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NEWS RELEASE

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PSC Grants Rate Increase to Northern Kentucky Water *Questionable spending is disallowed; district warned against repeat*

FRANKFORT, Ky. (Jan. 7, 2011) – The Kentucky Public Service Commission (PSC) today granted a rate increase to the Northern Kentucky Water District, but reduced the requested amount to reflect questionable expenditures by the district.

In an order issued today, the PSC found that Northern Kentucky Water had justified the need for additional revenue in order to meet increased costs and to pay for system improvements.

However, the PSC also criticized the district for spending money on club memberships, employee gifts, promotional items and other expenditures not tied to the delivery of water to customers. The PSC said the expenses could not be charged to customers and should not be repeated in the future.

Today's order allows Northern Kentucky Water to increase its rates across all classes of customers in order to generate an additional \$8.07 million in revenue per year, which reflects a reduction of \$84,000 from the requested amount. A PSC analysis indicated that Northern Kentucky Water could have justified an increase of as much as \$11.6 million, based on its revenue needs for operations and debt service.

The company estimated that its proposal would increase the average quarterly bill for residential customers to \$122.98, an increase of \$24.36, or about 25 percent from the current average of \$98.62. Those increases will be slightly smaller due to the \$84,000 revenue reduction ordered by the PSC.

In order to reduce the impact on customers, Northern Kentucky will implement the rate increases in two equal phases at the beginning of 2011 and 2012.

Northern Kentucky's last rate increase took effect in December 2007. The water district serves about 80,000 customers in Boone, Campbell and Kenton counties in northern Kentucky and provides wholesale water service to the city of Walton and the Bullock Pen and Pendleton County water districts.

The PSC conducted a hearing in the case on Oct. 27, 2010. The PSC also held a meeting in Fort Mitchell on Oct. 14, 2010, to take comments from the public.

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Other parties to the case were the Kentucky Office of Attorney General and the Northern Kentucky Tea Party, Inc.

In opposing the rate increase, the Northern Kentucky Tea Party argued that the additional revenue was needed only because Northern Kentucky Water was spending the money to comply with new U.S. Environmental Protection Agency (EPA) drinking water regulations which the Northern Kentucky Tea Party characterized as unconstitutional. Northern Kentucky Water failed to challenge the regulations or propose less costly options for complying with them, the Northern Kentucky Tea Party said.

The PSC said it has no jurisdiction over or authority to consider the constitutionality of EPA regulations. If the Northern Kentucky Tea Party wishes to challenge those regulations, it should do so through the federal courts or Congress, the PSC said.

Northern Kentucky Water's failure to challenge those regulations cannot serve as a basis for denying the rate increase, the PSC said. The PSC noted that the district had applied for and received PSC approval for the necessary improvements to its water treatment plants.

In considering Northern Kentucky Water's proposals for meeting the EPA requirements, the PSC determined that the options chosen by the district were reasonable and necessary. The Northern Kentucky Tea Party failed to produce evidence that the proposed projects are not reasonable or cost-effective or that fighting the EPA regulations would lower their cost, the PSC said.

The PSC found no reason to reconsider its earlier approval of the projects.

Furthermore, the PSC found that the cost of complying with the new EPA regulations accounts for only a small portion of the requirement for a revenue increase. A portion of the increase will go to debt service on \$32.5 million in bonds that the PSC authorized Northern Kentucky Water to issue. The Northern Kentucky Tea Party had asked the PSC not to authorize the bond issue.

Only a small portion of the bond revenue will be used to meet the new EPA requirements, with most going to pay for new water meters, water main extensions or replacements and replacement of obsolete water treatment facilities, the PSC said.

The PSC calculated that the cost of complying with the EPA requirements is about 11.5 cents per 1,000 gallons, or less than one-fifth of the total rate increase.

While approving the overall rate request, the PSC identified \$83,969 in inappropriate expenditures that could not be charged to customers. The expenditures were incurred despite long-standing PSC precedents disallowing such costs.

They included donations to community service organizations and sponsorships of charitable events; memberships in civic organizations and a local dining club; promotional items such as toys and water bottles; and employee awards, gifts and dinners.

"The Commission finds no relationship between these expenses and the delivery of utility service," the PSC said. "They provide limited, if any, benefit to ratepayers."

“In a period of economic hardship when the public expects governmental officials to manage public funds frugally, these expenditures have the potential to engender public cynicism and distrust, to erode public support for the water district, and to create a more difficult environment for the governmental body to perform its mission,” the PSC said.

The PSC also cited previous opinions from the Kentucky Office of Attorney General that held that a water district is restricted in how it may expend funds and that donations fall outside the permitted uses.

In light of both its own precedents and formal Attorney General’s opinions, the PSC disallowed the questionable expenses and strongly cautioned Northern Kentucky Water “to refrain from such expenditures in the future.”

Northern Kentucky Water bills most of its customers on a quarterly basis. The PSC has encouraged utilities to bill on a monthly basis, in order to allow customers to better track usage, detect discrepancies that might indicate problems such as leaks, and ease budgeting, thus preventing billing disputes, late payments and disconnections.

The PSC noted that it has authorized Northern Kentucky Water to invest in meters that can be read automatically, which would enable monthly billing. The PSC ordered Northern Kentucky Water to make periodic progress reports on its transition to monthly billing and, if that transition is not completed by the time it next files for a rate adjustment, to expressly explain why it cannot bill all its customers on a monthly basis.

The PSC also noted that Northern Kentucky Water’s rate structure includes a declining cost as usage increases, which generally does not promote water conservation. If this rate structure is retained in future rate applications, Northern Kentucky Water will be asked to justify why it should be continued, the PSC said.

Today’s order and related documents are available on the PSC website, psc.ky.gov, by going to this location: http://psc.ky.gov/efs/EFS_Search.aspx, and entering case number 2010-00094. Videos of the hearing and public meeting also may be viewed on the website.

The PSC is an independent agency attached for administrative purposes to the Energy and Environment Cabinet. It regulates more than 1,500 gas, water, sewer, electric and telecommunication utilities operating in Kentucky and has approximately 100 employees.