

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF HARDIN COUNTY WATER)	
DISTRICT NO. 1 FOR (1) ISSUANCE OF)	
CERTIFICATE OF PUBLIC CONVENIENCE AND)	
NECESSITY; (2) AUTHORIZATION TO BORROW)	CASE NO. 2001-211
FUNDS AND TO ISSUE ITS EVIDENCE OF)	
INDEBTEDNESS THEREFOR; (3) AUTHORITY TO)	
ADJUST RATES; AND (4) APPROVAL TO REVISE)	
AND ADJUST TARIFF)	

ORDER

Hardin County Water District No. 1 (Hardin District) has moved for authority to place its proposed rates into effect immediately while its application for rate adjustment is pending. Finding that Hardin District has failed to meet the statutory prerequisites for this relief, we deny the motion.

Hardin District is a water district organized pursuant to KRS Chapter 74. It provides retail water service to approximately 9,000 customers in Hardin and Meade counties and wholesale water service to the city of Vine Grove, Kentucky and Meade County Water District.

On October 16, 2001, Hardin District applied for a Certificate of Public Convenience and Necessity to construct \$4.6 million in water main extension projects, for authority to issue \$4.8 million in 20-year revenue bonds, and for an adjustment in its retail and wholesale rates. Hardin District proposed to place its proposed rates into effect on November 15, 2001. Finding that further investigation into the reasonableness

of the proposed rates was required, the Commission, on November 6, 2001, suspended the proposed rates for 5 months.

On November 20, 2001, Hardin District moved for authority to place its proposed rates into effect immediately. On December 10, 2001, the Commission held a hearing on this motion. Testifying at this hearing were: Jim Bruce, Hardin District's General Manager; Robert Cramer, a financial consultant; and Kevin J. Brian, a professional engineer.

Hardin District argues that its credit and operations will be materially damaged if the proposed rates are not immediately placed into effect. It projects that its operations for calendar year 2001 will suffer a loss of \$350,000. Hardin District states that its bond covenants require its net revenues to be equal to at least 1.2 times its average net annual debt service requirements. It projects its revenues for calendar year 2001 to be only 0.64 times its net annual debt service requirements. It is, therefore, technically in default on its bond covenants and will likely have its credit rating lowered by credit rating services. Such a rating, Hardin District argues, will likely increase its debt costs and limit its ability to access credit markets.

Mr. Bruce testified that Hardin District's operations were also suffering. The water district has cancelled several capital projects, limited employee travel, and postponed several customer service projects. It has also reduced its materials inventory to below normal levels. Mr. Bruce also testified that the water district has had severe cash flow problems, requiring extraordinary cash management efforts. These efforts and the delay expenditures have, Mr. Bruce testified, adversely affected employee morale.

KRS 278.190(2) permits the Commission to suspend the operation of a proposed rate schedule for a 5 months to hold a hearing and make a decision on the reasonableness of that schedule. It further provides that

if the commission, at any time, during the suspension period, finds that **the company's credit or operations will be materially impaired or damaged by the failure to permit the rates to become effective during the period**, the commission may, after any hearing or hearings, permit all or a portion of the rates to become effective under terms and conditions as the commission may, by order, prescribe.

Id. (emphasis added). Accordingly, a utility seeking to place its proposed rates in effect during the suspension period must demonstrate that the failure to place proposed rates into effect will materially impair or damage its credit or operations.

We find that continued suspension of the proposed rates will not materially impair Hardin District's credit. The damage created by the operating losses has already been done. Hardin District's witnesses concede that, even if the proposed rates were allowed to become effective, the water district would fall short of its debt service coverage requirements and would still be considered in default. Moreover, while a rate adjustment that permanently increases the water district's revenues is likely to allay the concerns of the bond rating agencies and restore the water district's standing, an interim increase subject to refund is not.

Hardin District witness Robert Cramer testified that the timing of a final decision on the proposed rates is the crucial factor to Hardin District's credit rating. No default occurs until the issuance of an independent auditor's report of Hardin District's financial statements for calendar year 2001. Hardin District expects such a report to be issued in late March 2002. If permanent rates that restore Hardin District's net revenues to the

proper levels are in effect when the report is issued, Mr. Cramer testified, then the financial community's reaction to the audit results and the effect on Hardin District's credit rating should be minimal. We fully expect to issue a final Order in this proceeding no later than March 8, 2002.

The Commission further finds no evidence that the suspension will materially impair the water district's operations. While Hardin District is experiencing some cash flow problems, the record clearly shows the utility has the ability to remedy these problems without an interim rate adjustment. Hardin District currently has \$1.4 million in certificates of deposit that could be used as security for short-term financing to meet immediate cash needs. While subject to some financial penalty, it could also redeem those certificates to obtain needed cash.

The record also contains no evidence that the water district is currently experiencing any reductions in operations or quality of service. Hardin District has not eliminated any employee positions in the last 3 years. It has not reduced salaries or wages. In fact, in January 2001, it implemented a new benefit program for its employees. While some maintenance programs have been reduced or improvements postponed, Hardin District acknowledges that no tangible reduction in services has occurred.

In light of Hardin District's failure to demonstrate that its credit or operations will be materially affected by the continued suspension of the proposed rates, the Commission finds that Hardin District's motion should be denied. While we recognize that Hardin District's current financial condition limits its flexibility and presents some

challenges to management, it does not justify the immediate imposition of the proposed rates.

Hardin District officials must recognize their responsibility for the water district's present financial conditions. Hardin District officials concede that its current financial condition stems from the loss of Hardin County Water District No. 2 (District No. 2) as a wholesale customer. The record indicates that Hardin District officials have known since 1991 that District No. 2 would cease purchasing water from the water district in 2001. Despite this knowledge, they did not act to adjust rates until District No. 2's departure. This failure to act in a timely manner is the principal cause of Hardin District's current condition.

IT IS THEREFORE ORDERED that Hardin District's motion for authority to place its proposed rates into effect immediately is denied.

Done at Frankfort, Kentucky, this 14th day of January, 2002.

By the Commission

ATTEST:


Executive Director