

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF HARDIN COUNTY WATER)
DISTRICT NO. 1 FOR APPROVAL OF A)
CONTRACT WITH THE UNITED STATES ARMY) CASE NO. 2011-00416
TO PROVIDE WATER SERVICE TO THE FORT)
KNOX MILITARY INSTALLATION)

ORDER

Hardin County Water District No. 1 ("Hardin District") has applied for a Certificate of Public Convenience and Necessity to acquire and operate certain water production and treatment facilities, to approve tariff revisions that implement the terms of a contract between the United States Government and Hardin District, and a deviation from 807 KAR 5:066 as it applies to the operation of the facilities in question.

Based upon our review of the record in this proceeding, the Commission finds that:

1. The United States Government ("Government") owns and operates water treatment and distribution facilities that serve the Fort Knox Military Installation and provide potable water to the city of Muldraugh and Hardin District.¹

¹ DESC Solicitation No. SP0600-08-R-0803, *Utility Privatization of the Potable Water System at Fort Knox, KY*, (July 1, 2008), Attachment J1 at 32, available at <https://www.fbo.gov/?tab=documents&tabmode=form&subtab=core&tabid=b23c90>. See also Case No. 97-388, *Application of Hardin County Water District No. 1 For a Certificate of Public Convenience and Necessity to Construct The Fort Knox Interconnect Project* (Ky. PSC Nov. 21, 1997) (setting forth the reasons for Hardin District to purchase water from the Fort Knox Military Installation).

2. The Fort Knox Military Installation is located in Bullitt, Hardin and Meade counties, Kentucky and covers approximately 109,000 acres.² It has an on-post resident population of 10,124³ and a daytime population of over 40,000 persons.⁴

3. The Fort Knox Military Installation's water production and treatment facilities consist of 13 groundwater wells, two raw water intake structures, a low-lift pump station, 48,700 linear feet of raw water main, two water treatment facilities, three clear wells, two high lift pump stations, one booster pump station, eight elevated storage tanks, and approximately 857,726 linear feet of distribution main.⁵

4. The Fort Knox Military Installation has two water treatment facilities: The Central Water Treatment Plant and the Muldraugh Water Treatment Plant. The Central Water Treatment Plant, which was constructed in 1936, has a treatment capacity of 3.5 million gallons per day ("MGD"). The Muldraugh Water Treatment Plant, which was constructed in 1941, has a treatment capacity of 7.0 MGD. Both facilities use a treatment process that includes aeration, flocculation, sedimentation, filtration and chlorination.⁶

² *Id.* at 3.

³ Kentucky State Data Center, Profiles of Kentucky's 422 Cities and 102 Census Designated Places at 173 (Mar. 21, 2011), available at http://ksdc.louisville.edu/census/2010QTprofiles_524places.pdf.

⁴ See <http://www.knox.army.mil>.

⁵ DESC Solicitation No. SP0600-08-R-0803, Attachment J1 at 5.

⁶ *Id.* at 8-9.

5. During the period from 2005 through 2010, the average water production of the Fort Knox Military Installation's water treatment facilities was 1,067,538,000 gallons annually, or 2.92 MGD.⁷

6. During the period from 2005 through 2010, the Government sold to Hardin District from these facilities an average of 40,208,908 gallons of water annually, or 110,161 gallons daily.⁸

7. During the period from 2005 through 2010, the Government sold to the city of Muldraugh an average of 86,026,523 gallons of water annually, or 235,689 gallons daily.⁹

8. In addition to the water distribution system connected to its water treatment facilities, the Government operates three small potable water distribution systems on the Fort Knox Military Installation that are connected to other water providers. A water distribution system consisting of approximately 45,509 linear feet of distribution main connects to the Louisville Water Company ("LWC"). A second water distribution system, which consists of 2,500 linear feet of distribution main, connects to Hardin County Water District No. 2. The third water distribution system, which consists of 384 linear feet of distribution main, connects to Meade County Water District.¹⁰

9. The Government currently meters only a small portion of the end users on Fort Knox Military Installation water distribution systems. Only 50 meters are presently

⁷ Hardin District's Response to Commission Staff's Request for Information, Item 8.

⁸ *Id.*

⁹ *Id.*

¹⁰ DESC Solicitation No. SP0600-08-R-0803, Attachment J1 at 11.

installed. Four of these meters measure the city of Muldraugh's wholesale purchases. Three meters measure Hardin District's wholesale purchases.¹¹

10. The water treatment and distribution systems are located entirely within the Fort Knox Military Installation.

11. All water end users on the Fort Knox Military Installation are Government entities or Government tenant activities.

12. Pursuant to 10 U.S.C. § 2688, the Defense Energy Support Center ("DESC") on July 1, 2008 issued a solicitation for proposals to privatize¹² the Fort Knox water treatment and distribution systems, and to provide utility services to the Government.

13. Hardin District is a water district organized pursuant to KRS Chapter 74.

14. Hardin District owns and operates facilities that produce and distribute water to the public in portions of Breckinridge, Hardin, and Meade counties, Kentucky.¹³ Its territory includes the incorporated area of Radcliff, Kentucky but does not include the Fort Knox Military Installation.¹⁴

¹¹ DESC Solicitation No. SP0600-08-R-0803, Attachment J1 at 33-34.

¹² The solicitation states: "The desired goal of this transaction is to transfer all right, title, and interest of the United States in and to the utility systems. Consequently, the United States will retain no reversionary interests in the utility system sold, other than the terms regarding re-purchase option and rights of access." DESC Solicitation No. SP0600-08-R-0803 at § B.2.3. See also Contract No. SP0600-11-8271 at § C.2.3.

¹³ *Annual Report of Hardin County Water District No. 1 to Public Service Commission for the Year Ended December 31, 2010* at 5.

¹⁴ While Hardin District states in its application that portions of the Fort Knox Military Installation are within its present territory, it indicated in its response to a Commission Staff inquiry that the military installation lies outside its territory. Application For Approval to Acquire the Fort Knox Potable Water System With Tariff Change at 1 (filed Oct. 13, 2011); Letter from David T. Wilson II, legal counsel for Hardin District, to Gerald Wuetcher, Executive Advisor, Kentucky Public Service Commission (Jan. 16, 2012) at 2-3.

15. As of December 31, 2010, Hardin District provided water service to 10,211 customers.¹⁵

16. For the calendar year ending December 31, 2010, Hardin District had total water operating revenues of \$4,142,492.¹⁶

17. In addition to retail water service, Hardin District provides wholesale water service to the cities of Vine Grove and Hardinsburg and to Hardin County Water District No. 2 and Meade County Water District.¹⁷ Hardin District does not provide wholesale water service to or have a wholesale water contract with the city of Muldraugh.

18. Hardin District's currently filed rate schedules do not distinguish between the sale of water to a wholesale customer and the mere transportation of another party's water to a wholesale customer.¹⁸

19. Hardin District submitted a proposal in response to DESC's solicitation for proposals and subsequently engaged in extensive negotiations with DESC.¹⁹ On September 30, 2011, Hardin District and DESC²⁰ executed Contract No. SP0600-11-8271 ("Contract") for Hardin District's acquisition of the Fort Knox Military Installation's

¹⁵ *Annual Report of Hardin County Water District No. 1* at 27.

¹⁶ *Id.*

¹⁷ *Annual Report of Hardin County Water District No. 1* at 30.

¹⁸ See Hardin County Water District Tariff, P.S.C.Ky. No. 1, Second Revision, Sheet No. 11 ("The wholesale rate shall apply to all water used and shall be based upon each 1,000 gallons used . . .").

¹⁹ Hardin District submitted four proposals to DESC. For each of these proposals, see Hardin District's Response to Commission Staff's Request for Information, Item 2.

²⁰ On July 19, 2010, DESC was renamed "Defense Logistics Agency Energy." See <http://www.desc.dla.mil/DCM/DCMPPage.asp?LinkID=DESHISTORY> (last visited Jan. 26, 2012). This name appears on the contract between the Government and Hardin District.

“potable water utility system”²¹ and its provision of “potable water utility services” to the Fort Knox Military Installation.²² The contract does not include the purchase of any water supply or the right to withdraw water from within the Fort Knox Military Installation.

20. Under the Contract’s terms, the Government transfers “all rights, title and interest” of its potable water utility system to Hardin District.²³

21. The proposed contract requires Hardin District to:

a. Furnish all facilities, labor, materials, tools, and equipment necessary to provide potable water utility service;

b. Be responsible for providing capital investments and all other resources required to own, maintain, and operate its utility system in a safe and reliable condition; and

c. Obtain and maintain all licenses, permits, or certifications necessary to own, maintain and operate the Fort Knox Military Installation potable water utility system.

22. The proposed contract provides that Hardin District will purchase the Fort Knox Military Installation potable water utility system for \$8,903,000, payable over a ten-year period at an annual interest rate of three percent per annum. In lieu of a lump sum payment, Hardin District will credit \$85,968 to the Government’s monthly bill for service for ten years following the purchase.²⁴

²¹ Contract No. SP0600-11-8271 at § B.2.2.

²² *Id.* at § C.2.1.

²³ *Id.* at § C.2.3.

²⁴ Contract No. SP0600-11-8271 at § B.2.2.1.

23. The Contract provides for Hardin District's assessment of the following charges and credits to the Government:

a. A one-time Transition Surcharge of \$592,518 assessed upon the conveyance of the Fort Knox Military Installation potable water utility system.

b. A Monthly Service Charge of \$246,172 to cover operation and maintenance expense and renewals and replacements.

c. A monthly Credit as Payment of Purchase Price of \$85,968 applied to monthly bills for ten years.

d. A Purchase Price Recovery Surcharge of \$85,968 assessed monthly for a period of ten years to compensate Hardin District for the purchase cost of the Fort Knox Military Installation potable water utility system.

e. An Initial System Deficiency Corrections Surcharge of \$473,831 assessed monthly for a period of five years to recover Hardin District's cost to correct system deficiencies identified in the Contract.

24. The Contract's charges are not volumetric based.

25. During the first year of the Contract, Hardin District derives revenues of \$9,232,554 from its operation of the Fort Knox Military Installation potable water utility system.²⁵

26. The Contract has a term of 50 years.²⁶

27. The Contract further provides that:

²⁵ Transition Charge (\$592,518) + Monthly Utility Service Charge (\$2,954,064) + Initial System Deficiency Charge (\$5,685,972) + Purchase Price Recovery Surcharge (\$1,031,616) - Credit For Payment of Purchase Price (\$1,031,616) = \$9,232,554.

²⁶ *Id.* at § F.1.

a. Hardin District will maintain separate records on its operation of the Fort Knox Military Installation potable water utility system. If Hardin District collects excess funds from its rates, it will maintain these excess funds in a separate account for future use on the Fort Knox Military Installation potable water utility system only.²⁷

b. Hardin District will perform over a five-year period repair, replacement and improvement projects totaling \$ 28,429,860.²⁸

c. Water commodity supply is not included in the contract. The Government retains ownership of all water withdrawn from its well fields.²⁹

d. Hardin District may use the Fort Knox Military Installation potable water utility system to serve or benefit areas outside the Fort Knox Military Installation only with the Government's consent. The Government may withhold its consent for any reason and may require compensation for the use of the system.³⁰

e. Hardin District is responsible for reading, maintaining, and calibrating all sub-meters on the Fort Knox Military Installation water distribution system. The Government intends to use these meters for internal installation billing purposes and for commodity management and energy conservation purposes.

f. If the Government and Hardin District agree, Hardin District may assess a fee for any new connecting facilities.³¹

²⁷ *Id.*

²⁸ *Id.* at § B.2.2.3. For a list of system deficiencies, see *id.* at § B.5.

²⁹ *Id.* at § C.3.5.

³⁰ *Id.* at § C.4.1.

³¹ *Id.* at § C.11.3.2.

g. Certain clauses contained in the Federal Acquisition Regulation are incorporated by reference into the contract.

28. Upon the transfer of ownership of the Fort Knox Military Installation potable water utility system to Hardin District, the Government will continue to issue monthly bills to Hardin District and the city of Muldraugh for water originating from the Fort Knox Military Installation.³²

29. Hardin District has entered into an agreement with LWC under which LWC will assume responsibility for the operation, maintenance, and repair of the Central Water Treatment Plant and the Muldraugh Water Treatment Plant, and certain pump stations, underground wells, and raw water transmission mains. Hardin District retains responsibility for all other functions of the Fort Knox Military Installation's potable water utility system, including all water distribution facilities.

30. The charges set forth in the Contract are based upon detailed and reasonable estimates of the cost of operating the Fort Knox Military Installation's potable water utility system.

31. Hardin District will not issue any securities or evidences of indebtedness or assume any financial obligation or liability as part of the proposed acquisition.

32. Hardin District's proposed tariff merely restates the provisions contained in the Contract.

33. Hardin District has requested a deviation from 807 KAR 5:066, Section 6(3), which limits a water utility's unaccounted-for water loss for ratemaking purposes to

³² Letter from David T. Wilson II, legal counsel for Hardin District, to Gerald Wuetcher, Executive Advisor, Kentucky Public Service Commission (Jan. 16, 2012) at 2-3; E-mail message from Kenny Muse, Chief, Operations & Maintenance, Directorate of Public Works, to Jim Bruce, General Manager, Hardin District (Oct. 19, 2011 10:48 AM).

15 percent. Due to the lack of meters at the end user, Hardin District argues, no calculation of unaccounted-for water loss is possible. It further argues that the use of a fixed fee contract for water service addresses recovery of costs associated with unaccounted-for water loss.

Based upon our review of the record in this proceeding, the Commission makes the following conclusions of law:

1. The Commission's jurisdiction extends "to all utilities in this state."³³
2. A utility is "any person except . . . a city, who owns, controls, operates, or manages any facility used or to be used in connection with . . . [t]he distributing or furnishing of water to or for the public, for compensation."³⁴
3. A water district is a public utility and is subject to Commission jurisdiction in the same manner and extent as any other utility.³⁵
4. Hardin District is a utility and is subject to Commission jurisdiction.
5. The Commonwealth of Kentucky has ceded "all rights and jurisdiction" over the Fort Knox Military Installation as long as the installation remains the property of the Government.³⁶
6. The Government's operation of water treatment and distribution facilities within the Fort Knox Military Installation's boundaries does not render it a "utility."³⁷

³³ KRS 278.040(2).

³⁴ KRS 278.010(3)(d).

³⁵ KRS 278.015.

³⁶ KRS 3.030.

³⁷ See *Brandenburg Tele. Co. v. South Central Bell Tele. Co.*, 506 S.W.2d 513, 517 (Ky. 1974) (holding that the Government's operation of a telephone system on the Fort Knox Military Installation did not constitute the operation of a public utility).

7. KRS 278.020(5)³⁸ and 278.020(6)³⁹ require prior Commission approval of the transfer of control or ownership of any “utility.” As the Government’s ownership and operation of water treatment and distribution facilities within the Fort Knox Military Installation’s boundaries does not place it within the statutory definition of “utility,” KRS 278.020 does not require Commission approval of Hardin District’s proposed acquisitions.⁴⁰

8. KRS 278.300(1) requires that a utility obtain Commission approval prior to the issuance of any securities or evidences of indebtedness or the assumption of any obligation or liability with respect to the securities or indebtedness of others. As Hardin District will not issue any securities or evidences of indebtedness or the assumption of

³⁸ No person shall acquire or transfer ownership of, or control, or the right to control, any utility under the jurisdiction of the commission by sale of assets, transfer of stock, or otherwise, or abandon the same, without prior approval by the commission. The commission shall grant its approval if the person acquiring the utility has the financial, technical, and managerial abilities to provide reasonable service.

³⁹ No individual, group, syndicate, general or limited partnership, association, corporation, joint stock company, trust, or other entity (an “acquirer”), whether or not organized under the laws of this state, shall acquire control, either directly or indirectly, of any utility furnishing utility service in this state, without having first obtained the approval of the commission. Any acquisition of control without prior authorization shall be void and of no effect. As used in this subsection, the term “control” means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a utility, whether through the ownership of voting securities, by effecting a change in the composition of the board of directors, by contract or otherwise.

⁴⁰ See Case No. 2004-00157, *Ohio County Water District's Acquisition of Rockport Water System* (Ky. PSC July 12, 2004) at 2; Case No. 2000-00357, *Application of Northern Kentucky Water District For Authorization to Acquire the Waterworks Distribution System of the City of Ludlow* (Ky. PSC July 20, 2000) at 2; Case No. 89-211, *Application of Kenton County Water District No. 1 (A) For Authority to Merge the City of Independence Water Distribution System As Provided By An Existing Contract; (B) For a Certificate of Public Convenience and Necessity to Operate the Merged System Under the Uniform Rates of the District; and (C) For Authority to Defeas the Remaining Bond Indebtedness of the City Water System in the Principal Amount of \$269,000 With Funds Held By the District*, (Ky. PSC Nov. 1, 1989) at 3-4.

any obligation or liability of others as part of its proposed acquisition, KRS 278.300 does not require Commission approval of the proposed acquisition.

9. No person may begin providing utility service to or for the public or construct any plant, equipment, property, or facility for furnishing utility service to the public without first obtaining a Certificate of Public Convenience and Necessity for the service or construction.⁴¹

10. As Hardin District is already providing water service and as it will not immediately be constructing any new facilities, KRS 278.020(1) does not require it to obtain a Certificate of Public Convenience and Necessity to complete the proposed transaction.

11. Pursuant to the Contract's terms, the Government has consented to the Commission's jurisdiction over the operation and rates of the Fort Knox Military Installation potable water utility system. To the extent that the Government has consented to such jurisdiction, the Commission may authorize and regulate the provision of water service within the Fort Knox Military Installation.⁴²

12. KRS 278.160(1) requires each utility to file with the Commission "all rates and conditions for service established by it and collected or enforced."

13. 807 KAR 5:011, Section 13, requires every utility to "file true copies of all special contracts entered into governing utility service which set out rates, charges or conditions of service not included in its general tariff."

⁴¹ KRS 278.020(1).

⁴² See *Brandenburg Tele. Co. v. South Central Bell Tele. Co.*, 506 S.W.2d 513 (1974).

14. As the Contract contains provisions related to rates and conditions of service under which Hardin District provides utility service, KRS 278.160 and 807 KAR 5:011, Section 13, require that the proposed contract be filed with the Commission.

15. The rates and charges set forth in the Contract are reasonable.

16. Where a conflict exists between Federal Acquisition Regulation clauses that are incorporated in the Contract and the rules and regulations that Hardin District has filed with the Commission, the Federal Acquisition Regulation clauses shall control.

17. As a result of the Contract, Hardin District will transport Government-owned water through the Fort Knox Military Installation water distribution system to the city of Muldraugh. As Hardin District's filed rate schedules do not provide for the provision of this service, KRS 278.160 requires Hardin District to revise its filed rate schedules to provide for such service.

18. KRS 278.160 further requires Hardin District to set forth in its filed rate schedules any connection fees that Hardin District may assess to the Government to connect new facilities to the Fort Knox Military Installation potable water utility system.

19. KRS 278.020(1) requires that Hardin District apply for a Certificate of Public Convenience and Necessity for each project that the Contract identifies as an "initial system deficiency correction" and that involves significant capital outlays.

20. As the Contract is filed with the Commission and as the proposed tariff sheets are duplicative of the Contract's provisions, the proposed tariff sheets related to Hardin District's service to the Government should be rejected.

21. Given the Commission's acceptance and approval of rates and charges contained in the proposed contract, Hardin District's request for a deviation from 807 KAR 5:066, Section 6(3), is moot at this time.

22. KRS 74.100 permits a water district to acquire a water system within its territory, but does not authorize it to acquire any existing systems outside its boundaries.⁴³ As the Fort Knox Military Installation, and hence its potable water utility system, appears to lie outside Hardin District's territorial boundaries, Hardin District must enlarge its territorial limits to include the Fort Knox Military Installation if its proposed acquisition is to be lawful.

23. The Commission retains the authority to adjust or modify the proposed rates for water service if those rates are found to be "unjust, unreasonable, insufficient, unjustly discriminatory or otherwise in violation of [KRS Chapter 278]."⁴⁴

24. "The primary duty of a public utility is to serve on reasonable terms all those who desire the service it renders."⁴⁵ Hardin District must provide water service to all persons who request such service and meet the requirements for such service as set forth in its filed rate schedules. The Government's refusal to agree to Hardin District's provision of such service is not *per se* an appropriate basis for refusal of service.

IT IS THEREFORE ORDERED that:

1. Hardin District's application for a Certificate of Public Convenience and Necessity is denied.

2. The provisions of the proposed contract related to Hardin District's rates and service are approved for service that Hardin District renders to the Government on and after February 1, 2012.

⁴³ See *Olson v. Preston St. Water Dist.*, 163 S.W.2d 307 (Ky. 1942).

⁴⁴ KRS 278.260; KRS 278.270.

⁴⁵ 64 Am. Jur. *Public Utilities* § 21 (2d ed. 2011). See also OAG 75-719 (a "water district is under an obligation to serve all inhabitants, including the subject applicant, within its geographical area of service as fixed under KRS 74.010 and as defined by the certificate of convenience and necessity").

3. Hardin District's proposed tariff sheets related to Hardin District's service to the Government are rejected.

4. Hardin District's request for a deviation from 807 KAR 5:066, Section 6(3) is denied.

5. Within 45 days of the date of this Order, Hardin District shall revise its filed rate schedules to reflect its provision of transportation service.

6. Hardin District shall advise the Commission in writing within 45 days of this Order of its efforts to extend its territorial limits to include the Fort Knox Military Installation or, in the alternative, provide documentary evidence that the Fort Knox Military Installation is presently within Hardin District's territorial limits.

7. If Hardin District must obtain revisions to its territorial limits, Hardin District shall file with the Commission, within five days of the entry of all Orders from the appropriate county judges/executive revising those territorial limits, a copy of such Order(s).

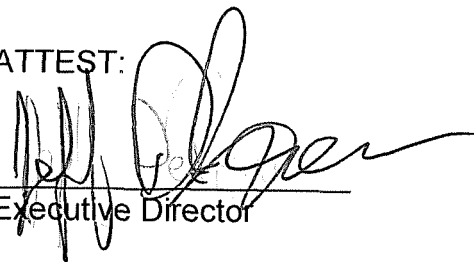
8. Hardin District shall maintain separate accounts for its operation of the Fort Knox Military Installation potable water utility.

9. Any documents filed with the Commission pursuant to Ordering paragraphs five and six of this Order shall reference this case number and shall be retained in the utility's general correspondence file.

By the Commission

ENTERED *PA*
JAN 27 2012
KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:



Executive Director

Case No. 2011-00416

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