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September 28, 2012

Mr. Joe Dan Taylor  
Dexter-Almo Heights Water District  
Almo, Kentucky 42020

Re: Dexter-Almo Heights Water District  
Hopkins Road Loop Project

**PSC STAFF OPINION 2012-021**

Dear Mr. Taylor:

Commission Staff acknowledges receipt of your letter of July 5, 2012 in which you requested on behalf of Dexter-Almo Heights Water District ("Dexter-Almo District") an opinion regarding the need for a certificate of public convenience and necessity for the construction of a water distribution main in Calloway County, Kentucky.

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.

Commission Staff understands the facts as follows:

Dexter-Almo District, a water district organized pursuant to KRS Chapter 74, owns and operates a water distribution system that provides water service to 767 customers in Calloway County, Kentucky.<sup>1</sup>

Dexter-Almo District proposes to construct an 11,640 linear feet of 6-inch polyvinylchloride water main along Hopkins Road in northern Calloway County to extend water service to approximately 25 households and to form a loop in its water distribution system. Creation of the loop is expected to increase overall system pressure and to improve system reliability by creating a redundant feed source. The total

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<sup>1</sup> *Annual Report of Dexter-Almo Heights Water District to the Kentucky Public Service Commission for the Year Ended December 31, 2011 ("Annual Report")* at 5, 21.

estimated cost of proposed water distribution main is \$300,000.<sup>2</sup>

Because of funding considerations, Dexter-Almo Height District has divided the project into two phases.<sup>3</sup> In the first phase, the water district proposes to construct approximately 3,630 linear feet of the proposed water main extension. Approximately \$80,093 of this cost is related to construction. The remaining \$15,683 is related to engineering fees, administrative expenses and contingencies. The project will be funded with \$95,776 of appropriated funds from the General Assembly.<sup>4</sup> Approximately six to eight customers will be added as a result of the Phase I extension.

Your letter presents the following question: Must Dexter-Almo 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

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<sup>2</sup> The project also includes the installation of 760 radio read meters to replace Dexter-Almo District's existing meters. See <http://wris.ky.gov/portal/DwPrjData.aspx?PNUM=WX21035006> (last visited Sept. 17, 2012).

<sup>3</sup> The entire project has been designated in the Kentucky Water Resource Information System as Project WX21035006.

<sup>4</sup> See 2012 Ky. Acts Ch. 144 (reauthorization and reallocation of \$95,775 to Hopkins Road Loop and Metering Installation).

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, Dexter-Almo District had net utility plant of \$866,380.<sup>5</sup> The proposed water distribution main upgrade represents an increase in Dexter-Almo District's net utility plant of 11.1 percent. Such an increase in net utility plant is not generally considered as ordinary.<sup>6</sup>

Commission Staff has also considered the effect of the proposed construction and the addition of eight customers on the utility's financial condition. Assuming that the proposed construction adds eight additional customers, it would result in increased annual revenues of \$1,716.<sup>7</sup> The construction and the additional customers would also result in additional annual expenses of \$2,121.<sup>8</sup> It would thus reduce net income by \$405, or approximately 7.6 percent.<sup>9</sup> Such a reduction in net income may be considered as material.

In its 2012 Session, the Kentucky General Assembly enacted legislation that provides:

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<sup>5</sup> *Annual Report* at 7.

<sup>6</sup> 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).

<sup>7</sup> Based upon the number of retail customers at the start of 2011 calendar year and total reported residential sales, a residential customer of Dexter-Almo District has a monthly usage of 3,550 gallons (31,271,000 gallons (total residential sales) ÷ 734 customers ÷ 12 months = 3,550 gallons per customer per month). Based upon Dexter-Almo District's current rate schedule, the addition of eight customers would produce additional annual revenues of \$1,716.48 (8 customers x 12 months x \$17.88 monthly bill).

<sup>8</sup> Assuming the proposed main has a useful service life of 50 years, the proposed construction will increase Dexter-Almo District's annual depreciation expense by \$1,916 (\$95,776 ÷ 50 years). For appropriate useful life, see National Association of Regulatory Utility Commissioners, *Depreciation Practices for Small Utilities* 11 (Aug. 15, 1979). The annual purchased cost of water for the eight additional customers will be \$205 (3,550 gallons x 8 customers x 12 months x \$1.66 per 1,000 gallons). Total annual cost will be \$2,121.

<sup>9</sup> For the calendar year ending December 31, 2011, Dexter-Almo reported net income before contributions of \$5,273.

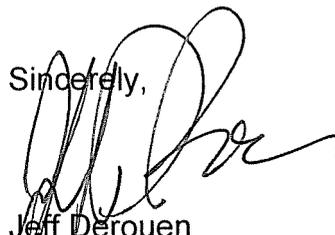
Water Districts and Water Associations: A water district created pursuant to KRS Chapter 74 and a water association created pursuant to KRS Chapter 273 that undertakes a waterline extension or improvement project shall not be required to obtain a certificate of public convenience and necessity pursuant 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.

2012 Ky. Acts Chapter 144.

This Act would not exempt the proposed construction from the requirement to obtain a certificate of public convenience and necessity. As Dexter-Almo District had annual revenues in calendar year 2011 of \$204,696, it is a Class C water utility<sup>10</sup> and therefore does not fall within the class of water utilities subject to the exemption.

Questions concerning this opinion should be directed to Gerald Wuetcher, Executive Advisor/Attorney, at (502) 564-3940, Extension 259. If Dexter-Almo District desires assistance in the preparation of an application for a certificate of public convenience and necessity or for authorization of the issuance of an evidence of indebtedness, contact Mr. Wuetcher.

Sincerely,



Jeff Derouen  
Executive Director

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<sup>10</sup> 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 A and B Water Districts and Associations* at 14 (2002) (found at <http://psc.ky.gov/agencies/psc/forms/usoa/0700ab02.pdf>).