

**STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DIVISION OF PUBLIC UTILITIES AND CARRIERS
89 JEFFERSON BOULEVARD
WARWICK, RHODE ISLAND 02903**

IN RE: Kent County Water Authority Application :
 for Authority to Refinance Previously : Docket No. D-01-2
 Approved Long-Term Debt :

REPORT AND ORDER

On March 22, 2001, the Kent County Water Authority (“KCWA”) filed an application with the Rhode Island Division of Public Utilities and Carriers (“Division”) seeking authority to refinance long-term debt previously approved by the Division. The application was filed in accordance with Section 39-3-15 of the Rhode Island General Laws, and Rule 14 of the Division’s Rules of Practice and Procedure.

According to prefiled direct testimony submitted with the application, the KCWA currently has \$13,270,000 of outstanding debt from its series 1994 revenue bonds, which were originally issued in the amount of \$16,500,000. These outstanding bonds bear coupons ranging from 5.4 percent in 2001 to 6.35 percent in 2014. This same prefiled testimony indicates that current interest rates for a 20-year bond issue would average approximately 5 percent.

According to the application, the KCWA’s refinancing request would be joined with \$10,000,000 in unissued long-term debt approved by the Division last year in Docket No. D-00-20 (KCWA Exh. 1). In that docket, the Division authorized the KCWA to issue bonds in the amount of \$10,000,000, and at an approximate interest rate of 5.87 percent. The KCWA explains that it plans to issue these bonds shortly and would like to refinance its 1994 bond debt at the same time.

In response to the application filing, the Division conducted a duly noticed public hearing on April 6, 2001. The hearing was conducted at the Division's hearing room, located at 89 Jefferson Boulevard in Warwick.

The following counsel entered appearances at the hearing:

For the KCWA:	Francis X. Flaherty, Esq.
For the Division's Advocacy Section:	Leo Wold, Esq. Special Assistant Attorney General

The KCWA proffered one witness in support of its application. The witness was identified as Mr. John P. Ryan, Vice President, Quick & Reilly (a subsidiary of Fleet Boston Financial Group). Mr. Ryan sponsored and authenticated pre-filed direct testimony, supra, and was made available for questioning from the Advocacy Section and the undersigned hearing officer.

Mr. Ryan testified that he has advised the KCWA to refinance its series 1994 bonds at the same time that it issues the \$10,000,000 in new debt. Mr. Ryan offered the following reason for his recommendation:

The Federal Reserve Board has recently been aggressively addressing concerns of a slower economy with adjustments to the discount rate. These adjustments manifest themselves in the form of interest rate reductions. Over the course of the last month, tax exempt interest rates have gone down an average of .5 percent. As a result of this decline as well as previous declines in the interest rates, it is now financially advantageous for the Authority to advance refund its series 1994 bonds (KCWA Exh. 2).

Mr. Ryan related that current interest rates for a 20-year bond issue would average approximately 5 percent. He contrasted this rate to the higher rates associated with the KCWA's series 1994 bonds. Based on this disparity, Mr. Ryan opined that there would be a "net present value savings of over \$400,000 or in excess of 3 percent of the par of the bonds being refunded" (Id., p. 3). He also noted that the savings calculations are after all expenses have been paid relative to the issuance of the bonds, including all fees (Id.).

Mr. Ryan testified that if interest rates remain comparable to those available today, he estimates that the KCWA would need to borrow approximately \$14,100,000 in order to fully refinance its series 1994 bonds (Id.). He stated that even though this amount exceeds the current outstanding debt of \$13,270,000, the KCWA will save money over the long term.

Mr. Ryan explained that the calculation of savings on a refunding transaction is based on a comparison of debt service (total principal and interest) of the bonds to be issued versus those bonds currently outstanding. He related that in order to refund the bonds, the KCWA will be required to issue bonds in an amount sufficient to fund an escrow which, when invested in U.S. Treasury Securities, will be sufficient to make all future debt service payments and any premium paid for the early redemption of the old bonds. He further explained that this escrow will be restricted as to yield and held by a trustee who will be responsible for the payments made to bond holders until the bonds are called (Id., p. 4). Mr. Ryan next explained that when the new bonds are issued, a mathematical calculation will be performed to assure that the proposed 3 percent savings is attained. He related that the calculation will compare the total principal and interest costs of the new bonds versus those being refunded. Mr. Ryan testified that the savings figure will then be discounted at the bond yield of the new issue to properly reflect the time value of money on the savings. Mr. Ryan predicted that engaging in this transaction should exceed the 3 percent target (Id.)

In his closing comments, Mr. Ryan urged the Division to act quickly with respect to the application filing. He reasoned that the tax exempt market is currently favorable. He also observed that if the transaction can be executed in conjunction with the KCWA's pending \$10,000,000 new issuance, the KCWA can take advantage of economics of scale and save on issuance costs (Id.)

The Division's Advocacy Section also proffered one witness. The witness was identified as John Bell, a Public Utilities Analyst. Mr. Bell sponsored pre-filed direct testimony (Advocacy Section Exh. 1).

In his testimony, Mr. Bell presented a summary of the KCWA proposal and a recommendation to the hearing officer. Mr. Bell recommended that the:

KCWA's application to refinance the remaining balance of the \$16,500,000 1994 series bonds on the condition that the refinancing results in the realization of an approximate present value benefit of at least 3% of the refunded principal (Id., p. 2).

FINDINGS

First, regarding the \$10,000,000 bond issue approved by the Division last year, the Division finds no need to modify its previous decision. The KCWA was authorized through Order No. 16464 in Docket No. D-00-20 (issued on November 22, 2000) to "*issue revenue bonds in the amount of \$10,000,000, at an approximate interest rate of 5.87 percent.*" Clearly, the KCWA does not need supplemental authority to issue its bonds at a significantly lower interest rate than initially projected.

Consequently, the Division's focus in this docket must be limited to a determination of whether it is in the interest of ratepayers to authorize the KCWA to refinance its series 1994 revenue bonds. Upon a thorough examination of the record in this docket, it appears that notwithstanding the additional issuance costs, the favorability of the current bond market sufficiently offsets the costs of refinancing the KCWA's 1994 bonds. Relying on the savings projections calculated by Mr. Ryan, the Division finds the instant refinancing request reasonable and in the best interest of ratepayers.

The Division also finds that the KCWA's current level of authorized revenues, restricted for debt service, will exceed its needs after the proposed refinancing proposal is effectuated. The KCWA was authorized by the Public Utilities Commission ("Commission")

to collect additional annual revenues in an amount not to exceed \$842,000 for the debt service on the \$10,000,000 bond issue approved by the Division last year. This amount was derived from an interest rate projection of approximately 5.87%. With the current tax exempt bond market standing at approximately 5.0 percent, the Division finds that the KCWA will be over collecting debt service-related revenues from ratepayers.

Similarly, the debt service-related revenues being collected by the KCWA to pay for its series 1994 bonds will also exceed financing needs after the completion of the proposed refinancing transaction. In this proceeding, Mr. Ryan testified that ratepayers will save over \$400,000 if the KCWA is permitted to refinance its series 1994 bonds. This savings translates into a commensurate surplus in the KCWA's debt service account.

Despite the projected surpluses, the Division has decided that it will take no action relative to the aforementioned debt service savings in the context of this docket. The Division notes that the KCWA's debt service account is currently restricted for debt service expenses only. Accordingly, the surpluses will accrue to the restricted debt service account until adjusted by order of the Commission.

Coincidentally, the KCWA filed a rate increase application with the Commission on March 30, 2001. The Division will alternatively address the KCWA's debt service surplus issue in the context of its rate case before the Commission.

Now, therefore, it is

(16573) ORDERED:

1. That the March 22, 2001 application filing by the Kent County Water Authority, which seeks authority to refinance its series 1994 revenue bonds in the amount of approximately \$14,100,000 is hereby approved.
2. That the Kent County Water Authority's request to effectuate the proposed refinancing by consolidating the borrowing with the issuance of a second

\$10,000,000 bond issue, previously approved by the Division (through Order No. 16424), is hereby approved.

3. That the combined bond issue shall approximate a total amount of \$24,100,000, at an approximate interest rate of 5.0 percent.

Dated and Effective on April 10, 2001, at Warwick, Rhode Island.

John Spirito, Jr., Esq.
Hearing Officer

Thomas F. Ahern
Administrator