

result of this failure, the wholesale rate may not accurately reflect the costs of the water district's transactions with Jeffersonville.

In its Order of October 2, 1997, the Commission ordered Montgomery District to submit certain information regarding its wholesale transactions with Jeffersonville. Following receipt of this information, the Commission established a procedural schedule and directed Commission Staff to submit written testimony. The Commission ordered Montgomery District and Jeffersonville to submit, no later than February 17, 1998, their objections to Commission Staff's position. It further ordered that, if neither party filed written objections to the Commission Staff's position, the procedural schedule would be vacated and the case would stand submitted for decision.

On February 6, 1998, Commission Staff filed written testimony in this matter. Neither party has filed objections to the Commission Staff position nor has it filed any other response to the Commission Staff testimony. Accordingly, the matter stands submitted for decision.

Discussion

Montgomery District, a water district organized pursuant to KRS Chapter 74, is a public utility subject to Commission jurisdiction. KRS 278.015. It owns and operates a water distribution system in Montgomery County, Kentucky which provides retail water service to 569 customers and wholesale water service to Jeffersonville. Montgomery District has no water production facilities and purchases its total water requirements from the City of Mount Sterling ("Mount Sterling").

In 1992 Montgomery District and Jeffersonville entered into a "Water Purchase Agreement" which provided for a "flow-through water arrangement." Under the terms of

this agreement, Jeffersonville agreed to pay all costs associated with upgrading an existing four-inch water line to an eight-inch water line. Jeffersonville further agreed to install a master meter and to pay the cost of meter testing on a dual metering station that has the ability to meter water from Jeffersonville to Montgomery District in emergency situations. The Agreement further provides that Montgomery District may charge Jeffersonville at the current Mount Sterling water rate plus a 5 cent per 1,000 gallon surcharge. The Agreement also requires Jeffersonville to pay one half of the costs associated with maintenance and repairs of the transmission line and in line pressure reducing valves. Finally, it requires the parties to review the surcharge every five years and "adjust upward as required based on demonstrative costs."

On April 2, 1996, Montgomery District applied for a rate adjustment to its retail service rates.² It did not propose any adjustment to its \$1.60 per 1,000 gallons wholesale rate to Jeffersonville. Commission Staff reviewed the proposed rate adjustment and, in its Staff Report on the application, recommended that changes be made to Montgomery District's wholesale rate. More specifically, Commission Staff recommended that the existing rate of \$1.60 per 1,000 gallons of water be increased to \$1.88 per 1,000 gallons, or approximately 18 percent.³ Commission Staff made this recommendation after a search of Commission records failed to reveal any contract

² Case No. 96-118, Application of the Montgomery County Water District No. 1 for an Adjustment of Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities (filed Apr. 2, 1996).

³ Staff Report on Case No. 96-118, June 20, 1996, at 6-7.

between Montgomery District and Jeffersonville.⁴ The lack of such contract or any other information to suggest a special relationship between the parties led Commission Staff to mistakenly conclude that Montgomery District was failing to allocate properly a portion of its increased costs to Jeffersonville. When no objections were made to Commission Staff's recommendations, the Commission on July 10, 1996 adopted the recommended rates.⁵

The existence of the Water Purchase Agreement undermines the premise upon which Montgomery District's current rates are based, namely that service to Jeffersonville creates the same costs as service to the water district's retail customers. In light of Jeffersonville's assumption of all costs associated with upgrading the eight-inch water line and one half the costs of maintaining and repairing that line, this premise is clearly false. The Commission finds that Jeffersonville should not have been required to bear

⁴ Under rules prescribed by the commission, each utility shall file with the commission, within such time and in such form as the commission designates, schedules showing all rates and conditions for service established by it and collected or enforced. The utility shall keep copies of its schedules open to public inspection under such rules as the commission prescribes.

KRS 278.160(1).

Special Contracts. Every utility shall 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. The provisions of this administrative regulation applicable to tariffs containing rates, rules and administrative regulations, and general agreements, shall also apply to the rates and schedules set out in said special contracts, so far as practicable.

807 KAR 5:011, Section 13.

⁵ Order of July 10, 1996 at 2.

a portion of Montgomery District's increased costs. The Commission further finds that the Water Purchase Agreement rate would permit Montgomery District to recover its full cost of serving Jeffersonville and should be the rate which Montgomery District charges Jeffersonville for wholesale water service.

To decrease Montgomery District's wholesale rate requires a corresponding adjustment to Montgomery District's remaining rates. In calendar year 1994, the historic test period used in Case No. 96-118 to establish Montgomery District's current rates, Jeffersonville purchased 32,793,000 gallons. At a rate of \$1.60 per 1,000 gallons, Jeffersonville would pay Montgomery District \$52,469. Based on a rate of \$1.88 per 1,000 gallons, Jeffersonville would be assessed \$61,651. If the wholesale rate is decreased, Montgomery District would experience a revenue decrease of \$9,183. Based on 1994 sales and using the revenue requirement found reasonable in Case No. 96-118, Montgomery District must increase its retail rates by approximately 5 percent to offset the reduction of its wholesale rate to \$1.60.

Summary

Having considered the evidence of record and being otherwise sufficiently advised, the Commission finds that:

1. Montgomery District's current wholesale service rate to Jeffersonville is based upon erroneous assumptions, fails to reflect Montgomery District's cost to provide water service to Jeffersonville, and is unreasonable.
2. Based upon Mount Sterling's current rate, Montgomery District's wholesale water service rate should be \$1.60 per 1,000 gallons.

3. To produce the revenue requirement found reasonable in Case No. 96-118, Montgomery District's retail rates must be increased by approximately 5 percent to offset the revenue reductions caused by a reduction in its wholesale water service rate.

4. The rates set forth in Appendix A to this Order will produce the revenue requirement found reasonable in Case No. 96-118 and are the fair, just and reasonable rates which Montgomery District should charge for water service provided on and after the date of this Order.

IT IS THEREFORE ORDERED that:

1. The procedural schedule set forth in the Commission's Order of February 2, 1998 is vacated.

2. The rates set forth in Appendix A to this Order are approved for water service rendered by Montgomery District on and after the date of this Order.

3. Within 30 days of the date of this Order, Montgomery District shall file with the Commission revised tariff sheets setting out the rates ordered herein.

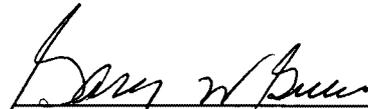
4. Within 30 days of the date of this Order, Montgomery District shall cause to be published notice of the rates ordered herein in a newspaper of general circulation within its service area.

Done at Frankfort, Kentucky, this 13th day of April, 1998.

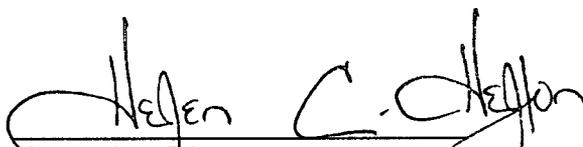
PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 97-400 DATED APRIL 13, 1998

The following rates and charges are prescribed for the customers in the area served by Montgomery County Water District No. 1. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

Retail Customers

First 2,000 Gallons	\$ 17.02 Minimum Bill
Next 3,000 Gallons	3.22 per 1,000 gallons
Next 5,000 Gallons	3.05 per 1,000 gallons
Over 10,000 Gallons	2.38 per 1,000 gallons

Wholesale Customers

City of Jeffersonville, Kentucky \$ 1.60 per 1,000 gallons