

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF MORGAN)	
COUNTY WATER DISTRICT FOR APPROVAL TO)	CASE NO.
ISSUE OF SECURITIES FOR THE PURPOSE OF)	2021-00476
REFINANCING CERTAIN HIGH INTEREST)	
INDEBTEDNESS)	

ORDER

On December 22, 2021, Morgan County Water District (Morgan District) filed an application seeking Commission approval to refinance two outstanding debts to the U.S. Department of Agriculture (Prior Loans) acting through Rural Development (RD) pursuant to KRS 278.300 and 807 KAR 5:001. Morgan District proposed to borrow funds from the Kentucky Rural Water Finance Corporation (KRWFC) of approximately \$2,080,000 for the refinancing via an Assistance Agreement (KRWFC Loan) with KRWFC. There are no intervenors in this case, and the matter now stands before the Commission for a decision based upon the evidentiary record.

LEGAL STANDARD

KRS 278.300 requires Commission approval 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 The legal standard contained in KRS 278.300(3) establishes the purview of Commission review, stating:

The commission shall not approve any issue or assumption
unless, after investigation of the purposes and uses of the

¹ KRS 278.300(1).

proposed issue and the 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 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.

PROPOSED REFINANCING

Morgan District proposed to borrow funds pursuant to the KRWFC Loan in the approximate amount of \$2,080,000 (subject to adjustment of up to 10 percent) for the purposes of refinancing existing outstanding indebtedness as follows²:

<u>Loan/Bond Series</u>	<u>Original Amount</u>	<u>Interest</u>	<u>Case Number Approved</u>
Morgan County Water District Waterworks Revenue Bonds, Series 2006	\$1,000,000	4.125%	2006-00204 ³
Morgan County Water District Waterworks Revenue Bonds, Series 2008	\$1,446,000	4.125%	2008-00242 ⁴

The refinancing is comprised of a single loan agreement, with an approximate 24-year term, funded by bonds that will be issued at interest rates that will vary between 2.25 percent and 3.00 percent per annum.⁵ Under current interest rates, the refinancing is estimated to yield net present value (NPV) savings to the district of approximately

² Application at 2–3, paragraph 5.

³ Case No. 2006-00204, *The Application of Morgan County Water District for a Certificate of Public Convenience and Necessity to Construct and Finance Pursuant to the Provisions of KRS 278.023* (Ky. PSC May 31, 2006).

⁴ Case No. 2008-00242, *The Application of Morgan County Water District for a Certificate of Public Convenience and Necessity to Construct, Finance and Increase Rates Pursuant to KRS 278.023* (Ky. PSC July 29, 2008).

⁵ Application, Exhibit A.

\$354,339.⁶ Morgan District stated that the final principal amount of the KRWFC Loan will be based upon interest rates at the date of sale.⁷ However, Morgan District clarified that no refinancing will occur if interest rates shift so that NPV debt service savings can no longer be achieved.⁸ Morgan District stated that the KRWFC Loan would provide the funds necessary to refinance the Prior Loans and other district bonds and to pay the fees and expenses incident to the issuance of the KRWFC Loan.⁹

DISCUSSION AND FINDINGS

Morgan District is a water utility providing service to approximately 2,902 customers in Morgan County, Kentucky.¹⁰ Regarding Morgan District, the Commission notes that Morgan District's last general rate adjustment was in Case No. 2020-00386 in which the Commission approved a 23.87 percent increase to its water service revenues.¹¹ Due to the recency of Morgan District's last rate case, the effects of the rate increase are not fully quantifiable, and the past annual reports on file with the Commission would not provide a current and accurate insight into the financial well-being of Morgan District.¹²

In Morgan District's 2020 rate case, the Commission discussed concerns over Morgan District's high level of water loss, and as part of the final Order in that case,

⁶ Application at 3, paragraph 9; see also Application, Exhibit C.

⁷ *Id.* at 3–4, paragraph 10.

⁸ *Id.*

⁹ *Id.* at 3, paragraph 7.

¹⁰ *Annual Report of Morgan District to the Public Service Commission (Annual Report) for the Year Ending December 31, 2020* at 12 and 49.

¹¹ Case No. 2020-00386, *Electronic Application of Morgan County Water District for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC June 9, 2021).

¹² The Commission notes that the refinancing is expected to provide NPV savings to Morgan District, which will in turn provide a cushion to stem future rate increase needs.

established a water loss control surcharge, currently monitored in case number 2021-00206.¹³

Morgan District's 2020 annual water loss was 35.50 percent.¹⁴ The cost of Morgan District's water loss at 35.50 percent is approximately \$269,870.¹⁵ 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 Morgan District's unaccounted-for water loss to 15 percent would result in an approximate \$155,853 decrease to its cost of water and associated purchased power.¹⁶ Morgan District's five-year water loss is as follows:¹⁷

¹³ Case No. 2021-00206, *Electronic Morgan County Water District's Unaccounted-For Water Loss Reduction Plan, Surcharge and Monitoring* (Ky. PSC June 9, 2021).

¹⁴ 2020 Annual Report at 57.

¹⁵

	Purchased Water	Purchased Power	Total
2020 Reported Expenses	\$ 719,009	\$ 41,104	\$ 760,113
Total Water Loss	35.50%	35.50%	35.50%
Excess Cost	<u>\$ 255,276</u>	<u>\$ 14,594</u>	<u>\$ 269,870</u>

¹⁶

	Purchased Water	Purchased Power	Total
2020 Reported Expenses	\$ 719,009	\$ 41,104	\$ 760,113
Multiplied by: Water Loss in Excess of 15 Percent	20.50%	20.50%	20.50%
Excess Cost	<u>\$ 147,425</u>	<u>\$ 8,428</u>	<u>\$ 155,853</u>

¹⁷ 2020 Annual Report of Morgan District at 57; 2019 Annual Report of Morgan District at 57; 2018 Annual Report of Morgan District at 57, calculation omitted from report shown below; 2017 Annual Report of Morgan District at 56; and 2016 Annual Report at 56.

Total Line Loss	115,280
Divide by: Total Produced and Purchased	<u>278,317</u>
Water Loss	<u>41.42%</u>

Year	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>	<u>2020</u>
Water Loss (%)	29.93	38.04	41.42	39.80	35.50

Morgan District provided a debt service schedule comparison that indicated the refinancing would save \$362,751 over the life of the KRWFC Loan, resulting in a positive NPV cash flow savings of \$354,339.¹⁸ 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, the Commission finds that Morgan District should not proceed with the refinancing unless the NPV of the refinancing results in positive cash flow.

The Commission further finds that Morgan District satisfied the legal standards established in KRS 278.300 to refinance the Prior Loans and district bonds, previously approved by the Commission, for the following reasons. First, the lawful object of Morgan District's purpose is to provide safe, adequate, and reliable water service to the public. The refinancing meets the lawful object of the utility's purposes because it is intended to strengthen the financial position of Morgan District through substantial NPV debt service savings. Second, the refinancing is appropriate for the proper performance by the utility and will not impair its ability to perform that service because the KRWFC Loan is exclusively for the purposes of refinancing existing debt and achieving debt service NPV savings. No other aspects of Morgan District's operations or finances will change, except those related to the refinancing of existing debt as outlined in the application and this Order. Third, the refinancing is a reasonably appropriate option for Morgan District to

¹⁸ Application, Exhibit C.

meet its statutory duty to provide safe, adequate, and reliable service because the current low interest rate environment will allow Morgan District to achieve such savings.

For the reasons set forth above, the Commission directs Morgan District to file for a general adjustment in base rates or an Alternative Rate Filing (ARF) by February 18, 2025, as to provide time to see the effects of the latest rate increase. In the alternative, Morgan District may file a formal motion with a detailed analysis of its rates and revenues and a statement of the reasons why a rate case is not necessary. The motion should also discuss the effectiveness of its water loss control plan. The Commission further directs Morgan District to review its finances on an annual basis and ensure that depreciation accounts are being fully funded. Should the need arise, Morgan District should file for a rate case or ARF before the February 18, 2025 deadline.

Lastly, the Commission finds Morgan District's application and proposal to be reasonable due to the lower effective interest rate and cash flow savings realized over the period of the KRWFC Loan, and Morgan District should be authorized to enter into the KRWFC Loan in order to refinance its existing debt obligations outlined in the application.

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

1. The KRWFC Loan is for lawful objects within the corporate purposes of Morgan District, 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. Morgan District shall secure the KRWFC Loan in the manner described in its application.

3. The final amount of the KRWFC Loan, legal expenses, and interest rates will not be known until the refinancing transaction is finalized. Therefore, Morgan District shall provide the Commission an updated version of the debt service schedule in Exhibit A, reflecting the cash flow analysis of the proposed KRWFC Loan within ten days of finalizing the transaction.

4. Within ten days of the execution of the KRWFC Loan documents, Morgan District shall file with the Commission an electronic version of the loan documents.

5. The proceeds from the KRWFC Loan shall be used only for the lawful purposes set out in Morgan District's application.

6. The terms and conditions of the KRWFC Loan shall be consistent with the loan proposal as described in Morgan District's application.

IT IS THEREFORE ORDERED that:

1. Morgan District is authorized to enter into the KRWFC Loan to borrow no more than the amount proposed in the application needed to pay off and refinance the RD indebtedness on the condition that the final NPV of the savings, determined upon closing, generate positive cash flow. The loan amount, maturity date, and interest rate shall be in accordance with the KRWFC Loan as described in Morgan District's application.

2. Morgan District shall execute the KRWFC Loan documents as authorized herein.

3. Morgan District shall comply with all matters set out in the findings paragraphs 2 through 6 above as if they were individually ordered.

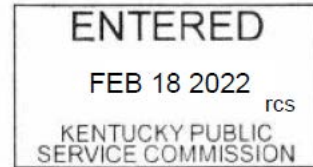
4. Any documents filed in the future pursuant to the findings paragraphs 3 and 4 above shall reference this case number and shall be retained in the post-case correspondence file.

5. Morgan District shall file an application for an adjustment in base rates for its water by February 18, 2025, to ensure that its rates are sufficient, or in the alternative, file a formal motion with a detailed analysis of its rates and revenues and a statement explaining the reasons why no 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.

By the Commission



ATTEST:


Executive Director

Case No. 2021-00476

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