

CHAPTER 24. SUBSTANTIVE RULES APPLICABLE TO WATER AND SEWER SERVICE PROVIDERS.

Subchapter A. GENERAL PROVISIONS.

§24.11. Financial Assurance.

- (a) **Purpose.** This section establishes criteria to demonstrate that an owner or operator of a retail public utility has the financial resources to operate and manage the utility and to provide continuous and adequate service to the current and proposed utility service area.
- (b) **Application.** This section applies to new and existing owners or operators of retail public utilities that are required to provide financial assurance pursuant to this chapter.
- (c) Financial assurance must be demonstrated by compliance with subsection (d) or (e) of this section, unless the commission requires compliance with both subsections (d) and (e) of this section.
- (d) **Irrevocable stand-by letter of credit.** Irrevocable stand-by letters of credit must be issued by a financial institution that is supervised or examined by the Board of Governors of the Federal Reserve System, the Office of the Controller of the Currency, or a state banking department, and where accounts are insured by the Federal Deposit Insurance Corporation. The retail public utility must use the standard form irrevocable stand-by letter of credit approved by the commission. The irrevocable stand-by letter of credit must be irrevocable for a period not less than five years, payable to the commission, and permit a draw to be made in part or in full. The irrevocable stand-by letter of credit must permit the commission's executive director or the executive director's designee to draw on the irrevocable stand-by letter of credit if the retail public utility has failed to provide continuous and adequate service or the retail public utility cannot demonstrate its ability to provide continuous and adequate service.
- (e) **Financial test.**
 - (1) An owner or operator may demonstrate financial assurance by satisfying a financial test including the leverage and operations tests that conform to the requirements of this section, unless the commission finds good cause exists to require only one of these tests.
 - (2) **Leverage test.**

To satisfy this test, the owner or operator must meet one or more of the following criteria:

 - (A) The owner or operator must have a debt to equity ratio of less than one, using long term debt and equity or net assets;
 - (B) The owner or operator must have a debt service coverage ratio of more than 1.25 using annual net operating income before depreciation and non-cash expenses divided by annual combined long term debt payments;
 - (C) The owner or operator must have sufficient unrestricted cash available as a cushion for two years of debt service. Restricted cash includes monetary resources that are committed as a debt service reserve which will not be used for operations, maintenance or other payables;
 - (D) The owner or operator must have an investment-grade credit rating from Standard & Poor's Financial Services LLC, Moody's Investors Service, or Fitch Ratings Inc.; or
 - (E) The owner or operator must demonstrate that an affiliated interest is capable, available, and willing to cover temporary cash shortages. The affiliated interest must be found to satisfy the requirements of subparagraphs (A), (B), (C), or (D) of this paragraph.
 - (3) **Operations test.** The owner or operator must demonstrate sufficient cash is available to cover any projected operations and maintenance shortages in the first five years of operations. An affiliated interest may provide a written guarantee of coverage of temporary cash shortages. The affiliated interest of the owner or operator must satisfy the leverage test.

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- (4) To demonstrate that the requirements of the leverage and operations tests are being met, the owner or operator shall submit the following items to the commission:
- (A) An affidavit signed by the owner or operator attesting to the accuracy of the information provided. The owner or operator may use the affidavit included with an application filed pursuant to §24.105 of this title (relating to Contents of Certificate of Convenience and Necessity Applications) pursuant to the commission's form for the purpose of meeting the requirements of this subparagraph; and
 - (B) A copy of one of the following:
 - (i) the owner or operator's independently audited year-end financial statements for the most recent fiscal year including the "unqualified opinion" of the auditor; or
 - (ii) compilation of year-end financial statements for the most recent fiscal year as prepared by a certified public accountant (CPA); or
 - (iii) internally produced financial statements meeting the following requirements:
 - (I) for an existing utility, three years of projections and two years of historical data including a balance sheet, income statement and an expense statement or evidence that the utility is moving toward proper accountability and transparency; or
 - (II) for a proposed or new utility, start up information and five years of pro forma projections including a balance sheet, income statement and expense statement or evidence that the utility will be moving toward proper accountability and transparency during the first five years of operations. All assumptions must be clearly defined and the utility shall provide all documents supporting projected lot sales or customer growth.
 - (C) In lieu of meeting the leverage and operations tests, if the applicant utility is a city or district, the city or district may substantiate financial capability with a letter from the city's or district's financial advisor indicating that the city or district is able to issue debt (bonds) in an amount sufficient to cover capital requirements to provide continuous and adequate service and providing the document in subparagraph (B)(i) of this paragraph.
- (5) If the applicant is proposing service to a new CCN area or a substantial addition to its current CCN area requiring capital improvements in excess of \$100,000, the applicant must provide the following:
- (A) The owner must submit loan approval documents indicating funds are available for the purchase of an existing system plus any improvements necessary to provide continuous and adequate service to the existing customers if the application is a sale, transfer, or merger; or
 - (B) The owner must submit loan approval documents or firm capital commitments affirming funds are available to install plant and equipment necessary to serve projected customers in the first two years of projections or a new water system or substantial addition to a currently operating water system if the application includes added CCN area with the intention of serving a new area or subdivision.
- (6) If the applicant is a nonfunctioning utility, as defined in §24.3(45) of this title (relating to Definitions of Terms), the commission may consider other information to determine if the proposed certificate holder has the capability of meeting the leverage and operations tests.