

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF WEBSTER COUNTY)	
WATER DISTRICT (1) FOR A CERTIFICATE)	
OF PUBLIC CONVENIENCE AND NECESSITY)	
AUTHORIZING CONSTRUCTION OF MAJOR)	
ADDITIONS AND IMPROVEMENTS TO ITS)	CASE NO. 98-182
WATER SYSTEM; (2) SEEKING APPROVAL OF)	
REVISED WATER SERVICE RATES AND CHARGES;)	
AND (3) SEEKING APPROVAL OF THE ISSUANCE)	
OF CERTAIN SECURITIES, PURSUANT TO THE)	
PROVISIONS OF KRS 278.020, KRS 278.300, AND)	
807 KAR 5:001)	

O R D E R

Webster County Water District (Webster District) has applied to adjust its rates for water service to produce \$267,506 in additional revenues, an increase of approximately 24.6 percent over adjusted test year revenues. By this Order, the Commission grants the proposed adjustment and authorizes Webster District to execute a loan for \$4,571,429 with the Kentucky Infrastructure Authority (KIA) to finance the construction of certain waterworks improvement projects.

PROCEDURE

On June 4, 1998, Webster District applied for a Certificate of Public Convenience and Necessity to construct a \$6,289,680 waterworks improvement project, approval of financing, and for an adjustment to its water service rates.¹ By Order of August 7, 1998, the Commission granted a Certificate of Public Convenience and Necessity to Webster

¹ Webster District submitted its application on April 20, 1998. Because the application failed to conform to Administrative Regulation 807 KAR 5:001, Section 10, the Commission did not accept for filing. Webster District cured all filing deficiencies on June 4, 1998.

District to construct its proposed Raw Water Intake Structure.² By Order of October 13, 1998, the Commission granted a Certificate of Public Convenience and Necessity to Webster District to construct its proposed Raw Water Transmission Line and perform its Water Treatment Plant Expansion and Renovation.³

During the pendency of Webster District's application, Commission Staff performed a limited financial review of the water utility's operations for the 12-month period ending December 31, 1997. Upon completion of this review, Commission Staff prepared a report of its findings and recommendations. The Commission served a copy of this report on all parties and directed that the parties comment upon the report. Both Webster District and the Attorney General⁴ have submitted comments upon the report.

Following the issuance of the report and submission of comments, Webster District moved to amend its application to reflect changes in its plan of financing and to propose rates that conform to Commission Staff's revenue requirement recommendations. On March 29, 1999, the parties submitted stipulations in which they agreed upon a proposed rate structure. Both parties have waived their right to a hearing in this matter and request that the matter be submitted for decision based upon the existing record.

² The proposed Raw Water Intake Structure has an estimated cost of \$877,877.

³ Total estimated cost of these projects is \$6,289,680.

⁴ On June 3, 1998, the Commission granted the Attorney General's motion for intervention. He is only party who has formally intervened in these proceedings.

PROPOSED FINANCING

In its original application, Webster District sought Commission approval of the issuance of 4 million dollars of bond anticipation notes. Webster District intended to issue these notes in conjunction with its receipt of a 2 million dollar grant from the Local Government Economic Development Fund and use of \$289,680 in reserve funds to finance its proposed waterworks improvements. Webster District has since amended its application and now seeks authority to enter into a 30-year loan agreement with KIA for \$4,571,429 at an expected interest rate of 5.5 percent. All proceeds from this loan will be used to finance its approved waterworks improvement projects. The Attorney General supports Webster District's request for authorization.

REVENUE REQUIREMENTS

In its report, Commission Staff found that Webster District's annual operating expenses (including depreciation), based upon adjusted test year operations, were \$1,118,451. Commission Staff further found that, based upon debt service coverage requirements contained in Webster District's current and proposed debt instruments, a reasonable revenue requirement ranges from \$1,293,578 to \$1,734,237. This range reflects consideration of depreciation expense. Webster District's current and proposed debt instruments do not consider depreciation expense in the determination of minimum revenue requirements. Kentucky courts, however, have recognized the need for recovery of that expense. See, e.g., Public Service Commission v. Dewitt Water District, Ky., 720 S.W.2d 725 (1986).

In its amended application, Webster District proposes rates that will generate revenues of \$1,355,246. Webster District and the Attorney General stipulated that such

a revenue level is reasonable. In their stipulations, both appear to endorse Commission Staff's findings regarding a range of revenue which, given Webster District's adjusted test year operations, is reasonable.

Having considered the evidence of record, the Commission adopts Commission Staff's findings regarding Webster District's test year operations. We further find that, given Webster District's adjusted test year operations and its debt service obligations, a reasonable revenue requirement ranges from \$1,293,578 to \$1,734,237. Webster District's proposed adjustment falls within this range.

RATE DESIGN

Webster District's current retail rate design is a 4-step declining block schedule, with usage allowances of 2,000 gallons, 4,000 gallons, 94,000 gallons and an over 100,000 gallon increment. Webster District has a single wholesale rate. In its amended application, Webster District proposes to retain its existing declining block structure for retail customers, but to spread the proposed increase in a manner that would fall more heavily on larger users. It proposes to increase its wholesale rate by approximately 34.5 percent. The Attorney General supports this proposal and has stipulated that the proposed rate structure is reasonable.

As part of its limited review, Commission Staff prepared a cost-of-service study of Webster District's operations.⁵ This study revealed that the rates of lower usage customers are failing to produce sufficient revenues to cover the cost of service.

⁵ This study is the first performed in regard to Webster District. No cost-of-service study was used to develop Webster District's present rate structure.

Commission Staff recommended significant changes in Webster District's current rate structure to remedy this condition.

Webster District's proposed rates do not remedy the conditions that the cost-of-service study reveal. While Webster District and the Attorney General have accepted the study's conclusions regarding Webster District's wholesale rates, their proposed rates do not accurately reflect the cost of service. Webster District argues that the proposed rates will avoid rate shock and will not place an undue burden upon any customer class. It further argues that the proposed rates are a first step toward implementing cost-based rates.

While the Commission prefers rates that are cost-based, it will accept Webster District's proposed rates as a first step toward such rates. The Commission, however, believes that the proposed rate structure is reasonable only as an interim measure. The Commission places Webster District on notice that in its next rate case proceeding a cost-of-service study will be required and that additional changes to its rate structure should be expected.

CONCLUSION

Having considered the evidence of record and being otherwise sufficiently advised, the Commission finds that:

1. Webster District's adjusted operating revenues for the test year period (January 1, 1997 to December 31, 1997) are \$1,087,740.

2. Webster District's adjusted test year operating expenses are \$1,118,451. This amount includes depreciation on existing facilities and the proposed waterworks

improvement projects for which the Commission has issued a Certificate of Public Convenience.

3. A detailed breakdown of Webster District's adjusted test year operating revenues and operating expenses is set forth in Appendix A.

4. Rates that generate total annual revenues of \$1,293,578 would permit Webster District to meet its adjusted test year operating expenses (excluding depreciation expense) and the minimum debt service requirements of its existing and proposed long-term debt instruments.

5. Rates that generate total annual revenues of \$1,734,237 would permit Webster District to meet its adjusted test year operating expenses, including depreciation expense, and the minimum debt service requirements of its existing and proposed long-term debt instruments.

6. None of Webster District's current or proposed debt instruments require Webster District's rates to generate revenues in excess of its actual operating expenses, exclusive of depreciation expense, and the minimum debt service requirements of its existing and proposed long-term debt instruments.

7. Webster District's proposed rates, which are set forth in Appendix B, will produce annual revenues of \$1,355,246 based upon adjusted test year sales.

8. Webster District's proposed rates do not fully reflect the cost of providing water service to low usage customers, but represent a first step toward the establishment of cost-based rates for Webster District. To ensure an equitable and fair allocation of costs for all customers, additional changes to Webster District's rate design will be necessary in future rate case proceedings.

9. Webster District proposes to enter into a loan agreement with KIA in the principal amount not to exceed \$4,571,429 at an interest rate not to exceed 5.5 percent for the purpose of financing waterworks improvement projects. The Commission has granted a Certificate of Public Convenience and Necessity for the construction of these projects.

10. The proposed loan agreement with KIA is for the lawful objects within Webster District's corporate purposes, is necessary and appropriate for and consistent with the proper performance by Webster District of its service to the public, and will not impair its ability to perform that service.

IT IS THEREFORE ORDERED that:

1. Webster District's Motion to Amend Application is granted.
2. Webster District is authorized to enter into the proposed loan agreement with KIA in the principal amount not to exceed \$4,571,429 at an interest rate not to exceed 5.5 percent. The proceeds of this issuance shall be used only for the lawful purposes specified in Webster District's amended application.
3. The rates set forth in Appendix A are approved for service rendered by Webster District on and after the date of this Order.
4. Within 30 days of the date of this Order, Webster District shall file revised tariff sheets reflecting the rates approved herein.
5. Within 3 years of the date of this Order, Commission Staff shall perform a limited financial review of Webster District's operations, and prepare a written report of its findings and recommendations. This report shall include a cost-of-service study.

Upon completion of the report, Commission Staff shall serve Webster District and the Attorney General with a copy.

6. Webster District shall cooperate fully with Commission Staff in the performance of the limited financial review, to make available for inspection all books, accounts, papers and records, and to provide at its own expense any copies of such documents which the Commission Staff may reasonably require to perform the review.

7. All Commission Staff recommendations not specifically addressed herein are denied.

Nothing contained herein shall be deemed a warranty or finding of value of securities or financing authorized herein on the part of the Commonwealth of Kentucky or any agency thereof.

Done at Frankfort, Kentucky, this 1st day of April, 1999.

By the Commission

ATTEST:

Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 98-182 DATED APRIL 1, 1999

STAFF'S RECOMMENDED OPERATIONS

	Actual		Staff Adjusted
	Test Year		Test Year
	Operations	Adjustments	Operations
Operating Revenues:			
Retail Water Sales	\$ 823,551	\$ (1,095)	\$ 822,456
Sales for Resale	246,815	-	246,815
Other Operating Revenue	17,624	845	18,469
Total Operating Revenues	\$ 1,087,990	\$ (250)	\$ 1,087,740
Operating Expenses:			
Salaries & Wages - Employees	253,995	27,766	281,761
Salaries & Wages - Officers	12,000	-	12,000
Employee Pensions & Benefits	66,773	5,636	72,409
Purchased Power	78,414	-	78,414
Chemicals	70,386	-	70,386
Materials & Supplies	58,214	-	58,214
Contr. Svcs. - Accounting	8,300	-	8,300
Contr. Svcs. - Legal	6,129	(3,129)	3,000
Rental of Equipment	2,086	(2,086)	-
Transportation Expenses	10,711	-	10,711
Insurance - Gen'l Liability	13,561	7,717	21,278
Insurance - Worker's Comp.	8,000	(36)	7,964
Insurance - Other	432	-	432
Advertising Expense	766	(766)	-
Amort. - Rate Case Expense	-	3,333	3,333
Amort. - Non-Recurring Expenses	-	1,738	1,738
Regulatory Comm. Expense	-	1,989	1,989
Bad Debt Expense	580	-	580
Miscellaneous Expense	24,200	-	24,200
Total Oper. And Maint. Expenses	\$ 614,547	\$ 42,162	\$ 656,709
Depreciation Expense	257,637	183,022	440,659
Taxes Other Than Income	23,110	(2,027)	21,083
Total Operating Expenses	\$ 895,294	\$ 223,157	\$ 1,118,451
Net Operating Income	\$ 192,696	\$ (223,407)	\$ (30,711)
Other Income (Expense):			
Interest Income - Unrestricted	43,556	(43,556)	-
Income Available to Service Debt	\$ 236,252	\$ (266,963)	\$ (30,711)

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 98-182 DATED APRIL 1, 1999

The following rates and charges are prescribed for the customers in the area served by the Webster County Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of the Commission prior to the effective date of this Order.

MONTHLY RATES

First	2,000 Gallons	\$17.50	Minimum Bill
Next	4,000 Gallons	7.95	Per 1,000 Gallons
Next	94,000 Gallons	6.95	Per 1,000 Gallons
Over	100,000 Gallons	4.19	Per 1,000 Gallons
Wholesale Rate		\$3.70	Per 1,000 Gallons