

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

THE PROPOSED MERGER OF THE MCKINNEY)
WATER DISTRICT AND THE MCKINNEY)
WATER ASSOCIATION, LINCOLN COUNTY,) CASE NO. 8974
KENTUCKY)

ORDER

On December 6, 1983, the Commission received a letter from Earl Butcher, Judge/Executive, Lincoln County, Kentucky, requesting that the Commission investigate the advisability of a merger of the McKinney Water District and the McKinney Water Association. Pursuant to KRS 74.361(2), the Commission has prepared a feasibility report regarding a merger (Appendix A).

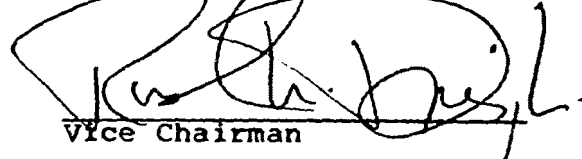
The Commission, having considered the report and being advised, is of the opinion and finds that it may propose that a merger of the McKinney Water Association be accomplished.

IT IS THEREFORE ORDERED That this matter be and it hereby is set for hearing on May 9, 1984, at 10:00 a.m., Eastern Daylight Time, in the Commission's offices at Frankfort, Kentucky, for the purpose of considering the proposed merger.

Done at Frankfort, Kentucky, this 9th day of April, 1984.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary

R E P O R T

TO: Claude G. Rhorer, Jr., Director
Division of Utility Engineering and Services *CR*

THRU: Byrnes C. Fairchild, Chief Engineer
Water and Sewage Section *BCF*

FROM: Robert N. Arnett *Robert N. Arnett*
Public Service Engineer
Water and Sewage Section

SUBJECT: The Merger of the McKinney Water District
and the McKinney Water Association

DATE: March 27, 1984

INTRODUCTION

On November 29, 1983, the Public Service Commission received a request from Lincoln County Judge/Executive Earl Butcher for a study to be conducted into the feasibility of merging the McKinney Water District ("District") and the McKinney Water Association ("Association"). The Public Service Commission is, by KRS 74.361, "authorized and empowered to initiate, carry out, and complete investigations, inquiries, and studies as may be reasonably necessary to determine the advisability as to the merger of water districts." KRS 74.361 further outlines the procedure to be followed in order to accomplish the merger of water districts (and water associations) by the Public Service Commission. A merger proposed by the Public Service Commission is required to be based on a written report and study. In addition, a formal hearing before the Public Service Commission must be held

on the subject of such proposed merger. At the conclusion of such proceedings the Commission enters an order, either merging the water districts into a single district, or abandoning the merger proposal. This report is the initial step required by KRS 74.361.

DESCRIPTION OF WATER UTILITIES

The District was created in 1964 or 1965 by order of the Lincoln County Court under the provisions of KRS 74. However, due to boundary problems the District was re-created by order of the Lincoln County Court on September 28, 1965. These actions by county courts did not require approval of the Public Service Commission prior to 1966. The Lincoln County Court order delineated the boundaries as that portion of Lincoln County southwest of the City of Stanford to McKinney (See Figure 1 attached). The communities served include McKinney, Geneva, and Turnersville. A certificate of public convenience and necessity for construction of a \$168,000 water system project was granted by the Commission's Order entered November 23, 1965, in Case No. 4563. This project included a 99,000 gallon standpipe and some 9 miles of pipelines (See Figure 1). Water service began in August 1966. The District purchases water from the City of Stanford and currently serves about 271 customers.

The Association, was incorporated under the provisions of KRS 273. A certificate of public convenience and necessity for construction of its \$230,800 initial water system project was granted by the Commission's Order entered January 23, 1973, in Case No. 5772. Water service began in June, 1974. The

communities served include Mt. Salem, New Salem, South Fork, Boneyville and Rowland. Certificates of public convenience and necessity for two additional construction projects were granted by Commission Orders entered April 15, 1974, and December 28, 1978, in Case No.'s 5996 and 7311 respectively. The project costs for the 1974 and 1978 projects were about \$148,500 and \$345,000 respectively. The present water system includes a 100,000-gallon standpipe and some 34 miles of pipeline (See Figure 1). The Association purchases water from the District, the Eubank Water System and the City of Stanford and currently serves about 566 customers.

ANALYSIS OF MERGER FEASIBILITY

In 1972, the general assembly of the Commonwealth of Kentucky enacted as a legislative finding of fact that the reduction of the number of operating water districts in the Commonwealth was in the public interest. The legislature further stated that the merger of such districts would tend to eliminate wasteful duplication of costs and efforts, result in a sounder and more businesslike degree of management, and would ultimately result in greater economies, less cost, and a higher degree of service to the general public. KRS 74.361 declares that the public policy favors the merger of water districts whenever feasible. This same theme was also expressed by the Bluegrass Area Development District in its 1973 Comprehensive Water and Sewer Plan for the bluegrass area. This plan recommends that water districts that would serve only a small number of people or

that would be of restricted geographical extent not be established in the future. It also states that whenever possible, existing water districts should be combined for increased efficiency of operation. This plan also states: (1) that the distribution system of the Association should have been constructed as extensions to the District, and (2) that "Once construction of the project (the Association project) is complete, the Association should be merged with the District."

Increased operational efficiency and the elimination of duplication of effort are among the obvious and immediate benefits of merging rural water utilities. Merger of the District and the Association would allow consolidation of the business activities for both utilities in one central location and thus eliminate the need for duplicate facilities, personnel and services. Merger would simplify the accounting activities, operation and work assignment of personnel to the day-to-day operation of each utility, and permit the more efficient use of all personnel. It would eliminate one of the two annual reports now made to the Public Service Commission, eliminate one of the two periodic audits now made and, as a result, would reduce expenditures for accounting services. The merged utility could also eliminate the duplication of expenses for legal, engineering and other professional services. The management of one merged utility could also be accomplished with fewer commissioners than for two separate utilities. The extent of actual monetary savings brought about by merger will depend on the merged utilities' method of operations (i.e. 1 office or 2 offices, 3 commissioners or 5 commissioners, 1

meter reader or 2 meter readers, 1 maintenance man or 2 maintenance men, etc.). The benefits of merger such as more responsive services, more efficient services and a reduction in the confusion about service areas would be significant benefits in themselves if the other potential benefits are not as significant as hoped for.

The existing 271 customers of the District, and the 566 customers of the Association would provide a more substantial customer base for the merged utility. The larger cash flow generated by the broadened customer count would afford a measure of financial stability to the operation of the merged utility. Such a moderately sized system would be better capable of meeting requirements for funds to meet the routine minor "emergencies" that plague operating water systems. In addition, a solid financial basis could facilitate the expansion of the district's water system and the extension of service to other areas of Lincoln County. Merger of the two utilities would eventually result in a more uniform rate structure among the various service areas as the total financial structure is realigned between the consolidated utilities. The District currently has a minimum monthly bill of \$9.00 for the first 1,000 gallons. The Association currently has a minimum monthly bill of \$9.80 for the first 1,000 gallons. The remainder of the rate schedules are not drastically different.

Merger of the District and the Association would enable more comprehensive planning of water facilities for the benefit of all citizens in this portion of the county.

KRS 74.361 provides that the outstanding obligations of a merged water district which are secured by a pledge of the income of the water system shall continue to be paid from such monies until such obligations have been retired. The District has a series of 5 percent private bearer bonds totaling \$168,000 which are scheduled to be retired in 2005. The American National Bank and Trust Co. of Chicago is the paying agent. The District is current on its repayment obligations and in CY 83 paid \$6,975 interest. It does not appear that the existing bond obligation of the District would present any problem to the formation of a merged district. The Association has a series of 5 percent bonds purchased by the Farmers Home Administration ("FmHA") totaling \$394,000. According to the FmHA, the Association - although current with its principle and interest payments - is technically in default on its bond ordinance because reserves required by the ordinance are not being maintained at the specified levels. The FmHA is willing to consider merger of the Association and the District, provided the rates of the merged utility can satisfy FmHA's bond ordinance requirements after coverage of debt service and operating expenses and provided that FmHA's bonds are placed on parity with the privately held bonds of the District. It is assumed that the concerns of the FmHA can be satisfactorily resolved should the merger be ordered by the Commission.

In October 1983, there were 145 operating water districts in the Commonwealth (along with 35 non-profit water associations) and an unknown number of established but non-operating water districts. In spite of the 1972 legislative mandate

there has been an actual increase in the total number of water districts and associations since 1972. In November 1972, there were 138 water districts (and 30 water associations) under Public Service Commission jurisdiction. True, there have been a handful of mergers and out-right purchases of districts, but more districts have also been established.

It would be unreasonable to expect that everyone will favor the merger of the District and the Association. Obviously some of the people with personal or vested interests in the existing utilities will be reluctant to accept a change in status. Water utility officials, employees, engineering consultants, attorneys, accountants, and others involved with the existing utilities can be expected to view the proposed merger with suspicion. Most of these individuals will probably express public agreement with the legislative finding that merger is in the public interest. Some of them, however, may also present detailed explanations as to why such a merger should be postponed until some future date. It is anticipated that the objections to merger formally raised by such groups or individuals can be adequately addressed by the Public Service Commission's order.

Possibly more critical to the prospect of a successful merger of the District and the Association will be the attitude of funding agencies. The federal agency primarily concerned with funding rural water systems is the Farmers Home Administration. Additional funding for specific programs is also available from the Department of Housing and Urban Development and the Appalachian Regional Commission. The Farmers Home Administration

funded the construction of the Association with grants of \$278,000 and 40 year loans of \$394,000. With such important financial considerations involved, FmHA has a substantial interest in any merger involving the Association. Federal funding agencies are generally in favor of consolidation of small water systems. However, due to the peculiarities of funding allocation procedures and general bureaucratic inertia, some funding agency personnel can be expected to favor a delay in merging the District and the Association.

CONCLUSIONS AND RECOMMENDATIONS

This report concludes, as did the General Assembly in 1972 and the Bluegrass Area Development District in 1973, that the merger of water districts is in the public interest. It was also determined that merger of the District and the Association is both feasible and advisable.

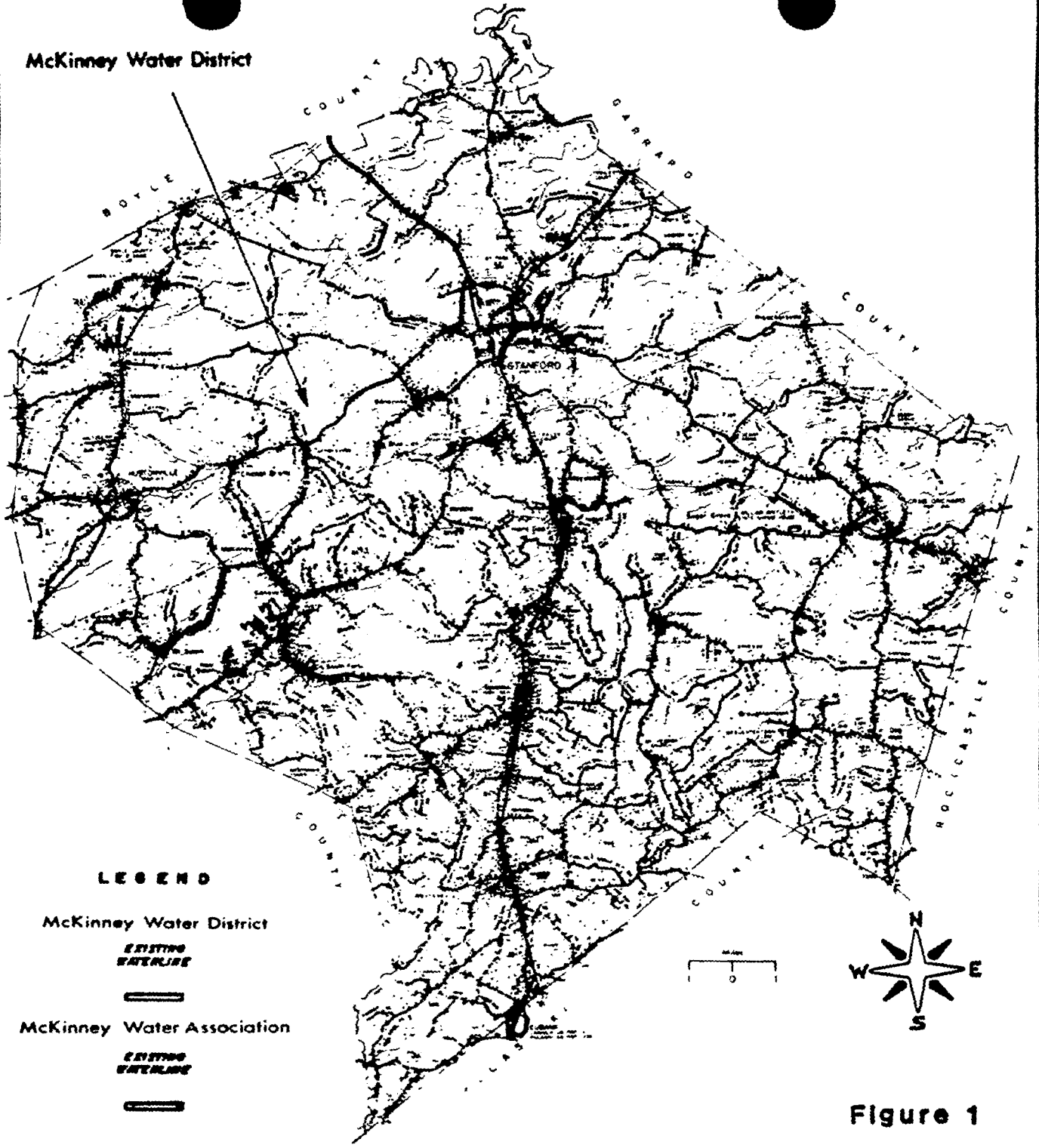
It is anticipated that there will be some local opposition to merger including a request from some parties that merger be delayed until a future date. This has occurred in the past. Nevertheless, this report concludes that the District and the Association should be merged.

This report should be entered into the record in this matter to meet the requirements of KRS 74.361 for a written report and study of those mergers proposed by this Commission.

A formal hearing on the proposed merger, as required by KRS 74.361 should be held in the near future.

RNA:jsb

McKinney Water District



LEGEND

- McKinney Water District
- EXISTING WATERLINE*
- McKinney Water Association
- EXISTING WATERLINE*

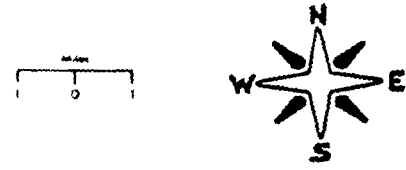


Figure 1

LINCOLN COUNTY
KENTUCKY