

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF THE)	
ROWAN WATER, INC. TO ISSUE)	
SECURITIES IN THE APPROXIMATE)	
PRINCIPAL AMOUNT OF \$2,450,000 FOR)	CASE NO.
THE PURPOSE OF REFUNDING CERTAIN)	2021-00042
OUTSTANDING INDEBTEDNESS OF THE)	
ASSOCIATION PURSUANT TO THE)	
PROVISIONS OF KRS 278.300 AND 807 KAR)	
5:001)	

ORDER

On February 24, 2021, Rowan Water, Inc. (Rowan Water) filed an application seeking Commission authority to enter into a loan agreement (Loan) with Kentucky Rural Water Finance Corporation (KRWFC) to borrow approximately \$2,450,000 (subject to adjustment of up to 10 percent), the proceeds of which will be used to refinance six outstanding debt obligations of Rowan 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.

Rowan Water, a water association organized pursuant to KRS Chapter 273, owns and operates facilities that provide retail water service to 6,494 residential customers in Carter, Elliott, Fleming, Morgan and Rowan counties, Kentucky.¹

¹ *Annual Report of Rowan Water 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 notes that in its 2019 Annual Report, Rowan Water reported a water loss of 21.0571 percent.² 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 Rowan Water's water loss to 15 percent would result in an approximate \$80,717.88³ decrease to purchased water expense. Potentially, Rowan Water is paying \$0.13 per 1,000 gallons sold, for expenses associated with water loss greater than 15 percent.⁴

The Commission also notes that Rowan Water has not sought a general adjustment in rates since 2002.⁵ According to Rowan Water's annual reports and audit reports, Rowan 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.⁶

² 2019 Annual Report at 57.

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Purchased Water from 2019 Annual Report	\$ 1,332,616
Times: Water Loss Above 15 Percent	<u>6.0571%</u>

Purchased Water Expense Reduction	\$ 80,717.88
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Purchased Water Expense Reduction	\$ 80,717.88
Divided by: Total 1,000 gallons sold from 2019 Annual Report	<u>636,864</u>
Cost per 1,000 gallons sold	\$ 0.13

⁵ Case No. 2002-00425, *An Adjustment of the Rates of Rowan Water, Inc.*

⁶ Rowan Water's Annual Reports can be found on the Commission's Website at:

- https://psc.ky.gov/UFR_PDF/Water/2019/35800_Rowan_Water%20_Inc.pdf
- https://psc.ky.gov/UFR_PDF/Water/2018/35800_Rowan_Water%20_Inc.pdf
- https://psc.ky.gov/UFR_PDF/Water/2017/35800_Rowan_Water%20_Inc.pdf
- https://psc.ky.gov/UFR_PDF/Water/2016/35800_Rowan_Water%20_Inc.pdf
- https://psc.ky.gov/UFR_PDF/Water/2015/35800_Rowan_Water%20_Inc.pdf
- https://psc.ky.gov/Utility_Financial_Reports_Net/uploaded/support/SD_35800_2017_1.pdf
- https://psc.ky.gov/Utility_Financial_Reports_Net/uploaded/support/SD_35800_2018_2.pdf
- https://psc.ky.gov/Utility_Financial_Reports_Net/uploaded/support/SD_35800_2019_1.pdf

Year	2015	2016	2017	2018	2019
Net Income	\$ (242,105)	\$ (252,512)	\$ (333,928)	\$ (324,169)	\$ (564,790)
Add: Depreciation Expense	515,727	518,171	505,181	508,832	518,192
Cash Basis Income	\$ 273,622	\$ 265,659	\$ 171,253	\$ 184,663	\$ (46,598)
Year		2016	2017	2018	2019
Cash and Cash Equivalents		\$ 590,246	\$ 562,988	\$ 521,117	\$ 472,475
Restricted Cash		335,125	366,552	380,661	335,943
Sum: End-of-Year Balance		925,371	929,540	901,778	808,418
Net Increase (Decrease) in Cash		\$ 95,272	\$ 4,169	\$ (27,762)	\$ (93,360)

A key recommendation that resulted from the investigation by the Commission in Case No. 2019-00041⁷ is 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. 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 principle 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 Rowan Water's financial records that provide more detail than its annual reports and audits filed with the Commission, coupled with the fact that Rowan Water has been operating with a negative net income for the preceding five calendar years, indicates to the Commission that Rowan 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.

The Commission is placing greater emphasis on monitoring utilities that consistently exceed the 15 percent water loss threshold and strongly encourages Rowan

⁷ Case No. 2019-00041, *Electronic Investigation into Excessive Water Loss by Kentucky's Jurisdictional Water Utilities* (Ky. PSC. Nov. 22, 2019).

Water to pursue reasonable actions to reduce its water loss. Failure by Rowan Water to make significant progress towards reducing water loss may cause the Commission to pursue additional action with the utility.

Rowan Water proposes to execute the Loan with KRWFC to borrow \$2,450,000.⁸ The proposed Loan will have a 24-year term subject to interest rates that will vary from 2.75 percent to 3.25 percent per annum.⁹ Rowan 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) dated July 19, 1991, with an original principal amount of \$1,298,000; a promissory note 1992 dated September 15, 1992, with an original principal amount of \$386,000; a promissory note 1998 dated May 13, 1998 with an original principal amount \$1,230,000; a promissory note 2001 dated May 9, 2001, with an original principal amount \$359,000; a promissory note 2004A dated January 27, 2004, with an original principal amount \$475,000; and a promissory note 2004B dated January 27, 2004, with an original principal amount \$210,200.¹⁰

Rowan Water estimates that it will expend \$2,623,145.70 to refund the prior bonds.¹¹ The estimated expended cost to refinance the outstanding indebtedness includes reoffering premiums of \$173,145.70.¹² Rowan Water provided a Debt Service

⁸ Application at 2, paragraph 5.

⁹ *Id.*, Exhibit B.

¹⁰ *Id.* at 2, paragraph 5.

¹¹ *Id.*, Exhibit C, Sources and uses. Uses of Funds: \$42,875.00 (Total Underwriter's Discount) + \$42,700.00 (Costs of Issuances) + \$2,537,260.25 (Deposit to Current Refunding Fund) + \$310.45 (Rounding Amount) = \$2,623,145.70.

¹² *Id.*, Exhibit C.

Comparison indicating that the refinancing would save \$481,578.73¹³ over the life of the proposed Loan, resulting in a positive net present value (NPV) cash flow savings of \$381,367.56.¹⁴

The Commission has reviewed the proposed refinancing and finds Rowan Water's proposal to be reasonable due to the lower effective interest rate and cash flow savings Rowan Water would realize over the period of the Loan. Although, if the new interest rate on the proposed refinancing is higher than the range of interest rates set forth in the application, Rowan Water should not proceed with the refinancing unless the NPV of the refinancing results in positive cash flow. The Commission commends Rowan 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 Rowan Water's prolonged absence from the Commission's review of its asset management through an application for adjustment of its rates given the length of time since Rowan Water's last generate rate adjustment and its negative net income for the last five years, as discussed elsewhere in this Order. Therefore, the Commission finds that Rowan Water's 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 Rowan Water; is necessary and appropriate for and consistent with the

¹³ *Id.*, Exhibit D.

¹⁴ *Id.*

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

3. The Commission directs Rowan Water to the Commission's March 16, 2020 and March 24, 2020 Orders in Case No. 2020-00085¹⁵ 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, Rowan 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.

5. Within ten days of the execution of the new KRWFC loan documents, Rowan 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 Rowan Water's application.

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

¹⁵ 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.

8. Rowan 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. Rowan 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 Rowan Water's application.

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

3. Rowan 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. Rowan 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.

By the Commission



ATTEST:


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