

MEMORANDUM

TO: Missouri Public Service Commission Official Case File
Case No. WF-2021-0016, Liberty Utilities (Missouri Water), LLC

FROM: Peter Chari, Senior Regulatory Auditor, Financial Analysis Dept.

/s/ Seoung Joun Won, PhD 03/15/2021
Financial Analysis

/s/ Jamie Myers 03/15/2021
Staff Counsel's Office

SUBJECT: Staff Recommendation concerning the Application of Liberty Utilities (Missouri Water), LLC (“Liberty Water,” “Company,” or “Applicant”), for the authority to issue up to \$18,405,000 of long-term unsecured debt.

DATE: March 15, 2021

1. **Type of Issue:** Unsecured Long-Term Debt
2. **Amount:** Up to \$12,690,000 (“New Note”) and \$5,715,000 (“Refinanced Note”); a total of \$18,405,000.
3. **Rate:** The interest rate for the Refinanced Note is a fixed rate of 2.079%. Interest rate for the New Note is a yield to maturity note rate equal to the yield to maturity of Liberty Utilities Finance GP1’s (“GP1”) next debt placement.
4. **Other Provisions:** The maturity for the Refinanced Note is 10 years. New Note’s maturity will match the maturity on GP1’s next debt issuance.
5. **Proposed Date of Transaction:** The Company is requesting that the financing approval granted by the Commission remain in effect for three years, starting on the effective date of the order in this case.
6. **Statement of Purpose of the Issues:** Liberty Water intends to use the proceeds of the Refinanced Note to refinance the existing \$5,715,000 short-term unsecured debt from its indirect parent company, Liberty Utilities Co. (“LUCo”). Liberty Water will use the proceeds from the New Note to pay for part of the cost of acquisition, control, operation and maintenance of the water and sewer system in Bolivar, Missouri.
7. **From a financial perspective, does Staff deem this Statement of Purpose of the Issue reasonable?** Yes, with conditions imposed.
8. **Type of Transaction:** The total debt proposed in this application will be in the form of affiliate promissory notes payable to LUCo.

** Denotes Confidential Information **

Appendix A

9. **Certified copy of resolution of the directors of applicant, or other legal documents authorizing the issuance of the securities reviewed:** No. Resolutions of the Board of Directors will be late filed.
10. **Pro-forma Balance Sheet and Income Statement reviewed:** Yes
11. **Capital expenditure schedule reviewed:** Yes
12. **Journal entries required to be filed by Liberty Water to allow for the fee schedule to be applied:** No. The New Note is yet to be issued and the fees are unknown at this time. Liberty Water stated that, “Only the proceeds from the New Note, (up to \$12.9 million) will be new funds and subject to the Commission’s fee schedule pursuant to Section 386.300, RSMo.”
13. **Recommendation of the Staff:** Conditional Approval granted pending receipt of definite terms of issuance (see Comments and Recommended Conditions)

COMMENTS:

Liberty Water is a Missouri limited liability company with its principal office located at 2370 High St., Jackson, MO 63755-8365. Liberty Water is owned by Liberty Utilities (sub) Corp., a direct subsidiary of LUCo. Applicant is qualified to conduct business as a public utility in the State of Missouri subject to the jurisdiction of the Commission as provided by law. Liberty Water is engaged, generally, in the business of furnishing water and sewer services, currently serving approximately 8,079 customers, comprised of approximately 7,441 water only, 443 sewer only and 195 water and sewer customers in the State of Missouri.

Liberty Water has filed an Application requesting that the Commission authorize the Company to issue up to \$18,405,000 in aggregate principal amount of long-term affiliate promissory notes through Liberty Utilities Finance GP1, comprised of \$5,715,000 in Refinanced Note and \$12,690,000 in New Note. GP1 is a financing vehicle for LUCo, a wholly-owned financing subsidiary of Algonquin Power and Utilities Corp (“APUC”).

Issuance of Debt. The long-term borrowings will be evidenced by a Promissory Note, payable to LUCo, attached as Appendix 1 to the Company’s Application.

Neither the Refinanced Note nor the New Note will be secured by a mortgage, lien or encumbrance on Liberty Water in the State of Missouri. The cost of the debt financing provided to Liberty Water under the proposed Promissory Notes would not be based on Liberty Water’s stand-alone creditworthiness; rather, it would be based on the creditworthiness of LUCo, which is the guarantor

of the debts held by GP1.¹ GP1's credit worthiness relies on LUCo's consolidated creditworthiness. GP1 pools together the financing requirements for LUCo's utility subsidiaries and then issues an aggregate amount of debt to an investor(s). This results in LUCo's subsidiaries, including Liberty Water, being assigned the same debt cost as originally charged to GP1 by the third-party lenders. GP1 is currently rated BBB and BBB+ by S&P and Fitch Ratings, respectively.

The Refinanced Note has a fixed interest rate of 2.079%, the same interest rate matching the yield on GP1's recent debt issuance.² The New Note will have the same interest rate matching GP1's next debt issuance.³ GP1's 2.079% interest rate compares to interest rates charged on debts issued by comparable utilities, generally, in the same time period. American Water Works (Baa1) issued a \$500 million, 10-year senior note at 2.8%, on April 8, 2020.⁴ Spire Inc. (Baa2) issued, on December 15, 2020, a \$150 million senior note with similar maturity at 2.04%.⁵ To the extent that Liberty Water is charged the same interest rate that is charged to GP1, Staff is of the opinion that Liberty Water's ratepayers are charged competitive and reasonable market rates.

Effect on Credit Quality. As of September 30, 2020, Liberty Water's capital structure is composed of 50.02% (\$5,719,842) equity, 49.98% (\$5,715,000) short-term debt and 0% long-term debt. The proposed financing authority in this Application will immediately change the capital structure to
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_____ **⁶ It is important to note that this change in capital structure does not impact Liberty Water's standalone credit quality, because as Staff already stated, Liberty Water's long-term debts are issued at, and guaranteed by, the parent company, LUCo.

** _____ **⁷ It is important to note that because ** _____ ** financial risk as reflected by the

¹ ** _____ ** (Fitch Ratings Commentary, October 22, 2020 – Liberty Water Response to Staff Data Request (DR) No. 0001).

² Liberty Utility Finance GP1 recently issued a \$600 million, 10-year unsecured Greed Bond note.

³ The yield on GP1's next debt issuance will depend on the capital market conditions prevailing at the time of issuance.

⁴ See Exhibit 1 attached.

⁵ Spire unit sells \$150M of senior notes in private placement | S&P Global Market Intelligence <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/spire-unit-sells-150m-of-senior-notes-in-private-placement-61824641>

⁶ Liberty Water Response to Staff DR No. 0007.

⁷ Response to Staff DR No. 0007.1.

capital structure could be much higher.⁸ Part of the debt, \$5,715,000, proposed in this Application does not increase LUCo's financial risk, because the \$5,719,842 will simply be drawn from GP1's already issued debt.⁹ The other debt, \$12,690,000, proposed in this Application will come from the debt yet to be issued by GP1. Because LUCo's capital structure will not significantly change and that the total, \$18,405,000**

_____, Staff does not think this transaction will have significant impact on LUCo's credit quality.¹⁰

Estimate of Capital Needs. Staff analyzed Liberty Water's financial data and proposed capital projects, to evaluate whether Liberty Water's requested amount of \$18,405,000 is reasonably required over the period of requested authority. Based on Staff's analysis of Liberty Water's financial information, Liberty Water has a total of \$5,715,000 in short-term unsecured debt obtained from its indirect parent company, LUCo. Liberty Water will use the requested \$5,715,000 in Refinanced Note to refinance the short-term unsecured debt. Liberty Water has a projected capital expenditure of \$23,500,000, for the acquisition of water and sewer system in Bolivar, Missouri. Liberty Water will use the requested \$12,690,000 in New Note, to pay, in part, for the acquisition of water and sewer system in Bolivar, Missouri.¹¹ Staff concludes that Liberty Water's requested amount of \$18,405,000 is reasonably required.

OTHER ISSUES:

Staff also emphasizes that although it is recommending approval of this financing transaction, it is in no way recommending Liberty Water's capital structure as the appropriate capital structure for ratemaking purposes. Although this qualification is covered generally in Condition 1 below, it is important to emphasize this specific point.

Staff has verified that the Company has filed its annual report and is not delinquent on any assessment.

RECOMMENDED CONDITIONS:

Staff recommends that the Commission approve the Application submitted by Liberty Water in this case subject to the following conditions:

⁸ Liberty Water Response to Staff DR No. 0001, Fitch Ratings, Rating Action Commentary, page 1.

⁹ The \$5,719,842 will be drawn from Liberty Utility Finance GP1 recently issued \$600 million, 10-year unsecured Greed Bond note.

¹⁰ Currently, LUCo has about **

_____**.

¹¹ The case for the acquisition of the Bolivar water and sewer systems is pending with the Commission (File No. WA-2020-0397).

1. That nothing in the Commission's order shall be considered a finding by the Commission of the value of this transaction for ratemaking purposes, which includes, but is not limited to, the capital structure, and that the Commission reserves the right to consider the ratemaking treatment to be afforded the financing transaction and its impact on cost of capital, in any later proceeding;
2. That the Company shall file with the Commission, all final terms and conditions of the proposed financing, including, but not limited to, the aggregate proceeds received, price information, and estimated expenses;
3. That the Company shall file with the Commission any information concerning communication with credit rating agencies concerning the proposed financing; and
4. That the approval of the issuance of the New Note be subject to Commission approval of Liberty Water's request for a CCN to acquire the Bolivar system, File Nos. WA-2020-0397 and SA-2020-0398.

Senior Debt (MI OFFERING KEY: 1937807; SPCIQ TRANSACTION ID: 662708148)

Overview

Basic Details

Company Name	American Water Capital Corp.
Primary Industry (MI)	Specialty Finance: Commercial Focused
Headquarters	Voorhees, NJ, US
Offering Type	Senior Debt
Status	Completed

Dates

Announcement Date	4/8/2020
Registration Effective Date	4/30/2018
Completion Date	4/8/2020
Shelf Filing Date	5/1/2018

Additional Details

Mandatory Redemption?	Yes
Transaction Feature Type	Domestic Offering Only; Securities Offered by Company

Issue Details

Security Details

Description	2.8% SNR PIDI NTS 01/05/2030 USD (SEC REGD)
ISIN	US03040WAW55
CUSIP	03040WAW5
Issue Currency	USD
Convertible?	No
Call Price	100.00
Call Period	2/1/2030 - 5/1/2030

Valuation Details

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Offer Price (%)	99.5910
Gross Amount Offered (\$000)	500,000
Amount Including Overallotment (\$000)	500,000
Minimum Increments (\$)	1,000

Current Security Ratings

	Current Issuer Ratings
Moody's Corporation	Baa1
Standard & Poor's Financial Services, LLC	A

Underwriting Fees

Gross Spread (%)	0.65
Aggregate Gross Underwriting Spread (\$000)	3,250

Transaction Fees

Administrative Fees

SEC Registration Fee (\$000)	65
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Summary

Transaction Comments

The issuer will pay interest semi-annually in arrears on the notes on May 1 and November 1 of each year, beginning on November 1, 2020. Certain legal matters in connection with the offering will be passed upon for the issuer by Jeffrey M. Taylor, Secretary of AWCC and Chief SEC & Corporate Governance Counsel and Assistant Secretary of the issuer. The yield to maturity on notes is 2.847%.

Use of Proceeds

Debt Repayment, General Corporate Purposes, Working Capital

Deal Advisers

Underwriters

UNDERWRITER	ROLE	SHARES UNDERWRITTEN (ACTUAL)	AMOUNT UNDERWRITTEN (\$000)	UNDERWRITING FEE (\$000)
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UNDERWRITER	ROLE	SHARES UNDERWRITTEN (ACTUAL)	AMOUNT UNDERWRITTEN (\$000)	UNDERWRITING FEE (\$000)
RBC Capital Markets, LLC	Book Manager	NA	100,000	650
BofA Securities, Inc.	Book Manager	NA	92,500	601
Mizuho Securities USA LLC	Book Manager	NA	92,500	601
U.S. Bancorp Investments, Inc.	Book Manager	NA	40,000	260
Wells Fargo Securities, LLC	Book Manager	NA	40,000	NA
J.P. Morgan Securities LLC	Book Manager	NA	25,000	163
MUFG Securities Americas Inc.	Book Manager	NA	25,000	163
PNC Capital Markets LLC	Book Manager	NA	25,000	163
TD Securities (USA) LLC	Book Manager	NA	25,000	163
BNY Mellon Capital Markets, LLC	Co-Manager	NA	8,750	57
Truist Securities, Inc.	Co-Manager	NA	8,750	57
Regions Securities LLC	Co-Manager	NA	7,500	49
Cabrera Capital Markets, LLC	Co-Manager	NA	2,500	16
Goldman Sachs & Co. LLC	Co-Manager	NA	2,500	16
Loop Capital Markets LLC	Co-Manager	NA	2,500	16
Morgan Stanley & Co. LLC	Co-Manager	NA	2,500	16

Other Advisers

Morgan, Lewis & Bockius, LLP

Legal Counsel

Sullivan & Cromwell LLP

Legal Counsel to Underwriters

PricewaterhouseCoopers LLP

Accountant

Related Shelf Registration

TRANSACTION ID	ANNOUNCEMENT DATE	OFFERING TYPE	AMOUNT INCLUDING OVERALLOTMENT (\$000)
SPTRO1035309	5/1/2018	Shelf Registration	NA

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† This number reflects the estimated value of the total new money raised through private placement rounds.