

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE LAKE VILLAGE)
WATER ASSOCIATION, INC.,) CASE NO. 8317
RATE INCREASE)

O R D E R

On August 19, 1981, Lake Village Water Association, Inc., ("Lake Village") filed an application with this Commission giving notice of an adjustment of rates to become effective September 15, 1981. The proposed rates would produce additional revenue of \$57,958 annually, an increase of 39 percent based on test year revenue. However, Lake Village amended its application on October 19, 1981, requesting an additional revenue increase of \$21,662 based on an additional charge by its water supplier, the City of Danville ("Danville"). The amended rates would produce a total increase of \$79,620 based on test year revenue, an increase of 53.1 percent. By Commission Order, the effective date of the proposed tariffs was suspended until February 15, 1982, pursuant to the provisions of KRS 278.190. Based on the determination herein the annual revenue will increase by \$36,695, an increase of 24 percent.

On August 25, 1981, Lake Village filed a motion requesting that the Commission enter an emergency order permitting it

to increase its rates immediately by the amount requested in its original application. On November 25, 1981, the Commission issued an Interim Order authorizing Lake Village to place into effect an interim rate subject to refund pursuant to KRS 278.190. The Commission further ordered Lake Village to file monthly reports on the progress of its efforts to reduce line loss to an acceptable level.

A hearing was held at the Commission's offices in Frankfort, Kentucky, on October 27, 1981. There were no intervenors. The matter is now submitted for final determination by the Commission.

Commentary

Lake Village is a non-profit water association organized and existing under the laws of the Commonwealth of Kentucky, serving approximately 976 customers in the Kentucky counties of Boyle and Mercer. Lake Village purchases all of its water from Danville.

Test Period

Lake Village proposed and the Commission has adopted the 12-month period ending June 30, 1981, as the test period for determining the reasonableness of the proposed rates. In utilizing the historical test period, the Commission has given full consideration to known and measurable changes found reasonable.

Revenues and Expenses

Lake Village proposed several adjustments to revenues and expenses as reflected on its revised statement of income on Exhibit 1 to the application. The Commission finds that the adjustments proposed by Lake Village are generally acceptable for rate-making purposes with the following modifications:

Depreciation Expense

It is the policy of the Commission to compute depreciation expense for rate-making purposes on the basis of the original cost of the plant in service less contributions in aid of construction. The record herein reflects that the level of contributions in aid of construction at the end of the test year was \$211,200 which is approximately 22 percent of the total cost of utility plant in service. In determining the pro forma depreciation expense the Commission has utilized the level of plant in service at the end of the test year and the depreciation rates proposed by Lake Village. After excluding depreciation associated with contributed property the adjusted depreciation expense for rate-making purposes is \$23,256.

Miscellaneous Expense

Based on an analysis of miscellaneous expense, the Commission determined that Lake Village incurred rent expense during the test year of \$280. The witness for Lake Village, Mr. Lanham, testified that during the test year Lake Village moved into its own office building and as a result of this

move would no longer incur this rent expense. Therefore, the Commission has reduced the test year miscellaneous expense by \$280 to exclude this cost for rate-making purposes.

Rate Case Expense

Lake Village proposed an adjustment for rate case expense of \$1,500. This was based on an estimated cost of \$4,500 to be amortized over 3 years. Based on details of the costs actually incurred for this rate case, provided subsequent to the public hearing, the actual rate case expense was \$3,424. The Commission has reduced the proposed adjustment to \$1,141 based on a 3-year amortization of the actual expenses.

Purchased Water Expense

Lake Village initially proposed an adjustment to increase purchased water expense by \$23,811 to reflect the increase in wholesale water cost from Danville effective July 1, 1981. In an amended application, Lake Village proposed to include an additional \$21,636 for a total pro forma adjustment of \$45,447. The counsel for Lake Village, Mr. William S. Stevens, stated that upon receipt of the first bill from Danville under the July 1, 1981, rates, Lake Village learned that the rate for all purchases over 800,000 cubic feet would be doubled. This provision was not clear in the rate schedule supplied by Danville and was not anticipated by Lake Village in its initial application. Mr. Stevens stated further that Lake Village had filed an action in Boyle Circuit Court to determine whether the rate was legally imposed under

the terms of the contract and to request an order restraining the imposition of the rate for purchases over 800,000 cubic feet. At the time of the hearing in this matter the restraining order was in effect.

The Commission is of the opinion that the purchased water expense should be adjusted to include the cost associated with the increase from Danville as provided in the schedule of rates effective July 1, 1981. The legality of the additional rate for purchases in excess of 800,000 cubic feet will be decided by the Boyle Circuit Court and should not be considered herein. When the final rate has been established Lake Village may file an application with this Commission for a purchased water adjustment pursuant to 807 KAR 5:067.

In determining the pro forma purchased water expense Lake Village applied the new wholesale water rate to the actual purchases during the test year. Lake Village incurred line losses of 46 percent of its purchases. In accordance with past policy the Commission has adjusted purchased water expense to include a maximum 15 percent line loss. This adjustment results in pro forma purchased water expense of \$62,527.

In the Interim Order in this matter of November 25, 1981, the Commission found that Lake Village had excessive line loss and ordered it to begin immediately to file monthly reports of the line losses and the efforts to reduce line loss to an acceptable level. At this time Lake Village has not complied with that provision of the Order. Lake Village is hereby advised, however, that this Commission will not permit any future disregard of the law and may seek to impose the maximum statutory

penalties pursuant to KRS 278.990 if additional offenses occur. The Commission finds that Lake Village should within 10 days of the date of this Order file the reports required in the Interim Order for each month beginning with November 1981.

Interest Income

Lake Village proposed an adjustment to reduce interest income to \$2,135, based on a reduction of sinking fund reserves during the test year. The adjusted interest income was based on an interest rate of 5.25 percent which was earned on the invested sinking fund during the test year. The Commission is of the opinion that sinking fund reserves at the end of the test year should yield interest income greater than 5.25 percent if these funds are prudently invested. Therefore, the Commission has increased pro forma interest income to \$3,684 to reflect a 10 percent return on sinking fund reserves. This is the minimum that should be earned on these funds.

Commissioner Fees

In January 1980, the commissioners of Lake Village voted to increase their monthly fee from \$150 to \$200. The witness for Lake Village, Mr. Jack Farmer, stated that the increase in the monthly fee was due to increased responsibilities of the commissioners. The functions of the commissioners include attendance at monthly meetings, survey of customers' premises for approval of new services, and taking daily water samples. The daily operations of the system are supervised by the manager.

The Commission is of the opinion that the monthly commissioner fee of \$200 is excessive and should not be allowed for

rate-making purposes. Moreover, the Commission is concerned about the adverse effects of the decision of the commissioners of Lake Village to pay bonuses to employees and increase their monthly fee during a period of financial difficulty. It is obvious to the Commission that prudent management would not allow excessive line losses. Furthermore, the fact that Lake Village has five commissioners should reduce to some extent the time required of each commissioner for utility affairs. Based on fees paid to commissioners of similar water utilities and the number of other personnel employed by Lake Village, the Commission finds that the monthly commissioner fee should be reduced to \$150. Therefore, we have reduced commissioner fees by \$4,000.

The Commission finds that Lake Village's adjusted test period operations are as follows:

	<u>Actual Test Period</u>	<u>Pro Forma Adjustments</u>	<u>Adjusted Test Period</u>
Operating Revenues	\$ 150,004	\$ -0-	\$ 150,004
Operating Expenses	154,082	(7,092)	146,990
Operating Income	\$ (4,078)	7,092	3,014
Interest Income	5,865	(2,181)	3,684
Interest Expense	25,276	-0-	25,276
Net Income	<u>\$ (23,489)</u>	<u>\$ 4,911</u>	<u>\$ (18,578)</u>

Debt Service Coverage

The Commission is of the opinion that the adjusted operating loss of \$18,578 is clearly unjust and unreasonable. A debt service coverage of 1.2 will be adequate to allow Lake Village to pay its operating expenses, meet its debt service

requirements, and maintain a reasonable surplus. In order to achieve this debt service coverage, Lake Village's operating revenues should be \$186,699 which will require additional revenues of \$36,695 annually. The increase allowed herein is \$20,719 above the amount granted in the Interim Order on November 25, 1981. The total increase in operating revenues is computed as follows:

Debt Service Coverage (\$36,161 x 1.2)	\$ 43,393
Add: Adjusted Operating Expenses	<u>146,990</u>
Subtotal	\$190,383
Less: Operating Revenue - Test Year	150,004
Interest Income	<u>3,684</u>
Increase in Revenues	<u><u>\$ 36,695</u></u>

Rate Structure

Lake Village has proposed to change its rate structure by adjusting the usage levels in the various rate blocks to reflect the actual usage levels of its customers more accurately. The Commission is of the opinion that the proposed usage levels are reasonable and will enable Lake Village to achieve a fairer allocation of usage and billing, thus benefitting both the utility and its customers, and should therefore be approved.

Summary

The Commission, after consideration of the evidence of record, finds that:

(1) The rates proposed by Lake Village would produce revenues in excess of those found reasonable herein and should be denied upon application of KRS 278.030.

(2) The rates in Appendix A are the fair, just and reasonable rates for Lake Village and will provide net income sufficient to meet the requirements in Lake Village's mortgage securing its long-term debt.

(3) The rates found reasonable herein are in excess of those found reasonable in the Interim Order dated November 25, 1981, and therefore, Lake Village will not be required to refund any portion of the interim rates.

(4) The line loss reports requested in the Interim Order of November 25, 1981, should be filed within 10 days after the date of this Order.

IT IS THEREFORE ORDERED that the rates in Appendix A be and they hereby are approved for service rendered by Lake Village on and after February 15, 1982.

IT IS FURTHER ORDERED that the rates proposed by Lake Village be and they hereby are denied.

IT IS FURTHER ORDERED that Lake Village shall file with this Commission within 30 days from the date of this Order its revised tariff sheets setting forth the rates approved herein.

IT IS FURTHER ORDERED that Lake Village shall file within 10 days of the date of this Order monthly reports beginning with November 1981, setting out the gallons of water purchased and sold and the progress of its efforts to reduce line loss to an acceptable level.

Done at Frankfort, Kentucky, this 15th day of February,
1982.

PUBLIC SERVICE COMMISSION

Marlin M. Wolf
Chairman

Katherine Randall
Vice Chairman

Don Clugston
Commissioner

ATTEST:

Secretary

Ed

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION IN CASE NO. 8317 DATED FEBRUARY 15, 1982

The following rates and charges are prescribed for all customers in the area served by Lake Village Water Association, Inc. All other rates and charges not specifically mentioned herein shall remain the same as those in effect prior to the date of this Order.

RATES: Monthly

First	1,000 gallons	\$7.45 Minimum Bill
Next	2,000 gallons	2.80 per 1,000 gallons
Next	2,000 gallons	2.20 per 1,000 gallons
Next	5,000 gallons	1.55 per 1,000 gallons
Over	10,000 gallons	1.25 per 1,000 gallons