

**DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA**

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IN THE MATTER OF the Investigation of the)
Montana Public Service Commission into) REGULATORY DIVISION
whether Mountain Water Company's rates are)
Just and Reasonable) DOCKET NO. D2016.2.15
)

MOUNTAIN WATER COMPANY'S OPENING POST-HEARING BRIEF

Pursuant to the May 10, 2016 Notice of Staff Action, Mountain Water Company ("Mountain Water"), through its counsel, hereby submits its Opening Post-Hearing Brief. The Public Service Commission ("Commission") should not adjust Mountain Water's rates in this matter for the reasons set forth below.

BACKGROUND

Mountain Water's current rates were set by the Commission in Docket No. D2012.7.81. In that case, there was no discussion of the source of Carlyle's acquisition capital, its capital structure or cost of capital. Rather, the Commission accepted the capital structure Mountain Water proposed based on the capital structure of Mountain Water's parent, Park Water Company ("Park Water"). Order 7251c, ¶ 16 (citing Application, introduced as MW-6), Docket No. D2012.7.81. In setting its authorized return on equity ("ROE"), the Commission carefully considered the testimony of experts for both the Montana Consumer Counsel ("MCC") and Mountain Water, and selected a "common group of water utilities" to determine its own DCF calculations. *Id.* ¶ 28. The Commission expressly considered and rejected contentions that Carlyle's acquisition impacted the cost of capital of Mountain Water. The Commission specifically noted that any benefits (or even perceived benefits) of Carlyle's ownership were "offset by the small size, regulatory climate, and other risks."

Id. ¶ 36. Ultimately, the Commission authorized Mountain Water “to increase its rates to allow for annual revenues of \$18,604,260.” *Id.* ¶ 50. This rate increase was based on a rate base of \$36,185,831, with an allowed ROE of 9.8% and a capital structure of 43.88% debt and 56.12% equity. *Id.* ¶¶ 16, 34, 48.

The Commission expressly concluded the rates authorized in Order 7251c were “just and reasonable.” *Id.* ¶ 53. The Commission also successfully defended the rates it awarded against the MCC’s appeal to the Fourth Judicial District Court. Order, *Mont. Consumer Counsel v. Pub. Serv. Comm’n*, Cause No. DV-14-49 (Mont. 4th Jud. Dist. Apr. 28, 2015). The District Court specifically found Dr. Wilson’s “own cost of capital studies . . . did not support his theory that Carlyle’s acquisition of the stock of Park Water Company had significantly lowered Mountain Water’s cost of capital [however they] supported Mountain[] [Water’s] position that the cost of capital for Mountain [Water] had not changed.” *Id.* at 12:5-8 (FOF No. 5), 13:16-20 (FOF No. 11), 16:19-17:20.

The Commission initiated this docket on February 3, 2016 to “inquire into whether Mountain Water Company’s current water rates for its Missoula, Montana customers are just and reasonable.” Notice of Investigation & Intervention Deadline (“Notice”), at 1. The Commission’s vote was prompted by the closing of Liberty Utilities Co.’s (“Liberty”) acquisition of Mountain Water’s upstream parent, Western Water Holdings (“Western Water”) through merger (the “Acquisition”). *Id.* The Commission indicated it would “investigate Mountain Water’s rates to determine if they are just and reasonable under the current capital structure and cost of capital now that Liberty Utilities is the new owner of Mountain Water.” *Id.*

At its request, the MCC was granted general intervention. The City of Missoula (“City”) and Clark Fork Coalition (“CFC”) were also granted intervention, but on the specific condition that they would not be allowed to expand the scope of the docket beyond the issues identified in the Notice of

Investigation. Order 7475b. The Commission expressly denied the City's request that Mountain Water's current ultimate upstream parent company, Algonquin Power and Utilities Corp. ("APUC"), be joined.

The Procedural Orders in this matter evolved through the course of the docket, but ultimately permitted two rounds of discovery and a single round of testimony by all parties. Procedural Order 7457a, at 2. The MCC pre-filed testimony by its long-time cost of capital expert, John W. Wilson. Mountain Water pre-filed testimony by its President, John Kappes, and its cost of capital expert, Thomas J. Bourassa. Commission staff, Mountain Water, and the MCC all propounded data requests, and all parties responded to data requests. The hearing on this matter was held May 3 and 4, in Missoula, and the Commission accepted into evidence the responses to all data requests, the parties' pre-filed testimony, as well as live testimony from witnesses, including Liberty's Director of Regulatory Operations, Bill Killeen. Due to the limited exchange of testimony, Mountain Water was permitted to offer additional live direct testimony from Messrs. Kappes and Bourassa to rebut contentions asserted in Dr. Wilson's pre-filed testimony and responses to data requests. The MCC was allowed to call Dr. Wilson in rebuttal after Mountain Water's case.

Dr. Wilson submitted testimony and responses to data requests indicating he considered this matter a continuation of the Commission's review of the Acquisition rather than a rate case. In that context, Dr. Wilson recommended significant reductions to Mountain Water's rates under the guise of an acquisition adjustment, while admitting he had not conducted any review whatsoever of Mountain Water's current capital structure or cost of capital. *See, e.g.*, MCC Resp. to PSC-029(c). Dr. Wilson recommended that the Commission impose a rate reduction based on the assertion that APUC had substituted low-cost debt for at least a portion of Carlyle's equity capital. Pre-filed Direct Test. of John W. Wilson ("Wilson Test.") 13:17-19. These assertions were based on Dr.

Wilson's original claim that Carlyle's equity had a "Commission-authorized and ratepayer-funded cost of more than 16 percent." *Id.* 8:10-14. However, at the hearing Dr. Wilson disavowed any assertion that Carlyle's equity capital had any authorized return at all. May 3-4, 2016 Hr'g Tr. 300:11-20.

Mr. Kappes offered testimony indicating that Mountain Water's gross revenues had remained relatively flat since the rate case, while increasing its rate base and seeing increases in ongoing costs. At the hearing, Mr. Kappes offered testimony and Exhibit MWC-2 reflecting Mountain Water's budgeted revenues and costs for 2016. The Commission accepted Mountain Water's 2015 Annual Report as Exhibit MWC-3, which shows Mountain Water's actual revenues and expenses, and balance sheets for 2014 and 2015.

Mr. Bourassa offered testimony challenging Dr. Wilson's assertions regarding Carlyle's ROE and that APUC debt could be used to determine an ROE for Mountain Water. Additionally, at the hearing Mr. Bourassa supported Exhibits MWC-5 and MWC-6, which demonstrated that Dr. Wilson's assertions were incorrect and that his recommendations would result in significant losses for Mountain Water and confiscatory rates.

ARGUMENT

There is no factual or legal basis to reduce Mountain Water's rates in this matter. The Commission's Order setting Mountain Water's current rates was based on all necessary and relevant factors. Therefore, it is *prima facie* evidence Mountain Water's rates are lawful, and any party challenging the rates bears the burden of proof in this matter—not Mountain Water. Here, the Commission elected not to call any witnesses and did not participate in the docket as a party. Additionally, both the MCC and the City affirmatively disclaimed any burden of proof in this

matter.¹ As a result, neither the intervenors nor the Commission have met the burden of proof in this matter to demonstrate Mountain Water's current rates are not just and reasonable.

As in the Carlyle acquisition and as determined in the last rate case, very little has changed at Mountain Water as a result of the Acquisition. Mountain Water and Park Water remain closely held with limited access to capital when compared to their publicly traded peers, and there have been no positive changes to regulatory or operational risks or to the utility's size. *See* Order 7251c, ¶ 35. As a result, there is simply no basis on which the Commission can reduce Mountain Water's rates.

As a separate matter, the January 4, 2016 Term Loan Agreement and April 15, 2015 Loan Purchase Agreement should remain confidential. Mountain Water moved the Commission for its protection, pursuant to appropriate administrative procedures. The MCC and City did not oppose the motion, and the Commission found the documents are protected trade secret. The testimony offered at the hearing further supports the Commission's decision, and there is no evidence in the record that would invalidate the Commission's finding of confidentiality regarding these documents. Accordingly, the motion by the City and MCC should be rejected, and the documents should remain confidential.

I. NO PARTICIPANT IN THIS MATTER HAS MET THE BURDEN OF PROOF TO SUPPORT A REDUCTION OF MOUNTAIN WATER'S RATES IN THIS CASE.

As noted above, the Commission set just and reasonable rates for Mountain Water in Docket No. D2012.7.81. This determination considered all issues that must be considered during a ratemaking hearing, including the appropriate rate base, capital structure, cost of capital, historical and projected revenues, and relevant expenses. *See generally* Order 7251c, Docket No. D2012.7.81. As a result, Mountain Water's rates are *prima facie* lawful and any

¹ Hr'g Tr. 10:14-21; *See e.g.* City's Resp. to MWC-033(a) ("Further, the City does not have the burden of proof in this proceeding.")

party challenging these rates carries the burden of proof. *See* Mont. Code Ann. § 69-3-110(2); *Qwest Corp. v. Dep't of Pub. Serv. Reg.*, 2007 MT 350, ¶ 34, 340 Mont. 309, 174 P.3d 496.

No party in this matter has presented evidence that Mountain Water's rates are not just and reasonable under the current approved capital structure and cost of capital. No party seeks or has recommended an adjustment to the capital structure or cost of capital. The Commission cannot rely on the evidence presented by the MCC because it is outside the scope of these proceedings. In fact, widely-accepted financial theory, and watershed regulatory case law regarding ratemaking prohibit the Commission from reducing Mountain Water's rates in this matter. Adjusting Mountain Water's rates in this context also violates the Commission's longstanding precedent of determining the appropriate rates through full ratemaking proceedings and amounts to improper single-issue ratemaking, which the Commission must reject.

A. Intervenor has refused to acknowledge this matter as a rate case or present proper evidence, and no party contends the capital structure or cost of capital has or should change.

The Commission initiated this matter as a rate case pursuant to Mont. Code Ann. § 69-2-324. Notice, at 1. The Commission appropriately indicated its intent to review Mountain Water's current rates under the same "just and reasonable" standard it applies to all other rate cases. Notice (citing Mont. Code Ann. § 69-3-201, MCA); *see, e.g.*, Order 7251c, ¶ 53, Docket No. D2012.7.81 (citing the same).

Despite the Commission's clear legal direction as to the nature of this proceeding, the MCC and its expert continue to contend this matter is some type of review of the Acquisition. *See, e.g.*, MCC Resps. to MWC-055(e); MWC-057(b) & (c); PSC-022; and PSC-029(c). In fact, Dr. Wilson admits he is not suggesting any changes to Mountain Water's cost of equity in this matter. *See* Resp. to PSC-032(a) ("This is not a rate case and I am not recommending a change in the approved cost of

equity.”) As a result, the MCC has made no effort to introduce testimony or evidence on which the Commission can determine the reasonableness of Mountain Water’s rates within the legal standards applicable to this case.

In fact, the testimony and evidence provided by the parties in this administrative record establishes that neither the capital structure nor cost of capital should be changed in this docket. “No money went to Western Water, Park Water, or [Mountain Water].” Pre-filed Direct Test. of Thomas J. Bourassa (“Bourassa Test.”) 4:21-22. The debt and equity of Western Water, Park Water, and Mountain Water was the same before and after the transaction. *Id.* 4:22-5:2. “The books, and more importantly, the capital structures did not change as a result of the Acquisition.” *Id.* 5:3. “The sale of Western Water to Liberty has no effect on Mountain[] [Water’s] actual cost of capital.” Pre-filed Direct Test. of John Kappes (“Kappes Test.”) 3:13-14. Mountain Water does not seek an adjustment to the capital structure or cost of capital in these proceedings.

The MCC’s own expert does not dispute these facts. As explained above, Dr. Wilson indicated in response to data requests “[t]his is not a rate case, and I am not recommending a change in the approved cost of equity.” MCC Resp. to PSC-032(a). He also testified there would be no change to the cost of debt. *Id.* (stating the 4.13% rate “has nothing at all to do with” the approved cost of debt for Mountain Water). He also indicated he was not recommending a change to the WACC. MCC Resp. to PSC-029(c). As a result, no party has provided any admissible evidence on which the Commission can adjust Mountain Water’s capital structure or authorized ROE in this matter.

B. Adjusting Mountain Water’s capital structure or cost of capital in this matter violates financial theory and binding legal precedent and must be rejected.

It is undisputed in this matter, and cannot be reasonably disputed in any matter, that the capital structure and cost of capital of Mountain Water do not depend on the financing Liberty used

to purchase Western Water. “[T]he capital structure is unaffected by the transfer of stock from one investor to another.” Bourassa Test. 12:20-21. A change in equity can come only from “the issuance of new equity, repurchase of existing equity (e.g. treasury stock), from the net earnings of the company, and distribution of earnings (e.g. dividends or distributions.” *Id.* 12:21-26. The acquisition of stock using debt does not change the nature of the stock as an equity investment. *Id.* 12:9-15. “[E]quity is equity regardless of its ownership or funding source.” *Id.* 12:13-14.

Likewise, the cost of capital is not a function of how the investment was funded. *Id.* 12:14-15. This is best illustrated by a simple example. A share of stock that was given as a gift from one person to another, or was inherited, does not result in a zero ROE simply because the investor received the stock for free. *Id.* 6:11-17. “The utility’s cost of debt and equity depends on the return investors expect to receive on investments of comparable risk.” *Id.* 14:13-14. The parent’s business and financial risks are not necessarily the same as the utility it owns, especially where the utility is ring-fenced, as Mountain Water is in this case. *Id.* 14:14-19. This testimony remains undisputed.

Mr. Bourassa’s testimony is consistent with binding legal authority as well. The flagship cases of regulatory ratemaking require “the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks.” *Fed. Power Comm’n v. Hope Nat. Gas Co.*, 320 U.S. 591, 603 (1943); see also *Bluefield Water Works & Improv. Co. v. Pub. Serv. Comm’n of W. Va.*, 262 U.S. 679, 692 (1923) (“A public utility is entitled to such rates . . . equal to that generally being made at the same time and in the same general part of the country on investments in other business”) These cases do not permit an adjustment based on the identity of the investor or on the financing used to obtain the funds for investment.

No fact or legal argument in this matter disputes this widely accepted financial theory or binding case law. The Commission followed proper procedure in the last rate case by setting

Mountain Water's ROE rate based on proxy group analyses. Accordingly, the Commission's determinations should remain in effect. The Commission must not and cannot legally make an adjustment to Mountain Water's capital structure or cost of capital in a limited scope docket nor based on the evidence (or lack of it) in this case.

C. Reducing Mountain Water's rates in this matter is improper because the Commission has not held full ratemaking proceedings, and a reduction in rates would be improper single-issue ratemaking.

The Commission's longstanding precedent and Montana law require the Commission hold full ratemaking proceedings to set Mountain Water's rates in this matter. "The Commission remains committed to the principle of establishing just and reasonable rates through comprehensive review in rate cases" Order 7375a, ¶ 36, Docket No. D2014.6.53 (discontinuing NorthWestern Energy's "lost revenue adjustment mechanism" because it "is single-issue ratemaking that provides an increase in utility revenue, without regard to the universe of other factors that influence utility returns"). The Commission rejects procedures that undermine "this important element of sound rate regulation." *Id.* Montana statutes and the Commission's own rules provide the proper procedure for setting rates, which require the submission and consideration of extensive information, including revenues, operating expenses, rate base, depreciation, and other issues. *See* Mont. Code Ann. §§ 69-3-301, *et seq.*; ARM 38.5.101, *et seq.*

The Commission must abide by its precedent in this matter. "[I]t is a well-established principle of agency law that an agency has a duty to either follow its own precedent or provide a reasoned analysis explaining its departure." *Waste Mgmt. Partners of Bozeman, Ltd. v. Dep't of Pub. Serv. Reg.*, 284 Mont. 245, 257, 944 P.2d 210, 217 (1997). There is simply no valid reason for the Commission to depart from its long-observed standard of setting rates through thorough and complete ratemaking proceedings.

Reducing Mountain Water's rates without full ratemaking proceedings is single-issue ratemaking and must be rejected. "The Commission has traditionally rejected single-issue filings for good reasons." Order 5986r, ¶ 23, Docket No. D97.7.90 (rejecting Montana Power Company's "rate increase based solely on increased QF costs"). In this matter, reducing Mountain Water's rates "would ignore other offsetting rate considerations and create unjust and unreasonable tariffs." Kappes Test. 5:7-8. Further, a reduction in this matter "would constitute an extreme form of single-issue ratemaking that does not take into account changes in revenues, operating expenses, depreciation, taxes, and rate base." Bourassa Test. 20:1-9. The proper mechanism for adjusting rates is a full ratemaking proceeding.

Adjusting Mountain Water's rates in this docket without a full consideration of all the changes to Mountain Water's expenses violates fundamental principles of regulatory ratemaking. Doing so within the scope of this proceeding is inappropriate. The Commission should reserve its decision on Mountain Water's rates for the next ratemaking case.

II. THE COMMISSION MUST REJECT THE MCC'S RECOMMENDED RATE REDUCTION BECAUSE IT IS BASED ON PHANTOM SAVINGS, FLAWED DATA, AND WILLFUL IGNORANCE.

The MCC was the only opposing party to file testimony and evidence seeking a reduction of Mountain Water's rates. The MCC's expert witness, Dr. Wilson, recommended the Commission reduce Mountain Water's rates by \$6.127 million per year. Wilson Test. 27:1-3. However, the Commission must reject this recommendation because it is based on a number of false assumptions and results in unreasonable, confiscatory rates, which are prohibited under Montana and federal law. When these errors are corrected, there are no cost savings in this matter.

A. The MCC's proposed "cost savings" analysis is invalid because it is based on false assumptions and is fundamentally flawed.

Dr. Wilson's recommended rate reduction of \$6.127 million assumes Carlyle was earning a 16%² pre-tax rate of ROE on a claimed \$250 million equity interest in Park Water. *Id.* 7:12-9:8 & n.5; Hr'g Test. 217:3-218:3, 218:22-219:3. He claims APUC "financed at least \$160 million of the \$250 million acquisition cost of Carlyle's equity interest in Park Water with debt capital costing 4.13 percent annually for thirty years." Wilson Test. 8:10-12.

According to Dr. Wilson, the difference between the two rates, 16% and 4.13%, applied to the \$160 million, creates a cost savings of \$20 million. *Id.* at 15:1-6. He asserts that since "Mountain Water accounted for 31.81% of Park Water's consolidated capital," 31.81% of the cost savings, which is \$6.127 million, should be used to reduce Mountain Water's rates. *Id.* at 23:7-15. Expressed as an equation, this is \$160 million x (16%-4.13%) x 31.81% = \$6.127 million. *Id.* at 23, n.13.

These assumptions are patently false, and largely abandoned by Dr. Wilson on rebuttal. Therefore they do not provide any factual or legal basis for the Commission to adopt Dr. Wilson's recommendation. As an initial matter, Dr. Wilson's proposal is flawed because it is outside the scope of these proceedings. The Commission initiated this docket "to determine if [Mountain Water's rates] are just and reasonable under the current capital structure and cost of capital now that Liberty Utilities is the new owner of Mountain Water." Notice, at 1. However, Dr. Wilson does not contend the structure and cost of capital are inappropriate or should be changed. Wilson Resp. to PSC-032(a). Instead, he proposes only that the alleged "acquisition-

² The 16% is calculated by increasing the 9.8% ROE to account for combined federal and Montana income taxes of 39.3875%. Expressed as an equation: $.098/(1-.393875)=.16168$, which Dr. Wilson then rounded down to 16%. Wilson Test. at 20-21 & n.11.

enabled cost reduction be passed through to ratepayers.” *Id.* The Commission should reject Dr. Wilson’s proposal on this basis alone.

Dr. Wilson’s proposal is independently undermined by a number of other false assumptions. First, Carlyle was not authorized to earn a 16% ROE on \$250 million (or \$160 million) equity interest in Park Water, as Dr. Wilson initially asserted. The utilities owned by Carlyle were authorized to earn an ROE on only \$90 million in rate base, with Mountain Water comprising roughly \$20 million³ of that rate base. Mountain Water does not dispute Dr. Wilson’s 16% as an accurate calculation of pre-tax ROE for Mountain Water, despite it being an unusual way to present an ROE figure. *Id.* 222:15-22. However, his application of that figure to anything other than Mountain Water’s authorized rate base is an inappropriate and inaccurate method for calculating the impact of ROE on Mountain Water rates. It is universally accepted that a utility earns a return only on its authorized rate base. A utility’s ROE applies only to the percentage of rate base that is designated as equity-funded through the authorized capital structure. These principles are undisputed and apply in this and all regulatory matters.

Even if the Commission were to accept Dr. Wilson’s assertion that the Commission should determine the impact at the Park Water level, his proposal must be rejected. Park Water currently owns three utilities with a combined authorized rate base of \$161 million. *Id.* 219:10-15. The authorized capital structure allows an equity percentage of approximately 56%. *Id.* 219:16-23. Applying the equity percentage to the combined rate base results in an equity-funded portion of rate base of approximately \$90 million to which the 16% applies. *Id.* 219:16-23. Therefore, the premise of Dr. Wilson’s recommendation is flawed and his entire analysis is invalid.

³ \$36,185,831 of rate base x 56.12% of authorized equity= \$20,307,488.

In addition, Dr. Wilson's recommendation is based on demonstrably false factual assertions. Mountain Water has repeatedly informed the MCC that Liberty did not use the \$160 million from the April 30, 2015 Note Purchase Agreement to purchase Western Water. *See, e.g.,* Resp. to MCC-001; Resp. to PSC-009. Mountain Water made the financing documentation, the January 4, 2016 Term Loan Agreement, available to the Commission, counsel, and Dr. Wilson in these proceedings, but he chose not to review it. Wilson Test., p. 8 & n.4. All parties are aware of this fact. Despite this, Dr. Wilson refused to acknowledge that Liberty funded the acquisition with short term debt rather than the APUC debt issued in 2015. *Id.*

Dr. Wilson argues the Commission should rely on a press release APUC issued at the time it issued the first tranche of long term debt, rather than undisputed evidence actually produced by Mountain Water in this case regarding the source of closing funds. Additionally, Dr. Wilson's assertion completely ignores that the press release on which he relies actually states the proceeds would be used in part for the acquisition and also "for general corporate purposes." *See* JW-1 to Wilson Test. As a result, there is absolutely no evidence in the record in this case or APUC's public filings to support Dr. Wilson's assertion that Liberty used \$160 million of APUC's 4.13% debt to acquire Western Water.

Finally, the acquisition did not consist of APUC purchasing Park Water, as Dr. Wilson claims. In the acquisition, Liberty purchased the membership units of Western Water. *See* Bourassa Test. 1:26-2:2; Kappes Test. 3:13-14. All parties are aware of these facts, but Dr. Wilson refuses to accept them.

Given the numerous flaws in Dr. Wilson's analysis, and his refusal to consider the facts presented in this matter, the Commission must reject his recommendation. It is unreliable and

does not provide the Commission the factual and legal basis necessary for an administrative decision.

B. The correct analysis shows there are no cost savings in this matter.

Once the errors in Dr. Wilson's analysis are corrected, it is clear there are no cost savings as a result of the acquisition. These corrections are illustrated in MWC-5. Dr. Wilson's calculated "cost savings" hinge on the pre-tax ROE being higher than the rate used for acquisition financing. However, if one were to carry through Dr. Wilson's analysis, the proper calculation would reveal a pre-tax ROE of only 4.09%, while the financing rate is 4.13%, eliminating the alleged cost savings entirely.

In Mountain Water's last ratemaking proceedings, the Commission authorized Mountain Water to earn a pre-tax return of \$3,250,470 on the equity-funded portion of its rate base. MWC-5. The Commission authorized a rate base of approximately \$36,200,000. *Id.*; Order 7251c, ¶ 48. Applying the Commission-approved capital structure of 56.12% provides an equity-funded rate base of \$20,315,440. MWC-5; Order 7251c. Using Dr. Wilson's 16% pre-tax ROE, which Mountain Water agrees is correct, yields an authorized recovery on an equity-funded rate base of \$3,250,470. MWC-5.

Reversing Dr. Wilson's equation reveals the true pre-tax return on the equity-interest of Park Water, as explained in MWC-5. *Id.* Applying Dr. Wilson's 31.81% allocation to Mountain Water's authorized pre-tax ROE of \$3,250,470 demonstrates the actual before-tax equity return Park Water is authorized to recover from ratepayers is \$10,218,392 for all three utilities. *Id.* This return is only 4.09% on what Dr. Wilson asserts is Carlyle's \$250 million equity interest in Park Water, which is obviously lower than the 4.13% financing Dr. Wilson claims was used in the acquisition.⁴ *Id.*

⁴ This return is only marginally higher if one adopts Dr. Wilson's rebuttal assertion that Mountain Water is now only 27.95% of Park Water. Hr'g Tr. 302:2-4. Under this assertion the overall "authorized ROE" for Park Water is only

Accordingly, there are no changes at the Mountain Water level to justify a change in return, and there are no cost savings at the Western Water level to support Dr. Wilson's assertions regarding acquisition savings. Therefore, there is no basis to reduce Mountain Water's rates according to Dr. Wilson's recommendation.

C. Dr. Wilson's recommendation would result in unreasonable, confiscatory rates.

In addition to the flawed and unsupported nature of Dr. Wilson's proposal, the reduction he proposes would result in a confiscatory penalty against Mountain Water. Montana law prohibits the Commission from setting "rates so low that they are confiscatory and deprive the utility of its property without due process of law." *Mtn. States Tel. & Tel. Co. v. Dep't of Pub. Serv. Reg.*, 191 Mont. 331, 339, 624 P.2d 481, 485 (1981). This is a universal foundation of regulatory ratemaking. "[I]t is important that there be enough revenue not only for operating expenses but also for the capital costs of the business[,]" including "service on the debt and dividends on the stock." *Hope*, 320 U.S. at 603. The utility must be permitted sufficient revenue to "assure confidence in the financial integrity of the enterprise, so as to maintain its credit and attract capital." *Id.* Under this universal standard of ratemaking, Dr. Wilson's proposal is inappropriate, contrary to established law, and confiscatory.

The undisputed testimony during the hearing shows adoption of Dr. Wilson's recommendation would leave Mountain Water unable to pay its bills or attract capital in any respect. Dr. Wilson conceded that the Commission cannot reduce rates below the level required to cover operating expenses, debt costs, taxes and depreciation. Hr'g Tr. 58:20-59:1. Without basis, Dr. Wilson asserted that his recommendation would not have that impact on Mountain Water because its current revenues "are substantially greater" than test-year figures. *Id.* 57:18-58:4. However, Dr.

\$11,630,000 (\$3,250,470/27.95%), which results in an actual before tax ROE on Carlyle's \$250 million of equity of 4.65% (\$11,630,000/\$250,000,000).

Wilson admitted he had not done the calculation to determine whether his recommendation would leave Mountain Water unable to cover its operating expenses, taxes, and depreciation. *Id.* 58:17-19. Dr. Wilson's failure to analyze the impact of his recommendation on Mountain Water's rates and his blatantly false assertions should be sufficient to disqualify his testimony from being given any consideration by the Commission.

Mr. Bourassa summarizes the relevant calculations through MWC-6. This exhibit shows that if the Commission accepts Dr. Wilson's recommendation, Mountain Water will be left with a negative operating income, negative net income, negative return on rate base, negative earnings before interest and taxes, and times-interest-earned ratios, all of which is unprecedented and illegal. *See* MWC-6. Moreover, even under conservative estimates of Mountain Water's debt service ratios, it would not be able to service the debt that its current rates assume it must service. *Id.*; Bourassa Test. 234:16-18. This would leave Mountain Water unable to pay its bills or function as a utility, which would destroy the business and ultimately harm its customers.

These facts are undisputed in the record. The sole credible testimony on this issue shows accepting Dr. Wilson's recommendation is confiscatory. Bourassa Test. 235:4-5. Accordingly, the Commission must reject Dr. Wilson's proposal.

The MCC and other opposing parties, which bear the burden of proof in this matter, have failed to present any evidence supporting an adjustment to Mountain Water's rates. Dr. Wilson's cost savings calculations must be rejected because they rely on false assumptions and ignore key facts in these proceedings. Even using Dr. Wilson's calculations, his pre-tax ROE rate, and his allocation assumptions, there are simply no cost savings in this matter. His proposal represents a confiscatory penalty, which is illegal under Montana law. As a result, there is no basis to reduce Mountain Water's rates.

III. THE COMMISSION SHOULD UPHOLD ITS PRIOR DETERMINATION THAT THE JANUARY 4, 2016 TERM LOAN AGREEMENT AND APRIL 15, 2015 LOAN PURCHASE AGREEMENT ARE CONFIDENTIAL.

The motion by the MCC and the City to remove confidential protections from the January 4, 2016 Term Loan Agreement and the April 15, 2015 Loan Purchase Agreement (“Financial Documents”) is baseless and should be denied.

On March 17, 2016, Mountain Water filed its motion to protect the Financial Documents. Mountain Water’s Mot. for Order Protecting Info. Requested in Data Requests MCC-001 and MCC-002 & Aff. of William Killeen (Mar. 17, 2016). Citing the affidavit of Mr. Killeen, Mountain Water satisfied all of the requirements for a protective order. It explained that disclosure of the Financial Documents would damage Liberty’s economic interests because Liberty is able to obtain access to capital, which benefits Liberty, Mountain Water, and its customers, based in part on its ability to maintain the confidentiality of the Financial Documents. *Id.* at 7. By forcing disclosure of these Documents, Liberty would be less likely to obtain this capital. *Id.*

In addition, the Financial Documents are otherwise legally protectable because they contain nonpublic information provided to the SEC and rating agencies, which is the type of confidential information the Commission has protected in the past. *Id.* As the Commission is aware, Liberty remains active in utility acquisitions throughout the U.S. A ruling by the Commission requiring Liberty to disclose short term debt information, which the SEC protects and its competitors do not have to disclose, will put Liberty at a significant disadvantage in that highly competitive environment. Neither the MCC or City lodged an objection to Mountain Water’s original motion. After considering the original motion and affidavit, the Commission granted Mountain Water’s motion for protective order to maintain the confidentiality of the January 4, 2016 Term Loan Agreement and the April 15, 2015 Loan Purchase Agreement. Protective Order 7475c. Specifically,

the Commission found “Mountain Water has demonstrated the information . . . is secret . . . derives independent economic value from its secrecy . . . [and is] entitled to protection under constitutional due process requirements.” *Id.* ¶ 15.

The MCC and City have provided no basis for the Commission to reverse its original decision. At the hearing, the MCC claimed the testimony “demonstrates that [the assertions in Mountain Water’s motion] are simply not accurate.” Hr’g Tr. 205:20-22. The MCC provided no basis for this statement, and none exists.

In fact, the testimony given at the hearing strengthens Mountain Water’s argument that the information should remain under the protection the Commission granted. Mr. Killeen testified that the terms of the Financial Documents, including discounts, are a product of a sustained and ongoing relationship with financial institutions, which must not be shared publicly. Hr’g Tr. 117:19-118:6; 149:2-7. As Mr. Killeen stated in his affidavit, if Liberty were to disclose these terms publicly, it would damage this relationship and inhibit its ability to obtain funding that benefits Liberty, and the customers of all utilities within the Liberty family, including Mountain Water and its customers.

Neither the City nor the MCC have indicated any appropriate need for this information to be released publicly or how the protective order impeded their case presentation or the Commission’s consideration in this matter. While the City’s counsel have at least accessed the information, the MCC’s counsel and expert have refused. Moreover, the MCC’s expert had indicated previously that he does not believe Liberty’s short term borrowing should have any impact on the rates in this matter. Hr’g Tr. 70:11-72:3. As a result, there is simply no basis on which the City or the MCC can claim a need for this information to be made public.

No testimony or evidence in the record invalidates the Commission’s protective order. No facts have changed. The Financial Documents remain trade secret information that derive economic

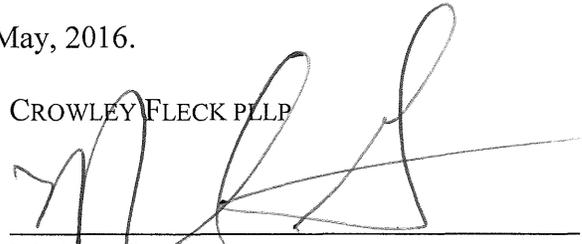
value from their secrecy and are entitled to constitutional protections. There is no basis for the Commission to reverse its decision and publicly disclose the documents at this late time in the proceedings.

CONCLUSION

For the foregoing reasons, the Commission should not adjust Mountain Water's rates in this matter, and should maintain its prior determination that the Financial Documents are confidential.

Submitted this 16th day of May, 2016.

CROWLEY FLECK PLLP

A handwritten signature in black ink, appearing to read 'Michael Green', is written over a horizontal line. The signature is stylized and overlaps the text 'CROWLEY FLECK PLLP' above it.

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CERTIFICATE OF SERVICE BY MAIL

I hereby certify that on May 16, 2016, the foregoing was served via electronic and U.S. mail on:

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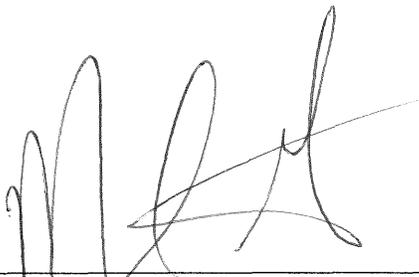
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