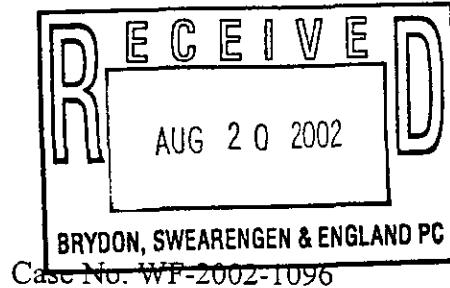


**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

In the Matter of Missouri-American Water )  
Company for Authority (1) to Issue up to )  
\$85,000,000 in Aggregate Principal )  
Amount of Secured or Unsecured Long )  
Term Debt and (2) to Issue and Sell )  
Additional Common Stock to, or Receive )  
Additional Paid-in-Capital From, Its )  
Parent Company in an Aggregate Amount )  
up to \$15,000,000. )



**FILED<sup>3</sup>**

**JAN 23 2004**

**AMENDED STAFF RECOMMENDATION**

**Missouri Public  
Service Commission**

COMES NOW the Staff of the Missouri Public Service Commission (Staff), by and through Counsel, and for its Recommendation, states as follows:

1. On or about May 30, 2002, Missouri-American Water Company (MAWC or the Company) filed an Application for Commission approval to borrow up to \$85,000,000 in secured or unsecured debt and to issue and sell additional common stock to, or receive additional paid-in-capital from its parent company, American Waterworks, in an aggregate amount up to \$15,000,000.

2. The Staff has reviewed the MAWC's Application and has summarized its conclusions in a Memorandum that is attached to this Recommendation, labeled Appendix A, and incorporated by reference. (Staff filed an earlier Recommendation in this case on July 25, 2002.)

Exhibit No. 100  
Case No(s). WRC-2003-0500  
Date 12/16/03 Rptr SKM

3. § 393.200.1 RSMo 2000, provides, among other things, that a regulated water or sewer company may issue notes (indebtedness) when necessary for the acquisition of property, the extension or improvement of its plant or system or to discharge lawful obligations. This statute also states, in part, that the Commission can issue an Order approving indebtedness if the money sought is "reasonably required" for the purposes approved by the Commission in its Order.

4. The application indicated that the financial authority sought was based upon objectives articulated in the statute summarized in paragraph 3 just above. Staff concluded in its Recommendation that the proposed transaction was reasonable, subject to the imposition of certain conditions.

5. Staff has amended its Recommendation based on discussions with the Company in an attempt to provide greater financial flexibility as intended by the "shelf registration" proposed in this Application. Staff's conditions of approval, as amended, will allow the Company the opportunity to file a Request for Approval asking the Commission to increase the interest rate cap based on new pro forma financial information submitted by the Company should market conditions arise that prohibit the Company from obtaining financing at Staff's recommended interest rate cap of 7.25 percent.

**WHEREFORE**, based upon the foregoing, the Staff respectfully recommends that the Commission enter an Order approving the Application with the following conditions:

A. That nothing in the Commission's Order shall be considered a finding by the Commission of the value of this transaction for rate making purposes, and that the Commission reserves the right to consider the rate making treatment to be afforded these financing transactions and their results in cost of capital, in any later proceeding.

B. That the Company shall file with the Commission any information concerning deviations from the stated use of the funds or any information that would materially change the pro forma capitalization and financial ratios.

C. That at no time will the Company's total borrowings, including all instruments, exceed its Missouri-regulated rate base.

D. That the interest cost of financing obtained through the efforts of American Water Capital Corporation shall not exceed 200 basis points (2 percentage points) above the yield on U.S. Government Treasury Bonds having similar terms of maturity as published in The Wall Street Journal on the date prior to the date or dates on which the terms and conditions of the indebtedness shall be determined. However, at no time shall the interest rate exceed 7.25 percent, without prior Commission approval.

E. That the interest cost of the General Mortgage Bonds issued by the Environmental Improvement and Energy Resource Authority (EIERA) shall not exceed 200 basis points above the most current Bond Buyer Revenue Bond Index at the time of issuance. However, at no time shall the interest rate exceed 7.25 percent, without prior Commission approval.

F. That the interest cost of financing obtained through the State Revolving Fund administered by the Department of Natural Resources shall not exceed 7.25 percent (i.e., the estimated interest rate utilized by the Company for purposes of this filing) without prior Commission approval.

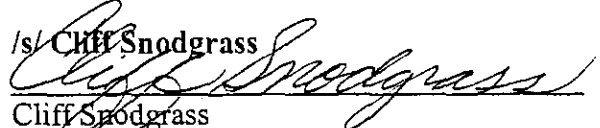
G. That the Company file with the Commission all final terms and conditions on the proposed financing, including, but not limited to, the aggregate principal amount to be sold or borrowed, price information, estimated expenses, portion subject to the fee schedule and loan or indenture agreement concerning each issuance.

H. That the Company file with the Commission any information concerning the use of the funds from the issuance(s) with regard to redemption of any outstanding debt, including Net Present Value calculations indicating the amount of interest cost savings.

Respectfully submitted,

DANA K. JOYCE  
General Counsel

/s/ Cliff Snodgrass

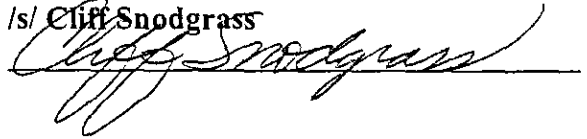
  
Cliff Snodgrass  
Senior Counsel  
Missouri Bar No. 52302

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### **Certificate of Service**

I hereby certify that copies of the foregoing have been mailed, hand-delivered, transmitted by facsimile or emailed to all counsel of record this 19<sup>th</sup> day of August, 2002.

/s/ **Cliff Snodgrass**

A handwritten signature in cursive script, appearing to read "Cliff Snodgrass", is written over a horizontal line.

MEMORANDUM

TO: Missouri Public Service Commission Official Case File,  
Case No. WF-2002-1096, Missouri-American Water Company

FROM: Roberta McKiddy, Financial Analysis Department

  
Project Coordinator / Date 8/14/02

  
General Counsel's Office / Date 8/15/02

SUBJECT: Staff Recommendation for Approval of Authorization and Sale of General Mortgage Bonds and Issuance of Common Stock

DATE: August 14, 2002

1. (a) **Type of Issues:** Secured and Unsecured Long-term Debt and Common Stock
  - (b) **Amounts:** Debt not to exceed \$85,000,000; Stock not to exceed \$15,000,000
  - (c) **Rate:** The interest rate on the proposed indebtedness will not exceed 200 basis points above the yield on U.S. Government Treasury Bonds having similar terms of maturity as published in The Wall Street Journal on the date prior to the date or dates on which the terms and conditions of the indebtedness shall be determined. For purposes of this filing, the Company has estimated the interest rate at approximately 7.25 percent, which is based upon the projected 10-year Treasury note for 2003 plus about 150 basis points. The additional 150 basis points is American Water Capital Corporation's (AWCC) best estimate of the spread at which AWCC will be able to secure financing. Should the company choose to seek financing from the Environmental Improvement and Energy Resources Authority (EIARA), the interest rate will not exceed 200 basis points over the Bond Buyer Revenue Bond Index as published in the most current available issue of The Bond Buyer. As of June 27, 2002, the Bond Buyer Revenue Bond Index rate was 5.41 percent. This would equate to an interest rate not to exceed 7.41 percent for any financing secured through EIARA. Financing obtained through the State Revolving Fund will be issued at a tax-exempt rate. The most current rate available as of this filing is 5.14 percent.
  - (d) **Other Provisions:** The exact provisions of the loan will be determined at the time of closing.
2. **Proposed Date of Transaction:** As soon as practical

3. (a) **Statement of Purpose of the Issues:** Applicant intends to apply the net proceeds from the financing program for the acquisition of property, the construction, completion, extension or improvement of or additions to its facilities, other capital investments, all of which shall be necessary and proper for the rendition of public water supply and wastewater service, the improvement or maintenance of its service, the discharge or lawful refunding of indebtedness outstanding at the time of closing and to reimburse its treasury for any costs heretofore incurred subsequent to July 1, 2001. Further details will be provided in the Comments Section of this Staff Recommendation.
- (b) **From a financial perspective, does Staff deem this purpose reasonable?:**  
Yes X No
4. **Type of Sale:** Long-term taxable debt will be made for maturities not to exceed thirty-five (35) years at market interest rates by American Water Capital Corporation on behalf of Missouri-American Water Company. General Mortgage Bonds will be issued and sold to an underwriter by the State Environmental Improvement and Energy Resources Authority at the request of Missouri-American Water Company. The State Revolving Fund offers two loan programs. Under the direct loan program, the Department may make or authorize low cost loans through the purchase of an applicant's general mortgage bonds, revenue bonds, short-term notes or other acceptable obligation for the planning, design and construction of Qualifying Facilities. Under the leverage loan program, the Authority may issue bonds and loan the proceeds for the construction of Qualifying Facilities. The Common Stock will be sold for an aggregate price instead of a price per share to the parent corporation of Missouri-American Water Company (MAWC), American Water Works Company, Inc. (AWWC).
5. **Copies of executed instruments defining terms of the proposed securities:**
- \_\_\_ (a) If such instruments have been previously filed with the Commission, a reference to the Case Number in which the instruments were furnished.
- X (b) If such instruments have not been executed at the time of filing, a statement of the general terms and conditions to be contained in the instruments, which are proposed to be executed.
- \_\_\_ (c) If no such instruments are either executed or to be executed, a statement of how the securities are to be sold.
6. **Certified copy of resolution of the directors of applicant, or other legal documents authorizing the issuance of the securities reviewed:**
- Yes X No
7. **Pro-forma Balance Sheet and Income Statement reviewed:**
- Yes X No

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8. **Capital expenditure schedule reviewed:**

Yes X No

9. **Journal entries are required to be filed by the Company to allow for the Fee Schedule to be applied:**

Yes X No

(Note: Fee schedule applies only to new long-term debt.)

10. **Recommendation of the Financial Analysis Department:**

- X Grant by session order (see Comments)
- Conditional Approval granted pending receipt of definite terms of issuance (see Comments)
- Require additional and/or revised data before approval can be granted (see Comments)
- Formal hearing required (see Comments)
- Recommend dismissal (see Comments)



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**COMMENTS:**

Missouri-American Water Company (Missouri-American, Company) is a Missouri corporation with its principal office and place of business at 535 N. New Ballas Road, St. Louis, Missouri 63141. Applicant is qualified to conduct business as a public utility in the State of Missouri subject to the jurisdiction of the Commission as provided by law. Applicant is engaged, generally, in the business of furnishing water and wastewater service to the public in over one hundred (100) municipalities within twelve (12) counties throughout the State of Missouri.

Missouri-American has filed an Application requesting the Missouri Public Service Commission (Commission) authorize the Company: (1) to issue up to \$85,000,000 in aggregate principal amount of secured or unsecured long-term debt and (2) to issue and sell additional common stock to, or receive additional paid-in-capital from, its parent company, American Water Works Company, in an aggregate amount up to \$15,000,000. Applicant intends to apply the net proceeds from the financing program for the acquisition of property, the construction, completion, extension or improvement of or additions to its facilities, other capital investments, all of which shall be necessary and proper for the rendition of public water supply and wastewater service, the improvement or maintenance of its service, the discharge or lawful refunding of indebtedness outstanding at the time of closing and to reimburse its treasury for any costs heretofore incurred subsequent to July 1, 2001. Applicant seeks approval of a financing program for a three (3) year period commencing with the effective date of the Commission's approval that would permit Applicant, from time to time during this period to:

- (1) issue additional long-term taxable debt in an aggregate principal amount not to exceed \$85,000,000 through its affiliate American Water Capital Corporation.
- (2) obtain low cost or tax advantaged funding from the State Environmental Improvement and Energy Resources Authority in the form of private activity bonds for qualifying projects and from the State Revolving Fund for qualifying facilities, provided the amount of such new debt in combination with the debt described in (a) does not exceed \$85,000,000; and
- (3) issue and sell to Applicant's parent company, American Water Works Company, Inc. additional common stock for cash, or receive additional paid-in-capital, for an aggregate sale price not to exceed \$15,000,000.

Missouri-American provided the following detail estimating how the net proceeds would be utilized. Spending that is in excess of the proposed financing will be supplemented by internally generated funds and short-term financing. [Source: Company response to Staff Data Request No. 3801.]

<u>Description</u>	<u>7/1/01 – 12/31/01</u>	<u>2002</u>	<u>2003</u>	<u>Total</u>
Capital Investments Net of Advances and Contributions	\$28,872,000	\$40,900,000	\$38,562,000	\$108,334,000
Acquisitions	-0-	\$24,000,000	\$11,200,000	\$35,200,000
Retirement of Long-term Debt	-0-	\$15,696,000	-0-	\$15,696,000
Total	\$28,872,000	\$80,596,000	\$49,762,000	\$159,230,000

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Applicant proposes to issue some or all of the proposed long-term debt financing through its affiliate, American Water Capital Corporation. American Water Capital Corporation was established June 2000 for the purpose of providing financial services to American Water Works Company and its twenty-five (25) utility subsidiaries, which includes Missouri-American. In creating American Water Capital Corporation, American-Water Works Company's intent (AWWC) was to replace multiple bilateral lines of credit held by its utility subsidiaries and consolidate financing functions at American Water Capital Corporation (AWCC). In a June 26, 2000 press release, the company stated, "This consolidation will streamline the financing function, creating cash management efficiencies and a lower cost of capital for the utility subsidiaries."

AWCC obtains its funds through two primary sources: (1) short-term notes in the commercial paper and money market loan markets and (2) it registers its own debt securities for sale in the public market by filing a "shelf registration" with the U.S. Securities and Exchange Commission ("SEC"). Any long-term debt issued pursuant to Missouri-American's agreement with AWCC will be made for maturities not to exceed thirty-five (35) years at market interest rates. The market interest rates will not exceed 200 basis points (2 percentage points) above the yield on U.S. Government Treasury Bonds having similar terms of maturity as published in The Wall Street Journal on the date prior to the date or dates on which the terms and conditions of the indebtedness shall be determined. For purposes of this filing, the Company estimated the interest rate at approximately 7.25 percent, which is based upon the projected 10-year Treasury Note for 2003 plus about 150 basis points. The additional 150 basis points is American Water Capital Corporation's (AWCC) best estimate of the spread at which AWCC will be able to secure financing.

Missouri-American also proposes to utilize some General Mortgage Bonds, which will be issued and sold to an underwriter by the State Environmental Improvement and Energy Resources Authority at the request of Missouri-American Water Company. Should the company choose to seek financing from the Environmental Improvement and Energy Resources Authority ("EIERA" or "the Authority"), the interest rate will not exceed 200 basis points over the Bond Buyer Revenue Bond Index as published in the most current available issue of The Bond Buyer. As of June 27, 2002, the Bond Buyer Revenue Bond Index rate was 5.41 percent. This would equate to an interest rate not to exceed 7.41 percent for any financing secured through EIERA.

In addition, Missouri-American intends to obtain some financing from The State Revolving Fund, which is administered by the Department of Natural Resources. The State Revolving Fund offers two loan programs. Under the direct loan program, the Department may make or authorize low cost loans through the purchase of an applicant's general mortgage bonds, revenue bonds, short-term notes or other acceptable obligation for the planning, design and construction of Qualifying Facilities. Under the leverage loan program, the Authority may issue bonds and loan the proceeds for the construction of Qualifying Facilities. The Common Stock will be sold for an aggregate price instead of a price per share to the parent corporation of Missouri-American Water Company (MAWC), American Water Works Company, Inc. (AWWC). Financing obtained through the State Revolving Fund will be issued at a tax-exempt rate. The most current rate available as of this filing is 5.14 percent.

Staff reviewed the pro forma financial statements submitted by Missouri-American and has determined that the Company's capital structure will be affected by the proposed financing. The resulting capital structure will consist of 40.87 percent common equity, 0.58 percent preferred stock, and 58.64 percent long-term debt (see Attachment A). Coverage ratios of the Company will decline with this proposed financing. However, the ratios should remain well within the Standard & Poor's Guidelines for an "A" rating (see Attachment B). It should also be noted that the pro forma financial statements submitted by Missouri-American indicate the Company will be able to retire \$60,253,343 in bank debt along with the associated interest expense of \$1,253,694. Based on this review, Staff finds the proposed interest rate and capital structure reasonable.

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Staff, therefore, recommends that the Commission approve the Company's Application in this case with the following conditions:

1. That nothing in the Commission's order shall be considered a finding by the Commission of the value of this transaction for rate making purposes, and that the Commission reserves the right to consider the rate making treatment to be afforded these financing transactions and their results in cost of capital, in any later proceeding.
2. That the Company shall file with the Commission any information concerning deviations from the stated use of the funds or any information that would materially change the pro forma capitalization and financial ratios.
3. That at no time will the Company's total borrowings, including all instruments, exceed its Missouri-regulated rate base.
4. That the interest cost of financing obtained through the efforts of American Water Capital Corporation shall not exceed 200 basis points (2 percentage points) above the yield on U.S. Government Treasury Bonds having similar terms of maturity as published in The Wall Street Journal on the date prior to the date or dates on which the terms and conditions of the indebtedness shall be determined. However, at no time shall the interest rate exceed 7.25 percent, without prior Commission approval.
5. That the interest cost of the General Mortgage Bonds issued by the Environmental Improvement and Energy Resource Authority (EI ERA) shall not exceed 200 basis points above the most current Bond Buyer Revenue Bond Index at the time of issuance. However, at no time shall the interest rate exceed 7.25 percent, without prior Commission approval.
6. That the interest cost of financing obtained through the State Revolving Fund administered by the Department of Natural Resources shall not exceed 7.25 percent (i.e., the estimated interest rate utilized by Company for purposes of this filing), without prior Commission approval.
7. That the Company file with the Commission all final terms and conditions on the proposed financing, including, but not limited to, the aggregate principal amount to be sold or borrowed, price information, estimated expenses, portion subject to the fee schedule and loan or indenture agreement concerning each issuance.
8. That the Company file with the Commission any information concerning use of the funds from the issuance(s) with regard to redemption of any outstanding debt, including Net Present Value calculations indicating the amount of interest costs savings.

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Attachments:

A: Capitalization  
B: Ratio Analysis

Copies: Director - Utility Operations Division  
Director - Research and Public Affairs  
Director - Utility Service Division  
General Counsel  
Manager - Financial Analysis Department  
Manager - Water and Sewer Department  
Manager - Accounting Department  
David P. Abernathy, Missouri-American Water Company  
Office of the Public Counsel

**Pro Forma Capitalization as of May 31, 2002  
for Missouri-American Water Company**

Capital Component	Percentage of Capital	Capital Dollars	Pro Forma Adjustments	Pro Forma Capital Dollars	Pro Forma Percentage of Capital
Common Equity	46.69%	\$207,510,709	\$15,000,000	\$222,510,709	40.87%
Preferred Stock	0.61%	2,704,000	0	2,704,000	0.58%
Long-Term Debt(1)	52.70%	234,250,000	85,000,000	319,250,000	58.64%
Short-Term Debt	0.00%	0	0	0	0.00%
Total	100.00%	\$444,464,709	\$100,000,000	\$544,464,709	100.00%

**Financial Medians  
Adjusted Total Debt / Capital (%)**

		AA	A
Standard & Poor's Corporation's	Upper Quartile	46.33%	61.00%
Utilities Rating Service	Median	43.25%	55.90%
Financial Statistics, July 2000	Lower Quartile	40.18%	53.10%

NOTE: Standard & Poor's recently assigned a corporate credit rating of "A-" to American Water Capital Corporation and also placed it on CreditWatch with positive implications, reflecting the proposed acquisition of American Water Works by RWE AG, a higher-rated entity. [S&P's Rating Direct, June 26, 2002.]

**Notes:**

(1) Long-term debt includes current maturities of long-term debt.

### Pro Forma Capitalization as of May 31, 2002 for Missouri-American Water Company

<u>RATIO ANALYSIS</u>	Ratios as of 5/31/02	Pro-Forma Ratios	S&P Guidelines "A" Rating (1)
Pre-Tax Interest Coverage:	4.45 x	3.36 x	2.89x (2)
After-Tax Coverage of Interest and Preferred Dividends:	2.61 x	2.07 x	N.A.
Funds Flow Interest Coverage:	8.26 x	6.32 x	3.02x
Funds from Operations to Total Debt:	36.98%	33.17%	13.10%
Adjusted Total Debt to Total Capital:	52.70%	58.64%	55.90% (4)

**Formulas:**

Pre-Tax Interest Coverage: (Earnings before int. and taxes) / interest

After-Tax Coverage of  
Interest and Preferred Dividends: (Gross Income) /  
(Gross Interest + Preferred Dividends)

Funds Flow Interest Coverage: (Funds from Operations + Interest Charges Paid) /  
(Gross Interest Expense)

Funds from Operations to Total Debt: (3) (Funds from Operations) / (Total Debt Outstanding)

Adjusted Total Debt to Total Capital (4)

Numerator	Notes payable + current maturities + current capitalized lease obligations + long-term debt + capitalized lease obligations + total off-balance sheet debt
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Denominator	Notes Payable + current maturities on long-term debt and preferred + current capitalized lease obligations + long-term debt + capitalized lease obligations + minority interest + total preferred and preferred stock + common equity + total off-balance sheet debt
-------------	---

**Notes:**

(1) Standard & Poor's, Utilities Rating Service - Financial Statistics, July 7, 2000.

(2) 2.89x is the median. Interest coverages ranged from the lower quartile of 2.43x to an upper quartile of 3.13x

(3) Standard & Poor's Risk Adjusted Ratio Guideline formula uses an average total debt figure. For purposes of this analysis, however, a total debt figure is used to account for the incremental change in the capital structure.

(4) Standard & Poor's Risk Adjusted Ratio Guideline formula includes off-balance sheet data. For purposes of this analysis, however, Staff's calculation of total debt to total capitalization does not include off-balance sheet data.