

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

* * * * *

In the Matter of:

NOTICE OF ADJUSTMENT OF THE)
RATES OF KENTUCKY-AMERICAN) CASE NO. 8836
WATER COMPANY)

O R D E R

PETITION FOR REHEARING OF
SETTING RATES BASED ON CAPITAL STRUCTURE

On December 20, 1983, the Commission entered an Order granting Kentucky-American Water Company, Inc., ("Kentucky-American") \$704,343 in increased operating revenue. On January 6, 1984, the Attorney General and the Lexington-Fayette Urban County Government ("AG") filed a petition for rehearing requesting that the Commission reconsider its decision to set rates based on capital structure rather than net investment rate base. The AG contended that the decision to set rates based on capital structure was violative of past Commission Orders and was contrary to good rate-making principles. Specifically the AG stated that the Commission allowed Kentucky-American to earn a return on non-utility property by including inflated capital containing temporary cash investments of \$1,175,506. On January 18, 1984, Kentucky-American filed a response to the AG's petition asking the Commission to deny the AG's request for rehearing.

The Commission is of the opinion that further review and consideration of this issue is necessary and will grant the AG's petition. The Commission however is of the opinion that no formal hearing is necessary and will take the matter under advisement and will issue another Order in this matter at a future date.

PETITION FOR REHEARING OF FIRE PROTECTION SERVICES

On January 9, 1984, the Lexington-Fayette Urban County Government ("LFUCG") filed a petition for rehearing. It contends that the increase to fire service is unreasonable.

The petition recites several of the following facts: Kentucky-American proposed an overall increase in revenue of 17 percent but an increase to fire service of 53.6 percent. The LFUCG witness proposed only a 5.8 percent increase. At the time of the filing, the fire service rate was \$171.96 per year. Kentucky-American proposed a charge of \$264.12, LFUCG proposed \$181.98.

In its final Order, the Commission granted an overall increase of 5.3 percent, which was 31.3 percent of Kentucky-American's request. If the Commission would have followed Kentucky-American's proposal strictly, fire service would have been granted an increase of 16.8 percent. Instead, the Commission granted a 15.1 percent increase to fire service which resulted in a charge of \$198 per year.

In the final Order, the Commission raised objections with the cost-of-service methodologies of both Kentucky-American and LFUCG but indicated it would be more dependent upon the Kentucky-American study for the purposes of revenue allocation and rate

design but it would recognize its other rate-making objectives. Given these bounds, the Commission believes the rates established in its final Order are reasonable.

The LFUCG petition raises one other point. It requests an annual review procedure to determine the growth on the Kentucky-American system. The basis for this request is that Kentucky-American's cost-of-service method is a residual method and allocates to fire service all costs which cannot be directly assigned to general water service. There is some merit to LFUCG's claim but it can best be dealt with on an ongoing basis in rate proceedings and updating of Kentucky-American's study. The rate proceedings will also provide a better forum for other parties to present alternative cost allocation methodologies.

FINDINGS

The Commission, having considered the AG's and LFUCG's petitions and the evidence of record, is of the opinion and finds that the request for rehearing on the issue of setting rates based on capital should be granted, and that the request for rehearing on the issue of fire protection service should be denied. Further, LFUCG's request for an annual procedure to determine the growth on the Kentucky-American system should also be denied.

IT IS THEREFORE ORDERED that the AG's request for a rehearing on the issue of setting rates based on capital be and it hereby is granted.

IT IS FURTHER ORDERED that a formal hearing in this matter is not necessary and shall be denied.

IT IS FURTHER ORDERED that the Commission will issue another Order in this case at a future date.

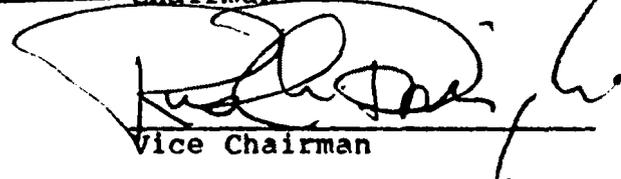
IT IS FURTHER ORDERED that LPUCG's request for a rehearing on the issue of fire protection service be and it hereby is denied.

IT IS FURTHER ORDERED that LPUCG's request for an annual procedure to determine the growth of the Kentucky-American system be and it hereby is denied.

Done at Frankfort, Kentucky, this 26th day of January, 1984.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary