

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF MARTIN)	CASE NO.
COUNTY WATER DISTRICT FOR AN)	2018-00017
ALTERNATIVE RATE ADJUSTMENT)	

ORDER

On November 15, 2019, the Commission entered an Order that, among other things, directed Martin County Water District (Martin District) to enter into a management contract with Alliance Water Resources, Inc. (Alliance), approved rates and surcharges, established certain reporting requirements, and closed this proceeding. On June 1, 2020, the Commission issued an Order reopening this case for the purpose of scheduling a hearing to take evidence regarding compliance with reporting requirements contained in the November 15, 2019 Order. The hearing was held on June 16, 2020. Martin District filed responses to a post-hearing data request. In response to a *subpoena duces tecum*, Evans Hardware, Inc. (Evans Hardware), a creditor that provides supplies to Martin District, filed statements and supporting invoices for two customer accounts owned by Martin District with significant arrearages.

During the hearing, the Commissioners and Commission Staff questioned Martin District Commissioners, Jimmy Don Kerr and John Hensley, and Alliance Water Resources, Inc. (Alliance) executives and managers about financial reports filed with the Commission and provided in the Martin District board packets, prepared for Martin District board meetings. As a result of the questioning, Alliance made certain changes to the

financial reports that clarified column labels and provided additional information in footnotes to the reports.

Of particular consequence for Martin District ratepayers, the Commission is now aware that the Martin District Board acquiesced¹ to interest rates paid to Evans Hardware and CI Thornburg Co., Inc. (CI Thornburg) that allegedly violate usury laws by charging an interest rate that is substantially higher than the 8 percent legal interest rate established by Kentucky's interest and usury law, KRS 360.010.² A threshold issue is whether KRS 360.010 applies to the interest charged Martin District by Evans Hardware and CI Thornburg. KRS Chapter 360 does not define the term "interest." Pursuant to the statutory interpretation authority afforded to courts under KRS 446.080(4), Kentucky courts have held that interest is compensation allowed by law "for the loss of money by one who is entitled to its use."³ Courts look beyond the label of "finance charge" and examine the substance of a transaction when evaluating whether a charge is disguised interest.⁴ Under facts similar to those presented here, courts have held that a penalty or delinquency charge assessed by a vendor for an amount past due on goods purchased by or service provided to a debtor falls within the ordinary legal meaning of "interest"

¹ June 16, 2020 Hearing Video Transcript (HVT) at 13:13:30. Martin District Board Chair Kerr testified he was aware of the interest rate charged by Evans Hardware and that there was a discussion of Evans Hardware waiving a portion of the bill and interest once the unpaid balance was paid.

² KRS 360.010 establishes a legal interest rate of 8 percent, but permits parties to agree in writing to a higher interest rate that is capped at the lesser of 19 percent or 4 percent over the federal discount rate on 90-day commercial paper. Further, Kentucky laws permit higher interest rates on written agreements for credit cards and consumer loans.

³ *Grace v. LVNV Funding, Inc.*, 22 F.Supp.3d 700, 704 (W.D. Ky. 2014). See also *Brown v. Hiatts*, 82 U.S. 177, 185 (1872).

⁴ *Grace*, 22 F.Supp.3d at 703-704; *Hurt v. Crystal Ice & Cold Storage Co.*, 286 S.W. 1055, 1056-1056 (Ky. 1926).

because it is a form of compensation for the vendor's loss of money that vendor is entitled to use, and thus KRS 360.010 governs.⁵

Although not binding law, the Attorney General of the Commonwealth of Kentucky (Attorney General) issued an opinion based on similar reasoning that the substance of the transaction and not a label is determinative of whether KRS 360.010 applies to a transaction. The Attorney General found that KRS 360.010 applies to accounts remaining unpaid after their due date regardless of how a charge is styled, absent the applicability of other statutes establishing interest rates, such as laws pertaining to interest on judgments, credit cards, or consumer loans.⁶

Based on settled law discussed above, the Commission finds that interest on the unpaid amounts due to Evans Hardware and CI Thornburg for goods purchased by and services provided to Martin District is governed by KRS 360.010.

Martin District stated that it does not have a written agreement, contract, promissory note, or obligation with Evans Hardware regarding the amounts due for past purchases.⁷ According to Evans Hardware's invoices and Martin District, Evans Hardware charges simple interest at a rate of 18 percent per annum for unpaid invoices.⁸ As of June 30, 2020, on one of its two accounts, Martin District owed Evans Hardware \$30,200.99 for purchases made between 2015 and 2017, and \$25,789.80 in interest

⁵ *Grace*, 22 F.Supp.3d at 703-705.

⁶ OAG 70-800. See also OAG 72-598 (finding that KRS 360.010 applies to the legal interest rate that a county hospital could charge interest on delinquent accounts).

⁷ Martin District's Response to Commission Staff's Post-Case Request for Information (Staff's Post-Case Request), Item 3; June 16, 2020 HVT at 13:13:22.

⁸ Evans Hardware Response to *Subpoena Duces Tecum* (filed July 8, 2020); Martin District's Response to Staff's Post-Case Request, Item 3.

charged between 2016 and 2020 for those purchases, for a total due of \$55,990.79.⁹ Based upon the finance charges on this account, it appears that Evans Hardware has charged Martin District approximately 20 percent simple interest on this account, but the actual amount is not readily determinable because payments made by Martin District were not included on account statements. Also, as of June 30, 2020, Martin District owed Evans Hardware on a second account \$18,820.64 for purchases made between 2018 and 2019, and \$3,326.32 in interest charged between 2018 and 2020, for a total of \$22,146.96.¹⁰

Martin District filed written agreements with CI Thornburg to repay amounts due on three unpaid accounts, but the agreements do not set forth an interest rate. According to Martin District, CI Thornburg charged simple interest at a rate of 18 percent per annum between September 2018 and May 2020 on two of the accounts, which resulted in finance charges of \$2,997.55 and \$4,403.04 respectively.¹¹ Because the written agreement provided by Martin District does not set forth an interest rate, the provision in KRS 360.010 for higher interest rates charged on written agreements is not applicable. Even if the provision were applicable, the permissible interest rate on written agreements established by KRS 360.010 is the lesser of 19 percent or 4 percent over the federal discount rate for 90-day commercial paper. Given that the federal discount rate for 90-day commercial paper fluctuated between 2.30 percent in September 2018 and 0.18 percent in July 2020,

⁹ The purchases were made between August 4, 2015, and March 14, 2016, and between December 22, 2016, and March 29, 2017. The interest charges accrued between May 31, 2016, and June 30, 2020.

¹⁰ The purchases were made between May 8, 2018, and December 31, 2018, and November 4, 2019, and December 30, 2019. The interest charges accrued between August 31, 2018, and June 30, 2020.

¹¹ Martin District's Response to Staff's Post-Case Request, Item 4.

with a high of 2.56 percent in January 2019, the effective maximum annual interest rate permitted by KRS 360.010 would be 8 percent.¹²

KRS 360.020, which sets forth the penalty for charging excessive interest, states:

The taking, receiving, reserving, or charging a rate of interest greater than is allowed by KRS 360.010, when knowingly done, shall be deemed a forfeiture of the entire interest which the note, bill, or other evidence of debt carries with it, or which has been agreed to be paid thereon. In case the greater rate of interest has been paid, the person by whom it has been paid, or his legal representatives, may recover, in an action in the nature of an action of debt, twice the amount of the interest thus paid from the creditors taking or receiving the same: provided, that such action is commenced within two (2) years from the time the usurious transaction occurred.

As the Commissioners stated at the June 16, 2020 hearing, had the Commission been informed of the interest rates that exceeded the legal limit, it would never have approved the priority of payment with Evans Hardware and CI Thornburg being paid last, along with ZipZone and Martin District's former bookkeeper-accountant.¹³ Concurrent with this Order, the Commission is opening a new proceeding to monitor Martin District's managerial, financial, and operational position. In that Order, the Commission, among other things, directs the Martin District Board to take immediate steps to address the excess interest charged by and paid to Evans Hardware and CI Thornburg, up to and including seeking remedies available to Martin District pursuant to KRS 360.020.

With the initiation of a new proceeding, the Commission finds that administrative efficiency will be achieved if Martin District ceases filing the reports required to be filed

¹² Federal Reserve Bank of St. Louis, Economic Research, 90-Day AA Nonfinancial Commercial Paper Interest Rate, September 2018-July 2020, available at: <https://fred.stlouisfed.org/series/RIFSPNAAD90NB>.

¹³ June 16, 2020 HVT at 13:12:10. The Commission notes that, according to Martin District, neither ZipZone nor the former bookkeeper-accountant is charging interest on the unpaid balances.

with the Commission in ordering paragraphs 6, 7, and 11 of the November 15, 2019 Order in this proceeding and instead files said reports into the case record of the new proceeding.

The Commission further finds that, given the initiation of a new monitoring proceeding, this matter should be closed and removed from the Commission's docket.

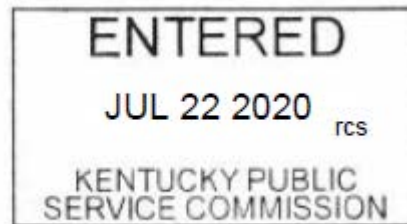
IT IS THEREFORE ORDERED that:

1. Effective as of the date of this Order, all filings made pursuant to ordering paragraphs 6, 7, and 11 of the November 15, 2019 Order shall be filed into Case No. 2020-00154, *Electronic Martin County Water District Management and Operation Monitoring Pursuant to KRS 278.250*, which is initiated on the same date as the entry of this Order.

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

By the Commission

Vice Chairman Kent A. Chandler did not participate in the deliberations or decision concerning this case.



ATTEST:



Deputy Executive Director

Case No. 2018-00017

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