

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

In the Matter of the Application of)
)
KRWC CORPORATION, dba)
KOHALA RANCH WATER COMPANY)
)
For Approval of Financing and)
Security Arrangements.)
_____)

Docket No. 2007-0376

DECISION AND ORDER

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DEPARTMENT OF LAND & NATURAL RESOURCES
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PUBLIC UTILITIES
COMMISSION

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DECISION AND ORDER

By this Decision and Order, the commission approves the request of KRWC CORPORATION, dba KOHALA RANCH WATER COMPANY ("KRWC" or the "Company"), to enter into certain financing and security arrangements, in accordance with Hawaii Revised Statutes ("HRS") §§ 269-17, 269-19, and 269-7(a), and subject to the conditions described herein.

I.

Background

KRWC is a Hawaii corporation and public utility authorized to provide potable water service in Kohala, island of Hawaii. KRWC presently provides potable water service to approximately 350 customers within its service area, which generally encompasses the Kohala Estates, Kohala Ranch, Kohala Waterfront, and the Kohala by the Sea developments. KRWC's sole shareholder is Robert Acree, who acquired KRWC pursuant to a series of transactions approved by the commission.

A.

KRWC's Application

On November 7, 2007, KRWC filed an Application seeking the commission's approval to enter into two separate long-term financing and related security arrangements in accordance with HRS §§ 269-17, 269-19, and 269-7(a).¹

B.

Financing and Related Security Arrangements

1.

The First Loan

Under the first financing and security arrangement, Mr. Acree intends to issue a \$5.5 million loan with an eleven-year term, plus a \$1 million revolver, to KRWC (the "First Loan"). As noted by KRWC:

. . . . Mr. Acree is currently in the process of obtaining a personal loan of up to \$5.5 million from Bank of Hawaii to fund a majority of the proposed First Loan. Mr. Acree will be imposing on KRWC substantially the same loan covenants and restrictions that will be placed on Mr. Acree with respect to his personal loan with Bank of Hawaii. As security for Mr. Acree's personal loan with Bank of Hawaii, he will be providing as collateral other personal and real property, not including KRWC's assets. Thus, no approval is needed under HRS §§ 269-17 and/or 269-19 for Mr. Acree's personal loan from Bank of Hawaii. Nevertheless, once Mr. Acree obtains approval for this personal loan, Applicant will submit a copy of the

¹Application; Exhibits 1 - 8; Verification; and Certificate of Service, filed on November 7, 2007 (collectively, "Application"). KRWC served copies of its Application upon the DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS, DIVISION OF CONSUMER ADVOCACY ("Consumer Advocate"), an ex officio party to this proceeding, pursuant to Hawaii Revised Statutes § 269-51 and Hawaii Administrative Rules ("HAR") § 6-61-62(a).

commitment letter or applicable financial document received from Bank of Hawaii for review within this docket.

KRWC's Application, at 5 n.7.

The terms of re-payment during the eleven-year term of the First Loan are as follows: (1) for the first year, monthly interest only payments at the prime rate listed by Bank of Hawaii, plus 100 basis points; (2) for years two through six, principal and interest payments will be required at a fixed interest rate not to exceed the five-year Federal Home Loan Bank of Seattle ("FHLB") Index,² plus 250 basis points, with fixed monthly payments based on a ten-year amortization period;³ and (3) for years seven through eleven, principal and interest payments will be re-set at the then current five-year FHLB Index plus 250 basis points, with fixed monthly payments amortized over the remaining five years of the term.

Interest on the \$1 million revolver will accrue at the prime rate listed by Bank of Hawaii, plus 100 basis points.

The First Loan will be secured by all of KRWC's assets.

KRWC will utilize the proceeds from the \$5.5 million to finance: (1) Well No. 3 and Reservoir No. 4a, \$4,279,487; (2) capital expenditure charges from 2000 to 2006, \$524,231;

²KRWC's Application states four years, while the Consumer Advocate, in its Statement of Position, states five years, pursuant to its informal confirmation with KRWC. Consumer Advocate's Statement of Position; and Certificate of Service, filed on May 9, 2008 ("Statement of Position").

³According to KRWC, "[a]t the time of this Application, the FHLB Index plus 250 basis points would result in an indicative interest rate of 7.33%." KRWC's Application, at 5 n.8.

(3) earthquake and flood costs for 2006 and 2007, \$245,759; (4) costs associated with Well No. 1, \$117,402; and (5) back-up replacement costs for Well No. 1 or Well No. 2, or both, \$267,336.⁴ "The \$1 million revolver will provide funds to be used by KRWC toward future foreseen and unforeseen capital expenditures, as well as to potentially cover debt service in the early years of the loan."⁵

2.

The Second Loan

Under the second financing and security arrangement, KR Properties LLC ("KR Properties"), an affiliate of KRWC, will loan \$1.2 million to KRWC (the "Second Loan"), "to finance the acquisition of the Well No. 3 site and the improvements thereon presently owned by KR Properties."⁶

⁴See KRWC's Application, Section III.B.1.a - 1.e, at 7-10 (detailed descriptions of each item); see also KRWC's response to CA-IR-1 (drilling costs for Well No. 3).

With respect to the breakdown of the \$5.5 million, KRWC notes:

. . . the described uses of funds set forth in this Application for the \$5.5 million loan total \$5,434,215, which is slightly less than the \$5.5 million loan amount. The \$65,785 difference is provided to account for loan costs and costs to process this Application, as well as a contingency for possible additional increases in costs, as many of the bids received are only open for a fixed time and may expire before processing of this Application is completed.

KRWC's Application, at 6 n.9.

⁵KRWC's Application, at 6.

⁶KRWC's Application, at 10.

"The \$1.2 million loan will be made pursuant to a 10-year term loan with a balloon payment due at the end of the 10-year term. Interest, equivalent to the interest rate charged by Mr. Acree at that time with respect to the First Loan above, will accrue during years one (1) to five (5) with no payments due to KR Properties. Monthly interest only payments, based on an interest rate equivalent to the interest rate charged by Mr. Acree at that time with respect to the First Loan above, will be required during years six (6) to ten (10) based on the balance at that time (i.e., original loan plus accrued interest). All assets of KRWC will be pledged as collateral for the \$1.2 million loan."⁷

C.

KRWC's Position

In support of its position, KRWC states:

1. With respect to the First Loan, "KRWC believes that it would not be able to secure a loan from external sources at [the] same or better terms than the arrangement offered to KRWC by Mr. Acree, and KRWC would not be able to secure any loan of this size without pledging at least its assets as security for the loan."⁸

2. KRWC needs to fund the items designated under the First Loan in order to provide safe and reliable service to its existing and future customers. Specifically:

⁷KRWC's Application, at 10-11.

⁸KRWC's Application, at 6.

A. KRWC presently obtains its water supply from Well No. 1 and Well No. 2. The combined sustainable yield of both of these wells is one million gallons per day ("gpd"). KRWC's peak day pumping currently exceeds that amount, requiring the operation of both wells to ensure a sufficient water source to meet these peak periods. Moreover, if either of the existing wells, at the present time, became non-operational due to maintenance, repair, or other reasons, KRWC would be unable to meet its average daily capacity requirements.

For these reasons, the addition of Well No. 3 is necessary to provide sufficient capacity for the existing lots in KRWC's service area, and to meet future capacity requirements of these existing lots. Furthermore, Well No. 3 will provide additional reliability benefits as a source of back-up capacity during peak usage periods.

B. KRWC's water system includes nine reservoirs. Presently, water is pumped from the existing wells into Reservoir No. 3. From Reservoir No. 3, three other reservoirs are gravity fed (Reservoirs Nos. 0, 1, and 2), while approximately 167,000 gpd of water must be "boosted" to the other four remaining reservoirs (Reservoirs No. 4 to No. 8).

"The addition of storage capacity by adding Reservoir No. 4a at the proposed Well No. 3 site location will eliminate the need to boost water from Reservoir No. 3, thus providing certain cost efficiencies. In addition, this additional storage capacity means that the full amount of water for the existing KRWC customers served via Reservoir Nos. 4 to 8 can be pumped and

stored during off-peak periods, and then distributed as demand warrants. This will provide reliability benefits by allowing service to continue during periods when the pump is unavailable, such as during repairs or electric outages."⁹

C. The capital expenditure costs incurred during 2000 to 2006 include "the installation of a turbine bowl assembly pump in 2000, various motor installations in 2001 and 2002, landscaping of wells and reservoirs in 2004, and the replacement of the Well No. 1 pump in 2006."¹⁰

D. The various costs incurred in 2006 and 2007 results from "the damage caused to KRWC's water system by the October 15, 2006 earthquake and the October 10, 2006 flood that struck the island of Hawaii. These costs include structural assessments, damage related work to Reservoir Nos. 4, 7 and 8, and piping and welding costs in order to install and operate a temporary tank required to continue service while this work occurred."¹¹

E. Costs incurred during 2007 for the repair and maintenance of Well No. 1.¹²

F. "[A]cquiring a back-up pump/motor, column pipe, transformer and other equipment for use at Well Nos. 1 and/or 2 .

⁹KRWC's Application, at 8-9.

¹⁰KRWC's Application, at 9; see also KRWC's Application, Exhibit 2 (breakdown of the capital expenditure costs incurred during 2000 to 2006).

¹¹KRWC's Application, at 9; see also KRWC's Application, Exhibit 3 (breakdown of the earthquake and flood-related costs incurred in 2006 and 2007).

¹²See KRWC's Application, Exhibit 4 (breakdown of the costs incurred during 2007 for Well No. 1).

. . . Having this equipment readily available will ensure rapid repair or at least minimize any potential service disruptions that may result from the failure of Well Nos. 1 and/or 2."¹³

3. With respect to the Second Loan, during the early 1990s, KR Properties or its predecessor-in-interest expended approximately \$1,223,180 to drill a well, presently referred to as Well No. 3, on land that is currently owned by KRWC. The purpose of drilling the well was to establish a water source to ensure a sufficient supply of water for future use and development.

KR Properties agrees to transfer its well rights and improvements to KRWC, at a purchase price of \$1,223,180, a below market value amount that is intended to reimburse KR Properties for the original drilling costs it incurred.¹⁴ Conversely, if the Second Loan is not allowed to proceed, "Applicant will be forced to develop a new well at a different site location, which will be significantly more expensive to Applicant and its customers."¹⁵

¹³KRWC's Application, at 10; see also Exhibit 5 (breakdown of the estimated replacement costs).

¹⁴According to KRWC:

KR Properties currently values Well No. 3 at a minimum of \$1.8 million, which consists of approximately \$1.4 million for well drilling, \$200,000 for land acquisition, and \$200,000 for related site work at today's estimated costs and valuations.

KRWC's Application, at 11 n.10.

¹⁵KRWC's Application, at 11. KRWC estimates that it will cost at least \$500,000 more to construct a new well at a new site location.

4. The financing and security arrangements are for the purposes permitted by HRS § 269-17, and:

. . . will serve the public interest by enabling KRWC to provide sufficient capacity for its existing customers and to meet future capacity and usage requirements of its existing customer base, provide various reliability benefits and operational efficiencies, as well as finance various capital expenditures and other costs, including costs incurred in connection with the 2006 earthquake and flood. These proposed financing and security arrangements will also be transparent to customers and KRWC's customers will continue to benefit from the ability of KRWC to assure the continued provision of quality water services. Finally, these proposed financing and security arrangements will not impair Applicant's financial status, will not impair its ability to attract capital, nor will it impair Applicant's ability to provide safe, reliable and adequate service.

KRWC's Application, at 13.

5. The financing and security arrangements will not have a materially adverse affect on KRWC's public utility operations.

D.

Consumer Advocate's Position

On May 9, 2008, the Consumer Advocate filed its Statement of Position, recommending that the commission approve, subject to certain reporting requirements: (1) KRWC's request to enter into the two financing arrangements; and (2) KRWC's pledge of assets as security for the debt instruments, pursuant to HRS §§ 269-17 and 269-19.

The First Loan

With respect to the First Loan, the Consumer Advocate, states:

1. KRWC proposes to utilize \$4,279,487 of the proceeds from the First Loan to finance the construction of Well No. 3 and Reservoir No. 4a. The Consumer Advocate's independent analysis confirms that the addition of Well No. 3 is needed for KRWC's utility operations, and that the construction of Reservoir No. 4a appears reasonable.¹⁶ Specifically, "[t]he Consumer Advocate concurs that a third well and the additional reservoir to be constructed at the well site will provide sufficient capacity for KRWC to: (a) meet the average daily water demand of KRWC's customers in the event that a pump for one of the existing two wells is out of service for more than one day; and (b) allow KRWC to be in compliance with the off-peak pumping requirements for [Hawaii Electric Light Company, Inc.'s] Rider M tariff. As a result, the Consumer Advocate has concluded that the estimated funds of \$4.3 million (approximate) from the First Loan and the \$1.2 million Second Loan will be used to acquire plant facilities that are necessary for the provision of KRWC's utility service."¹⁷

2. KRWC proposes to utilize \$524,231 of the proceeds from the First Loan to reimburse Mr. Acree for cash advances that

¹⁶See Consumer Advocate's Statement of Position, Section IV.A, at 6-13.

¹⁷Consumer Advocate's Statement of Position, at 13.

were used to acquire utility plant during 2000 to 2006. The \$524,231 in cash advances were used to acquire property and equipment that is used and useful for the provision of public utility service, consistent with HRS § 269-17.¹⁸

3. KRWC proposes to utilize \$117,401 of the proceeds from the First Loan to reimburse itself for costs incurred in 2007 for the repair and maintenance of Well No. 1. It appears that the \$117,401 will be used for the acquisition of plant and equipment used in the provision of public utility service, consistent with HRS § 269-17.¹⁹

4. KRWC proposes to utilize \$267,336 of the proceeds from the First Loan to purchase a spare pump to replace the existing pump in either Well No. 1 or Well No. 2. The Consumer Advocate concurs that it is reasonable to purchase a spare pump as a timely replacement for a failed pump; thus, the \$267,336 will be used to acquire plant and equipment that is used and useful for the provision of public utility service, consistent with HRS § 269-17.²⁰

5. KRWC proposes to utilize \$245,759 (\$119,395 in 2006, and \$126,364 in 2007) of the proceeds from the First Loan to reimburse itself for costs related to expenditures resulting from a 2006 earthquake and by flood damage sustained in 2007 due

¹⁸See Consumer Advocate's Statement of Position, Section IV.B, at 14-15; and KRWC's response to CA-IR-2a.

¹⁹See Consumer Advocate's Statement of Position, Section IV.D, at 16-17.

²⁰See Consumer Advocate's Statement of Position, Section IV.E, at 17-18.

to heavy rain. This proposal, in the Consumer Advocate's view, is not reasonable:

The Consumer Advocate attempted to reconcile the amounts listed in Exhibit 3 to the detailed fixed assets schedule to confirm that the 2006 and 2007 earthquake and flood damage costs were capitalized as utility plant. Not being able to do so, the Consumer Advocate inquired in CA-IR-3 why the amounts listed on Exhibit 3 did not appear as fixed asset additions during this period. In response, KRWG stated that the Company expensed the \$119,395 incurred in 2006 because the Company did not have current Commission approval to defer the expenditures for future recovery. Furthermore, KRWG contended that it likely will expense the \$126,374 incurred in 2007 and has reflected that treatment in its preliminary details of other assets and repairs and maintenance expenses for 2007. The Company, however, has included the amounts as deferred charges on the preliminary income statement provided as an Attachment to the response to CA-IR-4c.

Given the above, the Consumer Advocate contends that KRWG should not be authorized to enter into long term debt to be reimbursed for the 2006 amounts that were previously expensed. Similarly, the Consumer Advocate contends that KRWG should not be allowed to defer the 2007 repair and maintenance costs for future cost recovery since KRWG did not seek prior Commission authorization for such deferral and has indicated in its preliminary financial statement for 2007 that these amounts would be expensed, and not deferred. Allowing KRWG to utilize the proceeds from the First Loan to reimburse itself for repair and maintenance expenses would be akin to entering into long term debt for purposes of acquiring working capital funds, which is prohibited in HRS § 269-17.

Consumer Advocate's Statement of Position, Section IV.C, at 15-16 (footnote and text therein omitted).

That said, the Consumer Advocate ultimately recommends that the commission authorize KRWC to enter into the First Loan, reasoning:

As discussed in Sections IV.A. through IV.E. [of its Statement of Position], the Consumer Advocate has determined that with the exception of the proposal to use \$245,759 of the loan proceeds for the 2006 and 2007 earthquake and flood repair costs, the intended uses of the proceeds from the First Loan comply with the requirements set forth in HRS § 269-17. Although \$245,759 of the loan proceeds will not be used for the intended purposes set forth in HRS § 269-17, the Consumer Advocate notes that all but the Well No. 3 and Reservoir No. 4a costs are known at this time. Since the \$4,279,487 cost estimates to develop Well No. 3 and Reservoir No. 4a are based on a bid proposal received in 2007, the costs may change due to the passage of time from when the bid was initially submitted.

As a result, it is reasonable to allow KRWC to enter into the First Loan and have the additional \$311,544 of loan proceeds²¹ available to pay for any reasonable cost increases that may be incurred to complete the construction of Well No. 3 and Reservoir No. 4a.²² In addition, the Company may use the \$311,544 to acquire assets that are used in the provision of the regulated utility service. As a result, rather than limit the amount of the First Loan proceeds, the Consumer Advocate recommends that the Commission

²¹Footnote 25 of the Consumer Advocate's Statement of Position reads:

\$245,759 (2006 and 2007 costs expensed) + \$65,785 (unaccounted for funds) = \$311,544[.]

²²Footnote 26 of the Consumer Advocate's Statement of Position reads:

The Consumer Advocate reserves its right to review the actual completed costs and take a position on the reasonableness of such costs in the rate proceeding following the in-service date of such assets.

authorize KRWC to enter into the \$5.5 million First Loan, and provide an accounting that demonstrates use of the \$311,544 proceeds for the acquisition of utility plant assets.

Consumer Advocate's Statement of Position, Section IV.F, at 18-19 (emphasis added).²³

6. "[T]he \$1 million revolver is intended to be used to provide funds for future foreseen and unforeseen capital expenditures, as well as potentially cover debt service in the early years of the loan. To the extent that the proceeds are used to cover debt service and are repaid within one year, which is generally consistent with revolver funds, the Consumer Advocate will not object to such use of funds. On the other hand, if funds from the revolver are to be used to acquire utility plant, then the Consumer Advocate recommends that KRWC annually submit a list of the plant assets that were acquired with the revolver funds. The list should provide the date of acquisition and the related costs of the asset."²⁴

2.

The Second Loan

KRWC proposes to utilize the \$1.2 million in proceeds from the Second Loan to purchase the Well No. 3 improvements, which are currently owned by KRWC's affiliate, KR Properties.

²³See also Consumer Advocate's Statement of Position, Section V, at 23 (the Consumer Advocate recommends that for the \$311,544 in proceeds from the First Loan, KRWC provide an accounting that demonstrates the funds were used for the acquisition of utility plant).

²⁴Consumer Advocate's Statement of Position, Section IV.G, at 19-20; see also id., Section V, at 23 (if any of the \$1 million revolver proceeds are used to acquire utility plant, an accounting should be provided to document such use).

The purchase price of \$1,223,180 is below market value, and is intended to reimburse KR Properties for the cost incurred to drill the well back in the early 1990s. "[T]he Consumer Advocate has determined that KRWC's proposal to acquire the Well No. 3 improvements is reasonable and will result in the acquisition of assets that are used in the provision [of] the regulated utility service. Thus, the Consumer Advocate recommends Commission approval of KRWC's request to enter into the Second Loan."²⁵

3.

Pledging of KRWC's Assets as Security

The Consumer Advocate does not object to the proposed terms of the First and Second Loans, and does not oppose KRWC's request to pledge its assets as security for the loans.²⁶ In this regard, the Consumer Advocate reasons:

As noted on the unaudited financial statements as of December 31, 2007, KRWC reports utility plant with a net book value of only \$4,884,278. Furthermore, based on the source and application of funds statement provided as Exhibit 8, KRWC expects to generate positive cash at the end of each year from 2007 through 2011, with the exception of 2009. Finally, as a regulated utility, KRWC will be able to seek Commission approval to adjust the rates charged customers for the utility water service provided, if the existing rates are not sufficient to pay the debt service costs in the future, pursuant to the terms of the proposed First and Second Loans.

Consumer Advocate's Statement of Position, at 22.

²⁵Consumer Advocate's Statement of Position, Section IV.H, at 20-21.

²⁶Consumer Advocate's Statement of Position, Section IV.I, at 21-23.

E.

KRWC's Response

In its Response filed on May 14, 2008,²⁷ KRWC states that with respect to the Consumer Advocate's concern over the use of the \$245,759 in loan proceeds under the First Loan:

Although KRWC does not necessarily agree with the Consumer Advocate's allegations and/or contentions in connection with KRWC's proposed capitalization of the \$245,759 of the loan proceeds (i.e., for the reimbursement of the 2006 and 2007 earthquake and flood repair expenditures as described in Section IV.C of the SOP), KRWC does not believe that these allegations and/or contentions are relevant for purposes of the Commission's review and disposition of the instant Application. However, KRWC reserves its right to address these allegations and/or contentions including, without limitation, providing support or justification of seeking future recovery of the earthquake/flood expenditures in KRWC's next rate case.

KRWC's Response, at 2 n.1

That said, "KRWC does not object to the Consumer Advocate's position in connection with KRWC's proposed financing and security arrangements and the Consumer Advocate's two (2) recommended regulatory conditions, for purposes of this Application only."²⁸ In conclusion, KRWC states that this proceeding is ready for decision-making by the commission.

²⁷KRWC's Response Statement to the Consumer Advocate's Statement of Position; and Certificate of Service, filed on May 14, 2008 (collectively, "Response").

²⁸KRWC's Response, at 2 (footnote and text therein omitted).

II.

Discussion

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 (emphasis added).

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.²⁹

"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."³⁰

HRS § 269-19 provides that no public utility shall sell, lease, assign, mortgage, or otherwise dispose of or encumber the whole or any part of its road, line, plant, system, or other property necessary or useful in the performance of its duties to the public, nor by any means, directly or indirectly, merge or consolidate with any other public utility, without first having secured from the commission "an order authorizing it so to do. Every such sale, lease, assignment . . . [or] disposition . . . made other than in accordance with the order of the

²⁹See In re Citizens Comm. Co., dba The Gas Co., Docket No. 03-0051 ("Docket No. 03-0051"), Decision and Order No. 20354, filed on July 25, 2003, at 42-43.

³⁰Docket No. 03-0051, Decision and Order No. 20354, at 43.

commission shall be void." The purpose of HRS § 269-19 is to safeguard the public interest. In re Honolulu Rapid Transit Co., Ltd., 54 Haw. 402, 409, 507 P.2d 755, 759 (1973).

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 commission, at the outset, addresses the \$245,759 in proceeds from the First Loan that KRWC, as part of its Application, proposed to utilize to reimburse itself for costs incurred as a result of the 2006 earthquake and by flood damage sustained in 2007 due to heavy rain.

The Consumer Advocate, in essence, reasons that because KRWC expensed the \$119,395 it incurred in 2006, and in all likelihood will expense the remaining \$126,374 it incurred in 2007, allowing KRWC to reimburse itself for these repair and maintenance expenses is inconsistent with HRS § 269-17, which authorizes public utilities to enter into long-term debt for the purposes of financing the acquisition of utility plant assets.

KRWC, in response, does not affirmatively object to the Consumer Advocate's position. As such, for purposes of this proceeding, the commission concurs with the Consumer Advocate that: (1) the \$245,759 in loan proceeds should not be utilized by KRWC to reimburse itself for the subject repair and maintenance expenses incurred in 2006 and 2007; (2) the \$245,759 in loan proceeds will instead be combined with the \$65,785 in unaccounted

for funds, for the purpose of acquiring utility plant assets; and (3) KRWC shall provide an accounting which demonstrates that the \$311,544 in loan proceeds were used to acquire utility plant assets. The issue, however, of whether KWRC may ultimately recover, for ratemaking purposes, the \$245,759 in costs it incurred for the subject repair and maintenance expenses, is an issue for adjudication in its next rate case.

With respect to the reasons for having Mr. Acree secure the First Loan from Bank of Hawaii, instead of KRWC, the Consumer Advocate notes:

. . . . In response to an informal information request issued by the Consumer Advocate regarding the basis for having Mr. Acree obtain the financing and the interest rates to be charged KRWC for obtaining such financing, KRWC represented as follows. In attempting to obtain the proposed long-term financing, KRWC approached three commercial Hawaii banks ("Lenders"). However, KRWC was not able to obtain long-term financing for the \$5.5 million merely by pledging KRWC's water plant assets. Lenders also wanted: (1) personal guarantee(s) by Mr. Acree and (2) the pledge of additional real property collateral, neither of which KRWC was able to provide on its own. In light of the above, the proposed long-term financing will be to Mr. Acree as opposed to the Bank of Hawaii. Under this arrangement, Mr. Acree is personally able to obtain a \$5.5 million loan from Bank of Hawaii on the following terms: (1) interest rate fixed at the 5-year FHLB Index plus 130 basis points; (2) interest only for the first 12 months; (3) balance amortized over 10 years with a call at the end of year five; and (4) obligations secured by (a) 24 lots in Kohala Ranch (not owned by KRWC), which lots the bank has appraised at \$12 million, and (b) a personal guarantee of Mr. Acree.

Consumer Advocate's Statement of Position, at 21.³¹

³¹KRWC, in its Response, does not affirmatively dispute or expand on the Consumer Advocate's representations.

Based on the representations set forth in KRWC's Application and in its Response, together with the Consumer Advocate's assertions, the commission finds that: (1) the proceeds from the financing arrangements will be used for the purposes permitted under HRS § 269-17; provided that with respect to the \$311,544 in loan proceeds under the First Loan, KRWC must provide an accounting to the commission and the Consumer Advocate which demonstrates that the \$311,544 in loan proceeds were used to acquire utility plant assets; and (2) there is no evidence in the docket record that the financing arrangements will have a materially adverse effect on KRWC's utility operations.

The commission also finds that the encumbrance of KRWC's utility assets under HRS § 269-19, as part of the financing arrangements, is consistent with the public interest, as the monies will be used: (1) to fund plant infrastructure and other capital improvements for KRWC's utility operations; and (2) "for the reimbursement of moneys actually expended" for such purposes. HRS § 269-17.

The commission approves the financing and security arrangements, consistent with HRS §§ 269-17, 269-19, and 269-7(a), and subject to the following conditions: (1) KRWC shall comply with the reporting requirements proposed by the Consumer Advocate and agreed-upon by KRWC; and (2) KRWC's use of the proceeds from the First and Second Loans shall be consistent with the representations (as updated) made in this docket, as required by HRS § 269-17.

III.

Orders

THE COMMISSION ORDERS:

1. The financing and security arrangements, as described by KRWC in its Application, filed on November 7, 2007, are approved, consistent with HRS §§ 269-17, 269-19, and 269-7(a), and subject to KRWC complying with the following conditions:

A. With respect to the \$311,544 in loan proceeds under the First Loan, KRWC must provide an accounting which demonstrates that the \$311,544 in loan proceeds were used to acquire utility plant assets. Unless ordered otherwise by the commission, KRWC shall file its report within sixty days from the date it has completed expending the \$311,544 in loan proceeds.

B. If any of the loan proceeds from the \$1 million revolver are used to acquire utility plant assets, KRWC shall annually submit a list of the plant assets that were acquired with the revolver funds, and include the date of acquisition and the related costs of the asset. Unless ordered otherwise by the commission, KRWC shall file its annual report by March 1st of each year, which covers the previous calendar year period. The first annual report shall be due by March 1, 2009.

C. KRWC's use of the proceeds from the First and Second Loans shall be consistent with the representations (as updated) made in this docket, as required by HRS § 269-17. KRWC shall certify its compliance with this requirement as part

of its annual report filed with the commission by March 1st of each year.

2. Within thirty days of each closing, KRWC shall notify the commission and the Consumer Advocate accordingly, including whether the terms and conditions of each transaction materially differ from the terms and conditions set forth in the docket record. If the terms and conditions materially differ, additional investigation, if necessary, will ensue.

3. The failure to comply with the requirements set forth in the Ordering Paragraphs, above, may constitute cause to void this Decision and Order, and may result in further regulatory action as authorized by law.

DONE at Honolulu, Hawaii JUN 18 2008.

PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

By Carlito P. Caliboso
Carlito P. Caliboso, Chairman

By: John E. Cole
John E. Cole, Commissioner

APPROVED AS TO FORM:

Michael Azama
Michael Azama
Commission Counsel

By: Leslie H. Kondo
Leslie H. Kondo, Commissioner

2007-0376.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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