

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

KENTUCKY PUBLIC SERVICE COMMISSION)	
)	
VS.)	CASE NO. 9478
)	
FLOYD COUNTY, KENTUCKY AND)	
EAST KENTUCKY UTILITIES)	

O R D E R

On July 10, 1986, the Commission ordered Floyd County Fiscal Court ("Floyd County") and East Kentucky Utilities ("EKU") to show cause why the Commission should not conclude that EKU's management of the gas system owned by Floyd County has not been adequate to operate a gas system in a safe and efficient manner; that a reliable, reasonably priced supply of gas to its customers is threatened; and further, why Floyd County should not terminate the operating lease with EKU.

A hearing was conducted on August 26, 1986. Kentucky-West Virginia Gas Company's ("Kentucky-West") motion to intervene was sustained by the Commission. Incorporated into this record by reference were Cases No. 9236, 9159, 9109, 8114 and 7561 by agreement of the parties.

WRITTEN RESPONSE BY EAST KENTUCKY UTILITIES

On August 26, 1986, EKU filed a response to the Show Cause Order. Exhibit G of EKU's response provides information relating

to a leak survey conducted on the Floyd County gas system in June and July 1985 by Heath Consultants. The results of the leak survey show that 160 "leak indicators" were found. EKU's response states that all the leaks were repaired, and many of the locations have since had new polyethylene pipe installed. Exhibit H of EKU's response states that 66,046 feet of polyethylene pipe has been installed through August 6, 1986, and 621 noncorrosive meter riser installations have been completed. Exhibit K of the response depicts the reduction in unaccounted-for gas on the gas system from 1981 through 1985, a 46.13 percent reduction which resulted in 14.83 percent unaccounted-for gas for 1985.

According to information in item (C) of the Summary of EKU's response, a regulator is installed at each customer installation. Each regulator has a range up to 125 pounds of pressure. Additionally, all regulator stations are checked regularly and are currently operating in a safe manner. Finally, in regard to the delinquent wholesale gas account, EKU asserts that the delinquency is due to insufficient rates and revenues from the sale of gas; that is, that its present rates will not generate enough funds to pay its delinquent purchased gas accounts.

COMMENTARY

The Commission recognizes the improvements that have occurred in the gas system during the past two years. In fact, the information EKU has presented to demonstrate its progress included excerpts from safety inspection reports prepared by the Commission's utility investigators. The Commission is also aware that the renovation accomplished through November 1985 was the result

in part of a Floyd County decision to use Bond Current Depreciation Funds, as recommended in Case No. 8114 and Case No. 9236, in the amount of \$72,795.¹ Based upon the evidence in the current proceeding, this appears to be the extent of Floyd County's participation in the activities of the gas system since the lease arrangement with EKU was initiated in 1979. The Commission concludes that a direct relationship exists between Floyd County's action and the subsequent reduction in line loss from 25.43 percent at the end of 1983 to 14.83 percent at year-end 1985.² The Commission further concludes that had Floyd County exercised greater responsibility as an owner of a gas distribution utility and provided more effective oversight of the management of its gas system by EKU, the financial and physical condition of the system would have been much different during 1980-1985.

However, Floyd County asserts that it is now willing to initiate whatever steps are necessary to ensure that the system's gas supply is not cut off. (Kentucky-West, the principal supplier, filed on September 4, 1986, with the Federal Energy Regulatory Commission for permission and approval to abandon sales and deliveries of natural gas to EKU.) Floyd County asserts that it will activate the Floyd County Utility Commission to supervise EKU's management of the gas system, to oversee the expenditure of bond money and monitor the operating expenses of EKU. The

¹ Letter to Commission from W. W. Burchett regarding Case No. 9405 and Case No. 9236, dated December 4, 1985.

² Exhibit K, EKU Response to Show Cause.

Commission notes, however, that although Floyd County offered to file a supplemental response within 14 days of the hearing outlining "acceptable programs to ensure the system's proper management and construction," none has been received. The Commission presumes that Floyd County has been waiting to review the disposition of this case, and that such a response will be filed following the issuance of this Order.

During the 1980-86 period, ECU requested higher rates and requested surcharges to raise money to renovate the gas system, apparently on the assumption that these are the only means by which funds can be made available for this purpose. The Commission disagrees with this conclusion. In the past the Commission has questioned the prudence of ECU's spending practices, given its need to renovate the system, and has pointed out that ECU has experienced "annual losses from operations equal to 21 percent of its gross assets, and current liabilities 47 times greater than net equity."³

It appears that Floyd County has reached a similar conclusion and has asked for an increase in rates which "are sufficient to support the issuance of a bond issue." The County Attorney stated that it was the County's position ". . . that a stopgap measure such as a surcharge is not preferable to a long range solution, such as a bond issuance which would eliminate the problem that has

³ Final Order, Case No. 9236, issued September 30, 1985, page 12.

caused the need for a surcharge."⁴ The Floyd County Judge-Executive, John Stumbo, further supported the bond issue alternative, stating that he agrees "to assist the utility to try to obtain funding through bonds. . .in order to correct the situation."⁵

In its motion to intervene filed on August 6, 1986, in Case No. 9545, Floyd County requested that the Commission enter an Order authorizing Floyd County to issue bonds on behalf of the system. The motion stated that the bonds were to retire ECU's currently outstanding bond indebtedness, pay all delinquent gas accounts, and upgrade the system to reduce line loss. However, the motion did not include information necessary for the Commission to adequately consider the request, per 807 KAR 5:001, Section 11, including: the amount, terms, rate of interest and how the bonds will be secured; nor did ECU amend its application requesting authority from the Commission to include this financing in Case No. 9545. The Commission issued its Final Order in Case No. 9545 on September 25, 1986, without disposing of Floyd County's motion. The Commission was not in a position to rule on the appropriateness of the proposal or to consider its potential effects on the operations of ECU, given the lack of information presented in the motion to have the bond financing considered for rate-making purposes.

⁴ Transcript of Evidence ("T.E."), August 26, 1986, page 13.

⁵ T.E., page 128.

FINDINGS AND ORDERS

After reviewing the record and being advised, the Commission is of the opinion and hereby finds that:

1. Floyd County is the owner of a gas utility distribution system under the jurisdiction of this Commission and its regulations. KRS 278.010(3).

2. Floyd County entered into a long-term lease with EKU to manage its gas system in 1979.

3. During the 1980-83 period, the physical condition of the system deteriorated, as evidenced by an increase in unaccounted-for gas.

4. During the 1984-86 period, improvements have been made on approximately 59 percent of the system as a direct result of intervention by Floyd County, and this portion of the system appears to meet the minimum safety requirements of the Commission's regulations.

5. Floyd County needs to assume a more active role in the operations of its gas system, particularly relating to the resolution of a delinquent bill with Kentucky-West and more effective oversight of EKU's management of the system and the remaining construction to be done by EKU.

6. Floyd County should contact Kentucky-West and develop a payment schedule to resolve the delinquent bill and to determine what other actions Kentucky-West requires to prevent the abandonment of gas service to EKU.

7. To demonstrate its concern about the delinquent bill with Kentucky-West, and to help maintain gas supplies from

Kentucky-West during the 1986-87 heating season, Floyd County should make a good faith payment towards the balance of the bill.

8. To demonstrate its desire to see its entire system meet the minimum safety requirements of the Commission's regulations as soon as practicable, Floyd County should purchase additional pipe, meter risers and associated equipment to allow EKU to continue its renovation program.

9. A bond issue by Floyd County on behalf of the gas system to retire EKU's current bond indebtedness, pay all delinquent gas accounts and upgrade the system to eliminate the current percent of unaccounted-for gas appears to be the most effective means to a long-term solution of EKU's financial and physical problems with the gas system.

10. If Floyd County demonstrates its concern for and responsibility of its gas system by arranging a payment schedule to resolve the delinquent bill with Kentucky-West and purchasing additional materials for EKU to continue construction, the Commission will look favorably upon a bond application submitted by Floyd County in compliance with 807 KAR 5:001, Section 11.

11. Floyd County needs to establish an independent board whose members will oversee all aspects of EKU's management of the gas system and submit all pertinent information regarding the establishment of the board, including the names of the board members, to the Commission for approval.

12. To the extent Floyd County pursues the actions dictated in this Order, the issue of EKU's management should be resolved; and termination of Floyd County's lease with EKU should be unnecessary.

IT IS THEREFORE ORDERED that:

1. Within 20 days of the date of this Order, Floyd County shall initiate contact with Kentucky-West to arrange a payment schedule to eliminate the delinquent bill, including an initial good faith payment towards the balance and determine what other action is required by Kentucky-West to continue its supplies of gas to EKU during the 1986-87 heating season.

2. Within 20 days of the date of this Order, Floyd County shall consult with EKU to determine what materials are required to continue renovation of the gas system; and Floyd County shall purchase for EKU enough pipe, meter risers and associated equipment, over and above what is presently on hand, to complete an additional 3 months construction and supply funds, if necessary, to allow construction through the current construction season.

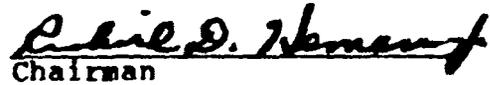
3. Pending performance of Floyd County's promised interim actions concerning resolution of the delinquent bill with Kentucky-West and Floyd County's purchase of additional materials to enable EKU to continue its renovation program, the Commission shall be inclined to favorably review an application for bond issuance which would retire EKU's current bond indebtedness, pay all delinquent gas accounts and upgrade the system to eliminate current line loss.

4. Any application submitted to the Commission requesting approval of a bond issuance shall be made in compliance with 807 KAR 5:001, Section 11.

5. Within 20 days of the date of this Order, Floyd County shall establish an independent board to oversee EKU's management and operation of the gas system and submit to the Commission for review and approval all pertinent information regarding the establishment of the board and selection of its proposed members.

Done at Frankfort, Kentucky, this 5th day of November, 1986.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Executive Director