

MEMORANDUM

TO: MO PSC Official Case File
Case No. WM-2005-0058
Aqua Missouri, Inc. and LTA Water Company

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/s/ Dale W. Johansen 12/01/04

Project Coordinator Date

/s/ Cliff E. Snodgrass 12/01/04

General Counsel's Office Date

SUBJECT: Staff Recommendation Regarding Joint Application

DATE: December 1, 2004

BACKGROUND

On September 3, 2004*, AquaSource/RU Incorporated d/b/a Aqua Missouri, Inc. (Aqua) and LTA Water Company (LTA) (collectively, the Joint Applicants) filed a Joint Application requesting authority from the Commission for Aqua to purchase the water utility supply and distribution system assets of LTA. Additionally, the Joint Application sought the transfer of LTA's certificate of convenience and necessity (certificate) to Aqua, or alternatively the issuance of a new certificate to Aqua for LTA's existing service area. Further, the Joint Applicants request that LTA be authorized to cease providing service and Aqua be authorized to begin providing service upon the closing of the proposed asset transfer. At the time they filed the Joint Application, the Joint Applicants also filed a motion for the issuance of the Commission's standard protective order so that the subject asset purchase agreement between Aqua and LTA could be filed under seal.

On September 13, the Commission issued its **Order Adopting Protective Order and Directing Notice**, in which it adopted its standard protective order for this case and directed that notice of the Joint Application be given to LTA's customers. On October 8, LTA filed its **Response to Order Directing Filing**, by which it advised the Commission that notice of the proposed asset sale had been provided to its customers, after consultation with the Staff regarding the content of the customer notice. In its customer

* Unless noted otherwise, all dates herein refer to the year 2004.

notice, LTA advised its customers that comments regarding the Joint Application should be submitted to the Staff and/or the Office of the Public Counsel (OPC) within twenty days after the date of the notice.

On November 1, the Commission issued its **Order Directing Filing of Staff Recommendation**, in which it directed the Staff to file its recommendation regarding the Joint Application on or before December 1. The Commission subsequently changed the filing date for the Staff's recommendation to December 3, at the request of the Staff.

THE JOINT APPLICANTS

LTA is a Commission-regulated utility that provides water service to approximately 90 residential customers in a subdivision known as Lake Taneycomo Acres near Branson, MO. Ms. Jean Liscum is the owner of LTA and is also in charge of the operation of the water system. Ms. Liscum and her husband Tom Liscum, who is deceased, purchased what is now LTA's water supply and distribution system in 1990 from the developers of the subdivision that the system serves.

Aqua is a Commission-regulated utility that provides water service to approximately 960 customers in various locations in Missouri, including locations near Branson. Aqua began operation as a regulated utility in Missouri in 1999 by acquiring Riverside Utility Corporation.

STAFF'S INVESTIGATION

As noted at the beginning of this Memorandum, Staff members from the Auditing Department, the Engineering & Management Services Department, the Water & Sewer Department and the General Counsel's Office participated in the Staff's investigation of the Joint Application.

All participants in the Staff's investigation were provided the opportunity to review and comment on the initial draft of this Memorandum, which Dale Johansen of the Water & Sewer Department created. Comments received from the reviewers were then incorporated into the initial draft to create the final version of this Memorandum.

Items reviewed as a part of the Staff's investigation included the Joint Application and the attachments to the application, including the subject asset purchase agreement. Additionally, the Staff performed a review of LTA's books and records for the purpose of determining LTA's current ratemaking rate base, which in turn was used to determine if the proposed transactions involve an acquisition adjustment. The Staff also reviewed the impact of the proposed transactions on Aqua to determine if they would have an adverse financial impact, and also reviewed LTA's existing depreciation rates to determine if any changes to the rates are needed.

In addition to the items noted above, the Staff reviewed the status of the Joint Applicants' annual report submittals and assessment payments, and reviewed the Commission's active cases to determine if the Joint Applicants have any other matters pending before the Commission. Additionally, the Staff reviewed available information regarding Aqua's other operations and its compliance history with regard to the

regulations of the Department of Natural Resources and the Commission, and also generally reviewed the status of the condition of LTA's water supply and distribution system.

Regarding a review of customer comments responding to the notice of the Joint Application that was sent to LTA's customers, the Staff notes that it did not receive any comments from LTA's customers.

STAFF'S FINDINGS & CONCLUSIONS

Regarding the determination of LTA's ratemaking rate base, the Staff first calculated the balances for LTA's total plant in service ** HC----- **, depreciation reserve ** HC----- ** and net contributions in aid of construction ** HC----- **, all as of September 30. The Staff then subtracted the depreciation reserve and contributions balances from the plant in service balance to arrive at a ratemaking rate base value of ** HC----- **.

To determine whether the proposed asset transfer involves an acquisition adjustment, the Staff compared the purchase price for the subject assets ** HC----- ** to LTA's ratemaking rate base. This comparison results in the Staff's determination that an acquisition premium of ** HC----- ** will exist if the proposed transactions are closed under the terms of the asset purchase agreement. Consistent with the Staff's established position regarding acquisition premiums, the Staff will recommend that the Commission's approval of the proposed asset transfer contain a condition that the acquisition premium not be recovered by Aqua through customer rates.

Regarding the financial impact of the proposed transactions on Aqua, the Staff has determined that the transactions will not substantially affect Aqua's financial condition, particularly when evaluated at the level of Aqua's parent company.

Regarding LTA's depreciation rates, the Staff has concluded that no changes are needed at this time.

Though it is not specifically stated in the Joint Application that Aqua will utilize LTA's existing customer rates, it is the Staff's understanding that this will occur based upon the language included in Paragraph 11 of the Joint Application. The Staff agrees that this should be done, and believes that this would best be accomplished by Aqua adding a service area description sheet and a rate sheet to its tariff applicable to LTA's service area, which will also necessitate the filing of a revised tariff index sheet. This approach will allow the Commission to cancel LTA's current tariff subsequent to the closing of the proposed transactions, which the Staff believes will be less confusing and more efficient with regard to tariff administration matters.

Regarding the matter of the transfer of LTA's certificate to Aqua or the issuance of a new certificate to Aqua for LTA's service area, the Staff believes that the Commission should act consistent with its past practices regarding this matter. The Commission has historically taken the position that certificates are not "transferable" and has thus cancelled the certificate of the seller and issued a new certificate to the buyer, with both actions normally set to be effective upon the closing of the asset transfer transactions. The Staff believes that this practice is appropriate and sees no reason to depart from that practice in this instance.

Regarding LTA's water supply and distribution system, the Staff notes that it is not aware of any specific deficiencies, capacity issues or service problems that need attention at this time.

Regarding Aqua's ability to operate LTA's system, the Staff notes that Aqua, along with its parent company and affiliated companies, own and are successfully operating a number of water and sewer systems under the Commission's jurisdiction and as such has demonstrated that it has the technical, managerial and financial resources necessary for the operation of LTA's system.

Regarding Aqua's compliance with regard to the regulations the Department of Natural Resources, and of this Commission, the Staff notes that Aqua generally has a good history of compliance with those regulations and that in those instances when problems are brought to its attention it normally responds in a timely and positive manner.

Lastly, the Staff notes that neither Aqua or LTA have any delinquencies with regard to their annual report submittals or their assessment payments, and also notes that neither company has any other matters pending before the Commission that would affect this case.

STAFF'S RECOMMENDATION

Based on the above, it is the Staff's position that the proposed asset transfer will "not be detrimental to the public interest", if certain conditions are placed on the Commission's approval of the Joint Application. Accordingly, the Staff recommends that the Commission issue an order that:

- 1) Authorizes Aqua to purchase the water supply and distribution assets of LTA, as those assets are described in the asset purchase agreements;
- 2) States that the approval of the subject asset purchase is based on the condition that the acquisition premium resulting from the proposed transactions will not be recovered through customer rates in the future;
- 3) Grants a certificate to Aqua authorizing it to provide water supply and distribution service in LTA's service area effective upon the closing of the asset transfer transactions;
- 4) Directs Aqua to file the tariff sheets necessitated by the asset transfer, as discussed in this Memorandum, with the proposed effective date of those sheets to coincide as closely as possible to the date of closing of the asset transfer transactions;
- 5) Directs Aqua to file a notice in this case advising the Commission as to when the closing of the asset transfer transactions takes place;
- 6) Relieves LTA of the obligation to provide service and cancels LTA's certificate and tariff effective upon the closing of the asset transfer transactions; and
- 7) Makes no finding that would bind the Commission or any other party to any ratemaking treatment of the actions related to approval of the Joint Application in any future proceeding, except as noted in item 2 above.