

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

In the Matter of Missouri-American)
Water Company for a Certificate of)
Convenience and Necessity Authorizing)
it to Install, Own, Acquire, Construct,) File No. WA-2021-0376
Operate, Control, Manage and Maintain) SA-2021-0377
a Water System and Sewer System in)
and around the City of Eureka, Missouri.)

MAWC’S RESPONSE TO STAFF RECOMMENDATION

COMES NOW Missouri-American Water Company (MAWC or Missouri-American) by and through the undersigned counsel, and for its *Response to Staff’s Recommendation* states as follows to the Missouri Public Service Commission (“Commission”):

SUMMARY

MAWC is extremely well qualified from a technical and financial perspective to own and operate the water and wastewater assets of Eureka, Missouri, which are located within St. Louis County, Missouri. The voters of Eureka have approved a transaction permitting MAWC to purchase those assets and the City of Eureka has negotiated and entered into an agreement to sell those assets to MAWC. This was the culmination of many years of discussions between MAWC and Eureka, Eureka is the last remaining municipality in St. Louis County that still operates its own water treatment and distribution system and its own wastewater system.

MAWC seeks to establish the rate base of the Eureka assets utilizing Section 393.320, RSMo. MAWC is a “Large Water Utility,” and the Eureka systems are “Small Water Utilities” within the meaning of the statute and an appraisal was performed in accordance with the statute, delivered to Eureka, and taken into account when the voters addressed this question.

In spite of this, the Staff has recommended that the Commission reject MAWC's Application. Staff's Memorandum summarizes by stating ". . . that the transaction as requested by MAWC in its Application, i.e., utilizing the appraisal method contained in [Section] 393.320, RSMo, is not in the public interest." (Staff Memo., p. 21) (emphasis added). Staff's attempt to effectuate a "regulatory veto" of Section 393.320, RSMo, is inappropriate. The Commission should approve MAWC's Application without condition.

BACKGROUND

1. MAWC proposes to purchase substantially all of the water and sewer assets of the currently unregulated system of Eureka, and requests certificates of convenience and necessity ("CCN") for water and wastewater systems for the public in an area in and around the City of Eureka, Missouri. To provide service to the proposed area, MAWC will purchase the water and sewer systems from Eureka, a Fourth-Class City located in St. Louis County.

2. An appraisal of the water and wastewater systems was completed, and the Valuation Report provided to the City of Eureka. On May 19, 2020, the Eureka Board of Aldermen passed Bill No. 2657 and designated it to be Ordinance No. 2543, *An Ordinance Submitting To The Qualified Voters Of The City Of Eureka A Question Concerning The Sale Of City Water and Wastewater Utilities (" Ordinance")*. The *Ordinance* provided notice of an election to be held on August 4, 2020, to vote on (Proposition S), whether the water and wastewater utility owned by the City of Eureka should be sold. The question on the ballot was as follows:

SHALL THE CITY OF EUREKA, MISSOURI BE AUTHORIZED TO SELL ITS WATER AND WASTE WATER (SEWER) UTILITIES TO MISSOURI AMERICAN WATER COMPANY FOR THE SUM OF \$28,000,000.00 (TWENTY-EIGHT MILLION DOLLARS)?

3. There were three virtual Town Hall Meetings to discuss the proposed sale. The Town Hall Meetings were held on July 16, 2020, July 23, 2020, and July 30, 2020. MAWC

representatives attended the virtual Town Hall Meetings and were available to answer any questions. The election was held on August 4, 2020, and a majority of votes cast were in favor of Proposition S. Proposition S garnered 2,289 yes votes (67 percent) to 1,127 no votes (33 percent).

4. On November 17, 2020, MAWC entered into a *Purchase Agreement* with Eureka.

5. The Application in this case was filed on April 26, 2021. MAWC seeks to utilize the appraisal method contained in §393.320, RSMo, to establish the rate base of both the Eureka water and wastewater systems.

RESPONSE TO STAFF RECOMMENDATION

6. On October 1, 2021, Staff filed its *Staff Recommendation*. Therein, Staff recommended that “the Commission reject MAWC’s request for CCNs to install, own, acquire, construct, operate, control, manage, and maintain a water and sewer system in and around the City of Eureka, Missouri. . . .” (Staff Rec., para. 20).

7. In its Memorandum, Staff summarizes its position as follows:

Staff’s conclusion is that MAWC has the requisite TMF capacities to own and operate the Eureka systems. However, Staff further concludes that MAWC’s proposal to acquire Eureka’s water and sewer assets do not meet the Tartan Criteria, and it is Staff’s position that the transaction as requested by MAWC in its Application, i.e., utilizing the appraisal method contained in §393.320, RSMo, is not in the public interest.

(Staff Memo., p. 21).

8. MAWC disagrees with this conclusion, as further explained below, and as will be stated in greater detail in MAWC’ direct testimony in this case.

9. Staff’s Memorandum further recommended that “Should the Commission approve the Application,” it should do so subject to certain conditions. (Staff Memo, p. 21-23). MAWC states that it also objects to these proposed conditions.

PUBLIC INTEREST

10. Staff's position as to public interest attempts to effectuate a "regulatory veto" of Section 393.320, RSMo (the Missouri appraisal statute). Through the enactment of §393.320, RSMo, the General Assembly has already addressed the public interest. The Staff should not be allowed to add its own layers of analysis on a statute that is clear in its intent and execution.

11. Section 393.320, RSMo, applies where the buyer (MAWC) is a "Large Water Public Utility" and the seller (Eureka) is a "Small Water Utility." There appears to be no dispute in this case that MAWC and Eureka's systems so qualify. In that situation,¹ the statute requires as follows:

2. **The procedures contained in this section may be chosen by a large water public utility, and if so chosen shall be used by the public service commission to establish the ratemaking rate base of a small water utility during an acquisition.**

5. (1) **The lesser of the purchase price or the appraised value, together with the reasonable and prudent transaction, closing, and transition costs incurred by the large water public utility, shall constitute the ratemaking rate base for the small water utility as acquired by the acquiring large water public utility; provided, however, that if the small water utility is a public utility subject to chapter 386 and the small water utility completed a rate case prior to the acquisition, the public service commission may select as the ratemaking rate base for the small water utility as acquired by the acquiring large water public utility a ratemaking rate base in between. . . .**

6. Upon the date of the acquisition of a small water utility by a large water public utility, whether or not the procedures for establishing ratemaking rate base provided by this section have been utilized, **the small water utility shall, for ratemaking purposes, become part of an existing service area**, as defined by the public service commission, of the acquiring large water public utility that is either contiguous to the small water utility, the closest geographically to the small water utility, or best suited due to operational or other factors. **This consolidation shall**

¹ The Staff Recommendation does not dispute the applicability of the statute to this transaction.

be approved by the public service commission in its order approving the acquisition.

8. **This section** is intended for the specific and unique purpose of determining the ratemaking rate base of small water utilities and **shall be exclusively applied to large water public utilities in the acquisition of a small water utility.**

(emphasis added).

12. In this case, the purchase price (which was *specifically identified* in the public election held in Eureka) is equal to the appraised value. Therefore, that amount together with the reasonable and prudent transaction, closing, and transition costs incurred by MAWC shall be used by the public service commission and shall constitute the ratemaking rate base.

13. In addition to alleging that utilizing Section 393.320, RSMo, is “not in the public interest,” the Staff also alleges that the existing appraisal is “insufficient as a matter of law.” (Staff Rec., para. 14). However, it is unclear what legal standard Staff believes it fails to meet.

14. Section 393.320.3(1), RSMo requires an appraisal be performed by three appraisers. The Valuation Report was prepared for the City of Eureka. (See Appendix A to the Application). The appraisers were Edward W. Dinan, CRE, of Dinan Real Estate Advisors, Inc.; Joseph Batis MAI, R/W-AC, of Edward J. Batis & Associates, Inc.; and, Elizabeth Goodman Schneider, ASA, of Goodman Appraisal Consultants, LLC.

15. Section 393.320.3(2)(a), RSMo, further states that the “determination of fair market value shall be in accordance with Missouri law and with the Uniform Standards of Professional Appraisal Practice.” The appraisal contains a joint assessment of the fair market value of the water system and sewer system and states that it has been:

. . . prepared in conformance with Standards Rule 2-2(a) of the 2020-2021 Edition of the Uniform Standards of Professional Appraisal Practice (USPAP). In addition to being prepared in compliance with USPAP, this appraisal has been prepared in

accordance with the Code of Ethics and Standards of Professional Practice of the Appraisal Institute.

(App. A, p. 2).

16. Credible valuation opinions require 1) professional education and formal training, 2) competency in the areas of market, property type, and technical issues, 3) relevant professional experience, and 4) judgement. The appraisers' work in the subject case, as compared to the USPAP standard - *what an appraiser's peers' actions would be in performing the same or similar assignment* - exceeds the professional standards established by USPAP.

17. Moreover, what Staff described as "significant deficiencies" in the engineering report are neither "significant," nor "deficiencies." MAWC responds to those allegations as follows:

- Report is not signed, sealed, and dated
 - Section 393.320, RSMo, does not require signed, sealed engineering report, or any an engineering report at all.
 - The lack of a Professional Engineer's (PE) seal does not negate the fact that this report was prepared by a licensed PE in good standing in the State of Missouri.
- Two versions of the report...
 - This situation, although not mentioned by Staff, has been explained in response to Staff Data Request 35, provided on July 15, 2021.
- "... did not physically observe the assets, but makes assertion to physical condition and functionality of the assets" and "fails to acknowledge the known deficiencies with the physical condition and functionality. . . ."
 - It is common practice to base observations for this purpose on photos.
 - The engineer is never able to observe below ground assets.
 - The impact of these matters on the appraisal would be a question for the appraisers.
 - The intent of the Flinn Report and the limitations experienced by the engineer are described on the first page of the report as follows:
"The purpose of this Engineering Report is to provide a high-level review of the condition of the system, estimate the 2019 installation cost, and estimate the depreciated book value of the assets. The City provided limited information on the assets. The original installation costs were not recorded by the City. The above ground assets are listed with 2019-2020 replacement

costs in the City's insurance list of assets (Appendix A). The City provided the year of installation for the above ground assets. The buried assets (water distribution and sewer collection systems) are not listed in the insurance list of assets. The 2019 estimated cost of installation for the buried assets was calculated using a combination of an engineering opinion of cost to install the assets based on knowledge of other systems of similar size, as well as correspondence from the City, vendors, and contractors. The year of installation for the buried assets was estimated based on the installation of the above ground assets, described in more detail below. The 2019 estimated installation cost was depreciated based on the age of each asset. The estimated values listed in this report do not include the value of land or easements.

The high-level review of the condition of the system is based on the data provided by the City and photos that were taken by others during a site visit. Flinn Engineering did not visit the site.”

- Further, the report notes that “Although many of the assets are fully depreciated, they are still in operation and could continue to stay in operation well beyond the depreciation period.” Operational assets have a value, whether fully depreciated or not.
- “. . . fails to acknowledge that the wells and treatment are to be functionally abandoned as a part of the acquisition.”
 - It is unclear what “functionally abandoned” means.
 - No wells will be “abandoned as a part of the acquisition.” Their use will change if MAWC purchases the assets and after an alternate primary supply is constructed.
 - Even after an alternate supply is constructed, the wells will be maintained to provide back-up supply, something required by Safe Drinking Water Act requirements. The assets still have value.
 - Lastly, it is improper and misleading for an appraiser to assume, for valuation purposes, the occurrence of some act, event, or change in the future when developing a market value opinion for a property “as is” (as it actually is known to exist) as of the effective date of value.

18. MAWC would also note that while one of the criticisms of the engineering report was that it finds the assets to be in generally good condition, Staff itself states as follows in regard to the water system:

. . . the facilities appeared to be in fair to good condition, with the equipment well maintained and exhibiting ordinary wear and tear from normal operation. At the time of the inspection, Staff found the general housekeeping, grounds and maintenance and site security to be very good.

(Staff Memo., p. 10).

19. Lastly, if the Staff was concerned about the appraisal or engineering report, it had plenty of opportunity to discuss these matters with MAWC and the appraisers or the engineer involved. There was continuous contact between MAWC and Staff as a result of the data request process and multiple meetings between MAWC and Staff to discuss the Eureka acquisition. Throughout the process there were many opportunities for Staff to express any concerns it might have had in regard to the appraisal or engineering report. At no point in the process did Staff bring up any alleged “significant deficiencies” in the Flinn Report or make any mention that the appraisal was insufficient “as a matter of law.” MAWC counsel Tim Luft further offered to provide Staff access to MAWC personnel, Flinn Engineering, and/or the appraisers, if they had any questions for them about the appraisal or engineering report. Staff never took the Company up on this offer.

20. MAWC believes that the intent of Section 393.320 is to incentivize larger utilities to acquire smaller utilities and spread costs among more customers. That intent is very much addressed by MAWC’s proposal in this case.

21. Eureka’s approximately 4,000 water customers will be added to a customer base in St. Louis County of approximately 343,000 customers. Further, the purchase price for those water assets (\$18,000,000) would be added to the current rate base associated with those St. Louis County water customers, which is approximately \$1,200,000,000 (\$1.2 Billion). Thus, the Eureka water customers would represent about 1.1527% of the customers going forward, while the Eureka rate base would represent approximately 1.4778% of the district’s rate base. This slight difference does not represent a result that is contrary to the public interest.

22. On the sewer side, Eureka’s approximately 4,000 customers will join the “Other Missouri” sewer rate category customer base of approximately 8,500 customers.² The

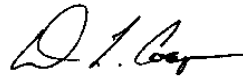
² MAWC serves approximately 15,000 sewer customers state-wide.

\$10,000,000 purchase price for those sewer assets would be added to the Other Missouri Sewer rate base of approximately \$34,000,000. Thus, the Eureka sewer customers would represent about 32% of the customers going forward, while the Eureka rate base would represent approximately 22.727% of the district's rate base. This addition of Eureka, at the appraisal price, will actually be a benefit to the existing MAWC customers.

CONCLUSION

23. MAWC disagrees with, and objects to, the *Staff Recommendation*. MAWC further objects to certain of the conditions identified by the Staff, in the case the Commission should approve the Application.

WHEREFORE, Missouri-American submits this Response and requests that the Commission set a procedural schedule in this matter.



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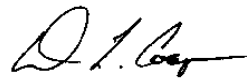
CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been sent by electronic mail this 12th day of October, 2021, to:

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A handwritten signature in black ink, appearing to read "D. Linton", is positioned in the center of the page.