

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF NORTHERN KENTUCKY)	
WATER DISTRICT FOR (A) FOR AN)	
ADJUSTMENT OF RATES; (B) A CERTIFICATE)	CASE NO.
OF PUBLIC CONVENIENCE AND NECESSITY)	2003-00224
FOR IMPROVEMENTS TO WATER FACILITIES)	
IF NECESSARY; AND (C) ISSUANCE OF BONDS)	

O R D E R

On June 14, 2004, the Commission issued an Order in this proceeding authorizing Northern Kentucky Water District's ("Northern District") requested financing, a Certificate of Public Convenience and Necessity, and rates that will produce an annual increase in revenues from water sales of \$1,499,982. On July 1, 2004, Northern District moved for rehearing on the following issues: (1) Commissioner retirement benefits; and (2) Cost of service to the city of Florence ("Florence") and Boone County Water District ("Boone District"). On July 9, 2004, the Attorney General, the sole intervenor in the case, filed his response to the petition for rehearing. The Commission's findings on each of these issues are set forth below.

Commissioner Retirement Benefits

In its application, Northern District proposed to increase its test-period employee pensions and benefits expense of \$1,585,314 by \$121,030 to reflect a 7.6 percent

increase in health insurance costs.¹ At the hearing Ron Barrow testified that there was a further increase in Northern District's employee health insurance premiums in 2004.² To reflect the impact of the 2004 premium increase and the increase in the employer retirement contribution, Northern District revised its proposed adjustment to \$190,118 for a revised pro forma employee pensions and benefits expense level of \$1,896,462.³

Until the day of the hearing, Northern District had not proposed to adjust its employee pensions and benefits expense to reflect the increase in its retirement contribution rate; therefore, the detail showing Northern District's test-period retirement contributions per employee was not in the record. The record did indicate, however, that Northern District provides its Commissioners with the same health, life, and dental insurance benefits that it provides to its employees. Therefore, using the employee payroll schedule Northern District provided in response to a hearing request, the Commission included a retirement contribution for Northern District's Commissioners in the calculation of the unadjusted total of employee pensions and benefits expense of \$1,755,637. Finding that Northern District's Commissioners are part-time employees that are not entitled to receive employee benefits, those benefits were eliminated. In addition, capitalized overhead costs were removed to arrive at the Commission's pro forma level of employee pensions and benefits expense of \$1,685,436 as shown in the below table from the June 14, 2004 Order.

¹ Northern District's Application, Exhibit N, Schedule 2, Test-Year Operation and Maintenance Expense.

² Transcript of Evidence ("T.E.") for Hearing of February 10, 2004 at 44-45.

³ Northern District's Hearing Exhibit 2, Estimated Adjustments to Expenses for the Year 2004.

<u>Description</u>	<u>Health</u>	<u>Life & Dental</u>	<u>Retirement</u>	<u>Totals</u>
Unadjusted Totals	\$ 1,148,359	\$ 89,308	\$ 517,970	\$ 1,755,637
Less: Commissioners	20,331	1,780	1,320	23,431
Less: Capitalized (2.7%)	<u>- 30,457</u>	<u>- 2,363</u>	<u>- 13,950</u>	<u>- 46,770</u>
Totals	<u>\$ 1,097,571</u>	<u>\$ 85,165</u>	<u>\$ 502,700</u>	<u>\$ 1,685,436</u>

In its motion for rehearing, Northern District states that, because it does not provide retirement benefits to its Commissioners, the \$1,320 adjustment to remove those benefits is inappropriate. However, as noted above, the Commission erroneously included retirement benefits in its calculation of Northern District's retirement expense of \$517,970. Therefore, the adjustment to remove the benefits is appropriate and actually corrects the error in the Commission's calculation. The Commission finds that Northern District's request for rehearing on this issue should be denied.

Cost of Service to Florence and Boone District

On November 9, 2000, the Commission approved the Termination Agreement between Northern District, Florence, and Boone District.⁴ Thereafter, Florence and Boone District notified Northern District that they would cease purchasing water from Northern District in March 2003.⁵ In Case No. 2002-00105, the Commission approved Northern District's proposal to adjust its test-period revenues from wholesale water sales to reflect the loss of Florence and Boone District as wholesale customers. In addition, to reflect the decrease in expenses that would result from Florence and Boone

⁴ Case No. 2000-00206, An Investigation of Boone County Water District's Decision to Change Water Suppliers and of the Amendment of Water Supply Agreements between Northern Kentucky Water Service District and Boone County Water District and the City of Florence, Kentucky (November 9, 2000).

⁵ Case No. 2002-00105, Application of Northern Kentucky Water District for (A) an Adjustment of Rates; (B) a Certificate of Public Convenience and Necessity for Improvements to Water Facilities if Necessary; and (C) Issuance of Bonds (April 30, 2003), Brief of Northern District at 5.

District's departures, Northern District proposed, and the Commission approved, the elimination of test-period variable costs totaling \$1,091,120. The adjustment was based on Northern District's representations that the average variable cost to produce water at the Fort Thomas Treatment Plant was \$.40 per 1,000 gallons.⁶

In the present application, Northern District proposed to adjust its test-period revenues from wholesale water sales to reflect the loss of Florence and Boone District as wholesale customers, but failed to remove the expenses associated with those sales. When the Attorney General requested an explanation for the absence of such adjustment and the calculations and assumptions to determine the operating expense savings associated with the removed water sales, Northern District stated, "No adjustment to O&M are [sic] required. The actual cost of chemicals and electric have gone up during 2003 which is not reflected in the pro forma test year."⁷ Northern District submitted no further information or proposals to the Commission with regard to these operating expenses until the day of the hearing when it introduced an exhibit that purportedly reflects the current variable cost associated with producing water system-wide as \$0.1884 per ccf or \$0.252 per 1,000 gallons.⁸

⁶ Response to Item 6 of Commission Staff's First Set of Interrogatories and Requests for Production of Documents to Northern District issued July 29, 2002. "The District took the gallons purchased by City of Florence and Boone County Water District during 2001 . . . times the average variable cost to produce water at our Ft. Thomas Treatment Plant. The average cost per 1,000 gallons during 2001 was 40 cents. Purchased 2,727,797,300/1,000 *.40 = \$1,091,120."

⁷ First Request for Information of the Attorney General, Item 11(b).

⁸ T.E. at 60.

The Commission was not persuaded by Northern District's evidence and chose to use the variable cost found reasonable in Northern District's last rate proceeding. In its petition for rehearing, Northern District states that the factors used to calculate the variable cost of water have changed since the last rate case and thus the variable cost of water is different. Northern District asserts that it used the same methodology to calculate the variable cost of water in this case as it did in Case No. 2001-00105. Northern District argues that the Commission's decision is erroneous, is based on inaccurate test-period costs, and does not provide Northern District sufficient revenue to meet its needs. It further argues that the decision reflects a misunderstanding of the evidence presented and that Northern District should be given an opportunity to clarify the information.

The Attorney General, citing Commission precedent,⁹ argues that KRS 278.400 "requires parties to Commission proceedings to use reasonable diligence in the preparation and presentation of their case and serves to prevent piecemeal litigation of issues." He contends that Northern District did not act in a diligent manner and its late production of the information deprived the Attorney General and the Commission of a reasonable opportunity to review and analyze the evidence. He further asserts that Northern District has not demonstrated a need for rehearing.

KRS 278.400 states in part:

After a determination has been made by the commission in any hearing, any party to the proceedings may, within twenty (20) days after the service of the order, apply for a hearing with respect to any of the matters determined. . . . Upon the

⁹ Case No. 2000-00120, Adjustment of the Rates of Kentucky-American Water Company (Order dated February 26, 2001).

rehearing any party may offer additional evidence that could not with reasonable diligence have been offered on the former hearing. Upon the rehearing, the commission may change, modify, vacate or affirm its former orders, and make and enter such order as it deems necessary.

At all times during a rate proceeding, the applicant has the burden to prove that the adjustments proposed are reasonable. Northern District did not propose an adjustment to the variable cost associated with serving Florence and Boone District and, in fact, specifically asserted that no adjustment was necessary. Only under cross-examination at hearing did a Northern District witness suggest that an adjustment to the variable cost of production was necessary.

The Commission agrees with the Attorney General that Northern District's late proposal and introduction of evidence prohibited effective cross-examination. Furthermore, Northern District provided no explanation for the unavailability of this information earlier in the proceeding.

After having reviewed the motion for rehearing and the response thereto, the Commission finds that rehearing should be denied.

IT IS THEREFORE ORDERED that Northern District's motion for rehearing is denied.

Done at Frankfort, Kentucky, this 21st day of July, 2004.

By the Commission

ATTEST:



Executive Director

Case No. 2003-00224