BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Application of Osage Utility Operating Company, Inc. to Acquire Certain Water and Sewer Assets and for a Certificate Of Convenience and Necessity	)))))	**Case No. WA-2019-0185**

OUOC REPLY BRIEF

COMES NOW Osage Utility Operating Company, Inc. ("OUOC" or "Company"), and, as its *Reply Brief,* respectfully states as follows to the Missouri Public Service Commission ("Commission"):

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REPLY SUMMARY

OUOC will respond to the initial briefs of the Public Water Supply District No. 5 of Camden County, Lake Area Waste Water Association, Inc., and Missouri Water Association, Inc. (collectively "Joint Bidders"); Cedar Glen Condominium Owners Association, Inc. ("Cedar Glen"); and the Office of the Public Counsel ("OPC").

The fact that OUOC does not respond to each and every statement contained in those briefs should not be taken as acquiescence and the matters not addressed.

Rather, OUOC's decision simply reflects the fact that those matters were adequately addressed in its Initial Brief.

As suggested in OUOC's opening statement, the argument of the Joint Bidders, Cedar Glen, and OPC is primarily that this Commission will not do its job in the future to ensure that safe and adequate service is provided at just and reasonable rates. The Joint Bidders and OPC specifically allege that Confluence Rivers' proposed acquisition *will* result in the following:

- The rate payer "will pay substantially higher costs for utility services due to the cost of unnecessary improvements." (Joint Bidders, p. 4) (emphasis added)
- Ratepayers "will be subjected to unreasonable rates . . . ." (Joint Bidder, p. 9) (emphasis added)
- OUOC is ". . . . seeking to charge customers beyond that which is necessary to provide safe and adequate service." (OPC, p. 7-8)
- "The OWC's rates will also likely be higher under OUOC's management than the Joint Bidders' with no noticeable benefits because of OUOC's requested acquisition incentive." (OPC, p. 11) (emphasis added)

While the Commission certainly can take into account the possible rate impacts of a proposed acquisition in assessing whether or not there is "no net detriment," the Commission should not completely abandon its statutory responsibilities as suggested by these parties. No one can know with certainty what rates will be in the future for the systems at issue in this case or how those rates would compare to rates each of the

Joint Bidders currently charge their respective customers. And in every rate case where a utility seeks to include in its rate base investment in its system, the Commission must examine the prudence of each investment, the prudence of the construction process, and the prudence of the amounts expended. The Commission in each rate case also examines and establishes the appropriate cost of capital based, upon other things, its view of the appropriate capital structures and debt costs.

As to the requested acquisition incentive, Commission Rule 20 CSR 4240-10.085(2), specifies that even where an incentive has been found to be in the public interest, the commission may only apply that acquisition incentive in the applicant's next general rate "if the commission determines it will not result in unjust or unreasonable rates."

There is no evidence in this case, nor could there be any evidence, that costs to customers will result from "unnecessary improvements," that customers will be subject to "unreasonable rates," that the costs of financing will be passed onto customers without review, or that rates will be higher merely because OUOC "requested" an "acquisition incentive." That is because any concern as to the Commission's ability to do its job is unfounded.

OUOC's application provides the following benefits for OWC systems that have been in receivership for over 14 years:

- OUOC would be a single, known owner/operator for all of the OWC water and sewer systems. This is important as each of the four OWC services areas

(eight total systems) have experienced issues over the last fourteen plus years and need attention;

- OUOC is an owner/operator with a solid track record of rehabilitating, maintaining and operating small water and sewer systems;
- OUOC's financial and technical resources are sufficient to provide improved service options for customers; and,
- OUOC's ownership will result in continued regulation of operations by the Commission to ensure safe and adequate service at just and reasonable rates.

When the benefits are considered, OUOC's acquisition of the OWC utility assets and CCNs is not detrimental to the public interest and should be approved by the Commission subject to the conditions proposed by the Staff.

APPLICABLE LEGAL STANDARD

Must Approve If Not Detrimental to the Public Interest

Under applicable law, the Commission must approve those acquisition applications over which it has jurisdiction unless the transaction is shown to be "detrimental to the public interest," a standard established by the Missouri Supreme Court in *State ex rel. City of St. Louis v. Public Service Commission*, 73 S.W.2d 393 (Mo. 1934) and reaffirmed in *State ex rel. AG Processing, Inc. v. Public Service Commission*, 120 S.W.3d 732, 735 (Mo. banc 2003).

Both the Joint Bidders and OPC seem to propose a new standard for

acquisitions. The Joint Bidders ask rhetorically "who is a better judge of risk to the rate payer than the rate payer themselves?" (Joint Bidders, p. 14) OPC proposes a new standard for acquisitions by suggesting that the Commission act as a proxy for the "free market" where it believes "the public's choice for a service provider would win out." (OPC, p. 1)

Both of these suggestions ignore the well-established case law starting with the definition of the "public interest."

> The public interest is found in the positive, well-defined expression of the settled will of the people of the state or nation, as an organized body politic, which expression must be looked for and found in the Constitution, statutes, or judicial decisions of the state or nation, and not in the varying personal opinions and whims of judges or courts, charged with the interpretation and declaration of the established law, as to what they themselves believe to be the demands or interests of the public.

In the Matter of the Joint Application of Great Plains Energy Incorporated, Kansas City Power & Light Company, and Aquila, Inc., Report and Order, Case No. EM-2007-0374, 2008 Mo. PSC LEXIS 693, 458-459 (MoPSC July 1, 2008).

The "not detrimental" standard finds its basis in the constitution itself and the idea that an owner (in this case as represented by the bankruptcy trustee) has a constitutional right to determine whether to sell their property or not. *State ex rel. City of St. Louis v. Public Service Commission*, 73 S.W.2d 393 (Mo. 1934). The public further has an interest in safe drinking water and wastewater that does not harm the environment as reflected in both federal and state statutes and rules.

The General Assembly created the Public Service Commission to make these types of decisions, in part, because the "public interest" has many aspects. But a

suggestion that somehow a Commission decision should be based on an expression of opinion from some of the customers misinterprets the law and the Commission's role in this process.

The "public interest" necessarily is more than the customers:

> Determining what is in the interest of the public is a balancing process. In making such a determination, the total interests of the public served must be assessed. This means that some of the public may suffer adverse consequences for the total public interest. Individual rights are subservient to the rights of the public. The "public interest" necessarily must include the interests of both the ratepaying public and the investing public; however, as noted, the rights of individual groups are subservient to the rights of the public in general.

In the Matter of the Joint Application of Great Plains Energy Incorporated, Kansas City Power & Light Company, and Aquila, Inc., Report and Order, Case No. EM-2007-0374, 2008 Mo. PSC LEXIS 693, 458-459 (MoPSC July 1, 2008).

As described in OUOC's *Initial Brief*, the analysis calls for a *netting* of detriments and benefits. Even if the Commission were to believe there is the possibility of some detriment:

> The presence of detriments . . . is not conclusive to the Commission's ultimate decision because detriments can be offset by attendant benefits. The mere fact that a proposed transaction is not the least cost alternative or will cause rates to increase is *not detrimental to the public interest* where the transaction will confer a benefit of equal or greater value or remedy a deficiency that threatens the safety or adequacy of the service.

In the Matter of the Joint Application of Great Plains Energy Incorporated, Kansas City Power & Light Company, and Aquila, Inc., Report and Order, Case No. EM-2007-0374, 2008 Mo. PSC LEXIS 693, 454-455 (MoPSC July 1, 2008), quoting *Re Union Electric Company,),* Case No. EO-2004-0108, 13 Mo.P.S.C.3d 266, 293 (2005).

In this case, the benefits provided by a single owner/operator, with a solid record as to small water and sewer systems, having financial and technical resources necessary to provide better service, all subject to the continued regulation by the Commission, should result in a determination of no detriment.

OUOC is an affiliate of CSWR. (Exh. 1, Cox Dir., p. 5) The following CSWR affiliates are public utilities authorized to provide water and sewer service in Missouri subject to the regulation of the Commission and have acquired small Missouri water and sewer companies, brought capital to improve those systems, upgraded the services provided to customers, and delivered safe and adequate service where that was not the case prior to acquisitions. CSWR companies have purchased multiple systems in Missouri that were in state-appointed receivership, with numerous MDNR deficiencies and brought those systems back into regulatory compliance for the provision of safe and reliable service. (Exh. 5, Cox Sur., p. 8-9)

CSWR has customer service systems at each Missouri utility it currently operates that provide benefits to the customers and comply with the Commission's Chapter 13 rules. (Exh. 1, Cox Dir., p. 7)

CSWR has been able to attract investment capital to construct and maintain facilities necessary to provide safe and reliable water and wastewater service and is willing and able to invest the capital necessary to bring the water and wastewater systems at issue in this case up to standard and maintain compliance with applicable MDNR regulations. (Exh. 1, Cox Dir., p. 8, 10)

In each of their previous applications, the Commission has determined CSWR-

affiliated companies have the technical, managerial, and financial capability to own and operate water and wastewater systems in Missouri. OUOC, another CSWR-affiliated company, similarly has the technical, managerial, and financial capability to own and operate the systems and provide safe and adequate service for the customers.

No party has seriously challenged OUOC's qualifications to provide the service required at the eight OWC systems. OUOC's acquisition of the OUOC assets and CCNs is not detrimental to the public interest.

ESTIMATES

Joint Bidders, Cedar Glen, and OPC make much of the OUOC estimates of repairs for the eight OWC systems. Before going further, it bears mentioning that *all cost estimates are preliminary*. OUOC will make known, necessary improvements immediately. (Tr. 123-125, Cox) However, it will further operate the system for a time to see if the range of improvements can be narrowed. (*Id*.) After final engineering has been performed, the projects are put out for competitive bid by a third-party engineer to entities that include local contractors. (Tr. 147, Cox) The bidders on these projects do not include any CSWR affiliates. (*Id*.) Only after this process is completed, will OUOC know exactly what repairs are required and what they cost.

It is for this reason that OUOC is not aware of any CCN proceeding where the Commission has "approved" expenses. In fact, OPC witness Roth agreed that "the Commission doesn't historically approve costs of improvements in an acquisition case."

(Tr. 314, Roth) Ultimately, the Commission will review actual expenditures for prudence in a future rate case. (*Id*.)

Still there is criticism that "OUOC's estimates are likely inflated." (OPC, p. 8) This criticism, however, is based on no critical analysis but rather on a comparison of OUOC's estimates, which address all eight OWC systems, and the other estimates that do not address six of the eight systems.

OPC witness Roth stated that she did not do any analysis specifically as to those repair estimates, she merely recognized that some of OUOC's estimates were less than some estimates provided by the Joint Bidders. (Tr. 311, Roth) She later admitted that one reason for this difference is OUOC had provided estimates for all four OWC service areas (eight systems) while the Joint Bidders had not. (Tr. 311-313, Roth)

Moreover, Staff witness Roos indicated that the OUOC proposal is "a complete preliminary proposal," but that the Joint Bidders' proposal is not a complete proposal or a complete cost estimate. (Tr. 252, Roos) Mr. Roos further explained that he believed OUOC "has provided a proposal that is a good road map for safe and adequate service," but that he did not feel as confident about the Joint Bidders' proposal. (Tr. 252-253, Roos) This is not surprising as the Joint Bidders have NO ESTIMATE for repairs at the Cimarron Bay, Chelsea Rose, and Highway KK systems.

OPC's and the Joint Bidders' testimonies as to estimates relates to Cedar Glen only and relies upon statements from a Lake Ozark Water and Sewer ("LOWS") employee that the necessary repairs for Cedar Glen are "largely 'cosmetic, building repairs, paint, cleaning the interior of the well house.'" (OPC, p. 8; Joint Bidders, p. 9)

The first question that comes to mind in this situation is if the problems are largely "cosmetic," why LOWS has not taken care of them.

Additionally, in regard to the sand filter at Cedar Glen and its ability to produce effluent within the ammonia limits, Staff witness Roos' was asked whether he had "any reason to disagree with certain statements made by LOWS to DNR regarding whether the Cedar Glen waste water system could meet effluent limitations without further upgrades." Mr. Roos responded that he did, and explained that:

> The same type of letter was submitted to DNR for other sewer systems at [Osage Water Company] and those systems have now shown to be exceeding permit limits.

(Tr. 249-250, Roos) Mr. Roos further clarified that he was referring to the Cedar Glen, Cimarron Bay, and the Eagle Woods systems. (*Id*. at 250)[1]

OPC further criticizes Staff for not having done a review of the repairs estimate amounts. (OPC, p. 9) This is, of course, different than reviewing the need for the repairs themselves. As stated above and in OUOC's *Initial Brief*, Staff did review the conditions of all four service areas (eight systems) as well as OUOC's plan for addressing deficiencies at in those service areas. It is from that review that Staff's indicated that OUOC's plan provides a "good road map for safe and adequate service." (Tr. 252-253, Roos)

[1] This is not surprising as even MWA/LAWWA witness Goss indicated that he has experience with sand filters that "cannot meet the ammonia limits on a regular basis." (Tr. 427, Goss)

RATES

Concern is expressed as to rates that may result after the OWC systems have rehabilitated. Of course, no one knows what rates will be in the future. Staff witness Bolin acknowledged that she has no way to say with certainty what rates will be two years from now if OUOC acquires the systems because she does not know all of the expenses, the final plant improvements and any prudency adjustments, and any disallowances of cost. (Tr. 276, Bolin) OPC witness Roth agreed that she also cannot say with any certainty what rates will be two years from now. (Tr. 318, Roth)

This being said, a future rate increase for Osage Water Company ("OWC") customers under either OUOC's or Joint Bidders' proposals will not be surprising. The rates for OWC last changed on September 19, 2009. (Osage Water Company, PSC Mo No. 1 (water), Sheet 5 and PSC Mo. No. 1 (sewer), Sheet No. 10) Based on inflation alone, it would be hard to imagine the cost of operating the OWC systems has not increased over the past ten years. In addition, any upgrade in service and the corresponding cost of those upgrades, as well as any additional investment in the systems since 2009, all else being equal, would suggest a rate increase of some sort for OUOC in a future rate case, subject to the review of the Commission as identified above.

In fact, one can determine easily form the record that any suggestion that customers will not experience a rate increase under the Joint Bidders' proposal is absolutely erroneous. MWA and LAWWA indicate that their initial bill will total $94.00 per month ($60.00 for water and $34.00 for sewer). (Exh. 401, Goss Dir., p. 5) And this

is without taking into account the costs of any improvements necessary for the Cimarron Bay, Chelsea Rose, and Highway KK systems. For an OWC customer using 5,000 gallons from a 5/8 inch meter, a current monthly water bill would be $42.34 ($24.76 + ($5.86 * 3), and a current monthly sewer bill would be $29.02, for a total current bill of $71.36. (Exh. 1, Cox Direct, p. 22-23)

Accordingly, to the extent one sees a detriment in a potential rate increase for systems that have not seen a rate increase for ten years, that detriment is clearly present for the Joint Bidders proposal, as under the Joint Bidders proposal rates will be increased for almost one-half of the OWC customers on day 1.

FINANCING

OPC and the Joint Bidders wrongly suggest that the PWSD#5 bond financing is a positive for OWC customer rates. (OPC, p. 10, Joint Bidders, p. 11) Regardless of the ultimate impact on the PWSD#5 rates, OPC and the Joint Bidders ignore the fact that, at best, the referenced bond financing is only available for the PWSD#5's activities at Cedar Glen. OPC witness Roth acknowledged this fact and agreed that she did not know what the situation would be for the other OWC service areas. (Tr. 310, Roth) That is because there is NO FINANCING (bond or otherwise) identified for the Cimarron Bay, Chelsea Rose, and Highway KK systems purchase or repairs.

ENVIRONMENTAL INDUSTRIES

OPC cites *Environmental Industries v. Public Service Commission*, 219 S.W.3d 256 (Mo.App. 2007) as support for the concept that rate increases should be considered as a part of acquisition cases. In fact, there is no holding in *Environmental Industries* that supports OPC's claim that the Commission should consider future rates as part of an acquisition case.

In *Environmental Industries*, Missouri-American Water Company ("MAWC") had contracted to buy most of the same Osage Water Company ("OWC") properties that are the subject of this case. However, MAWC requested a rate increase as a part of the acquisition, and it did not want to purchase the Cedar Glen sewer system. (*Id*. at 259-260) The Court of Appeals noted that "[t]he case before the Commission was not a standard transfer of utility assets case and, therefore, raised a number of unique issues – not least among that of the bootstrapped rate increase." (*Id*. at 261)

The only questions presented to the Court of Appeals for resolution were: 1) Did the Commission hold an evidentiary hearing as required by § 393.190?, and 2) Was the Commission's order supported by competent and substantial evidence? As to the rate increase requested by MAWC, the Court merely stated that "[w]hether the Commission even had the authority to bootstrap a rate increase into the sale application process is unclear at best." (Id. at 260) OPC's reliance on that case is unfounded and without merit.

What the Commission should take from the *Environmental Industries* case is that the Commission has long been afraid of an OWC acquisition outcome that would benefit some, but not all, of the OWC systems. The Court of Appeals stated that:

> The evidence in the record indicated that the parties proposed a sale of only part of Osage Water's assets leaving the bulk of the sewer customers to be served by the distressed utility. As proposed by the Application, some customers would continue to receive substandard service from a distressed utility.

(*Id*. at 266)

The Court further noted that the Commission itself had recognized the danger that some of the OWC systems might be left behind:

> Indeed, in its 2003 report the Commission anticipated the scenario proposed by the Application, but in the context of a receivership action. The Commission noted that "some of the utility systems of Osage Water might be more easily sold than others. That raises the possibility that economically non-viable systems that still must serve customers might be left orphaned after the more valuable systems are sold." The Commission cautioned the receiver that the assets left in the hands of Osage Water after other assets were sold must be able to be operated effectively.

(*Id*. at 266, Fn. 5)

Understandably, Cedar Glen's interest in OWC then, and now, is only as to the Cedar Glen properties. Cedar Glen recounts that its opposition to the MAWC purchase in the *Environmental Industries* case was based its contention that "the OWC water system assets serving Cedar Glen, and the wastewater system assets as well, should be transferred to Cedar Glen for its separate management and operation." (Cedar Glen, p. 3) But Cedar Glen's interest should not thwart the broader public interest associated with removing all the OWC assets from receivership and bankruptcy and providing a path forward for all of the OWC systems and service areas.

PWSD#5 REGIONALIZATION PROPOSAL

In supporting their plan for Cedar Glen (to the exclusion of Chelsea Rose, Cimarron Bay, and Highway KK service areas), the Joint Bidders **erroneously** state that "[MDNR] previously approved the interconnection of the Cedar Glen and Cedar Heights Systems." (Joint Bidders, p. 12) The Joint Bidders generally cite to Ex. 9, Mr. Krehbiel's engineering report, for this proposition, but do not point to exactly where there is an MDNR approval for connection to Cedar Glen. That is because MDNR did not approve the connection to Cedar Glen. Cedar Glen was not even an option for compliance considered by Mr. Krehbiel within the engineering report he submitted to MDNR in 2016 for improvements to the PWSD water system. (Ex. 9, bate-stamp PWSD 1.47-000052) As Mr. Krehbiel's report states, "a feasibility and engineering study would have to be made at such time that these areas would show an interest." (Ex. 9, bate-stamp PWSD 1.4.7-000069)

The Joint Bidders further allege that approval of OUOC's application may "thwart PWSD#5's regionalization of water and sewer service in Camden County." (Joint Bidders, p. 4) However, as indicated above, a new feasibility and engineering study would have to be made to even consider the potential for regional expansion. Moreover, Mr. Krehbiel admitted in his testimony at the hearing that "there's no formal plan [for regionalization] but it is [PWSD] that wants to be the primary service to all these water systems." (Tr. 362, Krehbiel) (emphasis added).

Mr. Krehbiel states the purpose of his engineering report is to "provide an engineering analysis of the Public Water Supply District No. 5 (District) water system for

necessary improvements or modifications to the system **to achieve and maintain technical, managerial, and financial capability** with respect to the National Primary Drinking Water Regulations." (Ex. 9, bate-stamp PWSD 1.4.7-000055) (emphasis added) Mr. Krehbiel states:

> There is one Compliance Agreement that affects the District (See Exhibit G). The Compliance Agreement became effective May 2, 2013, and is basically in regard to the well at Cedar Heights Condominiums. This well is not State Approved.

(Ex. 9, bate-stamp PWSD 1.4.7-000068) (emphasis added)

Within the 2013 Compliance Agreement referenced above, MDNR states it has determined that the Cedar Height Condominiums public water system, owned by PWSD, does not meet acceptable construction standards for a public water system. (Ex. 9, bate-stamp PWSD 1.4.7-000094) MDNR outlined its concerns with wells like the one PWSD#5 continues to use to this day to serve the public:

> . . . the construction of water wells not meeting the standards creates an increased risk of exposure to microbiological and/or chemical contaminants to those served by wells that meet construction standards. Substandard wells also create an increased risk of contamination of ground water resources which can adversely affect neighboring private and public wells. Furthermore, wells constructed without proper casing, wells constructed to an inappropriate depth, and wells lacking adequate backflow protection give an unfair economic advantage compared to the cost of wells meeting public water system construction standards.

(Ex. 9, bate-stamp PWSD 1.4.7-000095) (emphasis added)

Mr. Krehbiel concludes in his report that PWSD#5's first priority should be:

> . . . the drilling of a new State Approved well at the Cedar Heights complex. This should include the construction of a well house and security fencing along with installation of approved chlorination equipment. During this construction, piping accommodations should be made for the eventual consolidation of the two systems. The second priority should be

> the acquisition of a well and tower site in the vicinity of the intersection of Clearwater Drive and Ozark Isle Drive. **This acquisition would be the first step in the implementation of Alternative No. 1.**

(Ex. 10) (emphasis added)

Mr. Krehbiel testified that he recommended PWSD#5 take the corrective actions outlined as construction funds become available. (Tr. 359, Krehbiel) As of today, more than six years have passed since MDNR's 2013 findings and PWSD#5 has not completed all of the corrective actions recommended by Mr. Krehbiel in his engineering report. (Tr. 361, Krehbiel) Mr. Krehbiel testified that PWSD#5 has only taken the first step in implementation of Alternative No. 1, the purchase of a well and tower site. (Tr. 360, Krehbiel).

PWSD#5 continues to place the public at risk as determined by MDNR. The simple truth is that PWSD#5 does not have the financial capacity necessary to own and operate its own systems in a safe and adequate manner, let alone the capacity to take on another system such as Cedar Glen. Mr. Stone testified that PWSD#5 has $1,426,000 in unissued bonds available. (Tr. 385, Stone) But Mr. Krehbiel's engineering report has an estimated total project cost of $1,800,400.00 for Alternative No. 1. The estimated total project cost for both Alternative No. 2 and 3 are above PWSD#5's bonding capacity, at $1,582,100.00 and $1,430,900.00, respectively.

ACQUISITION PREMIUM

The OPC Brief attacks both whether OUOC has met the requirements of Commission Rule 20 CSR 4240-10.085, and whether Commission Rule 20 CSR 4240-10.085 is lawful.

As to the standards found within the rule, OPC only challenges the requirement that "the acquisition would be unlikely to occur without the probability of obtaining an acquisition incentive." Commission Rule 20 CSR 4240-10.085(4). Granted this "but for" test is a tough standard. The difficulty of the proving this item was discussed by the Commission during the rulemaking process. (Order of Rulemaking, Case No. AX-2018-0240, Comment #19 (October 4, 2018)) A witness's testimony on behalf of the acquiring company is likely the only way to present this item

In this case, testimony was provided by Mr. Cox who stated that acquisition of all the OWC utility systems, all requiring some level of investment in improvements, is unlikely to occur without the probability of obtaining an acquisition adjustment and if the Commission decides not to award the incentive requested, OUOC will need to reevaluate its risk in taking on numerous failing systems to determine how it will move forward. (Exh. 1, Cox Dir., p. 25-26)

OPC argues that OUOC cannot meet this standard, in part, because CSWR attempted to purchase the OWC systems from the receiver before the Camden County Circuit Court and because CSWR has formed "companies for the purpose of acquiring distressed water and wastewater systems. . . ." in a variety of states. (OPC, p. 15, 17)

As starting point, it must be remembered that until this case, no potential purchase of the OWC assets has been brought before the Commission for consideration since the OWC assets were placed in permanent receivership.

Moreover, the fact OUOC made acquisitions in Missouri prior to the adoption of the Nonviable Utility Incentive Rule or that OUOC's affiliates have made or propose to make acquisitions in Arkansas, Tennessee, Kentucky, and Louisiana is not determinative as to application of this Commission rule, nor necessarily representative of the situations in Missouri that drove promulgation of the Nonviable Utility Incentive Rule. What is important is that as of January 30, 2019, the Commission has made available premiums to companies willing to acquire non-viable water and wastewater companies. The decision regarding OUOC's request for a premium in this case should be based solely on that rule and whether OUOC qualifies for a premium under the rule's standards. (Exh. 5, Cox Sur., p. 3)

For many years, this Commission has wrestled with the problem of how companies like CSWR and its affiliates, who have the operating and managerial expertise and the capital necessary to convert small non-viable utilities into utilities that consistently comply with applicable regulations and are able to provide safe and reliable service to customers, can be encouraged to acquire, maintain and operate the many non-viable systems operating in this state. In the workshops the Commission held prior to adoption of 4 CSR 240-10.085, CSWR and other similarly-situated companies argued in favor of incentives because viable utilities aren't likely to invest in non-viable utilities unless it makes business sense to do so. Consequently, if viable utilities were going to

be enticed to invest in non-viable utilities, some investment incentive needed to be provided. That's why the Commission adopted its rule. OUOC shouldn't be penalized for attempting to now take advantage of those incentives just because those same incentives didn't exist in the past and don't currently exist in other states. (Exh. 5, Cox Sur., p. 3-4)

In the near future, affiliates of OUOC plan to seek regulatory commission authority to acquire, own, and operate small water and wastewater systems in Texas and North Carolina. Each of those states recently enacted legislation allowing regulators to value rate base for those systems based on the appraised market value of the acquired systems. (Missouri has adopted similar legislation, but it's our understanding that benefit is currently only available to acquisitions by "large water public utilities" (those of 8,000 customers or more)). Would it be fair for regulators in Texas and North Carolina to deny CSWR affiliates in those states the market value rate base available to other acquiring utilities just because their affiliates acquired similar systems in Arkansas, Tennessee, Kentucky, Louisiana, and Missouri where market value treatment isn't available? Of course not. And it's similarly not appropriate for the Commission to deny acquisition incentives in this case just because they haven't been sought previously in Missouri or in other states where premiums aren't available. (Exh. 5, Cox Sur., p. 4)

But there is perhaps an even more compelling reason to reject the argument made by OPC in this case. If a utility like OUOC is barred from taking advantage of the incentives available under 20 CSR 4240-10.085, then the rule will be rendered a nullity.

It is hard to imagine there is any utility who may try to take advantage of that rule in the future that did not make acquisitions in the past when no incentive was available. If those prior acquisitions are a disqualifier – as OPC seems to argue – then the benefits the rule purports to provide are purely illusory. (Exh. 5, Cox Sur., p. 4-5)

OPC also argues the Nonviable Utility Incentive Rule is "without express statutory authority" and, therefore, "foundationless and unlawful." (OPC, p. 22) However, the rule seems to track quite nicely with two appellate cases that have involved the Commission. Those are:

1) *State ex rel. AG Processing v. PSC,* 120 S.W.3d 732 (Mo banc 2003). (The Aquila acquisition premium case);
2) *Missouri Gas Energy v. Public Service Commission*, 9768 S.W.2d 434 (Mo.App. 1998).

In *AG Processing*, the Supreme Court held that "the PSC erred when determining whether to approve the merger because it failed to consider and decide all the necessary and essential issues, primarily the issue of UtiliCorp's being allowed to recoup the acquisition premium." *Ag Processing* at 736. Thus, the Nonviable Utility Incentive Rule merely specifies a process for doing something that the Commission would be required to do anyway – assess the Company's possible recoupment of the acquisition premium and whether its ability, or inability, to recoup the premium will have any effect on the Commission's determination that the merger is not detrimental to the public interest.

Interestingly, the Supreme Court in *Ag Processing*, provided the following footnote describing when recovery of an acquisition premium might be appropriate:

> See *State ex rel. Martigney Creek Sewer Co. v. Pub. Serv. Comm'n*, 537 S.W.2d 388, 399 (Mo. banc 1976) (stating that, for ratemaking purposes, recovery of the cost of an asset acquired from another utility depends on the reasonableness of the acquisition, considering the factors of whether the transaction was at arm's length, if it resulted in operating efficiencies, and if it made possible a desirable integration of facilities).

Ag Processing at 736. OUOC believes these factors are all present in this case and provides another reason to find that the requested acquisition premium is in the public interest.

If the Commission determines that an acquisition premium would be in the public interest, Commission Rule 20 CSR 4240-10.085(2) states that the "commission may apply an acquisition incentive in the applicant's next general rate proceeding following acquisition of a nonviable utility if the commission determines it will not result in unjust or unreasonable rates."

This approach is very similar to that found by the courts to be lawful in regard to accounting authority orders. In *Missouri Gas Energy*, the Court of Appeals reiterated that "AAOs are not the same as ratemaking decisions, and that AAOs create no expectation that deferral terms within them will be incorporated or followed in rate application proceedings." *Missouri Gas Energy* at 438. Similarly, the Commission has in the Nonviable Utility Incentive Rule made clear that an acquisition premium found to be in the public interest at the time of acquisition will be examined, along with all relevant factors, in a future rate case to determine what rate will be just and reasonable. This is certainly an approach that is within the Commission's statutory powers.

Given the history of the OWC companies, the Commission should find that an acquisition premium is in the public interest based on the facts of this case. If it does so find, the amount can be, and, ultimately, should be, addressed in the next rate case where the Commission has before it the actual rate information and is considering all relevant factors to determine the just and reasonable rate at that time.

WHEREFORE, OUOC respectfully submits this *Reply Brief* for the Commission's consideration.

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CERTIFICATE OF SERVICE

I certify that a true and correct copy of the foregoing was served electronically on all parties of record herein on this 17th day of October, 2019.