

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF SANDY HOOK WATER)	CASE NO.
DISTRICT FOR RATE ADJUSTMENT)	2016-00265
PURSUANT TO 807 KAR 5:076)	

ORDER

By this Order the Commission approves an increase to Sandy Hook Water District's ("Sandy Hook") monthly water service rates. The approved water rates will generate \$117,393 in additional annual revenues, a 19.04 percent increase to pro forma present water rate revenues of \$616,568. A typical residential bill will increase from \$42.80 to \$50.95 per month, an increase of \$8.15, or 19.04 percent.¹

Pursuant to 807 KAR 5:066, Section (6)3, water loss is limited to 15 percent for ratemaking purposes. As noted in the Commission Staff Report issued November 15, 2016 ("Staff Report"), Sandy Hook reported a test-year water loss of 18.51 percent. Accordingly, Commission Staff ("Staff") reduced test-year expenses by \$1,924 to account for the 3.51 percent excess water loss.²

The Commission is placing greater emphasis on monitoring utilities that consistently exceed the fifteen (15) percent unaccounted-for water loss threshold and strongly encourages Sandy Hook to pursue reasonable actions to reduce its unaccounted-for water loss. Failure by Sandy Hook to make significant progress

¹ A typical residential customer is assumed to purchase 4,000 gallons of water per month through a 5/8-inch x 3/4-inch meter.

² Staff Report (filed Nov. 15, 2016) at 13.

towards reducing unaccounted-for water loss may cause the Commission to pursue additional action with the utility.

Pursuant to 807 KAR 5:076, on July 19, 2016, Sandy Hook tendered an application ("Application") requesting to increase its monthly water service rates. On August 1, 2016, the Attorney General ("AG") filed a motion to intervene in the proceeding, and the Commission granted the AG's motion to intervene by an Order entered on August 3, 2016.

To ensure the orderly review of the Application, the Commission issued a procedural schedule on August 4, 2016, and thereafter amended the procedural schedule in this case by an Order entered on October 17, 2016, requiring that Staff prepare and file a report containing its findings regarding the rates requested by Sandy Hook. The Order required that all parties file comments or objections to Staff's findings. On August 9, 2016, the AG submitted data requests to Sandy Hook, and Sandy Hook filed its responses to the AG's requests into the record on August 31, 2016.

On November 15, 2016, Staff issued a report summarizing its findings. In its report, Staff found that Sandy Hook's adjusted test-year operations support an overall revenue requirement in the amount of \$824,420 and that an annual revenue increase in the amount of \$165,363, or 26.82 percent, is necessary to generate the overall revenue requirement. Staff further found that that the revenue increase should be distributed evenly to Sandy Hook's current water service rates.

On November 22, 2016, Sandy Hook filed with the Commission its comments on Staff's report wherein it agreed with Staff's findings and requested that the case stand

submitted to the Commission for a decision without holding an informal conference or a formal hearing.³

On November 29, 2016, the AG submitted written comments to the Staff Report. The AG stated that he wished “to highlight areas of concern which could lead to rates which are unfair, unjust, and unreasonable,” and he addressed compensation, operational expenses, and rate design and impact.⁴ The Attorney General stated that “[a]lthough the Attorney General supports Sandy Hook’s decision not to burden ratepayers with the higher rate recommended by Commission Staff, the record does not demonstrate the reasonableness of certain expenses.”⁵

Following a review of the written comments and consideration of the record, Staff amended its original findings, and by an Order entered on January 26, 2017, the Commission found that Staff’s amended report (“Amended Staff Report”) should be filed into the record.⁶ In its amended report, Staff found that Sandy Hook’s adjusted test-year operations support an overall revenue requirement in the amount of \$776,450 and that an annual revenue increase in the amount of \$117,393, or 19.04 percent, is necessary to generate the overall revenue requirement.

With regard to compensation, Staff noted in the Amended Staff Report that it had reviewed Sandy Hook’s board meeting minutes, and during the years 2014, 2015, and

³ Letter from James H. Lewis, Board Chairman, Sandy Hook Water District, to Talina R Mathews, Executive Director, Public Service Commission (Nov. 22, 2016).

⁴ AG’s Comments (filed Nov. 29, 2016) at 3 through 8.

⁵ *Id.* at 3.

⁶ Order (Ky. PSC Jan. 26, 2017) at 2.

2016, employees received raises of 2.5 percent, 1.5 percent, and 2 percent respectively.⁷ Staff further stated that the staffing level and Salaries and Wages expense reported in Sandy Hook's 2011 Annual Report to the PSC called into question the accuracy of information filed into the record by Sandy Hook in response to the AG's request for information.⁸

With regard to operational expenses, Staff noted in the Amended Staff Report that Sandy Hook had included \$48,750 associated with the replacement of water mains in reporting test-year expenses of \$132,524 as miscellaneous expenses.⁹ Staff removed the cost of main replacements from miscellaneous expenses and increased test-year depreciation by \$780.¹⁰ Staff stated that it had reviewed the other entries to the Miscellaneous Expense account and believed them to be reasonable.¹¹

With regard to rate design and the frequency of Sandy Hook's rate applications, Staff noted in the Amended Staff Report that Sandy Hook's current rates were established in 2013 in Case No. 2013-000379,¹² a proceeding in which, pursuant to KRS 278.023, the Commission had no authority to modify or reject any portion of the agreement between Sandy Hook and Rural Development ("RD"), an agency of the

⁷ Amended Staff Report (filed Jan. 26, 2017) at 4 (footnotes omitted).

⁸ *Id.*

⁹ *Id.* at 5.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Application of Sandy Hook Water District for a Certificate of Public Convenience and Necessity to Construct, Finance and Increase Rates Pursuant to KRS 278.023* (filed Oct. 25, 2013).

United States Department of Agriculture.¹³ Staff noted that Sandy Hook's current rates have been in effect for less than five years, and Staff anticipated that the life of the rates approved in the instant case will be approximately five years.¹⁴ Staff stated that the principle of gradualism, raised by the AG in his comments, concerns the gradual shifting of costs between customer classes and that gradualism does not support any reduction to Sandy Hook's overall revenue requirement or the rates calculated by Staff.¹⁵

Sandy Hook and the AG were each given 14 days from the date of the January 26, 2017 Order to file written comments on and any objections to the findings and recommendations contained in Staff's amended report.¹⁶

On February 2, 2017, Sandy Hook filed with the Commission its comments on Staff's amended report wherein it agreed with Staff's findings and requested that the case stand submitted to the Commission for a decision without holding an informal conference or a formal hearing.¹⁷

The AG filed his comments to the Amended Staff Report on February 9, 2017. The AG "reiterated the concerns raised in his initial Comments, especially that Sandy Hook remain cognizant of its financial condition when considering annual raises or other changes to compensation, since even the recommended 19.04% increase may have a

¹³ Amended Staff Report at 5.

¹⁴ *Id.* at 6.

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ Letter from Philip Justice, Chairman, Sandy Hook Water District, to Talina R Mathews, Executive Director, Public Service Commission (Feb. 2, 2017).

large impact on Sandy Hook's customers."¹⁸ The Attorney General stated that "[i]f Sandy Hook's operating revenues are insufficient to meet necessary expenses, its own policies recognize that annual raises may be inappropriate."¹⁹ The AG did not propose a specific adjustment to Sandy Hook's operating revenues. The AG stated that he supported "the recommendation that any increase in rates be applied evenly across customers classes in the absence of a cost of service study."²⁰ The AG further stated that he did not believe that a formal hearing or informal conference is necessary.

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

1. Sandy Hook was organized pursuant to KRS Chapter 74. It owns and operates a water distribution system through which it provides water service to approximately 1,194 customers in Elliot and Morgan counties, Kentucky.²¹

2. The calendar year ended December 31, 2015, should be used as the test year to determine the reasonableness of Sandy Hook's existing and proposed water rates.

¹⁸ Attorney General's Comments (filed Feb. 9, 2017) at 2.

¹⁹ *Id.*

²⁰ *Id.*

²¹ *Annual Report of Sandy Hook Water District to the Public Service Commission for the Calendar Year Ended December 31, 2015 ("Annual Report")* at 12 and 53.

3. Based upon pro forma test-year operations, Sandy Hook's total pro forma present rate revenue and total pro forma operating expenses, after adjusting for known and measurable charges, are \$659,057²² and \$653,675²³ respectively.

4. Sandy Hook currently has six outstanding bond issuances payable to the RD. The five-year average principal and interest payments for the years 2016 through 2020 on the RD bonds is \$102,312.²⁴

5. The Commission has historically used a Debt Service Coverage ("DSC") method to calculate the revenue requirements of water districts with long-term debt.

6. Application of the Commission's DSC method to Sandy Hook's pro forma operations results in an overall revenue requirement of \$776,450. A revenue increase of \$117,393 from water service rates is necessary to generate the overall requirement.²⁵

7. The monthly water service rates calculated by Staff and agreed to by Sandy Hook are appropriate and should be approved.

8. The water service rates requested by Sandy Hook will produce more revenues than required and should be denied.

9. During the test year, Sandy Hook used service lives for various water assets that are at variance with those found in a survey by the National Association of Regulatory Utility Commissioners ("NARUC Survey") of "average service lives currently

²² Amended Staff Report at 3. \$616,568 (Sales of Water) + \$42,136 (Miscellaneous Service Revenues) + \$353 (Interest Income) = \$659,057.

²³ *Id.*

²⁴ *Id.* at 7.

²⁵ *Id.*

being used by water utilities throughout the country for water facilities designed and installed and maintained in accordance with good water works practice.”²⁶

10. The Commission has previously used the NARUC Survey to establish the services lives of water assets when there is no evidence in the record that supports alternative lives.²⁷

11. Sandy Hook’s assignment of service lives for these asset groups is not reasonable and should be revised to conform to the NARUC Survey for ratemaking and accounting purposes in all future reporting periods.

IT IS THEREFORE ORDERED that:

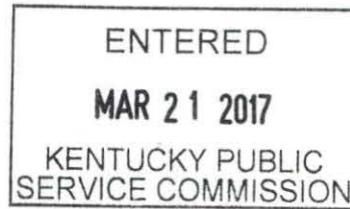
1. The water service rates requested by Sandy Hook are denied.
2. The water service rates set forth in the Appendix to this Order are approved for water service rendered on and after the date of this Order.
3. Within 20 days of the date of this Order, Sandy Hook shall file revised tariff sheets with the Commission, using the Commission’s electronic Tariff Filing System, setting forth the water service rates approved herein.
4. Sandy Hook shall use the Commission-approved service lives set forth in the table below to depreciate water plant assets for accounting purposes in all future reporting periods. No adjustment to accumulated depreciation or retained earnings should be made to account for this change in accounting estimate.

²⁶ National Association of Regulatory Utility Commissioners, *Depreciation Practices for Small Water Utilities* (Aug. 15, 1979) at 11.

²⁷ Case No. 2006-00398, *Application of Northern Kentucky Water District for Approval of Depreciation Study* (Ky. PSC Nov. 21 2007); and Case No. 2012-00278, *Application of Graves County Water District for an Adjustment in Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Sept. 5, 2012).

<u>Asset Group</u>	<u>Used by Sandy Hook</u>	<u>Commission Ordered</u>
Wells	35-50 years	30 years
Mains	40-50 years	62.5 years

By the Commission



ATTEST:


Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2016-00265 DATED **MAR 21 2017**

The following water rates are prescribed for the customers in the area served by Sandy Hook Water District. 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 Meter

First	2,000 gallons	\$ 28.57 Minimum bill
Next	8,000 gallons	11.19 per 1,000 gallons
Next	40,000 gallons	10.00 per 1,000 gallons
All Over	50,000 gallons	8.81 per 1,000 gallons

1-Inch Meter

First	5,000 gallons	\$ 62.14 Minimum bill
Next	5,000 gallons	11.19 per 1,000 gallons
Next	40,000 gallons	10.00 per 1,000 gallons
All Over	50,000 gallons	8.81 per 1,000 gallons

1 1/2-Inch Meter

First	10,000 gallons	\$ 118.09 Minimum bill
Next	40,000 gallons	10.00 per 1,000 gallons
All Over	50,000 gallons	8.81 per 1,000 gallons

2-Inch Meter

First	20,000 gallons	\$ 218.09 Minimum bill
Next	30,000 gallons	10.00 per 1,000 gallons
All Over	50,000 gallons	8.81 per 1,000 gallons

3-Inch Meter

First	30,000 gallons	\$ 318.09 Minimum bill
Next	20,000 gallons	10.00 per 1,000 gallons
All Over	50,000 gallons	8.81 per 1,000 gallons

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