

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

In the Matter of the Application of)
KAUAI ISLAND UTILITY COOPERATIVE)
For Approval of \$1,300,000)
Irrevocable Letter of Credit From)
National Rural Utilities)
Finance Corporation.)

DOCKET NO. 2008-0068

DECISION AND ORDER

RECEIVED
2008 AUG 27 A 8:28
DIV. OF CONSUMER ADVOCACY
DEPT. OF COMMERCE AND
CONSUMER AFFAIRS
STATE OF HAWAII

PUBLIC UTILITIES
COMMISSION

2008 AUG 26 A 10:40

FILED

All electric utility customers on the island of Kauai are members/owners of KIUC, except those customers that have elected against becoming a member/owner.

A.

Procedural Background

On April 17, 2008, as supplemented on April 28, 2008, KIUC filed an application seeking the commission's approval to enter into an irrevocable letter of credit with its lender, CFC, in the amount of \$1.3 million in favor of KIUC's petroleum fuel supplier, Chevron Products Company ("Chevron"), a division of Chevron U.S.A., Chevron Finance Company, or both.² By letter dated August 6, 2008, KIUC amended its application by submitting its Revised Exhibit 1, i.e., the irrevocable letter of credit, revised version.³

²The Consumer Advocate notes:

At this time, it is unclear which of these affiliated companies will be the possible beneficiary of the line of credit to be entered into by KIUC. Notwithstanding this uncertainty, the determination of which entity might be directly impacted by KIUC's ability to draw upon the line of credit does not appear to be critical to the decision that the Commission must make regarding KIUC's request to enter into the proposed line of credit.

Consumer Advocate's Statement of Position; and Certificate of Service, filed on August 7, 2008 (collectively, "Statement of Position"), at 2 n.3.

³See Application; Exhibit 1; Verification; and Certificate of Service, filed on April 17, 2008, as supplemented with Exhibit 2, filed on April 28, 2008, and as amended with the Revised Exhibit 1, filed on August 6, 2008. (collectively, "Application").

KIUC makes its request pursuant to HRS § 269-17 and to the extent applicable, HRS § 269-7(a).⁴

On August 7, 2008, the Consumer Advocate filed its Statement of Position. No reply was filed by KIUC.

B.

Letter of Credit

As part of its fuel supply arrangements with KIUC, Chevron is requiring that "a letter of credit be in place to provide Chevron additional security with respect to KIUC's payment obligations. Specifically, the letter of credit will provide Chevron with the right to apply the whole or any part of the letter of credit amount to the outstanding balance of any payments due by KIUC to Chevron."⁵

The material terms of the letter of credit include:

1. The letter of credit will be issued by one of KIUC's existing lenders (i.e., CFC), in an aggregate principal amount not to exceed \$1.3 million, for a one-year term, with two one-year options to extend that can be exercised by KIUC upon written request to CFC at least sixty days prior to the expiration of the then applicable term.

2. Three-hundred sixty-four days from the date of each draw under the letter of credit, KIUC promises to pay to CFC the principal sum of the aggregate unpaid principal amount of

⁴KIUC notes that: (1) the letter of credit will be unsecured and will not encumber the whole or any part of the utility's property; thus (2) HRS § 269-19 does not apply. See Application, at 1 n.2 and 6 n.9.

⁵Application, at 5.

such draw, and to pay interest on all remaining unpaid amounts from the date of such draw.

3. Interest on any draws will be equal to the total rate per annum as may be fixed by CFC from time to time, not to exceed the Prime Rate plus one percent per annum. Interest will be computed on the basis of a 365-day year for the actual number of days that any draw is outstanding.

4. Any draw downs on the line of credit will not be secured by any of KIUC's assets.

5. As consideration for the issuance of the proposed letter of credit, KIUC will be required to pay CFC an initial letter of credit fee equal to \$6,500 (i.e., the greater of fifty basis points (50/100 of 1%) of the face amount of the letter of credit, or \$400). In the event the letter of credit is outstanding for more than a year, then such fee shall be due and payable annually.

C.

KIUC's Position

In support of its request, KIUC states:

. . . the proposed letter of credit is for purposes permitted by HRS § 269-17. Although not previously required by Chevron, this letter of credit is now being required by Chevron as part of its fuel supply arrangements with KIUC to ensure KIUC's ability to satisfy its payment obligations under these arrangements. This letter of credit will not have any material negative impact on the costs of the existing and future operations or on the efficiency of KIUC's operations. The proposed letter of credit will be transparent to customers and KIUC's customers will continue to benefit from the ability of KIUC to assure the continued supply of fuel for KIUC's operations, which is essential

to the continued provision of quality utility services. Finally, the proposed letter of credit will not impair [KIUC's] financial status, will not impair its ability to attract capital, nor will it impair [KIUC's] ability to provide safe, reliable and adequate service.

Application, at 7 (emphasis added).

D.

Consumer Advocate's Position

In its Statement of Position, the Consumer Advocate states that "Commission approval to enter into the line of credit with CFC is not required since the term of the line of credit will be for 12 months⁶ and CFC will require KIUC to repay any amounts drawn on the line of credit within 364 days of the draw down."⁷ In support of its position, the Consumer Advocate states:

. . . . KIUC confirmed that the intent of the letter of credit was that all draw downs would be fully paid off within a one (1) year period (i.e., twelve months) from the date of the draw down. To clarify this intent, CFC modified the line of credit to require KIUC to repay any amounts drawn on the line of credit within 364 days of each particular draw-down. Thus, the debt, if any, which would be outstanding under the line of credit would not be in existence for more than 12 months. In addition to the above,

⁶Footnote 8 of the Consumer Advocate's Statement of Position states:

Although the modified terms provide for two (2) 1-year options to extend the line of credit, exercisable by KIUC, there presently is no guarantee that KIUC will exercise either of the two options. More importantly, each option merely extend[s] the term of the line of credit for an additional twelve months.

Consumer Advocate's Statement of Position, at 7 n.8.

⁷Consumer Advocate's Statement of Position, at 7.

CFC also modified the term of the line of credit. Instead of, . . . providing for an outright 3-year term, the line of credit will be available for an initial period of one (1) year, with two (2) one (1) year options to extend, exercisable by KIUC. This modification further clarifies that the actual term of the line of credit will not be for a period that extends beyond 12 months. See KIUC's letter filed on August 6, 2008.

Thus, although the line of credit may be available for up to three years, the term of the line of credit will be for one year (i.e., twelve months). Furthermore, debt will not be incurred under the line of credit unless KIUC fails to make a payment when due on a fuel bill from Chevron, and Chevron then applies the line of credit balance against the outstanding balance owed by KIUC under the fuel contract with Chevron. Finally, the draw down amounts must be repaid within 364 days (i.e., less than 12 months). Based on the above, the Consumer Advocate contends that Commission approval under HRS § 269-17 to enter into the line of credit with CFC under the modified terms set forth in KIUC's August 6, 2008 letter to the Commission is no longer required.⁸

Consumer Advocate's Statement of Position, at 5-6.

The Consumer Advocate further notes that: (1) KIUC does not intend nor anticipates a need to draw on the line of credit; and (2) the proceeds from the line of credit will not be used for the purposes set forth in HRS § 269-17. The Consumer Advocate concludes by noting that while KIUC also sought the commission's approval under HRS § 269-7, this provision "merely allows the Commission to examine and investigate matters

⁸Footnote 7 of the Consumer Advocate's Statement of Position provides:

As noted above, Commission approval to enter into any debt instrument is required when the debt is payable at periods of more than twelve months (i.e., 365 days) after the date thereof.

Consumer Advocate's Statement of Position, at 6 n.7.

that affect the operations of a public utility's operations and does not explicitly provide for approval of such transactions, unlike the provisions of HRS § 269-17."⁹

II.

Discussion

A.

Non-Submittal of Certain Information

With respect to its Application, KIUC requests that "it not be required to submit a source and application of funds statement, statement of capital structure, and statement showing interest coverage for the latest year and for each successive five years, under HAR § 6-61-101(b)(5) to (7)."¹⁰

In support thereto, KIUC states:

. . . . (1) the purpose of the proposed letter of credit is to provide Chevron with security, or a backstop, in the event KIUC does not meet its payment obligation; (2) KIUC plans to fully meet its payment obligations to Chevron and as such there is no expectation that any funds will be drawn under the proposed letter of credit during its 3-year term; (3) as such, with the exception of the initial letter of credit fee mentioned above, there is no expectation that any interest or other expenses will be incurred as a result of this letter of credit; and (4) it is thus not expected that the issuance of this letter of credit will have any impact on KIUC's source and application of funds, capital structure or interest coverage results or ability. Therefore, KIUC contends that the preparation of these statements is not relevant for purposes of

⁹Consumer Advocate's Statement of Position, at 6.

¹⁰Application, at 6 n.10.

analyzing whether or not to approve this Application. Furthermore, it would be unduly burdensome and overly time consuming for KIUC to prepare these statements under the circumstances.

Application, at 6 n.11.

HAR § 6-61-1 provides that the commission shall liberally construe HAR chapter 6-61 "to secure the just, speedy, and inexpensive determination of every proceeding." Based on KIUC's representations, the commission, on its own motion, determines that KIUC should not be required to submit the information set forth in HAR § 6-61-101(b)(5) to (7).

B.

Letter of Credit

HRS § 269-17 provides that, upon the commission's prior approval, a public utility corporation may issue stocks and stock certificates, bonds, notes, and other evidences of indebtedness, payable at periods of more than twelve (12) months after the date thereof, for the following purposes, and no other:

for the acquisition of property or for the construction, completion, extension, or improvement of or addition to its facilities or service, or for the discharge or lawful refunding of its obligations or for the reimbursement of moneys actually expended from income or from any other moneys in its treasury not secured by or obtained from the issue of its stocks or stock certificates, or bonds, notes, or other evidences of indebtedness, for any of the aforesaid purposes except maintenance of service, replacements, and substitutions not constituting capital expenditure in cases where the corporation has kept its accounts for such expenditures in such manner as

to enable the commission to ascertain the amount of moneys so expended and the purposes for which the expenditures were made, and the sources of the funds in its treasury applied to the expenditures.

HRS § 269-17.

Conversely, "[a] public utility corporation may not issue securities to acquire property or to construct, complete, extend or improve or add to its facilities or service if the commission determines that the proposed purpose will have a material adverse effect on its public utility operations."

HRS § 269-17. "All stock and every stock certificate, and every bond, note, or other evidence of indebtedness of a public utility corporation not payable within twelve months, issued without an order of the commission authorizing the same, then in effect, shall be void." Id.

Thus, the permitted purposes contemplated under HRS § 269-17, are limited to:

1. The acquisition of property;
2. The construction, completion, extension, or improvement of or addition to its facilities or service;
3. The discharge or lawful refunding of its obligations; or
4. The reimbursement of moneys actually expended for any of the above purposes.¹¹

¹¹See In re Citizens Comm. Co., dba The Gas Co., Docket No. 03-0051, Decision and Order No. 20354, filed on July 25, 2003, at 42-43.

"Purposes 1 and 2 of [HRS § 269-17] contemplate situations where funds for capital acquisition or construction are to be expended after or nearly contemporaneously with the issuance of securities. On the other hand, purposes 3 and 4 relate to the past expenditure of funds, e.g., purpose 3 contemplates the discharge or refinancing of debt incurred in the past for the acquisition or construction of capital facilities."¹²

In addition, HRS § 269-7(a) authorizes the commission to examine the condition of each public utility, its financial transactions, and "all matters of every nature affecting the relations and transactions between it and the public or persons or corporations."

The purpose of the letter of credit is to provide Chevron, KIUC's petroleum fuel supplier, "additional security with respect to KIUC's payment obligations. Specifically, the letter of credit will provide Chevron with the right to apply the whole or any part of the letter of credit amount to the outstanding balance of any payments due by KIUC to Chevron."¹³ The commission finds that the proceeds from the letter of credit will not be used for any of the purposes contemplated under HRS § 269-17.¹⁴ Accordingly, HRS § 269-17 does not apply.

¹²Docket No. 03-0051, Decision and Order No. 20354, at 43.

¹³Application, at 5.

¹⁴See In re KRWC Corp., dba Kohala Ranch Water Co., Docket No. 2007-0376, Decision and Order, filed on June 18, 2008 (Consumer Advocate's position that HRS § 269-17 authorizes public utilities to enter into long-term debt for the purpose of financing the acquisition of utility plant assets).

Furthermore, KIUC represents that the letter of credit will be unsecured and will not encumber the whole or any part of the utility's property. Thus, the commission, on its own motion, likewise finds that HRS § 269-19 does not apply.

Given KIUC's representations that the letter of credit will be unsecured and will not encumber the whole or any part of the utility's property; will have no material negative impact on KIUC's utility operations; and will not impair KIUC's financial status, its ability to attract capital, or its ability to provide safe, reliable, and adequate service, the commission approves KIUC's request to enter into the irrevocable letter of credit with CFC, to the extent that such approval is required under HRS § 269-7(a). In reaching this decision, the commission notes that KIUC has chosen not to withdraw its Application. Instead, it seeks affirmative commission action.

III.

Orders

THE COMMISSION ORDERS:

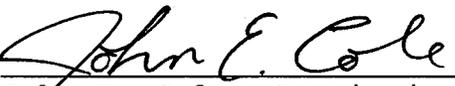
1. KIUC is not required to submit the information set forth in HAR § 6-61-101(b)(5) to (7).
2. KIUC's request to enter into an irrevocable letter of credit with the National Rural Utilities Cooperative Finance Corporation, as described in its Application, is approved, to the extent that such approval is required under HRS § 269-7(a).

3. This docket is closed unless ordered otherwise by the commission.

DONE at Honolulu, Hawaii AUG 26 2008.

PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

By 
Carlito P. Caliboso, Chairman

By 
John E. Cole, Commissioner

By 
Leslie H. Kondo, Commissioner

APPROVED AS TO FORM:


Michael Azama
Commission Counsel

2008-0068.laa

CERTIFICATE OF SERVICE

The foregoing order was served on the date of filing by mail, postage prepaid, and properly addressed to the following parties:

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