

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

In the Matter of Elm Hills Utility Operating)
Company, Inc's Request for a Water and)
Sewer Rate Increase) File No. WR-2020-0275

ELM HILLS' RESPONSE TO OPC'S MOTION TO DISMISS

COMES NOW Elm Hills Utility Operating Company, Inc. (Elm Hills or Company), by and through the undersigned counsel, and for its response to the Office of the Public Counsel's (OPC) *Motion to Dismiss Case or Provide Other Relief in the Alternative (Motion to Dismiss)*, filed on December 2, 2020, states as follows to the Missouri Public Service Commission (Commission):

ELM HILLS HAS COMMITTED NO VIOLATION OF STATUTE, RULE, OR ORDER

1. The *Motion to Dismiss* requests the Commission sanction Elm Hills by either dismissing its pending rate case, suspending the current procedural schedule until entities that are not parties to this case (i.e. not Elm Hills) respond to the Commission's *Order Granting Motion for Production*, or striking all testimony filed by Elm Hills in this case. (Motion to Dismiss, para. 31-33). Significantly, the *Motion to Dismiss* contains no allegation that Elm Hills itself has violated any statute, or Commission rule or order and, further, contains no suggestion, and no reasonable implication, that the records/information sought by OPC are in Elm Hills' possession or control.

2. The power and control in a corporate structure flows down, and not up, the corporate chain. This Commission has stated as follows in regard to a previous examination of this type of situation:

As to Staff's suggestion that Missouri-American should be required to attempt to obtain the information Staff seeks on the theory that, as an affiliate or subsidiary, Missouri-American enjoys superior access to the information in question, such superior access is an assumption and has not been demonstrated. Certainly, Missouri-American has no legal authority to obtain information and documents from its corporate parent and affiliates. An order requiring Missouri-American to attempt to acquire the information and documents from its parent and affiliates is likely to be unworkable in practice.

In the Matter of Missouri-American Water Company's Tariff, et al., Case No. WR-2003-0500, 2003 Mo. PSC LEXIS 1552, *19 (Mo. P.S.C. December 2, 2003) (emphasis added).

3. As with Missouri-American, Elm Hills has no legal authority to obtain information from the entities or individuals subject to the Commission's October 28, 2020, *Order Granting Motion for Production*. Therefore, it would be unwarranted and unfair to impose sanctions on Elm Hills as proposed in the *Motion to Dismiss*, for a situation it has no legal authority to remedy.

NO ENFORCEMENT OF ORDER

4. If OPC believes it truly needs the information sought under the *Order Granting Motion for Production*, it has the authority to seek to compel production through further legal action. Sections 386.570.2, and 386.600, RSMo, provide an enforcement mechanism for the violation of Commission orders. As described in 386.600, an action to "enforce the powers of the commission under this or any other law may be brought in any circuit court in this state in the name of the State of Missouri and shall be commenced and prosecuted to final judgment by the general counsel to the commission." With regard to penalties authorized under Section 386.570.2, RSMo, the

Courts have indicated that that administrative agencies can authorize the filing of a penalty case after a contested hearing. See *State ex rel. Sure-Way Transp., Inc. v. Division of Transp. Dept. of Economic Development, State of Mo.*, 836 S.W.2d 23 (Mo.App. W.D. 1992) (relying on *State v. Carroll*, 620 S.W.2d 22 (Mo. App. 1981)); See also *The Staff of the Missouri Public Service Commission v. 2nd Century Communications*, Case No. TC-2002-331, 2002 Mo.PSC LEXIS 334 (March 7, 2002).

5. Neither of these steps has been taken to enforce the Order in question. The *Motion to Dismiss* thus represents OPC's attempt to short-circuit this statutorily based enforcement mechanism for the Commission's orders by moving directly, and inappropriately, to penalize Elm Hills, a party which is not even subject to the *Order Granting Motion for Production*. Therefore, no action should be taken in the pending rate case until OPC and/or the Commission take steps available under law to enforce the *Order Granting Motion for Production*.

6. As the Commission may recall, questions related to the Commission's jurisdiction over the subject non-parties were raised prior to the issuance of the *Order Granting Motion for Production*. (See *Elm Hills' Response to OPC's Motion for Order Regarding the Production of Documents and Request for Rule Waiver* (September 25, 2020)). It is possible that the best way to answer those questions is through the statutory enforcement process and not by penalizing Elm Hills, an operating company that has made necessary improvements to its various water and sewer systems over the past three years to bring those systems in compliance with environmental statutes and regulations and implemented an operations and maintenance process that will keep

the systems in good condition for many years to come, without a prior rate increase.

THE COMMISSION HAS NO AUTHORITY TO DISMISS OR SUSPEND ELM HILLS' RATE CASE

7. No law allows the Commission to dismiss or indefinitely suspend a rate case. Indeed, actions proposed by OPC in its *Motion to Dismiss* conflict with the Commission's constitutional and statutory duty to set rates that are just and reasonable.

8. The United States Supreme Court has clearly stated the constitutional standards applicable to utility rates.

Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the services are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment.

Bluefield Water Works & Improv. Co. v. Pub. Serv. Comm'n of West Virginia, 262 U.S. 679, 690; 43 S.Ct. 675, 678; 67 L.Ed. 1176, 1181 (1923). But ensuring rates provide a fair return on investment is not enough. They also must ensure a utility recovers its reasonable cost of service:

The compensation which the Constitution guarantees an opportunity to earn is the reasonable cost of conduction the business. Cost includes, not only operating expenses, but also capital charges . . . a rate is constitutionally compensatory if it allows the utility to earn the cost of service as thus defined.

State ex rel. Southwestern Bell Tel. Co. v. Pub. Serv. Comm'n of Missouri, 262 U.S. 276, 291; 43 S.Ct. 544, 547; 67 L.Ed. 981, 986 (1923).

9. The Commission has also recognized that its constitutional duties extend beyond return on investment to operating expenses and more:

The Commission is of the opinion that it must draw primary guidance in the evaluation of the expert testimony from the Supreme Court's *Hope* and *Bluefield* decisions. Pursuant to those decisions, returns for Empire's shareholders must be commensurate with returns in other enterprises with corresponding risks. Just and reasonable rates must include revenue sufficient to cover operating expenses, service debt and pay a dividend commensurate with the risk involved.

In the Matter of the Filing of The Empire District Electric Company, et al., Case No. ER-2004-0570, 2005 Mo. PSC LEXIS 348, *68 (Mo. P.S.C. March 27, 2005) (emphasis added).

10. In recognition of these constitutional mandates, Missouri statutes specifically obligate the Commission to set "just and reasonable" rates. Section 393.130, RSMo, in pertinent part, requires a utility's charges to be "just and reasonable" and not in excess of charges allowed by law or by order of the Commission.

11. The Court of Appeals has confirmed this duty:

The Commission must insure just and reasonable rates. To determine whether the rates were just and reasonable, we must consider whether the order could reasonably be expected to maintain financial integrity, attract necessary capital, fairly compensate investors for the risk they assume, and protect relevant public interest.

State ex rel. Union Elec. Co. v. Pub. Serv. Com., 765 S.W.2d 618, 625 (Mo. Ct. App. 1988).

12. The Commission itself has similarly described its duty as follows:

The Commission has the duty to ensure that rates are just and reasonable in a manner that will allow a utility to adequately recover its costs. The Commission cannot set rates at a level that could place a utility in serious financial jeopardy. Further, without adequate revenues, a utility cannot ensure safe and adequate service for its customers.

In the Matter of the Tariff Filing of The Empire District Electric Company, et al., Case

No. EO-2006-0315, 2006 Mo. PSC LEXIS 1735, *71-72 (Mo. P.S.C. December 21, 2006), *affirmed State ex rel. Praxair, Inc. v. PSC*, 328 S.W.3d 329, 344 (Mo. Ct. App. 2010).

13. Staff, OPC, and Elm Hills agree Elm Hills' current rates are not just and reasonable, and each party supports some level of rate increase. The *Nonunanimous Disposition Agreement Regarding Disposition of Small Utility Company Revenue Increase Request* reflects the Staff and the Company belief that to be fully compensatory Elm Hills' current rates for water service must be increased by \$77,818, and current rates for sewer service must be increased by \$389,269. It is unclear from the testimony precisely what revenue requirement OPC supports. However, even if the Commission were to find in favor of OPC's position, a significant rate increase would still be due for both Elm Hills' water and sewer service. In the face of such gross deficiencies, the Commission may not suspend or abrogate its responsibility to set just and reasonable rates as suggested by the OPC without ignoring its duty to provide just and reasonable rates.

INFORMATION SOUGHT IS NOT NECESSARY TO DETERMINE JUST AND REASONABLE RATES

14. The information at issue – again, not Elm Hills' information or information to which Elm Hills has access or control - concerns the question of how alleged private equity investors, multiple layers above the operating company, fund their investments and what "internal rate or return" a mixture invested funds from various sources might produce. But the source(s) of funds used to make equity investments are irrelevant

because in setting rates the Commission is required to provide a reasonable return based on the risk profile of the utility and the returns being earned by *enterprises* of similar risk. How or whether investors manipulate the sources of their investment to produce an internal rate or return is of no concern or consequence.

15. This is because applicable constitutional standards require the Commission to establish a return on equity (ROE) based on the risks inherent in the operating utility and returns being earned in the region by investors in enterprises of comparable risk.

16. The United States Supreme Court has described this standard as follows:

A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures.

Bluefield Water Works & Improv. Co. v. Pub. Serv. Comm'n of West Virginia, 262 U.S. 679, at 692-93; 43 S.Ct. 675, at 679; 67 L.Ed. 1176, at 1182-1183 (1923).

17. The source of funds used to make the equity investment, or how investors account for their investment (i.e. compute an internal rate of return), are irrelevant, so long as the ROE embedded in rates is fair and reasonable, because an investor's internal rate of return doesn't affect rates charged utility customers. Nothing that has happened in this case prevents the Commission from developing a full and fair record on factors and considerations relevant to determining a fair ROE or overall rate of return for Elm Hills that complies with applicable constitutional standards.

“PIERCING THE CORPORATE VEIL” NOT APPLICABLE

18. OPC suggests that the concept of “piercing the corporate veil” somehow supports its position. (*Motion to Dismiss*, para. 25-27). OPC’s decision not to “belabor the extensive study of the case law regarding corporate veil piercing” should be seen as self-serving, since the only case cited in the motion holds that such action is called for only when “corporate separateness . . . is devised or used to accomplish fraud, injustice, or some unlawful purpose.” OPC has not – and cannot – show those preconditions exist.

19. More on point is the Commission’s following ruling in a 2014 case:

A corporation such as Lake Region is a legal entity separate and distinct from its owners. Courts look to the corporation, not the shareholders, in determining the corporation's rights and duties in respect to third parties unless the owners use the corporate form to engage in wrongful conduct. One of the rare circumstances where the corporate form is disregarded is when a corporation is so dominated by a person as to be an alter ego of that person. In that case the two are treated as one, which is known as "piercing the corporate veil". This theory is usually used when a third party is attempting to reach a shareholder's assets in litigation with a corporation. Staff's position is, in effect, a reverse pierce by using the shareholders' debts to affect the debt of the company. However, Staff has presented no evidence of fraud or wrongful conduct to justify disregarding Lake Region's corporate form and treating the shareholder loan as company debt. Therefore, the shareholder loan should not be considered in calculating Lake Region's amount of debt.

In the Matter of Lake Region Water & Sewer Company's Application, et al., Case No. WR-2013-0461, et al., 2014 Mo. PSC LEXIS 358, *91-92 (Mo. P.S.C. April 30, 2014) (emphasis added).

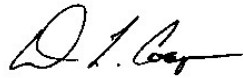
20. Again, there is no evidence of fraud or wrongful conduct that would justify a piercing of the corporate veil or even a “reverse pierce,” as the Commission has

described it. Elm Hills is an unlawful and inappropriate subject of the remedies sought by OPC.

21. For the reasons stated above, there is no justification for the remedies sought by the *Motion to Dismiss* and, thus, it should be denied.

WHEREFORE, Elm Hills Utility Operating Company, Inc. respectfully requests that the Commission deny the OPC's *Motion to Dismiss* for the reasons stated herein.

Respectfully submitted,



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**ATTORNEYS FOR ELM HILLS UTILITY
OPERATING COMPANY, INC.**

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served by electronic mail on this 8th day of December 2020, to all counsel of record.