

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

In the Matter of the Application of)
Environmental Utilities, LLC for)
Permission, Approval, and a Certificate of)
Convenience and Necessity Authorizing it)
to Construct, Install, Own, Operate,)
Control, Manage and Maintain a Water)
System for the Public Located in)
Unincorporated Portions of Camden)
County, Missouri (Golden Glade)
Subdivision).)

Case No. WA-2002-65

STAFF'S REPLY BRIEF

COMES NOW the Staff of the Missouri Public Service Commission and, for its Reply Brief, states to the Missouri Public Service Commission as follows:

I. Introduction

The Staff argued in its Initial Brief that the Commission should grant the certificate of convenience and necessity that Environmental Utilities (“Environmental” or “Company”) has requested, provided that certain conditions are met, which will insure that the Company’s proposal is economically feasible, and that the Company complies with the requirements of the Missouri Department of Natural Resources.

For the most part, the Office of the Public Counsel and the Company agreed with this position in their Initial Briefs. The OPC expressed some reservations, but said Environmental has minimally satisfied the first four requirements for a certificate,¹ and said that the Commission should grant a certificate if the Company satisfies a long list of conditions. The Company said, without reservation, that it is qualified, but agreed to accept the conditions that the Staff and the Public Counsel have asked the Commission to impose.

¹ OPC Initial Brief, page 5.

Intervenor Hancock Construction Company, on the other hand, expressed unqualified opposition to the application. Hancock contends that the Company does not satisfy any of the five *Tartan Energy*² criteria. Hancock emphasizes the poor record-keeping and poor management practices of Osage Water Company, an entity that is closely related to Environmental.

In this brief, the Staff will first, and most extensively, respond to the arguments in Hancock's Initial Brief, and will then briefly address the arguments in Environmental's Initial Brief and in Public Counsel's excellent Initial Brief.

II. Reply to the Initial Brief of Hancock Construction Company

A. Hancock's Position as Stated in its Initial Brief.

The Initial Brief of Intervenor Hancock is almost undecipherable. The Staff opposes most of the points that Hancock attempts to make, but finds it very difficult to respond to an argument that it does not understand. At the risk of making clear the incomprehensible argument of another party whom the Staff generally opposes, the Staff will first attempt to summarize Hancock's arguments, as the Staff understands them, and then respond to the principal points therein.

As the Staff understands it, Hancock's argument is essentially as follows: Osage Water Company, an entity that is closely related to Environmental, is near bankruptcy, because of poor management by its principals; Greg Williams was one of the principal managers of Osage, and will be a principal manager of Environmental; in fact, the management of Environmental will be substantially the same as the management of Osage; Mr. Williams's demonstrated inability to manage Osage has been "inherited" to Environmental; and to the extent that the management of Environmental is different from the management of Osage, it will be provided by Debra

² See *Application of Tartan Energy Company*, 3 Mo. P.S.C. 3d 173 (1994).

Williams, who has already demonstrated that she is a poor manager. Hancock especially emphasizes that Osage, and therefore Mr. and Mrs. Williams, have been particularly poor at record-keeping and compliance with NARUC's Uniform System of Accounts, and that they have been litigious, used illegal operations, and had an impervious attitude toward the Commission's authority, and that as a result, Environmental will also be poor at record-keeping, and will also be litigious, engage in illegal operations, and have an impervious attitude toward the Commission's authority.

As the Staff understands it, Hancock also argues that Osage is – or at least ought to be – in competition with Environmental, and that Osage's best interest would be served if the Commission would authorize – or require – Osage to provide water service to the Golden Glade Subdivision. Hancock further suggests that, in this case at least, doing what is in the best interest of Osage would also be in the best interests of Osage's customers and of Osage's creditors, specifically including Hancock itself. Hancock makes this suggestion even though Osage has neither applied for a certificate nor given any other indication that it wants to serve Golden Glade. And in making this argument, Hancock seems to overlook all of the management shortcomings that would be “inherited” from Osage to Environmental.

B. Overview of Staff's Response.

Hancock's baffling argument seems to be essentially as follows: Osage is poorly managed, and if the certificate is granted, Environmental will be just as poorly managed; therefore the Commission should grant – or require – Osage to serve this new service territory, Golden Glade Subdivision.

Hancock appears to contend that Environmental is in competition with Osage; that if a disinterested third party were managing Osage, Osage would seek to provide water service to

Golden Glade; and that since Osage has failed to do so or to intervene in this case, the Commission should reject Environmental's application, in order to protect Osage and its customers.

The basic flaw in this argument is that Osage is not in competition with Environmental. *Black's Law Dictionary, 7th Edition* defines "competition" as follows: "The effort or action of two or more commercial interests to obtain the same business from third parties." Thus competition only occurs when two entities want the same business. In this case, Osage obviously does not want the business that Environmental now seeks, and there is no competition for the sale of water to Golden Glade.

Osage is owned by Greg Williams and William P. Mitchell. Environmental is owned by Greg Williams and Debra Williams. Although there is some similarity in the ownership, the ownership is not identical. Furthermore, the economic circumstances and management dynamics of the two companies are significantly different. Mr. Mitchell's views may differ from Ms. Williams' views. It would not be surprising if Osage and Environmental have different business plans, and do not seek the same customers. Osage does not want to serve Golden Glade, and the Commission cannot force them to.³ There is no competition to sell water in Golden Glade.

The Commission should also note that Hancock's Initial Brief is loaded with statements that do not cite the record at all and appear unsupportable,⁴ or for which the cited portion of the record does not appear to support Hancock's statement.⁵

³ As the well-know baseball philosopher Yogi Berra once said: "If the people don't want to come out to the ball park, you can't stop them."

⁴ See, for example, the following: "This is a less expense (*sic*) alternative available to them" (Hancock Initial Brief, page 2); "He still maintains control after the departure of Mr. Mitchell through his surrogate, Mrs. Williams" (page 2); "The Commission also relied on assurances that O.W.C. would use this well, distribution mains, excavator and bobcat to serve Eaglewood (*sic*) customers" (page 6); Golden Glade customers "are already being served by O.W.C." (page 6); Mr. Williams is the "sole management voice" of Osage (page 7); and "there appears to be additional problems with the reporting and cost sharing of equipment between O.W.C. and E.U." (page 9).

C. The *Tartan Energy* Criteria.

The legal standard for granting certificates of convenience and necessity was established in *Application of Tartan Energy Company*, 3 Mo. P.S.C. 3d 173, and has been consistently followed since 1994. *Tartan Energy* identified five criteria, which were identified as Issues 1 through 5 in the List of Issues that the parties filed in this case. Hancock's Initial Brief pays little heed to these issues, however, but argues, with respect to each of them, that Environmental fails to satisfy the criteria because of Osage's poor record-keeping and inadequate management.

The Staff is indeed concerned about Environmental's record-keeping and management, but believes that the Company satisfies the *Tartan Energy* criteria, and that these concerns can best be addressed by granting the application for certificate, if certain conditions are satisfied.

An issue-by-issue analysis of Hancock's arguments on the five *Tartan Energy* criteria follows.

1. The Need for Service. Hancock's brief discussion of this issue dealt primarily with record-keeping, which, as far as Staff knows, is not relevant to the determination of whether there is a need for service. Hancock did say, however, that Golden Glade's eight customers⁶ "are already being served by O.W.C. or if they should so chose (*sic*) Golden Glade's own homeowner's association."

The first part of that statement is untrue. Osage is not providing service to the residents in Golden Glade Subdivision; the residents there receive service from individually owned wells.

⁵ See, for example, the following: O.W.C. "has worked hard to circumvent adherence to administrative regulations and orders historically" (Hancock Initial Brief, pages 3-4); the Hancock Debenture "was further explained to be in the rate base by Keith R. Krueger, Esquire, Deputy Counsel for P.S.C." (page 5); and "Staff has confirmed Mr. Williams (*sic*) incompetence" (page 7).

⁶ There are actually no "customers" in Golden Glade. There are, in fact, now eight residences in Golden Glade, but the residents there are not customers of anyone. They are served by individually owned wells, or multi-family wells. These residents are, of course, potential customers of any water corporation that receives a certificate of authority to serve the subdivision.

The second part of the statement is slightly misleading. The residents in Golden Glade cannot choose to be served by the homeowners association, unless Mr. and Mrs. Williams agree, because the Williamses own the existing well and control the homeowners association. It does appear, however, that if the Commission does not grant a certificate to Environmental, the homeowners association will provide service to these customers; in fact, the covenants and restriction of the Golden Glade Subdivision require residents to connect to a central water system. There is, nonetheless, a need for service, because if the Commission grants Environmental's application, the residents of the subdivision would enjoy the additional advantage of receiving water service from a regulated company.

2. Applicant's Qualifications. Hancock contends that Environmental is not qualified to operate a water system to serve Golden Glade, because a closely related entity, Osage Water Company, has been losing customers in some of the service territories that it now serves. "These lost customers and revenue are due solely (*sic*) to Mr. Williams' incompetence, misrepresentations, illegal, illusionary and hazardous operations combined with his ongoing callous disregard for the public," Hancock says.⁷ Hancock also says that Mr. Williams has made "all policy decisions" for Osage since 1994,⁸ and characterizes him as the "sole management voice" for Osage.⁹ Hancock's reasoning is that, because Greg Williams has unsuccessfully managed Osage, it is reasonable to conclude that he will unsuccessfully manage Environmental, and that Environmental is therefore not qualified to serve Golden Glade.

The record, however, reveals that William P. Mitchell, not Greg Williams, was in charge of the day-to-day operation of Osage until July 7, 2001, when Debra Williams assumed those duties. The record also reveals that the management of Osage has improved since Ms. Williams

⁷ Hancock Initial Brief, page 7.

⁸ Hancock Initial Brief, page 7.

assumed control of the day-to-day operations. Ms. Williams will also be in charge of the day-to-day operations of Environmental Utilities.

Although Mr. Williams was an officer, director, and attorney for Osage, one cannot properly blame him for all of Osage's problems. And even if he did mismanage Osage, one cannot properly assume that he will also mismanage Environmental, because Debra Williams will be primarily responsible for the management of the Company.

The Staff submits that the problems that Osage has experienced are certainly relevant to this proceeding, because Environmental is closely related to Osage; and it is reasonable to believe that Environmental's management will be similar to Osage's. But one must not overlook the fact that the applicant in this case is Environmental, not Osage.

For the reasons stated in Staff's Initial Brief, Environmental possesses the qualifications that are needed to provide water service to the Golden Glade Subdivision.

3. Environmental's Financial Ability to Provide Service. Most of Hancock's discussion of the "financial ability" criterion would more properly be addressed in the discussion of Issue No. 2 (regarding the qualifications of the applicant).

Hancock here addresses (again) Osage's "dismal" record-keeping, and its failure to timely file annual reports, as required by the Commission. The Staff is certainly concerned about Environmental's record-keeping and its filing of annual reports. But it is impossible to see how Hancock's discussion of these matters sheds any light on Environmental's ability to finance its proposal to serve the Golden Glade Subdivision. Furthermore, the discussion in Hancock's brief pertains only to Osage's compliance with record-keeping and filing requirements, rather than Environmental's compliance. There is reason to believe that Environmental's performance in this regard will be better than Osage's has been.

⁹ Hancock Initial Brief, page 7.

Hancock also points to a difference of about one million dollars between the value of the assets that Osage showed on its annual reports for 1998 and 1999 and the amount of assets that were included in Osage's rate base in its most recent rate case. Hancock incorrectly described this as a "discrepancy" or a "disagreement" between Osage and the Staff. In fact, it is not a discrepancy, because the figure that is shown on the annual reports is not supposed to represent rate base, and it is not surprising that the amounts would not be the same. Furthermore, even if there is a discrepancy, the discrepancy pertains to Osage, not Environmental, and it is not relevant to the question of whether Environmental is able to finance its proposal.

Environmental does not require additional financing to provide water service to Golden Glade. Its proposal is therefore financially feasible.

4. Economic Feasibility of the Proposal. As the Staff understands this *Tartan Energy* criterion, an applicant's proposal is considered economically feasible if, by charging its customers just and reasonable rates, the applicant would be able to fully recover its cost of service, including a reasonable return on equity.

However, in its Initial Brief, Hancock gives little attention to whether Environmental can recover the cost of serving its customers. Instead, Hancock argues that engineers (not accountants) must determine whether the applicant's water plant is sufficient, points out that its witness, Bill Cochran was once successful in excluding some plant from Kansas City Power and Light's rate base, and again asserts that Osage's record-keeping is deficient. Those facts are interesting, but none of them is relevant to the question of whether Environmental's proposal is economically feasible.

Hancock does state that eight customers cannot support a \$76,000 water system. The Staff would agree. However, this also is beside the point, for Environmental has never proposed

to serve only eight customers with this system. What Environmental proposes is to serve the 50 residences in Golden Glade with this system (when the subdivision is fully developed), and in addition, to sell water at wholesale to Osage for use by the customers in Eagle Woods Subdivision. It is quite common, in fact it is the norm, for a water company to receive a certificate of authority to provide service to a service territory before the area is fully developed, or even before development begins.

The Staff does agree with Hancock, however, that Environmental's proposal depends upon obtaining an agreement to sell water to Osage at wholesale for use in Eagle Woods. In fact, it is essential that Environmental obtain such an agreement, and provide it to the Commission before a certificate is issued to the Company.

5. The Public Interest. Hancock's brief argument on this last *Tartan Energy* criterion is essentially a reiteration of its claim that the principals of Environmental are not qualified to provide the water service that Environmental seeks to provide. As such, it is properly analyzed under Issue No. 2. For the reasons expressed at pages 4-5 of its Initial Brief, the Staff submits that Environmental is qualified to provide service to Golden Glade, if it obtains a permit to dispense prior to providing service to the residents of the Golden Glade Subdivision.

D. Other Issues on the List of Issues.

The parties to this case agreed to include three additional issues on the List of Issues in this case. Those issues involved: the amount of investment to include in rate base, whether conditions should be imposed on the Applicant, and whether any proposed tariffs should be withdrawn. Hancock did not address any of those issues in its Initial Brief, so no response is necessary. Nor did Hancock even address any of the four additional issues that it, alone, sought

to include on the List of Issues. There is therefore no need to supplement Staff's discussion of any of these seven issues, which appears at pages 8-12 of Staff's Initial Brief.

III. Reply to Briefs of OPC and Environmental Utilities

With a few exceptions, the Staff agrees with most of the points that Environmental makes in its Initial Brief. The Staff agrees that, if the Company produces an executed agreement for the sale of water to Osage for distribution to the residents of Eagle Woods, on terms that are satisfactory to the Commission, and if it obtains from the Missouri Department of Natural Resources a permit to dispense, the Company will satisfy each of the five *Tartan Energy* criteria.

The Company has, however, conveniently overlooked the difficulty that Osage has had in complying with Commission requirements and in providing satisfactory service to its customers. These problems are not insignificant. Environmental is, indeed, different from Osage, with somewhat different management. However, the claim that Greg and Debra Williams played no role in the management of Osage, despite being stockholders, officers, directors, and attorney for Osage, is not credible, and the Commission should justly be wary of claims that everything will be fine, because now Debra Williams will be in charge of Environmental. To guard against a repeat of the kind of problems that Osage has experienced, it is reasonable for the Commission to impose conditions upon the granting of a certificate to Environmental.

In their briefs, the Staff, Company, and Hancock have all emphasized a point-by-point analysis of the *Tartan Energy* criteria. Although the Office of the Public Counsel has also addressed each of the *Tartan Energy* criteria, its Initial Brief places primary emphasis on the conditions that should be imposed upon Environmental if the Commission grants Environmental's application for a certificate. OPC's analysis is very thorough and excellent, and the Staff supports it in every respect. In addition, Environmental stated in its Initial Brief that is

“has agreed that the conditions proposed by OPC and by Staff in their testimony and position statements are reasonable and appropriate under the circumstances.”¹⁰ As noted above, Hancock did not address the issue of conditions (Issue No. 7) in its Initial Brief. The Commission should therefore impose the conditions as proposed in OPC’s Initial Brief.

The Company has maintained throughout this case, and has again argued in its Initial Brief, that it should be allowed to include in rate base an additional 10% for a “general contractor’s fee.” There is no precedent for including such a sum in the rate base, and the Company included in its Initial Brief only a single, unpersuasive sentence in support of this claim. If the Commission finds it necessary to rule on this issue at this time, Environmental’s claim should be rejected.

IV. Summary

Hancock’s Initial Brief is rambling and unpersuasive. It addresses only Issues 1-5 (the *Tartan Energy* criteria), and seems to regard each of those five issues as a question about Environmental’s record-keeping and management. This argument should be rejected.

There is good cause for concern about Osage’s record-keeping and management. However, Environmental does satisfy each of the five *Tartan Energy* criteria, and the Commission should grant the certificate of convenience and necessity, at such time as the Company provides to the Commission proof that it has executed a wholesale contract for water service to the Eagle Woods Subdivision, and for the sharing of equipment with Osage. The Commission should also impose the other conditions proposed by Staff and by the Public Counsel, and should require the Company to obtain from the Department of Natural Resource a permit to dispense before it provides water service on a retail or wholesale basis.

¹⁰ Initial Brief of Environmental Utilities, L.L.C., at page 8.

Finally, the Commission should make it clear that the certificate that it issues in this case is granted because of the particular circumstances of this case, and that if Environmental again applies for a certificate of authority, that it will be again subjected to strict scrutiny as to whether it satisfies the *Tartan Energy* criteria.

WHEREFORE, the Staff prays that the Commission approve Environmental's application and issue a certificate of convenience and necessity at such time as Environmental complies with the foregoing conditions.

Respectfully submitted,

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Certificate of Service

I hereby certify that copies of the foregoing have been mailed or hand-delivered to all counsel of record this 14th day of May 2002.

/s/ Keith R. Krueger

Keith R. Krueger