BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

Cathy J. Orler, et al	)	
	)	
Complainants,	)	
v.	)	**Case No. WC-2006-0082**
	)	
Folsom Ridge, LLC, Owning and Controlling Big Island Homeowners Association,	)	
	)	
Respondent.	)	
	)	
AND	)	
	)	
In the Matter of the Application of Folsom Ridge, LLC and Big Island Homeowners Water and Sewer Association, Inc., for an Order Authorizing the Transfer and Assignment of Certain Water and Sewer Assets to Big Island Water Company and Big Island Sewer Company, and in Connection Therewith Certain Other Related Transactions.	)	**Case No. WO-2007-0277**

Post Hearing Brief of Interveners
Big Island Water Company and Big Island Sewer Company

COMES NOW the RSMo Chapter 393 companies Big Island Water Company and Big Island Sewer Company (hereinafter "393 Companies"), who are Interveners in Case No. WO-2007-0277, and through their counsel do present the following Post Hearing Brief, filed at the request of the Commission in lieu of closing arguments:

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Factual Background

Folsom Ridge

Colorado based investors purchased approximately 350 acres of real estate on and around the area known as "Big Island", at Lake of the Ozarks in Camden county Missouri, in April of 1998. The property was purchased by the Colorado corporation Folsom Ridge, L.L.C. (Brunk , Ex. 12, page 3, lines 12-20). Folsom was formed expressly for the purpose of developing the Big Island property. (Transcript Testimony Rusaw, P. 562, lines 3-5) At the time of the purchase there were already many homes in existence on Big Island (pre-existing homes).

Folsom decided to install a community water and wastewater treatment system to service their Big Island development project. Owners of the pre-existing homes were given the opportunity to purchase the right to connect to one or both of the new utilities. (Rusaw, Ex. 10, page 8, line 3 AND page 23, lines 3-5).

Big Island homeowner association (HOA)

A homeowners association (HOA) was formed in July 1998 for the purpose of eventually owning and operating the proposed community water and wastewater sewer sytem. (Ex. 88; Rusaw Ex. 9, p. 3, lines 10-11; and Brunk Ty, Ex. 12, p. 13, lines 16-19). Like most homeowner associations, the bylaws provided voting would be based on one vote per lot. (Rusaw, Ex. 9, p. 3, line 18 ; and Brunk Ex. 12, Sch BB-6, p. 9) Owners of the pre-existing homes, who had purchased the right to tap into the system when it was complete, were eventually asked to ratify the HOA covenants and thereby join the homeowners association. (Rusaw Ty, Ex. 10, p. 12, lines 20-23) However, some of these individuals refused to join the HOA. (Ex.56) Approximately 60 of the 100 pre-existing residents became members of the

homeowners association while Folsom owned over 300 lots within the HOA. (T.T. Rusaw, p. 585, lines 4-22).)

Past DNR Violations

Mr. David Lees was the compensated Folsom Ridge representative who lived on site and was initially in charge of the Big Island development project. (Rusaw Ex. 10, p. 7, lines 9-19) On May 25, 1999 D.N.R. issued a violation notice due to installation of a one inch water line on a portion of the system that called for a two inch line. (Brunk, Ex. 12, p. 9, lines 21-23) The investment partners became concerned with Mr. Lees lack of compliance and with complaints about him from Big Island residents. (T.T. Rusaw, p. 563, lines 6-19) In April 2001, Mr. Lees association with the project was terminated and the Colorado investment partners became more directly involved in the Missouri project. (Brunk, Ex. 12, p. 12, lines 3-11). A test "dig" in January 2004 confirmed, that under Mr. Lees supervision, water and sewer mains had been placed side by side in the same trench in violation of DNR requirements. (Brunk Ex. 12, p. 12, lines 17-23)

Folsom entered into a settlement agreement in April of 2004 with the Department of Natural Resources and the Attorney General's office agreeing to separate the mains and correct all violations. (Ex. 91) Engineer Dave Krehbiel provided observation services for the relocation of the mains in accord with the terms of the settlement agreement. (Krehbiel, Ex. 14, p. 5, lines 10-13) The provisions of the settlement agreement have since been satisfied. (Ex. 92 ; Ex. 93; & Rusaw Ex. 10, p. 8, lines 15-19; Krehbiel Ex. 14, p. 6, lines 1-4). There has never been a bad discharge report on the Big Island wastewater system and the current drinking water system has passed all DNR standards. (T. T. McDuffey, p. 730, lines 1-6)

Rates & Service

The homeowner association began providing water and sewer services in the year 2000 to fewer than 25 households on Big Island. Sewer connections reached 25 in the year 2001 with water connections reaching 25 in 2002. (Ex. 9, R.R. Sch. 1) Sewer service is currently provided to 61 residents, of which 49 also receive community water service. (Rusaw Ty. Ex. 9, p. 8, lines 21-23).

The HOA charges a monthly fee of $10 for water and $14 for sewer. (Snyder Ty. Ex. 99, p. 3, lines 18-19) In 2000, the HOA voted to assess a monthly availability fee (now $5) to all residents who purchased the right to connect to the community system but have not elected to do so. (Rusaw Ex. 10, page 29, lines 5-7 ; Brunk Ex. 12, p. 15, lines 14-16) A few residents have refused to pay the availability fee because they are not members of the HOA. (Orler Ex. 1, p. 8, lines 11-15) All monthly fees collected by the HOA , in excess of expenses, are held in reserve with no profits being paid to any entity. (Hughes Ex. 13, p. 3, lines 4-15) Folsom has received payments from the HOA for repayment, or reimbursement, of costs incurred. (Ex. 13, pp. 3-4, lines 19-23) The Missouri D.N.R. has published guidelines for the amount of "reserve funds" which should be maintained by non-regulated utilities (Merciel Ex. 104, p. 5, lines 20-21) The Big Island HOA Board has been conservative in allowing for revenue in excess of expenses. (Hughes Ex. 13, p. 4, lines 18-22)

Complaints

The 3 Complainants who provided testimony to the Commission all own homes which were in existence prior to Folsom's purchase of the Big Island property. Ms. Orler's right to tap into the systems had been purchased by the prior owner of Ms. Orlers home. (Rusaw Ex. 10, p. 2, lines 18-19) In August 2005, Ms. Orler filed a complaint with the P.S.C. (WC-2006-0082)

which was prompted by HOA attempts to collect the monthly availability fee for her unconnected utility taps. (Orler Ex. 1, p. 8, lines 11-15). Ms. Orler did not ratify the HOA covenants, did not consider herself a member of the HOA, and contested the HOA's right to assess fees against her. (Orler, Ex. 1, p. 3, lines 14-16) Ms. Fortney, also filed a complaint contesting the right of the HOA to assess availability fees against non-members for unconnected taps. (Fortney Ex. 7, p. 6, lines 1-3) Complainant Benjamin Pugh is a customer of the community sewer system who has not joined the HOA. (Pugh, Ex. 4, p. 2, lines 1-2) Mr. Pugh believes improprieties still exist regarding water and sewer mains on Big Island and is especially concerned with the lack of governmental regulation over individual customer service lines. (Pugh Ex. 5, p. 5, lines 10-14). Mr. Pugh believes customers should not be required to be "members" of anything. (Pugh, Ex. 4, p. 1, lines 18-19) All three complainants are advocates for P.S.C. regulation.

The 393 Companies

In response to the above referenced complaints, P.S.C. staff generated a Report of Investigation dated February 9, 2006 which suggested a possible solution to the issues on Big Island would be for a group of customers to create a RSMo chapter 393 nonprofit utilty company to assume ownership and control of the Big Island utilities. (Merciel Ex. 104, Appendix A). When 40 of the 60 customers indicated a desire to move forward, Big Island Water Company and Big Island Sewer Company were organized as non profit 393 utility companies. The Board of Directors drafted appropriate bylaws, and negotiated an asset transfer agreement with Folsom and the HOA. (Ex. 102) In January 2007, all Big Island residents were asked to cast written ballots regarding the proposed transfer of utility assets to the 393 companies. Fifty of the sixty utility customers favored the transfer with five opposed. (Rusaw Ex. 9, p.8, lines 21-24)

It is currently not clear whether the P.S.C. has jurisdiction over Folsom or the Homeowners Association or both. Should the Commission determine it has jurisdiction over either Folsom or the HOA, the transfer of the utility assets to the 393 companies cannot take place unless approved by the Commission. For that reason, Folsom and the HOA have filed an application and proposed transfer agreement with the Commission seeking P.S.C. approval of the transfer. (Ex. 20)

The 393 companies want the Commission to assert jurisdiction for the limited purpose of approving the transfer of assets and imposing any appropriate conditions on said transfer. In February 2007, Complainants filed legal action against Folsom, the HOA, and the 393 companies in the Circuit Court of Camden county. (Ex. 36) Among other things, their suit is aimed at stopping the transfer of assets. It would be in the best interest of the Big Island utility customers and the 393 companies if the transfer of assets is reviewed and sanctioned by the Missouri Public Service Commission.

Legal Analysis

1. Are Folsom Ridge and/or the Big Island homeowners association (HOA) Public Utilities pursuant to Sec. 386.020(42) RSMo Supp 2006, And Thus Subject to the Jurisdiction, Control and Regulation of the Missouri Public Service Commission pursuant to Sec. 386.250 RSMo Supp. 2006

The statutory definition of a public utility under RSMo 386.020 (42) includes every "water corporation" and "sewer corporation" which meets the definitions set forth in sub sections (58) and (48) of the statute.

A. Is Folsom Ridge a water corporation pursuant to Sec. 386.020(58) RSMo 2006, in that it owns, controls, operates, or manages a water system, plant or property and distributes, sells or supplies water for gain.

Folsom Ridge is the owner of the real estate on which the Big Island water system and water plant are located. (T.T. Rusaw, p. 567, lines 12-15). Folsom Ridge owns the majority of lots on Big Island which, since voting is "one vote per lot", gives it controlling interest in the homeowners association. Customers who receive water from the system pay the HOA a fee for that service. The predominate issue is whether or not Folsom realizes any "gain" from the sale of water services. If Folsom receives "gain" then, under RSMo 386.020 (58) it is a " water corporation" and therefore under section (42) of that statute it is also a "public utility" and is therefore subject to P.S.C. jurisdiction.

The definition of the word "gain", as it appears in the statutes, is paramount to determining jurisdiction. There are two primary sources for determining the definition of the word "gain": Case law and Dictionary definition.. In the case *Osage Water Co., v. Miller County Water Authority,* 950 SW 2d. 569, 574 (Mo App. S.D. 1997*)*, a Missouri Court concluded the term "gain" was synonymous with the word "compensation" and suggested any entity providing water service in exchange for a fee, or compensation, would be subject to P.S.C. jurisdiction. This is an extremely broad definition which would clearly bring Folsom under the umbrella of P.S. C. control by virtue of the fact a fee is being charged to customers of the water system and Folsom owns the real estate on which the system is located.

Black's Law Dictionary (Fifth Edition) defines "gain" as being synonymous with "profits" or the "excess of revenue over expenses" . Under this limited definition, the argument can be made that Folsom received no gain as a result of its ownership of the water plant. No

evidence was presented to show Folsom received any monetary payments other than those characterized as repayment of construction costs expended or monies advanced to the H.O.A. However Black's definition of "gain" goes on to describe gain derived from capital as **value** proceeding from the property . . . "received or drawn by claimant for his separate use, benefit, and disposal." **Id.** Quoting : *Commissioner of Internal Revnue v. Simmons Gin Co*. C.C.A. 10, 43 F 2nd 327, 328. Utilizing the analysis attributed to the I.R.S. case, one would then pose the question: Did Folsom receive anything of value as a result of its ownership and/or control over the Big Island water system? Folsom Ridge partner, Rick Rusaw, testified, "Property values on the Island continue to appreciate because of the facilities Folsom Ridge has installed for wastewater management and water distribution." (Ex. 10, Rusaw, p. 2, lines 7-8) "We know having water and sewer adds value to everyone's property." (T.T., Rusaw, p. 610, lines 1-2) Since Folsom owns in excess of 300 lots , Folsom is positioned to enjoy increased profits, or gains, from the sale of those lots as a result of the continuing presence of the utility systems. Therefore, Folsom is receiving something of value (increased property value) and stands to realize a profit or "gain" which means Folsom is a "water corporation" under the statutes and subject to P.S.C. jurisdiction.

B. Is Big Island HOA a water corporation pursuant to Sec. 386.020(58) RSMo 2006, in that it owns, controls, operates, or manages a water system, plant or property and distributes, sells or supplies water for gain.

The Big Island homeowners association was established for the purpose of eventually owning and controlling the water and sewer systems on Big Island. . (Ex. 88; Rusaw Ty. Ex. 9, p. 3, lines 10-11; and Brunk Ty, Ex. 12, p. 13, lines 16-19). However, ownership has been retained by Folsom with the duties of operation and management being delegated to the HOA. (T.T. Rusaw, p. 567, 12-15). The H.O.A. charges a fee for water services. (Snyder Ty. Ex. 99,

p. 3, lines 18-19). The record reflects the H.O.A.'s income has exceeded its expenses during the years 2005 and 2006 . (Hughes Ex. 13, Sch. 1, page 2). However, the excess amounts were held in reserve with no profits being paid to any entity. (Hughes. Ex. 13, p. 3, lines 4-15). The amounts being held in reserve are conservative. (Ex. 13, p. 4, lines 18-22) Later discussion will reveal the reserve funding most likely falls short of DNR reserve funding recommendations.

Clearly, if the Commission follows the line of thinking in the Osage case (supra) and finds the terms gain and compensation to be the same, jurisdiction will follow because a fee is being charged. However, if the Commission follows the dictionary definition of "gain" then it cannot assert jurisdiction over the homeowners association because the H.O.A. has invested no capital, incurred no profits, paid no dividends, and since it owns no real estate it is not in a position to enjoy increased property values, or "gains" flowing from the community utility systems. Therefore the HOA does not meet the statutory definition of a "water corporation"; and is not subject to the Commission's jurisdiction.

C. Is Folsom Ridge a sewer corporation pursuant to Sec. 386.020(48) RSMo Supp. 2006, in that it owns, controls, operates, or manages a sewer plant with twenty-five or more outlets and is in the business of collecting, carrying, treating, or disposing of sewage for gain.

It has already been established that Folsom owns the real estate on which the Big Island sewer plant is located. The record reflects sewer services were provided to 25 households sometime during the year 2001. (Ex. 9, RR Schedule 1). Once again the issue on which jurisdication is predicated is the meaning of the word "gain" as used within the statute. Following the same line of reasoning used above in the water corporation analysis, it follows, under the definition provided in **Black's Law Dictionary,** that Folsom became a "sewer corporation" sometime during the year 2001 (when outlets numbered twenty-five) by virtue of

the increased value of its real estate holdings stemming from the presence of a community sewer system to service those holdings. Folsom is therefore a sewer corporation and subject to the jurisdiction of the Commission.

D. Is Big Island HOA a sewer corporation pursuant to Sec. 386.020(48) RSMo Supp. 2006, in that it owns, controls, operates, or manages A sewer plant with twenty-five or more outlets and is in the business Of collecting, carrying, treating or disposing of sewage for gain.

The H.O.A. did not receive "gain" as a result of managing the sewer utility for the same reasons it received no "gain" from its management of the water utility. The H.O.A. has not profited in any way, directly or indirectly, from its activities in managing the the wastewater treatment plant and since it enjoyed no profits or other benefits, it realized no "gain", does not meet the statutory definition of a "sewer corporation", and is not subject to P.S.C. jurisdiction.

2. Have Folsom Ridge or the HOA , or both of them, violated Sec. 393.170 RSMo 2000, by constructing and operating a water system or a sewer System, or both, without having first obtained authority from the Commission in the form of a Certificate of Convenience and Necessity.

Neither Folsom, or the H.O.A. have been granted authority, by the Commission, to construct or operate a water or sewer system on Big Island. An earlier application for the appropriate Certificate was withdrawn by the parties when it was decided to instead transfer the utility ownership to a 393 non profit utility corporation which, by statute, would not be subject to P.S.C. jurisdiction.

A. Folsom Ridge and the Big Island HOA have provided safe and adequate water and sewer service and are not in violation of Sec. 393.130.1, RSMo 2000.

Substantial and competent evidence indicates the quality of the drinking water on Big Island is safe and adequate and there have been no bad discharge reports in connection with the waste water system. (Transcript Ty. McDuffey, p. 730, lines 1-6). All parties concur there were problems with the initial installations performed under the supervision of former Folsom partner, Mr. David Lees. However, those problems were addressed, following Mr. Lees departure, to the satisfaction of DNR personnel and the on site engineer, Dave Krehbiel. The record as a whole reflects the water and sewer utilities are properly equipped and providing service well within capacity. (Krehbiel, Ex. 14, p. 3, lines 5-12) Concerns have been expressed by complainants regarding the lack of regulation over installation of individual customer service lines; however, the Commission lacks authority to address those concerns. (Merciel, Ex. 118, p. 5, lines 10-22)

B. Folsom Ridge and the Big Island HOA have NOT discriminated against any customers and have Not provided preferences to any customer in assessing rates and charges for water and sewer service and tap-on and connection fees.

The evidence supports the fact all customers of the Big Island utilities are being charged the same monthly fee of $10 for water and $15 for sewer. Non-customers, who have purchased the right to tap into the system, are being charged the uniform availability fee of $5 per month. The record was not clear whether Folsom had any unconnected taps for its lots and if so, whether Folsom was paying the $5 per month availability fee. (T.T. Rusaw, p. 584, lines 9-18). The initial rate charged to pre-existing residents for the right to tap into the utility systems was $2,000 for water and $4,800 for sewer, with all of said fees going to the developer to offset

construction costs. These fees were determined by dividing the estimated cost of constructing the initital system by eighty (80), the number of households the initial system could adequately service. (T.T. Rusaw, p. 573, lines 1-12). The systems are now capable of servicing 320 households. (Krehbiel, Ex. 14, p. 3, lines 11-12)

3. The Application of Folsom Ridge and the Big Island HOA to transfer water and sewer assets to the 393 companies, Big Island Water Company and Big Island Sewer Company, is NOT detrimental to public interest.

If Folsom or the H.O.A. fall under the jurisdiction of the Commission, an order must be secured from the Commission prior to the transfer of assets to the 393 companies. (RSMo 393.190) Generally speaking, the courts allow transfers to take place under the statute if the transfer is not detrimental to public interest. *State ex rel. City of St. Louis v. Public Service Commission of Missouri,* 73 S.W. 2d, 400 (Mo. Banc 1934). The courts are obviously concerned that safe and adequate service to the public is not halted, interrupted, or endangered, which is why the Commission has considered such factors as experience, history, financial health, and the ability to operate the assets safely and efficiently. (*See Frimel Water System et al Authority to Transfer Assets and Cease Operations. Case No. WM-2006-0459 – Report and Order issued November 7, 2006, 2006 WL 3371567 (Mo. P.S.C.).*

The current management company for the Big Island utilities is Lake Ozark Water and Sewer (LOWS) whom the record reflects is licensed, certified, and has a substantial amount of experience in the management of water and wastewater treatment facilities. (Ex. 17, pages 2 & 8). Since the same management company will remain in place upon a transfer of assets to the 393 companies (Ex. 17, p. 10, lines 102) (Ex. 102), and given the experience and qualifications of the management company, it is logical to believe the operation of the utility system will continue to be safe and efficient. The only aspect of the transfer which may benefit from

Commission scrutiny is the financial health of the utility under the terms of the proposed transfer agreement.

A. A condition should be imposed on the transfer to insure the reserve assets being tranferred to the 393 companies are in compliance with DNR's TMFC Assessment guidelines.

The H.O.A. has been functioning without the need for financial subsidization from Folsom since 2003, or for only 3 full years. (T.T. Rusaw, P. 628, lines 17-24) The 393 companies have no assets prior to the transfer and the record reflects they will be receiving the H.O.A. bank balance of approximately $7,000 - $9,000 at the time of the transfer.(Ex. 10, p. 19, lines 13-16) A portion of the transferred funds would be utilized for the continuing operation of the utility and a portion of those funds represent money being held in reserve for unanticipated expenditures. The Department of Natural Resources has adopted guidelines pertaining to appropriate reserve amounts for non-regulated utilities which can be found at www.dnr.mo.gov/services/tmfc-assessment.pdf (page 4) and suggest ten percent of each year's operating expenses be placed into an **operating reserve** during the first ten years of operation. In addition, it is recommended an additional **equipment reserve** be maintained in the amount necessary to replace the most expensive piece of equipment within the system. Operating expenses for the H.O.A. in the years 2005 and 2006 were $17,374 and $20,460 (Ex. 13, Sch 1, p. 2) Under DNR guidelines, nearly $3,800 should have been deposited into an **operating reserve** account for those two years alone.

Under the terms of the transfer agreement tap fees ($2,000 for water & $4,800 for sewer), collected from pre-existing homes over the next ten years by the 393 companies, will be paid to Folsom and no tap fees will be charged to Folsom for its properties. (T.T. Rusaw, p. 648, lines 2-17) The only way for the 393 companies to build their reserves is through monthly

charges to customers. The 393 companies have already informed customers there will be a 40% increase in monthly charges in order to compensate for the fact the 393 companies will no longer be assessing availability fees to residents with unconnected taps. (Ex. 102) The proposed budget prepared by the 393 companies anticipates first year expenses of $20,980 with income of $23, 436. (Ex. 99, Schedule A) .

The most important condition the Commission could impose on the proposed 393 transfer would be to require Folsom to transfer to the 393 companies reserve funding amounts which are in harmony with the Missouri Department of Natural Resources standards outlined in their financial capacity (TMFC) assessment guidelines.

IN CONCLUSION

The interveners, Big Island Water Company and Big Island Sewer Company , ask the Commission to utilize Black's Law Dictionary definitions in interpreting the word "gain" and and find Folsom has profited from the installation of the community utility systems by way of increased property values and is therefore subject to regulation by the Commission. Utilizing the same definition of "gain" we ask the Commission to recognize the homeowners association has not profited from the community utility systems and is not subject to PSC regulation. We pray the Commission will assert jurisdiction over Folsom for the limited purpose of examining and approving the transfer of the Big Island utility assets to the 393 companies with the condition Folsom transfer reserve funding to the 393 companies, in the amount suggested by D.N.R. "Financial Capacity" guidelines, as part of the assets being transferred.

Respectfully submitted:

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Certificate of Service

I hereby certify that a true and correct copy of the foregoing document was sent via electronic mail on this 30th day of April, 2007 to :

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