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May 22, 2006

RE: Case No. 2006-00191

We enclose one attested copy of the Commission's Order in the above case.

Sincerely,

A handwritten signature in black ink, appearing to read "Beth O'Donnell".

Beth O'Donnell  
Executive Director

BOD/jc  
Enclosure

Honorable D. Berry Baxter  
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COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

EXAMINATION OF THE OPERATION AND )  
REASONABLENESS OF THE OFFSETTING ) CASE NO. 2006-00191  
IMPROVEMENT CHARGE OF HENRY COUNTY )  
WATER DISTRICT NO. 2 )

ORDER

On July 22, 2002, the Commission authorized Henry County Water District No. 2 ("Henry District") to assess an Offsetting Improvement Charge to any customer who connects to its water distribution system or to any real estate subdivision developer that proposes a real estate development and seeks certification from the water district for water service to the proposed development.<sup>1</sup> Noting that the proposed charge presented a case of first impression, the Commission directed that the operation and reasonableness of the charge be reexamined after three years to determine if it should continue.

On August 11, 2005, Henry District advised the Commission of its intent to continue with the assessment of the Offsetting Improvement Charge pending completion of any Commission examination on the operation of this charge. Henry District further advised the Commission that, based upon its recalculation of the charge

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<sup>1</sup> Case No. 2001-00393, The Tariff Filing of Henry County Water District No. 2 to Add Tariff Language for an Offsetting Improvement Charge (Ky. P.S.C. July 22, 2002).

as required in the Commission's Order of July 22, 2002, the charge should be reduced to \$950 per gallon per minute peak flow.

Based upon the foregoing, the Commission finds that:

1. A proceeding should be initiated to examine the operation and reasonableness of Henry District's Offsetting Improvement Charge.
2. During the pendency of this proceeding, Henry District should be permitted to continue to assess the Offsetting Improvement Charge subject to refund.
3. All parties to Case No. 2001-00393 should be made parties to this proceeding.
4. The record of Case No. 2001-00393 should be incorporated by reference into the record of this proceeding.

IT IS THEREFORE ORDERED that:

1. This proceeding is initiated to examine the operation and reasonableness of Henry District's Offsetting Improvement Charge.
2. The record of Case No. 2001-00393 is incorporated by reference into the record of this proceeding.
3. During the pendency of this proceeding, Henry District shall continue to assess the Offsetting Improvement Charge subject to refund.
4. Henry District shall for all Offsetting Improvement Charges assessed on and after the date of this Order, calculate the amount of the charge based upon \$950 per gallon per minute peak flow.
5. a. All interrogatories and requests for production of documents shall be appropriately indexed. All responses shall include the name of the witness who will

be responsible for responding to the questions related to the information provided, with copies to all parties of record and 6 copies to the Commission.

b. Each response shall be under oath or accompanied by a signed certification of the preparer or person supervising the preparation of the response on behalf of the entity that the response is true and accurate to the best of that person's knowledge, information, and belief formed after a reasonable inquiry.

c. A party shall make timely amendment to any prior response if it obtains information upon the basis of which it knows that the response was incorrect when made, or though correct when made is now incorrect in any material respect.

d. For any request to which a party refuses to furnish the requested information, the refusing party shall provide a written explanation of the specific grounds for its failure to furnish.

6. All parties to Case No. 2001-00393 are hereby made parties to this proceeding.

7. Any party filing documents with the Commission shall serve a copy of those documents upon all other parties.

8. Service of any document or pleading shall be made in accordance with Administrative Regulation 807 KAR 5:001, Section 3(7), and Kentucky Civil Rule 5.02.

9. Henry District shall, no later than June 9, 2006, file with the Commission the original and 6 copies of the information listed in Appendix A, with a copy to all parties of record. Each copy of the requested information shall be placed in a bound volume with each item tabbed. When a number of sheets are required for an item, each sheet should be appropriately indexed, for example, Item 1(a), Sheet 2 of 6. Henry


District's response shall conform to the requirements set forth in Paragraph 4 of this Order.

10. Nothing contained herein shall prevent the Commission from entering further Orders in this matter.

Done at Frankfort, Kentucky, this 22nd day of May, 2006.

By the Commission

ATTEST:



Executive Director

## APPENDIX A

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2006-00191 DATED May 22, 2006.

1. Provide the calculations and supporting information that Henry District used to determine that the Offsetting Improvement Charge should be reduced to \$950.
2. Explain why Henry District requested an extension of the Offsetting Improvement Charge in lieu of seeking a system surcharge as KRS 74.395 permits.
3. Henry District's existing Offsetting Improvement Charge rate schedule provides: "It is the policy of the District that development should pay to offset its hydraulic impact on the water distribution system, rather than such costs being paid by the District's customers." Explain why, in light of this policy statement, Henry District has not applied for authority to assess a system development charge in lieu of an extension of the Offsetting Improvement Charge.
4. Describe the actions that Henry District would take regarding its rates (e.g., application for a system development charge, general rate adjustment) if the Commission refuses to extend the time period in which the Offsetting Improvement Charge may be assessed.
5.
  - a. Provide Henry District's current long-term plan for the construction of water mains.
  - b. Provide all previous versions of this plan that were in effect at any time on or after July 22, 2002.
6.
  - a. List and describe the criteria Henry District uses to locate and upsize water mains.

b. Provide the policy statement, resolution or other documents that reflect that Henry District's Board of Commissioners has adopted these criteria.

7. a. List and describe all water main extension or upsizing projects that Henry District has currently planned. The description should include the estimated project cost and the source of funding for the project.

b. Rank the planned projects listed in the response to Item 7(a) in terms of the priority that Henry District has placed on them.

8. List and describe all water main extension projects conducted from July 22, 2002 through April 30, 2006 and financed through the proceeds of the Offsetting Improvement Charge. The description should include the project cost and the amount funded with Offsetting Improvement Charge proceeds.

9. Provide a schedule that lists all deposits and withdrawals from the escrow account which Henry District maintains for the Offsetting Improvement Charge proceeds. This schedule should also list for each deposit or withdrawal the date of the deposit or withdrawal, the amount, the source of the deposited funds (e.g., payee, number of lots, amount attributable to payee), the withdrawal's purpose, and the balance of funds remaining.

10. List and describe all known operating deficiencies in Henry District's water distribution system.

11. List and describe each complaint of inadequate water service that Henry District has received from its customers since July 22, 2002. Provide a copy of all written complaints.



12. State whether Henry District's present rates for general water service recover the full cost of providing water service including depreciation expense. Explain.

13. State whether Henry District agrees with the following statement: "General rates for water service should recover the cost of providing water service including depreciation expense associated with contributed and non-contributed property." Explain.

14. State whether Henry District agrees with the following statement: "The cost of normal wear and normal growth of system facilities should be funded through depreciation expense component of general rates." Explain.

15. For each project listed in Henry District's Response to Items 7(a) and 8, explain why the project is not an extension or replacement made necessary by normal wear or normal growth and should not be funded through general rates.

16. a. List and describe all water system improvement projects, including water main extensions, that Henry District constructed from January 1, 2002 through December 31, 2005 and funded through revenues from general rates.

b. Identify and describe the characteristics of the projects listed in Henry District's Response to Items 7(a) and 8 that distinguish those projects from those listed in Henry District's Response to Item 16(a).

17. State when Henry District expects to apply for a general rate adjustment.

18. Refer to Table I below which calculates the level of Henry District's depreciation expense funded through revenues. State whether Henry District agrees with the calculation that it has underfunded depreciation expense \$1,522,695. Explain.

TABLE I <sup>1</sup>				
	2004	2003	2002	Totals
Net Operating Income	\$ 343,413	\$ 319,638	\$ 454,370	\$ 1,117,421
Plus: Interest Income	<u>98,002</u>	<u>69,524</u>	<u>78,371</u>	<u>245,897</u>
Income Available to Service Debt	<u>\$ 441,415</u>	<u>\$ 389,162</u>	<u>\$ 532,741</u>	<u>\$ 1,363,318</u>
Principal <sup>2</sup>	\$ 298,508	\$ 285,508	\$ 228,008	\$812,024
Interest	<u>528,428</u>	<u>545,351</u>	<u>519,208</u>	<u>\$ 1,592,987</u>
Total Debt Payment	826,936	830,859	747,216	\$ 2,405,011
Times: 120 percent to gross-up for 20% debt coverage requirement	120%	120%	120%	120%
Total Debt Service	<u>\$ 992,323</u>	<u>\$ 997,031</u>	<u>\$ 896,659</u>	<u>\$ 2,886,013</u>
Difference in Income Available to Service Debt and Debt Service or Debt Service Funded Through Depreciation Expense	\$(550,908)	\$(607,869)	\$(363,918)	\$(1,522,695)
Reported Depreciation Expense	<u>771,042</u>	<u>684,409</u>	<u>616,873</u>	<u>\$ 2,072,324</u>
Depreciation Funded Through Revenues	<u>\$ 220,134</u>	<u>\$ 76,540</u>	<u>\$ 252,955</u>	<u>\$ 549,629</u>

19. In his Letter of July 14, 2005 to Thomas Dorman, Merle Brewer states that Henry District's Offsetting Improvement Charge had generated revenues of \$270,000 to date. State whether, in light of having net utility plant of \$15,697,727 as of December 31, 2004, Henry District regards this level of revenues as significant. Explain.

20. State for each year beginning with 1995, the number of customers that Henry District had as of December 31 of that year and the increase in the number of customers from the previous year.

<sup>1</sup> Unless otherwise noted, the information contained in Table I is from Henry District's Annual Reports to the Commission.

<sup>2</sup> The entries for calendar years 2003 and 2004 are based upon information from Henry District's Audit Reports.

21. For each year beginning with 1995, state the total amount of gallons of water sold during the year and the increase in the total amount of gallons sold over the previous year.

22. Provide all studies and reports that Henry District has prepared or commissioned that discuss or otherwise address the projected customer growth or demand in the water district's area.

23. In his letter of April 12, 2005 to Tom Green, Thomas Dorman on behalf of Commission Staff recommended that Henry District revise its Offsetting Improvements Charge rate schedule to provide for subdivisions made for agricultural purposes.

a. Describe the actions that Henry District has taken in response to this letter.

b. Describe Henry District's current policy toward the assessment of the Offsetting Improvements Charge for subdivisions of agricultural land.

24. Provide a copy of the minutes of each meeting of Henry District's Board of Commissioners since July 22, 2002 in which the Offsetting Improvements Charge has been discussed.