

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF NORTH)	
MERCER WATER DISTRICT FOR A)	
CERTIFICATE OF PUBLIC CONVENIENCE)	
AND NECESSITY TO CONSTRUCT A SYSTEM)	CASE NO.
IMPROVEMENTS PROJECT AND AN ORDER)	2021-00317
APPROVING A CHANGE IN RATES AND)	
AUTHORIZING THE ISSUANCE OF)	
SECURITIES PURSUANT TO KRS 278.023)	

ORDER

On August 11, 2021, North Mercer Water District (North Mercer District) filed an application, pursuant to KRS 278.023, requesting a Certificate of Public Convenience and Necessity (CPCN) to construct water system improvements project, approval of the proposed plan of financing the project, and approval of the proposed rates in its application.¹

On August 13, 2021, North Mercer District filed a motion to expedite the final Order in this case. In support of this motion, North Mercer District stated that the water utility had been advised by the Bluegrass Area Development District officials that certain Community Development Block Grant (CDBG) funds are available through the Kentucky Department for Local Government to provide funding for projects that are ready to proceed. However, such funds must be spent prior to September 1, 2021, or be returned to the Department for Housing and Urban Development (HUD). North Mercer District

¹ Application at 3.

wishes to acquire these CDBG funds for cost overruns associated with the proposed project; therefore, North Mercer District requests a final Order on or before August 25, 2021. No party has sought intervention in this matter.

LEGAL STANDARD

North Mercer District has submitted its application pursuant to KRS 278.023. The Commission is required, pursuant to KRS 278.023, to accept agreements between water utilities and the United States Department of Agriculture Rural Development (USDA/RD) regarding construction projects, and to issue the necessary orders to implement the terms of such agreements no later than 30 days after filing the application with the Commission. KRS 278.023 does not grant the Commission any discretionary authority to modify or reject any portion of the agreement between the USDA/RD and North Mercer District or defer the issuance of all necessary orders to implement the terms of that agreement. It further denies the Commission any authority to reject an application when the evidence of record indicates that a water utility's proposed construction will result in the wasteful duplication of facilities, result in an excessive investment, or its proposed rates are unfair, unjust or unreasonable. As explained in KRS 278.023(1), the limits on the Commission's review are because federal financing of these projects entails prior review and oversight by a federal agency and obligates the utility to take certain actions; conflicting requirements between the federal agency and the Commission may jeopardize the project and place the utility in an untenable position. The Commission, therefore, is not able to review this application using the same standards that are used for applications that are not filed pursuant to KRS 278.023.

The legal standard established in KRS 278.023 requires that (1) the applicant be a water utility formed under KRS Chapter 74 or 273; and (2) the construction project must be funded in whole or in part under terms of an agreement between the water utility, USDA or United States HUD

BACKGROUND

North Mercer District, a water district organized under KRS Chapter 74, provides retail water service to approximately 4,606 water customers² in Anderson, Boyle, Mercer, and Washington counties, Kentucky.³ The Commission's Division of Inspections last inspected North Mercer District on November 12, 2020. Commission Staff noted one deficiency in a letter that it furnished to North Mercer District on November 30, 2020. North Mercer District responded to the deficiency wherein North Mercer District stated that its board of commissioners is aware of the increasing water loss over the past three years and began taking steps to correct the water loss issue in late 2018. North Mercer District continued stating that upon review of data on water loss and areas of breakage, the water district determined it would need to replace approximately 22 miles of aged water mains as well as the remaining asbestos cement pipe. The letter also notified the Commission that North Mercer District had applied for a grant to help with infrastructure project costs and had been approved for a loan with the USDA/RD for infrastructure improvements.

² *Annual Report of North Mercer Water District* for the Year Ended December 31, 2020 at 49.

³ *Id.*, at 12.

The Commission notes that North Mercer District reported a water loss of 18.81 percent in its 2020 Annual Report.⁴ Commission regulation 807 KAR 5:066(6)(3) states that, for ratemaking purposes, a utility's unaccounted-for water loss shall not exceed 15 percent of the total water produced and purchased, excluding water used by a utility in its own operations. At the proposed rates, reduction of North Mercer District's unaccounted-for water loss to 15 percent would result in an approximate \$37,590 decrease to its cost of water annually.⁵ The Commission also notes that at the proposed rates, North Mercer District's total cost of water loss is \$185,581 annually at the current 18.81 percent rate.⁶

⁴ *Annual Report of North Mercer Water District for the Year Ended December 31, 2020* at 57.

2020 Water Loss	18.81%
Less: 15% Allowable Water Loss	<u>-15.00%</u>
Water Loss in Excess of 15%	<u>3.81%</u>

	Purchased Water	Purchased Power	Total
	\$		
2020 Reported Expenses	958,329	\$ 28,279	\$ 986,608
Multiplied by: Water Loss in Excess	-3.81%	-3.81%	-3.81%
	\$		
Excess Purchased Water and Pumping Cost	<u>(36,512)</u>	<u>\$ (1,077)</u>	<u>\$ (37,590)</u>

	Purchased Water	Purchased Power	Total
	\$		
2020 Reported Expenses	958,329	\$ 28,279	\$ 986,608
Multiplied by: Water Loss in Excess	-18.81%	-18.81%	-18.81%
	\$		
Excess Purchased Water and Pumping Cost	<u>(180,262)</u>	<u>\$ (5,319)</u>	<u>\$ (185,581)</u>

The proposed project consists of the replacement of approximately 111,000 linear feet of problematic 3-, 4-, 6-, and 8-inch PVC and asbestos cement water mains and appurtenances as well as replacing approximately 460 existing service lines from the new mains to the existing meter.⁷ This proposed project is concentrated in the southwest and northern sections of Mercer County.⁸ The total estimated cost of the proposed project, including but not limited to development, legal expenses, engineering, construction, and contingencies, is \$3,400,000.⁹ North Mercer District proposes to finance the construction of the proposed project through the issuance of \$3,400,000 of its Water System Revenue Bonds as set out in the USDA/RD Letter of Conditions.¹⁰ North Mercer District has a commitment from USDA/RD to purchase the \$3,400,000 in bonds maturing over 40 years, at an interest rate not to exceed 1.875 percent per annum.¹¹ In addition, North Mercer District will submit for CDBG funds to cover any cost overruns associated with the proposed project.

The proposed rates contained in the application are the minimum rates and charges required under the agreement with USDA/RD.¹² North Mercer District's proposed rates meet the total revenue requirements recommended in the engineering

⁷ Application, Exhibit A, Project Description.

⁸ *Id.*

⁹ *Id.*, Exhibit B, RD Letter of Conditions and Form RD 1940-1 (Exhibit B) at 10.

¹⁰ Application at 1, paragraph 5.

¹¹ *Id.*, and Exhibit B, Request for Obligation of Funds.

¹² *Id.*, Exhibit B at 10.

reports. The monthly bill of an average residential water customer who uses 5,000 gallons will increase from \$48.98 to \$57.60, an increase of \$8.62, or 18 percent.¹³

DISCUSSION AND FINDINGS

Based upon the evidence of record, the Commission concludes that the KRS 278.023 legal standard to approve the proposed financing is met because North Mercer District is a water district formed by KRS Chapter 74 and the financing for the proposed project is being obtained through a federal agency, USDA/RD. Although the Commission's scope of review is limited, we note that North Mercer District appears to have been aware of the need for Commission review as of June 2, 2021. It also appears that North Mercer District may have relied upon its engineering firm for a legal determination on how to proceed. The Commission cautions the North Mercer District board that an engineering firm should not replace sound legal advice from the utility's counsel.

Although we approve the financing, the Commission has concerns regarding the financial condition of North Mercer District. Based on the information provided in the application, the Commission finds that this case should remain open to allow Commission Staff to monitor whether North Mercer District's proposed rates meet the total revenue requirements recommended in the engineering reports. To clarify this issue, North Mercer District should file on or before September 15, 2021, its responses to Staff's Request for Information, attached as Appendix B to this Order.

¹³ *Id.*, Exhibit E, Notice of Proposed Rate Charge.

IT IS THEREFORE ORDERED that:

1. North Mercer District is granted a CPCN for the proposed project as submitted.
2. North Mercer District's proposed plan of financing is approved.
3. North Mercer District is authorized to issue \$3,400,000 of its Water System Revenue Bonds in the amount of \$3,400,000 maturing over 40 years at an interest rate not to exceed 1.875 percent per annum.
4. The proceeds from the issuance of the Water System Revenue Bonds shall be used only for the purposes specified in North Mercer District's application.
5. North Mercer District shall obtain approval from the Commission prior to performing any additional construction not expressly authorized by this Order.
6. North Mercer District shall file with the Commission documentation of the total costs of this project, including the cost of construction and all other capitalized costs (e.g., engineering, legal, and administrative), within 60 days of the date that construction is substantially completed. Construction costs shall be classified into appropriate plant accounts in accordance with the Uniform System of Accounts for water utilities prescribed by the Commission.
7. North Mercer District shall file a copy of the "as-built" drawings and a certified statement from the engineer that the construction has been satisfactorily completed in accordance with the contract plans and specifications within 60 days of substantial completion of the construction certified herein.
8. North Mercer District shall require the construction to be inspected under the general supervision of a professional engineer with a Kentucky registration in civil or

mechanical engineering to ensure that the construction work is done in accordance with the contract drawings and specifications and in conformance with the best practices of the construction trades involved in the project.

9. North Mercer District shall notify the Commission in writing one week prior to the actual start of construction and at the 50 percent completion point.

10. Any documents filed in the future pursuant to ordering paragraphs 6, 7, and 9 of this Order shall reference this case number and shall be retained in the utility's post-case correspondence file.

11. The Executive Director is delegated authority to grant reasonable extensions of time for filing of any documents required by this Order upon North Mercer District's showing of good cause for such extension.

12. The rates set forth in Appendix A to this Order are approved for service that North Mercer District renders on and after the date of this Order.

13. Within 20 days of the date of this Order, North Mercer District shall file revised tariff sheets with the Commission, using the Commission's electronic Tariff Filing System, containing the rates set forth in Appendix A to this Order.

14. This case shall remain open to allow the Commission sufficient time to evaluate North Mercer District's financial condition.

15. On or before September 15, 2021, North Mercer District shall submit its responses to the Staff's Request for Information attached to this Order as Appendix B.

Nothing contained herein shall be deemed a warranty of the Commonwealth of Kentucky, or any agency thereof, of the financing, herein approved.

By the Commission

ENTERED
AUG 19 2021 rcs
KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:


Executive Director

Case No. 2021-00317

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2021-00317 DATED AUG 19 2021

The following rates and charges are prescribed for the customers in the area served by North Mercer Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of the Commission prior to the effective date of this Order.

Monthly Water Rates

5/8- x 3/4-Inch Meters

First 1,000 gallons	\$ 20.00 Minimum Bill
Over 1,000 gallons	0.0094 per gallon

1-Inch Meters

First 2,500 gallons	\$ 35.50 Minimum Bill
Over 2,500 gallons	0.0094 per gallon

2-Inch Meters

First 10,000 gallons	\$ 105.00 Minimum Bill
Over 10,000 gallons	\$ 0.0094 per gallon

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2021-00317 DATED AUG 19 2021

COMMISSION STAFF'S FIRST REQUEST FOR INFORMATION
TO NORTH MERCER WATER DISTRICT

North Mercer Water District (North Mercer District), pursuant to 807 KAR 5:001, is to file with the Commission an electronic version of the following information. The information requested is due on September 15, 2021. The Commission directs North Mercer District to the Commission's July 22, 2021 Order in Case No. 2020-00085¹ regarding filings with the Commission. Electronic documents shall be in portable document format (PDF), shall be searchable, and shall be appropriately bookmarked.

Each response shall include the name of the witness responsible for responding to the questions related to the information provided. Each response shall be answered under oath or, for representatives of a public or private corporation or a partnership or association or a governmental agency, be accompanied by a signed certification of the preparer or the person supervising the preparation of the response on behalf of the entity that the response is true and accurate to the best of that person's knowledge, information, and belief formed after a reasonable inquiry.

North Mercer District shall make timely amendment to any prior response if North Mercer District obtains information that indicates the response was incorrect when made or, though correct when made, is now incorrect in any material respect. For any request

¹ Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC July 22, 2021), Order (in which the Commission ordered that for case filings made on and after March 16, 2020, filers are NOT required to file the original physical copies of the filings required by 807 KAR 5:001, Section 8).

to which North Mercer District fails or refuses to furnish all or part of the requested information, North Mercer District shall provide a written explanation of the specific grounds for its failure to completely and precisely respond.

Careful attention shall be given to copied material to ensure that it is legible. When the requested information has been previously provided in this proceeding in the requested format, reference may be made to the specific location of that information in responding to this request. When applicable, the requested information shall be separately provided for total company operations and jurisdictional operations. When filing a paper containing personal information, North Mercer District shall, in accordance with 807 KAR 5:001, Section 4(10), encrypt or redact the paper so that personal information cannot be read.

1. Provide a schedule in Excel spreadsheet format with all formulas, columns, and rows unprotected and fully accessible showing that North Mercer District will meet the debt service coverage requirements of its lenders (existing and proposed long-term debt) for the three years following the completion of its proposed construction project. Include all calculations, assumptions (customer growth and increases in operating expenses), and workpapers used by North Mercer District in its response.

2. Provide a schedule in Excel spreadsheet format with all formulas, columns, and rows unprotected and fully accessible showing North Mercer District's debt service coverage (existing and proposed long-term debt), including full recovery of its depreciation expense (existing plant and the completed project) for the three years following the completion of its proposed construction project. Include all calculations,

assumptions (customer growth and increases in operating expenses), and workpapers used by North Mercer District in its response.

3. Provide copies of the following and, when appropriate, provide in Excel spreadsheet format with all formulas, columns, and rows unprotected and fully accessible: The general ledger and trial balance for the calendar years 2020 and 2021 to date.

4. Provide a three-year projected average debt service coverage calculation including all current debt of North Mercer District, including the financing approved in this case using the table below.

*North Mercer Water District
4795 Louisville Road
P. O. Box 79
Salvisa, KY 40372

*Mischell Lee
North Mercer Water District
P. O. Box 79
Salvisa, KY 40372

*Riley Sumner
Kentucky Engineering Group, LLC
PO Box 1034
Versailles, KENTUCKY 40383

*Honorable W. Randall Jones
Attorney at Law
Rubin & Hays
Kentucky Home Trust Building
450 South Third Street
Louisville, KENTUCKY 40202