based on data that is approximately eight years old and which does not reflect the current operation of the system.

Therefore, the Commission should not rely on the Staff's 2002 audit to set a reasonable interim rate increase for R.D. Sewer.

Public Counsel Witness Ted Robertson's Proposal Is Reasonable

The use of Public Counsel witness Ted Robertson's proposal is reasonable because it is based on a current review of the utility's operations and costs.

Public Counsel witness Ted Robertson developed a cost structure under a limited review scenario which was reflected in Exhibit 13. (Tr. 209 L. 10-11) This cost structure was developed based on Mr. Robertson's knowledge of small rate case procedures, recent Missouri Public Service Commission cases and the 2007 Annual Report filed for Stoddard County. (Tr. 211 L. 10-12) Based on his limited review, Mr. Robertson testified that a reasonable interim rate would be somewhere in the range of \$8,000 to \$10,000 per year, with the caveat that R.D. Sewer comes in under the small rate case procedure and has an audit relatively soon so a more accurate determination of what the actual cost structure can be made. (Tr. 214 L. 4-13; Tr. 230 L. 7-9)

Mr. Robertson testified that the revenues are meeting the current operating costs of the utility, with the exception being that Mr. Owens is not receiving a reasonable salary as operator of the utility. (Tr. 232 L. 23-25; Tr. 233 L. 1-2) Current rates do include a salary for the operator, but that salary amount was probably built into rates in 1979 and is not relevant today. (Tr. 203 L. 25; Tr. 204 L. 1-3; Tr. 213 L. 14-19) Mr. Robertson testified that the company is incurring a deficit of approximately \$8,000 per year, mainly due to the addition of a salary for Mr. Owens. (Tr. 212 L. 13-19) Otherwise, the rest of the operating costs of the company are being met by current revenues. (Tr. 212 L. 20-24)

The biggest difference between The Bonadio Group's proposal and the proposal of Public Counsel witness Ted Robertson is in the areas of plant, depreciation and most of the labor and

repair costs. (Tr. 211 L. 24-25) Mr. Owens has no investment in the company, so he should not earn a return on the plant and should not earn depreciation on that plant either. (Tr. 219 L. 25; Tr. 220 L. 1-3) Even though the Commission does not allow a return on plant when the company has no investment in that plant, the current rates being collected by Mr. Owens most likely include a return on plant. (Tr. 203 L. 20-24; Tr. 204 L. 7-9) The current rates also include depreciation on the plant in which Mr. Owens has no investment. (Tr. 204 L. 4-6) Mr. Owens testified that he owed money to Maco for the replacement of equipment, but none of this loan from Maco has been paid. (Tr. 135 L. 1-7) Without support for the payment of this loan, those costs cannot reasonably be included in rates.

Public Counsel put together a limited review to say what the interim rate increase should be, which is about one-third of what Staff, Stoddard County and R.D. Sewer has requested. Public Counsel's number is based on more current information, particularly the company's own 2007 Annual Report, whereas Staff, Stoddard County and R.D. Sewer is basing their proposal on preliminary audit numbers that could be as old as 1999 and which far exceeds the zone of reasonableness for the cost structure of this company. (Tr. 227 L. 4-11)

Therefore, the Commission should rely on the testimony of Public Counsel witness Ted Robertson to set a reasonable interim rate increase for R.D. Sewer, which should be somewhere in the \$8,000 to \$10,000 per year range. Additionally, the Commission should condition its approval on R.D. Sewer's agreements to request a rate increase within thirty days after the effective date of the Order in this case, to prosecute that case to conclusion regardless of whether it results in an increase or a decrease in the rates that it would be able to charge, and that the interim rate would be subject to refund based upon that rate increase case.

F. If the Commission determines that a rate increase for the customers who are now served by Stoddard County should be approved, should the Commission make the increased revenues subject to refund?

All parties to this case are in agreement that, if the Commission determines that a rate increase should be approved, the Commission should make the increased revenues subject to refund.

Public Counsel in its opening statement indicated that it is not opposed to an interim rate increase, as long as it is subject to refund and in a reasonable amount. (Tr. 31 L. 1-3) In his opening statement, the Attorney for Staff stated that R.D. Sewer is willing to make the interim rate increase subject to refund based upon an audit and a subsequent rate case. (Tr. 30 L. 3-6) The Attorney for applicants Stoddard County and R.D. Sewer also stated in his opening statement that Mr. Owens does not object to a provision for a refund of the interim rate. (Tr. 23 L. 11)

Given that all the parties have agreed on this issue, if the Commission determines that a rate increase should be approved, the Commission should make the increased revenues subject to refund. Additionally, the Commission should condition its approval on R.D. Sewer's agreements to request a rate increase within thirty days after the effective date of the Order in this case and to prosecute that case to conclusion regardless of whether it results in an increase or a decrease in the rates that it would be able to charge.

G. Is the utility providing safe and adequate service to its customers?

This issue was added by the Commission in its August 1, 2008 Order Adopting List of Issues, Order of Opening Statements, List and Order of Witnesses and Order of Cross-

Examination, and Notice Advising Parties of Witnesses Regarding How to Participate in the Evidentiary Hearing by Phone.

Evidence and testimony has shown that the sewer system is currently in violation of Missouri Department of Natural Resources (MDNR) regulations and is in negotiations with MDNR and the Attorney General's Office on a compliance schedule. (Tr. 138 L. 24-25; Tr. 139 L. 1-4; Tr. 151 L. 5-25; Tr. 152 L. 1-20; Tr. 155 L. 7-12; Tr. 279 L. 11-24) A system that is in violation of the State's environmental regulations and has been referred to the Attorney General's Office for enforcement is not providing safe and adequate service to its customers.

Therefore, the Commission may make a determination that Stoddard County is not providing safe and adequate sewer service to its customers.

H. If the utility is not providing safe and adequate service to its customers, should the Commission issue an order for General Counsel to go to Circuit Court to seek penalties?

This issue was also added by the Commission in its August 1, 2008 Order. At this time, no party to this case is requesting that the Commission issue an order for General Counsel to go to Circuit Court to seek penalties and no statements regarding the parties' position on this issue in the future have been made.

Therefore, the Commission should not issue an order for General Counsel to go to Circuit Court to seek penalties at this time.

I. Public Counsel's Motion to Dismiss.

As an Officer of the Court, it is Public Counsel's duty to inform the Commission of the possibility that the Commission has no jurisdiction to hear this case or to approve the transfer of the assets of Stoddard County to R.D. Sewer.

As Public Counsel stated in its Motion to Dismiss, it was recently determined that a closer reading of RSMo §393.190 (2000) reveals that §393.190.2 does have a requirement for Commission approval of the transfer of stock. According to §393.190.3, a transfer of stock in violation of any provision of that chapter shall be void and of no effect.

As Mrs. Bien’s transfer of all of the stock of Stoddard County was not to a “sewer corporation,” Commission approval was required per §393.190.2. Even though it is classified as a limited liability company (LLC), R.D. Sewer was formed specifically to take the stock of Stoddard County. (Tr. 154 L. 25; Tr. 155 L. 1-2) Commission approval was not received for the transfer of all of the stock of Stoddard County from Ms. Bien to R.D. Sewer. (Tr. 155 L. 3-6) Therefore, the transfer was in violation of §393.190.2 and is void per §393.190.3.

Legally, Mrs. Bien is the owner of the stock in Stoddard County and as such, she is a necessary party in any application regarding the transfer of Stoddard County’s assets. However, Mrs. Bien is not a party to this case. The Commission has no jurisdiction to approve the transfer of assets of Stoddard County without the presence of the owner of the Stoddard County stock.

Respectfully submitted,

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/s/ Christina L. Baker

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CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing have been mailed, emailed or hand-delivered to the following this 18th day of September 2008:

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