

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

In the Matter of the Joint Application of )  
Hickory Hills Water & Sewer Co., Inc. and )  
Missouri-American Water Company, for )  
MAWC to Acquire Certain Water and Sewer )  
Assets of Hickory Hills and, in Connection )  
Therewith, Issue Indebtedness and )  
Encumber Assets. )

**Case No. WA-2016-0019**

**RESPONSE TO ORDER DIRECTING FILING**

**COMES NOW** the Staff of the Missouri Public Service Commission, by and through counsel, and for its *Supplemental Recommendation*, states as follows:

1. Hickory Hills Water & Sewer Company, Inc. and Missouri-American Water Company (“MAWC”) filed their *Joint Application and, if Necessary, Motion for Waiver* to sell and transfer utility assets from Hickory Hills Water & Sewer Company to Missouri-American on July 28, 2015, thereby initiating Case Nos. WA-2016-0019 and SA-2016-0020.

2. On August 3, 2015, the Missouri Department of Natural Resources (“DNR”) was allowed to intervene. In its *Application to Intervene*, DNR pointed out that it “has a pending case against Hickory Hills in the Circuit Court of Moniteau County, Case No. 12MT-CC00027, asserting, *inter alia*, violations of water quality standards, failure to upgrade the wastewater treatment facility, and substandard operation of the facility.”<sup>1</sup>

3. The Commission consolidated Case No. SA-2016-0020 into Case No. WA-2016-0019 on August 18, 2015.

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<sup>1</sup> *Missouri Department of Natural Resources’ Application to Intervene*, ¶ 3.

4. On October 2, 2015, Staff recommended that the proposed acquisition be approved.

5. On October 9, 2015, the Office of the Public Counsel (“OPC”) indicated that it would not oppose the acquisition, although it does not necessarily agree with all of the elements of Staff’s *Recommendation*. OPC also requested a local public hearing.

6. On October 13, 2015, MAWC and DNR responded to Staff’s *Recommendation*. Also on that date, Staff responded in opposition to OPC’s request for a local public hearing.<sup>2</sup>

7. On October 14, 2015, the Commission directed Staff to file a reply to OPC’s *Response* filed on October 9, 2015, and to MAWC’s *Response* filed on October 13, 2015.

#### ***Request for a Local Public Hearing***

8. Staff has already responded in opposition to OPC’s request for a local public hearing, as has MAWC.

#### ***Service Area Assignment***

9. In its response to Staff’s *Recommendation*, MAWC stated that § 393.320, RSMo., requires, upon the acquisition of a small water utility by a large water utility, that the Commission assign the small water utility to an existing service area of the large water utility for ratemaking purposes; that MAWC is a “large water utility” and Hickory Hills is a “small water utility” for the purposes of this statute; that the Joint Applicants proposed in the *Joint Application* that the Commission assign Hickory Hills to MAWC’s

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<sup>2</sup> As did MAWC.

St. Louis Metro District; and that Staff failed to address this point in its *Recommendation*.

10. Staff did not overlook this issue in its *Recommendation*, but did not stress it.<sup>3</sup> Staff repeats that the Commission, upon approving the proposed transaction, should assign Hickory Hills to MAWC's St. Louis Metro District as proposed in the *Joint Application*.

### ***Acquisition Premium***

11. Staff stated in its *Memorandum* that the purchase price for the Hickory Hill's assets in this transaction was agreed to in an amount allowing transfer of the assets at their current net book value (\$8,902.00) and also allowing the Receiver to recover a portion of his outstanding receivership costs (receiver fees and repayment of the personal loan). Staff further stated that In Staff's view, the proposed payment made by MAWC to Hickory Hills that allows the Receiver reimbursement of a portion of his outstanding receivership fees and to pay off the personal loan is a reasonable and necessary investment by MAWC to enable the transfer of assets of a "troubled" utility under receivership to an experienced utility operator. Accordingly, under the specific facts and circumstances present in this case, Staff is recommending that MAWC establish a regulatory asset ("Deferred Receivership Costs") on its balance sheet, split equally between water and sewer, to be amortized to expense over a five-year period. This amortization would begin the month after the Commission issues its order approving the proposed transfer. The regulatory asset represents the difference between the amount of the purchase price and the amount of Hickory Hills' net rate

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<sup>3</sup> See *Staff's Memorandum*, bottom of p. 4 to top of p. 5.

base, and will be used to satisfy a portion of the outstanding receivership fees owed and the outstanding loan.

12. The normal practice by a purchasing water utility to account for the difference between the purchase price for a property and the net book value of the property is to book that difference to Uniform System of Accounts No. 114, *Utility Plant Acquisition Adjustments*. The Staff does not believe this accounting practice is appropriate in relation to MAWC's proposed purchase transaction of Hickory Hills because the difference between the purchase price of Hickory Hills and its current net book value is entirely due to the reimbursement of a portion of Hickory Hills' unrecovered receivership costs as part of the purchase price. This is in contrast to the normal case in an acquisition adjustment situation where the difference between the purchase price and the net book value of the property in question is due to the purchasing entity assuming a different future economic value for the property than what is embedded within the current net book value of the property. In that instance, the question has been whether customers should be asked to provide rate recovery for the difference in cost associated with the purchasing utility's estimate of the future economic value of a purchased property.

13. The Circuit Court of Cole County, Missouri, has approved the purchase price and the proposed disbursement of the proceeds.

14. In a purchase transaction in which an acquisition premium exists, the Commission is required to consider the acquisition premium as a "relevant and critical issue" in determining whether or not to approve the transaction. ***State ex rel. AG Processing, Inc., v. Public Service Commission***, 120 S.W.3d 732, 736

(Mo. Banc 2003). The Commission must determine whether the acquisition premium is “reasonable” in the circumstances and consider it when determining whether or not the proposed transaction would be detrimental to the public interest. *Id.* For the reasons stated above, the Staff does not recommend that the Commission order MAWC to account for the excess of its purchase price above Hickory Hills’ net book value as an acquisition adjustment. However, if the Commission finds that this amount should be appropriately considered as an “acquisition premium” in light of the *Ag Processing* case, Staff asserts that the premium is indeed reasonable given the unique facts and circumstances of this case. Hickory Hills is a long-time troubled water and sewer system that has been in receivership since its owners walked away from it. DNR has sued Hickory Hills in Moniteau County Circuit Court because its discharges into the waters of the state are not compliant with the Clean Water Act. The receiver has been unable to generate sufficient revenues to correct the system’s deficiencies or even to pay his own fees. Hickory Hills’ purchase by a large utility with well-trained, professional employees and the financial resources to bring Hickory Hills into compliance with the law is the only rational and available solution to this problem. If the transfer is not approved, Hickory Hills will likely cease operations, leaving its ratepayers stranded with now valueless and uninhabitable homes. The Commission should approve the *Joint Application*.

**WHEREFORE**, having responded to the *Order Directing Filing* as set out above, Staff recommends that the Commission **APPROVE** the *Joint Application* and assign Hickory Hills to MAWC's St. Louis Metro District and order the accounting treatment recommended by Staff in its *Memorandum*. Staff further requests that the Commission approve the *Joint Application* as expeditiously as possible.

Respectfully submitted,

**/s/ Kevin A. Thompson**

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### **CERTIFICATE OF SERVICE**

The undersigned hereby certifies that a true and correct copy of the foregoing has been served, by hand delivery, electronic mail, or First Class United States Mail, postage prepaid, to all parties of record on the Service List maintained for this case by the Data Center of the Missouri Public Service Commission, on this 15<sup>th</sup> day of October, 2015.

**/s/ Kevin A. Thompson**