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David L. Armstrong
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Vice Chairman

June 5, 2008

Mr. Greg Pridemore
Letcher County Water and Sewer District
Post Office Box 827
Whitesburg, Kentucky 41858

Re: Crafts Colley Phase III Waterline Extension Project

Dear Mr. Pridemore:

Commission Staff acknowledges receipt of your letter of May 21, 2008, in which you request an opinion regarding the need for a Certificate of Public Convenience and Necessity for a water distribution main extension project in Letcher County, Kentucky.

Based upon your letter and your telephone conversation with Commission Staff, Commission Staff understands the facts as follows:

Letcher County Water and Sewer District ("Letcher District"), a water district organized pursuant to KRS Chapter 74, provides water service to 556 customers in Letcher County, Kentucky. It proposes to construct approximately 11,560 linear feet of 6-inch polyvinylchloride ("PVC") water distribution main and approximately 15,840 feet of 3-inch and 4-inch PVC water distribution main. The proposed project does not involve the construction of any other facilities. The proposed project will make water service available to approximately 180 households.

Total estimated cost of the project is \$650,000. Based upon awarded bids, Letcher District estimates the cost of construction, excluding contingencies and legal, engineering, and other fees, to be \$538,000. Letcher District anticipates that construction of the proposed project will begin between July 15, 2008 and August 15, 2008. Letcher District will finance the cost of the project with the proceeds of a grant from the Department of Abandoned Mine Lands. The

proposed construction will not require a rate adjustment.
Letcher District will not issue any evidences of indebtedness.

Your letter presents the following question: Must Letcher District obtain a Certificate of Public Convenience and Necessity for the proposed project?

KRS 278.020(1) provides:

No person, partnership, public or private corporation, or combination thereof shall commence providing utility service to or for the public or begin the construction of any plant, equipment, property, or facility for furnishing to the public any of the services enumerated in KRS 278.010, except retail electric suppliers for service connections to electric-consuming facilities located within its certified territory and ordinary extensions of existing systems in the usual course of business, until that person has obtained from the Public Service Commission a certificate that public convenience and necessity require the service or construction.

Administrative Regulation 807 KAR 5:001, Section 9(3), further provides:

Extensions in the ordinary course of business. No certificate of public convenience and necessity will be required for extensions that do not create wasteful duplication of plant, equipment, property or facilities, or conflict with the existing certificates or service of other utilities operating in the same area and under the jurisdiction of the commission that are in the general area in which the utility renders service or contiguous thereto, and that do not involve sufficient capital outlay to materially affect the existing financial condition of the utility involved, or will not result in increased charges to its customers.

Under the method of analysis that Commission Staff has historically employed, the construction of the proposed water distribution main upgrade does not appear to be in the ordinary course of business and would require a Certificate of Public Convenience and Necessity. According to its Annual Report, Letcher District had net utility plant of \$2,854,091.¹ The proposed water distribution main upgrade represents an increase in Letcher District's net utility plant of 22.77 percent. Such an increase in net utility plant is not generally considered as ordinary.²

¹ Annual Report of Letcher County Water and Sewer District to the Kentucky Public Service Commission for the Year Ended December 31, 2006, at 7.

² See, e.g., *City of Covington v. Board of Commissioners of Kenton County Water District No. 1*, 371 S.W.2d 20, 22 (Ky. 1963).

In 2006 the Kentucky General Assembly enacted legislation that provides:

Water Districts and Water Associations: A water district created pursuant to KRS Chapter 74 and a water association created pursuant to KRS Chapter 273 that undertakes a waterline extension or improvement project shall not be required to obtain a certificate of public convenience and necessity pursuant to KRS 278.020(1) if the water district or water association is a Class A or B utility as defined in the Uniform System of Accounts established by the Public Service Commission, pursuant to KRS 278.220, as the system of accounts prescribed for utilities in Kentucky, and either: (a) The water line extension or improvement project will not cost in excess of \$500,000; or (b) The water district or water association will not, as a result of the water line extension or improvement project, incur obligations requiring Public Service Commission approval pursuant to KRS 278.300. In either case, the water district or water association shall not, as a result of the water line extension or improvement project, increase rates to its customers.

2006 Ky. Acts Chapter 252. This Act expires on June 30, 2008.

Based upon the facts presented in your letter, Commission Staff is of the opinion that, assuming that the proposed construction commences prior to July 1, 2008, the Act would not exempt the proposed construction from the requirement to obtain a Certificate of Public Convenience and Necessity. As Letcher District had annual revenues in calendar year 2006 of \$247,597, it is a Class C water utility³ and therefore does not fall within the class of water utilities subject to the exemption.

You have suggested in your letter that Letcher District's annual revenues for the year ending December 31, 2007 will exceed \$250,000. This increase in annual revenues will not alter Letcher District's status as a Class C water utility. The Uniform System of Accounts provides:

The class to which any utility belongs shall originally be determined by the average of its annual water operating revenues for the last three consecutive years. Subsequent changes in classification shall be made when the average annual water operating revenues for the three immediately preceding years exceed the upper limit or are less than the lower limit, of the annual water operating revenues of the classification previously applicable to the utility. For a utility

³ The Kentucky Public Service Commission's Uniform System of Accounts defines a Class C water utility as a utility "having annual water operating revenues of less than \$250,000 or less than 400 customers." *Uniform System of Accounts for Class C Water Districts and Associations* at 8 (2002) (found at <http://psc.ky.gov/agencies/psc/forms/usoa/0700c02.pdf>).

Mr. Greg Pridemore
June 5, 2008
Page 4

with water and wastewater operations, the classification shall be based on the operation with the highest annual revenues.⁴

Given the level of Letcher District's annual revenues for calendar years 2005 and 2006, a significant increase in the water district's annual revenues would be required to change Letcher District's status.

Assuming that Letcher District achieves such an increase, the exemption which the Act established ends on June 30, 2008. To qualify for the exemption, Letcher District must commence construction of the proposed project no later than that date. Letcher District currently does not anticipate construction to begin earlier than July 15, 2008.

This letter represents Commission Staff's interpretation of the law as applied to the facts presented. This opinion is advisory in nature and not binding on the Commission should the issues herein be formally presented for Commission resolution. Questions concerning this opinion should be directed to Gerald Wuetcher, Assistant General Counsel, at (502) 564-3940, Extension 259.

Sincerely,



David S. Samford
General Counsel

⁴ *Id.*