

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF THE LAKE)	
VILLAGE WATER ASSOCIATION, INC. TO ISSUE)	
SECURITIES IN THE APPROXIMATE PRINCIPAL)	
AMOUNT OF \$2,100,000 FOR THE PURPOSE OF)	CASE NO.
REFUNDING CERTAIN OUTSTANDING)	2021-00020
INDEBTEDNESS OF THE ASSOCIATION)	
PURSUANT TO THE PROVISIONS OF KRS)	
278.300 AND 807 KAR 5:001)	

ORDER

On January 22, 2021, Lake Village Water Association (Lake Village Water), filed an application seeking Commission authority to enter into a loan agreement (Loan) with Kentucky Rural Water Finance Corporation (KRWFC) to borrow approximately \$2,100,000 (subject to adjustment of up to 10 percent), the proceeds of which will be used to refinance two outstanding debt obligations of Lake Village Water and to pay the costs of issuance of the Loan. There are no intervenors in this case, and the matter is submitted to the Commission for a decision based upon the evidentiary record.

Lake Village Water, a water association organized pursuant to KRS Chapter 273, owns and operates facilities that provide retail water service to 2,226 residential customers in Boyle and Mercer counties, Kentucky.¹

¹ *Annual Report of Lake Village Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2019* (2019 Annual Report) at 12 and 49.

The Commission also notes that Lake Village Water has not sought a general adjustment in rates since 2003.² An examination of finances outlined in the annual and audit reports filed with the Commission reveals that Lake Village Water has been operating with a negative net income for all the past five calendar years.³ A key general recommendation that resulted from the investigation by the Commission in Case No. 2019-00041,⁴ was that water districts with sustained excessive water loss should monitor the sufficiency of their base rates closely and, in general, apply for base rate adjustments on a more frequent basis.⁵ While this statement was made in the context of Case No. 2019-00041, which involved water utilities that were under examination due to high water loss, the theory that a closer examination of a water district's finances with regard to the sufficiency of rates by the Commission still applies in this instance. The lack of insight into Lake Village Water's financial records that provide more detail than its annual reports and audits filed with the Commission, coupled with the fact that Lake Village Water has been operating with a negative net income for the preceding five calendar years, indicates to the Commission that Lake Village Water should file an application for a traditional adjustment in rates or an alternative rate adjustment within one year of the date of filing of this Order.

² Case No. 2003-00401, *The Application of the Lake Village Water Association, Inc., for Approval of a Proposed Increase in Rates for Water Service* (Ky. PSC Feb. 2, 2004).

³ Lake Village Association's Comprehensive Net Income for the calendar years 2015 through 2019 was \$(227,641), \$(216,124), \$(208,843), \$(322,870), and \$(223,391), respectively.

⁴ Case No. 2019-00041, *Electronic Investigation into Excessive Water Loss by Kentucky's Jurisdictional Water Utilities* (Ky. PSC. Nov. 22, 2019).

⁵ See generally, *Id.*

The Commission notes that in its 2019 Annual Report, Lake Village Water reported a water loss of 17.009 percent.⁶ Commission regulation 807 KAR 5:066(6)(3) states that for ratemaking purposes, a utility's water loss shall not exceed 15 percent of total water produced and purchased, excluding water consumed by a utility in its own operations. Reduction of Lake Village Water's water loss to 15 percent would result in an approximate \$10,453.49⁷ decrease to purchased water expense. Potentially, Lake Village Water is paying \$.05 per 1,000 gallons sold, for expenses associated with water loss greater than 15 percent.⁸

The Commission is placing greater emphasis on monitoring utilities that consistently exceed the 15 percent water loss threshold and strongly encourages Lake Village Water to pursue reasonable actions to reduce its water loss. Failure by Lake Village Water to make significant process towards reducing water loss may cause the Commission to pursue additional action with the utility.

⁶ 2019 Annual Report at 57.

⁷

Purchased Water from 2019 Annual Report	\$ 520,333
Times: Water Loss Above 15 Percent	<u>2.009%</u>
Purchased Water Expense Reduction	\$ 10,453.49

⁸

Purchased Water Expense Reduction	\$ 10,453.49
Divided by: Total 1,000 gallons sold from 2019 Annual Report	<u>208,854</u>
Cost per 1,000 gallons sold	\$ 0.05

Lake Village Water proposes to execute the Loan with KRWFC to borrow \$2,100,000.⁹ The proposed Loan will have a 30-year term subject to interest rates that will vary from 2.75 percent to 3.35 percent per annum.¹⁰ Lake Village Water proposes to use the proceeds from the KRWFC Loan to fully refund the Rural Development (RD) loan held by the United States Department of Agriculture (USDA) No. 91-09 dated November 8, 2007, with an original principal amount of \$885,000, and promissory note 91-10 dated January 12, 2010, with an original principal amount of \$1,544,000.¹¹

Lake Village Water estimates that it will expend \$2,180,376.90 to refund the prior bonds.¹² The estimated expended cost to refinance the outstanding indebtedness includes reoffering premiums of \$80,376.90.¹³ Lake Village Water provided a Debt Service Comparison indicating that the refinancing would save \$362,235.66¹⁴ over the life of the proposed Loan, resulting in a positive net present value (NPV) cash flow savings of \$245,416.65.¹⁵

The Commission has reviewed the proposed refinancing and finds Lake Village Water's proposal to be reasonable due to the lower effective interest rate and cash flow savings Lake Village Water would realize over the period of the Loan. Although, if the

⁹ Application at 2, paragraph 5.

¹⁰ *Id.*, Exhibit B.

¹¹ *Id.* at 2, paragraph 5.

¹² *Id.*, Exhibit C, Sources and uses. Uses of Funds: \$36,750.00 (Total Underwriter's Discount) + \$37,100.00 (Costs of Issuances) + \$2,105,311.98 (Deposit to Current Refunding Fund) + \$1,184.92 (Rounding Amount) = \$2,180,376.90.

¹³ *Id.*, Exhibit C.

¹⁴ *Id.*, Exhibit D.

¹⁵ *Id.*

new interest rate on the proposed refinancing is higher than the range of interest rates set forth in the application, Lake Village Water should not proceed with the refinancing unless the NPV of the refinancing results in positive cash flow. The Commission commends Lake Village Water for taking advantage of the financing alternatives available to it, thereby securing savings for itself and its customers. However, the Commission is concerned with Lake Village Water’s prolonged absence from the Commission’s review of its asset management through an application for adjustment of its rates. The Commission notes that, according to Lake Village Water’s audit reports, Lake Village Water has had a negative net income for the last five years and a continuous decrease in cash during the last four years, as shown below.¹⁶

Year	2015	2016	2017	2018	2019
Net Income	\$(227,641)	\$(216,124)	\$(208,843)	\$(322,870)	\$(223,391)
Add: Depreciation Expense	239,252	292,770	306,829	312,039	312,915
Cash Basis Income	\$ 11,611	\$ 76,646	\$ 97,986	\$ (10,831)	\$ 89,524

Year	2015	2016	2017	2018	2019
Cash and Cash Equivalents	\$ 47,545	\$ 13,740	\$ 32,243	\$ 4,996	\$ 9,577
Restricted Funds	306,258	277,947	241,704	132,759	117,307
Net Increase (Decrease) in Cash	18,016	(71,675)	(33,203)	(124,598)	(25,904)

KRS 278.300(4) states that the Commission may grant or deny an application for approval of financing in whole or in part, or upon such terms and conditions as deemed necessary or appropriate. Therefore, the Commission finds that Lake Village Water’s

¹⁶ Lake Village Water’s Audit Reports can be found on the Commission’s Website at:
https://psc.ky.gov/Utility_Financial_Reports_Net/uploaded/support/SD_34800_2019_1.pdf
https://psc.ky.gov/Utility_Financial_Reports_Net/uploaded/support/SD_34800_2018_1.pdf
https://psc.ky.gov/Utility_Financial_Reports_Net/uploaded/support/SD_34800_2017_1.pdf
https://psc.ky.gov/Utility_Financial_Reports_Net/uploaded/support/SD_34800_2016_1.pdf
https://psc.ky.gov/Utility_Financial_Reports_Net/uploaded/support/SD_34800_2015_1.pdf

proposal should be granted with the condition that it file an application for adjustment of its base rates through an alternative rate filing within one year of the date of filing of this Order.

After consideration of the evidence of record and being sufficiently advised, the Commission finds that:

1. The proposed Loan from KRWFC is for lawful objects within the corporate purposes of Lake Village Water; is necessary and appropriate for and consistent with the proper performance by the utility of its service to the public; will not impair its ability to perform that service; is reasonable, necessary, and appropriate for such purposes; and should be approved.

2. Lake Village Water should execute its note as security for the proposed Loan in the manner described in its application.

3. The Commission directs Lake Village Water to the Commission's March 16, 2020 and March 24, 2020 Orders in Case No. 2020-00085¹⁷ regarding filings with the Commission. The Commission expects the original documents to be filed with the Commission within 30 days of the lifting of the current state of emergency.

4. The final amounts of the RD payoff, the legal fees, and the new KRWFC loan will not be known until the refinancing transaction is finalized. Therefore, Lake Village Water should provide the Commission an updated version the application, Exhibit D, reflecting the cash flow analysis of the new KRWFC Loan within ten days of finalizing the transaction.

¹⁷ Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC Mar. 16, 2020), Order at 5–6. Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC Mar. 24, 2020), Order at 1–3.

5. Within ten days of the execution of the new KRWFC loan documents, Lake Village Water should file with the Commission one copy in paper medium and an electronic version of the loan documents.

6. The proceeds from the proposed Loan should be used only for the lawful purposes set out in Lake Village Water's application.

7. The terms and conditions of the new KRWFC Loan should be consistent with the KRWFC assistance program as described in Lake Village Water's application.

8. Lake Village Water should file for an adjustment in base rates or file for an alternative rate filing within one year of the date of filing of this Order to ensure that its rates are sufficient.

IT IS THEREFORE ORDERED that:

1. Lake Village Water is authorized to enter into the Loan with KRWFC to borrow no more than the total amount to pay off the indebtedness proposed to be refinanced as identified in the application on the condition that the final NPV of the savings, determined upon closing, generate positive cash flow. The Loan maturity date and interest rate shall be in accordance with the KRWFC assistance program as described in Lake Village Water's application.

2. Lake Village Water shall execute the KRWFC Loan documents as authorized herein.

3. Lake Village Water shall comply with all matters set out in finding paragraphs 3 through 7 as if they were individually so ordered.

4. Any documents filed in the future pursuant to finding paragraphs 4 and 5 shall reference this case number and shall be retained in the post-case correspondence file.

5. Lake Village Water shall file for an adjustment in base rates or file for an alternative rate filing within one year of the date of filing of this Order.

6. This case is closed and will be removed from the Commission's docket.

Nothing contained herein shall be deemed a warranty or finding of value of securities or financing authorized herein on the part of the Commonwealth of Kentucky or any agency thereof.

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By the Commission



ATTEST:


Executive Director

Case No. 2021-00020

*Kristen Millard
Raymond James Financial Services
300 West Vine Street
Lexington, KENTUCKY 40507

*Lake Village Water Association, Inc.
801 Pleasant Hill Drive
P. O. Box 303
Burgin, KY 40310

*Mike D Sanford
Executive Director
Lake Village Water Association, Inc.
801 Pleasant Hill Drive
P. O. Box 303
Burgin, KY 40310

*Honorable W. Randall Jones
Attorney at Law
Rubin & Hays
Kentucky Home Trust Building
450 South Third Street
Louisville, KENTUCKY 40202