

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF NORTHERN KENTUCKY)	
WATER DISTRICT FOR A CERTIFICATE OF)	
CONVENIENCE AND NECESSITY FOR THE)	CASE NO. 2007-00131
CONSTRUCTION OF SUBDISTRICT G)	
WATER MAIN EXTENSIONS, FINANCING)	
AND SURCHARGE)	

ORDER

Northern Kentucky Water District (“NKWD”) has applied for a Certificate of Public Convenience and Necessity to construct certain water main extensions within its proposed Subdistrict G and authority to assess a surcharge to all customers within that area. The Commission has previously issued a Certificate to NKWD. By this Order we authorize the formation of Subdistrict G and the assessment of the proposed surcharge.¹

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

1. NKWD, a water district organized under KRS Chapter 74, provides retail and wholesale water service to Boone, Campbell, Kenton, and Pendleton counties, Kentucky.

¹ On March 28, 2007, NKWD tendered its application for a Certificate of Public Convenience and Necessity and for authority to assess a surcharge. Because the application failed to conform to the requirements of 807 KAR 5:001, the Commission did not accept the application for filing. On June 21, 2007, after NKWD cured all deficiencies in its application, the Commission accepted the application for filing purposes. On June 26, 2007, the Commission granted NKWD’s application for a Certificate of Public Convenience and Necessity, but took no action on the request for a surcharge. On December 21, 2007, NKWD provided additional information regarding the proposed water main extensions in response to a request from Commission Staff and further waived its right to a hearing in this matter. No persons have sought to intervene in this matter.

2. NKWD proposes to create for administrative, financing, and rate-making purposes a subdistrict known as “Subdistrict G.”

3. Under NKWD’s proposal, Subdistrict G will consist of the following areas in Kenton County, Kentucky:

- a. Banklick Road, Bramlage Road, and Independence Road;
- b. Klein Road, Estate Lane, and Petty Road;
- c. Misty Lane, Pleasure Isle Drive, Bullock Pen Road, Cody Road,

Upton Drive, and Webster Road; and

- d. Fowler Creek Road, Sugar Camp Road, Lieberman Road, Wolf Road, and Hollyhock Road.

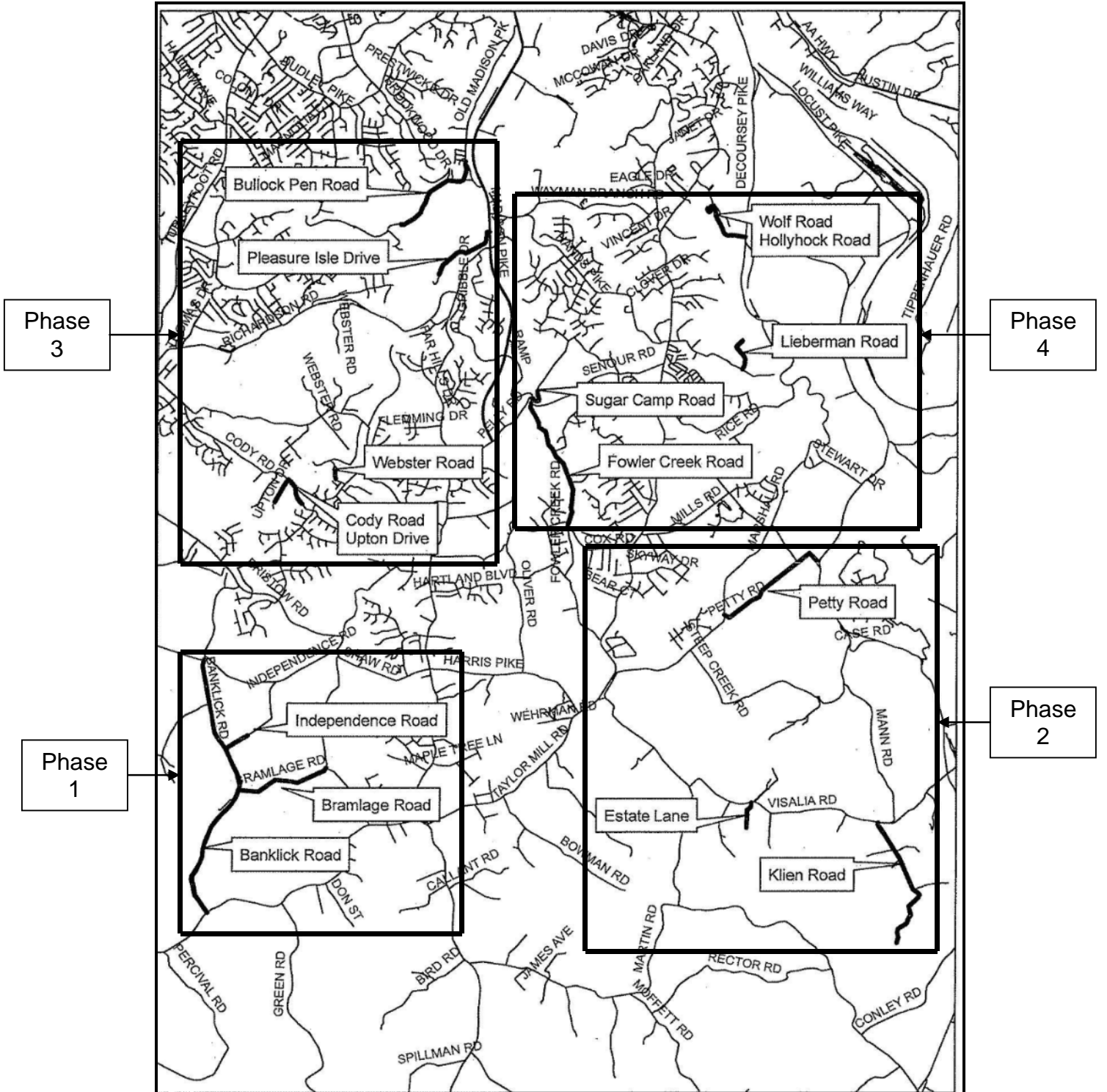
4. As reflected in Figure 1, the areas of the proposed Subdistrict G are not contiguous or otherwise share a common geographical characteristic.

5. NKWD proposed and has been issued a Certificate of Public Convenience and Necessity to construct approximately 14,520 linear feet of 24-inch water main; 5,658 linear feet of 12-inch water main; 33,548 linear feet of 8-inch water main; 1,511 linear feet of 6-inch water main; and related appurtenances within Subdistrict G to serve 243 additional customers. Approximately 123 of these customers have contracted for water service. The project has a possible customer density of 22.13 customers per mile.²

6. The total construction cost is approximately \$5,520,822.

² NKWD has provided conflicting accounts as to the number of potential households within the Subdistrict G area. At Exhibit A of its Application, it states that 258 households are located within the area. At Exhibit F, it lists 243 available customers are present in the area. In its response to Commission Staff’s request for information, it lists 243 households in the areas contained in Subdistrict G.

FIGURE 1
SUBDISTRICT G – KENTON COUNTY, KY



Source: Application, Exhibit C. The highlighted roads and streets within boxed areas represent the proposed Subdistrict G area.

7. The project is divided into four phases. The characteristics of each phase are set forth in Table I below.³

TABLE I

Phase	Cost	Customers		Main Extension		Cost Per Foot	Customers Per Mile
		Total Available	Contracting for Service	Miles	Feet		
1	\$ 1,702,292	60	36	3.83	20,222.40	\$84.18	15.66
2	\$ 627,102	61	32	1.97	10,401.60	\$60.29	30.96
3	\$ 902,435	63	34	2.63	13,886.40	\$64.99	23.95
4	\$ 1,306,178	59	21	2.55	13,464.00	\$97.01	23.13
Totals	\$ 4,538,007	243	123	10.98	57,974.40	\$78.28	22.13

8. NKWD determined the areas for inclusion in proposed Subdistrict G through an analysis of all unserved areas of Kenton County that are within its territory. While hydraulic conditions, the availability of sewer service, geotechnical factors, the location of existing water distribution facilities, and conditions of financial grants were considered, NKWD grouped areas for inclusion within the proposed subdistrict primarily on customer density.⁴

9. The selection of unserved areas with the highest customer density maximizes the number of households added, ensures the most effective use of limited funds from government grants, and reduces the level of the surcharge.

³ See NKWD Application at Exhibit F. NKWD's reported differing levels of available customers and contracting customers in its Application and its Response to Staff Request. At Exhibit A (Project Description), NKWD reports 123 contracting customers and 258 total households. At Exhibit F (Sources of Construction Funds), it reports 121 contracting customers and 243 total households. In its Response to Staff Request, NKWD reports 243 households along the segments that comprise Subdistrict G. The total number of contracting customers stated in Exhibit F appears to be the result of an error in addition.

⁴ NKWD included three segments of the proposed water main extension in Subdistrict G that had lower customer densities because of the need for hydraulic improvements in the general area to permit future extensions in unserved areas. It included four segments whose customer densities were below the average project density of 22.13 because of the availability of public sanitary sewers to structures along those segments. (Customer densities along these lines ranged from 15.78 to 20.69 customers per mile. See NKWD's Response to Staff Request and Waiver of Hearing (filed December 21, 2007).

10. The areas selected for inclusion in Subdistrict G have among the highest customer density of the unserved areas of Kenton County that are located in NKWD's territory.

11. No public or municipal utility currently provides water service to the proposed Subdistrict G.

12. NKWD funded the total construction cost from the following sources:

a. Appropriated funds from the Kentucky State Treasury and a grant from the Kentucky Infrastructure Authority collectively totaling \$3,000,000;

b. A grant of \$50,000 from the Kenton County Fiscal Court;

c. Proceeds of existing and future debt instruments of \$2,471,381.

13. NKWD has allocated the funds that it will use for the proposed project to various debt instruments in the following manner:⁵

a. \$750,000 from the proceeds of a previous debt issuance;

b. \$1,721,381 from the issuance of the 2007 bond anticipation notes.

14. Of the \$2,471,381 which NKWD is funding through debt instrument proceeds, NKWD has designated \$1,103,095 as a "hydraulic improvement contribution" that should be funded through general rates. This amount represents the difference in cost between using 12-inch water mains and 8-inch water mains on certain portions of the proposed construction. NKWD states that the benefits of the use of the larger size mains accrue to all water customers, not merely those customers within Subdistrict G.

15. Of the \$2,471,381 which NKWD is funding through debt instrument proceeds, NKWD has designated \$750,000 as an "extension contribution." This amount

⁵ See Case No. 2007-00135, Application of Northern Kentucky Water District for an Adjustment of Rates and Issuance of Bonds (Ky. PSC. filed May 29, 2007); NKWD Application, Exhibit O at 13.

represents the share of project costs that all NKWD customers will be funding through general service rates.

16. NKWD proposes that the remaining portion of the cost of the water main extension be apportioned to customers within Subdistrict G through a monthly surcharge not to exceed \$30. It estimates that such a surcharge will recover approximately \$618,286 of the extension's cost, exclusive of any interest on debt instruments issued to finance the proposed construction.

17. In its application NKWD does not state an interest rate upon which the proposed surcharge is based or state a period of time during which the surcharge will be assessed.

18. Were NKWD to extend service to persons residing in the proposed Subdistrict G under its present water main extension rules,⁶ each customer would be required to deposit \$9,945⁷ with NKWD. It is highly unlikely that NKWD would be required to refund this deposit.⁸

⁶ NKWD Tariff, PSC No. 2, Sheet No. 16.

⁷ \$5,521,381 (Total Cost of Project) - \$3,000,000 (State Appropriated Funding) - \$50,000 (Kenton County Grant) - \$1,103,095 (NKWD Hydraulic Contribution) = \$1,368,286 (Remaining Cost Subject to Customer Finance).

Average Cost of Water Main Extension = \$1,368,286 ÷ 57,974.40 feet = \$23.60 per foot.

NKWD's Required Contribution per Customer = 50 feet x \$23.60 = \$1,180.

NKWD's Total Required Contribution = 123 customers x \$1,180 = \$145,140.

Total Cost of Project Subject to Customer Deposit: \$1,368,286 - \$145,140 = \$1,223,146.

Required Customer Deposit = \$1,223,146 ÷ 123 customers = \$9,944.28.

Assuming that 243 customers contracted for service within the first 5 years of the date on which the water mains were placed into service, each customer would contribute \$4,450.80. The record does not indicate that all potential customers would request service within this period. Given that any obligation to contribute to the cost of the water main extension ends after 5 years, it is likely that many customers would defer applying for service until the end of the 5-year period to avoid making any contribution.

⁸ Supra, note 3.

19. Assuming the proposed surcharge is not revised during the proposed authorization period of 25 years, a customer located in Subdistrict G would pay a total of \$9,000 toward the surcharge.⁹

Based upon these findings, the Commission makes the following conclusions of law:

1. Where a subdistrict is created for rate-making purposes, the areas placed within that subdistrict should have some common characteristic or interest. The proponent of the subdistrict's creation bears the burden of demonstrating the reasonableness of the subdistrict's boundaries. At a minimum, it should demonstrate that the subdistrict's territories are served by common utility plant and facilities or share common geographic characteristics. Absent such demonstration, any rate that is based solely on a customer's location within the subdistrict's territory may be deemed unreasonable.¹⁰

2. The areas within the proposed Subdistrict G share a common characteristic – high customer population density – when compared to other unserved areas with Kenton County.

⁹ $\$30 \times 12 \text{ months per year} \times 25 \text{ years} = \$9,000$. Assuming an interest rate of 3 percent per annum, the present value of these payments is \$6,279.

¹⁰ Case No. 2000-00171, Application of Northern Kentucky Water Service District for a Certificate of Public Convenience and Necessity for the Construction of Sub-District D Water Main Extensions and Surcharge (Ky. PSC May 31, 2000) at 8.

3. The use of customer density as the distinguishing factor to develop a rate to recover the cost of water main extensions to unserved areas may be reasonable depending upon the circumstances of the extension.¹¹

4. KRS 278.040(3) and KRS 278.280(1) authorize the Commission to develop rules for the furnishing of utility service to the public.

5. Administrative Regulation 807 KAR 5:066, Section 11(1) and (2), establishes a methodology for water main distribution extensions. Administrative Regulation 807 KAR 5:066, Section 11(4), permits a water utility to develop arrangements for water distribution main extensions that differ from this methodology.

6. The proposed surcharge represents a different arrangement for making water distribution main extensions.

7. Under the circumstances NKWD has demonstrated that its formulation and calculation of the proposed surcharge results in a fair and reasonable rate and a reasonable alternative to existing methods of making water distribution main extensions.

8. NKWD's proposed plan of financing the water distribution main extension does not involve the immediate issuance of any long-term evidences of indebtedness and, therefore, does not require Commission authorization.¹² Prior to the issuance of any long-term evidences of indebtedness that will refund or retire any bond anticipation

¹¹ In any future proceeding in which NKWD applies for authority to assess a surcharge to finance a water distribution main extension to an unserved area, it should include in its application a listing of all unserved areas within its territory ranked according to customer density. Such listing should clearly indicate the unserved areas that are included in the proposed subdistrict and identify any special circumstances that supported inclusion of the unserved area in the proposed subdistrict (e.g., area located along a route needed to connect higher density areas; inclusion allows for hydraulic improvement for future extensions). NKWD should also clearly identify all other factors that were considered in its selection of the areas to be included in the proposed subdistrict and describe the effect of these factors on its decision.

¹² KRS 278.300(8).

notes used to finance the proposed construction, however, NKWD should seek Commission authorization for such action.

IT IS THEREFORE ORDERED that:

1. NKWD is authorized to assess each customer of Subdistrict G a monthly surcharge of \$30 subject to the conditions set forth in Ordering Paragraphs 2 through 10.

2. NKWD shall cease collection of the surcharge 25 years from the date of this Order or upon the billing of \$1,107,000¹³ to customers of Subdistrict G facilities, whichever occurs first.

3. NKWD shall identify the surcharge as a separate line item on its bills to Subdistrict G customers.

4. On April 1, 2009, and each year thereafter so long as NKWD assesses the surcharge, NKWD will adjust the surcharge level to reflect the number of Subdistrict G customers as of December 31 of the preceding year and the annual expected revenue of \$44,280.¹⁴ In no event, however, shall the level of the surcharge exceed \$30 per month.

5. Beginning in calendar year 2008, for the period from the date of this Order, and for each calendar year thereafter in which the surcharge is effective, NKWD shall submit with the annual financial and statistical report required by Administrative Regulation 807 KAR 5:006, Section 3(1), a written report stating:

¹³ This amount is based upon the assumption that Subdistrict G would serve an average of 123 households during the 25 years following the construction of the proposed water distribution mains. \$1,107,000 = 123 households x \$30 per month x 300 months.

¹⁴ \$44,280 = 123 households x \$30 per month x 12 months.

- a. The number of customers in Subdistrict G as of December 31 of the preceding year;
 - b. The total surcharge billed during the preceding calendar year;
 - c. The total surcharge billed since the date of this Order;
6. In its written report submitted for calendar year 2012, NKWD shall describe how Subdistrict G facilities have been integrated into NKWD's overall operations, shall list and describe the benefits, if any, that Subdistrict G facilities provide to non-Subdistrict G customers, and shall state whether further adjustments to the surcharge are necessary to reflect these benefits.¹⁵
7. NKWD shall for accounting purposes maintain separate accounts for the billing and collection of surcharge proceeds.
8. Within 20 days of the date of this Order, NKWD shall revise its filed rate schedules to contain the Subdistrict G surcharge and a description of the area that Subdistrict G comprises. At a minimum, this description shall include a map of the general area and a listing of all streets and roadways within Subdistrict G.
9. NKWD shall maintain a current description of Subdistrict G in its filed rate schedules so long as the Subdistrict G surcharge is effective.
10. All persons who receive water service through the Subdistrict G facilities or through water mains that are laterals to or extensions of those facilities and are not part of any NKWD subdistrict that is subsequently created, shall be considered within Subdistrict G and shall be assessed the surcharge.

¹⁵ The Commission reserves the right to periodically examine NKWD's use of subdistricts for the purpose of funding water main extensions and whether changing circumstances render the continued assessment of previously authorized surcharges reasonable. Such examination may be conducted in a separate proceeding initiated pursuant to KRS 278.260 or in a general rate adjustment proceeding that NKWD has initiated.

11. Within 60 days of the date of this Order, NKWD shall file with the Commission revised tariff sheets in which it sets forth its criteria and procedures for creation of a subdistrict to fund a water main extension. This filing shall also clearly explain the differences between the use of subdistricts to fund such extensions and the use of the practices currently set forth in Section XIV-C of NKWD's existing rate schedules.

Done at Frankfort, Kentucky, this 31st day of January, 2008.

By the Commission

ATTEST:

A handwritten signature in black ink, consisting of several overlapping loops and flourishes, positioned above a horizontal line.

Executive Director