

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC VERIFIED JOINT APPLICATION)	
OF EASTERN ROCKCASTLE WATER)	
ASSOCIATION, INC. AND KENTUCKY-)	CASE NO.
AMERICAN WATER COMPANY FOR THE)	2017-00383
TRANSFER OF CONTROL AND ASSETS)	

ORDER

On September 22, 2017, pursuant to KRS 278.020(6), Kentucky-American Water Company (“Kentucky American”) and Eastern Rockcastle Water Association, Inc. (“Eastern Rockcastle”) (collectively “Joint Applicants”) filed an application (“Application”) for the approval of Kentucky American to acquire Eastern Rockcastle’s assets pursuant to an Asset Purchase Agreement (“APA”), and for authorization to provide water services to Eastern Rockcastle’s customers in accordance with Kentucky American’s current water tariff on file with the Commission, except that the rates to be charged would remain the same as set forth at page 4 of Eastern Rockcastle’s current tariff.¹ The Commission issued a letter on September 28, 2017, accepting the application as filed.

PROCEDURAL

To ensure the orderly review of the Application, the Commission established a procedural schedule by Order dated October 17, 2017. On October 20, 2017, James E. Ballinger and Thomas P. Dupree, Jr. (collectively “Intervenors”) filed a Motion for Leave to Intervene, which the Commission granted in its October 30, 2017 Order. The Joint

¹ Joint Application at 2.

Applicants responded to two rounds of requests for information issued by both the Commission Staff and the Intervenors. The procedural schedule allowed the Joint Applicants and the Intervenors until December 8, 2017, to either request a formal hearing, or request the case be submitted on the existing record for a Commission decision.

On December 8, 2017, the Joint Applicants filed a joint statement that a formal hearing was not necessary and that this matter should be submitted to the Commission for a decision. However, on December 8, 2017, the Intervenors filed their Statement Regarding Hearing, Motion to Admit Documents into Evidence, and Motion for Briefing Schedule, (“Intervenors’ Motions”). The Intervenors requested that in lieu of a hearing, the Commission allow certain documents to be entered into the record. The Intervenors further requested permission to file written briefs within a reasonable time to address whether the proposed transfer of control meets the appropriate legal standards.

On December 13, 2017, Joint Applicants filed a Response to the Intervenors’ Motions (“Joint Applicants’ Response”), arguing that the Intervenors should not be able to admit extraneous evidence into the record, and that in order to conserve time and resources, the Commission should not allow briefing in this case. However, Joint Applicants stated that if the Commission allowed briefs to be filed, they would submit a simultaneous brief to ensure that the Intervenors did not distort the record.

On December 15, 2017, the Intervenors filed a Reply to Joint Applicants’ Response and stated that it would be a violation of due process not to allow the Intervenors an opportunity to be heard in this matter, and that a written brief would provide for the Intervenors to be heard in a meaningful way. Pursuant to the Commission’s December

21, 2017 Order granting the Intervenor's Motions, simultaneous briefs were to be filed with the Commission by December 29, 2017.

Both the Joint Applicants and the Intervenor's filed briefs with the Commission on December 29, 2017. The Commission, on its own motion, then issued a January 2, 2018 Order providing that simultaneous reply briefs on the issues of whether the proposed transfer would be made in accordance with law and consistent with the public interest should be filed no later than January 5, 2018. On January 5, 2018, the Joint Applicants filed a Reply Brief, and the Intervenor's filed a Response Brief. The matter is now submitted to the Commission for a decision based upon the record.

DISCUSSION

Kentucky American is a corporation engaged in the distribution and sale of water in its Central Division, serving customers in Bourbon, Clark, Fayette, Harrison, Jessamine, Nicholas, Scott, and Woodford counties and its Northern Division, with customers in Gallatin, Owen, and Grant counties.² Kentucky American owns, operates, and maintains potable water production, treatment, storage, transmission and distribution systems for the purpose of furnishing potable water for residential, commercial, industrial, and governmental users in its service territory.³ Kentucky American also is engaged in the collection and treatment of wastewater in Franklin, Owen, Bourbon, and Clark Counties.⁴ Eastern Rockcastle is a water association and a utility that is incorporated for the provision of water services in Rockcastle County, Kentucky.⁵

² Joint Application at 1.

³ *Id.*

⁴ *Id.*

⁵ *Id.* at 2.

Pursuant to KRS 278.020(6), the Joint Applicants petitioned the Commission for approval of the APA by which Kentucky American will acquire Eastern Rockcastle's assets. Further, pursuant to 807 KAR 5:011, Section 11, Kentucky American further petitioned the Commission to permit service to Eastern Rockcastle's customers in accordance with Kentucky American's current water tariff on file, except that the water rates to be charged would remain the same as set forth at page 4 of Eastern Rockcastle's current tariff.⁶ The proposed purchase of assets includes all of Eastern Rockcastle's tangible assets and real property interests that are devoted to the provision of water service, including but not limited to: mains; distribution system valves; hydrants, service lines, meters; pump stations; tanks; and land.⁷

Kentucky American asserts that if the Commission grants the Joint Application, it will then assume responsibility for the operation of Eastern Rockcastle and provide service to its customers.⁸ Kentucky American further pledges to make any necessary improvements over time to ensure that the existing and future customers are provided with the same quality of service as is currently being provided to Kentucky American customers.⁹

Pursuant to KRS 278.020(6), "[n]o person shall acquire or transfer ownership of, or control, or the right to control, any utility under the jurisdiction of the commission... without prior approval by the commission. The commission shall grant its approval if the

⁶ Joint Application at 2.

⁷ Joint Applicants' Response to Commission Staff's Second Request for Information ("Response to Staff's Second Request") (filed Dec. 4, 2017), Item 3.

⁸ Joint Application at 2 and 3.

⁹ *Id.*

person acquiring the utility has the financial, technical, and managerial abilities to provide reasonable service.” KRS 278.020(7) further provides that “[n]o individual, group, syndicate, general or limited partnership, association, corporation, joint stock company, trust, or other entity (an ‘acquirer’), whether or not organized under the laws of this state, shall acquire control, either directly or indirectly, of any utility furnishing utility service in this state without having first obtained the approval of the commission.” KRS 278.020(7) additionally provides that the “commission shall approve any proposed acquisition when it finds that the same is to be made in accordance with law, for a proper purpose and is consistent with the public interest.”

The Joint Applicants argue that Kentucky American has the financial, technical, and managerial abilities to skillfully and efficiently operate the acquired assets as required by KRS 278.020(6). Kentucky American cites its annual reports on file with the Commission as evidence of Kentucky American’s financial integrity and ability to ensure the continuity of water service to Eastern Rockcastle’s customers as required by KRS 278.020(10).¹⁰ Finally, the Joint Applicants argue that the Application was made in accordance with the law, for a proper purpose, and is consistent with public interest.¹¹

The Intervenors argue that Joint Applicants have not demonstrated that the proposed acquisition was made in accordance with the law due to not complying with KRS 273.297, which identifies the procedure for a non-profit corporation to sell its assets.¹² The Intervenors assert that pursuant to KRS 273.297, and its governing

¹⁰ *Id.* at 3; Joint Applicants’ Response to Commission Staff’s First Request for Information (“Response to Staff’s First Request”) (filed Nov. 6, 2017), Item 3.

¹¹ Joint Application at 3; Response to Staff’s First Request, Item 16.

¹² Intervenors’ Brief (filed Dec. 29, 2017) at 2.

corporate documents, Eastern Rockcastle's Board of Directors ("Eastern Rockcastle's Board") was required to adopt a resolution recommending the sale of the assets, and submit the proposed sale to a vote by the members of the association at a meeting.¹³ Further, Intervenor's argue that written notice of the meeting was to be given, and at least two-thirds of the members present at the meeting or appearing by proxy must have approved the sale.¹⁴ Thus, the Intervenor's conclude that because Eastern Rockcastle failed to strictly comply with KRS 273.297, the proposed transfer is not in accordance with the law.¹⁵ The Intervenor's further argue that the proposed transfer is not consistent with the public interest, because Eastern Rockcastle did not seek competitive bids for the acquisition or operation of its system. Additionally, the Intervenor's state that Eastern Rockcastle provided unfair information to the customers indicating that if the transfer was not completed, then there would be a substantial rate increase.¹⁶

The Joint Applicants' argue that the APA was made in accordance with the law because KRS 273.297 does not require a written resolution from Eastern Rockcastle's Board recommending the proposed sale, and in the alternative, even if it did require a written resolution, then the purpose of the statute was achieved in all material respects.¹⁷ The Joint Applicants argue that the plain language of KRS 273.297 lays out the process that *may* be used to authorize a sale of property and assets, and does not state that it

¹³ *Id.*

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ Joint Applicants' Reply Brief (filed Jan. 5, 2018) at 2.

shall be used.¹⁸ Thus, the Joint Applicants conclude that they were not required to strictly adhere to KRS 273.297.¹⁹

Second, the Joint Applicants argue that even if it were determined that a resolution was required, the statute does not say it must be a written resolution, and that the communications provided from Eastern Rockcastle's Board to its customers demonstrate that the intent and purpose of the statute to provide notice and recommend a sale to the members was fulfilled.²⁰ Moreover, Eastern Rockcastle's Board encouraged its customers to attend the July 17, 2017, board meeting at which the transfer to Kentucky American would be discussed.²¹ According to the July 17, 2017 meeting minutes, customers did attend, and Eastern Rockcastle's Board made a recommendation and decision to conduct a customer vote on the proposed transfer.²² Eastern Rockcastle's Board issued letters to the customers as well as public postings and newspaper articles before the customer vote was taken, providing them with information concerning the Kentucky American transfer, and recommending the transfer of the water association to Kentucky American in order to better serve the customers.²³ Eastern Rockcastle mailed ballots in order to allow each customer to vote on the proposed transfer.²⁴ More than 85

¹⁸ *Id.*

¹⁹ *Id.* at 3. (Emphasis added.)

²⁰ *Id.*; Response to Staff's First Request, Item 1; Joint Applicants' Response to Intervenor's First Request for Information ("Response to Intervenor's Request") (filed Nov. 6, 2017), Item 1.

²¹ Joint Applicants' Reply Brief at 3 and 4; Response to Staff's First Request, Item 1; Response to Intervenor's Request, Item 1.

²² *Id.*

²³ *Id.*

²⁴ Joint Applicants' Reply Brief at 4; Response to Staff's First Request, Item 1; Response to Intervenor's Request, Item 1.

percent of the customers voted to approve the proposed transfer to Kentucky American, with a final tally of 231-41 in favor of the proposed transfer.²⁵

Additionally, Joint Applicants state that the proposed transfer is consistent with the public interest, and that the Intervenors cite to no authority that would require Eastern Rockcastle to seek competitive bids for the acquisition or operation of the system.²⁶ The Joint Applicants also argue that even after the vote was taken, the Eastern Rockcastle Board considered other alternatives, such as an operations contract with Western Rockcastle Water Association (“Western Rockcastle”), in order to engage in further negotiations with Kentucky American and obtain the best deal possible.²⁷ However, Western Rockcastle’s proposal was deemed inferior to Kentucky American’s proposal because it was not a long-term solution as Western Rockcastle could withdraw by only providing a 30-day notice, and was unable to assist financially.²⁸

The Joint Applicants summarize their position by stating the following: the record demonstrates that Kentucky American has the financial, technical, and managerial ability to provide reasonable service to Eastern Rockcastle’s customers as indicated by its financial resources, stability, and long track record of successfully handling similar acquisitions; Eastern Rockcastle’s 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; the record proves that Eastern

²⁵ Joint Applicants’ Reply Brief at 2; Response to Staff’s First Request, Item 1.

²⁶ Joint Applicants’ Reply Brief at 5 and 6.

²⁷ *Id.* at 5; Response to Staff’s First Request, Item 1.

²⁸ Joint Applicants’ Reply Brief at 8; Response to Staff’s First Request, Item 1.

Rockcastle is in need of capital to complete necessary projects, but has been unable to obtain such funding; the customers voted overwhelmingly in favor of the proposed transfer; and the General Assembly, and the Commission, have encouraged entities like Kentucky American to pursue regionalization and consolidation of water and wastewater systems such as the pending transfer request.²⁹

The Commission agrees with the Joint Applicants' arguments that if compliance with KRS 273.297 is required, the record proves that Joint Applicants substantially complied with the statute. The intent and purpose of KRS 273.297 is to provide notice of a proposed sale to members of the corporation, with a recommendation from the Board of Directors, and two-thirds of the votes to authorize the sale, whereby after such voting authorization the Board of Directors, in its discretion, may abandon the sale without further action or approval by the voting members. In the present case, based upon the record, the Eastern Rockcastle Board provided notice to the customers of the proposed transfer and communications indicating it was recommending the proposed transfer to Kentucky American; held multiple open meetings discussing the proposed transfer; issued ballots for the customers to cast votes on whether they wanted to approve or deny the proposed transfer; and then acted on the customers' overwhelming majority vote to transfer the water system to Kentucky American.

Having reviewed the evidentiary record and being otherwise sufficiently advised, the Commission finds that:

²⁹ Joint Applicants' Reply Brief at 9.

1. Eastern Rockcastle, the Seller under the APA, is a water association and a utility that was incorporated for the provision of water services in Rockcastle County, Kentucky.

2. Eastern Rockcastle serves approximately 608 active customers.³⁰

3. Pursuant to the APA, Eastern Rockcastle agrees to sell the Eastern Rockcastle Water Association system, with specific exclusions, to Kentucky American for the dollar amount required for the Seller to clear its books, but not to exceed \$770,000.³¹

4. Kentucky American, the Buyer under the APA, is a corporation and utility engaged in the distribution and sale of water in its Central Division, consisting of Bourbon, Clark, Fayette, Harrison, Jessamine, Nicholas, Scott, and Woodford counties and its Northern Division, of Gallatin, Owen, and Grant counties.

5. Kentucky American serves approximately 130,756 water customers.

6. Eastern Rockcastle will continue to operate the water association system through the date of the closing of the APA.

7. After the transfer is complete, Kentucky American will provide water services to Eastern Rockcastle's customers in accordance with Kentucky American's current water tariff on file with the Commission, except that the rates to be charged will remain the same as set forth at page 4 of Eastern Rockcastle's current tariff.

³⁰ Response to Staff's First Request, Item 5.

³¹ Joint Application, Exhibit 1.

8. As of October 26, 2017, Eastern Rockcastle held \$20,221.38 in customer deposits. Eastern Rockcastle will apply the customer deposit amounts to customer's final bills, and then mail the remaining balance to the customer.³²

9. Kentucky American will not require customer deposits.³³

Based upon these findings, the Commission makes the following conclusions of law:

1. Eastern Rockcastle is a utility subject to Commission jurisdiction as defined in KRS 278.012 and KRS 278.040.

2. Kentucky American is a utility and subject to the Commission's jurisdiction as defined in KRS 278.010(3)(d) and (f) and KRS 278.040.

3. Pursuant to KRS 278.020(6), "[n]o person shall acquire or transfer ownership of, or control, or the right to control, any utility under the jurisdiction of the commission... without prior approval by the commission. The commission shall grant its approval if the person acquiring the utility has the financial, technical, and managerial abilities to provide reasonable service."

4. KRS 278.020(7) further provides that "[n]o individual, group, syndicate, general or limited partnership, association, corporation, joint stock company, trust, or other entity (an 'acquirer'), whether or not organized under the laws of this state, shall acquire control, either directly or indirectly, of any utility furnishing utility service in this state without having first obtained the approval of the commission." KRS 278.020(7) further provides that the "commission shall approve any proposed acquisition when it

³² Response to Staff's First Request, Item 4.

³³ Response to Staff's Second Request, Item 3.

finds that the same is to be made in accordance with law, for a proper purpose and is consistent with the public interest.”

5. The transfer of Eastern Rockcastle’s water system to Kentucky American is a transaction subject to the jurisdiction of the Commission and requires Commission approval.

6. Kentucky American has sufficient financial integrity to ensure the continuity of service.

7. Kentucky American has the financial, technical, and managerial abilities to provide reasonable service to the Eastern Rockcastle customers.

8. The proposed transfer is in accordance with the law, for a proper purpose, and is consistent with the public interest.

9. KRS 224A.300(1) provides that the regionalization and consolidation of water and wastewater systems should be encouraged, and the transfer of ownership and control of the Eastern Rockcastle system to Kentucky American is consistent with regionalization.

IT IS HEREBY ORDERED that:

1. The proposed transfer of ownership and control of the Eastern Rockcastle system pursuant to the terms of the APA is approved, subject to the conditions set forth in ordering paragraphs 2 through 9, as of the date of entry of this Order.

2. The Joint Applicants shall notify the Commission in writing of the closing of the transaction within ten days of the closing.

3. If the transaction does not close within 90 days of the date of entry of this Order, Joint Applicants shall file with the Commission a report on the status of the efforts to complete the transfer.

4. Any material revision to the proposed transaction shall require approval by the Commission in order for the amendment to be effective.

5. Eastern Rockcastle shall continue to operate the water system until the closing of the transaction, at which time Kentucky American will begin operating the system and serving the customers.

6. No later than July 1, 2018, Eastern Rockcastle shall submit its Annual Report for 2017, and the Gross Report for 2017 and 2018 through the date of the transfer.

7. Eastern Rockcastle shall submit the journal entries associated with the transfer of the Eastern Rockcastle water system within 30 days of the date of closing.

8. Kentucky American shall submit the journal entries associated with the transfer of the Eastern Rockcastle water system within 30 days of the date of closing.

9. Any documents filed pursuant to ordering paragraphs 2, 3, 6, 7, and 8 shall reference this case number and shall be retained in Joint Applicants' general correspondence file.

10. The Executive Director is delegated authority to grant reasonable extensions of time for the filing of any documents required by this Order upon a showing of good cause for such extension.

11. A copy of this Order shall be served on the Kentucky Division of Water and the Rockcastle County Judge Executive.

12. This case is closed and removed from the Commission's docket.

By the Commission



ATTEST:


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