

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

PURCHASED WATER ADJUSTMENT )  
OF BATH COUNTY WATER DISTRICT ) CASE NO. 9504

O R D E R

On January 26, 1986, Bath County Water District ("Bath County") filed its application with the Commission requesting authority to adjust its rates in accordance with its purchased water adjustment clause. Bath County proposed to recover the increase in purchase water expense from its wholesale supplier, City of Morehead ("City"), which became effective January 1, 1986. 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, 1985, as the test period in this matter. Adjustments deemed proper and reasonable have been included to more accurately reflect current operating conditions.

### REVENUES AND EXPENSES

Bath County did not propose any adjustments, as such, to its test-year statement of operations. However, Bath County did include information regarding the increase in purchased water costs resulting from the increased wholesale rate charged by the City. The Commission, after examination of Bath County's test-year operating statement has made the following adjustments in accordance with its normal rate-making practices for water utilities:

#### Purchased Water Expense

Bath County's purchased water expense for the test year was \$91,595. Bath County's normalized purchased water expense including the increase from the City effective January 1, 1986, is \$98,912. Accordingly, the Commission has increased Bath County's operating expenses by \$7,317 to reflect the increased purchased water expense.

#### Depreciation Expense

Bath County's test-year depreciation expense was \$19,564. It is the normal practice of the Commission to compute depreciation expense for rate-making purposes on non-contributed plant only. Such treatment insures 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.

Bath County's balance sheet at the end of the test period reflects contributions in aid of construction of \$948,042 which represents 62.7 percent of the total cost of utility plant in service. In determining the pro forma depreciation expense, the Commission has excluded this percentage of the reported test year amount. The adjusted depreciation expense for rate-making purposes is \$9,178 which reflects a reduction of \$10,386.

Adjustments to the test period operations produced the following results:

	<u>Actual</u>	<u>Commission Adjustments</u>	<u>Commission Adjusted</u>
Operating Revenues	\$214,060	-0-	\$ 214,060
Operating Expenses	<u>187,914</u>	<u>\$ &lt;3,069&gt;</u>	<u>184,845</u>
Operating Income	\$ 26,146	3,069	29,215
Other Income	6,536	-0-	6,536
Other Deductions	<u>19,375</u>	<u>-0-</u>	<u>19,375</u>
Net Income	<u>\$ 13,307</u>	<u>\$ 3,069</u>	<u>\$ 16,376</u>

#### REVENUE REQUIREMENTS

Bath County's debt service for the test period was \$26,348. Based on the adjusted net income, Bath County would earn a debt service coverage ("DSC") of 1.36X. The Commission is of the opinion that a DSC of 1.2X is a fair, just and reasonable coverage for Bath County to maintain in that it meets the requirements of its lenders and provides an adequate surplus for equity growth. Furthermore, the Commission allowed a 1.2X DSC in the most recent case to which Bath County was a party. Based upon adjusted test period operations, the Commission finds that Bath County's current

rates generate sufficient revenues to meet its operating needs and therefore, no rate adjustment is necessary. This is demonstrated as follows:

Adjusted Operating Expenses	\$184,845
1.2X Debt-Service Coverage	<u>31,618</u>
Revenue Requirement	\$216,463

Less:

Adjusted Operating Revenue	\$214,060
Adjusted Operating Income	<u>6,536</u>
Total Excess Revenues	<u>\$ &lt;4,133&gt;</u>

Thus, Bath County's current revenue levels exceed its required revenues by \$4,133. Therefore, the Commission is of the opinion that Bath County can and should absorb \$7,317, which is the full amount of the increase in purchased water cost.

#### RATE DESIGN

In its application, Bath County requested permission to adjust the rates of its wholesale customers only and to absorb the remaining increase pending the filing of an application for construction and general rate adjustment.

807 KAR 5:067 provides that the purchased water adjustment is to be calculated based on the total gallons sold during the test period to arrive at an adjustment factor per cubic feet or gallons sold. The base rate is assumed to be reflective of the cost of service for each billing class, with any purchased water adjustment applied on a per unit basis in order to maintain the cost-reflective rates. Thus in applications for purchased water adjustments, the adjustment must be applied to all rates on a per unit basis in all billing classes.

SUMMARY

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

1. Bath County has the potential to absorb \$7,317 which is the full amount of the increase in its purchased water cost.

2. The rates proposed by Bath County produce revenues in excess of those found reasonable herein and should be denied upon application of KRS 278.030.

IT IS THEREFORE ORDERED that:

1. The rates proposed by Bath County be and they hereby are denied.

2. The rates currently charged by Bath County are fair, just and reasonable and should continue to be charged.

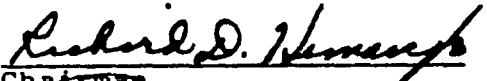
3. For the purpose of future application of the purchased water adjustment clause of Bath County the base rates for purchased water shall be:

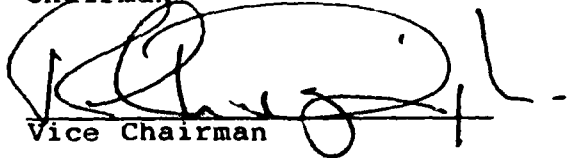
<u>Supplier</u>	<u>Rate</u>
City of Morehead	\$2,426.00 Capital Costs
	10.00 Meter and Billing Charge
	.523 per 1,000 gallons (all usage)

4. Bath County shall file with the Commission within 30 days from the date of this Order its revised tariff sheets showing the new base rate established herein to be used in future application of its purchased water adjustment clause.

Done at Frankfort, Kentucky, this 7th day of March, 1986.

PUBLIC SERVICE COMMISSION

  
Chairman

  
Vice Chairman

  
Commissioner

ATTEST:

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Secretary