

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

In the Matter of the Application of Confluence Rivers)
Utility Operating Company, Inc., for Authority to) **File No. WA-2019-0299**
Acquire Certain Water and Sewer Assets and for a)
Certificate of Convenience and Necessity)

STAFF’S INITIAL POST HEARING BRIEF

COMES NOW Staff of the Missouri Public Service Commission, through counsel, and files its initial post hearing brief.

BACKGROUND

This case comes before the Commission for the second time for the limited purpose of providing the Commission with information regarding the net book value of the water and wastewater assets currently owned and operated by Port Perry Service Company, LLC (“Port Perry”).

Confluence Rivers Utility Operating Company, Inc. (“Confluence”) filed an application March 29, 2019, seeking authorization to acquire the Port Perry water and sewer assets and their accompanying certificates of convenience and necessity (“CCNs”). In its original *Memorandum*, Staff found that Confluence possesses the requisite technical, managerial, and financial (“TMF”) capacities to operate the systems and satisfies the requirements of the Tartan Factors.¹ Staff estimated the systems’ combined net book value as of March 31, 2019, to be \$58,133.² In summary, Staff stated

¹ *Memorandum*, P. 4 – 6 (May 31, 2019). The factors are referred to as the “Tartan Factors” or the “Tartan Energy Criteria.” *Report and Order*, In re Application of Tartan Energy Company, L.C., 3 Mo. P.S.C. 173 (Sept. 16, 1994), 1994 WL 762883. The Tartan Factors weigh (1) the need for service, (2) the utility’s qualification, (3) the utility’s financial ability, (4) the proposal’s feasibility, and (5) promotion of the public interest.

² *Memorandum*, P. 7 (May 31, 2019).

that Commission approval of the utilities' sale and transfer of the CCNs is not detrimental to the public interest and recommended approval.³

The first evidentiary hearing was held October 7 and 8, 2019. On February 13, 2020, following a discussion at its Agenda Meeting that same day, the Commission issued its *Order Setting Procedural Conference* requesting information regarding the net book value of the Port Perry assets and reopening the evidentiary record to receive additional testimony. Confluence filed its *Waiver Concerning Acquisition Premium* on March 4, 2020 stating that it would not seek to recover any acquisition premium⁴ in future rates.

Staff reviewed invoices Confluence provided to the parties and updated its calculation of the Port Perry assets' rate base as of December 31, 2019 to be \$79,262 (\$21,169 for the water assets and \$58,093 for the sewer assets).⁵ Staff met with the Office of Public Counsel ("OPC") to further refine the rate base, and all parties agree that the Port Perry assets' rate base as of December 31, 2019, is \$77,936 (\$20,070 for the water assets and \$57,866 for the sewer assets).⁶

A second evidentiary hearing was held on May 19, 2020, and the parties now file their initial post hearing briefs.

³ *Memorandum*, P. 9 – 10 (May 31, 2019).

⁴ "For regulatory purposes, an acquisition premium is simply the difference between the consideration that the purchaser pays for the assets and the net book value of those assets." *In re Utilicorp United Inc.*, 2004 WL 431561 (Feb 24, 2004).

⁵ *Memorandum*, P. 2 (Mar 24, 2020) and Ex. 800, *Direct Testimony of Kimberly K. Bolin*, P. 4:8 – 17 (Apr 14, 2020).

⁶ Ex. 800, *Direct Testimony of Kimberly K. Bolin*, P. 4:18 – 5:13 (Apr 14, 2020).

ISSUES

- 1. What is the net book value of the Port Perry Service Company’s (“Port Perry”) water and wastewater assets?**

All parties agree that the assets’ net book value as of December 31, 2019, is \$77,936 (\$20,070 for the water assets and \$57,866 for the sewer assets).⁷

- 2. Given the answer to the first question, should the Commission find that Confluence Rivers Utility Operating Company, Inc.’s (“Confluence Rivers”) acquisition of Port Perry Service Company’s (“Port Perry”) water and wastewater assets and certificates of convenience and necessary is not detrimental to the public interest, and approve the transaction?**

Yes. Given that Confluence does not request recovery of an acquisition premium,⁸ the calculated net book value of \$77,936 for the Port Perry assets does not cause the transfer of Port Perry’s water and wastewater assets and accompanying CCNs to Confluence to be detrimental to the public interest, and therefore, the Commission must approve this acquisition.

There is no evidence in the record that the Port Perry assets’ purchase price is unreasonable. ** _____

_____ . **⁹ Josiah Cox testified that Confluence has legitimate reasons to purchase the assets because their acquisition is consistent with the company’s mission

⁷ *Stipulation and Agreement as to Net Book Value* (Apr 9, 2020) and *Partial Objection of Lake Perry Lot Owners Association to Stipulation and Agreement as to Net Book Value* (Apr 10, 2020).

⁸ *Waiver Concerning Acquisition Premium* (Mar 4, 2020), Ex. 800, *Direct Testimony of Kimberly K. Bolin*, P. 5:20 – 6:3 (Apr 14, 2020), and Ex. 600, *NBV Rebuttal Testimony of Josiah Cox*, 4:6 – 18 (Apr 28, 2020).

⁹ **

_____ . ** Ex. 601C, *Recent Missouri Small Water and Sewer Transactions*. This exhibit was entered into evidence with no objection from any party.

to deliver safe drinking water and sewer service, and the acquisition premium is small compared to the assets of the parent company and Confluence.¹⁰ Further, Confluence has the financial capability to purchase the systems at the agreed upon price, and Confluence's owners will pay the acquisition premium, because it will be excluded from rates.¹¹ Should the Commission approve its application, Confluence will continue to charge Port Perry's Commission-approved 2002 rates under the current tariff until Confluence's next rate case.¹² At the next rate case, the agreed upon book value of \$77,936 will be the starting point for setting rate base.¹³

Consistent with the Commission's *In re UtiliCorp United Inc.* decision, there is no need for the Commission to speculate, as the Lake Perry Lot Owners Association

¹⁰ Chair Silvey: Mr. Cox, why does Confluence want to purchase the system if the net book value is so far below the sales price and the company has stated that it will not seek an acquisition premium?

Mr. Cox: Yes. Chairman Silvey, there are two reasons why we still want to do consummate this transaction. One is that Port Perry, is, you know, the typical type of system that we specialize in. They are under 500 individual connections. And really our company, our mission vision, is to bring safe and reliable water resources to every committee [sic] in the US. And small communities, particularly those under 500, they really represent the communities that are most at risk for a lack of safe and reliable service.

...

The second reason is we -- if you think about from a total company perspective, the delta between the net book value and the forward purchase price is, you know, 0.24 percent of our current investment in property plant and equipment. You know, from a Confluence Rivers standpoint it's 3.9 percent of our total investment of property, plant, and equipment.

And Confluence Rivers has continued to acquire systems under the same company. So we know that we have the wherewithal to deal with this system. We know that we are the right company to go provide safe and reliable service to these customers, so that's why.

Tr. 379:2 – 380:14.

Commissioner Holsman: ...I'm asking if it is possible for you to bolster the request in other ways that would make up the difference in the cost versus net book value?

Mr. Cox: No, Commissioner. None that I am aware of. Like I said before, the reason why we are willing to proceed with this transaction is it fits within our wheelhouse in terms of the type of communities that we are experts at serving and from an overall company perspective, the premium is such a small part of our overall company. Like I said, 0.24 percent of the overall company and only 3.2 percent of Confluence Rivers. So we don't have to -- there's no -- there's not an impetus on the company that they have to recover that. Tr. 384:10 – 21.

¹¹ Ex. 800, *Direct Testimony of Kim Bolin*, P. 5:20 – 6:6 (Apr 14, 2020) and Ex. 600 *NBV Rebuttal Testimony of Josiah Cox*, P. 4:20 – 5:10 (Apr 28, 2020).

¹² Ex. 800, *Direct Testimony of Kim Bolin*, P. 3:18 – 22 (Apr 14, 2020) and Ex. 600 *NBV Rebuttal Testimony of Josiah Cox*, P. 2:12 – 21 (Apr 28, 2020).

¹³ Tr. 406:18 – 22.

("Association") and OPC do, whether Confluence may attempt to recover the acquisition premium in an intangible manner. The Association and OPC misguidedly argue that the **price** Confluence will prospectively pay for the systems is detrimental, overlooking the fact that, should the Commission approve Confluence's Application, Port Perry customers will pay rates based on net book value, not on purchase price. Net book value is not the same as purchase price. The Commission has clearly made this distinction, stating that purchase price is not relevant if the company will not recover the acquisition premium in rates:

There is no evidence in the record by which the Commission could determine that the price UtiliCorp chose to pay to acquire SJLP was not reasonable. Much of UtiliCorp's interest in acquiring SJLP may have been based on unregulated properties and businesses over which the Commission has no authority. Indeed, since today's decision makes it clear that it is the responsibility of UtiliCorp's shareholders to pay any acquisition premium, there is no need for the Commission to determine whether the price that UtiliCorp chose to pay for SJLP is reasonable.

With the Commission having decided that UtiliCorp will not be allowed to recover any acquisition premium from its ratepayers, the existence of an acquisition premium cannot alter the Commission's evaluation of whether the merger would be detrimental to the public. Therefore, the Commission will reaffirm its determination from its initial Report and Order that the merger between UtiliCorp and SJLP is in the public interest because it is not detrimental to the public.¹⁴

The Association recognizes that Confluence will not seek to recover an acquisition premium, and its arguments based on a supposed acquisition premium of an "extremely inflated price" are, speculative, equivocal, and lacking in underlying evidentiary support.¹⁵ The Association believes that this intangible acquisition premium will be detrimental to

¹⁴ *In re UtiliCorp United, Inc.*, 2004 WL 431561 (1994) (on remand from *State ex rel. AG Processing, Inc. v. Public Service Commission*, 120 S.W.3d 732 (Mo. Banc 2003)).

¹⁵ Ex. 701, *Rebuttal Testimony of Richard DeWilde*, P. 4:11 (Apr 28, 2020).

the public interest, because it “might” cause Confluence to become overleveraged, jeopardize service, foster self-dealing, encourage gold-plating, and/or Confluence will unfairly spread the acquisition premium among all Confluence customers.¹⁶ But the Association presents no evidence that these things will actually occur, or even that they are likely to occur. The Association’s mere conclusions, offered without supporting evidence, speculating what it says “might” come to pass is not competent and substantial evidence.¹⁷

The evidence shows that Confluence has committed – unequivocally – to not recouping any acquisition premium.¹⁸ Confluence’s evidence that any acquisition premium is small compared to the overall size of the company and its investments in the system is supported by other evidence.¹⁹ That evidence supports Confluence’s evidence that it is both willing and able to deliver safe and reliable water and sewer service regardless of any acquisition premium. The net book value of the Port Perry systems does not alter the conclusion that the proposed acquisition is not detrimental to the public interest.

CONCLUSION

Staff’s initial estimate of the systems’ net book value was \$58,133.²⁰ After reviewing Confluence’s invoices and meeting with OPC, Staff recalculated net book value to be \$77,936.²¹ All parties agree to this net book value, which is more than 25% higher than

¹⁶ Ex. 700, *Rebuttal Testimony of Glen Justis*, P. 3:19 – 4:14 (Apr 28, 2020) and Tr. 415:7 – 417:10.

¹⁷ *State ex rel. Pub. Counsel v. Pub. Serv. Comm’n*, 289 S.W.3d 240, 254 (Mo. App. W.D. 2009).

¹⁸ *Waiver Concerning Acquisition Premium*, P. 3 ¶ 5 (Mar 4, 2020).

¹⁹ Tr. 384:10 – 21.

²⁰ *Memorandum*, P. 7 (May 31, 2019).

²¹ Ex. 800, *Direct Testimony of Kimberly K. Bolin*, P. 4:18 – 5:13 (Apr 14, 2020).

Staff's original estimate.²² The Association's and OPC's arguments about the effect of an acquisition premium on customer rates are inconsistent with their agreement to a net book value – the amount upon which future rates would actually be based. Moreover, a higher net book value further mitigates the already-small size of any acquisition premium compared to the overall size of the company and its investments in the system.

The Association and OPC confuse purchase price and net book value. Because the Commission will not allow Confluence to include an acquisition premium in rates, the assets' net book value does not create a detriment. The Missouri Court of Appeals stated in *State ex rel. Fee Fee Trunk Sewer, Inc. v. Litz* that the “[t]he Commission may not withhold its approval of the disposition of assets unless it can be shown that such disposition is detrimental to the public interest.”²³ This evidence of net book value, combined with Staff's analysis of the TMF capacities and the Tartan Factors, make plain that Confluence's acquisition of the Port Perry systems and CCNs is not detrimental to the public interest, and the Commission must approve the transaction.

Respectfully submitted,

/s/ Karen E. Bretz

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²² *Stipulation and Agreement as to Net Book Value* (Apr 9, 2020) and *Partial Objection of Lake Perry Lot Owners Association to Stipulation and Agreement as to Net Book Value* (Apr 10, 2020).

²³ *State ex rel. Fee Fee Trunk Sewer, Inc. v. Litz*, 596 S.W.2d 466, 468 (Mo. App. E.D. 1980) (citing *State ex rel. City of St. Louis v. Public Service Commission of Missouri*, 73 S.W.2d 393, 400 (Mo. Banc 1934)).

CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing have been electronically mailed to all parties and/or counsel of record on this 2nd day of June, 2020.

/s/ Karen E. Bretz