

**COMMONWEALTH OF KENTUCKY**  
**BEFORE THE PUBLIC SERVICE COMMISSION**

**IN THE MATTER OF:** )  
 )  
**THE VERIFIED JOINT APPLICATION OF** )  
**EASTERN ROCKCASTLE WATER ASSOCIATION** ) **CASE NO. 2017-00383**  
**AND KENTUCKY-AMERICAN WATER COMPANY** )  
**FOR THE TRANSFER OF CONTROL AND ASSETS** )

**JOINT APPLICANTS' REPLY BRIEF**

Kentucky-American Water Company (“KAW”) and Eastern Rockcastle Water Association (“ERWA”) (collectively, the “Joint Applicants”) hereby submit this joint reply brief in response to the Intervenor’s<sup>1</sup> December 29, 2017 Brief and in accordance with the Commission’s January 2, 2018 Order in this matter.

Joint Applicants filed this case to obtain the Commission’s approval of the sale of ERWA’s assets to KAW, as well as a “change of control” of utility services provided by ERWA to its customers. After the close of discovery and in their December 29, 2017 Brief, the Intervenor, for the first time, set forth the following arguments against the Joint Applicants’ proposed transaction: (1) the sale of assets is not “in accordance with law” because ERWA’s Board of Directors did not pass a formal written resolution recommending the sale;<sup>2</sup> (2) the proposed transaction is not consistent with the public interest because ERWA’s Board did not seek competitive bids;<sup>3</sup> and (3) ERWA’s Board did not provide “fair information” to ERWA’s customers as to the reasons for and the desirability of a deal with KAW.<sup>4</sup> These arguments are

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<sup>1</sup> Messrs. James E. Ballinger and Thomas P. Dupree, Jr. (“Intervenor”) intervened in this matter by Order of October 30, 2017.

<sup>2</sup> Intervenor’s Brief, pp. 2-3.

<sup>3</sup> Intervenor’s Brief, pp. 4-7.

<sup>4</sup> Intervenor’s Brief, pp. 7-8.

without merit or factual support. Therefore, as set forth below and in Joint Applicants' December 29, 2017 Brief, the proposed transaction must be approved because KAW has the "financial, technical, and managerial abilities to provide reasonable service"<sup>5</sup> to ERWA's customers and because the proposed transaction is "in accordance with law" and "consistent with the public interest."<sup>6</sup>

**I. ERWA's decision to enter into the September 19, 2017, Asset Purchase Agreement ("APA") with KAW was made "in accordance with law."**

The Intervenors essentially argue that the lack of a written board resolution from the ERWA Board should render the proposed transaction null and void. Joint Applicants have spent countless hours and significant resources to reach the point at which the proposed transaction is ripe for Commission decision. The Intervenors, consisting of a mere two customers who are apparently unhappy with the results of a 231-41 customer vote in favor of the proposed transaction, would have the ERWA Board start over in its efforts to sell ERWA's water system based on a ministerial record-keeping matter. The Intervenors' request for such a senseless waste of resources is that KRS 273.297, which applies to the sale of assets by a non-profit corporation, requires a written resolution from the ERWA Board recommending such sale. But no such written resolution is required, or, if it is, its purpose was achieved in all material respects. KRS 273.297 states as follows (emphasis added):

**273.297 Sale, lease, exchange, mortgage, or pledge of assets.**

A sale, lease, exchange, mortgage, pledge or other disposition of all, or substantially all, property and assets of a corporation may be made upon such terms and conditions and for such consideration, which may consist in whole or in part of money or property, real or personal, including shares of any corporation for profit, domestic or foreign, as *may* be authorized in the following manner:

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<sup>5</sup> KRS 278.020(6)

<sup>6</sup> KRS 278.020(7).

(1) If there are members entitled to vote thereon, the board of directors shall adopt a ***resolution recommending such sale***, lease, exchange, mortgage, pledge or other disposition and directing that it be submitted to a vote at a meeting of members entitled to vote thereon, which may be either an annual or a special meeting, written notice stating that the purpose, or one of the purposes, of such meeting is to consider the sale, lease, exchange, mortgage, pledge or other disposition of all, or substantially all, the property and assets of the corporation shall be given to each member entitled to vote at such meeting, within the time and in the manner provided by KRS 273.161 to 273.390 for the giving of notice of meetings of members. At such meeting the members may authorize such sale, lease, exchange, mortgage, pledge or other disposition and may fix, or may authorize the board of directors to fix, any or all of the terms and conditions thereof and the consideration to be received by the corporation therefor. Such authorization shall require at least two-thirds (2/3) of the votes which members present at such meeting or represented by proxy are entitled to cast. ***After such authorization by a vote of members, the board of directors, nevertheless, in its discretion, may abandon such sale, lease, exchange, mortgage, pledge or other disposition of assets, subject to the rights of third parties under any contracts relating thereto, without further action or approval by members.***

(2) If there are no members, or no members entitled to vote thereon, a sale, lease, exchange, mortgage, pledge or other disposition of all, or substantially all, the property and assets of a corporation shall be authorized upon receiving the vote of a majority of the directors in office.

First, the plain language of the statute says that a sale of assets “may” be authorized in the manner describe thereafter. Thus, although ERWA agrees that its governing corporate documents, common sense, and good judgment all made it appropriate for a customer vote to be taken on the proposed transaction, the statute itself says that approval “may” be authorized via a process beginning with a resolution. It does not say “shall.”

Second, even if a resolution is required, the statute does not say it must be a *written* resolution of the type Intervenors have in mind or that it has to say the phrase “corporate resolution” at the top. Indeed, communications from the ERWA Board to ERWA customers demonstrate that the intent and purpose of a “resolution recommending such sale” were met in all respects. The ERWA Board encouraged customers to come to the July 17, 2017 board

meeting at which a possible transaction with KAW would be discussed.<sup>7</sup> The minutes of that board meeting show that customers attended and the ERWA Board made a recommendation and decision to conduct a customer vote on the proposed transaction (“after much discussion the Board of Directors informed the customers, all ERWA customers will get a ballot through the mail and get to vote”).<sup>8</sup> No formal written resolution reflecting that decision was issued, but board resolutions are not required to be made in writing: “Resolutions need not be, in the absence of some express requirement, in any set or particular form. A resolution, particularly when used to express a ministerial act, need not partake of any definite form and need not be a written instrument.”<sup>9</sup>

Third, to the extent some sort of writing was required, the ERWA Board issued those writings after its July 17, 2017 board meeting. In letters to customers and in various public postings before the customer vote was taken, the ERWA Board made the following statements which are, in fact, the *exact* sort of recommendation contemplated by the statute:

This letter is being sent to all Eastern Rockcastle Water Association customers to inform them of a proposal by ERWA. The Board of Directors of Eastern Rockcastle Water Association has had many meetings looking for a solution to better serve our customers and after meeting with Kentucky American Water, we feel they are an excellent company that is better equipped to serve the needs of ERWA. Kentucky American Water is a large corporation that serves a large portion of Kentucky. They have the resources to provide better services than have been provided in the past by Eastern Rockcastle Water Association. If ownership

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<sup>7</sup> See Joint Applicants’ November 10, 2017 response to Item 1 of the Intervenors’ Request for Information, pp. 3 and 6 of 12.

<sup>8</sup> See the Joint Applicants’ November 6, 2017 response to Item 1 of Commission Staff’s First Request for Information, p. 8 of 27.

<sup>9</sup> *City of Cleveland v. Bradley County*, Case No. 030A01-9804-CV-00140, 1999 Tenn. App. LEXIS 261, at \*13 (Tenn. Ct. App. April 16, 1999) (internal citations omitted); *see also Steward v. Rust*, 252 S.W.2d 816 (Ark. 1952) (“Appellee says that, under the authority of *Hill v. City of Rector*, 161 Ark. 574, 256 S.W. 848, the election was void because no resolution was first presented. This case, however, does not define a ‘resolution.’ In our opinion a resolution, particularly when used to express a ministerial act by a deliberative body, need not partake of any definite form and need not be a written instrument.”).

stays with Eastern Rockcastle Association there will have to be a substantial rate increase.<sup>10</sup>

Finally, after the vote was taken and more than 85 percent of the voters voted to move forward with the KAW transaction, the ERWA Board did not consider the KAW proposal the “foregone conclusion” the Intervenors allege. Instead, the ERWA Board followed through on its effort to make sure ERWA received the best deal possible by considering a Western Rockcastle Water Association alternative and engaging in further negotiations with KAW.<sup>11</sup> Ultimately, the ERWA Board decided the proposed transaction with KAW was best and the ERWA Board voted 5-0 in favor of proceeding with the KAW deal.<sup>12</sup>

In summary, the absence of a formal written resolution from the ERWA Board is meaningless. ERWA has extremely limited resources. If anything, the “public interest” demands that a mere two dissatisfied voters should not be able to waste those resources by forcing any sort of “do-over” – especially when the overwhelming will of the overall customer base and the ERWA Board is to move forward with the KAW transaction.

**II. The ERWA Board worked diligently to find the best solution to meet its dire needs and provided accurate information to its customers, both of which mean that the proposed transaction is “consistent with the public interest.”**

All of the Intervenors’ discussion about competitive bidding, alleged misinformation, and guarding against “favoritism, extravagance, fraud, and corruption” is both misplaced and offensive and should not distract the Commission from what it is required to do in considering the “public interest” requirement of this case. As to that requirement, the Commission has held that its inquiry must remain focused “upon the qualifications of the acquiring party and the

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<sup>10</sup> See Joint Applicants’ November 10, 2017 response to Item 1 of the Intervenors’ Request for Information, pp. 2 and 4 of 12.

<sup>11</sup> See the Joint Applicants’ November 6, 2017 response to Item 1 of Commission Staff’s First Request for Information, p. 12 of 27.

<sup>12</sup> See ERWA’s December 4, 2017 response to Item 2 of the Intervenors’ Second Request for Information.

potential effects of the transfer actually before us.”<sup>13</sup> Here, it is undisputed that KAW is an appropriate acquiring party and the record proves that the sale to KAW is in the best interests of ERWA customers.

The Intervenors allege that the ERWA Board did not adequately consider or pursue alternatives beyond a sale to KAW, including the issuance of a request for bids. However, the Intervenors cite to no authority applicable to ERWA that required any sort of request for bids. But beyond that, the record demonstrates that the ERWA Board had worked for a long time with county officials in an effort to solve its problems. In late July 2017, when the ERWA Board issued its recommendation and made its decision to hold a customer vote, newspaper reports<sup>14</sup> documented the severity of ERWA’s problems. And those reports also chronicled ERWA Board President Russell Barron’s and Rockcastle County Judge/Executive Doug Bishop’s efforts to find possible purchasers before finding KAW. One newspaper report stated:

The 600-plus customers of the Eastern Rockcastle Association are about to reportedly see much better service, thanks to the efforts of ERWA President Russell Barron and Rockcastle County Judge/Executive Doug Bishop and the Rockcastle County Fiscal Court.

“My goal here is to better serve the people and that is what we will be doing,” said Barron . . . . “We have a tremendous debt and we have to make that payment every month. But we haven’t had rate increases. We just can’t keep up with the debt without placing a hardship on our customers by raising rates. [KAW] has agreed to pay off that debt . . . .”

Judge Bishop said the takeover will solve many problems with the current company and he and Congressman Hal Rogers worked very hard to make this takeover happen. “The company still owes \$770,000 in debt service and serving a little over 600 customers, it’s too hard to dissolve that debt.”

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<sup>13</sup> *In the Joint Petition of Kentucky-American Water Company, Thames Water Aqua Holdings GmbH, RWE Atkiengesellschaft, Thames Water Aqua US Holdings, Inc., Apollo Acquisition Company and American Water Works Company, Inc. for Approval of a Change of Control of Kentucky-American Water Company* (Case No. 2002-00317) (Ky. PSC Dec. 20, 2002), at 12.

<sup>14</sup> See Joint Applicants’ November 10, 2017 response to Item 1 of the Intervenors’ Request for Information, pp. 10-12 of 12.

Bishop said he and the fiscal Court have been searching for a solution for a very long time and he is excited about the takeover. “We offered the company to many other companies but no one was interested. We had to do something. Eastern doesn’t have the resources they need. It was just last Christmas that many customers went 17 days without water and that is simply unacceptable.”

Barron said the company has paid on the debt for building a water system for 20 years and is unable to maintain operations unless something is changed. “We had tried to sell to several other water companies but no one was interested until American Water came along. This will be a wonderful thing for customers and service will be so much better for everyone involved.”

“I’m a customer too,” said Barron. “If we had not made this move, there would have to be a significant rate increase and we just can’t do that to our customers.”<sup>15</sup>

After the customer vote was taken but before the ERWA Board approved the transaction,

Elmer Whitler wrote a letter to the newspaper editor further elaborating on these same issues.

He said:

The ERWA board recently met to count the votes of its members whether to have the Kentucky American Water Company assume ownership of the water system or to keep it under ERWA.

The results were clear. More than 85% (6 to 1) voted for Kentucky American Water. However, the ERWA chairman would not commit to honoring the results. When asked about it he would only say he had to consider all proposals and then negotiate.

The ERWA chairman opened the meeting saying the ERWA had received another proposal. He said that he had been contacted by the manager and board chairman of the Western Water Association with a proposal to do an “operational contract” with the ERWA, an arrangement that would keep the ERWA in control. Several ERWA members asked why Western Water Association would do this given that the ERWA owed almost \$800,000 and could not afford to maintain its water lines, and struggle to pay its monthly debts. In an earlier ERWA monthly meeting it was reported that all surrounding water associations had been contacted and none was interested in taking over the ERWA because of its large indebtedness and problems with his infrastructure. Why would “Western” saddle its users with such a burden?

Kentucky American Water representatives said they had sent ERWA a proposal in June. They want to know what was needed so progress could be made. They

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<sup>15</sup> *Id.*

said they were willing to maintain a local office, retain current staff, keep water rates low, and pay off ERWA debts.

It is possible that we will lose our safe treated water if the ERWA squanders the offer from American Water. The approximately 1200 adults and 2000 children whose health and quality of life depend on this water want ERWA to respect the overwhelming vote of its members.<sup>16</sup>

Mr. Whitler's letter discusses ERWA's dire financial predicament, but also shows that Mr. Barron carefully considered all options and made no rush to judgment even after the overwhelming vote in favor of the KAW transaction.

The record also proves the serious financial predicament ERWA is in as referenced above by Messrs. Barron and Whitler and Judge/Executive Bishop. Monthly financial reports frequently show expenses exceeding revenues and a resulting inability to make necessary improvements.<sup>17</sup> The Intervenors complain about the absence of any sort of formal study on the issue of what a rate increase would have to be, but even a cursory review of ERWA's financial statements leave no doubt that ERWA will have to increase rates if it is going to provide reasonable service.

As for the possibility of some sort of operational contract by which Western Rockcastle Water Association would assist ERWA, the ERWA Board considered it and correctly decided it was inferior to the KAW proposal. ERWA has explained in discovery:

Eastern Rockcastle was unclear on the terms of the proposal and viewed them as unfavorable. Western Rockcastle's proposal did not seem to position them as a concrete, long-term solution as they could withdraw by only providing a 30 day notice and were unable to help financially. Eastern Rockcastle's board of directors felt they needed at least a six month commitment.

Clearly, the ERWA Board properly exercised its judgment and concluded the Western Rockcastle proposal was not an adequate solution for ERWA's needs. And even if it were

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<sup>16</sup> *Id.*, p. 7 of 12.

<sup>17</sup> See ERWA's December 4, 2017 response to Item 12(b) of the Intervenors' Second Request for Information and the accompanying monthly financial information, pp. 17, 35, 53, 70, and 104 of 106.



appropriate to second-guess that business judgment decision, which it is not, the short-term nature of the Western Rockcastle proposal with no possibility of assisting with ERWA's debt problems are plain evidence of the inferiority of that proposal when compared to the KAW proposed transaction.

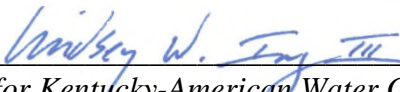
As for the remainder of Joint Applicants' arguments that the KAW proposed transaction is consistent with the public interest, they hereby rely on their December 29, 2017 Brief which, along with the record, demonstrates the following: (1) KAW has the financial, technical, and managerial ability to provide reasonable service to ERWA's customers as indicated by its financial resources, stability, and long track record of successfully handling similar acquisitions; (2) ERWA customers will see many benefits ranging from cost efficiencies based on economies of scale, better customer service options, and an enhanced ability to make needed capital improvements; (3) the documents related to an ERWA project submitted into the record by the Intervenor illustrate perfectly the capital needs of the ERWA system while also showing ERWA's inability to secure the capital to meet those needs; (4) the "public," *i.e.*, ERWA customers, voted overwhelmingly in favor of the KAW transaction (and were not misled whatsoever); and (5) the General Assembly and the Commission have both encouraged entities like KAW to pursue regionalization and consolidation through the exact type of transaction before the Commission in this case.

WHEREFORE, Joint Applicants respectfully request the Commission approve the relief requested in the Joint Application.

Respectfully submitted,

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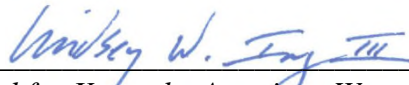
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**CERTIFICATE**

This certifies that the electronic filing of this document is a true and accurate copy of the documents to be filed in paper medium; that the electronic filing has been transmitted to the Commission on January 5, 2018; that an original and six paper copies of the filing will be delivered to the Commission within two business days of the electronic filing; and that no party has been excused from participation by electronic means.

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