

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF HENDERSON COUNTY)
WATER DISTRICT FOR AN ALTERNATIVE RATE) CASE NO. 2013-00154
FILING ADJUSTMENT)

ORDER

Henderson County Water District ("Henderson District") has applied to adjust its rates for water service. By this Order, the Commission approves a two-phased rate adjustment that will ultimately produce annual water sales revenues of \$3,041,033, an increase of \$363,846 or 13.59 percent, over pro forma present rate revenues. Our action will increase the monthly bill of a residential customer who uses 5,000 gallons of water monthly from \$33.13 to \$37.63, or 13.59 percent.

On May 16, 2013, Henderson District applied for a rate adjustment pursuant to 807 KAR 5:076. On August 15, 2013, after reviewing the application and Henderson District's records, Commission Staff issued a report containing its findings regarding the proposed rate adjustment. Commission Staff found that Henderson District's proposed rates would generate additional revenues of \$219,188 over pro forma test-year revenues.¹ It further found that, using the approach that the Commission has historically employed to determine a water district's revenue requirements, Henderson District's financial condition would support a revenue requirement from water sales of \$3,041,033 and, therefore, a revenue increase of \$363,846.² Commission Staff also

¹ Staff Report at 1.

² *Id.* at 16.

recommended that the Commission direct Henderson District to revise its method for calculating and recording depreciation expense for accounting and ratemaking purposes and to take certain actions to improve internal controls.³

In response to this report, Henderson District advised the Commission that it accepted Commission Staff's findings regarding the need for a higher revenue requirement and the rates that Commission Staff found would generate the higher revenue requirement.⁴ It proposed that the rates recommended by Commission Staff be implemented in two phases, that Henderson District's originally proposed rates be authorized immediately as the first phase of the rate adjustment, and that the rates recommended by Commission Staff be authorized one year later.⁵ It further advised of its agreement with Commission Staff's findings regarding Henderson District's internal controls and the adjustment of the depreciable lives of certain assets.

On September 17, 2013, the Commission directed Henderson District to publish in a newspaper of general circulation in its territory notice of its revised request for rate adjustment. Henderson District caused this notice to be published on September 26, 2013. On October 15, 2013, having received no comments on Henderson District's request nor any requests for intervention in this proceeding, the Commission, pursuant to our Order of September 17, 2013, closed the record and submitted the matter for decision.

³ *Id.* at 2-5.

⁴ Response of Henderson County Water District to the Order of August 27, 2013 at 1 (filed Aug. 26, 2013).

⁵ *Id.* at 3.

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

1. Henderson District, a water district organized pursuant to KRS Chapter 74, owns and operates facilities that distribute water to approximately 6,384 customers in Henderson and Webster counties, Kentucky.⁶

2. The calendar year ending December 31, 2012 should be used as the test year to determine the reasonableness of Henderson District's existing and proposed rates.⁷

3. Based upon pro forma test-year operations, Henderson District's total pro forma revenue is \$2,783,627.⁸

4. Based upon pro forma test-year operations, Henderson District's total pro forma operating expenses, after adjusting for known and measurable changes, is \$2,549,283.⁹

5. The statement of Henderson District's test-period operations, as adjusted for known and measurable changes, is set forth in Appendix A of this Order.

6. Henderson District presently uses service lives for six groups of assets that are at variance¹⁰ with those found in a survey of the National Association of Regulatory Utility Commissioners ("NARUC") that contained "a range of average service

⁶ *Annual Report of Henderson County Water District to the Public Service Commission of Kentucky for the Calendar Year Ending December 31, 2012 ("Annual Report")* at 5, 27.

⁷ 807 KAR 5:076, Section 8.

⁸ Staff Report at 6. \$2,677,187 (Sales of Water) + \$86,395 (Other Operating Revenue) + \$20,045 (Interest and Dividend Income) = \$2,783,627.

⁹ *Id.* \$2,082,250 (Operation and Maintenance Expenses) + \$430,590 (Depreciation Expense) + \$36,443 (Taxes Other than Income) = \$2,549,283.

¹⁰ *Id.* Attachment C.

lives currently being used by water utilities throughout the country for water facilities designed and installed and maintained in accordance with good water works practice.”¹¹

7. The Commission has previously used the same survey to establish the service lives of utility assets.¹²

8. The record contains no evidence that the service lives that Henderson District uses are based upon a depreciation study or its own historic plant records.

9. Henderson District’s assignment of service lives for these six groups of assets is not reasonable and should be revised for ratemaking and accounting purposes.¹³

10. Appendix B to this Order sets forth the groups of assets whose service lives should be adjusted, the accounts within each group that require adjustment, the previously assigned service life of each account, the service life range that the NARUC survey suggests for each account, and the assigned service life that should be used for ratemaking and accounting purposes for all future reporting periods.

11. As of December 31, 2012, Henderson District had outstanding long-term debt in the principal amount of \$4,256,032.¹⁴ These debts and its outstanding principal amounts are set forth in Table 1.

¹¹ National Association of Regulatory Utility Commissioners, *Depreciation Practices for Small Water Utilities* (Aug. 15, 1979) at 10.

¹² See, e.g., Case No. 2012-00390, *Application of Crittenden-Livingston Water District for an Adjustment in Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Dec. 20, 2012); at 4, n. 10.

¹³ These reassignments require a reduction of \$143,239 in Henderson District’s test-period depreciation expense. Staff Report at 14.

¹⁴ *Annual Report* at 9. In its annual report Henderson District reports the note that Henderson County Fiscal Court holds as a current liability. It reports the note as a long-term liability in its most recent audit report. Myriad CPA Group, *Henderson County Water District: Report on Audited Financial Statements For the fiscal years ended August 31, 2012 and 2011* (Dec. 3, 2012) at 11.

TABLE 1

Debt	Date of Issuance	Outstanding Principal Amount
Kentucky Rural Water Finance Corp. Agreement	08/15/2003	\$ 280,000
Kentucky Rural Water Finance Corp. Agreement	04/11/2006	\$3,972,000
Henderson County Fiscal Court Note	08/31/1989	\$ 4,032
Total:		\$4,256,032

12. In addition to the long-term debt listed in Table 1, Henderson District has received Commission authorization to issue revenue bonds in the total amount of \$1,995,000 to Rural Development to fund a water system improvement project.¹⁵ Debt-service payments on these bonds are a known and measureable event that should be reflected in the calculation of Henderson District's annual debt service.

13. The five-year average of Henderson District's principal and interest payments on its existing long-term debt and its authorized bond issuances is \$509,196.¹⁶

¹⁵ Case No. 2012-00352, *Application of the Henderson County Water District for a Certificate of Public Convenience and Necessity to Construct and Finance Pursuant To KRS 278.023* (Ky. PSC Aug. 23, 2012) (authorizing the issuance of \$1,695,000 of Henderson County Water District Waterworks Revenue Bonds, Series 2013); Case No. 2013-00345, *Application of Henderson County Water District to Modify the Commission's Order of August 23, 2012 in Case No. 2012-00352 to Reflect Modifications in Financing Agreement With Rural Development* (Ky. PSC Oct. 1, 2013) (authorizing the issuance of \$300,000 of Henderson County Water District Waterworks Revenue Bonds, Series 2013A).

¹⁶ As Henderson District has had only two general rate adjustment proceedings in the last 13 years, a five-year average better matches the life of the rates that will be established by this Order and should be used to determine adjusted test-year principal and interest payment. See Case No. 99-388, *The Application of Henderson County Water District for (1) Issuance of a Certificate of Convenience and Necessity and (2) Authorization to Borrow Funds and to Issue Its Evidence of Indebtedness* (Ky. PSC Nov. 1, 2000); Case No. 2005-00072, *Application of the Henderson County Water District for Approval of a Proposed Increase in Rates for Water Service* (Ky. PSC Apr. 28, 2005). The calculation of the average principal and interest payment appears below.

	2014	2015	2016	2017	2018	Average
2003 KRWFC Assistance Agreement	\$101,578	\$102,250				\$ 40,766
2006 KRWFC Assistance Agreement	324,970	317,190	\$411,370	\$407,350	\$413,681	374,912
2013 Waterworks Bonds	63,563	84,563	84,469	84,469	84,625	80,299
2013A Waterworks Bonds	10,500	10,500	14,360	14,360	14,220	12,816
Fiscal Court Note	2,016					403
Total Principal and Interest Payment						\$509,196

14. The Commission has historically used the Debt Service Coverage Methodology to calculate the revenue requirements of water districts with long-term debt.

15. Applying the Debt Service Coverage Methodology to Henderson District's pro forma operations and using a 120 percent ratio results in a total revenue requirement from all revenue sources of \$3,160,237,¹⁷ and water sales revenues of \$3,053,797.¹⁸

16. Based upon pro forma test-year sales, Henderson District's proposed Phase I rates, which are set forth in Appendix C, will produce annual revenues from water sales of \$2,891,362 and permit Henderson District to obtain total annual revenues of \$2,997,802.

17. Based upon pro forma test-year sales, Henderson District's proposed Phase II rates, which are set forth in Appendix D, will produce annual revenues from water sales of \$3,041,033 and permit Henderson District to obtain total annual revenues of \$3,147,473.

18. Henderson District's revised proposed Phase I and Phase II rates will produce levels of revenue to enable Henderson District to recover its cash-related

¹⁷ Operation and Maintenance Expenses	\$2,082,250
Depreciation Expense	430,590
Taxes Other Than Income	36,443
Average Principal and Interest Payment	509,196
Debt Service Coverage (\$509,196 x 0.2)	<u>101,758</u>
Overall Revenue Requirement	\$3,160,237

¹⁸ \$3,160,237 (Overall Revenue Requirement) - \$86,395 (Other Operation Revenues) - \$20,045 (Interest Income) = \$3,053,797.

expenses, produce adequate cash working capital, and meet the debt-service requirements of its bonded debt.¹⁹

19. Where a utility has requested rates that are less than a regulatory commission determines “would furnish a fair return then, in the absence of some factor which would in the public interest require that larger rates be charged, the rates requested by the utility ought to be allowed.”²⁰

20. The Phase I rates, which are set forth in Appendix C, should be charged by Henderson District for service rendered on and after the date of this Order up to and including November 14, 2014.

21. The Phase II rates, which are set forth in Appendix D, should be charged by Henderson District for service rendered on and after November 15, 2014.

22. No earlier than 30 days but no later than 20 days prior to November 15, 2014, Henderson District should publish notice of the Phase II rates at least once in a

¹⁹ As shown below, Phase I and Phase II rates will produce a debt service coverage ratio in excess of the 120 percent required by the KRWFC Assistance Agreements or the revenue bonds issued to Rural Development.

	Phase I	Phase II
Gross Revenues	\$2,997,802	3,147,473
Less: O&M Expenses and Taxes	(2,118,693)	(2,118,693)
Note to Henderson County Fiscal Court	<u>(2,016)</u>	<u>(2,016)</u>
Net Revenues for Debt Service Coverage Calculation	877,093	1,026,764
Divided by: Average Principal and Interest Payment	<u>508,792</u>	<u>508,792</u>
Debt Service Coverage Ratio on Average Payment	172%	202%

Under the terms of the KRWFC Assistance Agreements, Henderson District’s note to Henderson County Fiscal Court is not considered a bonded obligation and is not considered when determining the amount of principal and interest payments. Accordingly, it was removed from Average Principal and Interest Payment.

²⁰ *Utilities Operating Co. v King*, 143 So.2d 854, 45 PUR3d 439, 443 (Fla. 1962) (“[I]n the absence of some showing that the service to the public will suffer by allowing . . . [a] utility to charge rates which will not produce a fair return, the utility and not the Commission has the right of decision as to the rates it will charge so long as they do not exceed those which would produce a fair return as determined by the Commission.”). See also Case No. 2006-00410, *The Application of Hardin County Water District No. 1 for a General Rate Adjustment Effective On and After December 2, 2006* (Ky. PSC Aug. 2, 2007); Case No. 98-398, *Adjustment of Rates of Kentucky Turnpike Water District and the Imposition of an Impact Fee* (Ky. PSC June 30, 1999).

newspaper of general circulation in its territory and should file with the Commission proof of publication of such notice no later than ten days after publication of notice. Notice should be in form set forth in Appendix E to this Order.

23. Certain of Henderson District's internal controls regarding the salaries and wages and the recording of the cost of utility plant are insufficient and should be revised.

IT IS THEREFORE ORDERED that:

1. Henderson District shall, for accounting and ratemaking purposes, use the "PSC Approved Service Life" set forth in Appendix B to this Order for the listed classes of assets when calculating and reporting depreciation for all reporting periods after the date of this Order, but shall make no retroactive adjustment to its books to account for the cumulative effect of this change in accounting estimate.

2. Henderson District's proposed rates, as revised in its Response to the Commission's Order of August 27, 2013, are approved.

3. Henderson District shall charge the rates that are set forth in Appendix C for service rendered on and after the date of this Order up to and including November 14, 2014.

4. Henderson District shall charge the rates that are set forth in Appendix D for service rendered on and after November 15, 2014.

5. No earlier than 30 days but no later than 20 days prior to November 15, 2014, Henderson District shall publish notice of the Phase II rates at least once in a newspaper of general circulation in its territory and shall file with the Commission proof

of publication of such notice no later than ten days after publication of notice. Notice shall be in form set forth in Appendix E to this Order.

6. Within 20 days of the date of this Order and using the Commission's Electronic Tariff Filing System, Henderson District shall file with the Commission revised tariff sheets that contain the rates approved in this Order.

7. Within 90 days of the date of this Order, Henderson District shall revise its internal controls to establish a work order system that complies with the Uniform System of Accounts and that clearly shows the source or sources of all costs related to the construction and retirement of utility plant in service and shall file with the Commission a copy of these revised controls and evidence of its Board of Commissioners' formal adoption of such procedures.

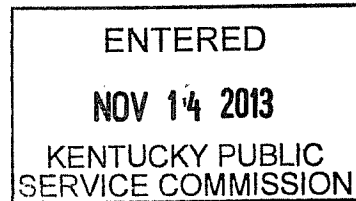
8. Within 90 days of the date of this Order, Henderson District shall file with the Commission documentary evidence of Henderson County Fiscal Court's approval of the current salary level of the members of Henderson District's Board of Commissioners.

9. Henderson District shall revise its written internal controls to provide that Henderson District's Board of Commissioners shall approve the salaries and wage rates of all Henderson District employees, including Henderson District's General Manager, and shall routinely review payroll documents to ensure that actual employee salaries and wages accord with approved salaries and wage rates. Henderson District shall file with the Commission a copy of these revised internal controls no later than 90 days from the date of this Order.

10. Any documents filed pursuant to ordering paragraphs 5 and 7 through 9 shall reference this case number and shall be retained in the utility's general correspondence file.

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

By the Commission



ATTEST:

Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2013-00154 DATED NOV 14 2013

Henderson County Water District's Adjusted Operating Statement

Operating Revenue	
Water Sales	\$2,677,187
Other Operating Revenue	<u>86,395</u>
Total Operating Revenue	<u>2,763,582</u>
Operating Expenses	
Operation and Maintenance Expenses	
Salaries and Wages - Employees	385,983
Salaries and Wages - Officers	10,500
Employee Pension and Benefits	297,291
Purchased Water	1,097,370
Purchased Power	50,076
Materials and Supplies	192,909
Contractual Services - Accounting	14,565
Contractual Services - Legal	0
Contractual Services - Other	1,825
Rental of Equipment	535
Transportation Expenses	57,758
Insurance - Vehicle	7,514
Insurance - General Liability	22,541
Insurance - Workers Compensation	8,622
Insurance - Other	229
Advertising Expense	318
Bad Debt	15,164
Miscellaneous Expenses	<u>9,050</u>
Total Operation and Maintenance Expenses	2,082,250
Depreciation Expense	430,590
Taxes Other Than Income	<u>36,443</u>
Total Operating Expenses	<u>2,549,283</u>
Net Operating Income	214,299
Interest and Dividend Income	<u>20,045</u>
Income Available to Service Debt	<u>\$ 234,344</u>

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2013-00154 DATED **NOV 14 2013**

Proposed Modifications to the Service Lives of
Certain Assets of Henderson County Water District

Asset Group	Henderson District Acct. No.	NARUC Range	Previous Assigned Service Life	PSC Approved Service Life
Buildings and Improvement: Office Building	179	35 - 40 years	30 years	37.5 years
Buildings and Improvement: Parking Lot	373	35 - 40 years	15 years	37.5 years
Meter Installation	120-146, 247, 254, 267, 319, 404, 418	40 - 50 years	10 - 40 years	45 years
Meters	79-97, 107- 114, 246, 253, 262, 275, 288, 295, 300, 312, 323, 335, 347, 357, 361,371, 402-417, 420-434, 442	35 - 45 years	10 - 40 years	40 years
Structures and Improvements	331, 355	20 years	10 years	20 years
Transmission	28-57, 59- 77, 244- 245, 251, 259, 260,286, 287, 292, 298, 310, 317, 321, 333, 345, 353, 359, 369, 384- 393	50 - 75 years	40 - 50 years	62.5 years

APPENDIX C

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2013-00154 DATED NOV 14 2013

The following rates and charges are prescribed for the customers in the area served by Henderson County Water District for service rendered from the date of this Order until and including November 14, 2014. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of the Commission prior to the effective date of this Order.

Monthly Water Rates

5/8-Inch x 3/4-Inch Meter

First	2,000 gallons	\$17.38	Minimum bill
Next	8,000 gallons	6.13	per 1,000 gallons
Next	20,000 gallons	5.63	per 1,000 gallons
Over	30,000 gallons	5.13	per 1,000 gallons

1-Inch Meter

First	5,000 gallons	\$35.77	Minimum bill
Next	5,000 gallons	6.13	per 1,000 gallons
Next	20,000 gallons	5.63	per 1,000 gallons
Over	30,000 gallons	5.13	per 1,000 gallons

2-Inch Meter

First	16,000 gallons	\$100.20	Minimum bill
Next	14,000 gallons	5.63	per 1,000 gallons
Over	30,000 gallons	5.13	per 1,000 gallons

3-Inch Meter

First	30,000 gallons	\$179.02	Minimum bill
Over	30,000 gallons	5.13	per 1,000 gallons

4-Inch Meter

First	50,000 gallons	\$281.62	Minimum bill
Over	50,000 gallons	5.13	per 1,000 gallons

6-Inch Meter

First	100,000 gallons	\$538.12	Minimum bill
Over	100,000 gallons	5.13	per 1,000 gallons
Volunteer Fire Department (Metered Services)		\$17.38	per month

APPENDIX D

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2013-00154 DATED NOV 14 2013

The following rates and charges are prescribed for the customers in the area served by Henderson County Water District for service rendered on and after November 15, 2014. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of the Commission prior to the effective date of this Order.

Monthly Water Rates

5/8-Inch x 3/4-Inch Meter

First	2,000 gallons	\$18.28	Minimum bill
Next	8,000 gallons	6.45	per 1,000 gallons
Next	20,000 gallons	5.92	per 1,000 gallons
Over	30,000 gallons	5.39	per 1,000 gallons

1-Inch Meter

First	5,000 gallons	\$37.63	Minimum bill
Next	5,000 gallons	6.45	per 1,000 gallons
Next	20,000 gallons	5.92	per 1,000 gallons
Over	30,000 gallons	5.39	per 1,000 gallons

2-Inch Meter

First	16,000 gallons	\$105.40	Minimum bill
Next	14,000 gallons	5.92	per 1,000 gallons
Over	30,000 gallons	5.39	per 1,000 gallons

3-Inch Meter

First	30,000 gallons	\$188.28	Minimum bill
Over	30,000 gallons	5.39	per 1,000 gallons

4-Inch Meter

First	50,000 gallons	\$296.08	Minimum bill
Over	50,000 gallons	5.39	per 1,000 gallons

6-Inch Meter

First	100,000 gallons	\$565.58	Minimum bill
Over	100,000 gallons	5.39	per 1,000 gallons
Volunteer Fire Department (Metered Services)		\$18.28	per month

APPENDIX E

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2013-00154 DATED **NOV 14 2013**

NOTICE TO THE CUSTOMERS OF HENDERSON COUNTY WATER DISTRICT

Pursuant to the Order of November 14, 2013, of the Kentucky Public Service Commission in Case No. 2013-00154, the following rates shall become effective on November 15, 2014 for water service that Henderson County Water District provides.

Monthly Water Rates

5/8-Inch x 3/4-Inch Meter

First	2,000 gallons	\$18.28	Minimum bill
Next	8,000 gallons	6.45	per 1,000 gallons
Next	20,000 gallons	5.92	per 1,000 gallons
Over	30,000 gallons	5.39	per 1,000 gallons

1-Inch Meter

First	5,000 gallons	\$37.63	Minimum bill
Next	5,000 gallons	6.45	per 1,000 gallons
Next	20,000 gallons	5.92	per 1,000 gallons
Over	30,000 gallons	5.39	per 1,000 gallons

2-Inch Meter

First	16,000 gallons	\$105.40	Minimum bill
Next	14,000 gallons	5.92	per 1,000 gallons
Over	30,000 gallons	5.39	per 1,000 gallons

3-Inch Meter

First	30,000 gallons	\$188.28	Minimum bill
Over	30,000 gallons	5.39	per 1,000 gallons

4-Inch Meter

First	50,000 gallons	\$296.08	Minimum bill
Over	50,000 gallons	5.39	per 1,000 gallons

6-Inch Meter

First	100,000 gallons	\$565.58	Minimum bill
Over	100,000 gallons	5.39	per 1,000 gallons

Volunteer Fire Department (Metered Services)	\$18.28	per month
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