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October 24, 2003

**FILED**

OCT 24 2003

Missouri Public  
Service Commission

Mr. Dale Hardy Roberts  
Secretary/Chief Regulatory Law Judge  
Missouri Public Service Commission  
P.O. Box 360  
Jefferson City, Missouri 65102

**RE: Missouri-American Water Company and Warren County Water & Sewer Company  
Case No. WM-2004-0122**

Dear Mr. Roberts:

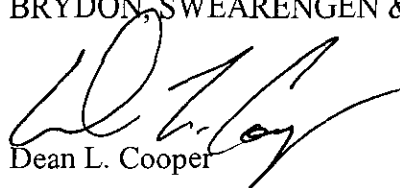
Enclosed for filing in the above-referenced matter are the original and eight (8) copies of Missouri-American Water Company's Response to Staff Recommendation. A copy of the foregoing document has been hand-delivered or mailed this date to all parties of record.

If you have any questions concerning this matter, please do not hesitate to contact me. Thank you for your attention to this matter.

Sincerely,

BRYDON, SWEARENGEN & ENGLAND P.C.

By:

  
Dean L. Cooper

DLC/jar  
Enclosures  
cc: Keith Krueger  
Ruth O'Neill  
Paul S. DeFord

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

**FILED**  
OCT 24 2003

Missouri Public  
Service Commission

In the Matter of the Joint Application of )  
Missouri-American Water Company and Warren )  
County Water & Sewer Company for Authority )  
for Missouri-American Water Company to )  
Acquire Certain Assets of Warren County Water )  
& Sewer Company and, in Connection Therewith, )  
Certain Other Related Transactions. )

Case No. WM-2004-0122

**RESPONSE TO STAFF RECOMMENDATION**

COMES NOW Missouri-American Water Company ("MAWC" or the "Company"), in accordance with the Missouri Public Service Commission's ("Commission") Order Granting Motion for Expedited Treatment and Extending Time for Filing, and, states the following in response to the Commission Staff's ("Staff") Recommendation Regarding Joint Application for Authority for Missouri-American Water Company to Acquire Assets of Warren County Water & Sewer Company ("Staff Recommendation"):

**SUMMARY**

MAWC responds to the Staff Recommendation. MAWC first provides commitment as to improvements it will make to the subject system, if the requests contained in the Joint Application are granted. In response to the Staff's suggestion that the Commission deny MAWC's request that the subject assets be valued at the purchase price for ratemaking purposes, MAWC points out that various factors cited by the Staff leave uncertainty as to the original cost of the assets and explains why the circumstances in this case warrant the treatment request by MAWC. MAWC further expresses its disappointment with the Staff's preference that the assets be purchased by a public water supply district and describes what it believes to be inconsistencies in the Staff's reasoning. Lastly, MAWC discusses the consequences of the Staff Recommendation and the issue of

outstanding Commission assessments.

### **BACKGROUND**

1. On September 4, 2003, MAWC and Warren County Water & Sewer Company (“Warren County”) filed with the Commission a Joint Application for authority for MAWC to acquire certain assets of Warren County.

2. The Joint Application includes two specific requests in regard to the Commission approval. First, MAWC has asked that the Warren County rates existing at the time MAWC acquires the assets will continue in effect until the operation of law date associated with MAWC’s next general rate filing after May 1, 2004, and/or thereafter, until changed as a result of a Commission Order. Second, MAWC has asked that the Commission find that the assets that are the subject of the Joint Application will be valued for ratemaking purposes at the purchase price contained in the Agreement.

3. On October 17, 2003, the Staff filed its recommendation wherein, among other things, the Staff recommended:

- A. That the proposed rate moratorium be approved;
- B. That the proposal in regard to the value of the property for ratemaking purposes be denied; and,
- C. That any approval be conditioned on the receipt of a commitment from MAWC to undertake certain system improvements.

### **COMMITMENT**

4. MAWC disagrees with the Staff Recommendation on several levels in regard to the value of the property for ratemaking purposes. However, MAWC will make the following

commitment in response to the Staff Recommendation. If the Commission order in this case approves the moratorium proposed by MAWC and finds that the value of the property for ratemaking treatment will be equal to the purchase price, MAWC will commit to make the system improvements identified on Appendix A, attached hereto.

5. Customer support for a completion of this transaction has been provided to the Commission previously. The correspondence and petition attached hereto as Appendix B was previously provided to the Commission by the "Property Owners of Incline Village." The letter provides support for this transaction on behalf of these property owners and is provided for the Commission's reference.

#### **VALUE OF PROPERTY FOR RATEMAKING PURPOSES**

6. Staff indicates its view that the Warren County rate base, for ratemaking purposes is "substantially less than the purchase price set forth in the . . . contract for sale." Staff, thereafter, for an assortment of reasons, opposes MAWC's request that the purchase price represent the value of the property for ratemaking purposes.

7. MAWC does not believe that Staff's stated reasons lead to the conclusion that MAWC's request should be denied. In fact, some of those same reasons support MAWC's requested ratemaking treatment. For example, Staff states as follows:

The major contributing factor to the Staff's position regarding [Warren County's] ratemaking rate base is that much of the plant that [Warren County] uses to provide its water and sewer services is plant that was originally installed by the development company that developed the main part of [Warren County's] service area (a development known as Incline Village), and which was conveyed to a water utility and a sewer utility that were formed by the developer for the purposes of ownership and operation. Recovery of this plant investment was subsequently realized through the sale of lots and/or homes in the development. As a result, this plant is considered contributed plant and has no current value for ratemaking purposes, which is also the

approach taken with regard to this plant when the rates were set for the original utility companies. Other problems in this regard are that the development company went bankrupt, and that the developer's utility companies' assets were subject to a sale forced by Warren County for past due property taxes and were obtained by the owner of [Warren County]. *As a result of these two situations, there are essentially no good historical records regarding the cost of the facilities that the development company originally installed.*

(Emphasis added). The fact that Staff admits that “there are essentially no good historical records regarding the cost of the facilities” certainly raises some doubt as to the approximate rate base number identified by Staff. Additionally, because of the lack of records Staff has made a great leap in assuming that the original property meets the definition of “contributed property.” Again, this is very suspect because of Staff’s explanation that “there are essentially no good historical records.” It appears to be unknown what exactly transpired in regard to the original construction of the system, as well as in certain follow on transactions.

8. This lack of records leads one to the conclusion that the “acquisition premium” the Staff focuses on may not even exist. It is this same lack of certainty and lack of records that drives MAWC to request up front that the Commission find that purchase price be used as the value of the property for ratemaking purposes. As the Commission is aware, it previously found as follows in regard to Warren County in Case No. WC-2002-155: “the Conclusion that the Company is unable or unwilling to provide safe and adequate service is inescapable” (Report and Order at p. 8). The Commission’s General Counsel later filed a Petition for Receivership in the Circuit Court of Warren County, Missouri. It was only after these actions were taken that MAWC entered into a contract to purchase certain Warren County assets.

9. Obviously, MAWC did not create the lack of good historical records referred to by the Staff. Accordingly, MAWC should not be forced to bear the risk of a lack of such records. If

the Commission really desires to place this burden on a purchasing utility in the situation at hand, MAWC believes there will rarely be a time when a regulated company will be in a position to purchase a small, troubled water or sewer system such as Warren County.

10. Staff further indicates the following concern about a possible acquisition premium:

Approval of MAWC's request for rate base recognition of the purchase price would thus be approval of the recovery of an acquisition premium, which would not be consistent with historical Commission actions regarding this matter. While the Staff certainly agrees that the sale of [Warren County's] water and sewer systems is necessary, the Staff does not believe that [Warren County's] current situation necessitates or justifies the recovery of an acquisition premium by a Commission-regulated utility. Additionally, because of the magnitude of the acquisition premium in this situation, the Staff believes that recovery of the acquisition premium by a Commission-regulated utility could result in rates that would be detrimental to the ratepayers in [Warren County's] service area.

As an initial matter, for the reasons stated above, it is unclear what, if any, premium would be associated with the proposed purchase.

11. However, even if a premium would exist, the Staff's reasoning that "recovery of the acquisition premium by a Commission-regulated utility could result in rates that would be detrimental to the ratepayers in [Warren County's] service area" is flawed. MAWC believes that recovery of an acquisition premium would only be authorized by the Commission in a situation where customer benefits and/or savings justified such recovery. One of the benefits here is that the Commission has found that Warren County is not providing safe and adequate service. MAWC, on the other hand, has a long history of providing safe and adequate service. Recovery of any premium would, by definition, not be detrimental to the ratepayer in this circumstance.

12. MAWC asks the Commission to remember that through its proposal, MAWC is merely looking for a fair evaluation of the property to be purchased. As Staff indicates, "MAWC

would be purchasing a great deal of plant that is used to provide service to customers.” The Staff seeks to use a rate base estimate (“at maximum approximately \$50,000”) that is so low that the system could not possibly be operated profitably. Fifty Thousand Dollars (\$50,000) of rate base, utilizing a 60/40 equity ratio and a twelve percent (12%) return on equity, results in a weighted cost of capital of 4.8%. In other words, if the Staff’s approach were accepted, the Commission would presumably design the rates for this system to produce an *annual operating profit of Two Thousand Four Hundred Dollars (\$2,400)*. A system with 393 water customers and 374 sewer customers cannot be operated profitably for that return and certainly no level of future investment could be agreed to with that starting rate base amount.

13. The Staff’s approach ignores the best evidence of the value of these assets. St. Charles Public Water Supply District No. 2 (the “Water District”) made an offer for the Warren County assets that was of a similar magnitude as the purchase price contained in MAWC’s purchase agreement. Thus, two parties, in arms length negotiations, have come to very nearly the same value for the subject properties.

#### **SUPPORT FOR THE WATER DISTRICT**

14. MAWC is also disappointed that the Staff has taken this opportunity to choose sides and support the Water District’s efforts to purchase the Warren County assets. The Staff’s approach to the situation implies that Missouri customers are better served by an entity that is not regulated by this Commission. In fact, the favoring of the Water District creates real doubt as to whether the Staff supports the private ownership/regulatory model. This is because the concern for MAWC customers expressed in the Staff’s “not detrimental” analysis seems to vanish when its eye is turned toward the Water District.

15. It is particularly disturbing to read one of the reasons that Staff supports the Water District's purchase of the assets. Staff states that it "is also aware that the District's customer rates are set on district-wide basis, and thus that the system improvements would not be borne solely by [Warren County's] customer base, but would be absorbed by the District's entire customer base." What the Staff is saying, of course, is that the WATER DISTRICT HAS SINGLE TARIFF PRICING and that Staff believes that this would be a benefit to the Warren County customers. Hopefully, the Commission will not rely on the Water District's use of single tariff pricing as a reason to deny this aspect of MAWC's application. As a reminder, it was the Commission's decision in Case No. WR-2000-281 that forced MAWC into district specific pricing, based in great part on Staff's opposition to single tariff pricing. Furthermore, there is no guarantee what pricing structure will be used by the Water District in the future in regard to the Warren County water and sewer customers. Because it is not regulated, the Water District has no impediment to using, or not using, single tariff pricing as to its water rates. In fact, MAWC understands that on the sewer side of the business, the Water District uses multiple sewer rates. The Water District may price its water and sewer services in a variety of ways to ensure that it receives its return. Also, if the Commission does find this "district wide pricing" to be advantageous, MAWC is not opposed to treating the Warren County customers as a part of either MAWC's St. Charles or St. Louis operating districts, as directed by the Commission.

16. As to the lack of concern about non-regulated customers, the Commission again must be mindful of the fact that if there is a premium associated with this transaction, it is there for the Water District's purchase, as well as MAWC's. As stated above, the Water District has made an offer that is similar to that made by MAWC. Whether MAWC or the Water District purchases



Warren County, the purchase price will eventually be recovered. In fact, in the case of the Water District, if there is a premium, it must be recovered from the Water District's customers. It is curious that the potential for this recovery is deemed to be detrimental if MAWC purchases the assets, but apparently not detrimental if the Water District makes the purchase.

### **CONSEQUENCE OF THE STAFF RECOMMENDATION**

17. The Staff's simplistic statement of the Commission's options and the potential consequence of a denial of MAWC's request as to the ratemaking treatment is misleading. The Staff states, in part, that "the Commission can grant the relief requested in the prayer clause of the Joint Application, approve the request for a rate moratorium described in Paragraph 13 of the Joint Application, and deny the request for special ratemaking treatment that is described in Paragraph 16 of the Joint Application."

18. MAWC has asked the Commission as a part of the application for a decision as to the value of the subject property for ratemaking purposes. Case law cited by the Staff, *State ex rel. AG Processing, Inc. v. Public Service Commission* (Mo.App. W.D., opinion issued April 22, 2003) currently indicates that this is an appropriate, if not required, question to be addressed at the acquisition case stage. The Commission may not rule against MAWC's request without the provision of due process and hearing. Thus, while the Commission might eventually issue an order as described by the Staff, the Commission cannot do so in response to the pleadings before it at this point in time.

### **ASSESSMENTS**

19. The "Wherefore" clause of the Staff's Recommendation states in part that the Commission should "condition the sale of Warren County's assets on the payment of Warren

County's past due assessments." It is unclear from this statement what entity the Staff expects to pay these assessments. As indicated in the Joint Application, MAWC is proposing to purchase certain assets, not the Warren County corporate body. MAWC believes whatever assessments are outstanding is between Warren County and the Commission. The Staff's Memorandum attached to its Recommendation states more specifically that "the approval of the sale of [Warren County's] assets on the payment of [Warren County's] past due assessments by [Warren County] from the proceeds of the sale." The statement contained in the Staff's Memorandum is a more palatable and appropriate treatment of the assessment than the statement contained in the Staff's Recommendation.

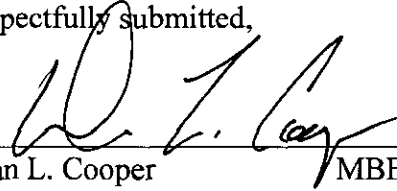
### **CONCLUSION**

WHEREFORE, MAWC respectfully requests that the Commission issue its order:

- (A) authorizing MAWC to acquire the assets of Warren County identified in the Joint Application;
- (B) authorizing MAWC to enter into, execute and perform in accordance with the terms described in the Agreement attached to the Joint Application and to take any and all other actions which may be reasonably necessary and incidental to the performance of the acquisition; and,
- (C) granting such other relief as may be deemed necessary and appropriate to accomplish the purposes of the Agreement and the Joint Application and to consummate related transactions in

accordance with the Agreement.

Respectfully submitted,



Dean L. Cooper MBE#36592  
BRYDON, SWEARENGEN & ENGLAND P.C.  
312 E. Capitol Avenue  
P. O. Box 456  
Jefferson City, MO 65102  
(573) 635-7166  
(573) 635-3847 facsimile  
[dcooper@brydonlaw.com](mailto:dcooper@brydonlaw.com)

ATTORNEYS FOR  
MISSOURI-AMERICAN WATER COMPANY

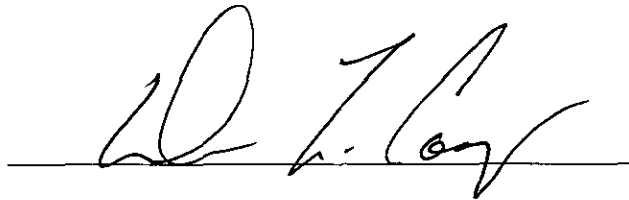
### CERTIFICATE OF SERVICE

The undersigned certifies that a true and correct copy of the foregoing document was hand-delivered, or sent by U.S. Mail, postage prepaid, on October 27, 2003, to the following:

Mr. Keith Krueger  
Office of the General Counsel  
Governor Office Building, 8<sup>th</sup> Floor  
Jefferson City, Mo 65101

Ms. Ruth O'Neill  
Office of the Public Counsel  
Governor Office Building, 6<sup>th</sup> Floor  
Jefferson City, MO 65101

Mr. Paul S. DeFord  
Lathrop & Gage, L.C.  
2345 Grand Boulevard, Suite 2800  
Kansas City, MO 64108



MISSOURI-AMERICAN WATER COMPANY  
WARREN COUNTY WATER & SEWER COMPANY  
CAPITAL IMPROVEMENTS

<u>QUANTITY</u>	<u>DESCRIPTION</u>
<u>SEWER TREATMENT PLANT -</u>	
1 ea.	Sewer Treatment Plant (40K GPD)
<u>SEWER LIFT STATION UPGRADE -</u>	
1 ea.	Sewer Lift Station Upgrade
<u>SEWER SYSTEM STUDY -</u>	
1 ea.	Sewer System Evaluation Survey
<u>WATER STORAGE TANK -</u>	
1 ea.	Water Storage Tank (250K Gallons)
<u>SCADA UPGRADE</u>	
1 ea.	Upgrade Water & Sewer SCADA

Property Owners of Incline Village  
1172 Hillside Drive  
Foristell, MO 63348

October 15, 2003

Secretary, MOPSC  
Post Office Box 360  
Jefferson City, MO 65102

RE: Approval of sale of Warren County Water & Sewer

Dear Sir/Madam:

We are submitting this petition on behalf of property owners at Incline Village who have signed same. These signatures represent approximately 95% of those in attendance at the monthly Board Meeting on October 14, 2003, this was just a spur of the moment opportunity which we availed ourselves of. In order to collect signatures as rapidly as possible to submit same. If necessary we can go door to door and collect pages of signatures. The vast majority of property owners in Incline would like to see an end to this situation. We are asking for priority consideration and expedient action in the approval of the sale of Warren County Water & Sewer to Missouri-American Water Company. The growth of this community has been stalemated by the much publicized situation involving the water & sewer company and its troubles. Missouri-American is willing to come in here and make major investments to improve the water and sewer service not only to our community, but some of the surrounding areas also serviced by Warren County Water & Sewer.

The sooner the sale is approved and completed, the sooner the new owners can begin the improvements, the sooner the building can resume and the sooner the property values can appreciate comparable to the rest of the area. This is an area which is growing rapidly and the property owners are not responsible for the situation that exists, however they are the ones who have been paying for it, with loss of property values, derogatory press, etc. We would like to turn this thing around and with your help by approving the sale as fast as possible, we would halt further decline.

It would seem to us that the sale is quite beneficial to every party, but certainly to no one more than us, the property owners who have been innocent victims of the whole situation.

On behalf of the property owners of Incline Village we wish to thank you for giving this your full attention and consideration.

Respectfully,  
Robyn Flack, Communications Committee Member  
and Fellow Petitioners

cc: Bob LeGrand, Missouri-American Water Company  
Paul Mueller, DNR Warren County

## PETITION

**I, THE UNDERSIGNED, A RESIDENT/LOT OWNER OF INCLINE VILLAGE, HEREBY ASK THE PSC TO EXPEDITE THE COMPLETION OF THE SALE OF THE WARREN COUNTY WATER AND SEWER COMPANY TO MISSOURI-AMERICAN WATER COMPANY:**

NAME	ADDRESS	LOT #
Carolyn Lack	1172 Hillside Dr	148
Debra Palmer	2874 Magnolia	626
Frank N. Scott	1145 Hillside Dr	441
Paul Kunkle	2563 Fairway Dr	381
Sharon E. Bennett	Lot 500	
Erica Bruce Brand	Lot 134	
Paul McJeannot	2392 Village Dr East	73 & 74
Deanne Mura	1002 Sugar Maple Ct	663
Salvatore Pulando	1091 Mulberry	539+540
Shirley Pulando	1091 Mulberry	539+540
Lynn Wald	27400 Ridge Rd	<del>2</del> 530A
Lynn Cisneros	2435 Fairway Dr.	171
Nancy Cisneros	" " "	171
Sharon Ka Buckheit	2540 Walnut Ln.	316 & 317
Ethel M. Melchior	2544 Fairway Dr.	400 & 401
D + L 671	1200 St. ... Pt	219

Richard Shulecky 2544 Fairway Dr. 400-401  
 Tony Okamoto apt 1 Village WA 116  
 Roger Brumby 901 Sweet Gum Ct 618A  
 Jordan Paulsen 901 Sweet Gum Ct 618A  
 Emily Darr 900 Sweet Gum Ct 619A  
 Lane Darr 900 Sweet Gum Ct 619A  
 Denis & Denise Roy 2581 Fairway Dr #377 & 37.  
 Kenneth & Mary Osborne 2612 Cottonwood Ct. 499

# PETITION

**I, THE UNDERSIGNED, A RESIDENT/LOT OWNER OF INCLINE VILLAGE, HEREBY ASK THE PSC TO EXPEDITE THE COMPLETION OF THE SALE OF THE WARREN COUNTY WATER AND SEWER COMPANY TO MISSOURI-AMERICAN WATER COMPANY:**

NAME	ADDRESS	LOT #
<u>Shirley Burnett</u>	<u>1700 N. Dutch Rd.</u>	<u>436</u>
<u>Al Wiley</u>	<u>1018 N. STRINGTOWN</u>	<u>773 + 774</u>
<u>Tom &amp; Betty</u>	<u>17 Tappan Way, St. Charles</u>	<u>180</u>
<u>Diana Jones</u>	<u>14850 Phelps Dr. Bridgeton, MO.</u>	<u>6229623</u>
<u>Pete &amp; Mary</u>	<u>14850 Phelps Dr. Bridgeton, MO.</u>	<u>6229623</u>
<u>Don &amp; Linda</u>	<u>1010 BUTTERNUT CT</u>	<u>756</u>
<u>Tom Wilkinson</u>	<u>1027 SUGAR MAPLE</u>	<u>722</u>
<u>JL Salen</u>	<u>509 W Springdale Gr Prairie TX</u>	<u>665</u>
<u>Patricia Salen</u>	<u>509 W Springdale Gr Prairie TX</u>	<u>665</u>
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____



