

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

THE CERTIFICATION OF PROPOSED )  
IMPROVEMENTS, APPROVAL OF THE )  
PROPOSED PLAN FOR FINANCING THE )  
IMPROVEMENTS AND APPROVAL OF AN ) CASE NO. 8359  
ADJUSTMENT IN THE WATER SERVICE )  
RATES OF THE JONATHAN CREEK WATER )  
ASSOCIATION )

INTERIM ORDER

On October 5, 1981, Jonathan Creek Water Association, Inc., ("Jonathan Creek") filed an application with this Commission requesting authority to increase its rates and charges by approximately \$38,768 annually, an increase of 21.5 percent based on test year revenue. Furthermore, Jonathan Creek is seeking a certificate of public convenience and necessity for improvements to its existing water system and approval of the financing of these improvements. This Interim Order addresses only the requested rate increase. The Commission will issue a final order on the construction and financing aspects after the bids have been received and submitted.

A hearing was held at the Commission's offices in Frankfort, Kentucky, on January 12, 1982. There were no intervenors. The matter is now submitted for final determination by the Commission.

COMMENTARY

Jonathan Creek is a nonprofit water distribution system organized and existing under the laws of the Commonwealth of

Kentucky. Jonathan Creek serves approximately 1,050 customers in Marshall County.

#### TEST PERIOD

Jonathan Creek proposed and the Commission has adopted the 12-month period ending December 31, 1980, 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

Jonathan Creek proposed several adjustments to revenues and expenses as reflected on its comparative income statement in Exhibit B to the application. All expense adjustments with the exception of insurance expense were based on a comparison of the first 8 months of 1980 actual operating expenses to the first 8 months of 1981 actual operating expenses. The difference between the two periods was annualized to reflect an increase or decrease in each individual expense account. The Commission in the past has allowed adjustments to the historical test year that are known and measurable. This approach to ratemaking is widely used by regulatory bodies throughout the country and has been upheld by the courts in the Commonwealth of Kentucky.

The method used by Jonathan Creek to arrive at pro forma operations is one means of estimating future operations based on the actual historical experience. However, the Commission is of the opinion that this method results in adjustments which are extremely speculative in nature and not reasonably representative

of future operations. The Commission has consistently denied adjustments based on estimates of this nature and finds no compelling reason in this instance to depart from its past policy. Therefore, the Commission has not included the proposed adjustments based on estimates derived from past experience for rate-making purposes. The Commission, based on the evidence of record herein, has made the following modifications to Jonathan Creek's comparative income statement:

Electric Expense

The Commission has adjusted test year electric expense to reflect the current rates in effect from Jonathan Creek's electric supplier, West Kentucky Rural Electric Cooperative. In determining the pro forma electric expense the Commission has applied the current rates to the actual KWH used by Jonathan Creek during the test year. This results in an adjusted electric expense of \$17,757.

Payroll Tax Expense

The Commission has adjusted payroll taxes to reflect the FICA rate in effect January 1, 1982, of 6.7 percent. The FICA rate was applied to salaries allowed herein resulting in an increase of \$201 to the actual test year.

Salary Expense

The Commission has adjusted salaries for the test year by \$4,367. This adjustment reflects the annual salaries based on wage increases effective January 23, 1981, and July 3, 1981, for all employees.

### Sales Tax

The Commission has adjusted revenue and expenses by \$1,072 to exclude sales taxes erroneously charged to revenue and expense accounts during the test year.

### Insurance Expense

Jonathan Creek proposed an adjustment to reduce test year insurance expense by \$2,626 based on premiums for the 1982 policy period. However, in response to a request for information to support this adjustment Jonathan Creek submitted information which reflected the 1981 insurance premiums. Therefore, the Commission has further reduced insurance expense by \$139 to an adjusted amount of \$6,250 based on the actual premium payments for 1981.

### System Maintenance Expense

Jonathan Creek's actual system maintenance expense was \$3,311 for the test year. The expense consisted of \$1,751 in materials and \$1,560 in labor.<sup>(1)</sup> The chairman of Jonathan Creek, Mr. Gay, testified at the hearing of January 12, 1982, that the labor cost of \$1,560 was included in the salaries paid to the employees of Jonathan Creek.<sup>(2)</sup> Therefore, the Commission has reduced system maintenance expense by \$1,560 because the salaries included in the Commission's adjustment to reflect the test year wage increases will reflect the total pro forma salaries expense.

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- (1) Item 5 (D) to Exhibit B to the application.  
(2) Transcript of Evidence, page 60.

### 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 \$274,924 which is approximately 18.9 percent of the total cost of utility plant in service. After excluding depreciation associated with contributed property the adjusted depreciation expense for rate-making purposes is \$28,598.

The Commission finds that Jonathan Creek'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	\$ 181,300	\$ (1,072)	\$ 180,228
Operating Expenses	146,439	(448)	145,991
Operating Income	<u>\$ 34,861</u>	<u>\$ (624)</u>	<u>\$ 34,237</u>
Interest Income	8,228	-0-	8,228
Interest Expense	<u>62,918</u>	<u>-0-</u>	<u>62,918</u>
Net Income	<u>\$ (19,829)</u>	<u>\$ (624)</u>	<u>\$ (20,453)</u>

### DEBT SERVICE COVERAGE

Based on the adjusted operating statement Jonathan Creek would realize a net loss of \$20,453. Jonathan Creek's proposed rates were designed to produce revenues sufficient to cover pro forma operating expenses and provide a 1.2 debt service coverage on the proposed financing. However, in determining its revenue requirements Jonathan Creek failed to include debt service coverage on the debt outstanding at the end of the test year. The

Commission finds the debt service coverage method to be a fair, just and reasonable method of determining revenue requirements for Jonathan Creek for the debt outstanding at the end of the test year.

The rates proposed by Jonathan Creek will produce total revenues of \$218,471. In addition, Jonathan Creek had miscellaneous service revenue of \$525 during the test year. The debt service coverage produced from the proposed rates allowed herein for water sales is calculated as follows:

	Adjusted Operating Revenues	\$218,996
Add:	Interest Income	8,228
Less:	Adjusted Operating Expenses	<u>145,991</u>
	Adjusted Operating Income	<u>\$ 81,233</u>
	Adjusted Operating Income	\$ 81,233
	- Total Debt Service	<u>74,388</u>
	Debt Service Coverage	<u>1.09</u>

The Commission is of the opinion that this level of revenue is not unreasonable and should be approved. The revenue allowed herein should be sufficient to pay Jonathan Creek's operating expenses and improve its financial condition.

#### RATE STRUCTURE

Jonathan Creek's present rate structure for residential and commercial customers consists of 10 rate blocks ranging from a 1,200 gallon minimum to an over 40,000 gallon usage level. Jonathan Creek proposed to change its rate structure by combining various usage levels to reduce the number of rate blocks from 10.

to 4. The Commission is of the opinion the proposed change is appropriate in that it will simplify billing procedures and ultimately benefit both the utility and the customers. The proposed rate structure should, therefore, be approved.

SUMMARY

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

(1) The billing analysis filed by Jonathan Creek contained a mathematical error in the allocation of usage to the proposed rate structure which showed revenue to be generated from the proposed rates greater than that which would actually be realized. The Commission has, therefore, adjusted the rates for the second and fourth rate blocks to correct this error. Accordingly, rates proposed by Jonathan Creek insofar as they differ from those in Appendix A should be denied.

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

IT IS THEREFORE ORDERED that the proposed rates and charges in Jonathan Creek's application, insofar as they differ from those in Appendix A, be and the same are hereby denied.

IT IS FURTHER ORDERED that the rates and charges in Appendix A be and they hereby are approved for water service rendered by Jonathan Creek on and after the date of this order.

IT IS FURTHER ORDERED that within 30 days of the date of this order, Jonathan Creek shall file its revised tariff sheets setting forth the rates and charges approved herein.

Done at Frankfort, Kentucky, this 6th day of April, 1982.

PUBLIC SERVICE COMMISSION

Marlin M. Toke  
Chairman

Katharine Sandall  
Vice Chairman

Jim Carrahan  
Commissioner

ATTEST:

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Secretary



APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE  
 COMMISSION IN CASE NO. 8359 DATED APRIL 6, 1982

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

Residential and Commercial  
5/8" Meter

Gallage Block

Monthly Rate

First 1,200 gallons	\$ 7.40 (Minimum)
Next 23,800 gallons	2.55 per 1,000 gallons
Next 15,000 gallons	1.35 per 1,000 gallons
Over 40,000 gallons	1.15 per 1,000 gallons

Minimum Bills for Larger Meters\*

3/4-inch meter	First 1,200	\$11.00 Minimum
1-inch meter	First 1,200	17.50 Minimum
1-1/2-inch meter	First 1,200	25.75 Minimum
2-inch meter	First 1,200	37.50 Minimum
3-inch meter	First 1,200	73.75 Minimum
4-inch meter	First 1,200	110.00 Minimum

\*Usage in excess of 1,200 gallons will be billed at the same rates as for the 5/8-inch meter.

Ken Lake  
6" Meter

Gallage Block

Monthly Rate

First 1,200 gallons	\$ 150.00 Minimum
Over 1,200 gallons	1.15 per 1,000 gallons
Tap-on Fee 5/8-inch meter	\$ 400.00