

## Oversight of Retail Water Providers

### I. Purpose

1. The purpose of these rules is to:
  - a. Implement Ark. Code Ann. § 14-234-801 et seq.;
  - b. Provide oversight of retail water providers to promote efficiency in service and stability in fiscal management;
  - c. Provide training and education to governing bodies of retail water providers; and
  - d. Provide training of local, state, and federal leaders on the issues surrounding provider personnel, finances, compliance, and environmental factors.
2. The rules shall be read in conjunction with Ark. Code Ann. § 14-234-801 et seq.

### II. Definitions

The following definitions are supplemental to the definitions in Ark. Code Ann. § 14-234-801 et seq.:

1. "Annualized Revenue Requirement" means the projected revenue if the recommended increase, as well as all previous recommended increases, is in effect for the full 12-month period.
2. "Commission" means the Arkansas Natural Resources Commission.
3. "Debt Service Coverage Ratio" ("DSCR") means Net Operating Income divided by Total Debt Service.
4. "Department" means the Arkansas Department of Agriculture, including the Natural Resources Division thereof.
5. "Future Capital Expenses" means the design and construction of new and replacement infrastructure, including any associated labor and fees.
6. "Non-operating Revenue" means revenue derived from sources other than water use charges.
7. "Net Operating Income" means earnings before interest, tax, depreciation, and amortization (EBITDA) less capital expenditures.
8. "Provider board" as used herein shall have the definition provided in Ark. Code Ann. § 14-234-801(b)(3).
9. "System" means:
  - a. For a provider that provides water service only, the provider's water system.
  - b. For a provider that provides water service and sewer service, but where the water system and the sewer system are not operated as a joint and integrated undertaking (i.e., when a separate audit is prepared for water and for sewer), the provider's water system.
  - c. For a provider that provides water service and sewer service, and the water facilities are operated as a joint and integrated undertaking (i.e., when water and sewer are combined in a single audit), the provider's joint and integrated water and sewer system.
10. "Total Debt Service" means current debt obligations, including but not limited to any interest, principal, sinking fund, and lease payments due in a given year.

### III. Refurbishment and Replacement Account

1. Providers may designate existing depreciation or replacement accounts as the Refurbishment and Replacement Account required by Ark. Code Ann. § 14-234-802(e), so long as the amount deposited therein complies with the provisions of Ark. Code Ann. § 14-234-802(e).
2. The calculation of the amount required to be deposited into a Refurbishment and Replacement Account pursuant to these Rules and Ark. Code Ann. § 14-234-802(e) shall be based on the gross operating revenues of a System.
3. Utilization of funds from the Refurbishment and Replacement account must be approved by the Provider Board prior to its use.

#### **IV. Rate Studies for Retail Water Providers**

1. Retail water providers shall obtain rate studies pursuant to the requirements in Ark. Code Ann. § 14-234-802.
2. Rate studies shall be based on the guidelines of the American Water Works Association and the Water Environment Federation.
  - a. The rate studies shall include:
    - i. Reports containing the following information for the current year and projections for the next five years:
      1. A comprehensive cost analysis, including:
        - a. Operations and maintenance (O&M) expenses;
        - b. Financing expenses, including but not limited to debt service payments, bond issuance costs, and commercial paper fees, if applicable;
        - c. Any required cash reserves unavailable to pay for expenses, including but not limited to the annual refurbishment and replacement account deposit requirement as set out in Ark. Code Ann. § 14-234-802(e);
        - d. Depreciation expenses;
        - e. Future capital expenses;
        - f. Expenses required for an annual audit or agreed-upon procedures and compilation report;
        - g. Expenses required for rate studies required under Ark. Code Ann. § 14-234-802; and
        - h. Any other expenses not accounted for in paragraphs (a) through (g).
      2. A comprehensive revenue earnings analysis, including:
        - a. Available Cash balance;
        - b. Non-rate revenue;
        - c. Rate revenue without recommended increases;
      3. For the five projected years, recommended rate increases and the projected additional revenue derived therefrom;
      4. Debt Service Coverage Ratios;
      5. The number of days that the available cash balance could cover O&M expenses without additional revenue;
      6. Annualized revenue requirement.
    - ii. The provider's asset management plan, including:

1. inventory of essential assets and for each essential asset, without limitation, the following information:
  - a. Asset type;
  - b. Annual maintenance costs;
  - c. Year installed;
  - d. Vendor-specified useful life, if available;
  - e. Anticipated date of replacement;
  - f. Installation or replacement cost estimate; and
  - g. Projected consequence of failure.
2. The provider's plan for replacement of essential assets.
- iii. Proposed changes in rates should be based on achieving and maintaining a Debt Service Coverage Ratio of 1.1 or higher.
- iv. An explanation of the provider's chosen rate design; and
- v. Recommendations for any changes to the provider's operations, including a plan on how the changes should be implemented.
- vi. Certification by the entity performing the rate study that such study complies with Ark. Code Ann. § 14-234-801 et. seq. and these Rules.
- b. Rate studies shall be provided to the Department at the time it is provided to Arkansas Legislative Audit under Ark. Code Ann. § 14-234-802(i).
- c. The Commission may request further information necessary to determine a provider's fiscal status, and providers shall cooperate with the Commission's requests.
- d. The Commission may waive any one or more requirement in Section IV(3)(a), above, upon written request.
3. Rate studies for providers that operate a joint and integrated water and sewer system shall analyze the total System.
4. Rate studies performed shall be an objective and unbiased review of the provider's fiscal status.
5. The Commission will maintain a list of approved entities to conduct rate studies as required under Ark. Code Ann. § 14-234-802(f)(1). The Commission may remove an approved entity from its list of approved entities if it determines that an entity violated Arkansas law or Commission rules in performing a rate study.

**V. Determinations of Fiscal Distress**

1. A Provider will be in Fiscal Distress if the Provider:
  - a. Fails to obtain a rate study as required;
  - b. Fails to implement the rates contained in the completed rate study within the time requirements provided under Ark. Code Ann. § 14-234-802(c)(2)(B)(ii)-(iv); or
  - c. Fails to maintain a Debt Service Coverage Ratio of 1.05 or higher.
2. A Provider may be determined to be in fiscal distress if the Provider:
  - a. Does not comply with the training required by Ark. Code Ann. § 14-234-805 and Section VII, below;
  - b. Fails to file with Arkansas Legislative Audit an audit report or agreed-upon procedures and compilation report required by Ark. Code Ann. § 14-234-120;

- c. Fails to maintain unincumbered cash or cash equivalents in an amount equal to one-twelfth of the total expenses from the most recent fiscal year;
  - d. Fails to adopt budget before the beginning of a new fiscal year providing for sufficient revenues to meet or exceed anticipated expenses during that fiscal year;
  - e. Fails to make all required payments due to the United States Treasury – Internal Revenue Service, Arkansas Department of Finance and Admission, or Arkansas Department of Health;
  - f. Fails to make any bond, loan, or lease payment; or
  - g. Fails to comply with an administrative order of the US Environmental Protection Agency, Arkansas Department of Health or Arkansas Division of Environmental Quality concerning operation and maintenance of the system.
3. Providers determined to be in fiscal distress shall submit to the Department an improvement plan as required in Ark. Code Ann. § 14-234-802(k) detailing in writing the provider’s plan to resolve the violation or violations of rule or law or the provider’s plan to resolve its fiscal insufficiency that caused it to be considered in fiscal distress.
  4. A provider will be determined by the Commission to no longer be in fiscal distress if:
    - a. The provider resolves the violation of rule or law that caused it to be considered in fiscal distress and obtains written verification from the Commission that the violation has been resolved; or
    - b. The provider implements a change of rates that is shown by the study to resolve the provider’s fiscal insufficiency.

**VI. Miscellaneous**

1. A provider seeking approval from the Commission under Ark. Code Ann. § 14-234-802(g) shall demonstrate its fiscal sustainability by submitting to the Commission a business plan demonstrating its technical, financial, and managerial capacity.
2. Pursuant to provisions relating to Commission intervention under the conditions provided for in Ark. Code Ann. § 14-234-804(d), upon request of a municipal provider or a customer or unserved customer of a municipal provider, the Department will assist in the resolution of the issue or issues if the party or parties involved demonstrate that all parties involved made a good faith effort to resolve the issue or issues.
  - a. Such intervention may include without limitation negotiation or mediation with the party or parties involved.
  - b. If the Department determines that a party is not acting in good faith, the Department may end its intervention.

**VII. Training**

1. A majority of the members of provider boards shall receive a minimum of eight hours of provider training.
2. If a change in membership of a provider board causes the provider board to have less than a majority of members who have undergone provider training, enough members of the provider board shall receive provider training within one year of the change in membership such that a majority of the board has received training.

3. Each provider board shall report the following information annually, by January 31, to the Department:

- a. the names and contact information of each member on the provider board;
- b. an identification of which members have obtained eight hours of provider training; and
- c. an identification of which members have served on the board for more than ten (10) years and are exempt from the training requirement pursuant to Ark. Code Ann. § 14-234-805(a)(3).