

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

JOINT APPLICATION OF CONSUMERS WATER)
DISTRICT, FANCY FARM WATER DISTRICT,)
HARDEMAN WATER DISTRICT, AND SOUTH) CASE NO. 2007-00496
GRAVES WATER DISTRICT FOR APPROVAL)
OF MERGER AND FORMATION OF GRAVES)
COUNTY WATER DISTRICT)

ORDER

Consumers Water District (“Consumers District”), Fancy Farm Water District (“Fancy Farm District”), Hardeman Water District (“Hardeman District”) and South Graves Water District (“South Graves District”) (collectively “Joint Applicants”) have applied for Commission approval of the merger of their water districts.¹

Having considered the application and being otherwise sufficiently advised, the Commission finds that:

1. Consumers District, a water district organized under KRS Chapter 74, owns and operates facilities that are used to distribute water to approximately 1,669 customers in south central and southeastern Graves County, Kentucky.²
2. A three-member board of commissioners manages Consumers District.³

¹ The Joint Applicants filed their application on November 30, 2007. No persons have sought to intervene in this matter. On January 10, 2008, the Commission established a procedural schedule in this matter that allowed for discovery and a hearing. Discovery has been completed in this matter. In view of the existing record and the lack of any request from the Joint Applicants for a hearing, the Commission finds that a hearing in this matter is not necessary and the case stands ready for decision.

² *Annual Report of Consumers Water District to the Kentucky Public Service Commission for the Calendar Year Ended December 31, 2007* at 5 and 27.

³ *Id.* at 6.

3. For the fiscal year ended December 31, 2007, Consumers District reported utility plant in service of \$4,242,634 and accumulated depreciation of \$1,322,625, for a net utility plant of \$2,920,009.⁴

4. For the fiscal year ended December 31, 2007, Consumers District reported total operating revenues of \$429,761 and total operating expenses of \$444,831, for a net operating loss of \$(15,070).⁵

5. As of December 31, 2007, Consumers District had outstanding long-term debt of \$65,323 and total current and accrued liabilities of \$100,528.⁶

6. Fancy Farm District, a water district organized under KRS Chapter 74, owns and operates facilities that are used to distribute water to approximately 436 customers in northwestern Graves County and eastern Carlisle County, Kentucky⁷ and to provide sewer services to approximately 216 customers in Graves County, Kentucky.⁸

7. A five-member board of commissioners manages Fancy Farm District.⁹

⁴ *Id.* at 7.

⁵ *Id.* at 11.

⁶ *Id.* at 9.

⁷ *Annual Report of Fancy Farm Water District to the Kentucky Public Service Commission for the Calendar Year Ended December 31, 2007 (Water Operations)* (hereinafter *2007 Fancy Farm Water Annual Report*) at 5 and 21.

⁸ *Annual Report of Fancy Farm Water District to the Kentucky Public Service Commission for the Calendar Year Ended December 31, 2007 (Sewer Operations)* (hereinafter *2007 Fancy Farm Sewer Annual Report*) at 8.

⁹ *Annual Report of Fancy Farm Water District to the Kentucky Public Service Commission for the Calendar Year Ended December 31, 2006 (Water Operations)* at 6.

8. For the fiscal year ended December 31, 2007, Fancy Farm District reported water utility plant in service of \$1,191,508 and accumulated depreciation of \$624,241, for a net utility plant of \$567,267.¹⁰

9. For its water operations for the fiscal year ended December 31, 2006, Fancy Farm District reported total operating revenues of \$161,871 and total expenses at \$189,053, for a net operating loss of \$(27,182).¹¹

10. For the fiscal year ended December 31, 2007, Fancy Farm District reported sewer utility plant in service of \$1,564,569 and accumulated depreciation of \$1,012,647, for a net utility plant of \$551,922.¹²

11. For its sewer operations for the fiscal year ended December 31, 2007, Fancy Farm District reported total operating revenues of \$138,057 and total operating expenses at \$92,761, for a net operating loss of \$(31,299).¹³

12. As of December 31, 2007, Fancy Farm District had outstanding long-term debt of \$553,976 and total current and accrued liabilities of \$17,886 for its water operations¹⁴ and outstanding long-term debt of \$136,920 and total current and accrued liabilities of \$14,566 for its sewer operations.¹⁵ The Kentucky Infrastructure Authority holds all of Fancy Farm District's long-term debt.

¹⁰ 2007 Fancy Farm Water Annual Report at 7.

¹¹ *Id.* at 9.

¹² 2007 Fancy Farm Water Annual Report at 2.

¹³ 2007 Fancy Farm Sewer Report at 8.

¹⁴ 2007 Fancy Farm Water Annual Report at 8.

¹⁵ 2007 Fancy Farm Sewer Report at 3.

13. Hardeman District, a water district organized under KRS Chapter 74, owns and operates facilities that are used to distribute water to approximately 336 customers in northeast Graves County, Kentucky.¹⁶

14. A three-member board of commissioners manages Hardeman District.¹⁷

15. For the fiscal year ended December 31, 2007, Hardeman District reported water utility plant in service of \$437,315 and accumulated depreciation of \$388,796, for a net utility plant of \$48,518.¹⁸

16. For the fiscal year ended December 31, 2007, Hardeman District reported total operating revenues of \$106,386 and total expenses at \$114,994, for a net operating loss of \$(8,593).¹⁹

17. As of December 31, 2007, Hardeman District had outstanding long-term debt of \$65,323 and total current and accrued liabilities of \$1,210.²⁰

18. South Graves District, a water district organized under KRS Chapter 74, owns and operates facilities that are used to distribute water to approximately 670 customers in southwestern Graves County, Kentucky.²¹

19. A three-member board of commissioners manages South Graves District.²²

¹⁶ *Annual Report of Hardeman Water District to the Kentucky Public Service Commission for the Calendar Year Ended December 31, 2007* at 5 and 21.

¹⁷ *Id.* at 6.

¹⁸ *Id.* at 7

¹⁹ *Id.* at 9.

²⁰ *Id.* at 8.

²¹ *Annual Report of South Graves Water District to the Kentucky Public Service Commission for the Calendar Year Ended December 31, 2007* at 5 and 21.

²² *Id.* at 6.

20. For the fiscal year ended December 31, 2007, South Graves District reported water utility plant in service of \$1,930,959 and accumulated depreciation of \$1,034,072, for a net utility plant of \$896,257.²³

21. For the fiscal year ended December 31, 2007, South Graves District reported total operating revenues of \$254,687 and total operating expenses at \$256,076, for a net operating loss of \$(1,389).²⁴

22. As of December 31, 2007, South Graves District had outstanding long-term debt of \$941,954 and total current and accrued liabilities of \$52,500.²⁵

23. Consumers District, Fancy Farm District, and South Graves District currently contract with Mayfield Electric and Water Systems ("Mayfield") for operation, maintenance and management services.²⁶ These water districts have no employees. In addition to the contractual services that Mayfield provides to it, Consumers District contracts for administrative services.

24. Hardeman District has one employee and contracts with certain individuals for maintenance, administrative and meter reading services.

25. The map set forth on the following page accurately depicts the current public and municipal water utilities in Graves County, Kentucky and the areas in which each utility provides water service.

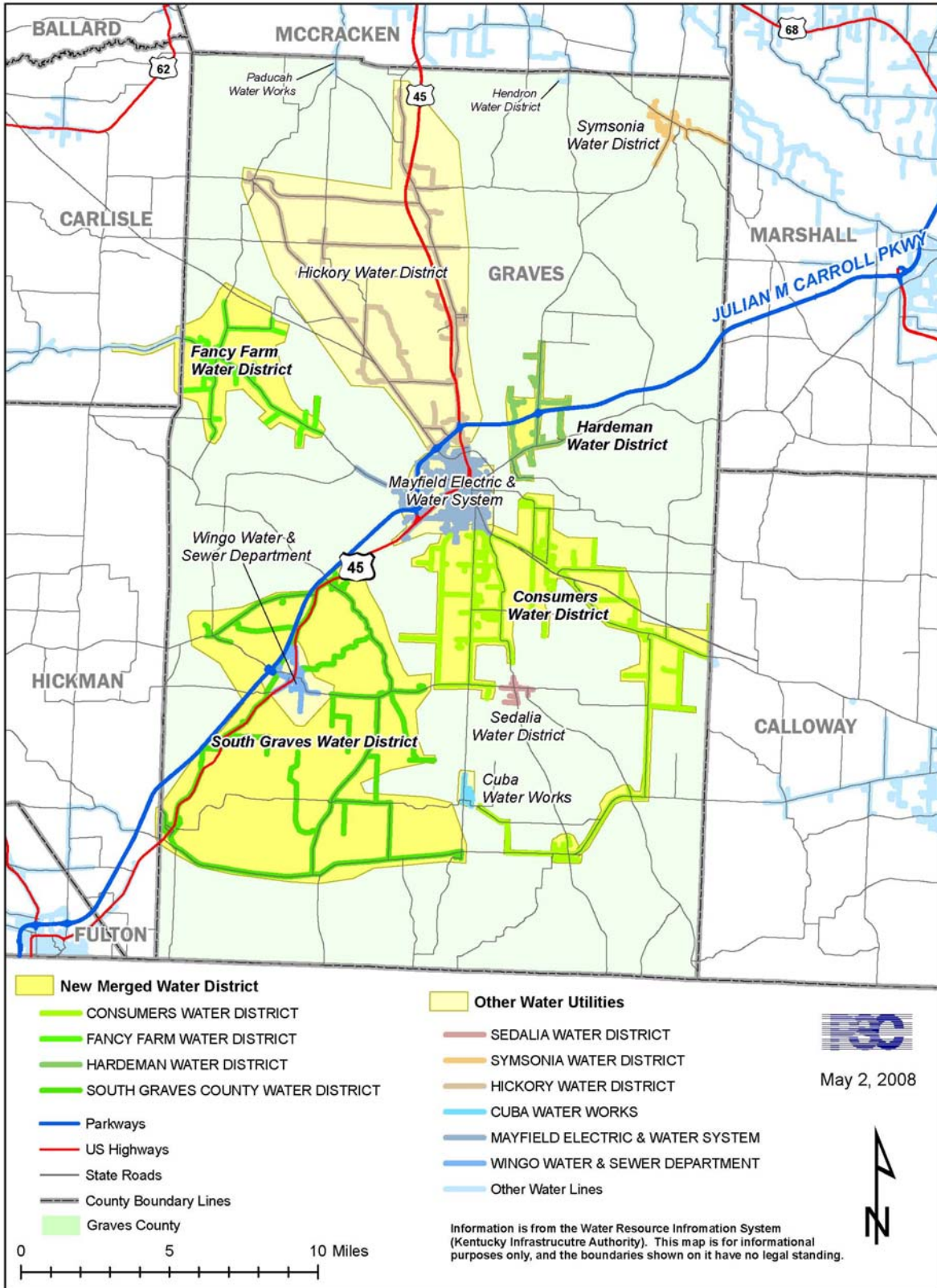
²³ *Id.* at 7.

²⁴ *Id.* at 9.

²⁵ *Id.* at 8.

²⁶ Joint Applicants' Response to Commission Staff's First Data Request, Item 5.

PUBLIC AND MUNICIPAL WATER UTILITIES IN GRAVES COUNTY, KENTUCKY



26. The board of commissioners of each of the Joint Applicants has adopted a resolution that approves the voluntary merger of the Joint Applicants and a proposed merger plan. This plan provides that:

a. All of the Joint Applicants' assets and liabilities will be eventually consolidated under the name of "Graves County Water District."

b. The newly merged district will seek \$1,000,000 from Kentucky State Government for the construction of appropriate interconnections between each of the Joint Applicants' water systems.

c. For up to the first 18 months following Commission approval of the proposed merger, the rates for each of the Joint Applicants will remain unchanged.

d. At the end of the first 12 months of operation, the merged district will perform a cost-of-service study to establish a new rate for all customers that will consist of a base rate and a debt surcharge rate.

e. The proposed base rate will recover all operation and non-debt-related expenses and will be uniformly applied throughout the merged district.

f. The proposed debt surcharge rate is intended to recover the principal and interest payments on any debt existing at merger. It will be assessed based upon a customer's location (i.e., his presence in the predecessor water district's territory) and the debt payments attributable to that predecessor water district.

g. Within five years of the Commission's approval of the proposed merger, the merged district will charge a uniform rate to all customers.

h. All persons with whom the Joint Applicants have contracted for services as of April 1, 2007 or whom they have employed as of April 1, 2007 shall be offered similar contractual arrangements or employment with the merged district.

i. Upon completion of the merger, the merged district will seek an expansion of its territory to include all unincorporated and unserved areas of Graves County, Kentucky.²⁷

27. The General Assembly has determined that “reduction of the number of operating water districts in the Commonwealth. . .[is] in the public interest, in that mergers of such districts will tend to eliminate wasteful duplication of costs and efforts, result in a sounder and more businesslike degree of management, and ultimately result in greater economies, less cost, and a higher degree of service to the general public; and that the public policy favors the merger of water districts wherever feasible.”²⁸

28. The Kentucky Infrastructure Authority has authorized a grant of \$500,000 to reduce the Joint Applicants’ long-term debt and promote the proposed merger.

²⁷ In their Joint Application, the Joint Applicants suggest that the proposed merger will require the creation of a new water district that will include the Joint Applicants’ existing territory and that upon the creation of this new water district, the Joint Applicants will transfer their present assets and liabilities to this new district. Our reading of KRS 74.363 suggests that the creation of a new water district to assume the Joint Applicants’ existing assets is not required. KRS 74.363(4) provides:

The resulting district shall have all the assets and legal liabilities of the water districts joining in the merger. The separate existences of the water districts joining in the merger, except the resulting district, shall cease, and the title to all real estate and other property owned by the water districts joining in the merger shall be vested in the resulting district without reversion or impairment. Bonded obligations of any district secured by the right to levy an assessment as provided by KRS 74.130 through 74.230 or secured by the revenue of the systems operated by the district shall continue to be retired or a sinking fund for such purpose created from the tax assessments or revenue from the system operated by the district from funds collected over the same area by the new board of commissioners in accordance with the laws under which the bonds were issued until all bonded obligations of the old district have been retired.

Moreover, the creation of a new water district whose territory includes the territory of existing water districts appears contrary to law. See OAG 63-666. The merger will occur upon the execution of a merger agreement and the Commission’s approval of the proposed merger. No direct action is required from the Graves Fiscal Court. We note that a merger agreement that sets forth a specific date for merger does not yet exist.

²⁸ KRS 74.361(1).

29. The proposed merger is likely to produce greater economies of scale, reduce the cost of service, and improve service quality.

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

1. Consumers District, Fancy Farm District, Hardeman District, and South Graves District are utilities subject to Commission jurisdiction.²⁹

2. KRS 278.020(5) provides that “[n]o person shall acquire or transfer ownership of, or control, or the right to control, any utility under the jurisdiction of the commission. . .without prior approval by the commission.”³⁰

3. The proposed merger of the Joint Applicants into a single water district constitutes a transfer of control that requires Commission approval.

4. KRS 74.363(2) implies that Commission approval of a voluntary merger of two or more water districts is required.

5. Upon completion of the proposed merger, the merged water district will have the financial, technical, and managerial abilities to provide reasonable service to the Joint Applicants’ existing customers.

6. The proposed merger is consistent with the legislative finding of fact and policy set forth in KRS 74.361(1).

²⁹ KRS 74.015; KRS 278.010(3)(d).

³⁰ In our Order of January 10, 2008, we suggested that KRS 278.020(6) and KRS 278.300 applied to the proposed merger. Upon further review, we find that neither section is applicable. We note that while four water districts are transferring control of their property to a new entity, the new entity does not yet exist. As there is no acquirer, KRS 278.020(6) is not applicable. See, e.g., Case No. 2006-00197, The Joint Petition of Kentucky-American Water Company, Thames Water Aqua Holdings GmbH, RWE Aktiengesellschaft, Thames Water Aqua US Holdings, Inc., and American Waterworks Company, Inc. for Approval of a Change in Control of Kentucky-American Water Company (Ky. PSC Aug. 14, 2006). Similarly, as no utility currently exists that will assume the Joint Applicants’ indebtedness, KRS 278.300 is not applicable.

7. The proposed merger is in accordance with law and for a proper purpose and is consistent with the public interest.

IT IS THEREFORE ORDERED that:

1. The proposed merger of Consumers District, Fancy Farm District, Hardeman District, and South Graves District is approved subject to the conditions set forth in Ordering Paragraphs 2 and 3.

2. Within 120 days of the date of this Order, the Joint Applicants shall execute all documents and perform all other actions necessary to effect the proposed merger. Failure of the Joint Applicants to act within this time period shall render the Commission's approval null and void.

3. Any material revisions to the Joint Applicants' merger proposal shall be approved by the Commission before the merger as amended may occur.

4. Within 10 days of the completion of the proposed merger, the merged district shall advise the Commission in writing of the merger's completion.

5. Within 10 days of completion of the merger, the merged district shall file a signed and dated adoption notice in accordance with 807 KAR 5:011, Section 11, adopting, ratifying, and making its own all rates, rules, classifications, and administrative regulations of the Joint Applicants in effect at the time of the merger.


6. Within 10 days of the filing of its adoption notice, the merged district shall issue and file with the Commission in its own name each utility's tariff as it proposes to put into effect in lieu thereof in the form prescribed in 807 KAR 5:011, Section 11.

7. Twenty days prior to the date of the merger, the Joint Applicants shall file with the Commission the journal entries that will be used to record the proposed merger.

8. Beginning on July 1, 2008 and every month thereafter until the proposed merger has been completed, the Joint Applicants shall advise the Commission in writing on the status of the proposed merger.

Done at Frankfort, Kentucky, this 21st day of May, 2008.

By the Commission

ATTEST:

Executive Director