

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF MONTGOMERY COUNTY)
WATER DISTRICT NUMBER ONE FOR A RATE) CASE NO.
ADJUSTMENT PURSUANT TO THE ALTERNATIVE) 96-118
RATE FILING PROCEDURE FOR SMALL UTILITIES)

O R D E R

On April 2, 1996, Montgomery County Water District Number One ("Montgomery Water") filed its application for Commission approval of proposed water rates. Commission Staff, having performed a limited financial review of Montgomery Water's operations, has prepared the attached Staff Report containing Staff's findings and recommendations regarding the proposed rates. All parties should review the report carefully and provide any written comments or requests for a hearing or informal conference no later than 15 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have no more than 15 days from the date of this Order, or 90 days after the date the application was filed, whichever is later, to provide written comments regarding the attached Staff Report or requests for a hearing or informal conference. If no request for a hearing or informal conference is received, this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky, this 20th day of June, 1996.

ATTEST:


Executive Director

PUBLIC SERVICE COMMISSION


For the Commission

COMMONWEALTH OF KENTUCKY
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THE APPLICATION OF MONTGOMERY COUNTY)
WATER DISTRICT NUMBER ONE FOR A RATE)
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STAFF REPORT

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STAFF REPORT

ON

CASE NO. 96-118

A. Preface

On April 2, 1996, Montgomery County Water District Number One ("Montgomery County") filed an application with the Commission seeking to increase its water rates pursuant to the Alternative Rate Filing Procedure for Small Utilities. The proposed rates would generate approximately \$32,140 annually in additional revenues, an increase of 16.9 percent over normalized test-year revenues of \$190,039.

In order to evaluate the requested increase, the Commission Staff ("Staff") chose to perform a limited financial review of Montgomery County's operations for the test period, calendar year 1994. Since Montgomery County requested and received Staff assistance in preparing this application, the field review was done prior to the filing of the application. Carl Salyer Combs conducted the review on February 16, 1996, at Montgomery County's office. Mr. Combs is responsible for this Staff Report except for the sections on operating revenues and rate design which were prepared by Christopher Smith of the Commission's Division of Rates and Research.

Processing of Montgomery County's rate application was delayed for some time due to the fact that its Report of Gross Operating Revenues for calendar-year 1995 filed with the Commission in March, 1996, showed a total of \$377,975. That amount represents an increase over reported 1994 gross operating revenues of \$175,656, or 86.8 percent. A

revised statement filed in April, 1996, listed 1995 gross operating revenues of \$214,819, an increase of 6.2 percent over the preceding year. If the original total of \$377,975 had been correct, Staff would have had to recommend that Montgomery County be granted no increase in its water service rates. Montgomery County is advised to take greater care to ensure the accuracy of its Report of Gross Operating Revenues in the future.

During the course of the review, Montgomery County was informed that all proposed adjustments to test-year expenses must be supported by some form of documentation, such as an invoice, or that all such adjustments must be known and measurable. Based upon the findings of this report, Staff recommends that Montgomery County be authorized to increase its annual operating revenues by \$30,640.

Scope

The scope of the review was limited to obtaining information to determine whether reported test-period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

B. Analysis of Operating Revenues and Expenses

Operating Revenues

Montgomery County's net operating income statement for the test year showed test-year revenues from water sales in the amount of \$200,819. The City of Mount Sterling, Montgomery County's wholesale water supplier, increased its water rates effective October 1, 1995. Montgomery County's billing analysis, which staff prepared, produced normalized revenue from water sales in the amount of \$188,539. Montgomery County adjusted its

income statement to reflect the operating revenue shown in the billing analysis. After reviewing the billing analysis, Staff has concluded that it more accurately reflects Montgomery County's revenue from water sales. Therefore, total test-year operating revenue from water sales is considered to be \$188,539.

Operating Expenses

Montgomery County incurred, and the Staff-assisted application included, test-period operating expenses of \$174,879. Montgomery County proposed to increase that amount by \$20,985. Montgomery County's proposed adjustments and Staff's recommendations are discussed in the following sections:

Salaries

Montgomery County reported test-year salaries expense of \$23,843. According to its office manager, Peggy Coburn, the current annual salary level is \$23,700. Therefore, Staff recommends that annual salaries expense of \$23,700 be included for rate-making purposes.

Purchased Water

Montgomery County reported test-year purchased water expense of \$109,698 which was supported by invoices. Effective October 1, 1995, the City of Mount Sterling increased its water rates to Montgomery County. Based upon that increase, Montgomery County's purchased water expense would have been \$120,042, an increase of \$10,344. Therefore, Staff recommends that annual purchased water expense of \$120,042 be included for rate-making purposes.

Electricity

Montgomery County reported test-year electric expense of \$260. Staff reviewed invoices from Kentucky Utilities which totaled \$209. Therefore, Staff recommends that annual electric expense of \$209 be included for rate-making purposes.

Insurance

Montgomery County proposed to increase reported test-year insurance expense of \$2,298 by \$522 based upon an increase from its insurance agent. As Montgomery provided documentation from its agent, Staff recommends that annual insurance expense of \$2,820 be included for rate-making purposes.

Miscellaneous Expense

Montgomery County's test-year miscellaneous expense of \$10,146 included higher than normal legal expense of \$2,702. According to Ms. Coburn, 1995 legal expense totaled \$1,179, an amount which is more representative of a normal year. Staff therefore recommends that test-year legal expense be reduced by the difference of \$1,523, and annual miscellaneous expense of \$8,623 has been included for rate-making purposes.

Depreciation Expense

Montgomery County reported test-year depreciation expense of \$12,304 on its annual report operating statement. Staff observed that the balance sheet reflected an increase to accumulated depreciation of \$24,140. Furthermore, a schedule in the annual report showing a breakdown of accumulated depreciation also reflected test-year charges of \$24,140 to depreciation expense.

Test-year depreciation expense of \$24,140 yields a composite depreciation rate of 2 percent, a reasonable rate. When Staff asked for an explanation of the discrepancy, Ms. Coburn confirmed that \$24,140 should have been reported on the 1994 annual report operating statement. Therefore, Staff recommends that annual depreciation expense of \$24,140 be included for rate-making purposes.

Operations Summary

Based on the recommendations of Staff contained in this report, Montgomery County's operating statement would appear as follows:

	<u>Test Period Application</u>	<u>Recommended Adjustments</u>	<u>Test Year Adjusted</u>
OPERATING REVENUES:			
Water Sales	\$ 200,819	\$(12,280)	\$ 188,539
Other Revs.	<u>1,500</u>	<u>-0-</u>	<u>1,500</u>
Total Oper. Revs.	\$ 202,319	\$(12,280)	\$ 190,039
OPERATING EXPENSES:			
Salaries	\$ 23,843	\$(143)	\$ 23,700
Pens./Benefits	5,890	-0-	5,890
Purchased Water	109,698	10,344	120,042
Electricity	260	(51)	209
Mat./Supplies	5,375	-0-	5,375
Contract. Serv.	1,398	-0-	1,398
Insurance	2,298	522	2,820
Miscellaneous	10,146	(1,523)	8,623
Depreciation	12,304	11,836	24,140
Taxes Other Than Income Taxes	<u>3,667</u>	<u>-0-</u>	<u>3,667</u>
Total Oper. Exp.	\$ <u>174,879</u>	\$ <u>20,985</u>	\$ <u>195,864</u>
OPERATING INCOME	\$ 27,440	\$(33,265)	\$(5,825)
Other Income	<u>1,899</u>	<u>-0-</u>	<u>1,899</u>
INCOME AVAILABLE FOR DEBT SERVICE	\$ <u>29,339</u>	\$ <u>(33,265)</u>	\$ <u>(3,926)</u>

C. Revenue Requirements Determination

Staff has calculated Montgomery County's annual debt service to be \$22,262.¹ Montgomery County's adjusted operations reflect \$(3,926) in income available for debt service which results in a debt service coverage ("DSC") of (.18X). Staff is of the opinion that Montgomery County's current rates are inadequate and will not cover payment of operating expenses and debt service requirements. In cases involving water districts, the Commission's normal practice is to allow a 1.2X DSC which provides a 20 percent margin above annual principal and interest requirements. In this instance, Staff is of the opinion that Montgomery County should be granted an increase in revenues sufficient to produce a DSC ratio of 1.2X. Therefore, Staff recommends an increase in annual revenues of \$30,640 calculated as follows:

1.2X DSC	\$ 26,714
Adjusted Operating Expense	<u>195,864</u>
Total Revenue Requirement	\$ 222,578
LESS:	
Adjusted Test-Year Revenues	190,039
Other Income	<u>1,899</u>
Increase Required	<u>\$ 30,640</u>

D. Rate Design

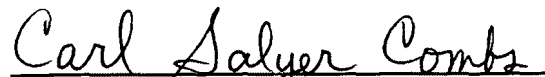
Montgomery County's current rate design consists of a four step declining block rate. Montgomery County's application did not include any changes in rate design. Staff agrees that the current rate structure should not be altered at this time. While no increase was proposed for the City of Jeffersonville, a wholesale customer, based on a review of

¹ 3-year average of principal payments due	\$ 12,667
3-year average of interest payments due	<u>9,595</u>
Total of 3-year avg. of P&I payments due	<u>\$ 22,262</u>

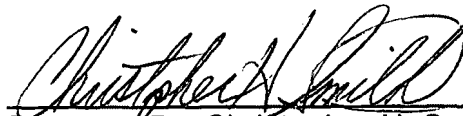
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Montgomery County's expenses Staff determined that the increase should be passed on to all customers. Therefore, Staff recommends that each rate increment be increased by approximately 17 percent. The rates recommended by Staff will generate annual water sales revenues of \$219,179.

E. Signatures



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APPENDIX A
TO STAFF REPORT CASE NO. 96-118

The Staff recommends the following rate be prescribed for customers in the area served by Montgomery County Water District No. 1.

Monthly Rates

First 2,000 gallons	\$16.20 (Minimum Bill)
Next 3,000 gallons	3.06 per 1,000 gallons
Next 5,000 gallons	2.89 per 1,000 gallons
Over 10,000 gallons	2.25 per 1,000 gallons

Monthly Wholesale Rate

Per 1,000 gallons	\$ 1.88
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