

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF TRI-VILLAGE WATER )  
DISTRICT: (1) FOR A CERTIFICATE )  
THAT PUBLIC CONVENIENCE AND )  
NECESSITY REQUIRE THE CONSTRUCTION )  
OF EXTENDED AND IMPROVED WATER )  
FACILITIES; (2) SEEKING APPROVAL OF )  
THE ISSUANCE OF CERTAIN SECURITIES; )  
AND (3) FOR AN ORDER AUTHORIZING )  
ADJUSTMENT OF WATER SERVICE RATES )  
AND CHARGES )

CASE NO. 9381

O R D E R

The Tri-Village Water District ("Tri-Village"), by application filed July 9, 1985, and revised during the proceedings in this matter, is seeking approval to increase its water service rates, authorization to construct a \$330,187 waterworks project, and approval of its financing for the proposed project. The project financing includes a loan of \$318,000 from the Farmers Home Administration ("FmHA") and \$12,187 in local funds. The FmHA loan will be secured by waterworks revenue bonds maturing over a 40-year period at an interest rate of 10 percent per annum. The proposed rates as provided in the application would produce annual revenues of approximately \$280,240, an increase of \$50,679 above normalized test period revenues.

On August 9, 1985, the Commission entered an Interim Order addressing and approving the Phase I construction and the

associated interim financing plan. The Phase I construction consisted of parallel waterline construction between the City of Owenton and the Owen County schools. This Order will address the Phase II construction, the permanent financing plan, revenue requirements and rate design.

The proposed Phase II construction includes improvements to and maintenance on the existing water distribution system. Plans and specifications for the Phase II construction prepared by Parrott, Ely and Hurt, Consulting Engineers, Inc., of Lexington, Kentucky, ("Engineer") have been approved by the Division of Water of the Natural Resources and Environmental Protection Cabinet.

A hearing was held in the offices of the Public Service Commission, Frankfort, Kentucky, on April 17, 1986. There were no intervenors present and no protests were entered.

On April 18, 1986, Tri-Village, by letter of counsel, sought to address an issue raised at the hearing in regards to specific compliance with the notice requirements set forth at 807 KAR 5:011 and expressly as to Section 8(3). Tri-Village contends that it has substantially complied with the notice requirements. The Commission has accepted Tri-Village's letter as a motion to deviate for good cause shown as per 807 KAR 5:011, Section 14.

#### TEST PERIOD

Tri-Village proposed and the Commission has accepted the 12-month period ending December 31, 1984, as the test period in this proceeding.

## REVENUES AND EXPENSES

Tri-Village had actual test period operating income before interest expense and debt service of \$4,948 which it adjusted via an amended application filed March 27, 1986, to an operating loss of \$2,210 to reflect the increased cost of water from its supplier, the city of Owenton, Kentucky. The Commission has accepted Tri-Village's actual operations as adjusted for rate-making purposes with the following exceptions:

### Normalized Revenues

Tri-Village had actual test period revenues of \$188,613. In Case No. 9025<sup>1</sup> the Commission allowed Tri-Village to change from four rate schedules to one. Only 2 months of the test period reflect this change in rate design. Normalized revenues have been determined using the approved rate design change and increased rates for the entire test period. Therefore, the Commission has determined Tri-Village's normalized test period revenues to be \$231,136, an increase of \$42,523 based on a billing analysis performed by Commission staff, which will be discussed in greater detail in a later section of this Order.

### Purchased Water Expense

In its amended application Tri-Village utilized its 1985 sales volume as the basis for its calculation of increased

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<sup>1</sup> The Application of Tri-Village Water District for an Order Permitting the Applicant to Revise Its Rates, Order entered October 26, 1984.

purchased water costs as a result of an increased rate from its supplier. Since the test period in this proceeding was 1984 and the financial statements for that period were the basis of interrogatives issued in this proceeding, the Commission, in an effort to more closely match all of Tri-Village's expenses to the period in which revenues were earned, has based Tri-Village's allowable purchased water expense on its 1984 sales volume. Therefore, the Commission has determined the adjusted test period purchased water expense to be \$89,591,<sup>2</sup> an increase of \$167 over Tri-Village's adjusted expense of \$89,424. This calculation is based on an allowance of 15 percent line loss, the maximum allowed for rate-making purposes.

#### Rate Case Expense

Tri-Village expensed during the test period \$3,672 of rate case expenses. The Commission is of the opinion that for rate-making purposes these expenses should be amortized over a 3-year period since they should provide benefit to Tri-Village for this time period. Therefore, the Commission has reduced this expense by \$2,448.

#### Depreciation Expense

Tri-Village recorded depreciation expense of \$22,091 during the test period. In response to an information request filed October 28, 1985, Tri-Village admitted that contributions in aid

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<sup>2</sup> (Test Period sales of 68,606,100 gallons + .85 for allowable line loss) X (\$1.11/1000 gallons) = \$89,591.

of construction were included in determining the above depreciation expense. It is the Commission's practice, not to allow depreciation on contributed property for rate-making purposes. Utilizing Tri-Village's overall depreciation rate of 2.87 percent,<sup>3</sup> the Commission has determined Tri-Village's allowable depreciation expense for rate-making purposes to be \$16,329.<sup>4</sup>

Interest Expense

Tri-Village incurred interest expense of \$6,040 on a loan from Citizens Bank during the test period. Seventy-three thousand dollars of the proposed bond issuance approved herein will be used to retire this loan. Therefore the Commission has eliminated this interest expense in determining Tri-Village's revenue requirement.

Tri-Village's adjusted operations are as follows:

	<u>Actual</u>	<u>Adjustment</u>	<u>Adjusted</u>
Operating Revenues	\$188,613	\$42,523	\$231,136
Operating Expenses	183,665	<885>	182,780
Operating Income	\$ 4,948	\$43,408	\$ 48,356
Short-term Interest	6,040	<6,040>	-0-
Net Income <loss> Before Debt Service	\$< 1,092>	\$49,448	\$ 48,356

<sup>3</sup> \$22,091 ÷ plant in service of \$768,413 = 2.87%

<sup>4</sup> (\$768,413 plant in service - \$199,436 contributions in aid of construction) X 2.87% - \$16,329.

REVENUE REQUIREMENTS

With the proposed bond issuance, Tri-Village will have a debt service requirement of \$60,533.<sup>5</sup> The above adjusted operations result in a debt service coverage of .80X. The Commission is of the opinion that this coverage is unfair, unjust and unreasonable. To achieve a debt service coverage of 1.2X, which the Commission is of the opinion is the fair, just and reasonable coverage necessary for Tri-Village to pay its operating expenses and to meet the requirements of its lenders, Tri-Village would require revenues of \$255,420.

The rates proposed by FmHA in its letter of conditions to Tri-Village, dated March 18, 1985, produce revenues of \$269,775. Based on the differences discussed in the billing analysis section of this Order the Commission finds these rates reasonable. However, at the conclusion of the first year's operation with the new rates the Commission will review Tri-Village's operating revenues to confirm this finding and if necessary take action to adjust Tri-Village's rates.

Billing Analysis

From January through October of the test year, Tri-Village billed its customers on four separate rate schedules. On October 26, 1984, in Case No. 9025, the Commission entered an Order

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5	5-Year Average of:	
	\$206,000 Bond	\$16,033
	\$190,000 Bond	12,160
	Proposed \$318,000 Bond	<u>32,340</u>
		\$60,533

adjusting Tri-Village's rates and placing all customers, except bulk sales, on a single rate schedule.

On Pages 5 and 5A and again on Pages 9 and 9A of Exhibit B to the application, Tri-Village provided water usage and income data based on current and proposed rates for the existing system; however, Tri-Village did not file billing and usage information sufficient to determine test year revenue.

On September 11 and 12, 1985, Public Service Commission staff performed an on-site billing analysis, copies of which were provided to Tri-Village at the hearing on April 17, 1986, with a request that it examine the billing analysis and file either its acceptance or objections thereto. By letter from Tri-Village's Accountant, filed May 2, 1986, Tri-Village accepted the billing analysis as correct based upon the billing information provided; however, it was subsequently determined that during the test year meters were not read each month resulting in numerous estimated bills, some meters were customer read and reflected the minimum usage allowance rather than actual usage; and in some instances where adjustments for leaks were made to amounts billed, such adjustments were not reflected in the usage records, all of which could produce a distortion of the actual usage. In addition, the change in rate design was in effect for only 2 months of the test year and changes in customer usage patterns resulting from this change, if any, would not be reflected in the test year usage data. Thus, the Commission is of the opinion that actual usage and revenue generation may be substantially different than that reflected in the test year billing and usage data.

Tri-Village is now reading meters on a monthly basis and steps are being taken to insure accurate usage records. The Commission urges Tri-Village to carefully review all areas which might affect the accurateness of these records and to continue to take appropriate action where indicated.

#### Tap Fee and Special Charges

Tri-Village proposed to increase its tap fee for 5/8-inch x 3/4-inch meters to \$375, to increase the reconnect charge and to institute a service run fee where the customer makes a special request. The Commission is of the opinion these charges are reasonable and should be approved.

Tri-Village also proposed to establish a flat rate deposit amount of \$25 to begin with all new customers after June 1, 1986. The Commission is of the opinion the proposed deposit should be approved in accordance with the provisions of 807 KAR 5:006, Section 7.

#### FINDINGS AND ORDERS

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

1. Tri-Village's motion to deviate from 807 KAR 5:011, Section 8 (3), should be approved; however, Tri-Village should exercise care in future notices to make certain that all regulatory requirements are met.

2. Public convenience and necessity require that the construction proposed in Phase II be performed and that a certificate of public convenience and necessity be granted.



3. The proposed project for the Tri-Village water system includes the replacement of two existing water loading stations, the cleaning and painting of the existing water storage tanks, the installation of four meter vaults and one pressure reducing valve and the replacement of one altitude valve and miscellaneous appurtenances. The low bids received for the proposed Phase II construction totaled \$89,050, which will require about \$330,187 in project funding after allowances are made for the refinancing of \$73,000 in existing debt, fees, contingencies, other indirect costs, the Phase I construction previously approved, additional Phase I engineering fees and additional improvements being considered to utilize any funds remaining after completion of the Phase II construction.

4. Tri-Village should obtain approval from the Commission prior to performing any additional construction not expressly certificated by this Order.

5. Any deviations from the construction herein approved which could adversely affect service to any customer should be done only with the prior approval of this Commission.

6. Tri-Village should furnish duly verified documentation of the total costs of this project including the cost of construction and all other capitalized costs (engineering, legal, administrative, etc.) within 60 days of the date that construction is substantially completed. Said construction costs should be classified into appropriate plant accounts in accordance with the Uniform System of Accounts for Water Utilities prescribed by this Commission.

7. Tri-Village's contract with its Engineer should require the provision of full-time resident inspection under the general supervision of a professional engineer with a Kentucky registration in civil or mechanical engineering to insure that the construction work is done in accordance with the contract plans and specifications and in conformance with the best practices of the construction trades involved in the project.

8. Tri-Village should require the Engineer to furnish a copy of the "as-built" drawings and a signed statement that the construction has been satisfactorily completed in accordance with the contract plans and specifications within 60 days of the date of substantial completion of this construction.

9. A 5/8-inch x 3/4-inch meter should be the standard customer service meter for all new customers and should be installed at all points of service unless the customer provides sufficient justification for the installation of a larger meter.

10. The financing plan proposed by Tri-Village is for lawful objects within the corporate purposes of its utility operations, is necessary and appropriate for and consistent with the proper performance of services to the public and will not impair its ability to perform these services and should, therefore, be approved.

11. The financing secured by Tri-Village for this project will be needed to pay for the work herein approved. Tri-Village's financing plan should, therefore, be approved.

12. The rates proposed by Tri-Village in its amended application should be denied upon application of KRS 278.030.

13. The rates proposed by FmHA in its letter of conditions to Tri-Village dated March 18, 1985, should be accepted as the proper rates to be charged by Tri-Village.

14. The special charges and deposit proposed by Tri-Village are reasonable and should be approved.

15. The basis of the billing analysis submitted by Tri-Village may be deficient for determining future revenue requirements in that estimated usages provided by customer read meters were not verified.

16. The operating revenues of Tri-Village will be examined at the end of the first year's operation under the rates approved in this Order and if necessary adjusted to a level adequate to produce the revenue requirements of \$255,420 based on the analysis of customer bills for that period.

IT IS THEREFORE ORDERED that:

1. Tri-Village's motion to deviate from 807 KAR 5:011, Section 8 (3), be and it hereby is sustained.

2. Tri-Village be and it hereby is granted a certificate of public convenience and necessity to proceed with the proposed construction project as set forth in the drawings and specifications of record herein.

3. Tri-Village's plan of financing consisting of a loan from the FmHA in the amount of \$318,000 with an interest rate of 10 percent and a 40-year term and \$12,187 in local funds be and it hereby is approved.

4. If under new FmHA loan conditions Tri-Village is notified and granted the option of accepting a lower interest rate at

the date of closing, Tri-Village shall file with the Commission the FmHA notification of the lower interest rate and shall provide all correspondence from and to FmHA concerning this notification within 30 days of the closing date.

5. Tri-Village shall file a statement of the interest rate accepted from FmHA within 30 days of the date of closing.

6. If Tri-Village accepts an interest rate different from the rate approved herein, it shall file amended pages to its bond resolution and an amended amortization schedule.

7. If Tri-Village is eligible but does not take advantage of a lower interest rate at the time of closing, it shall fully document why the lower rate was not accepted showing an analysis of the higher costs associated with the loan over its life.

8. Tri-Village shall comply with all matters set out in Findings 3 through 8 as if the same were individually so ordered.

9. The rates proposed by Tri-Village in its amended application are hereby denied upon application of KRS 278.030.

10. The rates, charges and deposit proposed by FmHA in its letter of conditions as set out in Appendix A be and they hereby are approved for service rendered on and after the date of this Order.

11. Tri-Village shall provide at the conclusion of the first 12 months using the rates approved herein a billing analysis showing actual usage for that period.

Nothing contained herein shall be deemed a warranty of the Commonwealth of Kentucky, or any agency thereof, of the financing herein authorized.

Done at Frankfort, Kentucky, this 9th day of May, 1986.

PUBLIC SERVICE COMMISSION

*Richard D. Hensley Jr.*  
Chairman

*Richard J. L.*  
Vice Chairman

*Spencer H. Williams Jr.*  
Commissioner

ATTEST:

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Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 9381 DATED MAY 9, 1986.

The following rates and charges are prescribed for customers receiving water service from Tri-Village Water District. 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>Rate</u>
First 2,000 gallons	\$11.75
Next 4,000 gallons	3.40
Next 4,000 gallons	3.30
Next 10,000 gallons	3.15
Over 20,000 gallons	2.90
 <u>Tap Fee</u>	
5/8-inch x 3/4-inch meter	\$375.00
 <u>Reconnect Charge</u>	
	20.00
 <u>Service Run Charge</u>	
<u>Distance from District Office to Customer's Premises</u>	
0-10 miles	10.00
10-20 miles	15.00
Over 20 miles	20.00
 The service run charge shall be applied only in instances where customer has made a request and it is subsequently determined that the trip was unnecessary and no problem exists in which the District is at fault.	
 Deposit	 \$ 25.00