

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

In the Matter of the Water Rate)	
Increase Request of)	
Hillcrest Utility Operating)	
Company, Inc.)	
)	
Consolidated with,)	Case No. WR-2016-0064
)	
In the Matter of the Sewer Rate)	
Increase Request of)	
Hillcrest Utility Operating)	
Company, Inc.)	

INITIAL BRIEF OF THE OFFICE OF THE PUBLIC COUNSEL

The Missouri Office of the Public Counsel ("OPC") offers this brief on the unresolved issues regarding Hillcrest Utility Operating Company, Inc. ("Hillcrest" or "Company") requested rate changes. As stated during the hearing, OPC and the other parties to the case do not dispute nor challenge the prudence of the improvements to the water and wastewater treatment facilities performed by Hillcrest.¹ The open issues remaining in this case revolve around the operational and management costs of the Company. OPC will also address the question, directed from the bench, related to the ability of the Commission to order phased-in rates in this case.

Further, OPC highlighted its serious concern related to the creditability of the Company's President, Josiah Cox. The OPC showed Mr. Cox made several unsupported statements in his pre-filed testimony.² Additionally, during the questioning of Mr. Cox related to his personal bankruptcy, it came to light Mr. Cox failed to disclose

¹ Hearing Transcript page 19, lines 24-25, page 39, lines 1-6, Harrison Direct Testimony, Staff Exhibit 8. page 4 lines 13-16.

² Hearing Transcript page 72, and page 73, lines 1-13.

his interest in both the holding company, Central States Water Resources Inc. (“CSWR”), and the wholly owned subsidiary, First Round CSWR LLC (“First Round CSWR”)³. This failure to disclose those interests could lead to a reopening of his personal bankruptcy placing the utility operation’s equity at risk and thus irreparably harming the ratepayers it serves.⁴ Moreover, Mr. Cox’s failure to truthfully disclose these interests during his bankruptcy proceeding must be weighed against the overall credibility of his testimony. Given Mr. Cox was the only witness presented by the Company, the weight this Commission should give to his testimony as well as any evidence admitted for which he laid foundation should be minimal given these very serious concerns surrounding his veracity.

As the Commission contemplates these issues, the OPC asks for it to be mindful of the standard proscribed by Missouri courts: “[t]he dominant thought and purpose of the [public utility law] policy is the protection of the public while the protection given the utility is merely incidental.” ***State ex rel. Crown Coach Co. v. Public Service Commission***, 179 S.W.2d 123, 126 (Mo. App., 1944).

A. Allocation Factor

Of the open issues remaining for consideration, the allocation factor is the most critical in terms of dollar for dollar impact to customer rates. The difference between Staff, Hillcrest, and OPC’s calculations is approximately \$34,000.00. For a system facing such increases to its cost of service, this amount will make a significant impact to

³ See Hearing Transcript page 83, line 16 to page 91, line 12.

⁴ A Chapter 7 bankruptcy case can be reopened after discharge and case closure. Bankruptcy Code Section 350(b) authorizes the bankruptcy court to reopen a case for various reasons including to "administer assets, to accord relief to the debtor, or for other cause." Failure to disclose known assets is considered “good cause” to reopen a bankruptcy. ***Goldenberg v. Deutsche Bank Nat'l Tr. Co.*** U.S. B.A.P. 9th Cir. May 30, 2013.

Hillcrest ratepayers. It is OPC's position that the appropriate corporate allocation percentage to apply to corporate costs must be based on Mr. Cox's actual time spent on Hillcrest as shown on his timesheets. Because the timesheets do not break down the amount of time performed by Mr. Cox in the various categories titled "engineering", or "admin", or "research", the only amount of time actually known with any degree of certainty is time entered under the category "HC" directly relating to work performed on Hillcrest.⁵ In looking at the time sheets for Mr. Cox, a decreasing trend between August of 2015 and October 31, 2015 of time devoted to Hillcrest is revealed.⁶ The other two employees of the company, Mr. Jack Chalfant and Ms. Brenda Eaves, did not start recording their time and activities until after the test year and update period in this case⁷. Since the only evidence in the record is Mr. Cox's uncategorized time spent on Hillcrest, the Commission should use Mr. Cox's actual percentage of 10.49% as an appropriate allocation for both time and expenses.

Neither the Staff nor the Company provided any evidence to support their recommended allocation of 14%⁸ except that it was based on estimated, future costs. Further, using estimated, future costs violates the known and measurable standard used by the Commission, which will be explained below. There is no evidence before this Commission as to how that number was arrived at, the inputs that went into

⁵ See Direct Testimony, Keri Roth, OPC Exhibit 2, schedule KNR-4 HC. Hearing Transcript page 205-209 and page 212. Roth Direct, OPC Exhibit 2, page 6 line 6. Per the time sheets, 329.04 hours are the annualized total hours directly attributable to Hillcrest.

⁶ *Id.* Per the timesheets reflected in KNR-4 HC, the average hours spent on Hillcrest directly amounts to 25.29 hours per month, or less than 7% of Mr. Cox's annualized hours worked.

⁷ Hearing Transcript page 199, lines 11-18.

⁸ Hearing Transcript page 95, lines 11-17, Harrison Direct Testimony, Staff Exhibit 8, page 8, lines 18-23.

calculating that factor, or the formula used to reach that allocation factor.⁹ This number was provided by the Company without any justification or evidence while the Staff accepted it on face value.¹⁰ In fact, only OPC has provided this Commission with any evidence as to how it reached its allocation factor of 10.49%¹¹ and why that allocation factor is reasonable to use in this case. Given the serious concerns surrounding Mr. Cox's creditability, the number provided by the Company and accepted by Staff without evidence of additional analysis should be given no weight. This Commission should use an allocation factor of 10.49% to allocate corporate costs and time to Hillcrest, as both figures are reasonable and supported by the evidence.

B. Payroll

OPC remains concerned about the appropriate job title and classification for Hillcrest's employees. Primarily, Hillcrest has no employees itself¹² and an allocation and classification from its holding company, First Round CSWR, must be adopted for the work performed for Hillcrest. OPC's concern about each employee's payroll and job classification with Hillcrest is that they are arbitrarily assigned. The salaries paid are not the result of the job title or function matching up for purposes of assessing salary. Since the job titles were created without any regard for industry standards or metric¹³, this

⁹ Sarver Direct, Staff Exhibit 11, page 3, footnote 1 states, "This allocation factor was based upon the current number of water and sewer customers in Hillcrest as compared to the total number of customers that CSWR expects to have once it continues to pursue acquisition of other properties." (emphasis added). Even this allocation factor is not based on known and measurable amounts in the record but asks this Commission to speculate on potential growth that may or may not happen and should be rejected.

¹⁰ *Id.*

¹¹ Hearing Transcript page 205-209 and page 212. See also Keri Roth's Rebuttal Testimony, OPC Exhibit 3, page 6, lines 18-22 and Schedule KNR-1 attached to the rebuttal testimony.

¹² Hearing transcript page 96 lines 13-15 and page 131 lines 11-17, Keri Roth's Rebuttal Testimony, OPC Exhibit 3, page 1 lines 16-19.

¹³ Hearing transcript page 52 lines 20-25 and page 53 lines 1-6.

Commission should not accept that title for purposes of determining an appropriate job classification or salary.

The Commission has regularly used the Missouri Economic Research and Information Center (“MERIC”) rates and job classifications as well as comparisons to other water and sewer utilities as a yardstick to determine appropriate job classification and salary determination for each position¹⁴. OPC has used MERIC job titles for each employee to compare salaries¹⁵. Based on the evidence presented during this case. Mr. Cox should be treated as “General and Operations Manager” to be most appropriate for Mr. Cox and “Accountants and Auditors” for Mr. Chalfant¹⁶ as these titles best fit the job duties of each employee and have typically been utilized by OPC and Staff in the past to compare salaries.

In a review of small water and sewer utilities¹⁷ performed by OPC witness Keri Roth, comparing Hillcrest and First Round CSWR to other similarly-sized utilities, no chief operator or owner was allowed more than ** ** per hour toward regulated operations.¹⁸ Under the Company and Staff’s proposal, using the job titles assigned by the Company, Mr. Cox’s hourly rate would be ** **, Mr. Chalfant’s hourly rate would be ** **, and Ms. Eave’s hourly rate would be ** **. ¹⁹ OPC recommends Mr. Cox’s hourly for regulated operations be set at ** **, Mr. Chalfant’s at ** **, and Ms. Eaves at ** **. ²⁰ OPC’s proposal is more in

¹⁴ Hearing transcript page 204, lines 2-21, page 216 lines 17-24, Keri Roth Rebuttal, OPC Exhibit 3, page 3, lines 16-18, Harrison Direct, Staff Exhibit 8, page 5 lines 6-23 and page 6 lines 1-9.

¹⁵ Keri Roth Direct, OPC Exhibit 2 page 6 lines 21-22 and KNR-4(HC) attached to Roth Direct.

¹⁶ *Id.*

¹⁷ Keri Roth Direct OPC Exhibit 2, Schedule KNR-3(HC).

¹⁸ *Id.*

¹⁹ Keri Roth Direct, OPC Exhibit 2, page 5, lines 3-5.

²⁰ Keri Roth Direct, OPC Exhibit 2, page 6, lines 16-20.

line with those hourly rates and job titles seen amongst similarly-situated small water and sewer utilities.

OPC also maintains it is reasonable to include MERIC's "mean", or average, experience level to base employee salaries in this case²¹. With that in mind, OPC notes, at the end of the update period in this case, Hillcrest employees had less than one year of experience with regulated water and wastewater utilities. No evidence was provided during the hearing to indicate anything other than the "mean", or average, experience level should be used. If the Commission is inclined to follow OPC's recommendation firmly planted in precedent and industry standards, the Employment Cost Index inflation rates should not be applied to the MERIC rates chosen by the Commission for each employee²² as they have not typically been applied to MERIC rates in the past and should not be adopted in this case as there was no evidence provided for its use despite being requested by the Company in written testimony.

C. Property Taxes, Auditing and Accounting Expenses

Property tax, audit, and accounting expenses requested by the Company are all figures that are either not known nor are they measured with a high degree of accuracy. They are not grounded in information contained in the test year or update period for this case. The audit and accounting expenses are not based on contracted amounts but rather quotes for services not yet performed²³. The property tax amount won't be known until September 1 of 2016 at the earliest. The Commission has explained, in its

²¹ *Id.* line 22.

²² Paul Harrison Rebuttal Testimony, Staff Exhibit 10, page 4 lines 14-19.

²³ *Id.* at page 5 lines 13-22. See Josiah Cox Direct, Hillcrest Exhibit 1, page 20 lines 1-13. No contract was ever provided to substantiate the stated claim that an accounting firm had been hired.

Report and Order in Case No. ER-2014-0370, its position on the “known and measurable” standard:

256.....The term “known and measurable” relates to items or events affecting a utility’s cost of service that must have been realized (known) and must be calculable with a high degree of accuracy (measurable).

The known and measurable standard is not an “either or” issue; it must be both. Even though these requested expenses may satisfy one of the prongs of this test, they fail to satisfy both. As indicated in the hearing, it is known that the property tax expense will likely be increasing but cannot be calculated with a high degree of accuracy until September 1, 2016 due to the changes in the tax levies over the summer.²⁴ Any inclusion of an amount over and above what was included in the test year and true up period would be speculative at best and would violate the known and measurable standard. These expense must be held-over until the next rate case so the Commission truly knows the amounts at issue.

D. Rate Design and Phased in Rates

OPC’s asks the Commission to consider different options for a phased-in rate. Regardless of whether the Commission chooses to phase in rates, there are several items of rate design not in dispute between the parties. One of the agreements is that Hillcrest’s rates should be divided into three customer classifications: residential, apartment, and commercial class for both water and sewer service²⁵. Currently there is just one class of customer for water service (residential) paying a monthly fixed

²⁴ Hearing Transcript page 215, lines 1-10.

²⁵ James Russo Direct, OPC Exhibit 5, page 6, lines 1-3. Hearing Transcript page 92, lines 5-9.

customer fee as well as a volumetric rate per 1000 gallons used. Sewer customers currently pay a flat fee and has two classes of customers, residential and apartment.

In addition to this, OPC proposes to assign the expenses listed in the accounting schedules to either the fixed charge or volumetric rate for water service²⁶. OPC is the only party to the case that provided evidence to the Commission of how expenses should be assigned between the fixed customer charge and volumetric rate.²⁷ Under OPC's rate design, all costs were assigned directly as a customer charge or a volumetric rate or, alternatively, a representative portion of the costs were allocated by a percentage to either the customer charge or volumetric rate based on the particular characteristics of the cost. An explanation of the percentages and methodologies used for the allocations between the customer charge and volumetric rate are detailed in OPC witness James Russo's direct testimony.²⁸ In contrast, Staff witness Jarrod Robertson was unable to provide an explanation for Staff's percentage allocation between the fixed and volumetric charge.²⁹ Both Staff and the Company agree on the surface with the customer equivalents put forward by OPC.³⁰ While the total amount of the customer charge and the volumetric rate will depend on the ultimate revenue requirement set by the Commission, the rate design in terms of the customer classes, customer equivalents, and the allocation of the fixed vs. volumetric rate under traditional rate making are largely uncontroverted.

²⁶ James Russo Direct, OPC Exhibit 5, page 6, lines 10-14.

²⁷ Hearing Transcript page 145 lines 7-13, page 146 line 5 to page 147 line 6.

²⁸ James Russo Direct, OPC Exhibit 5, pages 7-8.

²⁹ Hearing Transcript page 145 lines 7-13, page 146 line 5 to page 147 line 6, page 149 lines 18-21, page 154 lines 8-23.

³⁰ Hearing Transcript page 155 line 4-9. The customer equivalent factors that OPC has proposed are .8 for the apartment class, 1 for residential class, and 1.5 for commercial class. See James Russo Direct, OPC Exhibit 5, schedule 4. See also Josiah Cox Rebuttal, Hillcrest Exhibit 2, page 2 lines 2-7.

During the hearing, parties were asked to provide authority of the Commission to implement phased in rates of water and sewer utilities. The authority for the Commission to phase in rates comes from Section 386.270 RSMo in pertinent part: “all rates, tolls, charges, schedules and joint rates fixed by the commission shall be in force and shall be prima facie lawful....” There is a statutory presumption in favor of the validity of Commission orders³¹. Nor is there a statutory limitation placed on the Commission prohibiting them from OPC’s proposed phased-in rate proposal.

Under OPC’s phased-in rate design proposal, there are dates certain with amounts certain for the phased-in adjustment to rates. This “certain” factor is important because it does not leave the tariff open but allows for a final order that the Commission and Company may implement at the stated times; a process allowed by Section 386.266 RSMO for the collection of transmission charges in an electric utilities fuel adjustment clause (“FAC”).³² Additionally, there are no statutory authorizations for such tools as accounting authority orders (“AAO”) and trackers that both help to carry costs a utility incurs over from one date in time until a future review. Yet the Commission routinely uses these to help Companies during times of extraordinary expenses. While the use of such tools has not been appealed to date, the likely source of their use comes from Section 386.266 RSMo. OPC asks this Commission to use the same interpretation of this statute in creating AAO or other accounting mechanism to help a utility to establish phased in rates to help the ratepayer.

³¹ *State ex rel. Public Counsel v. Mo. Pub. Serv. Comm’n*, 210 S.W.3d 344 (Mo. Ct. App. 2006).

³² *See Union Elec. Co. v. Mo. Pub. Serv. Comm’n*, 422 S.W.3d 358 (Mo. Ct. App. 2013).

E. Bankruptcy

During the course of this case, it was revealed Mr. Cox had filed for a personal bankruptcy as the result of a prior, failed business venture³³. This bankruptcy is significant in this case for two reasons. First, Mr. Cox has repeatedly claimed he was unable to obtain any other financing other than the loan from Fresh Start Ventures to fund his improvements at Hillcrest.³⁴ However, Mr. Cox's inability to obtain traditional bank financing may be directly attributable to his credit worthiness as acknowledged by Staff witness Shana Griffin.³⁵ The high cost of debt at which Fresh Start has financed this loan (at an 14% interest rate) is likely not due to the riskiness of the operations at Hillcrest themselves, there is no evidence of that on the record, but rather the riskiness of the individual seeking the loan. Ratepayers should not bear the extra cost associated with the reality Mr. Cox himself may not have had any other choice in financing because of his personal bankruptcy, inability to grant personal guarantees, and overall lack of creditworthiness. If there is a risk, it must be the responsibility of the Company.

Secondly, during the course of questioning Mr. Cox during the hearing, a much larger and more direct concern for Hillcrest was discovered. Mr. Cox admitted during questioning that he failed to disclose any interest in CSWR or First Round CSWR in this bankruptcy proceeding³⁶. By his own admission, he failed to disclose as required by section 341 of the bankruptcy code, his salary had substantially increased from the date of his bankruptcy filing to the date of his 341-creditor hearing.³⁷ He signed his

³³ OPC Exhibit 8, Certified Bankruptcy Petition and OPC Exhibit 9 PACER version of Bankruptcy Petition.

³⁴ Josiah Cox Direct, Hillcrest Exhibit 1, page 24 lines 9-10.

³⁵ Hearing Transcript page 166 lines 7-17.

³⁶ Hearing Transcript page 89 lines 12-25 and page 90 lines 20-22.

³⁷ *Id.* lines 9-16.

bankruptcy petition under oath and penalty of perjury³⁸ yet knew on the date of the bankruptcy filing he had procured significant capital contributions through First Round CSWR.³⁹ Those dollar amount reflect funds the bankruptcy trustee could potentially use to satisfy the debts of the other creditors in Mr. Cox's bankruptcy filing. This failure to disclose these significant, relevant assets and income also constitute grounds for the Trustee to reopen Mr. Cox's bankruptcy and placing the entire utility holding company at risk as well as the customers relying on this service.

The point of bringing to light the bankruptcy was not to air Mr. Cox's "dirty laundry" but to make the Commission aware of a very serious issue related to the operations of the holding company as well as pointing out Mr. Cox lacks creditability as a witness. As a reasonable observer would note, Mr. Cox's failure to disclose his significant interest in CSWR and First Round CSWR was done with intention to deny his other creditors with the ability to satisfy their debts. While it is not this Commission's job to determine if he indeed defrauded his creditors⁴⁰, the Commission's job is to ensure that the owners and operators of regulated utilities can be trusted with its operations as well to provide those regulating them with truthful and accurate information. Mr. Cox's own testimony and behavior is self-proving that he is an untrustworthy party.

³⁸ Hearing Transcript page 90 lines 17-19. OPC Exhibit 8 and 9, pages 3, 63, 72, 73, 78, and 103.

³⁹ First Round Ledger, OPC Exhibit 7.

⁴⁰ There are ethical guidelines and case law that actively direct attorneys and members of government agencies to report activity that potentially violates criminal law. According to the American Bar Association "there is a duty on the part of a lawyer as a good citizen to aid in the enforcement of criminal laws . . . to report unprivileged knowledge of criminal conduct to the appropriate authorities." ABA Comm. on Ethics & Prof'l Responsibility, Informal Op. 1210 (1972). Further, in *In re Grand Jury Subpoena Duces Tecum*, the Eighth Circuit noted "Even more importantly . . . the general duty of public service calls upon government employees and agencies to favor disclosure over concealment." 112 F.3d 910, 920 (8th Cir. 1997) [highlighted on pg. 9 of 27]. OPC takes this obligation seriously feels obligated to further bring these matters up in a public record, including at hearing before the Commission.

Respectfully Submitted,
OFFICE OF THE PUBLIC COUNSEL

By: /s/ Cydney D. Mayfield

Cydney Mayfield
Deputy Counsel
Missouri Bar No. 57569
PO Box 2230
Jefferson City MO 65102
(573) 522-6189
(573) 751-5562 FAX
Cydney.mayfield@ded.mo.gov

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served by electronic mail, or First Class United States Postal Mail, postage prepaid, on this 3rd day of June, 2016, to all counsel of record.

By: /s/ Cydney D. Mayfield