

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application for increase in water and)
wastewater rates in Brevard, Citrus, Duval,) DOCKET NO. 20250052-WS
Highlands, Marion, and Volusia Counties by)
CSWR-Florida Utility Operating Company, LLC)
_____)

DIRECT TESTIMONY OF

JOSIAH COX

on behalf of

CSWR-Florida Utility Operating Company, LLC

INTRODUCTION

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Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Josiah Cox. My business address is 1630 Des Peres Road, Suite 140, St. Louis Missouri, 63131.

Q. WHAT IS YOUR POSITION WITH CSWR-FLORIDA UTILITY OPERATING COMPANY?

A. I am President of CSWR-Florida Utility Operating Company, LLC (“CSWR-Florida” or “Company”). I am also President of CSWR, LLC (“CSWR”) and Central States Water Resources, Inc., (“Central States”), each of which is a CSWR-Florida affiliate.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL EXPERIENCE.

A. I received a Bachelor of Science with a major in Environmental Science from the University of Kansas. In 2007, I earned an MBA from Washington University in St. Louis.

Professionally, I have worked at the Kansas state biological survey where I performed wildlife habitat studies. I then worked at a civil engineering firm where I was involved in various facets of the land development process including permitting, entitlement, civil design, project management, and construction management. I focused mainly on the water and wastewater side of the civil engineering business and was involved in every part of that business from waste-load allocation studies (now known as the anti-degradation processes), design, permitting, project management, and construction management. I also was responsible for the firm's environmental consulting division and was the second private consultant to submit a water quality impact study in the state of Missouri in 2003. I later joined the engineering firm's executive leadership team and helped manage and oversee all the firm's operations.

1 Beginning in 2005, I raised money from a group of investors and formed a full-
2 service civil engineering, environmental consulting, general contracting, and
3 construction management firm. I served the firm as the Chief Operating Officer and
4 Chief Executive Officer, and while there I obtained extensive experience with rural
5 communities in every facet of the water and wastewater compliance process, including
6 environmental assessment, permitting, design, construction, operation and community
7 administration of the actual water and wastewater (sewerage) systems. The firm
8 performed stream sampling and built waste-load allocation models to determine
9 permissible sewerage effluent pollutant loads for receiving water bodies. The firm did
10 full engineering design of multiple whole community wastewater and water
11 infrastructure systems including wells, water distribution, water treatment, water
12 storage, wastewater conveyance, and wastewater treatment plants, pursued the designs
13 through federal and state administered permitting processes in Missouri and Illinois,
14 and supervised the construction of these water and wastewater systems from green field
15 site selection all the way through system startup and final engineering sign off.

16 In addition to running a firm that designed and built small water and wastewater
17 systems, beginning in 2008 I took over responsibility for the operations of an existing
18 rural sewer district. I acted as the administrator of this system, managing the system's
19 operations, testing, maintenance, billing, emergency response, accounts
20 payable/accounts receivable, collections, budgeting, customer service, and public
21 meetings required to service the community.

22 In late 2010, after working on several small, failing water and wastewater
23 systems, I created a business plan to acquire and recapitalize failing systems as
24 investor-owned, regulated water and wastewater utility companies. In early 2011, I
25 went to the capital markets to raise money to implement my plan. Over a period of

1 approximately three years, I met with over fifty-two infrastructure investment groups
2 trying to raise necessary financing. In February 2014, I achieved my goal, and used
3 the debt and equity capital I was able to raise to start CSWR. In 2018, I was able to
4 attract an additional large institutional private equity investor, which allowed me to
5 expand the scope of my business plan.

6 Since its formation, CSWR has acquired, and currently is operating through
7 various affiliates, systems that serve approximately 177,000 water and/or wastewater
8 connections in Missouri, Kentucky, Louisiana, Texas, Arkansas, Tennessee,
9 Mississippi, Arizona, North Carolina, South Carolina, and Florida. Utilities within the
10 CSWR affiliate group have additional applications pending in several of these states,
11 which seek authorization from state utility regulators to acquire even more systems and
12 customers. A corporate organization chart is attached hereto as **Exhibit JC-1**. For all
13 companies shown in that Exhibit, Central States serves as the designated manager.

14 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE FLORIDA PUBLIC**
15 **SERVICE COMMISSION (“COMMISSION”)?**

16 A. Yes. In addition to my testimony before numerous state utility commissions outside
17 Florida, I previously appeared before the Commission in support of various of the
18 Company’s applications to acquire water and wastewater systems in Florida.

19 **Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY IN SUPPORT OF**
20 **CSWR-FLORIDA’S REQUEST TO INCREASE ITS SERVICE RATES?**

21 A. The purpose of my direct testimony is fourfold. ***First***, I will briefly describe CSWR-
22 Florida’s operations, including a general description of the condition of the systems the
23 Company acquired. ***Second***, I will generally describe CSWR-Florida’s request for a
24 rate increase, why that increase is necessary, and why the Commission should grant the
25 Company’s request. In this section, I will also introduce the various CSWR-Florida

1 witnesses providing direct testimony in this case and identify the topics and issues
2 covered in each witness's testimony. ***Third***, I will briefly describe and discuss CSWR-
3 Florida's requests to recover acquisition adjustments for its North Peninsula (Docket
4 No. 20250038-WS), Aquarina (Docket No. 20250043-WS), and Sunshine (Docket No.
5 20250047-WS) systems, which are based on the Commission's rule governing
6 recovery of acquisition adjustments (Rule 25-30.0371. F.A.C.). This portion of my
7 direct testimony will be somewhat limited because even though the Company is
8 seeking in this case to include the acquisition adjustments in the rate base the
9 Commission uses to set rates, acquisition adjustment requests for each of the systems I
10 just mentioned are the subjects of separate dockets dealing exclusively with that issue.
11 ***Fourth***, I will discuss CSWR-Florida's request to consolidate rates across all its Florida
12 water and wastewater systems. This portion of my direct testimony will discuss how
13 consolidation helps mitigate rate shock and encourages the acquisition of small,
14 distressed systems by companies like CSWR-Florida.

15 **Q. ARE YOU SPONSORING ANY EXHIBITS?**

16 A. Yes, I am sponsoring the following exhibits:

17 **Exhibit JC-1:** Corporate Organization Chart

18 **Exhibit JC-2:** Florida Service Area Map

19 **Q. WERE THESE EXHIBITS PREPARED BY YOU OR YOUR STAFF UNDER**
20 **YOUR SUPERVISION AND CONTROL?**

21 A. Yes.

22 **DESCRIPTION OF CSWR-FLORIDA'S OPERATIONS**

23 **Q. PLEASE DESCRIBE THE COMPANY'S CURRENT WATER AND**
24 **WASTEWATER UTILITY OPERATIONS IN FLORIDA.**

25 A. CSWR-Florida currently provides water and/or wastewater service to customers

1 located in the following counties: Brevard, Citrus, Duval, Highlands, Marion, and
2 Volusia. As of the end of the January 31, 2025, test year, CSWR-Florida provided
3 service to approximately 12,600 water connections through 29 water systems and
4 wastewater service to approximately 7,500 wastewater connections through 9
5 wastewater systems. A map showing CSWR-Florida's service area is attached to my
6 direct testimony as **Exhibit JC-2**. In his direct testimony, Mr. Jacob Freeman CSWR's
7 Director of Engineering describes and discusses each of the water and wastewater
8 systems the Company currently owns and operates. As of the date of this testimony,
9 CSWR-Florida has invested more than \$74 million to acquire, upgrade and improve,
10 and operate its water and wastewater systems. This includes working capital necessary
11 to cover operating losses totaling \$5 million.

12 **Q. DOES CSWR-FLORIDA PROPOSE TO ACQUIRE ADDITIONAL SYSTEMS**
13 **IN FLORIDA?**

14 A. Yes. CSWR continues to look for water and wastewater systems that may be available
15 for sale and hopes to acquire even more Florida systems in the future.

16 **Q. PLEASE DESCRIBE THE GENERAL NATURE AND CONDITION OF THE**
17 **WATER AND WASTEWATER SYSTEMS ACQUIRED BY CSWR-FLORIDA.**

18 A. In his direct testimony, Mr. Freeman provides a detailed description of the condition of
19 each of the water and wastewater systems the Company has acquired and that are
20 included in this rate case. His testimony amply demonstrates the deteriorated state of
21 the plant facilities we acquired, the generally poor history these systems had complying
22 with applicable health, safety, and environmental regulations, and the challenges these
23 systems present in terms of the capital improvements required to address those issues
24 for the present and future. That said, I can provide a general description of the water
25 and wastewater systems, including providing some highlighted examples. I won't

1 burden the record by repeating information included in Mr. Freeman’s testimony, but
2 I will note that since its initial acquisition in Florida in 2022 CSWR Florida has invested
3 more than \$74 million to repair, renovate, upgrade, and improve the water and
4 wastewater systems we acquired. And the Company is prepared to make additional
5 investments necessary to bring those systems to a point where they can operate in a
6 manner that complies with all health, safety, and environmental regulations and ensure
7 customers receive safe and reliable service.

8 **Q. CAN YOU BRIEFLY COMMENT ON THE IMPORTANCE OF**
9 **COMPLIANCE AND SYSTEM MAINTENANCE AND INVESTMENT?**

10 A. Yes. Most people take the provision and availability of water and wastewater services
11 for granted. The public generally does not give much thought to the safety of water
12 and wastewater, largely because the quality and reliability of water and wastewater are
13 generally high in most parts of the country. Indeed, it is CSWR’s experience in Florida
14 and elsewhere in its eleven-state footprint that most water and wastewater customers
15 cannot name even basic components of a water or wastewater systems serving their
16 community.

17 Ensuring water and wastewater systems operate properly and provide safe and
18 reliable service is due, in large part, to how those systems are maintained and whether
19 necessary investment has been made to upgrade and replace system components. If a
20 system is not well-maintained and falls into a state of disrepair and deterioration, the
21 safety and reliability of the service that system can provide will deteriorate as well.
22 Service will become increasingly less safe and less reliable, which can have severe and
23 detrimental impacts on the health and well-being of customers.

24 The deterioration of assets providing service and the quality of service they can
25 provide also adversely impacts their ability to consistently comply with applicable

1 health, safety, and environmental regulations. And, as is described in detail in Mr.
2 Freeman's direct testimony, each of the systems included in this rate case recorded
3 numerous incidents of non-compliance during the five-year period immediately
4 preceding their acquisition by CSWR Florida. Those regulations ensure water and
5 wastewater service are provided in a manner that is safe for both the customers and the
6 environment in which they live and failure to comply with the regulations poses risks
7 to both. CSWR Florida takes seriously its obligation to provide safe, reliable, and
8 compliant utility services, and the Company is committed to making plant investments
9 and operation changes necessary to ensure its systems can consistently comply with
10 applicable regulations.

11 **Q. HAVE CUSTOMERS EXPERIENCED TANGIBLE BENEFITS FROM CSWR-**
12 **FLORIDA'S ACQUISITION OF THESE SYSTEMS?**

13 A. Yes. As is explained in the direct testimonies of Messrs. Todd Thomas, Aaron Silas,
14 and Michael Duncan, in addition to its ability and willingness to make required capital
15 improvements to these systems, CSWR Florida already has provided levels of
16 technical, managerial, and financial capability and expertise not present at the acquired
17 systems under previous ownership. Therefore, customers are receiving improved water
18 and wastewater services since the Company's acquisition of these systems.

19 In addition, CSWR Florida is able to provide these services to its customers by
20 leveraging the economies of scale inherent from its affiliation with CSWR and the
21 eleven-state affiliated group of utilities for which CSWR provides services. A prime
22 example is discussed in Mr. Silas's direct testimony. It would be impossible for a small,
23 stand-alone, water/wastewater system to provide twenty-four hours a day/seven days a
24 week customer service to the limited number of customers such systems routinely
25 serve. But, because of its affiliation with a large number of systems over the affiliate

1 group's eleven-state footprint that have similar service requirements, CSWR Florida is
2 able to benefit from the systems and structures CSWR has put in place to serve those
3 affiliates and the economies of scale it has been able to realize. The same economies
4 of scale that apply to the customer service function also allow CSWR Florida to cost-
5 effectively receive and benefit from other professional services CSWR provides,
6 including finance, accounting, billing, human resources, engineering, information
7 technology, regulatory support, corporate communications, legal, and overall
8 managerial support. Because of the small size of each of the individual systems the
9 Company has acquired, it would have been virtually impossible for the previous owners
10 to cost-effectively provide a similar level of services on a stand-alone basis.

11 **RATE CASE OVERVIEW**

12 **Q. HOW DID CSWR FLORIDA CALCULATE THE LEVEL OF RATE**
13 **INCREASE IN THIS CASE?**

14 A. This is CSWR Florida's initial general rate case, and the Company requested and the
15 Commission has approved the use of a historic test year ending January 31, 2025, to
16 calculate the revenue requirement. This test year fairly represents a normal, full year of
17 operations; however, our filing also includes pro forma adjustments to expenses and
18 revenues to reflect known and measurable changes in expenses that will be incurred
19 during the period rates set in this case will be in effect and also to annualize data for
20 systems CSWR-Florida did not own during the entirety of the test year. A more
21 detailed discussion of the revenue requirement and how it was calculated is contained
22 in the direct testimony of Mr. Brent Thies, CSWR's Vice President and Corporate
23 Controller.

24 **Q. PLEASE SUMMARIZE THE RATE INCREASE THAT CSWR FLORIDA IS**
25 **PROPOSING IN THIS CASE.**

1 A. CSWR Florida is asking that the Commission approve a total annual revenue
2 requirement for the water operations of \$7,076,871.00. Based on adjusted current
3 revenues of \$3,853,102.03 this represents an annual increase of \$3,223,768.97. For its
4 wastewater operations, the Company is seeking a total annual revenue requirement of
5 \$4,287,199.83. Based on adjusted current revenues are \$3,332,318.59, this represents
6 an annual increase for wastewater operations of \$954,881.24. The specific elements of
7 these revenue requirements and how each was derived are discussed in detail in Mr.
8 Thies's direct testimony.

9 **Q. WHAT WITNESSES ARE PROVIDING DIRECT TESTIMONY IN SUPPORT**
10 **OF THE COMPANY'S RATE INCREASE REQUEST AND WHAT SUBJECTS**
11 **WILL EACH OF THOSE WITNESSES ADDRESS?**

12 A. Including me, a total of six witnesses will provide direct testimony in support of the
13 proposed rate increase. The other witnesses and the subjects they will cover in their
14 respective testimonies are as follows:

- 15 ● Todd Thomas – Mr. Thomas, CSWR's Senior Vice President, will discuss CSWR
16 Florida's use of third-party contractors to perform operations and maintenance
17 services and the process the Company uses to qualify and select those contractors.
- 18 ● Mike Duncan – Mr. Duncan, CSWR's Vice President, will discuss CSWR-
19 Florida's request to consolidate its rates statewide and how consolidation will help
20 stabilize rates, mitigate rate shock, and encourage the acquisition of small,
21 distressed systems.
- 22 ● Aaron Silas – Mr. Silas, who serves as CSWR's Assistant Vice President –
23 Customer Experience and Regulatory Operations, will testify to our consolidated
24 customer service and communications initiatives and related economies of scale,
25 rate design, and the proposed water and wastewater tariffs.

- 1 ● Brent Thies – Mr. Thies, CSWR’s Vice President and Corporate Controller, will
2 testify about development of the proposed test year revenue requirement, including
3 annualization of operating expenses and test period revenues, depreciation expense,
4 income taxes, and development of the rate base, which includes acquisition
5 adjustments for the former North Peninsula, Aquarina, and Sunshine systems. He
6 also will describe the accounting controls and budget procedures in place at CSWR
7 and CSWR Florida,
- 8 ● Jacob Freeman – In his capacity as CSWR’s Director of Engineering, Mr.
9 Freeman’s direct testimony identifies each of the acquired water and/or wastewater
10 systems that are included in this case, describes each system’s condition at
11 acquisition, discusses each system’s pre-acquisition compliance history, describes
12 actions taken to date to restore, improve, and upgrade each of the acquired systems,
13 and set’s out CSWR Florida’s plans for longer-term improvements.

14 **Q. ARE THE PROPOSED RATE INCREASES REASONABLE?**

15 A. Yes. As mentioned above, and as set forth in the direct testimony of our witnesses, the
16 systems CSWR Florida acquired were typically poorly managed and the previous
17 owners lacked the technical, managerial, and financial ability to make the necessary
18 capital investments to ensure regulatory compliance and provide safe, efficient, and
19 reliable service to customers. Moreover, most of the previous owners failed to seek
20 timely rate increases necessary to properly operate and maintain the systems. As a
21 result, at the time of acquisition many of these systems were losing money, which
22 means the rates the Company adopted when it acquired these systems – *i.e.*, rates in
23 effect at closing – were not fully compensatory even under the cost and investment
24 structures previously in place. The additional costs CSWR Florida has and continues
25 to incur to upgrade and improve the systems and operate them in a manner that ensures

1 customers receive safe and reliable service that complies with all applicable health,
2 safety, and environmental regulations have significantly increased operating losses. To
3 address those losses, CSWR Florida is forced to seek an increase in rates, which for
4 some of the systems included in this case have not changed for many years.

5 This rate filing is designed to achieve two primary objectives. First, the
6 Company wants to increase rates to a level that allows it to recover its reasonable
7 operating costs and provides a reasonable opportunity to earn a fair return on the
8 investments it has made to serve customers. This level of rate relief is necessary to
9 ensure customers continue to receive safe and reliable service and the systems serving
10 those customers can comply with applicable health, safety, and environmental laws and
11 regulations. Second, CSWR Florida seeks to unify its terms of service and consolidate
12 rates statewide in a manner that streamlines and simplifies the Company's tariff and
13 allows it to reflect the economies of scale and the benefits provided to all its Florida
14 customers.

15 **Q. WHY ARE THE RATE INCREASES THAT CSWR FLORIDA SEEKS IN THIS**
16 **CASE NECESSARY?**

17 A. There is no question that, from either an operating expense or a capital investment
18 standpoint, it costs more to professionally operate water and wastewater systems in a
19 manner that complies with applicable law and regulatory requirements than it costs to
20 operate failing, non-compliant systems. Several of the systems CSWR Florida acquired
21 had significant long-term compliance and operational issues and this rate request
22 reflects the increased capital and operating costs required to address those serious
23 deficiencies.

24 As an example, many systems did not have operational mechanical components
25 – e.g., severely deficient hydropneumatic tanks at the Sunshine water system and

1 various wastewater systems with pumps or other major system components that were
2 not functioning at all, and were in need of significant repairs or overhaul, or needed
3 replacement because they were at or near the end of their useful lives. There is an
4 obvious capital impact associated with the replacement of these failed components, but
5 something that is often forgotten is the fact that replacement of these failed components
6 also results in an immediate increase in operating costs. For this and other reasons, it
7 costs more to professionally operate a system, both from a capital investment and
8 operating cost standpoint, than it does to operate a failing, non-compliant system.

9 Finally, as I mentioned earlier, many of the systems included in this case have
10 not had rate increases in many years. Consequently, the rates in effect at acquisition,
11 which CSWR Florida adopted, do not come close to covering current operating and
12 compliance costs, including recent inflation-driven cost increases. Therefore, the rate
13 increase proposed in this case seeks not only to recover the increased operating
14 expenses for these systems, but also a fair return on the value of the investments made
15 in these systems to ensure they comply with applicable laws and can provide safe and
16 reliable service to customers.

17 **Q. HOW DOES THE COMPANY PROPOSE TO MITIGATE THE EFFECT ON**
18 **CUSTOMERS OF THE RATE INCREASES IT SEEKS IN THIS CASE?**

19 A. CSWR Florida acknowledges that rates required to cover increases in operating costs
20 and provide a fair rate of return may significantly increase customers' monthly costs
21 for water or wastewater service. This effect will be especially substantial if rates are set
22 on a system-specific basis for the worst systems the Company acquired – those
23 requiring significant increases in required capital investment and operations and
24 maintenance costs. To mitigate the effect of these investment and cost increases,
25 CSWR Florida proposes to consolidate its rates on a statewide basis. It is well

1 established that consolidating costs and rates across an increasingly large customer base
2 can mitigate the amount of required rate increases, especially for the most deficient
3 systems. Consolidated rates also streamline and simplify the Company's tariff and
4 enable customers to share and benefit from the economies of scale and other benefits
5 from the consolidation of many smaller systems under a single, statewide utility
6 operating company.

7 **INCLUSION OF ACQUISITION ADJUSTMENTS IN RATE BASE**

8 **Q. EARLIER IN YOUR TESTIMONY YOU STATED THE RATE BASE CSWR**
9 **PROPOSES FOR RATEMAKING PURPOSES IN THIS CASE INCLUDES**
10 **ACQUISITION ADJUSTMENTS FOR THREE OF THE SYSTEMS THE**
11 **COMPANY ACQUIRED. PLEASE EXPLAIN.**

12 A. Generally speaking, an acquisition adjustment allows a utility to include in rate base
13 the portion of an acquisition purchase price that exceeds the net book value (NBV) of
14 the acquired assets. However, the acquisition adjustment the Company seeks in this
15 case includes, in addition to the difference between NBV and purchase price,
16 transactional and regulatory costs associated with its acquisitions. As I stated earlier in
17 my direct testimony, the rate base CSWR Florida proposes to use to set rates in this
18 case includes this acquisition adjustment, for the following systems: the wastewater
19 system acquired from North Peninsula Utilities Corporation, the water and wastewater
20 systems acquired from Aquarina Utilities, Inc., and the water systems acquired from
21 Sunshine Utilities of Central Florida, Inc.

22 **Q. DOES ALLOWING THE RECOVERY OF AN ACQUISITION ADJUSTMENT**
23 **ASSOCIATED WITH THE PURCHASE OF DISTRESSED WATER AND**
24 **WASTEWATER SYSTEMS REPRESENT SOUND REGULATORY POLICY?**

25 A. Yes. The regulatory, investment, and operational risks and challenges associated with

1 the acquisition of smaller, distressed water and wastewater systems justify a method
2 for calculating the post-acquisition rate base of such systems in a manner that differs
3 from the method applicable to large, mature, well-established, electric, gas, water, and
4 wastewater utilities. Through its acquisition of literally hundreds of small water and
5 wastewater systems across its eleven-state footprint, CSWR has learned that owners of
6 most small water and wastewater systems, including systems in severe financial,
7 operational, or regulatory distress, are unwilling to sell those systems for a purchase
8 price equal to or less than the net book value of their assets. This is the case because
9 despite the system's problems those owners still receive financial benefit from being
10 the system's owner. Under such circumstances, regulatory policy that prevents a
11 potential buyer from earning a return on or recovering any portion of a purchase price
12 that exceeds net book value creates a disincentive for larger, better managed, and better
13 capitalized utilities to acquire small, distressed systems. Such disincentives can be
14 eliminated by regulatory policies that allow prospective buyers the opportunity to
15 include in the formula used to set future rates all or a portion of a purchase price that is
16 above net book value.

17 **Q. HAVE THE BENEFITS OF THE REGULATORY POLICY THAT ALLOWS**
18 **RATE RECOGNITION OF ABOVE NET BOOK VALUE PURCHASE PRICES**
19 **BEEN WIDELY RECOGNIZED?**

20 A. Yes. For several decades, various utility regulatory groups have recognized the need
21 to encourage the acquisition of small water systems by larger, better managed and well-
22 capitalized water companies. Oftentimes, this has focused on the need to allow
23 recovery of some acquisition price above net book value.

24 **Q. WHAT SUPPORT CAN YOU PROVIDE FOR YOUR STATEMENT?**

25 A. In October 2011, in its report entitled *The Small Water Company Dilemma: Processes*

1 *and Techniques for Effective Regulation*, the National Regulatory Research Institute
2 succinctly framed the problem associated with the traditional regulatory model for
3 dealing with problems associated with small water systems and said the following
4 regarding a possible solution:

5 When dealing with small water systems, the traditional regulatory model
6 breaks down, for three main reasons. First, the primary tool employed by
7 regulatory commissions to induce improved performance is the ability to
8 reward or penalize shareholders, thereby focusing the attention of utility
9 management on particular issues of importance to regulators. Because
10 many small water systems have part-time, often absentee management and
11 part-time employees, and because these systems contribute little or no
12 compensation to the owners, that tool is ineffective. Second, most
13 regulatory processes and tools, including filing requirements, templates,
14 and timelines, require substantial utility staff, systems, and expertise that
15 small systems do not have. Third, at the most basic level, many small
16 systems do not have the scale to be viable operationally and financially;
17 therefore, no amount of regulation, incentive or otherwise, will work in the
18 long term.

19 The solution to the myriad problems associated with regulating small water
20 systems is not simple. As the report indicates, “[s]ometimes the best option is to get the
21 existing owner / operator out of the water business, using whatever means are available
22 under the commission’s authority.”¹ Ultimately, the report concludes that one of the
23 best “means” available under a commission’s authority is the recovery of an acquisition

¹ *Id.* at page 16.

1 adjustment. In fact, the report concludes that, while an acquisition adjustment may lead
2 to higher rates in the short term, rates will decline over the long term as costs are spread
3 over a larger customer base.

4 While some of the incremental costs of bringing the system up to par are in
5 a sense absorbed by the economies of scale of the acquiring system, there
6 may be an acquisition premium involved or the new system may need an
7 infusion of capital. The commission must recognize those costs and allow
8 them in the cost structure of the acquiring system, or the process of
9 improving the small, acquired system will be offset by a deterioration, albeit
10 much smaller in scale, of the acquiring company.

11 * * * * *

12 The consequences to the acquiring system, when looked at in isolation, are
13 not very appealing. But over the long term, as consolidation occurs, fixed
14 costs and associated rates of the acquiring system decline on a unit basis
15 as they are spread over a larger customer base. (emphasis added)

16 * * * * *

17 If the mandatory option is not available statutorily, commissions have a
18 variety of incentive and penalty mechanisms to encourage acquisitions.
19 Potential incentives include recognition of an acquisition premium, as
20 well as incentive rate of return, zone rates, or phase-ins of rate increases.

21 (emphasis added)

22 **Q. DID THIS REPORT SEEK TO APPLY ITS CONCLUSIONS REGARDING**
23 **THE RECOVERY OF ACQUISITION ADJUSTMENTS TO LARGER**
24 **UTILITIES?**

25 A. No. The authors were very clear that their conclusions should only apply to “special

1 cases” including small, troubled, non-viable systems. The report emphasized the
2 limitation as follows:

3 Observation: Most commissions have an aversion to allowing recovery of
4 an acquisition premium by the acquiring entity. Many jurisdictions will
5 allow recovery of an acquisition premium in special cases. *A classic special*
6 *case in which premiums are allowed is the commission-mandated or*
7 *commission-encouraged takeover of a troubled system.* (emphasis added)

8 Such a premium is typically not allowed in a takeover of a well-performing
9 system. We would call this a perverse incentive. *Small systems present an*
10 *interesting conundrum that we think mandates a revisit.* (emphasis
11 added)

12 **Q. DO YOU HAVE ANY OTHER EVIDENCE SUPPORTING THE**
13 **REGULATORY POLICY PERSPECTIVE ALLOWING RECOVERY OF**
14 **ACQUISITION ADJUSTMENTS?**

15 A. Yes. The treatise *Accounting for Public Utilities* discusses the rationale underlying the
16 historic reason for disallowing recovery of acquisition adjustments but also discusses
17 the situations in which state utility commissions have deemed it appropriate to allow
18 recovery of such adjustments. The reasons most commonly cited for allowing rate base
19 treatment of acquisition adjustments are as follows:

- 20 • when acquisitions represent an essential or desirable part of an integration of
21 facilities program devoted to service the public better;
- 22 • when acquisitions are clearly in the public interest, because operating efficiencies
23 purchased offset the excess price over net original cost; and
- 24 • when acquisitions are determined to involve arm’s-length bargaining.

1 Q. YOU MENTIONED PREVIOUSLY THAT THE ACQUISITION AND
2 CONSOLIDATION OF SMALL WATER AND WASTEWATER SYSTEMS
3 TYPICALLY REQUIRES SOME ENCOURAGEMENT BY STATE
4 REGULATORS IN THE FORM OF AN ACQUISITION ADJUSTMENT.
5 WHAT IS THE COMPANY’S EXPERIENCE WITH OTHER STATE UTILITY
6 COMMISSIONS ALLOWING ACQUISITION ADJUSTMENTS?

7 A. CSWR’s utility affiliates now operate in eleven states so our affiliate group is very
8 familiar with various mechanisms state utility regulators use to encourage the
9 acquisition of small water and wastewater systems. In addition to Florida, such
10 mechanisms are in place in Arizona, Texas, and Tennessee, each of which is designed
11 to encourage the acquisition and consolidation of small systems by a larger water
12 utility.

13 Texas: On August 20, 2020, the Public Utility Commission of Texas adopted
14 Rule 24.41(d) regarding the recovery of positive acquisition adjustments (“When a
15 utility acquires plant, property, or equipment for which commission approval is
16 required under §24.239 of this title, relating to Sale, Transfer, Merger, Consolidation,
17 Acquisition, Lease or Rental, a positive acquisition adjustment will be allowed. . .”).

18 Tennessee: In 2021 the Tennessee Public Utility Commission adopted Rule
19 1220-04-14-.04 related to the recovery of an acquisition adjustment. That rule sets out
20 specific factors to be considered including, improvements in public utilities services
21 resulting from the acquisition; remediation of public health, safety and welfare
22 concerns; and the financial situation of the operationally troubled system.

23 Q. YOU STATED PREVIOUSLY THAT OWNERS OF SMALL SYSTEMS
24 TYPICALLY REFUSE TO SELL FOR NET BOOK VALUE. CAN YOU
25 EXPAND ON YOUR PREVIOUS TESTIMONY REGARDING THAT

1 **CIRCUMSTANCE?**

2 A. There are many reasons. For example, the current owner, regardless of their managerial
3 and technical competency, may perceive that a system provides an opportunity for
4 increased revenue and profits over and above what the utility currently receives. This
5 would particularly be the case for a system that may be capable of organic growth.
6 Therefore, the current owner perceives that future revenues justify a sales price in
7 excess of net book value.

8 Another common reason is because the current owner may also be the primary
9 operator of the system. In the ratemaking formula, rates typically include not only a
10 return on invested capital but also recovery of operating expenses. Operating expenses
11 include salaries of employees that operate the systems, but also those that handle
12 billing, regulatory, bookkeeping and management functions. Therefore, an owner that
13 is also an employee responsible for operations, billing, and other functions may also
14 receive recovery in rates a salary for all those activities. Because the owner of a small
15 system may not have another job or income stream, that owner will not be willing to
16 give up the regular salary for an acquisition price based solely upon net book value.
17 Instead, the owner will demand as part of the purchase price some recognition of the
18 lost income stream associated with the proposed sale transaction. As such, a premium
19 above net book value must be paid to incentivize the owner to sell the small, distressed
20 water or wastewater system. Given this reality, it would be inequitable to expect an
21 acquiring company to pay this premium to acquire the system but then disallow it in
22 the calculation of post-acquisition rates.

23 **Q. DOES THE RECOVERY OF AN ACQUISITION ADJUSTMENT CREATE AN**
24 **INCENTIVE FOR A UTILITY TO OVERPAY IN AN ACQUISITION?**

25 A. No. There is no incentive for a company like CSWR Florida to overpay for any

1 acquisition. The Company must still raise the capital necessary to pay the full purchase
2 price and there is no incentive to increase the purchase price any more than is absolutely
3 necessary if there is a chance regulators will not allow any return on or return of the
4 portion of the purchase price above net book value. A prudent investor does not assume
5 more regulatory risk than is absolutely necessary to complete a transaction.

6 In addition, our affiliate group is constantly in search of acquisition
7 opportunities in Florida and elsewhere. And while we are confident we have access to
8 capital sufficient to acquire systems we decide to buy, make investments in those
9 systems required to ensure they comply with applicable law and provide customers safe
10 and reliable service, and provide sufficient working capital to operate those systems
11 until fully compensatory rates can be set sometime in the future, CSWR's supply of
12 available capital is not limitless. Therefore, it would be foolish for CSWR or its
13 affiliates to spend more than necessary on any individual transaction because capital
14 not expended to purchase one system can be deployed to purchase another or make
15 upgrades and improvements to systems our group already has acquired.

16 **Q. PLEASE DISCUSS THE IMPORTANCE TO COMPANIES LIKE CSWR**
17 **FLORIDA, WHICH REGULARLY ACQUIRE SMALL WATER AND**
18 **WASTEWATER SYSTEMS, OF A PREDICTABLE REGULATORY POLICY**
19 **THAT ENCOURAGES SUCH ACQUISITIONS.**

20 A. Like all other states, Florida's water and wastewater utility industry has historically
21 been highly fragmented, with numerous small systems spread across the state. This is
22 problematic because small water/wastewater utilities often lack an ability to raise
23 necessary capital for repairs and replacement of facilities, lack management and
24 technical expertise necessary to plan for growth or to meet ever changing regulatory
25 requirements, and do not have enough customers to provide a revenue base large

1 enough to support rates necessary to fund required investments and operating costs on
2 a stand-alone basis.

3 However, absent regulatory support, which includes a real prospect for
4 recognition of an acquisition premium as part of the formula used to set future rates,
5 companies like CSWR Florida, which have the capacity to acquire, consolidate, and
6 successfully operate small water and wastewater utilities, have no incentive to do so.
7 Indeed, concerns they will not be allowed to recover any portion of an above net book
8 value purchase price or the transactional and regulatory costs required to complete such
9 acquisitions are a major disincentive to potential purchasers. Without clear and
10 consistent regulatory support, the kinds of acquisitions regulators should want to
11 encourage either will not be made at all or will be made much less frequently.

12 **Q. YOU PREVIOUSLY NOTED THE COMMISSION’S ADOPTION OF RULE**
13 **25-30.0371 GOVERNING ACQUISITION ADJUSTMENTS. WHAT IS YOUR**
14 **UNDERSTANDING OF WHAT THAT RULE REQUIRES A UTILITY TO**
15 **SHOW TO RECOVER AN ACQUISITION PREMIUM ADJUSTMENT?**

16 A. Commission Rule 25-30.0371 establishes two sets of requirements for recovery of an
17 acquisition premium – one if the utility from which a system is acquired is found to be
18 “non-viable” and another if it is found to be “viable.” Under the rule, a utility is
19 considered “non-viable” if it is currently unable or projected to be unable to provide
20 and maintain safe, adequate and reliable service and facilities over the five-year period
21 following the date of its acquisition due to its:

- 22 • failure to comply with federal, state, or local regulations governing primary or
23 secondary water quality or other health, safety, or environmental standard or has a
24 history of violations of such regulations or standards, and
- 25 • has a record of insufficient investment, repair or maintenance of assets or an

1 inability to acquire and maintain adequate managerial, operational, financial, or
2 technical capabilities to ensure safe and reliable Service OR is insolvent, i.e. unable
3 to pay its debts.

4 A “viable” utility is one that does not satisfy the rule’s definition of “non-viable.”

5 The rule allows companies that acquire non-viable utilities to recover a full or
6 partial acquisition adjustment if it can show its purchase price was made as part of an
7 arms-length transaction and customers of the acquired utility will benefit from the
8 acquisition. Factors the Commission should consider in deciding whether an
9 acquisition adjustment should be authorized are stated in subsection (3)(a) of the rule.

10 Companies that acquire viable utilities may also recover a full or partial
11 acquisition adjustment, however the evidence required to support such a request differs
12 from what is applicable to transactions involving non-viable utilities. Companies that
13 acquired a viable utility must show the purchase price was made as part of an arms-
14 length transaction and must also show that allowing the acquisition adjustment is
15 projected to provide a positive cumulative present value of the acquiring utility’s
16 revenue requirement (“CPVRR”) over the five-year period immediately following the
17 acquisition. However, if the CPVRR does not result in a positive customer benefit over
18 that period, subsection (4)(a) of the rule lists alternative benefits the Commission
19 should consider.

20 The rule allows a utility seeking an acquisition adjustment to file its request
21 either as a stand-alone application (which must be filed within prescribed timeframes)
22 or as part of a general rate case.

23 **Q. PLEASE DISCUSS THE ACQUISITION ADJUSTMENTS CSWR FLORIDA IS**
24 **SEEKING TO RECOVER IN THIS CASE.**

25 **A.** As mentioned earlier in my testimony, CSWR Florida has included in the revenue

1 requirement in this case acquisition adjustments related to three transactions: the
2 acquisition of a wastewater system from North Peninsula Utilities Corporation, the
3 acquisition of water and wastewater systems from Aquarina Utilities, Inc., and the
4 acquisition of several water systems from Sunshine Utilities of Central Florida, Inc.
5 The Company has opted to request those acquisition adjustments in separate, stand-
6 alone dockets as permitted under Rule 25-30.0371. The docket numbers for those three
7 cases are, respectively, as follows: Docket No. 20250038-WS, Docket No. 20250043-
8 WS, and Docket No. 20250047-WS.

9 **Q. DO THE ACQUISITIONS YOU JUST MENTIONED QUALIFY FOR**
10 **ACQUISITION ADJUSTMENTS UNDER THE COMMISSION’S RULE?**

11 A. Yes. Because these three matters are each the subject of a separate Commission docket,
12 I don’t want to unnecessarily burden the record here with evidence that likely will be
13 repeated in those cases. But I would like to briefly summarize why the Commission
14 should recognize for ratemaking purposes all purchase price amounts paid above net
15 book value as well as all transaction and regulatory costs incurred to complete each of
16 the transactions.

17 **North Peninsula**: The North Peninsula wastewater system was non-viable at the time
18 of its acquisition by CSWR Florida. As I previously testified, a non-viable utility under
19 the Commission’s rule is one that is either unable to provide and maintain safe,
20 adequate, and reliable service and facilities to its customers, or that is insolvent. North
21 Peninsula was both -- it was unable to provide and maintain safe, adequate and reliable
22 service, and it was insolvent. Photographs attached to the Company’s petition in
23 Docket No. 20250038-WS show the North Peninsula wastewater system was falling
24 apart at the time of its acquisition. In addition, the years preceding the acquisition were
25 marked with relentless enforcement and compliance actions against the prior owner by

1 the Florida Department of Environmental Protection (“FDEP”) and Volusia County
2 (“County”). There also were many years of insufficient investment, repair and
3 maintenance of the system. At the time of acquisition, all three of North Peninsula’s
4 package sewage treatment plants were failing. And the available evidence demonstrates
5 North Peninsula was insolvent at the time of acquisition because in the years
6 immediately preceding the acquisition by the utility recorded several years of negative
7 net income from utility operations and its last-filed annual report showed
8 approximately \$230,000 in assets against \$1.3 million in liabilities. A company with
9 such a financial record cannot be expected to remain in business for long.

10 **Aquarina**: Like North Peninsula, the Aquarina water and wastewater systems were
11 non-viable at the time of acquisition. Aquarina was unable to provide and maintain
12 safe, adequate and reliable service, and its annual reports indicate it was insolvent. In
13 2021, as part of its pre-acquisition due diligence CSWR-Florida commissioned
14 engineering studies of the water and wastewater systems. Those studies indicated much
15 of the water and wastewater plant to be acquired was at or near the end of its useful
16 life. Indeed, the condition of most major plant components was evaluated to be only
17 “fair.” In addition, there had been many years of insufficient investment, repair and
18 maintenance of the system. Leading up to the acquisition, Aquarina also recorded
19 many years of negative net income from utility operations, and its financial records
20 reflected a retained earnings balance of negative (\$938,831) by 2021, indicating the
21 utility was insolvent.

22 **Sunshine**: The Sunshine water systems also were non-viable at the time of acquisition.
23 As part of its pre-closing due diligence, CSWR-Florida commissioned a non-affiliated
24 engineering firm to perform a preliminary engineering study for each of the twenty-
25 three Sunshine water systems. The engineering firm was able to observe the poor

1 quality of system assets, which suggests the systems were nearing the end of their
2 useful lives because of age, neglect, or a combination of both. In addition, Sunshine's
3 annual reports to the Commission reveal many years of insufficient investment and
4 inadequate expenditures for repair and maintenance of the systems. Those same annual
5 reports also show that during the period immediately preceding the acquisition
6 Sunshine experienced several years of negative net income from utility operations. The
7 cumulative effects of those earnings shortfalls caused the value of the enterprise to
8 decline, as reflected in Sunshine's negative retained earnings, which by 2020 was
9 negative (\$335,074).

10 The petitions in each of the aforementioned cases also show that customers have
11 benefitted from the Company's acquisition of those systems. For example, costs and
12 rates for the Aquarina system are projected to decrease under CSWR Florida's
13 ownership compared to those of the prior owner. Since the acquisition of each system,
14 CSWR-Florida has engaged in substantial repairs and upgrades to the systems to the
15 benefit of customers. Those repairs and upgrades, including before and after
16 photographs, are included in Mr. Freeman's direct testimony in this rate case. Customer
17 service improvements the Company has implemented include a call center that is
18 available 24 hours per day/7 days per week as well as electronic communications and
19 billing. Customers further benefit from economies of scale achieved through CSWR
20 Florida's access to CSWR's centralized engineering, accounting, billing, legal and
21 purchasing operations. The customers of the North Peninsula, Aquarina, and Sunshine
22 systems have already benefitted from CSWR Florida's acquisition and will continue to
23 benefit into the future as longer-term system upgrades, improvements, and
24 replacements are completed, which will ensure that, unlike in the pre-acquisition past,
25 the systems will be able to provide customers with safe and reliable service that

1 complies with applicable health, safety, and environmental laws and regulations.

2 **RATE CONSOLIDATION**

3 **Q. PLEASE DISCUSS THE COMPANY'S RATE CONSOLIDATION**
4 **PROPOSAL.**

5 A. CSWR Florida proposes to consolidate rates across all of its Florida water and
6 wastewater systems to mitigate "rate shock" to customers if rate increases, especially
7 those for systems requiring an immediate investment of substantial amounts of capital
8 and/or those with a relatively small number of customers, are calculated on a system-
9 specific basis. The reasons why statewide rate consolidation benefits Florida
10 customers is discussed in greater detail in the direct testimony of CSWR Florida's
11 witness Aaron Silas.

12 **Q. WOULD YOU BRIEFLY DESCRIBE SOME OF THE BENEFITS OF**
13 **CONSOLIDATED RATES AND TARIFFS?**

14 A. It has been CSWR's experience across its eleven-state footprint that consolidated
15 pricing results in several benefits. First, it is well-established that single tariff pricing
16 helps to encourage the acquisition of small, troubled water and wastewater systems by
17 spreading costs to a larger customer base. Second, the consolidation of systems into a
18 single tariff mitigates rate shock and makes service more affordable for all the
19 Company's Florida customers. Third, while there may be different technologies
20 utilized at different systems, all the Company's systems share many of the same costs
21 of service, which minimizes cross-subsidization as a rate consolidation concern.
22 Fourth, the development of a single set of tariffs provides for a heightened level of
23 regulatory, administrative, and billing efficiency. Specifically, CSWR Florida and the
24 Commission will not have to maintain multiple sets of rules and rates. Fifth, because
25 all systems will eventually require the same types of large capital investments over

1 time, any perceived inequities or subsidies associated with rate consolidation will
2 render those concerns invalid in the long-run. And lastly, because consolidated tariffs
3 provide a more simplified approach to rates and rules, they are more consumer friendly
4 than dozens of different rate sheets.

5 **Q. HAVE CONSOLIDATED RATES BEEN RECOGNIZED AS A SOLUTION TO**
6 **THE PROBLEM OF SMALL WATER AND WASTEWATER SYSTEMS?**

7 A. Yes. For years it has been recognized that single tariff pricing and the consolidation of
8 rates encourages the consolidation of small water and wastewater systems into larger
9 utilities. For instance, in a 2008 report, the National Regulatory Research Institute
10 stated:

11 Single tariff pricing is another way to encourage mergers. Enabling a
12 uniform rate structure or consolidated rates for systems owned by the same
13 entity may encourage a corporate utility to grow its business by acquiring –
14 whether contiguous or interconnected or not – other systems. With
15 consolidated pricing, customers pay the same price even though their
16 individual system may have unique operating characteristics and needs.
17 Single tariff pricing makes it easier to share costs among larger numbers of
18 customers.²

19 **Q. WILL CONSOLIDATED RATES REQUIRE CUSTOMERS SERVED BY**
20 **“BETTER” SYSTEMS TO SUPPORT THE COST OF IMPROVEMENTS**
21 **CSWR FLORIDA IS MAKING TO SOME OF ITS WORST SYSTEMS?**

22 A. No. Although there may appear to be subsidization in the short run, it isn't true if you

² *Small Water Systems: Challenges and Recommendations*, National Regulatory Research Institute (“NRRI”), February 7, 2008 (citing to *Joint Report of the US EPA and NARUC, Consolidated Water Rates: Issues and Practices in Single Tariff Pricing*, September 1999).

1 take a longer-term view. In each of the systems the Company owns and operates, all
2 the distribution and treatment systems will eventually require major repairs and
3 replacements. Some systems require more urgent investment; however, over time all
4 systems will require those same or similar investments. So, whatever short-term
5 subsidies may flow between at any particular point in a system's life cycle, that
6 situation will inevitably reverse over time.

7 I also note that average cost pricing and state-wide rates are the rule rather than
8 the exception in the broader utility industry. For example, although it may cost an
9 electric or gas utility much more to serve some individual customers than it does to
10 serve others, electric and gas utilities have for decades had uniform rates for all
11 customers within each rate class.

12 **Q. HAVE CONSOLIDATED RATES BEEN IMPLEMENTED FOR OTHER**
13 **CSWR AFFILIATES?**

14 A. Yes. CSWR affiliates operating in Louisiana, Mississippi, Texas, Missouri, and
15 Kentucky have all seen rates and tariffs for water and wastewater systems consolidated.
16 I believe the following language from a rate case decision by the Kentucky Commission
17 reflects the views of regulators in the states I just mentioned regarding the consolidated
18 rates they approved for our affiliates:

19 The Commission supports the principle that utility rates should be cost
20 based, and that in most circumstances each class of utility ratepayers should
21 pay the costs which the utility incurs to provide that class with utility
22 service. The majority of Bluegrass Water's customers are in the residential
23 class. A separate rate for each geographically distinct merged system of
24 Bluegrass Water would create unreasonable and undue hardship to

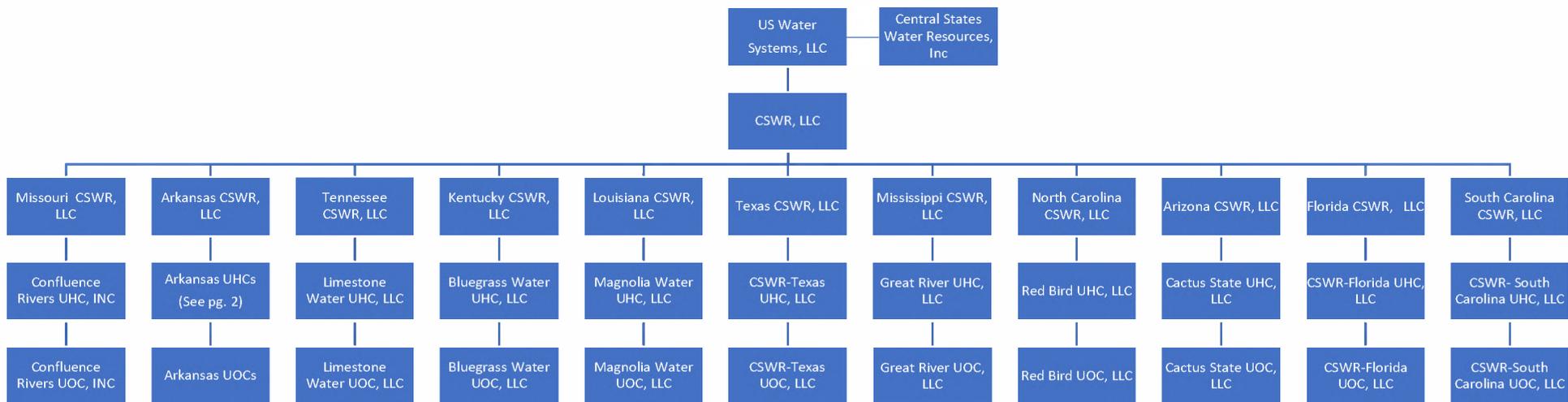
1 individuals in some areas served by Bluegrass Water.³

2 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

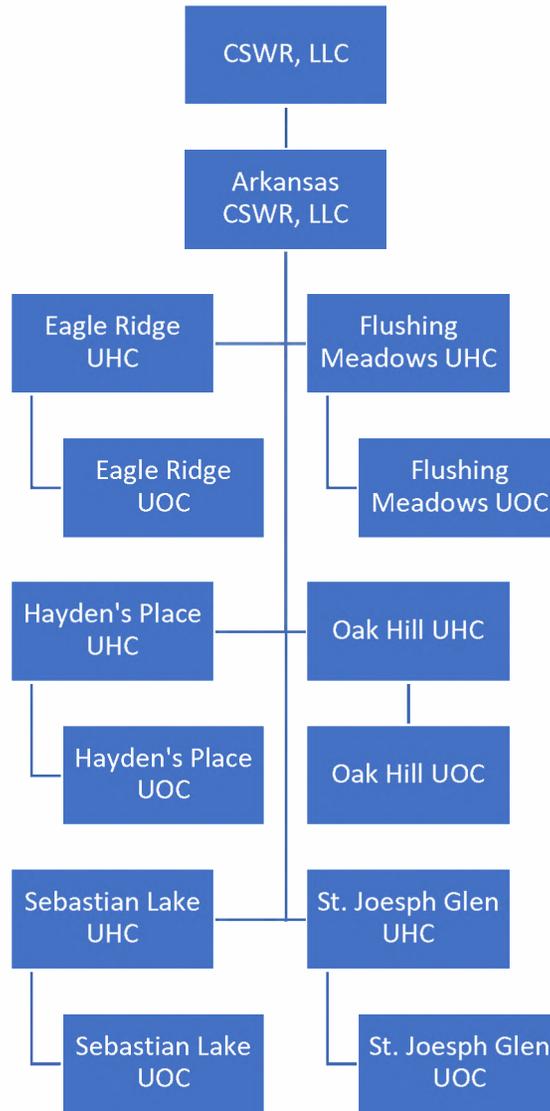
3 A. Yes it does.

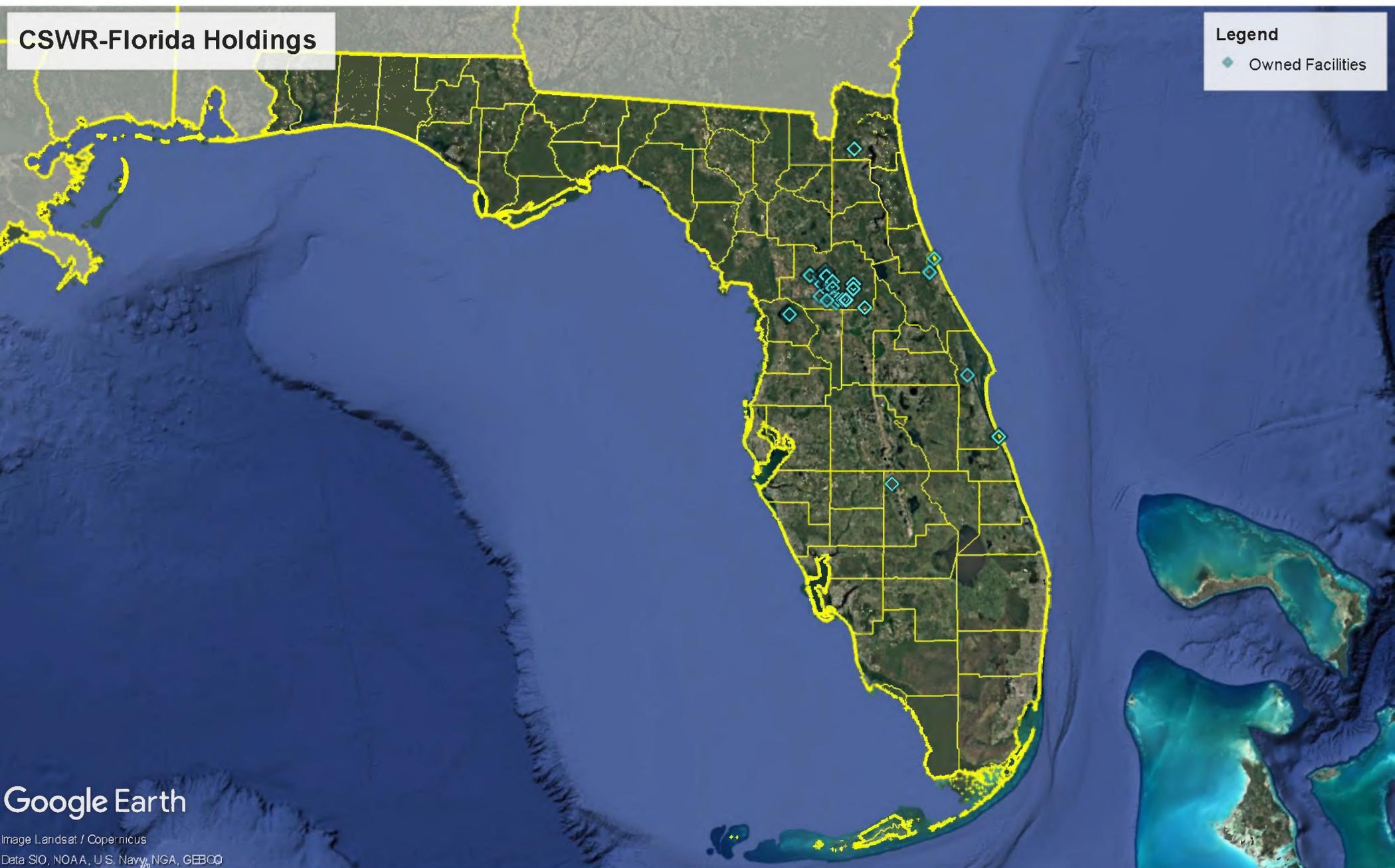
³ In re: Bluegrass Water Utility Operating Company, Case No. 2022-00432, issued February 14, 2024, at page 96.

Central States Water Resources Corporate Entity Organizational Chart



Arkansas CSWR Organizational Chart Detail





CSWR-Florida Holdings

Legend
◆ Owned Facilities