

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

In the Matter of Missouri-American Water)
Company's Request for Authority to)
Implement General Rate Increase for Water)
and Sewer Service Provided in Missouri)
Service Areas)

Case No. WR-2022-0303

MOTION FOR PRODUCTION OF DOCUMENTS PURSUANT TO § 386.450 RSMO.

Comes now the Office of the Public Counsel (the “OPC”) and pursuant to § 386.450 RSMo.¹ respectfully states as follows:

The OPC requests that the Public Service Commission of the State of Missouri (the “Commission”) require American Water Works Company, Inc. (“American Water”) to produce documents responsive to the data requests attached to this motion as Exhibit A no later than February 16, 2023. As required by § 386.450 RSMo., good cause exists to grant this request because this information is vitally important to this general rate case. Specifically, the OPC requires this information to evaluate the financing arrangements between American Water and its subsidiaries, including Missouri American Water Company (“MAWC”). The OPC will use this information to evaluate the merits of each parties’ (including its own) recommended ratemaking capital structures, and resulting rate of return (“ROR”) recommendations. The appropriate capital structure and corresponding ROR are issues that the Commission must determine in this case. Therefore, the importance of this information serves as the good cause necessary to grant this request.

¹ The OPC does not bring this Motion pursuant to 20 CSR 4240-2.090. However, to the extent that the Commission determines that the requirements of 20 CSR 4240-2.090 apply, the OPC has attempted to obtain this information from Missouri American Water Company (“MAWC”). MAWC has either objected to the requests or not provided the requested information. The OPC addressed several of these concerns during the January 12, 2023 Discovery Conference with MAWC, the presiding regulatory law judge, and the Staff of the Commission.

I. Background

A. The Importance of Capital Structure

“Capital structure represents how a company finances its assets.” (Murray Direct Testimony 39, Doc. 78). “The typical capital structure consists of common equity, long-term debt, and short-term debt.” (*Id.*). However, in some circumstances, it may be appropriate to exclude consideration of short-term debt. (*Id.* 39-40).

In a general rate case, the Commission determines the appropriate capital structure and then uses that capital structure to determine the utility’s appropriate ROR. (*See id.* 40).

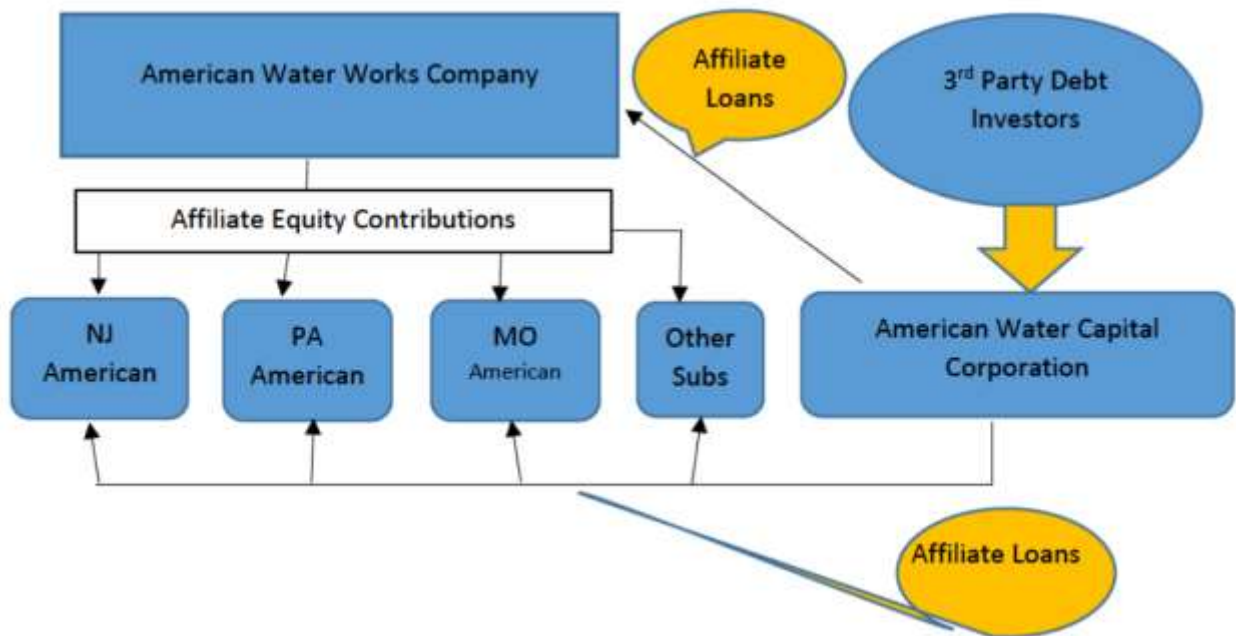
B. American Water’s Financial Relationship to MAWC

American Water is MAWC’s parent company. (*Id.* 2). In addition to MAWC, American Water operates regulated subsidiaries in several other states, including, but not limited to, Pennsylvania, New Jersey, Iowa, Virginia, West Virginia, and Indiana. (*See* Watkins Rebuttal Test. 7, Doc. 109).

American Water also has a “financing subsidiary,” known as American Water Capital Corporation (“AWCC”). (Murray Direct Test. 21 n.28). AWCC was “created for purposes of accessing third-party debt markets.” (*Id.*). It “issues long-term and short-term debt directly to third-parties on behalf of American Water and its subsidiaries.” (*Id.* 41). AWCC’s “credit rating and cost of debt is based on American Water’s consolidated credit profile.” (*Id.*). American Water’s consolidated credit profile “includes the business risk of its regulated utility subsidiaries and the total amount of debt it issues to finance the subsidiaries (whether it is through direct affiliate loans or indirect investment through loans to American Water to purchase equity in its subsidiaries).” (*Id.* 41-42).

This corporate structure allows “American Water . . . to take advantage of very low debt capital costs by issuing significant amounts of debt through its financing subsidiary, AWCC.” (*Id.*

40 (footnote omitted)). American Water then “provides most of the debt capital it raises through AWCC at cost to its subsidiaries, including MAWC.” (*Id.*). However, “approximately 29% of this debt is loaned to American Water, which then uses this debt capital to purchase equity in its subsidiaries.” (*Id.*). Doing so, “allows American Water to achieve a much higher ROR than its cost of capital” because “equity capital is allowed a much higher return than the cost of the debt capital used to purchase subsidiary equity.” (*Id.*). The OPC’s witness, Mr. David Murray, provides the following graphical representation of American Water’s financing strategy (*Id.* 41):



C. The Dispute Regarding Appropriate Capital Structure in the Instant Case

In this general rate case, at least two positions exist regarding what capital structure the Commission should utilize in determining MAWC’s ROR.

First, MAWC recommends that the Commission use MAWC’s capital structure. (Merante Direct Test. 10, Doc. 14; Swiz Rebuttal Test. 4, Doc. 116²). Specifically, the “capital structure

² In his Rebuttal Testimony, Mr. Swiz adopts Mr. Merante’s Direct Testimony. (Swiz Rebuttal Test. 3). He maintains that if he were “asked the same questions as those asked in Mr. Merante’s Direct Testimony,” his responses would be the same, with one exception related to “the role that [he] play[s] regarding MAWC’s debt financing.” (*Id.*)

that finances MAWC’s rate base and operations for setting rates in this case.” (Merante Direct Test. 10). MAWC maintains that it “is a stand-alone business enterprise with independent state operations, capital investments, management, and corporate governance.” (Swiz Rebuttal Test. 4). MAWC also asserts that its “stand-alone capital structure appropriately reflects its distinct risk profile, which . . . is unlike the business and financial risks of American Water.” (*Id.* 5).

Alternatively, the OPC recommends that the Commission use a capital structure that “is consistent with American Water’s average quarterly consolidated capital structure, net of short-term debt, for the period June 30, 2021 through June 30, 2022.” (Murray Direct Test. 40). The OPC’s recommended capital structure “best represents the amount of debt capacity American Water considers reasonable and appropriate for its regulated utility assets, including those of MAWC.” (*Id.*). Further, “[u]se of this capital structure ensures that MAWC’s ratepayers receive credit for their contribution to American Water’s debt capacity, which is much higher than that reflected on MAWC’s internally-managed balance sheet.” (*Id.*). The OPC points out that MAWC’s capital structure does not exhibit the same characteristics of Missouri’s other major utility subsidiaries and that “MAWC does not issue its own long-term debt, short-term debt or common equity directly to third-parties.” (*Id.* 41). Mr. Murray explains how American Water has controlled the amount of leverage shown on MAWC’s balance sheet. (*Id.* 42).

D. The Discovery Requests

As explained in Mr. Murray’s memorandum, attached as Exhibit B, the OPC requests the information identified in the attached data requests from American Water so that the OPC can investigate MAWC’s requested ROR in this case, as well as MAWC’s position that MAWC is financially independent from American Water. (Ex. B “Murray Memorandum” 1).

For example, MAWC asserts that the Commission should find that the appropriate capital structure to use to set its ROR is one that is consistent with MAWC's independent capital structure. (*See* Merante Direct Test. 10, Swiz Rebuttal Test. 4). Mr. Murray explains in his memorandum that in order to verify MAWC's claims of financial independence, the OPC must have access to American Water's books and records, including American Water's Board of Director materials and the Board of Director's Audit, Risk and Finance Committee materials. (Murray Mem. 1). This will allow the OPC to compare American Water's corporate governance standards, financing strategies, and considerations to the MAWC Board of Directors' materials to assess MAWC's claims of financial independence and its request for a higher cost of capital than American Water. (*Id.* 1-2).

Similarly, as explained above and in Mr. Murray's memorandum, American Water or AWCC raise nearly all of the capital used to fund MAWC's assets. (*Id.* 2). American Water intends to raise significant amounts of common equity in 2023. (*Id.*). This will affect American Water's capital structure and cost of capital, which impacts the ROR American Water requests MAWC's ratepayers fund through the requested rate increase. (*Id.*). Therefore, the OPC needs information related to this planned common equity issuance such as, but not limited to, copies of all investment bank/financial advisor presentations and information regarding when and in what amount American Water plans to issue the common equity.

The information responsive to these discovery requests is similar to that requested from other Missouri utilities, including Ameren Missouri,³ Spire Missouri, Evergy Metro, and Evergy Missouri West. (*Id.* 1).

³ For instance, in Staff Data Request 0001, Staff requested, in part,

Ameren Corporation and Ameren Missouri Board of Directors' meeting minutes, Board of Director Committee meeting minutes, all related reports, documents and all accompanying materials or

II. Legal Authority

Section 386.450 RSMo. grants the Commission, at the request of the OPC, the power to require “any corporation” to produce within the State of Missouri “any books, accounts, papers or records kept by said corporation . . . in any office or place within or without this state . . . so that an examination thereof may be made by the public counsel” The Commission has determined that § 386.450 RSMo. “is broader than the general right to discovery allowed under Missouri’s rules of civil procedure.” *In re Elm Hills Util. Operating Co., Inc.’s Request for a Water & Sewer Rate Increase*, Case No. WR-2020-0275, Order Granting Mot. for Production 2, Doc. 48 (hereinafter “*Elm Hills Order*”). The Commission “has consistently interpreted this statute broadly, given the unique grant of investigative power bestowed upon OPC and the Commission by the Missouri General Assembly via this statute.” *Id.* 2-3 (footnote omitted).

The Commission has previously addressed an OPC discovery request made in the context of a general rate case related to information that affects the Commission’s consideration of capital structure. *See generally id.* In that case, the Commission stated that § 386.450 RSMo. “unambiguously allows for the production of out-of-state records” and “has no requirement that the subjects be jurisdictional utilities.” *Id.* 3. The Commission also noted that the statute “imposes no requirement of exhaustion of remedies.” *Id.* Further, the Commission recognized that § 386.450 RSMo. “does not express a relevance requirement.” *Id.* 4. However, the Commission addressed relevance because the OPC made its request in the context of a general rate case and not a separate investigation. *See id.*

handouts presented or distributed (whether electronic presentations or materials in hardcopy format or provided via an electronic document system for board members) pertaining to Ameren Corporation, Ameren Services, and Ameren Missouri electric operations for the period covering April 1, 2021 through June 30, 2022 and through December 31, 2022, when available.

(Case No. ER-2022-0337, Staff Data Request No. 0001).

In regards to relevance, the Commission stated “[r]elevance can be established by a showing of the connection of OPC’s requested information to this file” *Id.* The Commission maintained that the case, which was also a general rate case, “as a matter of course involve[d] apportionment of capitalization, which involves assessments of capital structure.” *Id.* It recognized that it “is expressly required to examine the dealings of regulated entities with their unregulated affiliates, and specifically to ‘inquire as to, and prescribe the apportionment of, capitalization, earnings, debts and expenses.’” *Id.* (citing § 393.140(12) RSMo.). Therefore, the Commission found that the information sought was relevant. *Id.*

When addressing § 386.450 RSMo.’s good cause requirement, the Commission further addressed the relevance of the information to the proceeding. *Id.* 7, 9. It concluded that the importance of the information formed sufficient good cause to grant the OPC’s motion in that case. *Id.* 7. To support these conclusions, the Commission relied on its statutory duty to ensure “just and reasonable” rates, which includes “an evaluation of the capital structure (funding)” of the utility. *Id.* 7-9. The Commission then explained how it used the identified capital structure to set rates and how a corporate structure could be used to manipulate a subsidiary’s capital structure to inflate rates. *Id.* Because the information sought by the OPC in that case affected the Commission’s decision regarding the appropriate capital structure, the Commission found that the OPC’s motion was relevant and that good cause existed “in carrying out OPC’s (and the Commission’s) statutory duties with respect to [the utility] and the apportionment of its capitalization, earnings, debts, and expenses.” *Id.* 9. Therefore, the Commission granted the OPC’s motion and required the identified entities to produce the requested information. *Id.*

III. Analysis

The OPC requests that the Commission, pursuant to its powers set forth in § 386.450 RSMo. issue an order requiring American Water to produce documents and information in response to the OPC's data requests attached to this Motion as Exhibit A.

In these data requests, the OPC seeks information that will help it to evaluate American Water's financing arrangements, which will, in turn, allow the OPC to examine American Water's capital structure. (*See generally* Murray Mem.). This information may provide evidence that assists the Commission with evaluating the credibility of each party's ROR recommendations in this case. (*See id.*). It will also allow the OPC and the Commission to verify MAWC's claims of independence. (*See id.*).

Although § 386.450 RSMo. "does not express a relevance requirement," the Commission addressed relevance in a similar circumstance and concluded that relevance can be established when the information sought is connected to the proceeding. *Elm Hills* Order 4. Similar to *Elm Hills*, the information sought in response to the attached data requests is relevant because it is connected to this general rate case. *See id.* As the Commission found in *Elm Hills*, this general rate case will "as a matter of course involve apportionment of capitalization, which involves assessments of capital structure." *Id.* Further, the Commission is "statutorily required to ensure that [a utility's] rates are just and reasonable." *Id.* 7 (citing § 393.130 RSMo.). This statutory duty "includes an evaluation of the capital structure (funding) of" the utility. *Id.* As Mr. Murray explains in the attached memorandum, the information requested will allow the OPC to evaluate American Water's financing of MAWC and will allow the OPC to investigate MAWC's claims of independence. (*See* Murray Mem.). Therefore, for this and all of the reasons discussed in Mr.

Murray's memorandum, the information sought by the attached data requests is relevant to this proceeding.

As to § 386.450 RSMo.'s good cause requirement, the Commission has concluded that good cause exists to grant the OPC's request under § 386.450 RSMo. when the information sought is important to the case at hand, such as when the information relates to capital structure and the request is made in the context of a general rate case. *Elm Hills* Order 7-9. The OPC makes this request in the context of MAWC's pending general rate case and, as explained above and in Mr. Murray's memorandum, this information relates to the appropriate ratemaking capital structure. (*See generally* Murray Mem.). This will directly affect the appropriate ROR, which, as the Commission has recognized, affects the Commission's decision regarding "just and reasonable" rates. *See Elm Hills* Order 7-9 (explaining how capital structure is used in setting a utility's rates). Similar to *Elm Hills*, for the same reasons that the OPC's requests are relevant to this proceeding, good cause also exists. *See id.* 9.

For these reasons, the OPC requests that the Commission grant this motion and order American Water to provide documents and information responsive to the data requests in Exhibit A.

IV. Conclusion

WHEREFORE, the Office of the Public Counsel respectfully requests the Commission grant this Motion and, pursuant to its authority under § 386.450 RSMo., order American Water to provide documents and information responsive to the data requests in Exhibit A no later than February 16, 2023.

Respectfully submitted,

/s/ Lindsay VanGerpen
Lindsay VanGerpen (#71213)
Associate Counsel

Missouri Office of the Public Counsel
P.O. Box 2230
Jefferson City, MO 65102
Telephone: (573) 751-5565
Facsimile: (573) 751-5562
E-mail: Lindsay.VanGerpen@opc.mo.gov

CERTIFICATE OF SERVICE

I hereby certify that copies of the forgoing have been mailed, emailed, or hand-delivered to all counsel of record this 3rd day of February 2022.

/s/ Lindsay VanGerpen