

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC PROPOSED ACQUISITION BY)	
BLUEGRASS WATER UTILITY OPERATING)	
COMPANY, LLC AND THE TRANSFER OF)	
OWNERSHIP AND CONTROL OF ASSETS BY P.R.)	
WASTEWATER MANAGEMENT, INC., MARSHALL)	CASE NO.
COUNTY ENVIRONMENTAL SERVICES, LLC, LH)	2019-00104
TREATMENT COMPANY, LLC, KINGSWOOD)	
DEVELOPMENT, INC., AIRVIEW UTILITIES, LLC,)	
BROCKLYN UTILITIES, LLC, FOX RUN UTILITIES,)	
LLC, AND LAKE COLUMBIA UTILITIES, INC.)	

ORDER

On April 16, 2019, Bluegrass Water Utility Operating Company, LLC (Bluegrass Water), P.R. Wastewater Management, Inc. (P.R. Wastewater), Marshall County Environmental Services, LLC (Marshall County Environmental), LH Treatment Company, LLC (LH Treatment), Kingswood Development, Inc. (Kingswood), Airview Utilities, LLC (Airview), Brocklyn Utilities, LLC (Brocklyn), Fox Run Utilities, LLC (Fox Run), and Lake Columbia Utilities, Inc. (Lake Columbia), (collectively Joint Applicants) filed a joint application for approval of the transfer of the wastewater treatment plants, collection systems, and other assets of P.R. Wastewater, Marshall County Environmental, LH Treatment, Kingswood, Airview, Brocklyn, Fox Run, and Lake Columbia to Bluegrass Water. The utilities proposed for acquisition have approximately 1,300 sewer customers in Bullitt, Franklin, Hardin, Madison, Marshall, McCracken, Scott, and Shelby counties.

The Commission's jurisdiction to investigate and approve the acquisition and transfer of a utility arises under KRS 278.020(6) and 278.020(7). Pursuant to KRS

278.020(7), the Commission extended the 60-day period for a decision set forth in KRS 278.020(7) by an additional 60 days. The Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention (Attorney General), requested and was granted intervention. The Joint Applicants responded to several rounds of requests for information from both Commission Staff and the Attorney General, in addition to responding to a list of conditions proposed by the Attorney General. A public hearing was held on July 2, 2019, and the Joint Applicants and the Attorney General both filed post-hearing briefs. The case is now ripe for a decision.

BACKGROUND

Bluegrass Water is a newly formed limited liability corporation whose principal office is in Saint Ann, Missouri. Bluegrass Water Utility Holding Company, LLC (Holding Company) is the member owner of Bluegrass Water. Kentucky Central States Water Resources, LLC (CSWR) is the member owner of Holding Company. First Round CSWR, LLC (First Round) and Central States Water Resources, Inc. (CSWR) are affiliates of each other and sit atop the corporate structure (CSWR Group). First Round and CSWR also own water and wastewater utilities in Missouri and Arkansas, and have an application pending in Tennessee for the acquisition of water assets there.¹

The stated goal of CSWR Group is “to acquire and recapitalize failing systems as investor owned regulated water and wastewater utility companies.”² To date, CSWR

¹ Verified Application at 4.

² *Id.*

Group has acquired 9 small water systems and 16 small wastewater systems in Missouri and Arkansas, and serves approximately 4,000 customers.³

According to Bluegrass Water's application, in 2018 CSWR Group attracted an additional large private equity investor, allowing CSWR Group to invest in utilities beyond Missouri and Arkansas. CSWR Group states that it, "leverages extensive regulatory expertise and financial resources to facilitate cost-effective solutions to upgrade facilities to meet the ever more stringent state and federal standards."⁴

The Utilities

P.R. Wastewater provides wastewater service to 358 residential customers and 3 commercial customers in the Persimmon Ridge development in Shelby County.⁵ P.R. Wastewater is in generally good physical condition, but has struggled to meet some disinfection requirements, required by the Kentucky Division of Water (DOW). P.R. Wastewater recently received a rate increase on April 12, 2019, using the alternative rate filing procedure for small utilities.⁶

Marshall County Environmental provides wastewater service to 126 single-family and 4 condominium customers in two subdivisions: Great Oaks in McCracken County, and Golden Acres Subdivision in Marshall County. Marshall County Environmental is currently the subject of enforcement action for failing to file its annuals reports with the Commission. A fine has been levied, but the Commission has not taken any enforcement

³ Verified Application at 4.

⁴ *Id.*

⁵ *Id.* at 6.

⁶ *Id.*

efforts, pending the outcome of this proceeding.⁷ Marshall County Environmental has been administratively dissolved by the Secretary of State.

Both systems are in poor shape. The Golden Acres system does not have a current DOW permit. It has been exceeding limits for ammonia, *E. coli* bacteria, and other contaminants. The Great Oaks system is in particularly poor shape. At the time the Joint Applicants filed the application it appeared as if the system had not had a Division of Water (DOW) discharge permit since 2012. The system has not been properly maintained in years, and appears to be discharging wastewater directly to the ground.⁸ Great Oaks recently has been sued by the Energy and Environment Cabinet (EEC), which has supervisory authority over the DOW, to correct the improper discharges.⁹

LH Treatment provides wastewater service to 261 single-family homes and 16 condominium customers in the Longview and Homestead subdivisions in Scott County. The system's DOW permit expired in December 2018. The system has exceeded its DOW permit limits for some environmental contaminants.¹⁰

Kingswood provides service to 124 customers in the Kingswood subdivision in Bullitt County. The system has had sporadic violations of environmental contaminant standards.¹¹

⁷ *Id.* at 7.

⁸ Verified Application at 7–8.

⁹ The Energy and Environment Cabinet brought an action in Franklin Circuit Court seeking the appointment of a receiver to operate the Great Oaks system. See, Franklin 19-CI-00633, *Energy and Environment Cabinet v. Allen Artis*.

¹⁰ *Id.* at 8–9.

¹¹ *Id.* at 9.

Airview provides wastewater service to 203 customers in Hardin County.¹² Airview has filed with the Commission for permission to abandon the system.¹³ The case is pending before the Commission, and the Commission has not approved the abandonment. Airview's DOW operation permit has expired. According to Bluegrass Water, the system is in serious disrepair, with extensive contamination concerns as the various portions of the plant continue to fail. The system requires major renovations.¹⁴

Brocklyn provides wastewater service to 168 customers (70 single-family homes and 98 condominiums) in Madison County.¹⁵ The system is in an overall state of disrepair and exceeds DOW permit limits for contaminants, with a tank that is barely able to meet the needs of its residents. Its DOW permit has expired.¹⁶

Fox Run provides wastewater service to 34 customers in Fox Run Subdivision in Franklin County. Fox Run's DOW permit has expired. The plant is in general disrepair and has exceeded DOW permitted discharge limits. According to Bluegrass Water, an independent engineer has identified necessary updates to the facilities.¹⁷

Lake Columbia provides wastewater service to 33 residents in Bullitt County. Lake Columbia is in bad standing with the Secretary of State. The plant is in disarray and has not been properly maintained, and the system has exceeded its DOW permit limits. An

¹² *Id.* at 10.

¹³ *Id.*, See also, Case No. 2016-00207, *Airview Utilities, LLC's Notice of Surrender of Utility Property* (filed July 15, 2016).

¹⁴ Verified Application at 10.

¹⁵ *Id.*

¹⁶ Verified Application at 11.

¹⁷ *Id.* at 11–12.

independent engineer has opined that a complete overhaul is necessary, or possibly an entirely new treatment facility.¹⁸

The Transaction

Bluegrass Water has executed a sales agreement with each utility for the transfer or sale of each utilities' assets.¹⁹ Bluegrass Water will assume all liabilities for all of the acquired utilities. Airview, however, will remain responsible for fines imposed by the EEC.²⁰

Bluegrass Water proposes a 50/50 capital structure. If the Commission approves the transaction, Bluegrass Water will be funded by CSWR Group affiliates, with equity capital from First Round and debt financing from US Water Capital, LLC.²¹ Bluegrass Water "anticipates a rate of interest for the Long-Term Debt that is at the market rate for small, distressed water and wastewater utilities."²²

After the close of the transaction, Bluegrass Water will assume responsibility for the operation of each system. Bluegrass Water will engage Midwest Water Operations, LLC (Midwest Water), an independent third-party operator, to operate the acquired systems. Midwest Water, in addition to normal operations, will have a 24-hour emergency

¹⁸ *Id.* at 12.

¹⁹ No customer deposits are held by any utility.

²⁰ Verified Application at 14.

²¹ Verified Application at 14–15.

²² Joint Applicants' Response to Commission Staff's First Request for Information, Request No. 6.

service line and notices of disruptions will be forwarded to Josiah Cox, CSWR's president.²³

Bluegrass Water will engage Nitor Billing Services to handle billing and service-related billing questions.²⁴ CSWR will be responsible for all management, financial reporting, underground utility, and locations services, regulatory reporting and management, record keeping etc.²⁵ Proportional costs for these services will be allocated to Bluegrass Water.²⁶

Bluegrass Water claims that it will make all necessary improvements to ensure that the acquired systems remain functional and customers receive adequate service. Even though Bluegrass Water will have no employees in Kentucky, this service will include 24-hour emergency phone lines for service issues, on-call service contractor personnel, and a variety of other options relating to billing and payments.²⁷

CSWR will engage an independent engineer to conduct site inspections and make recommendations regarding necessary improvements. Bluegrass Water states that it has secured the necessary funding and plans to bring each system into compliance within a year of closing.²⁸ Bluegrass Water anticipates that it will need to spend \$2.9 million to

²³ Verified Application at 16.

²⁴ *Id.*

²⁵ *Id.* at 17.

²⁶ *Id.*

²⁷ Verified Application at 17.

²⁸ *Id.*

address the problems identified by the engineer, and has listed the planned improvements for each utility system.²⁹

Bluegrass Water initially will operate under the current tariff for each utility. Bluegrass Water states that it eventually will seek to move its customers to a unified rate.³⁰

DISCUSSION

In order for the Commission to approve the transfer of a wastewater treatment system it must determine that: (1) the acquirer has the financial, technical, and managerial abilities to provide reasonable service;³¹ (2) that the transfer is in accordance with law, for a proper purpose and is consistent with the public interest³²; and (3) that the person acquiring the utility has provided evidence of financial integrity to ensure the continuity of sewage service in the event that the acquirer cannot continue to provide service.³³ The Commission may also attach any conditions it deems necessary in approving a transfer.³⁴ Based on the evidence of record, the Commission finds that Bluegrass Water will meet the statutory standards for acquisition of the various wastewater systems only if it agrees to the conditions discussed below.

²⁹ *Id.* at 18.

³⁰ *Id.* at 19.

³¹ KRS 278.020(6).

³² KRS 278.020(7).

³³ KRS 278.020(10).

³⁴ KRS 278.020(7).

The Attorney General, absent the imposition of certain conditions, objects to the proposed transfer, asserting that Bluegrass Water has not met its burden of proof, specifically stating that Bluegrass Water has not proven that it has the financial and managerial ability to provide reasonable service, and has not provided evidence of financial integrity to ensure continuity of service.³⁵

The Attorney General submitted a list of 28 proposed commitments to Bluegrass Water and requested that Bluegrass Water agree to the commitments.³⁶ Bluegrass Water agreed to only four of the commitments. Bluegrass Water agreed to abide by Commitment 15 (agreeing to file the post-closing accounting entries for each of the Joint Applicants and the direct affiliates involved in the transaction(s), including those that provide post-closing capital); Commitment 20 (that post-closing customers would experience no adverse change in service if the transaction(s) is approved); Commitment 26 (No later than March 31st of every year, Bluegrass Water will file with the Commission a detailed organizational chart showing all subsidiaries and affiliates as of the end of the previous calendar year; and Commitment 27 (post-closing, Bluegrass Water will adequately fund and maintain the transferred systems.)³⁷

It is evident that several of the systems that Bluegrass Water seeks to acquire are distressed, failing, and in need of significant investment and repair. The record is replete with evidence that many of the systems have suffered from neglect and a lack of

³⁵ Attorney General's Post-Hearing Brief (filed July 24, 2019) at 2.

³⁶ Attorney General's Post-Hearing Requests for Commitments (filed July 12, 2019).

³⁷ Response to Attorney General's Post-Hearing Requests for Commitments (filed July 19, 2019).

investment, particularly those owned by Marty Cogan and Larry Smithers³⁸, who have generally failed to maintain their systems, or seek the necessary revenues over time to pay for the cost of maintaining and repairing the systems.³⁹ Mr. Cogan and Mr. Smithers, in the case of Airview, have sought to abandon the utility rather than attempt to repair it. Because several of the current owners are unwilling, or unable, to maintain their systems, Bluegrass Water is the only option that has presented itself as a viable solution for rehabilitating the wastewater facilities and providing reasonable service to the customers. Accordingly, subject to the conditions discussed below, we will approve the proposed transaction.

Financial Ability

The Attorney General argues that there is no evidence proving that Bluegrass Water has the financial ability to operate the systems it proposes to acquire. First, the Attorney General questions whether CSWR has the finances on hand to acquire the systems. Second, the Attorney General questions whether Bluegrass Water has a commitment for debt financing. Last, the Attorney General states that there is no evidence of a commitment for equity capital. The Attorney General concludes that Bluegrass Water has failed to meet its burden of proof.

Bluegrass Water argues that the Attorney General's concerns are misplaced, and that the Attorney General's concerns appear to be about the form of the evidence of debt and equity, and that the lack of a formal written agreement as to equity and debt financing

³⁸ Fox Run, Airview, Brocklyn, and Lake Columbia.

³⁹ We note, however, that some of the systems, particularly P.R. Wastewater, LH Treatment, and Kingswood have generally maintained their systems in good repair.

means there is no commitment.⁴⁰ However, Bluegrass Water argues that it continues to have access to equity and debt financing, and that this commitment allows CSWR Group to treat the debt financing described in its application as a default source of debt financing while it shops the market for lower-cost debt.⁴¹ Bluegrass Water argues that CSWR Group would have made a poor financial decision if it had already borrowed funds and drawn on equity for an acquisition that had not been approved and for capital projects on systems not yet acquired.⁴² Bluegrass Water also points out that the current owners of the systems sought to be acquired, currently lack access to equity or long-term debt, and instead rely on personal assets to fund the systems.⁴³ Bluegrass Water asserts that CSWR Group has had the financial means to borrow money and attract capital to sustain and improve systems acquired in Arkansas and Missouri, and that the same ability will allow it to provide and improve service in Kentucky.⁴⁴ On August 9, 2019, Bluegrass Water filed an affidavit into the record indicating that it had obtained the equity capital necessary to acquire the assets that are subject to the Joint Application.⁴⁵

⁴⁰ Applicants' Attorney General's Post-Hearing Brief (filed July 30, 2019) at 2–3.

⁴¹ Applicants' Attorney General's Post-Hearing Brief at 3.

⁴² *Id.*

⁴³ *Id.* at 3–4, *citing*, R. Pulliam testimony, Hearing Video Transcript (HVT) 0:20:30 (worried about risk and capitalization; no financing available); A. Artis testimony, HVT 1:20:10 (capital needed to make actual repairs); L. Smither testimony, HVT 2:37:40 (no money to make improvements), 2:59:00, 3:08:25 (no money to replace a smashed lift station and cannot get it; member-owners personally lend money to utilities for needed repairs).

⁴⁴ *Id.* at 4.

⁴⁵ Notice of Filing of Affidavit, (filed Aug. 9, 2019) (Affidavit of Phil Macias stating that CSWR, LLC has received the necessary equity capital required to acquire the assets.).

The Commission acknowledges that an out-of-state entity willing to acquire several small wastewater treatment systems, some of which require significant capital improvements, is an issue of first impression to the Commission. The business model itself is novel; therefore, the financing of the acquisition and operations might be unorthodox as well. The Commission finds that Bluegrass Water and its affiliates have the financial ability to acquire and operate the various systems and provide reasonable service. The record reflects that Bluegrass Water and its affiliates have arranged for the necessary equity and debt to acquire the systems and to provide reasonable service.⁴⁶ Josiah Cox testified that CSWR, as a fallback position for debt if a better rate cannot be found, could obtain a loan with a rate ceiling from U.S. Water Capital.⁴⁷ Mr. Cox also testified that at CSWR it is common not to draw on equity funding until regulatory approval has been obtained.⁴⁸ This equity and debt model appears to have worked in CSWR's Arkansas and Missouri systems, and should work in Kentucky.

We also note that the EEC has tools at its disposal to condition a wastewater permit to ensure the plant's owner has the requisite financial and technical ability to provide reasonable service. These tools include, but are not limited to, requiring the maintenance of a financial instrument or letter of credit, requiring an asset management plan, and conducting a structural analysis of the plant.⁴⁹ Oversight by the EEC and the Commission will ensure that the systems operate to provide reasonable service, while Commission

⁴⁶ See, Joint Applications at ¶¶ 44–45.

⁴⁷ J. Cox testimony, HVT 10:20.

⁴⁸ J. Cox testimony, HVT 15:15.

⁴⁹ See KRS 224.73-140.

review of annual financial reports will help ensure adequate revenues to maintain reasonable service.

Managerial Ability

The Attorney General argues that Bluegrass Water lacks the managerial experience to provide reasonable service. The Attorney General notes that Bluegrass Water has no plans to have a physical presence in Kentucky, and will not oversee the third-party contractors that will handle the day-to-day operations in Kentucky. The Attorney General expresses concern about Bluegrass Water's reliance on its out-of-state parent company, CSWR, to manage the third-party contractors because CSWR is not subject to the Commission's jurisdiction. For this reason, the Attorney General concludes that Bluegrass Water does not have the managerial ability to provide reasonable service.⁵⁰

Bluegrass Water argues that it will be providing service in Kentucky and will be the jurisdictional utility subject to the Commission's jurisdiction.⁵¹ Bluegrass Water notes that, like all of the transferring utilities; it will not directly employ people, and will contract with third parties or be able to call on CSWR Group for access to specialized functions.⁵² Bluegrass Water notes that CSWR Group, from St. Louis, Missouri, has been able to provide management services and reasonable service for its systems in Missouri and Arkansas.⁵³ Bluegrass Water also states that it has not executed contracts with third parties because it would not make business sense to do so absent regulatory approval.

⁵⁰ Attorney General's Post-Hearing Brief at 4–5.

⁵¹ Applicants Response to Attorney General's Post-Hearing Brief at 4.

⁵² *Id.* at 4–5.

⁵³ *Id.* at 5.

Bluegrass Water notes that CSWR Group's third-party contractors in Arkansas and Missouri, Midwest Water Operations and Nitor Billing Services, have performed well and can accomplish the same tasks in Kentucky.

The Commission finds that Bluegrass Water will have the managerial ability to provide reasonable service in Kentucky. The fact that CSWR has worked with, and can contract with, two proven entities like Midwest Water Operations and Nitor Billing Services, as well as the fact that Bluegrass Water has kept the option open for better-suited entities, reassure the Commission that Bluegrass Water has the managerial ability to operate the transferred utilities. CSWR has apparently operated its systems in Missouri and Arkansas in such a way as to provide reasonable service, and that will allow Bluegrass Water to do the same.

The Commission also notes that it has the ability, pursuant to KRS 278.260-280 to investigate the rates and services of any utility, and prescribe how the utility should perform its functions in order to provide reasonable and adequate services at reasonable rates.

However, due to the business structure of Bluegrass and its intent to have no employees and no office in Kentucky, there must be at least one individual with responsibility for the operations of Bluegrass Water. Based on the record in this case, that individual should be the President of Central States Water Resources, Inc., and should agree to be subject to service of process in Kentucky as if a resident of Kentucky. Should Bluegrass Water's model fail in any other manner to provide the requisite managerial ability to provide reasonable service, the Commission will investigate and correct the deficiency.

Financial Integrity to Ensure Continuity of Sewer Service

The Attorney General argues that Bluegrass Water has failed to provide evidence of financial integrity to ensure continuity of sewer service. The Attorney General proposes that the Commission require Bluegrass Water to set aside, through some sort of financial mechanism, at least six months of funds to pay the eventual third-party operations entity that will operate in Kentucky. The Attorney General asserts that this will ensure continued operation should Bluegrass Water be unable to provide reasonable service.⁵⁴

Bluegrass Water argues that the continuity of service will be ensured by inclusion of the acquired systems into one operating company, inclusion in the multi-state CSWR Group, and greater access to equity and debt.⁵⁵ Bluegrass Water asserts that being part of CSWR Group has ensured the continuity of service for its utilities in Missouri and Arkansas.⁵⁶ Bluegrass Water states that it would not reject a short-term requirement that it post a bond of up to \$100,000, if the condition would expire upon the filing of its 2019 Annual Report.⁵⁷

As an initial matter, *contra* Bluegrass Water's belief, KRS 278.020(10) applies to the matter at hand and evidence of the financial integrity to ensure continuity of service is necessary. Bluegrass Water is similarly mistaken that the Commission's recent

⁵⁴ Attorney General's Post-Hearing Brief at 9.

⁵⁵ Applicant's Response to Attorney General's Post-Hearing Brief at 7.

⁵⁶ *Id.*

⁵⁷ *Id.* at 8, FN 23.

decision in Case No. 2017-00383⁵⁸ supports the conclusion that evidence of financial integrity exists automatically when a smaller utility is purchased by a larger utility that is part of a multi-state entity. Kentucky-American Water Company (Kentucky-American) is Kentucky's largest water utility, and has operated in Kentucky for several decades. Its finances and operations are well known to the Commission, and its Kentucky office is an approximate 30-mile drive from the Commission's office.

Bluegrass Water and its affiliates share little resemblance to Kentucky-American. Bluegrass Water's business model has not been applied in Kentucky, and while CSWR Group has reported promising results from its Missouri and Arkansas operations, it simply has not been operating long enough to provide sufficient assurance to the Commission absent a financial commitment to ensure continued operations should Bluegrass Water be unable to provide reasonable service. To that end, the Commission will require Bluegrass Water to post a financial instrument equivalent to two-months of the cost of its third-party contractors. This requirement will be terminated by further order of the Commission upon the Commission's confirmation that Bluegrass Water's financial condition is sufficiently strong to ensure the continued operation of sewer service.

Capital Structure

As discussed above, Bluegrass Water will finance the acquisition and operations utilizing a 50/50 capitalization structure.⁵⁹ The Attorney General argues that Bluegrass

⁵⁸ Case No. 2017-00383 *Electronic Verified Joint Application of Eastern Rockcastle Water Association, Inc. and Kentucky-American Water Company for the Transfer of Control and Assets*, (Ky. PSC Jan. 19, 2018)

⁵⁹ Joint Application at 14.

Water should maintain a minimum debt-to-capitalization ratio of 40% and a maximum debt to capitalization ratio of 60%.⁶⁰ The Attorney General argues that maintaining this range would ensure that Bluegrass Water's debt ratio is not too high and also ensure that the weighted cost of capital is not too high.⁶¹ The Attorney General proposes that Bluegrass Water be required to submit a plan to ensure that the proposed range is maintained.⁶²

Bluegrass Water asserts that the proposed capital structure will allow it the necessary flexibility to meet challenges in the acquired systems, and that adopting the ratios proposed by the Attorney General will constrain that flexibility.⁶³ Bluegrass Water states that the 50/50 capitalization plan was developed after the acquisition of the systems in Missouri and Arkansas.⁶⁴ Bluegrass Water states that the systems in Missouri and Arkansas have a combined debt/equity ratio of 1.86 and an equity-to-capitalization percentage of 35%.⁶⁵ Bluegrass Water also notes that the Commission can adjust the capitalization ratio in any future rate cases.

We reject the Attorney General's request to impose a different capital structure than that proposed in the application. First, given the distressed nature of most of the acquired systems, the proposed capital structure should provide the necessary flexibility

⁶⁰ Attorney General's Post-Hearing Brief at 6.

⁶¹ *Id.* at 7.

⁶² *Id.*

⁶³ Applicants Response to Attorney General's Post-Hearing Brief at 12.

⁶⁴ *Id.*, *citing*, Macias Testimony, HVT 2:28.

⁶⁵ *Id.*, *citing*, Joint Applicants' Response to Commission Staff's First Request for Information, Request No. 6.

to address any unknown issues arising after the acquisition of the system. Second, as evidenced in the capitalization ratios in CSWR's Missouri and Arkansas systems, the equity to capitalization percentage is 35%, and we hope that the systems in Kentucky will migrate towards those ratios. Third, we can adjust the capitalization ratio upon investigation or during a rate case, and disallow unreasonable or imprudent costs associated with the capital structure.

We also find that Bluegrass Water's equity-to-capitalization percentage should not exceed 50% and that every effort must be made to lower that percentage. If the equity-to-capital percentage exceeds 50%, Bluegrass Water shall notify the Commission in writing within 30 days of this occurring and submit to the Commission a detailed plan explaining how it will revise its capital structure to achieve its approved equity-to-capital ratio.

Employer or Purchaser of Last Resort

The Attorney General asserts that the Commission has imposed as a condition on previous out-of-state acquirers, that the acquirer would not be the employer or purchaser of last resort for employees, assets, services, or products associated with any affiliate of the acquirer and encourages the Commission to impose the same on Bluegrass Water.⁶⁶ We agree that this is a reasonable condition to impose to ensure that the acquisition is in the public interest. We will also require Bluegrass Water to inform the Commission, within

⁶⁶ Attorney General's Post-Hearing Brief at 7, *citing*, Case No. 2006-00197, *The Joint Petition of Kentucky-American Water Company, Thames Water Aqua Holdings GmbH, Rwe Aktiengesellschaft, Thames Water Aqua Us Holdings, Inc., and American Water Works Company, Inc. for Approval of a Change In Control of Kentucky-American Water Company* (KY PSC Apr. 16, 2007) at 20.

30 days of the occurrence of the transfer, sale, or abandonment of any of Bluegrass Water's affiliates' utilities in other jurisdictions.

Monitoring adequacy and reliability

The Attorney General recommends that the Commission impose reporting conditions on Bluegrass Water to ensure that service quality is not degraded. Specifically, the Attorney General recommends that the Commission should require for a reasonable time that Bluegrass Water file reports regarding discharge quality, number of service interruptions, employee or contractor response times, number of customer complaints and customer inquiry time. The Attorney General also exhorts the Commission to establish metrics for discharge and inspection purposes, including monitoring and reporting on DOW citations or violations.

We believe that a detailed and ongoing report such as the Attorney General recommends might be too onerous and costly, but we do believe some manner of monitoring and reporting is necessary. It is no secret that several of the acquired systems are in varying states of disrepair, with ongoing DOW violations; therefore, ongoing reports of such violations will only inform the Commission of what it already knows. However, it would be useful to be able to monitor the improvement in service quality. To that end, the Commission will require that, one month after the closing of the transaction, Bluegrass Water file a report listing discharge quality, number of service interruptions, employee or contractor response times, and DOW violations or citations for the preceding month. This will serve as a baseline against which to judge improvements to the systems. Bluegrass Water shall also file, at six months and one year after the closing of the transaction, a report listing discharge quality, number of service interruptions, employee or contractor

response times, and DOW violations or citations for the preceding year. This will allow the Commission to review the anticipated progress that Bluegrass Water has made in improving quality in the systems.

In addition to the reports above, we will also require Bluegrass Water to maintain its records in such a way to be able to readily distinguish between violations, repairs, investments, etc. for each system. This will allow review of Bluegrass Water's practices and will assist the Commission in determining how Bluegrass Water has used its resources in the operation and management of the various systems, as well as the reasonableness of the expenses and practices in any future ratemaking proceeding.

Local Office

The Attorney General expresses grave concerns about the level of service that will be provided and Bluegrass Water's lack of a local office or other physical presence in Kentucky, and opines that several Commission regulations indicate that a utility must maintain a local office in Kentucky.⁶⁷ The Attorney General also asserts that Bluegrass Water, upon the completion of the transfer, will immediately be out of compliance with several Commission regulations, including several that address a utility's maintenance of an office in Kentucky, and hours of operation, records maintenance, display of customer rights, etc.⁶⁸

Bluegrass Water argues that no statute or regulation requires that a utility maintain an office in Kentucky and that Bluegrass Water's requirements and plans relating to

⁶⁷ Attorney General's Post-Hearing Brief at 7.

⁶⁸ *Id.* at 5.

customer access and communication meet the letter and intent of such regulations.⁶⁹ Bluegrass Water notes that there is no requirement that a utility's records be maintained within Kentucky, pointing out that KRS 278.230(2) addresses inspection of a utility's documents that are maintained outside of Kentucky.⁷⁰ Bluegrass Water also states that, even if it had an office in Kentucky, it might not serve any purpose because it could be located over 100 miles from the nearest treatment system.⁷¹

Maintaining an office in Kentucky is not a prerequisite to providing service in Kentucky. Numerous non-resident telecommunications utilities, such as competitive local exchange carriers and commercial mobile radio service providers, provide service in Kentucky . . . Other types of utilities, such as Navitas KY NG, LLC, a gas utility, have no offices in Kentucky. Duke Kentucky, Inc. does not maintain a local office in Kentucky that is open to customers. Thus, while a utility is required to maintain office hours to discuss rate and service issues, those discussions can be conducted using a toll-free phone number rather than in person at a Kentucky-based office.

Moreover, the conditions of the plants of many of the systems to be acquired will require critical capital repairs necessitating a level of capital investment that will be significant. The additional expense of maintaining an office in Kentucky, which inevitably would be at some distance from a significant portion of Bluegrass Water's customers, cannot be justified and would not represent the best use of capital investment in the overall system. However, the Commission will require Bluegrass Water to maintain a

⁶⁹ Applicants Response to Attorney General's Post-Hearing Brief at 11.

⁷⁰ *Id.*

⁷¹ *Id.*

website that should, at a minimum, contain: (1) a summary of customers' rights; (2) tariffs, or links to the tariffs, for each system; (3) contact information to report service issues or emergencies both within and outside of regular business hours; (4) links to any tariffs filed in the future with the Commission; and (5) links to Bluegrass Water's system maps on the Kentucky Infrastructure Authority Wastewater Mapping website.

Proposed Purchase Price of Acquired Systems

The record reflects that the proposed purchase price for each of the systems exceeds the net utility plant reported in the most recent annual reports on file with the Commission for each of the systems proposed to be acquired.⁷² In the case of Lake Columbia and Fox Run, the net utility plant is reported as \$0.00. Airview's reported net plant value is \$450.⁷³

As discussed above, Messrs. Cogan and Smithers have sought to abandon the Airview system. They notified the Commission that they were "surrendering and abandoning all of [their] property interests and rights in and to the property owned by Airview" ⁷⁴ Because they proposed to walk away uncompensated from the Airview,

⁷² See, Confidential Joint Application, Exhibit D, p. 3, and P.R. Wastewater's Annual Report for the Calendar Year Ending 2018, p. 12 of 44; Confidential Joint Application, Exhibit F, p. 3, and L.H. Treatment's Annual Report for the Calendar Year Ending 2018, p. 12 of 44; Confidential Joint Application, Exhibit G, p. 3, and Kingswood's Annual Report for the Calendar Year Ending 2018, p. 12 of 44; Confidential Joint Application, Exhibit H, p. 3, and Airview's Annual Report for the Calendar Year Ending 2018, p. 12 of 44; Confidential Joint Application, Exhibit I, p. 3, and Brocklyn's Annual Report for the Calendar Year Ending 2018, p. 12 of 44; Confidential Joint Application, Exhibit J, p. 3, and Fox Run's Annual Report for the Calendar Year Ending 2018, p. 12 of 44; and Confidential Joint Application, Exhibit K, p. 3, and Lake Columbia's Annual Report for the Calendar Year Ending 2018, p. 12 of 44.

⁷³ Mr. Cogan attested the annual reports for Lake Columbia, Fox Run, Brocklyn, and Airview that the amount of the net plant value is correct and the Commission accepts those as accurate for the purposes of this proceeding.

⁷⁴ Case No. 2016-00207, *Airview Utilities, LLC's Notice of Surrender of Utility Property*, Airview Utilities, LLC's Notice of Surrender and Abandonment of Utility Property (filed July 15, 2016) at 2.

we see no reason for Bluegrass Water to pay anything beyond the net utility plant value as reported in Airview's most recent annual report. Accordingly, we will not approve this transaction should Bluegrass Water pay Airview more than \$450 for the purchase of its system. We will not disturb the purchase price of any of the other systems despite our concerns regarding the purchase price of Messrs. Cogan's and Smither's other systems.

Other Conditions

We also find that the imposition of the following conditions is necessary to ensure that the proposed transaction is in the public interest.

Pursuant to KRS 278.020, Bluegrass Water shall not begin the construction of any plant, equipment, property, or facility for furnishing wastewater services to the public, except ordinary extensions of existing systems in the usual course of business, until Bluegrass Water has obtained a Certificate of Public Convenience and Necessity from the Commission.

Pursuant to KRS 278.300, Bluegrass Water shall not issue any securities or evidences of indebtedness, or assume any obligation or liability in respect to the securities or evidences of indebtedness of any other person, until Bluegrass Water has been authorized to do so by an order of the Commission.

Pursuant to 807 KAR 5:011, Section 11(1)(a), within 30 days of the close of the acquisition of each system, Bluegrass Water shall file adoption notices for each of the systems' tariffs.

CONCLUSIONS OF LAW

Based upon the discussion and findings above, the Commission makes the following conclusions of law:

1. P.R. Wastewater, Marshall County, LH Treatment, Kingswood, Airview, Brocklyn, Fox Run, and Lake Columbia are utilities subject to the Commission's jurisdiction.

2. Bluegrass Water is a "corporation" and a "person" for purposes of KRS Chapter 278.⁷⁵

3. KRS 278.020(6) provides that "[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) 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 directory 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 finds that the same is to be made in accordance with law, for a proper purpose and is consistent with the public interest."

5. KRS 278.020(10) provides that "[t]he commission shall not approve any application under subsection (6) or (7) of this section for the transfer of control of a utility described in KRS 278.010(3)(f) unless the commission finds, in addition to findings required by those subsections, that the person acquiring the utility has provided evidence

⁷⁵ KRS 278.010.

of financial integrity to ensure the continuity of sewage service in the event that the acquirer cannot continue to provide service.”

6. Based on its financial commitments and subject to its acceptance of the conditions set forth in the Appendix to this Order, Bluegrass Water has sufficient financial integrity to ensure the continuity of service.

7. Bluegrass Water, subject to its acceptance of the conditions set forth in Appendix A to this Order, has the financial, technical, and managerial abilities to provide reasonable service to those persons located in the acquired systems.

8. To avoid any potential adverse effects that the proposed transaction may have on the quality of service that Bluegrass Water provides, the proposed transaction will be consistent with the public interest only under the conditions set forth in Appendix A to this Order.

IT IS THEREFORE ORDERED that:

1. The transfer of P.R. Wastewater, Marshall County, LH Treatment, Kingswood, Airview, Brocklyn, Fox Run, and Lake Columbia to Bluegrass Water is conditionally approved, subject to Bluegrass Water and Josiah Cox accepting the conditions set forth in the Appendix to this Order.

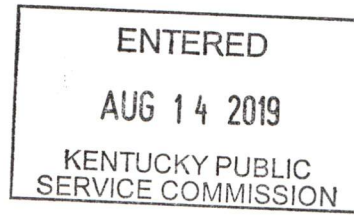
2. The proposed transfer of control shall not proceed unless, within 20 days of the date of this Order, the Commission receives written acknowledgments of Josiah Cox and, on behalf of Bluegrass Water and its affiliates by each entity’s chief executive officer, that these entities each accept and agree to be bound by the commitments set forth in the Appendix to this Order.

3. Within ten days of completion of the transfer of P.R. Wastewater, Marshall County, LH Treatment, Kingswood, Airview, Brocklyn, Fox Run, and Lake Columbia to Bluegrass Water, Bluegrass Water shall notify the Commission in writing of the date that each transfer occurred.

4. Within 90 days of completion of the transfer of P.R. Wastewater, Marshall County, LH Treatment, Kingswood, Airview, Brocklyn, Fox Run, and Lake Columbia to Bluegrass Water, each entity shall file with the Commission a final annual report covering the reporting period of January 1, 2019, to the date of closing, in addition to any outstanding annual reports for periods prior to the calendar year 2019.

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By the Commission



ATTEST:


Executive Director

Case No. 2019-00104

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2019-00104 DATED **AUG 14 2019**

The proposed acquisition of P.R. Wastewater, Marshall County, LH Treatment, Kingswood, Airview, Brocklyn, Fox Run, and Lake Columbia by Bluegrass Water is approved upon the following conditions:

1. Within 30 days of the closing of the transaction, Bluegrass Water shall file with the Commission and parties in this case, its post-closing accounting entries in accordance with the Commission's Uniform System of Accounts for Class C and D Sewer Utilities.

2. Upon Bluegrass Water's closing on a transferring utility's assets, the customers served by those assets will experience no adverse change in service.

3. No later than March 31st of each year, Bluegrass Water shall file with the Commission a detailed organization chart showing all subsidiaries and affiliates as of the end of the previous calendar year.

4. Bluegrass Water, post-closing, will adequately fund and maintain the transferred systems.

5. Within 60 days of the closing of the transaction, Bluegrass Water shall post a guaranteed financial instrument that is the equivalent of two-months of the cost of its third-party contractors.

6. If the equity-to-capital percentage exceeds 50%, Bluegrass Water shall notify the Commission in writing within 30 days of this occurring and submit to the Commission a detailed plan explaining how it will revise its capital structure to achieve its approved equity-to-capital ratio.

7. Bluegrass Water shall not be the employer or purchaser of last resort for employees, assets, services, and/or products associated with any affiliate of Bluegrass Water.

8. Bluegrass Water shall inform the Commission within 30 days of the occurrence of the transfer, sale, or abandonment of any of its affiliates' utilities in other jurisdictions.

9. One month after the closing of the transaction, Bluegrass Water shall file for each of the acquired systems a report listing discharge quality, number of service interruptions, employee or contractor response times, and DOW violations or citations for the preceding month.

10. Six months after the closing of the transaction, Bluegrass Water shall file for each of the acquired systems a report listing discharge quality, number of service interruptions, employee or contractor response times, and DOW violations or citations for the preceding month.

11. One year after the closing of the transaction, Bluegrass Water shall file for each of the acquired systems a report listing discharge quality, number of service interruptions, employee or contractor response times, and DOW violations or citations for the preceding month.

12. Bluegrass Water shall maintain its records in such a way to be able to readily distinguish between violations, repairs, investments, etc. for each system.

13. The President of Central States Water Resources, Inc., and its successors or assigns, shall be subject to service of process in Kentucky as if he was a resident of Kentucky.

14. Bluegrass Water shall maintain a toll-free phone number and a website that contains: 1) a summary of customers' rights; 2) tariffs, or links to the tariffs, for each system; 3) contact information for emergencies during regular and after-hours to report service issues; 4) links to any tariffs filed in the future with the Commission; and 5) links to Bluegrass Water's systems maps on the Kentucky Infrastructure Authority Wastewater Mapping website.

15. Bluegrass Water shall not pay more than \$450 for the acquisition of Airview.

16. Bluegrass Water shall not begin the construction of any plant, equipment, property, or facility for furnishing wastewater services to the public, except ordinary extensions of existing systems in the usual course of business, until Bluegrass Water has obtained a Certificate of Public Convenience and Necessity from the Commission.

17. Pursuant to KRS 278.300, Bluegrass Water shall not issue any securities or evidences of indebtedness, or assume any obligation or liability in respect to the securities or evidences of indebtedness of any other person until Bluegrass Water has been authorized to do so by an Order of the Commission.

18. Pursuant to 807 KAR 5:011, Section 11(1)(a), within 30 days of the close of the acquisition of each system, Bluegrass Water shall file adoption notices for each of the systems' tariffs.

19. Pursuant to KRS 278.130 and KRS 278.140, Bluegrass Water shall pay the annual assessments for the acquired utilities as calculated using the gross revenue reports for the 2019 calendar year and shall pay the annual assessment for each year thereafter based upon its total gross revenue.

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