



Missouri Public Service Commission

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March 8, 2002

Mr. Gary L. Smith
President
WARREN COUNTY WATER & SEWER COMPANY, INC.
1248 Mimosa
Foristell, MO 63348

RE: Warren County Water & Sewer Company
Small Company Rate Increase Procedure Requests
MO PSC File Nos. 2002 00019 (water) & 2002 00020 (sewer)

Dear Gary:

Pursuant to our last meeting on the above-mentioned requests, the Missouri Public Service Commission Staff (Staff) has considered the recommended changes to the cost of service proposed by Warren County Water & Sewer Company, Inc.'s (WC W&S Company) for water and sewer service.

Set out below are the Staff's comments related to its reconsideration of Company proposals:

Corporate Status

The problem listed before that the Staff discovered during its audit was that the Company has been administratively dissolved by the Secretary of State's Office.

Until such time that the WC W&S Company provides proof that it is in good corporate standing with the Missouri Secretary of State's Office, the Staff will not recommend a permanent increase in any rates.

Exhibit No. 9
Case No(s) WM-2004-0122
Date 11-2-03 Rptr KF

March 8, 2002

### **Bookkeeping, Records and Documentation**

As we reported before, the Staff encountered many problems in the following areas during the audit.

The Staff found that the WC W&S Company's records were commingled with the records of an affiliated construction company, Gary Smith and Associates, LTD (Construction Company). Because of this commingling, there was not a clear audit trail between revenues and expenditures of the WC W&S Company and the Construction Company. In many cases there was no documentation of services performed and billed by the Construction Company for the WC W&S Company. The WC W&S COMPANY used two separate checking accounts with the same check numbers. These duplicate check numbers being entered into the WC W&S COMPANY's financial records caused further audit problems. This made it very difficult for the Staff to track and reconcile the WC W&S Company's expenditures.

The Staff also discovered numerous checks written to Gary Smith and/or to one of his affiliated Companies during the one-year review period ended June 30, 2001. Specifically, total amounts written were Warren/Lincoln Investments, Inc. \$19,600 (a new affiliated company), the Construction Company \$40,520 and Gary L. Smith \$28,439. Staff found no supporting documentation for the majority of these checks.

Gary Smith is the only employee of the WC W&S Company. His affiliated Construction Company performs all of the work for the WC W&S Company. The WC W&S Company does not have a written contract for services with the Construction Company, nor is there any supporting documentation attached to the monthly bills for service. Additionally, the WC W&S Company uses no kind of work order system to track the work performed, hours spent and items used for construction. As a result, the Staff is unable to differentiate between tasks that were performed by the WC W&S Company and those that were performed by the Construction Company.

Again, until such time as the company that provides water and sewer service keeps detailed records for its dealings with all of Gary Smith's affiliated companies, the Staff will not recommend a permanent increase in any rates. These detailed records shall include documentation of all services performed and billed.

Again, until such time as the company that provides water and sewer service keeps its records completely separate and apart from all of Gary Smith's affiliated companies, the Staff will not recommend a permanent increase in any rates.

### **Utility Assets**

Again, it has come to the Staff's attention that Gary Smith has attempted to transfer the assets of the WC W&S Company, by the use of a general warranty deed, to a new affiliated company, Warren/Lincoln Investments, Inc. (Investments Company). It is the Staff's understanding that such transfer has been attempted without what the Staff considers the required Commission approval. Pursuant to our last meeting, it is the Staff's understanding that Gary Smith now agrees with the Staff's opinion that such a transfer needs Commission approval. If the assets of the WC W&S Company have been transferred to another entity, the return on equity, depreciation, income taxes and property taxes related to all such assets transferred would no longer be included as "cost of service" items to set rates for the WC W&S Company.

Again, until such time as these ownership and transfer issues are resolved and agreed upon, the Staff will not recommend any rate increases for the WC W&S Company. Settlement of these issues will have to include the Company providing governmental verification that the transfer of assets has not occurred, and a promise that any future sale of assets will be accomplished only with the approval of the Commission.

### **Delinquent Property Tax Payments**

During its audit, the Staff became aware that the WC W&S Company is delinquent on the payment of both current and past property tax assessments for various parcels of land and other property used by the WC W&S Company in the provision of utility service. The Staff's understanding is that all such properties have a minimum of two years delinquent property taxes, which may subject them to a tax certificate sale by the Warren County Collector. However, the Staff is unsure of the exact status of the delinquent property taxes because of the attempted transfer of the WC W&S Company assets to the affiliated Investments Company.

Again, until such time that the delinquent property taxes on utility property have been made current, the Staff will not recommend any rate increases for the WC W&S Company.

### **Delinquent Commission Assessment Payments**

The Staff has recently been made aware that WC W&S Company has again become delinquent on its current Commission assessments. The Staff's policy regarding the payments on a company's assessments is that the company must stay current on such payments in order for a pending small company rate increase procedure to continue. This policy is consistent with the requirements of this procedure that pertain to the initial submission of a rate increase request under the procedure.

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Until such time that the delinquencies on the WC W&S Company's current Commission assessments have been made current, the Staff will not consider recommending any rate increases for the WC W&S Company.

### **Billing Issues**

The Staff discovered numerous billing errors and inconsistencies with the WC W&S Company's Commission approved tariff during its audit. "Late charges" were imposed and/or removed on an inconsistent basis. Non-tariffed "customer deposit charges" were collected in several instances. "Disconnection and reconnection fees" were not charged on a consistent basis. The additional "temporary connection charge" of \$10 per month was charged to many customers for the entire test year. The tariffed monthly "customer charge" was not charged to every customer every month.

The Staff has also discovered that many customers appear to have been billed for charges in excess of the approved tariff for service line installations. These excess charges appear on bills with the heading "W C W & S". The Staff believes these charges are related to service line installations, and that some of these, or a portion of these charges, generated monies that should have been provided by the WC W&S Company pursuant to its tariff, not the utility customer. The investigation for this area will take some time for discovery. Actual bills provided to customers, developers and home builders need to be obtained, and many interviews will need to be performed to find out the nature and extent of the work actually performed before the Staff can determine the magnitude of refunds the company should be required to make for these charges.

The Staff will be seeking the opening of a complaint docket to allow for the investigation of the WC W&S Company's billing, or of an affiliate's billing, of these service line installation charges, as they relate to tariff inconsistencies. The Staff will contact customers to see their actual bills and request the explanations of the actual service line extension work performed for each utility extension. Because of the poor documentation and lack of detail in the WC W&S Company records, as noted above, the Staff will likely need to obtain much of the detail of these transactions from the affected customers, contractors and developers. The Staff expects that many thousands of dollars have been demanded by the WC W&S Company and/or its affiliate(s) from the public (customers, developers and house builders), contrary to the Commission approved service line installation rules of the WC W&S Company, for the public's ability to obtain water service.

Until such time the WC W&S Company, and/or any of its affiliates cease charging customers for service line installation costs that the WC W&S Company should be

providing under its tariff, the Staff will not recommend any rate increases for any of the utility's charges.

### **Ability to Provide Adequate Water Service**

The Staff is considering filing a formal complaint and seeking penalties regarding the low pressure and lack of storage on WC W&S Company's water system. Low water pressure is commonplace for service on the system. While the WC W&S Company has been promising since 1996 to construct a new, elevated storage tank to help with system pressure and storage, it has not yet provided such needed system improvements. The service area is growing rapidly. Staff does not consider service to be adequate when considering its "safe and adequate" service standard. Until such time that the Company puts a new, elevated storage tank on the water system, Staff will not consider an increase in rates.

### **Current Cost of Service Run**

Despite the record keeping problems noted above, the Staff has attempted produced a cost of service run that incorporates costs the Staff feels comfortable with, *if all other issues have been satisfactorily addressed*. A cost of service run is attached for both water service and sewer service. Because of the company's inadequate record keeping, the Staff felt it was necessary to disallow certain expenditures that the WC W&S Company may be entitled to recover. The Staff included estimated expenditures for expenses such as fuel, telephone and plant maintenance based on its experience with similar sized companies. In addition, the Staff questionably has included an annual salary of \$24,000 for Mr. Smith to be allocated between the water and sewer operations.

These water and sewer cost of service runs assume all of the other items of contention mentioned above are not at issue. Additionally, based upon these cost of service runs the Staff has determined that a net increase in rates for WC W&S is not now warranted.

If the utility plant has been transferred to Mr. Smith's affiliate, the Commission's Accounting Staff determined that the Company is now over-collecting annual revenues for water service by the amount of \$39,297. If the utility plant has been transferred to Mr. Smith's affiliate, the Commission's Accounting Staff determined that the Company is now over-collecting annual revenues for sewer service by the amount of \$2,036.

If the utility plant has not been transferred to Mr. Smith's affiliate, the Commission's Accounting Staff determined that the Company is now over-collecting annual revenues for water service by the amount of \$30,057. If the utility plant has not been transferred

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to Mr. Smith's affiliate, the Commission's Accounting Staff determined that the Company is now under-collecting annual revenues for sewer service by the amount of \$6,782.

### **The Employment of Gary Smith by WC W&S Co**

Pursuant to a plea agreement before the Environmental Protection Agency (EPA), Gary Smith has knowingly violated EPA standards related to his operation of the system for WC W&S Co. At that time, Mr. Smith was sentenced to probation for these violations. It has recently come to Staff's attention that Mr. Smith has yet again been accused of violating more EPA standards, which is a violation of his existing probation. Because of his intentional and continued violations of EPA standards, the Staff will not consider an increase in the company's rates until such time as Mr. Smith is not responsible for any of the operation and maintenance of the sewer system. Staff will also allow no monies in salary expenses while Mr. Smith is in charge of operation and maintenance of the sewer and water systems.

### **Company Proposed Changes To Staff's Initial EMS Recommendations:**

Pursuant to our last meeting of January 16, 2002, the Company proposed changes to Staff's cost of service run for the following:

(1) **Sludge hauling**

Test year sludge hauling expense was \$2,500. The level of expense that the Company wanted to build in was \$26,000. Staff will not build into rates monies that have not been expended for hauling. Recently, a load of sludge has been transported every other week. In representation of this current payment pattern Staff has increased the expense amount included in its cost of service run to \$ 9,780.

(2) **Salary of Management (Gary Smith)**

Gary requested that \$36,000+ annual salary for himself be incorporated into the Staff's cost of service run. Staff had incorporated \$24,000 per year for both systems. Upon further review of knowing EPA violations, grotesque customer service, and other poor operation and maintenance activities, Staff is removing all salary for Gary Smith from the EMS run (see above for discussion of Gary Smith payroll.)

(3) **Telephone Expense:**

Staff did not increase the amount from \$1,400 per year to \$2,400 per year.

(4) **Office Rent:**

Staff did not increase the Company requested amount to \$7,200 per year.

(5) Chemical Expense:

Staff did not increasing the amount of chemical expense past what was actually incurred during the test year. When chemical expense levels are actually incurred, Staff will consider including such appropriate expenses at that time. The amount of expense will stay at \$1,193 per year, instead of the Company recommended level of \$2,400 per year.

(6) Rate Case Expense:

Staff did not include any monies for rate case expense.

(7) Revenues Annualization:

Staff did not modify the its revenue annualization contained in its original cost of service run which was developed from the Company's books.

**SUMMARY**

The results of Staff's audit are that no increase is warranted at this time, especially considering all of the other above listed issues and concerns of Staff, contained in this document, which the Company has not remedied.

I have determined that the Staff and Company cannot agree on changes to the Company's cost of service that will yield a net positive revenue requirement, and which will satisfy all issues associated with the other problems listed in this document. This treatment is consistent with the Commission's Rules. **Staff is now closing these small company rate cases.** The Company now has the option to file a formal general rate proceeding.

If you have any questions regarding any of these matters, please contact me at your convenience at (573) 751-3437.

Sincerely,



Wendell R. (Randy) Hubbs  
Assistant Manager, Rates  
Water & Sewer Department

Enclosures

Copy: Office of the Public Counsel – M. Ruth O'Neill