

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

PURCHASED WATER ADJUSTMENT )  
FILING OF THE MILFORD WATER ) CASE NO. 9315  
COMPANY )

O R D E R

On March 29, 1985, Milford Water Company ("Milford") filed its application with the Commission requesting approval of its purchased water adjustment clause and authority to adjust its rates in accordance with that clause. Milford proposed to recover the increase in purchased water expense from its wholesale supplier, the City of Richmond ("Richmond"), which became effective April 1, 1985. The Commission has accepted this proposal subject to the absorption test described herein.

COMMENTARY

Prior to approving increased rates resulting from purchased water cost increases 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

The Commission has adopted the 12-month period ending December 31, 1984, as the test period in this matter. Adjustments deemed proper and reasonable have been included to more accurately reflect current operating conditions.

### VALUATION

The net investment and capital structure established herein was determined in accordance with the provisions of the Order in Milford's last general rate case dated July 6, 1982, Case No. 8420.<sup>1</sup>

#### Net Investment

The Commission finds from the evidence of record that Milford's net investment rate base at December 31, 1984, is \$112,384.

#### Capital Structure

The Commission finds from the evidence of record that Milford's capital structure at the end of the test period was \$117,628 and consisted of \$94,081 in equity and \$23,547 in long-term debt.

The Commission has given due consideration to these and other elements of value in determining the reasonableness of the rate increase requested herein.

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<sup>1</sup> An Adjustment of Rates of the Milford Water Company of Madison County, Kentucky.

## REVENUES AND EXPENSES

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

### Purchased Water Expense

Milford's purchased water expense for the test year was \$46,391. Based on adjusted test-year sales of 53,046,353 gallons, and the Commission's practice of limiting line loss to 15 percent for rate-making purposes, normalized purchased water expense including the increase from Richmond effective April 1, 1985, is \$67,842. Accordingly, the Commission has increased Milford's test period expenses by \$21,451 to reflect the increased purchased water expense.

### Depreciation Expense

Milford's test-year depreciation expense was \$5,217. This reflects depreciation on total plant in service with a resulting composite depreciation rate of approximately 2.25 percent. The Commission, in Milford's last general rate case, computed depreciation expense for rate-making purposes on non-contributed plant only, to insure that ratepayers pay only for the plant in which the utility has made an investment and not the plant which the utility has acquired through contributions.

Milford's balance sheet at the end of the test period reflects contributions in aid of construction of \$60,494 which represents approximately 26.1 percent of the total cost of utility plant in service. In determining the pro forma depreciation expense, the Commission has utilized Milford's composite depreciation rate and excluded contributed property. This results in the exclusion of approximately 26.1 percent of the test-year depreciation expense. The adjusted depreciation expense for rate-making purposes is \$3,856, which reflects a reduction of \$1,361.

Adjustments to the test period operations produced the following results:

	<u>Actual</u>	<u>Commission Adjustments</u>	<u>Commission Adjusted</u>
Operating Revenues	\$111,334	\$ -0-	\$111,334
Operating Expenses	<u>97,694</u>	<u>20,090</u>	<u>117,784</u>
Operating Income	<u>\$ 13,640</u>	<u>\$ &lt;20,090&gt;</u>	<u>\$ &lt; 6,450&gt;</u>

#### RATE OF RETURN

Based on the determination herein, Milford would realize a deficit operating income of \$6,450. This adjusted operating income is clearly unjust and Milford should be allowed to increase its revenue to earn a reasonable return on its investment.

In Case No. 8420, the Commission allowed a return on equity of 14 percent. In the instant case, the Commission is of the opinion that a return on equity of 14 percent is fair, just and reasonable. In order to achieve a return on equity of 14 percent, Milford should be allowed to increase annual revenues by \$19,621 which will require absorption of \$4,898 of the increase in its

purchased water cost. This will yield a return on the net investment rate base established herein of 11.7 percent.

Therefore, the Commission is of the opinion that Milford can and should absorb \$4,898 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 filed by Milford is in compliance with 807 KAR 5:067, is in the best interest of Milford and the public, and should be approved.

2. Milford has the potential to absorb \$4,898 of the total purchased water cost increase of \$24,519.

3. The rates as proposed by Milford are unfair, unjust and unreasonable and should be denied upon application of KRS 278.030.

4. A purchased water adjustment in the amount of 44 cents per 1,000 gallons and the rates in Appendix A will provide the additional revenues granted herein and are fair, just and reasonable, and therefore should be approved.

5. The base rate for future application of the purchased water adjustment clause of Milford should be:

<u>Supplier</u>	<u>Rate</u>		
City of Richmond	First	300 cu. ft.	\$5.65 Minimum
	Next	400 cu. ft.	1.65 per 100 cu. ft.
	Next	5,000 cu. ft.	1.50 per 100 cu. ft.
	Next	5,000 cu. ft.	1.25 per 100 cu. ft.
	Over	10,700 cu. ft.	.94 per 100 cu. ft.

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

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

IT IS FURTHER ORDERED that the rates in Appendix A are the fair, just and reasonable rates to be charged for water service rendered on and after the date of this Order and are hereby approved.

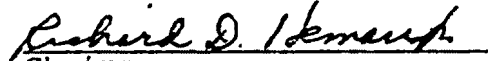
IT IS FURTHER ORDERED that for the purpose of future application of the purchased water adjustment clause of Milford the base rate for purchased water shall be:

<u>Supplier</u>	<u>Rate</u>		
City of Richmond	First	300 cu. ft.	\$5.65 Minimum
	Next	400 cu. ft.	1.65 per 100 cu. ft.
	Next	5,000 cu. ft.	1.50 per 100 cu. ft.
	Next	5,000 cu. ft.	1.25 per 100 cu. ft.
	Over	10,700 cu. ft.	.94 per 100 cu. ft.

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

Done at Frankfort, Kentucky, this 2nd day of July, 1985.

PUBLIC SERVICE COMMISSION

  
Chairman

  
Vice Chairman

  
Commissioner

ATTEST:

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Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 9315 DATED JULY 2, 1985

The following rates and charges are prescribed for the customers receiving water service from Milford Water Company. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

<u>Usage Blocks</u>	<u>Monthly Rates</u>
First 2,000 gallons	\$ 8.78 Minimum
Next 2,000 gallons	2.59 per 1,000 gallons
Next 2,000 gallons	2.09 per 1,000 gallons
Over 6,000 gallons	1.74 per 1,000 gallons