

ORIGINAL

[Handwritten signatures and initials]

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

IN THE MATTER OF THE PETITION OF)
KINGSBURY UTILITY CORPORATION, A FOR-)
PROFIT WATER AND WASTEWATER INDIANA)
CORPORATION FOR AUTHORITY TO)
ESTABLISH CERTAIN NON-RECURRING)
CHARGES; SYSTEM DEVELOPMENT)
CHARGES; TO ISSUE LONG-TERM DEBT;)
APPROVAL OF NEW RULES AND)
REGULATIONS; AND FOR APPROVAL OF A)
CHANGE IN ITS RATES AND CHARGES)
THROUGH A TWO-PHASE PROCEEDING)

CAUSE NO. 44327

PHASE II ORDER

APPROVED:

APR 09 2014

ORDER OF THE COMMISSION

Presiding Officers:

Carolene Mays, Commissioner
David E. Veleta, Administrative Law Judge

On March 27, 2013, Kingsbury Utility Corporation (“Petitioner” or “Kingsbury”) filed with the Indiana Utility Regulatory Commission (“Commission”) a Verified Petition requesting authority to adjust its rates and charges, approve new rules and regulations and seek authority to issue financing. Petitioner requested that the Commission bifurcate this proceeding into two phases. Phase I to address approval of new rules and regulations, a proposed system development charge, certain non-recurring charges and a proposed excessive strength surcharge. Phase II to address Petitioner’s request to issue long-term debt and change its rates. Following an evidentiary hearing held on July 17, 2013, the Commission entered a Phase I Order on September 11, 2013.

On November 12, 2013, Petitioner filed a Verified Petition for Interim Financing Authority under this Cause requesting approval to issue debt or otherwise seek financing sufficient to support its immediate operational and repair needs. Petitioner indicated that it was seeking this relief prior to seeking rate relief. Thus, we are treating the request to issue long-term debt as Phase II. On December 6, 2013, Petitioner filed testimony and exhibits constituting its case-in-chief. On January 29, 2014, the Indiana Office of Utility Consumer Counselor (“OUCC”) prefiled the testimony of the OUCC Water/Wastewater Division. Thereafter, on February 12, 2014 Petitioner filed its rebuttal testimony. On February 21 and March 3, 2014, the Commission issued docket entries requesting Petitioner respond prior to the Evidentiary Hearing, to which Petitioner responded on February 24 and March 5, 2014, respectively.

On February 24, 2014, the Parties filed a Stipulation and Settlement Agreement (“Settlement Agreement”).

Pursuant to proper legal notice, an evidentiary hearing to address Phase II of this proceeding was held on March 6, 2014 in Room 224 of the PNC Center, 101 West Washington Street, Indianapolis, Indiana. The evidence offered by Petitioner and the OUCC was entered into evidence without objection. No members of the public appeared at the hearing or otherwise sought to testify.

Based upon the applicable law and evidence herein, and being duly advised in the premises, the Commission now finds:

1. **Notice and Jurisdiction.** Due, legal, and timely notice of these proceedings was given and published as required by law. Kingsbury is a public utility as defined in Ind. Code § 8-1-2-1. Petitioner seeks to issue long-term debt pursuant to Indiana Code § 8-1-2-77 for purposes of funding certain necessary utility plant replacements and upgrades; pay off short-term interim funding; and provide funds for Petitioner's costs associated with a specific interconnection and main relocation project. Thus, the Commission has jurisdiction over Petitioner and the subject matter of this Cause.

2. **Petitioner's Characteristics.** Kingsbury is a for-profit, combined water and wastewater utility that serves residential, commercial, and limited small industrial customers in LaPorte County, State of Indiana. Kingsbury's water and wastewater infrastructure is over 60 years old and was originally installed to serve a United States Army munitions plant covering an area of approximately 3,000 acres.

3. **Relief Requested.** In the Phase II portion of this proceeding, Petitioner seeks Commission authority to issue long-term debt for the purposes of: (a) making needed treatment plant replacements and upgrades; (b) paying off short-term interim funding expended to-date; and (c) providing funds and a reserve fund for Petitioner's portion of the necessary costs associated with interconnection and main relocation as requested by the InLand Port developer.

4. **Evidence of the Parties.**

A. **Petitioner's Case-in-Chief.** Mr. Jeff L. Johnson is the President of Kingsbury. In his testimony, Mr. Johnson presents the reasons and need for Kingsbury to initially enter into and establish long term debt arrangements with a local bank. Additionally, Mr. Johnson stated that Petitioner requested this interim financing authority in advance of its rate request to be able to promptly obtain necessary funds required to: (a) pursue and make vitally needed sewer treatment plant replacements and upgrades; (b) pay off short-term interim funding expended to-date; and (c) provide a reserve fund for Petitioner's portion of the necessary costs associated with interconnection and main relocation as requested by new customer needs in the Kingsbury Industrial Park economic development project ("KIP"). Mr. Johnson testified that the proposed financing would involve a ten year loan from the LaPorte Savings Bank in an amount up to \$375,000 at an interest rate not to exceed 7.5%. Kingsbury will be required to pledge its assets and the owner will be required to personally guarantee the loan. Mr. Johnson indicated that the financing authority requested in this phase is only for an amount needed to bridge the gap until the next phase of this case, in which Petitioner will seek comprehensive rate relief and financing authority.

Witness Jerry Jackson is Kingsbury's licensed water and wastewater operator. He presented direct and rebuttal testimony on the two main capital projects underlying the majority of the financing request. Mr. Jackson stated that he was intimately knowledgeable about the condition and status of the utility plant and facilities. He testified to the fact that the Kingsbury mechanical operating facilities, like the sewer trickle filtering system, have been in continuous motion for over 60 years and some of it has simply worn out or deteriorated and now needs to be replaced. Mr. Jackson also noted that a complete assessment and replacement of all of the Kingsbury plant is both premature and cost prohibitive. He noted that the utility will need to pursue certain additional capital improvements as the new larger KIP customers come on line, but exactly what that involves is not yet known. Mr. Jackson specifically provided details about the replacement of the worn out distributors on the two trickling filters; the details of and need for replacement of the supporting pumps; and he described the need for and cost associated with the 4th and 5th water line project and its role in serving the KIP area and a new customer requesting service. Mr. Jackson also described and provided Kingsbury's bid sheet summary (Petitioner's Exhibit FIN-JJ-5) for the construction of Kingsbury's 4th and 5th line interconnection water main replacement project. In rebuttal Mr. Jackson responded to the OUCC's proposal that only one of the two trickling filter distributors be replaced. He indicated that the Kingsbury treatment system operates together and thus requires both trickling filters to be actively in operation at all times.

B. OUCC's Case-in-Chief. Mr. Edward R. Kaufman outlined his fundamental review process for any financing case which includes the important determination as to whether the utility can afford to take on additional debt. This process included reviewing the utility capital structure to assess whether the utility will have reasonable coverage ratios. Further, Mr. Kaufman observed that if a utility incurs an excessive amount of debt, it may struggle to pay its obligations necessary to provide service. Thus, Mr. Kaufman reasoned that excessive debt may impair a utility's ability to provide safe, reliable and adequate service.

Witness Kaufman testified that Kingsbury should provide separate balance sheets for each utility (water and wastewater) and then seek specific borrowing authority for each utility. Mr. Kaufman explained that this would allow for each utility to be independently evaluated to determine the appropriateness of any borrowing, including whether each has sufficient financial integrity, and to ensure each utility can provide ongoing utility service. Mr. Kaufman also testified that capital expenditures tend to increase rate base, which projects provide a future source of funds to repay the debt. Mr. Kaufman proposed the Commission should not grant Petitioner financing authority for the debt that is to be used to fund previous operating expenses, service repairs, and regulatory costs. Mr. Kaufman also stated that, with any grant of financing authority in this cause, the authority should be subject to certain post-authority reporting requirements, including: Petitioner should identify how much debt is allocated to each utility; within 30 days of issuing its proposed debt, Petitioner shall file a report with the Commission and serve a copy on the OUCC, explaining the terms and purpose of any new loans, indicating whether any new debt was used to refinance existing debt or to fund new capital projects; and if used to refinance existing debt, Petitioner should describe what outstanding debt is being refinanced and explain and provide calculations of how the refinancing will lower Petitioner's overall cost of debt and equity capital; unless Petitioner seeks and is granted an extension, any unused financing authority approved in this case shall expire on

June 30, 2016 or the effective day of the order in Petitioner's next financing case, whichever first occurs; and Mr. Kaufman testified that the financing authority should be limited in time and any capital projects funded by such financing be subject to further prudence review by the OUCC.

Larry McIntosh presented testimony and his assessment of Petitioner's two proposed capital projects, namely the trickling filter distributor and pump replacements, and the new development expansion including the 4th and 5th water line project. Mr. McIntosh discussed Kingsbury's plan to replace both trickling filter distributors and supporting pumps. He based his recommendation on an objective evaluation of the actual use of the Petitioner's treatment facilities and reasoned that, based on current inflow and infiltration, only one of the two trickling filter distributor and corresponding pumps should be replaced at this time. Mr. McIntosh further testified that the funding for the 4th and 5th water line project be approved with certain additional suggestions, and that any remaining funds proposed to be held in reserve be subject to Petitioner notifying the Commission and the OUCC within ten days of any decision regarding projects for use of the remaining funds. Mr. McIntosh suggested the proposed ten-day notice should include a detailed justification for any project, project cost estimates, and any other pertinent information.

5. Settlement Agreement. The parties submitted for the Commission's review a Settlement Agreement on February 24, 2014. According to the parties, the Settlement Agreement fairly and reasonably resolves or addresses all issues presented in this phase of the Cause.

The Settlement Agreement provides that Petitioner should be granted interim financing authority to secure and obtain at long term debt financing in the amount of \$285,000. This includes authority to borrow \$185,000 for the fabrication and installation of two (2) fifty foot trickle filter mechanisms and purchase and installation of four supporting pumps to replace existing facilities. The Settlement Agreement further includes authority to borrow \$100,000 to pay the expenses associated with Petitioner's 4th and 5th water line relocation projects as outlined in Petitioner's testimony. The Parties further agreed that any amounts remaining from the \$100,000 are to be held in reserve ("Reserve Amounts") to support necessary replacements and additions to address and serve the new development occurring in the KIP. With respect to these Reserve Amounts, the parties also agreed that any Reserve Amounts not otherwise spent on the 4th and 5th water line project should be subject to an advance notification obligation by Petitioner to the OUCC. Petitioner agreed to certain post-authority reporting requirements as outlined in OUCC witness Mr. Kaufman's testimony.

Finally, the third identified portion of Petitioner's Interim Financing Authority request, that portion noted as \$90,000 to refinance a short-term promissory note, was withdrawn with the intention by Petitioner and consent of the OUCC to seek approval of such request in the rate case portion of this Cause. Finally, the Settlement Agreement provides that on or before August 1, 2014, Petitioner shall file its request for new rates and charges for the water and wastewater service to better reflect Petitioner's current, respective water and wastewater revenue requirements and costs.

6. Commission Discussion and Findings. Settlements presented to the Commission are not ordinary contracts between private parties. *United States Gypsum, Inc. v. Indiana Gas Co.*, 735 N.E.2d 790 (Ind. 2000). When the Commission approves a settlement, that settlement "loses its

status as a strictly private contract and takes on a public interest gloss.” *Id.* (quoting *Citizens Action Coalition v. PSI Energy*, 664 N.E.2d 401 (Ind. Ct. App. 1996)). Thus the Commission “may not accept a settlement merely because the private parties are satisfied; rather [the Commission] must consider whether the public interest will be served by accepting the settlement.” *Citizens Action Coalition*, 664 N.E.2d at 406. Furthermore, any Commission decision, ruling, or order, including the approval of a settlement, must be supported by specific findings of fact and sufficient evidence. *United States Gypsum, Inc.*, 735 N.E.2d at 795. The Commission’s own procedural rules require that settlements be supported by probative evidence. 170 IAC 1-1.1-17(D). Therefore, before the Commission can approve the Settlement, we must determine whether the evidence in this Cause sufficiently supports the conclusions that the Settlement is reasonable, just, and consistent with the purpose of Ind. Code ch. 8-1-2, and that such Settlement serves the public interest.

Pursuant to Ind. Code § 8-1-2-77, the Commission has the authority to approve or disapprove a financing proposal by a public utility to issue bonds, notes or other evidence of indebtedness, payable more than one year from the execution thereof for the purpose of, and to the extent required for, obtaining funds sufficient for the discharge or lawful refunding of its obligations. The Commission must determine whether the proposed financing program is in the public interest and reasonably necessary in the operation and management of the business of the utility in order that the utility may provide adequate service and facilities.

OUCC Witness Kaufman stated in his prefiled testimony that “[p]etitioner’s testimony does not provide coverage ratio analysis or any other review (such as a projected balance sheet) that I can rely on to confirm that it has the financial capacity to take on additional debt.” Nonetheless, the OUCC and Petitioner submitted a Settlement Agreement which if approved, permits Petitioner to incur additional amounts of debt.

On March 5, 2014, the Presiding Officers issued the following question through a Docket Entry:

On page 3 of the Docket Entry Response, Petitioner states that “[u]pon new reasonable rates being established, the utility should then be in a position to generate sufficient revenue to support its ongoing operations, including reasonable debt service payments.” Please provide the financial analysis that was prepared showing Petitioner should be able to meet the debt service payments on its existing and proposed debt after new rates have been established. If no financial analysis was prepared, on what basis was this statement made?

Petitioner’s Docket Entry Response stated the following:

Initially, Petitioner must respectively note that the inquiry goes to issues inherent to KUC’s yet-to-be filed Phase 2 rate request. As noted in elsewhere in the same KUC prior Docket Entry responses, Petitioner raised the continuing, practical limitations of time and limited resources – both monetarily and staff-wise, (that) do not

practically allow us to do everything at once – which likewise includes an advance “financial analysis” to definitively show Petitioner is able to meet the debt service payments. In lieu of that KUC’s owner stated he would act as guarantor and ensure any payments in the interim would be made. Furthermore, KUC has stated in both its testimonial filings as well as its prior responses that it intends to and will provide necessary supporting financial analysis as part of the Phase 2 rate proceeding....

Petitioner has repeatedly indicated that its owner will ensure that the necessary payments are made. However, Petitioner has not offered any evidence to support these statements. Further, the parties did not offer any additional evidence in support of the Settlement Agreement. We are unwilling to approve a utility to incur additional debt when there is no evidence of their ability to service such debt. Accordingly, we hereby deny Petitioner’s request to incur additional debt.

7. **Rate Relief.** Petitioner has indicated its intent to file a formal request supporting new base rates and charges for both the water and wastewater utility as well as seek whatever additional financing authority is deemed necessary. We would strongly encourage Petitioner to take advantage of the Commission’s small utility filing procedures for addressing its needs regarding rate change and financing approval. The procedures set out in 170 IAC 14-1 for small utilities are intended to be a less costly regulatory alternative to a typical rate case. Further, issues can be dealt with in a more direct manner as filings under 170 IAC 14-1 are exempt from the ex parte rules of the Commission.

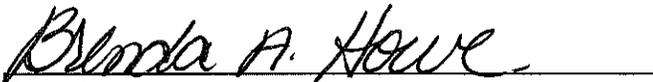
IT IS THEREFORE ORDERED BY THE INDIANA UTILITY REGULATORY COMMISSION that:

1. The Phase II Settlement Agreement is hereby denied.
2. This Order shall be effective on and after the date of its approval.

ATTERHOLT, MAYS, STEPHAN, WEBER, AND ZIEGNER CONCUR:

APPROVED: APR 09 2014

I hereby certify that the above is a true and correct copy of the Order as approved.



Brenda A. Howe
Secretary to the Commission