

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE NOTICE BY LAKE VILLAGE WATER)
ASSOCIATION, INC. OF A TARIFF AMENDMENT) CASE NO. 89-075
ADJUSTING RATES AND IMPOSING CONSTRUCTION)
SURCHARGE)

O R D E R

This matter arises upon petition for rehearing filed by Lake Village Water Association, Inc. ("Lake Village") on February 20, 1990 requesting the Commission reconsider its January 29, 1990 Order regarding the rate-making treatment of the cash deficit of Lake Village, the 1.2 x debt service coverage ("DSC"), allowable line loss of 15 percent; and that the Commission correct the Appendix to its January 29, 1990 order to reflect a surcharge amount of \$3.83 instead of \$3.38. For the reasons stated herein, the Commission denies Lake Village's request for rehearing on the cash deficit, 1.2 x DSC and allowable line loss issues and clarifies certain portions of its earlier Order. By separate Order entered this same date, the Commission addresses the mistake in the surcharge amount.

CASH DEFICIT

Lake Village has requested that it be allowed rates sufficient to reduce a cash deficit of approximately \$70,000. In its petition for rehearing Lake Village stated that the cash deficit was a direct result of the city of Danville's increases in

water rates to the association, a wholesale customer, and that regulatory lag in processing Lake Village's purchased water adjustments depleted cash reserves. The disallowance of line loss in excess of 15 percent, according to Lake Village may have also contributed to cash reserve depletion.

In the January 29, 1990 Order, Lake Village's request to recover past deficits from its current ratepayers was denied since to do so would constitute retroactive rate-making. In its petition for rehearing Lake Village argues that application of the "policy" against retroactive rate-making is inappropriate given Lake Village's circumstances. This Commission disagrees.

The principal that "rates are exclusively prospective in application and future rates may not be designed to recoup past losses" has been recognized by numerous courts to include the legislative rate-making function exercised by public utility commissions. Public Service Commission v. Diamond State Telephone, 468 A.2d 1285 (Del. Supr. 1983) citing Transcontinental & Western Air, Inc. v. Civil Aeronautics Board, 336 U.S. 601, 69 S.Ct. 756, 93 L.Ed. 911 (1949); Claridge Apartments Co. v. Commissioner of Internal Revenue, 323 U.S. 141, 65 S.Ct. 172, 89 L.Ed. 139 (1944); Los Angeles Gas & Electric Corp. v. Railroad Commission of California, 289 U.S. 287, 53 S.Ct. 637, 77 L.Ed. 1180 (1933). The U.S. Supreme Court has ruled that the clearest legislative mandate is needed to accord rate orders retroactive effect. Claridge, supra.

To allow Lake Village to recoup its past operating losses would clearly constitute retroactive rate-making. Furthermore, Lake Village has presented what it considers to be the causes of its cash deficit, but has failed to show the deficit exists and that it is not the result of an accounting or book loss. Thus, the Commission finds that Lake Village's request on this issue should be denied.

DEBT SERVICE COVERAGE

In its petition for rehearing, Lake Village argues that debt service coverage of 1.2x will not allow it to have sufficient revenues to meet its obligations and, thus, the Commission should reconsider its use. The debt service coverage of 1.2x is used to determine the reasonable revenue requirements for utilities with long-term indebtedness based upon a utility's operating expenses and debt requirements. The Commission has used a debt service coverage of 1.2x for Lake Village in the past¹ and determined that due to outstanding indebtedness owed to FmHA, found the methodology appropriate for Lake Village in the instant case.

Use of the 1.2 x DSC will result in a positive cash flow for Lake Village and sufficient revenues to meet its expenses on a

¹ Case No. 9290, The Notice by Lake Village Water Association, Inc. of a Tariff Amendment Adjusting Rates; Notice of Tariff Amendment Imposing a Temporary Special Rule to Limit the Availability of Water Service Connections; Application for a Certificate of Public Convenience and Necessity; Application for Authority to Issue a Promissory Note and Mortgage to the Farmers Home Administration; and Application and Request that it be Included in the Demonstration Project to Define Excessive Water Loss, Order issued December 30, 1985.

prospective basis. Therefore, the Commission finds that Lake Village's request for rehearing on this issue should be denied.

LINE LOSS

Lake Village requested that the Commission reconsider its disallowance of line loss in excess of 15 percent. Lake Village stated that the unwaivering application of the 15 percent limit violates its right to a fair hearing, to due process, and constitutes an arbitrary and capricious imposition of power on Lake Village.

The Commission's policy of limiting line loss in excess of 15 percent is not new to Lake Village. In its last rate case proceeding, Case No. 9290, Lake Village was placed on the Commission's line loss demonstration project and its purchased water was reduced to the 15 percent limit.

In this proceeding Lake Village was given every opportunity to present evidence as to why its line loss could not be reduced. In its supplemental response to the informal conference, filed October 27, 1989, Lake Village stated, that in the event a waiver of the line loss limitation cannot be had, then Lake Village requested to be included in the demonstration project. In lieu of the now defunct demonstration project, the Commission granted Lake Village a surcharge for the purpose of reducing its line loss and placed upon it the same restrictions and requirements of the demonstration project.


Based upon its second request to be included in the demonstration project, and its success in reducing line loss under

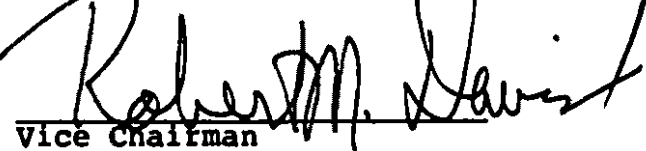
the initial demonstration project, Lake Village has shown that a reduction in its line loss is attainable. Therefore, the Commission finds that Lake Village's request for rehearing on this issue should be denied.

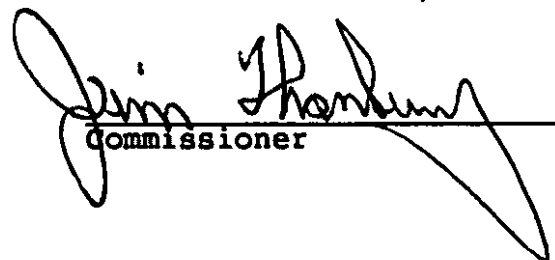
IT IS THEREFORE ORDERED that Lake Village's request for rehearing on the issues of the existing cash deficit, use of the 1.2 x DSC and the 15 percent line loss be and it hereby is denied.

Done at Frankfort, Kentucky, this 9th day of March, 1990.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director