

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF WEST LAUREL)	
WATER ASSOCIATION, INC. TO ISSUE)	
SECURITIES IN THE APPROXIMATE PRINCIPAL)	
AMOUNT OF \$1,875,000 FOR THE PURPOSE OF)	CASE NO.
REFUNDING CERTAIN OUTSTANDING)	2021-00097
OBLIGATIONS OF THE ASSOCIATION)	
PURSUANT TO THE PROVISIONS OF)	
KRS 278.300 AND 807 KAR 5:001)	

ORDER

On February 23, 2021, West Laurel Water Association (West Laurel Water) filed an application seeking Commission authority to refinance certain debt of up to \$1,875,000 via an Assistance Agreement (Loan) with the Kentucky Rural Water Finance Corporation (KRWFC). There are no intervenors in this case, and the matter is submitted to the Commission for a decision based upon the evidentiary record.

APPLICABLE LAW

KRS 278.300 requires Commission authorization before a utility may “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.”¹ KRS 278.300(3) clarifies the scope of Commission review and states:

The Commission shall not approve any issue or assumption unless, after investigation of the purposes and uses of the proposed issue and proceeds thereof, or of the proposed assumption of obligation or liability, the commission finds that the issue or assumption is for some lawful object within the corporate purposes of the utility, is necessary or appropriate

¹ KRS 278.300(1).

for or consistent with the proper performance by the utility of its service to the public and will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose.

As discussed more fully below, the Commission finds that West Laurel Water should be authorized to enter into the proposed assistance agreement with KRWFC refinancing up to \$1,875,000 of outstanding indebtedness to the U.S. Department of Agriculture, acting through Rural Development (RD).

BACKGROUND AND DISCUSSION

West Laurel Water proposes to borrow funds from KRWFC in the approximate amount of \$1,875,000 (subject to adjustment of up to 10 percent) for the purpose of refunding outstanding indebtedness, which is outlined herein. In evaluating West Laurel Water's proposal, the Commission notes that in its past five annual reports filed with the Commission, West Laurel Water reported a total water loss of near 15 percent every year.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. The Commission is placing greater emphasis on monitoring utilities that consistently exceed the 15 percent water loss threshold and strongly encourages West Laurel Water to pursue reasonable actions to prevent water loss in excess of 15 percent.

² *Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2015* at 61; *Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2016* at 56; *Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2017* at 56; *Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2018* at 57; *Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2019* at 57.

In addition, the Commission notes that West Laurel Water has not sought a general adjustment in base rates since 2002. An examination of finances outlined in the annual and audit reports filed with the Commission finds that, when accounting for both the water and sewer divisions of West Laurel Water, the utility has been operating with a negative net income for three of the past five years, which indicates that cash needs may have been supplemented by depreciation reserves, as shown below.³

Year	2015	2016	2017	2018	2019
Net Income	\$ (216,002)	\$ (114,743)	\$ (49,319)	\$ 565,820	\$ 75,222
Add: Depreciation Expense	202,313	191,703	192,169	239,752	293,204
Cash Basis Income	\$ (13,689)	\$ 76,960	\$ 142,850	\$ 805,572	\$ 368,426

Year	2015	2016	2017	2018	2019
Cash and Cash Equivalents	\$ 203,539	\$ 249,387	\$ 219,489	\$ 366,433	\$ 456,428
Restricted Cash	219,391	231,245	231,168	234,269	238,553
Sum: End-of-Year Balance	422,930	480,632	450,657	600,702	694,981
Net Increase (Decrease) in Cash	-	57,702	(29,975)	150,045	94,279

³ *Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2015 at 29; Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2016 at 24; Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2017 at 24; Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2018 at 25; Annual Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2019 at 25.*

⁴ *Audit Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2016 and 2015 at 6; Audit Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2017 and 2016 at 6; Audit Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2018 and 2017 at 7; Audit Report of West Laurel Water Association to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2019 and 2018 at 7.*

A key general recommendation that resulted from the investigation by the Commission in Case No. 2019-00041⁵ 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.⁶ The lack of insight into West Laurel Water's financial records, coupled with the fact that West Laurel Water has reported near excess water loss in every recent year indicates to the Commission that West Laurel 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 to ensure its financial situation is sufficient to combat excessive water loss.

West Laurel Water intends to use the proceeds from the proposed KRWFC Loan to refinance and discharge \$1,875,000 of outstanding indebtedness to RD. The outstanding RD balance consists of four fixed-rate debts with remaining principals of \$102,259 carrying an interest rate of 5.00 percent per annum, \$307,599 carrying an interest rate of 5.25 percent per annum, \$1,154,266 carrying an interest rate of 4.750 percent per annum, and \$334,187 carrying an interest rate of 5.00 percent per annum.⁷ The total refinancing amount is \$1,875,000 that is comprised of one loan agreement with a 21-year term funded by bonds that will be issued at interest rates that will vary between 2.75 percent and 3.25 percent per annum.⁸

⁵ Case No. 2019-00041, *Electronic Investigation into Excessive Water Loss by Kentucky's Jurisdictional Water Utilities* (Ky. PSC. Nov. 22, 2019).

⁶ See generally, *Id.*

⁷ Application, Exhibit E.

⁸ *Id.*, Exhibit B.

West Laurel Water stated that the KRWFC Loan would provide the funds necessary to refund the RD indebtedness and pay the fees and expenses incident to the issuance of the Loan.⁹ West Laurel Water provided a cash flow analysis that indicates that the refinancing would save \$357,048 over the life of the proposed Loan, resulting in a positive net present value (NPV) cash flow of \$354,533.¹⁰

The Commission has reviewed the proposed refinancing and finds West Laurel Water's proposal to be reasonable due to the lower effective interest rate and cash flow savings West Laurel Water would realize over the period of the KRWFC Loan. However, in the event that the new interest rate on the proposed refinancing is higher than the range of interest rates set forth in the application, West Laurel Water should not proceed with the refinancing unless the NPV of the refinancing results in positive cash flow.

The Commission is concerned with West Laurel Water's prolonged absence from the Commission's review of its asset management through an application for adjustment of its rates, its near excess water loss, and negative net income. Therefore, the Commission finds that West Laurel Water's proposal should file an application for adjustment of its base rates through a traditional or 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 West Laurel Water, is necessary and appropriate for and consistent with the

⁹ *Id.*, paragraph 7.

¹⁰ *Id.*, Exhibit D.

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

3. 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, West Laurel Water should provide the Commission an updated version of the application, Exhibit B, reflecting the cash flow analysis of the new KRWFC Loan within ten days of finalizing the transaction.

4. Within ten days of the execution of the new KRWFC Loan documents, West Laurel Water should file with the Commission one copy in paper medium and an electronic version of the Loan documents.

5. The proceeds from the proposed Loan should be used only for the lawful purposes set out in West Laurel Water's application.

6. The terms and conditions of the new KRWFC Loan should be consistent with the KRWFC Loan Agreement as described in West Laurel Water's application.

7. West Laurel 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 or, in the alternative, file a formal motion with a detailed analysis of its rates, and state the reasons why no rate modifications are necessary.

IT IS THEREFORE ORDERED that:

1. West Laurel Water is authorized to borrow from KRWFC an amount up to \$1,875,000, but no more than the total amount needed to pay off the RD indebtedness proposed to be refinanced in the application and 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 Loan Agreement as described in West Laurel Water's application.

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

3. West Laurel Water shall comply with all matters set out in the findings paragraphs 3 through 7 above as if they were individually ordered.

4. Any documents filed in the future pursuant to the findings paragraphs 3 and 4 above shall reference this case number and shall be retained in the post-case correspondence file.

5. West Laurel 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 to ensure that its rates are sufficient or, in the alternative, file a formal motion with a detailed analysis of its rates, and state the reasons why no rate modifications are necessary.

6. This case is closed and 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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