

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

THE APPLICATION OF THE NORTH )  
NELSON WATER DISTRICT FOR A ) CASE NO. 9209  
PURCHASED WATER ADJUSTMENT )

O R D E R

On November 5, 1984, the North Nelson Water District ("North Nelson") filed an application with this Commission requesting approval of its purchased water adjustment clause and authority to adjust its rates in accordance with that clause. North Nelson proposed to recover the increase in the cost of purchased water from its wholesale supplier, the City of Bardstown, Kentucky ("Bardstown"), scheduled to become effective December 1, 1984. The Commission has accepted this proposal subject to the absorption test described herein.

COMMENTARY

Prior to approving a rate adjustment that results from an increase in purchased water costs pursuant to 807 KAR 5:067, the Commission must examine a utility's financial condition to determine whether it can absorb any of the increased cost. If there is potential for absorption, the Commission may adjust rates to offset only that portion of the increased water cost which cannot be absorbed.

### TEST PERIOD

North Nelson proposed and the Commission has accepted the 12-month period ended December 31, 1983, as the test period in this proceeding. Adjustments deemed proper and reasonable have been included to more accurately reflect current operating conditions.

### REVENUES AND EXPENSES

North Nelson did not propose any adjustments, as such, to its test-period statement of operations. However, it did submit a calculation of the increase in purchased water costs resulting from the increased wholesale rate charged by Bardstown. The Commission, after careful examination of North Nelson's financial condition, has made the following adjustments to North Nelson's test-year operating statement in accordance with established rate-making policies:

#### Purchased Water Expense

During the test period North Nelson incurred purchased water costs of \$61,542 which, according to the annual report for the year ended December 31, 1983, reflected total unit purchases of 102,569,900 gallons of water. To this amount the Commission has applied the purchased water rate made effective by Bardstown on December 1, 1984, thereby resulting in a normalized purchased water expense of \$82,056. Therefore, to reflect this normalized amount, the Commission has increased North Nelson's test-period operating expenses by \$20,514.

### Depreciation Expense

During the test period, North Nelson incurred depreciation expense of \$38,937 which reflected depreciation on total utility plant in service at a composite rate of 2.57 percent.<sup>1</sup> In accordance with its established rate-making policy, the Commission has determined the allowable amount of this expense to be \$20,560, based upon the application of the composite depreciation rate to the test-year end balance of North Nelson's total utility plant in service net of contributions in aid of construction.<sup>2</sup> Therefore, to reflect this allowable amount, the Commission has reduced North Nelson's test-period depreciation expense by \$18,377.

These three adjustments which the Commission has made to North Nelson's test-period operations produce the following results:

	<u>Actual Test Period</u>	<u>Adjustments to Actual</u>	<u>Adjusted Test Period</u>
Operating Revenues	\$194,544	\$ -0-	\$194,544
Operating Expenses	<u>169,286</u>	<u>2,137</u>	<u>171,423</u>
Operating Income	\$ 25,258	\$ <2,137>	\$ 23,121
Other Income	38,687	-0-	38,687
Other Deductions	<u>36,058</u>	<u>-0-</u>	<u>36,058</u>
Net Income	<u>\$ 27,887</u>	<u>\$ &lt;2,137&gt;</u>	<u>\$ 25,750</u>

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1 Actual depreciation expense \$ 38,937  
Total utility plant in service ÷ 1,515,414  
Composite depreciation rate 2.57%

2 Total utility plant in service \$1,515,414  
Less:  
Contributions in Aid of Construction 715,403  
Net utility plant \$ 800,011  
Composite depreciation rate 2.57%  
Allowable depreciation expense \$ 20,560

REVENUE REQUIREMENTS

The Commission, in its consideration of the information presented in this proceeding, has concluded that the debt service coverage method is the appropriate method to be utilized in calculating North Nelson's required level of revenue. In addition, the Commission is of the opinion that a debt service coverage of 1.2 is a fair, just and reasonable coverage for North Nelson to maintain as it will enable North Nelson to meet the requirements of its lenders and will provide an adequate surplus for equity growth. The Commission has applied this factor to a 5-year average of North Nelson's annual debt service and has combined the resulting amount with North Nelson's adjusted test-period operating expenses as determined herein to achieve a total revenue requirement of \$224,379.

Based upon the adjusted test-period operations, the Commission finds that North Nelson's current rates generate sufficient revenues to meet its operating needs, and, therefore, no rate adjustment is needed. This finding is demonstrated as follows:

Adjusted Operating Expenses	\$171,423
1.2X Debt Service Coverage	52,956
Revenue Requirement	<u>\$224,379</u>
Less:	
Adjusted Operating Revenues	194,544
Adjusted Other Income	<u>38,687</u>
Increase Required	<u><u>\$ &lt; 8,852 &gt;</u></u>

As North Nelson's current revenue levels exceed its required revenues by \$8,852, the Commission is of the opinion that North Nelson can, and should, absorb the full amount of the increase in its purchased water cost.

SUMMARY

The Commission, after consideration of the evidence of record and being advised, is of the opinion and finds that:

1. The purchased water adjustment clause proposed by North Nelson is in compliance with 807 KAR 5:067 and should be approved.

2. North Nelson has the potential to absorb the full amount of the increase in its purchased water cost.

3. The rates proposed by North Nelson produce revenues in excess of those found reasonable herein and should be denied upon application of KRS 278.030.

4. The base rate for future application of the purchased water adjustment clause of North Nelson should be:

<u>Supplier</u>	<u>Rate</u>
City of Bardstown	\$.80 per 1,000 gallons

IT IS THEREFORE ORDERED that the purchased water adjustment clause proposed by North Nelson be and it hereby is approved effective on and after the date of this Order.

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

IT IS FURTHER ORDERED that the rates currently charged by North Nelson are fair, just and reasonable and should continue to be charged.

IT IS FURTHER ORDERED that, for the purpose of future application of the purchased water adjustment clause of North Nelson, the base rate for purchased water shall be:

<u>Supplier</u>	<u>Rate</u>
City of Bardstown	\$.80 per 1,000 gallons

IT IS FURTHER ORDERED that, within 30 days of the date of this Order, North Nelson shall file with the Commission its revised tariff sheets setting out the purchased water adjustment clause approved herein.

Done at Frankfort, Kentucky, this 14th day of January, 1985.

PUBLIC SERVICE COMMISSION

  
Chairman

  
Vice Chairman

  
Commissioner

ATTEST:

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Secretary